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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
AND
INTERNATIONAL DEVELOPMENT ASSOCIATION
ACTING AS ADMINISTRATOR OF THE MULTI-DONOR TRUST FUND FOR CO-FINANCING OF THE MOLDOVA DEVELOPMENT POLICY PROGRAM

SUPPLEMENTAL FINANCING DOCUMENT FOR A PROPOSED GRANT
FINANCED BY MULTI-DONOR TRUST FUND FOR CO-FINANCING OF THE MOLDOVA DEVELOPMENT POLICY PROGRAM
IN THE AMOUNT OF US$43.76 MILLION
TO

THE REPUBLIC OF MOLDOVA
FOR THE

Moldova Emergency Response, Resilience, and Competitiveness Supplemental Development Policy Operation

December 2, 2022

Macroeconomics, Trade And Investment Global Practice
Europe And Central Asia Region

Public Disclosure Authorized

Republic of Moldova

GOVERNMENT FISCAL YEAR

January 1– December 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of November 28, 2022)

Currency Unit: Moldovan leu (MDL)

MDL 19.25 = US$1 = EUR 0.96

ABBREVIATIONS AND ACRONYMS

AFD	Agence Française de Développement (French Development Agency)
APRA	Ajutor pentru Perioada Rece a Anului (Cold Season Benefit)
AS	Ajutor Social
CFM	Calea Ferată din Moldova (Railway Company)
CPF	Country Partnership Framework
CPSD	Country Private Sector Diagnostic
CRW	Crisis Response Window
DPO	Development Policy Operation
EBRD	European Bank for Reconstruction and Development
ECF	Extended Credit Facility
EFF	Extended Fund Facility
EU	European Union
EVRF	Energy Vulnerability Reduction Fund
FDI	Foreign Direct Investment
G2B	Government-to-Business
GD	Government Decision
GDP	Gross Domestic Product
GFCC	Global Concessional Financing Facility
GHG	Greenhouse Gas
GMI	Guaranteed Minimum Income
HBS	Household Budget Survey
IFIs	International Financial Institutions
IMF	International Monetary Fund
IPF	Investment Project Financing
JICA	Japan International Cooperation Agency
LPAs	Local Public Authorities
MAIC	Multi-Annual Contracts for Railway Infrastructure
MDTF	Multi-Donor Trust Fund
MFA	Macro-Financial Assistance
MGRES	Moldavskaya GRES
MSMEs	Micro, Small, and Medium Enterprises
NBCOs	Non-Bank Credit Organizations
NBM	National Bank of Moldova
NBS	National Bureau of Statistics
NCFM	National Commission for Financial Markets
NDC	Nationally Determined Contribution
NFRLD	National Fund for Regional and Local Development
NPL	Non-Performing Loan
OCHA	Office for the Coordination of Humanitarian Affairs
PEFA	Public Expenditure and Financial Assessment
PFM	Public Financial Management
PLR	Performance and Learning Review
PPG	Public and Publicly Guaranteed Debt
PSCs	Public Service Contracts
RBF	Results-Based Financing
RE	Renewable Energy
SA	Social Assistance
SCAs	Savings & Credit Associations
SCD	Systematic Country Diagnostic
SCM	Superior Council of Magistracy
SCP	Superior Council of Prosecutors
SMEs	Small and Medium Enterprises
SOEs	State-Owned Enterprises
VAT	Value-Added Tax
WB	World Bank
WDI	World Development Indicators
yoy	Year-on-year

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REPUBLIC OF MOLDOVA

MOLDOVA EMERGENCY RESPONSE, RESILIENCE, AND COMPETITIVENESS

SUPPLEMENTAL DEVELOPMENT POLICY OPERATION (DPO)

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SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Project ID	Parent Project
P180359	P175640

Proposed Development Objective(s)

The DPO aims to (i) mitigate the impact of the war in Ukraine on refugees and households; and (ii) build resilience and enhance competitiveness to reduce vulnerabilities to future shocks.

Organizations

Borrower:	REPUBLIC OF MOLDOVA
Implementing Agency:	Ministry of Finance

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Financing	**43.76**

DETAILS

Trust Funds	43.76
Trust Funds	43.76

INSTITUTIONAL DATA

Overall Risk Rating

High

Results

Indicator Name	Baseline	Target
Results Indicator #1: Share of employed Ukrainian women as percentage of total refugees' employment contracts registered at the National Employment Agency.	Zero percent (2021)	75 percent (2024)
Results Indicator #2: Share of refugees from Ukraine (age 6-18 years) requesting education services enrolled in the educational system.	Zero percent (2021)	85 percent (2024)
Results Indicator #3: Number of female-headed families receiving social assistance.	26,784 (2021)	32,000 (2024)
Results Indicator #4: Amount of renewable energy capacity auctioned by the Government to the private sector.	Zero MW (2021)	40 MW (2024)
Results Indicator #5: Share of insurance companies that comply with the new capital requirements.	60 percent (2021)	100 percent (2024)
Results Indicator #6: Share of local infrastructure projects financed through the National Fund for Regional and Local Development.	Zero percent (2021)	80 percent (2024)
Results Indicator #7: Signed Multi-Annual Infrastructure and Public Service Obligation contracts.	No (2021)	Yes (2024)
Results Indicator #8: Share of new active G2B digital services envisaged by the reform.	Zero percent (2021)	75 percent (2024)

IBRD AND IDA SUPPLEMENTAL FINANCING DOCUMENT FOR A PROPOSED GRANT TO THE REPUBLIC OF MOLDOVA

1. INTRODUCTION AND COUNTRY CONTEXT

1. **The proposed operation provides US$43.76 million in supplemental grant financing for the first Moldova Emergency Response, Resilience, and Competitiveness Development Policy Operation (DPO[1]) to help the Government of Moldova (GoM) cover an unanticipated financing gap related to severe spillovers from the war in Ukraine and energy prices.** On June 2, 2022, the World Bank's Board of Executive Directors approved the first in a series of two operations, in the amount of US$159.24 million, to support the Republic of Moldova's efforts to respond to unprecedented challenges, while maintaining momentum on the long-term agenda of building resilience and enhancing competitiveness. The DPO's program development objectives are to: (i) mitigate the impact of the war in Ukraine on refugees and households; and (ii) build resilience and enhance competitiveness to reduce vulnerabilities to future shocks. The operation is aligned with the World Bank Group's Global Crisis Response Framework.

2. **Energy prices have increased substantially since the approval of DPO1, reaching levels that are placing a severe strain on households and threatening social cohesion.** Due to the spillovers from the war in Ukraine, the Republic of Moldova is facing unprecedented challenges, which are straining its households, economy, and public finances, despite the country's strong development efforts. With the price of imported gas reaching a record high of US$1,883 for 1,000m^3 in September 2022, the average tariff faced by households has reached US$1,578, from a tariff of US$974 at the time of the approval of DPO-1. Moreover, since electricity and heat generation in the Republic of Moldova is more than 90 percent based on natural gas, tariffs for residential heating and electricity have also increased. The increase in tariffs for electricity has so far been less dramatic due to competitive imports from Ukraine and cheap electricity from the Moldavskaya GRES (MGRES) in Transnistria, which relies on preferential supplies from Gazprom. However, these two sources of electricity, which accounted until recently for about 80 percent of Moldova's electricity supply, have become unavailable due to a decision by MGRES, made in November 2022, no longer to sell electricity to Moldova's Energocom, and a decision by Ukraine to stop the export of electricity because of the severe damage to the Ukrainian power system caused by targeted Russian strikes in October 2022.

3. **The authorities are moving swiftly to address the energy crisis before the beginning of the cold season.** In October 2022, the Government recapitalized Energocom for an advance payment to Gazprom to avoid the potential interruption of the gas supply and for a purchase of electricity from Romania and European market to offset the reduction of electricity from MGRES and Ukraine. The GoM also purchased gas from the European Union (EU) over October to early November, utilizing the first tranche of a European Bank for Reconstruction and Development (EBRD) line of credit. The authorities have also decided to reduce the risk of future gas interruptions and potential spikes in gas prices by planning to purchase in November and December 2022 a substantial amount of gas to meet Moldova's needs for the winter at an average price expected to be considerably cheaper than the expected price for January through March 2023 based on the gas prices in the futures market. The authorities are also finalizing the purchase of the entire oil needs for the cold season necessary for the largest cogeneration powerplant in Chișinău (i.e., combined heat and electricity powerplant Thermoelectrica) to switch from gas generation

[1] P175640

to oil. The authorities are also setting up the Energy Vulnerability Reduction Fund (EVRF) to mitigate the impact of gas, heating, and electricity tariffs on households during the winter.

4. **A substantial increase in financing needs can be expected, especially during the last months of 2022 and the first months of 2023.** Thanks to higher tax revenues and grants than forecast at the time of DPO1 and a prudent fiscal policy undertaken by the authorities in the first nine months of 2022, the overall 2022 executed deficit is expected to be smaller than originally projected. The authorities plan to use some of the fiscal savings that have been accumulated during the year, together with the remaining balance of the EBRD line of credit, for the advance purchase of gas and oil for the winter and to cover the additional cost of electricity. The procurement of energy resources will not affect the overall deficit, as the transactions are recorded as financing to the overall deficit (below the line). In 2023, the large part of the unanticipated additional expenditure needs, which are mostly concentrated in the first quarter of 2023, will emerge from the measures to mitigate the impact of higher tariffs on households, including through the newly established EVRF. Increased spending on social protection (about 2 percent of GDP) will be partially absorbed by spending reprioritization, but it is still expected to result in a higher overall deficit in 2023. As a result, the general financing needs are expected to be US$175 million higher than the DPO1 estimates. The increased financing needs are expected to be fully financed by an increase in support from multilateral and bilateral partners of US$190m, including the recently announced financing from the EU, the Japan International Cooperation Agency (JICA) and the Agence Française de Développement (AFD). This Supplemental DPO is expected to play a critical role in the first two months of 2023, by supporting general financing needs until programmed domestic and external resources materialize, reducing the risks of constraining the capacity of the GoM to support the reform program supported by DPO1.

5. **The expected increase in financing needs due to the impact of the higher energy prices is accompanied by still large spending related to the massive influx of refugees from Ukraine who decided to remain in the Republic of Moldova.** As of September 2022, almost 91,000 refugees from Ukraine have remained in the Republic of Moldova (similar figures to at the time of DPO1). About 40 percent of the refugees are mothers who are reported to be travelling with children (about 50 percent of total refugees), while the remaining 10 percent are mostly elderly people or with disabilities. About 65 percent of refugees are women or girls under 18. The influx of refugees is overwhelming for such a small country: those refugees, who have decided to remain, represent about 4 percent of the total population; the adults represent 6 percent of the active labor force;[2] and school-age refugees represent about 9 percent of the pupils that regularly attend pre-kindergarten to secondary schools.

6. **To support the GoM's reform efforts under the DPO series and in recognition of the impact of the war in Ukraine, including the country's generous hosting of refugees, the World Bank has established a Multi-Donor Trust Fund (MDTF) for Co-financing of the Moldova Development Policy Program (TF073849).** The MDTF is designed to provide a targeted and rapid mechanism to channel donor contributions to provide grants to the GoM in support of reforms over the course of the DPO series, through Recipient-Executed Trust Fund grants. Importantly, the MDTF simplifies the process for the Republic of Moldova of receiving funds, while ensuring that the donors' support is provided under the DPO's established operational arrangements, including an adequate macroeconomic policy framework, thereby reducing the transaction costs for the Government and partners. To date, contributions have been received from Norway and the United States to finance this Supplemental DPO. Dialogue is

[2] In 2021, 843,400 Moldovan were employed and 28,200 were unemployed for active labor force of 871,600.

advancing with other donors to provide co-financing grant support through the next planned DPO in the series (DPO2, P179086).

7. **The Program supported by the first DPO is being successfully implemented and remains in compliance with the provisions of the legal agreement.** Following the approval of DPO1, the authorities continued to implement reforms despite a more challenging operating environment. Some triggers for DPO2 – which is expected to have a Board date in early March 2023 – have already been completed, while others are still under preparation.

8. **The overall risk to the achievement of the DPO program development objectives remains high.** While a strong domestic consensus remains around the DPO reform agenda, the impact of the war in Ukraine and the spike in energy prices have created significant uncertainty and risks to the reforms supported by the Program. A further increase in energy costs due to the challenging relationship with Gazprom, given the dispute over the settlement of the historical debt, estimated by Gazprom at about US$700 million, cannot be ruled out. High and rising energy prices may cause increasing social discontent which, combined with the strong polarization of the electorate, could reduce the popular support for the Government's agenda, even if the Government maintains its strong commitment to the Program. These risks are partially mitigated by the GoM's emphasis on social protection measures and its proactive strategy towards diversification of energy sources, including through the implementation of reforms supported by the DPO series. These risks are also mitigated by strong support from other development partners through technical and financial assistance. Nevertheless, the residual risk remains high.

2. THE IMPACT OF CRISIS, ECONOMIC DEVELOPMENTS AND OUTLOOK

9. **The spillovers from the war in Ukraine and the heatwave during the summer of 2022 have brought significant challenges to the Moldovan economy.** With the loosening of COVID-19 restrictions, economic activity bounced back with growth of 13.9 percent in 2021, from a decline of 7.4 percent in 2020. However, on the back of eroding disposable incomes, growth has decelerated significantly in 2022, resulting in zero growth in the first half of the year. Lower remittances, together with high inflation and uncertainties, led to only modest growth in private consumption, despite the substantial increase in social assistance and the increase in minimum pensions. Trade disruptions, lower foreign investment inflows, and high interest rates have taken a significant toll on private investment. Strong public consumption added 1.3 percentage points to growth, while net exports contributed 3.9 percentage points to overall growth, thanks to a surprising uptick in exports of goods (45.4 percent). On the production side, agriculture and construction were the most adversely affected due to higher input costs (building materials and fertilizers) and high interest rates. The financial and insurance sector performed well and contributed 0.4 percentage point to the overall growth.

10. **Despite strong export performance, Moldova's external position has deteriorated.** The current account deficit increased by 16.1 percent in the first half of 2022, as the cost of energy imports expanded rapidly, while remittances decreased by 5.8 percent. On the upside, the trade balance in services improved by 81.3 percent due to strong growth in export of transport services, following the closure of the port of Odessa in Ukraine and subsequent re-routing of a portion of the Ukrainian exports through the Romanian port of Constanta by using Moldovan railways. At the same time, exports of the IT sector

increased by almost 38 percent. The CAD was financed primarily by reserve assets and foreign direct investment (FDI) in the form of reinvested profits. External debt, both public and private, marginally decreased to 60.9 percent of GDP.

11. **Inflationary pressures have accelerated since the approval of DPO1, despite a significant tightening of the monetary stance.** Upward pressure on prices started in 2021 and has been further fueled by higher gas and food prices, and supply chain disruptions exacerbated by the war in Ukraine. As a result, inflation surged in 2022, reaching 34 percent in September 2022, with the consumer price index (CPI) for the regulated prices of utilities increasing by 60.3 percent year-on-year (y-o-y). The National Bank of Moldova (NBM) has increased the policy rate regularly since 2021, bringing it to 21.5 percent in August 2022. The NBM has also used a prudent exchange rate policy, resulting in comfortable foreign reserves that currently stand at around US$4 billion and cover more than four months of imports.

12. **The banking sector shows signs of resilience, although the share of non-performing loans (NPLs) remains high.** After an initial steady withdrawal of bank deposits due to rising concerns from the public in the first weeks of the war in Ukraine, the situation has now normalized. Although the ratio of NPLs to total loans has continued its long-term decline since the 2014 banking crisis— decreasing to 6.8 percent in August 2022, down from 7.4 percent in 2020, - it remains, however, relatively high and may further increase, as interest rates rise and the full impact of the war in Ukraine on economic activity and household disposable income materializes.

13. **The fiscal position proved to be resilient in the first three quarters of 2022, despite headwinds from the war in Ukraine.** Revenues increased by 21.3 percent in the first nine months of 2022, due to higher import and domestic prices, and strong corporate income tax collections, which more than compensated for the increase in spending of 19.4 percent. As a result, the fiscal deficit was smaller than expected, reaching less than 1 percent of GDP as of September 30, 2022. Protecting the purchasing power of the households against high food and energy prices has been a key priority for the authorities, as reflected in the increased social spending and subsidies of 30.1 percent and 44 percent, respectively. In the second quarter of 2022, public and publicly guaranteed (PPG) debt decreased to around 30.2 percent of GDP, as the authorities borrowed on the domestic market only to refinance the existing debt.

14. **The combined impact of rising energy prices and reduced purchasing power due to high levels of inflation could lead poverty rates to double compared to the winter of 2021, if not mitigated.** The main sources of disposable income for households—salaries, remittances, and the majority of social transfers—are already registering negative growth in real terms. Moreover, utility expenditures (electricity, network gas and central heating) for households during the 2022–2023 heating season are, on average, 2.7 times higher than in the same period last year. With inflation at around 30 percent, and consumption and income growth expected to increase by 15 percent, the poverty rate during the 2022–2023 heating season is estimated to be 28.0 percentage points higher than the previous heating season, equivalent to a doubling of poverty rates across heating seasons. The overall impact on poverty is mostly driven by higher energy tariffs, accounting for 19.6 percentage points, while the increase in prices on non-energy products is expected to contribute 7.0 percentage points. With the current government measures in place, including the EVRF, and the enhanced Ajutor pentru Perioada Rece a Anului (Cold Season Benefit, or APRA) and redesigned Ajutor Social (AS) (both supported by DPO1), the impact of rising energy prices can be mitigated by as much as 12.7 percentage points, but not completely offset.

Table 1: Key macroeconomic indicators

	DPO1					Supplemental DPO				Difference	
	2021	2022	2023	2024	2025	2022	2023	2024	2025	SDPO-DPO1 2022	SDPO-DPO1 2023
Real economy											
Nominal GDP (MDL, billion)	241.9	273.9	299.6	327.9	359.1	271.8	303.3	332.9	363.9	-2.1	3.7
Real GDP (percent change)	13.9	-0.4	2.7	4.2	5.0	-1.5	1.6	4.2	4.1	-1.1	-1.1
Contributions:											
Consumption (percentage points of GDP)	13.2	1.1	3.4	4.0	4.1	0.5	2.9	4.3	4.1	-0.6	-0.5
Gross investment (percentage points of GDP)	5.7	-0.3	1.0	1.2	1.9	-0.8	0.5	1.2	1.9	-0.5	-0.5
Net exports (percentage points of GDP)	-5.0	-1.2	-1.9	-1.3	-1.0	-1.2	-1.9	-1.3	-1.0	0.0	0.0
Exports (percent volume change)	17.5	0.8	4.1	4.3	5.9	59.5	4.1	4.1	4.3	58.7	0.0
Imports (percent volume change)	19.2	2.0	4.6	3.9	4.3	33.8	4.5	3.4	3.3	31.8	-0.1
GDP deflator (percent change)	6.3	13.9	6.4	5.1	4.3	14.1	9.8	5.1	5.0	0.2	3.4
Consumer price index (CPI) (average) (percent change)	5.1	24.7	7.8	5.5	4.9	28.6	14.1	6.2	4.9	3.9	6.3
Fiscal Accounts											
Expenditure (percentage of GDP)	33.9	37.0	36.7	36.6	36.5	36.4	37.9	36.6	36.5	-0.6	1.2
Revenues (percentage of GDP)	32.0	30.3	31.7	32.2	32.4	32.6	31.9	32.2	32.5	2.3	0.2
General government balance (percentage of GDP)	-1.9	-6.7	-5.0	-4.4	-4.1	-3.8	-6.0	-4.4	-4.0	2.9	-1.0
Public and publicly guaranteed debt (eop) (percentage of GD	33.8	37.6	40.2	42.3	42.1	37.7	40.3	42.2	42.0	0.1	0.1
Balance of Payments											
Current account balance (percentage of GDP)	-12.4	-13.0	-12.2	-10.6	-9.9	-13.4	-14.5	-10.8	-9.9	-0.4	-2.3
Imports (percentage of GDP)	57.8	61.6	64.2	63.6	63.4	72.7	74.2	75.1	76.0	11.1	10.0
Exports (percentage of GDP)	30.6	31.7	35.6	36.1	36.2	48.9	49.7	50.5	51.3	17.2	14.1
FDI (percentage of GDP)	1.7	0.5	1.5	1.5	1.7	0.4	1.4	2.5	2.3	-0.1	-0.1
Remittances (percentage of GDP)	14.8	14.7	15.2	15.0	14.9	14.5	14.5	14.7	14.8	-0.2	-0.7
External debt (percentage of GDP)	64.1	68.8	73.8	75.6	73.0	64.5	65.0	65.6	66.0	-4.3	-8.8
Terms of trade (percentage change)	14.8	-2.3	-2.5	0.1	0.2	-2.3	-4.7	-0.1	0.2	0.0	-2.2
Nominal GDP (US$, billion)	13.7	13.8	13.8	14.5	15.3	14.3	14.1	14.5	14.3	0.5	0.3

Source: World Bank calculations.

Table 2: Key fiscal indicators for the public sector (% of GDP)

	DPO1					Supplemental DPO				Difference (p.p.)	
	2021	2022	2023	2024	2025	2022	2023	2024	2025	SDPO-DPO1 2022	SDPO-DPO1 2023
Total revenues (and grants)	32.0	30.3	31.7	32.2	32.4	32.6	31.9	32.2	32.5	2.3	0.2
Tax revenues	29.4	28.4	29.8	30.5	30.7	29.7	29.7	30.2	30.4	1.3	-0.1
Personal income tax	2.1	2.1	2.1	2.2	2.3	2.2	2.2	2.3	2.3	0.1	0.1
Corporate income tax	2.5	2.3	2.4	2.5	2.5	2.6	2.5	2.6	2.6	0.3	0.1
Property tax	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.4	0.4	0.0	0.0
Value added tax	10.5	9.8	10.4	11.2	11.3	10.6	10.6	10.8	10.9	0.8	0.2
Excises	3.1	3.0	3.2	3.3	3.3	3.1	3.0	3.0	3.1	0.1	-0.2
Taxes on international trade	0.9	0.9	1.0	1.0	1.0	1.0	0.9	0.9	1.0	0.1	-0.1
Social benefits	9.0	9.1	9.4	9.2	9.2	9.0	9.2	9.2	9.2	-0.1	-0.2
Other	0.9	0.9	1.0	0.8	0.8	0.7	1.0	1.0	0.9	-0.2	0.0
Non-tax revenues and other revenues	1.5	1.3	1.3	1.2	1.2	1.5	1.4	1.5	1.6	0.2	0.1
Grants	1.0	0.6	0.6	0.5	0.5	1.7	0.8	0.5	0.5	1.1	0.2
Expenditures	33.9	37.0	36.7	36.6	36.5	36.4	37.9	36.6	36.5	-0.6	1.2
Wages and compensation	7.8	7.9	7.8	8.0	8.1	7.8	7.8	7.8	8.1	-0.1	0.0
Goods and services	6.9	7.7	7.3	7.2	7.1	6.9	7.0	7.1	7.1	-0.8	-0.3
Interest payments	0.8	1.1	1.5	1.1	1.0	1.1	1.8	1.1	1.0	0.0	0.3
Subsidies	1.5	1.9	1.7	1.6	1.6	2.1	1.9	1.7	1.6	0.2	0.2
Social benefits	11.7	12.8	13.3	12.7	12.7	13.5	15.3	13.1	12.7	0.7	2.0
Other current expenses	1.6	2.1	1.6	1.7	1.6	1.6	1.3	1.5	1.6	-0.5	-0.3
Nonfinancial assets	3.6	3.5	3.5	4.3	4.4	3.4	2.8	4.3	4.4	-0.1	-0.7
Primary balance	-1.0	-5.6	-3.5	-3.3	-3.1	-2.2	-4.2	-3.3	-3.0	3.4	-0.7
Overall balance	-1.9	-6.7	-5.0	-4.4	-4.1	-3.8	-6.0	-4.4	-4.0	2.9	-1.0

Source: World Bank calculations.

Table 3: Balance of payments financing requirements and sources, (US$ million)

	DPO1					Supplemental DPO				Difference	
	2021	2022	2023	2024	2025	2022	2023	2024	2025	SDPO-DPO1 2022	SDPO-DPO1 2023
Financing requirements	**1,954**	**2,233**	**2,099**	**1,976**	**1,985**	**2,358**	**2,655**	**2,070**	**2,037**	**125**	**556**
Current account deficit (incl. errors and omissi	1,595	1,792	1,664	1,532	1,508	1,917	2,032	1,549	1,519	125	368
Private debt amortization	181	185	189	193	198	185	189	193	198	0	0
Public debt amortization	178	256	246	251	279	256	434	328	320	0	188
Financing sources	**1,954**	**2,233**	**2,099**	**1,976**	**1,985**	**2,358**	**2,655**	**2,070**	**2,037**	**125**	**556**
FDI	239	65	203	224	252	58	217	224	252	-7	14
Portfolio investments (net)	-6	3	3	3	3	0	3	3	3	-3	0
Private external debt disbursements	1,357	944	1,578	1,752	1,595	944	1,576	1,752	1,595	0	-2
Public external debt disbursements	532	744	405	539	338	999	738	539	338	255	333
Change in reserves (- increase)	-118	515	-37	-489	-147	395	174	-395	-95	-120	211
Other capital flows (net)	-50	-38	-53	-53	-56	-38	-53	-53	-56	0	0

Source: World Bank calculations.

MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

15. **GDP growth is expected to contract by 1.5 percent in 2022, and slowly rebound to 1.6 percent in 2023, reaching its full potential only in 2024 due to inflation dynamics, the disruption in energy supplies and developments in the ongoing war in Ukraine.** Reduced household purchasing power due to higher energy and food prices, together with depressed consumer confidence, is expected to severely affect private consumption. The measures taken by GoM in 2021 and 2022 (e.g., increase in minimum pensions and indexation, social protection measures, and higher minimum wage) and higher projected remittance receipts from the EU, are expected to partially mitigate the impact of higher energy and food prices on households. However, the main sources of disposable income—salaries, remittances, and most social transfers—are already registering negative growth in real terms. As a result, projected GDP growth in 2022, which has been downgraded by 1.1 percentage points compared with the projection at the time of DPO1, is now 5.4 percentage points below the pre-war forecast (3.9 percent vs -1.5 percent). Growth is expected to remain subdued and to slowly rebound to 1.6 percent in 2023 (also 1.1 percentage points below the DPO1 projection), reaching its full potential only in 2024.

16. **High inflation is expected to persist throughout 2023 and remain well above the NBM's inflation target until 2024.** Inflationary pressures are expected to persist due to higher international prices, particularly for food, energy and other imports, and the disruption of trade routes. The inflation rate is expected to peak in the fourth quarter of 2022, and average inflation is projected to be around 28.6 percent y-o-y for 2022. High inflation will persist in 2023, only receding back slowly toward the NBM inflation target of 5 percent +/- 1.5 percent in 2024, under the assumption of a moderation in import prices and limited passthrough into wages and pensions. It is also expected that the EVRF will play an important role in containing the pressure on regulated prices of utilities, which were a major driver of inflation in 2022, increasing by over 60 percent. The NBM is expected to be moderately active on the forex market and smooth the fluctuations of the national currency, particularly in the heating (winter) season when demand for foreign currency increases due to energy imports.

17. **Moldova's external position is expected to weaken, reflecting an increase in the price of imports, coupled with subdued capital inflows due to the heightened uncertainty.** With high imported inflation leading to a nominal increase in the level of trade imbalances, and with slowing remittances, the current account balance is expected to deteriorate. In the medium term, the inflow of remittances will stabilize, as Moldovan migrants move to other destinations, and this will help reduce the structural deficit of the current account. Overall, the CAD is expected to be higher than in the pre-COVID-19 period. The

increased external financing requirements compared to the projections in DPO1 are expected to be met through financing from bilateral and multilateral partners, smoothing the pressure on the foreign reserves.

18. **A weakening of Moldova's fiscal position can also be expected in the medium term.** The fiscal stance will be confronted by increasing social spending to: (i) protect the purchasing power of households against higher food and energy prices; (ii) procure alternative energy resources; (iii) support refugees from the war in Ukraine; and (iv) bolster investment and the reform program. The additional spending is expected to be partially compensated by the containment of the wage bill, a reprioritization of spending, and efficiency gains. Meanwhile, despite the relatively strong performance in 2022, revenues are expected to decline in real terms, as the spillovers from the war materialize and economic activity subsides. As a result, the fiscal deficit is estimated to increase to 6 percent of GDP in 2023 (up by 1 percentage points on the projection in DPO1). In addition, possible contingent liabilities, including from the historical commercial debt of Moldovagaz to Gazprom and social pressures, will need to be monitored closely. Public debt is expected to peak at about 42 percent of GDP in 2024, after which it is expected to stabilize, as fiscal support normalizes and growth dividends are generated from the planned reforms.

Table 4. General Government financing requirements and sources, 2022–2023 (US$ million)

	DPO1		Supplemental DPO		Difference	
	2022	2023	2022	2023	SDPO-DPO1 2022	SDPO-DPO1 2023
Financing Requirements	2358	2060	2599	2235	241	175
Overall Deficit	920	683	544	846	-376	163
Amortization on external PPG debt	134	127	134	127	0	0
Amortization of domestic PPG debt	1304	1250	1345	1262	41	12
Energy procurements - below the line 1/			576		576	0
Financing Sources	2358	2060	2599	2235	241	175
Domestic borrowing	1304	1480	1345	1494	41	14
Privatization and others 2/	47	144	48	145	1	1
Total external financing 3/	658	405	876	711	218	306
Of which budget support from official creditors	*578*	*371*	539	549	-39	178
Cash balance (- increasing cash balance)	349	31	330	-115	-19	-146
Memo						
Cash Balance (end of year)	322	291	341	456	19	165
Grants	86	0	123	27	37	27

Source: World Bank calculations.

1/Loans to Energocom for advance purchase of gas in 2022 and for additional cost of the pruchase of electicity in the EU;
It includes $52m of loan to Moldovagaz in 2022

2/ Includes privatization receipts and other one-off items

3/ Includes Bilateral and Multilateral Loans for project financing

19. **An increase of US$241 million in general government financing needs is expected in 2022, compared to DPO1 estimates, concentrated in the last two months of 2022.** While the deficit in 2022 is expected to be lower than that forecasted at the time of DPO1, the recent decisions by Gazprom (to reduce the supply of gas) and by MGRES (to halt the supply of electricity) are forcing the authorities to replace them with imports from the EU. In October 2022, the Government recapitalized Energocom, which provided about US$52 million to Moldovagaz for an advance payment to Gazprom to avoid the potential interruption of the gas supply. Similarly, the recapitalization of Energocom helped with the

purchase of electricity from Romania and other European markets and to offset the reduction of supply of electricity from MGRES and Ukraine. GoM also purchased a total of EUR100 million worth of gas from the EU between October 17-November 2, 2022, utilizing the first tranche of the EBRD line of credit. Going forward, the authorities have decided to reduce risks of future gas interruptions and potential spikes in gas prices by planning to purchase in November and December a substantial amount of Moldova's gas needs for the winter at an average price that is expected to be up to US$500 per 1,000m³ cheaper than the price that is expected to be paid in January through March based on the gas prices in the futures market (US$1,493 per 1,000m³). To this end, the authorities plan to use part of the accumulated fiscal buffers (about US$200 million) during 2022 thanks to a prudent fiscal policy and increase in revenue collection and grants from development partners, and the remaining EUR$200 million of the EBRD line of credit for the advance purchase of gas and oil and for additional cost of electricity in 2022, by recapitalizing and on-lending EBRD loans to Energocom. While the procurement of energy resources will not affect the overall deficit, as the transactions are recorded as financing to the overall deficit (below the line), it will lead to a depletion of cash balance, exposing the fiscal stance to increased pressures in the first months of 2023. The fast processing of the Supplemental DPO aims to reduce said pressure.

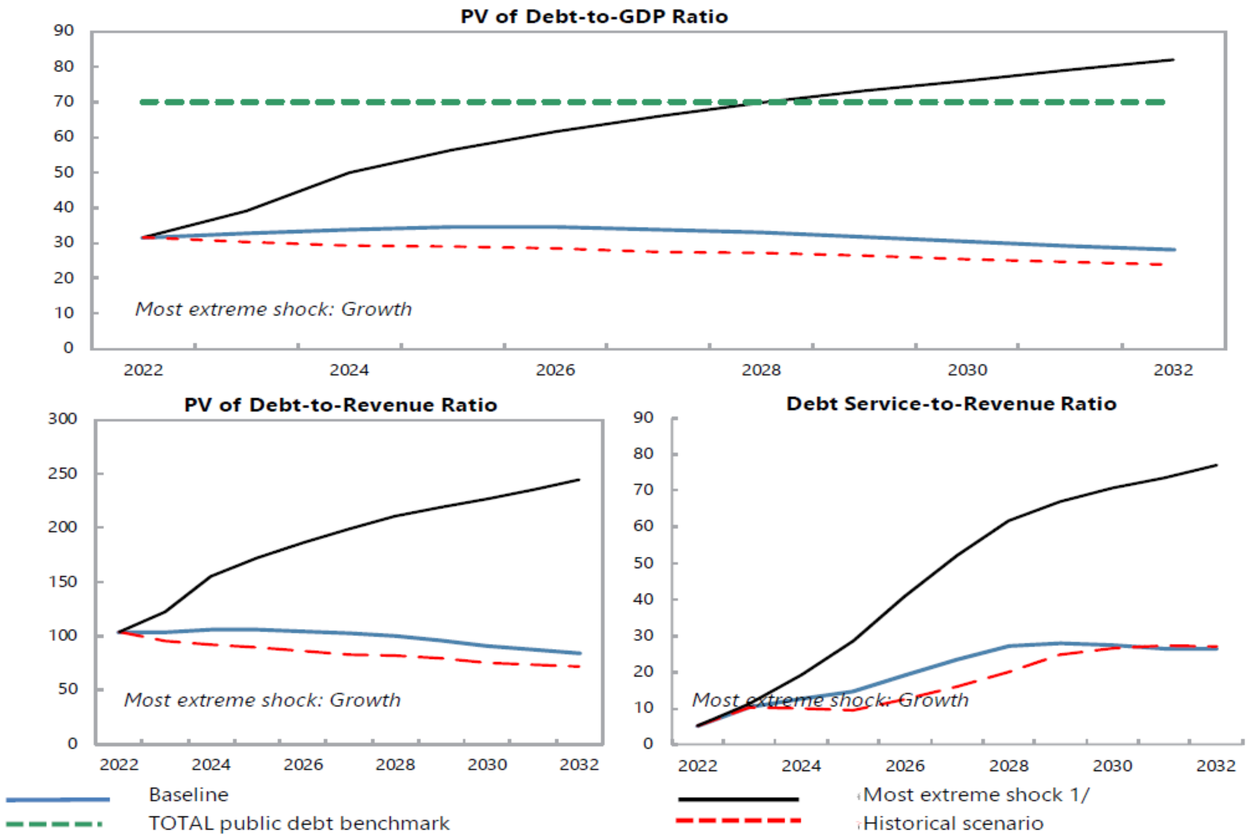
20. **Based on the updated projections, there will be an unexpected increase in general government financing needs in 2023 of USS175 million, concentrated in the first quarter of 2023.** The size of the financing needs for 2023 depends primarily on energy supplies, prices, and weather conditions. Under the baseline, the spending category that is expected to increase substantially from the spike in gas prices is related to the measures put in place by the Government to mitigate the impact of higher tariffs on households, including through the newly established EVRF.[3] The increased spending of social protection (about 2 percent of GDP) will be partially absorbed by spending reprioritization, but it is still expected to result in a higher overall deficit in 2023. The increased general financing needs are expected to be fully financed by an increase in support from multilateral and bilateral partners of US$190 million, including the recently announced financing from the EU, the planned parallel financing of JICA to DPO2 and a AFD policy loan. The supplemental DPO is expected to play a critical role in the first two months of 2023 by complementing the reduced cash balance to support spending until the programmed domestic and external resources materialize.

21. **Public debt remains sustainable despite the deterioration of the short-term outlook.** Public debt is expected to increase in the short term because of the anticipated large primary deficit. After reaching a peak of about 42 percent of GDP in 2024, total public debt is expected to stabilize at around 40 percent of GDP, once the fiscal support retrenches and growth dividends are generated from the planned reforms. The present value of the public debt-to-GDP ratio remains below the indicative threshold under the baseline scenario, reaching about 35 percent of GDP in 2025. During this period, the increase in the projected debt will be driven mainly by the widening primary deficit and exchange rate movements, which more than offset the real GDP growth and other factors. New financing is expected to consist primarily of borrowing from the multilateral and bilateral lenders in the medium term, while private sources are expected to start playing a greater role in the longer term. These outcomes hinge on continued prudent

[3] GoM also plans to spend US$47 million for the Energy Vulnerability Reduction Fund partially financed by the grant from Germany (EUR40 million).

fiscal policy, together with sound macroeconomic policy, as envisaged under the IMF Program. Lower-than-expected growth[4] remains the largest risk to debt sustainability.

Figure 1: Indicators of public debt under alternative scenarios, 2022–2032



22. **The macroeconomic policy framework, anchored to the IMF Program, is adequate for this proposed operation despite the deterioration of global and domestic economic conditions.** The impact of the war in Ukraine is expected to put further pressure on Moldova's short-term economic activity, weakening the country's fiscal position both from a decline in revenues due to the lower economic activity and from an increase in social spending to mitigate the impact of the shock, and higher-than-expected energy prices. The exchange rate continues to be the first line of defense against external shocks and the NBM has demonstrated a swift response to the increase in inflation. The financial sector entered the crisis well-capitalized. On the fiscal front, despite the weakening of the fiscal position in the short term, public debt remains sustainable and is expected to stabilize in the medium term, when fiscal support retrenches, and growth dividends are generated from the planned reforms.

23. **Major risks stem from the uncertainties over the duration and severity of the ongoing war in Ukraine and associated spikes in gas and electricity prices.** The supply of gas from Gazprom could be completely halted over the dispute of the historical commercial debt between Moldovagaz and Gazprom,

[4] Growth shock is defined as one standard deviation of growth rates in the past 10 years.

estimated by Gazprom at around US$700 million (5 percent of GDP). It also represents a contingent liability for the Government with an impact on financing needs, depending on the repayment schedule that is eventually agreed upon. The lack so far of a longer-term agreement with MGRES in Transnistria on supplying electricity is also adding to the uncertainties, after Ukraine suspended its export of electricity following the destruction by Russian strikes of critical energy infrastructure[5]. Moreover, further weakening of economic activity and/or tightening of financial conditions could dampen growth prospects and risk reducing the willingness of domestic investors to roll over debt. These risks are partially mitigated by Moldova's commitment to a full adherence to the IMF Program, which serves as a macro-fiscal anchor. Moreover, a substantial part of the Government's additional financing needs, arising from the impact of the war, is expected to be met by bilateral donors, the IMF and multilateral development banks.

24. **On December 21, 2021, the IMF Board of Executive Directors approved an economic reform Program under the Extended Credit Facility (ECF) and the Extended Fund Facility (EFF) arrangements for an amount equivalent to US$558.3 million (SDR 400 million).** The 40-month Program's objectives are to sustain the post-pandemic recovery, address pressing developmental needs, and strengthen governance and institutional frameworks. Structural reforms supported by the Program aim to address vulnerabilities to improve the rule of law and the anti-corruption framework, and strengthen fiscal and financial governance, ultimately accelerating income convergence between the Republic of Moldova and its European peers. The first disbursement of about US$79.8 million (SDR 57.2 million) was released with the approval of the Program. The authorities requested an increase of access under the ECF/EFF program by about US$267 million (SDR 195 million) to help Moldova cope with the impact of the war in Ukraine and surging international energy and food prices. The augmentation request was approved by the IMF Executive Board on May 11, 2022. The IMF Executive Board completed the first reviews under the ECF/EFF arrangements in September 2022, providing access to about US$27 million (SDR 20.65 million). At end-November, 2022, the IMF staff reached staff-level agreement on policies for completion of the second review, which is expected to be discussed by the IMF Executive Board in January 2023.

3. RESPONSE TO THE CRISIS

3.1. THE GOVERNMENT'S RESPONSE

25. **The GoM acted promptly to the unprecedent social and economic challenges arising from the war in Ukraine**. The Government declared a State of Emergency and took immediate action to integrate refugees from Ukraine and to mitigate the potential economic impact on households due to the expected increase in food and gas prices. All these measures were supported by DPO1 and provide an important social safety net for both refugees and households.

26. **More recently, the Government approved the Law on Energy Vulnerability Reduction Fund (Law No. 241/2022 of July 28, 2022) and is now finalizing the secondary legislation to address the energy crisis.** Law No. 241/2022 establishes the legal basis of the organization of the EVRF with the aim of

[5] Additional cost might materialize for the purchase of electricity by Energocom from the EU in January to March if a longer-term agreement with MGRES is not reached. The additional costs will be financed through a reduction of the government cash balance.

decreasing households' energy vulnerability at times of energy price volatility, ensuring the supply of natural gas, heating energy and electricity to socially vulnerable energy consumers, and increasing energy efficiency. The EVRF regulation determines households' energy vulnerability based on their income and energy consumption (capped at last year's average consumption), dividing households into five categories, ranging from "not vulnerable" (5) to "very vulnerable" (1).

27. **The Government has also taken measures to reduce the country's dependency on a single source of supply for both gas and electricity.** The synchronization of the transmission power systems of Ukraine and Moldova with ENTSO-E,[6] together with the completion of the first cross-border gas pipeline between Moldova and Romania (Iasi-Ungheni-Chișinău pipeline), connecting the Moldovan gas transmission system with ENTSO-G,[7] is helping Moldova to have direct access to new sources of electricity and gas supply. Moldova is currently replacing the Ukrainian and MGRES electricity imports with supplies from Romania and other EU countries. The recent decision by Gazprom to reduce the supply of gas is forcing the authorities to accelerate this process of diversification for both gas and electricity.

3.2. THE BANK'S RESPONSE, STRATEGY, AND COLLABORATION WITH DEVELOPMENT PARTNERS

28. **To address the unexpected financing needs, the Government has requested this proposed Supplemental DPO for US$43.76 million.** The World Bank set up the MDTF for Co-financing of the Moldova Development Policy Program to help mobilize additional financing from bilateral donors in the form of grants, in order to provide immediate budgetary resources in support of the Government's program, should the unexpected financing needs materialize. The MDTF was established with a recognition of the undue and unpredictable impacts of the war in Ukraine on Moldova's households, economy, and fiscal position, as well as the interest of development partners in supporting Moldova at this critical juncture, following its reform efforts and socioeconomic improvements. The MDTF was designed to provide a mechanism to simplify the process for the Republic of Moldova to receive funds by channeling multiple donors' support under the DPO's established operational arrangements.

29. **This Supplemental DPO is aligned with the priorities of the upcoming FY23–FY27 Country Partnership Framework (CPF), as part of the WBG's broader effort to support the authorities in their response to the immediate impact of the combined energy and refugee crises, and efforts to build resilience against future shocks.** The financing from this supplemental DPO operation and the program it supports is aligned with the WBG's Global Crisis Response Framework, in particular its pillar 2 on "Protecting People and Preserving Jobs" (prior actions 1 to 3), pillar 3 on "Strengthening resilience" (prior actions 4 and 5) and pillar 4 on "Strengthening policies, institutions and investments for rebuilding better" (prior actions 6 to 8). The DPO series is accompanied by a broader program of technical support, including just-in-time technical advice on issues related to energy security and efficiency, as well as social protection. The World Bank is also conducting a poverty assessment with a focus on the impact of the energy crisis on the poor, as well as an assessment of impacts and needs arising from forced displacement in Moldova. The DPO series is complemented by the Micro, Small, and Medium Enterprises (MSMEs) Competitiveness Project (P177895) under implementation and the pipeline Energy Efficiency (P179280) and Education Quality Improvement (P179363) projects.

[6] The European Network of Transmission System Operators for Electricity.
[7] The European Network of Transmission System Operators for Gas.

30. **The proposed Supplemental DPO is complementary to other multilateral financing, including the IMF.** The DPO series is part of a package of coordinated financial assistance to the Republic of Moldova from international partners prepared in response to the ongoing socioeconomic emergency. This package includes the IMF Extended Credit Facility (ECF) and Extended Fund Facility (EFF), the EU Macro-Financial Assistance (MFA), a line of credit from the EBRD, and grants from bilateral partners.

4. THE REFORM PROGRAM SUPPORTED THROUGH ORIGINAL OPERATION: AN UPDATE

31. **The Program supported by DPO1 is under implementation in compliance with the provisions of the legal agreement and progress has been made toward the indicative triggers for DPO2 , although further time is needed for their completion.** Following the approval of DPO1, the authorities continued to implement reforms, despite a more challenging, than originally anticipated, operating environment. First, a draft law is currently under discussion to make permanent the temporary measures introduced by the Commission for Exceptional Situations in relation to the refugees' prior actions (1 and 2). Second, the Government has already approved with a Government Decision to update normative aspects of the Ajutor Social implementation in accordance with the amended law (Trigger 1). The Government has already approved the Government Decision to set up the Railways Agency/Authority and is in the process of finalizing the Government Decision on Public Service Obligations (PSO) for the railway passenger services (Trigger 5). Finally, a Government Decision has been approved to adopt the framework of the Public Depository of Financial Statements (Trigger 6).

5. RATIONALE FOR PROPOSED SUPPLEMENTAL FINANCING

32. **This proposed Supplemental DPO meets the criteria for supplemental financing, as laid out in the World Bank's DPF policy.** The Bank's DPF policy provides for supplemental financing—a separate financing to a DPO that has not been closed—in exceptional cases when the DPF program is on track and an unanticipated gap in financing jeopardizes a reform program that is otherwise proceeding on schedule and in compliance with the agreed policy agenda. More specifically, supplemental financing is approved when: (i) the program is being implemented in compliance with the provisions of the legal agreement with the Bank; (ii) the Member Country is unable to obtain sufficient funds from other lenders or guarantors on reasonable terms or in a reasonable time without the supplemental DPF; (iii) the time available is too short to process a further free-standing Bank DPF; and (iv) the Member Country remains committed to the program and the implementing agencies have demonstrated competence in carrying it out.

33. **On criterion (i), the program supported by DPO1 has been under implementation in compliance with the provisions of the legal agreement.** While the Government's focus has shifted toward the management of the energy crisis, as described above, it remains committed to making further progress in the implementation of the Program. Following the approval of DPO1, the authorities continued to implement reforms despite a more challenging operating environment. Nevertheless, fiscal pressures have increased, and these could lead to significant underfunding or diversion of allocated budget funds that would constrain the capacity to support the social protection pillar of the program thereby , with the risk of jeopardizing a reform program that is otherwise proceeding on schedule and in compliance with the agreed policy agenda

34. **On criterion (ii), the energy crisis has created large and unanticipated financing needs, while significant constraints remain in domestic financing.** The sizable fiscal financing needs arise within a challenging environment for domestic financing. The steady withdrawal of bank deposits in the first weeks of the war in Ukraine due to rising concerns from the public over the unfolding war forced the authorities to adopt a prudent approach with domestic financing by rolling over only existing debt coming due and not issuing new debt. The pressure on bank deposits has subsided now. However, with NBM policy rates at 21.5 percent to combat inflation, borrowing in the domestic markets is costly for the Government. Given the timeframe for when resources are needed, together with the expected liquidity pressures, and the limited resources available from domestic financing, the timing of the financial assistance from development partners, this Supplemental DPO is needed to provide resources in the first two months of 2023, to cover the increase of general financing needs of the Recipient.

35. **On criterion (iii), given the urgency of unanticipated financing needs, there is insufficient time to process a new DPO, such as through advancing the upcoming DPO2 under preparation.** The second DPO in this series is under preparation, but more time is needed for completion of the supported reforms, with a Board date expected in early March 2023. Advancing the timeline of DPO2 is not possible, given the need to complete the reforms envisaged under the programmatic series, the time for consultations with stakeholders and international partners, and time needed to build sufficient buy in for the reform program, to support its sustainability. The proposed Supplemental DPO will, therefore, help support the reform program by providing a bridge financing, while maintaining the ambition, pace, and sequencing of the supported reforms in DPO2.

36. **On criterion (iv), the Government remains committed to the Program and the policy dialogue remains robust.** The World Bank team continues the policy dialogue and to provide technical assistance, as part of the preparation of DPO2.

6. OTHER DESIGN AND APPRAISAL ISSUES

37. **The current socio-economic situation highlights further the relevance of the policy measures supported under DPO1, especially the social and distributional effects of the measures under Pillar 1.** The policy measures in Pillar 1 of this operation aim to connect refugees from Ukraine in Moldova to employment opportunities and key public services, and alleviate the adverse social and economic impacts caused by the war in Ukraine (e.g., PA3 on the reform of the social assistance). These reforms already have immediate positive social and distributional impacts. The overall impact on poverty is mostly driven by higher energy tariffs, accounting for 19.6 percentage points, while the increase in prices on non-energy products is expected to contribute 7.0 percentage points. With the current government measures in place, including the EVRF, the enhanced APRA and redesigned Ajutor Social (both supported by DPO-1), the impact of rising energy prices can be mitigated by as much as 12.7 percentage points, of which 4.1 percentage points are due to the two measures supported by DPO1. The reforms supported under Pillar 2 aim to build resilience against increasingly frequent crises, which disproportionately affect the poor and vulnerable, and to strengthen the competitiveness of Moldova’s economy. The reforms under Pillar 2 are unlikely to have significant distributional impacts in the timeframe of this DPO series. PA7, which starts the process of reforming the railway sector, focuses on safety regulation, track access charging, or a multi-

annual infrastructure contract, and does not require, prescribe, or recommend labor rightsizing in the sector. More details on the poverty and social impacts, and environmental impacts, are available in the Program Document for DPO1 parent operation (P175640).

38. **There are no changes to the assessment of environmental impact of policy measures supported by DPO1.** PA4 on diversifying energy sources and increasing the capacity of renewable energy, including the sustainable use of biomass, will contribute to further reducing greenhouse gas (GHG) emissions and fulfilling the Republic of Moldova's obligations under the Paris Agreement. PA6 on establishing the National Fund for Regional and Local Development to support infrastructure projects for local development (especially water and sanitation projects) is expected to provide a series of environmental benefits, such as improved water supply, and the reduction and prevention of water-course pollution. At the same time, supported projects in this sector may cause some adverse impacts associated with necessary civil works and wastewater treatment operations, if adequate environmental requirements are not put in place: dust, noise, and soil and water pollution, solid wastes, adverse impacts on flora and fauna, etc. In addition, it could also lead to occupational health and safety impacts and risks, if environmental requirements are not considered in project design and during project implementation. PA7 on the reorganization of railways will help indirectly make this sector more competitive and attractive for users, gradually shifting the mix of transport both for passengers and freight away from the road transport.

39. **Fiduciary risk for the proposed Supplemental DPO is assessed as moderate.** This rating appreciates the consistent achievement of high PEFA ratings and also considers the overall robustness of financial management arrangements at the NBM. Moldova has in place fundamental systems for aggregate fiscal discipline, a relatively strong framework to enable strategic allocation of resources, and efficient use of resources for service delivery. There has been significant achievement in realizing a comprehensive medium-term expenditure framework. The Republic of Moldova has a broad array of information regarding the finances of budgetary central government, and the budget document is publicly available. The Parliamentary Oversight over the external public audits produced by the Court of Accounts has been enhanced through creation of a new dedicated Public Finance Control Commission. Public procurement is governed by the Public Procurement Law (Law No. 131/2015), as subsequently amended, which brings the Republic of Moldova's legal framework closer to EU standards and is based on international best practice. There are ongoing reforms supported by various development partners in several of these areas, including reforms in tax and customs administration, budget planning and execution, and capital investments. The updated IMF Safeguards Assessment of the NBM was completed in 2020, covering the NBM's governance and control framework.

40. **The World Bank standard disbursement procedures for DPOs will apply to this operation.** Following the approval and notification by the World Bank of effectiveness, the Government will submit a withdrawal application. The proceeds will be deposited by the World Bank in a dedicated account at the NBM designated by the borrower and acceptable to the World Bank. The Borrower should ensure that an equivalent amount is credited in the Treasury current account at the NBM and used for financing budgeted expenditures. Within seven days of remittance of funds by the World Bank, the Government will provide a confirmation to the World Bank that the funds have been received by the dedicated account in the NBM. The Government will maintain accounts and records showing that disbursements were made in accordance with provisions of the Grant Agreement. If the proceeds are used for ineligible purposes

(for example, to finance goods or services on the World Bank's standard negative list), the World Bank will require the Government to promptly, upon notice from the World Bank, refund an amount equal to the ineligible expenditure to the World Bank. Amounts refunded to the World Bank upon such request will be cancelled. This condition will be reflected in the terms of the Grant Agreement. The Ministry of Finance, as the main entity responsible for financial aid coordination and management, will be the main coordinating agency for monitoring and evaluation among the other participating ministries.

41. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies, supported as Prior Actions or tranche release conditions under a World Bank Development Policy Financing, may submit complaints to the responsible country authorities, appropriate local/national grievance mechanisms, or the Bank's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Project-affected communities and individuals may submit their complaint to the Bank's independent Accountability Mechanism (AM). The AM houses the Inspection Panel, which determines whether harm occurred, or could occur, as a result of Bank non-compliance with its policies and procedures, and the Dispute Resolution Service, which provides communities and borrowers with the opportunity to address complaints through dispute resolution. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the Bank's Accountability Mechanism, please visit https://accountability.worldbank.org.

7. SUMMARY OF RISKS AND MITIGATION

42. **The overall risk rating for the proposed operation is assessed as high, as for the parent operation DPO1 at approval.** The risk ratings are included in the table below. Triggered by the war, the global economic landscape has deteriorated drastically, particularly in terms of global energy prices, inflation, and low growth in Moldova's main trade partners.

43. **Political and Governance.** Social pressure emerging from the impact of high food and fuel prices, combined with the strong polarization of the electorate, could undermine support for the Government's agenda, despite the GoM maintaining its strong commitment to the Program. These risks are partially mitigated by reforms supported under the DPO series, in particular the social protection measures, and the GoM's commitment to protect the most vulnerable.

44. **Macroeconomic.** High macroeconomic risks stem mainly from the dependency of the economy on imports of energy and associated challenges regarding fiscal sustainability. These risks are partially mitigated by Moldova's proactive strategy towards diversification of energy sources, including through reforms supported by this DPO series. Fiscal risks associated with the increase in energy prices are also mitigated by a strong support from development partners, as well as by Moldova's macroeconomic policies and commitment to a full adherence to the fiscal and monetary targets of the IMF Program. Further weakening of economic activity and/or a tightening of financial conditions could dampen the growth prospects and impact the willingness of domestic investors to roll over debt. These risks are partially mitigated by the fact that most of the Government's financing is expected to be provided by

bilateral donors, the IMF and multilateral development banks. Nevertheless, the residual risk remains high. Moreover, vulnerability of the economy, specifically agriculture, to extreme weather conditions is high, given the increase in the frequency of floods and droughts, as witnessed in summer 2022.

45. **Sector Strategies and Policies.** High risks in sector strategy relate to the fact that some prior actions of the parent DPO are part of comprehensive and complex reforms. The strong commitment of the Government to reforms and coordinated support by the international community are key mitigating factors. Also, the design of the program, as a programmatic series of two DPOs, together with technical assistance, is expected to mitigate these risks.

46. **Institutional Capacity for Implementation and Sustainability**. High risks in implementation relate to capacity constraints, which could hinder the effective implementation of the reforms and undermine the impact of the operation. The risks are partially mitigated by technical assistance provided by the WBG and other development partners to strengthen the capacity of selected agencies, (e.g., the EU in the energy sector, and the IMF in relation to economic governance). The design of the operation, as a programmatic series of two DPOs, together with technical assistance, is expected to mitigate these risks.

Table 5: Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	Substantial
2. Macroeconomic	High
3. Sector Strategies and Policies	High
4. Technical Design of Project or Program	Moderate
5. Institutional Capacity for Implementation and Sustainability	High
6. Fiduciary	Moderate
7. Environment and Social	Moderate
8. Stakeholders	Moderate
9. Other	Moderate
Overall	High

ANNEX 1: PARENT PROJECT POLICY AND RESULTS MATRIX

Prior Actions and Triggers		Results		
Prior Actions under DPO 1	**Triggers for DPO 2**	**Indicator Name**	**Baseline**	**Target**
Pillar 1--- Mitigate the impact of the war in Ukraine on refugees and households.				
Prior action #1: The Recipient has adopted provisions to: (i) allow refugees from Ukraine to enter the territory of the Republic of Moldova with their national ID; and (ii) grant Ukrainian citizens the right to work in the Republic of Moldova without obtaining the right of temporary residence for work purposes, as evidenced by decisions of the Commission for Exceptional Situations No. 1 (1st disposition) and No. 4 (7th disposition), dated February 24, 2022 and March 1, 2022, respectively, and published on the same date by the Commission for Exceptional Situations on https://gov.md/ro/content/decizii-cse.		Results Indicator #1: Share of employed Ukrainian women as percentage of total refugees' employment contracts registered at the National Employment Agency.	Zero percent (2021)	75 percent (2024)
Prior action #2: The Recipient has adopted provisions to grant school-age refugees from Ukraine the right to access educational institutions in the Republic of Moldova, as evidenced by decision of the Commission for Exceptional Situations No. 10 (disposition No. 12.1), dated March 15, 2022, and published on https://www.gov.md/sites/default/files/document/attachments/dispozitie_cse_nr_10_din15.03.2022_modif_13.pdf, and Order No. 178 from the Recipient's Ministry of Education and Research dated March 15, 2022, and published on the same date on https://mecc.gov.md/sites/default/files/ordin_mec_178_instructiune.pdf.		Results Indicator #2: Share of refugees from Ukraine (age 6–18 years) requesting education services enrolled in the educational system.	Zero percent (2021)	85 percent (2024)
Prior action #3: The Recipient has taken measures to: (i) mitigate the immediate impact of the increase in gas prices by increasing the APRA and broadening its coverage; and (ii) strengthen the main social protection programs, by improving the targeting and	(Indicative) Trigger #1: The Recipient has adopted complementary by-laws to update normative aspects of the Ajutor Social implementation in accordance with the	Results Indicator #3: Number of female-headed families receiving social assistance.	26,784 (2021)	32000 (2024)

Prior Actions and Triggers		Results		
adequacy of the benefit for the most vulnerable families, such as families with children and with members with severe disabilities, while strengthening the incentives to work, as evidenced by the Government Decision No. 332 dated November 10, 2021, published in the Official Gazette on November 12, 2021, and submission to the Recipient's Parliament of the Legislative Initiative No. 118 dated April 4, 2022, amending Law No. 133/2008 on social benefit (Ajutor Social).	amended law, including the subsistence minimum guaranteed for children and the amount of additional income disregard per child.			
Pillar 2--- Build resilience and enhance competitiveness to reduce vulnerabilities to future shocks.				
Prior action #4: The Recipient has taken measures to increase the capacity of renewable energy generation, including the quotas for sustainable biofuels and biogas, as evidenced by Government Decision No. 401, dated December 8, 2021, and published in the Official Gazette on December 10, 2021.	(Indicative) Trigger #2: The Recipient has adopted a regulatory framework for auctions and tenders in renewable energy.	Results Indicator #4: Amount of renewable energy capacity auctioned by the Government to the private sector.	Zero MW (2021)	40 MW (2024)
Prior action #5: The Recipient has enacted laws on the insurance sector to strengthen households' financial resilience by enhancing the regulatory framework and prudential requirements, as evidenced by Law on Insurance and Reinsurance No. 92/2022, dated April 7, 2022, and published in the Official Gazette on April 29, 2022, and Law on Motor Third Party Liability Insurance No. 106/2022, dated April 21, 2022, and published in the Official Gazette on April 29, 2022.	(Indicative) Trigger #3: The Recipient has expanded the coverage of the deposit guarantee scheme and established a new collateral registry to strengthen households' financial resilience, reinforcing the secured transaction framework and easing access to finance.	Results Indicator #5: Share of insurance companies that comply with the new capital requirements.	60 percent (2021)	100 percent (2024)
Prior action #6: The Recipient has: (i) taken measures to establish the National Fund for Regional and Local Development to support local development of infrastructure projects, including water and sanitation projects; and (ii) adopted regulations for its operationalization as evidenced by Law No. 27/2022, dated February 10, 2022, published in the Official Gazette on March 1, 2022; Government Decision No 152/2022 Dated March 9, 2022, published in the Official Gazette on March 18, 2022, Government	(Indicative) Trigger #4: The Recipient has adopted a framework to the reform water and sanitation services.	Results Indicator #6: Share of local infrastructure projects financed through the National Fund for Regional and Local Development.	Zero percent (2021)	80 percent (2024)

Prior Actions and Triggers		Results		
Decision No. 172/2022, dated March 16, 2022, published in the Official Gazette on March 18, 2022; and Government Decision No. 271/2022 dated April 20, 2022 and published in the Official Gazette on April 22, 2022.				
Prior action #7 The Recipient has adopted the Railway Transport Code and its associated implementation Action Plan to reorganize the railway sector and spur competition, including: (i) the creation of a national authority for railway safety; (ii) the delegation of the market regulation competencies to the autonomous public authority in the field of competition; and (iii) the establishment of a framework for multi-annual infrastructure contracts for railway infrastructure and public service contracts for railway passenger operations, as evidenced by Law No. 19/2022, dated February 3, 2022, published in the Official Gazette on February 18, 2022, and Government Decision No. 264, dated April 20, 2022, published in the Official Gazette on April 22, 2022.	(Indicative) Trigger #5: The Recipient has adopted complementary by-laws to further support the railway reorganization and harmonize the national legislation with the EU standards	Results Indicator #7: Signed Multi-Annual Infrastructure and Public Service Obligation contracts.	No (2021)	Yes (2024)
Prior action #8: The Recipient has facilitated access to and improved the quality, efficiency and transparency of public services for businesses and citizens, including the digitalization of services for business life-cycle, (registration, reorganization, trading, and closing of companies), as evidenced by Law on Public Services, Law No. 234, dated December 23, 2021, published in the Official Gazette on March 22, 2022, and Articles 14 and 18 of the Amendment approved by Law No.175, dated November 11, 2021, published in the Official Gazette on December 10, 2021.	(Indicative) Trigger #6: The Recipient has supported the digitalization of services to MSMEs, by introducing e-commerce, e-notary and Public Depository of Financial Statements.	Results Indicator #8: Share of new active G2B digital services envisaged by the reform.	Zero percent (2021)	75 percent (2024)

ANNEX 2: FUND RELATIONS INDEX

PRESS RELEASE

PR22/316

IMF Executive Board Concludes First Reviews Under the Extended Credit Facility and Extended Fund Facility Arrangements for the Republic of Moldova

FOR IMMEDIATE RELEASE

- The IMF Executive Board completed the first reviews under the ECF/EFF arrangements with Moldova, providing the country with access to SDR 20.65 million (about US$ 27 million).
- The impact of the war in Ukraine has yet to fully materialize, with the economy projected to stagnate in 2022 amid spillovers from the war, rising food and energy costs, and fragile confidence.
- Moldova's program is advancing governance reforms critical to increasing the country's resilience to shocks, while also providing additional resources to meet urgent socio-economic needs.

Washington, DC – September 21, 2022: The Executive Board of the International Monetary Fund (IMF) concluded the first reviews under the 40-month Extended Credit Facility (ECF) and Extended Fund Facility (EFF) Arrangements[1] for the Republic of Moldova.[2] This allows for the immediate disbursement of SDR 20.65 million (about US$ 27 million), usable for budget support, bringing Moldova's total disbursements under the blended ECF/EFF arrangements to SDR 185.95 million (about US$ 242 million).

Spillovers from the war in Ukraine continue to weigh on Moldova's outlook. The economy is expected to stagnate in the near term, with inflation remaining high amid rising food and energy prices. Despite signs of resilience, the current account and fiscal deficits are expected to widen significantly in the current year. Risks to the outlook remain exceptionally high, including those related to the regional energy crisis. Moldova's program implementation remains strong despite the difficult environment, with completion of important program commitments in the areas of fiscal and financial governance, as well as rule of law and anti-corruption.

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[1] Arrangements under the ECF provide financial assistance that is more flexible and better tailored to the diverse needs of low-income countries (LICs), including in times of crisis (e.g., protracted balance of payments problems). Those under the EFF provide assistance to countries experiencing serious payment imbalances because of structural impediments or slow growth and an inherently weak balance-of-payments position.

[2] The 40-month ECF/EFF arrangements were approved in December 2021 (Press Release) and augmented in May 2022 to increase total access under the arrangements to SDR 594.26 million (Press Release).

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Following the Executive Board discussion, Mr. Kenji Okamura, Deputy Managing Director and Acting Chair, made the following statement:

"Multiple challenges continue to weigh heavily on Moldova, including spillovers from Russia's war in Ukraine, the negative impact of soaring inflation on purchasing power, and energy security concerns. As a result, Moldova's economic outlook remains subject to exceptionally high domestic and external risks.

"Despite these challenges, the authorities remain firmly committed to the Fund-supported program, which aims to support the vulnerable, while advancing governance reforms and addressing developmental needs to create conditions for sustainable and inclusive growth. They have successfully completed structural commitments on fiscal governance, financial sector oversight, and on strengthening anti-corruption legislation, and even included additional conditionality to support the fiscal structural agenda.

"Maintaining this strong policy momentum will be critical to secure additional grant and concessional financing from donors needed to finance one-off spending pressures, retain adequate fiscal buffers, and reduce reliance on short-term domestic financing. Continued reform implementation and contingency planning will also help Moldova create a solid foundation for strong and inclusive growth.

"The authorities' near-term efforts remain appropriately focused on curbing soaring inflation, while protecting the most vulnerable from escalating energy and food costs. Maintaining an appropriate policy mix will be critical going forward, given persistent inflationary pressures, budget financing constraints, and exceptional downside risks around the baseline. Furthermore, concerted efforts are needed to improve spending efficiency, foster budget credibility, mobilize domestic revenue, and advance energy and SOE reforms.

"Safeguarding the independence of the National Bank of Moldova is essential to reinforce its credibility and strengthen policy effectiveness, particularly given the current highly uncertain environment. In this regard, prompt adoption of the legislation to reinforce the institutional autonomy of the National Bank of Moldova by end-October is critical. Strengthening financial supervision and regulation also remains important, especially given vulnerabilities to the non-bank sector. "