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Republic of Moldova - at the confluence between East and West

Cristian CARAMAN*

Abstract

Recent developments in relations between the European Union and the Russian Federation are of major interest for the international community. The way in which the two will cooperate in the context of the Crimean crisis and in other issues related to the Eastern European space is very important not only for them, but also for the other countries, which are find themselves at the confluence between them, such as the Republic of Moldova. The role of the Republic of Moldova in securing stability and peace in the region is growing, and with it, the responsibility of the Moldovan authorities to manage their relations with the great powers is growing as well. The study aims to present the effect which the relations between Moldova and the great powers have on its economy and future political perspectives and their evolution in the context of recent events.

Keywords: Eastern Europe, economy, relations, perspectives

Introduction

The geographical position of the Republic of Moldova was a defining factor for its evolution as a state, but also for its relations with the great powers in the area. At first glance, this strip of land would not be of great interest to the states that have influence, but if we look closely, history shows that the Republic of Moldova has always been a major concern for the Russian Federation and the European Union. The Moldovan state is often seen as a protection shield for Russia in the context of the NATO-Russia conflict, but also a peacekeeping zone between the Kremlin and Brussels.

The difference between Eastern Europe and the former republics of the Soviet Union is, however, quite large. In the countries of Eastern Europe, the Soviet era usually remembered as a nightmare while the Russian population feels deeply insecure. In Moldova, however, there is a genuine nostalgia for the Soviet times, in fact this is characteristic for almost every former Soviet republics. Actually, in Moldova, the communist rule did not end in 1992. The Communist Party of the Republic of Moldova (PCRM), continued to lead Moldova until 2009. In fact, the party did not

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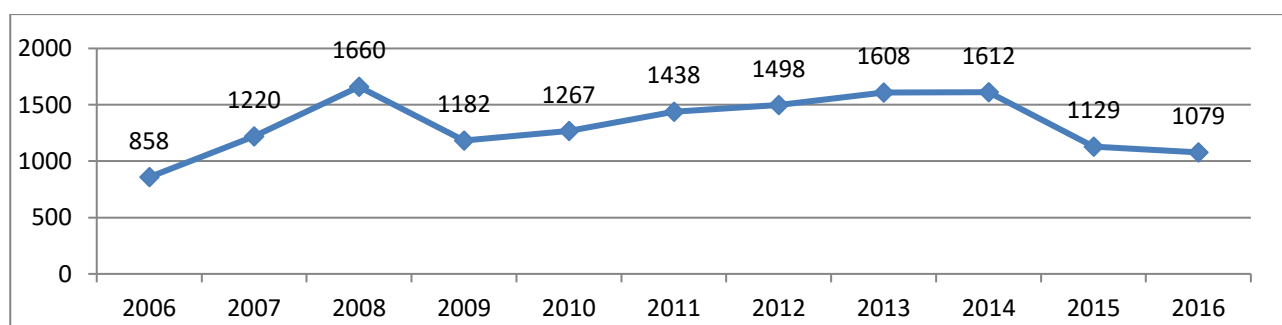
have a real ideology, but offered a continuation of ties with Russia and a sense of familiarity for a country that prefers the comfort instead of change.

The permanent changes in the Moldovan political arena have led to a lack of confidence among Europeans towards the success of implementing several fundamental reforms, in particular those related to justice and free market competition. Even though Moldova has been largely listening to financial institutions since it gained its independence, the government had failed to provide the necessary amount of real changes in order to assure the development of the country.

1. Moldova's economic background and its dependency on big powers' economies

The state of the Moldovan economy is quite precarious. The republic is often considered to be one of the poorest countries in Europe, if not the poorest. The most recent case that demonstrates the reality it's facing is the banking system crisis as a result of the fraudulent extortion of one billion euros from several commercial banks subsidized by the National Bank of Moldova. To be more specific, this amount at that time represented about 12.5% of the country's gross domestic product (GDP) and shattered the confidence in the banking system, but also in the Moldovan political class (Chiroiu, 2015). Besides, the Moldovan economy is basically dependent on remittances from abroad, especially from Russia and Central or Western European countries such as Italy, Spain or Portugal. In the same order of ideas, the ease with which the citizens of Moldova can obtain the Romanian has conditioned their mass exodus in the last period in search for a better paid job. It is also worth mentioning that the official statistics may be far from reality as long as a large number of those who have emigrated and work abroad are often illegally doing it (Nica, 2017).

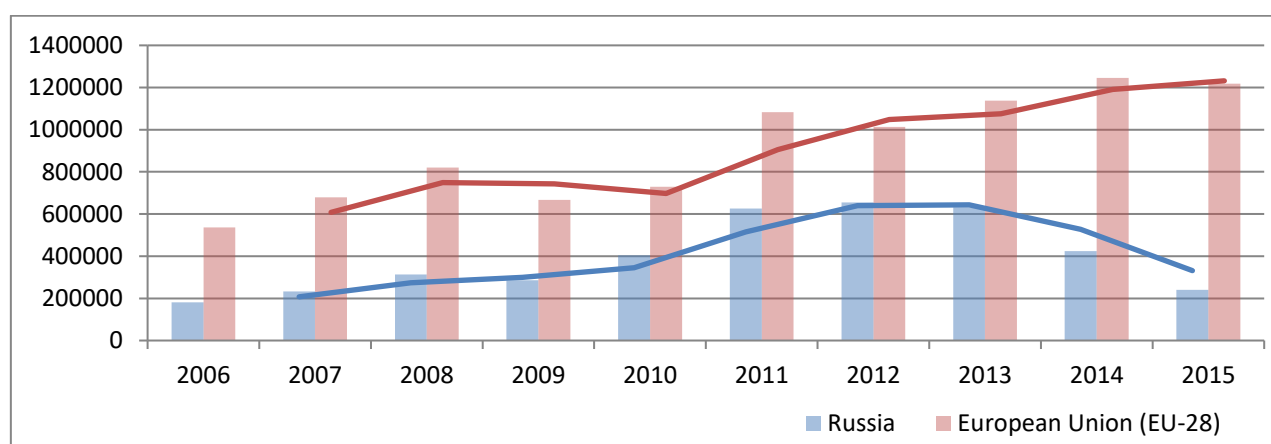
Figure 1. The evolution of remittances entering Moldova (mln. USD)



Source: own representation based on data from Moldovan National Bank of Statistics

Contrary to its neighbors, until recently, Moldova has not used its proximity to the European Union market to its advantage, partly due to the EU's restrictive policies towards agricultural products from non-member countries. At the same time, it has rarely developed new markets outside the former Soviet Union. Thus, Moldova remains strongly dependent on the CIS market, especially Russia and Ukraine due to its exports dominated by agricultural and fuel imports. There are recent signs of exports to the EU, mainly due to German and Italian investments in the textile industry and the use of their distribution channels throughout Europe and of course in the wine industry due to the recent Russian embargo. Trade with Romania is significant - its western neighbor is the third trading partner, but the investments in this country are very low due to the lack of interest from both the Romanian business community and the Romanian government. In addition to that, the relations between the two countries have deteriorated since the Moldovan authorities abandoned the reform plan.

Figure. 2. Moldovan exports in Russia and EU (thousands USD)



Source: Moldovan National Bank of Statistics

Russia remains the destination of many Moldovan exports, and around 7% of the total FDI in Moldova are coming from Russian Federation. In reality the amount could actually be higher, since the Russian businessmen are well-known for using other states banking systems like Cyprus to move money around due to less-restrictive policies. In addition, at least 300 000 Moldovans work in the Russian Federation on a temporary or permanent basis, and their remittances are enormous (Barbăroșie, 2013).

However, from 2013 onwards, EU markets have become more accessible to Moldovan producers and their exports have increased. As a result, relations between the EU and Moldova have experienced a dramatic improvement. The Russian Federation saw this as a danger to its influence in the area and hit the Moldovan economy with serious sanctions, especially in the agro-food sector. As

a result, trade relations between them have suffered. At the same time, we do not have to hyperbolize the economic importance of the Republic of Moldova for the European Union, with just over 3 million inhabitants, the Moldovan market is not expanded enough to attract a major interest from the EU.

From the investment point of view, we should be able to distinguish the interests of economic entities from those of the country in which the money is invested. While state resources are not being properly exploited, the arrival of foreign investors can only bring benefits to the recipient country of investment. De facto, with increasing investment flows in Europe, more jobs would be provided for Moldovans, wages would increase, and the economy would modernize and bring additional revenue to the state budget. On the other hand, the free movement of production factors would also provide Moldovan investors with the opportunity to internationalize their business and sell on far more extensive markets. But it is important to determine whether they can compete in the already very competitive environment in the European Union. Taking this into consideration, the European financial assistance goes further in the public domain than in the private sector in order to ensure a process of economic and legal reform of the Republic of Moldova.

Currently, according to Chisinau authorities, Moldova has around 100 projects funded exclusively by money coming from the European Union. A major drop in the flow of funds occurred after the theft of the billion in the banking system, and the recovery of the confidence of European investors will take some time. In addition to major donors such as the United States, the EU, the World Bank or the United Nations, direct development help has been also provided by countries such as Romania and Germany. Romania is actually one of the most generous donors, followed by other EU countries such as Germany, Austria and Sweden. At the same time, at the level of 2015, the private FDI level was 182.4 million euros, with the EU accumulating a share of 52.4% of the total, while the CIS countries accumulated only 11.1% (Nica, 2016).

3. The evolution of Moldova's economic performances in correlation with the economic sanctions imposed by Russian Federation

While the economic integration processes of the last period has intensified, the Moldovan economy has been put under severe pressure, especially following several sanctions imposed by the Russian Federation. As it has been mentioned several times before, the signing of the Association Agreement with the European Union was seen by the Kremlin as an attempt to diminish Russian influence in the area. Euro-integration aspirations have also been seen very negatively by the Russians, and their response came very quick.

The insecurity of the Moldovan producers and their skepticism towards constructive cooperation with the Russian partners increased several times as a result of the harsh reactions to the political aspirations of the Moldovan state. In the last 10 years, the Republic of Moldova has faced at least three embargoes imposed by the Moscow authorities on a group or several groups of products of Moldovan origin. Most of the times, the reason of the embargoes was Moscow's will to put political pressure on Moldova. Since then, many of the Moldovan entrepreneurs have long stopped exports to the Russian Federation for many of their products and went searching for other markets.

Being an economy where the agricultural sector is still very important, the embargoes on wine and agrarian products in 2006, 2009 and 2013 respectively have caused major damage to the Moldovan economy as a whole. The wine branch is considered a pillar of the Moldovan economy and rightly so. By 2006 it was the most profitable domain, and the Russian market managed to absorb up to 70% of total Moldovan wine exports sometimes. Even if the quota was lowered during the years, Russia kept its status as the main Moldovan wine importer. The embargo brought enormous damage to local producers and the economy in general. The GDP that year fell by 3.4% and value losses were over 60 million US dollars. It is clear that we cannot put it all on the decrease of wine exports, but the events of that time posed many questions for Moldovan wine producers, who now understood the need to export their product to other markets, especially in the West.

The year 2013 was marked by a third shock for the Moldovan wine industry. Due to the negotiations and the signing of the Association Agreement with the EU, Russia totally prohibits imports of Moldovan wines in September of the same year. This meant huge losses for companies such as Bostavan, which had lost more than 14 million euros, and wine exports to Russia were reduced by more than 3 quarters and total exports by over 40 percent (Ciochină, 2014).

This meant that the Moldovan wine producers started to focus their efforts on the European Union market. Judging by the data provided by the National Bank of Moldova, with the reforms initiated and the European Parliament's abolition of export quotas for Moldovan wines, the share of Moldovan wine exports to EU countries increased from 15.1% in 2009 to 25.9% in 2014. At the same time, the import of agricultural products has been increasing during this period, the countries of the European Union becoming more important partners for the Moldovan farmers. It is worth mentioning that Romania has become the most important trading partner for Moldova, covering 13.5% of total Moldovan imports and 13.1% of exports, judging by the date from 2014 (Pristas, 2015). However, the director of the most famous Moldovan winery - Purcari, said that the market share held by the company on the Russian market was only 16% and the revenues suffered even less due to the better prices obtained on the EU markets (Macovei, 2013).

With the signing of the EU Free Trade Agreement, the Kremlin authorities have acted quickly and imposed a new embargo in the summer of 2014 - this time on Moldovan fruit. Under the pretext of health and standards issues, several fruits, especially Moldovan apples, were confiscated and destroyed. Shortly after the embargo on fruit, the Russian Federation declares that imported meat from the Republic of Moldova is showing signs of concern, and for this reason, based on a report by Rospotrbnadzor, both meat and meat products of Moldovan origin were forbidden on the Russian market (Ceapai, 2014).

4. Moldova's security problems in the context of Ukrainian crisis

After the annexation of Crimea and Sevastopol by the Russian Federation, the Moldovan authorities are more reticent about a possible repetition of the scenario in the region on the left bank of the Dniester. Moreover, for more than two decades, the loyal to Russia authorities in Tiraspol are still trying to hurry a possible accession process to Russia. Now that there is a precedent, territories like Transnistria could follow the fate of Crimea as long as the Russian-speaking population, which consists the majority, demands it. It is clear that in the present context, such a scenario would be risky for the Russians and could hit the country with new economic sanctions, but such a future perspective cannot be totally excluded.

In November 2013, Moldova signed an association agreement with the European Union. Thus, like Ukraine, Moldova is in a precarious situation because of its political proximity to the European Union and the tendency to maintain its economic partnership with the Russian Federation. Unlike Ukraine, Moldova did not give up to Moscow's pressures and began the process of officially signing the Association Agreement in November of the same year and finalized it on June 27, 2014. Moldova's decision did not prevent the Russian Deputy Prime Minister from visiting Moldova, threatening to introduce economic sanctions against the country. Deputy Prime Minister Dmitri Rogozin said that the measures taken to prevent Transnistria from communicating with the rest of the world will constitute a direct threat to the security and constitutional freedom of the 200,000 Russian citizens permanently residing in Transnistria. Rogozin remarked later that Russia considers itself "the guarantor of the constitutional rights of its citizens" (Soloviev, 2014). The Kremlin has used similar tactics as in Ukraine and Armenia, leading to the abandonment of the agreement. Through pro-Russian parties and Gazprom's representatives, the Moldovan authorities were virtually blackmailed that the signing of the Association Agreement would have serious repercussions on the political and

economic situation in the region and could lead to a destabilization of the Transnistrian situation (Dumitraș, 2013).

Besides Transnistria, Gagauzia's situation is also delicate, the authorities even organized a referendum, considered illegitimate by Chisinau, in order to get closer to Russia. Its results showed that the population of the territorial unit is over 98% pro-russian (Mihăeș, 2014). All this not only hinders the prospects of the European integration of the Republic of Moldova but has serious economic and political effects in the long run. The Moldovan government still seems interested in adopting the EU vector, but is also concerned that the Crimean crisis could generate a new wave of separatism in Transnistria and Gagauzia. At the same time, the challenges faced by the country in the context of the crisis in Ukraine remain the responsibility not only of the country itself but also of the international community as a whole.

From the economic point of view Moldova has recovered during 2016 and has registered a growth in the GDP department, stimulated by a rise in consumption and fiscal stimulus. However, the risk for the economy to slow down is very real, taking into consideration the upcoming parliamentary elections in 2018. It is very possible that the implementation of reforms is not going to be the main concern for Moldovan politicians. Secondly, Moldova might be affected by the growth in other economies like Russia and EU which is also expected to be weaker than in the previous years. Meanwhile slow productivity growth and capital accumulation, combined with low labor force participation, point to a need to rebalance the drivers of growth. At the same time it is very important to advance key economic reforms to create a more transparent and rules-based environment for private sector employment creation in the future. The main challenges that the Moldovan politicians have to adjust are: the weak rule of law and the well-functioning of economic institutions, in particularly the financial system and the energy sector; numerous tax exemptions and efficiency of fiscal spending, especially those related to health and education, and the need for better salaries, which would stop the mass exodus of the labor force and also ease the pressure that is now on the pension system.

Conclusion

In the current geopolitical and economic context, the Republic of Moldova is just one of the strategic points on the European continent. However, although it has more territorial problems, the Moldovan authorities seem to have chosen the vector they will follow. Or have they? Perhaps four years ago, the prospects for Moldova's integration into the European Union seemed much more real.

Meanwhile, a series of events in the Eastern European space area made this mission more difficult and divided the Moldovan society even more. The economy of the Republic of Moldova remains in a precarious state and its dependence on the Russian market remains a cause for concern for Moldovan producers. They constantly find themselves forced to search for new markets just to be able to keep their businesses running. Even if the European Union seems to be trying to help Moldova in this matter that may not be enough since the European institutions have to take care of their own citizens' interests first. At the same time, from the political point of view, we are in the situation where the European Union does not seem so interested in its prospects for enlargement to the East, but countries like Moldova continue to see European integration as the most obvious and perfect way to ensure a durable development. In essence, the EU is not concerned about the affiliation of these countries to an economic block or another. However it considers that the normative policy and its core values such as democracy, human rights, free economy and good governance are the way to provide these countries a lasting development internally and stability and prosperity throughout the European space as a whole.

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