

■ Evolution of the Economic Leading Indicator

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Real Economy is a monthly economic review, tracking the most important economic evolutions and policy developments. Its readers are policymakers, CEOs of domestic and international companies and banks, representatives of the international institutions and foreign embassies, political parties and economic journalists.

Acronyms and abbreviations used:

y-o-y - year on year; q-o-q - quarter on quarter; m-o-m - month on month; e-o-p - end of period; Q4:07 - fourth quarter 2007; Jan:09 - January 2009; NBS - National Bureau of Statistics; NEA - National Employment Agency; NBM - National Bank of Moldova; MDL - Moldovan leu (national currency); FDI - foreign direct investments; p.p. - percentage points.

EXPERT-GRUP is a Moldovan policy think-tank whose mission is to create a working environment in which free and non-trivial thinking thrives in order for the institution to be a leading source of unbiased economic analysis and to effectively advocate for innovative ideas and solutions to the economic problems that Moldova encounters along its path of economic transformation, societal development and European integration.

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Economic Leading Indicator (ELI)

ELI is formed by aggregating six macroeconomic indicators: exports, transfers to individuals, new loans, share of allowances for loan losses, currency in circulation (M0), and bank margin. The indicators were selected depending on their relevance for the economic trends. For more details about the calculation methodology see the website of EXPERT-GRUP.

Moldovan economy keeps recovering, but not quickly enough.

In October, the Economic Leading Indicator (ELI) increased by 2 points compared to the previous month (98.9 compared to 96.9 points), highlighting a continuation of the ascending trend, followed during the current year.

Nevertheless, compared to the recovery in 2010, the trend is much slower and volatile, revealing the existence of many risks, both external and internal, which slow down the economic growth and development.

Recovery is not inclusive, being distributed unevenly across the economic sectors.

Although the amount of industrial output increased in Jan-Sep'13 by 6.3%, the branches that ensure about one third of the gross value added of the sector are still in recession compared to the previous year.

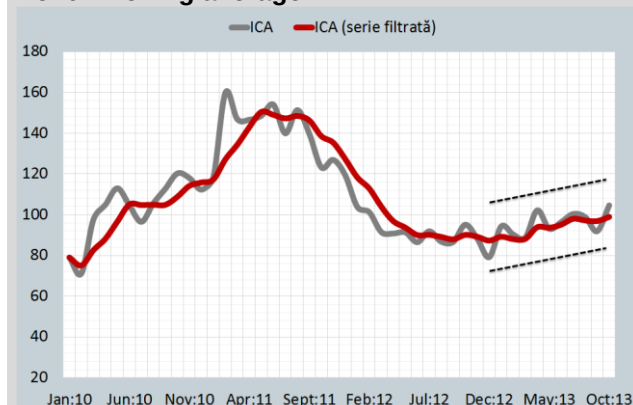
The increase of the Economic Leading Indicator was mainly determined by some improvements in the banking sector, as well as by the growth in consumption. Thus, in October, the banks provided 35% more loans compared to the previous year and the share of nonperforming loans shrank to 12.3% (by 0.1 p.p. compared to September). At the same time, the amount of currency in circulation registered one of the fastest growths in the past 3 years (+35% y-o-y). However, the expansion of lending is not homogeneous, being fed by the loans contracted by companies in national currency, which advanced about twice y-o-y. At the same time, the amount of loans provided to individuals grew by only 1.5% y-o-y, while the loans provided in foreign currency decreased by 33% y-o-y.

Similar contradictory trends are also noticed in investment activity. Thus, the real 3.3% y-o-y increase in Jan-Sep'13 was mainly generated by public institutions (+7.5%) and domestic private companies (+5.9%). Instead, the investments run by companies with foreign participation increased by only 3.7%, while the joint ventures cut their investment activity by 20.2%, compared to the previous year.

The instable economic conditions in the region paralleled with the peculiarities of an electoral year can be considered as the main short-term risks for the Moldovan economy.

The main trading partners of the country face a difficult economic situation, which undermines the external demand for Moldovan products and the inflow of investments and remittances. Thus, in the 3rd quarter, the Euro-Zone remained in recession (-0.4% y-o-y), EU economy increased by only 0.1% y-o-y, while Russia's growth rate slowed down to 1.2% y-o-y. The external constraints are amplified by the specific pre-electoral period within the country, basically consisting of a relaxed and pro-cyclical fiscal policy, and, at the same time, delaying the systemic reforms and inducing higher uncertainty.

Economic Leading Indicator, raw data and 4-month moving average¹

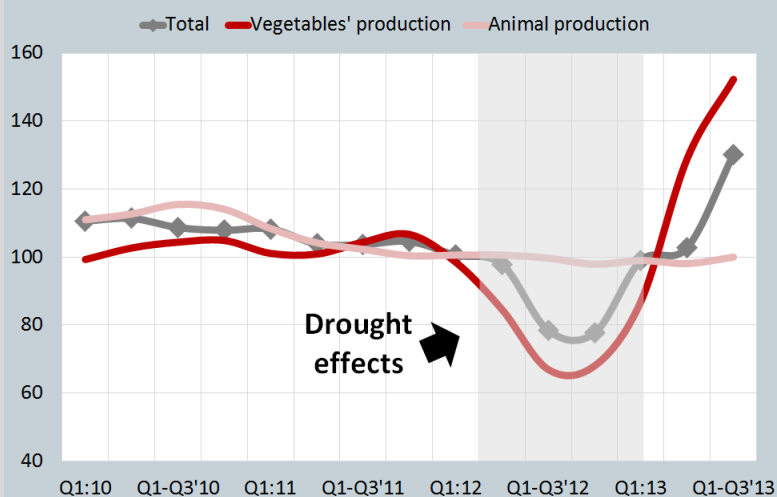


Source: EXPERT-GRUP calculations on the basis of the data provided by the NBS and NBM;

¹For October, the volume of remittances and exports was estimated by the authors.

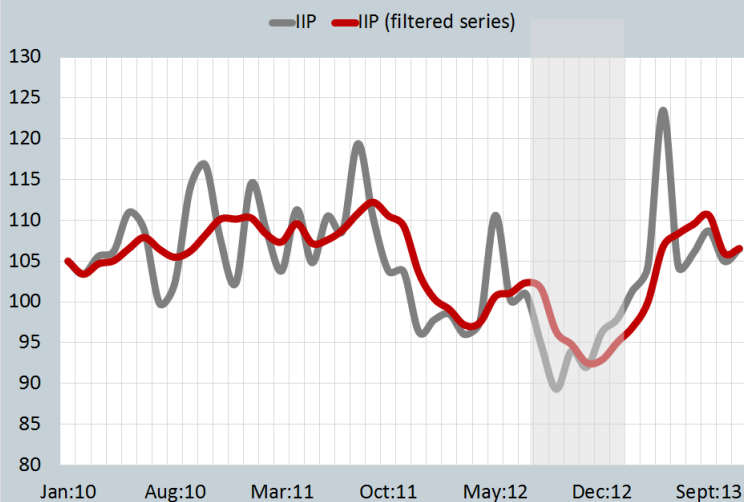
■ Main Economic Trends

Figure 1. Gross agricultural production, increase y-o-y, %



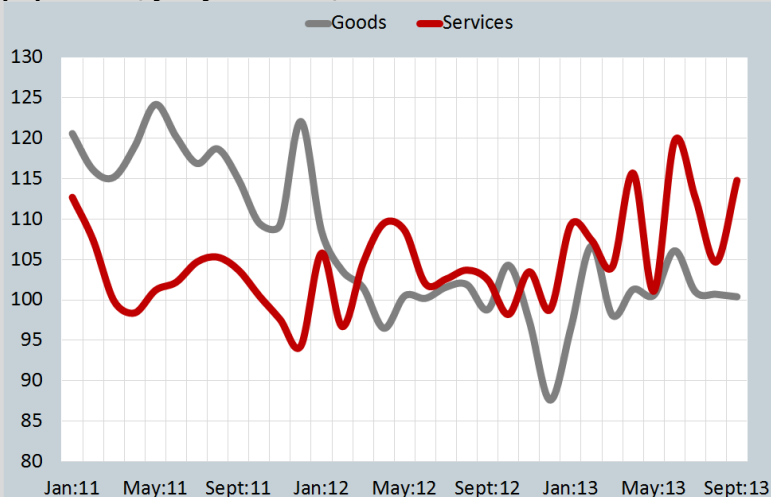
Source: NBS

Figure 2. Industrial Output Indicator, gross series and filtered series (4-month moving average), y-o-y increase, %



Source: NBS

Figure 3. Retail trade with goods and services provided to population, y-o-y increase, %



Source: NBS

AGRICULTURE

The sector is still recovering after last year's drought. In Jan-Sep'13, the gross agricultural production increased by **30.2%** y-o-y, being determined mainly by the robust increase of vegetal production (**+52.3%** y-o-y). At the same time, the livestock sector is still stagnating (0%), revealing a series of structural problems it is facing (informal economy, insufficient investment and limited sales market).

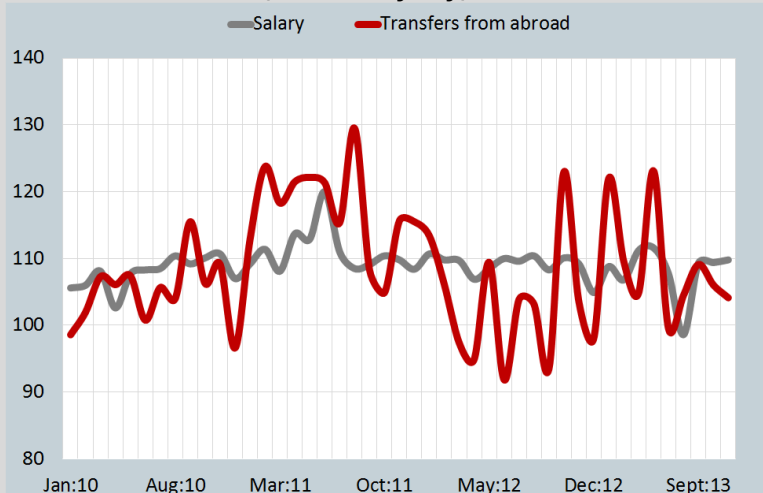
INDUSTRY

The growth was ensured only by the branches that provide about 66% of the gross added value in this sector. In Sep:13, the Industrial Output Indicator increased by **6.5%** y-o-y. During the first 9 months the IOI increased by **6.3%** y-o-y. The biggest contributors to the increase were: production of electric machinery and appliances (**+39.9%**); production of other goods made of non-metallic minerals (**+21.6%**) and food and beverages industry (**+2.7%**).

DOMESTIC TRADE IN GOODS AND SERVICES

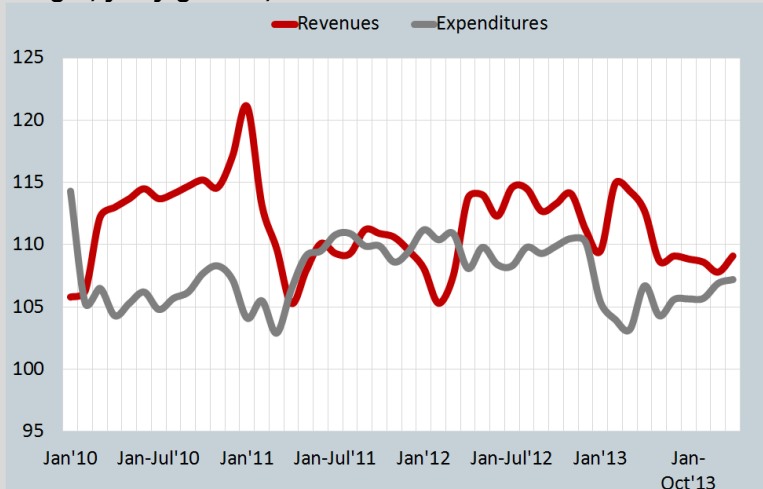
This sector continues to be volatile on the background of a non-homogeneous economic recovery and foreign risks. In Sep:13, the turnover of firms that practice retail trade was constant (**+0.4%**, y-o-y), while the amount of services provided to the population continued its ascending trend (**+22.0%**, y-o-y).

Figure 4. The average salary per economy and transfers from abroad to individuals, increase y-o-y, %



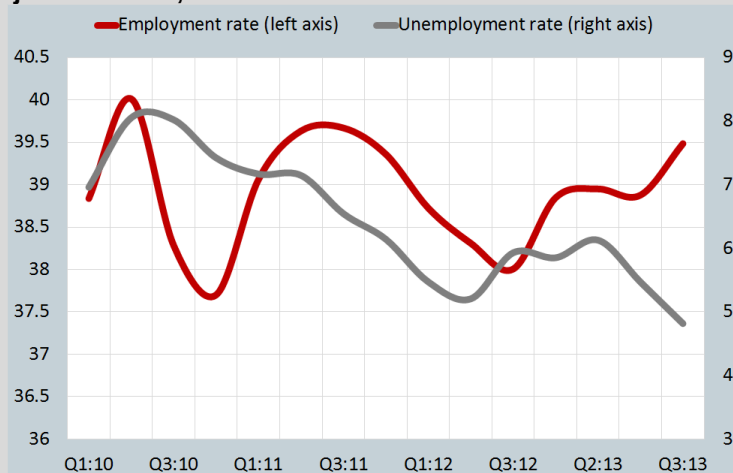
Source: NBS and NBM

Figure 5. Revenue and expenditures of the National Public Budget, y-o-y growth, %



Source: Ministry of Finance

Figure 6. Employment and unemployment rates, seasonally adjusted series, %



Source: NBS

INCOME AND EXPENSES OF THE POPULATION

The volatility of population's consumptions is mainly induced by the unstable growth of remittances. In Sep:13 the transfers from abroad to individuals increased by **4.1%** y-o-y, slowing down if compared to Aug:13(+6.0%) and Jul:13(+9.1%). The growth was fostered by the transfers in US dollars. The average salary per economy in Sep:13 increased by **9.8%** in nominal terms and by **5.7%** in real terms, y-o-y.

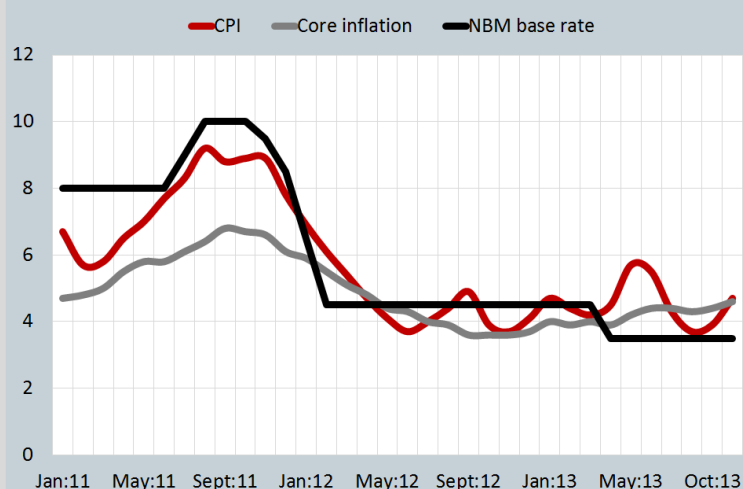
PUBLIC FINANCE

The budgetary revenue is growing, but at a lower rate than expected. During Jan-Oct'13, the NBP revenue increased by **9.1%** y-o-y, this growth being mainly determined by the receipt of VAT (**+13.0%**) and excise taxes (**+18.6%**). However, due to the failure to harness fully the external grants (**59%** of the planned volumes) and of the taxes on international trade (**97.9%** of the planned), the revenue was by **1.9%** than planned. The expenses increased by **7.2%**, at a higher rate than during the previous months.

LABOR MARKET

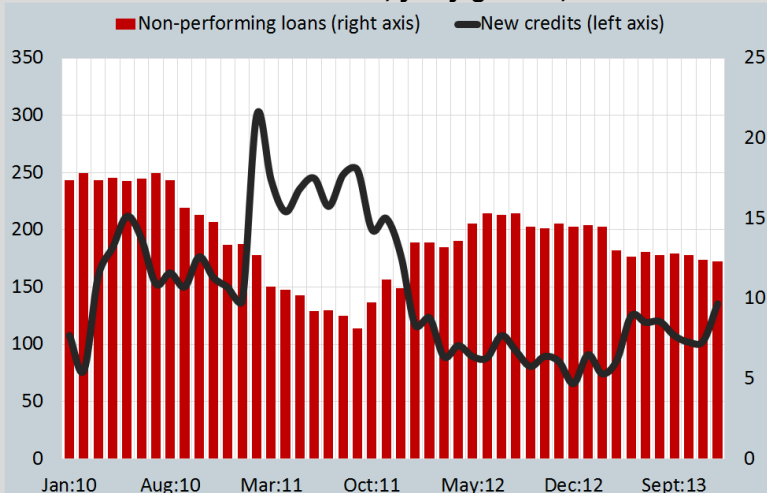
The favourable climate conditions and economic recovery contribute to job creation. In Q3:13 the employment rate constituted **42.7%**, being higher than during the previous year (**41.1%**). If the seasonal factor is excluded, a positive trend is outlines for this year. The number of employed people increased by **4.3%** y-o-y. The unemployment rate constituted only **3.9%**, following a descendant trend over the past years.

Figure 7. Consumer Price Index and core inflation, y-o-y growth, NBM base rate, %



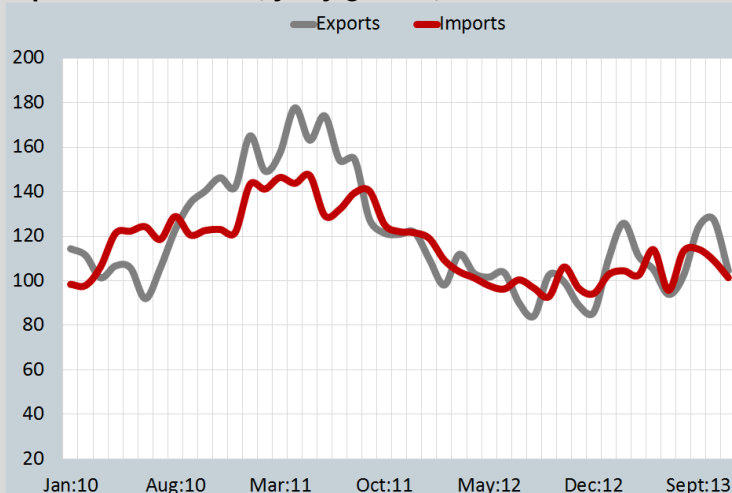
Source: NBM

Figure 8. Share of non-performing loans in total loans, %; volume of new loans extended, y-o-y growth, %



Source: NBM

Figure 9. The total volume of exports and imports of the Republic of Moldova, y-o-y growth, %



Source: NBS

PRICES AND MONETARY POLICY

Without any major inflationary pressures, the monetary policy remains relaxes. In Oct:13, the Consumer Price Index constituted 4.7% y-o-y, slightly higher than in the previous month. About half of this increase was induced by foodstuffs, which were by 6.9% y-o-y more expensive. The core inflation was the same as CPI (+4.6%). NBM continued to promote a relaxing monetary policy, maintaining the base rate at 3.5%, under the CPI level.

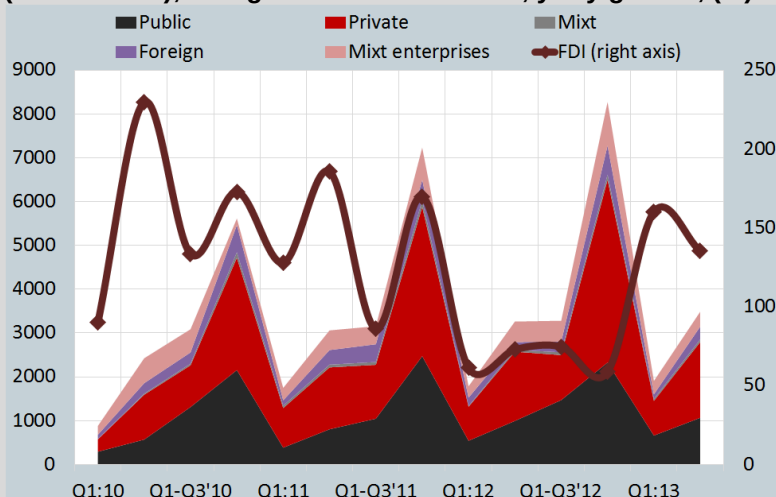
BANKING SYSTEM

The lending activity is augmenting on the background of improved economic conditions. In Oct:13 banks provided by 35.4% more credits y-o-y. The growth was determined by the loans extended in national currency to legal entities, whose volume literally doubled y-o-y. The situation in the banking sector is improving gradually, with the share of non-performing loans decreasing to 10.3%. However, it remained higher than in 2011.

EXTERNAL TRADE

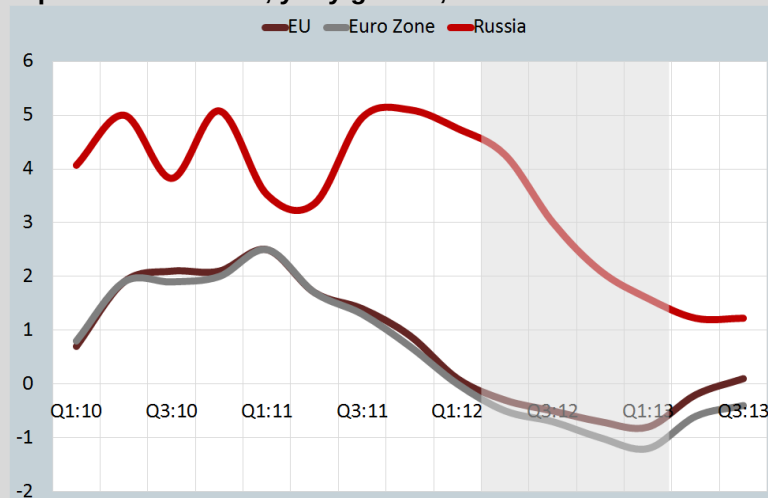
Export activity - triggered by EU and Turkey and slowed down by the CIS market. Thanks to the improved economic situation in the region, in Jan-Sep:13, the Moldovan exports to EU increased by 9.6%, and to other markets (in particular Turkey) - by 49.7% y-o-y. Because of the economic slow-down in Russia, the exports to CIS increased by 3.4%, and to Russia - by only 2.5% y-o-y. The imports grew at a slower rate than exports (+6.3% against +11.0% y-o-y).

Figure 10. Investments in fixed capital by forms of ownership (million MDL); foreign direct investments, y-o-y growth, (%)



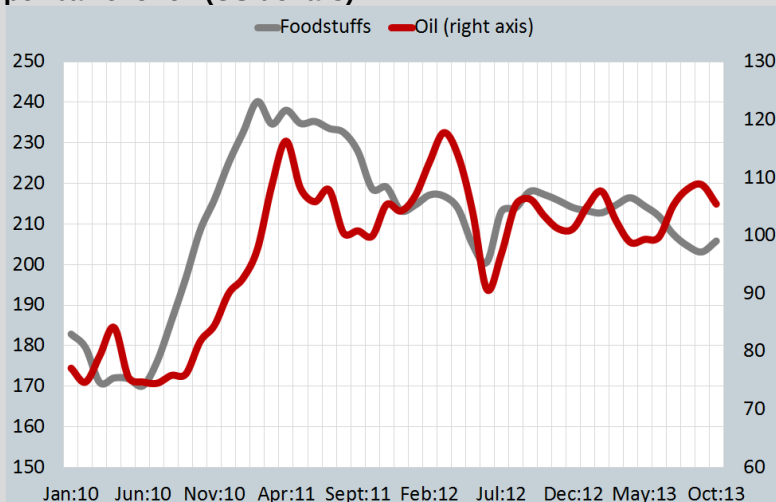
Source: NBS

Figure 11. Economic growth of the main trade partners of the Republic of Moldova, y-o-y growth, %



Source: Eurostat and the Russian Federal State Statistical

Figure 12. Global food price index (points) and average price per barrel of oil (US dollars)



Source: World Bank and FAOUN

INVESTMENT ACTIVITY

Investment growth fostered by the public sector. During Jan-Sep'13, the volume of investments in long-term material assets increased by **3.3%** y-o-y (in comparable prices), accelerating twice if compared with Jan-Jun'13. The growth was determined by public **(+7.5%)** and private institutions **(+5.9%)**. The investments made by companies with foreign participation increased by **3.7%** only, and the joint ventures shrunk their investment activity by **20.2%** y-o-y.

MAIN TRADE PARTNERS

Uncertain external economic conditions: the Russian economy is slowing down, and the EU one is not growing quickly enough. In Q3:13 the EU economy recorded a positive growth **(+0.1%** y-o-y) for the first time over the past 1.5 years. The Eurozone is still in recession **(-0.4** y-o-y). The Russian economy grew by **1.2%** y-o-y, slowing down continuously since 2011.

GLOBAL MARKETS

The situation on global markets is still very volatile and, respectively, insecure. In spite of a minor growth in Oct:13, the global food price index recorded a descending trend over the past few months. The trend is marked by the cheaper cereals, on the background of better weather conditions this year y-o-y. The price of refined petroleum is also volatile, cheapening in Oct:13 by **3.1%** m-o-m and **2.0%** y-o-y.

■ Key Policy Developments in November 2013

Policy Developments	EXPERT-GRUP Comment
1 November. "The Report on Inflation No 4, 2013" was presented. NBM reviewed the forecast inflation by 0.2 p.p. for 2013 and by 0.9 p.p. for 2014, if compared with the forecasts from "The Report on Inflation No 3, 2013". Thus, NBM forecasts an annual inflation rate of 4.5% in 2013 and 4.7% in 2014.	NBM explains that this increase in forecast is due to the more expensive foodstuffs on the international markets, higher growth rates in the regulated prices and expectation of higher prices for fuels. Likewise, the inflationary trends were also worsened by the depreciation of MDL in Q2:2013-Q4:2013. At the same time, in the short run there are real preconditions to maintain the inflation rate in the proximity of the targeted level.
4 November. The Dutch company Generashon Financial B.V. sold its participation of 26.75% in <u>Victoriabank</u>. These shares were bought by 7 legal entities and one individual. The seven legal entities include: Moldasig (4,9%), Asito (4,908%) and Moldindconbank (4,902%).	Buying less than 5%, the companies avoided the need to request the permission of the NBM, and the involvement of Moldasig-Asito tandem in this transaction indicates on the possibility of a concerted activity. Grawe Carat Asigurări already invoked an anti-trust attack on behalf of SA „Moldasig” S.A., CIA „Asito” S.A., CA „Victoria Asigurări” S.A. and CA „Klassika Asigurări” S.A.. The reason is that on 27.09.2013, during the meeting of the National Bureau of Motor Insurers a decision was taken through the vote of these 4 companies not to allow Grawe Carat Asigurări to issue Green Papers. It seems that this operation with Victoriabank shares continues the series of suspicious transactions that disrupted the financial market in 2013. It is very likely that the expected end result of these actions is concentration of an important part of the financial sector in the hands of a limited number of people.
13 November. The Cabinet approved the list of objects announced for privatization. This list includes: S.A. „Aroma”, S.A. „Barza Albă”, S.A. „Combinatul de Produse Cerealiere”, S.A. „Tutun CTC”, S.A. „Moldtelecom”, Î.S. „Fabrica de Sticlă din Chişinău”, Î.S. „Air Moldova”, Î.S. „Nodul Hidroenergetic de la Costeşti”, S.A. „Circul din Chişinău”, S.A. „Centrala Electrică de Termoficare Nord”, S.A. „Reţelele Electrice de Distribuţie Nord-Vest”, S.A. „Reţelele Electrice de Distribuţie Nord” and S.A. „Glass Container Company”. The privatizations were be based on an investment competition, and the market value of these assets is expected to be established by foreign experts. This privatization round is expected to be done within a record period of 6-8 months.	Conceptually, it is good to privatize the enterprises owned fully or partially by the Government. The transfer of these assets into private ownership could enhance their management and, finally, yield more benefits for the national economy. However, the experience of clumsy and non-transparent concessions of the state assets (Banca de Economii and Chisinau State Airport), as well as the speed at which these assets are intended to be privatized during an electoral year is not trustworthy and makes this Government Decision seem quite ambiguous. For a proper valuation of assets, efficient privatization and avoidance of a negative impact on the country's economic security it is of crucial importance to ensure a transparent privatization. At the same time, it is necessary to avoid establishing any entry barriers for tender participants, to ensure loyal competition in the investors selection process.
17 November Moldovan exporters will be able to file electronic customs declarations. The Government passed a decision on the electronic customs clearance of exported goods.	According to this document, once the export transaction is processed electronically, the Customs Service will allow exporters to become more competitive on the external market through a two-fold decrease of costs. This will be accompanied by a decrease in the number of documents required for the delivery of Moldovan goods on external markets. In addition, the customs clearance time will be shortened. Thus, business entities that have a digital signature or a tablet connected to the customs information system will have the possibility to fill in the electronic declaration in several minutes. Another important advantage of this system is the elimination of the direct contact between the business entity and customs service staff, thus the procedure will become more transparent and will be monitored online.
21 November. The Ministry of Economy submitted to the Government of Moldova for approval the final draft Law amending and complementing the "Law on Fuel Market" for purposes of market liberalization.	The draft envisages a series of conceptual changes, aimed to dismantle several entry barriers on the domestic market for oil products. It is envisaged to exclude the obligation of own or lease a warehouse for fuel products in the volume of at least 5 thousand m³ and a warehouse for liquid gas of at least 150 m³. Besides, it is envisages to annul the requirement for operators to have equity worth MDL 8 million. . It is recommended to cancel the licensing requirement for the

Policy Developments	EXPERT-GRUP Comment
	business entities that use fuels only for their own consumption and do not sell them on the domestic market and replace it with a notification system. Implementation of these provisions will facilitate the activity of participants on the fuels market and well establish the necessary preconditions for the development of competition on this market, which in the end will advantage the end consumers.
24 November The Contract on Iasi-Ungheni Gas Pipe was signed, which will connect the Moldovan and Romanian national gas delivery systems. The contract, worth up to EUR 5.3 million, was concluded by the Ministry of Regional Development and Public Administration (MRDPA) of Romania and Ministry of Economy (MoE) of the Republic of Moldova.	This initiative sets the necessary preconditions for the diversification of the transport routes and source of gas imports. This contract is based on an agreement signed in 2010 by the two Governments on the implementation of the technical and financial assistance program, which envisages a grant of EUR 100 million, provided to the Republic of Moldova by Romania. The Iasi-Ungheni gas pipe is the first direct link of the Republic of Moldova to the European gas market and a first step of a wider project aimed at connecting the country to the European gas market. The total project value is EUR 26.5 million, of which EUR 7 million come from the European Union. The pipe length in the Republic of Moldova is 10.5 km, and the contract will be implemented till December 2014.
27 November The European Commission proposed visa-free travels in the Schengen area for Moldovans who have a biometric passport, as a result of the conducted evaluation and fulfillment by the Republic of Moldova of all reference objectives established in the Visa Liberalization Action Plan (VLAP). Hence, the Commission proposed to include Moldova on the list of countries, whose citizens are exempted from a visa requirement.	Though the visa liberalization regime refers only to travels up to 90 days and do not give the right to work in the EU area, it is an important step towards European integration. This could improve people's perception of the European integration process, which currently is distorted due to the lack of information and frequent manipulations of the public opinion. At the same time, the visa free regime creates important preconditions for the country's reintegration, making the Moldovan citizenship more attractive for the population from the Eastern rayons of the Republic of Moldova. The possibility to travel in EU without visas will facilitate even more the personal contacts and will foster the business development, social and cultural relations between EU and Moldova. At the same time, the visa free regime does not pose any major risks of illegal migration at least because of two reasons: (i) the migration potential was already depleted during the past 10-13 years; (ii) visa is not the biggest barrier for Moldova citizens to migrate to EU.² The proposal to eliminate the visa requirement for Moldovan citizens who have a biometric passport will be discussed by the European Parliament and Council.
28-29 November During the Eastern Partnership Summit in Vilnius, Moldova and Georgia initialed the Association Agreements with EU, and Azerbaijan signed a Visa Free Agreement with the European Union. Pressed by the street demonstrations, the Ukrainian President participated in the Summit, but did not sign the Free Trade and Political Association Agreement with EU. The Summit was attended by heads of state and leaders from the 6 countries of the Eastern Partnership: Armenia, Azerbaijan, Belarus, Ukraine, Georgia and Republic of Moldova.	By initialing these agreements, Georgia and Moldova strengthened the political and economic relationships with EU. The pressures made by the Russian Federation are still hindering the European integration of Eastern Partnership countries. It is worth mentioning that the EU market offers at least 500 million consumers and 6-times larger economy than the Euroasian Union, project initiated and promoted actively by the Russian Federation. The EU-Republic of Moldova Association Agreement, including the Deep and Comprehensive Free Trade Agreement, initialed during the Summit, will strengthen the political, economic and trade relations between EU and the Republic of Moldova. It is a concrete way of harnessing the positive dynamics of the EU-Moldova relation. It is focused on support for the main reforms, economic recovery, governing, inter-sector cooperation and wide liberalization of the Moldovan trade with EU. Initialing this Agreement is an important step towards its signing and implementation by all EU Member-States and the Republic of Moldova. However, the Ukrainian case proves and an initialed agreement is not a guarantee that it will be signed. Indeed, the Government of the Republic of Moldova will have to cope

² National Human Development Report "European aspirations and Human Development in Moldova", 2012, UNDP Moldova

Policy Developments	EXPERT-GRUP Comment
	with a series of pressures in the next future, both external and internal. The external pressures will come mainly from the Russian Federation through economic leverages and eventual diplomatic blackmailing, invoking the acute dependence of Moldova on its energy sources. The internal pressures will come mainly from the opposition, which declared its open position against this Agreement, as well as the local governments from the rayons with certain separatist trends (Balti and Gagauzia TAU).

Statistical Annexes

Table 1. Main monthly indicators

Indicator	Nov:12	Dec:12	Jan:13	Feb:13	Mar:13	Apr:13	May:13	Jun:13	Jul:13	Aug:13	Sep:13	Oct:13
Industrial production, y-o-y, % change	-8.0	-3.7	-2.1	1.4	4.3	23.5	4.3	6.0	8.7	5.0	6.5	n.a.
Retail trade, y-o-y, % change	-2.6	-12.4	-3.5	6.7	-1.9	1.3	0.6	6.1	1.0	0.7	0.4	n.a.
Services to the population, y-o-y, change	3.5	-1.2	9.3	7.4	4.1	15.7	1.1	19.7	12.6	4.7	14.8	n.a.
Export of goods, y-o-y, % change	-11.0	-14.1	9.9	25.9	11.1	5.0	-6.1	2.3	24.0	27.7	4.6	n.a.
Export of goods, y-o-y, % change	-3.4	-5.7	2.8	4.5	2.5	13.9	-4.3	13.3	14.2	9.3	1.4	n.a.
Official reserve assets, million USD	2422.4	2515.0	2519.7	2488.1	2469.1	2481.0	2475.3	2466.6	2507.6	2629.9	2722.2	n.a.
Freighted cargo, y-o-y, % change	1.4	-16.4	-13.5	41.3	31.0	25.2	1.2	5.3	25.4	40.1	32.2	16.3
Registered unemployed at NEA (e-o-p)	25586	26297	26643	27160	26324	24723	22107	19991	18670	17582	16846	n.a.
Real salary, y-o-y, % change	9.2	4.9	8.8	6.8	11.2	11.6	7.7	-1.4	9.3	9.4	10.1	n.a.
Budgetary revenues, y-o-y, % change*	14.1	11.2	9.5	14.9	14.3	12.7	8.7	9.1	8.9	8.6	7.8	9.1
CPI, y-o-y, %	3.7	4.1	4.6	4.4	4.2	4.5	5.7	5.5	4.3	3.7	3.9	4.7
IPPI, y-o-y, %	4.1	4.5	1.6	2.8	3.4	3.7	3.0	2.9	3.3	3.4	3.4	4.1
Nominal exchange rate MDL/USD (e-o-p)	12.37	12.06	12.10	12.25	12.41	12.31	12.52	12.53	12.73	12.82	12.95	13.12
Money transfers from abroad, y-o-y, % change	3.6	-0.9	22.6	9.7	4.9	23.1	-0.5	4.5	9.1	6.0	4.1	n.a.
M2 monetary aggregate, y-o-y, % change	23.7	23.5	27.2	26.1	23.4	25.0	26.7	26.7	26.4	25.7	25.0	34.8
NBM base interest rate, y-o-y, %	4.5	4.5	4.5	4.5	4.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5
Bank deposits interest rate, % (e-o-p)	7.96	8.44	8.55	8.56	8.09	7.33	7.75	6.79	7.16	7.18	6.62	6.54
Bank lending rate, %	12.68	11.98	12.41	13.23	12.77	12.4	12.21	12.03	12.05	12.09	11.79	11.94
Non-performing loans, % of total loans	14.7	14.5	14.6	14.5	13.0	12.6	12.9	12.7	12.8	12.7	12.4	12.3

Source: NBS, NBM, and EG calculations and estimates:

Table 2. Main quarterly indicators

Indicator	Q3:11	Q4:11	Q1:12	Q2:12	Q3:12	Q4:12	Q1:13	Q2:13	Q3:13
Real GDP growth, y-o-y*, %	6.7	6.4	1.0	0.8	-0.2	-0.7	3.5	6.1	n.a.
Agricultural production, y-o-y, % change*	3.7	4.6	0.6	-2.1	-21.6	-22.4	-1.0	2.8	30.2
Construction works, y-o-y, % change*	3.1	1.4	4.9	3.6	0.8	-1.3	3.7	-0.1	-0.3
Fixed capital investment, y-o-y, % change*	111.3	109.3	95.4	-0.6	-0.7	-4.1	-2.4	1.5	3.3
Net FDI flows, y-o-y, % change	-1.8	33.3	-51.3	-26.3	-68.2	-22.2	102.0	35.3	n.a.
Unemployment rate, %	5.3	6.2	7.2	4.5	4.8	5.9	8.1	4.7	3.9
Employment rate, %	42.9	38.4	34.3	40.5	41.1	37.9	34.5	41.1	42.7

Note: * - cumulative, (e) - estimate;

Source: NBS, NBM, and EG calculations and estimates: