

PROJECT INFORMATION DOCUMENT (PID)

APPRAISAL STAGE

Report No.: PIDA4311

Project Name	MD Competitiveness Enhancement Project II (P144103)
Region	EUROPE AND CENTRAL ASIA
Country	Moldova
Sector(s)	Public administration- Industry and trade (17%), SME Finance (33%), General industry and trade sector (50%)
Theme(s)	Regulation and competition policy (34%), Other Financial Sector Development (33%), Micro, Small and Medium Enterprise support (33%)
Lending Instrument	Investment Project Financing
Project ID	P144103
Borrower(s)	Government of Moldova
Implementing Agency	PIU under Ministry of Economy, Credit Line Directorate under Ministry of Finance
Environmental Category	F-Financial Intermediary Assessment
Date PID Prepared/Updated	16-Apr-2014
Date PID Approved/Disclosed	16-Apr-2014
Estimated Date of Appraisal Completion	18-Apr-2014
Estimated Date of Board Approval	26-Jun-2014
Decision	

I. Project Context

Country Context

1. The Government of the Republic of Moldova (GoM) is pursuing a policy agenda to support export-led economic growth. To achieve this goal, the Moldova 2020 national development strategy focuses on improving the business enabling environment and promoting better access to finance for enterprises, as two of its top priorities. The 2014 Roadmap for Increasing Competitiveness also focuses on the need to improve competitiveness at the enterprise level. Therefore, to support the Government's objectives, the Second Competitiveness Enhancement Project (CEP II) will work with the Ministry of Economy to support implementation of: GoM's regulatory reform strategies, programs to increase enterprises' export competitiveness, and initiatives to improve access to medium to long-term finance for export-oriented enterprises (to be implemented together with the Credit Line Directorate under the Ministry of Finance). In this way, the project will increase the export competitiveness of Moldovan enterprises and decrease the regulatory burden they face.

2. Economic growth in Moldova from 2000-2008 was driven by a boom in domestic demand

funded by remittances, while agriculture and manufacturing struggled. In the early 2000s, Moldova began to recover some of the economic losses suffered after the disintegration of the Soviet Union in the 1990s, though there was also substantial migration abroad. From 2000 to 2008, Moldova became one of the world's most remittance-dependent countries, with remittances growing from 11.5 percent of GDP in 2000 to 30 percent by 2008. Remittance-fueled consumption, services, and housing were the drivers of growth in the period leading up to the global financial crisis.

3. In more recent years, macroeconomic performance has been volatile, reflecting vulnerability of Moldovan exports to global economic and climatic conditions. After a 6-percent contraction in 2009, real GDP grew at an average rate of 6 percent in 2010-11. Under favorable external conditions, remittances recovered and export growth was strong. However, GDP contracted again slightly (by 0.7%) in 2012, as a result of the Eurozone crisis combined with the effects of a severe drought on agricultural production. In 2013, growth made a strong recovery to 8.9 percent, with half of the growth coming from a strong recovery and expansion in the agriculture sector. In spite of strong growth in exports (10.7%), the Russian ban on wine imports from Moldova negatively affected that industry.
4. Since the mid-2000s, Moldova has reduced poverty and improved shared prosperity. The national poverty rate fell from 30.2 percent in 2006 to 17.5 percent in 2011. Over the same period, extreme poverty fell from 4.5 percent to 0.9 percent. Much of the reduction in poverty has been driven by economic growth and remittances. Also over the period, growth in the consumption of the bottom 40 percent of the population outpaced average growth in consumption, with growth averaging 5.8 percent per year for the bottom two quintiles, compared to 2.9 percent for the average. However, despite this decline in poverty, Moldova remains one of the poorest countries in Europe.

Sectoral and institutional Context

5. Moldova's economy has gone through significant sectoral changes, but there has been little job creation. The contribution of the service sector to economic growth has increased, while agriculture and manufacturing have stagnated. Over the past decade, Moldova's GDP growth has not been accompanied by job creation. In 2000-2012, Moldova's employment to population ratio decreased from 58 percent to only 38 percent.
6. There has been little dynamism in exporting sectors. Between 2004 and 2008, Moldova's exports of goods and services grew at less than five percent annually (in real terms): at a pace slower than overall GDP, and slower than exports in many other CIS countries. Much of the export growth that Moldova experienced was driven by re-exports – additional processing of goods using raw materials and design specifications produced elsewhere. The analysis presented in the 2011 Country Economic Memorandum (CEM) showed that re-exports do not create jobs, but direct exports do. There has been little expansion of direct exports from Moldova to non-CIS countries in the past several years, while exports have also remained relatively concentrated in a few traditional, low-value added industries – mainly wine, fresh fruit and nuts, and textiles.
7. The Government of the Republic of Moldova (GoM) has decided to pursue a reform strategy to support export-oriented economic growth. The national development strategy, Moldova 2020, is centered around the need to transition to a dynamic economic model based on increased investment and the development of goods- and services-exporting industries. The Moldova 2020 strategy is built around seven priorities: the business environment, access to finance, education, and

infrastructure, which are defined as critical areas; the judicial sector as an issue area that underpins all others; and consumption of energy resources and the pension system, which disproportionately affect the poor.

8. The recently initiated Deep and Comprehensive Free Trade Area (DCFTA) with the European Union presents a major and historic opportunity to boost private sector growth and economic development. In addition to targeting the EU as a priority export market, the Government of Moldova is also interested in expanding its export base (priority products and priority markets) outside of the EU.

9. Moldova should follow an export strategy of selling higher-quality and higher-value added products in its priority export markets. In order to be more competitive in these markets, Moldovan enterprises need to further develop their capacity to produce such products. Improvements in firms' strategic management, financial management, product quality, production processes, and other areas are needed in order to increase competitiveness. However, information asymmetries about the quality of business services that could help exporters make these improvements reduce companies' willingness to pay for them. Another crucial area that needs attention for Moldova to successfully pursue its export-based growth strategy is the business enabling environment. Although there has been some reform progress, the business environment in Moldova remains characterized by uncertainty, a lack of transparency, and high costs in firms' interactions with government. The competitiveness of Moldovan enterprises, particularly the SME segment, is also affected by challenges in financial sector development. Banks have limited access to medium to long term funding, tend to lack suitable products and credit evaluation techniques for loans to smaller companies, and face general deficiencies in risk management

10. The World Bank has been supporting the government in its competitiveness and reform efforts through the 2006-2013 Competitiveness Enhancement Project (CEP I), which closed successfully and focused on: i) regulatory reform; ii) SMEs' access to business development services and quality certifications, through a matching grant facility; iii) access to finance, through a credit line for exporters; and iv) quality infrastructure, including equipment and institutional reform in the area of metrology, standards, testing, and quality. This project helped make substantial progress and achieved its objectives. It also directly supported the achievement of several indicators under the "Improving economic competitiveness to support sustainable economic growth" pillar of the 2009-2013 Country Partnership Strategy. The Ministry of Economy (MoE), its Project Implementation Unit (PIU), the Credit Line Directorate (CLD) under the Ministry of Finance, and other beneficiaries were strong and committed partners during this project.

11. However, to meet the GoM's objective of re-orienting the economy to export-led growth, additional efforts are needed to address enterprise competitiveness in a more comprehensive way and build capacity in public institutions that provide services for businesses and facilitate private sector development. The Ministry of Economy (MoE) has expressed its strong desire for a project that builds on the successes of the previous project, addresses institutional capacity challenges, and takes a more comprehensive approach to enterprise competitiveness. Recent analytical work, including the June 2013 "Policy Priorities for Private Sector Development" study, its Enterprise Access to Finance chapter and Note, and the September 2013 OECD study on business support infrastructure, has underscored these needs.

II. Proposed Development Objectives

The project's development objective is to increase the export competitiveness of Moldovan enterprises and decrease the regulatory burden they face.

This PDO will be achieved through a set of measures that aim to: (i) strengthen firm competitiveness and market linkages; (ii) improve access to medium and long term finance; and (iii) improve the business enabling environment to reduce costs.

III. Project Description

Component Name

Regulatory Reform

Comments (optional)

12. The objective of the Regulatory Reform component is to support GoM in improving the business enabling environment in Moldova, and specifically in implementing its regulatory reform strategies over the next five years. These strategies include the Roadmap for the Government's Actions to Remove Critical Barriers in the Business Environment for 2013-2014; the Regulatory Reform Strategy and its Action Plan 2013-2020; and the Roadmap for Increasing Competitiveness. In order to achieve this objective, the project will support the following activities:

- (a) Reform governance and capacity building, to improve the timely delivery of reforms and quality of the business enabling environment
- (b) Reform implementation support, to provide direct assistance for implementing priority reforms.

Component Name

SME Development

Comments (optional)

13. SME Development Component: The objective of the SME Development component is to strengthen Moldovan SMEs' linkages to markets and ability to compete in those markets through two closely related aspects:

- (a) Strengthen the institutional capacity of ODIMM and MIEPO, so that they can play a more effective role in facilitating market-based SME growth
- (b) Providing matching grants to SMEs to implement business improvement projects focused on export competitiveness.

Component Name

Access to Finance

Comments (optional)

14. The objective of the Access to Finance component is to improve access to medium to long-term finance for export-oriented enterprises, reduce barriers to finance due to perceived high credit risk in SME finance and high collateral requirements, and promote suitable models for value chain financing, particularly in the agriculture sector. To achieve this objective, the component will provide:

- (a) Line of credit (LOC) to provide medium to long term financing for working capital and investment purposes
- (b) Technical assistance on Risk Sharing Facility (RSF) to revamp the existing credit guarantee scheme undertaken by ODIMM
- (c) Technical assistance to MoE and banks on developing value chain financing models.

Component Name

Project Management

Comments (optional)

15. Funding for project management will cover the costs of the Project Implementation Unit to implement the project.

IV. Financing (in USD Million)

Total Project Cost:	45.00	Total Bank Financing:	45.00
Financing Gap:	0.00		
For Loans/Credits/Others		Amount	
BORROWER/RECIPIENT		0.00	
International Bank for Reconstruction and Development		30.00	
International Development Association (IDA)		15.00	
Total		45.00	

V. Implementation

16. The Project Implementation Unit (PIU) established under MoE as a dedicated legal entity reporting to MoE to implement CEP I (Government Decision No. 895 of August 25, 2005) will also manage implementation of CEP II. This PIU worked well during the implementation of CEP I. The Implementation Completion Report confirms that this project, including its administrative and fiduciary arrangements, was successful. The PIU is currently administering a recipient-executed project preparation grant for preparation of CEP II. It currently has a Director (who has been with the PIU since 2006), Financial Management Specialist, Accountant, and part-time Procurement Specialist and Environmental Specialist. Once CEP II begins implementation, this PIU will be scaled up as necessary to implement project activities.

17. The Matching Grants Facility (MGF) will be implemented by an MGF Administrator. From the beginning of the project, the PIU under MoE will also be the MGF Administrator, and will recruit a dedicated team to manage the MGF. During the mid-term review the option of transferring the administration of this subcomponent to ODIMM will be evaluated, considering that the draft Law of Small and Medium Enterprises establishes that the State policy of support to the development of small and medium enterprises shall be implemented by ODIMM and other authorities.

18. The implementation arrangements for the Line of Credit will remain same as under CEP I project. The LOC will be administered through an apex arrangement. The apex is placed with the Credit Line Directorate (CLD) a specialized entity operating under MoF. The CLD has ample experience with World Bank-financed lines of credit, and has also administered credit lines of a number of other international institutions. The CLD also has extensive experience applying World Bank Safeguard policies outside of CEP I, as it has managed several other lines of credit financed under World Bank's Sector Rural Investment and Services Project (RISP2), and received adequate training to conduct screening of sub-loan applications for compliance with safeguards procedures.

VI. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	x	
Natural Habitats OP/BP 4.04		x

Forests OP/BP 4.36		X
Pest Management OP 4.09	X	
Physical Cultural Resources OP/BP 4.11		X
Indigenous Peoples OP/BP 4.10		X
Involuntary Resettlement OP/BP 4.12		X
Safety of Dams OP/BP 4.37		X
Projects on International Waterways OP/BP 7.50		X
Projects in Disputed Areas OP/BP 7.60		X

Comments (optional)**VII. Contact point****World Bank**

Contact: Melissa Rekas
 Title: Private Sector Development Specialist
 Tel: 473-8902
 Email: mrekas@worldbank.org

Borrower/Client/Recipient

Name: Government of Moldova
 Contact:
 Title:
 Tel:
 Email:

Implementing Agencies

Name: PIU under Ministry of Economy
 Contact: Aureliu Casian
 Title: Executive Director
 Tel: 373-22-296723
 Email: piu@mec.gov.md

Name: Credit Line Directorate under Ministry of Finance
 Contact: Raisa Cantemir
 Title: Head of the Credit Line Directorate
 Tel: 373-22-232963
 Email: raisa.cantemir@arax.md

VIII. For more information contact:

The InfoShop
 The World Bank
 1818 H Street, NW
 Washington, D.C. 20433
 Telephone: (202) 458-4500
 Fax: (202) 522-1500
 Web: <http://www.worldbank.org/infoshop>