

## THE IMPEDIMENTS EXISTING IN THE INVESTMENT PROCESS IN THE REPUBLIC OF MOLDOVA

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### *Abstract*

*This paper presents an analysis of the impediments that arise in the investment process in the Republic of Moldova. Although the investment in agriculture in the period 2009-2015 grew much faster than the investment in the economy and other areas, problems and obstacles that appear relate to several factors. Starting from the decisive role that agriculture plays in the sustainable development of the Republic of Moldova's economy, addressing the problems that hinder its development, in terms of investment, is very important as Agriculture and Food Industry in the Republic of Moldova are the most important sectors, designed to contribute to the increase of our economy. Thus, the need to assess the existing impediments in the investment process of the agricultural sector defined the topic of our research.*

**Key words:** financial assistance, impediments, investment, international projects

### INTRODUCTION

Agriculture today enjoys special attention in all countries, regardless of their economic development. As a main branch of the Moldovan national economy, agriculture stands out as a particularly complex field; its complexity is determined by the role of agriculture in economic development and its economic and social peculiarities. The analysis showed that the number of investments for different areas from the EU and the US amounted to hundreds of millions of Euro; a big part of them being offered to agriculture.

The suspension of external financial assistance for the Republic of Moldova at the end of 2015 as a result of lack of reforms and corruption, combined with the Russian Federation's embargo on Moldovan food products, produced a devastating effect on the economy of the country.

However, we should mention that the increase of investments in agriculture is one of the basic factors that contribute to the economic growth, to the comprehensive improvement of the national economy, to solving the problems of retrofitting and modernization of agricultural enterprises in the Republic of

Moldova.[9]

The issue of investment and economic growth has been researched by a large number of authors in their fundamental scientific works and publications in specialized journals, but some of the theoretical and methodological aspects are not sufficiently developed by renowned scholars in this field of research. Thus, having studied a large number of scientific papers on the subject we can see that the instruments of investment mechanism in agricultural sector, that will ensure sustainable economic growth, have not been finalized. Thus, the continued need for investment process in agriculture has defined the topic of our research that is influenced by the following factors:

- a. scientific and practical importance of the problem and the need for further research of funding instruments in the agricultural sector to ensure the economic growth of the sector;
- b. the need to improve and develop a viable mechanism for the growth of the agricultural sector in terms of investment.

### MATERIALS AND METHODS

The material used for the undertaken research consisted in the research, analysis and

interpretation of data from specialty literature. There were used such research methods as: analysis, comparison, deduction, monographic method. The information was gathered from the sources published by the National Bureau of Statistics, the National Agency for Employment, reports of various national and international bodies.

## RESULTS AND DISCUSSIONS

The investment process means all activities, works and operations carried out over a period of time, implying material, financial, human and information resources through the intervention of various political, economic, financial and social factors in order to achieve economic, social and other objectives. "Investment is the primary factor in national economic development strategy, it is important for all branches and industries, for revenues increase, it is the condition of raising the standard of living" [8].

Before investing, any investor analyses the investment climate and the investment potential of the state and of its economic sector, which, we consider, reflects their investment attractiveness.

The concept of "investment attractiveness" can be formulated and applied both at the level of an enterprise and at the level of a sector. Being considered as a normative one, this concept is used as a criterion for assessing the competitiveness of the sector. Thus, the competitiveness of the national economy is determined by its investment attractiveness. The process of research related to determining investment attractiveness operates with such categories as:

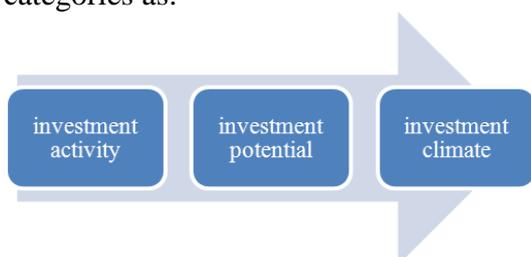


Fig. 1. The structure of investment attractiveness

The investment attractiveness reflects the subjective attitude of the potential investors towards the investment object.

The investment climate reflects the level of readiness of the social, environmental and economic system to the investment process or the objective situation of the external environment of the investment object.[1]

The notion of investment climate can be defined as the environment in which the investment process of economic units takes place, the totality of social, economic, political, legal, institutional, cultural premises that determine the attractiveness and usability level of investment implemented in an economic system. [3]

Most economists from the Republic of Moldova are of the opinion that the development of the country depends on the efficiency of all the components of investment sphere, supporting the idea of the positive impact of investments on economic development.

However, investment attractiveness of the Republic of Moldova, including the agricultural sector, has a downward trend due to the increasing number of factors that reduce the investment attractiveness of the country. [5]

However, according to the report "Doing Business 2015" ( "Doing Business 2015"), and the study "Cost of doing business 2014" ("Cost of Doing Business Survey 2014 ') the Republic of Moldova has made substantial progress in simplifying the regulation of economic activity and in improving the investment climate and business environment, but this progress has been irregular. In the report "Doing business 2015: Beyond efficiency" the Republic of Moldova is rated 63rd of 189 economies, an improvement of 19 places comparing to the previous year. This increase is due to the fact that the Republic of Moldova has eased business start-up by cancelling the minimum capital requirement, has eased tax payment through the introduction of an electronic system for completing the documents and for the payment of social security contributions. On the other hand, it has increased the minimum wage used to calculate the amount of environmental tax. [2]

The main factors that make Moldova attractive for foreign investments are:

1. The advantageous location of the state - it is a link between the East and the West and it has a favourable geographic location in the centre of Europe.

2. Fertile soils (80% of the territory is the black soils) -Moldova is rich in fertile soils. We have opportunities for ecologically clean production of goods. Agriculture is one of the areas that would most interest the foreign investors.

3. Low and qualified labour force - Moldova has skilled labour force, available at much lower prices than in many other European countries.

In market economy the main source of investment financing are own funds formed on the basis of profit obtained from economic activity or other financial means.[10] In most cases, the agricultural enterprises own insufficient resources to finance the necessary investments. Thus the farmers use borrowed sources such as bank loans, deposits from the founders or other funding sources. It is obvious that the role of credits in financing investment projects is a positive one; they contribute to the modernization of agricultural enterprises. But at the same time the interest payment is a burden which leads to reduced economic efficiency of production during the period of loan repayment.

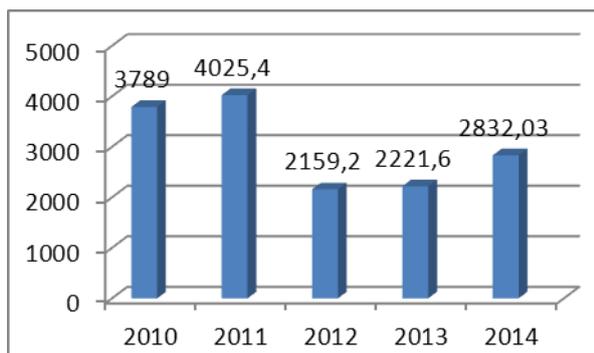


Fig. 2. The value of loans granted to the agriculture, mil. MDL

Analysing the data NBM (Fig.2), we can see a slow decrease of loans offered by commercial banks for the development of agriculture in 2010-2014.

However, in order to help increase the efficiency of the agricultural sector, there was introduced the concept of agricultural loans

extended by commercial banks of the Republic of Moldova and agreed by donors. Loans are granted to farmers to support agricultural development.

Thus, in 2014, there were awarded 956.9 mln. lei (9.5%) for investments in agriculture less than in 2010. The main reason why farmers give up investments made from bank loans is the suffocating rate of interest on the loans offered by commercial banks and the value of the pledge required by the banks. Another reason why the value of the loans offered to agricultural and food sector constitutes only a very small part of total loans is the fact that low income and low financial strength make farmers a less attractive target for commercial banks. Analysing the loan portfolio we can see that in 2013 only 12% of total loans were granted to food sector, 4.4% less than in 2010. Of these only 7.18% are used for agriculture. The most active banks that offer credits in this area are Moldova Agroindbank (30.93%), ProCredit Bank (23.89%) and Victoriabank (19.17%). The volume of the loans in this area doesn't depend too much on the price of these loans, e.g. Moldova Agroindbank grants loans at interest of 12.74% in MDL and 6.84% in foreign currencies, Victoriabank - 10.9% in lei and 7, 03% in currency and t ProCreditBank grant loans at interest of 17.28% in lei and 8.26% in foreign currency.

The purpose of granting loans for agriculture is to make long -term investments in performance equipment, in irrigation equipment, in the establishment of adequate premises for livestock growing, in the maintenance of plantations and others, all of them designed to increase agricultural production.

Experts say that in recent years there have increased the dependence on external sources of financing capital expenditures in agriculture. "The imposing dynamics of capital allocations during 2010-2015 was provided predominantly by higher volume of external grants and credits for agriculture. The largest increase in this area was recorded in 2012 and 2013; the volume of capital expenditures from external sources exceeded the expenditures from internal sources".

The result of those trends was a sharp rise in

the share of external sources from about 39% at the beginning of the period to 58% in 2013. From the total 43 projects, which were entitled to grant, only 27 projects or 56.2% have already been implemented and 10 projects are to be completed during 2016. Thus, in 2017- 2018 only 11 projects will be in working, which shows a rather low rate of contacting the new funds compared to previous years. A number of other donors have contributed to the implementation of vital projects in agriculture: United Nations (UN), World Bank (WB), and European Investment Bank (EIB). And several countries have granted individual assistance: the Czech Republic, Switzerland, Poland, Romania, the USA, Sweden, etc.

Despite the internal dissensions, a number of projects in agriculture had great success. They are:

- Compact Project (2010-2015), funded by the US through Millennium Challenge Corporation.

- "Competitive Agriculture" Project (MAC-P) from 2012 to 2017, the World Bank, the Government of Sweden.

- Agricultural Competitiveness and Enterprise Development Project (ACED) (2011-2016), funded by USAID and the Millennium Challenge Corporation.

Several other projects also contributed to improving certain subdomains of the country's agricultural sector, the most important are:

- IFAD 5 (2011-2016), financed by Denmark and the UN.

- IFAD 6 (2014-2020), Global Environment Facility funds and Denmark.

- ENPARD (2015-2022), funded by the EU.

- Assistance Project for unprivileged farmers 2KR funded by the Japanese Government.

- However, a number of projects remained at the "waiting" stage as for example:

- Support Program of the Government of Poland (initiated in 2014) amounting to 100 million EUR. The aim of this project relates to the agro-food production and development of poultry, meat and milk processing. Right from the beginning of the initiation dissensions arose referring to the project implementation.

- "Orchard of Moldova" Project, aimed to develop the horticultural value chain. Under

the contract signed by the Republic of Moldova and the European Investment Bank (EIB) the implementation of the project with a budget of 120 mln. EURO was planned for 2014-2020. The project's authors estimated that about 300 businesses and 52,000 farms could benefit from the program. The big problem was, however, the transparency of banks in the Republic of Moldova, which didn't suit the funder.[7]

Meanwhile, a large number of international funding and donor agencies such as USAID, SIDA, IFAD, Soros Foundation, organizations in Japan (Moldovan-Japanese project 2KR), Poland, Germany and the Netherlands, have increased their efforts to support agricultural activities, including investment grants, low interest rate loans, bank guarantees and technical assistance.

However the share of FDI in agriculture remains quite small, although in 2011 it increased to 2.85% and constituted 4.36% of the total volume of investments in agriculture compared to 1.51% in 2009, having a slight reduction of 0.23% in 2012 which indirectly confirms the instability of foreign investments in Moldova's agricultural sector. Investment activity in the Republic of Moldova is coordinated by legislation in force. The first legislative act that stipulated investment activity was the Law on Foreign Investment, no. 998 of 01.04.1992. [6]. In 2002, the Government adopted the Decision on the investment strategy in the Republic of Moldova, which stipulated the activities related to the investment system:

- ensuring a favourable investment climate;
- attracting foreign and local investments;
- businesses access to investment loans for modernization of enterprises;
- implementing investment projects;
- creation of a database on investment programs. [4].

In order to increase investments there has been developed the State economic growth strategy, the Bank for Development and Investment of the Republic of Moldova and the National Agency were created to attract investments. Agrarian sector activity also is coordinated by a series of laws, decisions and programs meant to recover and streamline the

activities in the sector.

The Republic of Moldova could unlock additional investments solving other regulatory problems. These problems vary in the degree of restrictions, complexity and unpredictability. With the outbreak of the crisis, investments in the EU and in Moldova have decreased significantly.

Some economists believe that the level of investments will increase, but the recovery could remain low, reflecting weak demand, deleveraging of enterprises, stricter lending conditions. The identification and elimination of these obstacles to investment is a part of the efforts to improve framework conditions and to eliminate bureaucracy and regulatory bottlenecks, as a part of the so-called "third pillar" of the Investment Plan for Europe.

## CONCLUSIONS

The carried out research allows us to highlight the following impediments that contribute to the decrease of investment attractiveness of the Republic of Moldova:

1. Political instability;
2. Bureaucracy, corruption and protectionism. For most foreign investors corruption is the main obstacle to doing business. Domestic and foreign investors are not satisfied that the bureaucratic formalities require a very long time and high costs;
3. The dependence of the economy on energy resources limits foreign investments in domestic-oriented sectors. The interruption of oil and gas supply will lead to halting economic growth, which will lead to the reduction of the country's attractiveness to foreign investors;
4. Instability of secure legislative basis. This phenomenon can lead to a high risk of change in legislation, to changes in economic and legal mechanism of regulation by the state of foreign investments, that doesn't correspond to reality;
5. The low level of business culture towards the investor;
6. Lack of confidence in the banking system. Low efficiency of other agents of the domestic financial market (insufficient development of the securities market, of

insurance companies, of the pension funds);

7. Market information and limited market access;

8. Food quality and safety remains unsatisfactory.

9. Low level of technical assistance in project implementation.

10. Providing technology for storage and processing of agricultural production.

It should be noted that the main purpose of investment must be directed towards the recovery of agriculture and increasing the living standards of people living in rural areas. It is necessary that all opportunities for agricultural growth and the development of rural areas should be reviewed and valued, both by adequate investment and by developing or updating integrated rural development strategies. Thus, knowing the mechanisms of intervention in the policy of agricultural sector development policy and the efficient use of the agricultural practice of developed countries are the necessary premises to build a functioning market economy.

In many parts of the country, agriculture is at the limit of subsistence: productivity is very low, products competitiveness is modest, and the products are sold at very low prices. Among the causes of the poor state of agriculture is excessive land fragmentation, poor mechanization of agricultural enterprises, competition from foreign states, modest state support, insufficient financial resources and few opportunities to attract foreign investments.

Thus, attracting investment becomes a strategic priority of farmers at present moment because investment is the material support of economic growth. The modernization of agrarian sector and of production capacities can be made only on the basis of considerable investments. Increased investment in agriculture is one of the basic factors that contributes to economic growth and improvement of comprehensive national economy, solving the problems of retrofitting and modernization of agricultural enterprises in the Republic of Moldova.

Although in the past decade there were made massive investments in agriculture, they did

not contribute to the sustainable growth of the sector. Moreover, animal and plant production practically did not increase in real terms, according to the analysis prepared by the Expert Group. Experts believe that the cause of this stagnation is inefficient allocation of financial resources.

At the same time budgetary transparency is poor. While the institutional framework responsible for agriculture has progressed quite significantly, in terms of budgetary transparency and reporting to the institutions responsible for agriculture the results are more modest. In this regard, experts point out that the low level of budgetary transparency does not allow the analysis of the expenditures impact on the economic growth in the agricultural sector.

The study considers successful the launch of BOOST database in 2010 and the publication of quarterly and annual reports on MAIA budget execution since 2014. However, the overwhelming majority of public institutions and state enterprises operating in the sector do not publish progress reports. "Of all the institutions analysed in this category, only AIPA and MAIA publish such reports, but without being accompanied by any narrative explanation", the authors of the analysis say.

The agricultural sector and the entire economy of the Republic of Moldova are facing increasing technical and scientific implications, whose "products" require for their application in manufacturing important investment funds. Mechanization, automation and robotics of production cannot become realities without spending by the state and the whole society major investment funds. For Moldovan economy investments are the key driver of sustainable growth and one of the main factors that can decrease the gaps between our country and economically advanced countries. Only through proper use of investment resources we can create new jobs, increase the gross national product per inhabitant, increase labour productivity and, as a result, the quality of life.

The EU Commission, EU countries and the US government gave assurances that they would continue to support Moldova's economy, but they conditioned their support

with stronger measures to combat corruption, including high-level, and the recovery of banking system, which is currently in a very deplorable situation.

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