EXECUTIVE SUMMARY

Introduction

This report aims to highlight the most important developments and features of the social protection and healthcare systems in Moldova, particularly analysing the impact of public policies on vulnerable and marginalised groups of the population. It briefly describes the development of macroeconomic, fiscal, demographic, labour market and education sectors and provides a thorough analysis of the social protection and social welfare system, poverty, and pension and healthcare systems. The analysis is built on the EU Open Method of Coordination and represents a basis for a comprehensive strategy designed to achieve sustainable economic growth, labour market inclusion and social cohesion. This report represents the first attempt to address the degree of harmonisation of the policies and statistical data between Moldova and the EU as well as countries in the region.

After being a part of the Soviet Union for a half century—benefiting from significant subsidies and the development of both the industrial and agricultural sectors that ensured an adequate income for the entire population—Moldova found itself at a crossroads when dissolution of the Soviet Union occurred. Moldova's transition to a market economy has been slow and extremely challenging, accompanied by a series of failures including: land reform, privatisation of state owned enterprises, and total collapse of the industrial sector. Its complete lack of energy resources together with the territorial dismantling of the country with the self proclamation of Transnistria (which once generated a third of Moldova's industrial output and almost entire energy production) has hit hard. Lack of sound economic and social reforms, coupled with political instability in the first phase of transition, has led to economic recession and increased poverty, thus qualifying Moldova as the poorest country in Europe.

Despite these setbacks, since 2000, Moldova's economy has been recovering, mainly due to migrant remittances, which currently represent about a third of GDP. Thus, over 2000–2008 the Moldovan economy recorded a cumulative growth of 62.9%, although this still represents only 56.6% of 1990 output. Remittances increased population incomes, raising aggregate demand and consumption. Consumption is satisfied largely by imported goods, with their more competitive prices and quality, dramatically increasing the trade and current account deficits. While over 2000-2008 salaries and pensions increased by more than 10% in real terms, they did not play a significant role in increasing population living standards. The current average net salary of €165 is well below the EU average salary.

Remittance-based economic growth was accompanied by poverty reduction, but the related population exodus created disruption within the domestic labour market. The population declined by more than a fifth during transition and emigration of almost a quarter of the active population has threatened the labour market, leading to a decrease in the economically active population and the population employed within the economy (also by almost one-fifth), whereas the inactive population has dramatically increased. At the same time, the unemployment rate is gradually decreasing, mainly due to emigration and, to some extent, as a result of legalisation incentives launched by the Government in 2007.

The informal economy, widespread in the first decade of transition, began to retract in the second phase. According to the National Bureau of Statistics (NBS), in 2008, the informal economy's contribution to GDP was 20.8%, compared to 34.6% in 2000. In the last eight years, the share of household production for own consumption, which constitutes a

component of the hidden economy, dropped from 18.5% to 6.7% as a share of GDP—the biggest drop caused by threefold shrinkage of production in subsistence farming.

Inefficient structural reforms during transition have not only damaged the economy but have also led to a shift in the labour force between sectors. The number of employed within the agricultural sector decreased considerably—from 50.6% of total employed in 2000 to 29.8% in 2008. Structural adjustments, migration, and shift of workers between sectors led to a doubling of revenues in non-agricultural activities in the last three years, amid a decrease in the incomes generated by agricultural activities—in total of about one-fifth. While some workers became engaged in other sectors of the economy, particularly in construction, most of them emigrated. Unlike the agricultural sector, the industrial sector, which was also unable to revive during transition, has nevertheless absorbed the labour force released from the agricultural sector (particularly in the construction sub-sector).

Moldova's transition to a market economy caused a number of disruptions to the educational system, affecting both the quality of the educational process and the accessibility of educational services. Though spending on education has been steadily growing, reaching 8.7% of GDP in 2008 compared to 5.7% in 2000 inter and intra-sector distribution of expenditures is inadequate. There is a huge gap in financing between the different levels of education—general compulsory education benefiting from almost one-half of the funds, and these are inefficiently used. Less than one-tenth of financing goes to secondary vocational education. This level of resourcing is insufficient for modernization of the system and training of specialists for the labour market. The lifelong learning concept in general, together with distance learning in particular, are poorly developed in Moldova. These problems in the education system, coupled with economic and social challenges among the population, have stunted education indicators. Over the last few years, gross enrolment rates in primary and lower secondary education have decreased. In contrast, the enrolment rate in preschool education is increasing, although there is a shortage of child care facilities, particularly in urban areas.

Moldova has been affected by demographic aging, generated mainly by a decrease in birth rates. This has resulted in an absolute and relative decrease among the young population and an increase in the share of elderly. The birth rate is falling alongside a decreasing mortality rate and life expectancy is increasing. The demographic projections are not positive. According to UN forecasts, the population of Moldova could drop by some 20% by 2050. The demographic crisis will have an adverse impact in the medium to long term, particularly on the labour market and pension system.

Transition to a market economy has caused significant disparities between the capital city and the rest of the country, between urban and rural areas and, more recently, between development regions. The biggest socio-economic gap is between Chisinau municipality and other administrative-territorial units. The capital is the key point of not only consumption and revenues, but also public spending and well-being. Unlike Chisinau, which suffered less from the industrial collapse, other towns that depended on one or more industrial enterprises were affected considerably more. Since 2006, the country has been split into six development regions, three of which in particular (North, Centre and South) will be considered by authorities in the medium term in order to reduce the gap both among these three regions and between these regions and Chisinau. Among the North, Central and South regions, the most developed is the North, while the least developed is the South, with the smallest industrial

output per capita, the lowest level of investment in fixed capital, and the smallest number of reporting enterprises.

Despite gradual recovery in the second phase of transition, the current world financial and economic crisis has set back Moldova's economy and eroded population living standards. At the beginning of 2009, the evolution of the Moldovan economy slowed, foreshadowing the impending problems that Moldova is likely to face in the short to medium terms. In the first quarter of 2009, exports, imports, industrial output and the transport sector all contracted, while the number of unemployed and wage arrears have increased dramatically. At the same time, budget revenues and National Bank of Moldova (NBM) official reserves continually dropped, while budget expenditures increased. A reduction in budget revenues due to aggregate demand contraction, coupled with a reduction in migrant remittances by one-third, will put not only vulnerable population groups at further risk but also active businesses. The economy will most probably not be able to absorb the domestic workforce, or emigrants returning to Moldova.

The political crisis in the country, which emerged after Parliament elections held in April 2009 and associated budget expenditures, represents a threat to the sharply declining economy, obstructing the proper implementation of anti-crisis policies to support the private sector and vulnerable groups. Response to the economic crisis was late and incomplete, mainly due to the political situation. Without a fully functioning Parliament, the most effective proposed fiscal measures cannot be adopted. Notwithstanding these measures, in 2009, the Moldovan economy is predicted to contract at least 5% and the unemployment rate to reach 10% with little prospect of recovery in the medium term.

ACCESS TO SOCIAL PROTECTION

With regard to the social protection system, there have been several transformations since 1998. The present system of social protection in Moldova is divided into state social insurance and social assistance—the latter non-existent prior to independence. Despite numerous institutional reforms, the current social protection system is centralized from both a political and administrative point of view, while the analytical and strategic planning capacities, including the capacity to assimilate external assistance, need to be strengthened. Implementation of administrative decentralization without fiscal decentralization undermines the capacity of local public authorities (LPAs) to support the sustainability of community-based social services. Lack of financial resources within territorial-administrative unit budgets does not allow LPAs to meet the demand for social services, resulting in heavily institutionalised and costly care.

The cost of social protection is on an upward trend, and in 2008 had reached 30% of the total expenditures of the national public budget and represented 12% of GDP. Donor assistance to the social protection sector was considerable, particularly in the second decade of transition. A total of €83 million in external assistance was directed into the social protection sector over an 8–9-year period. European Commission assistance in the field of social protection is significant, amounting to €27 million over 2008–2010, followed by technical assistance provided by the International Organisation for Migration (IOM), United Nations Children's Fund (UNICEF), Swedish International Development Cooperation Agency (SIDA) and other country development partners. The effectiveness of donor support varies, depending on the political will to implement a number of sensitive policies and quality of advice provided. It is

also dependent on donor coordination which initially was somewhat weak but which has significantly improved after strengthening of the partnership among donors.

Unlike the national public budget, the state social insurance budget (SSIB) performed as well in 2008 as in 2004, resulting in a budget surplus. Despite this performance, as a result of the contraction of national public budget revenues, the return of some 40 thousand emigrants, and increase in unemployment and the number of vulnerable people, the deficit of the state social insurance budget could further increase to unprecedented levels. The economic crisis, the effects of which are already visible, coupled with demographic and labour market disturbances, will undermine the sustainability of the SSIB. The impact of this would be reflected in slower increases in the size of social benefits as well as the occurrence of arrears.

Of note in relation to the role played by social protection benefits among the vulnerable population, is that they represent an important source of income for households after salary revenues. However, the impact of social assistance benefits on poverty reduction is highly insignificant, representing a difference of 1% compared to 11.9% for social insurance benefits. Moreover, those from households whose main source of income is from social benefits register a high poverty risk (33.6%). The marginal impact of social assistance benefits on living standards can be explained in part by the categorical approach to access. The fact that households obtaining social benefits are considered among the poorest, however, indicates that the problem does not reside only in targeting but also in the small size of benefits.

The most important and costly social insurance benefits are pensions, unemployment benefits, maternity benefits and child care allowances. The size of social insurance benefits are on an upward trend and, to some extent, contribute to avoiding social exclusion. However, the average size of social insurance benefits is small compared to that of the EU member states.

Social assistance schemes include 18 types of cash benefits and social services. Eligibility for cash benefits is based on the categorical approach and the payment is intended to be compensatory. Only in the case of three benefits is the income test applied to determine the eligibility of applicants (allowances for child care from the age of one and a half up to 16 years, material and humanitarian, and the newly introduced poverty benefit, named“social aid”).

The largest social assistance benefits in both monetary and coverage terms are the targeted compensations for utilities payment that are provided to 11 categories of the population. In 2004, this was identified as the most expensive social programme, holding a share of total social assistance transfers of about 47%. Although targeted compensations do help certain vulnerable categories to cope with poverty and social exclusion, the fact that the system of targeting is based on categories of the population and does not take into account the living standards of beneficiaries and their need for social assistance leads to certain failures of the system—targeted compensations benefiting both poor and non-poor households. For instance, in 2007, the richest two quintiles received one-third of the targeted compensations.

These inclusion errors in the compensatory system have forced the Government to replace targeted compensations with social aid that is based on means testing rather than the categorical approach, in an attempt to better target the poor. Social aid for poor families was introduced on 1 October 2008 , and is estimated on the basis of the average global income of the family tested by applying a proxy means testing mechanism where income is tested using

a number of measures to ensure proper targeting. The first stage of reform envisages the coexistence of social aid with targeted compensations, the size of the latter being frozen and no new beneficiaries allowed. Targeted compensations will subsequently be eliminated. This could happen by the end of 2009, depending on the evolution of both the political and economic crises in Moldova.

In relation to social services, the most important types of services provided by the state are residential care, home care and social canteens. Apart from these services the Government provides rehabilitation services and sanatorium and spa treatment to persons with disabilities, as well as prosthetic and orthopaedic services, and other locomotive aids, to war invalids and participants. There are also community-based services that have emerged mostly since 2003, when local public authorities established partnerships with civil society and donors. These partnerships are generally focused on providing social services, or opportunities to use free of charge fixed assets, and less on economic and community social development strategies.

The quality of services offered varies among providers. In the absence of a regulatory framework of social services, providers are confronted with outdated regulations constraining the delivery of services, and in most cases, the need to comply with the requirements of donors. The monitoring of social services is conducted by public authorities only on an outputs basis (counting the number of services and beneficiaries), without assessing outcomes (the costs and social effects on the groups at risk). This lack of proper evaluation hinders the development of an accreditation mechanism focused on meeting quality and efficiency conditions.

According to the Law on Social Assistance, children, families with multiple children or disabled children, disabled persons and elderly, especially singles, are considered the most vulnerable categories of the population. Roma can also be added to this group, as given lifestyle factors they are more excluded from the labour market, education and healthcare systems than other ethnicities. These categories, to a certain extent, overlap with the vulnerable categories identified by the Household Budget Survey (HBS).

There are, however, certain groups of the population who are not given sufficient attention by the Government. Therefore, although social protection programs include a significant number of beneficiaries and benefits, they do not contain measures of adult protection in situations of risk. Young people who have left a residential institution enter these excluded groups. With a low level of education, poor skills for independent living and lack of qualifications, they cannot integrate into the labour market. Without adequate housing and resources to survive, coupled with a passive degree of involvement of local authorities, they are also forced to seek means of survival that are not always legal. A further group considered to be excluded are those released from places of detention. On release from prison, institutions only grant them a one-time allowance for employment, and as with youth released from residential institutions they are not provided further support. Addressing these vulnerable groups and preventing the economic downturn from detriorating into a social crisis is crucial in the short to medium terms.

POVERTY AND SOCIAL EXCLUSION

Economic growth during the second decade of transition was accompanied by some poverty reduction. The absolute poverty rate, assessed on the basis of HBS data has registered a decreasing trend, with poverty incidence in 2006 representing about 30% of the total population, compared to 25.8% in 2007. The incidence of poverty in the context of achieving

the Millennium Development Goals (MDGs) in Moldova is also recording a similar picture. The share of the population with consumption below MDG thresholds decreased in 2006 and 2007, accounting for 34.5% and 29.8%, respectively, of the total population.

Poverty reduction was accompanied by a reduction in inequalities. In 2007, the Gini coefficient decreased compared to 2006, reaching the lowest value for the entire period under survey (0.298)—this measure indicating a decrease in the consumption expenditure gap between the rich and the poor. The decrease in inequality is also confirmed by the 90/10 distribution of the average expenditure per adult equivalent, which recorded values equal to 7.0 and 6.1 in 2006 and 2007 respectively,.

In regards to the territorial distribution of poverty, according to 2006 and 2007 HBS data, the highest poverty rates of 34.1% and 31.3%, accordingly, were registered in rural areas. These high rates are due to the large share of the population employed in the agricultural sector despite its considerable reduction in the second decade of transition. The absolute poverty risk is also relatively high in small towns representing 30.1% in 2006, and 23.8% in 2007. Insufficient development of services and infrastructure hindered the attraction of investments and economic rehabilitation of many small towns, leading to a high level of poverty. A lack of land plots, which would have ensured at least the minimum necessary food consumption, further aggravated the quality of life of the population in the small towns.

According to the HBS, the most vulnerable groups of the population in Moldova are households with children, headed by persons other than parents, families with many children, persons from households employed in agriculture, the elderly, disabled, unemployed, and persons without education or professional skills. Education remains one of the main factors that determines the level of household vulnerability. More specifically, poverty risk is dependent on the education level of the household head, decreasing substantially as the education level of the household head increases.

Income from remittances has a significant impact on the population's living standards. Households whose main source of income is remittances have the lowest degree of poverty risk (16.7%), in contrast to households receiving income from agricultural activities and social benefits. Migration is identified as one of the options among the poor to escape poverty, and members of households who consider themselves poor are more likely to go abroad to work than those in non-poor households. Emigration appears to contribute significantly to improving the standard of living among the poor.

The last few years have seen the majority of national policies concentrate on economic development and on poverty reduction. Poverty reduction objectives have focussed on increasing access of poor groups of the population to education, health, social protection and the labour market, all of which represent the key sectors in which the level of social inclusion and inequality can be measured.

PENSION SYSTEM

The pension system has gone through several transformations since 1998, when pension reform was launched. Reforms, among other measures, included expanded coverage, changes in benefit levels, increases in retirement contributions, alterations in retirement ages and contribution period, and application of highly sophisticated retirement formulas. The result is, perhaps inevitably, a very complex and poorly understood system that is far from transparent, making it inherently difficult to explain to new generations of workers and retirees exactly

how "their" system works. The present pension system under-performs on the adequacy of pension benefits, struggles with compliance and collection, and does not provide sufficient incentives to participate and contribute to the system.

In more detail, a number of factors continue to compromise the pension system in the country. First, while fiscal sustainability has improved, the pension system is not fully prepared for the inevitability of population ageing and mass migration. Second, the linkage between contributions and benefits has been strengthened, and the pension system is better suited to market conditions. However, the provision of preferential pensions and a large redistribution to farmers create discrepancies. Third, the level of income replacement is generally inadequate for common categories of pensioners and represents less than one-third of the current average net salary, while the minimum pension stands at an exceptionally high 70% of the average pension, reflecting efforts to protect the living standards of low-income individuals (including those with intermittent formal sector employment or low lifetime wages). Fourth, pension equity is compromised as different categories of retirees are treated unequally with regard to their retirement.

In order to strengthen the pension system, structural problems first need to be addressed. Re-establishing valorisation of past earnings in the pension formula accompanied by a lower accrual rate—the accrual rate is 1.4% of gross wage for up to 30 years of service, and 2% for over 30 years of service—would yield more sustainable long-run replacement rates and reduce differences among cohorts of pensioners. Strengthening incentives in the current pension system through a tighter link between contributions and benefits, avoiding contribution forgiveness, and adjusting minimum pension and contribution levels for the self-employed and farmers, would improve system finances and provide additional fiscal space for improvements in benefits, contribution rate reduction, and/or second pillar introduction when the time is right. Further reforms to cope with population ageing should focus on extending labour force participation by the elderly to avoid benefit cuts that may undermine adequacy and very high contribution rates, and discourage formal sector employment.

Measures to improve the pension system were recently addressed by the Government. It has contemplated continuing the 1998 reforms within a broader set of pension reform options, and is attempting to study the possible effects of the introduction of a second fully-funded pension pillar. However, a mandatory-funded pillar requires a sustainable first pillar, functioning capital markets and framework, and adequate administrative capacity. It also requires a sound and stable macroeconomic base, diametrically opposed to the one resulting from the current rumbling global recession. All these conditions have still not been met in Moldova and are unlikely to be met in the short to medium terms as a result of the economic crises that erode budget and population revenues and lead to the temporary disturbance of reforms.

HEALTH CARE AND LONG-TERM CARE

Turning to the health care system, the Semashko model of health care failed shortly after the independence of Moldova due to its incapacity to effectively utilize available resources. This incapacity was expressed in financing shortages, degradation of the quality of health services, and rapidly growing access barriers to health care for the citizens of the country. As a result, rent-seeking behaviours flourished. By the year 2000, almost half of health expenditure was paid through out-of-pocket means, although slightly improving over the following period. Reported by various sources, informal payments that bridged the gap after the state financing collapse still remain a strong impediment for the population in accessing health care services.

As a consequence of the social and economic disturbances during transition and the incapacity of the health care system to tackle old and newly appearing health threats, the health status of the population deteriorated considerably. Although tuberculosis (TB) management in the country has improved over the last five years, tuberculosis still represents a threat to society. The growing incidence of HIV/AIDS cases through heterosexual contacts (previously mostly among injection drug users), along with a high incidence of sexually-transmitted infections (STIs), is cause for immediate attention.

Health determinants such as lifestyle and living conditions are strongly influencing morbidity and mortality in the country. The alarming trends in alcohol consumption and increased smoking incidence have not been reversed and, along with pollution of water sources and conditional accessibility of water and sanitation, stand behind a large share of morbidity and mortality in the country. Moreover, Moldova remains an endemic zone for hepatitis. Although reforms of the last decade arrested the degradation of life expectancy in the country, Moldova is strongly lagging behind its neighbours and the EU.

A package of reforms, considered to have changed the face of health care in the country, was launched in 1996. It included introduction of a basic package of freely available health services along with a list of fees for health care services—virtually free before 1998—considerable reduction of secondary hospital capacity (1996–2006), re-enforcement of primary care and the country's emergency service, and introduction of compulsory health care insurance (2004). Although these reforms improved financing and administration of the health care sector, to date, universal access to health care services is still compromised by strong regional differences and inequalities in access between urban and rural areas. Moreover, hospitalization rates and ambulatory care favour the urban population.

Compulsory health care insurance provides access to health services within the limits of the annually approved packages of services to only three-quarters of the population, leaving some vulnerable groups out of the system. Upon the introduction of health insurance, universal access to primary and emergency care was declared; however, the universally accessible volume of services available to the non-insured is much smaller compared to the insured. Rural areas remain the most deprived of access to compulsory health care insurance. Although children have been included as a vulnerable category in the list of categories benefiting from free access to health insurance, the volume of services included and drugs reimbursed still triggers high out-of-pocket expenditure for families. Moreover, the cost of pharmaceuticals to the population represents a strong barrier to accessing all types of care. Both the insured and non-insured in many cases have to pay for most medicines at the primary and ambulatory level, and sometimes in hospital settings.

The health care services provided to the population are not supported by strong quality control mechanisms. The implementation mechanisms for the stipulations of laws regulating the obligations of medical personnel and patient rights are still under development. Proactive measures are being undertaken to develop modern clinical guides and protocols. However, clinical implementation of newly developed protocols in clinical practice is slow.

The technological side of the health care sector has been reported to be outdated by a number of sources. In addition to evidence of obsolete, faulty and, in many cases, lack of equipment at all levels of care, slow the pace of implementation of eHealth technologies in clinical practice, increasing the gap between quality of health care in Moldova and other European countries.

The low level of training and motivation of health care personnel raises questions about the capacity of the health care sector to provide an adequate number of well-trained and dedicated medical professionals. The challenge of the exodus of health professionals is obvious, and requires rectification.

Long-term care in Moldova has not been officially defined and represents a range of social and health services provided by different government bodies and non-government organizations. Most long-term care still comes from family networks. Existing state institutional capacity does not satisfy either the demand or quality standards for adequate care. A limited number of standards have been developed to date with the assistance of strong lobbying from the non-government sector and donor community.

Evaluation of the impact of the financial crisis on the health care sector is difficult under the present conditions, as it will depend to a large extent on the government response to be developed and introduced to address the situation, and the timing of implementation. The present lack of such a strategy points to the under-preparedness of health sector administration to deal with the present and future impact of the financial crisis. A possible decrease in financing of the health care sector due to a reduction in compulsory health care insurance collections, and drop in national public budget revenues, may lead to deterioration of the financial situation in health care institutions and compromise the sustainability of the sector. Possible financial shortages are likely to compromise the supply of pharmaceuticals in hospital settings and the availability of reimbursed medicines in primary care settings. The persistence of rent-seeking behaviour among health personnel and the incapacity to continue with the modernization of the health care sector are likely to reduce the accessibility and quality of health services.