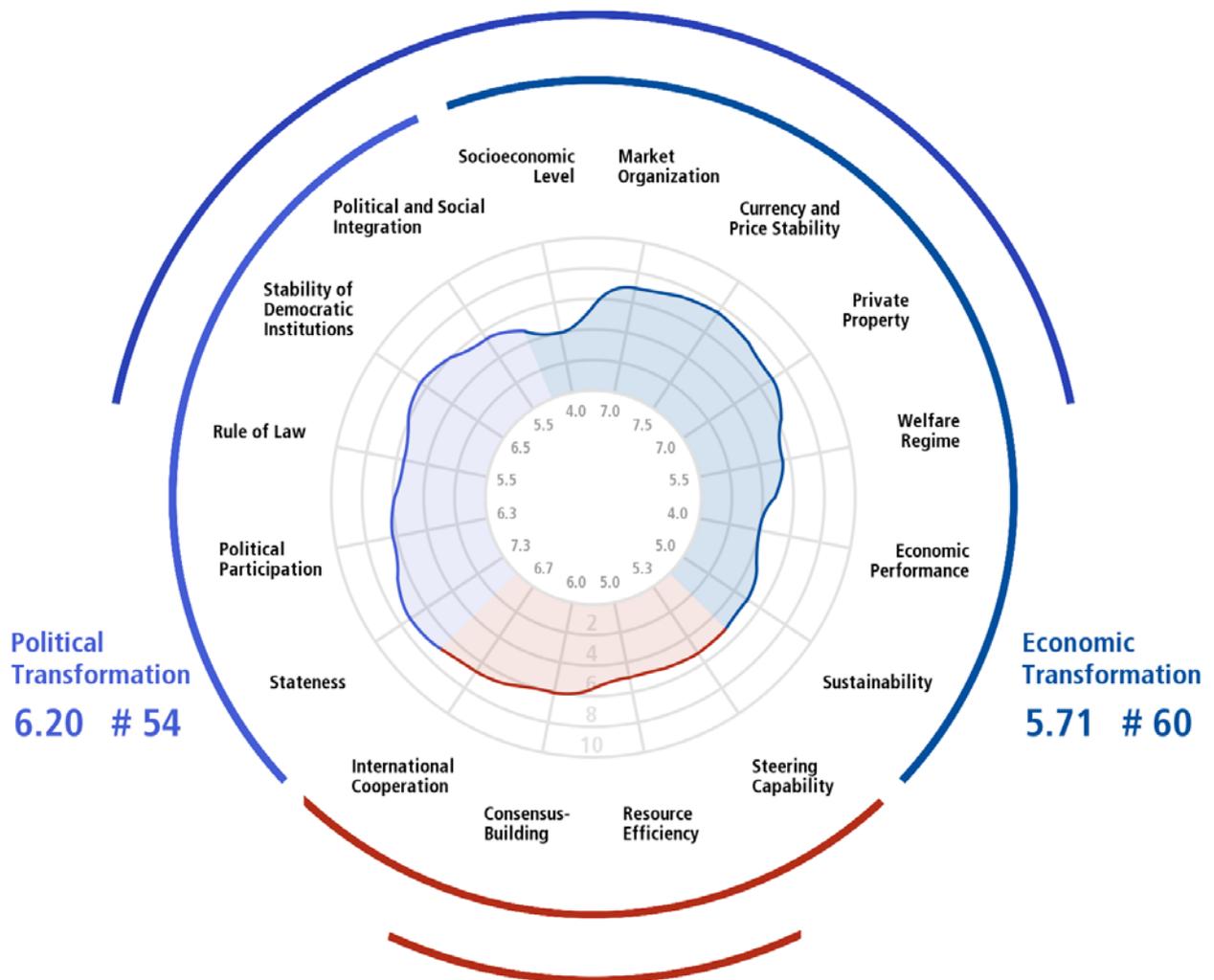


Moldova

Status Index

5.96 # 54

on 1-10 scale out of 129



Political Transformation
6.20 # 54

Economic Transformation
5.71 # 60

Governance Index

5.15 # 60

on 1-10 scale out of 129

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2018. It covers the period from February 1, 2015 to January 31, 2017. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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Key Indicators

Population	M	3.6	HDI	0.699	GDP p.c., PPP \$	5334
Pop. growth ¹	% p.a.	-0.1	HDI rank of 188	107	Gini Index	27.0
Life expectancy	years	71.4	UN Education Index	0.725	Poverty ³	% 1.4
Urban population	%	45.1	Gender inequality ²	0.232	Aid per capita \$	87.9

Sources (as of October 2017): The World Bank, World Development Indicators 2017 | UNDP, Human Development Report 2016. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

Executive Summary

The last two years have been exceptionally difficult for Moldova. In November 2014, it was revealed that around \$1 billion had been fraudulently siphoned from the country's banking system. As it turned out, the country's leading politicians knew about the situation and some of them had been involved in the embezzlement of funds. Meanwhile, the rivalry for control of the state apparatus between Vlad Filat and Vlad Plahotniuc, the two most powerful businessmen in Moldova and leaders of the main pro-European coalition parties, entered a decisive phase. The conflict ended abruptly on October 15, 2015, when Filat was arrested on charges of corruption and involvement in the banking scandal.

The participation of public authorities in a large-scale fraud, as well as the political chaos which was the result of the rivalry between Filat and Plahotniuc, seriously damaged the image of the government. A series of large demonstrations shook the capital city in 2015. The public's disappointment at the pro-European government resulted in a sharp drop in support for EU integration, which reached a historical low (32%) in 2015. At the same time, the popularity of pro-Russian groups increased.

The political turmoil coincided with a deterioration in the economic situation. In 2015, GDP suffered its biggest drop since independence, declining by 18% from 2014. The Russian trade embargo imposed on Moldova in response to initialing (in 2013) and signing (in 2014) the Association Agreement with the European Union significantly lowered Moldovan exports. For now, the Deep and Comprehensive Free Trade Area (DCFTA) deal with the European Union, which provisionally entered into force on September 1, 2014, has not managed to balance the losses on Russian markets. The remittances which are an essential source of income for many families in the country decreased by nearly a third. The loss of government credibility among Western partners resulted in the suspension of a large share of foreign financial assistance. The economic situation started to stabilize only in 2016 when Moldova managed to regain foreign financial aid, sign a new agreement with the IMF and achieve economic growth. The social

situation in the country remains bad as demonstrated by the massive emigration rate. As many as 15% to 25% of Moldovans are currently working abroad, which represents up to 40% of the working-age population.

The recent stabilization of the economic situation has not coincided with an improvement in the political situation. In 2016, control over the state apparatus was seized by the oligarch Vlad Plahotniuc. Plahotniuc is not interested in the implementation of any significant reforms, because his power derives from his control of the state apparatus and financial flows in Moldova. Plahotniuc's control over a discredited government continues to hamper public popularity for pro-European ideas. This was proven by the victory of pro-Russian politician, Igor Dodon, in the presidential elections at the end of 2016.

History and Characteristics of Transformation

As with many Commonwealth of Independent States member states, questions of nationhood and statehood were strongly disputed at the beginning of the transition period. During the late perestroika period, the pro-Romanian faction supported reunification with Moldova's western neighbors and gained dominance in Moldovan politics. This led to the formation of an opposition supported by Russia in the eastern (Transnistria) and southern (Gagauzia) parts of the country that culminated in the secession movement. The secession of the two regions in 1990 and especially highly industrialized Transnistria, located on strategic trade and transport routes, led to conflict in 1992. The armed conflict was between Moldovan government forces and Transnistrian volunteers supported by Russian troops stationed in the region. After five months of fighting Chisinau's forces were defeated and Moldova de facto lost control over Transnistria. While the conflict with the Gagauz minority was resolved in 1994 by an internationally praised autonomy arrangement, the Transnistrian issue remains unresolved.

The secession of the highly industrialized Transnistria region, which had accounted for 40% of Moldavian SSR's GDP, delivered a severe blow to the Moldovan economy. The economy had already been weakened by the disintegration of the Soviet Union. An absence of natural resources or competitive agricultural and industrial products further worsened the situation. Between 1990 and 1992, the GDP of the newly independent state shrank by as much as 35% and the downward trend continued for next few years. Economic growth was restored only after the government of Prime Minister Ion Sturza took office in 1999 and initiated the necessary reforms. Unfortunately, the Communists who took full power in Moldova in 2001 were not interested in wide-scale economic liberalization. The situation started to change in 2009 when the group of pro-European parties formed a government and initiated a broad program of pro-European reforms. However, as it turned out, lots of the reforms existed only on paper as the new coalition government signed the Association Agreement with European Union and introduced Moldova into Deep and Comprehensive Free Trade Area (DCFTA) in 2014. The new agreement accelerated the process

of reorienting Moldovan trade from Russian to EU markets. At the same time, Moldova remains highly dependent on Russian energy resources.

Ideological debates concerning nationhood and statehood, and geopolitical affiliation remain a central point of Moldovan politics. These debates have polarized the population and led to the postponement of economic reforms. The dominance of such issues in public debate facilitated the emergence of a populist political elite that lacked the proper managerial skills to conduct much-needed reforms and focused instead on their own personal enrichment. The general economic malaise and ongoing distrust of the political establishment continue to strengthen the conservative and populist camp, currently divided into three parties – the Party of Socialists – which is the largest party in the parliament and in strong opposition to the current coalition, extra-parliamentary Our Party and the Party of Communists, which plays the role of constructive opposition.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

Moldovan authorities exercise control and have a monopoly on the use of force over the vast majority of the country's constitutional territory. However, areas situated on the left bank of the Dniester river (including large urban centers like Tiraspol and Rîbnița) and certain territories lying on the right bank (including city of Bender and few small villages) remain an exception. This area, known as Transnistria is controlled by the self-proclaimed authorities of the Transnistrian Moldavian Republic (PMR), which has not been internationally recognized. Although unrecognized, Transnistria is a de facto independent state with its own police, armed forces and secret service, which allow local authorities to maintain a complete monopoly on the use of force over the territory controlled by the PMR. Units of the Russian army stationed on the territory of PMR (about 1,500 troops) strengthen the local authorities' control over the separatist republic. Despite the almost complete subordination of territories on the left bank of the Dniester river to PMR-controlled local authorities, the government of Moldova still exercises control (contested by Transnistria) over several smaller villages in the Dubasari region.

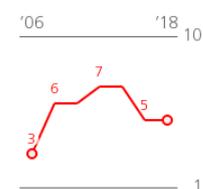
Although relations between the separatist authorities and Chisinau are traditionally tense, there were no cases of serious acts of violence or armed clashes after the end of hostilities in 1992.

However, Gagauzia returned to the control of the Republic of Moldova in 1994, and relations between the Autonomous Territorial Unit of Gagauzia and the Moldovan central government in Chisinau remain tense. In reaction to the planned signing of the Association Agreement with the European Union by Moldova in February 2014, the Gagauz authorities simultaneously carried out two referenda (both unrecognized by Chisinau) in which 98% of voters rejected the idea of integration with the European Union and voted for the right of the region to secede if Moldova would lose its independence. Although tensions between Chisinau and Gagauz authorities have eased slightly since 2015, the local and central authorities still regularly engage in

Question
Score

Monopoly on the
use of force

5



conflicts regarding their competences. For example, the adoption of law on education by Gagauz authorities in April 2016 was deemed unlawful by Chisinau. Additionally, Gagauzia is an openly pro-Russian region, which still remains (like Transnistria) an instrument of Moscow's pressure on the currently pro-European government in Chisinau and could be used to destabilize the situation in Moldova.

There is no consensus within Moldova's society regarding a civic and ethnic-based definition of the Moldovan nation-state. Certain parts of the population (including Russian-speaking minorities) and political parties (left and center-left) support the so-called Moldovenism, which firmly highlights the separateness of Moldovans and Romanians. Proponents of this approach advocate a multi-ethnic (sometimes multilingual) civic state. On the other hand, a considerable proportion of Moldovans (mostly ethnic Moldovans and Moldovan Romanians) as well as right and center-right parties support a more ethnic-based view, according to which Moldovan statehood should be based on the Moldovan/Romanian titular nation, with a dominant role for Romanian language and culture. Although both of these groups differ in their views, they are mostly consistent as to the issue of preserving the Moldovan statehood.

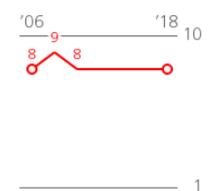
Certain political parties and organizations in Moldova are advocating unification of Moldova and Romania (tantamount to dismantling Moldovan statehood), but they are rather marginal. For a long time, the number of supporters of unification with Romania oscillated between 10% and 15% of the total population, but in 2015 the proportion slightly increased. In 2015 and 2016, due to - among other things - growing disillusionment with the political class and the worsening economic situation, the idea of reunification gained popularity. Currently, 20% of Moldovans declare that they would vote for a reunification with Romania.

Between 1991 and 2013, the number of Moldovans holding Romanian passports increased to between 400,000 and 500,000. This trend decreased, however, in 2014 when the European Union lifted the visa requirement for Moldovan citizens. Applying for Romanian citizenship is perceived by most Moldovans as a rather pragmatic (rather than an ideological) step which allows them to travel and work freely within the European Union.

Formally, the Republic of Moldova is a secular state in which churches and religious associations do not have an official role in the national political system or lawmaking process. At the same time, the Moldovan constitution provides for full freedom of religious practice. In reality, because of the traditionally conservative nature of the Moldovan population (95% of Moldovans associate with the Orthodox Church), Moldovan politicians often highlight their religiosity and seek the support of clergy in order to increase their popularity among the electorate. Metropolitanate of Chisinau and all Moldova (MOC) – which includes about 80% of Moldovans and is subordinated to the Moscow Patriarchate – plays a dominant role in the country. Although officially MOC is treated like any other church, in practice it enjoys

State identity

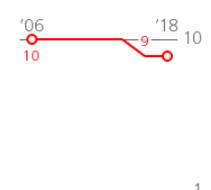
8



1

No interference of religious dogmas

9



1

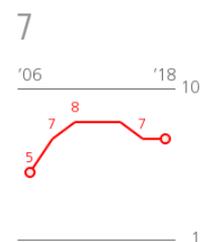
privileges from the government. The Orthodox Church is actively involved in promoting traditional, conservative values and fights with the influence of other religions on the territory of Moldova. It also opposes the rights of sexual minorities.

However, Orthodox dignitaries in Moldova traditionally take an active part in election campaigns. In the case of the presidential elections of 2016, their involvement was significantly greater than usual and concerned all levels of MOC representatives. The Metropolitan of Chisinau publicly supported the candidacy of Igor Dodon for president of Moldova, emphasizing his religious devotion to Christian values and the material assistance Dodon granted to the Orthodox Church. At the same time, some Orthodox notables officially criticized the main opponent of Dodon, Maia Sandu, inter alia for her alleged anti-Orthodox activity.

Moldovan state administration structures are firmly established across the country with the exception of Transnistria. Moldovan administration is split into three levels – central (national), regional (so-called raions) and local. However, although state administration structures are present across the whole territory controlled by Chisinau and possess significant competences, in many fields their efficiency (especially in the rural areas) remains limited due to the lack of sufficient funding, corruption and quality of staff. According to the World Bank, only 67% of rural population (2014) have access to improved sanitation facilities and 19% (2015) are still deprived of access to improved water sources. Another problem is the virtual lack of independence of local administrative structures from the central authorities. The effectiveness of the public administration is also limited by widespread corruption.

Over the last few years, Moldovan authorities have initiated a number of reforms which aim to improve local administration. On January 1, 2015, amendments to the law on local public finances entered into force. According to the new regulations, local authorities retain 75% of the personal income tax collected at the local level. They can also set expenditure priorities on their own, with the provision that raions and municipalities are able to dispose only 25% and 45% of the funds, respectively. In order to create proper conditions for the implementation of the reform, a National Council on Public Administration was established at the end of 2015. The council which is chaired by the prime minister is a high-level platform designed to take decisions on strategic directions regarding public administration reform at both central and local level. In July 2016, the government approved a Public Administration Reform Strategy for 2016-2020 which envisages reforms on both (local and central) levels of administration, modernization of public services, public finances management and administrative responsibility.

Basic
administration



2 | Political Participation

Elections to the Moldovan parliament and local authorities are universal, conducted with a secret ballot, and they are held regularly. Citizens can choose from a range of political parties and candidates, and political posts are filled according to the voting results.

In 2016, the Constitutional Court reinstated the right of citizens to directly elect the president of the republic (who, since 2000, was elected by the parliament). The decision raised a number of controversies. Among others, one of the key anti-government opposition candidates, Renato Usatîi, was prevented from participating in the election on the grounds that he was too young (38). For an unknown (probably political) reason, the Constitutional Court restored electoral regulations which had existed before 2000. However, at the same time, the Constitutional Court retained the minimum 40-year age limit for presidential candidates that had been adopted in 2000. Prior to 2000, the minimum age limit for presidential candidates had been 35 years.

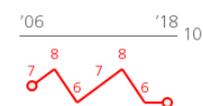
Local elections held in June 2015 were dominated by geopolitical issues. Despite the very high unpopularity of the ruling (pro-European) parties, the ruling parties succeeded because their leaders managed to convince the electorate that the victory of pro-Russian camp would lead to the termination of Moldova's integration process into the European Union and the Eurasian Economic Union. Local elections were generally assessed positively by the OSCE, despite a few violent incidents and a lack of balanced media coverage.

The presidential election organized in October and November 2016 was dominated by the struggle between two anti-government candidates: Igor Dodon and Maia Sandu. At the time, Igor Dodon led the pro-Russian Party of Socialists, while Maia Sandu was a representative of the pro-European opposition, and leader of the Party of Action and Solidarity (PAS). Despite the fact that OSCE rated the voting as generally corresponding to international standards (with minor infringements such as imbalanced media coverage), the elections have raised many questions concerning the accuracy of the process. Observers have pointed to a shortage of ballots in polling stations abroad and have drawn attention to the fact that a significant number of ballots (approximately 17,000) were cast by Moldovans residing in Transnistria. Additionally, it seems that Dodon had the advantage due to the unofficial support of the authorities. For example, the blocking of Usatîi's participation in the elections allowed Dodon to gain more votes. Finally, Dodon, was announced the winner, with a marginally higher support (52.11% of the vote) than Maia Sandu.

Democratically elected political representatives have limited power to govern. Political and business interest groups play a huge, if not a crucial, role in legislative and government decision-making processes. Certain political representatives (on local and central levels) tend to abuse their political offices in order to protect their

Free and fair elections

6



Effective power to govern

5

business interests. On the other hand, there are groups which are de facto shaping the policy of the country but have little legitimacy to rule. For example, the oligarch Vlad Plahotniuc has directly influenced the government decisions. Prime Minister Pavel Filip is a close aid and longtime business partner of Plahotniuc. Filip is fully dependent on the oligarch and secured the position of prime minister as a result of the Plahotniuc's efforts. Plahotniuc is the key sponsor and leader of the Party of Democrats. Furthermore, Plahotniuc also managed to subordinate number of other deputies which gives him a control over parliamentary majority. At the same time, Plahotniuc does not hold any official state position. Additionally, certain Moldovan politicians seem to remain under the influence of external actors. Russia's influence over President Igor Dodon has increased, and Dodon's statements and decisions often appear to represent the narrative of Russian officials.

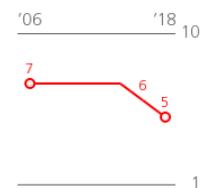
Freedom of association and assembly are guaranteed by several legal acts and governmental decisions including the constitution of the Republic of Moldova (Article 40).

Since 2009, the number of public demonstrations has gradually risen. In 2015, at least four mass anti-governmental demonstrations (with 10,000 to 20,000 participants) took place in Chisinau. The government decided to protect the participants and the security of official buildings, and refrained from any attempts to limit the right to protest. In February 2015, pro-European Dignity and Truth Movement set up a tent city in front of the government building. Then in September 2015, a similar city was set up by pro-Russian opposition in front of the building of parliament. In both cases, the authorities did not try to intervene and both tent cities existed for several months.

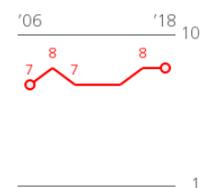
The Moldovan LGBT community also enjoys a formal right to assembly, but their parades and demonstrations always face aggressive counter-demonstrations organized by representatives of the Orthodox Church and conservative political parties. The authorities are usually unable to provide comprehensive security to the participants of such event and often push for the demonstrations to be held in less public places.

Freedom of expression in Moldova on the legal level is guaranteed by the constitution and legislation. Journalists are free to express their views and to conduct journalistic investigations, even against ruling politicians.

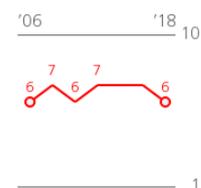
Unfortunately, the subordination of the media to key political and business groups in the country is a rising concern. For at least six years, media outlets have become increasingly concentrated in the hands of the oligarch Vlad Plahotniuc. It is estimated that the market share of media outlets controlled by Plahotniuc's is between 60% and 70%. The businessman is currently the owner of four out of the five national television stations. He has also allegedly subordinated certain public broadcasters, including the premier channel of Moldovan public television. At the same time, Plahotniuc's holding monopolized large part of the advertising sector and can use his



Association /
assembly rights
8



Freedom of
expression
6



monopoly to influence his competitors, who largely depend on advertising revenue. Officially, certain attempts to fight the monopolization of the media were made, but as far they have proved to be ineffective. In March 2015, the parliament passed amendments to the broadcasting code which require radio and television companies to disclose the names and shareholdings of their owners, and the names of board members, managers, broadcasters and producers.

Moldovan authorities are trying to limit journalistic access to official sources. Media claims for access to sensitive public information are sometimes denied.

Also, certain independent or openly anti-Plahotniuc media outlets (such as Ziarul de Garda or Jurnal TV) regularly face pressure and intimidation (such as threats of lawsuit) from the official state institutions.

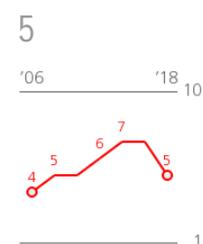
At the same time, there have been several – mostly unsuccessful – attempts by lawmakers to limit the freedom of expression of various media outlets under the guise of a “fight against propaganda.” Annual rankings compiled by Reporters Without Borders confirm a worsening situation of Moldovan medias. In 2016, Moldova scored 28.83 points, 10 points lower than in 2010 when pro-European coalition came to power.

3 | Rule of Law

Formally, since 2000, Moldova has been a parliamentary-cabinet republic, where the prerogatives of parliament and government are considerably stronger than the powers of president. In reality, however, the political system in Moldova depends on the position and influence of key political actors. President Vladimir Voronin (2001-2009), who also held the position of chairman of the Communist Party, was a key decision-maker with full control over the parliamentary majority and decisive influence on the decisions made by the government. After the election of Nicolae Timofti as president in 2012, the role of head of state became marginal, and power was returned to the government and parliament. In January 2016, Pavel Filip was appointed prime minister. As Filip is a close aide of the oligarch Vlad Plahotniuc, Filip’s appointment indicates that it is Plahotniuc who in fact decides government policies.

The government occasionally decides to bypass parliament in the legislative process by exercising its lawmaking right provided by the procedure of “taking responsibility for the law by the government.” Although the procedure is intended for emergency situations the government has decided to make use of it a number of times since 2015. The judiciary in Moldova is prone to corruption and servility toward business and political groups. This primarily concerns key institutions, such as the Prosecutor

Separation of powers



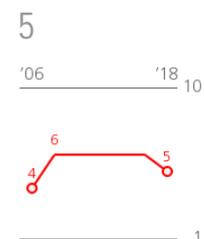
General's Office, the Supreme Council of the Judiciary, the National Anti-Corruption Center and the Constitutional Court.

The Moldovan judiciary remains highly corrupt, and demonstrates servile attitudes toward political and business groups. Currently, the justice system of Moldova (including the General Prosecutor's Office, the Supreme Court of Justice, the Supreme Judiciary Council and the National Anti-Corruption Center) is largely subordinated to the oligarch, Vlad Plahotniuc. Key positions in the justice system are filled in a non-transparent way with people loyal to the oligarch. For instance, on February 9, 2016, Mihai Poalelungi, a judge loyal to Plahotniuc, was re-appointed as president of the Supreme Court of Justice. It is worth noting that Poalelungi was the only candidate for this office. Obedience of the judiciary to the authorities (controlled by Plahotniuc) has been enforced using corrupt practices, business and clan ties, and intimidation. For example, in early 2016, an unfounded investigation was initiated against Judge Dominica Manole who had issued a verdict favorable to the anti-Plahotniuc opposition. The politicization of the judiciary is an instrument often used against Plahotniuc's rivals.

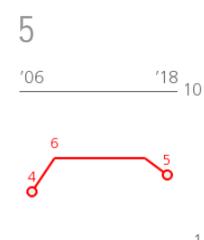
In February 2016, the long-awaited law on the Prosecutor General's Office was adopted, but this did not prevent the appointment in December 2016 of a new prosecutor general associated to Plahotniuc. Additionally, in September 2016, the anti-corruption authorities detained fifteen judges on corruption charges. This was the first time in modern Moldovan history that so many representatives of justice system had been made subject of criminal proceedings. However, it is highly likely that detainment of these fifteen judges was also politically motivated and was not associated with the actual will of law enforcement institutions to curb corruption.

Abuse of power by state officials remains one of the key problems in Moldova. Many public servants (regardless of rank) are either corrupted by influential business and political actors, or use their power to protect their own interests or enrich themselves. Despite the scale and intensity of this phenomenon, persecution and convictions of politicians and other officials (especially high-ranking public servants) are uncommon. Even where prosecutions are pursued, they are rarely motivated by the efficiency of justice but by political competition. In late June 2016, the former prime minister, Vlad Filat, was sentenced to nine years in prison for corruption related to the siphoning of \$1 billion in public finances. Even though it seems very likely that Filat as involved in this situation, there is plenty of evidence suggesting that other high-ranking members of the Moldovan government could have been involved in the fraud. It is highly possible that the arrest and conviction of Filat was a consequence of the long-lasting political struggle between him and the oligarch Vlad Plahotniuc. At the same time, Ilan Shor, mayor of Orhei and the main suspect in the banking fraud case, remains unpunished. It is alleged that a deal was agreed between Shor and Plahotniuc (Filat was arrested and convicted because of Shor's testimonies). Additionally, under political pressure, Moldovan administration of justice sometimes

Independent
judiciary



Prosecution of
office abuse



initiates criminal proceedings against lower-ranking officials in order to create the impression that the authorities are fighting the abuse of power and corruption effectively. This method is also used in order to get rid of the officials appointed by political competitors.

On the official level the Republic of Moldova is committed to respecting civil rights (which are codified by law). Yet in spite of positive developments in this regard over the recent years, fundamental freedoms are unfortunately still very often violated. This concerns the lack of fair trials, hate speech, the right to social protection and health care, bad conditions in prisons, the trafficking in human beings, and the rights of sexual minorities and the Roma community. And given the fact that Moldovan legislation prohibits torture, there have been even reports of violations of the right to life and physical integrity, including cases involving the deaths of prisoners or detainees.

During the first half of 2015 – despite the ongoing reform of the Ministry of Interior – more than 300 complaints of ill-treatment or torture were registered (compared to the one registered in the same period of 2014). Police officers responsible for the acts of violence are generally not punished or even prosecuted for their actions. However, some positive changes can be observed in this field.

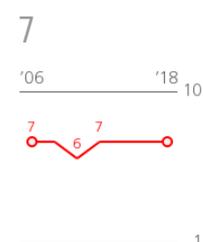
Another problem concerns the conditions in Moldovan prisons and detention centers which are poor. The right to a fair trial is also challenged, among other things, by the partiality of judges and corruption in the judiciary. The rights of sexual minorities are still not fully enforced, but they are protected by law. Hate speech against the LGBT community is common in Moldova and emanates not only from religious leaders but also influential politicians. Hate crimes remain generally unreported and badly (if at all) investigated. Moreover, these are not considered to be distinct crimes under the Moldovan Criminal Code and are usually qualified as hooliganism.

4 | Stability of Democratic Institutions

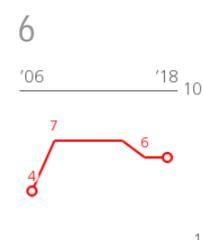
Between 2009 and 2015, the efficiency of democratic institutions in Moldova was seriously challenged by the extensive frictions and regular outbreaks of political conflicts between main political and business groups. However, with the growing concentration of power in the hands of the oligarch Vlad Plahotniuc, toward the end of 2015, the situation started to change. Plahotniuc managed to virtually take control of the government (he plays a decisive role in appointing the cabinet) and parliamentary majority. This eased previous tensions between these two institutions, but also hampered their democratic nature.

The only visible conflict exists currently between the President Igor Dodon, executive and parliamentary majority. Pro-Russian Dodon has strongly criticized the current – formally pro-European – government and parliamentary majority. Meanwhile, the

Civil rights



Performance of democratic institutions



ruling majority is gradually limiting (although marginally) the competences of the president, which contributes to the rising frictions. Given the limited prerogatives of the president in the Moldovan political system, this conflict has not significantly influenced the effectiveness of the democratic institutions in the country.

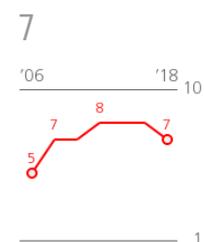
All mainstream political parties and civil society movements approve democratic norms and values. Even those extra-parliamentary, popular parties (e.g., Our Party, whose leader Renato Usatîi promotes undemocratic regimes, such as Belarus, as a model for Moldova) do not reject democratic procedures. The results of elections (on all levels) – although regularly contested by the opposition – are generally respected. Over the 25 years of Moldova’s independence, every ruling party which has lost an election conceded power without considerable resistance. The current opposition, which is openly critical of the government, has not made any attempts to illegally overthrow the government. The intrusion of protesters into the parliament building during a demonstration in January 2016 took place against the will of the leaders of the protest. However, attempts have been taken by key political and business actors to limit the power of certain high-level state officials. In December 2015, the Constitutional Court, which is allegedly under Plahotniuc’s influence, passed a decision restricting the president’s right to nominate candidates for prime minister. As a result, the prime minister’s post was taken by a close aide of the oligarch. The army plays a marginal role in the country and is not engaged in Moldovan politics whatsoever. Although the Orthodox Church openly comments on political decisions it has never denied the legitimacy of democratically elected authorities.

5 | Political and Social Integration

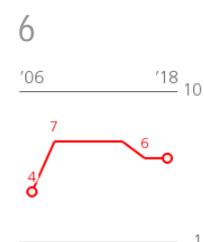
The Moldovan party system comprises a number of groupings which – at least nominally – represent a whole range of political views. Unfortunately, the party system in Moldova is being instrumentalized, only moderately stable and does not enjoy the trust of citizens. The vast majority of Moldovan political parties are chieftain-style groupings, organized around charismatic leaders and steered without intraparty democracy. Such parties naturally turn into instruments serving the political and business interests of their leaders and sponsors, instead of understanding and articulating the interests of particular sections of society. At the same time, the parties are relatively unstable, since the departure of the leader most often causes the disintegration or marginalization of the party. Political parties in Moldova in general are dependent on financial support from business tycoons rather than public funding or membership fees. Attempts to build bottom-up parties based on broad self-governing structures capable of influencing the party leadership have been undertaken only recently.

Political parties in Moldova tend not to compete by offering attractive economic or social programs but have primarily appealed to geopolitically (also historically and

Commitment to democratic institutions



Party system



culturally) understood notions of “left-wing” (pro-Russian) and “right-wing” (pro-Western). Such divisions are very convenient for the political elite because they make it possible to easily gain popularity among particular sections of the electorate. The persistence of these divisions prevents meaningful political debate on a wide range of political issues. Geopolitical polarization in the electorate is very strong and it is rather uncommon for pro-European or pro-Russian supporters to change his opinion. On the other hand, sympathies of Moldovan voters easily switch from one party to the other.

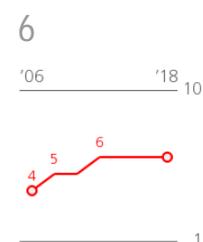
The level of social self-organization in Moldova is not very high. The vast majority of civil society organizations in Moldova (including NGOs and think tanks) are located in the capital city and usually limit their activities to the area of the city. To a much lesser extent, such organizations can be found in Bălți (northern Moldova) and in Comrat (the capital city of the Gagauz Autonomy). Trade unions, although these exist, have only a limited impact. Trade unions are unable to influence employers or legislation, which in turn means that they are not sufficiently able to defend workers’ rights.

At the same time, Moldovan society attaches great significance to family ties. In Moldova, families are traditionally understood to include not only actual relatives, but also wedding best men. As a result, in Moldova there is a variant of the phenomenon of clan relations (similar to the clan structures that exist in Central Asia). Being in a family involves very close relations and generates commitments, which are considered to be much more important than obligations toward the state or public institutions. Many Moldovan politicians are also involved in their own business activities. Politicians use their political influence and connections to ensure safety and prosperity of their own interests.

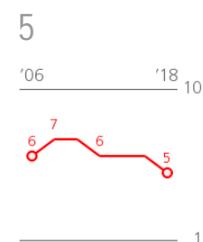
The Moldovan public is deeply disappointed about the performance of democratic institutions. According to the International Republican Institute (IRI), only 14% of Moldovans declared that they are very or somewhat satisfied with the way democracy is developing in Moldova, while 80% stated that they were very or somewhat dissatisfied. The level of trust toward key democratic institutions in 2016 was one of the lowest in Moldovan history (BOP, October 2016). Substantial or modest trust in parliament was declared by only 5.9% of the population. The government was trusted by 9.2%, the resident by 3.2% and political parties by 7.7% of the general public. Additionally, nepotism and favoritism are rampant in Moldova, because it is considered natural to involve clan and family members in the activities of political leaders. As a result, 78% of Moldovans (IRI, March 2016) consider the country to be governed in the interest of some groups, rather than the majority of people.

The Moldovan population in general is reluctant to engage in any collective actions. Moldovans are rather distrustful toward their neighbors. Only 23% of Moldovans (survey conducted by IMAS in August 2016) consider their compatriots trustworthy. An ethnic component also plays a certain (however not major) role in fostering social

Interest groups



Approval of democracy



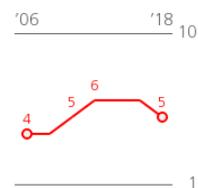
Social capital

5

distrust. According to the IMAS survey, 30% to 40% of the population stated that Moldovans and three key minorities in the country (Ukrainians, Russian and Gagauz) are either conflicted or ignore each other. As a result, social solidarity in Moldova is rather low, as has been proven among other things by the fact that despite the wide public discontent related to the embezzlement of \$1 billion the main suspect in the banking fraud – Ilan Shor – has been elected as mayor of Orhei.

Traditionally, family ties play a very important role in Moldova and it is expected that family members will help one another when in need. The vast inflow of remittances for Moldovan families from relatives working abroad demonstrates how important family ties are, especially given the hard economic situation in the country.

As the self-help networks in Moldova are based on personal trust and family ties, the level of social participation in NGOs or formal social organizations remains low. Public associations regularly face difficulties in engaging citizens. Even local, neighborhood associations remain marginal in Moldova. NGO activity is additionally limited by the fact that most of NGOs are concentrated in the capital and rarely operate in the rural areas. In small towns and villages, self-organization of the society is marginal or de facto non-existent.



II. Economic Transformation

6 | Level of Socioeconomic Development

Social exclusion in Moldova is caused by poverty and place of residence (urban vs. rural areas), or gender, ethnicity or religion. Since the beginning of 21st century, Moldova has made enormous progress in reducing poverty. The poverty ratio decreased from 68% in 2000 to 27% in 2004 to 11.4% in 2014 (World Bank). Poverty reduction was caused mainly by rapid growth in remittances, which are very important mainly to rural populations, and by the gradual increase of pensions.

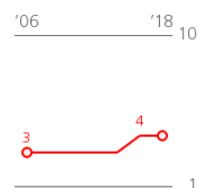
Despite the general success in poverty reduction, a huge imbalance between urban and rural areas persists. Rural poverty stands at 19% compared to urban poverty at 5% (World Bank). Additionally, the access of residents in urban areas to public services, such as health care, sanitation and quality education, is limited. The situation of pensioners is very bad as 89% of pensioners declare that their income is either insufficient to cover basic needs or allows them to cover only strictly necessary expenses (BOP, April 2016). Moldova's GINI Index score of 26.8 is very good but does not reflect the gap between urban and rural areas.

In Gender Inequality Index (included in 2015 UNDP Human Development Report), Moldova ranked 50 out of 155 countries and scored 0.248 points, which shows a

Question
Score

Socioeconomic
barriers

4



visible improvement compared to previous years. However, this result is higher than in the Ukraine or Romania and the gender gap still remains an important issue. The participation of women in the labor market is lower than man. Also, women's wages and pensions are significantly less than for men, and women are also underrepresented in the public offices.

Ethnic and language minorities face problems accessing public services. For around 25% of the population Romanian language is not native. At the same time, in regions where non-Romanian groups dominate, such as Gagauzia, the quality of Romanian-language teaching remains low. The inability to speak and write in the country's official language creates a substantial barrier for minorities.

According to the UNDP's Human Development Index, Moldova has scored roughly the same number of points since its independence (0.652 in 1990, 0.693 in 2015), which in practice means that the standard of living in Moldova has not improved in any significant way during that period.

Economic indicators		2013	2014	2015	2016
GDP	\$ M	7985.3	7983.3	6512.9	6749.5
GDP growth	%	9.4	4.8	-0.4	4.1
Inflation (CPI)	%	4.6	5.1	9.7	-
Unemployment	%	5.1	3.9	4.9	5.0
Foreign direct investment	% of GDP	3.6	4.4	3.6	1.8
Export growth	%	9.6	1.0	2.9	8.8
Import growth	%	4.4	0.4	-4.7	5.9
Current account balance	\$ M	-516.5	-569.1	-414.8	-276.6
Public debt	% of GDP	29.6	36.0	44.8	43.2
External debt	\$ M	6559.8	6568.7	6345.4	6594.7
Total debt service	\$ M	673.8	593.2	426.1	434.3

Economic indicators		2013	2014	2015	2016
Net lending/borrowing	% of GDP	-1.7	-1.6	-1.9	-
Tax revenue	% of GDP	18.4	19.8	19.5	-
Government consumption	% of GDP	20.2	19.9	20.5	19.0
Public education spending	% of GDP	-	7.5	-	-
Public health spending	% of GDP	5.0	5.3	-	-
R&D expenditure	% of GDP	0.4	0.4	0.4	-
Military expenditure	% of GDP	0.3	0.3	0.4	0.4

Sources (as of October 2017): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

7 | Organization of the Market and Competition

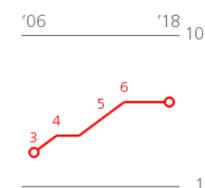
The institutional and legal framework for market-based competition in Moldova is strong due largely to reforms related to the implementation of the Association Agreement and Deep and Comprehensive Free Trade Agreement (DCFTA) with the European Union. Prices are generally liberalized and the government regulates only the prices of a few, socially important products. Also, certain tariffs (such as energy and fuels) are controlled by the state regulatory bodies. The tariff situation is stable. Since 2005, Moldova has scored 4 (on a scale from 1 to 4+) in the price liberalization rating conducted by the European Bank for Reconstruction and Development (EBRD). The Moldovan currency, the leu, is fully convertible and enterprises do not face problems with currency exchange.

In recent years, Moldova has been successful in eliminating market-entry barriers. In the World Bank's Doing Business Report 2017, Moldova ranked 44 out of 190 countries in the category for starting a business, which mean Moldova that has a better score than many EU member states. In comparison, in 2013 Moldova rank 92 out of 185 countries. The exit barriers are also lower than several years ago, but remain moderate. According to Doing Business Report 2017, Moldova ranked 60 for resolving insolvencies, which is comparable to its rating in 2016. Over recent years, the authorities have managed to improve the insolvency system by, among other things, introducing a licensing system for insolvency administrators and establishing supervisory bodies to regulate the profession of insolvency administrators.

Unfortunately, the informal sector remains a key problem for the Moldovan economy. According to the Economic Council under the prime minister of Moldova, the grey economy accounts for up to 82% of all economic activities in certain branches. More than 50% of the work force is employed in the informal economy.

Market-based competition

6



Also, the security of investments is jeopardized by cases of so-called raider attacks (hostile takeovers of assets) when a majority shareholding in a company is illegally acquired on the basis of a corrupt judicial decision. Additionally, the significant involvement of political class in the business activities and strong influence of business tycoons on the political decision-makers still distorts free market-based competition.

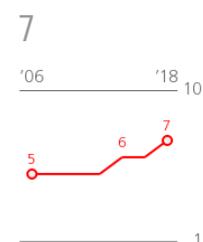
In July 2012, after a long process of drafting and consultations, the Moldovan parliament adopted the new law on competition in accordance with EU standards. New regulations began to be applied in 2012 and its last provisions came into force at the beginning of 2015. Among other things, the act prohibits any common actions or associations of undertakings that would distort market competition. Under the new law, unfair competition claims are considered by the Competition Council, a newly established de jure independent authority that reports to the parliament of Moldova. In the course of an investigation, if the Competition Council would find out that an act of unfair competition occurred, it can impose a fine on the infringer in the amount of 0.5% of its annual turnover in the previous financial year. Fines of up to 4% of the annual turnover can be imposed for serious violations of the law on competitions (such as formation of hard-core cartels). Council activity and effectiveness is increasing each year. For example, in May 2016, six companies that are responsible for supplying Moldovan medical institutions with medications were fined in the sum of MDL 17 million (about \$880,000) for abusing their dominant market position.

However, the situation with regard to the anti-monopoly policy is improving, members of influential political and business circles in Moldova are still widely engaged in different non-transparent economic activities. It is not uncommon for Moldovan tycoons to attempt to monopolize economic sectors or take control over the import of certain goods.

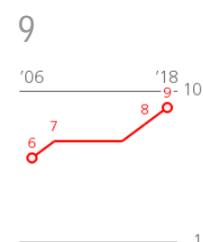
The foreign trade regime in Moldova is fairly liberal. Since its accession to the WTO in 2001, the Republic of Moldova has been strongly committed to the multilateral trading system. The Republic of Moldova's use of non-tariff barriers is very narrow. Existing licensing requirements are limited to certain goods such as alcoholic and tobacco products, and fertilizers. There were only a few cases when Moldova applied safeguard measures in order to protect the local market. Recently, in spring 2016, temporary restrictions were applied to meat and dairy products, and cement imported from Ukraine, but they were removed at the beginning of 2017. Exports of goods and services made up about 43% of the country's GDP, while imports constituted about 74% (World Bank, 2015).

In June 2014, Moldova signed the Association Agreement (along with the DCFTA) with the European Union. The provisional implementation of the Association Agreement regulations started on September 1, 2014. In July 2016, the agreement fully entered into force. Additionally, in December 2015, the European Union decided to extend the application of DCFTA (however on slightly different basis) to

Anti-monopoly policy



Liberalization of foreign trade

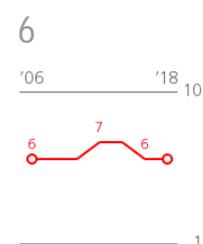


Transnistria. In reaction to the deepening of Moldovan integration with EU markets, Russia imposed severe restriction on certain Moldovan products. In September 2013, Russia closed its market for Moldovan alcoholic beverages, and extended restrictions to processed meat and most fruits in July 2014. In addition, Russia canceled its zero-rate customs duty on key products as wine, meat and apples. Implementation of DCFTA and the Russian trade restrictions changed the structure of Moldovan trade. Between January and November 2016, the share of exports to EU member states as a percentage of total exports increased to almost 65% (in comparison to 47% in 2013). At the same time, the share of CIS states decreased to 20.6% in comparison to 38% in 2013. In 2013, exports to Russia constituted 26% of total Moldovan exports, but in 2015 it dropped to about 12%, while the share of exports to Romania increased from 17% in 2013 to 23% in 2015. In 2014, Romania replaced Russia as the main destination for Moldovan exports.

Over the last two years, the situation in the banking system was directly shaped by the aftermath of the large-scale fraud which took place at the end of 2014. Due to the liquidation of three banks involved in the scandal (Banca de Economii, Banca Sociala and Unibank), the sector's assets dropped by about 34% in October 2015 (in comparison to September 2015) and totaled MDL 69.3 billion. In the second half of 2015, the condition of banking sector started to gradually stabilize. The share of nonperforming loans decreased from almost 16% in August 2015 to 11.7% in 2016, but has since risen again. At the end of 2016, the share of nonperforming loans had again reached 16%. This upward trend was the result of the requirements issued by the National Bank of Moldova (NBM) on the reclassification of loans made by banks under closer supervision (see below). The capital adequacy ratio fell after 2014 from about 20% to about 13% in December 2015, before rising to 26% (10 percentage points over the imposed limit). By the end of 2016, it had increased to over 30%.

To avoid a new scandal, the NBM established in June 2015 special supervision over three banks whose holdings total almost 65% of the whole banking sector assets (Moldova Agroindbank, Moldindconbank and Victoriabank). These banks were criticized for a lack of transparency regarding ownership, large exposures to some clients, lending to political parties and a rising share of nonperforming loans. Also, several times in 2016, the NBM used its prerogatives to oblige bank shareholders, who violated legislation to acquire their shares, to sell their assets. With the support of foreign partner authorities, Chisinau and the NBM initiated a comprehensive reform process in the banking sector (both in the central bank and commercial bank sectors). In April 2015, the Moldovan government adopted an amendment to the Law of Financial Institutions, which prohibits any quota holder of a bank's capital to offer bank shares as contribution to the capital of a company. Unfortunately, despite ambitious plans, Moldovan banks still do not comply with Basel II and Basel III requirements.

Banking system



However, transparency in the banking sector and its stability is improving, although the sector still remains at risk due to the rent-seeking of political elites, which are in control of certain part of assets in banking sector or fights to increase their shares. According to the Bank Shareholders' Transparency Rating conducted in August 2016 by Expert Group, 7 out of 11 Moldovan banks scored 5 or 4 (very high or high level of transparency), while only one scored below 3 points (average level of transparency).

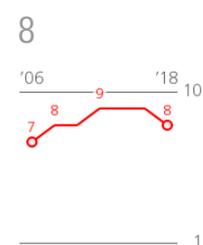
8 | Currency and Price Stability

Inflation in Moldova decelerated significantly in 2016. According the Moldovan National Bureau of Statistics annual inflation for the 12 months ending in December 2016 was 2.4% in comparison to 9.7% in 2015 (World Bank). The 2016 inflation rate was well below the central bank's target range of $5\% \pm 1.5\%$. The sharp fall in inflation was related to the stabilization of the Moldovan currency (leu) after its substantial depreciation between 2014 and 2015, and slowdown in international food and energy prices. Due to the reduction of inflationary pressures, the NBM loosened its tight monetary policy and started rebuilding its international reserves. Also, deceleration of inflation convinced the NBM to reduce the base rate from 19.5% in September 2015 to 9% in October 2016. The reserve requirement on leu deposits remains at the record high level of 35%. As short-term inflationary risks remain rather low, the inflation rate in 2017 is expected to decelerate further and should stabilize below the 5% level.

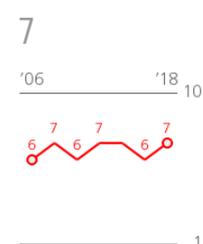
Despite the generally high effectiveness of the NBM, its political independence remains a key problem. Each head of the central bank is usually unofficially affiliated, related or loyal to the business and political elites. Though proper legislation aimed at increasing the independence of the NBM has been adopted, it is hard to assess its effectiveness at the current point.

The macroeconomic situation in Moldova has deteriorated since 2014. The banking scandal, Russian trade restrictions, recession in Ukraine and Russia, a decrease in remittances (which amount to 25% of GDP) and the unstable geopolitical situation largely influenced Moldovan economy and damaged the image of Moldova in the eyes of foreign investors. Traditional problems such as corruption and a lack of transparency hampered the situation. Public debt continued to increase rapidly. In 2015, it amounted to 41.5% of GDP, in comparison to 31.4% of GDP in 2014 and 23.8% of GDP in 2013. External debt in 2015 for the first time in modern Moldovan history exceeded 100% of the country's GDP (in comparison to 85.8% of GDP in 2014). However, the rise in the debt indicators (both public and external) was caused rather by the significant reduction of Moldovan GDP in 2015 and not by the nominal increase in liabilities. Total foreign currency reserves also decreased in the period between 2013 and 2015, mostly due to the numerous interventions in the currency

Anti-inflation /
forex policy



Macrostability



market and banking sector which National Bank of Moldova was forced to undertake. In 2015, total foreign currency reserves dropped to \$1.76 billion in comparison to \$2.16 billion in 2014 and \$2.82 billion in 2013.

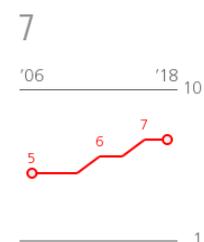
The macroeconomic situation began to normalize and even improve in the 2016. It was related to the stabilization of the political situation in the country and resumption of external financial assistance (in the second half of 2016), and in particular the signing of a new credit agreement with the IMF. As a result, foreign currency reserves increased in 2016 by 26% to about \$2.2 billion, which is equivalent to six and a half months of imports. Resumption of external financing also allowed authorities to increase the planned budget deficit for 2016 which equals 3.2% of GDP. (In 2015, the planned budget deficit amounted to 2.2% of GDP).

9 | Private Property

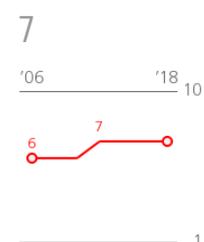
The right to private property is guaranteed by the Moldovan constitution and a number of other legal acts (such as the law on property). In reality, however, the rights of the owners are often repeatedly challenged by so-called raider attacks, where a majority stake in a company is illegally acquired on the basis of a corrupt judicial decision. Corporate raiding has been made possible due to loopholes in Moldovan law and high levels of corruption among local judges. According to the 2016 Index of Economic Freedom (published by the Wall Street Journal and The Heritage Foundation), Moldova scored 40 points in terms of property rights and was assessed as “Restricted.” Raider attacks used to happen very often in the 1990s and early 2000s. However, the scale of this phenomenon has diminished significantly, although opaque acquisitions of shares still occur in the Moldovan banking sector. In order to prevent such situations in 2013 to 2014, the government decided to amend the existing law on financial institutions. According to the amended law, the acquisition of 1% or more of the total bank’s shares requires prior permission from the NBM. However, while the amended law should be perceived as a step in the right direction, the law can be politically manipulated due to the lack of NBM independence. It is suspected that the law is already being manipulated by senior political and business actors in Moldova in order to block access to the Moldovan banking sector for rivals. An additional problem concerns the enforcement of intellectual property rights in Moldova, despite the existence of firm legal framework in this field.

The rights of entrepreneurs in Moldova are protected by law. The business climate for private entrepreneurs in Moldova is improving, among other things, due to the implementation of the DCFTA. According to Doing Business 2017 report prepared by World Bank, Moldova scored 72.75 points and ranked 44 out of 190 countries in comparison to 66.6 points and ranked 63 in 2015. However, the situation of private enterprises in Moldova is improving, although state-owned enterprises (SOE) still have an advantage over them. SOEs are generally better positioned to influence

Property rights



Private enterprise



decision-makers (government representatives usually sit on SOE boards) and sometimes use this advantage to prevent open competition with rival private sector enterprises. Moreover, some SOEs enjoy additional protection from the authorities because they serve as illegal sources of income for the political elite.

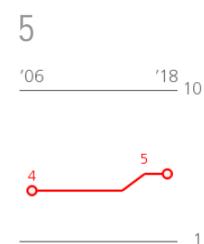
According to Moldovan legislation, the state treats SOEs and private enterprises equally. However, according to the Law on Entrepreneurship and Enterprises certain activities are restricted solely to state enterprises (such as, among others, human and medical research, manufacture of orders and medals, postal services). Position of private companies toward SOEs is improving as the government gradually privatizes state assets. Some large enterprises (such as state airline Air Moldova, telephone operator Moldtelecom and the state railway company) are still controlled by the government but should be privatized soon according to the government statements. Unfortunately, the privatization of SOEs does not always proceed consistently with market principles and opaque tenders remain a problematic issue.

10 | Welfare Regime

The efficiency of the Moldovan social assistance system is still very limited due to the bad financial condition of the country. Additionally, equal distribution of welfare still remains an important problem. Certain categories of citizens (judges, civil servants, members of parliament) are privileged with special pension terms such as lower retirement age. Proper targeting of assistance also remains a problem. However, the system has undergone a number of reforms in the last decade, as its effectiveness continues to be low and certain welfare institutions still operate based on the Soviet model. Public health care remains extremely under-financed and most of the population is forced to use their private funds in order to receive proper care. Additionally, this factor fosters corruption among medical personnel. The pension system, which is already inefficient, is on the verge of collapse due to an aging population. The proportion of elderly people has increased from 13.6% of the total population in 2005 to 16.2% in 2015. Government spending on pensions is constantly rising. In 1999, spending on pensions constituted only about 5% of total GDP, but this has increased to almost 8% in 2015. The inefficiency of the system is reflected in the low pension payment, which (on average) does not exceed \$65 per month (about \$10 less than the Moldovan subsistence minimum). In 2017, a reform of the pension system (which includes an increase in the retirement age) is expected. The level of unemployment benefits is also inadequate and matches the average pension payment.

In view of the inefficiency of social safety nets, remittances from relatives working abroad remain the only effective support for many Moldovans (especially in rural areas).

Social safety nets



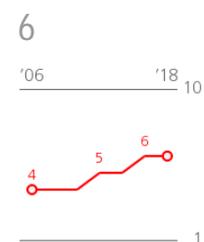
Over last few years, the legal framework for fighting discrimination in Moldova has improved. In 2012, the Moldovan parliament adopted the Law on Equal Opportunities, which created the legal basis for the fight against discrimination in various spheres of life - inter alia, political, economic and social. The new law prohibits discrimination based on race, language, religion, sex, political views, disability and sexual orientation. Additionally, in 2013, the Anti-Discrimination Council which collects, examines and analyses complaints about alleged acts of discrimination was created. Unfortunately, the institution can register cases of discrimination, but cannot apply sanctions against offenders which limits its effectiveness. Despite legislative changes, the level of inequality in Moldova remains relatively high. Women remain underrepresented in public offices. In 2015, women accounted for only 20.7% of all members of parliament. In 2016, only 24% of all ministers and about 20% of deputy ministers in the Pavel Filip government were women. Despite the fact that women represented 52% of the total population, women account for 48.5% of the total labor force. Access to education for women and girls in Moldova is generally good. The ratio of female to male enrollment equals 1.0 in primary and secondary schools. There are, however, significant concerns in respect to the equality of participation due to de facto gender segregation across subject areas such as math. The adult literacy rate is 99.2% overall, but is slightly higher for men (99.4%) than women (99.1%). The gross enrollment ratio is relatively low and equals 93.1% (primary education) and 87.3% (secondary).

In a study conducted by the WHO in 2015, a large share of respondents considered that people with disabilities face discrimination in employment, education, political life and interacting with the state. Additionally, in respect of discrimination on the basis of ethnicity reports show that Roma people are the ethnic group exposed to discrimination in Moldova. Also, LGBT people, people living with HIV and tuberculosis, and people suffering from mental health illnesses are perceived as socially stigmatized, which sometimes legitimizes ill-treatment by the authorities.

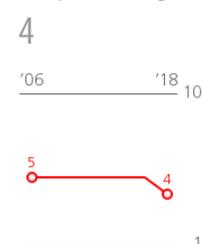
11 | Economic Performance

In 2015, the Moldovan economy (already one of the weakest and smallest in Europe) was hit by its biggest decline in GDP since independence. However, GDP per capita (PPP) remained practically on the same level as the year before (+0.6%), while overall GDP dropped by 18% (from almost \$8 billion in 2014 to around \$6.5 billion in 2015). Several factors were responsible for the deterioration in the economic situation. First, the total value of exports declined by 15.9% between 2014 and 2015. This was affected by the significant drop in exports to the post-Soviet states (down by 33%), especially to Russia (down by 43.2%), which had been the main recipient of Moldovan exports before 2014, and Ukraine (down by 58%). Trade with Russia decreased mainly due to the embargo on Moldovan products imposed by Russia in 2013 and 2014. The crisis was additionally fueled by the deep depreciation of the

Equal opportunity



Output strength



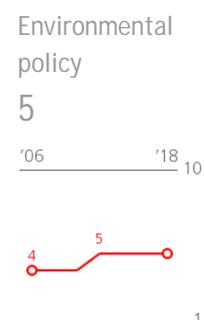
Russian ruble and the Ukrainian hryvnia, which reduced demand for imports in Russia and Ukraine. The DCFTA deal with the European Union, which provisionally entered into force on September 1, 2014, did not compensate for the losses on the Russian market. Total exports to the European Union actually decreased by 2.3% in 2015 and increased only by 1.7% in the first three quarters of 2016. Internal consumption was also limited, due to – among other things – a decline in remittances from Moldovan emigrants working in Russia. In 2015, total remittances decreased by nearly one-third from \$1.6 billion to \$1.1 billion. Additionally, the banking scandal, combined with the region’s general geopolitical situation, has also driven down the exchange rate of the Moldovan currency. The Moldovan leu lost more than 20% to the U.S. dollar in 2014 and another 26% in 2015. This negatively affected demand in Moldova and decreased the nominal level of GDP. Despite the attempts to limit the country’s dependency, Moldova remains fully reliant on Russian gas and – to some extent – on Russian electricity (produced by a Russian-owned power plant in Transnistria). The low unemployment figure (around 5%) is due to mass emigration and the country’s agricultural sector. Around 30% of the population are still employed in the agricultural sector or run independent farms. (Owners of independent farms are seen as private entrepreneurs and are not taken into account in unemployment statistics).

Public debt is on rise from 23.8% of GDP in 2013 to 31.4% in 2014 to 41.5% in 2015. In 2016, overall debt increased further mainly due to the government decision to issue \$700 million of government bonds, equivalent to around 10% of GDP, to compensate the central bank for intervening in the banking scandal. The net inflow of foreign direct investment remains moderate (4.1% of the GDP in 2015 in comparison to 4.4% in 2014). Inflation dropped sharply from 9.7% in 2015 to only 2.4% in 2016.

12 | Sustainability

In recent years, issues related to the protection of the environment became more important to the Moldovan political agenda. The legal framework improved significantly, among other things, as a result of signing of the Association Agreement which obligates authorities to promote energy efficiency and energy saving as well as the development and support of renewable energy.

The development of renewable energy sources (RES) is perceived by Moldovan authorities not only as a way to improve the condition of the environment but also as an element of a broader strategy aimed at diversifying Moldova’s energy supply. Currently, Moldova is fully dependent on supplies of Russian gas. It also imports about 70% to 80% of its electricity. According to the National Energy Regulatory Agency of the Republic of Moldova (ANRE), the total amount of electricity produced from renewable sources and sent to distribution networks increased by over 500% in 2015 compared to 2014 and 900% compared to 2013. Unfortunately, despite these



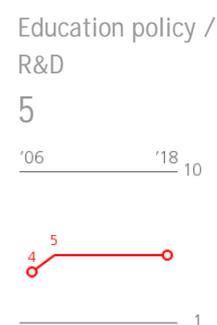
positive developments, the role of RES in the Moldovan energy mix remains marginal. The most important source of renewable energy in Moldova is biogas which accounts for 84.6% of the electricity produced from RES, but production of electricity from other sources (like wind and solar energy) is widely absent. Additionally, despite the fact that authorities are trying to support the development of RES through VAT and customs duties exemptions, Moldova does not have a reliable system of incentives that would generate a substantial transition to green energy (such as green tariff).

The quality of transmission and distribution networks for heat, natural gas and electricity is still one of the key problems. According to the Energy Strategy of Moldova 2030 adopted in 2012, approximately 70% to 75% of the equipment in the energy sector is obsolete. Fortunately, the situation is slowly improving. Losses in transmission and distribution networks for heat decreased from 22% in 2013 to 19.3% in 2015, while electricity losses dropped from between 10.5% and 12.01% (depending on the distribution company) to between 8.21% and 9.32%. According to the Energy Strategy and National Development Strategy 2020 losses in transmission networks should be reduced by up to 11% in 2020 for electricity and by 2% in 2020 for heating.

The general improvement in the environmental situation in Moldova is reflected by Environmental Performance Index. In 2016, Moldova ranked 55 out of 180 countries and scored 76.69 out of 100 points in comparison to a rank of 74 out of 178 countries and score of 53.36 in 2014.

The process of deep reform, which Moldova's education system is still undergoing, received additional impetus in the second half of 2012, with the appointment of Maia Sandu to the position of Minister of Education. Changes currently being introduced aim to adapt the Moldovan education to European standards, and increase efficiency and quality in teaching. In 2014, parliament adopted the new Education Code which envisages the modernization of the national education system (within the Bologna Process, among others) and its adjustment to European norms. The optimization of school networks which started a few years ago is still in progress. Budgetary expenditure on education in Moldova has traditionally been very high (over 8% of GDP) but the majority of funds are spent on maintaining the large number of schools (especially secondary schools). Optimization allows for the redirecting funds to other education institutions, improving their efficiency. Additionally, measures have been taken to reduce corruption in the education system. Control over exams has been radically increased which significantly limited cases of cheating. The improvement of school equipment is also noticeable. However, as the changes are still being implemented, it is too early to reliably assess the impact of the reform on the education system.

According to Global Competitive Index 2016-2017, Moldova ranked only 91 out of 138 countries for higher education and training. This reflects the poor quality of



Moldovan universities. More importantly, the same index reveals that Moldova is one of the least innovative countries, ranked 133 out of 138 countries. It is correlated with a marginal level of research and development spending, which oscillates around 0.4% of GDP.

An additional problem is the very limited competition in R&D. Most R&D funds are directed to the Academy of Sciences, an obsolete, Soviet-style institution, rather than Moldova's universities.

The Moldovan authorities are trying to improve the situation in the R&D sector using the support offered by the European Union. In 2014, Moldova became associated to Horizon 2020, an EU program designed to facilitate the mobility of scientists, strengthen national research systems and help countries integrate into the European Research Area (ERA). In 2015, a draft of National Strategy for Integration in the ERA was finalized. Moldovan activity within the Horizon 2020 program is gradually improving scientific cooperation.

Governance

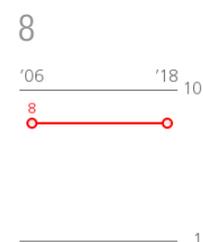
I. Level of Difficulty

One of the key structural difficulties in Moldova is the state of its economy. Since the early 1990s, Moldova has been one of the poorest countries in Europe with overall GDP of \$6.5 billion in 2015 (current U.S. dollars) or \$1,848 GDP per capita (current U.S. dollars), according to the World Bank. The Moldovan economy lacks competitive advantages, and it is not popular among foreign investors who are discouraged by corruption, a lack of transparency, an unstable political situation and certain security risks (such as, among other things, the protracted Transnistrian conflict and periodical sociopolitical tensions in Gagauz Autonomy). Extreme underinvestment in transport and energy infrastructure inherited from the Soviet Union additionally hampers economic development and deters investors. As a result, Moldova has the lowest total foreign direct investment per capita in the entire region (around \$1,010 in 2015 according to UNCTAD World Investment Report 2016). Moldova remains completely dependent on Russian gas supplies and can cover only about 20% of its electricity consumption. High emigration rates increase the phenomenon of brain drain and further constrains development. The Moldovan authorities have been totally unable to limit emigration or provide emigrants with incentives to attract them to return home. Non-professionalism among public officials is also a major problem. Many public servants are not prepared for their job accordingly, while it is difficult to hire professionals since state salaries remain low.

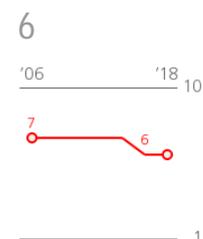
Civil society organizations in Moldova emerged and became active in the late 1980s as part of the anti-communist, reformist movements. In December 2015, according to the data of Ministry of Justice, there were more than 10,000 national-level CSOs in Moldova (about 2,500 organizations are registered in the Transnistrian region). However, only just over 2,000 CSOs have carried out any projects over the past three years.

Sustainability remains a key problem for Moldovan CSOs. The state does not support CSOs financially, and there are no partnerships between CSOs and businesses. The legal regulations regarding financing of CSOs not only did not improve recently, but even hampered their functioning. Until 2015, corporate taxpayers were able to donate up to 10% of their taxable income to CSOs, but the limit was lowered to only 2%. Additionally, donations can be deducted only if they are approved by the government.

Structural constraints



Civil society traditions



The new law, which would allow individual taxpayers to direct 2% of their total income tax to eligible organizations, remains unimplemented. Due to the lack of internal financing around 80% to 90% of CSO activity is funded from foreign sources, with the European Union and United States the largest donors.

Civil society is actively engaged in identifying problems, and in preparing and promoting policies. Unfortunately, reoccurring periods of political instability jeopardize cooperation between the government and CSOs. Due to the political crisis between 2014 and 2015, the mandate of the National Participation Council which was created in 2010 as an advisory body for the Moldovan government remained inactive during 2015 and 2016.

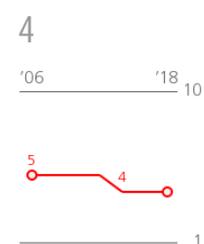
Public trust toward NGOs is very limited. Only 14.6% of Moldovans trust such organizations in “some” or “large” degree, while almost 64% don’t trust them (BOP, October 2016). On the other hand, younger generations are more trusting and generally more open to participating in the activities of NGOs.

Despite the fact that about 25% of Moldovan population consist of national minorities (primarily Ukrainians, Russians and Gagauz) ethnic tensions are minimal. The experience of the Transnistrian war in 1992 has not had a major influence on relations between people living on either side of the Dniester river. Both societies perceive themselves as practically separate nations and treat each other with moderate sympathy or indifference. Tensions can be observed only on the official political level.

Certain, yet moderate and not violent tensions result from differences in approach to the historical issues. A small proportion (10% to 20%) of the population considers Moldovans to be a part of the Romanian nation, and advocates for the reunification of Moldova and Romania. Many (about 40%) Moldovans acknowledge the Romanian cultural identity of their nation but at the same favor the idea of an independent Moldovan state. Both groups are however pro-Western. Others (including Russian-speaking minorities) claim that Moldovans are a separate nation with a distinct culture and even language (Moldovan instead of Romanian). Members of this group are usually pro-Russian in their views, and feel nostalgic for the USSR. Those differences are polarizing the population over the issue of Moldova’s geopolitical affiliation. Russian media (which is very popular in Moldova) and certain politicians (such as Igor Dodon) are utilizing these differences for propaganda purposes which creates additional tensions in society and further increases its west-east polarization.

Different views on history, identity or geopolitical issues have not led to violence. They are however provoking demonstrations and political conflicts. The issue of language and identity is also one of the key factors which regularly generates tensions between Chisinau and the pro-Russian autonomous region of Gagauzia.

Conflict intensity



II. Governance Performance

14 | Steering Capability

The rise to power of the pro-Western opposition in 2009 inspired hopes that the system created by the communists (2001-2009) would be democratized and that Moldova would undergo a structural reconstruction. Unfortunately, with every successive year of the new coalition government's rule it has become clearer that the leaders of its member parties are not interested in dismantling the old system, but rather in taking it over and using it to their own benefit. As a result, the declared long-term political priorities were often subordinated to the rivalry between the major political and business circles in the country. Despite five years of rule by a coalition government composed of pro-European parties, the country has not been subject to any structural reconstruction concerning how the state institutions operate.

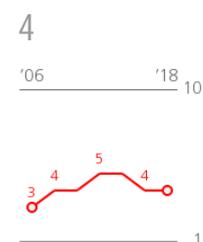
Since the end of 2015, tensions related to the rivalry of different political and business camps eased as political and business power concentrated in the hands of Vlad Plahotniuc. However, while Vlad Plahotniuc declares himself a firm pro-European politician, he is not interested in a structural transformation of the country, as his power and position depends directly on his control of the state apparatus and financial flows in Moldova. Therefore, it should be expected, that official political priorities will remain largely rhetorical. The widely declared process of EU integration is additionally hampered by the actions and narrative of openly pro-Russian President Igor Dodon. Currently, the pro-European opposition, civil society and media are too weak to be considered reform drivers and able to oppose the status quo.

Another threat to the stability of the strategic priorities is the significant polarization of Moldovan society, half of which is in favor of EU integration while the second half advocates for rapprochement with Russia's integration project, the Eurasian Economic Union. In the event of a transfer of power to pro-Russian parties, a partial reorientation of Moldovan politics and change the current priorities should be expected.

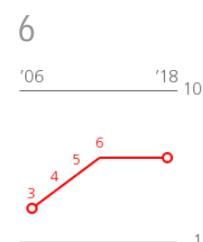
The capacity of government to implement its own policies is conditioned to a large extent by the political and business interests of the rent-seeking ruling elites. Reforms that do not seek to – among other things – depoliticize state institutions (such as the judiciary) or do not limit access to state finances (which serves as a source of illegal income) are usually implemented quickly. For example, educational reforms were successfully carried out in recent years because it did not challenge the interests of the elites. Also, the implementation of Visa Liberalization Action Plan (VLAP) was conducted rather swiftly. However, the authorities had a clear problem with the

Question
Score

Prioritization



Implementation



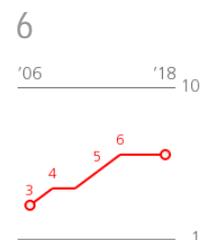
implementation of anti-corruption regulations (which threatened to undermine their power) included in the VLAP. In the end, the government managed to meet all VLAP requirements and, on April 28, 2014, the European Union introduced the visa-free regime for Moldovan citizens (for travel of up to three months). The implementation of VLAP – which was long awaited by the majority of Moldovan population – showed that Moldovan authorities can be very efficient in the implementation of policies that provide them with electoral support without threatening their power-base. On the other hand, the Moldovan government proved on several occasions that it is able to push through unpopular, but necessary policies. In 2016, in just few months, the authorities managed to adopt a set of new regulations (partially unpopular) required by the IMF in order to sign a new financial agreement with Moldova, which was crucial to maintaining fiscal stability in Moldova.

In general, it should be stressed that internal reform drivers in Moldova are very weak whether civil society, media or other groups. The most powerful reform drivers are development partners, especially the European Union and to some extent the United States.

Policy learning in Moldova has improved over recent years. However, mid-level civil servants remain underpaid and poorly motivated, while their competences are clearly rising due to – among other things – the support of external partners (especially European Union). Additionally, more and more people originating from civil society are employed in the public administration. The quality of staff is improving due to the influx of young specialists, educated in the West. As a result, civil servants are increasingly more open to external expertise (coming from both academia and civil society). This is very important because, due to the lack of financial resources or staff, not all state institutions are producing informative analytical reports regarding their activities. In such a situation policy papers and analysis provided by NGOs (usually thanks to the financial support of development partners) or the academic community are an essential source of expertise, which is necessary for proper policy learning.

For several years, the development of policy learning was undermined by tensions between the ruling, pro-European parties. Control over state institutions and ministries is distributed along political lines which causes rivalry within the state apparatus. This limits the government's ability to adapt to and take advantage of developmental opportunities. Paradoxically, however, this problem began to lose its importance with the increasing subordination of the state apparatus to the oligarch Vlad Plahotniuc. Elimination of his main political and business opponent, Vlad Filat, and the subjugation of the coalition government parties limited the tensions within the ruling camp.

Policy learning



15 | Resource Efficiency

The quality and capacity of civil servants – especially middle-management – have improved visibly since 2009. First, positive change was possible due to the financial and technical support from external partners, especially the European Union. Second, a significant number of young people, often educated abroad, decided to pursue a career in public service in Moldova, encouraged by the victory of the pro-European parties in the 2009 elections. Additionally, the civil service was further improved due to the influx of well-trained specialists from civil society.

Unfortunately, any further increases in the capacity of public administration is suppressed by several factors. Salaries of the low and middle level state bureaucrats are very low which does not stimulate efficiency or encourage well-trained employees to keep their positions. Moreover, low wages provide incentives for corruption. Also, recruiting procedures are still far from transparent. Nepotism is common, especially in local administration outside of Chisinau. However, while lower-level positions in the civil service are rather depoliticized, the proper political affiliation and loyalty is necessary for those who want to take a higher office. It is typical to change particular officials for political reasons. Competitive recruiting procedures exist, but they are rarely properly applied and therefore do not protect state institutions from politicization.

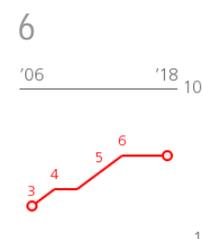
Local administration reform, which increases the financial independence of regions, was only introduced in 2015 and the results are yet to be seen. However, formally local authorities can now retain a greater portion of taxes collected on their territory, although their autonomy from the capital is still limited due to the informal, corrupt dependence on central authorities and business circles.

According to the annual audits carried out by the Court of Accounts, budget resources are extensively misused. Additionally, state institutions are rather unwilling to implement the recommendations received from the court in order to improve the situation. The assessments of budgetary expenditures are in general not performed properly.

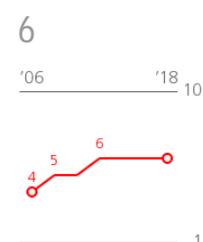
On the technical level, policy coordination is conducted by different state institutions, commissions and specialized task forces. Sector Coordination Councils have been established under all ministries and other central authorities. Additionally, the State Chancellery plays an important role in resolving possible difficulties in the process of policy coordination (regarding the division of competences, among other things).

Since the end of 2015, the Moldovan political scene has been dominated by the richest and most powerful oligarch, Vlad Plahotniuc, who directly controls the most important positions in the state such as prime minister, government and speaker of parliament. With such vast influence over the state apparatus, Plahotniuc is a key

Efficient use of assets



Policy coordination

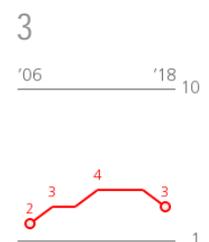


decision-maker in Moldovan politics. Since 2016, he has also officially been known as the “executive coordinator of the ruling coalition.” However, this position is very unclear and lacks legal foundations, Plahotniuc is using it to legitimize and formalize his official meetings with the coalition partners and foreign delegations. In general, the current system of policy coordination can be described as centralized and personalized, and to a large extent based on informal networks. Plahotniuc tends to use different instruments, incentives and allegedly intimidation to encourage or force his political partners to adopt his preferred political decisions. Despite the fact that the consolidation of power by Plahotniuc has had a negative effect on the modernization and democratization of the Moldovan state, it has improved the effectiveness of policy coordination.

Anti-corruption has been the declared priority of the government since 2009. However, despite many declarations, and tremendous financial and technical assistance offered by external partners, the enforcement by government agencies has been insufficient in containing corruption. Institutions, which are designed to fight with this phenomenon (such as the National Anti-Corruption Center), are highly politicized. This not only limits their ability to prosecute politicians, but also turns them into a tool used by the authorities to fight political and business competitors. In 2016, a number of low and mid-level public servants (including judges, police officers and custom officers) were arrested on corruption charges. However, this was not the result of improved effectiveness in anti-corruption structures, but an effect of the political decisions of widely discredited authorities, seeking popular support and external legitimacy. Additionally, the authorities regularly try to limit the access of media to information which would allow to reveal the corruption within public administration. Refusal to provide investigative journalists with certain data concerning property of public officials is often justified by the law on protection of personal data.

The framework for anti-corruption measures in the country is outlined in the National Anti-Corruption Strategy for 2011–2016. Unfortunately, the documents lack clear indicators of periods for fulfillment and do not provide concrete financial sources for the implementation of strategy, which further undermines its effectiveness. As a result, civil society actors monitoring the implementation of the strategy assess the progress in this field as rather modest. The long-awaited law on party financing was finally adopted in 2015, but the final version is softer than the original draft and may be not efficient in containing the phenomenon of instrumentalization of political parties by business tycoons. On the other hand, the presidential elections at the end of 2016 showed that their electoral spending became relatively more transparent – in spite of the fact that the parties remained under the full control of certain political and business actors. Another visible positive change was the fact that since 2016 political parties have received donations from state budget (in proportion to the number of votes), which may in time increase their independence.

Anti-corruption
policy



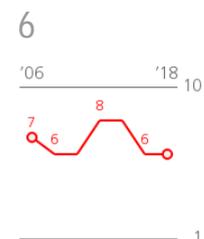
16 | Consensus-Building

There is a general consensus among all significant political actors in Moldova on the democratic system of government. The ruling political groups in Chisinau regularly refer to pro-democratic values and rhetoric, regardless of their ideological affiliation. Unfortunately, as the political class in Moldova is generally inefficient and highly corrupt, the perception of the liberal democratic model (praised by senior politicians) in the Moldovan society is becoming worse. 57% of Moldovans declare that their economic wellbeing is more important for them than the democratic system of government (IRI, March 2016). Rising disillusionment with democracy increases popular support for authoritarian rule, which is perceived as the only efficient way to eradicate corruption and improve the situation of ordinary citizens. That's why Vladimir Putin for many years now has been the most popular politician in Moldova – 67% of population state that they trust him (BOP, October 2016). For the same reason, Renato Usatfi has been one of the most popular Moldovan politicians during the past years – he advocated for the introduction of a Belarus-style regime in Moldova. However, the majority of Moldovans still value the democratic model of power, although the rise in sympathy for a strong head of state is alarming.

All key political parties and mainstream politicians – both left and right-wing – accept the market economy as a foundation for the modern Moldovan state. Although Moldovan communists and (to a lesser extent) socialists sometimes use anti-capitalist rhetoric, they do it only for electoral purposes, while in practice they favor free market economy. At the same time, however, leading business and political circles (connected to the mainstream parties) regularly use their influence and position to protect their interests. This includes activities, which limit the degree of free market activities, such as blocking business competition or even hostile takeovers of competitive companies (through so-called raider attacks). While the political elite agree on the idea of free market there is no consensus with regard to the proper economic model among the Moldovan population. Despite the reforms introduced over the last 25 years, the better part of the Moldovan population still lives below the standard of living known from the communist times. As a result, 59% of the Moldovans (IRI, March 2016) declare a certain nostalgia for the Soviet state and claim that the dissolution of Soviet Union was a bad thing. This sentiment and dissatisfaction with the recent economic reforms in Moldova is one of the causes of the rise in support for the Russian-led Eurasian Economic Union, which is perceived by a number of Moldovans as the successor to the USSR.

There are no anti-democratic actors in the mainstream of Moldovan political life. Both parliamentary and key non-parliamentary parties express a devotion to democratic norms and values. Their leaders also declare a commitment for further reforms aimed at strengthening democracy in Moldova. Unfortunately, influential political and business groups remain the key obstacle to further democratization in

Consensus on goals



Anti-democratic actors

6

Moldova. Their influence on the legislature, executive and judiciary limits the efficiency of the democratic institutions, undermines the balance of power, and makes the authorities to work in their interest and not in the interest of the population. As their influence on state institutions is a key element which allows these groups to protect their interest and security, it would be very hard to induce them to comply with constitutional rules. Additionally, the population of Moldova favors a higher standard of living than currently provided under Moldova's democratic system. Only about 35% of the overall population (IRI, March 2016) stated that democracy is more important than economic prosperity (this option was supported by 47% of respondents).

Moldovan society is traditionally divided over the issues of history, identity, certain national symbols, values and even the name of the language. There are also different opinions as to whether the state should continue to exist or reunite with Romania. While the number of supporters for reunification is small (estimated 10% to 20%), the topic causes strong emotions among Moldovans. Additionally, the population is very strongly polarized over Moldova's geopolitical alignment (pro-Russian or pro-European). Unfortunately, the local political class does not try to depolarize society and establish a broad consensus across the dividing lines. On the contrary, the ideology of Moldovan political parties reflects social divisions, and certain political leaders fuel and exploit existing cleavages in order to mobilize support. This is deepening the disagreements, and seriously impairs public debate in Moldova by effectively suppressing any deeper reflection about the nature of the state and necessary reforms. Moldovan authorities also proved to be ineffective when it comes to restoring a sense of unity between societies living on the right bank of the Dniester river and Transnistria.

In recent years, positive changes can be observed in the Moldovan legislation, which increases the ability of civil society to participate in the political process. Access to state information is increasing. Since 2012, official institutions have been required to publish on their websites information about new policies, legislation, strategic documents and monitoring reports. Access to public information is free of charge. The website of each ministry has a sub-page where drafts are published for consultation which de jure ensures transparency of the decision-making process. Among other things, the applicable law requires the publication of detailed annual state budgets and expenditure statements for central and local government. Meanwhile, the Ministry of Justice has to report every year on the results of monitoring and to publish the report on its website. Civil society also enjoys the right to give opinions on drafts elaborated by the government, ministries (10-15 working days for comments) and parliament (15 days). However, in reality the timeframe is sometimes shorter, the rule is generally respected. Additionally, institutions have to explain the reasons for not accepting an opinion. In addition, legislative initiatives of the government are consulted with civil society through an online platform, www.particip.gov.md, where all drafts are published before adoption. To foster the



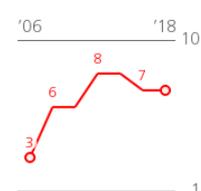
Cleavage /
conflict
management

6



Civil society
participation

7



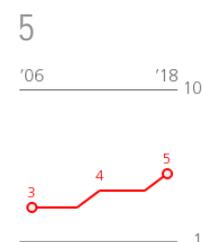
dialog with civil society, the government created in 2010 the National Participation Council (NPC), a consultative body composed of 30 civil society organization representatives selected by the government. It is also not uncommon to employ members of a CSO as advisers within ministries and other state institutions.

Unfortunately, in practice and despite a good legal base, the involvement of civil society in the political process remains limited and its influence on the policymaking process is rather small. Civil society actors still complain about problems with access to public information. Additionally, dialog between civil society and the authorities has suffered in last two years among other things due to the political crisis which started in 2015, and rising dissatisfaction with the policy of government and progress of reforms. The consultative NPC is currently not functioning, as its mandate expired in 2014 and the government was unable to select a new council. On the other hand, Moldovan civil society remains very active when it comes to monitoring of the government activities and reforms.

The key example of past injustice which still has not been fully addressed is related to the perception of the country's Soviet past. The problem lays in the lack of consensus among the Moldovan population and political class regarding this issue. Certain parts of society along with right-wing parties perceive the times when Moldova was a part of the Soviet Union as an occupation and advocates for the commemoration of the victims of the totalitarian regime. After the pro-European coalition came to power in 2009 certain steps were taken in this direction. In 2010, a provisional stone in memory of the victims of the Soviet occupation and totalitarian regime was set up in front of the House of Government and there are plans to replace it with a proper monument in the future. In 2013, a monument commemorating the people deported from the country during the times of Stalin's repression was erected in front of the Chisinau railway station. On the legal level, in 2012 the parliament of Moldova condemned the communist totalitarian regime, which sparked protests among the pro-Russian opposition. Besides such steps aimed at achieving certain moral justice, the authorities are also gradually paying financial compensations for confiscated property to the victims of communist political repressions. In 2015, the government spent almost MDL 21 million on compensation and MDL 13.6 million in 2016 with a further MDL 20 million already allocated in the budget for 2017.

As historical topics are raising tensions in the divided society, the ruling coalition government is trying rather to avoid bringing them up. For example, the Great Famine (1946-1947) which was deliberately caused in Moldova by Soviet authorities and took lives of more than 100,000 people is still widely unknown in the country (due to Soviet propaganda) and the authorities are not doing much to promote knowledge about this tragedy. The only exception is the highly pro-Romanian and anti-communist Liberal Party which regularly calls historical justice. On the other hand, the Moldovan left-wing (pro-Russian) parties regularly exploit the issue of Romanian

Reconciliation



fascism and Romanian activities on Moldovan territory during the Second World War in order to mobilize their electorate.

The Transnistrian war which took place in the beginning of 1990s remains a vivid experience only among the veterans which took direct part in the armed conflict. The majority of the population don't feel a need for retribution toward either other population groups, the authorities in Transnistria nor on the then authorities of Moldova. Yet, the pro-Russian Party of Socialists blames the pro-Romanian government, which ruled the country at the beginning of the 1990s, for the outbreak of the Transnistrian conflict.

17 | International Cooperation

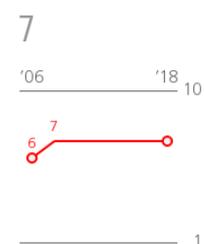
Official development aid (ODA) plays a very significant role for Moldovan state. In 2014, the influx of external assistance reached almost \$520 million, an amount that corresponds to 37% of the annual budgetary expenditures. The European Union, European financial institutions and the United States are the key donors of financial and technical assistance to Moldova (with almost 60% share in total development assistance). The European Union's technical assistance is implemented through different formats, such as TAIEX, SIGMA and Twinning. The European Union also contributes to the reforms of Moldovan institutions using the EU High Level Advice Mission, and the European Border Assistance Mission to Moldova and Ukraine.

Coordination of donor activity in Moldova is carried out by the State Chancellery with the supporting role of National Coordination Unit (NCU). Additionally, in 2011, a Joint Partnership Council was created. This is an advisory body, co-chaired by the prime minister of the Republic of Moldova, which aims to ensure the efficiency and effectiveness of the foreign assistance provided to the Republic of Moldova by international organizations and donor countries.

Despite the very high interest of foreign donors, Moldovan authorities still experience serious problems in using external support effectively. Assistance remains highly dependent on political stability, and the will to implement reforms and restructure the system. The key political parties and decision-makers are reluctant to implement comprehensive reforms, as they would affect certain political and business interests. Support is regularly misused or used ineffectively. As a result, the amount of external aid to Moldova dropped sharply in last years.

The credibility of Moldovan authorities in their relations with the international community decreased significantly over the last two years. Despite the officially expressed commitment to modernization declared by the pro-European coalition government – which has governed the country since 2009 – the government proved unable or unwilling to implement crucial reforms. Many reforms failed despite the tremendous financial support from the European Union. During just three years (from

Effective use of support



Credibility

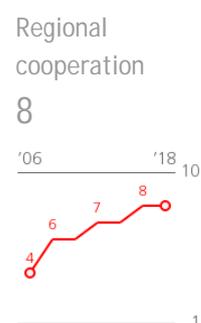
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2010 until 2013) Moldova received €50 million from the European Union, apart from funds made available under the “More for more” program. The main reason for the failure of modernization was the fact that from perspective of key politician, necessary reforms posed a threat to their political influences and business dealings. From the perspective of key international partners Moldova became a “captured state” in which the political system and economy is dominated by the oligarchic groupings. The image of Moldova was further aggravated by numerous corruption scandals (in which high-level politicians were involved) such as the embezzlement of \$1 billion from the banking system in 2014. The politicization and instrumentalization of state institutions (including the judiciary), and the persistent Transnistrian conflict reinforced the image of Moldova as an unstable and unpredictable country.

The decrease in Moldovan credibility was reflected in the reduction of financial assistance from different international organizations for Moldova in 2015. At the beginning of June 2015, the International Monetary Fund (IMF) suspended negotiations on a new loan program for Moldova (the previous program expired in 2013) and in mid-June 2015 the World Bank decided to withhold the payment of a loan worth \$45 million. Additionally, on July 5, 2015, the European Union froze its financial aid programs for Moldova worth €40 million to €50 million. Financial assistance was restored at the end of 2016 due to the implementation of certain reforms required by the IMF and fear of the collapse of the economic situation in the country. However, this did not improve the deteriorating perception of Moldova abroad.

Relations of the Moldovan government with Romania have remained very good since 2009, when the Party of Communists – which was reluctant to deepen cooperation with Bucharest – lost power to the pro-European coalition. Bilateral relations improved further after Klaus Iohannis replaced Traian Băsescu as president of Romania. Băsescu was a known supporter of Romanian-Moldovan reunification, and his frequent declarations regarding this issue regularly caused tensions between Chisinau and Bucharest. The current authorities in Moldova perceive Romania as the main advocate of the interests of Moldova in the European Union, and the biggest supporter within the European Union of Moldova’s integration. At the same time, Romania is one of the key partners of Moldova when it comes to the foreign aid. In August 2016, the Romanian government transferred to Moldova the first tranche (€60 million) of a low-interest, preferential loan totaling €150. Romania is also engaged in different development projects in Moldova. Additionally, despite the decline of confidence in 2015 toward Moldovan authorities in the European Union, Romania remained the firm supporter of the current government.

Cooperation between Moldovan and Ukrainian governments used to be rather limited for the better part of the post-soviet period. Bilateral relations intensified significantly after the “Revolution of Dignity,” change in the Ukrainian leadership, annexation of



Crimea and the outbreak of hostilities in the east of the country. Kiev – which fought Russian-supported separatist movements – begin to perceive Chisinau as a partner in terms of the Transnistria issue. A common pro-European agenda of both capitals additionally strengthened their partnership. An improvement in relations allowed the countries to make significant progress in resolving bilateral diverging issues. The protracted demarcation of borders should be finished in 2017 according to the declaration of Ukrainian officials. Kiev has also finally agreed to take steps to open the joint Moldovan-Ukrainian checkpoint on the de facto border with Transnistria. However, certain issues remain a problem, although an improvement in cooperation is very clear.

It is hard to assess to what extent the victory of Igor Dodon in the presidential elections in the end of 2016 will affect the relations of Moldova with Romania and Ukraine. Dodon is perceived very negatively in Kiev not only due to his pro-Russian views but above all for his statements that the Crimea is de facto Russian territory. He is also known for his cautious attitude toward Romania, and openly rejects the idea of common Moldo-Romanian identity or even language. This in turn traditionally causes tensions in Bucharest. On the other hand, Dodon may be helpful in improving very bad relations between Chisinau and Moscow. Relations had been deteriorating gradually over recent years due to the Moldovan pro-European aspirations and in particular efforts to sign the Association Agreement with the European Union. Igor Dodon, who made his first official trip as president to Moscow may be able to convince Russia to ease the current trade restrictions.

Moldova is a member of numerous international and regional organizations (for example CIS, OSCE, the Council of Europe, GUAM and CEFTA). Chisinau is also actively involved in the Eastern Partnership format. The cooperation between the European Union and Moldova resulted (among other things) in the signing of the Association Agreement and DCFTA with the European Union in 2014.

Strategic Outlook

The monopolization of power by one interest group needs to be addressed in order to limit corruption, unblock key structural reforms, and restore public confidence in the idea of democracy and EU integration. This issue can be resolved only with EU conditional support. Western partners of Moldova need to provide conditional support to encourage political reform. Conditional support would undermine the monopoly of the ruling oligarchic group by supporting political, economic and media competition. In this regard, depoliticization of the judiciary, which is regularly used by the ruling oligarchic group as an instrument to protect its political and business interests, is necessary. The politically dependent and corrupt judiciary have a very negative impact on the business and investment climate, as it does not provide security for private property and competition.

Despite the fact that the DCFTA entered into force in September 2014, Moldovan exporters still do not fully benefit from the opportunities offered by this agreement. This is related to a large extent to product quality, which needs to be increased. Further developments in trade with the European Union will reduce political and economic dependence of Moldova on Russia, which tends to use trade as an instrument of political pressure.

In order to limit Russia's ability to put political and economic pressure on the authorities in Chisinau, the government needs to continue its efforts to increase Moldovan energy independence. A new gas pipeline from Ungheni to Chisinau (where most gas is consumed) need to be constructed to enable supplies of Romanian gas in quantities that would cover Moldova's needs. Additionally, in order to minimize Moldova's dependence on the electricity produced in Transnistria, the long-protracted project of electricity inter-connectors between Moldova and Romania have to be put in place. In this regard, governmental support for the further development of renewable energy sources is also required. In order to protect its energy security Moldova, should also implement the third energy package.

Political groups in Moldova tend to manipulate the electorate by exploiting emotionally charged identity, linguistic or historical divisions (and the political preferences based on them). This in turn further polarizes an already partisan society and increases existing tensions. However, keeping these issues out of the political discourse is a short-term solution, in the long run it seems necessary for the Moldovan elites to push for a coherent national vision of Moldova's development capable of uniting Moldovan society. The lack of such a model renders it difficult (if not impossible) to resolve the problem of Transnistrian separatism, and ease the tensions between Chisinau and Gagauzia. As long as those two problems remain unresolved it will not be possible for Moldova to develop an effective and responsible political class or public administration, or consolidate society, develop civil society structures and instill a sense of civic responsibility.