

# CASE Network Reports

## Transfer of Know-how for Small and Mid-size Businesses in Georgia, Moldova and Ukraine

### White Paper: Moldova

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## **List of Acronyms and Abbreviations**

ACSA	National Agency for Rural Development in Moldova
AMCHAM	American Chamber of Commerce
APESM	Grapes Producers and Exporters Association of Moldova
CAPMU	Consolidated Agricultural Projects Management Unit
CASE	Center for Social and Economic Research (based in Warsaw, Poland)
CCI	Chamber of Commerce and Industry of Moldova
CIS	Commonwealth of Independent States
COMECON	Council for Mutual Economic Assistance
EIB	European Investment Bank
EKHO	Simplified contribution to public revenues (in Hungary)
ENPI	European Neighborhood and Partnership Instrument
EU	European Union
EU27	The 27 member States of the European Union
EVA	Simplified entrepreneurial tax (in Hungary)
FDI	Foreign Direct Investment
FGC	Special Credit Guarantee Fund
FP7	The 7 <sup>th</sup> Framework Programme for Research and Technological Development of EU (2007-2013)
GDP	Gross domestic product
GIZ	German International Cooperation Agency
GMU countries (in this project)	Georgia, Moldova, Ukraine
GNI	Gross National Income
HDI	The United Nations' Human Development Index
IOM	International Organization for Migration
IRI	Investment Reform Index
JNPGA	Japanese Non-Project Grant Aid
KATA	Small taxpayers' itemized lump sum tax (in Hungary)
KIVA	Small business tax (in Hungary)
LED	Liechtenstein Development Service
MDL	Moldovan Leu
MFO	Micro financial organization
MoSEFF	Moldovan Sustainable Energy Financing Facility
NEKIFUT	The Hungarian National Research Infrastructure Survey and Roadmap
NFFM	National Farmers Federation of Moldova
NGO	Non-Governmental Organization
NIP	National Indicative Program
NISZ	National Infocommunication Services
ODIMM	Organization for SME Sector Development of the Republic of Moldova



OECD	The Organization for Economic Co-operation and Development
PARE 1+1	Program of Attracting the Remittances in Moldovan Economy
PARP	Polish Agency for Enterprise Development
PFI	Participating Financial Institution
PO	Producers' Association (in this project)
R&D	Research and development
R&D&I	Research, development and innovation
RISP	Regional Integration Support Program
RFSMP	The Rural Financial Services and Marketing Program
RSI	Risk Sharing Instrument
SIDA	Swedish International Development Cooperation Agency
SME	Small and medium-sized enterprises
SOIP	Social Infrastructure Operational Program (of Hungary)
SZABASZ	Association for the Reduction of Administrative Burdens
UAP	National Union of Agricultural Producers Associations in Moldova
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDP	The United Nations Development Program
USAID	The United States Agency for International Development
V4	The four Visegrad countries: Czech Republic, Hungary, Poland and Slovakia
WEF	The World Economic Forum
wiiw	The Vienna Institute for International Economic Studies
WTO	World Trade Organization

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## **Abstract**

The report focuses on the potential of the development of small and mid-size businesses in Moldova. It provides an economic overview of the country, and then analyzes various best practices and lessons learned from the development of SMEs in the Visegrad countries, especially Hungary. The report provides a description of economic developments, main trade figures, relevant labor developments, migration and the role of remittances and defines the bottlenecks for SME development in the country. The authors built their analysis on available literature and statistics as well as their own survey and interview series. The study highlights six case studies relevant for SME development selected for deeper investigation such as simplified tax schemes, online tax reporting, entrepreneurship education, agriculture and producers' organizations, the wine industry and issues of measurement of the SME sector. Finally the report draws up potential intervention schemes for Moldovan stakeholders and provides further recommendations for longer term initiatives and actions taken for the support of economic and SME development.

## **Executive Summary**

This report focuses on the potential of the development of small and mid-size businesses in Moldova. It provides an economic overview of the country, and then analyzes various best practices and lessons learned from the development of SMEs in the Visegrad countries, especially Hungary.

The report starts with a description of the background of the project and the main key actors. This introduction is followed by a methodological note, presenting the main methodological considerations and challenges faced during the preparation of the report.

In the first chapter, the main features of economic and social development of Moldova are summarized, while the details and figures are presented in the Annex. The chapter describes how the financial and economic crises affected Moldova, the trends of main export and import figures as well as relevant labor developments and statistics. It can be noted that while the importance of the EU27 continues to grow in terms of foreign trade, the role of the CIS countries is still decisive. Another highlighted feature is the role of migration and consequently, remittances, which constitute a crucial portion of the incomes of the population while lacking sufficient resources in terms of tax-base.

In the following part, Moldova and Hungary are compared in terms of political/economic/social development in order to show that while there are major differences between the two countries, the similarities still allow for building on the lessons learned from the Hungarian (and other Visegrad 4) experiences.

The second chapter collects the main lessons learned from studies regarding the Moldovan SME sector, the main barriers to development, the relevant international literature as well as the V4 experiences in terms of SME development policies.

The third chapter builds on primary knowledge gathered during the various project phases, namely the interview series conducted in Moldova, the results of the online questionnaire survey and the outcomes of the workshop with relevant Moldovan stakeholders held in Chisinau.

The fourth chapter focuses on the six cases relevant for SME development selected for deeper investigation. In these cases, we take a look at the Moldovan situation and bring in lessons from Hungarian experiences. The six domains are: simplified tax schemes, online tax reporting, entrepreneurship education,

agriculture and producers' organizations, the wine industry and issues of measurement of the SME sector.

During the fifth chapter we draw up some potential intervention schemes for Moldovan stakeholders in order to further investigate these cases and to support the knowledge gathered in favor of the Moldovan SMEs. In the sixth chapter, further recommendations are summaries for longer term initiatives and actions taken for the support of economic and SME development.

The Annex following the paper provides deeper insight into the economic development and policy background investigated during the research exercise.

# 1. Introduction

## **Main aim of the project**

The GMU (Georgia, Moldova, Ukraine) Project aims to assist small and medium-sized enterprises (SMEs) in these three countries.

The main objective of the project is to provide support to stakeholders in the three beneficiary countries in their efforts to develop analytical and policy advocacy capabilities by opening new channels of communication with the SMEs and non-governmental organizations (NGOs) in four Visegrad countries (V4): Czech Republic, Hungary, Poland and Slovakia and the rest of the European Union (the EU). This effort is intended to facilitate the transfer of knowledge and the establishment of a permanent platform for sustainable co-operation, bringing SMEs in the GMU countries closer to EU standards, markets, and business opportunities.

The main beneficiaries of the project are experts, think-tanks, business and SME associations as well as NGOs in the GMU countries, who provide local support to the SMEs themselves as well as prepare policy recommendations for local policy makers. The authors hope that the outcome of this exercise is useful for their future work.

## **Why the Visegrad countries?**

Two decades ago, the V4 countries faced similar problems to those of the GMU countries. They began enjoying the benefits of strong EU ties in the early 1990s, when an (almost) free trade area with the EU was established. There seems to be considerable potential for the transfer of knowledge from the V4 countries to GMU countries.

## **Project participants and the organization of work**

The consortium set up for the project is led by CASE - Center for Social and Economic Research (based in Warsaw, Poland) and is supported by their network of spin-off organizations: CASE Moldova (based in Chisinau, Moldova), CASE Georgia (based in Tbilisi, Georgia) and CASE Ukraine (based in Kyiv, Ukraine). The other Visegrad country partners are CEVRO Institute (Prague, Czech Republic), The School of Management (Bratislava, Slovakia) and ICEG European Center (Budapest, Hungary). The project is supervised and the final GMU papers are edited by CASE, Poland, while the country-level work is organized in a bilateral way. ICEG European Center works together with CASE Moldova to gather knowledge and good practices for the Moldova-Hungary cooperation.

### **ICEG European Center and its team**

ICEG European Center is a Budapest-based economic research institute focusing on economic research and policy issues related to various domains, such as economic development, regional development, small and medium size businesses, R&D&I issues among others.

*Magdolna Sass* is a senior research fellow at ICEG European Center and at the Centre for Economic and Regional Studies of the Hungarian Academy of Sciences. Her main activities include socio-economic research in the area of multinational companies, foreign direct investments, SMEs, eServices (electronic services) and related topics. Between 2009 and 2011 she was part of a research team analyzing the internationalization of innovative SMEs in Hungary. Between 1997 and 2000 she worked for the Trade Department (tariffs, eCommerce) and DAFTEE (investment surveys) at the OECD. She obtained her Ph.D. in Economics at the Hungarian Academy of Sciences in 1998.

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Hereby we also thank those stakeholders and experts who replied to our questionnaires and participated at our events, especially to V. Veverita and E. Roscovanu.



## **2. Methodology and Context of the Work**

The report builds on various desk research exercises, literature and policy reviews on SMEs and economic development in Moldova and in the Visegrad countries. In the framework of the present project, we have compiled a list of publications and projects dealing with SMEs in Moldova. We have found 14 international publications which analyze Moldovan SMEs directly or indirectly in an international context, including scientific publications as well as studies prepared by international organizations (such as the OECD).

Regarding statistical data, problems and lack of information about the total population of Moldovan SMEs were repeatedly mentioned by the various experts and representatives of organizations and associations working with these firms during the interviews we conducted with them. While the National Bureau of Statistics of the Republic of Moldova (*Statistica Moldovei*) compiles and provides a set of data on SMEs, there is a large discrepancy between the total population of SMEs and the number of registered SMEs on one hand, and those included in these data on the other. Furthermore, *Statistica Moldovei* uses an SME definition which is different from that of the EU. (This may be justified on the basis of the different levels of per capita GDP; using the EU definition would result in a negligible number of large companies in Moldova). Besides national data sources, international sources are used for comparability reasons (Eurostat, OECD, etc.) where available.

Data on Hungarian SMEs, also presented in this report, are based on the EU definition of SMEs.

In the framework of the project, 12 local interviews were conducted with Moldovan SME stakeholders and experts, followed by an online survey resulting in 11 questionnaires. Respondents were asked about the factors impeding the development and activities of SMEs in the country and about the sectors they considered most important regarding international transfer of knowledge and support activities. Details of the survey are presented in the report.

The preliminary results and draft recommendations of the research were discussed at a validation workshop 20 May, 2014 in Chisinau.

## 3. Key Economic Aspects of Moldova and Hungary

### 3.1. Moldova

Moldova is a small, landlocked country lacking natural resources except for fertile agricultural land. It is a transition economy, having gained its independence from the former Soviet Union in 1992. In this chapter we summarize the main outcomes of the economic analysis conducted for Moldova. The details of the analysis can be found in the Annex.

#### 3.1.1. Longer term socio-economic development

The Moldovan economy has **converged to that of emerging markets and developing economies** in terms of GDP per capita. The role of remittances is crucial for the economy; they account for one-third of the Moldovan EUR 4 billion GDP. The recent recession (starting in 2008) was even deeper than in the advanced economies, causing multiple problems for SMEs doing business. The international competitiveness of the country is relatively low (87<sup>th</sup> out of 144 countries in the ranking of World Economic Forum, Global Competitiveness Index 2012-2013). The Republic of Moldova is in the medium category in terms of social and human development; In the Human Development Index (HDI) of the United Nations, the Republic of Moldova was 113<sup>th</sup> out of 187 countries considered in 2013 (UN, 2013).

#### 3.1.2. International economic transaction

In Moldovan exports, **the role of the CIS countries is traditionally high, but exports to the EU27 are also important**. The main European trading partners of Moldova are Romania, Germany, France, Italy and the United Kingdom. Key exported goods are: agricultural products (vegetable, food, beverages) as well as textiles and textile products. There is a growing importance of machinery and mechanical appliances. Services exports have been growing for years and there are certain signs of improvement with regards to service export

sophistication (i.e. exporting modern services like ICT, communication, financial services etc.). The value of imports from the EU27 has exceeded the value of imports from the CIS since 1998. The most important imported goods are mineral products (most of the oil and gas comes from Russia via Ukraine), machinery, mechanical appliances and electrical equipment.

The inflow of FDI declined in 2009 by 70% compared to 2008 and has remained subdued ever since. Yet looking at the **accumulated stock of FDI per GDP, Moldova has outperformed many rivals in the region.** After the 2008 financial and economic crisis, remittances were no longer able to be conducive to internal consumption to boost the economy. The current account and the trade balance succumbed into deficits.

### **3.1.3. Labor market**

The **active Labor force of Moldova has been decreasing since 2002**, which has also been the case for employment in SMEs. The decrease is partly due to people seeking job opportunities abroad. Whereas the activity rate was 59.9% in 2000, it deteriorated to 40.7% by 2012 because of pressures on the budget due to the **diminishing tax base**, which was related to increasing social security related expenditures.<sup>1</sup> The employment rate has also shown a downward trend since 2002, especially in the aftermath of the 2008 financial and economic crisis; the decline in employment was the biggest in the case of women (in 2000, the female employment rate was 52.2, decreasing to 36.5 by 2012).

For a more detailed presentation of the economy of Moldova, see the Annex.

## **3.2. Hungary and Moldova – Beyond differences**

Despite the differences between Hungary and Moldova, there are certain fields showing similarities originating in the past or current socio-economic development of the two countries. The collapse of the Soviet Union and the so-called transformation recession led to massive GDP losses in all affected countries. Hungary was able to regain its pre-transition level of GDP by 2000, while Moldova reached that level by the early 2000s. Furthermore, both are small countries, which need to follow an export-oriented growth model.

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<sup>1</sup> Those working abroad do not use Moldovan welfare services, however, they do not pay financial contribution for their maintenance either.

The agricultural sector plays a significant role in both economies. Various development strategies can be developed based on this (e.g. servitizing the products and forming intertwined and interconnected business models in the wine and tourism industries). Finally, SMEs are of key importance in driving economic development (and employment) in both countries.

For a more detailed comparison of the two economies, see the Annex.

## 4. SMEs in Moldova: Key Messages from Publications and Projects

There are various publications and international and national projects which deal with or analyze one or more aspects of the characteristics, activities and development of Moldovan SMEs. The main results of these can be summarized as follows.

### 4.1. SMEs in Moldova – main characteristics

According to Moldovan law, **SMEs are defined according to three parameters:** number of employees, turnover and size of the balance sheet. If a company fulfills all three criteria, then it is categorized as an SME. The criteria are different from those applied by Eurostat, which makes international comparisons problematic. (However, a complete harmonization would be useless for Moldova, as there would only be 29 large companies according to the criteria applied by the European Union.)

**Table 4.1 Categories of companies by size according to Moldovan statistics**

	<b>Employment size</b>	<b>Turnover</b>	<b>Total assets</b>
<b>Microenterprise</b>	0-9	up to 3 million MDL	up to 3 million MDL
<b>Small enterprise</b>	9-49	up to 25 million MDL	up to 25 million MDL
<b>Medium enterprise</b>	50-249	up to 50 million MDL	up to 50 million MDL
<b>Large enterprise</b>	250-and above	above 50 million MDL	above 50 million MDL

*Source:* Statistica Moldovei.

The Statistica Moldovei (the National Bureau of Statistics of the Republic of Moldova) collects data directly from the balance sheets of companies. Its database currently has approximately 50,000 enterprises.

According to the latest data (January 2014) published by the Statistica Moldovei<sup>2</sup>, in 2012 the number of small and medium sized enterprises was 49.4 thousand, which accounts for 97.5% of the total number of enterprises. The majority of SMEs operate in the Chisinau region and in urban areas (Bartlett et al., 2013). More than 300 thousand people worked for SMEs (57.7% of the total number of employees). Historically, SMEs have been the main generator of employment in the country (OECD, 2011), however, **SME employment started to decline** during the crisis, in parallel with an overall decrease in employment. (One-tenth of the population and over a quarter of the Labor force works abroad. (Cantarji, Minou, 2013) Problematically however, this decline in SME employment is due to the decline in the staff of medium-sized enterprises (Stratan and Aculai, 2013), while that of smaller sized ones has remained more or less constant.

According to the Ministry of Economy (2012), in international comparison with South East European and Caucasus countries, **the Moldovan SME sector generates a relatively low share of GDP** (28.3% in 2010), while its share in terms of the number of employees is relatively high in the same international comparison: 5<sup>th</sup>, behind Turkey, Romania, Ukraine and Greece, but above the ratio of other countries, including Bulgaria, Serbia, Armenia, Georgia and Russia (Stratan and Aculai, 2013). While the density of firms per thousand population is among the lowest, which reflects **low relative entrepreneurial inclination**, the entry density rate is average. (Bartlett et al., 2013) This may point to an increase in entrepreneurial activities over time in Moldova.

**The average size of SMEs in terms of employees is relatively low.** It was only slightly more than 6 persons in 2012, and has been continuously declining from almost 8 persons in 2008. The dominance of micro-companies is supported by the fact that around three-fourths of SMEs belong to that category. (OECD, 2011) According to the calculations of Stratan and Aculai (2013), the average medium-sized company had 61 employees in 2011, while the same number was 13 for small-sized firms and 2 for micro-firms.

SMEs were responsible for 34.5% of total sales in 2012, following a declining trend starting from 37.1% in 2008. According to Stratan and Aculai (2013), the contribution of SMEs to GDP was 28.3% in 2011, while their contribution to exports was around 12% in 2009. Thus the relative significance of large firms is higher than in the EU economies, as Bartlett et al. (2013) put it: **the business structure is still slightly more skewed towards large firms.** Moreover, Moldovan SMEs can be characterized by low labor productivity (Stratan and Aculai, 2013).

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<sup>2</sup> <http://www.statistica.md/libview.php?l=en&id=4120&idc=168>, see the tables in the Annex.

As for their sectoral breakdown, Moldovan SMEs are active **mainly in labor-intensive services and manufacturing** branches: 40.5% of the total number of SMEs was active in wholesale and retail trade. Real estate, renting and business activities came second with a 17.2% share in the total number of SMEs. In terms of turnover, wholesale and retail trade represented 49.7%, followed by manufacturing (13%) and transport, storage and communication (9.4%). Meanwhile, according to overall profits of the SME sector, wholesale and retail trade is again the leading sector at 49.7%, followed by manufacturing (13%), and construction (7.3%). Regional disparities in the Moldovan SME sector are large, as Sirodoev (2009) shows, with the capital, Chisinau hosting the highest number of SMEs. **Private ownership dominates** the SME sector, with indicators for all areas (number of enterprises, number of employees, profit and turnover) above 80% (Sirodoev, 2009).

Data about the **pre-tax profits/losses** of the SME sector broken down by the size groups of companies is also available from Statistica Moldovei, which shows that micro-companies as a group produce losses, while the group of small-sized companies produces almost twice as much profit as their medium-sized counterparts. A sectoral composition effect may be a factor, as the main sectors where small-sized companies produce profit are wholesale and retail trade as well as real estate, renting and business services.

There is a negligible number of analyses about the other characteristics of Moldovan SMEs. According to one paper, the main motivations for entrepreneurs can be grouped into pull and push factors. The **growth in self-employment** is important, and seems to be an escape route from unemployment and poverty and a possible answer to weak(ening) social security. This is resulting in a high number of new ventures in Moldova, mainly in retail trade. On the other hand, new opportunities act as pull factors, inviting people with an entrepreneurial spirit to set up firms as an answer to new market opportunities due to economic liberalization (Bartlett et al., 2013). The relative shares of the two factors are not assessed by the papers.

It is obvious from the previous review of the literature that data and information on SMEs is relatively limited in Moldova, partly due to the fact that **official data do not cover all SMEs** (OECD, 2011, p. 12). The reasons for that can be found in various factors. First, statistical data cover only part of non-agricultural registered SMEs, i.e. there is a large discrepancy between the number of registered SMEs and those included in the data calculated by Statistica Moldovei. (For more details see OECD, 2011.) Second, because of the relatively large illegal economy, many SMEs which are more inclined to work clandestinely may be left out of the statistics. Third, the number of indicators calculated by Statistica Moldovei is relatively limited, at least

in comparison with the needs of governmental offices, organizations etc. dealing with SMEs. This can be explained by the limited resources of the statistical office, which concentrates on fulfilling its legal and international obligations in terms of the data and indicators published. Fourth, there are various entities in Moldova which are SMEs by definition, but for various reasons do not provide data to the statistical office. From that point of view the most important (and numerous) groups are agricultural farms and people with liberal professions. According to Knuth (2010), "... 40% of the micro, 10% of the small and 10% of the medium enterprises report no activities" (p. 12). However, we can assume that the companies that provide data about their activities are the ones that are really functioning. Thus, the statistical data describe the activities and characteristics of SMEs of Moldova relatively accurately.

In terms of the **main actors of the institutional framework**, the Ministry of Economy is in charge of policy elaboration, legislative drafting and policy co-ordination and the Organization for SME Sector Development of the Republic of Moldova (ODIMM) acts as the implementation agency and is under the supervision of the Ministry of Economy (OECD, 2012a, p. 256). The other relevant governmental actors are the Ministry of Finance, which is responsible for allocating funds (and is therefore crucial from the point of view of financial support) and the Ministry of Education, which is responsible for education in general, and for entrepreneurship education in particular.

There are several chambers, associations and umbrella organizations, most importantly the Chamber of Commerce and Industry, National Confederation of Employers of the Republic of Moldova ("Patronat"), and the Association of Small Businesses (non-profit). It is important to mention the "Business portal" ([www.businessportal.md](http://www.businessportal.md)) bottom-up initiative that offers information, case studies of success stories, etc. International chambers (AMCHAM, etc.) are also present but their orientation is less relevant for SME development.

## **4.2. Main barriers to SME operation, entry and growth**

There is a relatively ample set of papers which analyze the most important barriers for Moldovan SMEs in terms of their entry, exit, operation and growth (and much less on their internationalization). While the relative "merits" of the listed factors differs from case to case, **access to finance** is usually at the top of the list.

The OECD (2011) underlines the importance of poor access to finance as one of the main hindering factors for SMEs, which is reiterated by Bartlett



et al. (2013), and in a later paper, the underdeveloped banking system is given as a cause for that. This is still a problem according to the OECD (2012a), and compared to the other five Eastern Partnership countries, Moldova does not fare well in that area (Moldova is fourth among the six countries, OECD, 2012b). The Ministry of Economy (2012) cites the report ‘Cost of State Regulation of Entrepreneurial Activity’ according to which 39% of enterprises and companies considered access to finance to be the main obstacle restraining business development in 2011 (p. 15). In the same year, the share of credits provided to the private sector constituted only 36% of GDP. This ratio is much less than the average one typical for the countries of Southeast Europe (52%) (p. 15). A 2012 survey (cited by Stratan and Aculai, 2013) also indicated access to financial resources as the most important barrier to SME development in Moldova. However, the Doing Business Index of the World Bank indicates significant progress in that area recently. On the other hand, it is important to note that a more nuanced view on financial barriers is presented in Bartlett et al. (2013), according to which “no amount of finance will assist small firms if institutional constraints inhibit entry and growth.” Additionally, experience shows that in former transition countries, the problem of access to finance for SMEs would be gradually subdued as the country progressed towards a market economy. A more thorough analysis is needed in the Moldovan case.

Kirchner and Giucci (2010) differentiate between two levels in the case of lack of finance for SMEs in Moldova: between the general problems regarding the banking sector and the specific problems of SMEs in obtaining finance for their activities. They show the relatively underdeveloped nature of the Moldovan banking sector in a regional (former transition and CIS economies) comparison, and the high and volatile interest rates applied in Moldova (above 10% in real terms). The reasons for that can be found in the lack of competition between banks and in the lack of information about potential borrowers. As for lack of access to finance, they point at the lack of reliable quantitative assessment on these firms. However, it seems to be true that there is mainly shorter term lending and mainly from sources provided by international donors. Problems include collateral constraints, lack of technology for SME-lending and the poor state of financial reporting by SMEs.

According to the OECD IRI Report (2010), non-banking capital is insufficiently developed in Southeast Europe, including Moldova. As a positive development, the Ministry of Economy (2012) states that “microfinancial organizations (MFOs), savings, as well as loan associations (S&L) and leasing companies were developing as alternative financing sources. In 2010 in the Republic of Moldova approximately 43 microfinancial organizations, 400 savings and loan associations and 27 leasing companies were functioning” (p. 16). They list the factors of the problems in access

to finance by SMEs in the following order: high and constantly changing interest on credits, lack of longer-term financing funds, lack of collateral and its low liquidity, long procedure of exercising rights against collateral, lack of appropriate banking technologies for SME financing, low quality projects proposed for financing, underdeveloped business infrastructure, and lack of companies with risk capital in the financial market (p. 16).

**Regulatory and administrative burden** is also relatively high in Moldova. Concerning entry and exit procedures, Demian and Dumbrava (2009) cited business licensing as the main inhibiting factor for construction companies in Moldova, as well as contract violation, corruption and anticompetitive practices. The importance of these external factors varies from company to company. They found that intrinsic factors are usually not an impediment to SME development. Entry barriers seem to have an average impact on the actual rate of entry in Moldova in international comparison (Bartlett et al., 2013). Furthermore, bankruptcy procedures are still not very compliant with international standards, as evaluated by the Doing Business Index, although they are relatively developed in comparison with the six Partnership Countries (Moldova is third behind Armenia and Georgia - OECD, 2012b).

According to the OECD (2012a), there has been significant progress in the area of **e-government services**. However, the services available there remain partial and incomplete though there were plans elaborated on further developments (p. 259-260). In terms of the overall operational environment for SMEs, including e-government services, Moldova is the ranks lowest among the Eastern Partnership Countries OECD, 2012b.

Knuth's study (2010) contains bits and pieces about Moldovan SMEs and their business environment. First, it states that there are **different tax schemes** in force in Moldova for different groups of SMEs (especially for entrepreneurs in liberal professions). Second, the chaotic regulatory framework concerning liberal professions is mentioned. Third, the inflexibility of labor market regulations and thus the problems caused by these for growth-oriented SMEs is mentioned. Furthermore, entrepreneurship patent holders are mentioned, who, similarly to the liberal professions, are subject to different regulations than SMEs. Thus, inside the SME group, at least three sub-groups are present, each of which has a completely different regulatory framework.

**The business and social environment** also contains elements which act as barriers to the development of SMEs. The OECD (2012a) underlines the importance of promoting a **culture of entrepreneurship and skills development**, emphasizing that there are certain good practices in place, though they were not widespread yet. Among the six Eastern Partner Countries of the European Union,

Moldova was fourth in the area of entrepreneurial learning and women's entrepreneurship, while in enterprise skills it was ranked fifth (OECD, 2012b). Thus the main priority action recommended by the document is to stimulate a widespread entrepreneurial culture in the country. Not only are entrepreneurial skills missing. The Ministry of Economy (2012) says that "according to EBRD and World Bank reports, about 15% of enterprises cite a lack of skilled workers as one of the major problems to growth, and that 36% of the working population between the ages of 25-34 has no vocational education" (p. 18). According to Demian and Dumbrava (2009), internal factors acting as barriers include lack of training and unqualified personnel. Indeed, Stratan and Aculai (2013) cite the results of a 2012 survey: after access to finance, the quality of staff is the second most critical problem of Moldovan SMEs. "More than a half of entrepreneurs indicate the absence or lack of professional qualification of the staff" (p. 18). (Similarly, Bartlett et al., 2013 cite the inadequately educated workforce as the second major constraint to SME activity in 2009).

The **large informal/black economy** is partly the reason for the existence of and partly a problem for SMEs. About 30% of the employed population had an informal job in 2011 (Cantarji, Minou, 2013). Among informally employed persons, 41% work in the informal sector, 27% in legal economic entities and 2% in households which produce for their own consumption. Among young people, the share of those employed in the informal sector is higher (36% compared to 30% in the total population, p. 23).

**Corruption** was cited in a 2009 survey as the fourth most important constraint to SME development in Bartlett et al. (2013). The underdeveloped nature of social networks, partly due to the heritage from the pre-1989 era, is an important impediment to establishing various forms of cooperation and networking in Moldova (Bartlett et al., 2013). Besides, the poor state of competition is singled out as an important problematic area by Bartlett et al. (2013).

### **4.3. Policies directly or indirectly affecting SME development**

SME development is one of the key policy goals in Moldova, which can be justified by the large share of SMEs in total employment as well as their important role in the economy. A detailed list of domestic policies is presented in the Annex Box A.3.1. International cooperation programs available for Moldovan enterprises are shown in Annex Box A.3.2.

There have been a number of positive reforms and programs concerning SMEs, including the State Program for Supporting SME Development, which came to an end in 2011. Compared to other Eastern Partnership Countries, Moldova

is the most advanced in the area of the **regulatory framework** for SMEs. OECD (2012b and 2012a) also emphasizes the relatively developed **institutional framework** with important initiatives taken to simplify Moldova's legislative and administrative procedures. For example, there has been significant progress in the area of starting a business. According to the OECD (2012b), Moldova offers the best services for SMEs and start-ups compared to the other five Eastern Partnership Countries. However, there is much to be done in the policy area. (OECD, 2011, p. 11). Furthermore, more recently, there progress was made in other areas, for example in the area of taxes, or the establishment of a one-stop shop for businesses at the State Registration Chamber (Slusarciuc, Prelipcean, 2013).

The OECD (2011) emphasized that the 2009-2011 State Program for Supporting SME Development represented a step in the right direction, though it could not address all the problems hindering SME operation and growth in Moldova. The same document emphasized the improvements in other policy areas in terms of **improving the framework conditions** for firm operation in Moldova as well as **significantly reducing the administrative burden** for enterprises by reducing the complexity of the regulatory framework and the tax burden on companies. However, in the areas of the rule of law and corruption and other areas of the regulatory framework, further measures are required. Similarly, according to Bartlett et al. (2013), while there has been progress in improving business legislation over the last decade, its impact on the actual business environment has been rather negligible. Thus the poor implementation of laws, **poor enforcement** and inefficient functioning of the regulatory institutions stand still out as important problems. That is why the OECD (2012b) considers Moldova to have the worst operational environment for SMEs among the Eastern Partnership countries (OECD, 2012b).

Concerning **specific SME policies**, the introduction and revision of the patent system, the simplification of the registration process, the entrepreneurship and training programs conducted by ODIMM and other organizations and the establishment of micro-credit facilities have been evaluated as having a positive impact on SMEs. (OECD, 2011, p. 13) The same document recommends developing "[...] a monitoring framework to assess the needs of SMEs and the policy barriers they face." (p. 14) The Ministry of Economy (2012) shows the various efforts executed in order to improve the regulatory environment of SMEs in Moldova, partly with the support of international development partners. An illustration is the considerable improvement of Moldova's rank in the World Bank's Doing Business index between 2011 and 2012. Another illustration quotes the survey conducted in 2011 on the Cost of State Regulation of Entrepreneurial Activity, in the course of which 600 SMEs were interviewed. SMEs spent 10% of their time annually on the fulfillment

of existing regulatory requirements in 2011, considerably less than the 19% reported for 2002 (p. 14).

Furthermore, the OECD (2011) emphasized that certain areas experienced minimal progress, such as **targeted enterprise support** and targeted provision of business services to SMEs. Support for high-growth and export-oriented SMEs seems to be neglected. However, in the area of support for SME internationalization, Moldova is third behind Armenia and Georgia among the Eastern Partnership countries (OECD, 2012b).

As far as progress in the area of **access to finance** is concerned, the Ministry of Economy (2012) points to programs which were financed by the state and/or by development partners which aim to support SMEs (p. 16-17). However, problems there still remain serious as shown in the previous subchapter.

As for the **illegal economy**, the government approved a National Action Plan on Employment in February 2011, and an Action Plan to tackle “illegal work” was launched in June 2011 (Slusarciuc, Prelipcean, 2013). The effect of these plans is still to be seen in practice.

In the area of **internationalization** of SMEs, WTO accession resulted in a significant decline in ad valorem tariffs in Moldova. The high cost of customs clearance is an important barrier, and the quality of products is perceived as one of the most important barriers for exporting. Strengthening the exporting capacities of SMEs is of key importance (DMI Associates, 2006).

Additionally, it is important to note that a **lack of policy dialogue** in the area of SME policies between the various actors is also underlined by both OECD (2012b) and OECD (2012a), of which the later states that “public-private dialogue rarely involves representatives from the SME community” (p. 253). Similarly, according to the Expert-Grup (2013), which is based on a survey of Moldovan companies, the main problem for firms is political instability, followed by the lack of social dialogue, which is connected to the lack of confidence between the public and private sectors. Moreover, Expert-Grup (2012) emphasizes that the new SME strategy is not based on the real needs of Moldovan SMEs.

There are various policy areas which **indirectly** impact SME developments. In the publications and documents we reviewed, we found reference to the following. The OECD (2011) points out the importance of reviewing the **innovation policy** (mainly through supporting technology transfer and increasing the technology absorbing capacities of SMEs), supporting business services and developing networks. These problems are reiterated by OECD (2012a). The OECD (2012b) shows that in an international comparison, Moldova’s situation is acceptable: in innovation policy it is third behind Belarus and Ukraine, and in the area of standards and technical regulations, Moldova

is second behind Belarus out of the Eastern Partnership countries. However, according to Pro Inno Europe (2011), the innovation system is highly centralized in Moldova, coordination is weak and there is modest funding for innovation. Innovation stimulation measures are implemented by an agency, which is subordinated to the Academy of Sciences with negligible links to the private sector.

Moreover, **SME participation in public procurement** and the support mechanisms for it reveal a problem in international comparison in Moldova (OECD, 2012b). SMEs are not encouraged to take part in these and their access to related information is limited. Furthermore, Moldovan SMEs are the least aware of green growth opportunities amongst the Eastern Partnership countries. A more detailed list of domestic policies and initiatives for SME development are presented in Annex Box A.3.3.

#### **4.4. Policy lessons learned from the Visegrad countries and other international experiences**

In this section we describe the various country-specific approaches in two levels. First, we look at general entrepreneurship and SME-supporting principles and instruments (for more details, see Annex Box A.3.4). Then, we present the knowledge-economy and innovation based growth-related aspect of R&D&I support mechanisms from the side of the state (listed in Annex Box A.3.5). While the performance of the V4 countries in these areas is still in the catch-up phase compared to that of more developed economies, V4 countries have made significant steps forward since the transition process started.

First, the development of governmental services, especially eServices, is needed to develop the proper applications for eTaxing, eReporting for taxes, social and health contributions, employment status, registry of various licenses and permissions, etc. Small enterprises do not have the capacity to conduct the same accountancy practices as larger ones can afford to do. This does not mean that they intend to cheat on taxes. Rather, many of them are willing to pay their fair share once it can be done easy and simply. Simplified tax schemes therefore can ease the burden on the SMEs while also leading to revenues on the state's behalf. Policy efforts with that aim are present in all four Visegrad countries.

Second, education, trainings, and consulting services promoting entrepreneurial activities through improving skills (including for internationalization, external financing etc.) are needed in many transition countries that aim to build on a strong SME base. In that area, not only are the national governments

of the Visegrad countries increasingly active, but there are also services available at the EU-level and open to Visegrad SMEs. Third, the support of cooperation among SMEs can help them to reach markets that they would not be capable of reaching on their own. Joint marketing activities, common development projects, and shared logistics methods can lead to stronger SME activities both on the domestic, as well as on the international market. Support for these types of activities has been on the agenda in all four countries, with various practical successes.

At least one specific SME policy and/or strategy is in place in each of the V4 countries, indicating on one hand that in the European Union, supporting SMEs is a valid policy aim executed at the national level, and on the other hand, that in the V4 countries policymakers are aware of the important role these companies play in their national economies. A common feature of the policies is the aim of improving the business environment for SMEs, mainly through reducing the administrative burden hitting them.

Furthermore, in the three smaller Visegrad countries (i.e. with the exception of Poland), the internationalization of SMEs (mainly exports) is promoted through various measures and institutions. In all the Visegrad countries, there are attempts to reduce the financial problems of SMEs through various measures, e.g. through providing grants or loans at below market interest rates. Hungary took specific measures to enhance cooperation between SMEs, and clustering is actually supported in all V4 countries. R&D&I is supported through various measures, not only because of its relatively low share in GDP compared to other EU-member countries (except for the Czech Republic), but also because of the recognized importance of R&D through improving the productivity and competitiveness of SMEs. From that short overview it can be seen that while the problems are similar in the five countries, their relative importance is different and the complex SME policies/strategies present in the V4 countries can serve as good examples and provide valuable lessons for Moldova, especially in the following fields: reducing administrative burden for SMEs, supporting cooperation between SMEs, helping internationalize SMEs, and lessening the financial constraint on SMEs.

## 5. SMEs in Moldova: Key Messages from the Present Project

### 5.1. Trade and FDI relations between Moldova and the Visegrad countries

On the basis of geographic closeness and common economic heritage (CMEA - membership, including inherited personal contacts and former socialist economies) and similar economic environment (transition process), one would expect relatively high trade flows between Moldova and the Visegrad countries. However, other factors (especially the EU-membership of the Visegrad countries, and strong integration of Moldova with the CIS economies and strong cultural ties with Romania) act against increasing trade flows. In terms of FDI, given the relatively low level of development and the low level of OFDI flows from the analysed countries, negligible FDI ties are expected between them.

In the framework of the present project, we have carried out the **analysis of trade and FDI flows between Moldova and the Visegrad countries** for the period between 2000 and 2012. Our main findings were the following.

There has been a dynamic increase between 2000 and 2012, both in exports and imports, temporary setback in imports from Moldova in 2010 (mainly due to the crisis), especially in its exports to Hungary, the Czech Republic and Slovakia, however, they regained their pre-crisis momentum by 2012 (except for exports to Slovakia).

Throughout the analysed period, there has been a massive and persistent negative balance of trade for Moldova in its trade with the four Visegrad countries.

Moldova is a partner of minor importance for the Visegrad countries: its share remains below 0.2% in total foreign trade of each Visegrad country and below 0.8% in their extra-EU trade. However, **there is an increase in Moldova's share over time, especially in the case of Poland and Hungary, both on the exports and imports side.**

In terms of the product structure of trade we found significant changes between 2000 and 2012 for Visegrad exports to Moldova. Overall, **there is a move towards a less diversified structure in terms of the number of product groups**, except



for Slovakia. The leading Visegrad export product group is *Machinery and transport equipment* (Czech Republic: over 60% of total exports to Moldova, Hungary: 44%, Poland: 29%, Slovakia: 50%). We assume that these may be mainly products of local affiliates of multinationals. The second most important product group is *Manufactured goods classified chiefly by material* (leading with 34% in the case of Poland, in Slovakia second with 28%, in the Czech Republic third with 11%), the third one is *Chemicals* (second in the Czech Republic (16%) and in Hungary (15%), in which latter case that is most probably pharmaceuticals). It is important to note, that *Food* is relatively significant in Polish (12%), Hungarian (11%) and Slovak (9%) export to Moldova.

Similarly, in the case of the Visegrad import from Moldova, there were significant changes taking place between 2000 and 2012, which meant mainly the move towards the dominance of *Miscellaneous manufactured articles*. While in Visegrad exports to Moldova, there were some similarities between the export structures of the countries, in their **imports from Moldova, differences prevail**. The leading product group is *Miscellaneous manufactured articles*: 51% in Czech imports from Moldova, 90% in Hungarian imports and 62% in Slovak imports. The second important product group is *Beverages*, 29% in Czech imports and 16 % in Slovak imports. Poland differs to a great extent: Moldova's export to this country has a more diversified structure with more product groups with similar shares: *Food and live animals* (28%), *Miscellaneous manufactured articles* (26%), *Manufactured goods classified chiefly by material* (14%), *Crude materials* (14%), *Beverages* (12%).

From the point of view of the internationalisation of Moldovan SMEs, it may be **important to go down to the product level and trying to identify the main exporters of the product groups** in question. Our analysis of 2013 trade data yielded the following result. It is important to note, that the concentration of exports is very high: the top five products represent at least 74% of total imports from Moldova (93%! in the case of the Czech Republic), thus also that fact justifies our research and approach. To the Czech Republic, Moldova's main export item is *Parts, bedding, mattresses, mattress supports, cushions and similar stuffed furnishings*, which represent half of Moldova's export to the Czech Republic. That product may be related to outward processing trade. The second item is *Wine of fresh grapes* (30%). In the case of Hungary, the same product is the top one as in the case of the Czech Republic, representing 68% of total Hungarian import from Moldova. The second product with 10% is *Apple juice*. For Poland, *Electricity meters* is the top product, with 20% of total imports, followed by *Bars, rods, angles, shapes and sections of iron or other alloy and non-alloy steel, n.e.s.* (20%) and *Apple juice* (16%). The structure of imports from Moldova is again the most diversified in the case of Poland. Slovakia imports

mainly *Sleeping bags* (50 % of total imports from Moldova), followed by *Wine of fresh grapes* (17%). Overall we found labour-intensive, mainly textile and clothing products and (processed or raw) food and beverages products amongst the most important export products of Moldova to the Visegrad countries. We assume, that items in the first product group are connected to outward processing trade, while SMEs may play (some) part in the export of the second product group.

**Investment relations are negligible between the Visegrad countries and Moldova.** The Visegrad countries, and inside the group, especially Hungary (since the mid-nineties) and Poland (since around 2000) became important outward investor countries. Hungary is third in NMS in per capita terms (behind Slovenia and Estonia) and second according to the stock of OFDI. The main target countries are neighbouring countries (Croatia, Slovakia) and economies in the larger CEE region (especially Bulgaria) and “tax optimisation” destinations (Dutch Antilles, Netherlands). Poland is first according to the stock of OFDI, the main target countries are those in Western, Central and Eastern Europe, but also tax optimisation locations. Inside the CEE region, Czech Republic, Lithuania and Romania are the major destinations. On the other hand, outward FDI is much smaller from the Czech Republic and Slovakia, and it is targeted mainly towards each other. However, there is a common characteristic of OFDI from the Visegrad countries: it is highly concentrated, that is a few large investor firms, even a few large transactions (in many cases related to privatisation) are responsible for the large share of OFDI stock.

**Moldova hosted a visible volume of Hungarian and Polish investments in 2012**, with the value of 13.3 and 13.6 million euro, respectively. In 2002, this was negligible in both cases and it remained so in the case of the Czech Republic and Slovakia. In terms of the % of total OFDI, these values represent 0.05% of Hungarian and 0.03% of Polish total stock of OFDI. FDI from Moldova was not recorded in any of the Visegrad countries. Thus FDI relations are negligible between Moldova and the Visegrad countries.

Overall we can state that the trade and FDI relations of Moldova and the Visegrad countries, though growing over time, remain well below potential or below what is expected on the basis of the geographic closeness and common heritage and existing personal ties between the countries in question. Thus there is certainly room for state intervention at least on the level of spreading information about opportunities in each other.

## 5.2. Outcomes of the expert interviews

In the framework of the present project, various activities were carried out in order to get further insight into the characteristics of SMEs in Moldova. First of all, **expert interviews** were carried out with a subset of the main factors listed in the previous chapter. The main findings of the interviews verified the problems identified in the literature, and also added new elements to them.

**Lack of access to finance** was confirmed as an important problem for the set-up, growth and internationalization of SMEs by numerous experts. The lack of real competition and high interest rates in the banking sector were mentioned as the most important reasons for that problem. On the part of SMEs, the main obstacles were the lack of collateral and the too small or not really “assessable” projects. The experts emphasized that the emergence of the relatively numerous microfinance actors and internationally financed projects together with national financing programs have a positive impact but they cannot solve the problem fully. The government/ministries acknowledge the importance of the problem, but we could not find any of them who would take the responsibility and provide action plans.

Similarly to the findings of the literature, the experts cited **bureaucracy and high administrative burdens** as important barriers to SME development in spite of progress made in that area. Enforcement and practical implementation is still weak according to the majority of the experts interviewed, for example registering a company takes 3 hours in principle, but the process is much lengthier in reality. One expert singled out the problem of **tax collection**, in which public authorities do not know how to communicate with the private sector, and there are incentives for companies to not pay taxes. On the other hand, “honest” private actors are fined strictly when they miss a deadline or when found guilty (rightfully or not) in any tax-related matter. According to the experts, the level of fiscal burden in itself is not a problem, but the method of tax collection is problematic.

In connection with bureaucracy, certain experts underlined the high level of **corruption** as one of the most negative factors hindering SME development in Moldova. Local taxes are especially high, and corruption and nepotism are especially significant at the local level. In that area, considerable improvement is expected starting from 2014, when there will be a cap on local tax. Other areas plagued by corruption include fiscal authorities, including tax collection, company registration and procurement. A further reduction in administrative barriers to SMEs is planned at the ministry, including simplifications in the tax area. Another solution recommended by experts is the further development of e-government services in many areas, for which the basis was already established by a World Bank program.

Many experts mentioned that there are **new government programs**, financed partly by the government, partly by international sources, which proved to have a considerable impact on SME development. For example, PARE 1+1 was mentioned more than once, which helps the reintegration of return migrants and channels their savings into the private sector through enabling and co-financing them to become entrepreneurs. Migration can be an important source of entrepreneurship knowledge and experience. Incubation projects for SMEs were also evaluated positively.

Various **trainings**, both for entrepreneurs and for students, were also mentioned as having a positive impact on SME development. As a connected problem, the lack of entrepreneurial spirit and mentality is an important hindering factor in the area. An entrepreneurship education program in vocational school was introduced to try to improve this situation and this year a similar course will be introduced in primary schools. A specific set of trainings has to be mentioned: microfinancing institutions also provide various and extensive trainings to their clients, which are SMEs or individual entrepreneurs. There is an initiative to improve the content of vocational education in other areas as well: to make it more practical and useful for use in factories. According to one expert, a skilled labor force is a real limitation to improving the competitiveness of SMEs.

While the role of ODIMM, a ministerial agency, is important, not only the government is active in introducing and managing **programs to help SMEs**. Many internationally financed projects are handled by other organizations. For example the chamber of commerce reaches out to numerous SMEs with trainings and other help. A criticism of these programs expressed by one expert was that they are not targeted enough; they do not take into account the heterogeneity of the SMEs. For example, innovative SMEs and start-ups are completely left out of the programs. Programs focusing on specific activities or sectors are also missing: in that respect, besides innovative firms, agriculture or IT was the most frequently mentioned prospective area. The exception in that respect is the USAID program which concentrates on the (potentially) competitive sectors of wine, apparel, IT-software, footwear, automotive and furniture. Moreover, overall, the budget resources spent on SME programs are negligible. The Ministry of Economy came up with the idea of setting aside a specific annual sum by law for these programs, however, the proposal was not backed by the Finance Ministry. Furthermore, evaluations of programs are usually missing.

**The technological backwardness** of SMEs and **low levels of innovation and R&D** were listed as important problems hindering the competitiveness of SMEs both on internal and external markets. A specific problem is that of **the innovation policy**, especially that the Academy of Sciences is “monopolizing” innovation, and so resources are not available to firms.

As was already mentioned, innovative companies lack any attention from public and private organizations, and there are no specific programs organized for them.

An important new development is that according to the representatives of company associations, (registered) SMEs became interested in **fighting the illegal economy**, as these entrepreneurs operating legally are at a competitive disadvantage compared to those operating in the black/grey economy. The share of the black economy is estimated by one expert to be very high (40-60% of GDP), and as such, it acts as one of the most important inhibiting factors for the development of the legal economy. According to one expert, the loss-making (or low profit-making) character of SMEs is partly due to the informal economy.

Experts from government agencies and ministries, together with those from independent think tanks as well as representatives of company associations, mentioned data problems concerning SMEs. **The lack of detailed data on SMEs** is a hindering factor for policy and project design as well as for the evaluation of existing programs. There are even organizations which set up their own databases on SMEs, which of course requires substantial financial and human resources, which these organizations usually lack. Experts from the statistical office are, ironically, in a similar situation. Their database is based on the balance sheets of registered companies. However, due to a lack of resources, they calculate only those indicators which they are required to do by law. Thus the database exists, but is not used fully (in 2008, they carried out a special statistical analysis with the financial support from UNDP).

In the area of **public-private dialogue**, reinforcing the findings of the literature, there is still much to be done according to the experts on both sides of the table. Both government organizations and representatives of company associations felt that there are problems in that area, however, they usually criticized the other party. The lack of fora organized on a regular basis was mentioned frequently. According to one expert, working with the government causes no problems, while cooperation with the parliament is much more problematic. According to the same expert, the dialogue should be more structured and more focused between the government and businesses. Another expert put the problem in terms of lack of confidence between the private sector and public authorities. Moreover, he highlighted the fact that company associations do not really represent the corporate (SME) sector, as many firms think its pointless to join these organizations.

The expert interviews showed that the relative importance of the factors inhibiting SME operation and development has changed over time. While lack of access to finance is still important, its significance has declined substantially. Meanwhile, bureaucracy and administrative burdens together with corruption

and the large grey/black economy now hinder the development of SMEs more substantially, reflecting advancement towards the establishment of a market economy.

Furthermore, the importance of various SME programs and trainings and their targeting has been underlined by our expert interviews. The lack of financing was more pronounced in the context of financing SME programs. The lack of data has already been emphasized by a few publications. Our expert interviews added to that in terms of showing that the data are there, thus resources are needed to carry out the necessary calculations in order to get a more substantial dataset on Moldovan SMEs. In terms of the technological backwardness of SMEs, we could make a link between the Moldovan innovation system centered around the Academy of Sciences, which concentrates on R&D projects with little practical relevance for SMEs. And as far as the public-private dialogue is concerned, our expert interviews provided more details about its nature.

### **5.3. Results of the online survey**

As a second step, a **questionnaire survey** was conducted with another subset of actors in the area. More than 50 persons/organizations were targeted, of which 11 answered the questionnaire positively. Targeted organizations included: ministries and other policy actors, SME organizations, agricultural associations, think tanks and expert groups, banks dealing with SME financing and local representatives of international organizations. Here we analyze the results of the replies. The questionnaire was translated into the local language. In this analysis, we use the English terms of the questionnaire. The target group was also reminded via phone calls to fill out the questionnaire.

The questions targeted six domains relevant for the development and daily activities of SMEs. Respondents were asked to evaluate to what extent the factors listed were impeding the development and activities of SMEs in the country. On a 1-4 scale, 1 represented “not at all”, 2 represented “somewhat”, 3 stood for “significantly”, 4 meant “very significantly”. NA was provided when the respondent did not/could not answer. The main domains were:

- Labor and skills;
- Red tape/bureaucracy;
- Tax burdens;
- Law and order;

- Market specificities;
- Finance and other issues.

In the tables below, we provide the list of those factors which were deemed the most significant barriers to SME development by the respondents.

In the field of **Labor and skills**, the followings were identified as impeding factors to SMEs (values above 3):

**Table 5.1 Results of the questionnaire survey (labor and skills)**

<b>Lack of experience in foreign trade, in EU in particular</b>	<b>3.60</b>
<b>Lack of knowledge of EU regulations</b>	3.55
<b>High emigration</b>	3.36
<b>Low business ethics</b>	3.18
<b>Low market skills of entrepreneurs/Inadequate business education</b>	3.18
<b>Lack of business experience</b>	3.09
<b>Lack of language skills and contacts abroad</b>	3.00

*Source:* ICEG EC questionnaire survey in the GMU project.

The replies evidently show the potential importance of EU27/V4 cooperation in the fields related to EU regulations and experiences with EU trade. Furthermore, help may also be needed in business education. Low business ethics and the high emigration of skilled workforce were identified as important, but these issues should rather be solved domestically/by the economic actors themselves.

In the domain of **red tape/bureaucracy**, the issues that are at least significant impediments to SME development are the followings:

**Table 5.2 Results of the questionnaire survey (red tape/bureaucracy)**

<b>Institutional differences with EU</b>	<b>3.30</b>
<b>Foreign trade barriers</b>	3.09

*Source:* ICEG EC questionnaire survey in the GMU project.

In the domain of **taxing and customs regulations** and charges, 5 out of the 7 obstacles were considered at least to be significant:

**Table 5.3 Results of the questionnaire survey (tax and customs)**

<b>Unstable and non-transparent tax rules and/or their applications</b>	<b>3.27</b>
<b>High cost of compliance</b>	3.09
<b>High custom charges</b>	3.09
<b>High effective SME presumptive tax rates</b>	3.00
<b>High effective value added tax/trade tax rates</b>	3.00
<b>Other high taxes and fiscal fees/charges</b>	3.00

*Source:* ICEG EC questionnaire survey in the GMU project.

In the field of **law and order**, there were only 4 topics listed, and 2 of them were considered significant obstacles by the respondents:

**Table 5.4 Results of the questionnaire survey (law and order)**

<b>Corruption/Clientelism/Favoritism</b>	<b>3.73</b>
<b>Weak judiciary</b>	3.45

*Source:* ICEG EC questionnaire survey in the GMU project.

In the domain of market obstacles, 12 out of the 14 questions received a value higher than 3, which evidently shows a lot of tensions in terms of availability and functioning of the markets.

**Table 5.5 Results of the questionnaire survey (market obstacles)**

<b>Monopolization/Excessive market power of some participants</b>	<b>3.82</b>
<b>Barriers for exports to foreign markets</b>	3.64
<b>Unfair competition/Uneven playing field/Informal economy</b>	3.64
<b>Political instability</b>	3.50
<b>Low level of activities of venture capital</b>	3.38
<b>Weak market position of SMEs</b>	3.36
<b>Weak professional organizations of SMEs</b>	3.27
<b>Insufficient market information/governmental support for SMEs</b>	3.27
<b>Small market size/Weak demand</b>	3.18
<b>Macroeconomic instability (demand, inflation, exchange rate)</b>	3.18
<b>Discriminatory practices of authorities</b>	3.11
<b>Weak analytical and policy advocacy of SME organizations</b>	3.10

*Source:* ICEG EC questionnaire survey in the GMU project.



It is important to highlight that the weak analytical and policy advocacy of SME organizations can clearly be targeted in the framework of this project, while some other obstacles – such as macroeconomic instability or fighting corruption or the black economy – are beyond the capacities of this exercise.

Finally, in the domain of **financial and other issues**, six questions were asked and five of those six were considered significant obstacles:

**Table 5.6 Results of the questionnaire survey (financial and other issues)**

<b>High cost of credit</b>	<b>3.40</b>
<b>Lack of open communication channels with EU</b>	3.40
<b>Difficulties in accessing financial services</b>	3.20
<b>Inappropriate infrastructure</b>	3.18
<b>Weak professional organizations of SMEs</b>	3.09

*Source:* ICEG EC questionnaire survey in the GMU project.

In the second part of the survey, respondents were asked which sectors they considered to be the most important ones regarding the international transfer of knowledge and support activities.

The majority of the responses (10) pointed to agriculture, including sustainable agriculture, and the food and beverages industry. The wine industry has been mentioned as of specific importance.

The tourism sector was mentioned on four occasions while the textile and the energy sectors were mentioned in three. It is important to note that among other sectors, the support and capacity-building of business associations and the development of consultancy services have also been mentioned.

Finally, in the third part of the survey, respondents were asked to provide any further suggestions they considered to be relevant for the V4-GMU project. The following areas were mentioned as areas in which an exchange of experiences and knowledge transfer may support Moldovan SMEs:

- Reducing bureaucracy;
- Reducing corruption;
- Carrying out an exchange of experiences, establishing contacts;
- Becoming more familiar with the requirements of the European market;
- Disseminating best practices in the field;
- Improving the harmony of the EU and Moldavian laws/legislation;
- Applying modern techniques and technology;
- Training specialists in relevant fields.

When it comes to the issue of the kind of priorities the Moldovan government has been striving for to stimulate SME development, one can arrive to the conclusion that several programs were introduced and carried out with mixed results. The priorities seem to have been focused on aspects that have been captured by this report (attracting migrants back, developing the potential of farmers, contributing to the modernization of SMEs, improving the financial flexibility of SMEs).

#### **5.4. Lessons learned at the expert workshop – programs and policies with a significant impact**

As for the third activity, a workshop was organized with the main experts and stakeholders in Chisinau in May 2014. It helped in many ways to get more detailed information about possible areas of intervention and project design. First of all, the participants were asked to evaluate the programs aimed at SMEs by indicating which five were the most important from the point of view of SME development.

According to the opinion of the experts at the workshop, the following main initiatives were likely to offer the biggest positive impetus to the development of Moldovan SMEs: entrepreneurship (education) connected to return migration, technological backwardness and agricultural activities.

##### **1) PARE 1+1: Project to Attract Remittances in the Economy**

The program aims to mobilize the human and financial resources of Moldovan migrants (and their remittances) in Moldova's sustainable economic development, by fostering the establishment and development of SMEs by migrant workers. The program operates under the rule of "1+1", i.e. 1 LEU invested by the migrant is coupled with LEU 1 as a grant invested by the state. It is financed by the government, with additional financing received from the EU after the success of the program was proven. The organization which is responsible for implementing the program is the Organization for Small and Medium Enterprise, in cooperation with different development partners, including the IOM. Since 2010, PARE has attracted 2.4 million Euros in remittances for the SME sector. Due to the high interest in the program on the part of the target group, the government plans to continue its implementation until 2015.

## **2) JNPGA: Program for SME Sector Support and Development (acquisition of equipment)**

The main objective of the program, funded by the government of Japan, is to promote economic structural adjustment efforts by facilitating the purchase by SMEs of a large variety of production equipment outside the capital city and Balti. The funds are awarded based on agreements between the governments of Moldova and Japan, concluded by the exchange of letters for each of the separate installments. The main activity is the acquisition of equipment through leasing for a period of one year, providing a grant of 40%. The purchase value varies from 500 thousand to 2.5 million MDL. The program can be used only for the import of new equipment. Funds were distributed in 2007-2012 to 73 beneficiaries. In 2012, 43 enterprises participated in the program and received LEU 13.4 million.

## **3) Subsidies for Farmers**

Over the last decade, a series of farmer-supporting measures and programs were introduced and implemented favoring the development of Moldova's agricultural sector. The country's fiscal situation allows small farmer enterprises and small farmer cooperatives to pay 0% in income tax, and a much more simplified accounting system. The Agriculture Recovery Project offered long term credits of 15 years for capital investments in agriculture. The Rural Investment and Service Projects (RISP I and RISP II) aimed to provide long term loans of up to 15 years dedicated exclusively to the food industry (20% grant). Additionally, the Agriculture Development and Food Production Increase (2KR) program aimed to offer leasing opportunities for agricultural equipment (e.g. 50% of the total cost should be paid by farmers and they enjoy a VAT exemption as well). According to evaluations, the allocated subsidies were not able to dampen the unpredictability built into the agricultural production activity since they followed some objectives aimed at the development of the agricultural sector and do not have a stable character. Since they change every year, farmers are unable to forecast their production activity.

## **4) IFAD IV: Rural Financial Services and Marketing**

The goal of the Rural Financial Services and Marketing Program (RFSMP) is to reduce rural poverty in Moldova by creating enabling conditions for the poorer and poorest in rural society to increase their incomes through greater access to markets and employment. The program's objective is to extend employment opportunities and the participation of small farmers in competitive commodity value chains through enhanced access to financial services for the small owners, women practicing off-farm

businesses and young farmers, as well as off-farm entrepreneurs and processing units. The program consists of two main components:

- (i) Value Chain Development for Rural Poverty Reduction, which aims at the mapping and pro-poor management of competitive commodity and services value chains with actual or potential strong linkages to the target groups, i.e. rural poor people, and
- (ii) Rural Financial Services, which is expected to consist of four sub-components: financing of Participating Financial Institutions (PFIs) of loans to poorer small-scale farmers, financing of PFIs for on-lending to off-farm rural micro-entrepreneurs, financing of PFIs for medium loans to rural processors, wholesalers, and possibly producer/marketing associations for investment purposes, and, last but not least, capacity-building of PFIs, credits follow-up, and subsidies.

## **5) 2KR: Increasing Food Production Project**

The objective of the project is to support the development of agriculture and to increase food production in Moldova. The program is dedicated to private legal entities, farmers, and individuals, regardless of their organizational form of activity, who are engaged in entrepreneurial activities and/or offer services for mechanized farming. The program supports the procurement of agricultural technology in installments (initially they pay 50% of the total cost and then they pay installments over two years). The price does not include VAT.

Overall, the information gained during the project through the various activities points to a very similar list of problems of SMEs in Moldova compared to the results of the desktop research carried out beforehand. However, our project resulted in further insights and more nuanced information as well as in the identification of the areas where specific projects based on good practices may result in instant benefits for SMEs in Moldova.

## **5.5. Lessons learnt at the expert workshop – programmes and policies with significant impact**

In October, 2014 a special consultation was held in the Ministry of Economy with the policy makers responsible for SME development and the experts of the HU-MD team. The most important outcomes were the followings:

- Entrepreneurial education is of crucial importance, especially in terms of EU regulations and EU economic relations;

- The Action Plan for the strategic implementation plan for SMEs is currently under programming, and will be valid for 2015-2017;
- Regarding funding opportunities, the main challenge is the diversification of funds;
- There is an existing strategy for the reduction of administrative burdens in Moldova which is under implementation;
- In addition, clustering and cluster development is one of the key topics to be developed in the future, in the framework of a join project.

The consultation was fruitful for both parties and offered the opportunity to discuss the SME development issues directly at the policy creation level.

## **5.6. Lessons from the validation conference**

On 17 October, 2014 a conference was held in Chisinau where the White Paper was presented and discussed in order to validate the findings of the report. Several experts from the relevant stakeholder groups were participating and debated the following topics:

- SME representatives called for more reduction in taxes and administrative burdens, while government representatives emphasized the need for tackling the grey economy;
- Data on foreign trade relations were presented and discussed at sectoral and sub-sectoral level. Several economic activities are based on outsourcing, which raises concerns about the longer-term sustainability of these sectors/activities. Nevertheless, at the present there are no systematic strategies to be prepared for the period when outsourcing is not profitable in Moldova anymore;
- The role of the fashion/clothing industry was highlighted, and the relation of the relevant multinational and local/outsourcing actors was discussed;
- SME growth was also debated, focusing at the difference between high-growth, nationally or internationally competitive “gazelle SMEs” and reliable, less intensively growing local SMEs that play part in family employment/family income and local goods production/services. These groups have different support, development and policy needs;
- Finally, methodological issues were also raised in terms of data reliability and data availability from the Transnistria region.

## **6. Recommendations – Selected Fields of Intervention**

Based on the analysis of the Moldovan economy and SME sector, as well as building on the lessons learned from interviews and surveys, certain fields of intervention were selected and elaborated on in more detail in order to provide support and munitions for Moldovan stakeholders for SME development.

The selected areas are:

**General support methods for a wide range of SMEs, regardless of their sector of activity:**

- Simplified tax schemes;
- e-Taxing and other eServices, and governmental one-stop shop portals;
- Entrepreneurship training and education, a field where Moldova already has important experiences that can be further developed. The Moldovan experiences, nevertheless, could be of use for other countries.

**Specific to agriculture:**

- Producers' associations to help small producers reach the market;
- Winery associations to promote local wine and wine tourism.

**Methodological aspects:**

- A more detailed statistics system on Moldovan SMEs.

### **6.1. Simplified tax schemes – Moldova and Hungary**

One of the most important barriers to the development of SMEs can be rules and regulations that are too complex in the area of taxation, because for these smaller enterprises with limited capacities, resources, and capabilities, compliance with these rules may result in an excess burden. Moreover, compared to their turnover or number of employees, SMEs bear a disproportionate regulatory

burden, including in the area of taxation.<sup>3</sup> While there are several factors responsible for that excess burden, one important way to reduce compliance costs for SMEs can be a simplified method for tax accounting and for establishing the tax base. This can take the form of a presumptive system for calculating the tax base or lump sum systems for taxes.

According to the “Doing Business Index” of the World Bank, overall, there are 31 tax payment occasions in a year in Moldova, requiring 181 hours of work, and resulting in a total tax rate of 40.4% of the profit. In Hungary, there are 12 tax payment occasions, but 277 hours are needed to fulfill the administrative requirements and 49.7% of the profit is paid in taxes. For corporate income tax, the same indicators are: 1 payment occasion, 42 hours of work and 9.6% of profit for Moldova, and 1 payment occasion, 35 hours of work and 5.8% of profit for Hungary. Compared to the best performer country, Moldova is 32% behind, while the distance for Hungary is 31.6%. While overall in taxation the two countries fare similarly, Hungary performs better in corporate taxation. That may be partly due to the various simplified tax schemes that are in effect in the country.

In Hungary, there are four tax schemes, which can be considered simplified way of paying taxes either for companies or for individuals. These schemes are clearly targeting and favoring small and medium-sized enterprises.

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<sup>3</sup> See e.g. for Europe [http://ec.europa.eu/enterprise/policies/sme/files/support\\_measures/taxsimple/taxsimp\\_en.pdf](http://ec.europa.eu/enterprise/policies/sme/files/support_measures/taxsimple/taxsimp_en.pdf).

**Table 6.1 Simplified tax schemes**

<b>Name</b>	<b>Eligibility criteria</b>	<b>Tax rate</b>	<b>Other characteristics</b>
Small business tax (KIVA)	<ul style="list-style-type: none"> <li>- average statistical headcount not exceeding 25 persons;</li> <li>- turnover not exceeding HUF 500 million;</li> <li>- balance sheet total not exceeding HUF 500 million;</li> <li>- tax number was not cancelled or suspended in the two years preceding the tax year;</li> <li>- balance sheet date of 31 December;</li> <li>- financial statements compiled in HUF;</li> <li>- business year may not differ from the calendar year.</li> </ul>	16%, which replaces corporate tax, social contribution tax and vocational contribution payment obligations	Companies must fulfill tax advance assessment, declaration and payment obligations monthly or quarterly
Small taxpayers' itemized lump sum tax (KATA)	<ul style="list-style-type: none"> <li>- up to a turnover of HUF 6 million; a 40 % tax is payable on the part of the revenue exceeding HUF 6 million;</li> <li>- through paying the lump sum tax, the taxpayer is released from the obligation of paying corporate tax, personal income tax, social contribution tax, healthcare contribution, pension contribution, employment contribution, and vocational contribution.</li> </ul>	Lump sum tax of HUF 50 000 monthly for each full-time employee registered as a small taxpayer (or HUF 75 000 for eligibility for higher social security service)	Monthly payments
Simplified entrepreneurial tax (EVA)	<ul style="list-style-type: none"> <li>- private entrepreneurs, single member companies, general partnerships and limited liability companies can register for it;</li> <li>- the average of the total annual turnover did and does not exceed HUF 30 million;</li> <li>- all members are natural persons and the company does not own shares in other legal entities;</li> <li>- a positive revenue in the preceding two tax years;</li> <li>- replaces the following taxes: value-added tax, entrepreneurs' personal income tax, tax on entrepreneur's dividend base, corporate tax and personal income tax on dividends.</li> </ul>	37%	Advance payments quarterly, and a top-up payment by the 20th of December each year
Simplified contribution to public revenues (EKHO)	<ul style="list-style-type: none"> <li>- only for certain professions: journalists, writers, artists, actors, musicians, professional athletes;</li> <li>- private individuals whose annual income is less than HUF 25 million;</li> <li>- private persons who have income from employment or other legal relationships, on which contributions are already paid.</li> </ul>	20% for the payer and 15% for the private individual	Private persons declare their EKHO income on personal income tax returns.

Source: <http://www.doingbusinessinhungary.com/taxation>.



According to our information, in Moldova, there are also various simplified tax schemes in operation, such as, for example for “liberal professions” or for entrepreneurs with an entrepreneurship patent. Moreover, while the corporate income tax rate of 12% can be considered relatively low, there are different tax rates applied to different professions/company groups: 7 and 18% for individual entrepreneurs, 7% for farming enterprises, 12% for legal entities whose income is estimated through indirect methods and 3% for SMEs below a certain threshold level of income in the previous fiscal year (6250 EUR).

Overall, both systems are made too complicated by the use of different tax rates for different groups of companies. This can be justified on the basis of economic policies favoring certain activities or groups of economic agents. However, the tax systems are made too complicated. Moreover, an unwanted result can be fiscal erosion, because firms (including large ones) may navigate the tax system in order to reduce the amount of taxes they pay.

The clear advantage of the simplified tax schemes over reduced tax rates is that they significantly reduce the administrative burden of taxation for entrepreneurs or individuals with limited resources. Another advantage is that in those countries where the share of the grey/black economy is relatively high, these simplified rules ensure that the whole or at least some of the activities carried out by these economic agents forms part of the white economy. However, for these firms operating in the illegal economy, even reduced tax burdens and/or simplified schemes may not offer enough benefits to be part of the legal economy, and thus to be registered and controlled by the authorities.

One clear disadvantage of a system with various tax rates can be the possibility of arbitrage, especially when tax rates and the income base on which they are based differ for incomes from employment and from entrepreneurship. The interests of employers seeking to minimize labor costs and employees seeking to maximize net incomes coincide in finding the best ways of reducing their tax liabilities. This situation prevails both in Hungary and Moldova. Thus, tax rules should be designed in order to prevent such arbitrage, which may make tax rules even more complex.

Furthermore, the existence of such tax schemes designed “individually” for certain groups of companies and/or private persons introduces distortions and market failures in the economy, with negative consequences for the resource allocation, performance and competitiveness of the economic agents. In the case of SMEs, another problem can be caused by discouraging these firms from growing “out” of the brackets of the schemes, for example by surpassing the required threshold levels of employment or turnover, which need to be fulfilled in order for preferential rates to apply.

Taking into account the advantages and disadvantages, a better way of reducing the administrative burden of paying taxes for companies may be through simplifying tax accounting and/or for calculating the tax base instead of using different schemes with different tax rates.

## **6.2. Online tax reporting system**

Economic agents performing a particular activity are required by law to submit their tax returns to the fiscal authority. Until 2011, each taxpayer submitted these tax reports on paper in Moldova. As of January 01, 2012 however, this method of report submission was substituted by an **electronic service, the “Electronic statement”**. Initially this change applied to the 15,000 VAT payer economic agents from Chisinau, Balti and Comrat, but as of 1 January 2013, the other 10,000 VAT-paying economic agents from the entire country were scheduled to start using the electronic tax service.<sup>4</sup>

Connecting these 10,000 economic agents to an electronic tax service falls within the enforcement of the “Government Action Plan for 2012-2015”, approved in 2012, which stipulates the implementation of a generalized tax declaration system using the information technologies (e-statements), so that 60% of tax returns would be submitted via Internet by 2014.<sup>5</sup> The VAT payer economic agents have to pay lei 550 annually for connecting to the electronic tax declaration system (while those who don't pay VAT are charged lei 340 for using the service).<sup>6</sup> An analysis conducted by the State Tax Service at the end of 2012 regarding the stage of adopting the service “Electronic Statement” shows that the integration efforts of the new service have been successful and the estimated trend should continue.<sup>7</sup>

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<sup>4</sup> “Din 1 ianuarie 2013, toți plătitorii de T.V.A. vor raporta prin intermediul serviciului „Declarație electronică”!”, raport prin intermediul serviciului „Declarație electronică”!”, 31 October, 2012, available on <http://www.contabilsef.md/libview.php?l=ro&idc=290&id=5775>.

<sup>5</sup> “Din 1 ianuarie 2013, toți plătitorii de T.V.A. vor raporta prin intermediul serviciului „Declarație electronică”!”, raport prin intermediul serviciului „Declarație electronică”!”, 31 October, 2012, available on <http://www.contabilsef.md/libview.php?l=ro&idc=290&id=5775>.

<sup>6</sup> “Declarația electronică – primele probleme”, 31 January 2012, available on <http://itmoldova.com/2012/01/31/declaratia-electronica-primele-probleme/>.

<sup>7</sup> “Progrese în implementarea raportării în implementarea raportării electronice de către Serviciul Fiscal de stat”, 26 September, 2012, available on <http://www.egov.md/index.php>

In Hungary, electronic tax services were introduced in February 2004 with the launch of the e-Bevallas (e-Reporting) program of the National Tax Authority. From 1st January, 2007, it has been compulsory to use e-Reporting for all enterprises (regardless of size or activity). Individuals can also use the system, but they are not obliged. There are no registration fees for the use of e-Reporting. The tax authority website offers an electronic framework program for e-taxation, and a specific application for all types of central taxes<sup>8</sup> that exist in Hungary. Reports are prepared (but not submitted) with this framework program that also offers various help/check services (to detect inconsistencies in the reporting).

Regarding the experiences of Moldovan e-Reporting, in an article entitled “Submission of tax returns electronically: advantages, problems and opportunities” in the online magazine focused on accountancy in Moldova, “Contabilsef.md”, one can find some of the commonly raised issues that the economic agents encounter regarding the use of the electronic system of tax returns. These problems are especially common in the small villages and towns of Moldova, where people lack material resources, such as a computer or an internet connection, as well as the necessary skills to use the new tax system.<sup>9</sup>

In some of the comments replying to the article, the users were critical about the day of the trainings organized by “Fiscservinform,” which is every Friday, a working day for all the employees and business owners.<sup>10</sup> According to the “Government Action Plan for 2012-2015”, in order to learn how to use the new electronic service, economic agents can attend free trainings organized by the State Enterprise “Fiscservinform” which are held in the national language and in Russian.<sup>11</sup> One solution proposed by the users that would provide more access to more people is to have the trainings on Saturdays as well.

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[/ro/comunicare/stiri/item/886-progrese-%C3%AEn-implemmentarea-raport%C4%83rii-electronice-de-c%C4%83tre-serviciul-fiscal-de-stat#.U10xCfmSzT8.](#)

<sup>8</sup> The local taxes are not harmonized. Budapest, the capital, and larger cities have online local tax reporting forms, but smaller settlements may not have that.

<sup>9</sup> “Prezentarea dărilor de seamă fiscale înformat electronic: avantaje, probleme, oportunități”, 14 November 2012, available on <http://www.contabilsef.md/libview.php?l=ro&idc=290&id=4513>.

<sup>10</sup> “Prezentarea dărilor de seamă fiscale înformat electronic: avantaje, probleme, oportunități”, 14 November 2012, available on <http://www.contabilsef.md/libview.php?l=ro&idc=290&id=4513>.

<sup>11</sup> “Din 1 ianuarie 2013, toți plătitorii de T.V.A. vor raporta prin intermediul serviciului „Declarație electronică”!”, 31 October, 2012, available on <http://www.contabilsef.md/libview.php?l=ro&idc=290&id=5775>.

Some users complained about time required to fill in the electronic statements and to submit them while other users argued that the system is well designed and implemented. It was claimed that the problem was with the people in Moldova, who are not used to something new and technical, that has been standard practice in more developed countries for several years, without any issues.<sup>12</sup>

In another article assessing the electronic tax return services, many users said they had to spend too many hours in order to understand how the system imposed by the tax authorities worked. Another problem raised was that the site “servicii.fisc.md” was often under maintenance. Nonetheless, there were also taxpayers declaring that the new electronic method saved them time and money.<sup>13</sup>

Last but not least, it was argued that several different methods of tax return submission should have been available for the economic agents during the transition period between the paper reports and the electronic system.<sup>14</sup>

**Besides the e-taxation applications and programs, all e-taxation systems need an entry point, or a portal** that offers a secure identification system for uploading business information. In **Moldova**, individuals, legal entities (businesses) and public authorities can log in and submit their tax return declarations via the “Electronic tax services” (or **servicii.fisc.md**).<sup>15</sup>

The services available here include:

- Electronic statement: the service gives all individuals/legal entities the opportunity to file tax reports with a digital signature or electronic signature authentication;
- Fast Statement: the service is an automated method for creating, checking, and printing statements on income tax. For both services, there are instructions about how to access them.

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<sup>12</sup> “Prezentarea dărilor de seamă fiscale înformat electronic: avantaje, probleme, oportunități”, 14 November, 2012 available on <http://www.contabilsef.md/libview.php?l=ro&idc=290&id=4513>.

<sup>13</sup> “Declaratia electronica – primele probleme”, 31 January, 2012, available on <http://itmoldova.com/2012/01/31/declaratia-electronica-primele-probleme/>.

<sup>14</sup> “Prezentarea dărilor de seamă fiscale înformat electronic: avantaje, probleme, oportunități”, 14 November, 2012 available on <http://www.contabilsef.md/libview.php?l=ro&idc=290&id=4513>.

<sup>15</sup> Website of the Electronic tax services in Moldova (Servicii fiscale electronice): <https://servicii.fisc.md/default.aspx>.

Other services related to access to information are:

- *The current account of the taxpayer* – this service is an online tool for viewing data on taxes and tax liabilities, with each taxpayer having access to his or her own current account;
- *Download Forms*;
- *Verification of tax liability*;
- *About taxpayer*;
- *Online ordering of standardized forms*;
- *E-Invoice* – this is a new software solution designed for economic agents in Moldova for creating, editing, and providing a digital signature and electronic circulation of bills and invoices.<sup>16</sup>

In **Hungary**, e-taxation is submitted through the governmental one-stop-shop portal, “Ügyfelkapu” (“Client gate”), at [www.magyarorszag.hu](http://www.magyarorszag.hu). Among others, the following services are offered:

- Submission of tax reports, information on tax account;
- Submission of social services reports, information on social services accounts (for companies: reporting and status of employed personnel, for individuals: pension account and medical history covered by social securities);
- Registration for (re)issuing ID cards, passports, etc.;
- Land and real estate cadastre;
- Various other services (e.g. filing a complaint for the National Consumer Protection Agency, etc).

The registration method and the identification system for such services are crucial, as they have to ensure safe identification (to avoid misuse) while still being easy to use, and they cannot create additional administrative burdens on tax payers. Once a proper registration and identification system is set up, it can be used for various services, not only on the central governmental portal.

The registration process on the website [servicii.fisc.md](http://servicii.fisc.md) follows three steps:

- Step 1: introducing personal data (as an individual, legal entity or individual registering on behalf of the legal entity) and email address, setting up a password, selecting services;

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<sup>16</sup> Website of the Electronic tax services for business entities in Moldova (Servicii fiscale electronice pentru persoane juridice): <https://servicii.fisc.md/Companies.aspx>.

- Step 2: introducing the Personal Identification Code (IDNP) – or the tax number in the case of a company – the first name, surname and phone number;
- Final step: if the registration was submitted successfully, the user will receive the following message: “You have successfully registered on the portal [servicii.fisc.md](https://servicii.fisc.md). Access to the required services will be provided after having signed The Agreement on Connecting to the Service “Electronic Statement”. For detailed information please contact “Support Center and Contact” of the “State Enterprise ‘Fiscservinform’, at the phone no (22) 822-222”.<sup>17</sup>

The registration in Hungary consists of two main elements:

- First, registration in the online one stop shop portal must be completed, with a personal meeting in one of the government offices (Okmányiroda), presenting the personal ID documentation. This leads to a password-based identification license to the portal;
- Second, the person authorized to sign on behalf of the enterprise has to post a request to the National Tax and Customs Administration stating that now he/she has access to the portal, and he/she is authorized to act on behalf of the company and therefore requests access to the tax-related services;
- It is important to note that other offices (such as local governmental tax offices) also started to use the same registry/identification process, meaning that once someone has access to the portal via his/her personal ID, he or she can also report taxes that are not related to the central National Tax and Customs Administration.

### **6.3. Entrepreneurship education - Moldova and Hungary**

A good practice, without a doubt, is the introduction of entrepreneurship courses. The Foundation Liechtenstein Development Service (LED) Moldova financed and executed a two-year project with Winrok Moldova which was executed between 2008 and 2010. It consisted of three components. 1) Life skills and job search training and assistance to students of Moldovan vocational schools;

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<sup>17</sup> Registration process on the website for Electronic tax services in Moldova: <https://servicii.fisc.md/UserRegistration.aspx>.

2) Entrepreneurship training for vocational school students and unemployed adults and start-up grants for those graduates of entrepreneurship courses who develop viable business plans; 3) Training of vocational school staff in the above two areas to ensure program sustainability (source: <http://led.md/led-moldova/>). According to our expert interviews, the reformulation of the strategy and the introduction of the modified course in tertiary education are being carried out now. It is important to note that trainings for (potential) entrepreneurs are carried out by the Chamber of Commerce, by ODIMM and by microinvesting financial institutions as well.

Hungary does not fare well in international comparison neither in the inclination of people to enterprise nor in the acceptance of the market economy. According to the Global Entrepreneurship Monitor (<http://www.gemconsortium.org/>) 2013 Global Report, in the EU-28 and European comparisons, while entrepreneurial intentions are similar to other European countries, Hungarians seem to spot opportunities and deem their capabilities at a lower level and have a stronger fear of failure. While they respect successful entrepreneurs on average more than in the peer countries, media attention towards them is more limited.

**Table 6.2 GEM 2013 Global report results for Hungary**

	<b>Hungary</b>	<b>EU-28</b>	<b>non-EU Europe*</b>
<b>Perceived opportunities</b>	18.9	28.7	36.8
<b>Perceived capabilities</b>	37.5	42.3	41.5
<b>Fear of failure</b>	44.8	39.8	30.8
<b>Entrepreneurial intentions</b>	13.7	13.5	13.7
<b>Entrepreneurship as a good carrier choice</b>	45.7	56.9	61.5
<b>High status to successful entrepreneurs</b>	74.1	65.5	69.7
<b>Media attention to successful entrepreneurs</b>	28.4	49.0	51.9

\*Bosnia and Herzegovina, Macedonia, Norway, Russia, Switzerland

Source: <http://www.gemconsortium.org/docs/download/3106>.

Moreover, in Hungary, the approval rate for the change to the market economy sank from 80% in 1991 to 46% in 2009 (Source: <http://www.pewglobal.org/2009/11/02/public-opinion-two-decades-after-the-fall-of-the-berlin-wall/>. Unfortunately, Moldova was not surveyed in this project). Hungary scored by far the worst in the country group taking part in the research (the Visegrad countries, East Germany, Bulgaria, Lithuania and Russia), and reached a higher rate only compared to Ukraine (36%). 72% of Hungarians felt in 2009 that they were better-off under communism, by far the worse result among the analyzed countries,

as the penultimate scores of Bulgaria and Ukraine are 62%, while Poland “boasted” with the lowest score of 35%.

The Moldovan project on employment and entrepreneurship education and training can be evaluated as crucial and providing a good practice for those countries, where knowledge about the functioning of a market economy is limited and/or where entrepreneurial ambitions or activities are lower than those of the peer countries. This group contains not only Hungary, but also other countries in the less developed parts of the former Soviet Union or in the Balkans.

There are many strengths of the project besides its content in a narrow sense. First, the students, who are trained, are in a “sensitive” age from the point of view of appropriating these skills. Second, training teachers provides not only for sustainability, but ensures the inclusion of a wider group in the training, with all its possible positive spill-over consequences. Third, hopefully the potential positive outcomes of the project are the increase not only in entrepreneurial activities but also in employability and in the acceptance and understanding of the functioning of the market economy.

#### **6.4. The agriculture and producers’ organizations**

According to the FAO (2013)<sup>18</sup>, 54% of the Moldovan population is classified as rural and agriculture traditionally has been regarded as the main pillar of the national economy. Therefore, 27% of the population is involved in agriculture and 15% in food-processing and marketing<sup>19</sup>, while other sources claim that altogether 33% of the Labor force of the country is involved in agriculture.<sup>20</sup>

Of the total area of agricultural land, as shown in the figure below, about 40% are private limited liability companies, 37% are farms,

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<sup>18</sup> FAO Regional Office for Europe and Central Asia, Agriculture and Rural Cooperation – Examples from Armenia, Georgia and Moldova, in *Policy Studies on Rural Transition No. 2013-2*, available on <http://www.fao.org/docrep/018/ar424e/ar424e.pdf>.

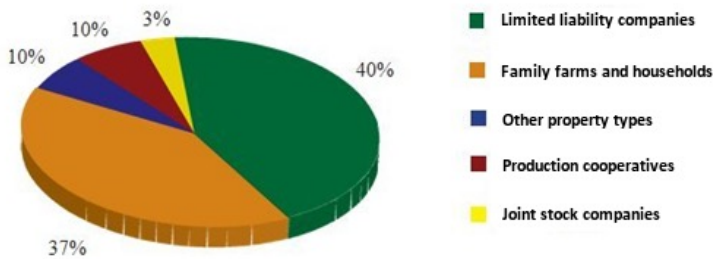
<sup>19</sup> FAO Regional Office for Europe and Central Asia, Agriculture and Rural Cooperation – Examples from Armenia, Georgia and Moldova, in *Policy Studies on Rural Transition No. 2013-2*, available on <http://www.fao.org/docrep/018/ar424e/ar424e.pdf>.

<sup>20</sup> The Agriculture of Moldova, General Data, available on <http://moldovagate.com/ro/article/show/224>.



10% are other forms of property, 10% are cooperative production and 3% are joint stock companies.<sup>21</sup>

**Figure 6.1 The structure of the agricultural land, according to legal and organizational form (% of the total)**



Source: <http://moldovagate.com/ro/article/show/224>

Approximately half of the total area of agricultural land is owned by 300,000 small farmers who own small plots of land, on average about 2.2 hectares of land. Often these plots of 1-2 hectares are divided into 3 or 4 smaller properties/plots that are used for different purposes. In this context some issues arise, such as the limited ability to achieve progress by circulating means of production and improved technology due to parceling, lack of irrigation, lack of finance and high interest rates for loans.<sup>22</sup>

Generally Moldova is considered to have very good conditions for the production of horticultural crops. The main fruits planted are apples, followed by stone fruits, especially plums and cherries, and grapes.<sup>23</sup> Cereal production, including wheat, barley, and corn as well as rape seed, sugar beet, sunflower, soya and tobacco are also significant. Moldova is also one of the largest exporters of walnuts in Europe.<sup>24</sup>

<sup>21</sup> The Agriculture of Moldova, General Data, available on <http://moldovagate.com/ro/article/show/224>.

<sup>22</sup> "Agriculture - a strategic sector for Moldova" <http://www.e-democracy.md/parties/docs/pprm/201209271/>.

<sup>23</sup> Market Research on Fresh Fruits and Vegetables in Moldova, Project Agricultural Competitiveness and Enterprise Development (ACED), December 2011, available on [EMS\\_Fresh&Dried\\_Fruits\\_in\\_Moldova\\_Rom.pdf](#).

<sup>24</sup> FAO Regional Office for Europe and Central Asia, Agriculture and Rural Cooperation – Examples from Armenia, Georgia and Moldova, in *Policy Studies on Rural Transition No. 2013-2*, available on <http://www.fao.org/docrep/018/ar424e/ar424e.pdf>.

Regarding the structure of the market and the distribution of fruits and vegetables, in Moldova there are four permanent wholesale markets: three in Chisinau (called: Izumrud, Sub Pod and Amir) and one in Bălți. Projects based on market research<sup>25</sup> argue that more than 80% of all production is purchased in traditional markets. Although a small factor, but growing in the market of fresh products, modern supermarkets face stiff competition between each other. Some of the major supermarket chains in Moldova are: Fouchette, Green Hills, N1, Fidesco, Metro Cash & Carry, IMC Market Piatiorochka, Unimarket Discounter and Linella.<sup>26</sup>

The concept of “**Producer organization**”<sup>27</sup> was established in 1996 in the European Union with the aim at promoting non-profit collaboration among people producing vegetables and fruits. The concept was to enhance collaboration farms by creating non-profit organizations to reduce costs through collective actions and to sell products jointly. Farmers deliver their products to a commonly used center, where after sorting and packing high and uniform quality products become available to provide to the customers and clients. This helps to reduce the likelihood of damages through a tight vertical integration so that producers can generate more income.

In Hungary, there are at least 46 examples of this type of collaboration. For instance:

- DélKer TЭСZ (Szentes);
- Kiskunsági TЭСZ (Kiskunfélegyháza);
- Kistér Tész (Kistelek);
- Fresh Fruit TЭСZ (Kecel);
- Alföld Régió Szövetkezet (Kecskemét).

DélKer Tész can be regarded as one of the biggest operating since 2002. The center of its production is around Szentes where natural water for irrigation,

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<sup>25</sup> Market Research on Fresh Fruits and Vegetables in Moldova, Project Agricultural Competitiveness and Enterprise Development (ACED), December 2011, available on [EMS\\_Fresh&Dried\\_Fruits\\_in\\_Moldova\\_Rom.pdf](#).

<sup>26</sup> Market Research on Fresh Fruits and Vegetables in Moldova, Project Agricultural Competitiveness and Enterprise Development (ACED), December 2011, available on [EMS\\_Fresh&Dried\\_Fruits\\_in\\_Moldova\\_Rom.pdf](#).

<sup>27</sup> Producer organizations (POs) are the basic actors in the fruit and vegetables regime. The regime requires national authorities to recognize any group of producers that applies for PO status – if they meet a number of requirements, especially that the grouping should: be voluntary, contribute to the general aims of the regime and prove its utility by the scope and efficiency of the services offered to members. For more details see [http://ec.europa.eu/agriculture/fruit-and-vegetables/producer-organizations/index\\_en.htm](http://ec.europa.eu/agriculture/fruit-and-vegetables/producer-organizations/index_en.htm).

good quality soil and plenty of sunlight are available which offers a fertile ground for producing fruit and vegetables of excellent quality. The main source of energy is thermal water, which allows economical heating of greenhouses and plastic tunnels around Szentes, where several thousand families are engaged in fruit and vegetable production. The goal of the organization is to reach out to customers throughout Europe.

The main products are green peppers (yellow, green, red), sharp pointed peppers (green), tomatoes, cucumbers, cabbage (early cabbage), Chinese cabbage, lettuce, tomatoes peppers, watermelon, and apple. The production meets the Quality Standard EN ISO 9001 and HACCP, GLOBALGAP. For processing the products, cold storage of 3700 m<sup>2</sup> and 4000 m<sup>2</sup> is available for the preparation of the goods. The grading, packing and sale of the products is helped by cutting edge sorting and packaging machines in the warehouse.

The given organization had to follow the learning curve: collaboration is a dynamic process and has to be treated and maintained by collective actions. The government is monitoring the performances of TЭСZs and is committed to sharing best practices with the public regarding how to govern towards success within this concept. Nevertheless problems arise at other TЭСZ organizations: fraud and tax evasion were noted in some occasions.

In respect to the farmers associations and their representation in Moldova, producers' organizations are not yet popular. Nevertheless, there are three bodies at the regional and national levels that lobby for farmers' interests and most farmers and their associations are members of one or the other (according to FAO). First, the National Farmers Federation of Moldova (NFFM) was established in 1995 by associations of farmer cooperatives from 29 villages and today it operates through 11 regional organizations across Moldova. Second, the National Union of Agricultural Producers Associations (UAP) composed of 17 Agricultural Associations represents more than 2000 smaller enterprises and almost 25,000 farmers managing 50% of the farmland.

And the third one is the Farmer Federation "Agroinform," established in 2001 as a network of NGOs. Today it maintains nationwide coverage of 27 regional non-governmental member organizations and engages more than 4,000 farmer members.<sup>28</sup> The Federation calls itself "a decentralized structure, where the regional organizations have an independent legal status (...) while maintaining

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<sup>28</sup> FAO Regional Office for Europe and Central Asia, Agriculture and Rural Cooperation – Examples from Armenia, Georgia and Moldova, in *Policy Studies on Rural Transition No. 2013-2*, available on <http://www.fao.org/docrep/018/ar424e/ar424e.pdf>.

a permanent dialogue and co-working relations among four levels: local, regional, national and international”.<sup>29</sup>

A number of other organizations represent farmers, traders and processing companies in specific areas, like the Fruit Producers and Exporters Association “Moldova Fruit”, the Oenologists Union of Moldova or the Sugar Beet Producers Association.<sup>30</sup> The Grape Producers and Exporters Association of Moldova or APESM, for instance, aims to become more competitive on the international market by ensuring the high quality of its products and aligning with the EU standards.<sup>31</sup>

However, small producers who are not involved in any organization face multiple challenges if they want to sell their products in supermarkets. Most farmers often complain about the lack of sales markets. Meanwhile, traders’ requirements for domestic products are far from being met by the small producers. Many farms, because of their size and lack of human resources, can’t meet these requirements. In this situation, experts propose as a solution the formation of Producers’ Associations. “The establishment of producers groups is recommended to promote the commercial interests of the farmers. They will streamline the work of small farmers and producers and will increase the possibility of market production in large stores”, said Lurie Fala, from Agroinform.<sup>32</sup>

## **6.5. The wine industry, clustering and local tourism**

Moldova has a long tradition of wine making, starting in the XVII century B.C. Over the years, the local population learned how to make wine from the Greeks, Romans and closer to our time, in the 1800s from the French, who brought classic

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<sup>29</sup> The National Farmer’s Federation of Moldova (Federația naționalăa agriculturilord in Moldova) Moldova (EN: the Farmer Federation) <http://www.agroinform.md/>.

<sup>30</sup> FAO Regional Office for Europe and Central Asia, Agriculture and Rural Cooperation – Examples from Armenia, Georgia and Moldova, in *Policy Studies on Rural Transition No. 2013-2*, available on <http://www.fao.org/docrep/018/ar424e/ar424e.pdf>.

<sup>31</sup> Grapes Producers and Exporters Association of Moldova (Asociația Producătorilor și Exportatorilor Strugurilor in Moldova) <http://www.apesm.md/>.

<sup>32</sup> “Asociațiile de producători - biletul de intrare în supermarket pentru fermierii mici” 24 February 2014, available on <http://agora.md/stiri/142/asociațiile-de-producători---biletul-de-intrare-in-supermarket-pentru-fermierii-mici>,

grape varieties to Moldova.<sup>33</sup> Apart from the recognized European varieties of wine, local quality wines are made from Rara Neagră, Feteasca, Plavaigrapes, while some of the most well-known wineries in the country are Purcari, Cricova, Ciumai, Romanești, Cojușna, Mileștii Mici.<sup>34</sup>

During the Soviet period Moldova delivered every bottle of wine to the USSR. Even after independence in 1991, Moldova remained the largest supplier on the Russian/CIS wine market. However, experts argued that the embargo imposed by Russia to the wines exported from Moldova in 2006 was a turning point for the wine industry of the country. Consequently, manufacturers chose a new course, developing new styles of wine and promoting their traditional production to a new international market.<sup>35</sup>

In 2010, Russia rejected almost 2 million liters of wine, because it claimed that it contained pesticides. Only 53 wineries in Moldova were authorized to export wine to the Russian market. Many, however, have found other outlets, like the ones from Czech Republic.<sup>36</sup> Also, on June 23, 2010 the Ministry of Agriculture organized a week-long Moldovan Wine Exhibition in Poland, with the hope of attracting investors to Moldova and to increase the sales market for Moldovan wines in European countries.<sup>37</sup>

The Russian embargo was reintroduced on September 10, 2013. In the given situation, the European Commission (EC) proposed the full opening of the EU market to imports of Moldovan wine before the entry into force of the Association Agreement between the EU and Moldova and the Agreement on Free Trade Zone as a measure to compensate for these difficulties. The wine industry is, apparently, strongly connected to promoting **tourism** in Moldova, by specially designed government programs, such as “DrumulVinului” (“The wine road”).<sup>38</sup> The National Program of Tourism: “DrumulVinului in Moldova” aims to boost wine tourism development and its integration into the international network

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<sup>33</sup> “Moldova chooses its path” by Mats Jonson, February 2011, published in the magazine “Dina Viner” (the Swedish wine magazine for connoisseurs and trade people), available on <http://www.suedia.mfa.md/img/docs/traducere-extras-Dina-Viner-februarie-2011.pdf>.

<sup>34</sup> “Drumul vinului in Republica Moldova”, on [http://www.informator.md/ro/despre-moldova/de-vizitat/traditii-vinicole/31\\_drumul-vinului-in-republica-moldova/](http://www.informator.md/ro/despre-moldova/de-vizitat/traditii-vinicole/31_drumul-vinului-in-republica-moldova/).

<sup>35</sup> “Moldova chooses ist path” by Mats Jonson, February 2011, published in the magazine “Dina Viner” (the Swedish wine magazine for connoisseurs and trade people), available on <http://www.suedia.mfa.md/img/docs/traducere-extras-Dina-Viner-februarie-2011.pdf>.

<sup>36</sup> “Zilele vinului moldovenesc la Praga: calitate și marketing” November 6, 2010, available on <http://www.winemoldova.com/presses/view/17>.

<sup>37</sup> “Curge vin moldovenescin Polonia”, June 23, 2010, available on <http://www.winemoldova.com/presses/view/14>.

<sup>38</sup> “Drumul vinului in Moldova” [http://www.informator.md/ro/despre-moldova/de-vizitat/traditii-vinicole/31\\_drumul-vinului-in-republica-moldova/](http://www.informator.md/ro/despre-moldova/de-vizitat/traditii-vinicole/31_drumul-vinului-in-republica-moldova/).

of wine tourism. At present, Moldovan vineyards occupy an area of 107,000 hectares. Moldova is among the top ten wine exporting countries in the world.<sup>39</sup> The “Wine Road in Moldova” includes 29 wineries, out of which the most famous are Cricova, Nisporeni, Milestii Mici, Purcari, Romanesti, Cimisia, Ciurnai, Comrat, Dubasari, Trifesti and Ialoveni.<sup>40</sup> There are also private organizations and projects that focus their work on what is called “Turism vinicol in Moldova” (“Wine making tourism in Moldova”), such as “Wine.md”.<sup>41</sup> This organization promotes trips to several wineries in Moldova that include wine tasting and full services for accommodation, restaurants and visiting the wine factory.<sup>42</sup>

### **Associations of wine producers in Moldova**

“Asociația micilor producători de vinuri din Moldova” (“The Wine Making Small Producers Association in Moldova”) is one of the associations which brings together several producers and their wineries.<sup>43</sup> The aims of the Association are to contribute to promoting the interests of small wine producers in Moldova, attracting investments to the wine sector and the development of best practices in the wine industry. The members of the associations are: Equinox, Et Cetera, Mezalimpe, Pelican Negru and VinăriaNobilă.<sup>44</sup> “Moldova Wine Ghilda” is a non-profit organization founded in August 2007 by several leading private Moldovan wineries. Together, the wineries export more than a third of all Moldovan wine. The wineries are united by the common idea of promoting the country's image as a European country with strong wine traditions. Members of the Ghilda are: Acorex Wine Holding Lion Gri, Chateau Vartely, DK-Intertrade and Vinaria Bostavan.<sup>45</sup>

At the same time there are emerging initiatives of creating homemade wine producers’ associations. According to the president of the Chamber of Commerce and Industry (CCI), Gheorghe Cucu, the idea is to obtain, by joint efforts, bottling

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<sup>39</sup> Programul National in domeniul turismului “DrumulVinului in Moldova”, 2011 <http://www.tur.md/rom/section/283/>.

<sup>40</sup> Moldova te invita sa parcurgi impreuna cu noi drumul vinului, available on <http://www.roportal.ro/articole/moldova-teinvita-sa-parcurgi-impreuna-cu-noi-drumul-vinului--2859.htm>.

<sup>41</sup> Winetourism in Moldova <http://wine.md/content/cat/about-moldova>.

<sup>42</sup> Winetourism in Moldova <http://wine.md/content/cat/about-moldova>.

<sup>43</sup> “Asociația micilor producători de vinuridin Moldova”: <http://www.winemoldova.com/pages/association>.

<sup>44</sup> Membri Asociației micilor producători de vinuridin Moldova: <http://www.winemoldova.com/manufacturers>.

<sup>45</sup> Despre Ghilda Vinurilor Moldovenești: <http://www.moldovawineguild.md/about/ro.html>.

facilities for home made wine, which will then be put on sale. Such practices exist in the Czech Republic, Poland, Romania, and other countries. Manufacturers also believe that an association of homemade wine producers would enable them to increase their sales and to promote their product.<sup>46</sup>

The future of small producers is still questionable, especially after the 2011 report, when over 150,000 grape producers in Moldova were likely to go bankrupt. Moldova signed a loan contract worth 75 million euros with the European Investment Bank (EIB) in the same year for the development of the wine sector. The loan was granted for a period of 12 years with another 12 year grace period.<sup>47</sup> More questions evolve around the right implementation of international funds for the development of the wine sector in Moldova and the success of the small wine producers' associations on the domestic market.

In Hungary, one key support tool for the winery industry is the facilitation of cooperation, especially of clusters. Clusters have been playing an ever increasing role when it comes to regional development and fostering local, regional and even country-wide competitiveness. As the European Cluster Memorandum pointed out: "The strategic importance of clusters for European innovation and global competitiveness is only now becoming fully recognized" (European Cluster Observatory, 2007). Clusters are of critical importance in driving open innovation, a key source of competitive advantages in the global economy. Creating and maintaining clusters in a sustainable way is primarily based on a bottom-up approach rather than fostering their creation in a policy-push (top down) way. However, the government has to pursue such framework conditions that are conducive to form and efficiently maintain clusters.

Hungary has several larger wine-regions (Balaton, Duna, Eger, North-Transdanubia, Pannon, Sopron, Tokaj, etc.), with several small actors besides some larger wineries. Winery-development may coincide with the aim of the Hungarian tourism sector to generate both domestic demand and attract more and more foreigners to come to Hungary.

Two larger wine-cluster organizations have been established (i) North Hungarian Wine-Cluster in 2009 by capturing 4 wine-regions (Tokaj-Hegyalja, Eger, Mátravidék, Bükkalja) and 24 wineries; and (ii) South Transdanubian Wine Tourism Cluster embracing four wine-regions (Pécs, Villány, Szekszárd, Tolna), which have close ties with more than one hundred wineries in the field of wine

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<sup>46</sup> "Producătorii de vin de casă vor crea o asociație", 09 October 2013, available on <http://voceabasarabiei.net/index.php/social/11734-producatorii-de-vin-de-casa-vor-crea-o-asociatie>.

<sup>47</sup> "Producătorii de struguri, în prag de faliment", Ziarul de Gardă, 13 October 2011, available on <http://www.zdg.md/social/producatorii-de-struguri-in-prag-de-faliment>.

tourism capacity, development coordination and in searching for support. The clusters were incentivized through operative programs<sup>48</sup>, by aiming at establishing a common marketing strategy, creating wine-routes, a common qualification system, and fostering collaboration with public and private (for, and not-for-profit) entities having an interest in sparking regional tourism and economic development. The results of this strategy are to be seen in the future. However, promoting cluster development may serve as an efficient policy tool for Moldova as well, thus the exchange of ideas and good practices between the two countries may benefit both sides.

## **6.6. Methodology of measuring SMEs**

Data problems and lack of information about the total population of Moldovan SMEs were repeatedly mentioned by the various experts and representatives of organizations and associations working with these firms during the interviews we conducted with them. While Statistica Moldovei compiles and provides a set of data on SMEs, there is a large discrepancy between the total population of SMEs and the number of registered SMEs on one hand, and those included in these data on the other. The total population of SMEs is estimated to be around 150,000, excluding farmers registered by local administrations, while the data of the statistical office cover 60,000 companies. Moreover, these sets of data and indicators are only a small proportion of what is required by the organizations, associations and government agencies that work on SME issues. The limited human and financial resources of the statistical office explain why it is limited in being able to fulfill its legal and international obligations in terms of the data and indicators published. Furthermore, there are various entities in Moldova, which are SMEs by definitions, but for various reasons they do not provide data to the statistical office, thus they are left out of the official statistics.

Statistica Moldovei publishes data regularly on the number of SMEs, number of employees in SMEs, their share in total sales, sectoral breakdown according to the number of companies and turnover, pre-tax profits and losses. The international comparison is aggravated by the fact that the Office uses an SME definition which is different from that of the EU (though this is justified

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<sup>48</sup> South Transdanubian Wine Tourism Cluster was brought to life with the support of the so-called “Turisztikai klaszterek fejlesztése” (Developing Tourism Clusters) call in 2010.



on the basis of the different levels of per capita GDP; using the EU definition would result in a negligible number of large companies in Moldova).

In the framework of the present project, we have compiled a list of publications and projects dealing with SMEs in Moldova. We have found 14 publications, which directly or indirectly analyze Moldovan SMEs, including scientific publications as well as studies prepared by international organizations (such as the OECD).

In Hungary, partly due to the obligations due to membership in the European Union and other international organizations (especially in the OECD), the Hungarian Central Statistical Office collects and calculates data for various characteristics of SMEs (based on the EU definition of SMEs). Besides the regularly published statistics, occasional publications also deal with the topic (see e.g. <http://www.ksh.hu/docs/hun/xftp/stattukor/kkv12.pdf>). The Central Statistical Office collects information from companies on a quarterly or annual basis, depending on the type of company (e.g. engaged in foreign trade or not). Data can be submitted both electronically and on paper (by fax or by mail). Companies which fail to comply with the data requirements may be fined.

Moreover, there are various surveys carried out by researchers and think tanks on the whole or part of the SME population in Hungary. For example, the internationalization of Hungarian SMEs has been addressed by numerous research projects. (See e.g. Inzelt (2011), Szerb and Márkus (2008) or the results of a survey conducted by the Hungarian Development Bank (Mikešy, 2013). Another frequently addressed topic is the barriers to SME growth (see e.g. GKI's analysis in András et al., 2009) and SME financing, including venture capital (see e.g. Karsai (2013); Némethné (2009) or ICEG EC (2006). Pitti (see e.g. 2011) calculates various statistical indicators for Hungarian SMEs on the basis of the tax declarations of companies. Altogether we could compile a list with 42 scientific publications on Hungarian SMEs in the framework of the present project, the overwhelming majority of which was published recently (after Hungary joined the European Union). Thus, while we cannot say that there is an abundance of relevant information in Hungary, research, policy formation and evaluation can be based on a sufficient and solid information base.

The final solution to the problem is of course complying with the requirements of Eurostat and applying the Small Business Act of the European Union, including the SME Performance Review. In the meantime, a systematic representative survey of Moldovan SMEs, preceded by a pilot survey and supplemented by a set of in-depth interviews with a representative group of SMEs would certainly be required in order to first, have a clearer picture than before about the main

characteristics of Moldovan SMEs, and second, to determine the possibilities (and costs) of extending the coverage of data collection of Statistica Moldovei. This type of database would be indispensable for formulating policies and measuring the efficiency of them. Existing data should be “converted” using the EU standard definitions of SMEs to make international comparisons easier. Public money as well as available foreign financial support should be used for these data collection aims, as at present, projects trying to help local SMEs are in many cases experimenting in the dark. On the other hand, the limited financing may justify carrying out surveys which concentrate only on a few areas, but may result in the collection of information and data, which would be especially relevant from a policy point of view. On the basis of the expert interviews, the following areas may be especially worth analyzing:

- high growth SMEs;
- internationalized SMEs (exporting and/or having invested abroad), including born globals;
- clustering activities of/cooperation among SMEs.

## 7. Roadmap of Proposed Actions

The roadmap prepared in the framework of this project consists of suggested actions and initiatives that are considered relatively low budget and build on the views of various SME associations, representatives of stakeholders and policy actors in Moldova. The exact timing, budget and implementing institutions of these activities should be decided by the local actors.

The team from ICEG European Center will help the relevant actors to establish contacts and to agree on a more detailed roadmap (timing, etc.) that suits all participants of the given initiatives.

### 7.1. Simplified tax, online tax reporting system and one stop shop portal

As the topics considering simplified tax methods, online taxing and governmental one stop shop portals are strongly interlinked and are relevant for the same set of actors, a joint action is proposed in order to realize the synergies across these domains in further development.

**1. Intervention:** twinning actors from the Moldovan and Hungarian side, policy best practices and lessons shared with a closing workshop.

**2. Date:** September 2015 – February 2016.

**3. Persons involved:**

From Moldova: SME representatives, business associations, IT experts and governmental actors/policy stakeholders.

From Hungary: SME representatives, business associations, Association for the Reduction of Administrative Burdens (SZABASZ), IT experts and representatives of the Hungarian National Tax and Customs Authority as well as representatives of NISZ (National Infocommunication Services, responsible for operating the governmental one stop shop portal).

**4. Justification:** Hungary has significant experience with simplified tax schemes, e-Taxing as well as with offering other relevant services for businesses via an online one stop shop portal. Although there are still many functions

to develop, there are already a number of services that could be useful to share with the Moldovan counterparts. E-Taxing is a major tool that can be used to reduce administration for the public sector and make taxation more transparent with up-to-date information. But the willingness of the business sphere to be partners in this exercise strongly depends on other factors, one being the public sector's capacity to provide valuable services for a major group of their "customers" – the enterprises.

**5. Description of the activity:** The basis of the activity is a twinning exercise between the relevant stakeholders from both countries: business associations and representatives of SMEs, policy and governmental actors and IT experts. The knowledge share element can be enhanced by a joint workshop that discusses the lessons learned by the twinned actors in their own areas of interest/responsibility.

**6. Expected outcomes:** the following topics should be discussed and the outcomes will support the Moldovan government to develop its services and benefit Moldovan enterprises: a) for governmental actors: simplified tax schemes – how they work, what are the criteria to enter these schemes, how these schemes influence the willingness of companies to administrate their revenues/costs and to pay their taxes; b) simple e-Taxation models including filling out forms with sufficient help/support tools, online tax reporting, online tax balance accounts; c) developing other online services for businesses (in the fields of employment registration, pension and health insurance coverage, land registry, legal registries – online company databases, etc.); d) operating the services – experiences on the side of the public sector.

For business associations and representatives, the following topics are recommended to be discussed in the twinning exercise: a) willingness of enterprises to enter and use the services offered; b) developing a "guild" method – realizing that those companies that follow the law and proper administrative methods will have to distinguish themselves from those that do not follow the law. In return, they have a strong legitimacy to push the government into better regulation; c) online services that are useful for businesses and urging the government to develop them; d.) technical and practical elements of how the use of electronic services can be learned and practiced by even small companies.

For IT experts, the technical details of building the relevant governmental databases, the electronization procedure of existing public information and the operational good and bad practices regarding these services can be shared.

At the workshop closing the twinning exercise, all actors can share the knowledge gained and can discuss the pros and cons of the future simplified

tax and online service development in order to reach a common statement that can be accepted by both the government and the business sphere and can be considered realistic from the IT point of view.

## **7.2. Entrepreneurship courses**

It is important to note that the experience of Moldova could also be used in Hungary and/or in other Visegrad countries + Georgia and Ukraine.

**1. Intervention:** raising awareness of the importance of entrepreneurship education and of courses aimed at “teaching” students aged 10-18 years about the basics of the functioning of a market economy; training the teachers who take part in the project possibly through a study tour to Moldova.

**2. Date:** May 2015 – December 2015.

**3. Persons involved:**

From Moldova: experts involved in the elaboration of course material and organizations which implemented the program: Foundation Liechtenstein Development Service (LED) Moldova and Winrok Moldova.

From Hungary: representatives of the ministry responsible for education (Ministry of Human Resources) and representatives of various teachers’ organizations (Democratic Trade Union of Pedagogues, Union of Hungarian Pedagogues etc.).

**4. Justification:** as was already described in detail, Hungary does not fare well in international comparisons, neither in the inclination of people to start a business nor in the acceptance of the market economy. Hungarian teachers as well as students lack knowledge about how the market functions. A program, the aim of which would be the introduction of an entrepreneurship course in the curricula, would increase not only the inclination to start a business, but would also provide knowledge about the functioning mechanisms of the market economy and thus it would increase employability as well as acceptance of the market economy.

**5. Description of the activity:** the first part would consist of study trips to Moldova by Hungarian stakeholders, with the aim of consultations with local participants in the program and attending relevant classes in secondary schools, as well as consulting the detailed description of the course and teaching methods used. Second, the adaptation of the course material for the use in Hungarian primary and/or secondary schools should be carried out by relevant experts (External/additional financing is needed for that activity).

**6. Expected outcomes:** The potential positive outcomes of the project are the increase not only in entrepreneurial activities but also in employability and in the acceptance and understanding of the functioning of the market economy in Hungary, through training students at a “sensitive” age from the point of view of the appropriation of market economy principles and entrepreneurship knowledge. Not only the students, but also the teachers involved would appropriate this knowledge. As another outcome, an increase in the employability of all the teachers and students involved can be expected.

### **7.3. Agriculture and producers’ organizations (POs)**

**1. Intervention:** study tour and sharing of knowledge, exchange of experiences in the fields of producers’ organizations; furthermore, developing assistance initiatives to business organizations.

**2. Date:** May 2015 – December 2015.

**3. Persons involved:**

From Moldova: representatives of agricultural associations, representatives of the industry – small entrepreneurs as well as major supermarket chains, policy actors (responsible for agriculture, trade and economic development).

From Hungary: policy actors from the Ministry of Agriculture, as well as representatives of existing POs (For example South Plains Fruits and Vegetables PO – successfully present in big market chains, <http://www.delkertes.hu/>, Address: 6600 Szentes, Szarvasi Str. 3/b, Tel: 00 36 63 311 411, several more producers’ organizations are listed here: [http://www.fruitveb.hu/index.php?option=com\\_weblinks&view=category&id=1:tagok](http://www.fruitveb.hu/index.php?option=com_weblinks&view=category&id=1:tagok)). Ideally, representatives of major supermarket chains can also be contacted in order to collect feedback on PO’s performance.

In addition, a representative from the European Commission can share European level experiences or other international actors: <http://www.copa-cogeca.be/Menu.aspx> can be invited.

**4. Justification:** Small producers in agriculture often find it hard to break into a relevant market (small local markets are often overloaded with the same seasonal products, larger markets are hard to reach and cannot be served with small quantities/uneven quality of products). A potential solution is to form a producers’ organization that manages joint activities such as labeling, packaging, marketing,

etc. while the production is still carried out by individual farmers/producers. This way the output of smaller producers can also enter in large markets.

**5. Description of the activity:** the activity starts with a study trip to Hungary and visiting existing POs as well as having a discussion with Hungarian stakeholders from the agricultural side as well as from the policy aspect. In the next phase an international workshop would be organized in Moldova, with the participation of international actors, as well as the representatives of large supermarket chains, to discuss the criteria which the products shall meet in order to get them into the large markets, and then to discuss how POs can meet that criteria. Finally, in the form of a workshop discussion and later in writing, assistance initiatives should be elaborated to support the Moldovan POs.

**6. Expected outcomes:** It is expected that the participants will learn and gain new knowledge regarding the: a) international situation and background of POs; b) setting up a PO (initial phase); c) management of a PO and facing basic problems, issues (standardization, marketing, negotiating with large buyers, liquidity management, etc.); d) overcoming the negative historical experience with communist cooperatives and convincing farmers to cooperate in POs. The lessons learned will help the Moldovan stakeholders to form their own POs according to international experiences but also according to the special needs of Moldovan producers and potential buyers.

## **7.4. Wine industry clustering and local tourism**

**1. Intervention:** study tour and exchange of experiences in the fields of wine clustering and developing wine tourism on a regional basis

**2. Date:** May 2015 – December 2015

**3. Persons involved:**

From Moldova: representatives of the Moldovan wine industry, representatives of wine and tourism related associations (Wine.md, Moldova Wine Guild, Wine Lovers Club Moldova), representatives of regional development (ACSA <http://www.acsa.md/index.php?l=ro>, Rural Investment and Services staff – CAPMU, with WB financing, <http://www.capmu.md/>, etc.), Tourism Agency of Moldova, [http://www.turism.gov.md/index.php?pag=proiecte\\_finalizate&opa=view&id=5&start=&l=](http://www.turism.gov.md/index.php?pag=proiecte_finalizate&opa=view&id=5&start=&l=), etc.) representatives of policy stakeholders from the Ministry as well as from ODIMM.

From Hungary: representatives of the South Transdanubian Wine and Tourism Cluster ([http://pannonborklaszter.hu/klaszter\\_fooldal](http://pannonborklaszter.hu/klaszter_fooldal), contact: Address: 7625 Pécs Vince u. 9/2., Tel: 0036 72 783-381, Fax:0036 72 783-381, E-mail: [ddbklaszter@gmail.com](mailto:ddbklaszter@gmail.com), Cluster manager: Ms Boglárka Dóra Kovács, 0036 30 332-8608) as well as representatives of regional development agencies (South Transdanubian Regional Development Agency, <http://www.deldunantul.com/>, Address: 7621 Pécs, Mária u. 3., Tel.: 0036 72 513-760, Fax: 00 36 72 513-768, E-mail: [info@deldunantul.eu](mailto:info@deldunantul.eu)) and representatives of Hungarian policy stakeholders (due for elections in the spring of 2014). The exact structure and responsibilities of the ministries are under formulation – no contact person can be named, but policy stakeholders from the Ministry of Agriculture should be contacted, as well as from the Ministry of National Economy responsible for tourism development. The latter is also responsible for the SZEP card which is a popular mechanism among the low-taxed cafeteria plan items in employment schemes and favors domestic tourism.

**4. Justification:** The research and the discussion with relevant experts clearly demonstrated the need to focus on the wine industry of Moldova which is undergoing a structural/marketing change. After independence, the role of small wineries gained importance compared to large “factories”, and Western markets became more relevant, although the Russian market was still essential (until the embargo). To create more diverse demand, it is elementary to enhance the role of domestic interest for quality wine, ideally together with the development of rural tourism. On the one hand, this needs increasing domestic demand, but on the other hand, improving services, promotion, marketing, clustering and joint development strategies are needed on the supply side. As Hungary has already taken major steps in this area, a study visit would be instructive for both parties.

**5. Description of the activity:** A study visit of the described Moldovan stakeholders to the South Transdanubian part of Hungary, visiting wineries, visiting the Cluster office and management, and sharing good practices. A meeting with the actors from the South Transdanubian Regional Development Agency would be organized, and potentially with local policy actors of Pécs, Szekszárd and Villány – cities close to main wine regions. In addition, meetings would be organized – either in South Transdanubia or in the capital, Budapest – with the policy stakeholders from the relevant ministries to see the available support mechanisms for the wine industry, clustering and developing domestic tourism.

**6. Expected outcomes:** It is expected that the Moldovan visitors gain experience both related to the: a) wine industry and local tourism (how a small enterprise running a winery also starts to open up a local accommodation place); b) related to clustering and cooperation (how small rural wineries cooperate with small restaurants, bakeries, handmade textile producers, etc. to create a set



of services that altogether are interesting enough for a long weekend trip for a family from a large city); c) related to local governance (how the mayor of a village/city manages to organize a festival that draws attention from people outside of the region as well and brings tourists in); d) how the ministry responsible for agriculture can act in order to protect quality producers of wine; e) how the ministry responsible for tourism can create initiatives that boost domestic demand, etc.

## **7.5. Methodology of measuring SMEs – data collection**

**1. Intervention:** elaborating detailed guidelines for collecting data based on the practices of the Hungarian Central Statistical Office and on the experience of various Hungarian research institutes in carrying out representative surveys of various groups of SMEs (depending on the interests of the involved parties, e.g. quickly growing gazelles, innovative SMEs, internationalizing SMEs, sectoral groups of SMEs etc.) and looking for the financial resources available for conducting the SME survey and for additional work on SME data at the statistical office of Moldova.

**2. Date:** November 2014 – May 2015.

**3. Persons involved:**

From Moldova: representatives of ministries (especially the Ministry of Economy) and of government agencies (especially ODIMM) and various company and SME associations, chambers of commerce, for whom up-to-date and detailed information about SMEs in Moldova would be indispensable; and the representatives of the Statistica Moldovei, which is responsible for publishing and compiling data on SMEs.

From Hungary: representatives of the Hungarian Central Statistical Office ([www.ksh.hu](http://www.ksh.hu)), who calculate data on Hungarian SMEs, Hungarian researchers and experts, who already carried out SME surveys or worked with data on SMEs (such as Annamária Inzelt, IKU, Pénzügykutató Zrt, László Kállay, Corvinus University of Budapest, Balázs Muraközy, Research Centre for Economic and Regional Studies, Hungarian Academy of Sciences; László Szerb, University of Pécs).

**4. Justification:** As described in detail in a section above, the available data published by Statistica Moldovei has been criticized by the various organizations, associations and government agencies in Moldova for not being detailed enough and having a sporadic coverage of the total population of SMEs in Moldova.

Moreover, detailed information is missing about the possible target groups of policy intervention among SMEs. As a positive example, a survey, conducted with the financial support of international organizations is cited by various experts, which could provide more detailed data on SMEs in Moldova. If financial support would not be available to cover the costs of a survey of the total population of Moldovan SMEs (including unregistered ones), a survey of the certain subgroups of SMEs can be carried out supplemented by in-depth personal interviews.

**5. Description of the activity:** Based on expert interviews conducted on the one hand at the Hungarian Central Statistical Office and on the other hand with Hungarian researchers carrying out surveys and/or working with data on SMEs, a detailed overview of the practices used in Hungary for SME data collection would be provided on one hand, and on collecting survey data for a certain group of SMEs, on the other hand. The criteria selection of the sub-group should be determined by the ministry or government agency which would use the data. The dissemination of the information could be carried out through organizing a workshop either in Budapest or in Chisinau with the participation of the stakeholders listed above.

**6. Expected outcomes:** As a best case scenario, we expect an improvement in the SME data available in Moldova. As a minimum output, we expect that in the future, a survey covering at least a sub-group of the most interesting SMEs from the policy point of view will be carried out. These data would be handed over to the department of the Ministry of Economy dealing with SMEs and to ODIMM, which is organizing support for SMEs, as well as to company associations and chambers of commerce. In our understanding, policy design would be helped to a great extent by this dataset.

## **8. Further Topics for Long-term SME Development**

The European Commission published its 2014 Competitiveness Report with the title “Helping firms grow”. Although the opinions expressed in the report are those of the external experts and do not represent the European Commission's official position, the report itself provides insights into the European Commission’s competitiveness and SME policy.

The policy question, if policymakers should help/promote the internationalization of SMEs and if yes, how – is valid for Moldova as well, where the internationalization of SMEs is well below the level of the EU-28, indicating their weak competitiveness in international comparison.

The findings of the study, which are based on various new and linked data sources, emphasize the importance of both internal to the firm and external to the firm factors in shaping and influencing internationalization.

Internal to the firms factors include various firm characteristics: the size, the age, the ownership structure and the industry of SMEs; and firm-specific advantages: innovativeness, skill intensity and productivity. On the other hand, external to the firm factors include home country characteristics: export barriers, business regulations, export promotion programs, export credits and the level of competition; and host country characteristics: distance from the home country, size of the market, barriers to import, cultural and political differences.

The main policy dilemma arises in finding the right mix of general, indirect policies (improving framework conditions) and targeted, direct policies. General policies can be preferred because of their non-distorting nature; however, targeted policies can be justified on the basis of the heterogeneity of firms, SME subgroup-specific market failures and limited resources for helping SME internationalisation.

Indirect policies include policy measures, which support firms’ innovation activities (e.g. improving education), enhance a competitive business environment, encourage smart specialisation strategies etc., i.e. indirectly promote firms’ productivity, growth, competitiveness. They are crucial in influencing and addressing the main drivers of company-specific advantages. Because of links between firms’ growth, productivity and internationalisation: general policies,

which improve productivity, innovation, skill intensity, indirectly promote internationalisation. Furthermore, they are important tools of addressing certain external factors (regulatory and bureaucratic barriers; further elements of transaction costs of exporting to or investing abroad). On the other hand, they can address the improvement of infrastructure, especially its certain elements, which are in connection with transport or ICT costs (which can be perceived as trade costs in a broad sense – transport for manufacturing goods and ICT for services).

Direct or targeted policies can address specific groups of SMEs, on the basis of links between various SME characteristics and internationalisation (e.g. exporting/FDI to/in non-EU markets, first-time exporters/young SMEs, mode of internationalisation etc.). Policies affecting various areas of firm-specific advantages (productivity, technology, innovation, skill-intensity etc.) may affect indirectly their internationalisation performance.

Further policy recommendations may be of special importance for Moldova on the basis of the findings of our project:

1. Increasing the awareness of the benefits of internationalisation for SMEs;
2. Finding the appropriate (and financeable) mix of direct and indirect policies (no single policy measure);
3. Especially: reducing administrative/regulatory costs of internationalisation, improving the infrastructure/business environment;
4. Targeted policy measures to correct market failures hitting SMEs and especially subgroups of SMEs.

### **8.1. Reduction of administrative burdens – identification of main “irritation” issues in a consultation series**

The financial-economic crisis started in 2008 hit Hungarian enterprises to a large extent. In order to support them in raising their competitiveness but without the presence of major available public funding, the government started a campaign of reduction of administrative burdens.

Administrative burdens (“red tape”) are the economic burdens imposed on a) enterprises; b) citizens; c) civil actors, NGOs; d) on the public sector itself by regulation. The administrative burdens are not the same as administrative costs (which are related to the existing administrative needs of the given actor). The administrative burden is imposed on the actors. Regulation in most cases

is justifiable, several rules were created in order to protect certain values, groups, well understood interests. But smart regulation and smart governance principles express the need to reduce unnecessary burdens while keeping useful regulation in place.

Potential beneficiaries of the reduction of administrative burdens: businesses and other legal entities, citizens and the public sector (creating, administering and enforcing regulation) can also benefit. Among businesses, we can differentiate according to: a) size (large, mid-size, small businesses); b) sector (sector-specific regulations, like for agro businesses, or reducing burdens for businesses NOT active in specific sectors e.g. not working with hazardous materials, etc.); c) life cycle (easing the start of a business, not requiring “zero” reporting if certain activities are not taking place, etc).

As part of the government’s initiatives between 2009-2011, a large national consultation series was launched in 2011, aimed at involving several stakeholders and at identifying the most important areas where the reduction should take place. The participants were: SME representatives (owners, executives), local chambers of commerce branches, various business and trade associations, experts and relevant public sector actors from the given fields (from the Ministry of Human Resources regarding employment, education, training, from the National Tax Authority regarding reporting of taxes and social obligations, from the Ministry of Agriculture regarding regulation on agriculture, etc). More than a 100 events (workshops, conferences) were held across the country and an online problem reporting scheme was offered.

More than 3000 problems were reported, and over 2000 solutions were suggested (many similar or overlapping, of course). Three main types of suggestions were made:

A) Suggesting the reduction or elimination of certain administrative burdens, regulations;

B) While acknowledging that the certain administration should be done, the task was suggested to be taken over by the government (mainly one stop shop solutions);

C) Some suggestions were made that on short term even would increase administrative burdens, but on a longer term would ease doing business for the business actors (in order to lessen business-to-business debts, in order to increase responsibility of company owners/managers therefore protecting those doing business with them, protection from black market actors, etc.).

The following key topics were identified:

- Sector-specific issues (tourism, agriculture, trade, etc);

- Tax reporting and accounting;
- Administration of employment;
- More simple and transparent law-making;
- Electronization, e-Government;
- Connecting already existing databases (reducing reporting for companies);
- Simplification for micro companies;
- Various authorities, permits (building, etc);
- Simplification of administration at issues handled by local governments;
- Simplification of applying for grants (EU grants managed by HU govt, etc);
- Public procurement;
- Speeding up and cutting costs related to judiciary matters;
- Setting up new business locations.

As the results of the consultation campaign, several measures were taken, for example the simplification of parallel reporting to the Tax Authority and the Statistical Office, raising the threshold for compulsory auditing of accounting books (accounting, reporting still compulsory), simplification of licensing road usage for large agricultural vehicles, further improvement of one-stop-shop governmental services (physical and electronic).

There were several problems as well. Business actors were not given proper feedback on what follow-up steps were made and were not properly involved into the later phases, and various groups were hard to win to the cause (e.g. the auditors, or specialists in providing consultation on those administrative needs). Unfortunately, the motivation of the public sector actors to cut red tape was not continuous in a longer period.

The reduction of administrative burdens is a useful tool for SME support and development, but the policy stakeholders shall be consistent on a longer term, and the administrative burden should be constantly monitored in order to achieve real success in the area.

## 9. Conclusion

The White Paper prepared in the framework of the project focuses on the small and mid-size businesses of Moldova and how their contribution to the economic growth in Moldova can be enhanced through using various best practices from Hungary and the other Visegrad countries. The analysis is based on an economic overview of the country and information gained during the project (analysis of available statistics, literature review, expert interviews, questionnaire survey and two workshops), and analysing various best practices and lessons learnt from SME development in the Visegrad countries, and especially in Hungary.

Moldova is a small, open economy, with one of the lowest per capita GDP in Europe and one of the highest shares of population working abroad. Its economy is specialised mainly on agriculture and food products and textile-clothing products. The country's economic ties are "ambidextrous": while the importance of the EU27 grows in terms of foreign trade and foreign direct investments, the role of the CIS countries is still characteristic. Another important feature is the role of migration and remittances that play a crucial part in maintaining, supplementing or simply ensuring the income level of the population while causes a lack of sufficient resources in terms of tax-base and in certain areas employable and skilled people. While at first glance, Moldova and Hungary seem to be worlds' apart, certain similarities still allow for building on the lessons learnt from Hungarian (and other Visegrad 4) experiences. These are among others the following: finishing transition from the planned, socialist economy to a market economy; landlocked economies with high openness; agriculture with long tradition and employing a relatively high share of the population.

SMEs form a very significant part of the economy of Moldova. The information we collected from various sources and analysed, concentrated on three areas: first, the main characteristics of Moldovan SMEs, second, the main barriers to SME operation, entry and growth, and third, policies affecting Moldovan SMEs directly or indirectly. First of all, it has to be noted, that one of the main problems the project team had to face and cope with was the lack of detailed and internationally comparable data on Moldovan SMEs. As far as the main characteristics of Moldovan SMEs are concerned, their important,

though declining share in GDP and employment; very low average size; labour intensive services and manufacturing as their main activity, technological backwardness, and low level of innovation came out from the review of the literature and analysis of available data and was reinforced by the expert interviews. Second, concerning the main barriers to SME operation, entry and growth, access to finance, bureaucracy and high administrative burden, corruption/illegal economy were singled out by the expert interviews as the main hindering factors. Our questionnaire survey indicated an overlapping with the previous ones list of factors, in the order of importance: monopolisation/excessive market power of some participants, barriers to exports to foreign markets, informal economy, corruption/clientelism, favouritism; lack of experience in foreign trade (EU in particular), political instability, weak judiciary – and high cost of credit. The information gained from the expert interviews and questionnaire survey and supported by the opinions of the participants of the two workshops, was more or less in line with those listed by the literature, however, the relative importance of these factors seem to change over time. Third, as far as direct or indirect SME policies are concerned, the regulatory and institutional framework can be assessed as relatively developed, though the administrative burden and the number of companies operating outside the legal economy is high. Specific SME policies try to address these problems, and also improve access to finance, provide specific trainings targeting SMEs in need, however, they remain small both in terms of importance and in terms of resources. Experts noted the lack of policy dialogue and thus the need for identifying the most important policy tools for helping SMEs. As for policies indirectly affecting SMEs, innovation policies are centred exceedingly on the Academy of Sciences, and there is a low participation of SMEs in international comparison in public procurement. Furthermore, the policy lessons learnt from the experience of Visegrad countries in these areas were also enumerated.

Based on the analysis of the information gained during the project, the Hungary-Moldova team identified six areas/cases relevant for SME development. The validation workshop confirmed the importance of these areas. Our selection was based on the high importance of agriculture for Moldova and Moldovan SMEs, on the problem with the administrative burden and with the availability of statistical data on SMEs. In these cases we took a look at the Moldovan situation and brought in lessons from Hungarian experiences (or in one case, vice versa). The six domains are: simplified tax schemes, online tax reporting, entrepreneurship education (a Moldovan good practice), agriculture and producers' organizations, the wine industry and issues of measurement of the SME sector. The first workshop reinforced the importance of agriculture and supporting SMEs there from the point of view of the Moldovan economy. The validation workshop showed that from the point of view of SMEs, high taxes

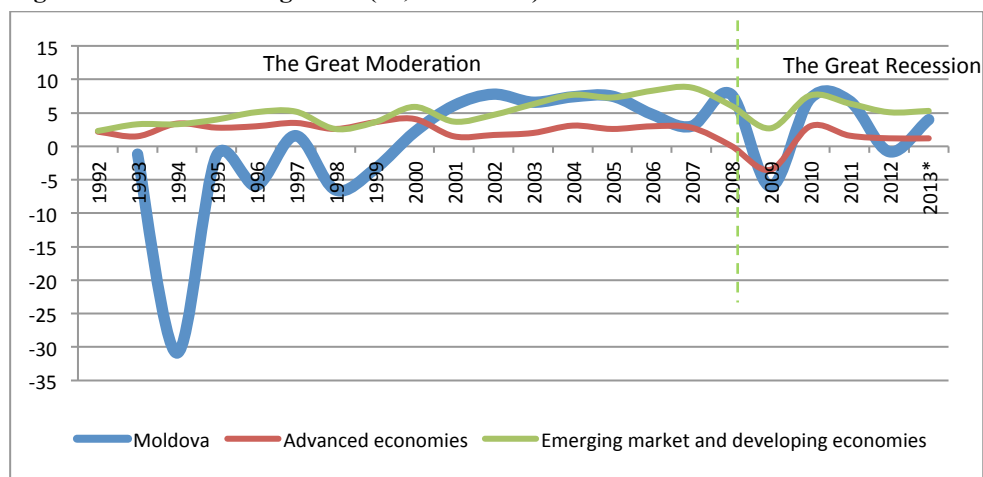


and administrative burdens were the first on their list of barriers. On the other hand, representatives of the ministries underlined the problems with lack of data, and the grey/black economy and corruption, which hinder their work the most. On the basis of these, we draw up some potential intervention schemes for Moldovan stakeholders in order to further investigate these cases and to support the knowledge gathered in favour of the Moldovan SMEs.

## Appendix 1. The economic features of Moldova

Until the mid-2000s, *the Moldovan economy converged to the emerging markets and developing economies in terms of GDP per capita*. Moldova's economic growth showed a good performance in the 2000-2008 period, but the global economic crisis had a strong negative impact on the country (See Annex Figure A.1.1).

Figure A.1.1 Real GDP growth (% , 1992-2013)

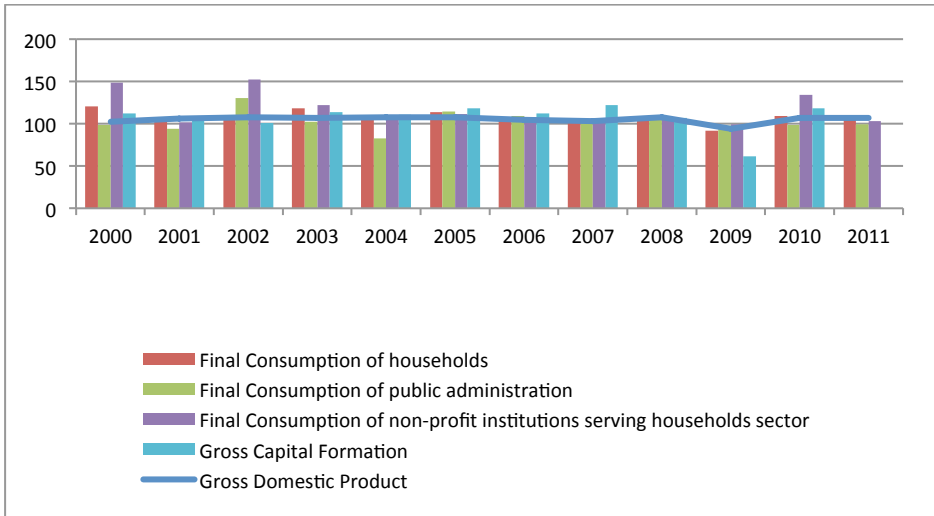


Source: World Bank.

Additionally, there was a significant decrease in FDI during the crisis period (from 2008 to 2009, the inflow of FDI fell by more than 83%, see: EBRD, 2010).<sup>49</sup> The 2008 financial and economic crisis had substantial repercussions in the CIS countries as they are dependent on countries from which remittances are transferred and the main energy resources are imported. *The role of remittances is crucial for the economy*, as they account for one-third of the Moldovan EUR 4 billion GDP. In Moldova, *the recession was even deeper than in the advanced economies*. The economy shrunk by 6% in 2009 (See Annex Figure A.1.2).

<sup>49</sup> While FDI as a percentage of grossed fixed capital formation was 30.9% in 2005-2007, its rate diminished substantially to 9.5% by 2012.

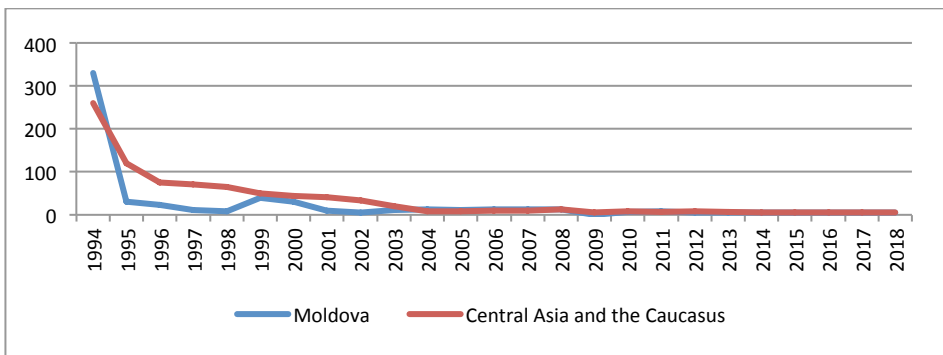
**Figure A.1.2 Growth of GDP and its selected components (%)**



Source: World Bank, National Accounts of Moldova.

SME development depends heavily on the economic conditions influenced by monetary and fiscal policies. While the first one affects financial stability (e.g. performance of the banking sector, integration of capital markets influencing investment activity along inflation trends etc.), fiscal policy can create the capacity to support SME development *via* various actions pervading the whole spectrum of economic policymaking horizontally. **Monetary policy has been strict** in ensuring low inflation since the mid-1990s (see Annex Figure A.1.3). However, **there are many shortcomings in the operation of the banking sector** which have repercussions on SME development.

**Figure A.1.3 Growth of GDP and its selected components (%)**



Source: Statistica Moldovei, World Bank.

**Fiscal policy was to reduce deficit and debt accumulation** through realizing primary surpluses. The debt-to-GDP ratio hit a historical record in 1998 by hovering around 160% of GDP. This high debt was then *conspicuously consolidated* first through a cold shower fiscal consolidation and then through a gradual and permanent consolidation. Still, the primary expenditures cascaded upwards from 2001 to 2009, manifesting serious deficit problems (i.e. 15% of GDP, in 2009). This left the **fiscal discretionary role quite limited** in dampening the recessionary effect of the crisis. Consequently, due to the small maneuvering room of fiscal policy, **public support to SMEs has been relatively weak**.<sup>50</sup> To highlight one specific aspect: SMEs can benefit from eGovernment, however, its infrastructure requires high initial investments, (including in human capital), which is problematic in the present fiscal environment with the lack of public funds for eServices.

The Moldovan **business environment** is far from efficient. Doing Business 2014, prepared by the World Bank, ranks the country 78<sup>th</sup> out of 189 economies. Although it has improved compared with 2013 (86<sup>th</sup>), there is still much room for improvement. Accessing and getting electricity is rather costly and problematic (in this regard, the country ranks in the 165<sup>th</sup> position), bureaucratic regulations inhibit the process of dealing with construction permits (174<sup>th</sup>), and trading across borders faces major difficulties (150<sup>th</sup>). As a corollary, **international competitiveness is relatively low** (i.e. World Economic Forum's Global Competitiveness Index ranked Moldova 87<sup>th</sup> out of 144 countries in 2012-2013).<sup>51</sup>

In terms of **social development**, the United Nations' Human Development Index (HDI) indicates that the Republic of Moldova stands in the medium category of human development. It was 113<sup>th</sup> out of 187 countries considered in 2013 (UN, 2013). Between 1980 and 2012, Moldova's life expectancy at birth increased by 5 years, mean years of schooling increased by 3.3 years and expected years of schooling decreased by 0.2 years. Contrastingly, the Moldovan GNI per capita decreased by almost 28% in the period 1990-2012. From a broader perspective, this kind of progress is above the average of countries in the medium human development category, but below the average of countries in Europe and Central Asia. With respect to the issue of how equal this progress is in terms of HDI, the inequality adjusted HDI can be taken into account. It reflects more and more inequality over time in Moldova. For instance,

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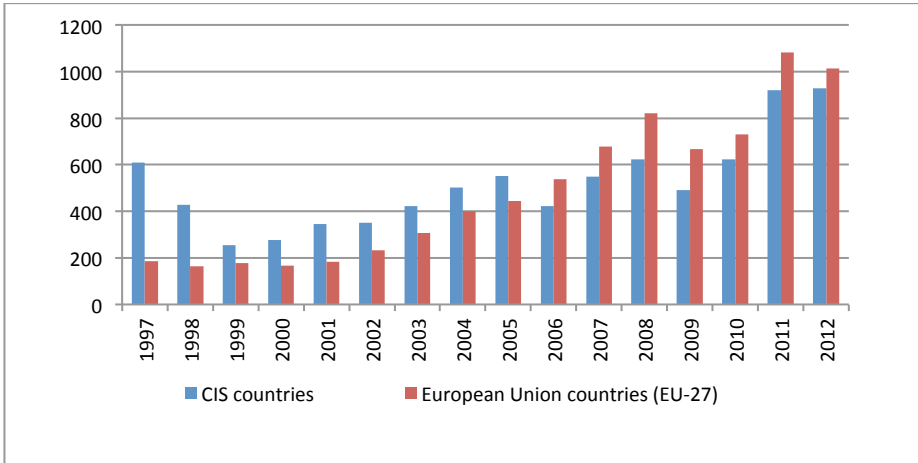
<sup>50</sup> See: OECD (2013): SME Policy Index 2012. Available <http://www.oecd.org/globalrelations/psd/SMEEasternPartnership.pdf> Accessed on 21.05.2014.

<sup>51</sup> See <http://www3.weforum.org/docs/CSI/2012-13/Moldova.pdf> Accessed on 20.05.2014.

the World Economic Forum ranks Moldova in 52<sup>nd</sup> place in its Gender Gap Index 2013 out of 136 countries.<sup>52</sup>

Concerning **export and import tendencies**, exports to CIS countries decreased slightly from 2008 to 2009. Since then, they have recovered and have been growing dynamically. (See Annex Figure A.1.4). This also holds for imports from CIS countries.

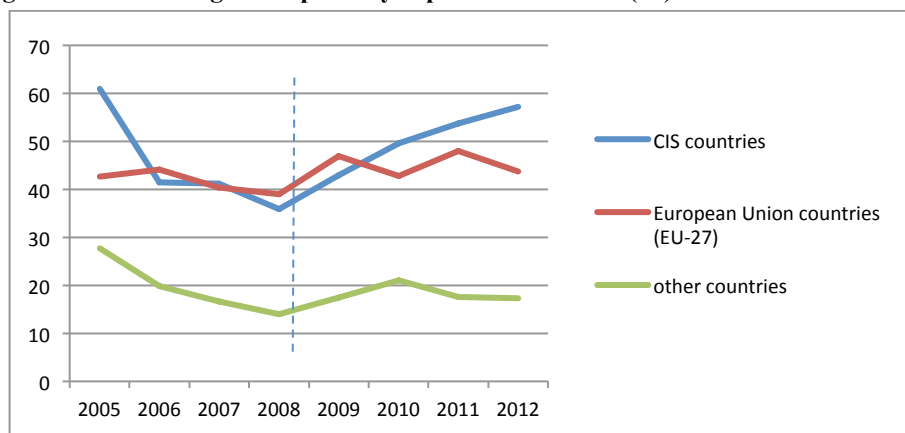
**Figure A.1.4 Export of goods (million USD)**



Source: World Bank.

As far as imports from the European Union is concerned, a 33% decline was documented by 2009 compared to the level of 2008. The trajectory of the coverage of imports by exports as a percentage of the total does not seem to illustrate the harmful effects of the recent crisis on export activities. Right after 2008, the coverage of imports by exported goods and services started to rise in all directions (See Annex Figure A.1.5). In 2012, the top five countries to where Moldova exported were: Russian Federation (accounted for 31% of total Moldovan exports), Romania (17%), Italy (10%), Ukraine (6%), and the United Kingdom (4%). From a dynamic perspective, exports of goods have undergone the sharpest increase between 2005 and 2012 to China (i.e. the value of exported goods to China grew by more than 1220%. Moldova predominantly exports beverages, spirits and vinegar as well as edible fruit and nuts, citrus peels and melons). The biggest decline in that respect was in Slovakia, in 2012 the value of exports was 61% lower than in 2005.

<sup>52</sup> See <http://www3.weforum.org/docs/GGGR13/Moldova.pdf> Accessed on 21.05.2014.

**Figure A.1.5 Coverage of imports by exports in Moldova (%)**

Source: Statistica Moldovei.

**Traditionally, the most prominent exported goods are as follows: (i) vegetables; (ii) prepared foodstuffs; beverages, spirits and vinegar; tobacco and manufactured tobacco substitutes; and (iii) textiles and textile products (10%).** 41% of exported vegetables go to CIS countries, while 58% of the prepared foodstuffs are exported to the EU27. As for vegetables, the dominant exported vegetables are cereals as well as edible fruit and nuts; citrus fruit peels or melons (56% of total vegetables export). There are disproportionately high shares of beverages, spirits and vinegar (54% of total prepared foodstuffs group) as well as preparations of vegetables, fruit, nuts or other parts of plants (15%). In the case of textiles and textile articles, the salient subgroups are as follows: articles of apparel and clothing accessories in both types: (not) knitted or crocheted (42% of total textile export). As for the main products of Moldovan exports to the CIS countries, these are **pharmaceutical products; beverages, spirits and vinegar; and nuclear reactors, boilers, machinery and mechanical appliances**, and parts thereof. A more detailed breakdown can be seen in the Annex Table A.1.1.

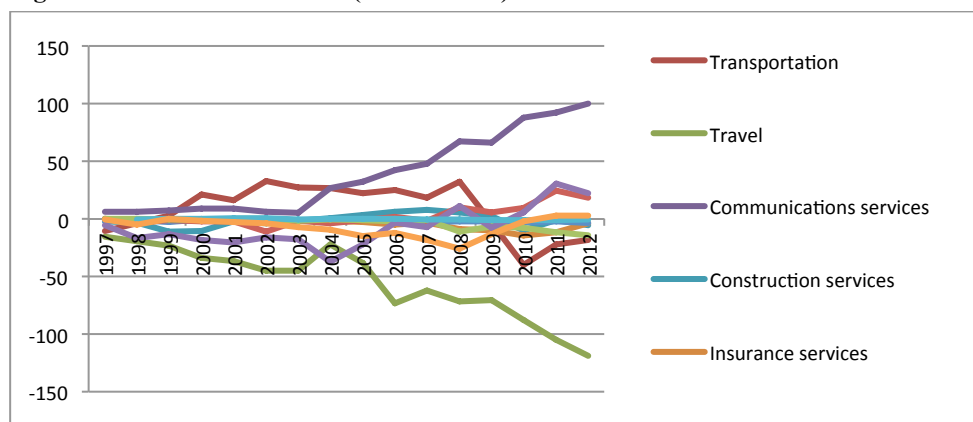
**Table A.1.1 Top three export products of Moldova to the CIS countries in 2011**

Armenia	Azerbaijan	Belarus	Kazakhstan	Kyrgyzstan	Russian Federation	Tajikistan	Turkmenistan	Ukraine	Uzbekistan
<b>Pharmaceutical products</b>	Pharmaceutical products	Beverages, spirits and vinegar	Beverages, spirits and vinegar	Beverages, spirits and vinegar	Beverages, spirits and vinegar	Footwear, gaiters and the like; parts of such articles	Organic chemicals	Oil seeds and oleaginous fruits; miscellaneous grains, seeds and fruit etc.	Pharmaceutical products
<b>Soap, washing preparations, lubricating preparations</b>	Glass and glassware	Edible fruit and nuts; peel of citrus fruit or melons	Carpets and other textile floor coverings	Glass and glassware	Pharmaceutical products	Pharmaceutical products	Paper and paperboard; articles of paper pulp, of paper or of paperboard	Beverages, spirits and vinegar	Footwear, gaiters and the like; parts of such articles
<b>Miscellaneous manufactured articles</b>	Furniture; bedding, mattresses, lamps and lighting fittings, illuminated signs, etc.	Salt; sulphur; earths and stone; plastering materials, lime and cement	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Pharmaceutical products	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof

Source: Statistica Moldovei.

*Services exports have been growing for years* and there are certain signs of improvement with regards to service export sophistication (i.e. exporting modern services like ICT, communication, financial services etc.). According to the balance of payment statistics of Moldova, the volume and value of other business services and that of communication services have been increasing dynamically since the mid-2000s, while traditional services like transportation, travel and construction services have been losing some dynamics. This issue may be related to the technology import of Moldova. In general, a low technology content of imports is observable (See Annex Figure A.1.6).<sup>53</sup>

**Figure A.1.6 Services balance (million USD)**



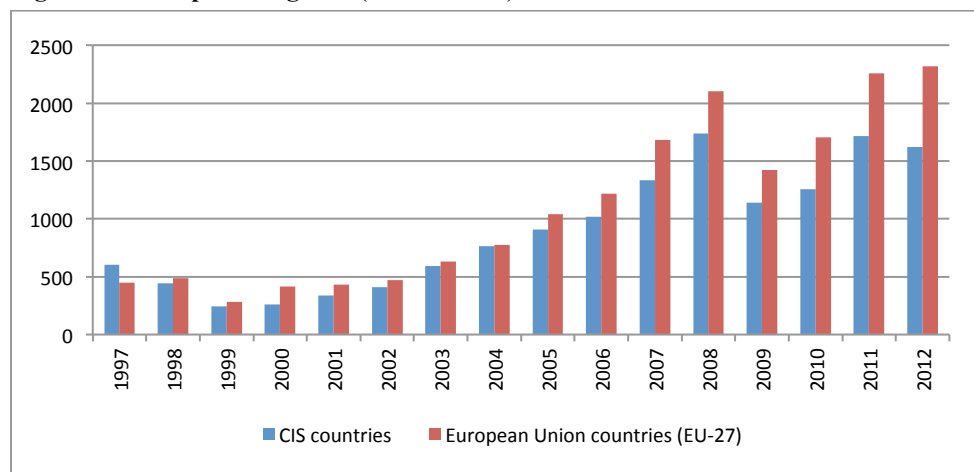
Source: National Bank of Moldova.

Imports from the EU27 outperformed the 2007 pre-crisis levels in 2010 (See Annex Figure A.1.7). Concerning imports from the EU27 countries, the biggest import values were coming to Moldova from Romania, Germany, Italy and Poland. In 2012, these countries were the main sources of imported goods and services with shares of 26%, 16%, 14% and 6%, respectively, within the total imported goods and services from the EU27. The Russian Federation, Ukraine, and Belarus are the countries from which Moldova imports the most.

<sup>53</sup> See World Bank Database <http://data.worldbank.org/indicator/TM.VAL.ICTG.ZS.UN/countries>.



**Figure A.1.7 Imports of goods (million USD)**



Source: World Bank.

Moreover, Turkey and China have also gained importance in Moldovan imports. The main import products from China are organic chemicals and pharmaceutical products. ***The three main groups of imported goods are as follows: (i) mineral products (23% of the total imported goods); (ii) machinery and mechanical appliances; electrical equipment***; parts thereof; sound recorders and reproducers (15% of the total imported goods); and ***(iii) products of the chemical or allied industries (10% of the total imported goods)***. In imports from the CIS countries, mineral fuels and mineral oils play a significant role (See Annex Table A.1.2).

Table A.1.2 Top three import products from CIS countries in 2011

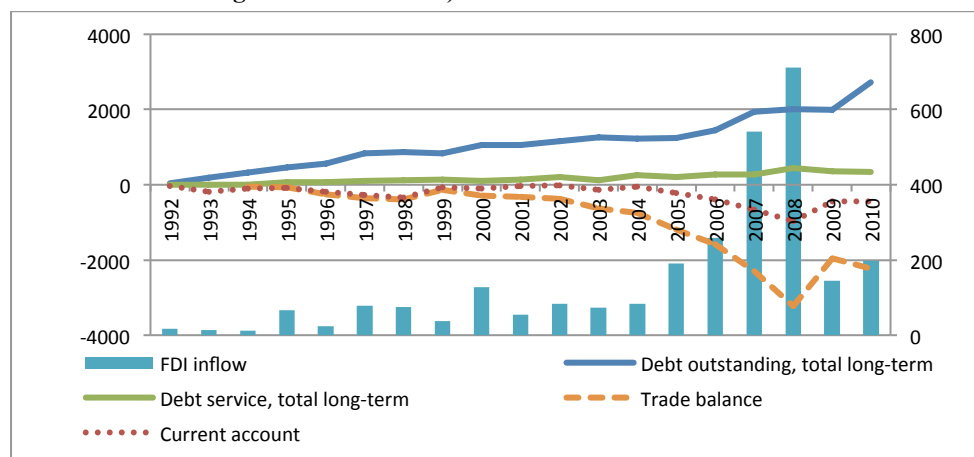
Armenia	Azerbaijan	Belarus	Kazakhstan	Kyrgyzstan	Russian Federation	Tajikistan	Turkmenistan	Ukraine	Uzbekistan
<b>Pharmaceutical products</b>	Pharmaceutical products	Beverages, spirits and vinegar	Beverages, spirits and vinegar	Beverages, spirits and vinegar	Beverages, spirits and vinegar	Footwear, gaiters and the like; parts of such articles	Organic chemicals	Oil seeds and oleaginous fruits; miscellaneous grains, seeds and fruit etc.	Pharmaceutical products
<b>Soap, washing preparations, lubricating preparations</b>	Glass and glassware	Edible fruit and nuts; peel of citrus fruit or melons	Carpets and other textile floor coverings	Glass and glassware	Pharmaceutical products	Pharmaceutical products	Paper and paperboard; articles of paper pulp, of paper or of paperboard	Beverages, spirits and vinegar	Footwear, gaiters and the like; parts of such articles
<b>Miscellaneous manufactured articles</b>	Furniture; bedding, mattresses, lamps and lighting fittings, illuminated signs, etc.	Salt; sulphur; earths and stone; plastering materials, lime and cement	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Pharmaceutical products	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof

Source: Statistica Moldovei.

The distribution of mineral products imports between CIS and EU27 is 68% to 32%. More than half of the amount of machinery imports originates from the EU27, while 83% of imported chemical products are from the EU27 countries.

The current account deficit together with the trajectory of trade balance shows that the *Moldovan economy was overheated right before the recent crisis, and it deteriorated further during the crisis. External equilibrium* deteriorated for multiple reasons. The inflow of FDI declined substantially to USD 145 million in 2009, a 20% decline compared to the previous year. Remittances were no longer able to be conducive to internal consumption to boost the economy, thus the current account and the trade balance succumbed into deficits (See Annex Figure A.1.8).

**Figure A.1.8 Indicators of external equilibrium (US Dollars at current prices and current exchange rates in millions)**

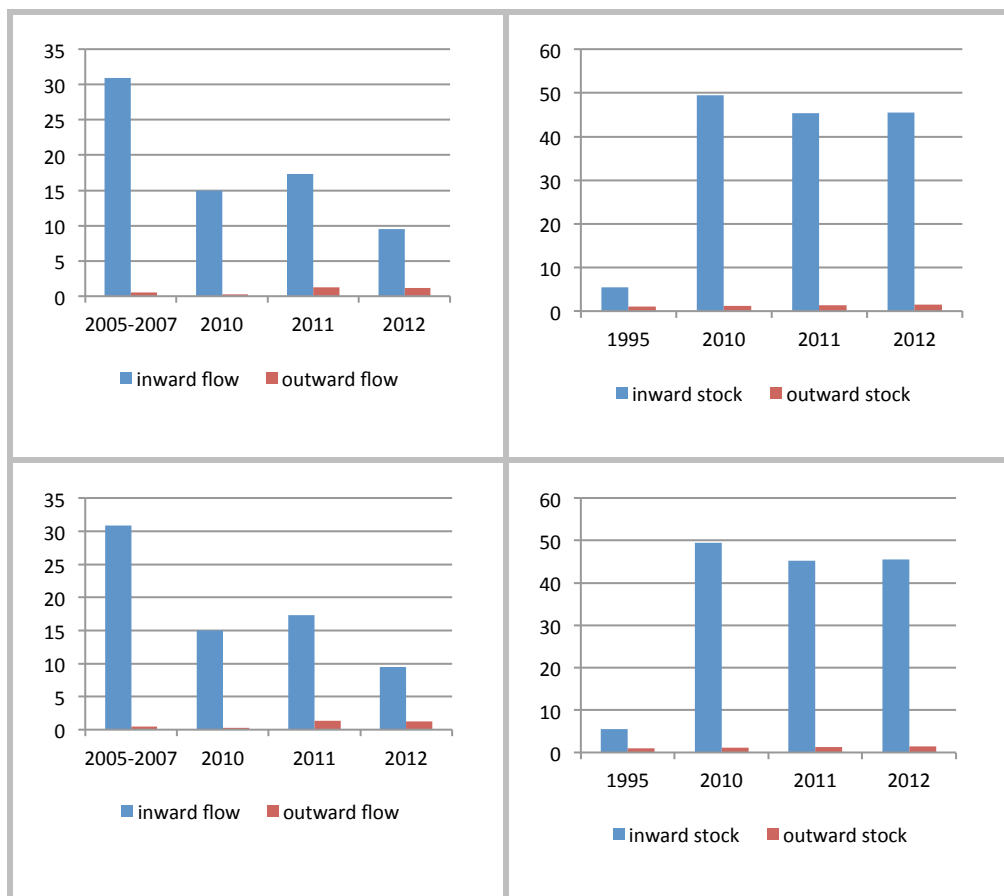


*Note:* right axis refers to FDI inflow, while left axis refers to other indicators.

*Source:* UNCTAD, World Bank, National Bank of Moldova.

In terms of *inflows and accumulated stock of FDI, Moldova has apparently outperformed many rivals in the region.* In spite of the drop of FDI inflow, FDI stock hovered around 45-50% of Moldovan GDP in 2010 and 2011, falling to 45% in 2012-2013 when economic growth resumed (See Annex Figure A.1.9).

Figure A.1.9 Inward and outward FDI flows and stock (% of GDP)



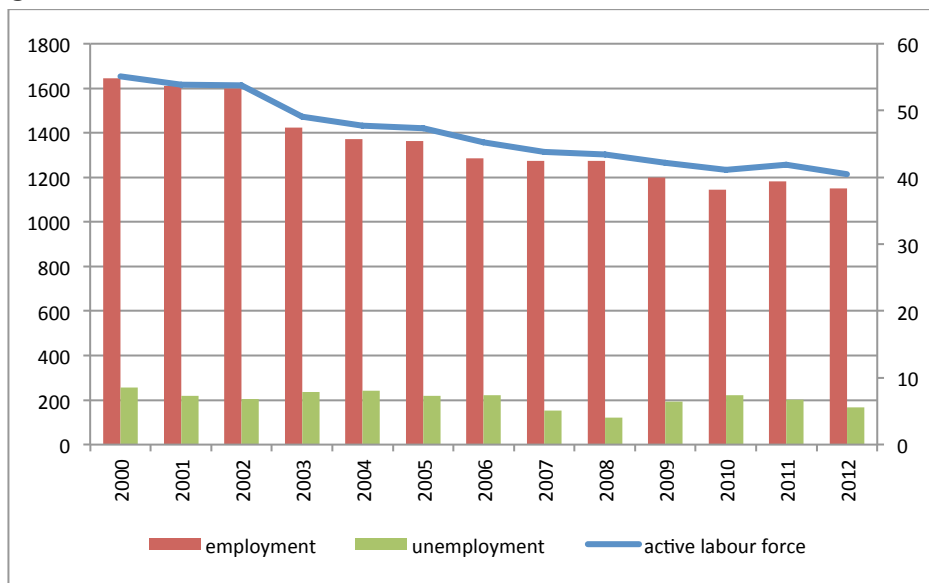
Source: UNCTAD, National Bank of Moldova.

The active labor force of Moldova has been decreasing since 2002, which has also been the case for employment in SMEs. The decrease is partly due to people seeking job opportunities abroad. Whereas the activity rate was 59.9% in 2000, it deteriorated to 40.7% by 2012 by triggering pressures on the budget due to the diminishing tax base burdened with more and more social security related expenditures.<sup>54</sup> The employment rate has also shown a downward trend since 2002, especially in the aftermath of the 2008 financial and economic crisis; the decline in employment was the biggest in the case of women (in 2000, women employment rate was 52.2 decreasing to 36.5 by 2012).

<sup>54</sup> People going to work abroad are not enjoying the Moldovan welfare services in the way they did before, however, they do not contribute to their financial sustainability in a vigorous way, either.

However, the unemployment rate is lowering (e.g. unemployment of men contracted from 9.7% in 2000 to 6.8% in 2012, the unemployment rate of women dampened from 7.2% of 2000 to 4.3% in 2012) (See Annex Figure A.1.10). Behind the decreasing unemployment is the propensity of Moldovan men and women to seek job opportunities abroad (by some estimates, one-third of the active population is working abroad).

**Figure A.1.10 Labor market indicators**



*Note:* left axis refers to active labor force (number of persons), while right axis refers to the rate of employment and unemployment (%).

*Source:* Statistica Moldovei, World Bank.

## Appendix 2. Similarities and Differences between Moldova and Hungary

Apart from the fact that Hungary and Moldova show considerable differences in many aspects, one can find certain similarities rooted either in their past or current socio-economic developments. Most importantly, the *dissolution of the Soviet Union and the transition to a market economy led to great losses in terms of GDP*. This was accompanied by significant export market losses and massive economic restructuring. Annex Table A.2.1 shows selected key indicators for the two countries.

**Table A.2.1 Selected key indicators for Hungary and Moldova**

	Hungary (2012)	Republic of Moldova (2012)
<b>Left the COMECON (Council for Mutual Economic Assistance, CMEA)</b>	1989	1991
<b>Population</b>	9,908,798	3,559,497
<b>GDP/capita (PPP)</b>	USD 22,635	USD 3,424
<b>Share of agriculture in GDP (%)</b>	4.02 %	13.1%
<b>Employment, thousand persons</b>	3,938	1,146
<b>Employment in agriculture, thousand persons</b>	193	303
<b>Unemployment rate</b>	10.4 %	6.6 %
<b>(Exports/GDP)</b>	82.5%	17.44 %
<b>Export to Russia in % of total export</b>	3.19 %	30.3 %
<b>Import from Russia % of total import</b>	9.54 %	15.7 %
<b>Share of SMEs in the total number of companies</b>	99.5%	97.5 %
<b>Employment share in SMEs in % of the total employment</b>	above 70%	57.7 %

*Source:* Hungarian Statistical Office, Hungarian National Bank, Statistica Moldovei.

Hungary was able to regain its pre-transition change level of GDP by the year 2000. In the run up to the European Union accession, economic growth accelerated, mainly driven by increasing external financing.

Moldova also lost a substantial share of GDP (e.g. between 1990 and 2012, the Moldovan GNI per capita decreased by 28%)<sup>55</sup> and was able to return to pre-transition levels only recently. Another similarity is that both countries are *small economies* (e.g. in terms of population or territory), therefore an export-oriented growth model seems unavoidable. Although the *services sector dominates* both economies, the *role of agriculture* is also important in the context of an export-led growth strategy.

In Hungary the level of *openness*, measured by exports/GDP is much higher than in Moldova. Official unemployment rates are below the European Union's average and the share of SMEs is almost the same, employing the predominant share of people in both countries. (Moreover, 16-18% of employees work in agricultural and related activities in both countries). Moldovan SMEs seem to have a huge potential to be utilized in fostering sectoral development with the aim of transforming the economy into a more open one by becoming efficiently and effectively integrated into the global economy.

In addition to the employment situation, the important role of remittances in Moldova and the high dependency of households on them calls attention to the withering future perspective offered by the country for young generations (in Hungary, remittances amounted only to 1.7% of the Hungarian GDP in 2012, while their share in Moldova was 24.5%)<sup>56</sup>. In both countries, innovative, creative minds are being attracted away to work abroad.

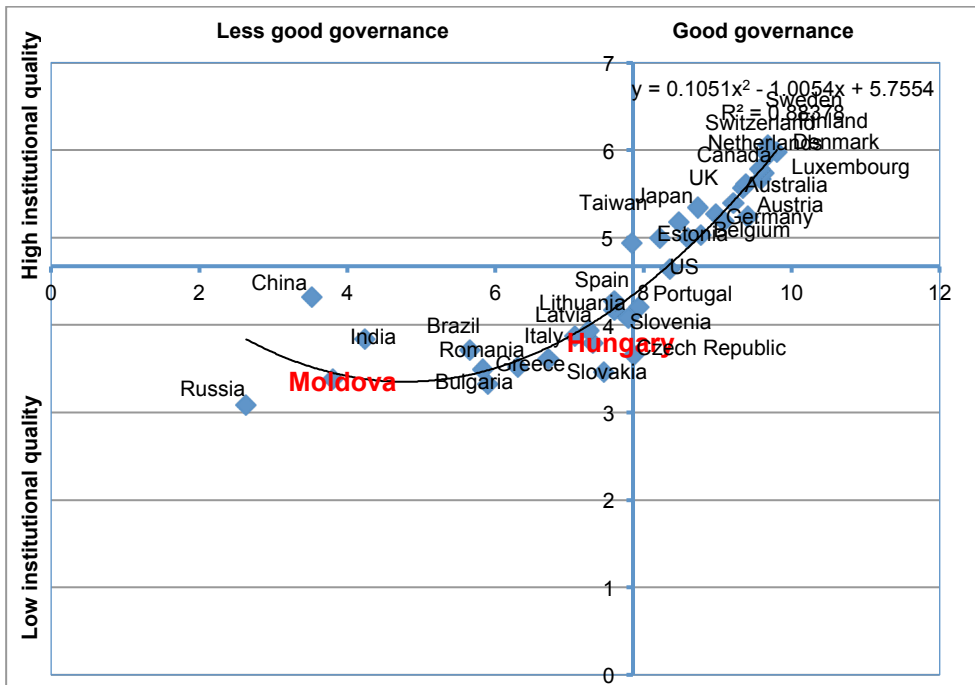
There are other factors which influence the business environment in which SMEs operate, but they are difficult to measure and compare. Especially the nature and operational characteristics of institutions matter from that point of view. Annex Figure A.2.1 shows the relationship between the quality of governance and international competitiveness in terms of formal institutions.

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<sup>55</sup> According to official statistics (World Bank, OECD, National Statistical Offices), five out of twelve post-Soviet countries – Ukraine, Moldova, Georgia, Kyrgyzstan, and Tajikistan – had not reached their 1990 GDP per capita levels in purchasing power parities by 2010.

<sup>56</sup> Source of data: Worldbank, see <http://data.worldbank.org/indicator/BX.TRF.PWKR.DT.GD.ZS>.

Figure A.2.1 Institutions and governance quality in selected countries (2010)



Note: the vertical axis refers to the institutional competitiveness of countries prepared by World Economic Forum in its Global Competitiveness Report 2011-2012, while the horizontal axis represents the aggregated Worldwide Governance Indicators prepared by the World Bank (See: Kaufmann et al. 2008). The intersection reflects the averages of the two indicators.

Source: own compilation based on data mentioned above.

We use the World Bank Worldwide Governance Indicators database as well as the sub-index for institutions of the World Economic Forum Global Competitiveness Report 2013. The first one is to capture the quality of governance by using six indicators that are ultimately geared towards political, economic and institutional dimensions (Kaufmann et al. 2010). The latter one offers us an opportunity to contemplate how the given economy performs in the case of international competitiveness with special attention to its institutions. This makes it possible to see the distribution of countries across these indicators according to whether they have *good* (above average) or *“less good”* (below average) governance as well as whether they have either *high* (above average) or *low* (below average) institutional quality.



It seems that, in international terms, Hungary has relatively less good governance but it is still better than that of Moldova, and Hungary's institutional quality outperforms Moldova's as well.

Hungary performs better than Moldova in the Doing Business Index developed by the World Bank. The Index ranks Hungary at 54<sup>th</sup> position, while Moldova is in 78<sup>th</sup> place out of 189 economies. Although formal institutions and the quality of governance in Hungary seem to outperform Moldova's, there is a field in which Moldova has advantages compared to Hungary that is of key importance when it comes to SME development. In the dimension of 'paying taxes', Doing Business Index ranks Hungary 124<sup>th</sup>, while Moldova is 95<sup>th</sup>. In both countries, the tax burden on labor is higher than the averages of the OECD as well as that of Europe and Central Asia. Compared to Hungary, less time is needed in Moldova to prepare, file and pay (or withhold) corporate income tax, value added tax and social security contributions (in hours per year). Starting a business is easier in Hungary (59<sup>th</sup>) than in Moldova (81<sup>st</sup>), while getting electricity is rather cumbersome in both countries in terms of time required (Hungary: 112<sup>th</sup>, Moldova: 165<sup>th</sup>).

## Appendix 3. Data on the Moldovan SME sector

**Table A.3.1 SMEs' share in total number of companies, employment and sales, 2008-2012**

Year	Number of companies (thousand)			Employees (thousand)			Sales (million Lei)		
	Total	SMEs	Share of SMEs in total (%)	Total	SMEs	Share of SMEs (%)	Total	SMEs	Share of SMEs (%)
<b>2008</b>	42.1	41.1	97.6	572.1	328.1	57.3	175,058.4	64984,1	37.1
<b>2009</b>	44.6	43.7	97.8	539.2	316.2	58.7	146,447.0	57480,0	39.2
<b>2010</b>	46.7	45.6	97,7	526.2	309.4	58.8	177,503.2	65263,2	36.8
<b>2011</b>	48.5	47.3	97.5	510.2	294.2	57.7	207,676.8	71887,6	34.6
<b>2012</b>	50.7	49.4	97.5	519.9	300.2	57.7	211,759.3	73057,0	34.5

Source: Statistica Moldovei.

**Table A.3.2 Sectoral distribution of SMEs (number of companies)**

Sector	2011			2012			2012 compared to 2011 (%)
	SMEs (thousand)	Share of SMEs		SMEs (thousand)	Share of SMEs		
		In all companies, %	In SMEs, %		In all companies, %	In SMEs, %	
<b>Total</b>	<b>47.3</b>	<b>97.5</b>	<b>100</b>	<b>49.4</b>	<b>97, 5</b>	<b>100</b>	<b>104.4</b>
<b>Agriculture, forestry</b>	2.4	97.4	5.1	2.5	97.6	5.0	104.2
<b>Manufacturing</b>	4.8	95.9	10.2	4.9	95.8	9.8	102.1
<b>Energy, gas, water</b>	0.2	84.4	0.4	0.2	86.8	0.5	100.0
<b>Construction</b>	2.6	97.0	5.5	2.7	96.9	5.5	103.8
<b>Wholesale and retail trade</b>	19.4	97,7	41.0	20.0	97.8	40.5	103.1
<b>Tourism and restaurants</b>	1.5	99,2	3.2	1.7	99.4	3.4	113.3
<b>Transport and communication</b>	3.2	98.0	6.8	3.3	98,1	6.7	103.1
<b>Real estate, leasing, business services</b>	7.9	98,4	16,6	8.5	98,4	17.2	107.6
<b>Other</b>	5.4	97.1	11.3	5.7	97.1	11.5	105.6

Source: Statistica Moldovei.

**Table A.3.3 Sectoral distribution of SMEs (according to sales)**

	2011				2012			
	Total (million lei)	SMEs (million lei)	Share of SMEs		Total (million lei)	SMEs (million lei)	Share of SMEs	
			In all companies, %	in SMEs, %			In all companies (%)	In SMEs (%)
<b>Total</b>	<b>207,676.8</b>	<b>71,887.6</b>	<b>34.6</b>	<b>100.0</b>	<b>211,759.3</b>	<b>73,057.0</b>	<b>34.5</b>	<b>100.0</b>
<b>Agriculture, forestry</b>	8307.8	5613.5	67.6	7.8	7257.6	4930.3	67.9	6.7
<b>Manufacturing</b>	31203.6	9316.4	29.9	13.0	33265.7	9522.8	28.6	13.0
<b>Energy, gas, water</b>	19995.8	258.7	1.3	0.4	22355.2	261.8	1.2	0.4
<b>Construction</b>	9144.7	5555.2	60.7	7.7	8439.8	5349.9	63.4	7.3
<b>Wholesale and retail trade</b>	97530.5	35319.2	36.2	49.1	98590.9	36299.0	36.8	49.7
<b>Tourism and restaurants</b>	1602.8	1115.6	69.6	1.6	1830.5	1365.8	74.6	1.9
<b>Transport and communication</b>	19881.6	6464.9	32.5	9.0	19423.7	6885.1	35.4	9.4
<b>Real estate, leasing, business services</b>	8434.4	5100.7	60.5	7.1	8021.7	5177.2	64.5	7.1
<b>Other</b>	11575.8	3143.4	27.2	4.4	12574.2	3265.0	26.0	4.5

Source: Statistica Moldovei.

**Table A.3.4 Pretax profits of SMEs in various sectors, 2011-2012**

	Pre-tax profit (+) or loss (-) million lei							
	2011				2012			
	SMEs total	In SMEs			SMEs total	In SMEs		
		medium	small	micro		medium	small	micro
<b>Total</b>	<b>5180.2</b>	<b>1972.1</b>	<b>2697.7</b>	<b>510.4</b>	<b>1084.6</b>	<b>393.6</b>	<b>715.9</b>	<b>-24.8</b>
<b>Agriculture, forestry</b>	951.8	382.7	498.7	70.4	-53.5	29.1	-41.6	-40.9
<b>Manufacturing</b>	503.7	277.2	233.3	-6.8	9.8	32.0	2.9	-19.3
<b>Energy, gas, water</b>	-23.8	-21.5	5.6	-7.9	-42.4	-22.9	-17.1	-2.3
<b>Construction</b>	517.1	193.9	290.4	32.9	97.0	-4.2	84.9	16.3
<b>Wholesale and retail trade</b>	1751.6	646.2	1011.6	93.8	695.4	271.6	540.5	-116.6
<b>Tourism and restaurants</b>	-47.6	21.4	-53.2	-15.9	-119.9	-14.4	-57.7	-47.7
<b>Transport and communication</b>	299.2	78.0	189.8	31.4	-37.1	-6.8	-48.6	18.3
<b>Real estate, leasing, business services</b>	975.7	284.6	421.2	269.9	469.1	72.1	251.2	145.8
<b>Other</b>	252.6	109.6	100.2	42.7	66.2	37.2	7.3	21.7

Source: Statistica Moldovei.

### **Box A.3.1 Domestic policies for economic development**

The most important economic development policy of Moldova is the National Development Strategy “Moldova 2020”: SEVEN solutions for economic growth and poverty reduction (approved by Law nr. 166 of July 11<sup>th</sup>, 2012). The strategy aims to stimulate growth and reduce poverty and to promote structural changes of the economy through building on FDI and export sectors. The seven priorities and the declaration of going toward green economic development are as follows:

- Aligning the education system to labor market needs in order to enhance labor productivity and increase employment in the economy;
- Increasing public investment in the national and local road infrastructure in order to reduce transportation costs and increase the speed of access;
- Reducing financing costs by increasing competition in the financial sector and developing risk management tools;
- Improving business climate by streamlining the regulatory framework and applying information technologies in public services for businesses and citizens;
- Reducing energy consumption by increasing energy efficiency and using renewable energy sources;
- Achieving financial sustainability of the pension system in order to ensure an appropriate rate of wage replacement;
- Increasing the quality and efficiency of justice and fighting corruption in order to ensure equity for all citizens.

Since January 2013, innovation policy in Moldova has focused on:

- Approving the draft R&D strategy and the draft innovation strategy for Moldova;
- R&D&I indicators for Moldova are to be adapted to EUROSTAT standards;
- Project selection and evaluation processes are to be substantially improved:
  - involving international experts in funding evaluations in a more dedicated way;
  - transparent and efficient performance criteria are to be used when it comes to funds allocation to research institutions;
  - introduction of innovation vouchers;
  - public procurement is being directed towards research intensive and innovative goods and services.
- Moldova’s integration into the European Research Area is to be continued;
- A committee has been installed to prepare the association of Moldova to the EU’s Horizon 2020 program;
- Lifelong learning is to be a pivotal priority;
- Doctoral schools will be further established and developed;
- Industrial PhD is planned to be introduced.

**Box A.3.2 International cooperation programs available for Moldovan enterprises**

- Moldova became associated with the FP7 as of 1 January 2012 (in May 2013, 249 FP7 proposals were submitted);
- The Academy of Sciences of Moldova is active in the two FP7 International Cooperation Networks (IncoNet projects);
- Third party status in the European Cooperation in Science and Technology (COST) framework program;
- EU: European Neighbourhood and Partnership Instrument (ENPI);
- EU: Neighbourhood Investment Facility (for key infrastructures, e.g. transport, water and energy) Allocation for 2007-2010: € 209.7 million; Allocation for 2011-2013: € 273.14 million;
- European Bank for Reconstruction and Development (Energy Efficiency program, so-called Energy Financing Facility);
- European Union Programs - 2011-2013 National Indicative Program (NIP);
- SIDA (Swedish International Development Cooperation Agency) in fields like democracy and human rights, energy and market development;
- US Millennium Challenge Account - 2010-2015 Compact;
- GIZ – German International Cooperation Agency: German support for Investments;
- OECD program, EaP GREEN: Greening economies in the European Union’s Eastern Partnership countries;
- The “Private Sector Development” initiative promotes and supports economic cooperation between Moldova and the Netherlands by providing financial assistance worth up to 50% of the investments size, but not more than 750,000 Euro. It is also providing consultancy in the initiation and development stages of the partnership.

### **Box A.3.3 Domestic policies and programs for SME development**

There are several policies and governmental or international initiatives that target SME development. The most important ones are (published at the ODIMM website):

- The PARE 1+1: Project of Attracting Remittances in the Economy aims to mobilize the human and financial resources of Moldovan migrants in Moldova's sustainable economic development by fostering the establishment and development of small and medium enterprises by migrant workers and recipients. The program will operate under the rule of "1+1", so every MDL invested from remittances will be substituted with a MDL in the form of a grant from the Pilot Program. The target groups are: migrant workers, citizens of Moldova and beneficiaries of remittances, including 1st degree relatives. The program provides the following activities:
  - Training courses for migrants and their first degree relatives, including free distribution of informational and support materials;
  - Grants in amounts of 50% of the investment, but not more than 200 thousand MDL;
  - Performing post-funding monitoring.
- FGC: The Special Credit Guarantee Fund aims to facilitate access to financial resources for micro and small enterprises. The target group are micro and small enterprises in the trade sector. The program provides loan guarantees for traders that lack sufficient collateral. For active business, the guarantee is up to 50% of loan size, but not more than 700 thousand MDL, over a period of up to five years. For start-ups, the guarantee may be up to 70% of the loan amount, but not more than 300 thousand MDL. The guarantee period is up to three years. For the beneficiaries of the Project of Attracting Remittances in the Economy - "PARE 1+1", the guarantee represents up to 50% of the credit size, but not more than 200 thousand MDL;
- JNPGA: Program for SMEs Sector Support and Development. The objectives are: promotion of economic structural adjustment efforts by facilitating the purchase by SMEs of a large variety of production equipment. The target group: SMEs (except for those from Chisinau and Balti). The program allows the acquisition of equipment through leasing for a period of one year, providing a grant of 40%. Purchase value varies from 500 thousand to 2.5 million MDL;
- The "2KR: Increasing Food Production Project" is an initiative in the field of agriculture and food production. The targeted groups are: Private legal entities, farmers and individuals, regardless of organizational form of activity, engaged in entrepreneurial activities and/or who offer services for mechanized farming. The project supports the procurement of agricultural technology in installments (initially they are paid 50% of the total cost and then the installments over two years). The price does not include VAT;

- The “Jobs for Youth” project for providing better opportunities for employment for vulnerable youth in rural Moldova targets young people under 35 from rural areas registered as unemployed. It includes the provision of business, legal and technical consultancy, learning courses in entrepreneurship, mentoring and well as financial support: grants and guarantee fund.
- The “Subsidiary for Farmers” initiative focuses on SMEs in the agricultural sector and rural communities. It provides farmer subsidies (mainly investment subsidies for establishing plantations, investment in machinery and equipment, etc.);
- The MoSEFF project, “Financing Line for Energy Efficiency in Moldova,” approaches advanced technology development in order to improve energy systems. Any company with at least 51% private capital registered and operating in Moldova (except for companies dealing with the production and distribution of tobacco products, alcoholic beverages, gambling games and arms) can apply for loans with a grant portion (5-20%) for financing renewable energy and energy efficiency projects, from 25 thousand to 2 million euro, for a period of up to 6 years. Loans are granted for activities such as thermal insulation, window changing, ventilation, solar heating, boiler replacement, pipe insulation, biomass burning, etc;
- Moldova's Wine Sector Restructuring Program works with the support of the European Investment Bank. The program was created to address the structural weaknesses in the Moldovan wine industry. According to the finance contract signed on November 23, 2010, the European Investment Bank offers a EUR 75 million loan destined for the realization of the program. With the aim of ensuring effective implementation and monitoring of the program, the public institution „Consolidated Unit for Implementing and Monitoring the Wine Sector Restructuring Program” has been established. The main target group are grape processing and wine making enterprises. The program provides 50% financial support for the upgrading, restructuring and working capital of wineries. The program’s objectives are:
  - Restructuring the wine sector and support industries and promoting the production of quality wine, i.e. wines of Protected Designation of Origin (P.D.O.) or Protected Geographical Indication (P.G.I.);
  - Improving the quality and consistency of wines produced in Moldova beginning with the quality of vineyards to the final packaging and dispatch of products;
  - Diversifying the country's export markets by guaranteeing the authenticity of wine products.

#### **Box A.3.4 General entrepreneurship and SME-supporting principles and instruments in the V4 countries**

In accordance with the objectives of the Small Business Act for Europe of the European Commission, the following development can be listed in the Visegrad countries.

**The Czech Republic** has had a “Small And Medium Enterprises Support Strategy 2014–2020” since 2012. Its priorities are as follows: (i) Enhancement of Business Environment, Development of Consultancy Services and Education for Business; (ii) Development of Enterprise Based on Support for Research, Development and Innovation, including the Innovation and Business Infrastructure; (iii) SME Internationalization Support; (iv) Sustainable Energy Management and Development of Energy Innovations.

- **Dampening administrative burdens:** In dealing with excessive administrative burdens on SMEs, the Czech Republic cut red tape by 8% in 2007 and 2008 and planned to achieve a 20% reduction by 2010. Abolishing relevant administrative burdens is also linked to the issue of making the labor market more flexible, however, this development is lagging in the Czech Republic since it has a relatively rigid one, as was indicated in the Global Competitiveness Index 2012-2013 prepared by WEF (the Czech Republic is 75th in this regard). Removing the administrative burden from businesses was also reflected in amendments of waste, income tax and social insurance laws, among others. Amendments for micro-enterprises were carried out by making possible electronic communication with the authorities, and makes getting business licenses easier;
- **Accounting principles are contextualized:** Micro-enterprises have to follow lower accounting requirements than standard companies. Micro-enterprises are not required to keep their receipts when making purchases in order to prove their expenses;
- **Financial flexibility is of key importance to improve:** regulatory rules have been changed to alleviate the situation, e.g. four months maturity dates are not exceptional especially in the construction sector;
- **Enhancing the general entrepreneurial environment targets particular types of companies or individual industries.** Lowering the social insurance contribution of employers helped to reduce the cost of labor;
- **Exporting companies are in focus as well:** loans via commercial banks and the Czech Export Bank are available and underpinned. The government is to ease SMEs’ access to EU funds. Education and training with the aim of extending knowledge of SMEs on internationalization is being accompanied with information, intelligence, and consultancy services on internationalization. Export funding and insurance system modernization is underway.



**Hungary** does not have a valid strategy for SMEs. The Strategy for SMEs for 2014-2020 is under public consultation.

- **Dampening administrative burdens:** Since administrative costs account for 10.5% of the Hungarian GDP, three times more than the EU average, in 2011, the program called “Egyszerű Állam” was introduced to reduce relevant administrative burdens identified by a wider group of stakeholders. The program identified 114 actions to take in favor of eliminating excessive bureaucratic burdens and the program was to be continued in 2013;
- **Simplified tax schemes:** as of January 2003, the Hungarian government introduced the “EVA” (simplified tax scheme) for small enterprises with limited revenues but without major costs, which is based on a flat tax rate on the total revenues. As of 2013, three more schemes were introduced: Small business tax (KIVA), Small taxpayers’ itemized lump sum tax (KATA) and Simplified contribution to public revenues (EKHO);
- **Governmental one stop shop portal:** has been developed since the mid-2000s, continuously adding new features to the [www.magyarorszag.hu](http://www.magyarorszag.hu) portal. Currently the available services for all business include: Reporting taxes and social contributions, reporting pension contributions, online company register, information on the health registry, reporting the start and end of employment, etc;
- **Financial flexibility is of key importance to improve:** as a consequence of depressed internal demand and net investment activities which is reflected in the substantial surplus observable in current account balance, SMEs’ access to finance is rather problematic and the uncertainties they face deter them from being risk-seeking. The Loan Program for Growth introduced by the Central Bank of Hungary is to offer cheap money to commercial banks to lend to companies (60% of new loans were to finance operations, not for replacing old credits);
- **Enhancing the general entrepreneurial environment would be of key importance:** the entrepreneurial mindset is not very prevalent in Hungary (only 44% Hungarians see entrepreneurship as an opportunity, compared to the EU average of 58%). Within the confines of the so called AROP 1.1.15 project, there is work which has started to recognize the need for an entrepreneurial-development function of municipalities to bring stakeholders together, to get them engaged in co-operations being geared towards competitiveness. The planned Strategy for SMEs 2014-2020 includes the recognition that, beyond infrastructural development, entrepreneurial skills are worth developing further;
- **Various support methods to enhance cooperation among enterprises.** From the operational program “Economic Development OP” of the Structural

Funds, 2007-2013, priority was given for the support of accredited clusters. Regional operational programs allocated funds for supporting the local and touristic cooperation of enterprises.

**In Poland**, the Polish Agency for Enterprise Development (in Polish, PARP) is in charge of supporting SME and enterprise activities for greater competitiveness and innovativeness. Among its main activities, one can find the following: enterprise development, application of new techniques, export development, creation of new jobs, tackling unemployment, human resources development, and regional development. In the financial perspective 2007-2013, the PARP is involved in the implementation of 7.2 bn EUR (8.4% of total NSRF budget) within three OPs: OP Innovative Economy (EUR 3.9 bn), OP Human Capital (EUR 672 m) and OP Eastern Poland Development (EUR 2.6 bn).

- **Exporting aspect is less important:** Polish SMEs are particularly active in services and trade, so they depend on domestic demand rather than exports. Regarding this issue, one important insight deciphered from the development of Polish SMEs is as follows: they have little confidence in external financing. The SME sector does not consider external financing as a chance for rapid and sustainable development. There is insufficient knowledge about financial instruments and skills of management of finance and anxiety over the debts. Against this background, the PARP is committed to tackle this problem by providing: support for clusters and technology parks, support for business support institutions active in the area of innovation, and support for alternative forms of external financing of SME development (investment funds, business angels, loan and loan guarantee funds);
- **Enhancing the general entrepreneurial environment is in order:** The PARP offers a complex set of activities in supporting better framework conditions for SMEs as well. It operates the so called National SME Services Network which serves as a catalyst for entrepreneurial activities via various services: (i) information services, (ii) pro-innovative advisory, (ii) financial services – guarantee funds, (iii) financial services – loan funds (that are linked to the issue of financial flexibility), (iv) new systemic services. The National SME Services Network launched three pilot projects: Environmental counseling, Cost optimization, and Assistance. Beyond this, the PARP offers SMEs support for property protection and supports the field of industrial design.

**In the Slovak Republic**, the Ministry of Economy, as the managing authority for the Operational Program “Competitiveness and Economic Growth,” published an updated program guide. The document juxtaposes and details the main priority axes such as (1) Innovation, growth, and competitiveness; (2) energy; (3) tourism; and (4) technical assistance. The first priority is of key importance from the perspective of innovation policy.

- **Dampen the administrative burdens:** In 2007, the document, “Better regulation in the Slovak Republic: Action program for reducing administrative burdens in Slovakia 2007–2012” was published and it is now fully implemented (the red tape was supposedly to be decreased by 25% by 2012). For example, the exemption of micro-enterprises from accounting requirements was introduced. Entrepreneurs are granted exemptions from double entry accounting in cases where their business has no other employees and its income does not exceed €170,000. Expenses can be written off according to the principles of "bookless accounting;
- **Enhancing the general business environment:** the above mentioned document puts emphasis on promoting innovation and technology transfer. The purpose of the measure is to support the private sector, where promoting innovation and technology transfer can be seen as the best way forward to solve energy consumption related problems, to reduce environmental impacts, and to increase the efficiency of production. The first priority axis contains a measure tailored towards improving conditions for business development and strengthening the links between SMEs. This measure supports the public sector in building infrastructure for business development in industry and services, in particular for SMEs, with a positive impact on employment and quality of life in the regions. The aim is also to support the public sector in promoting business in the context of balanced regional development, including the revitalization of former industrial sites. Support primarily focuses on the revitalization of brown field, and only in exceptional cases, greenfield, and only after the approval by the Ministry of Economy for the purpose of creating new job opportunities and joint activities in the region in collaboration with the Ministry of Labor. This has a regional dimension, but it is also an opportunity for networking in the context of international cooperation.
- **Exporting companies to be supported:** The mentioned document considers technology transfer to be promoted which is especially important in the case of exporting and internationally expanding companies. By triggering technology transfer and innovation, new jobs are expected to be created through supporting entrepreneurship (i.e. supporting start-ups). Therefore, this measure will support the participation of Slovak manufacturers in fairs, exhibitions and trade missions under a separate scheme of assistance.

### **Box A.3.5 Knowledge-economy and innovation based growth related R&D&I support mechanism in the V4 countries**

At least the following four dimensions can be considered:

- financial aid to R&D and innovation activities in firms and research institutions;
- support for cooperation, networking and cluster formation;
- funding of technology-oriented start-ups;
- institutional support for research institutions and knowledge transfer facilities.

In **Poland**: providing necessary financial support by promoting R&D activity in general (business, higher education); Government programs (Polish Agency for Entrepreneurship Development, National Research and Development Centre) are more or less direct instruments, while there are bridging tools tailored towards promoting collaborations among public-private sectors where the tools are indirect instruments. The focus is on stimulating technology transfer to enterprises to catalyze the commercialization of innovations. Few of these instruments are to stimulate firms' R&D efforts/expenditures and some are to advance the implementation of scientific-technological solutions. A foresight exercise was conducted to identify future technologies by 2030 worth taking into account with meticulous care. The PARP offers financial grants for innovative investment projects, for R&D and the implementation of the results of R&D projects; grants for the development of R&D activity of enterprises; innovation voucher system.

- **Regarding SMEs**: Despite the central role of micro SMEs (they provide more than a third of total employment in Poland, 37.4%, substantially above the EU average of 29.6%), innovation policy does not have effective instruments on hand to cultivate fertile ground for innovation through supporting the development as well as the utilization of skills (substantial innovation culture is missing).

In **Hungary**, state support to **business innovation** is mainly through direct funding such as competitive **grants, equity financing and venture capital, and innovation vouchers**, as well as a tax credit for R&D. As for public **research organizations** and labs, the state has been putting more emphasis on the development of **their qualities and environments** (e.g. the Social Infrastructure Operational Program (SOIP) and the National Research Infrastructure Survey and Roadmap (NEKIFUT). As far as how to **promote collaborations** is concerned, the Pole Program supports clusters of firms with export potential. **Supporting commercialization** is mainly carried out by Corvinus First Innovation Venture Capital Fund as well as the Start Equity Guarantee Fund. Regarding how to **boost innovative culture** in Hungary, skills and mobility are targeted via the program called Momentum: "From Brain Drain to Brain Gain" being directed at talented young researchers, while the Campus Hungary Program supports **international student mobility**. **Nanotechnology** has come to the forefront

as a potential breaking point and the NAP Nano Scheme was therefore established through an International Research and Development Agreement in 2005 with the Russian Federation.

- **Regarding SMEs:** However, the Hungarian mindset for innovation policy reflects the recognition that no one knows what the future has in store (i.e. picking up industries is a wrong interference). Instead, striving for an appropriate business eco-system should be seen as an instructive way forward. This is reflected in its SME support-related understanding as well. Still, the crisis and its consequences (increasing fiscal tensions, limited financial resources) suggest that prioritizing and choosing specific sectors are of key importance like in Austria, Belgium and Poland etc.

In the **Slovak Republic: boosting collaborations** (e.g. parks, business incubators) between academy and industry (e.g. Minerva 2.0 program) featured with the dominance of direct financial measures (**competitive grants**); **competitions** (Innovative Deed of the Year and Young Designer), Risk Capital Program. Phoenix Strategy focuses on establishing and **cultivating joint study programs** with prominent foreign actors.

- **Regarding SMEs:** The relatively weak scientific base is performing anemically, and direct financial measures are dominating the Slovak Republic innovation policy, whose approach has not proved to be a viable option in reinvigorating business R&D activity. Nevertheless, there are plenty of programs and initiatives geared towards the needs of SMEs. For instance, transfer of knowledge and technology from research and development into practice in the Bratislava Region, the operational program “Research and Development” (2007-2013), and R&D stimuli (2009-2013).<sup>57</sup> In the case of R&D stimuli, during the recent financial and economic downturn, all types of SMEs are welcome without sectoral limitations, but the scheme has a restriction for natural persons/businessmen. R&D stimuli were introduced quickly (obtaining grants within a period of 3-months).<sup>58</sup>

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<sup>57</sup> Further programs are as follows: Support for Research and Development SMEs (2007-2010); Support of innovation activities in enterprises; Operational program Competitiveness and Economic Growth (2007- 2013); Business innovation and applied research program support; Transfer of knowledge and technology from research and development into practice; and Operational program Research and Development (2007-2013).

<sup>58</sup> In the Mapeer Report, the authors highlight The Support for Research and Development SMEs program as a good practice. It supports businessmen’s research and development and the cooperation of SMEs with research organizations. It also considerably reflects SME needs. It was successfully accepted by SMEs (2007 call) and based on the results of the questionnaire, the program was highly appreciated by 72% of respondents who participated or participate in the program. Higher competitiveness and increase of sales

**As for the Czech Republic, skills, R&D, and science-industry linkages** are at the core of the Czech innovation policy. Measures and instruments that are of crucial importance in this regard are as follows: POTENCIAL Program (in support of technology centers and in-house R&D activities); **awards** (Innovation of the Year, Czech Innovation and Best Cooperation of the Year); **subsidized loans and guarantees** geared towards innovative start-ups through START, GUARANTEE and PROGRESS programs; **triggering cluster development** by the Co-operation Program; ALPHA Program supports industrial R&D&I activities together with public-private R&D actors.

- **Regarding SMEs:** The SME support measure-portfolio is far from simple, which tends to lead failures from the side of administration as well. SMEs are not well equipped with well-skilled and educated creative and innovative researchers/employees as the R&D employment rate has shown recently. Since early 2013, the European Investment Fund and Komerční banka have signed a guarantee agreement to support lending to innovative SMEs (EUR 100 million of new loans) under the Risk Sharing Instrument (RSI), a joint initiative of the European Investment Bank Group and the European Commission.

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and profits are a program benefit for participating firms. See more [http://mapeer-sme.eu/en/~media/MaPEer-SME/DocumentLibrary/RTD%20programs/Slovak\\_Republic\\_programm\\_report](http://mapeer-sme.eu/en/~media/MaPEer-SME/DocumentLibrary/RTD%20programs/Slovak_Republic_programm_report) Accessed on: 11.09.2013.

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