

■ 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.

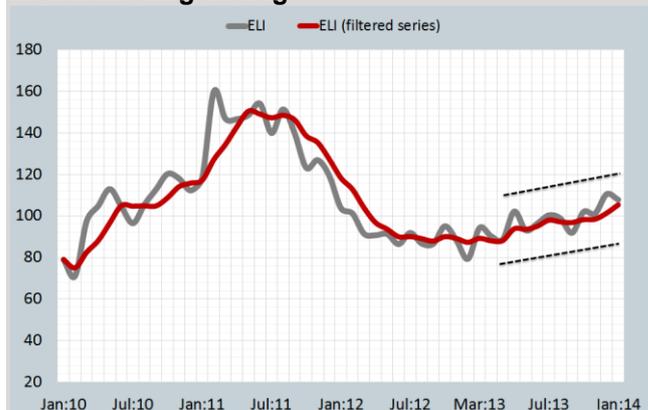
The economic situation keeps improving, but still some concerns arise.

The Economic Leading Indicator in Jan:14 continued an ascending trend, having increased up to 105.4 points (101.4 points in Dec:13). The rise was facilitated by the development of exports, domestic demand and lending activity. Nevertheless, several external and internal risks persist, that could undermine the pace of economic growth.

The growth is not balanced and, rather, unevenly distributed across the economic sectors. Despite the increase in the Industrial Production Index by 6.8% in 2013, y-o-y, it was fueled mainly by 3 branches that ensure 25.7% of the gross value added (GVA) in the industrial sector: production of electric machinery and devices; production of other foodstuff; and manufacture of other products from non-metallic minerals. At the same time, the sectors that ensured 48% of the GVA remained trapped in recession. In part, these imbalances were induced by a similarly ambiguous evolution of exports. Despite the rise in total exports by 11% y-o-y in 2013, a decline has been registered of exports to a number of countries representing over 40% of the external markets of Moldova. Particularly, the supplies to the first and third most important external markets (Russia and Italy) decreased by 3.5% and 8.4%, respectively, y-o-y. Some discrepancies are found with respect to the increase in remittances: despite the total growth of 14.2% y-o-y in Dec:13, the transfers from abroad to individuals in US dollars diminished by about 9% y-o-y. Along with the depreciation of the Russian ruble against the Moldovan leu, these trends undermined the incomes expressed in MDL of the families that have migrants in CIS. In the banking sector, the trends are also ambiguous. Thus, the amount of new loans increased robustly by 56.2% y-o-y in Jan:14 in parallel with an increase in the share of non-performing loans from 11.6% in Dec:13 to 11.8% in Jan:14. At the same time, the volume of new time deposits in foreign currency decreased by 18.2%, causing a 5.6% reduction in total deposits y-o-y in Jan:14.

In the upcoming months, the economic growth is expected to slow down on the ground of some internal and external constraints. The internal factors include the dissipation of the compensatory growth effect in agriculture and of the effects of easy monetary policy, the repercussions of national currency depreciation on the incomes of most of the population and the uncertainty related to the proximity of the Parliamentary elections. The external factors relate to restrictions on imports from Moldova applied by the Russian authorities and tightening of the migration regime for Moldovan citizens working in this country. At the same time, the difficult economic situation in Russia, Ukraine, Kazakhstan, as well as some EU countries (Italy, Hungary) could negatively affect the industrial branches oriented towards these markets, as well as the inflows of remittances during 2014.

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

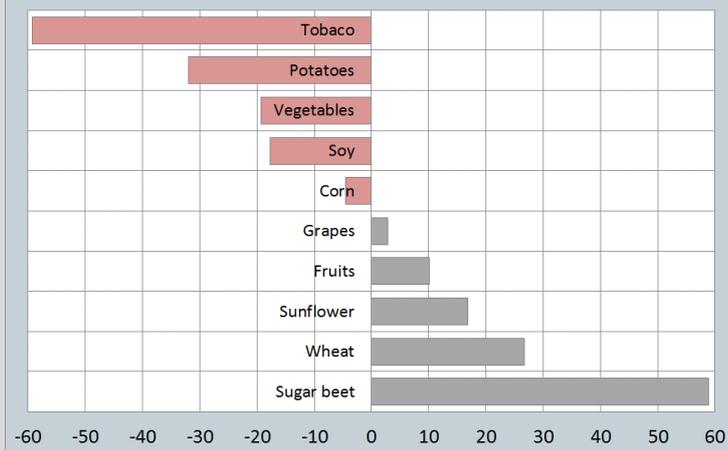


Source: EXPERT-GRUP calculations on the basis of the data provided by the NBS and NBM;

¹ For January, the amount of remittances and exports was estimated by authors.

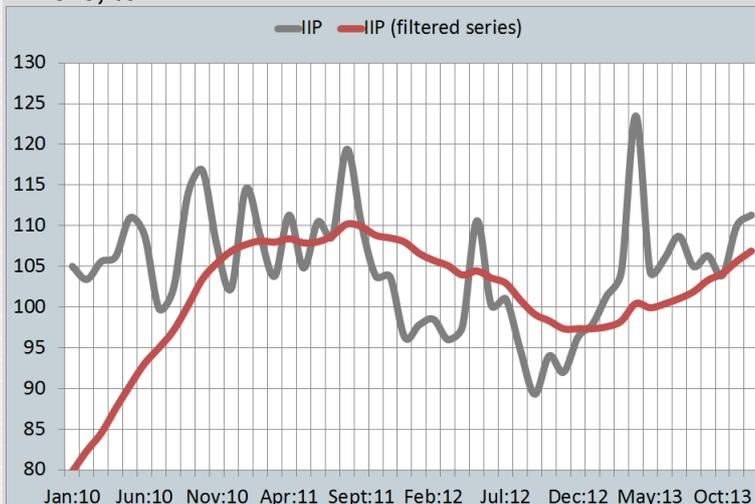
■ Main Economic Trends

Figure 1. Harvest by Agricultural Crops, change in 2013 versus 2011, %



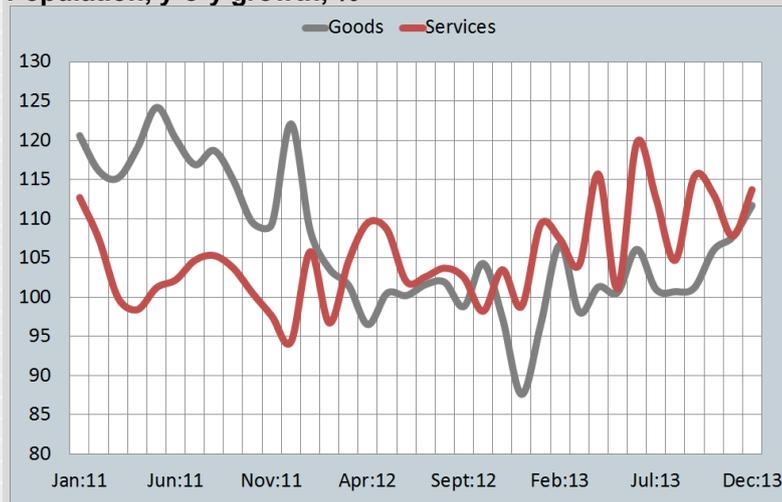
Source: NBS

Figure 2. Contribution of Sub-Sectors to the Industry Growth in 2013, %



Source: NBS

Figure 3. (Retail) Trade and Services provided to the Population, y-o-y growth, %



Source: NBS

AGRICULTURE

Despite the spectacular recovery of the vegetable sector in 2013 versus 2012, the harvest of several crops continued to be under the values of 2011. The following crops had a higher harvest in 2013 than in 2011: sugar beet (+59%), wheat (+26,7%), sunflower (+10,9%). On the other hand, the following crops had a lower harvest than in 2011: potatoes (-31,9%), vegetables (-19,3%) or corn seeds (-4,6%).

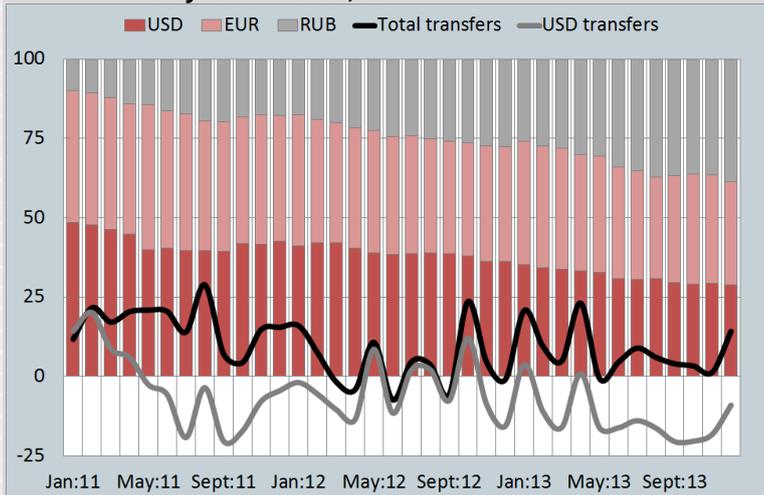
INDUSTRY

The 6.8% growth in 2013 was mainly due to the branches that together hold 25.7% of the value added in industry. A cumulated contribution of +7.2% was ensured by: production of electric machinery and devices (+3,7%), production of other foodstuff (+1,9%) and manufacture of other products from non-metallic minerals (+1,6%). At the same time, the sectors that hold a share of 48% of gross value added declined.

DOMESTIC TRADE IN GOODS AND SERVICES

The retail trade consolidated its growth and the services provided to population posted high growth rates. The retail trade had low dynamics and increased in 2013 by only 3.1%, despite the acceleration noticed at the end of the year: in Dec:13 it grew by 11.7%. In Dec:13, the services provided to the population increased by 13.7% y-o-y, while the annual growth was 10.7%.

Figure 4. Total and USD Transfers, y-o-y growth, %; Structure of Transfers by Currencies, %

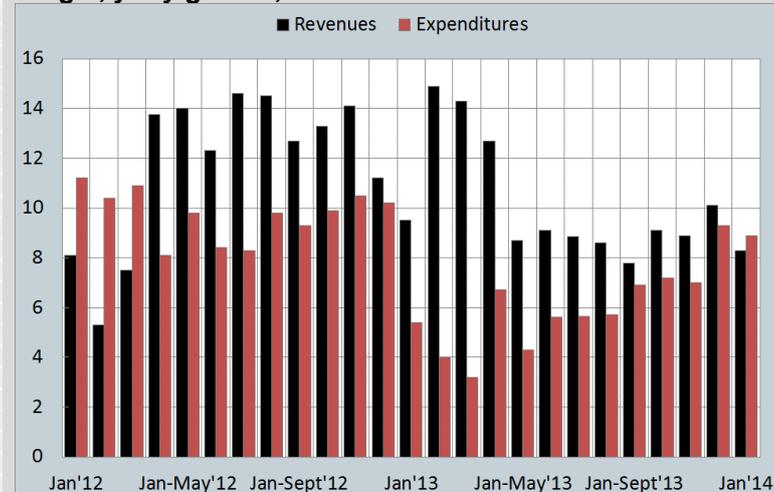


Source: NBM

INCOME AND EXPENSES OF THE POPULATION

The decrease in USD transfers and the depreciation of RUB with respect to MDL reduced the MDL incomes of families whose members are working in Russia. The RUB depreciated by 11.4% y-o-y in Jan:14 against USD and by 2.3% y-o-y in Jan:14 against MDL. Depreciation of MDL against USD (7% in Dec:13 y-o-y) did not compensate the decrease in remittances in USD (-9% y-o-y in Dec:13).

Figure 5. Revenues and Expenses of the National Public Budget, y-o-y growth, %

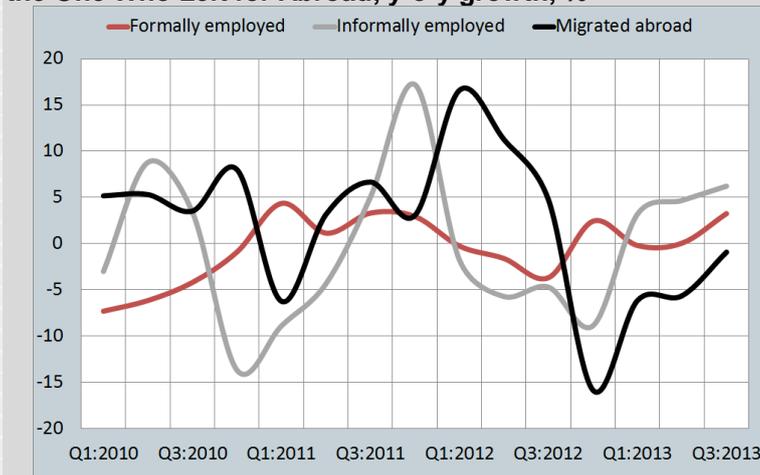


Source: Ministry of Finance

PUBLIC FINANCE

The year started with a growth rate of budgetary expenses exceeding the rate of public revenues, which put pressures on public finances. In Jan:14 the revenues of the National Public Budget increased by 8.3% y-o-y, whereas the public spending increased by 8.9% y-o-y. A stronger increase in budget expenses compared to revenues does not augur well for fiscal consolidation and could be induced by the upcoming Parliamentary elections.

Figure 6. Population with Formal/Informal Employment and the One Who Left for Abroad, y-o-y growth, %

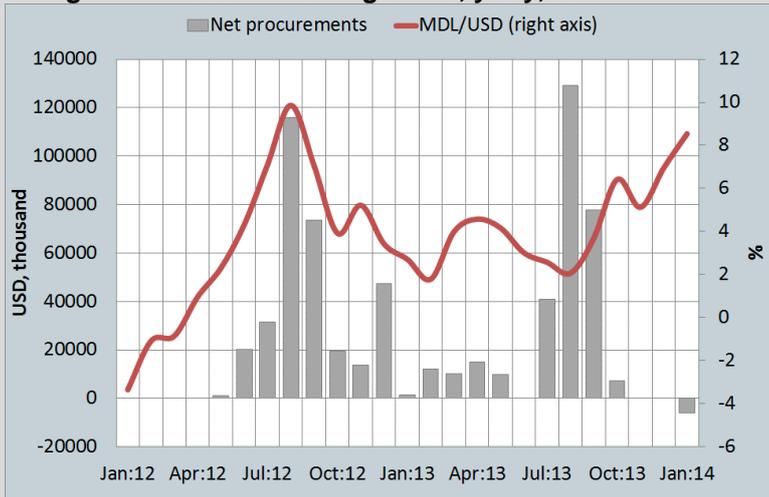


Source: NBS

LABOR MARKET

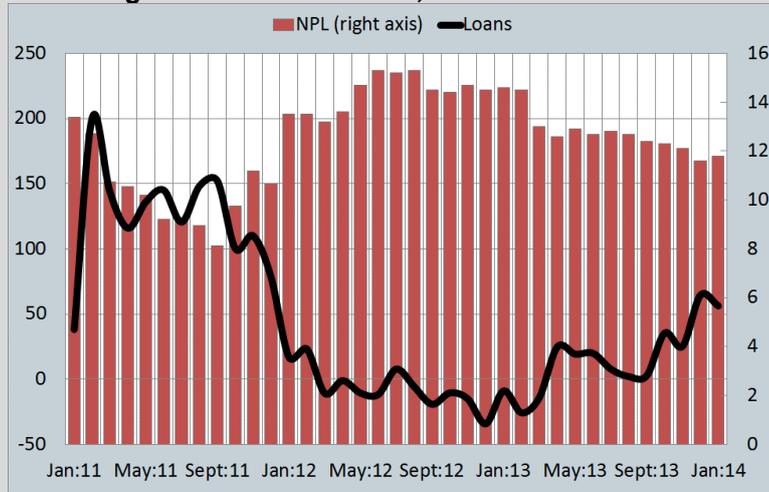
Informal employment increases faster than the formal one, while the number of citizens abroad is getting lower. The formally employed population increased by 3.2% y-o-y in Q3:13. The informally employed population increased by 6.2% y-o-y, thus having increased the third quarter in a row. The population that is abroad decreases. Thus, in Q3:13 the reduction accounted for -0.9% y-o-y compared to -5.6% in Q2:13 and -6.2% in Q1:13.

**Figure 7. Net Procurements of Currency, USD thousands;
Change of MDL/USD Exchange Rate, y-o-y, %**



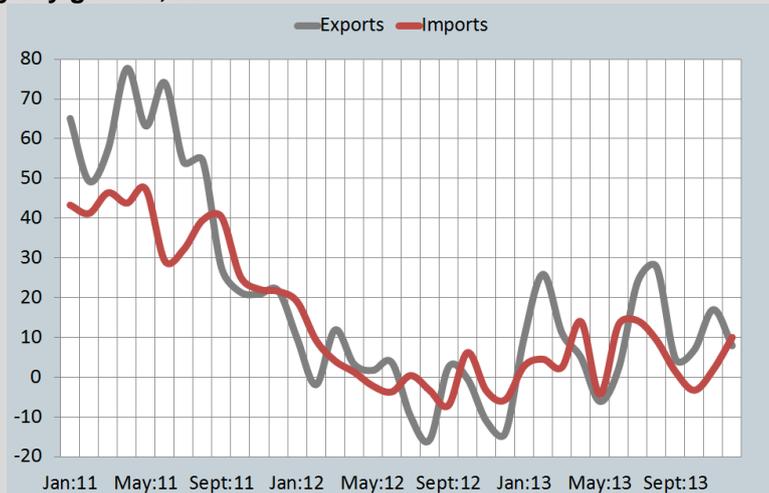
Source: NBS and NBM

Figure 8. New Loans, y-o-y growth and the Share of Non-Performing Loans in Total Loans, %



Source: NBM

Figure 9. Foreign Trade in Goods of the Republic of Moldova, y-o-y growth, %



Source: NBS

PRICES AND MONETARY POLICY

The central bank continues to promote an easy policy, though the depreciation of the national currency is not caused by the NBM interventions. In Jan:14, the national currency continued to depreciate compared to the main reference currencies - by **8,5%** y-o-y against USD and by **11.5%** y-o-y against EUR. NBM kept an accommodative monetary policy stance and maintained its policy rate at the historical minimum of **3.5%**, whereas the inflation forecast remain in the targeted interval.

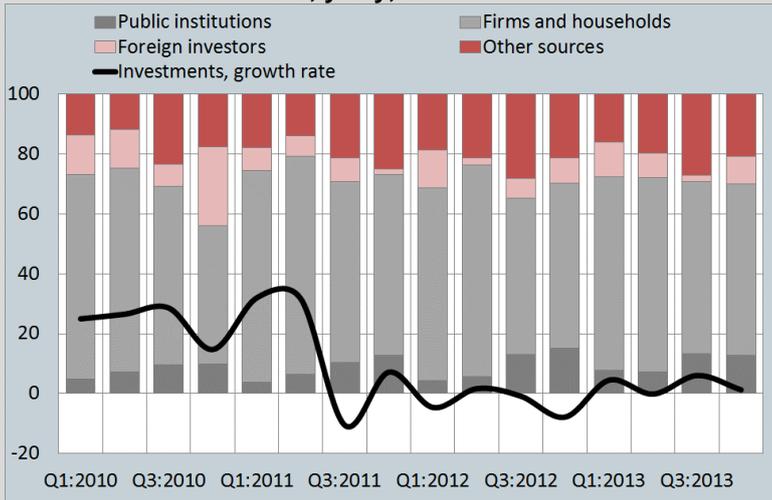
BANKING SYSTEM

The banks' lending activity continues to increase at a slower pace, while the share of non-performing loans is stabilizing. In Jan:14, the amount of new loans increased by **56.2%** y-o-y, slowing down compared to the increase of Dec:13, when it was **64.4%** y-o-y. In Jan:14, the share of non-performing loans in total credit portfolios accounted for **11.8%**, being close to **11.6%**, which was registered in Dec:13.

FOREIGN TRADE

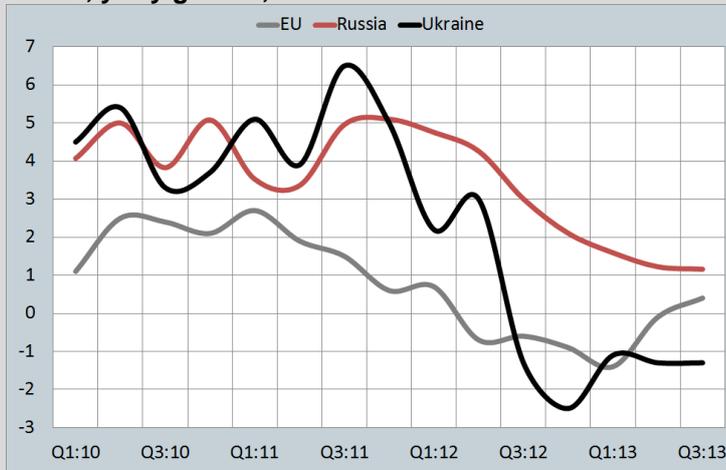
In 2013, the increase in exports slowed down, due to declining supplies to CIS. In 2013, the exports of goods increased by **11%**, while the imports increased by **5.4%**. However, in Sept-Dec:13, the export to CIS shrank by **9.2%** y-o-y, which was determined by a slowing of economic growth in the Russian Federation and the restrictions applied by the Russian authorities to imports of agricultural products and foodstuff from Moldova.

Figure 10. Structure of Investment by Funding Sources, %; Investment Growth Rate, y-o-y, %



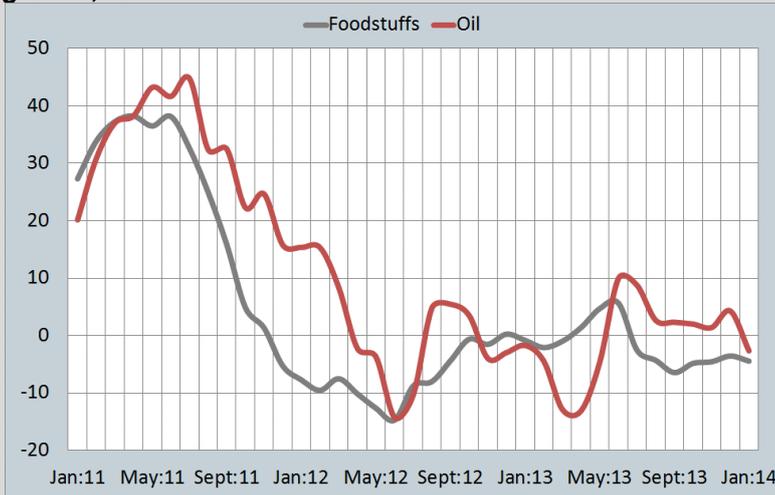
Source: NBS

Figure 11. Economic Growth of Moldova's Main Commercial Partners, y-o-y growth, %



Source: Eurostat, Federal State Statistics Service of Russia, State Statistics Service of Ukraine

Figure 12. World Food Price and Average Oil Price, y-o-y growth, %



Source: IMF and FAOUN

INVESTMENT ACTIVITY

Increase of investments by 2.3% in 2013 allowed just a partial recovery after the -4.2% decline in 2012. In 2013 the largest contribution to the increase was provided by investments from budgetary sources (+1.3%) and from other sources (+0.9%). On the other hand, the investment financed by businesses and population did not contribute to the increase (+0%), while the ones made by foreign investors had an insignificant influence (+0.1%).

MAIN TRADING PARTNERS

The biggest challenges for the Republic of Moldova come from the CIS. EU economy started to recover with a 0.4% growth y-o-y in Q3:13. However economic slowdown continues in the Russian Federation: in Q3:13 the GDP growth rate was 1.2% y-o-y and there is a persistent risk of setting additional restrictions on the imports from the Republic of Moldova. Economy of Ukraine is stagnating and the political developments could aggravate the situation this year.

GLOBAL MARKETS

Price decreasing trends are noticed on the global markets. Starting with Jul:13, the food prices have decreased and since Oct:13 the decrease has stabilized and varies between -3.5% and -4.8% y-o-y (-4.4% y-o-y in Jan:14). Since Jun:13, the growth of oil price slowed down (except for Dec:13). At the same time, a -2.6% decrease y-o-y was registered in Jan:14.

■ Key policy developments in February 2014

Policy Developments	EXPERT-GRUP comment
<p>6 February. The NBM decided to block the right to vote for 2 groups of shareholders that together hold about 30% of Victoriabank's stocks. On the same day, the General Meeting of shareholders was organized, where the new Administration Board and Steering Committee of the bank were elected.</p>	<p>This blocking affected the groups that include Asito and Moldasig companies, who previously procured in a "suspicious" way Victoriabank's stocks by buying packages under 5%, avoiding the need to ask the NBM's permission. The NBM action came exactly after the Chairperson of Victoriabank declared that the group of shareholders acted in concert. Most likely, there is some "revenge" taking place in the financial sector and the intervention of NBM, which is generally justified, came to favor one of the "belligerents". It seems that the conflict of interested has not ended yet and will keep affecting the sector in the future. In this context, the empowered institutions should be cautious and respond quickly and efficiently in order to ensure the financial security of the country.</p>
<p>11 February. The Ministry of Economy submitted its Activity Report for 2013. It stipulates that in 2013 almost all types of economic activities progressed, culminating with an economic growth of 8% in Jan-Sept:13. The Ministry estimated that the Gross Domestic Product will increase by 4% in 2014.</p>	<p>The GDP growth in 2013 was caused by circumstantial effects and is not underlain by a qualitative leap. The spectacular growth of agriculture by over 38% contributed to more than half of the economic growth, but the influence of this sector will not be constant in the future. The national economy continues to struggle with the traditional constraints: inefficient justice and public institutions; unfavorable business environment; high level of corruption. The failure to reform these sectors will not allow ensuring a sustainable social-economic development.</p>
<p>26 February. The Government decided to exclude 13 entities from the privatization list, including: Moldtelecom, Aroma, North and North-West Power Distribution Networks and Power and Heat Centrals).</p>	<p>This decision was influenced politically. Privatization is a specific issue, which the population has a reluctant attitude to. On the other hand, this Government has already got a negative reputation related to the concession of state-owned assets, so that launching a new round of privatization would be at once considered unsuitable or even fraudulent. In these circumstances, involvement in another privatization campaign in an electoral year could diminish the electoral score, which is not suitable for the current Government. At the same time, the postponement does not solve the issues related to the privatization process. Streamlining the management of public property, including the concession of assets to the private sector can be achieved only after raising the awareness of dignitaries and the transparency of the decision-making.</p>
<p>27 February. The National Bank of Moldova accused several banks of currency speculation. NBM suspects several banks from the Republic of Moldova of provoking artificial appreciation of the European currency and in order to investigate this phenomenon, a working group was established.</p>	<p>Most likely, some banks tried to speculate on the depreciations of the national currency. By setting exaggerated exchange rates, the intention was to alert the general public, who would have started buying massively foreign currency. At the same time, it is not excluded that this game is a move of one of the parties involved in the "revenge" on the financial market. NBM has the necessary tools to combat speculative games on the market, so just quick response is needed.</p>
<p>27 February. The European Parliament voted to annul the visa regime for the citizens of the Republic of Moldova. However, there's still at least 2 months left before this decision comes into force.</p>	<p>This decision will strengthen the relations between the Republic of Moldova and the EU and is an important step in the European integration process. Nevertheless, this success is not a direct consequence of implementing reforms in the Republic of Moldova. EU needs a "success story" in the "Eastern Partnership" and after the failure with Ukraine and Armenia, Moldova was assigned this role. At the same time, in the context of "pushing" the alternative of adhering to joining the Customs Union, crystallizing the Moldovans' preferences for European integration could be achieved by a tangible offer, the circulation to EU being liberalized for this reason.</p>

Statistical Annexes

Table 1. Main monthly indicators

Indicator	Jan:13	Feb:13	Mar:13	Apr:13	May:13	Jun:13	Jul:13	Aug:13	Sep:13	Oct:13	Nov:13	Dec:13	Jan:13
Industrial production, y-o-y, % change	-2.1	1.4	4.3	23.5	4.3	6.0	8.7	5.0	6.3	3.9	10.0	11.3	n.a.
Retail trade, y-o-y, % change	-3.5	6.7	-1.9	1.3	0.6	6.1	1.0	0.7	1.2	6	7.7	11.7	n.a.
Services to the population, y-o-y, % change	9.3	7.4	4.1	15.7	1.1	19.7	12.6	4.7	15.4	13.1	7.8	13.7	n.a.
Export of goods, y-o-y, % change	9.9	25.9	11.1	5.0	-6.1	2.3	24.0	27.7	4.6	6.9	17	7.9	n.a.
Import of goods, y-o-y, % change	2.8	4.5	2.5	13.9	-4.3	13.3	14.2	9.3	1.4	-3.3	1.9	10	n.a.
Official reserve assets, million USD	2519.7	2488.1	2469.1	2481.0	2475.3	2466.6	2507.6	2629.9	2722.2	2810.1	2813.1	2820.6	2812.6
Freighted cargo, y-o-y, % change	-13.5	41.3	31.0	25.2	1.2	5.3	25.4	40.1	34.3	19.5	33	65.9	n.a.
Registered unemployed at NEA (e-o-p)	26643	27160	26324	24723	22107	19991	18670	17582	14846	17252	19045	n.a.	n.a.
Real salary, y-o-y, % change	3.9	2.3	6.7	6.8	1.9	-6.5	4.8	5.5	5.7	3.8	2.5	4.6	n.a.
Budgetary revenues, y-o-y, % change*	9.5	14.9	14.3	12.7	8.7	9.1	8.9	8.6	7.8	9.1	8.9	10.1	8.3
CPI, y-o-y, %	4.6	4.4	4.2	4.5	5.7	5.5	4.3	3.7	3.9	4.7	4.9	5.2	5.1
IPPI, y-o-y, %	1.6	2.8	3.4	3.7	3.0	2.9	3.3	3.4	3.4	4.1	3	4	n.a.
Nominal exchange rate MDL/USD (e-o-p)	12.10	12.25	12.41	12.31	12.52	12.53	12.73	12.82	12.95	12.82	13.12	13.06	13.39
Money transfers from abroad, y-o-y, % change	22.6	9.7	4.9	23.1	-0.5	4.5	9.1	6.0	4.1	3.3	1.3	14.2	n.a.
M2 monetary aggregate, y-o-y, % change	27.2	26.1	23.4	25.0	26.7	26.7	26.4	25.7	25.0	34.8	29	29.2	26.3
NBM base interest rate, y-o-y, %	4.5	4.5	4.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5
Bank deposits interest rate, %	8.55	8.56	8.09	7.33	7.75	6.79	7.16	7.18	6.62	6.54	6.35	5.82	5.91
Bank lending rate, %	12.41	13.23	12.77	12.4	12.21	12.03	12.05	12.09	11.79	11.94	12.1	12.51	12.29
Non-performing loans, % of total loans	14.6	14.5	13.0	12.6	12.9	12.7	12.8	12.7	12.4	12.3	12.1	11.6	11.8

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

Table 2. Main quarterly indicators

Indicator	Q4:11	Q1:12	Q2:12	Q3:12	Q4:12	Q1:13	Q2:13	Q3:13	Q4:13
Real GDP growth, y-o-y*, %	6.4	1.0	0.8	-0.2	-0.7	3.5	6.1	12.9	n.a.
Agricultural production, y-o-y, % change*	4.6	0.6	-2.1	-21.6	-22.4	-1.0	2.8	30.2	38.3
Construction works, y-o-y, % change*	1.4	4.9	3.6	0.8	-1.3	3.7	-0.1	-0.3	1.6
Fixed capital investment, y-o-y, % change*	109.3	95.4	-0.6	-0.7	-4.1	-2.4	1.5	3.3	2.3
Net FDI flows, y-o-y, % change	33.3	-51.3	-26.3	-68.2	-22.2	102.0	42.1	2.1	n.a.
Unemployment rate, %	6.2	7.2	4.5	4.8	5.9	8.1	4.7	3.9	n.a.
Employment rate, %	38.4	34.3	40.5	41.1	37.9	34.5	41.1	42.7	n.a.

Note: * - cumulative; (e) – estimate;

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