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Summary

The most important **legal** documents, adopted during October-November are as follows: regulation for land consolidation, regulation and complimentary documents concerning the System for Animal Identification and Monitoring as well as Methodology for calculating the tariffs for passenger and luggage transportation. According to the first document, all land transactions that are conducted without public procurement bids, are not considered to be the object of land consolidation, which is a discriminatory approach.

Industry did not register significant progress, even though the monthly output rate grew by 0.4% in August and 1.5% in September. These indicators are not sufficient to overcome industrial recession registered this year. The key activities that generate the slow down are alcoholic beverage and tobacco production.

As it was expected, **agricultural** output was down in the first 3 quarters. Global production fell by 20%, because of a 32% decrease in crops yield. Several events occurred in October: controversies concerning the aid for combating the consequences of the summer drought, ending of the harvest season, discussions over the strategic document elaborated during the National Agribusiness Forum proposed scheduled for public debate in the beginning of September.

The volume of **services** continues to grow rapidly, however services delivered to the population registered a moderate growth – 4.8%. Retail sales grew by 10.7% in January-September.

Inflation was still high in October (1.6%). Prices for food had the fastest growing prices, which is a similar situation after the drought from summer of 2003. In October, inflation reached the National Bank 8-10% target. The cumulative inflation for the first 10 months constitutes 10.7%, while for the last 12 months – 14.5%. The IMF representative in Moldova is concerned with this dynamics, even though NBM applied the corresponding tools to diminish the inflation rate.

On the **labor market** companies are showing concerns for increasing the salary to their employees. In the real sector, the salary is growing strongly, increasing the gap with the state salary. State authorities expressed their intentions for creating new work places by developing small and medium business. In the meantime the risk for emigration of qualified specialists remains high.

Closer to the end of the year, it can be seen that the **state budget** is receiving higher revenues, however

expenditures are also rising. **National public budget** expenditures are increasing as well. Therefore in the first nine months of the year, the state accomplished 105.1% of the revenues planned in the budget, while the expenditures were 89.4%. The parliament has already examined and adopted the state budget project for 2008 and the Law on Mandatory Insurance Health Funds for 2008. The amount allocated for the prevention measures fund constitutes only 2% from the budget, which underestimates the importance of these measures. As of November 6, 2007 there were only 50mln lei accumulated as a result of the capital liberalization reform.

No significant changes in the **monetary policy** took place during the reference period. According to a press release issued on November 14, the NBM remains cautious concerning the situation on the market. The next day, on November 15, NB issued another important press release, according to which in the following 2-3 years the institution will start officially targeting the inflation. This regulation is the result of the changes which took place in the monetary policy for 2006-2007 (inflation became the primary concern of the NB). However there are several inflationary risks, which are not under NB control and can have a significant impact on measures taken to curb inflation.

Deposits that **local banks** accumulated in September have decreased compared to August. Legal entities deposited a smaller amount of money and as a result of a higher inflation, they prefer to purchase consumption goods, rather than deposit money. In the meantime, the average interest rate on deposits decreased to 14.87%. The volume of credits issued continues to rise. The joint IMF and World Bank visit at the beginning of October highly appreciated the trends registered in the banking sector of Moldova, where foreign investments constitute the key factor which generates this dynamics.

On the **financial market**, the decrease of the interest rate on state securities until September 2007 was curbed in October. Because of the strong inflation growth, the interest rates on state securities went up by 5pp in one month.

Monetary market, remains dependent on traditional factors for Moldovan economy (remittances from abroad and foreign direct investments), as well as global (depreciation of the US dollar against the European currency) and regional tendencies (depreciation of the US dollar against the Russian ruble). The national currency kept appreciating against the US dollar in



November, despite the measures taken by the NB to absorb in October the excess of \$70mln from the market.

The deficit of the **Foreign trade** of Republic of Moldova in September was \$1,6bn, which is 42.9% more compared to the previous year. The key export products continue to be textiles, agricultural, food and beverage products. There is a different dynamics concerning the latter group of products, mainly due to controversial trends of Moldovan wine exports. On one hand, Moldovan wineries started exporting again their products to Russia. On the other hand Romania has quality complaints against Moldovan wines, considering the products do not correspond to their standards. This is another proof that product quality has a crucial importance for promoting Moldovan exports.

Brent **oil** prices continue to rise, reaching \$90/barrel. This growth was generated by a soaring demand for oil, reduction of oil reserves and its derivatives in US, unfavorable climate conditions in the Gulf of Mexico, escalating geopolitical risks caused by conflicts in Iraq and a weaker US dollar.

The forecasts for 07/08 **wheat** harvest were revised up in October after receiving information on strong wheat harvest in Russia and Kazakhstan. Specialists forecast a strong wheat harvest in fall, due to favorable climate conditions and a growing land surface for wheat cultivation.

The US **dollar** continued to depreciate in October against the **euro**. This is the outcome of the problems American economy is facing and expectations for interest rate reduction applied by the FED. European Central Bank is also concerned with the strong euro. The big majority of analysts consider that the dollar/euro exchange rate will rise to \$1.5/€.

Russian economy grew slower in the third quarter: 6.7% against 7.9% and 7.8% in the 1st and 2nd quarters. The economic growth is generated by growing investments, construction and industrial growth. The liquidity crisis on the global market made the \$9,4bn of capital migrate from Russian economy.

Ukraine continues to register a strong economic growth: 7.3% in January-September 2007. This growth is generated by internal consumption and investment demand. Majority of analysts consider that investment demand will increase in the near future.

European Union is having a positive economic growth. However a certain industrial slow down is still applicable. Higher prices for oil, more difficult access to credits, and

appreciation of euro determine the slow industrial growth. In the meantime the inflationary risks represent the key concern for the Central European Bank. Nevertheless, majority of analysts consider that economy will strengthen in the beginning of the coming year.

Romanian economy continues to grow. Merely all sectors have a positive dynamics. However, the trade deficit continues to aggravate. It has increased by 58% in January – September. The strong national currency, high local demand for investments and consumption contributed to the increase of the trade deficit.



Regulatory Framework

There were few changes in the legal framework during October-November period. On October 2nd the Regulation concerning Land Consolidation was adopted¹. It stipulates that all expenditures for land consolidation – except from expenditures for elaborating the project– will be covered using the public funds. In the meantime – this is also a discriminating stipulation – the transactions of the legal and physical entities with land which do not fall under consolidation rules, will not be considered for privileges allocated by the state.

The Regulation on complimentary documents concerning the System for Animal Identification and Monitor was adopted in October as well². This regulation is necessary for applying in practice the law on Animal registration and identification. This is a required measure for providing a secure European food infrastructure.

The government has adopted the Methodology for calculating the tariffs for passenger and luggage transportation in the vehicles³. This methodology will be applied to all economic agents, which provide transportation services, disregarding the type of property form. The tariffs will be approved by the Ministry of Transport and Road Management. It appears that the approach used when elaborating the methodology has a centralized character. The methodology stipulates in details every regulation up to calculation of the salary. The mechanism for tariff calculation and regulation has to comprise several principles which imply determining a “reasonable” rate of profit.

Industry and Constructions

In September the industrial growth has slightly increased. In August production went up by 0.5%, while in September the growth rate was 1.5%. However due to the stagnation registered in August, the cumulative industrial growth during the three quarters was 0.6%.

The factors which contributed to this growth have not changed significantly. The growth in the mining industry continues to be small, which depends on the dynamics in the construction industry. As we

forecasted earlier, production of dairy and canned products is starting to decrease. Tobacco industry continues to stagnate due to branch problems.

Even though majority of wine companies are still facing problems, monthly output is registering a positive dynamics. Clothes production industry is in recession, which impacts the overall performance of the sector.

Agriculture

According to the statistical data, the agricultural output in January-September 2007 was 9010 mln. lei. This is 20.9% less compared to the similar period in 2006. This is a result of a 32.4% drop of the crops harvest⁴. Even though the volume of harvest of table and industrial grapes was higher in 2007, this did not transpose into a higher output of wines and distillates. A significant part of the harvest was exported to Ukraine.

The government declared that starting with 2008 it intends to cover 50% of irrigation costs as part of the subsidy program. However state authorities will need to make great efforts to develop the irrigation program in agriculture and provide subsidies for farmers. These measures have been already described in the National Strategy for Sustainable Development of the Agrifood Complex which requires 19bn lei to be allocated during 2008-2020. In the '90s the capacity of the irrigation system was 308 th ha, while in 2007 it constituted 60 th ha, out of which only 34 th ha of land were irrigated. The subsidy program has not been developed yet. The same applies for criteria according to which subsidy will be allocated.

It is to be mentioned that at least one year is required to elaborate the strategy project. Before elaborating the project the following data needs to be examined: similar strategies and their outcomes in the Central and Eastern Europe, internal and external demand for fresh and processed fruits, per capita consumption of the main products, productivity per 1 ha during the past 5 years, optimal amount of fertilizer to be applied etc. In this context the following suggestions made during the National Agribusiness Forum concerning facilitating the access to financial resources and irrigation infrastructure development can be applied in practice: creating a risk insurance fund for farmers who do not have sufficient warranty; issue credits with a smaller interest rate for purchasing irrigation equipment or elaborating

¹ Government decision nr.1075 from October 2, 2007, MO nr. 161-164 from October 12, 2007.

² Government decision nr.1093 from October 8, 2007, MO nr. 165-167 from October 19, 2007.

³ Government decision nr.1167 from October 29, 2007, MO nr. 171-174 from November 2, 2007.

⁴ According to the information on social-economic situations in Republic of Moldova during January-September 2007, NBS.



leasing instruments for purchasing modern and efficient equipment.

It is obvious that this strategy implies significant financial investments. According to the international experience the most attractive branch for these investments is the agricultural processing industry, because there are mainly family run estates in the primary agricultural sector. This is why higher investments in the agricultural processing industry, will generate consumption demand for these products. Respectively, the farmers will see an improved financing and risk insurance mechanisms applied in agriculture.

Services

The volume of retail sales have increased during January-September 2007 by 10.7%, including by 12.3% in the private sector (70.1% from the total), and 10.8% (24.4% from the total) – for the companies with mixed, private and public ownership. At the same time, the volume services provided to the population increased by 4.8% (figure 1).

The highest growth rate of services was experienced by the private companies (16.5%), while for the joint venture companies and companies with mixed ownership (private and public) the volume of services has reduced in real terms by 2.1% and respectively 1.9% as compared to January-September 2006.

The telecommunication services benefit from the most dynamic development and a constantly increasing number of customers. Thus, the Orange company has announced that it has 1 173 thousand clients due to the introduction of some innovative services. "Starnet" is developing a new network of accessing Internet through optical fibers; this network is almost completed and it can initially connect to Internet 30% of the population of the city, providing a high speed (100 Mbps inside the country) and high stability. The advantage of this network is the low connection cost, as well as the easiness of working in teams over common projects, organizing teleconferences, different multimedia services (for example, digital television). It is almost certain that these services will be attractive for corporate clients, central and local administration, as well as the population that has an income above the average. There is also a remarkable development of the services in the field of cable and satellite television. The TelefeM International⁵, with investors' support

⁵ This company has obtained a broadcast license for the second state network, which covers 90% of the territory of the Republic of Moldova. It intends to use 70% of the license to broadcast the Romanian television

from Great Britain, is expected to invest \$3 mln in a new television channel. It also has to be mentioned that on October 14, the largest communication company in Moldova– Sun Communications, has launched in Balti, offering its clients the connection to the favorite channels, and a free technical assistance.

The advertising market is growing very fast, because any type of services requires promotion. The Republic of Moldova is one of the eight top countries in which the advertising markets will register the highest growth rates in the next two-three years⁶. It is noteworthy the high demands for the quality and objectiveness of the information required by the National Agency for the Protection of Competition. Thus, if the companies will state that their products are the most qualitative and are the cheapest on the market, then it becomes mandatory for them to present proof for these statements.

Prices

The sharp increase of the prices, which is characteristic for the second half of the year, continued in November. Thus, the prices for the consumption goods have increased by 1.6% in October as compared to September 2007. The cumulative inflation since the beginning of the year reached 10.7%, and exceeded the 10% level set by the NBM. Prices for food again showed the highest increase (+2.4%), in particular due to higher prices for fruits, vegetables, milk and dairy products. Such a significant increase of prices for the food was not experienced since 2003, when the economy was also recovering from the summer drought of 2003, although less severe.

From the non-food products, prices for fuel have increased the most, by 2.1%, and consumer price index for the non-food products equals to 1.4%. Higher prices for Diesel oil registered at the beginning of November will fuel the inflation in the next months, and at the same time, this can contribute to an increase in prices of the natural gas. After prices for services increased in August, it appears that this dynamics has slowed down to only 0.8% compared to the previous month. Other factors that have influenced the inflation level were high remittances and the high demand for consumption goods.

channel TVR 1, and the rest 30% will be used for broadcasting its own programs.

⁶ According to a press release of the International Publicity Agency ZenithOptimedia, that was issued in October 2007 (Ukraine and Romania are on the 7th, and respectively 10th places)

Tabel 1. Monthly inflation rates, %

	Iul 2007	Aug 2007	Sept 2007	Oct 2007
Consumer price index	1,1	2,2	1,6	1,6
Food products	1,6	2,2	1,6	2,4
Non-food products	1,1	0,9	1,5	1,4
Services	0,4	5,2	1,6	0,8
Industrial price Index	0,8	1,2	1,8	-

Source: NBS

Thus inflation level already exceeded the limits set by the IMF and the local authorities. Not even the appreciation of the LEU against the US dollar can stop the process of rapid price increase in this period. The IMF mission that will be held in November is concerned about this issue and will discuss the inflation problem in Moldova.

Labor Market

In January-September 2007, the real salary has increased by 9%, and in September it was equal to 2130 lei (130 €). However, the average monthly salary in September was 0.65% less than the salary registered in July, and 3.96% less than in June 2007. The average salary in the budgetary sector was 1695 lei, in the real sector – 2352 lei. If to compare the salary in different fields of the economy, than financial sector employees have the highest average monthly salary– 3704 lei, construction sector employees – 3434 lei, and transport and communication sector employees– 3131 lei, which is respectively 18.9%, 25%, and 18.2% more than in September 2006. The reason is the fast development of these sectors, due to an increase of the fixed assets and the working capital. This was supported by an increasing volume of remittances that have stimulated the financial transactions, boosted construction sector due to a high demand for the apartments, and increased the number of clients in the telecommunication services. The high demand for the apartments, at its turn, has increased the volume of shipped goods needed in construction, and it has also increased the volume of services related to the construction sector.

At the same time, the lowest average monthly salary was registered in agriculture - 1278 lei, caused by the problems that this sector faces at all its levels.

On the other hand, the sectors with high salaries experience a shortage of qualified specialists (for example, in the field of financial management, engineering construction, etc.). There are three

reasons for this. First of all, the quality of education provided by the educational institutions does not meet companies' demands (both the curricula, and professors' qualifications). The second reason is the fact that since Romania joined the EU, the brain drain has become stronger. The third reason is the salary paid by the companies which does not correspond to the expectations of the qualified workers, so that the latter prefer to emigrate rather than work for low salaries. At the same time, reaching the goal set by the authorities to increase by 2009 the average monthly salary up to 300 USD (this was ensured at the Government meeting that was held this month), will mean little for the employed people, because this amount of money by 2009 will have the same or even a less purchasing power that the current salaries have now, taking into account the continuous price increase for goods and services.

As a result, the authorities, while regulating the labor market disequilibrium, should examine the instruments of the economic policy, such as laws, decisions, programs, and strategies, which have to be taken into account to identify solutions to these problems from the short-term and long-term perspective. Thus, the active promotion since September of the Work&Travel programs and the advantages of traveling and working in the United States had both a series of positive and negative effects on the students. The negative effects are: a decrease in students' responsibility to continue or finish their studies, the loss of the best students because of their unwillingness to come back to Moldova, a greater wish of the young people that have not been enrolled to universities (due to a limited number of places) to work abroad.

It is obvious that emigration was helping to reduce the pressure on the labor market. This argument is supported by the small number of unemployed population registered as of October 1, 2007 – 22,7 th people. In this context, the figures provided by the Ministry of Economy and Trade raise suspicion. Respectively according to MEC there were 47 th new work places created in the first quarter of 2007, including 9,8 th workplaces in industry, retail and wholesale – 8,9 th places, hunting and forestry – 5,6 th places, constructions – 5,2 th places, transports and communications – 2,9 th places, etc. Therefore there is a certain ambiguity concerning the 10 th workplaces created in industry in the framework of a general recession registered in this branch of the national economy.



Budget

Like the precedent months, revenues collected to the state budget in the first ten months of this year exceeded by 1.7 percent the planned returns in late October, turning over 11,106,300 lei. The execution of revenues and expenses of the national public budget continues to grow by the end of the year. As of September 30, 2007, revenues of the national public budget were executed 105.1 percent and expenditures 89.4 percent. However, the execution of expenses for foreign activity, science and innovation, as well as for some sectors for which large resources have been foreseen such as education and agriculture, forestry, fishery and water management the expense execution level is low so far.

Table 2. Evolution of national public budget, million lei

	Planned 1-9/07	Executed 1-9/07	Executed 1-9/06
Overall revenues	14,594.4	15,336.1	12,399.4
Including, revenues from VAT,	5,194.3	5,251.4	4,221.7
Including, revenues from income tax	840.3	1,088.2	780.3
Overall expenses	17,224.6	15,390.2	12,100.7

Source: NBS

The Parliament examined and passed the draft State Budget Law for 2008 in two readings on October 26. Like the precedent years, the revenues will be mainly based on imports. The introduction of the “zero” tax on reinvested profit of economic agents reduced the direct revenues compared with 2007. A new income is introduced in the draft law for 2008 – the revenue from the capital legalisation tax, which is expected to amount to 2,646,229 lei. A disproportional distribution of the means to the four funds is observed. Thus, the prophylaxis fund will comprise only 2 percent of the planned expenses, though it is more important than the reserve fund for which the same amount was planned. The Parliament is due to examine the draft state social insurance law for 2008.

The Ministry of Economy and Commerce has released new data on capital legalisation process. As of November 6, approximately 50 million lei was raised after legalisation of capital. Although these amounts could grow by the end of the legalisation deadline, accordingly to experience of other countries, the budget revenues are insignificant.

Monetary Policy

No essential changes have been operated in the NBM-promoted monetary policy in the period concerned, with the central bank maintaining a “cautious” position. The NBM Management Board did not change the interest rates at the November 1 sitting. At the same time, the bank released two very important communications.

The central bank said in the first communication on November 14 that the earlier taken measures (rise of basic rate on REPO operations and rise of mandatory reserves) have stabilized the price advance paces. Also, NBM anticipates that the inflation will start declining. However, an inflation rate below 13 percent should not be expected this year.

According to the communication released on November 15, the central bank reveals its long-term intentions (for 2-3 years) to exceed the explicit inflation target and to approve this action plan.

This will be an extremely important change in the monetary policy because the inflation targeting requires more responsibility for eventual failures to reach the assumed target. At the same time, the explicit inflation targeting involves the introduction of a new methodology of calculation of the basic inflation, which would prevent administrative influences on price rises. According to the 2007 developments, an inefficient governmental control on a price basket would produce strong inflationist shocks and this could be prevented if the controlled prices would be periodically revised.

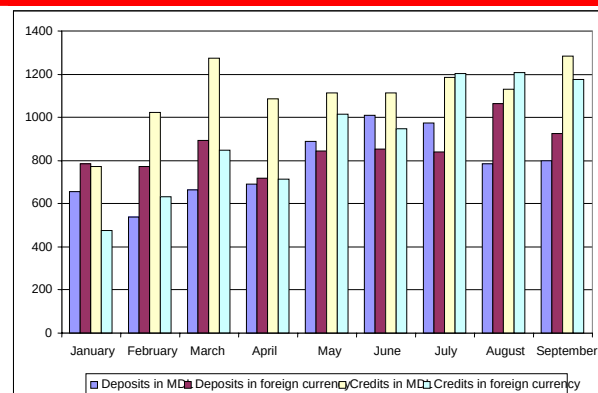
Banking System

The volume of credits released by commercial banks rose in September compared with August, up to 2,459,400 lei. Most of credits were released in domestic currency because the average interest rate decreased in September down to 18.87 percent, while the interest on credits in foreign currency reached 10.9 percent.

As regards deposits in commercial banks, they decreased in September compared with August, down to 1,721,900 lei, this being the lowest level in the past five months. Like the precedent month, deposits in foreign currency prevailed, as the average interest rate was 6.10 percent. The average interest rate on deposits in domestic currency was 14.87 percent. Forward deposits of individuals have declined. This is an expected phenomenon when the inflation rate is high, as population prefers to invest in consumer goods rather than to save their money in

banks, which could increase the interest rates on attracted deposits.

Chart 1 Evolution of credits and deposits in banking system, million lei



Source: NBM

The procedural rate used to calculate the 2008 annual mandatory payment to the fund guaranteeing deposits in the banking system⁷ was approved; it was lowered compared with this year and will be 0.0798% of the overall amount of guaranteed deposits registered in every authorized banks on September 30, 2007.

The joint IMF and World Bank mission that evaluated the Moldovan financial sector on October 1-12 appreciated the evolution of the banking system. Allowing foreign investors to purchase domestic banks played an important role in this process. However, the privatisation of Banca de Economii is very slow.

Financial Market

The trend of lowering the interests on state treasury securities which persisted until September reversed radically in October (Diagram 2). Thus, if treasury bonds maturing in 91 days (BT-91) were sold for a 10.55% interest rate in September, the rate in October was 15.15%. This evolution was linked to the accelerated inflation in July-September and the corresponding change of investment preferences of banks. The new interest rates were also observed at the November tenders and they will likely persist the next months.

⁷ Decision # 62/4 from October 19, 2007, Monitorul Oficial of Moldova # 168-170 from October 26, 2007 concerning the percent rate used to calculate the mandatory annual payment;

Chart 2 Evolution of well-balanced average annual rate on state securities, %



Source: NBM

Foreign Exchange

Unlike September, when the Moldovan leu appreciated quickly vs. U.S. dollar, the exchange rate in October was more stable, oscillating between 11.46 and 11.49 MDL/USD. The exchange rate has stabilized due to NBM interventions on currency market, in particular, the central bank has purchased a record volume of currency (more than 71 million USD). However, the depreciation trend restarted with new forces, with the dollar depreciating from 11.4517 (November 1) down to 11.2931 (November 20). The depreciation of the dollar was linked to traditional factors (intense foreign currency inflows from individuals and foreign investments) and persistence of global and regional factors (global depreciation of the dollar, appreciation of domestic currencies in Ukraine and Russia).

Foreign Trade

Statistics on evolution of foreign trade for September did not reveal essential changes of the recent developments. The trade deficit is on the permanent rise, exceeding 1.6 billion dollars by September 2007 and growing by 42.9%, compared with the similar period of last year. Also, the trade deficit is growing because imports (+37.2%) advance faster than exports (+28.4%)

Deliveries of mineral products, common metals, fat and vegetal oils, stone items, machines and appliances, footwear, textiles and vegetal products achieved the strongest rise among Moldovan exports. However, each of these products except for textiles and vegetal products cover less than 5% of all exports, so that their growth has limited effects on



global statistics on value of our exports. On the contrary, exports of food products and drinks are on the decline in continuation, following the Russian embargo on wine exports introduced in early 2006.

We note in this context that the first Moldovan wines have been delivered to the Russian Federation after the embargo was withdrawn. At the same time, majority of Moldovan producers “do not get drunk with cold water,” realizing perfectly how hard it will be to sell Moldovan wines, given the technical requirements and the increasing competition on Russian market. In this respect, the situation in Romania is very alarming, as after a recent control on wine trading and labeling in the neighboring country, the National Consumer Protection Agency has discovered a number of grave violations regarding the “sale of wines of inappropriate quality confirmed by laboratory tests” and “inappropriate certification of quality of wine on basis of sugar contents.” Such cases gravely affect the image of Moldovan wine producers and harden the promotion of our wines to foreign markets.

In November, the European Commission gave green light to awarding of autonomous trade preferences to Moldova. Now EU member states are due to make a decision in this respect. The awarding of “asymmetrical” trade preferences is a true appreciation of reforms implemented in Moldova to gain these preferences. Another question is when Moldovan companies will be able to enjoy them, given the insufficiently developed quality infrastructure in our country. In addition, it is important to see what shares the European authorities will introduce for the so-called sensible products, which could include some “strategic” Moldovan exports.

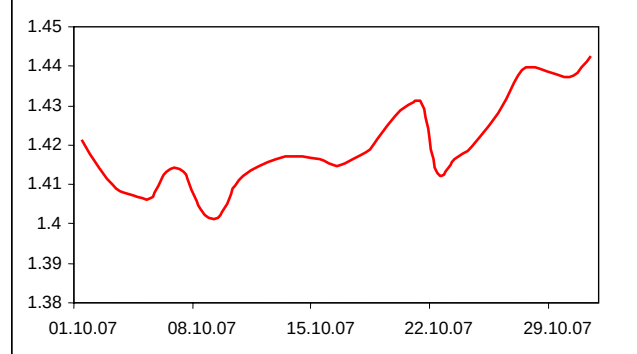
Global Markets

The **oil** prices continued to grow in October. But this rise was as dramatic as fluctuating. At the same time, a series of fundamental and speculative factors shaped it. Thus, the price has increased up to 90 dollars per barrel (of Brent) till late October particularly due to the rise of petrol demand (OPEC experts anticipate a higher demand for winter 2008) and geopolitical risks related to the complicated situation in the north of Iraq. The price has declined a little (down to 83 dollars per barrel) at the beginning of the last decade, but it went up again (90 dollars per barrel). Bad weather in Mexico, reduction of petroleum reserves in the United States completed the factors that fuelled the price. In addition, the continuous decline of the dollar contributed much to

the “dear oil”: according to estimates, the petrol price has increased by 53% in U.S. dollars and by 40% in euros. The oil price rose up to 93.26 dollars per barrel in early November, being fuelled by bad weather in the North Sea basin, geopolitical risks, smallest petrol reserves of the U.S. in the past two years (in the period when reserves for winter were prepared), and the firm OPEC attitude towards speculative nature of exuberant rise of oil price. Most of analysts anticipate that the oil price will keep growing on short term.⁸

Forecasts for the 2007-08 wheat crops have been updated and increased up to 602 million tons after Russia and Kazakhstan have improved their data. At the same time, the consumption forecasts have been updated and lowered down to 610 million tons. In general, prices have decreased a little after fears regarding the wheat crop had dissipated. The depreciation of the dollar, dearer oil and higher transportation costs are the factors which increase the prices. At the same time, the perspectives for the autumn grain crop are more optimistic due to a favorable weather and enlargement of wheat fields.⁹

Chart 3 Evolution of euro/dollar rate



Source: Rosbusinessconsulting

The **dollar** continued to depreciate versus **euro** in October (Diagram 3). The anticipated reduction of federal interest rate by FED, the difficult situation on the U.S. mortgage market and the concern of the European Central Bank with inflationist risks in the Eurozone influenced the dollar/euro rate. The worsening situation on real estate market (reduction of new constructions and number of new buildings permits), negative forecasts for consumer credit

⁸ Sources: The Economist, International Energy Agency, Reuters, RBC.

⁹ Sources: USDA, World Agricultural Supply and Demand Estimates, Wheat Outlook; International Grains Council, Grain Market Report; The Financial Times.

market and higher number of applications for unemployment indemnities fuelled the depreciation of the dollar. All these factors made the dollar decline down to \$1.4305/€ in the last decade of the month. This trend continued in late October and early November, with the rate of these currencies exceeding \$1.45/€. A new anticipated reduction of the federal rate, the decline of business and consumer confidence in the U.S. and the increased attention of the European Central Bank towards inflationist risks in the Eurozone influenced the decline of the dollar in the period concerned. The diversification (or even declaration of the need) of currency reserves from dollars into euros by some national banks was another important factor. Majority of analysts anticipate that the euro will test soon the \$1.5/€ rate.¹⁰

Trade Partners

The **Russian** economy developed slower in the 2nd quarter: 6.7% compared with 7.9% and 7.8% in the 1st and 2nd quarters. Anyway, these paces are pretty strong, and the Russian economy grew by 7.4% in January-September 2007, compared with 6.3% last year. The economy developed in the period concerned thanks to the investment demand (+21.2%), expansion of building sector (+23.5%) and industry (+6.6%). The slowing down trend of industry continued in September, too, and it was observed both in processing industry and in extractive industry. The consumption fuels the economic growth in Russia in continuation, being supported by a robust expansion of available real earnings of population (+12.4%) with a higher advance of real salaries (+16.2%). The retail trade (+23.5%) continues to grow on this background. Imports (+37.32%) still grow faster than exports (+11.4%), in spite of dearer oil on global markets. At the same time, the higher investment and consumer demand and a “dearer” Ruble fuel the import. The liquidity crisis observed on the global markets in August-September (see the precedent issues of BER) produces a capital return flow worth 9.4 billion dollars, but this trend will be reversed in October.¹¹

The **Ukrainian** economy continued its robust growth in September. Thus, it grew by 7.3% in January-September, being supported by expansion of internal demand, consumption and investments (+23.9%), needed to modernize the infrastructure and equipment. Perhaps the investment demand will

grow in continuation in the near future, playing a crucial role in ensuring the economic growth in Ukraine. The growth was sustained by industry (+10.7%) and constructions (+14.3), maintaining the growth trend: +7.5% compared with the same period of 2006. This growth was sustained first of all by private consumption (+30.6%), as well as by development of industry (+10.9%) and constructions (+12.7%). The trade deficit is growing in continuation. It reached 2.5 billion dollars in January-September or 2.6 percent of the GDP, as imports rose faster than exports, in particular, 33.8% and 30%. At the same time, the inflation accelerated in October like in many other regions. It is worth to note that the inflation has grown in spite of a cautious monetary policy and administrative measures, being particularly fuelled by dearer agro-food products. Dearer Russian natural gas will pose main risks in the near future, and they will have a serious impact on Ukrainian population and industry. Remedying the negative repercussions will be one of key tasks of the new Government.¹²

Table 3 Economic indicators of main trade partners of Moldova

	GDP		Industrial production,	Inflation	Unemployment
	Updated date	2007, forecast			
Russia	7.4 01-09/07	7.0	6.6 01-09/07	7.5 01-09/07	6.0 09/2007
Ukraine	7.3 01-09/07	7.5	10.7 01-09/07	8.6 01-09/07	7.1 T3/2007
Romania	5.8 2ndQ/07	6.5	6.1 09/07	6.9 annual	7.2 09/07
Germany	2.5 3rdQ/07	2.2	6.6 09/07	2.7 annual	8.1 09/07
Italy	1.9 3rdQ/07	1.7	0.3 09/07	2.3 annual	5.9 2ndQ, 2007

Sources: *The Economist*, IMF, World Bank, Derjkomstat, Goskomstat, Eurostat, INS Romania, EXPERT-GRUP.

Economic prospects in the **European Union** remain optimistic, though the deceleration of industrial growth observed at the beginning of the 3rd quarter is going on. The dearer petrol, the harder access to credits and the “strengthening” of the euro versus U.S. dollar reduce the economic growth paces. At the same time, inflationist risks are quite high (2.6% in October 2007) and they are raising the main concern of the European Central Bank. Dearer petrol and food products are the main causes of inflation growth. At the same time, Bank representatives hinted that they are not very concerned with the appreciation of the euro for the time being. At the

¹⁰ Reuters, RBC, Global Insight Inc., OECD, The Financial Times;

¹¹ Ministry of Commerce and Economic Development, Інститут Економіки Переходного Періода (Insitute of Transition Economy).

¹² Інститут економічних досліджень (Institute for Economic Research and Policy Consulting), Міжнародний центр перспективних досліджень (International Centre for Policy Studies), Експерт-Україна (Expert-Ukraine).



same time, majority of analysts anticipate better economic prospects for the Eurozone by early next year. Truly, the internal consumption remains robust, the unemployment rate continues to compress (7% in September 2007), and European companies still are very competitive internationally, in spite of the strong single currency. The 3.1-billion-euro commercial surplus registered in the Eurozone in September is also a proof in this respect.¹³

The **Romanian** economy is dynamically developing in continuation. Positive trends were observed in almost all sectors in January-September 2007: building (+33.3% in January-August, 2007), trade (17.4%) and industry (+5.8%). The processing industry (+6.7%) mainly ensures the development of industry. The trade deficit continues to grow, exceeding 15 billion euros in January-September 2007, which is by nearly 58% more than in the similar period of 2006. The appreciation of domestic currency and the high internal investment and consumption demand heated the trade deficit. Expectations of managers regarding evolutions in October-December are relatively positive for the retail trade, industry and services, though they anticipate a reduction of jobs in industry. Expectations for the building sector are less optimistic. Managers anticipate the stagnation of this sector as regards the general economic situation, job openings and future contracts and orders. According to majority of managers, only prices will grow.¹⁴



¹³ Eurostat, The Economist, RBC, Global Insight Inc.

¹⁴ Sources: Saptamina Financiara, Capital, Curentul, The Economist, www.anpc.ro.