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THE SUSTAINABILITY OF PUBLIC FINANCES IN REPUBLIC OF MOLDOVA UNDER EU FISCAL RULES

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Abstract

This paper analyses public finances sustainability in the Republic of Moldova under the European Union fiscal rules, by estimating the structural budget balance indicator using a three steps methodology. We concluded that, except for 2009, the Republic of Moldova complies with the Maastricht numerical fiscal rule; however it does not comply with the new fiscal rules regarding the structural deficit and public expenditures growth that had been set by the Fiscal Compact. The fact that budget deficits and public debt had been sustainable was mainly because of the concessions made by the external creditors in restructuring the public debt and was not a merit of national government. Moreover, since the regular budget deficit and the structural one tell different stories, we strongly advocate for using the latter in order to complement the existing data with a medium-term budgetary view.

Keywords: public finance, sustainability, public debt, budget deficit, output gap, structural deficit

JEL classification: H62, H63, E10

1. INTRODUCTION

The lack of fiscal discipline is a phenomenon that currently characterizes many countries of the world. The budget surpluses have come to represent rather a singular phenomenon, while budget deficits seem to be something common. Recently, the sovereign debt crisis in the European Union (EU) member states suggests that things should not be developed in such a way. The lesson learnt from the crisis is that countries need to enforce the long-term sustainability of public finances as recent reforms undertaken in EU member states show. This represents a major shift from the myopic short-term national fiscal policies to sustainable long-term goals.

The paper addresses the public finances sustainability in the Republic of Moldova, an issue which has not been properly discussed in the related literature so far. The main objective of the paper is to assess the public finances sustainability in the Republic of

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Moldova under EU fiscal rules. The main contribution of the paper consists in investigating the public finance sustainability of Republic of Moldova, by going beyond the Maastricht fiscal criteria and looking upon Fiscal Compact criteria. In doing so, we computed the structural budget balance of the general government, by applying a methodology derived from that of the European Commission. Our research has been conducted in three stages. The first stage consists in estimating the potential Gross Domestic Product (GDP) using the Cobb-Douglas constant scale function. In the second stage, we have estimated revenues and expenditures sensitivity to the economic cycle based on the corresponding elasticities. Subsequently, it the third stage, we have determined the cyclically adjusted balance. Based on these results we diagnosed the sustainability of public finances in the Republic of Moldova and identified the main factors that had an impact on it. Moreover, we checked if the overall budget balance indicator and the structural one tell the same story with regard to the soundness of public finance. Policy recommendations were made accordingly.

2. LITERATURE REVIEW

The literature on the public finance sustainability is extremely vast, but we have focused only on a specific aspect of the subject, namely the EU fiscal rules, as a prerequisite for the Republic of Moldova's aspiration to European integration. We have not focused on the theoretical aspects regarding the concept of fiscal rules, since there are plenty of papers that deal with these issues, such as for instance Schaechter *et al.* (2012), Wyplosz (2012), but we rather target the application of the fiscal rules in the EU countries.

Recent debt crisis has shown that there are certain problems with the sustainability of public finance in the EU member states. According to Dabrowski (2012, p. 14) the sovereign debt crisis in the EU member states has certain tax origins and hence the European Union's fiscal discipline is extremely important. Fiscal rules are important for the sound management of public finance not only because they ensure the stability of public finances but, as Sacchi and Salotti (2015) shown, they have a positive impact on macroeconomic stabilization.

Numerous empirical studies, such as those of Afonso and Rault (2015), Neaime (2015), Fatas and Mihov (2009) concluded that the period prior to the global economic and financial crisis was characterized by fiscal indiscipline in most of the European countries. Wyplosz (2013) argued that in order to avoid such scenarios in the future, EU has to implement a decentralized model of fiscal federalism, through the adoption of national fiscal rules that would ensure the compliance with the medium-term objective (MTO) concerning the structural budget balance that has been set by the Fiscal Compact.

Research on the public finances sustainability and the subsequent application of the Fiscal Compact provisions in EU member states were undertaken by Mourre *et al.* (2013), Puiu (2013), European Commission (2012), European Central Bank (2012), Barnes *et al.* (2012), Lane (2012) and others. In Romania similar studies have been performed by Dăianu *et al.* (2011), Altar *et al* (2009, 2011), Socol and Măntescu (2011), Oprea *et al.* (2013) etc. Only very few studies deal with the public finances sustainability in the Republic of Moldova, the most relevant being Enicov *et al.* (2009), which includes a comparative study of the budget deficit and public debt indicators in the Republic of Moldova and in the EU Member States. Thus, the paper enhances the results of the previous researches on the public finance sustainability in the Republic of Moldova, by performing a more in-depth analysis that includes the assessment of the structural budget balance, an indicator that has never been estimated before for the Republic of Moldova.

3. THEORETICAL BACKGROUND

The most important fiscal rules applied in EU Member States are the well-known Maastricht fiscal criteria, i.e. the debt rule that restricts the public debt to GDP ratio to 60% and budget deficit to GDP ratio to 3%. Although these budgetary rules were established more than two decades ago, compliance proved to be challenging for many European countries. However, studies show that the rules were too lax and that the fiscal policy's responses to economic fluctuations proved to be procyclical rather than being countercyclical (with budget surplus in periods of expansion and budget deficits during recessions), and this inevitably had led to excessive deficits in the period of the global economic crises (Wyplosz, 2013, p. 31). It is well-known that an expansionary fiscal policy stimulates aggregate demand, and hence, leads to growth, but its excessive use in times of economic expansion may lead to the shrinking of the fiscal space so much needed for stimulating the economy when recession hits.

In order to avoid such a scenario, the budget balance rule was supplemented by a new criterion, namely the MTO that was included in the national Medium Term Budgetary Frameworks (MTBF) as a target to be achieved and which refers to the structural budget balance as share of GDP. As stated by Socol and Măntescu (2011, p. 118) „the budget balance is an indicator of a very limited utility in the assessment of fiscal and budgetary policies. This is due to the fact that these policies cannot be analysed based on short-term (one year) indicators. Besides that, an indicator like the budget balance cannot capture „the fiscal burden of the future generations".

Cyclically adjusted or structural budget balance is used to evaluate the fiscal policy of EU member states, being extremely important when it comes to evaluate the safety margin for fiscal policies during recessions, when deficits go dangerously close or beyond the 3% of GDP threshold. The structural budget balance became the focus of the fiscal surveillance mechanism both of the European Commission and of the European Council. The structural budget balance is a proper metric for estimating the extent of discretionary fiscal policy and represents the net fiscal balance that is obtained if the effects of the economic cycle on budget revenues and expenditures are controlled for. A positive structural balance shows a restrictive fiscal policy, a negative structural balance signals an expansionary fiscal policy.

According to the Fiscal Compact, part of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, that came into force in 2013, a structural deficit may be up to 0.5% of GDP for states with a debt to GDP ratio exceeding 60%, or at most 1.0% of GDP for states with debt levels within the 60% limit. MTO is therefore computed for each state based on the potential growth of the country's public debt and on the cost of population aging.

In order to assess whether a state does engage in certain policy measures without having the corresponding financial coverage, the compliance with the rule of the public expenditure growth has to be watched closely. The stability, as well as the convergence programs should contain information about discretionary revenue measures if the expenditure growth rate exceeds the GDP's growth rate. In this case, total expenditures exclude expenditures related to the interest on public debt, expenditures covered from EU programs and funds and non-discretionary spending on unemployment benefits. Accordingly, an expenditure increase is not considered to be a violation of the rule if is entirely covered by revenue increases mandated by the tax law.

4. DATA AND METHODOLOGY

The public finances sustainability is investigated by looking upon several ratios, such as public debt to GDP, budget deficit to GDP, structural deficit to GDP as well as public expenditure elasticity with respect to GDP. The statistical data for computing these ratios were collected from the National Bureau of Statistics and the Ministry of Finance of Republic of Moldova.

With regard to the structural budget balance, its computation implies the assessment of the cyclical budget balance, given by the impact of the GDP deviation from its potential level. A significant variation of the estimates was detected in several empirical studies of the European Commission, International Monetary Fund and the European Institute of Romania (Altăr *et al.*, 2011, p. 52; Puiu, 2013, p. 179), which indicates that the estimates are not consistent and that they depend on the methodology used.

According to the Fiscal Council of Romania (2012, pp. 51-59), the European Commission estimates the structural deficit based on a standard procedure, which is carried out in three steps: the first step consists in estimating the output gap, as a difference between the real and potential GDP, in the second step the sensitivity of budget revenues and expenditures with respect to GDP are computed, and in the third step the cyclical revenues and expenditures are deduced in order to assess the structural component. We followed closely the European Commission's methodology, the only difference being the application of the Hodrick-Prescott filter approach in estimating the total factor productivity (TFP) and non-accelerating, (wage) inflation (NAWRU) instead of using the Kalman filter (the same approach has been used before in the study of Toaca and Tolocico (2012, p. 26). We did that in order to simplify the calculation since empirical findings do not change much.

Step 1. Estimating the potential GDP and the output gap. Potential GDP indicates the level of real GDP that would have been achieved in terms of maximum utilization of production factors (labour and capital) without creating inflationary pressure, i.e. the labour market and the stock market are in equilibrium (Toaca and Tolocico, 2012, p. 23). Computation of potential GDP is a problem that does not have a straightforward solution. However, the methods of estimating the potential GDP are grouped into two categories, the first one includes the estimation methods based on time series, the most accurate of them being the Hodrick-Prescott filter methodology, while the second category includes structural methods, the most popular being the Cobb-Douglas production function methodology (Toaca and Tolocico, 2012).

Although there are no data on the estimation of structural budget balance in the Republic of Moldova, still there are several papers that deal with the estimations of potential GDP. The latest results belong to Toaca and Tolocico (2012) and Rotaru (2011). In these estimates, the potential GDP was derived from the empirical estimation of Cobb-Douglas production function of the Moldovan economy. In the case of the methodology used by the European Commission, the potential GDP is determined using the formula based on the Cobb-Douglas constant scale function (Havik *et al.*, 2014):

$$YP = LP^{\alpha} K^{(1-\alpha)} * TFP \quad (1)$$

1. α – the flexibility to the labour factor. It is computed as the share of the labour factor in the national income. For all EU countries $\alpha = 0.65$. In the case of the Republic of Moldova for the 2000-2014 period the contribution of the employees remuneration to GDP represents approximately 41.53%, thus we consider $\alpha = 0.4153$

2. LP – the potential of the labour factor. The labour factor represents the total labour employment multiplied by average worked hours. According to the Commission's methodology, the potential labour factor is computed according to the following formula:

$$LP = N \cdot q \cdot (1 - u) \cdot H \quad (2)$$

N – the population of working age;
q – the trend of the participation rate of working age population (the share of the active population in the population of working age), that is obtained through the application of the Hodrick-Prescott filter (λ=6.25 for annual data);
H – the trend of the data series on average worked hours, that is obtained in a similar way through the application of the Hodrick-Prescott filter;
u – represents NAWRU, the structural unemployment rate. We used the Labour Force Survey's[1] unemployment rate, adjusted by the Hodrick-Prescott filter.

3. K- capital factor. It is considered that the real level of this factor is equal to the potential one. We have determined the capital factor with the following formula (Toaca and Tolocico, 2012, p. 26):

$$K_t = (1-\beta)\, K_{t-1} + FCF \quad (3)$$

β – annual rate of capital depreciation, which is considered to be 0.05;
FCF –fixed capital formation. To control for the influence of the inflation, it was adjusted by the deflator of fixed capital formation;

4. TFP – total factor productivity (Solow residual) that was obtained in two phases. First of all the total factor productivity was calculated as a residual component based on the recorded GDP (adjusted by the GDP deflator), the capital stock and the labour force. Subsequently, the results were adjusted using the Hodrick-Prescott filter.

$$\text{Output gap} = (Y - YP)/YP * 100 \quad (4)$$

Y – real GDP;
YP – potential GDP.

The data used for estimating the potential GDP are presented in the Appendix, the results of the output gaps estimates are presented in Table no. 1 and the graphical illustration of the results is shown in Figure no. 1.

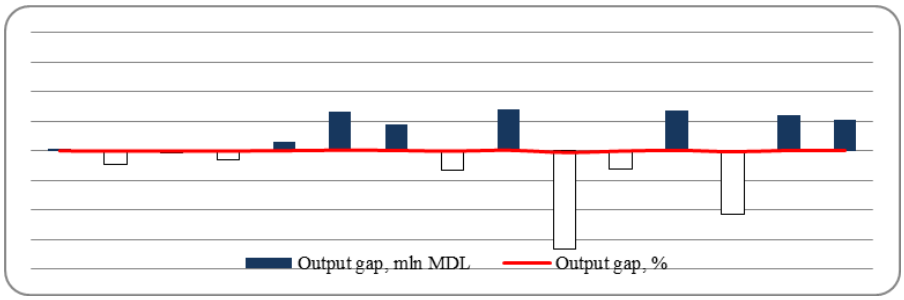
The data shows that during 2000-2008 the economy of the Republic of Moldova's grew steadily. The average growth rate of GDP, expressed in 1994 prices, was approximately 7% per year. Moreover, during 2000-2003 the real GDP was very close to the potential GDP, while during 2004-2008 period the economy grew even above its potential. The situation has worsened with the onset of the global financial crisis, which adversely affected Moldovan economy. In 2009, the real GDP contracted by 6% comparing to the previous year and by 5.3% comparing to its potential level. This was the year when the highest output gap was recorded. Although the return to a growth trend is achieved in 2010 and 2011, when GDP increased over the previous year on average by 7%, the year 2012 shows a decline in the economic growth, caused mainly by poor agriculture output triggered by adverse weather conditions[2]. However, the years 2013 and 2014 show not only a significant increase of the real GDP, but also a positive output gap, this time due to favourable weather conditions[3].

Table no. 1 – Real and potential GDP in Republic of Moldova

Years	Real GDP, mil.MDL*	Real GDP, deviation from previous year, %	Potential GDP, mil. MDL*	Output gap, mil.MDL*	Output gap,%
2000	4119.1	-	4111.7	7.4	0.2
2001	4373.8	6.2	4421.6	-47.8	-1.1
2002	4716.2	7.8	4723.2	-7.1	-0.1
2003	5030.3	6.7	5059.3	-29.0	-0.6
2004	5401.9	7.4	5373.0	28.9	0.5
2005	5809.4	7.5	5678.1	131.3	2.3
2006	6089.3	4.8	5999.1	90.2	1.5
2007	6272.3	3.0	6340.1	-67.7	-1.1
2008	6764.3	7.8	6625.3	139.0	2.1
2009	6356.6	-6.0	6691.3	-334.7	-5.3
2010	6806.2	7.1	6867.8	-61.6	-0.9
2011	7273.1	6.9	7137.5	135.7	1.9
2012	7221.9	-0.7	7438.2	-216.4	-3.0
2013	7903.2	9.4	7784.5	118.7	1.5
2014	8280.6	4.8	8175.9	104.7	1.3

* The indicators are expressed in 1994 prices, adjusted by the GDP deflator

Source: Based on authors' calculations



Source: Based on authors' calculations

Figure no.1 – Estimating potential output gap using the Cobb-Douglas production function

Step 2. Estimation of the revenues and expenditures sensitivity to the economic cycle. In order to assess the cyclical component of the budget balance we need to estimate the sensitivity of the budget revenues and expenditures to the GDP change, since a great part of revenues and expenditures are affected by GDP variations. In case of a recession, the tax revenues will be affected mainly because of the reduction of the tax base for personal and corporate income tax, social security contributions, health insurance premiums and indirect taxes, as national income and consumption contracted. At the same time, a recession normally triggers a rise on the expenditure side of the budget, because of the payments for unemployment benefits and welfare transfers (built-in or automatic stabilizers).

The first step in estimating the sensitivity is to compute the elasticity for budget components triggered by the economic cycle. Elasticity quantifies the percentage change in the categories of budget revenues and expenditures related to the percentage change in GDP. We have determined the average elasticity for the entire period, for each category of above mentioned revenues and expenditure. We have obtained the total revenue elasticity (1. 2731) by computing the sum of the products between the individual elasticity of each category of revenues and their weight in total revenues. The elasticity of expenditure (-0.0009) is given by the

product between the elasticity of the unemployment benefits expenditures and the weight of this category of expenditure in the total current primary expenditure (excluding capital expenditures and interest payments on public debt). The results show that in the Republic of Moldova, the automatic stabilizers operate more **on the revenue side of the budget**. Regarding automatic stabilizers on the expenditure side, their influence is insignificant, since the size of the unemployment benefits represent a very small percentage of the primary expenditures. The highest level of this indicator of 0.005% was in 2000, and has decreased even since to 0.001% in 2013. This suggests that this type of expenditure had no significant negative impact on the budget.

Sensitivity coefficients were obtained by multiplying the elasticity with the weight of public revenues and current primary expenditures variable in GDP for each year (Table no. 2).

Table no. 2 – Sensitivity coefficients and the budget balance indicators in the 2000-2014 periods*

Year	Sensitivity coefficients	Cyclical budget balance*, mln. MDL	Overall budget balance*, mln. MDL	Share of public revenues in GDP, %	Share of current primary expenditures in GDP, %
2000	0.431472417	3.19	-103.34	0,3386	0,3637
2001	0.409151054	-19.54	25.51	0,3211	0,3153
2002	0.414594958	-2.93	-80.69	0,3254	0,3425
2003	0.434395580	-12.61	49.12	0,3410	0,3312
2004	0.450391335	13.02	11.92	0,3535	0,3513
2005	0.491567661	64.56	89.24	0,3858	0,3705
2006	0.508089244	45.83	-17.16	0,3988	0,4016
2007	0.531566493	-36.00	-14.51	0,4172	0,4195
2008	0.516683761	71.84	-67.73	0,4055	0,4155
2009	0.495887925	-165.98	-403.57	0,3892	0,4527
2010	0.488129297	-30.08	-169.12	0,3831	0,4080
2011	0.466327636	63.27	-173.22	0,3660	0,3898
2012	0.484213415	-104.77	-150.87	0,3800	0,4009
2013	0.467750931	55.52	-137.75	0,3671	0,3846
2014	0.483919543	50.68	-140.15	0,3798	0,3972

* The indicators are expressed in 1994 prices, adjusted by the GDP deflator

Source: Prepared by the authors basing on the data of the Ministry of Finance, the National Bureau of Statistics and authors' own calculations

The results show that in the Republic of Moldova the sensitivity coefficients of the budget balance vary from 0.4092 in 2001 to 0.5316 in 2007. This is caused mainly by the variation of the share of public revenues in GDP. The highest value of sensitivity coefficient was in 2007, when the share of public revenues in GDP was at its peak, while the lowest value was in 2001, when the share of public revenues in GDP displayed its minimum value as well.

Step 3. Determination of the cyclically adjusted balance. Based on the sensitivity parameters, the cyclical balance is estimated as the product of the sensitivity parameter and the output gap. Subsequently, the structural balance is computed as the difference between the total budget balance and the cyclical balance (last column of Table no. 2).

4. RESULTS

The main public finance sustainability related indicators are presented in Table no. 3. In order to provide a better picture, we supplement the data with the evolution of public

sector size, measured as the share of public expenditure in GDP, the size of the interest paid on general government debt as a share of total expenditure and net lending to cover the budget deficit. Given the availability of statistical data the investigation was performed for the 2000-2014 time period. This time span is split into two periods, i.e. before and after the global economic crisis (before 2009 and from 2009 onwards).

Table no. 3 – Fiscal sustainability indicators in the 2000-2014 periods*

Year	Elasticity of public expenditures to GDP	Share of public expenditures, % in GDP	Budget balance, % in GDP	Structural budget balance, % in GDP	General government debt, % in GDP	Interest on government debt, % in total expenditures	Net lending, % in GDP
2000	0.43	36.4	-2.5	-0.66	73.0	17.5	2.59
2001	0.16	31.5	0.6	1.03	60.7	13.3	0.16
2002	1.56	34.3	-1.7	-1.65	56.9	6.3	2.13
2003	0.82	33.1	1.0	1.23	46.5	6.3	-0.42
2004	1.44	35.1	0.2	-0.02	37.3	6.9	0.68
2005	1.37	37.0	1.5	0.42	32.4	3.4	0.26
2006	1.53	40.2	-0.3	-1.03	29.2	2.4	-0.37
2007	1.27	42.0	-0.2	0.34	23.2	2.7	-0.02
2008	0.94	41.6	-1.0	-2.06	18.4	2.8	-0.47
2009	-1.17	45.3	-6.3	-3.74	24.2	3.0	6.15
2010	0.38	40.8	-2.5	-2.04	26.3	1.9	3.16
2011	0.65	39.0	-2.4	-3.25	23.3	2.1	0.68
2012	1.43	40.1	-2.1	-0.64	24.0	1.9	1.98
2013	0.67	38.5	-1.7	-2.45	23.4	1.3	1.24
2014	1.29	39.6	-1.7	-2.30	24.6	1.3	2.02

* The coloured cells represent a breach of the reference level

Source: Prepared by the authors basing on the data of the Ministry of Finance, the National Bureau of Statistics and authors' own calculations

As it has been argued before (Table no. 1), the period from 2000 to 2008 is considered to be a recovery period for Moldovan economy. However, the period of budgetary imbalance and debt accumulation in the '90s created serious imbalances to public finances and triggered the technical inability to pay the interest on the general government debt in 2001. This forced the government to bear a series of negotiations with foreign creditors on debt restructuring. The results of these negotiations consisted in a significant reduction of the interest paid on the general government debt from 17.5% of total public expenditure in 2000 to 6.3% in 2002. The downfall trend of this indicator had prevailed until 2006, when it recorded its lowest level, after which it began to increase again until 2009. Regarding the public debt indicator, it constantly reduced from 73% of GDP in 2000 to 18.4% in 2008. With regard to net lending we have found that only in four out of fifteen years Republic of Moldova actually repaid more debt than contracted. Moreover, the amount of the repaid loans is much smaller than the government debt reduction. This shows that the main factor that triggered the reduction of the public debt to GDP ratio was the foreign debt restructuring, while the repayment of debt was insignificant in this period. The positive effect of the debt restructuring resides in the fact that the budget balance indicator and the public debt were within the limits set by Community's numerical fiscal rules.

Another finding is that during this time period the Republic of Moldova did not totally comply with the Fiscal Compact rules, because the public spending have risen at a higher rate

than the GDP has. This has led to an increase of the public sector's size from 36.4% of GDP in 2000 to 41.6% in 2008, contrary to the objectives of the fiscal policy that were stated in the MTEF. The main cause is the sharp rise of social expenditures, as the share of this group of expenditures increased significantly from 54% in total expenditures in 2000 to 65.4% in 2008. Regarding the structural budget balance rule, the structural deficit has exceeded the 1% threshold in 2002, 2006 and 2008 which shows that the fiscal policy was not always prudent before the crisis. Moreover, the significant structural budget deficit of 2008 (2.06%) shows that the effects of the crisis began to emerge in 2008, while the authorities recognized the crisis just one year later. While looking at the regular budget deficit of 2008 (1%) does not provide too many clues about the onsetting crisis, the structural budget deficit appears to be more informative and acts as an efficient warning signal.

Despite the fact that there were some problems regarding the public finances sustainability before the global economic crisis, we conclude that during 2000 - 2008 the Moldovan public finances were rather sustainable. The situation has reversed in 2009, when Moldovan economy was affected by the global economic crisis. The regular budget deficit recorded an unprecedented 6.3% of GDP in 2009, the highest of the entire period. The imbalance of public finances in 2009 continued in the following year, when the deficit amounted to 2.5% of GDP. The structural deficit constantly exceeded the limit of 1% of GDP in every single year after 2009 (except 2012), despite the fact that authorities have made efforts to reduce the growth of public expenditures. This indicates a worsening of long-term sustainability of public finances. Moreover, if we look at the regular budget deficit and at the structural one, we found that they tell different stories. If the regular budget deficit did not signal any concern regarding public finance sustainability since it was permanently below the 3% threshold during 2010 - 2014 period, the structural budget deficit in turn shows a significant deterioration of public finance since it displayed values exceeding the 1% threshold in four of the five years considered (2010 - 2014).

Under these circumstances, the recent adoption of the Law on public finance and fiscal responsibility no. 181/2014 is a significant step forward towards the establishment of national fiscal rules in the Moldovan legal framework. The law includes provisions on three categories of fiscal rules that had not existed prior to 2014, namely fiscal policy rules, budget balance rules and the rules on the financial impact of political decisions on public budgets. However, in the light of this research, the law should be amended by including provisions regarding the structural budget balance rule and the expenditure growth rule.

5. CONCLUSIONS

The paper assessed the public finances sustainability in the Republic of Moldova under the EU fiscal rules. Compared to similar studies, a new in-depth analysis that includes not only the examination of the Maastricht numerical fiscal rules, but the assessment of the structural budget balance, an indicator that has never been estimated before for the Republic of Moldova was developed.

The analysis of the public debt, overall and structural budget balance indicators show that in general, public finances of Republic of Moldova are sustainable. Except for 2009, the Republic of Moldova complies with the Maastricht numerical fiscal rule; however it does not comply with the new fiscal rules regarding the structural deficit and public expenditures growth that had been set by the Fiscal Compact. Despite the fact that the structural deficit limit was mostly respected before 2009, the fiscal policy proved to be expansionary because of the

constant increase of the public sector's size in 2000-2008 periods. This rather contradictory situation when the budget deficits and public debt displayed sustainable levels in spite of the expansionary fiscal policy was due to the concessions made by the external creditors in restructuring the public debt and should not be considered as a merit of national government. The sustainability of public finances has worsened after 2009 when excessive structural deficit has been recorded. Hence, the global economic crisis, which inevitably affected Moldovan economy, represents a turning point in the fiscal policy in the Republic of Moldova, which has become less prudent in recent years. Although, this fact is not that obvious at present, since the regular budget deficit lies below the 3% threshold, on long term it will generate serious threats to the public finance sustainability as the structural deficit lies well above the 1% threshold.

From a policy perspective, we suggest that the authorities should pay close attention to the structural budget deficit indicator, since the regular deficit and the structural one may tell different stories, such is the case of Republic of Moldova. Despite the fact that it has some inconvenience in its estimation, the structural deficit indicator allows to assess the true nature of the fiscal policy and the real causes of budget deficits. By considering the risks related to population aging and labour migration, relevant information for national budget strategic planning is taken into account and sustainable policies can be designed well in advance.

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Notes

[1] The Labor Force Survey in households (LFS) is a modern method for the statistical survey of the labor force market having as a main objective the measurement of the active population – employed and unemployed – and of inactive population. For a more detailed information see: http://www.statistica.md/pageview.php?l=en&idc=351&id=2255.

[2] The gross added value of agricultural activity contracted by 23.3% in 2012. Given the important contribution of this sector of the economy to GDP (11.6% in 2012) it had the most significant influence on the GDP contraction.

[3] According to National Institute for Economic Research from Moldova, the agricultural activity had the largest contribution to GDP growth in 2013, as its gross added value registered a significant increase - of about 41%, generating a 4.5% GDP growth. In 2014 agricultural production registered a growth of 8.2% compared to 2013. Thus, the volume of agricultural production in 2014 recorded the highest value (in comparable prices) in the last decade.