COUNTRY REPORT

Belarus

Moldova

4th quarter 1998

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The Economist Intelligence Unit

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Summary

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Belarus

Outlook for 1999-2000: President Alyaksandar Lukashenka and his close entourage will remain the predominant force in Belarusian politics despite an increasingly tarnished economic record of spiralling inflation, widespread shortages and greatly reduced growth. The government will maintain its interventionist economic policy, although shocks from the crisis in Russia and the danger of hyperinflation will force Belarus's easy credit policy to tighten, leading to economic stagnation in 1999. The EIU expects only a slight increase in growth in 2000, owing to stabilisation in Russia and loosened monetary policy at home—which will also lead to an acceleration of inflation towards the end of the forecast period. The country's financing difficulties, as a result of a significant current-account deficit, will continue during 2000.

The political scene: Recent opinion polls indicate the continued popularity of Mr Lukashenka, as well as the weakness of the opposition caused by its inability to mobilise important constituencies. As another step towards closer union with Russia, Belarusian and Russian legislators have approved a draft law on joint Belarusian-Russian citizenship.

Economic policy: Mr Lukashenka interprets Russia's crisis as a vindication of his own anti-market economic policies. Monetary and credit expansion have continued to accelerate, in conjunction with foreign-exchange restrictions, price controls and consumer goods rationing. The government has tightened restrictions on private trade with Russia.

The economy: Inflation has soared since August, while shortages of consumer staples have proliferated. Although growth rates for the year remain high, both industrial and agricultural output have faltered. Stocks of unsold goods are increasing.

Foreign trade and payments: Although Russia remains Belarus's main trade partner, exports to Russia have declined dramatically. Exports to non-CIS markets have also fallen steeply, reinforcing a dangerous trend towards higher trade deficits with non-CIS countries.

Business news: The Danish container carrier, Maersk Line, has opened an office in Minsk despite the worsening economic situation.

Moldova

Outlook for 1999-2000: Although Moldova's economic crisis will trigger some government changes, we expect the governing Alliance for Democracy and Reforms (ADR) coalition to stay in place. The economic collapse in Russia will affect Moldova's growth profoundly and lead to recession in 1998 and 1999, before declining growth trends flatten out in 2000. Inflation will rise sharply through mid-1999, before falling gradually to 11% by the end of 2000. The exchange rate will continue its real depreciation in 1999 before stabilising in 2000.

The political scene: The ruling coalition has survived despite a Communist-sponsored vote of no confidence and persistent rumours of its imminent resignation. There has been no progress on the Transdniestr dispute, except for small unilateral troop reductions by Russia and Moldova. A bill on local administration has reorganised the country into nine counties and the autonomous region of Gagauz Yeri.

Economic policy: The Moldovan currency plunged in value in November after dangerously low foreign-exchange reserves forced the National Bank of Moldova (NBM, the central bank) to stop intervening. Although Moldova's recent decision to repay Gazprom through government securities has complicated relations with the IMF, the Fund has indicated that it will restart its loan programme towards the end of December. The government has approved an austere budget for 1999 and has put Moldtelecom up for sale—again.

The economy: GDP contracted by 5% in the first half of 1998, while the alarming fall in industrial output in recent months suggests an even greater decline in overall GDP by the end of the year. Inflation has resumed following the devaluation of the leu. Unemployment is rising, as are public-sector wage arrears. Foreign investment remains low.

Foreign trade and payments: The trade deficit rose by almost 18% in the first nine months of 1998, compared with the same period last year. Moldova's pattern of trade remains poorly diversified and heavily oriented towards the depressed markets of the CIS. However, the amount of trade transacted through barter deals has fallen. Unable to meet its payments, the government is seeking to restructure its foreign debt, thereby increasing the likelihood of default during the forecast period.

Business news: The government has sold a majority stake in Ciment, the largest cement producer in Moldova, to LaFarge of France.

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Belarus

Political structure

Official name	Republic of Belarus
Legal system	The constitution adopted in March 1994 was amended by referendum in November 1996 to increase presidential powers and establish a bicameral parliament
National legislature	Bicameral parliament (National Assembly): upper house, Council of the Republic, with 64 members; lower chamber, the House of Representatives, with 110 members
National elections	June 23rd and July 10th 1994 (presidential); May 14th and 28th, November 29th and December 10th 1995 (legislative); next presidential election due in 2001; the date of the next legislative election is to be decided by the president
Head of state	President Alyaksandar Lukashenka, elected with 80% of the popular vote on July 10th 1994
National government	The president appoints the Council of Ministers and has strong executive powers
Main political parties	The registered parties are: Communist Party of Belarus (CPB) and its ally, the Agrarian Party; parties of left-wing orientation include the Party of People's Accord and the Party of All-Belarusian Unity and Accord; parties of pro-reform orientation include the United Civic Party and the Belarusian Social Democratic Union (Gramada); the main opposition party is the Popular Front of Belarus (PFB)

Council of Ministers	Prime minister	Sergei Ling
	Deputy prime ministers	Vasily Dolgolyov
		Gennady Novitski
		Valery Kokorev
		Vladimir Zamyatalin
Key ministers	Agriculture	Ivan Shakolo
	Communications	Vladimir Goncharenko
	Defence	Alyaksandar Chumakov
	Economy	Vladimir Shymev
	Education	Vasily Strazhev
	Enterprise & investment	Alyaksandar Sazonev
	Finance	Mikolai Korbut
	Foreign affairs	Ural Latypov
	Fuel & energy	Valentin Gerasimev
	Internal affairs	Valentin Agolets
	Labour	Ivan Lyakh
	Social security	Olga Dargel
	State property & privatisation	Vasily Novak
Central bank governor	Piotr Prakapovich	

Economic structure

Latest available figures

Economic indicators	1993	1994	1995	1996	1997
GDP at market prices (BRb bn)	986	17,815	119,813	184,174	351,043
GDP at exchange rate ($ m)	312	3,830	10,407	13,778	13,383
GDP at purchasing power parity[a] ($ bn)	43.8	39.2	36.1	37.9	42.5
Real GDP growth (%)	–10.6	–12.6	–10.1	2.6	10.0
Consumer price inflation (av; %)	1,190	2,221	709	53	64
Population (mid-year; m)	10.36	10.31	10.28	10.25	10.22
Exports fob ($ m)	1,864	2,510	4,689	5,790	7,383
Imports fob ($ m)	2,428	3,066	5,466	6,939	8,718
Current-account balance ($ m)	–404	–506	–567	–516	–799
State budget balance (% of GDP)	–5.6	–3.6	–2.8	–2.0	–2.1
Reserves excl gold ($ m)	n/a	101.0	377.0	469.2	393.7
Foreign debt ($ m)	969	1,273	1,667	1,157	1,082[a]
Exchange rate (official; av; BRb:$)	3,160	4,652	11,513	13,368	26,205
Exchange rate (av; BRb:Rb)	3.39	2.12	2.53	2.61	4.53

November 28th 1998 BRb78,000:$1 (official); BRb210,000:$1 (Kiev exchange booths)

Origins of gross domestic product 1996	% of total
Agriculture & forestry	15.9
Industry	35.3
Construction	5.5
Housing & public utilities	4.0
Services	39.3
Total	100.0

Components of gross domestic product 1997	% of total
Private consumption	59.1
Public consumption	19.3
Gross fixed capital formation	24.7
Increase in stocks	1.0
Net exports of goods & services	–4.1
GDP	100.0

Principal exports 1997	% of total
Machinery & equipment	31.2
Chemicals	11.5
Textiles	11.3
Food & food products	8.6
Mineral products	8.2
Metals	9.2

Principal imports 1997	% of total
Mineral products	27.5
Machinery & equipment	20.0
Metals	12.5
Food products	12.9
Chemicals	10.4
Plastic & rubber	5.5

Main destinations of exports 1997	% of total
CIS	73.1
of which:	
Russia	64.7
Ukraine	6.0
Non-CIS	26.9
of which:	
Poland	3.4
Germany	3.0
Lithuania	1.9

Main origins of imports 1997	% of total
CIS	66.8
of which:	
Russia	53.6
Ukraine	11.2
Non-CIS	33.2
of which:	
Germany	8.0
Poland	2.9
Lithuania	2.2

[a] EIU estimate.

Outlook for 1999-2000

Mr Lukashenka will continue to dominate the political scene—

Backed by a tame legislature, obedient government officials and loyal security services, the president, Alyaksandar Lukashenka, will maintain his hold on the political scene and further promote his own vision of political and economic development. Broadly speaking, this vision is anti-democratic, anti-market and anti-Western. The presidential administration, under the leadership of Mikhail Miasnikovich, will increase its policymaking dominance, while ministries will assume a secondary role—making policy formation even less transparent. The president and his entourage will continue to arrive at decisions in private, using government ministers as convenient scapegoats in case of policy failure or as a background against which to display the superior leadership qualities of Mr Lukashenka. The president has until now retained his popularity among the majority of the electorate. The EIU expects this public support to persist, on the whole, as a consequence of the prevailing political apathy among the Belarusian people and a general lack of information about the increasingly secretive political process.

—while the opposition's influence will remain negligible

Despite a worsening economic crisis and the increasingly apparent shortcomings of Mr Lukashenka's economic policies, it remains unlikely that any strong political rivals to Mr Lukashenka will emerge. Opposition parties in Belarus have been suppressed in recent years and appear likely to remain weak and divided. They are isolated from any potential power base and suffer from their inability to mobilise support for their cause or to produce a well-developed programme. Unable to convey their message to the electorate, opposition groups will therefore remain on the sidelines during the forecast period.

The mounting economic crisis will force some changes—

However, the current trend of spiralling inflation and consumer shortages increases the likelihood of Mr Lukashenka's popularity waning, owing to the considerable additional hardship that Belarus's already suffering population will have to face. Presented with this risk, the president is likely to decide that he has no choice but to scale back policies such as unlimited easy credit to the industrial and agricultural sectors in order to avert hyperinflation.

—and even a return of the IMF—

The fact that the IMF and the World Bank visited Belarus in early November (see Economic policy) supports the notion that the regime may be forced to shift its stance. Belarus would not only like to see a resumption of loans allocated under its stalled IMF agreement, it would also gladly accept the $100m in additional funding that might be possible under the IMF's Compensatory and Contingency Financing Facility, a programme designed to assist states affected by adverse developments beyond their control. Increasingly, Belarus will face little option but to consider this route, given Russia's inability to absorb imports and the increasing likelihood of hyperinflation.

—which Mr Lukashenka will find difficult to accept

In order to receive this assistance, Belarus will need to show a willingness to tighten its current soft credit regime, liberalise prices and resume economic restructuring. These are fundamental elements of Mr Lukashenka's system that he will be loath to change. However, if the level of inflation or the balance of payments deteriorate sufficiently that the president appears at risk of losing control of the economy, we consider it likely that Belarus will tighten monetary policy and introduce a degree of economic liberalisation in an effort to secure multilateral support. Although this may be enough to stave off hyperinflation, it will hardly lead to a fruitful relationship with multilateral donors. Mr Lukashenka will stop short of the fundamental reforms required, and will keep the central elements of his policy in place. As a result, it appears likely that any renewed relationship with the IMF will break down.

The regime will not abandon its interventionist policy—

Even if they call on IMF assistance, Mr Lukashenka and his close advisors will remain suspicious of Western-style economic policy and firm in their belief that only direct and pervasive state control will ensure continued economic growth. Despite emergency measures needed to avoid hyperinflation, such as reining in credit, this prevailing doctrine of the Lukashenka regime will continue. Considerable restrictions on currency exchange will remain. As long as the government believes that they will help to avoid hyperinflation, price controls and rationing of consumer goods will intensify. Mr Lukashenka will also continue easy credit as long as he can, aided by the National Bank of Belarus (NBB, the central bank). The NBB's new governor, Piotr Prakapovich, has shown no hesitation in further expanding the money supply, already issuing over 20trn roubles in his first months in office in an effort to keep the economy growing at an impressive rate. With this reckless monetary and credit policy destined to continue at least during the first few months of 1999, the Belarusian monetary and banking system will become increasingly strained.

—while the black market will thrive

Price controls, consumer goods rationing and artificial currency-exchange rates will provide fertile ground for the country's already thriving black market. Many estimates suggest that less than 20% of foreign currency circulating in Belarus is traded at the official rates. The influence of the black market can only increase, with enterprises and individuals continuing to purchase foreign currency at black-market rates—the illegality of such transactions notwithstanding. The US dollar will remain the principal means of payment for foreign goods on the black market, while demand for foreign currency will grow further, owing to the withdrawal of the Belarusian rouble from all foreign transactions. The magnitude of the black market will make the enforcement of government restrictions necessarily selective. With almost all economic entities in Belarus liable to charges of illegal economic activities, because of the regime's steady criminalisation of even purely market transactions, enterprises are unlikely to resist any demands by government officials for fear of criminal charges. Thus, paradoxically, the omnipresence of the black market will provide the authorities with greater leverage in selectively enforcing their economic policy. At the same time, a situation wherein enterprises are unlikely to resort to legal protection will accelerate the corruption of government officials.

Belarus will prioritise trade with Russia—

Despite current difficulties, Belarus will move towards Mr Lukashenka's main goal of re-establishing the economic system of the late Soviet period. This economy will focus on an industrial system consisting of large and obsolete enterprises producing equally obsolete low-quality goods at high cost and low (subsidised) prices. Shielded from market signals, Belarus will rely on the Russian market and hope to regain its recently high growth rates, with little incentive to restructure or modernise. The success of Mr Lukashenka's current policies is contingent on continued Russian demand for low-price, low-quality Belarusian goods. While Russia's difficulties put this into serious question, the election of the new Russian prime minister, Yevgeny Primakov, bodes well for Belarus in the short term. Mr Primakov's distrust of the market and his reliance on direct government control will help to maintain the existing chains of supply that Belarus has been at pains to preserve with Russia since the dissolution of the Soviet Union.

—but will suffer as a result of Russia's recession

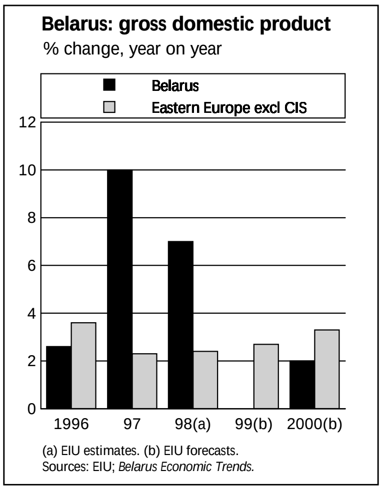
Russia's deep recession, however, will greatly diminish Mr Lukashenka's chances of continued high growth on the strength of booming exports to Russia. As a result of the effect of Russia's problems on Belarus, we have revised our growth forecast for Belarus sharply downwards. We now expect 7% growth in 1998 and no growth in 1999, down from the 10% recorded in 1997. Exports fell dramatically following Russia's crisis in August, and are unlikely to pick up much in 1999, owing to continued low Russian demand. Our forecast for improved growth in 2000, compared with next year's stagnation, is dependent on stabilisation in Russia. Because of policies favouring trade with Russia, as well as the low value-added content of exports, exporters will find it very difficult to switch to Western markets, and will face little option but to reduce industrial output targets or continue building up stocks. To avoid hyperinflation, we expect the government to rein in the easy credits enjoyed by both the industrial and agricultural sectors, resulting in a further sharp reduction in output and a temporary fall in the current account as a percentage of GDP.

Inflation will rise, but hyperinflation should be avoided—

The risk of hyperinflation will emerge as the country's major problem in 1999. For the time being, Belarus will continue using monetary emissions to address the short-term needs of the real economy, resulting in an erratic and unpredictable expansion of the money supply. Rather than tighten easy credits, the government will tighten price controls in an attempt to keep down visible inflation. This will ultimately fail, and will foster the emergence of latent inflation, a characteristic of centrally controlled economies that is reflected in severe shortages and increased black-market prices. The failure of price controls, however, will eventually force the government to begin controlling its rampant monetary expansion. Thus, whereas we forecast continued high inflation during the early part of 1999, we expect disinflation to bring official inflation levels down to 90% by the end of 1999. As the economy begins to recover, we expect a gradual loosening again in 2000, leading to a widened current-account deficit that will prove increasingly difficult to finance and renewed problems by the end of the forecast period. After slowed inflation throughout much of 2000, the annual average will be around 45%, although year-end inflation will reach approximately 75%.

—unless Mr Lukashenka defies all reason

The main risk to our forecast is that Mr Lukashenka does not alter his current path. This will happen if he rejects the IMF's conditions and gives up on multilateral assistance, or if he senses that his strong growth policy will topple without easy credits and command-driven output. Both of these options are possible. If Belarus chooses either, then hyperinflation will probably prove unavoidable, affecting growth and plunging the country into even deeper crisis.



Belarus: forecast summary
(% change year on year unless otherwise indicated)

	1997[a]	1998[b]	1999[c]	2000[c]
Real GDP	10.0	7.0	0.0	2.0
Industrial production	17.6	8.0	–1.0	2.0
Agricultural production	6.9	1.0	2.0	2.0
Consumer prices				
Annual average	64	71	240	45
Year-end	63	193	90	75
Exports fob ($ m)	7,383	6,909	5,458	5,840
Imports fob ($ m)	8,718	8,454	6,912	7,189
Current-account balance (% of GDP)	–6.0	–6.8	–8.3	–9.9

[a] Actual. [b] EIU estimates. [c] EIU forecasts.

Review

The political scene

Mr Lukashenka blames the economic crisis on others—

The president, Alyaksandar Lukashenka, has responded to the current troubles by portraying himself as the only person who can protect citizens from the careless mistakes of his ministers. For instance, during a cabinet meeting broadcast in September the president told ministers not to forget to feed the schoolchildren and to fight private traders who attempted to profit from the country's predicament. The broadcast showed the president threatening ministers and praising the KGB's efforts against corrupt officials. Whether or not the broadcast was a rehearsed exercise or an example of Mr Lukashenka's real leadership style, it showed a president comfortably in control of his government despite the troubles, not least because of help from loyal security forces. The president has recently carried out his threat to shake up the cabinet if conditions did not improve by December. On December 4th the presidential administration announced the dismissal of the foreign minister, the minister for CIS affairs and the minister for foreign and economic relations. Mr Lukashenka has now combined the three ministries into one, which will be led by Ural Latypov, a former colonel in the KGB.

—and remains popular among the general public

The president's strategy of blaming others appears to be working, as opinion polls consistently show Mr Lukashenka to be far more popular than his political opponents. In a poll in October 1998 by the Independent Institute of Socio-economic and Political Research, an organisation not linked to the government, over 50% of respondents indicated support for Mr Lukashenka. The three main opposition leaders, Gennady Karpenko, Zyanon Pazniak, and Stanislav Shushkevich, each polled under 3%. The same poll reported that over 30% of respondents felt that an election would not be necessary in 1999 (the date originally planned when Mr Lukashenka won in 1994) because no better candidate existed than the current president.

While left-wing parties form a pro-Lukashenka bloc—

Support among political groups is also strong. In September 15 left-wing political parties and organisations created a bloc of people's patriotic forces at a constituent conference held in Minsk. Among the participants were the Party of Communists of Belarus, the People's Patriotic Movement "Homeland", the Labour Union and the "Unity and Justice" movement. The new bloc issued a statement urging support for Mr Lukashenka and loyalty to the 1996 constitution that marked the beginning of the current regime. The opposition sees this constitution as a coup d'état by Mr Lukashenka, whereas the president uses it as a reason for not holding the election in 1999 as scheduled under the old system.

—the opposition remains weak and implausible

The main nationalist opposition party, the Belarusian Popular Front (BPF), is steadily losing its ability to mobilise supporters. On November 1st its rally commemorating a traditional national holiday near the mass graves of victims of Stalinist repression attracted only 3,000 supporters—less than one-third of the number that attended the first such rally ten years ago. Other opposition rallies attract only a fraction of that number, with attendance usually in the hundreds. One of the reasons for the opposition's lack of support is that its programmes for economic reform have so far failed to present any credible alternatives. The National Executive Committee of the Republic of Belarus, an opposition "shadow cabinet" that includes members of the 13th Supreme Soviet (the democratically elected legislative body disbanded by Mr Lukashenka in 1996) has issued an economic programme promising 500% growth in average wages and minimum pensions over the course of three years; full compensation to those whose bank deposits and treasury bonds were devalued; stability of the national currency; and plentiful foreign investments.

A draft law on joint Russian-Belarusian citizenship is approved

The president continues to pursue closer ties with Russia. On November 2nd Russian and Belarusian legislators approved a draft law on citizenship of the Union of Russia and Belarus. The law provides citizens of Russia and Belarus with equal legal status in both countries. If implemented, the law will have far-reaching implications for the political and economic situation in Belarus, bringing it under much more direct and open Russian influence. The president considers union with Russia to be one of his most important goals and repeatedly emphasises ties with Moscow and Russia's outlying regions.

Economic policy

Belarus seeks to replicate the economy of 1990

The president, Alyaksandar Lukashenka, has made clear his wish to regain the levels of economic development reached by Belarus in the late years of the Soviet period. He seeks to reach this goal by 2001, just in time for the presidential election provided for under the constitution of 1996. Mr Lukashenka has always regarded close economic ties with Russia as an important ingredient for continued economic growth and has downplayed the need for ties with the West. During his meeting with a delegation from the Smolensk region in October, Mr Lukashenka declared that the economic union of Russia and Belarus would be strong enough to ensure good economic performance without any increased contact with the West. While these goals have permeated all aspects of the country's economic policy, in particular through great emphasis on trade links with Russia, they are coming under pressure because of Russia's growing weakness.

Mr Lukashenka feels vindicated by Russia's problems—

Having never expressed doubts about his economic course, Mr Lukashenka was quick to announce that the recent Russian problems fully vindicated his regime's non-Western and highly interventionist economic policy. Speaking recently before a conference of ministers and other top officials, Mr Lukashenka reaffirmed current Belarusian economic policy. The visit on September 30th of Russia's newly appointed prime minister, Yevgeny Primakov, provided the leaders of Belarus with a further public opportunity to stress the success of their own economic policies by pointing to the adoption of similar measures under the new Russian government.

—and yet maintains contact with the IMF—

Despite this congratulatory tone, Belarus recognises the seriousness of the situation. In particular, it hosted visits in mid-November by both the IMF and the World Bank and has requested an IMF study on the likely social costs of reform. During their visits both multilateral institutions urged reform and condemned Mr Lukashenka's continued reliance on Soviet-style control. They painted a gloomy picture of the economy and predicted a worsening downward spiral unless Belarus returns to a path of restructuring and liberalisation. The IMF mission insisted on seeing signs of reform before resuming its funding, and indicated that it would return within a few months for further discussions. The World Bank will not consider any new loans at the moment, but will continue current assistance through its office in Minsk.

—which suggests a possible opening to the West

Thus, an important underlying shift seems to be occurring, notwithstanding the president's stridently anti-Western rhetoric and his recent statement that the IMF's visit showed it had understood the validity of his policies. In particular, Belarusian officials have made a series of overtures to the West and have sought to improve relations strained earlier this year by the row over diplomatic housing (3rd quarter 1998, page 10). The recently dismissed foreign minister, Ivan Antonovich, stated in a recent interview with a Western newspaper that his country had made "serious mistakes" in its relations with the West and that Mr Lukashenka had written to the US president to assure him that they would not be repeated. The recent reshuffle in the main external affairs ministries, including the dismissal of Mr Antonovich, was accompanied by statements from the president's office that Belarus needed to broaden its economic relations. Nonetheless, it would be easy to overstate the extent of this shift. A senior government official declared in early November that the economic situation was forcing Belarus to find a compromise with the West and with multilateral organisations, but that Belarus would not implement radical reforms. Although Belarus is desperate for assistance, it is not likely to reverse current policies until the situation worsens further. As this will probably happen next year, we expect co-operation with multilateral institutions to increase as Belarus attempts to stave off collapse.

Mr Lukashenka curbs private exports of foodstuffs to Russia—

Mr Lukashenka has assured Russians that Belarus will provide all possible help to its neighbour, and yet has clamped down on all exports to Russia not controlled by his government through a recent presidential decree that criminalises private exports of consumer goods. The decree has quickly become redundant, however, as the relative depreciation of the Russian rouble and rising consumer prices in Belarus have eliminated the profitability of small-scale trade. However, the decree is indicative of Mr Lukashenka's economic policy, including his distrust of the market; ignorance of its mechanisms; and a belief in the efficacy of direct state interference.

—and intensifies price controls and rationing

Mr Lukashenka has sought to control the country's rising inflation rate by prohibiting retail mark-ups of more than 15% and mounting a campaign against "unjustified" price increases. The government's pricing administration, an agency whose basic function of price control has not changed since the Soviet era, ensures that both private and state-controlled entities observe these regulations. Following the presidential decree on "urgent measures to protect the consumer market" issued on September 4th, rationing of basic food products and other consumer goods has proliferated. Buying and selling in excess of the centrally established quotas has been declared a criminal offence, while authorities in Minsk have threatened to revoke the licences of private retailers who exceed their selling quotas. Although local authorities in Belarus have often resorted to rationing food and other consumer items, this rationing has only recently become officially sanctioned and increasingly pervasive. Promoting these measures as perfectly normal, Mr Lukashenka has declared food rationing as something to which authorities and citizens should all be accustomed.

Reckless credit expansion is still presented as a positive policy

The Belarusian government continues to finance its economic policies through monetary emissions that far exceed projected figures. Instead of the planned monetary emission of BRb5,500bn for 1998, the National Bank of Belarus (the central bank) will issue at least BRb23,000bn by the end of the year. According to data provided by *Belarus Economic Trends*, Mr Lukashenka's recent decree to raise the 1998 budget deficit from 3.5% to 5% will alone require credits of BRb6,000bn. The bulk of credit expansion in Belarus takes the form of directed credit to the industrial and agricultural sectors, a policy supported by the governor of the central bank, Piotr Prakapovich, who has confirmed the bank's full support of the Council of Ministers' projects. Credits issued this year by the central bank, which Mr Prakapovich describes as vitally important for continued economic growth, have increased at twice last year's rate, including six new credit lines to finance food production programmes alone. Increasingly, however, these policies have failed to maintain high growth in the face of Russia's problems, and have played a significant role in fuelling unsustainable rates of inflation.

Foreign-exchange restrictions remain in place—

Although the government suggests the possibility of moving towards a single exchange rate for the Belarusian rouble next year, it has ruled out any progress this year and instead has tightened existing restrictions on currency trading. Currently, the distorted official rate coexists with interbank market rates and black-market rates, which are both considerably more representative of market-clearing rates. Belarusian companies have only been permitted to trade Belarusian roubles at the official rate, which at the end of October stood at less than one-third of the black-market rate. The Council of Ministers' decree of October 20th requires all payments for imports to be in foreign currency, thus in effect withdrawing the Belarusian rouble from foreign trade and further reducing demand for it.

—although exporters earn a reprieve

In addition, the government has required Belarusian enterprises to sell 40% of foreign-currency proceeds to the state at the official exchange rate. The authorities have recently announced a suspension of this policy for 1999 under the decision by the Council of Ministers on November 16th "on stimulating the return of currency revenue from the export of goods". Until now, Belarus's mandatory surrender requirements have acted as a considerable *de facto* tax on exporting enterprises. Two enterprises in particular, the Belarusian metallurgical plant in Zhlobin and the potassium fertiliser concern in Soligorsk, have between them accounted for 60% of the foreign-currency supply on the official currency market. It appears possible that the authorities will reinstate the surrender requirements earlier than planned if they do not appear to be achieving the desired results, given the government's dire shortage of foreign-currency reserves. A central bank statement on November 27th reveals the extent of this shortage, as it allows for purchases of foreign currency by authorised banks at a rate close to that currently prevailing on the black market. According to press reports, under this new policy banks will sell 95% of the currency received directly to the central bank. The new policy will remain in place at least until early January.

The economy

High GDP growth figures have now begun to fall—

Belarus's recent impressive real GDP growth figures, including the 10% increase registered last year, relied overwhelmingly on a mixture of concessionary trade with Russia, centrally allocated resources and generous directed credits. Rather than restructure existing production facilities, Belarus has chosen to use this easy credit to expand existing facilities to the limit in order to capitalise on the underutilised capacity in the economy caused by its considerable post-Soviet decline. In the first nine months of 1998 Belarusian output continued to post impressive growth rates, increasing by 10% over the corresponding period in 1997. These figures, however, belie the limits of Belarus's policies and the decline of the economy in the wake of Russia's crisis. This decline becomes more apparent through monthly growth figures, which reveal a slowdown that began even before the crisis in Russia. Cumulative growth since the start of the year, compared with similar periods in 1997, fell from over 12% at the mid-year mark to 11% at the end of August, 10% at the end of September and 9% by the end of October.

Belarus: gross domestic product

	1997	1998			
	Jan-Sep	Jan-Jun	Jan-Aug	Jan-Sep	Jan-Oct
% change year on year	11.0	12.0	11.0	10.0	9.0

Source: official statements.

—as growth in industrial production falters—

Although industrial production in the first nine months of 1998 registered robust 10.8% growth compared with the same period last year, figures for September showed a 4.5% drop over the preceding month, following a 3.3% month-on-month increase in August. These September figures present the first significant month-on-month decline in a year. Regional variations were large, from a 2.5% fall in the Gomel region to 8.8% in the Minsk region (the city of Minsk actually registered 2.5% growth) and 9.4% in the Grodno region. Among industries, oil processing fared the worst with a drop of more than 20% month on month in September, followed closely by the fuel industry with a decline of more than 19%. In all other industries, with the exception of energy, textiles, and garment and leather goods production, the decline in output varied from 0.1% to 9.6%.

—and agricultural output declines

The government has maintained considerable control over the agricultural sector in its attempts to boost output. Nonetheless, agricultural production in the first ten months of 1998 fell by 0.6% according to preliminary data. Grain output proved particularly poor, falling by 21% in 1998 compared with the preceding year, with the result that Belarus will probably need to increase its grain imports from hard-currency suppliers. While adverse weather conditions played a role, the agricultural sector's poor performance suggests the limits of government policies that have effectively forestalled significant restructuring by channelling credits to crop areas in which inefficient production methods still predominate.

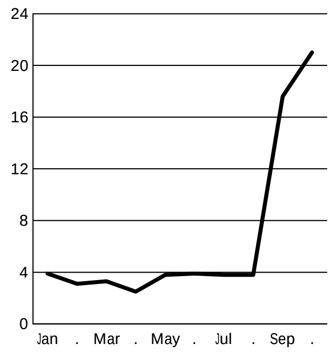
Manufactured goods remain unsold

Russia's inability to continue absorbing the levels of imports seen in recent years has quickly translated into an increase in the stocks of unsold industrial goods in Belarus. In October unsold stocks constituted 66.1% of monthly industrial output, compared with a level of 55.9% in January. For machine-building, the figure as of October 1st stood at over 129% of the sector's monthly output. Inventories will rise further, owing to the continued decline in demand in Russia, and will probably force the government to lower its production targets.

Inflation soars—

Devaluation in Russia has combined with continued monetary expansion in Belarus to produce a sharp increase in inflation during the third quarter. Monthly inflation for the first ten months of the year had ranged between 2.7% and 3.9%. However, following yet another round of emissions to finance the harvest collection, inflation rose to 17.6% in September, the highest monthly rise in four years, and then to 21% in October. Despite renewed efforts by the government to control key prices, this put the cumulative inflation rate for the first nine months at more than 80%, far exceeding the government's projected annual inflation for 1998. In the first week of October alone, prices of basic foodstuffs increased by up to 14%, while shortages of staple goods and imported products, particularly medical supplies, have become widespread and have triggered panic-buying among citizens.

Belarus: inflation, 1998
% change, month on month



Source: *Belarus Economic Trends.*

Belarus: consumer prices
(% change)

	Month on month	Year on year[a]
1997		
Jan	13.3	49.5
Feb	6.6	53.3
Mar	2.3	53.7
Apr	4.3	58.0
May	5.0	64.8
Jun	4.5	68.4
Jul	1.4	67.1
Aug	1.0	66.6
Sep	5.0	71.8
Oct	3.2	74.9
Nov	1.8	71.4
Dec	2.3	63.3
1998		
Jan	3.9	49.7
Feb	3.1	44.8
Mar	3.3	46.2
Apr	3.8	45.5
May	3.4	43.3
Jun	2.7	40.8
Jul	2.8	42.9
Aug	3.8	46.9
Sep	17.6	66.5
Oct	21.0	95.3

[a] EIU estimates based on monthly data.

Sources: *Belarus Economic Trends*; press reports.

—as the currency plunges

During the third quarter the Belarusian rouble continued to depreciate rapidly against the US dollar. After starting the year at BRb30,740:$1, the official exchange rate stood at BRb56,000:$1 by October 26th. The black-market exchange rate reached BRb180,000:$1 on the same day, having depreciated by over 13% in the preceding week. By November 28th the official rate stood at BRb78,000:$1. As reported by *Belarus Economic Trends*, the gap between the official rate and the parallel interbank market rate has widened considerably this year, from 35.1% at the end of January to almost 300% at the end of September, suggesting significant inflation and further depreciation.

The dollar becomes the currency of choice—

The dollar had already replaced the rouble as the standard unit of account in transactions involving imported goods or large-ticket items (cars, home electronics, household appliances, etc). Despite still being illegal, it has now also become the currency of choice for domestic, large-sum, cash transactions between private companies and between individuals. Tacitly recognising the failure of current policy and desperate for foreign currency, the government will soon partly legalise these transactions and open stores selling imported goods for foreign currency. According to official sources, foreign currency (mostly dollars) accounted for approximately 27% of the total money supply in Belarus as of October 1st, with actual figures probably even higher.

—and real wages fall

Data provided by the *Belarus Economic Trends* index of real wages and pensions indicates that both declined in August from their July levels. According to press reports, August levels of BRb4.4m ($62 at current rates) for average real wages and BRb1.7m ($24) for average monthly pensions present a decline of 1.4% for wages and 3.8% for pensions. The government appears intent on minimising the effect of rising inflation, although it is unlikely to stem successfully the decline in real values caused by accelerating inflation. In August the government decreed an increase of the minimum wage by 40% with effect from October 1st, while it has recently indicated its intent to raise nominal wage and pension levels again in December.

Belarus: monthly wages and pensions
(average; BRb '000 unless otherwise indicated)

	Nominal wage	Real wage index (Dec 1993=100)	Minimum wage	Total wage arrears (BRb bn)	Nominal pension	Real pension index (Dec 1993=100)
1997						
Jan	1,526.2	76.2	130.0	479.8	597.1	88.4
Feb	1,639.6	76.8	130.0	595.2	705.9	98.0
Mar	1,732.5	79.4	130.0	596.8	712.3	96.7
Apr	1,898.7	83.4	150.0	439.7	718.4	93.5
May	2,003.4	83.8	150.0	559.9	718.4	89.1
Jun	2,187.9	87.6	150.0	660.2	857.2	101.7
Jul	2,299.3	90.8	150.0	502.8	857.2	100.3
Aug	2,361.1	92.3	150.0	598.7	980.6	113.6
Sep	2,664.1	99.2	200.0	632.3	1,002.3	110.6
Oct	2,748.3	99.1	200.0	738.4	1,002.3	107.1
Nov	2,743.5	97.2	200.0	498.3	1,204.4	126.5
Dec	3,276.0	113.5	200.0	748.6	1,204.3	123.6
1998						
Jan	3,024.2	100.8	250.0	797.5	1,238.2	122.3
Feb	3,390.0	109.6	250.0	803.8	1,475.3	141.4
Mar	3,698.2	115.8	250.0	722.8	1,475.3	136.8
Apr	3,669.3	110.6	250.0	948.3	1,475.3	131.8
May	3,854.9	112.4	250.0	1,081.7	1,475.3	127.5
Jun	4,176.8	118.6	250.0	1,312.9	1,475.3	124.1
Jul	4,348.2	120.1	250.0	758.7	1,721.2	140.2
Aug	4,449.0	118.4	250.0	1,068.6	1,721.2	135.7

Source: *Belarus Economic Trends.*

Unemployment grows

Government statistics for September show a rise in unemployment for the second consecutive month. The number of people unemployed rose by 1,000 in August and by a further 1,400 in September, reaching 105,800. Although September's official unemployment rate of 2.3% still remains low, it represents a notable setback for a government committed to full employment.

Foreign trade and payments

Exports to Russia have decreased sharply—

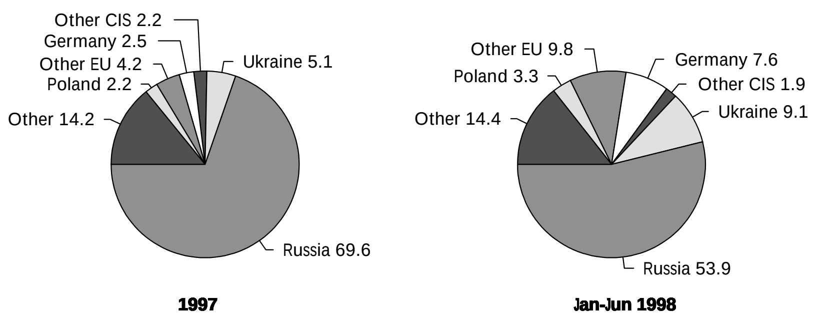
Belarus's exports to Russia continued their upward trend during the first six months of the year. However, figures for July and August show an alarming drop in month-on-month exports to Russia, which has since accelerated. In the first six months of the year average monthly export revenue from trade with Russia stood at $421m. Exports to Russia fell to $401m in July and then to

$346m in August. They have since dropped even more steeply, to $240m in September (a year-on-year fall of 45%) and $170m in October. Much of this decline is owing to the collapse of the banking system in Russia that began with the crisis in August and which resulted in suspension of payments for imports. Yet even with the recovery of the banking system exports to Russia and other CIS states will remain sharply lower because of reduced demand. Already, Belarus has begun denominating export contracts in dollars rather than Russian roubles, which has significantly raised the price of Belarusian goods for Russian importers.

—and non-CIS exports have dropped as well

Recent data show a dramatic decline in exports to non-CIS markets of 8.3% during the first eight months of 1998, in comparison with the corresponding period in 1997. Exports to non-CIS markets as a percentage of total trade have fallen consistently and now comprise only 23.1% of total trade, down from over 40% in 1996. In the first eight months of 1998 the share of exports to non-CIS markets, as a percentage of Belarus's total exports, had fallen by almost 4%, while Belarus's reliance on the Russian market had risen by over 5% as a percentage of total exports. These recent trends in the country's trade structure do not bode well for its ability to protect itself from the current regional turmoil.

Belarus: exports by destination
% of total



Source: *Belarus Economic Trends.*

Non-CIS imports have continued to rise

Over the first eight months of the year total imports grew by 9.2% compared with the same period last year. Whereas Russia increased its share of total exports to 68%, its share of imports has fallen to 53% of Belarus's total, as a result of an 18.8% surge in imports from non-CIS states over the first eight months of 1998. This increase in Western imports has further compounded Belarus's economic difficulties, by significantly increasing the trade deficit and contributing to a large current-account deficit that will likely create further financing problems. In the first nine months of 1998 the country posted a trade deficit of $1,301.9m, up from $1,093.7m over the corresponding period last year. Trade deficits with non-CIS states proved especially problematic, with eight-month data showing a rise of approximately 80% compared with last year—particularly as a result of increased deficits with Germany ($250m), Poland ($70m) and Italy ($61m). Belarus's declining market share outside the CIS will prove extremely difficult to recoup, largely as a result of neglect of trade diversification. Combined with the country's growing appetite for imports from the West, this will help lead to a current-account deficit that will become increasingly unsustainable, given the lack of foreign-currency inflows. According to recent press reports, the level of inflows over the first nine months of the year dropped by $650m compared with last year's level, including only $11.7m of foreign direct investment (FDI), down by 60% from last year—only Armenia, Georgia, Tajikistan and Uzbekistan rank lower among former Soviet states in terms of FDI per head.

Belarus: current account
($ m)

	1997				1998	
	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr
Exports	1,570.6	1,708.0	1,959.2	2,144.8	1,772.9	1,893.5
of which:						
barter	467.3	482.8	475.3	624.8	n/a	n/a
Imports	1,968.8	2,049.0	2,181.6	2,518.6	2,257.3	2,262.4
of which:						
barter	638.7	600.1	582.3	720.0	n/a	n/a
Trade balance	–398.2	–341.0	–222.4	–373.8	–484.4	–368.9
% of GDP[a]	–14.7	–11.3	–5.6	–10.5	–15.2	–9.9
Net services	140.2	138.4	116.3	142.9	111.8	137.0
Net income	–18.8	–15.9	–15.2	–29.4	–13.0	–25.1
Net transfers	16.1	26.6	21.0	14.7	15.2	43.4
Current-account balance	–260.7	–191.9	–100.3	–245.6	–370.4	–213.6
% of GDP[a]	–9.6	–6.3	–2.5	–6.9	–11.6	–5.7

[a] *Belarus Economic Trends* estimates.

Source: National Bank of Belarus, published in *Belarus Economic Trends*.

Trade figures provide an incomplete picture

As usual, Belarusian trade statistics will not have captured the full extent of the country's trade, as they omit "shuttle" trade and distortions arising through barter and export surrender requirements. Shuttle trade, especially with Russia, which has proved quite extensive in recent years, involves private individuals trading across borders on an informal basis unrecorded by official figures. The prevalence of barter in Belarus's trade, as well as the requirement that exporters sell a large portion of foreign-currency earnings to authorities at the official rate, probably leads to the underpricing of exports.

Business news

Russia agrees to receive Belarusian goods in exchange for gas

The Russian government has approved an agreement with Belarus stipulating that shipments of foodstuff and other goods would be accepted in lieu of money for 80% of Belarus's outstanding debt for gas supplied by Russia. This decision will help the cash-starved Belarusian government in the coming year, as it owes an estimated $230m for previous gas shipments. This agreement will further increase the share of barter transactions between the two countries, which already comprised 31.9% of Belarusian exports and 26.1% of imports in the first eight months of 1998. Barter is already especially prominent in trade with Russia, accounting for approximately 60% of the total volume of trade in August.

Maersk opens its office despite the region's crisis

The Danish container carrier company Maersk Line has decided to brave the current crisis and carry through with investment plans in Belarus. Maersk Line, the world's largest container company, opened up an office in Minsk in September. According to *Belarus Now*, an English-language Belarusian news source, the company based its investment decision on the success of Maersk Medical, a related company involved in a joint venture in Belarus since 1992, as well as on Belarus's geographic location and, until recently, the prospect of a large Russian market nearby. Although Maersk Line describes Belarus's shifting legislative framework and pricing policies as problematic, it plans to wait out the crisis by increasing its business with western Europe until regional prospects improve.

Moldova

Political structure

Official name	Republic of Moldova
Legal system	Moldova adopted a new constitution on July 28th 1994. The Transdniestr region has declared independence, which the central government has not recognised. The region inhabited by the Gagauz minority was granted special legal status in December 1994
National legislature	Unicameral assembly, the parliament, with 101 members, directly elected by proportional representation
National elections	November 17th 1996 (presidential) and March 22nd 1998 (legislative); next elections due in late 2000 (presidential) and by 2002 (parliamentary)
Head of state	President, Petru Lucinschi, sworn in on January 15th 1997
National government	Moldova has an executive presidency. The prime minister chairs the Council of Ministers; a new coalition government was approved by parliament on May 21st 1998
Main political parties	The Democratic Convention (26 seats in parliament), the Bloc for a Democratic and Prosperous Moldova (24 seats) and the Party of Democratic Forces (11 seats) form the ruling coalition. The Communist Party of Moldova holds the largest number of seats (40)

Council of Ministers	Prime minister	Ion Ciubuc
	Deputy prime minister & minister for the economy	Ion Sturza
	Deputy prime minister & minister of industrial policy	Valentin Dolganiuc
	Deputy prime minister & minister of social policy & science	Oleg Stratulat
Key ministers	Agriculture & food processing	Valeriu Bulgari
	Culture	Ghenadie Ciobanu
	Defence	Valeriu Pasat
	Education	Anatol Grimalschi
	Finance	Anatolie Arapu
	Foreign affairs	Nicolai Tabacaru
	Health	Eugeniu Gladun
	Industry & commerce	Ian Tanase
	Internal affairs	Victor Catan
	Justice	Ion Paduraru
	Labour & social protection	Vladimir Guritsenco
	National security	Tudor Botnaru
	Privatisation	Lurie Badir
Central bank governor	Leonid Talmaci	

Economic structure

Latest available figures[a]

Economic indicators	1993	1994	1995	1996	1997
GDP at current prices (Lei m)	1,821	4,737	6,480	7,658	8,655
GDP at exchange rate ($ m)	506	1,109	1,441	1,663	1,872
GDP at purchasing power parity[b] ($ bn)	10.3	7.3	7.3	6.9	7.1
Real GDP growth (%)	–1.2	–30.9	–1.9	–8.0	1.3
Consumer price inflation (av; %)	1,751.0	486.4	29.9	23.5	11.8
Population (mid-year; m)	4.36	4.35	4.35	4.33	4.31
Exports ($ m fob)	393	619	739	828	891[b]
Imports ($ m fob)	528	672	773	1,113	1,235[b]
Current-account balance ($ m)	–155	–82	–115	–214	–296[b]
Consolidated budget balance (% of GDP)	–7.5	–5.9	–5.8	–9.8	–7.7
Reserves excl gold ($ m)	76.3	179.9	239.8	313.6	366.0
Foreign debt ($ m)	285	504	677	834	1,067[b]
Exchange rate (av; Lei:$)	n/a	4.27	4.50	4.61	4.62

November 30th 1998 Lei9.7062:$1

Origins of gross domestic product 1997	% of total
Agriculture & forestry	32.2
Manufacturing	28.6
Construction	4.6
Services	33.8
Total	100.0

Components of gross domestic product 1997	% of total
Private consumption	70.5
Public consumption	26.1
Gross fixed investment	19.6
Increase in stocks	4.6
Net exports	–20.8
GDP	100.0

Principal exports 1997	% of total
Food products, beverages & tobacco	54.8
Vegetable products	8.6
Live animals & animal products	8.6
Textiles	6.6
Machines, electronic devices & equipment	5.2

Principal imports 1997	% of total
Mineral products & fuel	35.3
Machines, electronic devices & equipment	12.9
Chemicals	9.6
Textiles	5.3
Metals & metal products	4.5

Main destinations of exports 1997	% of total
Russia	58.0
Romania	6.7
Ukraine	5.9
Germany	4.1
Belarus	3.7

Main origins of imports 1997	% of total
Russia	26.0
Ukraine	20.5
Romania	9.3
Belarus	8.2
Germany	4.4

[a] Excluding Transdniestr. [b] EIU estimate.

Outlook for 1999-2000

An economic crisis will precipitate further government instability

Moldova's economic difficulties will destabilise the already tense political environment and further expose existing divisions within the three-party government. Although the coalition parties will continue to criticise each other in their search for scapegoats, this does not appear likely to precipitate a formal split in the coalition. Although the president, Petru Lucinschi, has blamed the government for ineptitude, he has refrained from replacing it for fear of exacerbating the economic problems and jeopardising multilateral loans. However, the president will probably exercise his prerogative to replace his prime minister, Ion Ciubuc, who entered hospital in November suffering from nervous exhaustion. This may provide an excuse for the president to change the head of government without appearing to undermine the cabinet.

The Communists will attempt to exploit public discontent

With the economy expected to decline further during 1999, the risk of prolonged political crisis remains high. The Communist Party of Moldova (CPM), which holds the largest number of seats in parliament and forms the parliamentary opposition, will continue to use the economic situation as an indictment of reformist policies. However, the CPM will not be strong enough to overthrow the government, as demonstrated by its failure to push through a motion of no confidence in November. Instead, it will use every opportunity to exploit the problems and increase support for the party, through such means as facilitating trade union protests and by emphasising its solidarity with the impoverished population. Conversely, however, this will help to maintain the fractious coalition, for fear of the CPM seizing the initiative.

There will be no progress on Transdniestr

The issue of Transdniestr, Moldova's breakaway region, will remain unresolved during the forecast period. Only Moldova, the weakest of the three parties involved, has any interest in a resolution. Transdniestr's well-entrenched leadership has no intention of ceding any power, and will respond negatively to any initiative that threatens the status quo. Russia will continue to maintain a regional military base as long as it can, claiming that the 1994 troop withdrawal agreement remains contingent on a resolution of the conflict—although it will further reduce its armed presence in Transdniestr for economic reasons.

Multilateral loans will resume

Moldova will depend heavily on disbursements from multilateral institutions, which should resume with a $35m disbursement from the IMF and up to $65m from the World Bank at the beginning of 1999. Both the Fund and the Bank suspended disbursements in 1997 as a result of stalled progress on reforms. In order to ensure continued multilateral support, the EIU expects Moldova to follow fiscal and monetary constraint and progress in such areas as energy and agriculture sector reform throughout the forecast period.

Moldova's energy shortfall will continue

Moldova's $614m gas debt to the Russian gas monopoly, Gazprom, will remain a problem for the country in 1999. Its inability to meet Gazprom debt obligations, despite some recent progress (see Economic policy), will result in a high risk of increased energy shortages. Supplies are already low as a result of reduced Gazprom deliveries, as well as recent significant cuts in gas supplies from Ukraine, Moldova's other major energy source. We do not envisage Gazprom stopping supplies altogether, given recent Gazprom assurances and the likelihood of intervention by the Russian government. However, increased energy cutbacks will prove necessary and will result in reduced industrial output, as well as additional hardship for much of the population—especially during the upcoming winter.

Budget austerity will be unavoidable

The government will be forced to reduce its spending considerably during the forecast period owing to a combination of strict IMF conditions, an already considerable debt load and a shortage of external borrowing possibilities. Although the government will resort to severe wide-ranging public spending cuts, it is not expected to meet its 2% budget deficit target in 1999 because of overoptimistic underlying growth assumptions. This will necessitate further cuts later in the year, with the government likely to resort to its usual device of increasing already high public-sector arrears rather than increasing monetary emissions.

Debt restructuring will continue

Moldova has debt repayment obligations of $215m in 1998 and $235m in 1999. The government appears unlikely to fulfil its 1998 debt-service obligations, let alone those for 1999, and is already in negotiations with Merrill Lynch and Commerzbank, two of its major creditors. The 1999 budget assumes that outstanding debt will be serviced through foreign borrowing and privatisation receipts—although borrowing prospects have dried up and foreign investors have recently offered extremely low prices for Moldovan assets. Moldova's prospects of issuing its planned DM50m Eurobond have all but vanished. It is rated as a speculative credit, while the Euromarkets in 1999 will only be open, if at all, for the better-known and better-rated emerging-market borrowers. Moldova will continue to seek debt restructuring and as a result will face an even harder time trying to re-enter international capital markets, once they begin to open up again in 2000.

The leu's value will fall further—

The leu has already plunged in value by over 100% since the Russian rouble devaluation in August. We expect the recent real depreciation to continue into 1999 as a result of the rouble's slide and the inability of the National Bank of Moldova (NBM, the central bank) to intervene. However, the leu's depreciation will be contained, given the unlikelihood of the NBM printing money to finance budget shortfalls or wage arrears, and the fact that the Moldovan banking system has not been paralysed by a lack of liquidity. Furthermore, the concept of an independent central bank is well enshrined in Moldova and is less subject to political interference than in Russia, while the NBM appears to have a tacit understanding in favour of currency stability with the commercial banks that are now largely responsible for deciding the currency's rate through over-the-counter market transactions.

—leading to high inflation in 1999—

The collapse of the leu in November produced an immediate inflationary effect on prices. With the leu expected to continue to slide, this will carry through into 1999, hitting Moldova's dollar-denominated oil and gas imports and feeding through into higher manufacturing costs. Further inflationary pressure will result from anticipated increases in energy tariffs over the next two years. This has led us to revise our inflation forecast sharply upwards, to year-end inflation of approximately 35% in 1999 and 11% in 2000.

—and lower domestic consumption—

The increase in domestic demand seen last year, largely owing to high levels of government spending and considerable growth in private consumption, will dampen in 1999 because of reduced real income and government spending cuts. Real income will fall in 1999 as a result of an increase in wage arrears, the currency's real devaluation and higher inflation, which will cause real wages, even when paid, to remain low throughout the forecast period. Combined with the government's need for austerity, this will lead domestic demand as a whole to fall sharply in 1999 and, at best, recover slowly in 2000.

—which should help to reduce imports

Imports will fall sharply over the forecast period, having risen steeply in recent years. Most of this rise had come from increased imports of consumer-related products, especially from Western markets, which will now decline as a result of reduced domestic demand. After a fall in imports of approximately 2.8% over the first eight months of 1998 compared with the same period last year, we forecast imports in 1998 to fall in dollar terms to a level of $960m by the end of the year, in comparison with $1,235m in 1997. Next year will see a further sharp reduction before imports increase again in 2000, owing to the gradual recovery of domestic demand and increased investment.

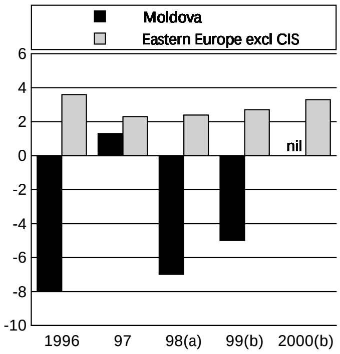
Exports will fall further—

Severe recessions and sharp real devaluations in Moldova's main export markets will result in a steep drop in export revenue next year. Russian GDP in 1999 is expected to decline by 6% and Ukrainian GDP by over 3%, while Romania will only achieve flat growth, following a contraction this year that is expected to reach 5% of GDP. Together, these three markets account for over 80% of Moldovan exports. Although we expect the weaker leu partly to counteract this decline in exports, we also predict relatively large rouble and hryvnya devaluations that will result in further large negative trade balances and high current-account deficits. Moldova's difficulty in diversifying its patterns of trade will hinder it from adjusting quickly to these external shocks. Its food industry is not geared towards the demanding standards of the EU and, in any case, will meet with stiff competition from other ex-Soviet exporters seeking to reorient themselves westwards. In the Russian market, Moldova's export prospects appear further diminished as a result of significant European and US food aid packages backed by export credits.

—leading to negative growth for 1999

The combination of depressed domestic demand and sharply reduced exports will result in further negative growth next year. We forecast a sharp fall in GDP growth this year and a contraction of up to 5% in 1999, followed by stagnation in 2000. Our forecast of declining growth flattening out in the second half of the forecast period assumes no further major turmoil in Russia or Ukraine and a gradual recovery in Romania. In mid-1999 we expect inflation to recede and currency stability to re-emerge, based on expectations of relatively responsible fiscal and monetary policy and increased stability in Russia. Output in the agricultural sectors should stabilise by 2000, while the industrial sector's decline is expected to slow, based on an improved external situation and continued reform at home. Because of Moldova's high dependency on agriculture, growth figures will be greatly influenced by weather conditions.

Moldova: gross domestic product
% change, year on year



(a) EIU estimates. (b) EIU forecasts.
Sources: EIU; *Moldovan Economic Trends.*

Moldova: forecast summary
(% change year on year unless otherwise indicated)

	1997[a]	1998[b]	1999[c]	2000[c]
Real GDP	1.3	–7.0	–5.0	0.0
Industrial production	–2.3	–11.0	–8.0	–2.0
Agricultural production	11.0	–4.0	–1.0	1.0
Consumer prices				
Annual average	11.8	8.2	50.0	13.0
Year-end	11.2	23.0	35.0	11.0
Exports ($ m)	891[b]	614	556	640
Imports ($ m)	1,235[b]	960	801	833
Current-account balance ($ m)	–296[b]	–281	–160	–103
% of GDP	–15.8[b]	–17.9	–17.2	–11.2
Exchange rate (Lei:$)				
Annual average	4.62	5.60	13.50	15.50
Year-end	4.66	11.00	15.00	16.00

[a] Actual. [b] EIU estimates. [c] EIU forecasts.

Review

The political scene

Coalition unity remains strained—

Beginning in August, Moldova's governing coalition, the Alliance for Democracy and Reforms (ADR), has faced its gravest turmoil since coming to power in May 1998. Critics have accused the three-party coalition of ineffectiveness in the face of plummeting output and exports, rising consumer prices, a currency freefall and a major energy crisis. Throughout, senior members of the coalition parties have shown little sign of unity and have repeatedly blamed each other for the country's malaise. With the coalition seemingly on the verge of disintegration, rumours have flourished over the likely dismissal or resignation of the prime minister, Ion Ciubic.

Although the government has remained in place, changes have occurred within the cabinet. In November the president, Petru Lucinschi, dismissed his transport and communications minister, Tudor Leanca, of the Party of Democratic Forces (PDF), for alleged incompetence. According to the coalition agreement, his replacement will come from the same party. Since then the Moldovan economy minister and deputy prime minister, Ion Sturza, has taken over the duties of the prime minister, who was admitted to hospital on November 17th reportedly suffering from chronic fatigue. Mr Sturza, one of the chief reformists in the government, had earlier threatened to resign over the administration's lack of unity in tackling the country's economic problems and in pushing through a realistic budget (see Economic policy).

—but a Communist initiative to remove the government fails

The Communist Party of Moldova (CPM) remains the government's staunchest critic. With the deepening of the crisis, the communists have initiated a no-confidence vote in the government, after having long blamed economic reforms and slavish adherence to IMF policies for Moldova's problems. The motion, debated on November 11th, won the support of only 38 of the 58 deputies present, thereby failing to gain the 51 votes required to pass under Moldovan law. The government's decision to allow only a core of faithfuls to vote on the no-confidence motion appears indicative of the leadership's lack of faith in the coalition's unity.

Political tensions rise—

Moldova's political institutions have not responded effectively to the growing crisis, with the worsening economic situation fuelling tension between the various branches of power. Little has resulted from a presidential decree in October establishing a commission charged with developing an anti-crisis programme, leading an exasperated Mr Lucinschi to blame the government and parliament for their insistence on endlessly debating every decision, however minor. Mr Lucinschi has warned that he may be forced to introduce a state of economic emergency, which is not fully provided for in the constitution, and has instructed the cabinet to draw up emergency measures including a reduction in the number of entities allowed to import energy and the creation of a state monopoly over alcohol and tobacco imports to recoup excise duties. For Moldova, these are uncharted waters and will probably result in further institutional paralysis.

—while strikes and protests increase

Arrears in wage and pensions payments are a long-standing but growing feature of Moldova's economy. Wage arrears have increased by over 43% in the first half of 1998 and are now equivalent to almost 20% of the government's expected revenue for this year. With the government obliged to cut spending, and with increased inflation reducing the value of these arrears, growing numbers of workers have resorted to industrial action in protest.

Moldova withdraws some troops from Transdniestr

Discussions over the status of Transdniestr, the breakaway region bordering Ukraine, and the withdrawal of Russian troops have progressed only slightly. The agreement signed in Odessa in March 1998 called for troop reductions to the level of 500 for each of the three parties involved—Russia, Moldova and Transdniestr. All sides continue to dispute each other's claims about total troop deployments in the region, with both Russia and Moldova recently claiming to have made unilateral cuts unmatched by the other signatories of the agreement. Officials in Tiraspol, the capital of Transdniestr, have condemned Moldova's reductions as cosmetic and protest at the removal of further Russian troops, which they see as a stabilising force. Transdniestr has used the Russian army's presence, for which it believes it is owed "rent", as a way of offsetting part of its Russian debt, while Russia has once again ignored Transdniestr's demand that the arms dumped in the region after the dissolution of the Warsaw Pact be transferred to its control.

Parliament passes bills on administrative reform

On November 12th parliament passed a bill on local administration reform required by the IMF and the World Bank as part of the political reform process. The bill streamlines local government into nine counties and the single autonomous region of Gagauz Yeri. Previously, Moldova had comprised 40 districts and 10 towns, as well as the region of Gagauz Yeri, which had held autonomous status since June 1995. The proposed reforms have strained relations with Moldova's Bulgarian community, located mainly in the district of Taraclia, who oppose being subsumed into a larger Moldovan-dominated county or being joined up with Gagauz Yeri. The Moldovan authorities accused Bulgaria of meddling in the country's internal affairs, after Bulgaria's ambassador to Moldova voiced an official protest in October. In the end, the new law has merged Taraclia into the larger Cahul county, but guarantees Bulgarian Moldovans their own deputy county chairman.

An economic zone is planned with Romania and Ukraine

The presidents of Ukraine and Romania travelled to Chisinau, the Moldovan capital, in October to discuss the creation of the Lower Danube Euroregion, a free economic zone (FEZ) that would include the Romanian ports of Galati and Remi, as well as the Giurgiulesti oil terminal currently under construction in Moldova. In addition to offering the usual value-added tax (VAT) and customs duty exemptions to potential investors, the Lower Danube FEZ hopes to attract oil from the Caspian pipeline project that would terminate in the Georgian port of Supsa. For landlocked Moldova, this project would prove important in providing a way to reduce dependency on Russian fuel products.

Economic policy

The central bank ends support for the leu—

The National Bank of Moldova (NBM, the central bank) bowed to the inevitable in November and ended support for the currency. Since 1994 the NBM's efforts had successfully maintained the stability of the leu to a nominal decline of only 3.7% against the dollar. After the devaluation of the Russian rouble in August, however, the leu came under increasing speculative pressure, since almost 75% of Moldova's trade is linked to Russia and Ukraine (which itself devalued sharply in September). Throughout September the pace of the leu's depreciation quickened, breaching the NBM's year-end target of Lei5:$1 in early October and the Lei6:$1 mark later that month. During this period the NBM intervened heavily on the Moldovan Interbank Currency Exchange, reducing foreign-currency reserves by 30% to around $200m, or only two months' worth of import cover. The central bank raised the minimum reserve requirement for commercial banks from 8% to 25% of total liabilities, effective from October 25th, in an effort to reduce the supply of local currency. By November 2nd the NBM was forced to declare its inability to intervene any longer.

—leading to a collapse against major currencies

This announcement led the leu to plunge quickly from Lei6.4:$1 to Lei 10:$1. The leu's rate is now determined by commercial bank interbank demand, with the NBM announcing an official weighted average rate each day. The NBM has largely withdrawn from currency auctions. By mid-November the currency had stabilised and recovered slightly, to Lei7.8:$1, before falling again to Lei9.7:$1 by the end of the month.

The IMF criticises NBM interventions—

The IMF's representative in Chisinau has described the leu's fall as positive, following long-standing IMF criticism of the central bank's determination to prop up the currency. The IMF has been particularly concerned by the NBM's efforts to support the leu and, simultaneously, to maintain secondary market liquidity in the Treasury-bill market, following a massive exodus by foreign investors. The Fund not only saw it as impossible for the NBM to pursue both targets at once, but also undesirable, given the effect on Moldovan exports of marked real depreciations in both Russia and Ukraine.

—but will resume lending

The Fund suspended disbursement of Moldova's three-year SDR130m ($186m) extended fund facility in July 1997 because of stalled economic reforms in the run-up to the parliamentary election. Following a recent assessment review, the IMF appears ready to release a further tranche of $35m by the beginning of 1999. As part of its agreement with the IMF, Moldova has agreed on the need for budget austerity, reduced government loan guarantees, tax reform and lower agricultural subsidies. A resumption of IMF lending would trigger an additional tranche of up to $65m from the World Bank's $100m package that was also suspended in 1997. The goodwill of both institutions remains particularly crucial to Moldova, which will rely increasingly on multilateral support as its primary source of foreign borrowing. The Fund has approved of earlier fiscal tightening, such as a revision of the 1998 budget expenditure in line with lower than expected revenue (3rd quarter 1998, page 27), and will welcome that Moldova is on track to meet its deficit target this year, owing to expenditure being lower than anticipated. At the same time, the IMF has specified additional reforms needed before restarting its disbursements. These include local government and administrative reforms, passed by parliament in November (see The political scene), as well as privatisation of the energy sector and pension reforms. The Fund will also insist that parliament proceeds quickly with passing an austere 1999 budget.

Moldova needs to agree on a budget—

The drafting process for the 1999 budget dragged on two months longer than planned and triggered several minor incidents, including the threatened resignation of the economy minister, Ion Sturza, over the government's initial proposal of a 5% deficit. Parliament gave its initial approval to the cabinet's proposed budget following its first reading on November 20th, although it has yet to give its final approval and continues to debate the draft. Projecting revenue of Lei2.8bn and expenditure of Lei3bn, the draft complies with IMF recommendations of a budget deficit of no more than 2% of GDP. Although debt servicing will reach a level approximately equal to 23% of the budget, the government has not included it in expenditure calculations, as it makes the optimistic claim that it can meet its financing needs through privatisation receipts and foreign loans. Because it anticipates that recent administrative reforms will cause problems involving local and central budget calculations, the government plans to propose further amendments to the budget during the first quarter of 1999.

—that will require deep cuts in spending

Preliminary details of the draft budget indicate that it includes a 5% tax on non-energy imports and higher excises on fuels and alcohol. Proposed spending cuts will lead to across-the-board reductions in such areas as education, social benefits, defence spending, agricultural subsidies and healthcare. Some of these cuts, if implemented, would reduce essential services to the bare minimum. Health workers in Chisinau have already heard of planned reductions in healthcare spending for the capital city from Lei150m to Lei48m, and have picketed government offices. Moreover, these spending cuts might need to reach even deeper. In drawing up its budget, the government has used several optimistic assumptions including moderate GDP growth in 1999. If the IMF does not pressure Moldova into rethinking its underlying budget assumptions, then even more cuts will become necessary, once lower than expected growth figures emerge.

Moldova: central government budget
(Lei m)

	1998 original	1998 amended	1999 proposed
Revenue	2,289.9	2,289.9	2,153.9
Expenditure	–2,639.0	–2,604.9	–2,353.9
Balance	–350.0	–315.0	–200.0

Sources: Moldovan Ministry of Finance, published in *Moldovan Economic Trends*; press reports.

Moldova suffers a growing energy crisis—

Moldova has struggled to settle its outstanding gas bill with Gazprom and avoid further supply cutbacks this winter. According to Gazprom, Moldova's debt has increased by $47m this year and now totals $614m, of which $391m is due from Transdniestr. Gazprom, under pressure to settle its own tax bills in Russia, halved supplies in July (3rd quarter 1998, page 29) and now threatens further reductions. It also wants cash, rather than the bartered goods that Moldova has traditionally supplied. With gas from Russia already significantly reduced, and Ukraine reportedly cutting its power supply to Moldova by 60%, a potential humanitarian disaster looms this winter. The government has already introduced rotating power cuts lasting from 12-20 hours per day. The typical family heating bill has reportedly risen to three times the average monthly wage, causing serious difficulties for citizens and resulting inevitably in increased debt to the sector. Government officials hope to avoid an even more serious energy crisis by introducing a system of rationed power supply to regional distribution networks based upon each network's ability to collect payment from consumers.

—and proposes settling gas debts with government securities—

Under a proposal approved by the government in September and passed by parliament on November 18th, Moldova would transfer $90m of seven-year government securities to Gazprom to pay for 1996-97 imports, with an annual interest rate of 7.5% and a two-year grace period. In a similar arrangement in 1997, Moldova transferred $140m of securities to Russia. Tiraspol has proposed that Moldovan government securities could also be used to settle part of Transdniestr's debt to Gazprom, thereby offsetting $15m of Moldova's debt to Transdniestr. In addition, Gazprom would receive a 50% stake in a new joint venture between Moldovagaz, the Moldovan gas monopoly, and Gasnabtransit, an earlier pipeline joint venture created with Gazprom to settle previous debts. Moldova and Transdniestr would hold 36% and 14% respectively in the venture.

—thereby angering the IMF—

The government's planned issuance of securities to cover part of its Gazprom arrears has concerned both the IMF and the NBM, which felt that Moldova's solution simply added to its growing debt mountain. As the NBM has pointed out, the new deal would add a further $18m a year in debt servicing at a time when the government is already struggling to finance the earlier $140m tranche of securities lodged with Gazprom. However, in a deal that paved the way for parliamentary approval, the IMF agreed to the government's plans once it promised to service the bonds through raised gas charges. According to the finance minister, Anatolie Arapu, gas fees of $70 per 1,000 cu metres would rise by $4.2 over the next two years and by $12.30 in the five years thereafter.

—which would rather see progress on energy reform

The Fund had also objected to the scheme because the government would once again assume the debts of various creditors, such as ministries and state-owned industries, instead of tackling the crucial issue of energy non-payment through privatisation of the energy sector, which would let new owners instil financial discipline. Not only are Moldova's accumulating energy bills a result of its massive dependency on foreign supplies, they are also the result of an unreformed energy system which has encouraged non-payment of bills. Under IMF and World Bank encouragement, Moldova has begun the slow process of restructuring its energy sector. It has transformed three of its four generators and five of its seven distributors into joint-stock companies in preparation for privatisation (the remainder are located in Transdniestr) and will soon issue international tenders to strategic investors. The procedure will involve budgetary costs, however, as companies will have debts cancelled to increase their attractiveness. The government will also rebalance electricity tariffs so that domestic consumers are no longer subsidised by industrial customers—although trade unions strongly resist this policy (3rd quarter 1998, page 28). Overall, energy prices remain artificially low by world standards, with electricity companies rarely receiving state compensation for the large number of exempted customers.

Moldtelecom is up for sale again

The government has renewed its efforts to sell a 40% share of Moldtelecom, the state telecommunications operator. It aborted its last attempt in August after OTE of Greece, the only bidder in the running, offered less than half of the $120m sought by the government for this flagship privatisation (3rd quarter 1998, page 35). Currently, the government offers prospective buyers a five-year monopoly on long-distance and international calls, as well as first refusal on the next mobile telephony licence. OTE will probably make another offer, having recently purchased a strategic stake in RomTelecom, in neighbouring Romania, as part of its strategy to dominate telecommunications in the region.

The economy

GDP slumps again—

After recording modest GDP growth of 1.3% in 1997, the Moldovan economy has deteriorated sharply in 1998. According to the State Department of Statistics, output in the first half of 1998 registered a 5% decline over the corresponding period in 1997. By mid-year the government had already revised its earlier forecast of up to 8% growth downwards, to 3%. By mid-November government officials further revised this downwards, forecasting negative growth in excess of 5%. The EIU forecasts a decline of 7% in 1998 and a further fall of 5% in 1999, before GDP growth levels out in 2000 (see Outlook for 1999-2000). None of these forecasts includes the shadow economy, which by some estimates comprises 65% of total economic activity.

Industrial performance falls sharply

Moldova has compiled grim industrial output figures in 1998. Monthly year-on-year figures show that, except in August, Moldova has suffered a drop in output since the start of the year. According to the *Moldovan Economic Trends*, an EU/TACIS-funded publication, the industrial index for the first nine months of 1998 declined by 8.7% over the corresponding period of 1997. Data for September indicate a severe downward trend following the Russian rouble devaluation, with year-on-year industrial production slumping by 32.5%. The nine-month downward trend has been owing mainly to a fall in output by 12.3% in the food, beverages and tobacco sector. Enterprises in the processed canned fruits and vegetables industry report a 13% reduction in production, mainly because of a lack of financing that has led to critical shortages of vital inputs.

Moldova's low inflation record comes to an end—

The successful strategy of the National Bank of Moldova (NBM, the central bank) of controlling inflation through tight monetary policy and a strong leu took a hammering in early November after it suspended support for the currency (see Economic policy). Average inflation during the first nine months of 1998 was a low 3%, benefiting from seasonally low food prices to post a decline of 0.6% in August and a modest 0.2% rise in September. However, the leu's drop caused chaos in early November, with petrol prices immediately shooting up by 25% and shops closing to revalue stock. The inflationary effects of the devaluation will prove profound, as the sharp rise in price of Moldova's dollar-denominated energy imports will feed into transport costs and manufacturing prices. The government has abandoned its hope of bringing annual average inflation down to 9% in 1998 from 11.8% in 1997. We anticipate year-end inflation of 23%, climbing to an average of 50% in 1999.

Moldova: consumer prices
(% change)

	Month on month	Year on year
1997		
Jan	1.9	13.3
Feb	1.4	10.9
Mar	1.0	10.8
Apr	0.8	10.8
May	0.6	11.3
Jun	2.0	13.8
Jul	–1.0	12.6
Aug	–0.8	10.1
Sep	1.2	9.7
Oct	0.9	10.6
Nov	1.1	10.3
Dec	1.5	11.2
1998		
Jan	1.3	10.4
Feb	0.4	9.3
Mar	–0.1	8.1
Apr	0.7	8.0
May	0.2	7.6
Jun	–1.1	4.3
Jul	–1.4	3.9
Aug	–0.6	4.1
Sep	0.2	3.1
Oct	1.4	3.6

Sources: *Moldovan Economic Trends*; EIU.

—while wage and benefits arrears mount

Wage arrears rose by almost half during the first two quarters of 1998 (see Economic policy). Approximately 40% of these arrears are in the agricultural sector, where debts extend back to 1996. However, this sector's percentage of the total has fallen from over 50% at the beginning of the year, because of a sharp increase in unpaid wages to public-sector and other budget-financed workers, who have borne the brunt of sharp cuts in 1998 budget expenditure. Employees in these sectors account for nearly 30% of the workforce.

Wage arrears by sector, Jan-Jul 1998
(Lei m unless otherwise indicated)

	Jan 1st 1998	% of total	Jul 1st 1998	% of total	% increase over Jan 1st
Agriculture, hunting & related services	183.62	50.64	202.94	39.10	10.52
Manufacturing industry	43.00	11.86	63.48	12.23	47.63
Construction	19.25	5.31	25.85	4.98	34.29
Transport & telecommunications	19.36	5.34	26.42	5.09	36.47
Real estate	10.08	2.78	16.66	3.21	65.28
State administration, defence & social insurance	23.03	6.35	56.89	10.96	147.03
Education	30.10	8.30	60.83	11.72	102.09
Healthcare & social assistance	17.51	4.83	33.22	6.40	89.72
Total incl others	362.60	100.00	519.04	100.00	43.14

Source: Department of Statistical and Sociological Analysis, published in *Moldovan Economic Trends.*

Foreign trade and payments

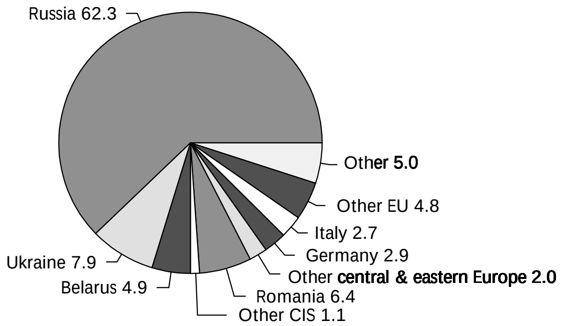
Moldova's foreign trade gap continues to widen—

Moldova's trade deficit for the first nine months of the year increased by 17.6% over the corresponding period in 1997, from \$278.2m to \$327.3m. Imports over the period fell by 2.9% compared with last year, to \$827.3m, while exports fell by 12.8% to \$500m. Statistics for September demonstrated a significant drop in overall trade, in revenue terms, largely owing to sharply reduced Russian demand. Exports fell particularly steeply, to 52.5% of last September's level, while imports fell by 34.8%. Trade statistics for the coming months promise to be exceptionally bad, with preliminary data indicating that by the end of October total exports had fallen by 19.3% and imports by 5.7% compared with last year.

—as trade remains poorly diversified

Moldova's trade depends heavily on CIS markets, which accounted for 76% of total exports as of June 1998. Russia alone took a 62% share of exports over that period, while the more lucrative EU markets together accounted for a mere 10% of total exports. The currencies of Moldova's important trading partners, Ukraine and Belarus, have also dropped substantially in real terms as a result of the Russian crisis. Together with Romania, which remains mired in a serious recession and has imposed a new 6% tax on imports, these countries accounted for more than 80% of Moldova's export markets in the first half of 1998. The closure of CIS markets beginning in August, therefore, will have a profound effect on the real economy, coinciding as it did with the peak season for Moldovan fresh food exports to Russia. Moldova's worsening trade balance with non-CIS states over the first nine months of the year compounds these trade diversification difficulties, as exports to non-CIS markets fell by 28.5% and imports rose by 21% over last year, according to *Moldovan Economic Trends*.

Moldova: exports by destination
% of total



Source: *Moldovan Economic Trends.*

Particularly alarming is the increase in imports from the EU by 43.1% in terms of revenue over the first nine months of 1998, compared with last year.

Barter's share of trade has fallen

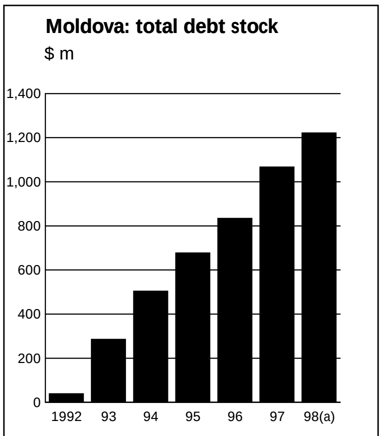
One encouraging trend in Moldova's trade is that cash settlements are playing a greater role, reducing the distortions inherent in non-cash transactions. According to data published in *Moldovan Economic Trends*, the amount of exports bartered fell from 19.3% in 1996 to 14.3% in 1997 and 13% in the first six months of 1998. In the case of imports, barter's share fell from 15.1% in 1996 to 10.8% in 1997 and 7.7% in the first six months of 1998. In the case of exports, vegetable products, food, tobacco, beverages, machinery and equipment accounted for most of the barter transactions, while most of the barter on the import side is for machinery and equipment, and mineral products, including fuel.

Moldova's current-account position appears unsustainable—

Moldova current-account deficit has continued to rise to dangerous levels. Data for the first half of the year show an increase in the deficit by 11.2% over 1997. Both the deficits in the trade balance and in the services balance increased considerably, by 22.9% and 20.3% respectively over last year's levels. On the capital account side, Moldova's situation looks similarly grim. Net figures for the capital and financial account show a decline of over 36%. Although direct investment grew by 39.2%, portfolio investments registered a net outflow of $8.27m, a stark contrast with last year's net inflows of $231.83m over the same period. Moldova's current-account financing gap of $185.3m for the first half of 1998 presents a significant problem, given the greatly reduced possibilities of accessing international capital markets or of accessing domestic savings. A resumption of multilateral disbursements will prove vital.

—as foreign investment remains modest and a debt crisis looms

The inflow of foreign direct investment (FDI) has increased, although the overall levels of foreign capital remain low owing to continued political and economic instability and a lack of progress in privatising larger companies. As of the first quarter of 1998 the largest amount of capital had been invested in energy and other utilities (41%), followed by manufacturing (32%), and wholesale and retail trade (15%). By country of origin, Russian companies accounted for the highest proportion (37%), followed by the US (13%).



(a) EIU estimate.
Source: EIU.

Moldova: current account

($ m)

	1997				1998	
	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr
Trade balance	–107.44	–72.30	–96.35	–67.92	–119.52	–101.34
Exports	190.77	204.88	210.47	284.66	174.58	184.20
Imports	–298.21	–277.18	–306.82	–352.58	–294.10	–285.54
Services balance	–17.96	–11.37	–6.51	–26.86	–20.37	–14.90
Income balance	13.98	6.75	7.80	5.43	8.96	12.14
Net transfers	17.46	4.44	27.11	27.96	23.22	26.47
Current-account balance	–93.96	–72.48	–67.95	–61.39	–107.71	–77.63

Source: National Bank of Moldova, published in *Moldovan Economic Trends*.

Moldova's debt situation remains serious, with the majority of the $215m owed in 1998 still due, and a further $235m coming due in 1999. The government has as much as conceded that it will not be able to meet its obligations for this year. Although very few details have been made available, the government has indicated that it is actively seeking a rescheduling of its debts with Merrill Lynch and Commerzbank, two major creditors which are also the lead managers on Moldova's planned Eurobond issuance. Although parliament approved the issue of a DM50m Eurobond in July, the markets remain in effect closed for all but the best-rated emerging markets credits. Even with resumed inflows from the IMF and the World Bank, Moldova will have difficulty meeting its obligations in 1999 and will have to seek further rescheduling.

Business news

There is a French buyer for Moldova's largest cement company

After two failed attempts, the government has finally succeeded in selling a majority stake in Ciment, the country's largest cement producer, to LaFarge of France. The government accepted a modest $200,000, as LaFarge will take over $7.6m of the company's debt and has committed to invest a further $12m.

Quarterly indicators and trade data

Belarus: quarterly indicators of economic activity

		1996			1997				1998		
		2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr
Industrial production	Monthly av										
General index	Jan 1994=100	84.3	90.3	92.3	94.1	97.2	97.6	100.1	104.2	106.3	n/a
Crude petroleum	'000 tonnes	154.3	156.0	154.7	149.7	151.7	154.0	155.0[a]	n/a	n/a	n/a
Natural gas	m cu metres	21.0	20.3	20.4	20.5	20.0	20.5	20.8[a]	n/a	n/a	n/a
Employment											
Unemployed	'000	176	185	183	178	157	140	126	118	109	n/a
	End-Qtr										
Employed, registered	'000	4,144	4,139	4,151	4,178	4,184	4,187	4,196	4,235	4,235	n/a
Wages & prices											
Nominal wages[b]	BRb '000	1,187	1,289	1,593	1,733	2,188	2,664	3,276	3,698	4,177	n/a
	Monthly av										
Consumer prices	1993=100	8,149	8,587	9,302	1,767	13,344	14,485	15,796	17,296	19,120	n/a
change year on year	%	50	41	36	52	64	69	70	47	43	n/a
Producer prices, ind	1993=100	5,132	5,547	5,990	8,131	9,867	10,632	11,380	12,509	13,598	n/a
Construction											
Houses completed	'000	2.57	3.20	5.67	1.60	3.03	3.73	n/a	n/a	n/a	n/a
Retail trade											
Sales	Jan 1995=100	91.1	110.4	123.0	99.4	108.7	118.5	137.2	134.3	138.8	n/a
Money											
M1	BRb bn	11,502	13,782	15,708	17,995	22,886	28,340	33,852	35,642	44,435	60,766
change year on year	%	65.2	64.2	56.7	82.3	99.0	105.6	115.5	98.1	94.2	114.4
Foreign trade	Qtrly totals										
Exports	$ m	1,431.2	1,429.8	1,483.9	1,439.4	1,774.1	1,961.4	2,126.3	1,758.2	1,878.3	1,165.0[c]
to CIS	"	961.5	933.6	888.8	955.3	1,096.4	1,404.6	n/a	n/a	n/a	n/a
Imports	"	1,752.4	1,630.7	1,890.8	1,939.2	2,040.5	2,187.0	2,522.1	2,257.4	2,255.8	1,376.0[c]
from CIS	"	1,143.7	1,073.9	1,272.1	1,345.5	1,289.7	1,387.7	n/a	n/a	n/a	n/a
Exchange holdings	End-Qtr										
Foreign exchange	$ m	367.9	410.6	469.0	427.3	376.2	383.5	393.7	291.3	286.1	299.4
Exchange rate											
Official rate	BRb:$	13,100	14,650	15,500	24,650	26,980	27,830	30,740	33,660	37,540	53,200

[a] October only. [b] Average monthly. [c] Total for July-August.

Sources: TACIS, *Belarus Economic Trends*, monthly; OECD, *Short-term Economic Indicators*; IMF, *International Financial Statistics*.

Moldova: quarterly indicators of economic activity

		1996			1997				1998		
		2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr
Construction	Monthly av										
Houses completed	'000	0.23	0.20	0.53	0.20	0.23	0.27	n/a	n/a	n/a	n/a
Employment											
Total	'000	1,700	1,670	1,630	1,580	1,690	1,660	n/a	n/a	n/a	n/a
Unemployed, registered	"	26.1	26.3	23.4	22.9	22.8	27.1	28.0	39.1	33.7	n/a
Wages & prices											
Nominal wages[a]	Lei	177	185	232	189	193	207	229	238	248	256[b]
Consumer prices	Jun 1994=100	157	159	165	171	176	177	181	187	187	183[b]
change year on year	%	25.6	24.2	14.6	10.9	12.0	11.1	9.9	9.4	6.3	n/a
Money	End-Qtr										
M1, seasonally adj	Lei m	1,005.5	893.8	888.0	1,029.8	1,121.4	1,075.5	1,159.7	1,356.5	1,209.5	1,126.0[c]
change year on year	%	64	33	12	6	12	20	31	32	8	n/a
M2	Lei m	1,186	1,246	1,292	1,261	1,411	1,585	1,740	1,689	1,603	1,649[c]
Foreign trade	Qtrly totals										
Exports	$ m	207.8	187.4	230.9	175.8	190.8	206.6	306.4	171.7	186.1	142.3
to CIS	"	149.1	125.9	149.7	135.6	150.4	155.6	182.4	126.6	n/a	n/a
Imports	"	259.1	272.9	292.4	301.9	213.8	295.7	321.0	287.0	288.9	251.4
from CIS	"	155.6	151.3	181.9	170.1	130.9	145.4	167.2	129.9	n/a	n/a
Exchange holdings	End-Qtr										
Foreign exchange	$ m	245.9	278.8	305.7	285.8	335.3	358.7	364.8	324.2	287.3	290.7[c]
Exchange rate											
Official rate	Leu:$	4.65	4.62	4.65	4.54	4.59	4.62	4.66	4.72	4.74	4.78[c]

[a] Average monthly. [b] Average for July-August. [c] End-August.

Sources: OECD, *Short-term Indicators*; IMF, *International Financial Statistics*; TACIS, *Moldovan Economic Trends*.

Belarus: OECD trade
($ '000)

	Germany		Italy		US	
	Jan-Dec 1995	Jan-Dec 1996	Jan-Dec 1995	Jan-Dec 1996	Jan-Dec 1995	Jan-Dec 1996
OECD exports fob						
Food	20,903	30,864	3,364	5,991	14,974	10,439
of which:						
cereals	4,065	3,835	395	1,178	75	1,096
Chemicals	68,795	88,773	2,575	4,343	4,443	4,167
Textile yarn, cloth & manufactures	23,874	29,916	13,713	14,162	411	827
Iron & steel	5,599	19,977	353	846	18	0
Metal manufactures	11,801	12,514	3,418	5,871	291	46
Machinery & transport equipment	316,816	228,173	34,237	38,541	11,218	15,011
of which:						
road vehicles	94,908	103,341	1,538	1,665	451	2,111
Clothing & footwear	25,689	24,456	8,690	10,157	806	100
Scientific instruments, etc.	24,119	21,124	1,423	5,046	4,382	2,809
Total incl others	733,825	620,628	85,292	107,738	47,330	52,836
OECD imports cif						
Food	14,061	17,386	2,125	1,864	164	448
Wood & cork & manufactures	22,182	20,933	2,971	3,151	105	1,137
Metalliferous ores & scrap	16,486	7,725	31	39	876	1,109
Petroleum & products	452	111	0	0	0	0
Chemicals	75,240	36,578	10,954	588	19,620	6,221
Textile yarn, cloth & manufactures	17,010	11,160	10,317	7,029	1,921	2,789
Non-metallic mineral manufactures	1,593	3,180	151	2	251	536
Non-ferrous metals	98,365	20,662	36	0	0	0
Metal manufactures	7,048	7,963	2,092	1,821	66	52
Machinery & transport equipment	26,336	30,831	2,200	3,909	9,169	8,029
Clothing	37,720	50,268	17,881	18,536	14,400	33,545
Scientific instruments, etc.	16,438	15,245	209	58	417	777
Total incl others	414,108	259,535	82,443	63,419	49,790	56,677

Source: UN, *External Trade Statistics*, series D.

Moldova: foreign trade

($ '000)

Imports cif	Total Jan-Dec 1994	Total Jan-Dec 1995	Russia Jan-Dec 1994	Russia Jan-Dec 1995	Ukraine Jan-Dec 1994	Ukraine Jan-Dec 1995	Romania Jan-Dec 1994	Romania Jan-Dec 1995	Bulgaria Jan-Dec 1994	Bulgaria Jan-Dec 1995
Food	34,477	49,447	3,360	6,620	5,166	10,902	1,913	2,205	459	983
Crude materials	19,141	31,562	5,438	8,188	3,318	8,939	3,023	2,651	217	155
Coal	55,657	50,278	7,390	6,317	47,676	43,485	0	0	0	0
Petroleum & products	132,394	182,568	67,721	63,991	24,345	66,427	15,332	16,281	49	3,045
Chemicals	44,439	77,722	8,482	15,765	6,503	13,433	4,331	5,745	3,239	2,270
Manufactured goods	74,979	120,505	25,895	39,303	14,005	21,888	3,932	10,813	3,491	11,024
of which:										
paper & manufactures	10,781	26,639	6,970	12,088	640	1,350	218	1,384	576	235
textile yarn, cloth & mnfrs	23,326	28,120	5,050	5,668	1,307	1,428	2,100	2,946	886	218
non-metallic mineral mnfrs	13,928	23,622	2,790	4,291	2,976	4,131	428	3,820	1,837	7,347
Machinery & transport eqpt	84,395	127,877	20,659	27,633	9,081	11,708	7,474	9,729	1,940	3,746
Total incl others	668,951	840,713	319,103	277,995	122,709	228,487	42,553	55,953	10,120	31,876

Exports fob	Total Jan-Dec 1994	Total Jan-Dec 1995	Russia Jan-Dec 1994	Russia Jan-Dec 1995	Ukraine Jan-Dec 1994	Ukraine Jan-Dec 1995	Romania Jan-Dec 1994	Romania Jan-Dec 1995	Germany Jan-Dec 1994	Germany Jan-Dec 1995
Food	230,598	295,954	118,144	132,842	27,113	8,886	33,836	63,788	10,851	23,464
of which:										
fruit, vegetables & preps	105,678	116,279	54,220	56,005	22,040	1,948	1,121	4,604	10,653	23,341
Beverages & tobacco	132,176	174,345	95,204	141,172	13,585	5,911	2,913	3,277	880	203
Manufactured goods	42,327	52,615	12,919	18,905	3,842	7,960	16,428	13,808	1,298	1,866
of which:										
non-metallic mineral mnfrs	5,640	15,378	1,365	9,319	1,463	2,768	2,504	2,457	0	0
Machinery & transport eqpt	65,148	58,793	36,259	27,607	15,249	14,783	5,777	5,773	313	81
Clothing	14,297	23,315	6,183	5,161	945	226	392	678	1,246	5,902
Total incl others	566,001	745,530	289,703	360,141	68,561	58,894	83,415	103,667	19,678	45,440

	Imports ($ m) Jan-Dec 1995	Imports ($ m) Jan-Dec 1996	Imports ($ m) Jan-Dec 1997	Imports ($ m) Jan-Jun 1997	Imports ($ m) Jan-Jun 1998	Exports ($ m) Jan-Dec 1995	Exports ($ m) Jan-Dec 1996	Exports ($ m) Jan-Dec 1997	Exports ($ m) Jan-Jun 1997	Exports ($ m) Jan-Jun 1998
CIS	568.9	664.1	612.4	305.8	247.0	466.9	546.1	612.5	293.7	272.6
Russia	278.0	295.3	305.1	154.0	145.3	360.1	430.1	509.8	242.2	223.0
Ukraine	228.5	297.1	240.2	127.8	75.3	58.9	47.6	52.1	23.5	28.3
Belarus	50.7	61.0	52.1	18.8	21.6	26.5	34.2	35.7	16.2	17.6
Central & eastern Europe	120.4	179.5	240.9	92.4	141.4	158.7	132.4	95.7	45.4	29.9
Romania	56.0	72.1	109.3	38.5	65.6	103.7	74.9	59.2	22.9	22.8
Bulgaria	31.9	58.4	62.9	25.8	22.9	21.4	12.7	10.0	4.0	1.6
Hungary	8.5	14.2	22.5	9.2	23.9	5.7	2.7	1.8	0.5	0.5
EU	115.2	162.6	227.2	101.0	157.7	86.2	78.3	90.4	34.8	37.2
Germany	45.6	65.9	95.5	43.9	55.6	45.4	29.9	32.5	13.5	10.4
Italy	19.3	33.9	42.1	17.8	32.6	15.6	21.1	23.8	10.1	9.7
Netherlands	6.6	10.5	12.9	5.3	6.9	2.3	8.7	5.6	2.5	2.1
Total incl others	840.7	1,079.2	1,172.4	556.6	575.9	745.5	801.6	879.6	391.2	357.7

Sources: UN, *External Trade Statistics*, series D; *Moldovan Economic Trends*.

Former Soviet republics: exchange rates

	Exchange rate per $									
	1996		1997				1998			
	Jul 5th	Oct 4th	Jan 1st	Apr 4th	Jul 11th	Oct 6th	Jan 12th	Apr 3rd	Jul 4th	Oct 7th
Outside rouble zone										
Armenia (dram)	410	412	440	469	505	501	496	502	502	508
Azerbaijan (manat)	4,300	4,304	4,200	4,074	3,968	3,928	3,891	3,858	3,861	3,857
Estonia (kroon)	12.2[a]	12.2	12.4[b]	13.4	14.0	14.2	14.5	14.8	14.5	13.1
Georgia (coupon/lari)	1.25[c]	1.27	1.29[d]	1.30[e]	1.30	1.30	1.31	1.34	1.35	1.37
Kazakhstan (tenge)	66.9	70.0	72.5	75.4	75.6	75.6	75.6	76.5	77.1	80.5
Kyrgyz Republic (som)	12.4	13.3	17.0	17.6[f]	17.3	17.3	17.4	18.1	19.3	22.4
Latvia (lat)	0.56[g]	0.55	0.56[d]	0.58	0.58	0.59	0.60	0.60	0.60	0.58
Lithuania (litas)	4.00[g]	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00
Moldova (leu)	4.65	4.61	4.60	4.57	4.57	4.62	4.66	4.72	4.75	4.99
Turkmenistan (manat)	3,935	4,075	5,000	4,110[e]	4,165	4,165	4,165	4,165	5,200	5,200
Ukraine (karbovanets/hryvnya)	178,900	1.77[h]	1.83	1.85	1.86	1.87	1.90	2.04	2.07	3.41
Uzbekistan (som)	37.8	40.0	55.0	58.9[i]	63.6	75.8	80.4	84.5	93.5	105.8
Inside rouble zone (local parallel currencies & Russian rouble)										
Belarus (rubel)	15,500	19,300	20,200	34,200	43,337	27,910	30,830	33,760	38,010	53,600
Russia (rouble)	5.131[a]	5.424	5.747[b]	5.737	5.788	5.865	5.972	6.112	6.202	15.794
Tajikistan (Tajikistan rouble)	280	298	330	380[i]	398[g]	747	748	754	754	754

[a] July 9th. [b] January 7th. [c] June 5th. [d] January 8th. [e] April 7th. [f] April 9th. [g] June 10th. [h] Karbovanets replaced by hryvnya on September 2nd, at the exchange rate of HRN1:KRB100,000. [i] April 11th.

Sources: OMRI; *FT*; BBC Monitoring, *Summary of World Broadcasts*; Reuters; Bloomberg.

Former Soviet republics: GDP and GDP per head

(at purchasing power parity)

	1989	1990	1991	1992	1993	1994	1995	1996	1997
Armenia									
GDP									
$ bn	17.6	17.0	16.1	7.9	6.9	7.3	8.0	8.6	9.0
per head ($)	5,058	4,804	4,467	2,142	1,853	1,942	2,122	2,287	2,389
Azerbaijan									
GDP									
$ bn	21.8	20.0	20.7	13.8	10.9	8.7	7.4	7.6	8.2
per head ($)	3,074	2,804	2,879	1,888	1,476	1,171	986	1,010	1,080
Belarus									
GDP									
$ bn	49.4	50.0	51.4	47.7	43.8	39.2	36.0	37.7	42.2
per head ($)	4,832	4,876	5,004	4,630	4,228	3,802	3,507	3,676	4,131
Estonia									
GDP									
$ bn	7.9	7.6	7.0	6.2	5.8	5.8	6.2	6.6	7.5
per head ($)	5,015	4,787	4,465	3,957	3,803	3,865	4,176	4,460	5,109
Georgia									
GDP									
$ bn	23.4	21.4	17.8	10.9	7.7	5.6	5.5	6.2	7.0
per head ($)	4,296	3,919	3,256	2,001	1,407	1,036	1,009	1,147	1,303
Kazakhstan									
GDP									
$ bn	71.8	74.6	72.3	64.6	56.0	43.0	40.0	41.2	42.8
per head ($)	4,342	4,477	4,302	3,825	3,316	2,569	2,421	2,495	2,587
Kyrgyz Republic									
GDP									
$ bn	11.1	11.9	11.2	9.7	8.3	6.3	6.0	6.5	7.0
per head ($)	2,553	2,706	2,523	2,163	1,863	1,405	1,336	1,419	1,529
Latvia									
GDP									
$ bn	13.6	14.6	13.6	9.1	8.0	8.2	8.3	8.8	9.5
per head ($)	5,094	5,469	5,114	3,460	3,070	3,213	3,313	3,516	3,847

continued

	1989	1990	1991	1992	1993	1994	1995	1996	1997
Lithuania									
GDP									
$ bn	20.3	20.1	19.7	16.0	13.7	12.7	13.4	14.3	15.4
per head ($)	5,505	5,412	5,278	4,268	3,681	3,409	3,612	3,853	4,164
Moldova									
GDP									
$ bn	15.9	16.2	13.9	10.2	10.3	7.3	7.3	6.9	7.1
per head ($)	3,664	3,723	3,193	2,335	2,362	1,675	1,681	1,583	1,637
Russia									
GDP									
$ bn	865.0	875.4	864.7	759.7	711.9	636.3	623.6	613.1	629.5
per head ($)	5,871	5,919	5,833	5,122	4,805	4,300	4,210	4,150	4,274
Tajikistan									
GDP									
$ bn	9.9	10.2	9.7	6.9	5.2	4.5	4.0	3.9	4.1
per head ($)	1,914	1,920	1,769	1,247	915	783	693	666	680
Turkmenistan									
GDP									
$ bn	10.0	10.7	10.5	10.2	9.5	7.7	6.8	6.4	4.8
per head ($)	2,797	2,903	2,806	2,541	2,195	1,757	1,513	1,404	1,053
Ukraine									
GDP									
$ bn	171.6	179.0	186.1	191.2	168.4	132.9	119.4	109.5	107.9
per head ($)	3,314	3,446	3,579	3,667	3,227	2,560	2,312	2,144	2,129
Uzbekistan									
GDP									
$ bn	44.5	47.2	48.8	44.6	44.7	43.7	43.9	45.4	47.4
per head ($)	2,215	2,312	2,341	2,089	2,048	1,963	1,952	1,982	1,998

Sources: IMF; World Bank, *Statistical Handbook: States of the Former USSR*; UN Economic Commission for Europe, *Bulletin for Europe*, Vol. 44 1992; EIU calculations.