

# 7 OBSTACLES for BUSINESS

## INTRODUCTION

*Pe parcursul ultimilor ani Guvernul a întreprins și adoptat un număr de măsuri, care vin în suportul mediului de afaceri și în scopul îmbunătățirii clasamentelor internaționale a RM inclusiv pe segmentul antreprenorialui. Efectul acestor măsuri încă urmează a fi resimțit de antreprenori.*

In recent years the government of Moldova has taken action and adopted a number of measures, which come in support of business and to improve international rankings of the Republic of Moldova including entrepreneurship. Nevertheless the effects of these measures are yet to be felt by private sector.

The Republic of Moldova has a vast development potential which is currently not explored to its fullest. The Moldovan economy continues to register modest performances, in spite of a geographical location favourable for the development of foreign trade, its fertile lands and weather conditions beneficial for agricultural development, and its human capital facilitating the development of the service sector, especially information technologies.

Private enterprise is the main mechanism by which the economy's resources and pro-

duction factors can be engaged in order to improve the general population's standards of living. In a modern state, private companies are the main engine for jobs creation.

The business environment comprises the most progressive layer of society, thus its regulation framework has to allow for a full capitalization of this potential

Only a strong and competitive private sector can ensure the increase of the employment rate, of the income and consequently, of the quality of life within a country. In turn, this sector depends on the quality of the business and competitive environment in which companies develop their activities.

Therefore, promoting private entrepreneurship and creating a friendly regulatory and institutional framework for entrepreneurial activities should be a top priority on the government's agenda.



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# BACKGROUND

The document represents an agenda for improving business climate in the Republic of Moldova, based on extensive research conducted by CNPM in 2013 following the ILO methodology on "Enabling Environment for Sustainable Enterprise (hereafter referred to as "EESE").

## WHERE WE ARE

The data provided by the rankings of DOING BUSINESS are particularly helpful because they provide policy makers with the possibility to find out how the local regulatory environment for business compares with the ones of other countries.

The rankings on the ease of doing business, and their underlying indicators do not measure all aspects of the business environment that impact firms and investors or that influence the competitiveness of the economy. Nevertheless, they do represent a real source of information for investors.

Although Moldova has made some progress lately, with 83rd place currently it still ranks below the regional average.

## OVERVIEW OF THE ECONOMY

**Region:** Eastern Europe & Central Asia

**Income category:** Lower middle income

**Population:** 3,559,000

**GNI per capita (US\$):** 1,980

**DB2013 rank:** 83

**DB2012 rank:** 86\*

**Change in rank:** 3

**Source:** Doing Business 2013 database.

According to the State's Chamber of Registration data, on 01.01.2013, 159576 economic agents<sup>1</sup> were registered in the Republic of Moldova.

**TABLE 1. THE EVOLUTION OF THE NUMBER OF ACTIVE ENTERPRISES**

	2005	2006	2007	2008	2009	2010	2011	2012
<b>Number of active enterprises</b>	33141	36158	39987	42121	44633	46704	48541	50700
<b>Growth rate of active enterprises, %</b>		9.1	10.6	5.3	6	4.6	3.9	4.4

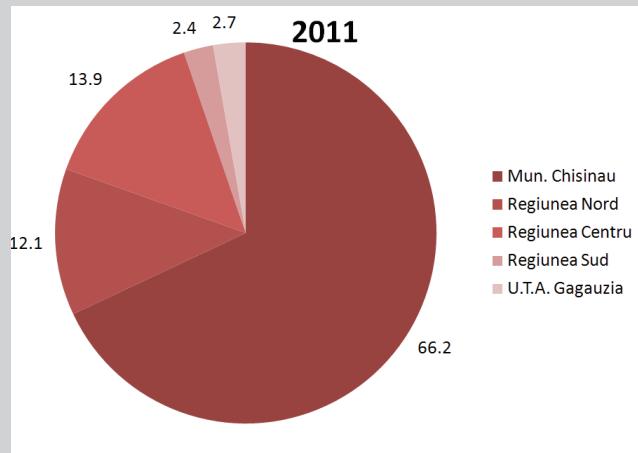
Source: BNS, CIS

<sup>1</sup> This number includes enterprises with the following types of legal organization: limited liability companies, individual enterprises, joint stock companies, cooperatives (production cooperatives, consumer cooperatives and business cooperatives), state and municipal enterprises, subsidiaries, representative offices, joint partnerships, limited partnerships, companies lease, inter-household enterprises, collectives, associations of farmers and other enterprises

The large gap between registered (159576) and active (50700) companies lead us to conclusion that in addition to barriers in deregistering of enterprises, there are a number of inactive companies that are “waiting” for favourable conditions to resume their economic activity.

The geographical distribution of active enterprises is also highly concentrated – over two thirds of these enterprises are located in Chisinau. This situation remains relatively constant over time and points to some serious gaps in the regional development of the country.

CHART 1. GEOGRAPHICAL DISTRIBUTION OF ACTIVE ENTERPRISES



Source: NBS

# 7 OBSTACLES for BUSINESS.

*As a result of a research based on ILO EESE methodology among key business representatives and after a thorough analysis of its regulatory and institutional framework, the seven main obstacles for improvement of business environment have been identified.*

- 1** *Unstable political climate and deficient relations with the state institutions. Stable political climate, good governance, absence of corruption and efficient institutions foster entrepreneurship and promote private sector growth and development*
- 2** *Ineffective social dialogue. An effective, genuine and regular social dialogue is fundamental for the achievement of mutually beneficial outcomes for the stakeholders and society at large*
- 3** *Burdening regulatory framework. Ensuring a transparent, predictable and non-inhibiting regulatory environment is the key for economic growth.*
- 4** *Deficient competition In order for the private sector and sustainable enterprises to develop and grow, it is important to have fair competition rules and eliminate monopolies.*
- 5** *Poor quality infrastructure. Our current quality of infrastructure is poor and hence rightfully considered as the "Achilles' heel" of the Moldovan economy.*
- 6** *Low-skilled labour force. The development of a skilled workforce and the expansion of human capabilities through high-quality systems of education, training and lifelong learning is important in helping workers to find good jobs and enterprises to find the skilled workers they require.*
- 7** *Inflexible labour legislation. Labour code should reflect economic realities of the country and provide more flexibility to employers and more employability to workers*

These most important problems and constraints that hinder the development of business in the Republic of Moldova can be removed or mitigated through a complex and correlated efforts by the government. Consultation with social partners and especially with the National Confederation of Employers of the Republic of Moldova is essential in assisting the government to find a right mix of appropriate policy responses and gradually improve business environment. The return of such "investment" would be significant and reflected through a stronger private sector, higher employment, reduced informal economy, significantly higher tax revenue and overall improved lifestyle of Moldovan people.

1



## UNSTABLE POLITICAL CLIMATE AND DEFICIENT RELATIONS WITH STATE INSTITUTIONS

***Unstable political climate and deficient relations with state institutions.*** Good governance, absence of corruption and efficient institutions foster entrepreneurship and promote private sector growth and development. Similarly, peace and political stability are key conditions for the creation and development of sustainable enterprises.

Since 2009, the Government of Moldova has launched significant reforms in the areas of democratization, freedom of the media, economy, policy, and education. Nonetheless, two of the most problematic factors still hindering growth in the country are corruption and judicial reform.

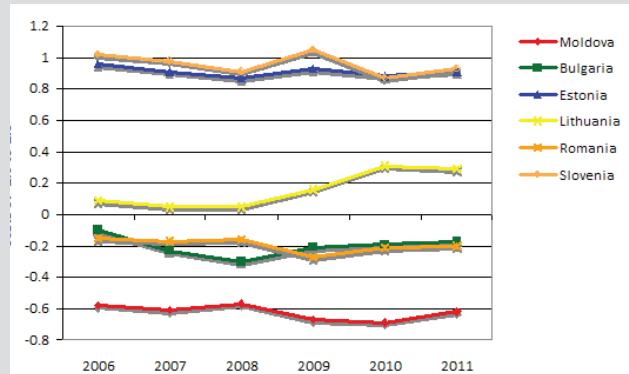
According to the Global Competitiveness Report 2012-2013, corruption is the greatest challenge for doing business in Moldova whilst political instability represents the second major problematic factor for doing business. Public power still appears to be exercised for private gains and there is significant room for improvement in this area.

Control of corruption scale goes from -2.5 to +2.5 where higher value reflects better performance (Chart 2).

## EESE SURVEY, KEY FINDINGS:

- 8 out of 10 entrepreneurs believe that periods of political instability negatively affect economic activity;
- About 2 out of 3 entrepreneurs consider corruption as a major obstacle to business development in the Republic of Moldova;
- Every third entrepreneur is forced to resort to bribery to solve problems;
- 2/3 of entrepreneurs believe that political ties are needed to benefit from governmental support;
- Two fifths of employers state that the government's involvement in fighting corruption is unsatisfactory

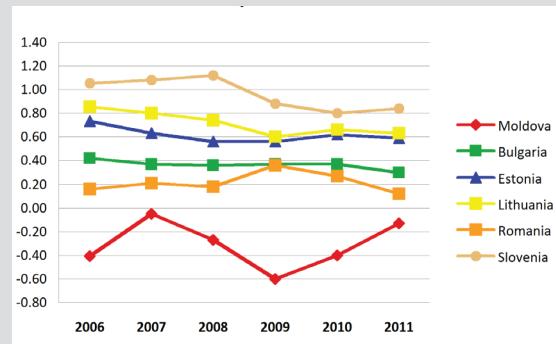
*Source: EESE Moldova*

**CHART 2. CONTROL OF CORRUPTION**

Source for Chart below: World Bank, Governance Matters database

**CHART 3. POLITICAL STABILITY AND ABSENCE OF VIOLENCE**

In terms of political stability, the Republic of Moldova registers one of the lowest indicators compared to other countries in the region (chart 3). Political instability in Moldova is a key concern for economic development and poverty alleviation, as it has been identified as a major hindrance in both regards. However despite the somewhat negative findings the country has made improvements in political stability in recent years and it has been recently praised by the EU Institute for Security Studies as potentially the best example of successful transformation under the EU Eastern Partnership.



Source: World Bank, „Governance Matters“ database



# KEY POLICY PRIORITIES

## ENSURING EFFECTIVE FUNCTIONING OF STATE INSTITUTIONS

- **DEVELOP** and implement a system of personal and institutional responsibility for civil servants activities in relation to business;
- **INTRODUCE** a monitoring system that would evaluate performance of the state institution by social partners and civil society through jointly developed and agreed performance indicators
- **ENSURE** the independence and strengthen staff competences of Regulatory Agencies (ANRE, ANPC, ANCERTI etc.).
- **CONSOLIDATE** the number of authorities responsible for inspection and control.

## ERADICATION OF CORRUPTION IN STATE INSTITUTIONS

- **IMPROVE** corporate governance at the level of public institutions;
- **IMPLEMENT** information technology in the work of state institutions, in particular, in areas related to the issuing permits and licenses for entrepreneurs (e.g. building permits, various business licenses, etc.).
- **STRICT ENFORCEMENT** of the law no. 235 of 20.07.2006 on the basic principles of regulation of entrepreneurial activity;
- **REDUCE** the margin of discretion of public officials in the process of issuing permits and licenses for the entrepreneurial activity;
- **OPTIMIZE** the number of employees working in public institutions and reinvest saved resources towards the training and remuneration of a competent and efficient officials



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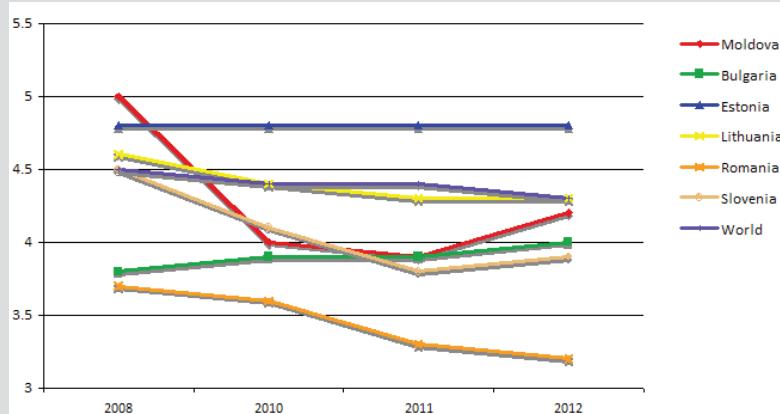
## INEFFECTIVE SOCIAL DIALOGUE

**Ineffective social dialogue.** Social dialogue is effective when founded on the recognition that the social partners constitute an important building block in ensuring social stability. It is also effective when based on the recognition that employers and employees, as the principal providers of goods and services and wealth creators, represent two important interest groups in a market economy

Officially, the National Commission for Consultation and Collective Bargaining exists in Moldova, which is a tripartite Council that convenes on a quarterly basis or when deemed necessary. The Council's main function is to provide solutions for labour and social-economic problems in order to develop social partnership at national, branch and regional levels. However, the Council's current relevance and visibility in our society and efficiency of the Commission is somewhat disappointing.

According to the Global Competitiveness Report for 2012-2013, the Republic of Moldova is ranked in 79th place out of 144 countries according to the cooperation between employers and employees (chart 4). In the chart below higher values indicate better cooperation

CHART 4. RESULTS OF THE SURVEY ON THE COOPERATION BETWEEN EMPLOYERS AND EMPLOYEES



Source: World Economic Forum, Survey of enterprise leaders

## EESE SURVEY, KEY FINDINGS:

- 4 out of 5 companies believe the social dialogue carried out through the tripartite commissions is ineffective;
- Most business people (about 70%) perceive government as insufficiently cooperative with its partners from the business side when it comes to social dialogue

## KEY POLICY PRIORITIES

### PROMOTE TRIPARTITE DIALOGUE AND CONSOLIDATE THE TRUST OF THE PRIVATE SECTOR IN THIS INSTITUTION

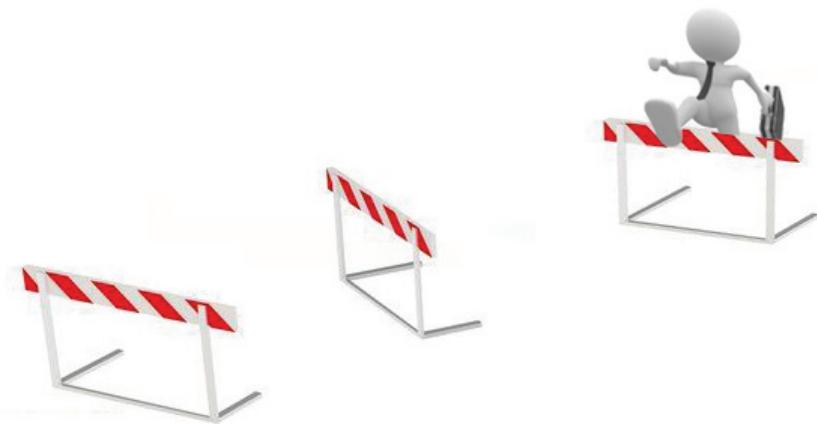
- **INCREASE** the relevance and effectiveness of the National Commission for Consultation and Collective Bargaining;
- **ENSURE TRANSPARENCY** by publicising the outcomes of consultation process to all relevant stakeholders;
- **CREATE** a framework for bipartite negotiations at the branch and territory levels;
- **DISENGAGE** and remove public officials from a bipartite -private sector negotiations

### MORE ACTIVE PARTICIPATION OF THE BUSINESS ASSOCIATIONS IN THE DECISION PROCESS

- **ALL** promises made and decisions taken during negotiations and consultation processes with business should be implemented;
- **ESTABLISH** an appropriate framework for strengthening and stimulating genuine consultation with business associations;



# 3



## BURDENING REGULATORY FRAMEWORK

**Burdening regulatory framework.** Well-designed and easy to follow regulations, including those that uphold labour and environmental standards, are necessary for promoting start-ups and for developing enterprises. They facilitate formalization and boost systemic competitiveness. The lack of transparency and the cumbersome bureaucracy in Moldova often hinder the registration and operation of private enterprise. It should be noted however that Moldova made some improvements in recent years when it comes to legal and regulatory framework. Nevertheless, according to the Global Competitiveness Report for 2012-2013, the inefficient bureaucratic system is the third most important factor in doing business in the Republic of Moldova and the country has been rated at 105th place out of 144 countries when it comes to burden of state regulations. Construction permits in particular are difficult to get and the World Bank rated Moldova on 168th place out of 185 countries when it comes to ease of issuing construction permits.

## EESE SURVEY, KEY FINDINGS:

- Two-thirds of companies' representatives consider the regulatory framework for companies as unfavorable.
- More than 62% of managers and owners of companies believe that the time spent to comply with government regulations is a major challenge for businesses.
- For a third of employers licensing processes represent a problem.
- Moldovan customs and trade regulations create significant problems in the development of international trade for about two thirds of the companies that engage in this kind of trade.
- Tax Administration, including the method of calculation and accounting, paying taxes, reporting and so on, is an important constraint for the development of the company for more than half of the enterprises.
- The tax burden is considered to be a strong or very strong constraint by 7 out of 10 business representatives.
- The share of social security and public health is a serious constraint to enterprise development in view of 52% of enterprises. For businesses outside Chisinau, this issue is even more pronounced

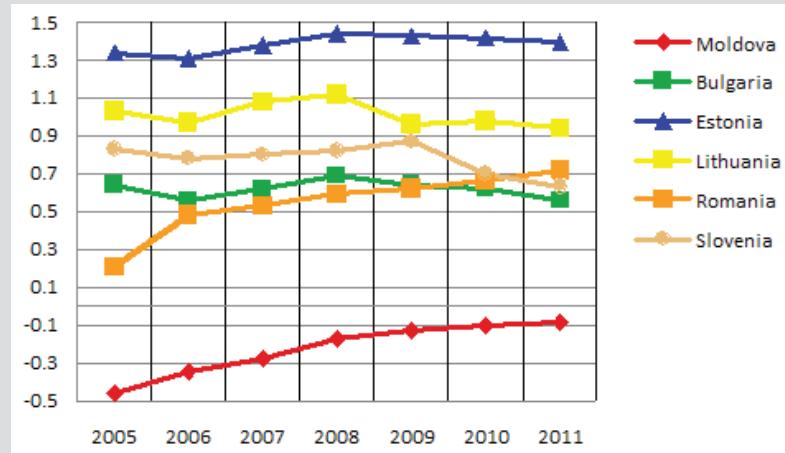
**Source: EESE Moldova**

Companies from Moldova need more time and considerable effort in order to comply with the general legal requirements, and this problem is even more severe for enterprises from the regions.

The “Regulatory Quality Index” measures the ability of a government to provide sound policies and regulations for the promotion of the private sector on a scale from -2.5 to 2.5, with higher values indicating better performance. Moldova’s performance in this regard has been poor and below 0, though the country has experienced some improvement in recent years (Chart 5).



CHART 5. THE QUALITY OF THE REGULATORY FRAMEWORK



Source: World Bank, „Governance Matters“ database

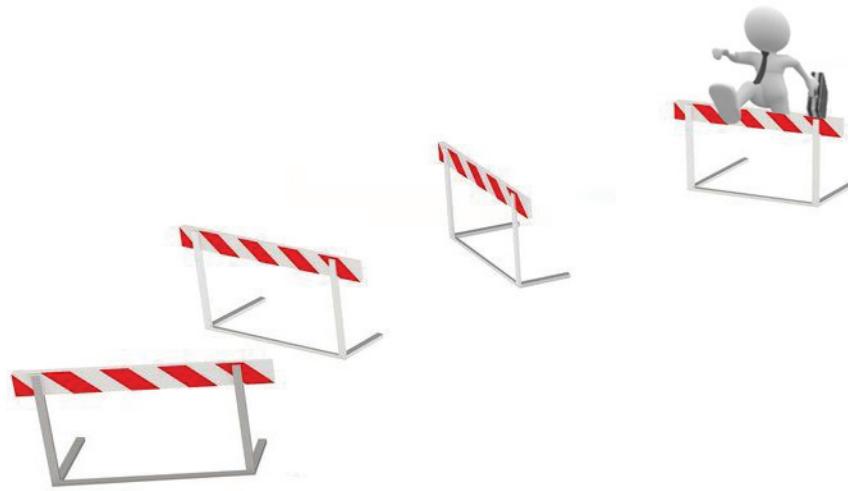
# KEY POLICY PRIORITIES



## **ENSURE A TRANSPARENT, PREDICTABLE AND EQUITABLE REGULATORY FRAMEWORK**

- **APPLY** the regulations for entrepreneurial activity in areas where they are strictly necessary;
- **SIMPLIFY** the regulatory framework;
- **SIMPLIFY** procedures for issuing business permits and licenses
- **REDUCE** the number and duration for obtaining business permits and licenses
- **SIMPLIFY** tax and customs administration;
- **ONGOING COMMUNICATION** with business on the public policy development and its implementation process;
- **CONTINUE** with regulatory reforms;
- **APPROVE** the regulation of entrepreneurial activity only through governmental decisions;
- **TRANSPARENT AND PREDICTABLE** fiscal rules;
- **EFFICIENT AND TRANSPARENT** judicial system.

# 4



## DEFICIENT COMPETITION

**Deficient competition.** In order for the private sector and sustainable enterprises to develop and grow, it is important to have and protect fair competition, including the rules ensuring respect for labour and social standards. Therefore, anti-competitive practices at national level must be eliminated.

Problems regarding the competitive environment were frequently mentioned in various analytic publications as well as policy documents, drafted both by the Government and several non-profit organizations. Thus, it was established that high levels of monopoly exist in important economic sectors, such as banking, oil products market, the market of agricultural intermediaries, the meat producing market etc.

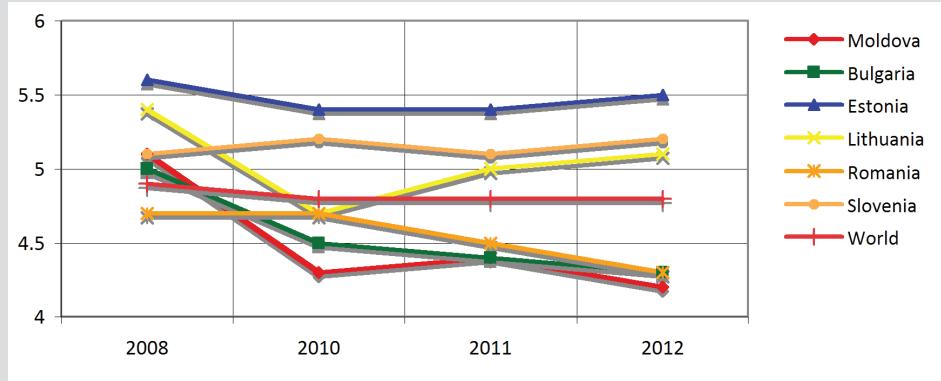
## EESE SURVEY, KEY FINDINGS:

- Every third company believes that there are anti-competitive practices in their sector
- 2 out of 5 employers consider antitrust law as being ineffective
- More than half of the companies see/consider the legal framework for small businesses as unfavorable.

Moldova is placed on the 130th place out of 144 countries, regarding the efficiency of antitrust policies, according to the Global Competitiveness Report for 2012-2013.

In spite of impressive legislation and protections on paper, ensuring fair competition in Moldova, it is hindered by weak enforcement and implementation of norms and legal mechanisms.

**CHART 6. EFFECTIVENESS OF ANTI-MONOPOLY POLICIES**



Source: World Economic Forum Executive Opinion Survey, the Global Competitiveness Report.

The situation in Moldova, when it comes to anti-monopoly practices, is clearly reflected when compared with other relevant countries. The "Effectiveness of Anti-Monopoly Policies Index" indicates the level of efficiency of anti-monopoly policies in promoting competition on a scale from 1 to 7 with higher values corresponding to better performance. Moldova performs the weakest relative to other countries used for comparison over the period 2010-12 (Chart 6).

# KEY POLICY PRIORITIES



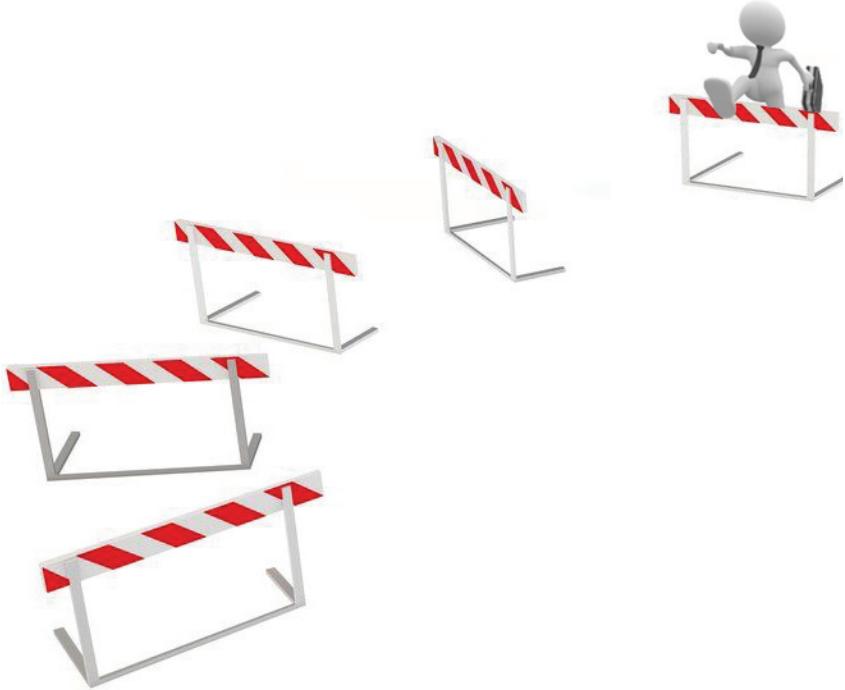
## ENCOURAGE COMPETITION IN ALL SECTORS OF THE ECONOMY

- **DISMANTLE** entry barriers to different markets, especially emerging markets
- **ELIMINATE** cases of favoritism through transparent procedures in granting state aid
- **ENSURE** efficient public procurement procedures;
- **REMOVE** barriers to the participation in processes of public procurement
- **INCREASE** the transparency of the public procurement process
- **ELIMINATE** state monopolies in sectors where competition from private companies is possible;
- **ACCELERATE** the privatization process based on principles of market economy.
- **PROVIDE** the Competition Council with real independence from the political and economic elites of the country.
- **REDUCE** the number of goods and services, the prices of which are established by the state.

## DECREASE THE INFORMAL ECONOMY

- **PRIORITISE** actions related to elimination of informal economy;
- **INCREASE CAPACITY** of controlling authorities in detecting informal activities.

# 5



## POOR QUALITY INFRASTRUCTURE

**Poor quality infrastructure.** Access to physical infrastructure is one of the most important factors that determine the emergence and development of an enterprise. Lack of access to the key elements of physical infrastructure, or their inappropriate quality makes it impossible to physically perform ones activity or may generate costs that will determine a significant decrease in competitiveness.

The development of sustainable enterprises critically depends on the quality and quantity of the physical infrastructure available, such as physical facilities and transportation systems. Access to water and energy also play a pivotal role.

The quality of infrastructure is rightfully considered the "Achilles' heel" of Moldova's economy. According to the Global Competitiveness Report for 2012-2013, the Republic of Moldova is ranked at the last place (144th place out of 144 countries) in terms of the quality of road infrastructure. The infrastructure of the air transportation is just as problematic, Moldova being placed on 133-th position out of 144 states. These aspects essentially undermine the external competitiveness of local producers, and thus, their access to foreign markets. For example, according to the Doing Business Report 2013, export procedures take 33 days on average (while the average of countries from Eastern Europe and Central Asia is 26 days).



## EESE SURVEY, KEY FINDINGS:

- 9 out of 10 employers outside Chisinau report having incurred high costs due to inadequate infrastructure.
- Only 7% of business leaders consider that the impact of investment in infrastructure was a substantial one.
- The businesses most affected because of inadequacies in infrastructure are farms.

**Source: EESE Moldova**

*It should be noted however, that in the last few years the Moldovan government made some improvements in the infrastructure as reflected in the "Quality of Overall Infrastructure Index" where Moldova consistently rose in the index ranging from 1 to 7 with higher values indicating better performance (Table 2).*

**TABLE 2. THE EVOLUTION OF THE INFRASTRUCTURE QUALITY INDEX**

Infrastructure quality index	2008 (GC 08/09)	2009 (GC 09/10)	2010 (GC 10/11)	2011 (GC 11/12)	2012 (GC 12/13)
<b>Moldova</b>	2.2	-	3.1	3.2	3.3
<b>Bulgaria</b>	2.5	2.8	3.1	3.1	3.3
<b>Estonia</b>	4.7	5.1	5.5	5.5	5.4
<b>Lithuania</b>	4.5	4.9	5.1	5.1	5.1
<b>Romania</b>	2.3	2.4	2.4	2.3	2.8
<b>Slovenia</b>	4.8	5.2	5.3	5.3	5.4
<b>World</b>	3.8	4.1	4.3	4.3	4.3

**1=underdeveloped, 7= as developed and as efficient as the country with the best infrastructure.**

*Source: World Economic Forum, Survey of enterprise leaders*

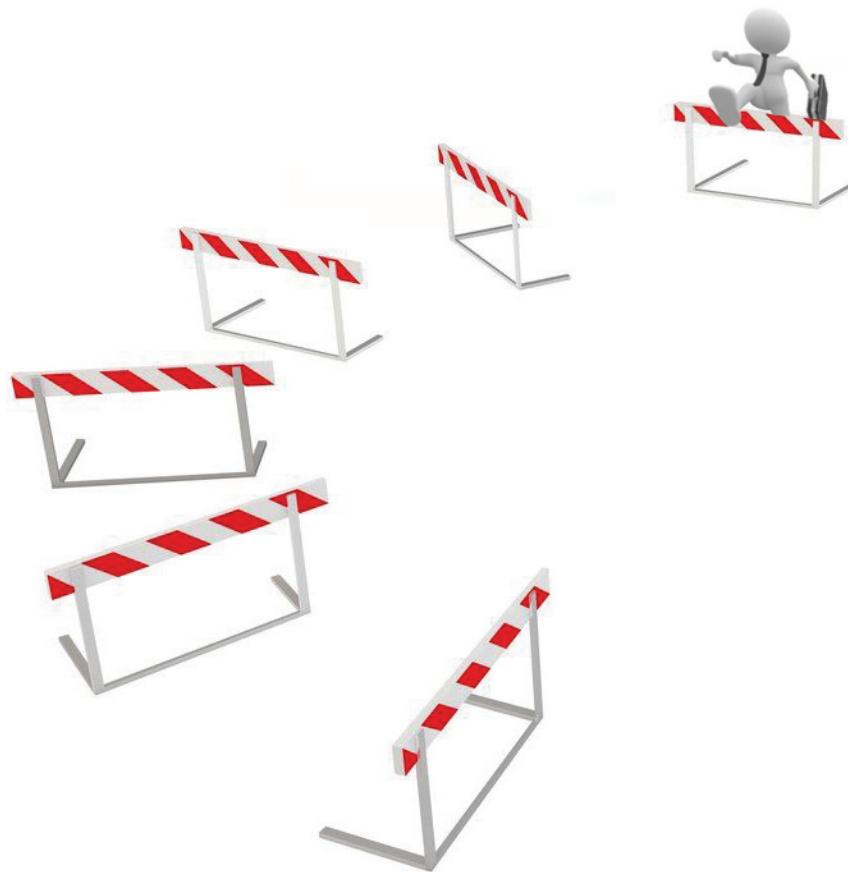
# KEY POLICY PRIORITIES



## MODERNIZE THE INFRASTRUCTURE

- **EFFICIENT** and transparent use of road funding;
- **IMPROVE** access of private companies to tenders concerning the reconstruction of road infrastructure;
- **ENHANCE** quality checking mechanisms of the performed work;
- **REMOVE** state companies' anticompetitive practices related to modernizing infrastructure;
- **DEVELOP** public-private partnerships in modernizing the infrastructure;
- **RENOVATE** the railways system;
- **ABANDON** the practice of cross-subsidization;
- **INCREASE** substantially the budgetary allocations for the improvement and construction of local infrastructure, particularly in terms of access to water supply, electricity, gas, and access to roads.

# 6



LOW-SKILLED LABOUR FORCE

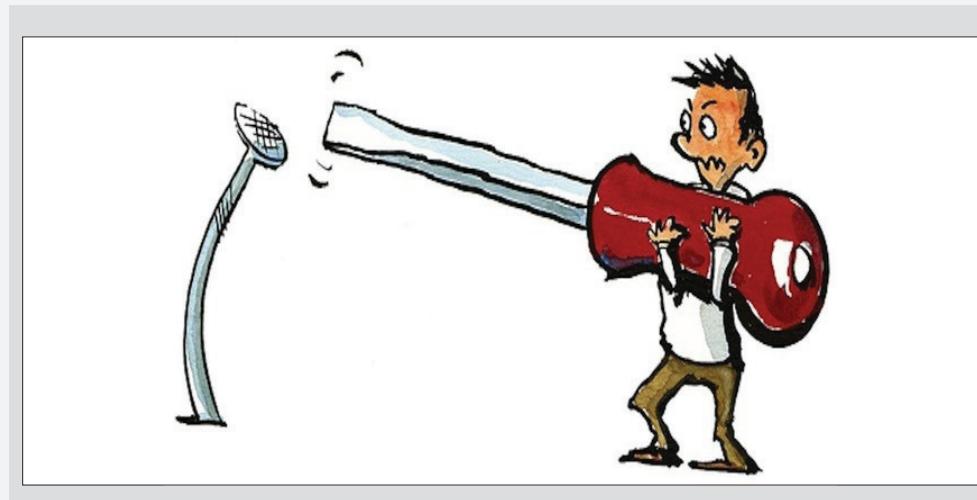
**Low-skilled labour force.** The development of a skilled workforce and the enhancement of human competencies through a high-quality system of education, training and lifelong learning are paramount in helping workers find good jobs, and companies in finding the skilled workers that they require.

A low-skilled labour force constitutes a serious challenge for the business environment in particular, as well as the economy in general.

Although Moldova allocates more funding to education than other countries, its level of education is consistently falling behind in comparison with those of other states. The educational system in Moldova is one of the main sectors where corruption is perceived as widespread.

In our state, there is a substantial gap in the financing received at different levels of education; while general compulsory education has allocated almost 50% of the funds which are inefficiently used, less than 10% goes to secondary vocational education. This level of funding is insufficient for modernizing the system and for training the specialists demanded on the labour market.

This factor also impacts the state in its capacity as employer, through the low-skilled public officials it provides it with, which in turn leads to the overall low efficiency of state institutions, and as a result, the process of elaborating and implementing policies is seriously defected.



## **EESE SURVEY, KEY FINDINGS:**

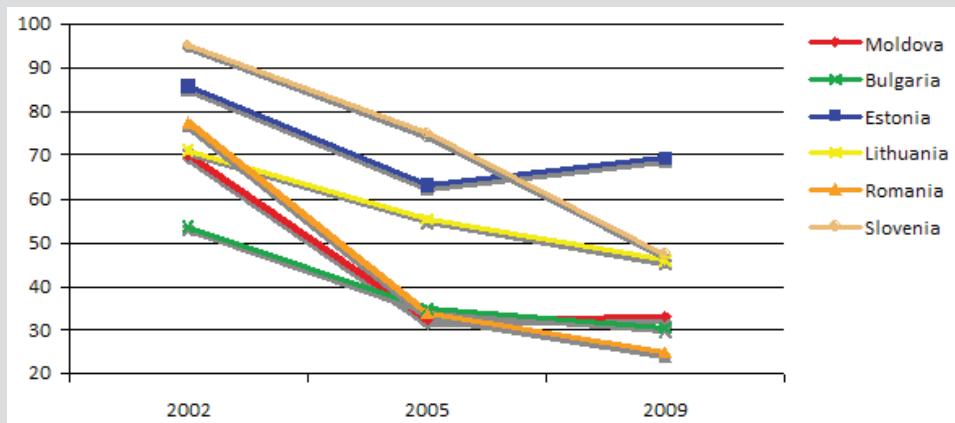
- Half of the companies have, more frequently or permanently, difficulty in finding people with adequate qualifications on the labour market;
- In addition to knowledge, professional skills and work skills, employers also take into consideration the general qualities and personality traits of a candidate;
- Companies that have more than 50 employees are most affected by the workforce quality;
- Employers believe that the quality of the labor force impacts on the development of their enterprise;
- Agriculture, transport and construction industry appear to be most affected by the shortage of skilled labour;
- Enterprises with more than 50 employees train their employees frequently;
- 40% of companies believe market prices for training services to be inaccessible;
- 6 out of 10 of companies, do not know about the government's education and training programs in different fields;
- Nearly 60% of businesses do not have a budget for training;
- Education in Moldova is poorly adjusted to the needs of the real economy;
- The majority (70%) of businessmen feel that the vocational education system does not meet the needs of the private sector in Moldova.

**Source: EESE Moldova**

Consequently, low-skilled labour force is in the top 5 most problematic factors for doing business and in terms of quality of the educational system, Moldova is only at the 103rd place out of 144 countries according to the Global Competitiveness 2012-2013.

The "Extent of Staff Training" indicates whether companies in a country invest little or heavily in training and employee development to attract, train and retain staff, on a scale from 1 to 7 with higher values indicating more investments. Moldova reflects stable, but relatively poor performance in this regard over the period 2008-12 (Chart 7)

CHART 7. PERCENTAGE OF FIRMS OFFERING FORMAL TRAINING TO EMPLOYEES



Source: World Bank

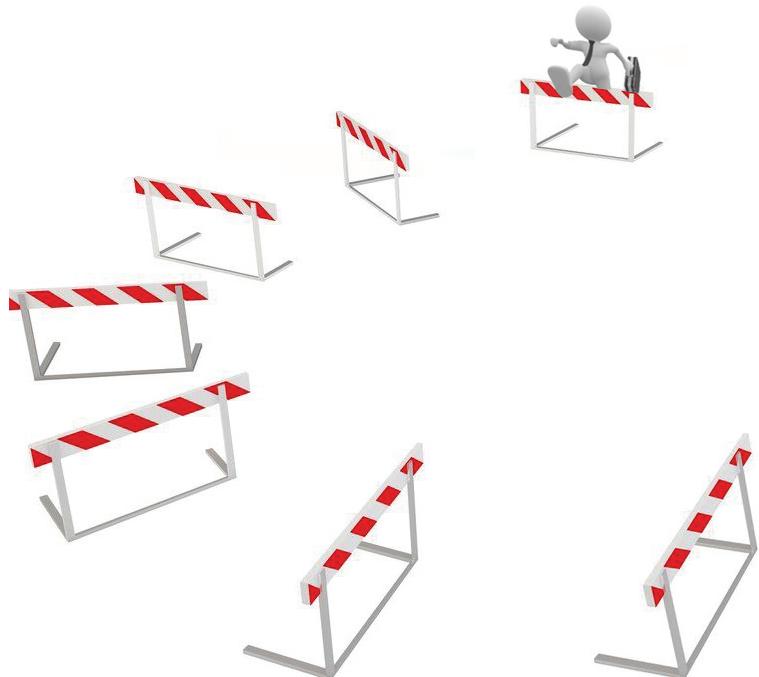
## KEY POLICY PRIORITIES

### DEVELOP THE EDUCATION SYSTEM AND VOCATIONAL TRAINING

- **CORRELATE** the national system of education and vocational training with the needs and realities of business;
- **SPEED UP** the occupational standards development process;
- **STIMULATE** the creation of partnerships between businesses and educational institutions;
- **INVOLVE** private companies in the process of evaluation and testing of the students in vocational schools and colleges with relevant profile;
- **INCREASE** the practical component of studies in the professional and vocational training;
- **CREATE** a system of certification of skills acquired in non-formal educational process.



# 7



## LEGISLAȚIA MUNCII NEFLEXIBILĂ

**Inflexible labour legislation.** The global competition in the manufacturing and service sectors creates greater pressure on business and directs enterprises towards new aspirations. Contextual changes raise many challenges for businesses. Often this pressure forces these companies to adopt strategies for becoming more flexible and more dynamic, in order to respond to the market's changing conditions as quickly as possible.

Flexibility is a business imperative and now a matter of urgency but in the Republic of Moldova, the achievement of this necessary level of flexibility is hindered by the rigidity of the legal framework governing labor relations, with an emphasis on bureaucratic nature of these relationships and the excessive protection of employees.

## EESE SURVEY, KEY FINDINGS:

- Business representatives consider the Labor Code's provisions, particularly those related to employment, payment and dismissal, as unadjusted to the needs of a market economy;

*Source: EESE Moldova*



# POLITICI CHEIE

## ADJUST THE LABOUR MARKET TO THE NEEDS OF THE MARKET ECONOMY

- **ENSURE FAIR BALANCE** in the labour code between the interests of employers and employees, without favoring any of the parties;
- **ACCEPT THE FUNDAMENTAL PRINCIPLE** that the companies are autonomous in its decision making and therefore free to replace unproductive workers with more efficient ones, at any time.
- **REMOVE** from the labor relations legislation the specific provisions inherited from a centrally planned economy;
- **PROVIDE** a legal framework that would reduce or in some cases remove over-protection of employees;
- **CHANGE** the provisions of the Labour Code to allow companies to restructure when necessary in order to stay competitive and in business
- **PROHIBIT** state interference in the internal decision-making process of enterprises.



