



## CHAPTER 2.

## TRANSITION. PROFILE OF HUMAN SECURITY IN MOLDOVA

*“Humans are not above the time, it’s time which is above the humans.”*

Miron Costin

### 2.1. Economic Reforms: Expectations and Realities

The aim of any reform is to make a change for the better. The reforms implemented in the transition countries are entirely directed towards improving the living standards of the population. Unfortunately, this has not taken place yet.

The Human Development Index (HDI) for the Republic of Moldova shows a negative trend during the transition period (Table 2.1.1).

to values of the HDI below 0.500. Unfortunately, below that threshold live about 1/3 of the world population. HDI levels above 0.500 are defined as “medium human development”.

Between 1990 and 1995, the ranking of the Republic of Moldova on the HDI has fallen from 64 to 113. This has in large measure been a consequence of the reforms of the state, society and economy that took place in the country, starting at the beginning of the 1990s.

The first steps of the reforms in the economy were: liberalization of prices, commerce and enterprise operations, adoption of the first set of laws oriented towards a market economy (laws regarding ownership, privatization, Land Code, etc.), penetration into new markets. The first legal documents that formed the basis of the changes in the national economy were: the resolution of Parliament “Regarding the concept of transition to market economy” (1990) and the “Program of transition to market economy in Moldova” (1991).

However, the main events took place after 1993, when in collaboration with the IMF and World Bank the first real program of stabilization of the Moldovan economy was worked out. It was targeted towards two objectives. The first related to improving the environment and incentives for business: macroeconomic stability, price and trade liberalization, setting up a credible regulatory environment and progress in transfer of assets from the public to the private sector. The second was the establishment of a dynamic financial sector (banking system, budget system), capable of withstanding the pressures of the transition period.

Thus, the main emphasis was put, in the framework of the neo-liberal model, on macroeconomic, financial stabilization. The first successes — reduction of inflation, stable currency, mass privatisa-

Table 2.1.1.

#### Trend of HDI in the Republic of Moldova

Years	Indices Life expectancy	Indices Access to education	Indices Welfare	Indicele HDPI
1993	0,708	0,881	0,564	0,718
1994	0,685	0,877	0,566	0,709
1995	0,680	0,880	0,508	0,689
1996	0,695	0,882	0,510	0,696
1997	0,693	0,886	0,517	0,699
1998	0,700	0,887	0,503	0,697

Source: Human Development Reports of the Republic of Moldova, 1995-1998; DSAS.

In the 1990s the trend of the HDI of the Republic of Moldova has been negative, particularly as a result of the worsening of the Life Expectancy Index and of the Welfare Index. Decreasing GDP *per capita* has had a particularly strong negative impact on the overall trend of the HDI. However, taking into account the cumulative effect of poverty, which reached about 50% of the country’s population, one could expect that, in the future, the two other components of HDI will also have a negative influence on its value.

In the framework of the Human Development Reports, the UNDP considers low human development to correspond

tion — induced hope, and it was this hope that was at the basis of “The Economist” magazine’s remark that: “Moldova is a model of correct reform, and the fact that it is a small country, transforms it into a perfect laboratory for running reforms” (March 1995).

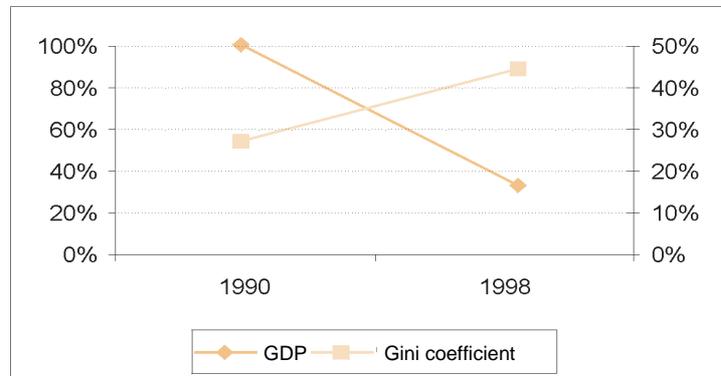
But the miracle did not happen. The promises to carry out quickly economic transformations and to create “people’s capitalism”, based upon tough actions in the financial sector, voucher privatization and the system of investment funds, proved to be illusory.

As is by now well known, a few reforms, no matter how well intentioned, cannot be expected to create a market economy where none existed before: a market economy is a far more complex set of inter-related institutions, both formal and informal, and it takes far longer to develop, than was earlier thought. In addition to this, the economy of Moldova was heavily dependent, at the beginning of the 1990s, on exports to the economies of the FSU, and was correspondingly vulnerable to unfavourable developments in those economies. Soon it became clear that establishing a well-functioning market economy is not just an important notion, but is crucial as a factor of increasing households’ standard of living and to ensure a basis for sustainable and democratic development, in compliance with principles of equity. In Moldova, as in other transition countries, economic stagnation followed the reforms, and as GDP fell by half, the skewed distribution of income (measured by the Gini coefficient) increased twofold.

In social and economic terms, the year 1998 was for the Republic of Moldova a year of disappointment. It became clear both to the Government and to the population that the “big leap” in implementing the reforms did not take place. Gradually during the years of transition there was an accumulation of structural disequilibria, internal and external debts, deepening of the budget crisis and reduction of export earnings. The social situation worsened sharply. After August 1998 the Russian financial crisis became

Fig. 2.1.1.

**GDP dynamics in Moldova vs. discrepancy of households’ income during the years of transition**



Source: CISR estimations

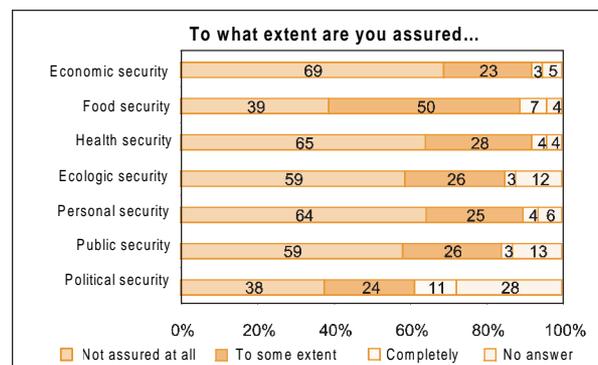
a catalyst for negative internal processes.

The official statistics registered, in 1998, falls of 8.6% in real GDP and 11% in both industrial and agricultural output. Thus, the first round of reform — from the crisis of 1991/92 to the crisis of 1998 — was completed but with depressing results. In accordance with the UNDP evaluations (1998) about 90% of the population of Moldova have incomes of less than US\$ 2 per day, while the ratio of the incomes of the 20% richest over those of the 20% poorest groups of population is 12.6 (against 7.0 in 1993).

CISR investigations show that the country’s population indicated the problem of „human insecurity” as one of the sharpest, particularly outlining such of its components as economic security, threats to health and personal security (box 2.1.1).

Box 2.1.1

**Opinion of the population regarding the human security**



Source: Opinion poll held by the Centre for Strategic Studies and Reforms (April 1999)

A retrospective analysis of seven years of transition attests to a *deep worsening of all parameters of the quality of life*. The social sector is not able to provide adequate protection against social risks. The situation registered at the end of 1998 confirms that activities in the social sphere are inconsistent and have a low efficiency. The reality of the transition has been quite different from what was envisaged during the 'romantic' stage of the reform period, which overestimated the speed and underestimated the costs of transition. The fall in GDP, accompanied by a tough monetary policy, has entailed significant social costs, which was rising during this period. Their adverse impact has been felt by the whole society, but it was (and will continue to be) especially painful for the elderly, the disabled, families with many dependent children and other vulnerable groups. In this sense the burden of the economic reform is borne by the people with low incomes, who in fact are in greater need of social protection. Consequently vulnerability and dependence are growing. This fact is confirmed also by the opinion poll made recently by INSOC-Market, which indicates that only 5% of the population has benefited from the reforms, while about 70% of the respondents said that their living standards have deteriorated.

The social implications of reform have a spillover effect onto all components of the quality of life, *deepening social polar-*

*ization*. Massive liberalization of economic activity at the early stages of reform, accompanied by widespread hidden unemployment and salary debts, has considerably decreased people's real income. According to some estimations the magnitude of this fall was of approximately 70 percent. As a result poverty has been growing significantly, which leads to a deeper social inequality. The Gini coefficient, which measures the dispersion of income distribution, increased from 0.34 in 1990 to 0.61 in the first half of 1998 (in comparison, Western countries have Gini coefficients of about 0.35; in Poland, Hungary and the Czech Republic they are about 0.43).

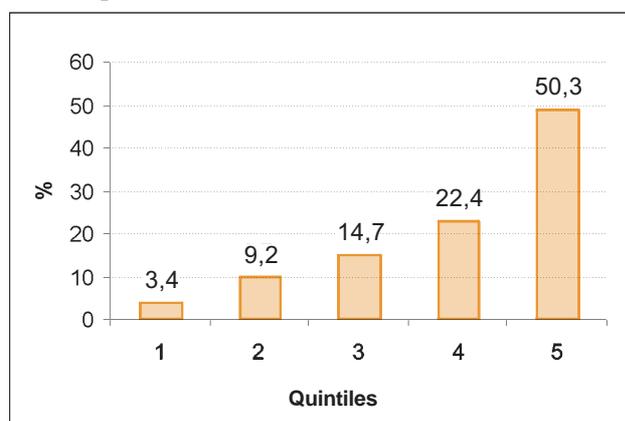
As a consequence of this process, *income inequality* is increasing in Moldova. According to household budget survey data, by the end of 1998 the total income received by the richest 20 percent of the population was 12.6 times the income received by the poorest 20 percent, which compares with a figure of 12.25 three years ago. Today the richest one-fifth of the population receives roughly half of the total disposable income, while the poorest one-fifth has only 3.4%. People with middle income, who form the main share (3/5) of the population, receive about 48% of the total disposable income. This is a clear indication that the middle class in Moldova is still too fragile to offset the social costs of reform.

The reduction in purchasing power led to a substantial shrinkage of individual consumption. From a society with a scarcity of consumption goods on the market Moldova has become a society with low individual consumption. All components of consumption decreased (foodstuffs, durable goods, and services). However, the most significant fall was registered in basic foodstuffs, namely meat, with minus 57%, milk, with minus 49%, and fish with minus 84%. Consumption is now close to critical limits, threatening people's normal development as human beings.

*Malnutrition* today affects not only people with low incomes, but partially also

#### Box 2.1.2.

#### Income Disparities in Moldova , 1998



Source: CISR calculations based on HBS data

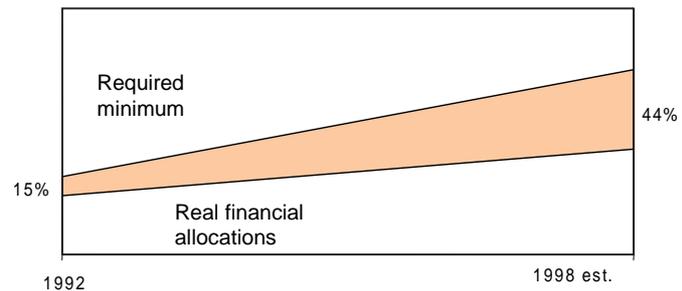
those with middle incomes who are employed in the budget sphere (teachers, public servants, medical workers), due to frequent delays in paying wages. The implicit effect of malnutrition has been felt in demographic aspects and the state of the population's health. By comparison with 1990, the general death rate has increased by 15% while the birth rate has dropped by 38%. In 1998 for the first time in Moldova the death rate has exceeded the birth rate. Consequently the rate of natural increase of the population has become negative (-0.2 per thousand). This could have a long-term impact on depopulation in Moldova. Complementarily, morbidity, which remains high due to widespread chronic diseases, such as black lung, digestion pathologies, tumours, and cardio-vascular diseases, could exert a great impact on further human development in Moldova. As a result the demographic dependency ratio is rising which could become a serious hindrance for economic reforms. Now at 0.77 (or 77 children and elder people to 100 persons able to work), this indicator has far exceeded the critical limit of 0.31.

In the conditions of massive pauperization of the population there is a tendency to maintain implicit subsidies of social services through indemnities and compensations. In 1998 the cost of these social privileges was at about 800 million lei, i.e. around 8% of GDP. The lack of a mechanism to nominally grant of social benefits has led to the fact that about one third of them have been directed towards the average and high-income strata of the population. This is a good reason to argue that income transfers should be better targeted and provided on the basis of means testing. Thus the poor still remain the most vulnerable point in the social assistance system.

Universal coverage and unclear eligibility criteria have been generating an explosive increase of social cost, which constituted a heavy burden for the economy. During the 1990s the share of social expenditures increased by 35%, until it represented, in 1998, 1/5 of the GDP.

#### Box 2.1.3.

#### Discrepancies in social finance



Source: CISR calculation based on MoF data

Economic recession accompanied by the fiscal crisis has been eroding resource inflows into the social sector, significantly undermining the sustainability of social finance. Misallocation of resources in concert with low rates of collection has widened the discrepancy between social commitments and financial possibilities. From 15% in 1990, the gap between real allocation of financial resources and the minimal required level reached 44% in 1998. Delays in paying wages, pensions, indemnities and other social benefits became chronic. This is a sign that the viability of social finance is on the edge of a crisis.

*Main lessons.* The year 1998 has once more proved the rule that when reforms are procrastinated social costs increase and people's belief in the reform process weakens. In the social sphere the *pace of reforms was too slow* and attempts to make some changes were done in a shallow and controversial manner. An exception is the legal framework, where several important laws have been approved. We can mention here the Law on Mandatory Health Care Insurance (27 Feb.); Law on State Pension Insurance (14 Oct.) and Law on Minimum Medical Services provided by State (1999 Feb. 3). Other draft laws have passed the 1st and 2nd readings in the Parliament, waiting for the final stage (Law on Non-State Pension Funds, and Law on Social Insurance). Attempts to pay off pension/salary arrears have failed due to a lack of consistency in promoting social reform.

*Government institutions have been concerned mainly with current issues, acting as a fire-fighting brigade. Time, money, and efforts have been spent on taking ad-hoc measures, which had insignificant and temporary results.*

*The institutional network for implementation of the new laws is not yet settled. In reality a huge gap can be seen between the new legal framework and outdated social security institutions. Consequently, pension, health care and other sector reforms are taking place slowly.*

Public social arrangements are too costly and badly targeted. Maintaining the *implicit nature of social expenditures*, as well as the *broad range of social privileges*, could undermine the fate of social reform. Desperate actions undertaken to fit expenditures with the revenues did not have a positive effect. Three times during 1998 the social fund budget was revised with a view to reducing either of its sides, but the result was insignificant. By the end of

the year, pension arrangements were paid at 60% of their initial rate.

Family allowances and compensations for public utilities are too diffuse and provided in a manner close to universal coverage. The *subsidy of electricity and thermal energy tariffs* is the most vulnerable point in the social safety schemes. Such subsidies captured nearly 20% of the public budget revenues, and are convenient only for the companies which produce/deliver energy resources. Phasing out the subsidies could, however, face strong institutional constraints, making this a politically sensitive issue.

*The administrative capacity of social institutions is too weak*, and this could be a serious impediment to the implementation of reform proposals. Besides, a lack of publicity about the aims and scope of social reform has strengthened opponents' positions and intensified rumours, which have had a negative impact on the success of the reform.

#### Box 2.1.2.

##### Initial Stage of Reforms: Imitation or Mistakes?

Eight years of intentions, efforts and actions directing the economy towards market relations have not yet brought perceivable results in the sense of ensuring economic and social stability. Reforms that were started and partially implemented can not yet put in motion the mechanisms and driving force of the new forms of economic organization and development, based upon principles of the market economy. Privatization, which is considered an axis of economic reforms, has not brought the expected result, especially in the real sector of the economy and in the sphere of material goods production. Patrimonial vouchers have not become, as expected, circulating securities.

The stability of the national currency, a considerable reduction in inflation, the establishment of a securities market did not bring an inflow of foreign investments in a volume that could have consolidated the situation in the real economy. The FDI per capita is one of the lowest in Europe. Moreover, efforts of macroeconomic stabilization have in fact generated a continuous decline of production in the real sector of the economy, a widening budget deficit and a considerable worsening of social indicators.

Macroeconomic conditions in Moldova are characterized by a critical contraction (by about 60%) of the GDP from the moment of declaration of independence. As a result of the negative evolution of events, poverty has become the problem number one, and the level of per capita income situates Moldova among the poorest countries in Europe.

Social stratification caused by the different level of households' income looks inevitable in a society that encourages private initiative and the spirit of entrepreneurship. But the access to power of those groups that by illegal means have acquired the initial capital obviously puts in danger the chances of economic prosperity for the majority of our citizens. The social market economy remains a good wish, without being backed by the state's real income. Poverty already accounts for 80% of the country's population, and the standard of living has fallen down to the line of basic vital needs.

At present we still have the choice: to continue further to fall slowly but firmly, or to undergo thorough, deep, complex and radical changes, which could bring the long awaited liberty and prosperity.

The possibility for change is still real.

*Source: Acceleration and deepening of the reforms - a unique path towards overcoming the crisis. Government declaration. Newspaper "Nezavisimaya Moldova", July 1999.*

## 2.2. Human Security in Moldova: Macroeconomic and Social Parameters

Each state should have as a priority guaranteeing human security. State authority is based on the extent to which it is able to provide the population of the country with decent living conditions and personal development, socio-economic and political stability, and to oppose both internal and external threats.

Ordinary people, the population of the country, perceive the notions of “human security” and “economic security of the state” somewhat abstractly and out of context. However, such negative occurrences as poverty and unemployment, low quality of education and health care, and criminality spoil people’s everyday life. This is why guaranteeing human security is a key national priority and is the state’s exclusive responsibility.

During the transition period the problem of human security in the concrete conditions of the Republic of Moldova appears both at the macro level (country), and at the micro level (household, family). The crisis put on first place the need to have a stable national economy, which would guarantee decent living conditions for the population, protect private property, promote entrepreneurship and suppress the factors of economic destabilization (such as criminalization of the economy, socially dangerous income distribution inequalities, etc.). The state needs to exercise rigorous control over the external debt and national resources, and to improve national competitiveness at the regional and global level.

Particularly important is the capacity of the society to develop itself on the basis of its scientific, technical and spiritual potential, and the capacity to attract investment, technology and new ideas.

If we assess the current situation of the Republic of Moldova from this point of view, we may conclude that, although the changes leading to a market economy have become irreversible, the society

has not yet overcome the stage of deep social and political crisis so as to be able to develop itself with confidence and security. The middle strata of the population — the one that ensures the social stability of a country — has not been formed yet, while legislative, executive and judiciary bodies have not delimited their responsibilities yet and are not performing their duties coherently, so that their image as guarantors of democratic transformations may be perceived correctly by the entire society.

During the transition the main threats to human security arising from within the economy of Moldova stem from the following processes:

- the state’s reduced financial capacity to choose a strategy of socio-economic development and to implement it effectively. The precarious situation of the financial sector is due not so much to the crisis of the large state enterprises in industry and the agrarian sector as to slow development of the private sector;
- the development of increasing economic instability (dynamics of household incomes, volume of GDP, exports, etc.), related to a fall in the share of the industrial sector and the consequent increase of the share of the agricultural sector, which depends to a great extent on climatic conditions and has limited possibilities to use advanced technologies (fertilizers, chemicals, irrigation techniques, etc.). The variability of climate, especially in the spring and autumn, has a negative impact on agriculture. Different climatic conditions, such as drought, frost, hail, etc. are causing significant losses to the economy as a whole. In the last two years (1997-1998) these losses were estimated at 2.5-3% of GDP;
- the low level of investment both in the social sphere and in creating new jobs. The state is not receiving the considerable resources necessary to resolve social problems.

*“You are what you are, what you want, what you do.”*

Nicolae Iorga

Although the share of social sphere expenditures in the state budget is about 50% (see box 2.2.1), these funds are obviously insufficient. Thus, the need for a reform of the social sphere is very pressing.

Particular attention must be paid to institutional threats, primarily the weakness of the state in exercising its functions of providing social support to the population and of regulating the activities of economic units through legal protection and administrative regulation.

Guaranteeing human security is a strategic problem, because it is based on supreme national long-term interests. It is not just a problem for the organs of the state administration. It is crucial that this be understood by political parties, public organizations, and by all strata of the population. Understanding the consonance of personal, group and national interests and formulating common actions with a view to avoiding internal and external threats are extremely complex social and psychological processes, which develop as a consequence of historical tradition, political maturity and the con-

fidence of the people in the institutions of government.

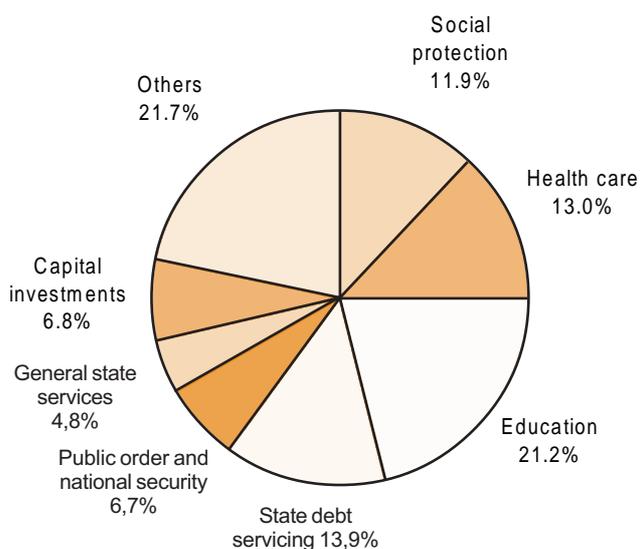
The following two to three years will probably be critical for the Republic of Moldova. There are two possible scenarios: either the crisis in the society and in the economy becomes irreversible and Moldova becomes a third-rate country, peripheral and stagnant, or it succeeds in overcoming the current situation and manages, after the year 2000, to find its own place in the economic and spiritual space of Europe.

Regarding human security requirements in the Republic of Moldova, it is possible to deduce certain criteria that indicate the critical levels of the most important indices of social and economic security. Their assessment takes into account the need for:

- a decent standard of living for the population, and the possibility to improve it;
- an increase in economic productivity; the sustainability of the financial system, which determines the level of the state budget deficit, through the sustainability of the banking system, level of internal and external debt, deficit in the balance of payments, conditions for stimulating investment and a rationalization of the structure of foreign trade;
- the strengthening of the scientific and cultural potential of the country;
- the creation of legal, economic and administrative conditions that would reduce corruption and the size of shadow economy, placing the society out of danger;
- the preservation of the economic-territorial integrity of the country, excluding regional separatism and developing local self-administration so as to use the territorial resources more efficiently while respecting the general interests of the state.

Box 2.2.1

**Structure of State Budget Expenditures in the Republic of Moldova, 1998**



Source: Ministry of Finance

The Centre for Strategic Studies and Reforms (CISR) assessed the state of human security in the Republic of Moldova from two perspectives: macroeconomic indicators (economic security of the state), and social parameters. Tables 2.2.1 and 2.2.2 present, for these indicators, both their current values and their critical levels.

An attempt has also been made to synthesize a group of key indicators and calculate an aggregate indicator (Prof. C. Zaman, CASE Expert, Romania/Poland). The **aggregate indicator** takes into account ten reference indices from the following domains: demographic — death and birth rates, life expectancy, etc.; social — unemployment, the GDP share of social expenditure (on health care, education, etc.); social welfare of the population — the share of food costs in a household budget, the number of calories consumed by an individual, etc; foreign economic relations — foreign debt, the degree of country dependency, the structure of imports and exports; fiscal domain — the domestic debt, tax evasion, the relative weight of the shadow economy; institu-

Table 2.2.1

### Republic of Moldova: Macroeconomic Indicators for Economic Security, 1998

#### Initial data for calculation of indicators

Foreign debt	USD 1.3 bn
GDP	MDL 9 bn
Foreign debt service	USD 60 m
Public debt service	USD 100 m
Total expenditures of state budget	MDL 2 bn
Exports	USD 0.7 bn
Imports	USD 1.1 bn

Indicators	Current Value	Critical level
1. Foreign debt/GDP	About 80%	65%
2. Foreign debt service/Exports	8.6%	5%
3. Public debt service/Total expenditures of state budget	25%	5-7%
4. Three groups of imported goods / Total imports (mineral products, including energy resources, equipment, chemical products).	57.8%	30-35%
5. Three groups of exported goods / Total exports (food products, drinks, cigarettes)	54.8%	20-25%
6. Exports to one country / total exports	58.2%	25-30%
7. Imports from one country / total imports	28.5%	15-20%
8. Exports/Imports	64%	95-100%
9. Degree of customs control in the country	About 70%	100%
10. Share of shadow economy	50-60%	15-20%

Source: DSAS, CISR estimations

Table 2.2.2

### Republic of Moldova: Social Indicators of Human Security

	1990	1998	Acceptable		1990	1998	Acceptable
Life expectancy, years	68.5	67.0		Value of nutrition, kcal/day	2969	1980.3	2100
For women	71.8	70.7		Social polarization	N/A	12.6	5-8
For men	65	63.2		of population, times			
Birth rate, per thousand	17.7	10.9		Gini coefficient	0.27	0.44	0.29-0.31
Total death rate, per thousand	9.7	11.9	7-8	Coefficient of demographic depend.	82	77	22
Natural increase, per thousand	8.0	-0.2		Coefficient of social dependency	0.44	0.71	0.2-0.25
Infant mortality, per thousand	19.0	17.8	10	Share of social expenditures, % of GDP	18.4	17	15
Fertility coefficient, number of births	2.39	1.667	2.1	Expenditure with health care, % of GDP	3.8*	5.9	8-9
Net reproduction ratio, %	112.6	78.1	100	Annual average health care expenditures per person, lei	N/A	114	210
Official rate of unemployment, %	N/A	2.0	4-6	Expenditure with education, % of GDP	7.8*	10	5-6
Hidden unemployment, %	N/A	9.4	4-6	Annual average expenditure per student, lei	N/A	1807	2460
Rate of employment of labour force, %	82.6	52	65-70	Expenditure with pensions, % of GDP	4.5*	7.4	10-1
Share of foodstuff expenditures, %	34.5	67.9	25-30	Rate of salary replacement by pension, %	40.4	33.5	33-35

\*1992 N/A - data not available.

Source: DSAS, CISR estimations

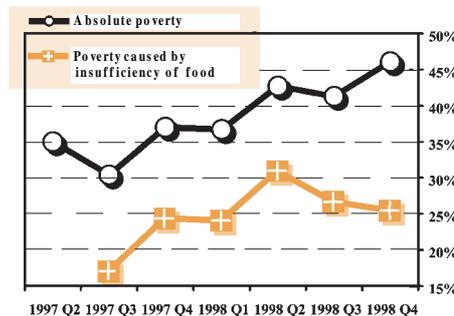
tional field — the degree of bureaucratization of the public administration, the intensity of corruption.

Based on the actual level of each indicator and comparing that with a unit level of reference that would express a normative value of the respective indicator from the point of view of social and economic security, we obtained the following aggregate indicator for the Republic of Moldova (see table 2.2.3).

As has been stated, the human security of the country is ultimately reflected in the indicators of social well-being of the nation. All these indicators (living standards, income inequality, degree to which cultural requirements are met, respect for personal rights and liberties, crime rate, the dynamics of fertility, mortality and population growth, life expectancy) have reached and exceeded maximum acceptable limits. The problem of

Box 2.2.2

**Poverty in Moldova**  
(% of population)



**Note:** Absolute poverty line: 82.1 lei in May 1997 prices. Line of poverty caused by insufficiency of food: 65.2 lei (at 2100 cal.) prices of May 1997

Source: calculus from Households Budget Survey

poverty has now acquired a particular sharpness (see box 2.2.2).

The aggregate indicator calculated above shows that in the Republic of Moldova an individual has a human (social and economic) security which is far less than he/she should have in conditions of a normal functioning of the economic, social and political systems. It may also be pointed out that the main responsibility for that situation lies with the state, since most of the indices used in the determination of the value of this aggregate indicator belong to the sphere of national economic policy.

The reality is such that it is imperative for the state to implement a number of measures of social policy aimed at decreasing and avoiding internal and external threats to the social security of Moldova. Actions in this field that need to be implemented immediately include monitoring and forecasting the basic factors that threaten economic security, and determining the thresholds for the indicators of the social situation which, if exceeded, will require the implementation of extraordinary measures of a legal, economic and organizational nature.

Table 2.2.3

**Calculation of the Aggregate Indicator of Human Security in Moldova**

Indicator	Actual	Reference
1. Demographic index	0.15	1
2. Unemployment	0.42	1
3. Social welfare of the population	0.2	1
4. Social expenditures	0.6	1
5. Foreign debt	0.21	1
6. Internal debt	0.25	1
7. Foreign trade	0.35	1
8. Tax evasion and shadow economy	0.56	1
9. Degree of bureaucratisation of state administration	0.5	1
10. Intensity of corruption	0.1	1
<b>Aggregate index of human security (social and economic)</b>	<b>3.34</b>	<b>10</b>

Methodological note:

- The calculation of the actual values of the indices of Moldova used either a linear or a logarithmic scale.
- The reference unit value of each index does not correspond to an ideal situation, but to a level considered desirable, taking into account both the real possibilities of Moldova and a reference situation which would express the normal functioning of a society.
- The aggregate level of the index corresponds to the sum of the values of the ten indices used.