Lucrări științifice ale Simpozionului Ştiinţific Internaţional al Tinerilor Cercetători, Ediția a XIX-a
16-17 aprilie 2021, Chișinău, Republica Moldova, e-ISBN 978-9975-155-41-0; DOI 10.5281/zenodo.5669643.

RETROSPECTIVE ANALYSIS OF THE BUDGETARY POLICY IN THE REPUBLIC OF MOLDOVA

ANALIZA RETROSPECTIVĂ A POLITICII BUGETARE ÎN REPUBLICA MOLDOVA

SCRIPNIC Diana, masterandă
Programul: Administrarea financiar-bancară
Academia de Studii Economice din Moldova
Republica Moldova, Chişinău, str. Bănulescu-Bodoni 61, www.ase.md
e-mail autor: dianascripnic@yahoo.com

Abstract: *Obiectivul primar al politicii bugetare a statului este asigurarea sustenabilității bugetului public. Prezentul articol propune o analiză retrospectivă a politicii bugetare în Republica Moldova prin prisma evaluării sustenabilității bugetare în contextul evoluțiilor macroeconomice din următoarele trei perioade: (i) 1991-2000, (ii) 2000-2008, și (iii) 2009-2019.*
Key Words: *finanțe publice, buget public national, politică bugetară, Republica Moldova*

JEL CLASSIFICATION: G2

INTRODUCTION

The primary objective of the budgetary policy is to ensure sustainability of the public budget. In the last three decades, since the proclamation of its independence, the Republic of Moldova has undertaken a complex process of reform and modernization of public finance management, which has been reflected in the applied budgetary policies.
The first period for analysing the budgetary policy can be considered the first years of independence of the Republic of Moldova, 1991-2000. From the public finance point of view, this period can be characterized by the establishment of the national budgetary system in the conditions of transition of the country to a market economy. This period was marked by the deepest economic recession in the Republic of Moldova and sharp deterioration of the fiscal balance.
The second notable period for which the budgetary policy is analysed is the period between 2000 and 2008. During this stage Moldovan economy registered a gradual recovery with a cumulative growth of 63% over 2000-2008, mainly due to migrant remittances. Therefore, the main priority of economic policies, including of the budgetary policy, became the stabilization and consolidation of this growth, by ensuring public finance equilibrium, i.e. a sustainable budget. Also, at the beginning of 2000s the public authorities initiated a comprehensive reform of public finance management.
Finally, the third period analysed in this study is the period between 2009-2019 which was marked by several economic, social and political events for the Republic of Moldova: 2009 economic crisis, 2014 EU-Moldova Association Agreement, famous billion-dollar theft of 2014 in three Moldovan banks resulted in a severe economic and financial crisis. All these challenges have had a great impact on the quality of public finance, and as a result, on the measures and actions undertaken by the authorities regarding public finance management.
In this context, the study proposes a retrospective analysis of the budgetary policy in the Republic of Moldova through the budget sustainability assessment point of view in the context of macroeconomic evolutions during the following three distinct periods: (i) years 1991-2000, (ii) 2000-2008, and (iii) 2009-2019.

SPECIALTY LITERATURE AND THE CONTRIBUTIONS OF THE STUDY

The main source for this research were the statistical official data and reports available on the official websites of the Ministry of Finance of the Republic of Moldova, the International Monetary Fund and the National Bureau of Statistics of the Republic of Moldova.

RESEARCH AIMS AND METHOD

The study is based on the analysis of the dynamics of main budgetary indicators calculated by the author based on the official data. The research methods used in this study are as follows: the documentary method, the qualitative and quantitative data method, the synthesis method, the comparison method, as well as the graphical method.

RESEARCH OF EMPIRICAL ASPECTS

Budgetary policy in 1991-2000

With the proclamation of the independence of the Republic of Moldova on August 27, 1991, the authorities initiated the process of establishing of the national budget system. Starting with this period and until the early 2000s, financial regulations, institutions participating in the budgetary process, mechanisms and tools used in the management of public finances were based on the principle of budgeting by means. At the same time, the applied budgetary policies and the main indicators of public finances were in direct correlation with the macroeconomic evolution of the national economy and main priorities of the general economic policy of the country.

During the period of 1991-2000, the Republic of Moldova was marked by a deep economic recession determined by various external and internal shocks. First, a sharp deterioration in its terms of trade, the loss of traditional markets after the break-up of the Soviet Union. The transformation from a centrally planned to a market-based economy implied drastic structural changes, resulting in output contraction and massive job losses. The adverse effects on output were compounded by droughts in 1992 and 1994 and the Transnistria military conflict in 1992. The declines in 1998 and 1999 reflected a collapse in exports following the 1998 regional crisis, as well as a slump in domestic demand. In 2000, the Moldovan economy again faced external shocks; this time in the form of drought and rising energy prices. As a result, real GDP have fallen on average by around 10% per year since 1991, bringing the cumulative decline to about 60% by 2000 (Figure 1).

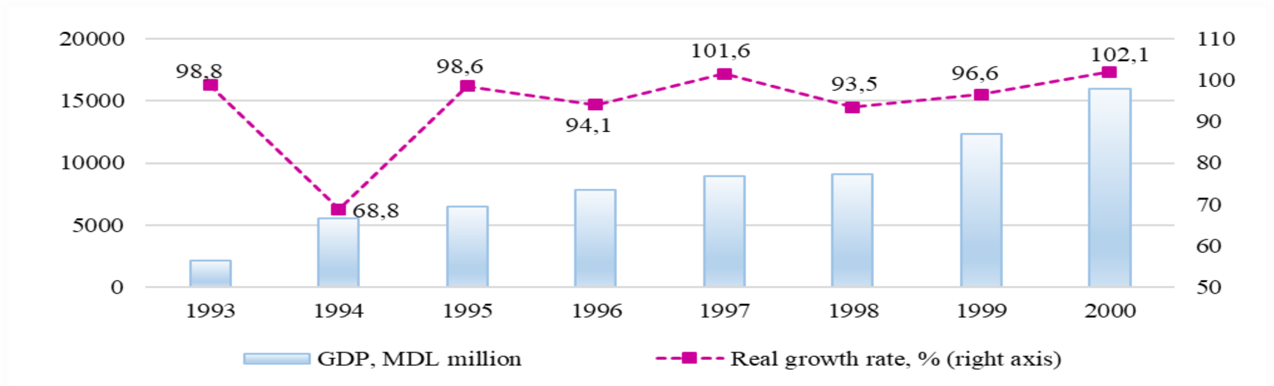

Figure 1. The dynamics of GDP in 1993-2000

Source: Elaborated by the author based on data of IMF and NBS

In line with the overall macroeconomic evolution, starting with 1991, the fiscal situation in Moldova deteriorated sharply as rising expenditures and lagging revenues pushed the consolidated government cash deficit to over 25% of GDP in 1992. From 1993, however, public finances improved as a result of expenditure cuts, especially in state enterprises, and of improved revenues. In 1993, the Government adopted a comprehensive program of financial stabilization supported by a stand-by arrangement with the International Monetary Fund. By 1995, the fiscal deficit had been cut to 5,8% of GDP (see Figure 2).

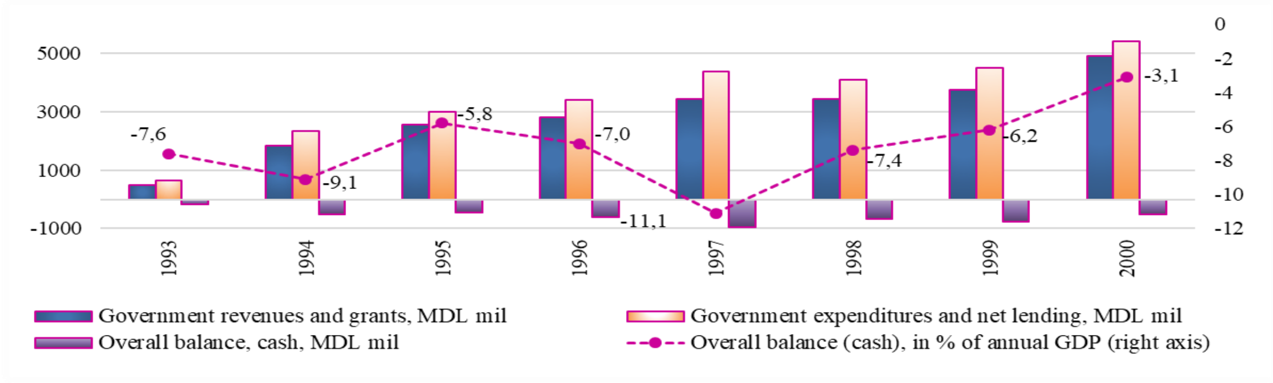

Figure 2. General Government Position in 1993-2000
Source: Elaborated by the author based on data of IMF and NBS

Between 1996 and 1998, Moldova's overall fiscal position severely deteriorated. The fiscal deficit was very high: 7,0% of GDP in 1996, 11,1% in 1999 and 7,4% in 1998, mostly because of non-payment of expenditure obligations that led to an increase in the stock of arrears on pensions and wages.

As a result, in 1996 the authorities adopted a 3-year program by resources under the extended IMF facility to accelerate and deepen structural reforms and consolidate the stabilization effort. It should be noted, that deficit financing reverted more to domestic source in 1997. Thus, in 1997 domestic financing was accounted for mainly by treasury bills sales, while external financing was denominated by proceeds of a Eurobond issue (USD 75 million) and the first tranche of the World Bank' s SAL II programme (USD 35 million).

Following the implementation by the Moldovan authorities of tight fiscal policies, and external financing, in 1999 and 2000 Moldova for the first time from 1991 achieved a fiscal adjustment, largely through a sizeable rationalization of public spending: the general government budget deficit decreased from over 11% of GDP in 1997 to about 3% of GDP in 2000. Underlying the fiscal tightening was a large reduction of expenditures, including, after years of delay, major efforts to eliminate excess capacity in the relatively sizable health and education sectors, as well as a partial hiring freeze, and the consolidated government revenues increasing, partly reflecting higher nontax revenues, although tax revenues increased also, reflecting buoyant indirect tax collections and improved VAT administration.

Conclusion: *During the period of 1991-2000 the applied budgetary policies and the main indicators of public finances were in direct correlation with the macroeconomic evolution of the national economy and main priorities of the general economic policy of the country. Thus, in the context of the deep economic crisis of the first years of independence of the Republic of Moldova the main objectives of budgetary policies implemented by public authorities were to ensure the financial resources necessary for the functioning of the fundamental social and economic sectors of the state: education and health systems, social protection, law enforcement, national defence and other public needs. In order to cover the budget deficit, the Republic of Moldova contracted external loans from the international financial institutions, which led to an increase in the level of the state debt.*

At the same time, substantial progress has been achieved during the first stage of the Republic of Moldova transition in transforming the national fiscal system into more effective instrument to implement public policy objectives within the framework of a market economy.

Budgetary policy in 2000-2008

The second notable period for which the budgetary policy is currently analysed is the period between 2000 and 2008, or namely the second decade of the Republic of Moldova transition. During this stage Moldovan economy registered a gradual recovery, mainly due to migrant remittances, which in 2004 represented about a third of GDP. Therefore, the main priority of economic policies, including for the budgetary policy, became the stabilization and consolidation of this growth, by ensuring public finance equilibrium, i.e. by ensuring a sustainable budget. In this context, and following Moldovan

16-17 aprilie 2021, Chişinău, Republica Moldova, e-ISBN 978-9975-155-41-0; DOI 10.5281/zenodo.5669643.

commitment to achieve the Millennium Development Goals, approved at the Millennium Summit in September 2000, the authorities initiated a broad reform of public finance management (PFM).

This period is also marked by continuous strategic planning actions at the country level, by developing the following national strategies: National Strategy for Economic Growth and Poverty Reduction, National Development Strategy for 2008-2011 and National Development Strategy of the Republic of Moldova - Moldova 2020. In order to support the practical application of the provisions of these policy documents, it was necessary to revise the budget planning process by increasing the time horizon, shifting the focus from resource-based planning (budgeting by means) to result-based approach (budgeting by program), but also to make a closer link between general economic policy and budgeting. This was possible through the introduction in 2002 of the Medium Term Budget Framework (MTBF) into the budgetary formulation process.

An important support for the PFM reform, as well as for the promotion of budgetary policies, was the development of the Unique Treasury Account (UTA) system, which was completed in March 2007, when all budgets, including the entire local budget system, as well as SSIB and MHIF, were executed through the UTA, opened at the National Bank of Moldova. All income is thus collected on the UTA, and all payments are made to this account. The operative control over the execution of expenditures is performed in the State Treasury within the Ministry of Finance and in the Territorial Treasuries. This has contributed to increasing the transparency and efficiency of budget management by consolidating all NPB balances.

An important stage of the reported period was the approval in December 2000 by the International Monetary Fund of a three-year loan under the Poverty Reduction and Growth Facility (PRGF) in an amount equivalent to USD 142 million to support the Moldovan government's new economic program The new economic program focused on policies that would help the country achieve sustainable economic growth and reduce poverty, and also reduce the country's high external debt burden.

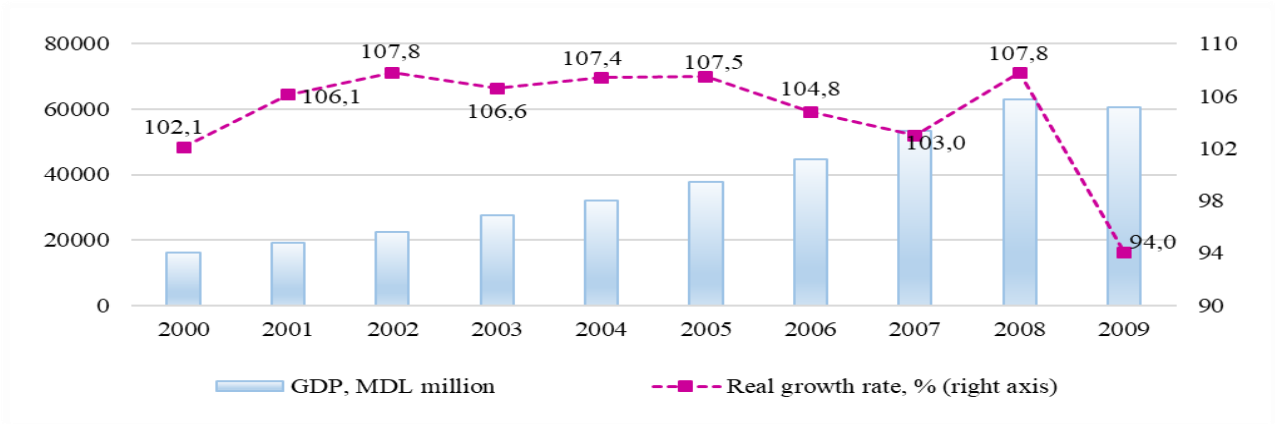

Figure 3. The dynamics of GDP in 2000-2009

Source: Elaborated by the author based on data of NBS

Moldova experienced strong growth over 2000–2008, accompanied by signs of overheating. Growth averaged 6 percent annually (Figure 3), boosted by remittances (in 2004, the total gross inflows of workers' remittances reached almost 27% of GDP) and foreign investment. Buoyant domestic demand, however, pushed up the current account deficit and generated inflation pressures. These pressures, together with large inflows, resulted in substantial appreciation of Moldova's real effective exchange rate. Monetary policy kept real interest rates low despite double-digit inflation.

Although budgetary policy maintained a small headline budget deficit under the IMF PRGF-program, it grew increasingly procyclical, with the estimated structural balance deteriorating from a surplus of 1,5% in 2005 to a deficit of 1% by 2008 (Figure 4).

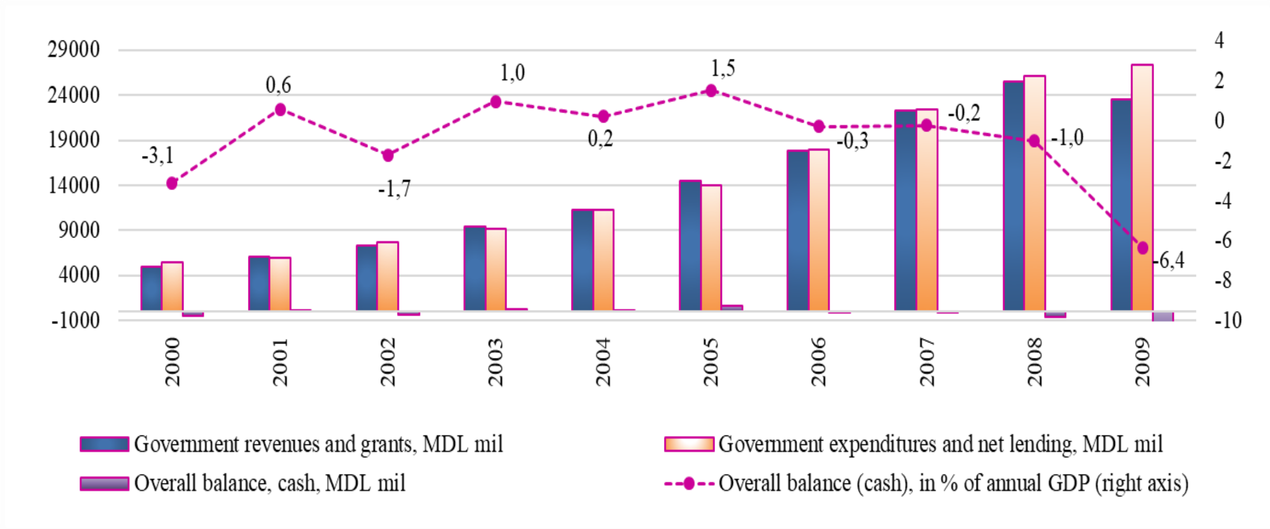

Figure 4. General Government Position in 1993-2000
Source: Elaborated by the author based on data of MF and NBS

Conclusion: During the period of 2000-2008 policy discussions were dominated by four interrelated topics: the sustainability of the economic growth; the appropriate macroeconomic policy mix; the role of remittances; and policies to improve the business environment. In the context of economic recovery and in order to ensuring macroeconomic stabilization for supporting the growth the budgetary policy applied by the authorities can be characterised as expansionary.
To ensure fiscal sustainability, the budgetary policy benefited from a more forward-looking perspective and greater reliance on a medium-term expenditure framework firstly introduced in the Republic of Moldova for the budgetary formation process in 2002 for the period of 2003-2005.
Budgetary policy in 2009-2019
Starting with 2009 the Republic of Moldova has experienced a very complex period marked by several economic, social and political events. Thus, at the beginning of 2009, due to the global financial crisis of 2007/2008, the economic activity slowed. The GDP decreased by 6% in 2009 as compared to 2008. A steep fall in household consumption was driven by a large drop in remittance inflows. Sharply higher domestic unemployment further constrained household consumption. Investment fell substantially owing to more difficult borrowing conditions and weak business confidence. With all of Moldova’s export markets entering into recession in 2009, foreign sales dropped significantly.
Another, with an unprecedented character shock on the Moldovan economy, was the 2014 massive fraud in three Moldovan banks. The banking crisis lowered confidence in the banking sector, leading to significant interest rate increases and reduced credit to the private sector.
The monetary and fiscal cost involved in rescuing the three insolvent banks (amounting to 12 percent of GDP) led to higher public debt and lower foreign exchange reserves, damaged business confidence, and reduced the macroeconomic buffers against economic shocks. Thus, after registered a comfortable high growth rate of 5,0% in 2014, the Moldovan economy contracted by 0.3% in 2015 (Figure 5).

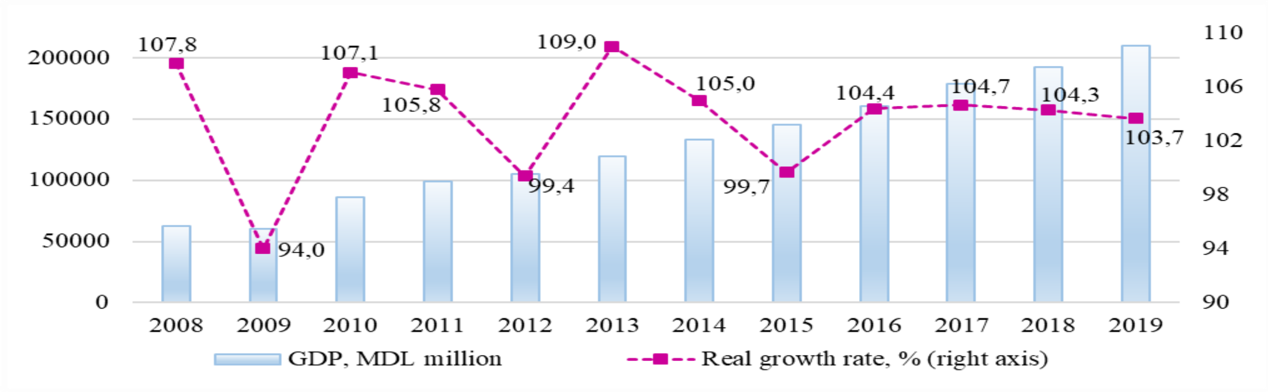

Figure 5. The dynamics of GDP in 2008-2019
Source: Elaborated by the author based on data of NBS

All these challenges, of course have had a great impact on the quality of public finance, and as a result, on the measures and actions undertaken by the authorities regarding public finance management.

Thus, the crisis of 2009, and pre-election spending hikes, resulted in a large increase in the fiscal deficit: from 1,0% in 2008 to 6,4% as a share of GDP in 2009 (Figure 6). In 2009, budget revenues dropped by about 10% in real terms relative to 2008. At the same time, current expenditures increased by over 13% in real terms, driven by large increases in public sector wages and pensions in the run-up to the elections of April 2009, financed partly by heavy domestic borrowing. Despite the recession, public sector wages rose in 2009 by 8.6% in real terms, whereas they decreased in the domestic economy. The previous government's pre-election wage policies were largely responsible for the overall increase in salaries during the recession. The budget began to experience financing shortfalls, and arrears started to accumulate. In this context, public debt as a percentage of GDP has registered a sharp increase.

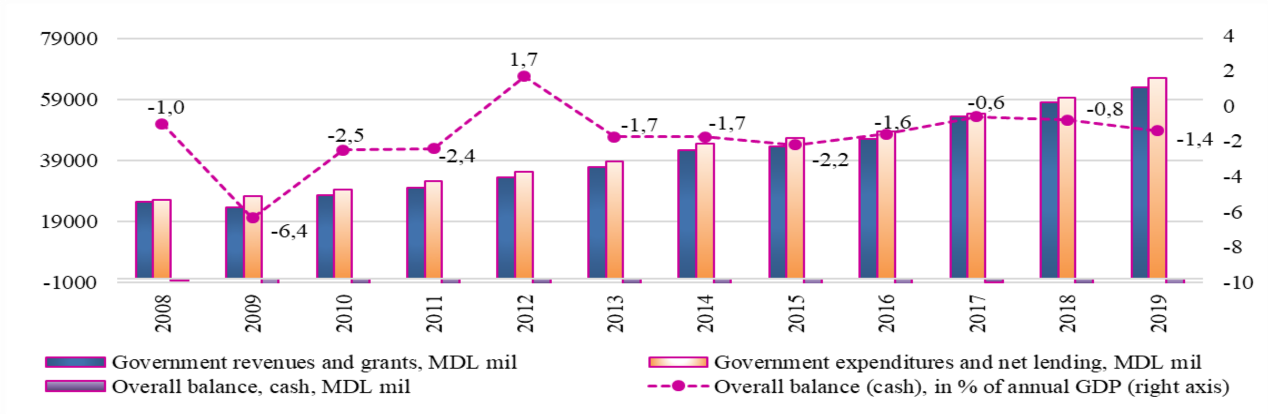

Figure 6. General Government Position in 2008-2019
Source: Elaborated by the author based on data of MF and NBS

Following the sharp deterioration of the fiscal position, in October 2009 Moldova signed a lending agreement with the IMF which provided support of around USD 560 million and an additional special loan of USD 150 million for short-term financing of the budget deficit. The economic programme linked to this agreement had four priority areas: i) fiscal policies to restore sustainability, while safeguarding public investment and social spending priorities; ii) flexible monetary and exchange rate policies to keep inflation under control, facilitate adjustment to shocks, and rebuild foreign reserves; iii) policies to ensure financial stability by early detection of bank difficulties and strengthening the legal framework for bank rehabilitation; and iv) structural reforms to raise the economy's potential. The programme's macroeconomic objectives for 2010 were optimistic: growth was projected to reach 1.5% as a result of gradual recovery in external and domestic demand and an improved business environment, and the programme allowed a return to budget balance towards 2014. Assuming that growth will return in 2010 and accelerate in the next few years in line with the authorities' recovery programme, the current upsurge should be temporary and should allow the debt to fall again as from 2012.

Also, a negative impact on the public finance equilibrium has had the 2014 banking crisis. Thus, this crisis resulted in an increase in the fiscal deficit: from 1,7% in 2014 to 2,2% as a share of GDP in 2015. Also, the crisis led to an unprecedented, by 3-times, increase in the amount of the domestic debt and the increase in the public debt. In order to avoid financial instability following the banking crisis, in September 2016, the Parliament of the Republic of Moldova approved the law on converting into a state debt the credit issued by the National Bank to three banks in 2014-2015. Converting MDL 13,34 billion NBM loan into public debt for the next 25 years meant: tripling the size of domestic debt from MDL 7,2 billion at the beginning of 2016 to over MDL 22 billion at the end of 2016. Also, the budget cost incurred with repayment and service of MDL 13,34 billion worth total of MDL 25 billion at the extent of the following 25 years.

Finally, in order to understand the evolution of the budgetary policies in 2009-2019 a general presentation of the actions undertaken by the authorities in the field of public finance management and budgetary policies priorities is necessary. Thus, during this period, the Public Finance Management Project launched in the Republic of Moldova in 2006 with the support of the World Bank has continued. The most important part of the project activities consisted in strengthening the budget formulation process and methodology applied, including the MTBF methodology. In this view, the methodological set for budget preparation, approval and modification of the budget was formulated in order to integrate the medium-term budgetary planning in the annual budget cycle.

The most important innovation of this reform, however, was the formulation of the methodology for planning and executing the budget on a program-based basis, which was later implemented in practice and initially implemented at the central government level. An important step in modernizing public finances was the elaboration in 2015 of the new budget classification developed in accordance with the requirements of IMF standards, Government Financial Statistics (GFS) of 2001. The extension of the reform in the field of budget planning in the Republic of Moldova was stipulated in the Association Agreement between the Republic of Moldova and the European Union (EU) in 2014. Thus, the application of best practices in public finance management will ensure sustainability, performance, transparency and responsibility in managing public finances.

Conclusions: Starting with 2009 the Republic of Moldova has experienced a very complex period marked by several economic, social and political events. All these challenges have had a great impact on the quality of public finance, and as a result, on the measures and actions undertaken by the authorities regarding public finance management and budgetary policies priorities.

From the budgetary policy priorities view, the main short- and medium-term objective remains the implementation of structural reforms, the consolidation of public finances and financial stability as prerequisites for achieving fiscal sustainability by maintaining a national public budget deficit at sustainable level, avoiding the risks posed by internal and external shocks, as well as dependency on external financial aid.

CONCLUSIONS

The budgetary policies promoted by the Republic of Moldova in 1991-2019 gradually evolved under a complex process of reforming and modernization of public finance management. At the same time, they must be examined under the following two aspects:

1. in the context of macroeconomic developments in the country and the general economic policy of the state: the analysis showed a strong correlation between macroeconomic evolution and the budgetary sustainability, especially, this correlation was significant during the major economic crisis in the Republic of Moldova in 1992, 1998, 2009 and 2014; and

2. in the context of the public finance management reform undertaken by the authorities in order to align with international standards: the analysis revealed a positive impact of the finance management reform on the budgetary process and fiscal sustainability.

Also, an important aspect that must be taken into account when analysing budgetary sustainability is the political context and political decisions (especially, in the pre-elections periods) that can affect the major components of the public budget and public debt.
External financing is also a very important component when analysing the evolution of the public budget. The survey revealed the positive impact of the external financing of the budget deficit, especially in the first years of the independence of the Republic of Moldova.

BIBLIOGRAPHY:

1. Official web site of the Ministry of Finance of the Republic of Moldova: https://mf.gov.md/en/buget
2. Republic of Moldova: Recent Economic Developments. International Monetary Fund. Country Report. No. 98/58. June 1998 https://www.imf.org/en/Publications/CR/Issues/2016/12/30/Moldova-Recent-Economic-Developments-2668. Moldova : Recent Economic Developments
3. Republic of Moldova: Recent Economic Developments. International Monetary Fund. Country Report. No. 01/22. January 2001 https://www.imf.org/en/Publications/CR/Issues/2016/12/30/Republic-of-Moldova-Recent-Economic-Developments-3999 Moldova: Recent Economic Developments
4. Republic of Moldova: Statistical Appendix. International Monetary Fund. Country Report. No. 04/40. February 2004 https://www.imf.org/en/Publications/CR/Issues/2016/12/30/Republic-of-Moldova-Statistical-Appendix-17195. Republic of Moldova: Statistical Appendix
5. Press Release: IMF Approves in Principle Loan of US$142 Million for Poverty Reduction and Growth in Moldova, December 15, 2000 https://www.imf.org/en/News/Articles/2015/09/14/01/49/pr0072
6. Moldova. Paths to sustained prosperity A Systematic Country Diagnostic. August 2016, World Bank Group. pag.6 http://documents1.worldbank.org/curated/en/465041475522681625/pdf/Moldova-SCD-clean-09232016.pdf
7. National Bureau of Statistics: Conturi nationale, Dinamica principalilor indicatori macroeconomici (1995-2019) https://statistica.gov.md/category.php?l=ro&idc=191&
8. Budgeting in Moldova. OECD Journal on Budgeting Volume 2010/3 © OECD 2010 https://www.oecd.org/gov/budgeting/48170693.pdf
9. Radiography Of A Bank Fraud In Moldova: From Money Laundering To Billion Fraud And State Debt. December 20, 2016. Transparency Moldova http://www.transparency.md/2016/12/20/radiography-of-a-bank-fraud-in-moldova-from-money-laundering-to-billion-fraud-and-state-debt/
10. The 2019-21 Medium-Term Budgetary Framework. Chapter. I. A. Introduction. pag.3 https://mf.gov.md/sites/default/files/documente%20relevante/CBTM%202019-2021_ENG.pdf

---

Coordonator științific: PETROIA Andrei, dr., conf. univ.
Academia de Studii Economice din Moldova,
Republica Moldova, or. Chișinău, str. Mitropolit Bănulescu-Bodoni, 61, www.ase.md
e-mail: apetroia@ase.md