Investment Risks in the Economy of Moldova in the Light of 2011 Crisis Phenomena

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Abstract. Please, find described below the world economic situation in the conditions of contemporary crisis transforming from "V" model to "W" modification, as well as actual economic situation of Moldova. There are given prerequisites of investment risks for the economy of Moldova, determined ways of their mitigation and submitted proposals to improve the national economy.

Keywords: risks, investment, crisis, world economy, Moldova.

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Introduction

Time is hard for the global economy nowadays. As far back as several months the crisis of 2008-2010 involving many regions and levels of global economy seemed to have been resolved. The strongest over the last decades recession of 2009 was followed by a more intensive period in the global economy. According to the information available from the International Monetary Fund, in 2010 increase in the world production volume amounted to 5,1%, after decrease by 0,5% in 2009, including the developed countries making up 3,0% and -3,4% while for the euro area it totaled 1,8% и -4,1%, respectively [1]. In fact, many countries came back to their pre-crisis levels of development. However the measures to recover national banking and finance systems were gradually transformed from recovery measures into mechanisms to form new global economic risks.

World Economy

Some countries increased their public spending at the expense of internal sources and external borrowings. As a result, some developed countries (the main engines of the global economy) faced the problems of budget deficit and state debt. Absolute level of the USA external debt almost triples the amount of the gross domestic product as per official exchange rate of the second world economy (China) [2]. In Japan the debt-GDP ratio amounted to 220%, in Germany – to 140%, in Italy – to 120%[3]. In the crisis year of 2009 the budget deficit exceeded 10% in some EU countries. This resulted in enormous perturbations which were faced in the middle of 2011 by two main global reserve currencies – dollar and euro.

These and some other factors led to market destabilization. Fall in leading stock indexes, instability at the markets of raw materials including gold market, problems at labor market increased in aggregate a possibility of second crisis wave in the global economy (transition from "V" model of crisis to its "W" modification).

Moldova in Conditions of Crisis

In Moldova the influence of 2008-2010 crisis turned out to be more significant than in the world economy on average. Fall in real gross domestic product in 2009 (-6,5%) was not recovered in general in 2010. One can notice a remarkable recovery in the majority of the national economy sectors (except for industry and transport). It is expected that by the end of 2011 most of the indicators will come back to the level of 2008. Over the first half of 2011 the GDP increased by 7,5%, volume of industrial production - by 9,1%, the one of agriculture - by 3,9%, fixed capital investment - by 31,8%. However, in the opinion of the Deputy Prime Minister, Minister of Economy, Mr Valery Lazar, the economic growth is still of recovery character to the extent of 90%. Although, there are sectors which have come out of crisis, they are already in progress [4].

Global economic trends of 2011 may have negative impact on the state of Moldovan economy. Among the main risks for the national economy of nowadays there should be mentioned such as rise in

prices for energy resources (gas, coal, fuel oil), import oriented economy, increasing state debt, state budget deficit, weakness and instability of stock market, decrease in population numbers, etc.

These actual risks are overlapping with traditional problems of the Moldovan economy of recent years (corruption, high share of shadow economy, degrading industrial production, etc.). According to our calculations, productivity of labor as per official currency exchange rate amounts to 80,3% of the world average level in agriculture, to 20,9% in industry and to 10,3% in services[5]. At that, Moldova of today is an economy of services, the share of which in GDP is close to 65%. Re-diversification of the national economy from industry to agriculture and then to services has not become a progressive trend for Moldova. Landline, mobile and internet providers (Orange, Moldcell and Moldtelecom) as well as gas monopolist (Moldovagas) belong to the largest enterprises of the country. A share and level of added value at these enterprises are not high and, in fact, these entities are just pumping over the population income transforming it to their profits.

Economic difficulties of the euro area countries are able to provoke a certain decrease of economic activity in the EU and creation of crisis conditions. This may bring to decrease in the Moldovan exports and reduction of money transfers by the Moldovan migrants from abroad.

In the conditions of the global economy developing as per "W" model money transfers of the country nationals temporary employed abroad are a considerable risk to stability of the Moldovan economy. More than 1,5 billion dollars were transferred by the Moldovan migrants from abroad to their home country in the pre-crisis year of 2008. In 2009 the country received 1,18 billion dollars, in 2010 – 1,24 billion dollars while during the first seven months of 2011 – 781 million dollars meaning 1,34 billion dollars as per year basis [6]. Notwithstanding the positive growth dynamics of money transfers by the Moldovan migrants from abroad in 2009-2010, the total amount of cash resources has not yet reached the pre-crisis level. It was expected that in 2011 Moldova would receive money transfers amounting to approximately 90% of 2008 level. However, given the growing economic problems of the euro area and the EU in general, a part of migrant workers will find themselves unemployed and some of them will come back to their home country. This will not only create virtual problems (increased share of unemployed population), but the budget receipts will be actually decreased, budget deficit will be increased, real income of the population will go down, social tension will become aggravated, etc.

Potential risk for the national economy to depend on money transfers of its nationals from abroad lies in significance of these revenues for the country's GDP. Having become one of the world leaders with money transfers from its citizens temporary employed abroad which make significant part of the country's GDP, Moldova has created "a center of delayed destabilization" within the national economy framework. In the conditions of global and regional economic growth the money resources of the citizens working abroad were favorably influencing the economy of the country. However, stagnation and economic slowdown in the world economy (-0,5%), in Europe (-3,4%) and in euro area (-4,1%) in 2009 led to almost 25% decline in money receipts from the citizens of Moldova working abroad.

Economic instability in Europe over the second half of 2011 may have heavy impact on the country's balance of payments. We assume that 1% decrease in the European production brings to 4,5% reduction in receipt of funds transferred to Moldova from abroad and decrease in the national GDP by 1,5-2%.

Apparently, the situation of Moldova in the coming second wave of the world crisis will be much worse than the average world one. The Moldovan markets show constant delay in falling with regard to the global leaders (the USA and EU) as well as to the neighbors (Ukraine and Romania). There is no argue that decrease in the indicators of the Moldovan economy will be conditioned among others by a forthcoming reduction of the country's export revenues. The struggle for outlets will become more violent under the crisis and Moldovan goods will be forced to cease their positions at the traditional markets. Export of petrol and oil products which became a usual item of revenues from the country's foreign trade, might make an exclusion. Although in this case it is a question of re-export or, as in tailoring industry – of temporary import to the territory of Moldova.

In general, in their aggregate reduced export and decreased money supply from the migrants working abroad will raise the risks for the national economy not in the order of arithmetic progression. This will speed up and aggravate the problems of Moldovan economy in the second part of W phase of the contemporary global economic crisis.

The conditions of crisis increase the need for financial instruments to influence the economy and in such small countries as Moldova – the need for foreign investment. The experience of the world financial and economic crisis in 2008-2010 shows the need for rational regulation of the national economy especially in the field of investment. It is evident that he measures to attract investment, to provide insurance for enormous aggregate of investment risks in the national economy and at the finance and banking market turned out to be inadequate to the requirements at this stage of development.

The main problems of the system lie in maladaptation of regulatory basis in the national investment process to the EU requirements and its incompliance with the modern challenges of crisis development. Significant administrative pressure is exercised on investment processes in the country, systematized and science-based activity to prevent and reduce consequences of investment risks is not being carried out, investment projects reveal insufficient degree and depth of development, there is no efficient control of their development and implementation, level of staffing is insufficient, process of investment decision making is highly influenced by external factors, etc. As a result, even launched investment projects do not reach implementation level. These are such objects as 17 story "National" hotel, Republican Stadium, "Valea Morilor" park and lake, Chisinau hotel at the address of 115, Stefan Cel Mare Av. etc.

One may regard as revealing the fate of investment projects in Moldova based on example of Moldovan-Russian enterprise Santek. In 2002 it launched production of facing tiles in the "Taraclia" zone of free economic activity. Further on, the assets of Santek were bought out by an enterprise with Ukranian investments Ispan-Lux which became a resident of the free economic activity zone in September 2010. However, due to administrative problems, the enterprise did not succeed to connect to power supply until September 2010. The government recommends to the new resident of the zone to independently solve the problem by means of collaboration on the basis of direct negotiations with legal entities outside the zone as represented by the court bailiffs [7]. In fact for more than a year the Ukrainian investment into the economy of Moldova cannot start working which brusquely reduces attractiveness of the Moldovan market for foreign investment.

The flow of foreign investment to Moldova is restrained by a high share of monopolists within the state and private sectors at the local market and long standing procrastination in privatization of enterprises attractive for foreign investors. Such enterprises as Air Moldova, Chisinau International Airport, Franzeluta, Metalferos, Moldovagaz, Moldtelecom, Moldovan Railway, Tutun-CTC and others are able to play a significant role in attracting investment into the economy of the country.

The stock market of Moldova appears to be at the same time a break and a significant potential for attracting foreign investment. The national stock market is characterized by considerable propensity for development and improvement but with regard to certain characteristics it has considerable reserves to improve its state (its level already in place) and trends [8]. This is referred to driving shadow economy out of the stock market, extension of rights and obligations of the Moldova Stock Exchange (MSE), raising attractiveness of the national stock market for foreign investors. There are suggestions to extend the MSE listings (now it numbers 12 issues including 6 of 15 licensed banks of the Republic of Moldova), to reincorporate the insurance market of Moldova as a joint stock company (on the basis of the open joint stock companies), etc.

Situation statement and ways of solution

Thus, the study of this problem brought us to the following considerations:

1. The economic crisis of 2008-2010 and the trends revealed in the middle of 2011 allow for the conclusion on continuity of this process, unity and integrity of the phase in the economic cycle of 2008-2010

2. The economic processes of 2008-2011 being though of discrete and at the same time global character, give us a possibility to assume that the crisis is being transformed from the "V" form into the "W" graphic representation..

3. International, regional and state regulation as well as correction of economic processes with a view to overcome the crisis of 2008-2010 turned out to be of low effectiveness in some global economies. The problems of budget consolidation and pressure exercised on the economy by such indicator as "gross debt/GDP" are aggravated in the majority of developed countries. The programs of social expenditures do not undergo reforms which could enable decrease in expenditures without suppressing consumer demand.

4. Crisis phenomena of the contemporary phase in the global and European economic development give us a possibility to word a thesis on the need for not only government regulation and correction of economic processes, but also for search and implementation of principally new, more precise and responsible mechanisms of regulation at all the world economy levels (global, regional and national).

5. The problems of national and European economies have their aggravated but somewhat delayed (time lag) impact on the economy of the Republic of Moldova. The risks for the national economy are conditioned by a high share of migrant workers and unique influence of their money transfers on the country's GDP, import orientation of the national economy, unreasonable transformation of the country's economy into an industrial, industrial and agricultural and then into an "economy of services" with insignificant share of added value and far more distant levels of labor efficiency than the world economy average, etc.

6. Investment activity in Moldova needs resetting and new radical adjustment. First of all, this pertains to setting priorities for investment activity. At the main entity (enterprise) level investment priorities are revealed with the help of methodological principles for effectiveness substantiation in the investment projects (PP, ROI, NPV, PI, IRR, MIRR, DPP). However, it is impossible to apply these methods at the macroeconomic level where a model of regional economic development previously formed under the influence of administrative decisions is often dominating as a criterion. Such mechanism for setting priorities of the national investment policy on the basis of previously formed sectorial structure (inertial type organization of the national investment sector) is especially characteristic for all the countries with transition economy, but at that it is brusquely revealed in the Moldovan economy.

7. The regulation mechanism of investment activity in Moldova is formed by the law on foreign investment (1992 and 2000), the law on investment into entrepreneurial activity (2004), the strategy to attract investment and promote export for 2006-2015), etc. There is a constant increase in the total volume of investment into the capital assets in Moldova (except for 2009). However, in Moldova the investments have not become the main driving force of the national economic growth. Low economic feasibility of priorities when investment is not sent to the most promising sectors of economy, from the world practice point of view, is seen as one of the reasons for the situation in place.

8. As to the global economy, the main share in the world gross domestic product belongs to services (64%) which are followed by industry (32%) and agriculture (4%). The value of indicator showing the GDP ratio per one employee (as per purchase power of currencies) are distributed the following way: services - $34,1 thousand USD, industry – 32,7 thousand USD, agriculture – 2,1 thousand USD. So, services are the biggest and most efficient sector of the world economy.

9. In Moldova a share of services in the sectorial structure of GDP amounts to 60,5%, the one of industry – to 21,7% and the one of agriculture – to 17,8%. Labor efficiency in services sector, industry and agriculture total 9,5 thousand USD, 13,2 thousand USD and 3,2 thousand USD, respectively amounting to 28%, 40% and 152% of the world level [9]. Growth potential of the national labor effectiveness up to the average world level is the highest in the sector of services (3,5 times)

10. Identified strategic prerequisites to determine innovation priorities in the investment policy of Moldova give a possibility to assume that potentially the services sector of Moldova is the most attractive from the point of the national economy effectiveness. At the same time the state regulation and correction of economic processes, including investment policy, are a product of administrative impact. They may lead to a negative result. In order to reduce the risks of negative administrative impact on the state investment policy it is necessary to form a system, based on experience of developed countries, that would not only attract investment in any, including non-efficient sectors, but an investment mechanism that would be selective, regulated and most efficient. Based on the world practice it is necessary to determine the most effective investment priorities and create conditions for their implementation. Moldova should apply the world experience to speed up a process of economic rehabilitation and to reduce the recovery period of the national economy. In our opinion, to this purpose it is essential to use a method of investment policy making based on principles of recording the world demand for goods and services with orientation the global and regional competitors. In fact, this refers to the "follow leader" method. It is reasonable to fix as a leader the world economy system in general, as it is the most stable economic structure in order to word priorities of the national investment policy based on the world experience.

11. The mechanism of investment transformation into the driving force of the national economic growth envisages as follows:

- Setting of priorities of the Moldovan investment policy on a principally new basis – "follow the leader" (the world economy);
- Study of development trends in the world economy at present stage; application of the new world and European experience for its modernization in order to speed up adaptation of the national economy to the regulated market mechanisms;
- Choosing services sector as a priority for investment strategy of Moldova ;
- Development of system measures including institutional, economic, technical-technological, social and other ones to implement the national investment policy based on suggested concept of priority formation;
- Identification of services which are potentially more attractive for the world economy and development of mechanism to implement their priority order;
- Reformation of regulatory basis (law, strategies) for attracting investment in compliance with contemporary trends of the world economy development, use of the world and European experience for its modernization with regard to the national peculiarities;;

12. In actual conditions the state regulation of investment sector should be made based on innovative economy principles. Innovative economic development of the region involves identification and use of ways and methods that are adequate to the world economic system. In broader terms the innovative way of economic development may involve implementation of management decisions that are new in a particular region but are just of really modern character. Principally new basis ("follow the leader – the world economy") applied for implementation of the national investment policy will inevitably bring to a change of priorities in the economic development of the country but it will give a possibility to raise effectiveness if the Moldovan economy. Reorientation of investment policy to the services sector and first of all to tourism is able to bring to the GDP growth by 3,6 if there are average world indicators of tourist load and labor efficiency in place.

Experience of the world financial and economic crisis of 2008-2010 shows the need for rational regulation of the national economy and especially of its finance and banking sector. It is evident that the measures to attract investment, to provide insurance for an enormous aggregation of investment risks in the national economy as well as in the finance and banking sector turned out to be inadequate to the requirements of economic development at present stage.

The main system problems lie in the insufficient regulatory basis of the national investment process, lack of methodical and science based activity to prevent and reduce the consequences of investment risks, insufficient development of investment projects, ineffective control of their development and implementation, poor staffing levels, influence of external factors on the process of investment decision-making, etc.

The above stated involves the need to :

- Correct the national investment policy
- Develop the National Strategy of the Economic Progress of Moldova ()coordinated in terms of time and successive in terms of content and target orientation with the aggregate of the national economic mechanisms for stabilization and growth of the national economy including at the expense of investment sector ;
- Review the Law on Investment in Economic Activity, Strategy of Investment Attraction based on principles of harmonizing national legislation with the EU regulatory basis, coordinated character of the National Strategy of the Economic Progress of Moldova, to raise efficiency of investment projects, to reduce investment risks envisaging certain tool for risk damping;
- To reconstruct the legal basis of investment activity with regard to feasibility of more effective opposition by society as well as banking and finance system to the challenges on behalf of different forms and types of investment risks;
- To create harmonious national system of economy insurance, to ensure its banking and finance sector from the risks appearing in the investment sector;
- To decrease dependence of the national economy from money transfers by the citizens of Moldova having temporary employment abroad. To develop a Program of Entrepreneurial Activization in the country based on eradication of corruption, law priority, improvement of justice, decrease of administrative influence on the economy, expansion and deepening of privatization processes, etc.;
- To foresee the measures of economy diversification, to overcome reduction trends in the agricultural and industrial potential of the country, to revive the elements in the field of national good manufacturers, legal development of export oriented activities in the sector of services (tourism, travelling, transport, etc).

Conclusions

The studies we undertook make it possible to suggest that the following measures may contribute to decrease of risks in the process of attracting investments to Moldova:

1. Activation and expansion in the field of state assets privatization based on recommendations of international experts (telecommunications, transport, food industry, etc.)
2. Expansion in the field of land market activity based on property and tenant rights for foreign investors in correlation with the stock market of Moldova.
3. Development and implementation of a system of measures to drive shadow turnover out of the country's economy (in production and sale of goods and services, in the field of customs, at the real estate and stock markets, etc.).

The following measures appear to be appropriate in order to create competitive business environment and to mobilize market mechanisms for the stock market of Moldova:

1. To review the current national legislation regulating stock market with a view to adapt it to the EU legislation subject to recommendations of the European experts, ideas underlying in the EU-Moldova Action Plan, world experience of stock market functioning.

2. To continue further institutional reformation of the national stock market in compliance with the international trends. To transform the Moldova Stock Exchange into a real public shareholding company in the form of public enterprise. To increase authorized capital stock of the MSE from the actual $48,1 thousand USD. To ban direct or indirect possession of 10 percent holding in common company stock by one person. To set permanent quoting norm at the market to the extent of not less than 25% of the MSE authorized capital. To keep not less than 50% of the total voting shares amount (at present 37 shareholders including 22 stock exchange members) as owned by brokers and dealers.

3. To establish public funds (in the form of JSC with obligatory circulation of shares at the MSE) for development of socially relevant enterprises (first of all, in the field of residential housing) including on the mortgage basis under the control of the state and local government bodies.

4. To lift unjustified administrative restrictions on the activity at the country's stock market. To provide a possibility for circulation of securities belonging to foreign issuers at the national stock market

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