


# Toward Green and Inclusive Growth: Case of the Republic of Moldova

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## Introduction

The pandemic COVID-19 crisis caused the biggest decline of the Moldovan economy in the last 20 years. In 2020 GDP decreased by 8.4%, with the most affected sectors being agriculture, food industry, HoReCa, tourism and transport. On top of that, unfavorable climate conditions have led to a significant decrease (-27.2%) in agricultural production. Unfortunately, through 2020 and most of 2021, the Moldovan government has not been able to provide an integrated response system to the multiple challenges posed by the COVID-19 crisis. The economic and social response package was quite modest. Mainly, VAT reductions were offered for the HORECA sector-at first by 5 percentage points, then by additional 9% (from 1st October 2021). As a result, the support to both businesses and individuals amounted to only 0.8 percent of the GDP (the lowest in the region) and only an estimated share of 6 percent of companies benefited from any form of direct or indirect support.

However, towards the end of 2021 the pandemic situation was brought under control. The government managed to mobilize financial resources to meet the basic needs of the population, as well as provide support for the SME sector. As result, in 2021, the Republic of Moldova recorded the highest annual economic growth of GDP (+13,8%) since its existence. From, August 2021, Moldova has a new government supported by a pro-European parliamentary majority. The new Government's program notes a degradation of the environment and proposes a clear vision and priority actions on improving the quality of the environment and the sustainable development of natural resources, also in the context of the post COVID recovery. Moreover, the Ministry of Environment has been re-established in the structure of the Government, while previously it was part of the Ministry of Agriculture, Regional and Rural development. The government has also prepared an action plan for an immediate and short period until 2022, which shows the government's policies to be promoted. This article is prepared as result of activities realized by author under OECD project and presents a summary of the main achievements, challenges encountered during the whole implementation period, as well as provides recommendations to support green recovery for the future of the Republic of Moldova.

## The Main Challenges

The initiation of the war by Russia against Ukraine, the energy crisis and political instability are the main challenges that the Republic of Moldova is currently facing. Russia's unprovoked war against Ukraine, with which Moldova has a border in the North, East and South, generated several shocks in several social and economic fields. Immediately after the start of the war, Moldova had to face the refugee crisis. As a country of less than three million people, Moldova has provided shelter for more than half a million refugees who fled the war. Approximately 80,000 refugees have chosen to stay in Moldova so far. Also, the war led to an additional disruption of international logistics chains and endangered the distribution of agri-food goods at the global level, which further intensified the trend of global price

increases that started in 2021. Moldova, likewise, has been affected by developments in the international economy and a rapid increase in prices. Another challenge imposed by Russian aggression was the triggering of the European energy crisis. Ever since October 2021, Moldova has been blackmailed by Gazprom with the threat of reducing or even stopping gas supply. Moreover, starting from November 2022, Gazprom reduced the gas supply by 50% and the separatist region of Transnistria totally stopped the supply of electricity. As Moldova is poorly endowed with energy resources and is totally dependent on imported energy, the government initiated the national action plan to mitigate the energy crisis.

The actions of this plan aim to achieve the following main objectives:

- A. Mitigating the impact of the energy prices increase on the population, in special, the most vulnerable groups and
- B. Using the crisis as an element to increase energy security and energy efficiency, in order to prevent similar situations in the future.

Thus, during the 2022, Moldova succeeded to:

- a) Purchase the natural gas from the European spot market.
- b) Connect to the European electricity network.
- c) Create the fund for reduction energy vulnerability.
- d) Create a fund for energy efficiency in the residential sector.

Politically, the crisis can have serious consequences. The economic situation caused many discontents, while the government had to deal with a prolonged protest, organized and financed by the oligarch and fugitive politicians accused of involvement in the famous billion-dollar theft from Moldova's banking system. For now, the government seems stable, but things could degenerate if the economic situation continues to deteriorate. With a weak army and no security guarantees, as a result of a neutrality that is now proving harmful, Moldova seems to be the weak link in the block of democracies in the face of Russian aggression. The country can only cope with the massive support of Western countries. A vital support not only for Moldova, but also for regional stability. In June 2022 the Republic of Moldova obtained the status of a candidate country for joining the European Union. This means many changes that will bring the country closer to the European standard of living and increasing political and financial support from the European Union for our citizens. In order to mitigate the negative consequences on the socio-economic stability of the Republic of Moldova and the overlapping crises generated by the war in Ukraine, the EU offers an assistance package worth 250 million euros for the management of the energy crisis.

## The Main Achievements

According to the new government vision, economic activity must be carried out with the greatest responsibility towards the environment and society, considering the sustainability of life by meeting the needs of both current and future generations. The government's action plan for the year 2021-2022 includes the development and approval of the new Environmental Strategy until 2033, as well as the development of several programs and projects aimed at implementing the green transformation ideology. But, along the way, the actions of the government had to be corrected to manage several crises-the pandemics, the energy crisis and inflationary prices.

In order to address the challenges of the pandemic crisis, the Government managed to mobilize important financial resources to meet the needs of the population, but also to ensure economic growth. Thus, in 2021 the budgetary expenses for health protection amounted to \$0.8 billion (5.6% of GDP) or 26% higher than in 2020. Of the total amount, over \$35.6 million were financed from external sources, including the "Covid-19 emergency response" Project-\$15.4 million (WB), the ambulance insurance project \$8.6 million (WB), the "Emergency response to COVID-19 and support for SMEs"-\$5.4 million (CEB). This allowed:

- A. Purchase of 400,000 rapid antigen tests, as well as reducing the fees for the virus testing service by 2.5 times.
- B. Ensuring access to the vaccine-with purchases from Pfizer and donations from Sinovac and AstraZeneca.
- C. Supplying hospitals with new batches of ventilators and equipment needed to fight the pandemic.
- D. Implementing an electronic system to access the Covid-19 Certificate online, but also a system that allows the online completion of the epidemiological file.
- E. Increasing salaries of the auxiliary staff in hospitals by 57%.

For the business environment, the government intervened with the following:

- a) Approval of the package of measures to support employers and employees during the Covid-19 pandemic.
- b) VAT reduction for HoReCa of up to 6%.
- c) Subsidizing vaccinated employees with 2 days off.
- d) Adopting mechanisms to subsidize wages in case of reduction in work activity.

As a result, by the end of 2021, Moldova is out of code red, the infection transmission rate has dropped below 1, and the number

<sup>1</sup>Support the Government of Moldova in developing and implementing the COVID-19-related socio-economic recovery plans and response measures that also accelerate the path towards green and inclusive growth, OECD, 2021.

of Covid cases have reached a level below the European average. The pandemic crisis was not the only one that intervened with corrections on the Government plan. Like the rest of the world, Moldova is facing price crisis with inflation above normal rates. There were several reasons for the increase in prices, including as a consequence of the pandemic. In Moldova, inflation reached 10% in 2021 and in 2022 it is expected to reach over 34%-the highest level in Europe. As inflation indirectly affects poverty by reducing the income purchasing power, the Government launched a social package to support the population. Thus, in 2021 the budgetary expenses for social protection amounted to \$1.7 billion (12.2% of GDP) or 13% higher than in 2020.

Two important governmental interventions could be mentioned here:

- a) Increasing the minimum pension and disability pension (for 78% of beneficiaries), and
- b) Creation of a mechanism for partial compensation by the state of the natural gas and heating bills (to mitigate the impact of the tariff increase on household expenses).

Along with taking urgent measures to mitigate the socio-economic consequences of the pandemic and the price crisis, the Government carried out several activities from the action plan, including policies to shift the economy into a greener and more sustainable path of development as follows:

- A. The National Development Strategy "European Moldova 2030", approved by the parliament in October 2022, includes 2 strategic objectives related to sustainable development: 1) Increasing incomes from sustainable sources and mitigating economic inequalities; and 2) Ensuring a healthy and safe environment.
- B. The Law on industrial emissions approved in July 2022, which establishes norms aimed not only at preventing and reducing harmful industrial emissions into air, water and soil, but also at preventing the generation of waste. Also, the law regulates the procedure for issuing integrated environmental authorizations, the conditions and terms for issuing permissive acts. The adoption of the legislative act is part of the commitments undertaken by our country within the RM - EU Association Agreement.
- C. The Law of waste was amended and several Regulations were adopted in order to implement the extended producer responsibility principle. In order to ensure waste traceability, the Waste Management Information System was developed, which represents all the program products and technical equipment intended for collecting, storing and processing information.

D. The National Environment Fund (FEN) was reorganized and a new Regulation on the administration of FEN was approved in October 2022. The FEN is intended exclusively for the financing of projects in the fields of environmental protection, climate change and sustainable management of natural resources. The FEN will be administered by the National Office for the Implementation of Projects in the Environment.

At the same time, several projects and activities were carried out in order to direct the economy on the path of greening and sustainable development. Thus, with the support of E4Environment project, the Report on Green Growth Indicators was launched, and the list of new indicators has been presented. Being updated, this list serves as a basis for assessing the current situation regarding the promotion of the green economy in Moldova and will be a new starting point for developing the measures of the green transition.

The government reorganized ODIM into the Organization for the Entrepreneurship Development (ODA) which manages several SME support programs. For example, 85 companies benefited from grants under Program for the SMEs Greening in 2021-2022. From October 2022, the value of the grants increased to from 10,000 to 25,000 USD, and the implementation period of the program was extended by another 36 months. Another program managed by the ODA is the SMEs Energy Efficiency and Refurbishment Program, launched in August 2022. This program supports companies to increase their competitiveness and productivity on the national and international market. Within the Program, SMEs will receive grants, from the state, in the amount of up to 2 million lei, for the technology and technology of businesses, as well as the purchase of equipment that will ensure the reduction of electricity consumption by at least 15% compared to the consumption existing.

Green City Lab Moldova Public Association (GCL) was created with the support of the UNDP's Sustainable Green Cities project in March 2021. The core objective of GCL is to catalyze investment in low-carbon green urban development, applying integrated urban planning approaches, encouraging innovation, participatory planning and partnerships between the public and private sectors. GCL initiatives promote modern solutions for the development of a smart city, comfortable for people and friendly to nature. Among the projects implemented by GCL can be mentioned:

- a) The development of the Strategy for transport and intelligent mobility for the municipality of Chisinau,
- b) The strategy for the development of the infrastructure for alternative transport in the city of Chisinau
- c) The Green Code for the design of public buildings, which is a certification system designed as a tool to encourage the transition of the construction sector towards environmental sustainability and to increase the quality of life of citizens.

<sup>2</sup><https://mf.gov.md/sites/default/files/Raport%20pentru%20cet%C4%83%C8%99Beni%202021.pdf>

## Recommendations to Support Green Recovery

### Conceptualization process of the Environmental Fiscal Reform (EFR)

With the assistance of the consultant, discussions regarding the necessity of environmental tax reform were launched. The draft of policy note that describes the issues and the main stage of the reform is elaborated. Several initiatives to adjust environmental taxes were undertaken in order to include in the new fiscal policy. A team of experts is working on the review of the Law regarding payment for environmental pollution. At the same time, the Ministry of Environment should develop a public policy document regarding environmental tax reform and initiate consultation with all governmental institutions, local authorities, the academic and the business community.

### Institutional coordination of policies for sustainable development and the green economy

Integrating environmental and sustainability aspects into sectoral policies is a complex and multidimensional process and requires an effective policy coordination mechanism. In Moldova, such a mechanism is implemented by the permanent inter-ministerial working group for sustainable development and green economy, supported by EU4Environment. It is recommended to increase the status of this structure at the level of an inter-ministerial Commission, led by the prime minister, with ministers or vice-ministers, and heads of agencies, supported logistically and technically by a specialized secretariat.

### Increase the capacities of public institutions in assimilating the budgetary sources

In order to meet its ambitious mitigation and adaptation objectives, Moldova will need to make significant investments in the energy, transport, building, industry, agriculture, land use, forestry

and waste sectors. Achieving low-carbon growth will require a significant increase in domestic resources and international support. Internal resources for financing environmental protection are quite modest. The problem is not only in small allocations but also the low level of capitalization of planned resources. The low degree of adaptability to climate change, practically requires Moldova to give up the strategy of "small steps" in the field of solving environmental problems. There are internal resources to implement more environmental projects and could at least double the amount of allocations to promote environmental policies. It is necessary to increase the capacities of public institutions in assimilating the budgetary sources allocated for environmental protection.

### Building the capacity of the ministry of environment subdivisions

A new division under the Ministry of Environment has been created Service on circular economy policies and economic instruments, which should play an important role in development policies on environment taxes and incentives. Unfortunately, the human capacity of this division is quite limited and requires support, especially taken into consideration the challenges related to the elaboration and implementation of EFR and NEF institutional, regulatory and operational improvements. The efforts to promote the need for EFR reform through organized seminars, discussions, round tables on the need for improved fund allocation procedures and fund accumulation required for environmental needs. All above mentioned efforts are channeled towards the building of a consensus among interested stakeholders for the need of improvement of fiscal policies, sector policies, institutional restructuring of National Environmental Fund and other environmental related issues. Building a consensus among interested stakeholders is key for the sustainable development of the environmental sector in the future.

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<sup>3</sup>Pollution\_Tax\_Reform\_Ci\_a\_Necessary\_Step\_to\_Ensure\_Green\_Economic\_Growth.pdf (expert-grup.org)