MOLDOVA

Table 1	2020
Population, million	2.7
GDP, current US$ billion	11.9
GDP per capita, current US$	4499.4
Lower middle-income poverty rate ($3.2)[a]	0.9
Upper middle-income poverty rate ($5.5)[a]	12.8
Gini index[a]	25.7
School enrollment, primary (% gross)[b]	89.5
Life expectancy at birth, years[b]	71.8

Source: WDI, Macro Poverty Outlook, and official data.
Notes:
(a) Most recent value (2018), 2011PPPs.
(b) WDI for school enrollment (2019); life expectancy (2018).

Moldova has one of the highest COVID-19 infection- and death rates per population in Europe. COVID-19 and the recent drought have drastically worsened the outlook for Moldova with a significant recession in 2020. Beyond 2020, high uncertainty on the duration of the pandemic and its economic and social ramifications could further constrain firms, workers and households, hampering the recovery. If downside risks materialize, reduced fiscal space may limit the capacity for further countercyclical measures.

Key conditions and challenges

Despite solid economic performance in recent years, Moldova has fallen short of its aspiration to achieve faster convergence towards EU income levels. The economic model continues to be reliant on remittances-induced consumption. Declining productivity growth resulting from deep structural and governance weaknesses constitutes a key challenge. State enterprises have a significant footprint and lower productivity than the private sector, while the business environment, anticompetitive practices, and taxes distort private initiatives. The bank fraud of 2014 uncovered deep weaknesses in the financial sector.

Moldova has one of the highest COVID-19 infection and death rates per population in Europe. Despite the restrictive measures, the number of cases has been rising progressively on the back of low enforcement and compliance.

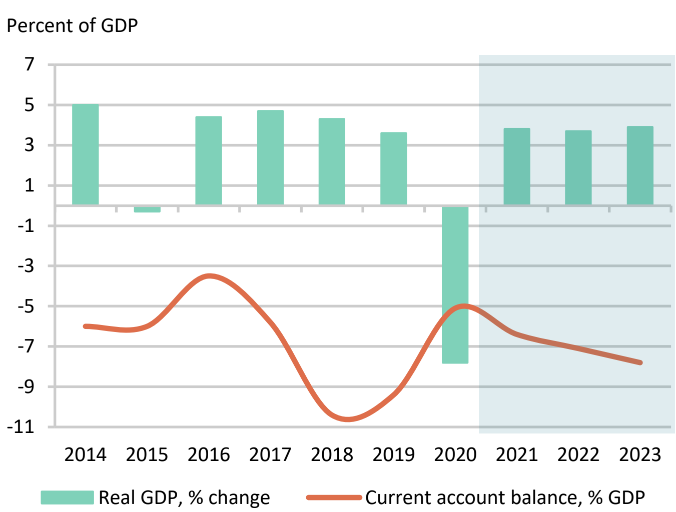
The global recession, disruptions in supply chains, measures to flatten the contagion curve, financial risk aversion, among others, are taking a heavy toll on the key components of aggregate demand. While the medium-term growth prospects remain positive, a sustained recovery hinges on the containment of the pandemic and favorable external environment. A new wave of restrictions in the country and in the main trading partners may further reduce consumer and business confidence leading to even lower remittances and exports. On the fiscal side, though the 2021 budget envisages an ambitious fiscal stimulus, it might not be enough in case of slow roll-out of vaccines and limited foreign financing. Domestic risks relate to political instability, institutional weaknesses, and political constraints to implement reforms of the judiciary and structural reforms. Fragile economic conditions and low productivity levels are exacerbated by the large footprint of the state in the economy, shrinking fiscal space, low financial intermediation and governance challenges. Additionally, as shown by the severe drought episode in 2020, the economy is highly vulnerable to extreme weather episodes.

Recent developments

The combination of the pandemic and the severe drought is expected to affect most sectors of the economy. The economic activity plummeted in 2020, with GDP declining by 7.0 percent. Primary drivers of this deceleration are households' consumption, which declined by 7 percent in 2020, and investments together with de-stocking.

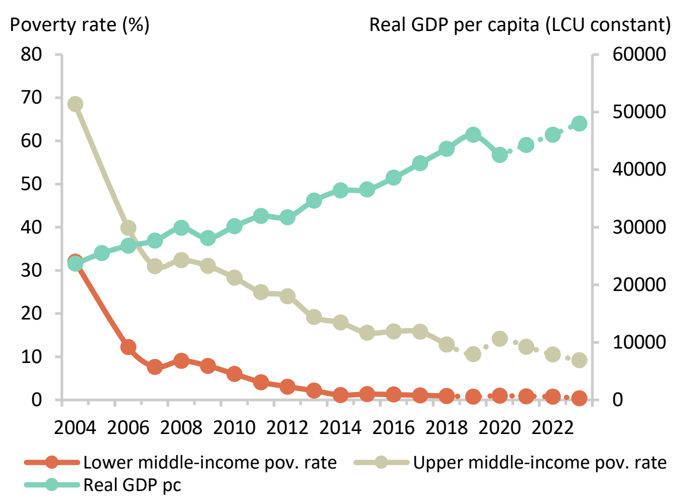
The lockdown measures have halted trade and industrial production while a severe drought has resulted in a decline in agriculture production by over 26 percent. Since the end of the lockdown, the economy has started to rebound gradually, but most of the short-term indicators remain in the negative territory.

FIGURE 1 Moldova / Actual and projected GDP growth and current account balance



Source: World Bank, based on national statistics.

FIGURE 2 Moldova / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Notes: see Table 2.

On the back of falling import prices and domestic demand, inflation has decelerated markedly in 2020, fluctuating below the lower band of the corridor of 5 percent (+/- 1.5 percent) since August. In response, the National Bank cut the prime rate 5 times to a new record low of 2.65 percent. The large import compression has led to an improvement in the current account deficit, which was mainly financed by debt instruments, predominantly public.

On this background, fiscal stance deteriorated substantially. From pre-COVID-19 level, tax revenue increased by about 0.3 pp of GDP while spending increased by 4.1 pp of GDP. As a result, the fiscal deficit reached 5.1 percent of GDP in 2020.

Employment dropped by 0.5 percent in the last quarter of 2020, with the most affected sectors being trade and hospitality, followed by agriculture and industry. Job losses, together with declining earnings, the return of the most vulnerable economic migrants, and rising food prices have led to increased strain on households' finances. As a result, poverty, as measured by the US$5.50 PPP a day, is projected to increase from an estimated 10.6 percent in 2019 to an estimated 14.2 percent in 2020.

Outlook

Uncertainties around the evolution of the pandemic will keep the economy below potential. Economic growth is expected to rebound to 3.8 percent in 2021, assuming favorable conditions thanks to the rollout of vaccines. Consumer and investment confidence are expected to improve on the back of favorable external conditions, increase in social transfers, and accommodative monetary stance. Most sectors are expected to bounce back, though the 2019 levels are estimated to be reached only in 2022. The agricultural sector is expected to rebound strongly after a bad yield in 2020. While the current account deficit is expected to have narrowed in 2020, it will gradually widen as the economy accelerates. Inflation is expected to remain lower than the target corridor of 5 percent +/- 1.5 pp in 2021-22 but to pick up as the recovery strengthens.

The authorities plan the fiscal deficit to reach 6.3 percent of GDP in 2021 and will remain higher than historical averages in the medium term due to a decline in revenues as businesses struggle and households suffer from weak job creation. Public debt is expected to increase (by 9.1 pp of GDP from pre-COVID-19 level) to 36.5 percent of GDP in 2021, while still remaining relatively low by international standards. The government faces considerable financing needs which might be difficult to meet domestically despite aggressive monetary loosening. The capacity to mitigate the impact of the crisis and support economic recovery will critically depend on external financing, particularly a successful renegotiation on an IMF program.

Under the assumption of an economic rebound in Moldova and its main migrant destination countries, poverty, as measured by the US$5.50 PPP/day poverty line, is projected to decline from 14.2 percent in 2020 to 12.3 percent in 2021. Going forward, Moldova will need to address the inequality of opportunities and accelerate private sector-driven job creation.

TABLE 2 Moldova / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
Real GDP growth, at constant market prices	4.3	3.7	-7.0	3.8	3.7	3.8
Private Consumption	4.5	3.2	-5.9	2.8	3.0	3.1
Government Consumption	-0.2	-0.5	-0.2	0.2	0.0	-0.1
Gross Fixed Capital Investment	14.5	12.9	-1.7	7.8	8.7	8.9
Exports, Goods and Services	7.2	7.3	-15.5	6.6	7.1	7.5
Imports, Goods and Services	9.7	6.7	-8.9	5.1	6.3	6.5
Real GDP growth, at constant factor prices	4.4	4.0	-7.2	3.8	3.7	3.8
Agriculture	2.6	-2.3	-26.4	10.0	5.0	7.0
Industry	8.3	7.1	-4.3	4.3	4.8	5.4
Services	3.3	4.2	-4.1	2.5	3.0	2.6
Inflation (Consumer Price Index)	3.1	4.7	4.1	4.4	5.0	5.0
Current Account Balance (% of GDP)	-10.4	-9.4	-5.5	-6.8	-7.5	-8.2
Net Foreign Direct Investment (% of GDP)	2.4	4.5	1.3	3.5	3.7	3.5
Fiscal Balance (% of GDP)	-0.8	-1.4	-5.1	-4.0	-2.8	-2.5
Debt (% of GDP)	30.1	27.4	33.5	36.0	37.3	41.4
Primary Balance (% of GDP)	0.0	-0.7	-4.3	-3.2	-2.0	-1.8
Lower middle-income poverty rate ($3.2 in 2011 PPP)[a,b]	0.9	0.7	1.0	0.8	0.7	0.4
Upper middle-income poverty rate ($5.5 in 2011 PPP)[a,b]	12.8	10.6	14.2	12.3	10.5	9.2

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.
Notes: e = estimate. f = forecast.

(a) Calculations based on ECAPOV harmonization, using 2018-HBS. Actual data: 2018. Nowcast: 2019-2020. Forecast are from 2021 to 2023.

(b) Projection using neutral distribution (2018) with pass-through = 0.87 based on GDP per capita in constant LCU.