

MOLDOVA

STRATEGIC PLAN

FOR

2001 - 2005

January 2001

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PART I: ANALYSIS OF ASSISTANCE ENVIRONMENT AND RATIONALE FOR STRATEGIC CHOICES

Since the break up of the Soviet Union, Moldova has been recognized as one of the newly independent states most committed to democracy, economic reform and integration with the West. In making this transition, it faces formidable obstacles, including lack of natural resources, entrenched interests in the old system and the social hardships that inevitably accompany any economic and political transformation.

Since 1991, the United States has supported Moldova in becoming a market-oriented, democratically governed state as a basis for establishing mutually beneficial political, economic and security relations. The United States government's goal in Moldova, as articulated in the U.S. Embassy's Mission Performance Plan, is to foster a unified Moldova, free of foreign military forces and capable of contributing to European security. The U.S. government also believes that if Moldova can successfully transform its political and economic processes, it can serve as a positive example of reform to its neighbors.

The USAID/Moldova program has played a dominant role in supporting these U.S. foreign policy interests by assisting Moldova in implementing the measures needed to transform its economic and political processes. While this transformation has proceeded largely on track, it has imposed significant hardships on the Moldovan people that could easily lead to an erosion of popular support for continuing the process. During the 2001-2005 period, USAID will seek to ensure that popular support for the reform process is maintained by focusing its efforts on bringing the benefits of living in a market-led democracy to the average Moldovan. To achieve this goal, USAID/Moldova's strategy for 2001-2005 will:

- help Moldova establish a **market environment** that supports and fosters broad-based growth
- stimulate **private enterprise growth** as a means of providing employment, income and services to the population
- promote the fundamental values of **democratic governance and citizen participation** which allow people to make choices about their future and
- address critical **social safety net** issues in order to reach vulnerable groups.

Country Conditions

The Political Environment: Moldova entered the new millennium in troubling circumstances. In 1999, there was ongoing governmental instability as neither left- nor right-wing political parties could maintain a governing majority. Relations between the presidency and the parliament were strained. Two successive governments were dismissed, followed by a period in which neither of the candidates for prime minister could accumulate the votes necessary to form a new government. While this crisis was resolved just before the end of the year, conflict between the different political parties continued through 2000. Political instability was further exacerbated in late 1999, when parliament refused to approve the privatization of winery and tobacco enterprises, thus leading to the suspension of International Monetary Fund (IMF) and World Bank adjustment programs. The threat of default and subsequent financial and social disruption were real.

Throughout this period of political turmoil, however, the Government of Moldova (GOM) continued the process of implementing structural reforms leading to a market-led democracy. Increasingly, the GOM demonstrated its recognition of the need to stimulate development and address the worsening economic conditions of the people in order to maintain support for the reform process. In its recently issued "Interim Poverty Reduction Strategy Paper," the GOM set forth a national plan for reducing poverty based on three pillars: sustainable and inclusive economic growth that will provide the population with productive employment; human development policies emphasizing increased access to basic services; and social protection policies targeting those most in need.

New parliamentary elections are scheduled in Moldova in early 2001. It is impossible to anticipate the results of these elections. It is unclear whether the communists, who currently control 40% of parliament and form the largest single bloc, will gain or lose seats. The make-up of the new parliament will have broad implications, as under the parliamentary republican system instituted in the fall of 2000 the next president will be elected by parliament, rather than by popular vote. While it is unlikely that any new government would abandon wholesale the broad spectrum of reforms currently underway, it is likely that the new government's make-up will influence the pace at which the reforms are carried out, particularly those related to privatization of state assets.

Economic Trends: Following independence in 1991, the Moldovan economy collapsed. Between 1990 and 1994, the country experienced a period of sharp economic decline. Between 1995 and 1998, however, economic reforms, supported in large part by the international donor community, helped to stabilize the economy and an upward trend began, with the gross domestic product (GDP) growing by 1.6% in 1997. The collapse of Russian ruble in 1998 temporarily halted this promising trend. As the major importer of Moldovan exports and a critical source of foreign remittances, Russia's economic downturn also slowed the Moldovan economy.

In spite of this setback, Moldova's economy resumed its growth trend the following year and the year 2000 promises to be a turning point. GDP grew by 1% in 2000, inflation was brought under control at around 18% (as opposed to the 38% inflation the previous year) and the foreign exchange rate stabilized at around 12.5 Moldovan lei to the dollar. In addition, the national budget deficit was narrowed to 2-3% of GDP and tax revenues increased by 40%. There is guarded optimism that the difficult economic decisions made over the past few years are beginning to pay off and that a period of growth is ahead.

While the general economic trend is positive, external debt remains a concern. In 2001, debt service will consume 34% of state budget expenditures and it is estimated that by the end of 2000, total public debt will equal 76% of GDP. Only by accelerating growth and continuing to restructure key sectors of the economy will Moldova be able to meet its foreign debt commitments and also address the needs of the people. The GOM's improved fiscal performance is a positive beginning. Privatization of the energy sector, the major source of external debt, is a critical next step. Additionally, increased exports through the development of the agriculture sector and increased foreign investment are essential.

The GOM recently launched a new medium-term economic development plan for the years 2001-2005. Under this plan, a GDP growth rate of 5-8% is projected, with inflation declining to 5-6%

by the end of the period and the GOM budget deficit constrained to 2-3% of GDP. It is USAID's belief that, while achievement of these targets is possible, the plan may be rather ambitious. The GOM has demonstrated its commitment to market reform and democratic society and has requested continued USAID assistance. The strategy outlined in this document will support the GOM in achieving its goals.

Social Needs: For the vast majority of Moldovans, living standards have worsened over the past ten years. Not only has purchasing power declined, but also unemployment has risen, the old social protection system has deteriorated, and the health care and education systems are in disarray.

Declining purchasing power, while affecting all, has had an extreme impact on those such as public sector employees, who rely on salaries for income. Due to IMF-set austere fiscal policies, minimum wages have been frozen, leaving monthly average salaries equal to only 40% of the estimated minimal consumption basket. As a result, the poor in Moldova are made up not only of the more "typical" socially vulnerable groups, but also of well-educated people employed in the national economy.

Although official statistics do not capture the true rate of un- and underemployment in Moldova, the rate is believed to be on the rise as a result of economic decline. The situation varies by region and season. Lack of mobility of the labor force is a constraint, as well as individuals' inability to adjust to the new market economy. Many of the unemployed are absorbed into the shadow economy as self-employed. Moldovan women, especially those who are pregnant, single mothers with young children, and those over thirty-five, are particularly affected by the lack of employment opportunities.

Moldova inherited a system of pensions, allowances, compensations and benefits from the old regime that protected socially vulnerable groups. However, the system does not adequately target the most vulnerable, including widows and female-headed households, and funding is insufficient to meet the needs of the growing poor. In the short-term, the government's guarantees of social protection are increasingly viewed as empty promises.

The impact of increased poverty is already being felt in terms of the health status of vulnerable Moldovans. While, for the most part, food is available in Moldova, unemployment and the GOM's inability to pay salaries and pensions as well as provide funding to institutions such as hospitals and orphanages, has resulted in vulnerable groups unable to purchase adequate and nutritionally balanced food supplies. Recent estimates indicate that caloric consumption has declined, with average per capita consumption now at 1980 calories, vs. the FAO standard of 2500. Rising malnutrition, along with the decline in access and availability of health services, is leading to an increase in the incidence of diseases like tuberculosis, hepatitis and AIDS and a declining life expectancy.

Access to education is also declining as underpaid teachers leave the field, government resources are insufficient to maintain and supply schools, and families lack the capacity to send their children for further education. This is a particularly disturbing trend in a country which, due to its lack of natural resources, must rely heavily on its human capital for development and prosperity.

Many Moldovans are responding to the declining standard of living by leaving the country. An estimated 120,000 to 600,000 people (of a population of 4.2 million) currently work overseas. While many of those who migrate are among the most qualified and are those who could most positively contribute to Moldova's economic transition, their remittances provide a lifeline for the families they leave behind. Another significant proportion of those working abroad are believed to be victims of trafficking—principally women who end up in the commercial sex industry.

Clearly Moldova's period of transition is having a negative impact on the social sector. The daily lives of most citizens were better under the Soviet regime. The implications of this situation are serious. First, there is a real possibility that the poverty initially assumed to be a temporary phenomenon during a period of transition will become a chronic condition. Second, the government's inability to pay wages and provide citizens with basic social services undermines the GOM's credibility, thus threatening social stability. Finally, the inability of economic and democratic reforms to deliver concrete results to the average citizen weakens support for the reform process, calls into question the validity of democracy and strengthens the hands of those who wish to undermine the process of change. Unless the burden on the poor is alleviated and social issues are addressed, Moldova's political stability cannot be assured.

Destabilizing Factors: The most likely cause of conflict in Moldova stems from social unrest directed against the government. If not addressed, the poverty and social hardships currently being experienced by the Moldovan population clearly have the potential to turn into social unrest. There is dissatisfaction among public employees, many of whom are owed months of back wages and whose base salary is not adequate to meet vital needs. Similarly, pensioners and others who depend on the social protection system have voiced threats against the government due to the low payments they receive and the fact that payments are in arrears. In the spring of 2000, when the GOM, at the urging of the IMF, eliminated transport privileges for students, the students took to the streets in protest. Unless people's standard of living improves, this type of protest could become more frequent.

In the near future, the political instability characterizing 1999-2000 could continue. As described earlier, Moldova will hold new parliamentary elections in early 2001 and the new parliament will elect Moldova's next president. It is too early to determine what the new political line-up will look like or how it will affect the GOM's position on reform. While it is unlikely that the election results will derail Moldova's broader economic and political transition, it is highly likely that they will affect the pace of Moldova's reform.

The Transnistria conflict is a continuing dark cloud in Moldova's efforts to transform its economic and political systems. Transnistria is a breakaway province, ruled by a corrupt, authoritarian regime, which continues to harbor a large number of Russian troops against the wishes of the GOM and international community. Its huge Soviet-era arms depot of over 40,000 tons potentially could supply armed conflicts both in Moldova and the region. During the period of this strategy, it is anticipated that tensions between Moldova and Transnistria will continue, but it is unlikely that they will erupt into violence. Similarly, tensions with Gagauzia may increase, but will most likely remain non-violent.

USAID/Moldova, 1992 to 2000

Since the inception of its Moldova program in 1992, USAID has cooperated with the IMF, World Bank and other donors to support the GOM in making and implementing the difficult decisions required to transform the country into a market-oriented democracy. Under previous strategic plans, USAID support has principally been directed toward economic restructuring, with lesser amounts being targeted at addressing democratic transition and social issues.

Privatization of State-Owned Assets: In late 1993 USAID technical assistance began helping the GOM to implement its plan to privatize state-owned assets. Under the first phase of its plan, the focus was on privatizing large numbers of small, medium and large enterprises. Initially this was done through the use of national patrimony bonds, with additional mechanisms evolving later. As a result of this program, 866 medium and large enterprises had been privatized by the end of 1999. Significantly, three of Moldova's five power distribution companies were among those privatized, with the remaining distribution companies and several other energy companies currently up for tender. Resistance to completing the process of privatizing state-owned assets was met in late 1999, when Parliament decided that certain strategic enterprises (wineries, tobacco companies and granaries) should not be privatized. Following GOM/donor discussions, this issue was resolved and the process of privatizing these industries is once again progressing.

The second phase of the GOM's privatization plan was dedicated to the privatization of urban and agriculture land. This program has made significant strides and is noted as a model for its achievements in the break-up of state and collective farms and the issuance of constitutionally valid, tradable land titles. As a result of this program, by December 31, 2000, 836 farms had restructured their debt and been liquidated, 2.41 million land titles had been issued to 790,045 people, and 1973 private enterprises had acquired their associated land. USAID technical assistance played a key role in 1999 in helping the GOM to prepare and pass legislation to restructure the debt of the former collective farms. With this legislation in place, the former collective farms can be completely liquidated and the new privately held farms are not burdened with debt from the socialist past. Moldova is the first country in the former Soviet Union to successfully deal with this difficult issue.

Market-Based Economic Restructuring: As the GOM shifted toward a market-oriented economy, it was clear that fiscal and financial reforms were critical. USAID technical assistance to the Ministry of Finance (MOF) has been instrumental in helping the GOM meet IMF conditionality related to fiscal and budgetary improvements. Capacity within the MOF in the areas of tax policy, tax administration, revenue forecasting, budgeting, accounting, and cash and debt management have been strengthened. USAID has also provided needed technical assistance to the Parliament to build its capacity for drafting and analyzing legislation required to support fiscal reforms. Within the financial sector, USAID assistance has helped in promoting an efficient private banking sector and a transparent and open securities system. Rationalization of the banking system has been completed, bank legislation and regulations have been updated, off-site bank supervision has improved, western-based accounting practices have been adopted and a stock exchange has been established. These efforts have been complemented by a USAID-supported legal reform program which helped to prepare a legal framework and commercial legislation compatible with a market economy. This draft civil code/commercial law is now being discussed by parliament.

Democratic Governance/Civil Society: USAID assistance in democratic governance has focused primarily on elections and civic education. During the 1998 electoral campaign, USAID technical assistance helped administer the election, disseminate information and materials about democracy and conduct an evaluation of the election process. USAID-provided experts have also assisted in the revision and passage of electoral laws and procedures and promoted the development of many of the institutions central to democratic governance, including the parliament, mass media and NGOs. Between 1997-99, USAID carried out a pilot program which provided mini-grants to rural communities. This program helped to strengthen community capacity and improve social services for rural populations. The successful pilot served as the model for the World Bank's Social Investment Fund, initiated in March 1999. Recently, USAID/Moldova-supported interventions have begun to target local governance. USAID-provided technical assistance was critical in the passage of key legislation to reform local government. A newly initiated local governance program is promoting fiscal autonomy, administrative efficiency and democratic governance at the local level.

Targeted Interventions: USAID-supported small, targeted grant and humanitarian programs have complemented USAID's larger efforts to facilitate Moldova's economic transition. Small grants have helped to encourage improvements in public service delivery, greater citizen involvement in civic decision-making and increased dissemination of information to citizens. A hospital partnership has improved health care at a number of Moldovan medical institutions. Humanitarian assistance has alleviated the hardships of vulnerable groups and strengthened the capabilities of service organizations that provide critical humanitarian and related development aid. In the winters of 1998-99 and 1999-2000, USAID's winter heat assistance program distributed coal to vulnerable groups outside the cities, including orphanages, hospitals, schools and needy households. In addition, almost fifty hospitals, orphanages and boarding schools were weatherized.

Taken together, USAID-supported programs have contributed significantly to the restructuring of Moldova's economy. Among the former Soviet states, Moldova is now a leader in land privatization, banking sector reform and accounting reform. Progress in privatization of the energy sector is already improving service delivery and will help contain Moldova's foreign debt. The Government of Moldova, the World Bank, International Monetary Fund and USAID all agree that, while it is necessary to continue to consolidate economic restructuring activities, it is time to shift the priority to stimulating economic growth.

A Framework for USAID Assistance, 2001 – 2005

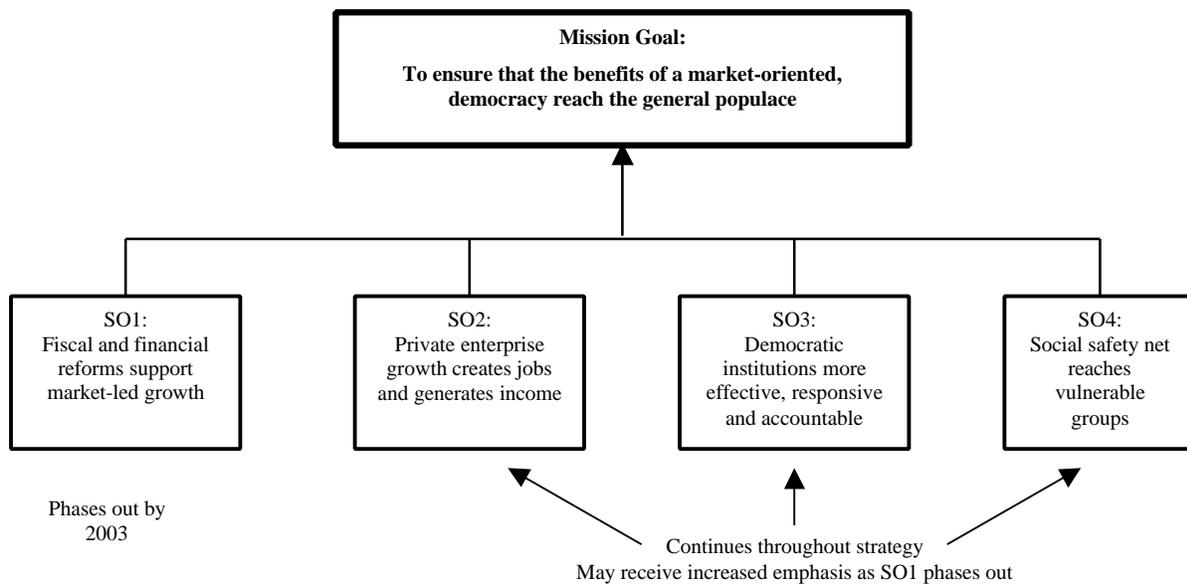
The strategy outlined in this document builds on the developments that took place during the previous strategic planning period, when program results were achieved, reforms were implemented and Moldova's political context matured. USAID's previous strategy was geared toward stabilization. As described above, GOM commitment, coupled with USAID and other donor support, has resulted in the basic restructuring of Moldova's economic and political systems. In the process, however, the standard of living for most Moldovans deteriorated. If popular support for the economic and democratic transition is to continue, Moldova's citizens must begin to reap the benefits of the new system. USAID's strategy for the 2001-2005 period,

therefore, is geared toward helping **ensure that the benefits of a market-oriented, democratically governed state reach the general populace.**

In order to achieve its goal, the strategy adopts a four-pronged approach. First, it focuses on developing a market environment as a necessary condition for economic development. Second, it emphasizes private sector development as a means of creating jobs and generating income. Together, these two approaches are expected to generate the broad-based, market-led growth that is key to bringing the benefits of the economic transition to Moldovans on a long-term, sustainable basis. Third, the strategy seeks to build democratic institutions which empower citizens to participate in the basic economic and political decisions that affect their lives and, fourth, it enhances the social safety net which protects the vulnerable.

During the five-year period included in this strategy, it is anticipated that Moldova's need for USAID assistance in developing a market economy (Strategic Objective 1) will diminish and that ongoing activities will conclude by late 2003. As USAID support for these activities is phased out, it is expected that support for private sector growth activities will be broadened and deepened and that additional opportunities in democratic governance will be investigated. At that time, it may also be appropriate to examine the possibility of providing assistance for human development activities in support of the third pillar of the GOM's poverty reduction plan.

SUMMARY OF THE USAID/MOLDOVA STRATEGY



The economic reform activities included in this plan are primarily continuations of programs initiated under USAID's previous strategy. **Fiscal and financial sector reform** activities will be completed and consolidated so that human and institutional capacity exists within the GOM to continue to make rational economic decisions. Similarly, activities supporting the establishment of a **legal environment** conducive to market-led growth will be concluded. USAID support for these activities will be phased out by the third year of this strategy.

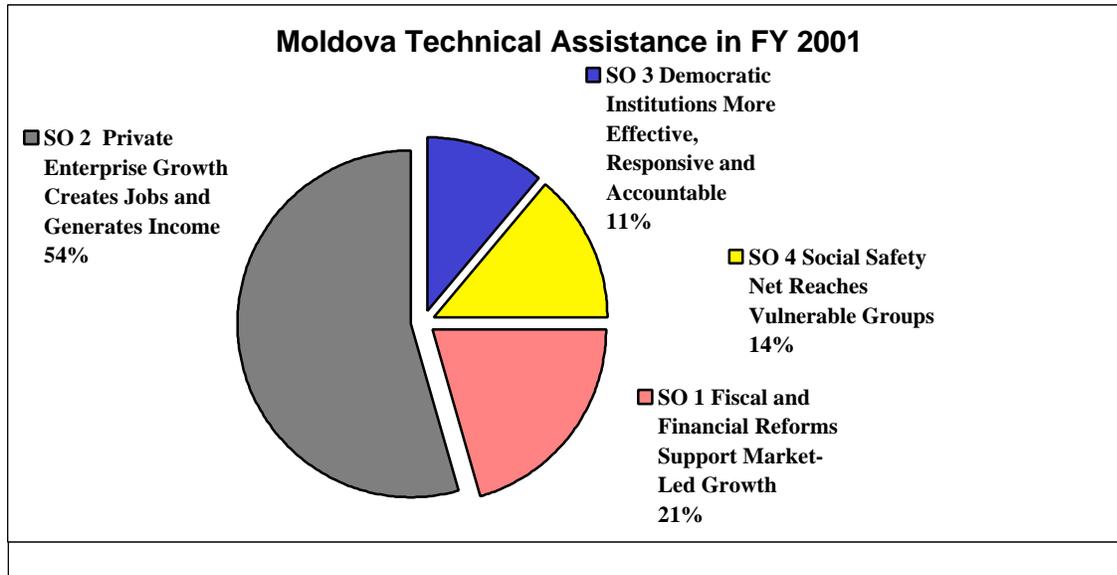
To stimulate private enterprise growth, USAID/Moldova's strategy gives new priority to the **agriculture sector and small and medium enterprise development**, while continuing to support the **restructuring of targeted strategic industries**. Recent assessments identified agriculture and small and medium enterprises (SMEs) as two areas in which Moldova has a comparative advantage and in which limited capital investments could have significant returns by providing employment, increasing productivity, stimulating investment and expanding markets. Agriculture is the backbone of the Moldovan economy, accounting for approximately 25% of the gross domestic product and employing over 40% of the workforce. With agricultural land now under private ownership, USAID believes that farmers must be treated as private entrepreneurs and farms as private enterprises. SMEs have burgeoned over the past four years and the estimated 195,000 SMEs now provide employment for almost 39% of the population, with over 40% of the SMEs operating in villages and rural areas. By focusing on agriculture and SME development, the USAID program will reach a large proportion of Moldova's citizens and help integrate them into the market-led economy. Furthermore, given women's key role in both Moldova's agricultural sector and small and medium enterprises, USAID's private sector focus will help ensure that women benefit from economic growth.

To complement and support private enterprise development, ongoing efforts to restructure the energy and telecommunications sectors will continue. Privatization of these industries is expected to improve service delivery for all Moldovans, facilitate private sector growth and encourage domestic and foreign investment. Energy sector reform is particularly crucial, due to its impact on the economy. By relieving the GOM of its primary cause of foreign debt and freeing revenues for domestic investment, privatization of the energy sector has far reaching consequences for economic development in Moldova.

While accelerating market-led growth is key to improving the lives of Moldovans, USAID/Moldova is convinced that this focus alone is insufficient for bringing the benefits of transition to the Moldovan people. Democratic governance, in which people participate in the economic and political decisions that affect their lives, is also essential. Under the previous strategy, USAID/Moldova's democracy initiative focused on encouraging the involvement of citizens at the grass roots level. Recent advances in local government development, however, led to a re-examination of this emphasis. With the passage of new local government laws, Moldova is now poised to make significant progress in reorganizing and reforming its public administration system. A local government needs assessment identified several key areas in which USAID assistance could make a marked impact. This strategy therefore shifts the focus of USAID/Moldova's democracy program from citizen participation only to building *democratic institutions*. Activities focus on supporting improvements in **local government**—the level of government with which most people come into contact—while also strengthening the **civil society organizations** that facilitate involvement of citizens and communities in the democracy process.

USAID/Moldova believes that a major focus on private sector-led growth, complemented by a democratic governance program, can help improve the standard of living for Moldovans by 2005. At the same time, it recognizes that this medium-term strategy does not respond to the immediate social needs of Moldova's vulnerable. The strategy therefore seeks to **strengthen the social safety net** to ensure that the vulnerable are reached. To the extent possible, social assistance activities will incorporate development goals and complement the strategy's primary emphases.

Social assistance efforts will be coordinated with United States Department of Agriculture (USDA) food aid programs, Department of Justice (DOJ) anti-trafficking programs and other U.S. government programs which directly target vulnerable groups.



Four crosscutting themes thread their way through the approaches outlined in this strategy. They are policy reform, privatization, gender equality and environmental sustainability.

USAID/Moldova views **policy reform**, at the macro, sectoral and local level, as a prerequisite to sustained development. Without policy reform, the activities supported by USAID will not have the expected impact, nor will they continue once USAID support ends. USAID/Moldova has adopted a broad interpretation of the phrase “policy reform” to include all those activities required to establish an enabling environment. This includes drafting and passing legislation, but, because much of the needed legislative reforms have already taken place, frequently focuses more on harmonizing laws, removing old laws from the books, incorporating citizen feedback into revisions of the laws, developing regulations related to new laws, establishing mechanisms for implementing new laws, and putting in place the structures, processes and systems needed for implementation and enforcement of the new laws.

Past experience indicates that USAID/Moldova can effectively work with the GOM on policy reform issues. Since the inception of the USAID/Moldova program, USAID has provided four successive GOM administrations and other key institutions with technical advisors in support of policy reform. These advisors have been well received, respected and listened to—and, for the most part, their presence has resulted in positive change. USAID assistance was instrumental in drafting many of the key legislative reforms that underpin Moldova’s economic and political transition, particularly in the areas of privatization, fiscal reform, banking reform and commercial law. Significantly, USAID assistance for policy reform has included a strong capacity building element, thus ensuring that local capacity for both drafting and reviewing new legislation has been enhanced. Future efforts in policy reform will place increasing emphasis on institutionalizing processes for incorporating citizen input into the policy reform process. During

the period covered by this strategic plan, assuming that the GOM remains committed to economic and political restructuring, USAID/Moldova believes that by building on its past successful performance in the policy area, it can maximize program impact and continue to produce significant results.

Privatization of state-owned assets, an important component of the previous strategy, continues as an overarching theme in this strategy, but is not included as a specific program objective. During the past five years, the principal goals of the privatization program were achieved. Specific actions necessary to complete privatization activities, particularly for key strategic industries, are incorporated into elements of the strategy and the overall direction of the strategy reinforces the importance of privatization in a market-led democracy.

As a third crosscutting theme, USAID/Moldova places great importance on advancing **gender equality** in all its activities to create more effective programs. The SME baseline study, the agriculture sector assessment and social sector assessments highlighted the different barriers faced by men and women. To ensure that gender issues are addressed, all programs designed, implemented and assessed under this strategy will take into account differences and inequalities between men and women. All results indicators will be disaggregated by gender to the extent feasible.

Environmentally sustainable development is a fourth theme that cuts across this strategy. While this strategy does not propose direct USAID involvement in environment issues, USAID/Moldova recognizes that its shift in emphasis from restructuring to growth introduces the need for greater awareness of the potential environmental impact of proposed activities. All activities carried out under this strategy will comply with 22 CFR 216 requirements. This topic is discussed more thoroughly in Part II of this strategy

Support for the development of capital markets is not included in this strategy. During the first two years of the previous strategy, USAID provided direct support for the establishment of the Moldova stock exchange and the development of the State Commission on Securities Markets. Since then, USAID's involvement in capital markets has been limited to a monitoring function as the two institutions learned to stand on their own.

This strategy does not include a plan for addressing long-term human development needs in Moldova. Both the health and education systems are in desperate need of assistance, with both requiring major restructuring. The World Bank is currently undertaking assessments of both sectors. Until these assessments are completed, sector strategies agreed upon and means of donor coordination developed, any major involvement in health or education is premature.

Moldova's Prospects for Transition

The Government and people of Moldova remain firmly committed to economic and democratic reform. Most Moldovans agree that the reforms implemented over the past few years represent the best prospect for Moldova's future. Macroeconomic stabilization has achieved significant and encouraging results. However, unless growth can take place and the lives of people improve, support for the reform process will inevitably waiver. In the near future, Moldova must stimulate

growth, attract foreign investors, open new markets and increase employment opportunities. At the same time it must address social and humanitarian issues.

Moldova's success in restructuring its energy sector will strongly influence the country's future. Unless Moldova can diversify its sources of energy and reduce dependence on Russia, its independence will be threatened. Without reducing its energy-related foreign debt, Moldova's ability to carry out domestic investments and finance social sector activities will continue to be severely circumscribed. Lack of reliable and adequate power will inhibit the growth of industry, domestic and foreign investment and overall economic development.

The GOM's medium-term economic development plan and poverty alleviation plan respond to these challenges by identifying the development of private sector activities in areas where the country has a comparative advantage (agro-industry and small/medium enterprise) as the most likely source of medium term economic development; discussing the need for improving the macro-economic investment climate; and pointing out the importance of public sector reform (including local government) to growth. The social protection section of the plan also discusses the critical need for a better-targeted social assistance system.

While the GOM's goals are ambitious, USAID/Moldova believes that the Moldovan economy is now poised for a period of growth. With USAID and other donors working to support the GOM, there is optimism that better days are ahead.

Formulation of the Strategic Plan

The approach outlined in this strategic plan is based on the findings and recommendations of many individuals and organizations (see Annex II). Over the past year, USAID has funded a series of studies and assessments which have provided critical input into this strategy. Key among these were a local government needs assessment, a study of the constraints to agriculture and agribusiness development, and a baseline study of small and medium enterprises. Past performance was critically analyzed, the new environment assessed and future prospects identified. The studies provided a critical means for dialog with the Moldovan citizenry, thus ensuring that their needs would be considered in the strategic planning process. In addition to the USAID-funded studies, analyses carried out by local organizations and other donors were reviewed.

The USAID/Moldova strategy also benefited from lessons learned in other nations of the former Soviet Union. Experience in the Ukraine, in particular, was important in helping to develop the SME strategy and also helped guide plans for agriculture and local governance. The "Draft Discussion Document: NIS Banking Strategy" provided input into the banking strategy. Experts from both the region and Washington were called upon for their knowledge in specific technical areas as well as their experience in the region. Their recommendations and suggestions were particularly invaluable in the development of the accounting, banking, energy, local governance and agriculture strategies.

Additionally, USAID sought the input of the technical team of grantees and contractors already working in Moldova under USAID-funded programs. Many of these consultants have years of experience in Moldova. They interact on a daily basis with the ministries, organizations and

people that USAID programs assist and have a “hands on” knowledge of the problems and possibilities. Furthermore, they have key data at their disposal, gathered through focus group discussions, project monitoring efforts or other means, that helped USAID/Moldova make strategic decisions.

USAID/Kiev provided on-going guidance and support throughout the strategy preparation process. Its comments and recommendations on draft documents contributed significantly to sharpening and strengthening the strategy.

Finally, USAID/Moldova's strategy was also shaped by other donors. The Mission has sought to ensure that USAID-supported programs do not replicate support being provided by other donors, but rather complement and reinforce other donor programs.

Other Donor Activity in Moldova

The major donors in Moldova are the International Monetary Fund (IMF), World Bank, USAID, European Union through Technical Assistance to the Central Independent States (EU-TACIS) and United Nations Development Program (UNDP). The IMF and World Bank have been instrumental in facilitating Moldova's economic restructuring. The IMF played a key role in establishing economic policy, while USAID-provided technical assistance helped the government meet the IMF targets and conditionality. The World Bank has disbursed approximately \$305 million in investment and technical assistance for economic restructuring since 1992. It also supports a \$20 million Social Investment Fund, which funds micro-projects at the village level. The EU committed some \$76 million between 1991 and 1999 for activities mainly geared toward economic restructuring, with modest activities in public administration and the environment. UNDP resources have mainly been targeted at democratization. Several other bilateral donors are involved in Moldova on a smaller scale. In addition, the Soros Foundation and several private organizations run small development programs in Moldova.

Donor coordination takes place through monthly meetings at which the U.S. Ambassador and the USAID Country Program Coordinator represent the United States. Topics of discussion range from the overall reform environment to pending GOM legislation to points of coordination. In addition, USAID staff meet frequently with counterparts from other donor organizations to discuss programs, compare notes and ensure complementarity.

The opportunity for achieving greater collaboration is enhanced by the fact that the World Bank and IMF are designing new plans for Moldova at the same time as USAID. Specific areas of cooperation are noted in the discussions of individual strategies. A summary of other donor programs is contained in Annex VI.

PART II: DETAILED STRATEGY

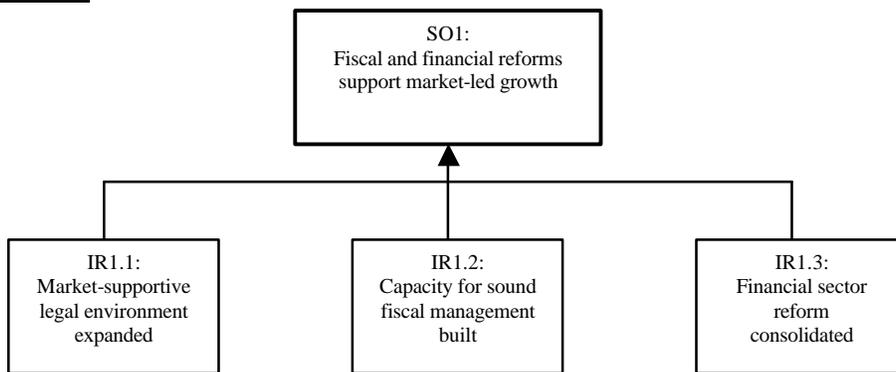
STRATEGIC OBJECTIVE 1: FISCAL AND FINANCIAL REFORMS SUPPORT MARKET-LED GROWTH

The areas of intervention outlined in this section of the strategy contribute directly to the E&E Bureau's Strategic Assistance Area I: Economic Restructuring. They will help foster the emergence of a competitive, market-oriented economy in which the majority of economic resources is privately owned and managed. The SO is also linked to the E&E Bureau's SO1.2: Increased soundness of fiscal policies and financial management practices and SO1.4: A more competitive and market responsive private financial sector.

Problem analysis: Since independence, the GOM has made major strides in restructuring its economy and developing the macroeconomic structures and institutions that support a market-led economy. Efforts between 1992-1998 resulted in the economy moving steadily toward stability. However, with the financial crisis in Russia, Moldova lost its principal export market, leading to shortfalls in tax and customs revenues. While the economy has now regained its footing, the GOM must continue to maintain a stable macroeconomic environment tailored to the country's financing constraints and conducive to economic growth. To assist in this effort, the GOM and IMF have jointly developed a macroeconomic framework for the next three years. A five percent per annum growth rate is projected for that period. In order to meet the targets in the IMF agreement, the GOM has requested that USAID continue to provide assistance in the three key areas of the economy which it has assisted in the past: the legal environment, the fiscal sector and the financial sector.

Capacity within Moldova to assume responsibility for the management of these sectors without the assistance of foreign technical advisors is growing. Over the course of the first three years of this strategy, USAID will complete the legal, fiscal and financial sector programs that were initiated under the previous strategy and progressively hand responsibility to the individuals and institutions which have been receiving USAID assistance. It is anticipated that by 2003, USAID support for macro-economic reforms will be phased out.

Results framework:



Development hypothesis: An enabling environment is a necessary condition for facilitating the type of economic growth in Moldova that will provide a better standard of living for the people. A clear set of commercial laws and a civil code is needed to define commercial relationships and provide legal stability that will attract domestic and foreign investment and provide employment and income. The building of indigenous capacity within the Ministry of Finance, other line ministries and the parliament to set and implement fiscal and other measures which reduce the budget deficit, enhance public accountability and provide for sustainable financing of social services is another requirement. Finally, the establishment a sound financial sector, including safe, stable and transparent banking system and a modern accounting and auditing system, is needed to decentralize control of financial resources and assure the allocation of capital to its most productive uses.

Critical assumptions

- The GOM will remain committed to economic restructuring.
- Budget outcomes will not be distorted by unexpected exogenous shocks.
- Parliament will act on laws presented to it.
- The market environment in Moldova can be improved to stimulate both internal and external investment.
- Financial sector reform and overall economic improvement will allow budget organizations to pay their energy bills and social sector subsidies.

Performance measurement: At the strategic objective level, the results of USAID's interventions in supporting a market environment will be measured by GDP growth.

IR 1.1: MARKET-SUPPORTIVE LEGAL ENVIRONMENT EXPANDED

Problem analysis: Moldova's transition to a market economy, and hence its ability to provide broad-based employment for the population, is constrained by its continued use of a Soviet-era civil code, written for use in a completely different economic system. In addition, numerous statutory and regulatory barriers contribute to a hostile environment which discourages both foreign and domestic investors. In April 1999, USAID initiated a two-year commercial law initiative to address these issues. With this support, a new civil code was drafted and presented to parliament, where it is currently under consideration. Following the parliamentary deliberations, revisions to the code will be necessary and supplementary commercial legislation will need to be drafted. Institutional and human capacity needs to be increased within Moldova to enact and implement commercial laws conducive to the growth of private enterprise and supportive of economic development.

Phase-out activities: Between 2001-2003, USAID will continue to support activities which will result in the development of a set of commercial laws which encourage private sector growth and supports a market-led economy.

USAID will continue the commercial law program initiated in 1999 by working with representatives from the GOM, the parliament, the Supreme Court of Justice, the Chamber of Industry and Trade and key private sector professional organizations. Technical assistance will be provided for continuing to develop laws related to commerce. Once parliament has discussed

the proposed civil code, carrying out analyses of proposed changes and drafting revisions will be supported. In addition, USAID will support the drafting of several other codes and laws, such as commercial law and the investment code, which are required for a comprehensive market-supportive legal system. Furthermore, an inventory of existing statutory and regulatory barriers to foreign and domestic investment in Moldova will be developed and changes proposed to the GOM, the judiciary and others.

Throughout the legal reform process, institution building for all partners will take place. Technical assistance will be provided to the parliament to assist in drafting laws, to help create and build capacity in a legislative center and to strengthen the legal information center. Within the Ministry of Justice, assistance will be provided for drafting the organizational law of the Ministry of Justice to define the responsibilities and authorities of the ministry, to strengthen the legal drafting department and to strengthen the legal information center. Technical assistance to the court system will focus on institution building, especially in the High Economic Court.

To support the institution building efforts, USAID will also provide training for the legal staff in the partner institutions. Moldovan attorneys will be exposed to concepts of western commercial law practice and legislative drafting. "On-the-job" training will be supplemented by formal training, study tours and seminars.

Impact and performance monitoring: Activities carried out in support of this intermediate result will have the following results:

- Proposed changes to the draft civil code will have been analyzed and appropriate revisions drafted.
- A commercial law, investment code, company law, bankruptcy law and collateral law will have been drafted.
- Capacity will exist within the Department of Justice to draft commercial legislation that reflects modern market economy principles.
- Methods for incorporating citizen input into the legislative process will be functioning.
- The capacity of attorneys and legal experts will be increased.

The impact of activities supporting this intermediate result will be monitored by tracking improvements in the legal environment.

IR 1.2: CAPACITY FOR SOUND FISCAL MANAGEMENT BUILT

Problem analysis: The transition from a centrally planned economy to a market-led economy required a major reform of Moldova's fiscal sector. USAID has been the GOM's principal partner in this process since 1994, when it initiated phase I of its fiscal reform program. Under that phase, activities focused on helping restructure the Ministry of Finance and its State Tax Service. Phase II of the program, which contributed to the consolidation of fiscal policies and fiscal management practices during the transition period, took place between 1997-2000. At that time, support was broadened to include parliament. As a result of these two phases, legislation outlining the budget process was adopted, budget classifications now meet IMF guidelines, and the budgeting process is improving. Similarly, the treasury system has improved, with a computerized system now in place. Significant progress was made in tax policy with the

adoption of several titles under a unified tax code. Increasing tax revenues are a testament to improved tax administration. Technical assistance to parliament resulted in the establishment of the Center for Budgetary and Financial Analysis to assist parliamentary committees in deliberations on fiscal and budget legislation. The center has responsibility for reviewing and commenting on most of the legislation passing through parliament. USAID coordinated with the World Bank in several of these areas, including treasury, debt management and computerization in the State Tax Service.

While this progress is significant and restructuring is essentially completed, the MOF still struggles to provide the government with sound fiscal policy advice. Capacity to carry out some key actions needed to ensure sound fiscal decision-making, including critical forecasts and analyses for both the budget and treasury and managing debt, is limited. Similarly, capacity in the areas of tax law, tax administration and the enforcement of tax laws needs to be strengthened.

Within parliament, capacity within the newly established Center for Budgetary and Financial Analysis is not yet strong enough to provide the independent and quality fiscal advice parliament requires to enact sound fiscal legislation. Analytical capacity of the center and its related committees needs to be strengthened and the quality of its publications improved.

Phase-out activities: Phase III of the fiscal reform program, which will be implemented from 2001-2003, focuses on ensuring increased soundness of fiscal policy and fiscal management and promoting the long-term sustainability of fiscal reform through capacity building.

USAID will continue to provide technical assistance, on-the-job training, and short seminars to strengthen the Ministry of Finance in the areas of the budget process, the tax system and the treasury, emphasizing building capacity in those areas that are weak. Specifically, USAID will assist the MOF in creating and using more rigorous macroeconomic forecasting and improving budget analysis, budget preparation and budget execution. These changes will come about through the establishment of fiscal analysis policy and budget policy units within the MOF and the training of staff within these units. Increased emphasis will be placed on not only increasing revenue, but also controlling expenditure as a key to helping Moldova breach the gap in the budget deficit.

Technical assistance will also be provided to strengthen the MOF's ability to prepare tax laws which create an economic environment conducive to investment promotion, private sector development and economic growth in a market-driven economy. The necessity of working with counterparts and stakeholders to build consensus among policy-makers will be stressed. These activities will be coordinated with policy reform activities supported under the commercial law program. To build capacity to fairly and efficiently administer and enforce the tax laws, USAID will provide technical assistance geared toward increasing voluntary compliance through outreach activities. The provision of information and services for taxpayers will be supported, along with training for tax officials. Additionally, technical assistance in areas such as using information technology and risk-based control systems to plan and allocate resources will be supported. The existing computer system for the administration of taxes will be enhanced to support increased effectiveness.

USAID support to the treasury will focus on providing managers with the tools to effectively forecast cash inflows and outflows and use this information for decision-making. Also, a debt management system which supports requirements at both central and local government levels will be developed. Continued support for computerization will facilitate effective financial management through an integrated information system.

Within the parliament, USAID will continue to build analytical capacity within the Center for Budgetary and Fiscal Analysis and its related committees by expanding training programs on tax policy, budget policy, revenue estimation and macroeconomic analysis. To build up analytical tools for use by the center, USAID will support the expansion and consolidation of data on expenditures, public debt, tax and non-tax revenue collections, local government fiscal information and general socio-economic data. USAID-provided technical assistance will also help the Center to improve the quality of its publications, such as the Bulletin of Analysis and Information. Finally, USAID will provide opportunities for senior staff and parliamentarians to improve their knowledge through formal training opportunities and study tours.

Impact and performance monitoring: Achievement of this intermediate result will result in the following:

- The Ministry of Finance will have the capacity to:
 - formulate and implement good fiscal policy through sound revenue and expenditure analysis, rational budget formulation and execution;
 - account for revenues and expenditures through an efficient functioning treasury and debt management system;
 - increase resource mobilization; and
 - provide taxpayers with quality service and information.
- The Center for Budgetary and Financial Analysis will be a permanent, credible and dependable fiscal policy center capable of formulating and presenting sound policy advice to the Parliament without assistance from foreign advisors.

This intermediate result will be monitored by tracking tax revenues and the budget approval process.

IR 1.3: FINANCIAL SECTOR REFORM CONSOLIDATED

Problem analysis: Moldova was one of the leaders in banking sector reform in the mid-1990s. Early on, the National Bank of Moldova aggressively pursued reforms to reorganize or close non-performing banks and to develop one of the best banking laws in terms of international standards. Recently, however, the momentum has slowed due to exogenous factors such as the financial crisis in Russia and domestic political turmoil. There is a need to recapture the forward motion and consolidate the gains made in developing a strong banking infrastructure.

Since independence, USAID has been cooperating with the IMF and World Bank to support Moldova in establishing a market-oriented private banking sector. Under its previous strategy, USAID initiated and completed phase I of a three-phase banking strategy. Under phase I, USAID provided technical assistance to the National Bank of Moldova to help strengthen its capacity to regulate and supervise the banking sector. As a result, significant progress has been

made in establishing the fundamentals of an effective bank supervision system and regulations are beginning to conform to western standards. In addition, with USAID support, international accounting standards have been widely adopted throughout the banking system. Essentially, Moldova's banking sector has successfully passed through the beginning stage of becoming market-oriented. Certain aspects of the financial infrastructure need further strengthening; key legislative and regulatory reforms are still needed; and the capacity to carry out fundamental banking functions, such as executing a payments system, resource mobilization and inter-mediation between savers and investors, needs to be built. Phases II and III of the banking strategy will address these issues.

Accounting reform was supported by USAID under its previous strategy both as a necessary process in privatizing the banking system and as a critical development for private enterprise growth. Over the past four years, USAID-support for accounting reform in Moldova has resulted in a solid understanding at all levels of the urgent need to revise the existing accounting practice and adopt international-based standards on accounting (IAS) and auditing (ISA). National standards on both accounting and auditing have been developed (based on the international standards) and the national bank, all commercial banks, the capital market and many enterprises have converted to national accounting standard-based practices. The national standards on auditing were adopted in August 2000 and their use is obligatory for audits for year-end 2001. This is a major step in facilitating improved bank supervision and also increases the transparency of the banking system.

To support private sector growth, use of the national accounting standard and adoption of the national standards on auditing must become more widespread. However, the skills of the accountants and auditors thus far trained in the international-based standards are still too narrow to fully support the emerging private sector. These professionals require continued training in a wider range of accounting methodologies, such as agricultural and management accounting, in order to respond to the needs of entrepreneurs.

To help ensure the long-term supply of well-trained accountants, USAID supported the reform of the accounting curricula at Academy of Economic Studies-Moldova (AESM). This institution will turn out its first graduates in the new program in 2004. To further ensure the sustainability of accounting reforms, USAID supported the development of the Association of Professional Accountants and Auditors (ACAP). This organization has become one of the most prominent accounting and audit associations in the former Soviet states.

Phase-out activities: Between 2001-2003, USAID will support phases II and III of the banking strategy in order to develop the banking infrastructure and promote fundamental banking functions. Additionally, USAID will support activities which help ensure the sustainability of accounting reform and enable accounting reform to support Moldova's emerging private sector.

Specifically, USAID will provide technical assistance to strengthen the on-site supervisory capacity of the National Bank of Moldova. Assistance to the Bank Supervision Department of the NBM will strengthen inspectors' ability to assess the condition of individual banks, develop examination reports and follow through on ensuring that the recommendations in the reports are implemented. In addition, USAID will provide assistance for dealing with problem banks and building capacity within the NBM to carry out the problem bank function.

In late 2000, the IMF began working with the NBM to update both the Central Bank Law and the Law on Banks and Banking. USAID will provide technical assistance to the NBM to rework banking regulations so that they will be in conformity with amendments to the two laws. USAID will also provide targeted assistance in other critical areas, possibly including the development of a payment system, deposit insurance, external communications or similar activities that support infrastructure development. Capacity building for carrying out basic banking functions in areas such as credit mobilization and loan procedures will be built through training.

To assist the banks in meeting the new audit requirements for 2001 and to meet the needs of the private enterprise, USAID will support the expansion of the use of international accounting standards to include international standards of auditing and management accounting. To that end, USAID will provide training and technical assistance to help develop a cadre of certified professional accountants and licensed auditors trained in accordance with international standards and capable of providing financial management training and advisory services to entrepreneurs and business managers. This activity will be coordinated with USAID-funded activities which support SME development.

To ensure the sustainability of USAID's support for accounting reform, USAID will continue to support the institutionalization of both (1) a sustainable education program capable of producing a new generation of accountants and auditors fully proficient in the national accounting standards and (2) a self-regulatory organization that can promote accounting and auditing principles and train and support professionals, international accounting standards and international standards on auditing. To this end, USAID will provide continuing support for the development of a partnership between AESM and the University of Nebraska at Omaha which will facilitate an exchange program to enhance skills in teaching methodologies, to provide training on discipline-specific topics, to facilitate information and experience sharing, and to deliver general support and guidance. Additionally, USAID will continue to support institutional strengthening activities that will enable ACAP to make the transition from an NGO to a self-regulating organization and become institutionally and financially self-sufficient.

Impact and performance monitoring: Activities carried out in support of this intermediate result will have the following results:

- NBM regulations will conform with the Central Bank Law and the Law on Banks and Banking.
- The NBM will have the capacity to carry out on site and off site inspections, prepare reports and follow-up on recommendations.
- The use of international standards of auditing and management accounting will be fully implemented in the banking sector.
- A GOM-approved certified auditor program (in accordance with IFAC international education guidelines) will be established.
- AESM will be producing graduates ready to sit for their certification examination.
- ACAP will have been accepted by the GOM as a self-regulatory organization.

The impact of activities supporting this intermediate result will be monitored through:

- savings in financial institutions

- loans made by financial institutions
- membership in ACAP, disaggregated by gender

Linkages between the Fiscal and Financial Reforms and Other USAID/Moldova-supported Programs

Economic reform is linked to all other USAID/Moldova programs as it helps set the overall environment in which all other USAID programs are implemented. Without a stable, well-managed economy, the implementation and sustainability of the other programs would be in peril. There is a particularly close link between fiscal reform and the local governance program, as fiscal reform will be carried down to the local government level. Fiscal reform is also closely linked to the GOM's ability to provide financing for social services and social protection. Financial sector reform is linked to private sector development as it helps ensure access to investment credit and mobilizes savings. It also provides the accounting and auditing tools required by all entrepreneurs for managing their businesses and the legal framework that allows them to operate securely. As financial reforms make their way through the government structure, they contribute to improved local governance.

Commitment of Development Partners

USAID/Moldova's legal, fiscal and financial reform activities are closely coordinated with both the International Monetary Fund and the World Bank to ensure that technical assistance is provided in support of the fulfillment of loan conditions. This work is also coordinated with other U.S. government institutions and with other public and private international donor organizations active in Moldova to ensure commonality of objectives and policy approaches and to avoid duplication of effort. The GTZ and EU-TACIS also support financial sector reform in selected areas.

STRATEGIC OBJECTIVE 2: PRIVATE ENTERPRISE GROWTH CREATES JOBS AND GENERATES INCOME

The areas of intervention outlined in this section of this strategy contribute directly to the E&E Bureau's Strategic Assistance Area I: Economic Restructuring. They will help foster the emergence of a competitive, market-oriented economy in which the majority of economic resources is privately owned and managed. This strategic objective is linked with the E&E Bureau's SO1.1, SO1.3 and SO1.5, increased transfer of state-owned assets to the private sector, accelerated development and growth of private enterprises and a more economically sound and environmentally sustainable energy system.

Problem analysis: Moldova's economy faces many challenges, including dependency on an inefficient agricultural sector, a large informal economy, high rates of un- and underemployment, and a large external debt fueled by inefficient state-owned industries. In order to bring the benefits of a market-led democracy to the Moldovan people, sustainable and inclusive economic growth that provides the population with productive employment and income is needed. To fuel this growth and transfer state-owned assets to private hands, the restructuring of key strategic industries, particularly the energy sector and telecommunications, is necessary.

In its poverty alleviation plan, the GOM states that "sustainable growth in the medium term is likely to stem from the development of private sector activities in areas where the country has a comparative advantage. These areas are likely to include the agro-industrial sector, the small and medium enterprise sector and the service sector..." These are areas of the economy that were underdeveloped under the previous economic structure and provide opportunities for broad job creation that will increase income, reduce poverty and improve the standard of living for the average citizen. Furthermore, the growth of the private sector will support the development of civil society by helping to establish new democratic principles and institutions.

Agriculture plays a key role in Moldova's economy. Employing more than 40% of the economically active population, agriculture directly contributed over 25% of the gross domestic product in 1999 and agricultural processing added at least another 9%. Agricultural exports amounted to about two-thirds of all Moldovan exports in 1999. Most agricultural production now comes from private holdings. Most individual farmers, however, have had title to their land for less than two years and have just recently begun to operate their private farms as small businesses. Both land and labor productivity have fallen since the early 1990s. The production of nearly all commodities is well below levels of ten years ago. In the near future, it is anticipated that agriculture will continue to be a major employer and the source of most exports. Significant growth in this sector is critical to achieving overall economic growth.

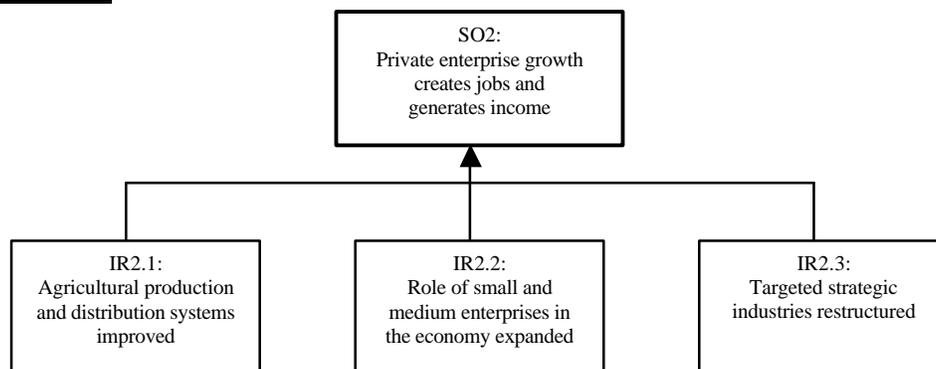
A recent baseline survey of small and medium enterprises (SMEs) in Moldova reported that an estimated 195,000 SMEs currently operate in Moldova, employing almost 40% of the population. 40% of these operate in villages and rural areas. As such, SMEs have the potential to play a vital role in ameliorating social issues associated with the economic transition by providing employment and income. Significantly, approximately 30% of the SMEs are owned or operated by women, with this number rising to 48% in rural areas. Hence, SME development will have a

positive influence in enhancing the economic role that women play in Moldova and help to further integrate women into the economic and democratic reform process.

While Moldova has made significant progress in privatizing its state-owned assets, key strategic industries such as the telecommunications sector and large segments of the energy sector remain in state hands. This is not only contrary to Moldova's goal of becoming a market-led economy, but also hinders broader economic growth. The energy sector, as the principal contributor to foreign debt, limits opportunities for improving Moldova's fiscal picture, absorbs government resources that could be utilized for social services and productive investments within the country, and negatively affects the investment climate for private entrepreneurs through its inability to provide adequate and reliable services. In addition, poor delivery of services has a negative impact on Moldovan's quality of life, while reliance on Russia as Moldova's principal energy supplier leaves Moldova politically vulnerable.

An unreliable and obsolete telecommunications sector constrains Moldova's economic growth by limiting public access to the information, technology and markets required by private entrepreneurs. Similarly, democratic development is hindered by people's inability to access information and freely communicate. Unless the telecommunications sector can be improved, Moldova's next generation will be unprepared for entry into the modern workforce. Lagging internet penetration and access prompted one telecommunications consultant to comment that "Moldova is on the wrong side of the digital divide." Restructuring and privatization offer the best hope for converting both the energy and telecommunications industries into positive assets for Moldova's transition.

Results framework:



Development hypothesis: Sound fiscal and financial management need to be accompanied and supplemented by a range of other institutional development and policy actions for significant market-led growth to create employment and income opportunities for the Moldovan population. The greatest opportunity for taking such actions and stimulating growth lies with private sector development, particularly within the agriculture and small and medium enterprise sectors. These two sectors reach the greatest percentage of the Moldovan population and offer possibilities for achieving significant returns with limited investments. Policy-level changes to improve the business environment are required to accelerate the process and to encourage needed investment. In addition, the institutions that support growth in these sectors need to be developed. For the

agricultural sector, the establishment and strengthening of backward and forward producer-processor-exporter links is feasible and will result in an expansion of marketing and production opportunities. SME development hinges on the strengthening of systems that can supply needed business services and that can represent SME interests. Private enterprise growth can be further stimulated through the restructuring of targeted strategic industries. Because the energy sector plays such a critical role in Moldova's economy, opportunities for growth are limited unless the energy sector can be reformed. Lacking in fuel resources, Moldova cannot become primary energy independent. However, there are sound approaches that can be followed to provide reliable, economic supplies of energy. Energy providers must operate as private enterprises, energy sources must be diversified and energy must be used more efficiently. Before the telecommunications sector can be restructured, capacity building within the newly established regulatory organization is essential.

Critical assumptions

- The GOM will remain committed to economic restructuring.
- Parliament will act positively on laws presented to it.
- The GOM will remain committed to agriculture and energy sector reform.
- The market environment in Moldova can be improved to stimulate both internal and external investment.
- The World Bank and IMF will remain engaged with programs that support both energy and agriculture sector reform and development. International financial institutions will continue to encourage investment by debt/equity support to new strategic investors.

Performance measurement: At the strategic objective level, the results of USAID's interventions will be measured by:

- the private sector's contribution to GDP
- the percent of the population employed by the private sector
- the number of people paying income tax

IR 2.1: AGRICULTURAL PRODUCTION AND DISTRIBUTION SYSTEMS IMPROVED

Problem analysis: The USAID-financed breakup of virtually all collective farms, the resolution of the farm debt issue and the distribution of agricultural land and property to hundreds of thousands of rural residents have established the fundamental base for a market economy. USAID's recent assessment of the constraints to agriculture and agribusiness development identified several factors, however, which inhibit this sector from leading Moldova's economic growth, including: a policy, legal and regulatory framework which does not support private agriculture, limited technical and management skills, few input/output markets, an undeveloped land market and limited availability of financial services.

Government rules and regulations continue to constrain agriculture sector growth. Multiple government agencies utilize abusive control practices that drive entrepreneurs into the informal economy. Regulations such as the three-year testing period before new agricultural varieties and new products can be registered for use in Moldova discourage the import and use of new technology and products. Export requirements are complicated and inconsistently applied. There

is no single government body charged with addressing these policy and regulation issues and public stakeholder input into the policy process is sporadic and limited. The development of a positive policy environment for private sector development requires that the GOM and private sector work together. The GOM must develop and implement a private sector strategy that revises policies, streamlines regulations, removes restrictions and simplifies procedures. This requires a rigorous review of existing legislation in light of sector goals and priorities; making recommendations and drafting legislation that promotes private enterprise growth; and developing and implementing regulations which enforce the new legislation. Such a strategy cannot be developed without input from those that implement and enforce the regulations (regional and local governments as well as other public institutions) and those that must comply with the legislation (the private sector).

Similarly, the tax system does not encourage economic growth nor provide the foundation for tax mobilization that will have the capacity to finance traditional government services. Instead, it helps drive potential taxpayers into the informal economy and discourages desperately needed local and foreign direct investment. Other legal obstacles to investment include excessive bribes to transport goods to an export market, complicated customs procedures, onerous multi-licensing and certification procedures, and multi-oversight of business practices by many government agencies. Restrictions on privatization have reduced foreign interest in certain areas.

Limited technical and management skills affect Moldovan farmers' ability to increase productivity and adopt new practices. Solid sources of information relative to new technologies, marketing opportunities, legal rights, etc. are still not readily available. New skills are needed not only by individual farmers, entrepreneurs and managers, but also by government officials involved in policy decisions affecting these groups.

Lack of input/output markets constrains entrepreneurs' access to the inputs needed to increase production as well as processors' ability to obtain the raw materials needed for processing. Following the farm break up and privatization process, input suppliers, most of which had been newly established after the break-up of the Soviet Union, did not have systems in place to provide thousands of small landowners with needed inputs. Neither did small private landowners have the financial resources to purchase inputs. USAID's initial experience with farm service centers and village stores suggests that there is a real demand for inputs available in small quantities in accessible locations. Similarly, agricultural output marketing, particularly at the farm level, is constrained by the low quantities and quality of produce from individual farmers. An effective chain linking producers to processors to markets needs to be created, with information, inputs and products flowing in both directions.

While the privatization of land was an important step in the development of a market-oriented agriculture sector, land consolidation is necessary. The development of a vibrant land market can encourage long term capital investment and provide capital for expansion. As of yet, the number of land transactions in Moldova is small and needed support institutions are under-developed. Appraisal services are available, but there is no common database of transactions or no uniform appraisal standards. Only a small pool of private land survey firms and land-transaction consulting firms exist. A long-term source of legal aid for landowners to replace current donor-funded programs is not available.

Short term credit for operating purposes and sources of medium and long-term credit for equipment and capital improvements and for the development of a land market and the long-term consolidation of land holdings are critical for agricultural growth. However, Moldovan farmers currently have very few options for accessing credit. Lending to this sector is severely constricted under current conditions of high interest rates, inflation and low sales prices for agriculture products.

First year activities: USAID's approach to helping accelerate the pace of growth of private agriculture in Moldova combines continued and special attention to policy reform with a focused set of activities aimed at giving the private sector the organizations, access, information, skills and inputs needed to capitalize on and function in an improved market environment. The strategy builds on the privatization, economic restructuring and policy reform that has already occurred, with the overall objectives of raising production, productivity, employment and incomes. Gender considerations will be integrated into all activities; ensuring that men and women both benefit from USAID support and that institution building includes gender awareness.

Under this strategy, USAID will continue to support and accelerate the policy reform process initiated earlier through a new Private Farmer Assistance Program. Importantly, the support will be broadened to ensure that local government is also reached. A high-level policy unit will be established to provide and promote improved policies to the government. Technical assistance will be provided to conduct economic and other analysis and to review and draft new laws, regulations and policies. Data collection and survey techniques will be used to ensure that the private sector participates and that its interests and concerns, including gender issues, are reflected in the policy development process. Specifically, USAID will provide technical assistance to conduct economic and other analysis, training, dissemination of information, policy reform coordination meetings, workshops and similar fora for bringing interested parties together. When relevant, activities will be coordinated with the Local Government Reform Project, the Fiscal Reform Project and SME development activities.

The development of input/output markets will be supported through the provision of assistance for the establishment of additional regional farm service centers and farm stores through a new Private Farmer Commercialization Project. Following the recent passage of a positive business services cooperative law, which could be a model for the E&E region, USAID will provide to the development of cooperatives that provide input/output services to private farmers. Additional assistance will be provided for the formation of farmer associations, the provision of legal and technical advice and information to small holders, the development of marketing channels at the farm and higher levels, the expansion of processor and exporter capability, and the building of processor ability to compete on international markets. Implementation of certain activities will be carried out in coordination with local government reform activities. Opportunities for facilitating the delivery of social services by helping communities access the World Bank and other donor-funded social services loans will also be explored.

To complement the strengthening of farm service centers, associations and cooperatives, USAID will also support nine regional agriculture offices. Other assistance will include agricultural newsletters, land problem solving and arbitration teams, providing information and training to farmers, farm store users, landowners and agricultural cooperative/association members. Special

technical and management skills development training programs will also be conducted. Processing/marketing managers and staff will be included in training programs.

In the short-term, USAID does not propose direct capital investment for expanding credit, although technical assistance and training are planned to expand the availability of financial services. The new Private Farmer Commercialization Program will continue to utilize funds and reflows from a completed USDA monetization program to support agribusiness activities and is seeking additional credit funds via the same mechanism. A memorandum of understanding has been negotiated between the GOM, the International Fund for Agriculture Development (IFAD) and a USAID contractor, that will closely link a new \$5.4 million IFAD credit program with the farm store and related work being funded by USAID. Some technical assistance is planned to strengthen, deepen and possibly expand savings and credit associations (SCAs) under the Micro-Finance Alliance and the new World Bank project (see below).

USAID assistance will target landowners' rights, including a continuation of legal support for small landowners through the legal problem solving and conflict mediation teams established under earlier USAID land programs. Limited assistance will also be provided in encouraging banks and possibly savings and credit associations to expand the USAID-supported purchase money mortgage programs. Further assistance will also be provided to complete any residual work for the privatization and registration of agricultural land in Moldova, including the regions of Gaguzia and Transnistria. Some technical assistance will be provided to complete the privatization of agriculture-related industries including wineries, tobacco processing and grain storage and related facilities. USAID will also review the need for involvement in land market development.

Impact and performance monitoring: By the end of the strategic planning period, it is expected that the following results will be achieved:

- The legal, regulatory and policy environment will better support private sector development (for agriculture, SMEs and industry) and investment in general.
- Mechanisms for incorporating feedback from local governments, the private sector and other interested parties will be institutionalized.
- Capacity within the GOM for drafting and reviewing legislation will be strengthened.
- Improved internal regulations and other subsidiary legislation will be implemented and operational.
- Cooperatives, farmer organizations and farm service centers will be offering input distribution, marketing and other services.
- Suppliers of business and agricultural information and services will be commercially viable.
- The advocacy capacity of agricultural associations and cooperatives will be stronger.
- Individual entrepreneurs and farmers will have higher technical and managerial skills.
- A higher level of technology enhancing input supplies will be available and accessible at a reasonable cost to thousands of small farmers and entrepreneurs.
- Additional processors, farm service centers and village level farm stores will have established linkages to small farmers.

Progress toward achievement of this intermediate result will be measured by:

- USAID consultant and other reports on the policy environment for business in Moldova, including tracking the passage of market-friendly legislation and regulations and the level of foreign investment inflows;
- the number of and membership in (M/F) agricultural cooperatives and associations providing services to their members;
- the number of rural producers (M/F) reached by the various training, legal and other USAID-supported activities;
- the number of farm service centers, farm stores and processing entities established or strengthened to provide input and marketing services to farmers; and
- the volume and number of real estate transactions, including enterprise land sales and land titles issued or transferred.

**IR 2.2: ROLE OF SMALL AND MEDIUM ENTERPRISES IN ECONOMY
EXPANDED**

Problem analysis: Over 73% of the small and medium enterprises operating in Moldova today, including those in the agriculture sector, were started in the last four years. While this dramatic growth indicates a positive trend in Moldova's movement toward a market economy, the fact that over 85% of the SMEs operate in the informal sector is cause for concern. Unless these enterprises are brought into the formal economy, an important potential sources of revenue is outside the GOM's reach, economic efficiency is not being maximized, and opportunities for Moldovan businesses to compete in the global economy are being missed.

Since the reorganization of the government in February 1999, the GOM has shown increased understanding of the key role that SME development can play in economic growth and, as a result, increased commitment to improving conditions for the SME sector. One major constraint to SME growth was overcome with the recent passage of new legislation that simplifies and expedites the business registration process. Businesses can now register in one day at one place, as opposed to the two to three month process that used to be required. Other new laws have also been passed that similarly have helped to stimulate the movement of unregistered activities to formal registration.

In spite of these positive changes, the legal, regulatory and policy environment continues to limit SME growth. In terms of national policy, all SMEs face the same constraints as private farmers operating in the agriculture sector. At the local level, issues related to implementation of the national policy frequently create a hostile environment for SMEs. Local government officials decide the degree and severity of enforcement of laws, the application of fines and the sanctions and granting of privileges such as access to business premises. As a result, there is a wide disparity in the business environment in different cities. Many local government officials neither understand how SME development can benefit their community nor know how to utilize current resources and legislation to maximize those benefits. At the same time, there are no mechanisms in place for businesses to lobby on their own behalf or otherwise participate in the policy-making process at the local, regional or national levels.

In addition to the poor policy environment, lack of adequate business skills is a serious constraint to SME growth both within and outside the agriculture sector. Most of the marketing, planning

and other business skills needed to successfully operate a small business in Moldova today were unnecessary under the former Soviet system of central planning. In the new open market economy, businesses of all sizes must learn to compete to survive. Entrepreneurs must be able to reduce costs, expand markets and increase profits. However, there are few local institutions able to provide businesses with quality training, technical assistance and business information. Those business service centers that do exist are relatively new and are located principally in urban centers, rather than in the rural areas where more than 44% of the SMEs are located. To compound this problem, many enterprises are unable to identify their training needs and remain reluctant (and often financially unable) to purchase the services required to upgrade their skills.

To expand (95% of the SMEs employ less than ten people), entrepreneurs must be able to invest in their businesses and engage in sound economic decision-making. However, few small entrepreneurs have access to affordable sources of credit. The majority of capital deployed in the SME sector is generated from the personal savings of entrepreneurs and their family and by retained earnings from business operations. The SME Baseline Survey found that only 14% of all SMEs applied for credit in the six months prior to the survey and that more than 77% of the credit originated from individuals, rather than from banks or other financial institutions. Banks in Moldova typically do not loan to SMEs and lack the skills necessary to build a successful SME-lending program. Furthermore, Moldovan SMEs do not usually apply for loans from banks because of stringent collateral requirements and high interest rates.

Under its strategy for the 1995-2001 period, USAID provided assistance to the Ministry of the Economy and key parliamentarians for drafting new laws facilitating the growth of SMEs both within and outside the agriculture sector. Support to business associations resulted in improved organizational development, information dissemination and increased lobbying capacity within the associations. The establishment of two business service centers helped to increase the skills of Moldovan entrepreneurs. USAID also supports a loan portfolio guarantee program with three Moldovan banks under which Agroinbank placed 66 SME loans and used more than one-half of its \$1 million coverage during the first six months of the program. Building on these achievements, lessons learned, and recent developments in Moldova, USAID is well poised to initiate a program of expanded, yet targeted assistance to SMEs both within and outside the agriculture sector.

First year activities: To help implement the SME strategy, USAID/Moldova plans to buy into the new BIZPRO project, which has recently been started in Ukraine. This will be in addition to the two major activities mentioned in the agriculture section above that will focus on agriculture-related SMEs.

Building on past achievements, USAID will capitalize on the GOM's interest in SME development and provide continued support for the policy reform process. Importantly, the support will be broadened to ensure that all levels of government are reached. Specifically, USAID will assist in the development and implementation of an SME strategy by supporting technical assistance, training, dissemination of information, policy reform coordination meetings, workshops and similar fora for bringing interested parties together. Furthermore, USAID will provide technical assistance in drafting new laws, regulations and policies. These activities will be carried out in coordination and working with the policy reform unit described in the section on agriculture, given that similar reforms are needed for both agriculture and SME development.

Business skill development for individual entrepreneurs, managers of SMEs and government officials involved in policy decisions affecting SMEs will be promoted as an essential prerequisite for the successful development of SMEs as well as for improving their level of competitiveness. In the past, USAID provided limited support for skill building through the creation and development of two business service centers and the provision of volunteer executives. Under the new strategy, USAID/Moldova will expand on these efforts and help to strengthen business associations and similar non-government organizations so that they can provide technical training for their members, offer a mechanism for sharing information and experiences, and build capacity in advocacy, thus allowing members to better participate in the policy-making process. USAID will also assist business service providers (firms and individuals that provide services for a fee) in becoming self-sustaining, financially viable private entities that provide technical and management skills support to entrepreneurs through the provision of information, training and advisory services in areas such as business plan development, accounting, bookkeeping, marketing, quality assurance, etc. It is anticipated that the system of work orders and vouchers, which provides for leveraged assistance to SMEs, as pioneered by USAID/Ukraine and partially implemented in Moldova, will be utilized.

USAID will also promote increased access to information for entrepreneurs and small businesses. Many of the policy-related activities discussed above (workshops, discussion sessions) will directly contribute to this effort. Support for GOM dissemination of information on public procurement and other business-related topics will also be provided. In addition, USAID will encourage business service providers to engage in more extensive outreach efforts, thereby reaching a greater number of rural inhabitants.

Moldovan SMEs need greater access to affordable sources of credit to be able to grow. Some potential approaches for USAID are discussed in the above section on agriculture. In addition, other donors are exploring options for microfinance. Under this strategy, USAID will strengthen ties with these other programs. Special emphasis will be given to help SMEs access various credit funds (WB, EBRD, IFAD and CNFA monetization), through commercial banks and saving and credit associations.

By the end of the strategic period, the following results will have been achieved:

- A legal, regulatory and policy environment more conducive to SME development will be in place.
- Mechanisms for incorporating feedback from local governments, the private sector and other interested parties will be institutionalized.
- Capacity within the GOM for drafting and reviewing legislation supportive of SME development will be strengthened.
- Business service provider outreach will be increased.
- The quality of services offered by business service providers will be improved.
- Business service providers will offer more services to entrepreneurs.
- The advocacy capacity of business associations will be stronger.
- More entrepreneurs will be requesting and receiving business skills training.

Progress toward achievement of this IR will be measured by:

- improvement of the policy environment (see the same indicators under IR2.1);
- access to market business skills and information;
- the capacity of business service providers; and
- access to credit.

IR 2.3: TARGETED STRATEGIC INDUSTRIES RESTRUCTURED

Problem analysis:

Energy sector: Moldova's energy sector has a long history of corruption, poor management, inefficient use and unreliable distribution. Electricity generation is currently only some 21% of installed capacity (this varies by generating unit) and there are commercial losses of up to 20% in the power distribution networks. Due to factors such as widespread non-payment, inefficient energy use and lack of investment, the system is not only financially unstable, but is also deteriorating. The failure of government-owned enterprises and government organizations to pay energy bills is a primary cause of foreign debt. In recognition of the depth of these problems, in September 1996 Government Resolution 478 ordered the development of a plan for economic restructuring of the energy sector, initiation of energy price increases, development of a new method for regulation of electricity, gas and heat prices, improvement of the social safety net and movement to settle payment arrears. Both the World Bank and IMF have actively supported energy sector reform and improved energy policy. World Bank loans to Moldova have been conditioned on progress in implementing reforms. USAID has played a key role in assisting the GOM to meet the conditionality.

Privatization has been a key element of energy sector reform. The privatization process underway is intended to move assets into the hands of private strategic investors (most likely international) with the expectations that they will establish commercial operations that will increase cash collections, reduce barter, make needed investments, implement modern management practices, and ultimately benefit the country both through improved service delivery and increased payment of taxes. The successful privatization of three of Moldova's five electricity distribution companies has thus far had the desired results. This now needs to be followed by privatization of the other two distribution companies and the three combined heat and power plants.

Electricity Sub-sector: As a result of GOM and donor efforts, between 1997 -2000 significant progress was made in the reform and privatization of the electric sub-sector, promising to break that sub-sector out of the cycle of non-payment, corruption and foreign and domestic debt accumulation. Key reforms include:

- Privatization of three distribution companies to Union Fenosa (Spain) was successfully completed, making Moldova the third country in the former Soviet Union to achieve this goal. Privatization of the remaining distribution and generation companies is now underway.
- Modern energy and electricity laws were enacted.
- The National Agency for the Regulation of Energy (ANRE) was established and has become a competent organization.
- Sound tariffs and licenses were established.

- The vertically-integrated electricity monopoly was broken into its constituent generation, distribution and transmission/dispatch units. Generation and distribution assets are slated for privatization.
- Humanitarian fuel supplies provided in the winters of 1998-99 and 1999-2000 included small, but effective, energy efficiency efforts that demonstrated a complementary approach to addressing sub-sector problems.

Since 1997, USAID has supported ANRE in becoming an independent, market-oriented and transparent regulatory body that can balance consumer and industry interests. Over the past three years, this agency has issued electric, gas and heat licenses and revised tariffs to maintain prices at cost recovery levels. It has also played a key role in the privatization process. However, there is steady and continuous pressure on the autonomy and authority of the ANRE. In order for energy reforms and privatization to succeed, it is critical that ANRE be capable of making sound economic regulatory decisions that strike a balance between sector and consumer interests in order to best serve national interests.

While three electricity distribution companies were privatized in 2000, further privatization needs to take place. At the time of this writing, a tender is underway to privatize the remaining two distribution companies and three thermal power plants. There is concern, however, because of the state of these plants and solvency of its largest customer, the Chisinau district heating company, Termocom, the tender may not result in their privatization. A review and revision of the privatization strategy may be required.

Gas and district heating sub-sectors: Progress in the gas and district heating sub-sectors has not been as positive as in the electricity sub-sector. Major obstacles, both outside and within Moldova, plague the gas sub-sector. As the meters for the Ukraine/Moldova exchange are located just inside the boundaries of the Ukraine, Moldova has no access to the meters and cannot verify Ukrainian figures. Within Moldova, the sub-sector has been unable to collect payment from its largest customers, the Moldovan combined heat and power plants. This contributed to Moldova being unable to pay its foreign gas debt. As a result, in 1999, a debt-equity swap took place in which Gazprom, the Russian gas company, gained a majority interest in Moldovagas. Now, with debt still rising, the Gazprom affiliated American joint venture company, Itera, is pressuring Moldova to relinquish its remaining 35% ownership in exchange for further debt forgiveness. Under these circumstances, reform is difficult.

The greatest challenge for the district heating sub-sector is customer non-payment, which has led to lack of investment and a continuous deterioration of the sub-sector. The Ministry of Environmental Protection and Territory Development recently estimated that 60% of the generated heating energy in Moldova is lost due to the distance between the power plants/boiler houses and the ultimate consumers, due to worn and heavily leaking underground piping, and because of energy inefficient buildings. The investment needed to renovate and modernize the sub-sector is enormous. With no mechanism for metering or disconnecting services to those who do not pay, prospects for privatizing this sub-sector and turning district heating into a financially viable enterprise are grim. (In spite of this, a tender is currently underway to privatize Termocom.)

Further complicating the restructuring of energy and utility enterprises is the recognition that commercial operation cannot be achieved without negatively affecting vulnerable groups within the population. As commercially run entities, the private enterprises will be unwilling to tolerate an accumulation of payment arrears by their customers. Payment enforcement through service disconnection will be practiced, while rising tariffs (to levels reflecting the full cost of service) will impose a heavy burden on vulnerable consumers. Rising dissatisfaction could result in lack of popular support for continued economic and democratic reforms.

Telecommunications: As part of its economic reform process, the GOM has committed to privatizing the national telephone company, MoldTelecom (MTel). This step will not only facilitate communication for economic growth, but will also reinforce democratic development by increasing opportunities for citizens to exchange views, access information and organize.

In order to help attract qualified strategic investors, the GOM agreed with the World Bank on several measures, including the establishment of a professional, independent regulatory agency. Under the previous strategy, USAID coordinated closely with the World Bank on privatization of this strategic enterprise and agreed to provide funding to support the regulatory agency, the National Agency for Regulation of Telecommunications and Informatics (ANRTI).

While the ANRTI was established during the previous strategic period, the regulatory regime required to assure transparency has not yet been established. As provided in the Telcom Law and other applicable legislation and regulations, a series of legal reforms need to be established for the ANRTI to become fully functional. These include, inter alia, internal regulations and other subsidiary legislation providing for a licensing regime, standards for new and existing services, equipment standards, dispute resolution mechanisms and an interconnection regime. In addition, technical and management skills within the organization are incipient.

First year activities:

Energy: Reforming the energy sector is an enormous undertaking requiring constant coordination between the GOM and the donor community. Through this coordination process, USAID has agreed to continue to support activities aimed at helping the sector to operate on a commercial basis, including privatization of the electricity sub-sector, improving and diversifying energy supplies, and supporting the World Bank in improving system efficiency.

Under this strategy, USAID will provide technical assistance in the development of new functions and systems at Moldelectrica (which is responsible for transmission and dispatch) to support the new contracting arrangements required by the decentralization of electricity market decisions to the distribution and generation companies. Additionally, USAID will participate in a working group that includes Moldelectrica, the ANRE and the Department of Energy to support the development of a least-cost plan which will provide a basis for assessing options for increasing and diversifying the electricity supply. USAID will support completion of the plan and will build capacity within the Department of Energy for managing implementation of the plan and engaging in a process of ongoing updating and modification of the plan.

Technical assistance will continue to be provided to support the institutional strengthening of ANRE and the development of a regulatory framework. Specifically, USAID will build, reinforce and broaden capacity within ANRE to deal with tariff and license issues as well as with new ownership issues not before encountered in a fully government-owned system. This will include heat energy as well as electricity. In addition, focused specialized assistance will enhance the regulator's independence, authority and equity towards consumers and the power industry alike.

USAID will provide assistance for the electricity market reforms that need to take place to strengthen the sub-sector's ability to attract investment and may continue to provide advice, support and technical assistance to the Department of Privatization.

USAID will support the World Bank's Energy II Project to upgrade metering, rehabilitate and upgrade the power system dispatch and communication, and carry out priority rehabilitation of the electricity transmission network by providing technical assistance for financial restructuring and corporate management as well as operational, institutional development and regulation of the electricity market.

As progress is made in the electricity sub-sector, USAID will coordinate with other donors to review opportunities for involvement in the district heating sub-sector. During the first year of this strategy, USAID will initiate this process by providing technical assistance to work with municipalities and institutions to enhance energy efficiency policy formation for district heating, assist in the development of effective and sustainable energy efficiency programs and projects at the municipal level and advise district heating companies on means of accessing and attracting international funds.

Telecommunications: USAID will provide assistance for building the ANRTI into a professional, independent regulatory agency. This assistance will basically mirror assistance provided to ANRE in the energy sector, as the ANRTI is expected to play the same critical role in the pre- and post-privatization of telecommunications that ANRE has played in energy privatization. Technical assistance and on-the-job training will be provided to build capacity within the ANRTI to establish and make operational the regulations, regimes, budgetary plans and other programs and policies require for ANRTI to sustainably operate as an independent regulatory body. Additionally, ANRTI staff will be trained in use of frequency management and monitoring equipment in order to assure fair competition among mobile operators and assure compliance with licenses for frequency-based services. Finally, USAID-funded technical assistance will work with the ANRTI to develop a "tool kit" for ANRTI use after assistance has ended. The tool kit will include model licenses and agreements and other resources to support ANRTI self-sufficiency. This activity is expected to end by December 2002.

Impact and Performance Monitoring: Activities supported under this intermediate result are expected to result in the following:

- The ANRE will be an active, highly professional, competent, well-trained and independent body which enables the attraction of strategic investors to the electricity and heating sub-sectors.
- Regulatory reporting requirements will be thorough and sufficient, but not burdensome, and will be fairly and uniformly applied.

- The two northern district heating companies will be privatized.
- If privatization of the three combined heat and power plants and the Chisinau district heating company has not taken place, they will at least be commercialized via a management contract.
- The least-cost plan will have been completed and capacity will exist within the Department of Energy to manage and continually modify this plan.
- Commercially viable energy efficiency investments will have been made in district heating in targeted municipalities.
- The ANRE will be involved in the World Bank Energy II Project.
- There will be increased capacity within the ANRTI.

Progress toward achievement of this intermediate result will be monitored by:

- cash collections for electricity;
- the energy intensity of the economy;
- commercial losses in the electricity sub-sector; and
- the establishment and implementation of internal regulations, standards for service, a licensing regime and a tariff setting regime for telecommunications.

Linkages between Private Enterprise Growth and Other USAID/Moldova-supported Programs

The ability of the private sector to grow and provide employment and income for Moldovans is clearly linked to achievements in the fiscal and financial sectors, particularly tax and policy reform. Banking reform directly supports private enterprise growth by providing a mechanism for saving and investing. Similarly, accounting reform will provide entrepreneurs and small businesses with the tools needed to keep records and make decisions based on sound financial information. Commercial law will help define the business relationships that the entrepreneurs will develop as they grow.

Private enterprise growth is also directly related to local government reform. Stronger local governments will provide a better environment for the market-oriented private enterprises. Conversely, the growth of private enterprise will reinforce democratization. Business associations, farmer owned and operated business service cooperatives, business service providers, and other private sector support groups are all forms of civil society organizations that represent the interests of their members. They all advocate for reform and/or the provision of services and otherwise engage in dialog with local/national governments in ways that reinforce democracy and demand accountability. Activities in these two areas will be closely coordinated.

There may be potential for linking agriculture activities with the delivery of social services. For example, villages could be helped to access the donor-supported Social Investment Fund. This might be done through farm stores and farmers' associations as well as through the nine regional agriculture offices. This possibility will be explored as activities are implemented.

Energy sector reform has direct implications for the fiscal sector. Energy and the social safety net are also linked. Energy reform is expected to negatively affect the vulnerable by increasing prices (in the short term) and by disconnecting services to those who cannot pay the new tariffs.

At the same time, privatization of the energy sector should free government resources for social protection. Energy sector reform is also linked to local government reform. Under the new legislation, local governments are responsible for supplying certain municipal services, including street lighting and heat. By assisting local governments to better manage the provision of these services, the burden on the energy sector will be reduced. Telecom reform supports democratic governance as more widespread, universal access to information leads to a citizenry that can communicate, organize and advocate. Furthermore, improvements in the energy and telecommunications sectors improve the daily lives of citizens, thus resulting in increased public support for Moldova's economic and political reform process.

Commitment of Development Partners

Agriculture sector: The EU-TACIS, IFAD/World Bank and IMF are all involved in agriculture and private enterprise development. EU-TACIS is supporting information development and dissemination as well as the improved marketing of agricultural products. In addition, TACIS has recently contracted for a \$3.0 million activity in agricultural education, research and advisory services. A second stage will focus on regional activities focusing on advisory services for agriculture and small-scale agribusiness. In addition to the IFAD \$5.8 million recently negotiated loan, the World Bank is preparing a new \$30 million rural investment and marketing project loan aimed at increasing rural incomes by promoting agricultural trade, diversification and productivity. Major components are likely to include market and advisory services, veterinary services and machinery and equipment services. As a follow-on to an earlier project, the World Bank is also expected to provide loan funding for a general credit line, a special credit line for newly formed farmer organizations, and micro-financing through the savings and credit associations. In the past the World Bank has worked closely with USAID's two land programs to provide assistance for rural land registration. The agriculture/rural sector has also been assisted through the Structural Adjustment Credit and Social Investment Fund projects. The International Monetary Fund has developed and signed a memorandum with the GOM, as well as approved a new \$150 million three year stand-by agreement that will make quarterly disbursements (about \$12 million) based on performance. USAID technical assistance will monitor certain aspects and help the GOM implement private sector and agriculture related aspects of this program.

Small and medium enterprises: The EBRD has supported SME development under two programs and is currently one of five shareholders for a new microfinance bank known as Micro Enterprise Credit (MEC). Other shareholders of MEC are the USAID WISNIS fund, IFC, KFW and Doone. TACIS has provided some assistance to SMEs in the past, mostly related to the agriculture sector. It is now planning additional activities, including one to foster SME development. The Moldova Microfinance Alliance (MNA) is one of the principle supporters of private enterprise development. This organization has received extensive assistance from the Soros Foundation and others.

Energy sector: The IMF and World Bank are highly committed to the energy sector. Over the years, energy has remained a key sector in the IMF program. The World Bank has supported the reform process from the beginning through its adjustment lending and conditionality. The Bank is now in the process of designing a new loan focused on strengthening transmission operations and is carrying out a district heating sector analysis. The EBRD and

International Finance Corporation are currently in the process of negotiating a program which would provide significant support for the privatization of the energy sector by providing equity and debt capital to the existing strategic investor.

Telecommunications: The World Bank is the lead donor in privatization of the telecommunications sector.

STRATEGIC OBJECTIVE 3: MORE EFFECTIVE, RESPONSIVE AND ACCOUNTABLE LOCAL GOVERNANCE

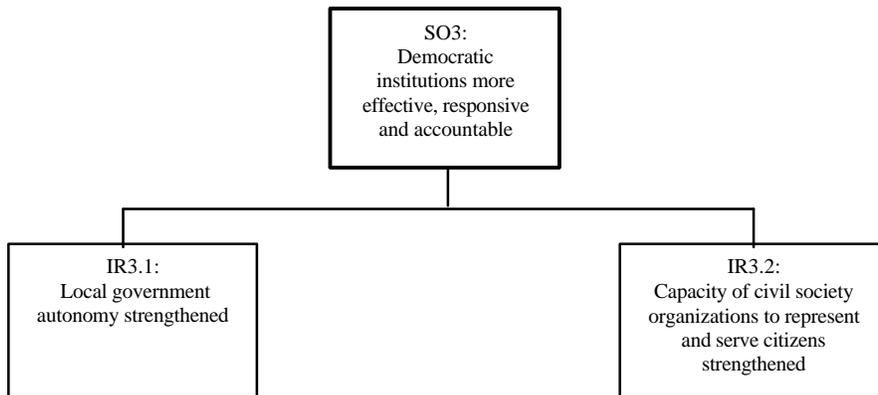
The activities described in this section of the strategic plan contribute directly the goal of E&E Strategic Assistance Area II: Democratic Transition, “to foster democratic societies and institutions through empowerment of citizens, independent media, rule of law and good governance.” The strategic objective is linked to E&E Bureau’s SO2.1, increased, better-informed citizens’ participation in political and economic decision-making, and SO2.3, more effective, responsive and accountable local governance.

Problem analysis: When USAID/Moldova developed its strategy for 1997-2001, encouraging the involvement of citizens at the grass roots level was identified as the area in which USAID could best support Moldova’s democratic transition. The recent passage of new laws on local government, however, led to a reexamination of this emphasis. It appeared that the GOM’s willingness to reform local government offered a target of opportunity that should be exploited. To assess the potential for USAID involvement in the reorganization and reform of local government, a study of local government needs was carried out and several key areas in which USAID assistance could make a marked impact were identified. As a result, it was decided that USAID/Moldova’s new strategy should include support for local government reform.

At the same time, it was recognized that there is a continuing need to foster greater citizen participation in Moldova’s social and political decision-making. While Moldovans are free to associate and voice their opinions, they do not have a history of involvement in the political and social decisions affecting their lives. There is a strong need to build civic activism to press for democracy from below. The rapid expansion of civil society organizations (CSOs) since independence is an indication that Moldovans are interested in and willing to organize around a topic of common interest. The capacity of many of the CSOs is limited, however. To capitalize on Moldovan’s interest in CSOs as well as USAID’s comparative advantage in supporting the strengthening of non-governmental organizations, USAID/Moldova concluded that support for building the capacity of CSOs should play an important role in its new strategy.

This strategic objective therefore focuses on building effective, responsive and accountable *democratic institutions* as a means of bringing government and citizens together in a positive relationship. In terms of government, the strategy focuses on assisting local government to play a positive role in Moldova’s economic and political transition by strengthening the autonomy of local government administration while building management capacity among elected local officials. At the people-level, activities are focused on strengthening civil society organizations (CSOs) that protect citizen’s rights and represent their interests.

Results framework



Development hypothesis: For citizens to benefit from Moldova’s democratic transition, public and private democratic institutions must become more effective, responsive and accountable. As the level of government most likely to impact the lives of ordinary citizens, local government can play a particularly critical role by providing concrete evidence that priority community concerns can be effectively addressed through local government initiative and citizen participation. For this to happen in Moldova, the new legislation providing for local government autonomy must be augmented and implemented. Of particular importance is the achievement of fiscal autonomy at the local level. Local governments will not be able to meet the needs of their citizens, nor provide the services for which they are now legally responsible, without access to own-source revenues. In addition, the management and technical skills of elected officials must be strengthened. To fulfill their role in democratic governance, citizens must be actively involved in political and social decision-making. Within Moldova, where there is not a culture of political involvement, strengthening civil society organizations so that they can represent and serve their constituents is an effective means of fostering a positive relationship between citizens and government.

Critical Assumptions

- The GOM will continue to be committed to decentralization and local government reform.
- Elected local government officials will be committed to reform.
- Citizens participation in political and social decision-making will be unhindered, i.e. there will not be political intimidation, NGOs will be allowed to flourish, free and fair elections for local officials will be held, etc.
- NGOs will advocate on behalf of their members.
- Citizens will join NGOs to advocate for their interests.

Performance Measurement: At the strategic objective level, impact will be measured by citizen participation in decision-making in target cities. The pilot projects in the target cities are expected to bring together the elements set forth in the results framework: Local government autonomy (including fiscal autonomy and improved management) and stronger CSOs which represent, inform and serve the public. Increased citizen participation in decision-making in the target cities will indicate that the cities have enough fiscal autonomy to make independent decisions about their budgets and strategic plans, that elected officials are aware of the

importance of participation and that citizens believe that participation is important and have been mobilized to play a role in their local government.

IR 3.1: LOCAL GOVERNMENT AUTONOMY STRENGTHENED

Problem analysis: The Law on Administrative and Territorial Organization was passed by parliament in December 1998. Its passage initiated local government reform by redrawing regional boundaries and reducing the number of regions in the country. The Law on Public Administration, passed by parliament in 1999, continued the reform process by establishing and regulating the organization and functioning of public administration in administrative-territorial units. This second law adopted a dual approach to local government reform. First, it strengthened the state administration and sought to improve central government efficiency through *decentralization*. Second, it promoted local government *autonomy* through the transfer of power and responsibility to the local level.

The law paved the way to decentralization by authorizing the president to appoint (based on the suggestion of the government) a prefect, or head of state administration, for each of Moldova's eleven regions and the Chisinau municipality. The law gives the prefect responsibility for the administration of the public services provided by ministries, departments and other central bodies in his/her respective administrative-territorial unit. Local government autonomy was provided in the law through the transfer of power and responsibility to local public authorities in villages and towns and to the mayors in cities. These elected officials are now legally responsible for provision of certain municipal services, including primary and secondary education, public health and public transport.

The new law essentially puts local public administrations on an equal footing with regional public administrations. However, while decentralization to the regional government is moving forward, implementation of local government autonomy is not taking place. As of yet, no transition mechanism, implementation plan or specific support for implementing this aspect of the law exists. Unless it is implemented, there is a strong potential that the Law on Local Public Administration will have the unintended consequence of reinforcing central government authority—without local government autonomy being realized.

In addition to lack of implementation of the Local Public Administration Law, fiscal dependency seriously constrains local government autonomy. Local governments have traditionally depended on shared revenues and transfers from the central government for over 75% of their budget. The new Law on Local Public Finance was passed in late 1999 to change the intergovernmental fiscal picture. However, while the intent of this law is clearly to provide for fiscal autonomy, the law has yet to be interpreted and implemented. This leaves local governments legally responsible for a series of unfunded mandates, without the authority or systems in place to efficiently generate their own revenues.

The lack of regulations and implementation mechanisms for devolving to local government the newly specified powers and authorities is common to all the new legislation. Furthermore, because the local government reform legislation represents a completely new way of carrying out government affairs in Moldova, the structures, processes and systems through which actual implementation of the legislation will take place have not been developed. Similarly, no process

for involving citizens in the drafting, revising, updating and amending of laws has been institutionalized.

Historically, local government in Moldova has been weak, with public services being managed by the center. Under the new legislation, local governments now have legal responsibility for a variety of administrative responsibilities and the provision of services for which elected local officials¹ do not have the technical or management skills. A series of rapid assessments identified strategic planning, finance and budgeting, social service and communal service delivery, economic development and asset management as critical skills currently lacking. The inability of local governments to take advantage of their new autonomy to create a positive environment for SME growth that could provide employment and stimulate local development is one example of officials' limitations. Furthermore, most local officials do not understand the benefits of citizen participation nor know how to constructively engage the citizenry in decision-making processes.

Since 1998, USAID has been providing technical assistance to help the GOM initiate the process of fiscal decentralization. As a result, both the Law on Local Public Finance, which reformed the financing of local government and the relationship between each level of local government and the central government, and the Law on Public Patrimony, which clarified the ownership of state property by the various levels of government, were passed in 1999. Other legislation, particularly the Law on Property Tax, which will provide a stable and efficient source of financing for local government, has not yet been passed.

First year activities: Given the limited human and financial resources available for local government activities, USAID will focus support for empowering local government on continuing the process of policy reform, on implementing fiscal decentralization and on improving the management capacity of elected local government officials. The emphasis will be on strengthening local governments as both democratic and service providing institutions.

Under this strategy, USAID will provide technical assistance to parliamentary working groups, the Ministry of Finance, the Ministry of Economy and other administrative bodies in (1) reviewing existing laws and regulations to ensure that a sound, transparent legal framework for local government is in place, (2) drafting and amending legislation as appropriate; (3) preparing regulations that will guide implementation of laws and amendment; and (4) developing implementation mechanisms for laws, including a strategic plan for implementation and the creation of needed local government bodies. The importance of citizen participation in the policy-making process will be emphasized and mechanisms for soliciting feedback and using this feedback to review and amend laws will be established.

In coordination with activities aimed at strengthening local government management (see below), pilot centers will be established in four cities and the Chisinau municipality. Within these

¹ Under Article 118 of the Electoral Code of Moldova, the mayors of towns and villages as well as town and village councils are freely elected by popular vote. Candidates can run either as a member of a political party or as an independent. Significantly, these elected local officials truly represent the communities in which they serve, whereas members of parliament are selected at large.

centers, local treasury systems, tax administrations and budget offices will be established and made operational. The pilot centers will serve as models for replication in the following years.

USAID will provide technical assistance for strengthening the management and administrative capacity of elected local officials in target cities and towns² through on-the-job and other training. The Local Government Reform Project is currently establishing three pilot centers to support the implementation of local service improvement projects (projects are identified through proposals received from cities in the pilot areas). During the first year of this strategy, mayors and local councils in the cities selected for a municipal service improvement project will receive training in skill areas identified by rapid assessments. They will then immediately apply these skills in implementing their local project. Through this hands-on approach, the effectiveness of the training will be maximized and officials will be more able to apply their new skills to the management of other municipal services. At the same time, officials will learn to incorporate citizen participation into the budgeting, planning and implementation process. A formative evaluation of the pilot centers and the projects implemented will be conducted in late 2001 and used as the basis for replicating and expanding to other areas.

USAID-provided technical assistance will also work with elected local government officials to help strengthen ties between elected officials and citizens, to operate more transparently and to establish mechanisms for encouraging citizen participation in decision-making processes. The use of public meetings, hearings and similar fora will be explored, as will the concept of gender awareness.

Activities to improve local government management will be coordinated with programs that support private enterprise development. In particular, training in strategic planning, budgeting and incorporation of citizen participation will raise awareness of the need to create a local environment supportive of growth, including incentives for attracting investors and means of directly supporting SMEs.

USAID will also support capacity building in the judicial system, with an emphasis on supporting local government autonomy through activities such as the provision of information on the Law of Local Public Administration and the Law on Local Public Finance for judges, lawyers and financial managers. Initial efforts will be targeted at the cities in which the Local Government Reform Project is carrying out pilot programs. Limited support for improving access to the judicial system, particularly in the areas of human rights and women's rights, will also be funded. These activities will help to protect vulnerable groups within the population through raising awareness of trafficking, helping to inform women of their rights and training women on how to assert their rights in court.

Impact and monitoring: Activities supported under this intermediate result will result in the following:

- Legal reforms devolving fiscal autonomy to local governments will have been enacted.

² Cities and towns, rather than municipalities, have specifically been selected targeted. In Moldova, a city or town must meet certain criteria before it can become a municipality. There are only a total of 13 municipalities in the entire country. By focusing on cities and towns, USAID-supported activities can include municipalities, but can also reach out to a broader range of reform-minded local officials.

- Implementation mechanisms for the new laws will have been developed.
- The institutional structures, processes and systems required to support implementation of more fiscal autonomy laws will be in place and operational in target areas.
- Citizen input will be incorporated into the legislative-making process.
- A process of soliciting feedback and using this feedback to review and amend laws will have been established.
- Targeted local governments will have improved technical and managerial capacity.
- Units of local government will be able to plan, organize and operate the delivery of social and communal services with responsiveness, quality, efficiency and effectiveness.
- Targeted local governments will take steps to provide an improved environment for SME development.
- Targeted local governments will regularly provide opportunities for citizen participation in local decision-making.
- The judicial system will better support local government reform in the target areas.

The impact of USAID-supported activities in fostering local government autonomy will be tracked by:

- the number of target localities with operational tax offices, budget offices and/or treasury offices;
- the number of target cities implementing their strategic plans;
- the number of people receiving training on the Law on Local Financing and the Law on Local Public Administration; and
- the number of households receiving utility services (such as garbage/solid waste disposal, water, district heat) from local governments in target cities. Under the new legislation, local governments were given responsibility for the provision of these services. An increase in households served indicates that local officials have not only been trained in managing the services, but are also putting their training to use to respond to the needs of their constituents.

IR 3.2: CAPACITY OF CIVIL SOCIETY ORGANIZATIONS TO REPRESENT AND SERVE CITIZENS INCREASED

Problem analysis: A functioning democracy involves not only functioning government structures, but also an active citizenry. A healthy exchange between those who govern and the governed is essential. However, not only does Moldova not have a history of active involvement of people at the grass roots level in political and economic decision-making, but also recent opinion surveys suggest that citizens' mistrust and/or apathy toward local government is endemic. Under these circumstances, strong civil society organizations that focus on good governance issues can play a critical role in facilitating dialog and positive interaction between government and citizens at all levels while also empowering citizens to make decisions affecting their political and economic futures..

The development of local government and professional associations, including three associations of mayors, are indications of Moldova's citizen's interest in organizing around subjects of interest to achieve a common goal. This theme is further reflected in the steady increase in the number of NGOs registered in Moldova. By 1999, over 1500 NGOs had registered at the national level and some 250 had registered at the county level. As a result of an NGO lobbying

campaign among parliamentary deputies, Moldova has a well-developed legal framework for NGOs and a tentative partnership between NGOs and government officials is beginning to grow. While this is a positive trend, the effectiveness of many of the NGOs is constrained by their relative weakness. A recent NGO sustainability assessment gave Moldovan NGOs an overall development rating of 4.6 (with 1 being high and 7 being low). The index's high mark for Moldova's positive legal environment, however, hides the low marks received for financial viability, advocacy, public image and service provision. The index reported that many new NGOs are operated by leaders with little experience in managing an NGO and are dependent on donor funding for financing their operations. Unless these organizations are able to strengthen their institutional structures, build capacity among their members, develop financial management skills and improve their public image, many will not be able to effectively serve their target audience. Specifically, they require increased capacity in areas such as strategic planning, policy research and advocacy, member services, financial planning, fund raising, information systems and organizational management.

Many of Moldova's non-governmental and civil society organizations engage in service provision rather than civic activism or good governance issues. Experience indicates, however, that many good democracy-building consequences can flow from work with social service groups. Support for such groups often helps to identify and mobilize active citizens that can serve as role models for others. Also, members of social service organization frequently discover the need to become proponents for legislative and regulatory reforms for their beneficiaries and thus widen citizen participation and reinforce citizen rights.

Under its Strategic Plan for 1997 – 2001, USAID/Moldova supported activities geared toward increasing citizens' participation in political and economic decision-making by supporting the provision of more unbiased information to citizens, the electoral process and an increase citizen confidence in the political and legal processes. During that period, the number of NGOs doubled; the laws on elections procedures were revised and adopted; and training for judges, lawyers and the media was held. In addition, USAID supported a program that made small grants to public, private and non-profit organizations to facilitate the transition from a centrally planned to a market economy, encourage improvement of public service delivery, foster greater citizen involvement in civic decision-making and improve the flow of information to citizens. An underlying theme of these grants was improving the management of the organizations. In conjunction with USAID/Ukraine and USAID/Belarus, an assessment of non-governmental and civil society organizations will be carried out shortly to provide guidance on how best to support NGO development in the Moldova context.

First year activities: USAID/Moldova will build on institutional strengthening activities initiated under its previous strategy and continue efforts to build civic organizations as a vehicle for engaging citizens in political and economic decision-making and pressing for democracy from below. The emphasis will be on building capacity within local NGOs and local government and professional associations (such as the associations of mayors, the Women Judges' Association and the Federation of Regional and Local Authorities) to increase public support of local government reforms and foster civic activism at the local level. Relatively less emphasis will be placed on capacity building within more broad-based democratic institutions (court system, media), always linking this type of support to local government reform.

Under the Local Government Reform Project, an assessment of local NGOs is being undertaken to identify and analyze the capacity of active NGOs which promote local civic and political activism and support improved local government performance. Initial capacity building training and technical assistance will focus on those groups promoting knowledge of the newly passed local government reform legislation and its ramifications for democratic local governance. The Local Government Reform Project will work with the mayors' associations, local NGOs and civic groups to produce training materials on local government reform and hold dissemination seminars.

USAID will also provide assistance for training local government associations, professional associations, legal associations and NGOs to deliver technical assistance and training to their members, increase the capacity of these organizations to advocate, and, where appropriate, train them to train local officials. NGOs that represent women and women's issues will be included in the training and dissemination seminars will include women.

To complement the above efforts, USAID will continue to support capacity building among a broader spectrum of NGOs. Small grants will be provided to NGOs to implement programs that support USAID's overall strategy, including agricultural development, SME strengthening, information dissemination, citizen participation, transparency, human rights, citizen's rights and other similar topics. NGOs receiving grant funding will also receive organizational development and management assistance.

By the end of the strategic planning period, it is anticipated that the following results will have been achieved:

- There will be an increase in the number and commitment of the member and client base of CSOs and associations that work for local government reform, whatever their larger purpose.
- There will be an increase in the number of CSOs expressing citizen views and interest in local issues.
- Indigenous CSOs and associations will begin to monitor and analyze reform agendas and other legal issues pertaining to local government and use their analyses to advocate for reform and to educate the citizens.
- The three mayors' associations will regularly sponsor public meetings to discuss new laws and policies and to disseminate information.
- The associations of mayors will offer some form of regular training for new members in public administration, financial management and other areas of interest to local officials.
- In target areas, the public and local officials will be well versed on the local government reform package and its implications for their communities.

An increase in the capacity of CSOs will be measured by the number of target CSOs completing education and training and implementing pilot projects.

Linkages between Democracy-building and Other USAID/Moldova-supported Programs

As already described, fiscal reform activities are an integral and essential aspect of local governance. Achievement of local government reform will directly contribute to private sector growth. As local governance improves, the legislation supporting private sector development

will be better implemented at the local level. Furthermore, improvements in the delivery of municipal services will facilitate the development of small and medium enterprises.

Improved efficiency in the delivery of municipal services is also linked to USAID's energy sector reform program. Many of the services provided by local government are in the energy sector.

Capacity building for CSOs, particularly for those that provide services to vulnerable groups, is directly linked to USAID's social safety net objective. As CSOs become better managed and more financially viable, they will be able to provide increasing services to those in need.

Commitment of Development Partners

A number of other donors are interested in local government reform in Moldova. While the USAID program supports democratic reform at the central level and local level, the UNDP and EU-TACIS programs focus on improving central government efficiency through decentralization at the regional level. The World Bank, the UNDP, the Swedish Agency for International Development and the Soros Foundation also operate programs and activities at the local level.

In the past, frequent communication between donors has resulted in the sharing of resources, such as research findings, publications and training materials. Reciprocal participation in training and conferences and complementary selection of clients, participants and special initiatives is also common. This type of excellent cooperation between donors is expected to continue, particularly in the area of CSO strengthening.

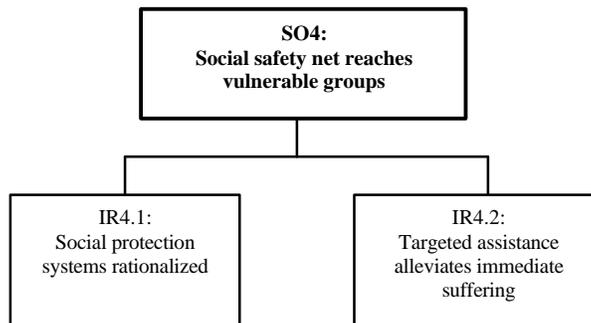
STRATEGIC OBJECTIVE 4: SOCIAL SAFETY NET REACHES VULNERABLE GROUPS

The activities described in this section of the strategic plan contribute directly to the goal of the E&E Bureau's Strategic Assistance Area III: Social Transition, "Enhance the ability of all persons to enjoy a better quality of live within market economies and democratic societies." The strategic objective is linked to the E&E Bureau's SO3.1, strengthened humanitarian response to crisis; SO3.2, increased promotion of good health and access to quality health care; and SO3.4, mitigation of adverse social impacts of the transition to market-based democracies.

Problem Analysis: As clearly articulated in the "Social Needs" section of Part I of this strategy, Moldova's transition to a market economy has placed a heavy burden on the social sector, with the standard of living declining over the past ten years and the number of vulnerable households rising. At the same time, limited resources constrain the GOM's ability to adequately respond with a social safety net for vulnerable groups. The need for social protection exceeds what the current system can deliver. Opportunities for improving the efficiency with which resources are used must be sought. In addition, institutional development of qualified local social service and rescue NGOs needs to be built.

Because of natural and manmade disasters and the inability of the social protection system to reach its targets, members of vulnerable groups in Moldova are suffering. Many are going with little food, clothing, heat or medical attention. Targeted assistance programs are needed to alleviate this suffering.

Results framework



Development hypothesis: Given the GOM's lack of funding for a social safety net, it is imperative that the limited funds available be accurately targeted to the most vulnerable and used as effectively as possible. Rationalization of the GOM's various social protection systems will help ensure that the systems are fiscally sustainable and reach the most vulnerable. Targeted programs can alleviate suffering when the social protection system is inadequate or when disasters and other unexpected circumstances cause hardship.

Critical assumptions

- The GOM will continue to be committed to social protection.

Performance measurement: Achievement of this strategic objective will be measured by the number of beneficiaries of USAID-supported programs, disaggregated by institution and individual (M/F).

IR 4.1: SOCIAL PROTECTION SYSTEMS RATIONALIZED

Problem analysis: Many Moldovan households are extremely cash-poor and lack the resources to cover their essential needs, including basic energy and utility services. The GOM's social protection system is unable to meet the needs of this growing group. The system has relied on pensions supplemented by poorly targeted and, to a large extent, under-financed benefits and privileges. It is estimated that over one-third of Moldova's population enjoyed privileges in 1998, accounting for approximately 8% of GDP that year. Reform of the system is essential so that limited funds are used efficiently.

In its poverty reduction strategy, the GOM recognized the need for reform of the social protection system and included this as one of the strategy's three pillars. The goal is to design a social assistance system that is transparent, fully funded, fiscally sustainable and well targeted. Initial steps have been initiated. In 1999, with assistance from the World Bank, the GOM embarked on a major reform of its pension system. In 2000, it attempted to rationalize utility subsidies by abolishing energy-related privileges issues in the past by law or government decree and approving a category-based subsidy scheme. It recognized, however, that this was an interim scheme that would require further rationalization. Several other social assistance benefit programs must also be redesigned to better target the vulnerable. These include the cash benefits program for families with children, unemployment assistance, disability benefits and utility subsidies.

Given USAID's involvement in energy sector restructuring and the anticipated impact of the restructuring effort on the vulnerable, USAID/Moldova has a strong interest in the energy subsidy scheme. As the energy sector is restructured, the human cost of the reform will be high unless measures are undertaken to address the issue of affordability to low-income consumers. As commercially run entities, private energy enterprises will be unwilling to tolerate payment arrears by customers and will enforce payment through disconnection of services. This has not only humanitarian consequences, but also the social consequences and popular dissatisfaction that might arise could jeopardize the future of this sector's reform, as well as reduce support for broader economic reforms in the country.

The interim utility subsidy scheme approved by the GOM in 2000, while significantly improving the previous system, targets support at the most needy *categories* of households. The scheme identifies a limited set of categories of the population based on demographic characteristics, then provides for assistance to be delivered based on a percentage of fixed consumption norms. Inevitably, there are inclusion and exclusion errors. In order to be able to better target its limited resources, the GOM has expressed a desire to develop an alternative approach to beneficiary targeting based on *means testing*.

First year activities: USAID will support the development and implementation of a two-year pilot program which will: (1) provide nominal targeted compensations for electricity

consumption in conjunction with current Moldovan legislation; (2) conduct a rigorous analysis and presentation of options for the transition to a system of social assistance recipient identification based on gender-blind means-testing; and (3) complete an assessment of information technology systems within the Ministry of Labor, Social Protection, and Family and procure the information services and systems equipment to facilitate implementation of social assistance delivery improvements according to this assessment.

Impact and monitoring: By the end of this pilot effort, it is expected that the following results will have been achieved:

- A viable, gender-blind scheme for using means testing to identify public benefit/compensation recipients will have been developed and approved by the GOM/Parliament as a modification to the current Law on Targeted Compensations.
- The capacity of the GOM to compile, maintain and manipulate data on rolls of public benefit recipients will be strengthened.
- Homes of a limited quantity of vulnerable households will be weatherized.
- Designated compensation funds will have been disbursed to vulnerable households.

In the longer term, it is expected that, if the means-testing approach works for targeting energy assistance, it will be adopted as a means of identifying benefit/compensation recipients for other subsidized social assistance programs.

Achievement of the intermediate result will be indicated by reforms in the social protection system adopted by the GOM.

This program is closely linked with USAID's support for energy sector restructuring. It responds to the increased social hardship that the restructuring program will cause.

IR 3.2: TARGETED ASSISTANCE ALLEVIATES IMMEDIATE SUFFERING

Problem analysis: Suffering in Moldova can principally be attributed to two causes: natural or manmade disasters and social problems caused by the economic and political transition coupled by the inability of the social protection system to adequately reach victims.

The suffering caused by natural and manmade disasters are clear to see. In the past few years, drought, ice storms, floods and windstorms have caused immediate hardship for people in the affected areas. In most cases, immediate, relatively short-term assistance can alleviate this type of suffering.

The suffering caused by Moldova's economic and political transition is much more insidious, with those affected spread throughout the country and often hidden from sight. Those affected include:

- cash-poor families who are unable to seek appropriate medical attention, especially pregnant women and their unborn children;
- women who cannot find employment and are vulnerable to trafficking; and
- institutions such as hospitals, boarding schools and orphanages which are not receiving payments from the state and are unable to purchase food and energy supplies.

In the past, USAID and other U.S. government agencies have supported programs to alleviate the suffering of these vulnerable groups:

Disaster programs have provided immediate humanitarian assistance such as medical supplies, ready-to-eat meals, clothing, blankets, generators and similar goods to disaster victims.

Programs providing **routine assistance to vulnerable** groups have mainly targeted hospitals, orphanages and other institutions. However, in 1999, when the Farmers' Association of Moldova demonstrated need for items such as tractors, tents and trailers in order to increase productivity, USAID's grantee was able to respond with the needed supplies. Significantly, for every USAID dollar provided for this humanitarian assistance, \$15-20 of assistance has been leveraged, greatly increasing the number of vulnerable reached.

Weatherization programs, which increase energy efficiency at selected sites, have been carried out as complements to USAID's 1998-99 and 1999-2000 Winter Heat Assistance Programs. In the first year, eight needy institutions and one residential complex, totaling twenty-seven buildings, were reached. In the second year, an additional forty institutions, including half of all orphanages and boarding schools requesting assistance through the Ministry of Labor, Social Protection and Family, were weatherized. An impact assessment of the first program showed positive quantitative and qualitative results, including an increase in indoor temperature in the weatherized buildings and increased cost savings. As consumers are increasingly required to pay in cash in full, measures that reduce consumption offer the hope of significant savings for all customers.

Women's health initiatives have received USAID support since 1993. In 1997, this support resulted in the opening of the Dalila Women's Wellness Center as a hospital partnership. Existing programs, administrative structures and professional relationships in the areas of family planning, health education and clinical and management training in obstetrics and gynecology were utilized. The center has filled a critical gap in the medical services provided to women in Chisinau, serving more than 20,000 women in a two-year period. Treatment and information on a wide range of issues, including contraceptives, STI/HIV/AIDS, menopause and partners in birth training have been delivered. Similar services are desperately needed in other areas of Moldova, where the economic and social transition has had an even more adverse impact on health care.

For several years, Moldova has received **food aid** or "monetization for humanitarian purposes" from USDA through section 416 (b). This assistance is used for monetization to run a food aid program focused on vulnerable pensioners and others, including orphanages and hospitals. In addition, a proposal for a school lunch program has been approved under the new Global Food for Education Initiative and is expected to start later this year.

While USAID has had no direct involvement in **anti-trafficking** activities, it participates in the U.S. Embassy's working groups on anti-trafficking and follows activities supported through other U.S. government offices. The Southern Europe Crime Initiative representative in Moldova, who deals with customs and border security, works with INTERPOL to intercept illegal emigrants, who are often trafficking victims. The Bureau for Drug Enforcement and Narcotics Interdiction provides training for the Moldovan police on trafficking and will soon open an anti-trafficking

center in cooperation with the UNDP. The U.S. Embassy's Public Affairs Office has provided a small grant for anti-trafficking, with an emphasis on reintegration counseling and job training for commercial sex workers. An embassy small grants program is producing two documentaries and television and radio spots to use in public education and is conducting a survey on trafficking. Moldova's Peace Corps training program also includes a trafficking awareness component.

First year activities:

USAID will continue to support basic humanitarian efforts, both disaster-related and routine, which target the vulnerable and strengthen the capabilities of service organizations that provide critical humanitarian and related development aid. It is expected that USAID's humanitarian assistance will continue to be channeled through the Counterpart Humanitarian Assistance Project (CHAP). CHAP has a history of successfully distributing aid in Moldova. Significantly, CHAP has demonstrated great flexibility in responding to the needs expressed by social service providers. It appears that requests in the near future will center on medical equipment and pharmaceuticals.

USAID will continue to weatherize needy Moldovan institutions. Those orphanages and boarding schools which requested, but have not yet received assistance, will be reached and weatherization of hospitals will continue. To encourage the sustainability of weatherization efforts, USAID will provide one to two years of training for energy service companies (ESCOs) so that they can become capable of marketing and delivering energy efficiency services on a commercial basis. As part of this training, USAID will link the ESCOs with existing sources of funding, so that ESCOs will be able to assist potential customers (private and government) to access the funds required to implement the recommended energy efficiency measures.

USAID will support to the replication of the Dalila Women's Wellness Center in one other city in Moldova. The U.S. partners and staff at the Dalila Center will provide ongoing assistance to the replication center.

Impact and monitoring: Activities supported under this intermediate result are expected to result in the following:

- Vulnerable groups will receive needed assistance.
- Needy institutions will be weatherized.
- A cadre of well-trained ESCOs will be providing energy efficiency services in a commercially viable manner (while USAID training will last only two years, the services should continue to be provided throughout the five year period).
- A replication of the Dalila Women's Wellness Center will be operational .

The impact of activities to relieve human suffering will be monitored at the strategic objective level through the number of institutions and people reached. Establishing targets for humanitarian activities is inappropriate as most of the programs are relatively short-term, they respond to requests by the GOM and/or vulnerable groups, and fluctuate widely depending on the occurrence or non-occurrence of disasters.

Linkages between social protection and other USAID/Moldova-supported programs

This assistance is linked to USAID's democracy program to the extent to which it strengthens the capabilities of service organizations. The weatherization program is linked to energy restructuring by reducing the demand for energy. It is also linked to private sector development as it enables the ESCOs to provide services on a commercially viable basis.

Commitment of Development Partners

The World Bank is involved in reform of the social protection system, particularly pension reform and its Social Investment Fund reaches needed communities. Several donors, including UNICEF, SIDA, EU-TACIS and GTZ, as well as several religious organizations provide humanitarian assistance to Moldova.

ENVIRONMENTAL ISSUES

USAID/Ukraine is in the process of procuring assistance for carrying out the biodiversity assessment required under Section 199 of the Foreign Assistance Act for the entire WNIS region. It is anticipated that the required assessment will be completed by May 2001.