

SME's Situation within a DCFTA Context through COVID-19 Crisis

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Abstract: Analyzing the negative impacts of the global pandemic (COVID-19) on the R. of Moldova economy, SMEs external trade performed within a DCFTA framework represents one of the most important vectors for keeping the local economy in good health. Once the COVID-19 pandemic struck the world, Republic of Moldova was no exception. The Covid-19 pandemic has caused a series of problems, and those caused by movement restrictions have led to economic bottlenecks for exporting companies which resulted in liquidity and cash flow problems.

Bringing our minds back to the Association Agreement and directly to the DCFTA, it is appropriate to estimate it's preliminary impact on Moldova's economy. After 5 years of DCFTA creation and implementation, it has been experienced a significant boost of the trade between Moldova and the EU, which resulted in the increase of investments, jobs, wages and goods export growth with 40% (1.5 billion USD). In spite of the positive effect the Free Trade Association Agreement is having on R. of Moldova, still, there are present some issues of healthy competitiveness and increasing production capacity type, key factors for exporting SMEs. With all these being stated, this study aims to identify COVID-19 influence on local SME's doing business within the EU marketplace. Also, this article presents some analysis of emergency projects established by the local authorities to support SMEs and deliver practical solutions that can bring about change. The methodology used in this research is based on the statistical data that reflect the development of Moldovan exporting enterprises after the entry into force of the Association Agreement and, implicitly, DCFTA; analysis of national legislation and policy documents to support SMEs in the country and foreign trade in the context of the DCFTA.

Keywords: *small and medium enterprises (SMEs); SME support policy; DCFTA; Covid-19; foreign trade.*

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Introduction

The implementation of the Association Agreement, inclusively the Deep and Comprehensive Free Trade Area (DCFTA) between the Republic of Moldova and the European Union had been having a positive impact for small and medium-sized enterprises. It consisted merely from boosting of the trade between Moldova and the EU, increase of investments, jobs, wages and economic growth of the whole nation. In this context, SMEs exports to the EU registered substantial growth in terms of value, being the most important vector for the economical resurgence in these strange times provoked by the COVID-19 pandemic.

These times of crisis has been produced a vast amount of issues, getting the governments and its citizens going through tough challenges. Social distancing measures resulted in closing the borders which dramatically affected the movement of the goods and services. Thus, SMEs operating internationally has been facing a certain dilemma in performing the duties mentioned in the contractual agreements with international partners.

In these circumstances, a whole bunch of challenges had gotten upon local institutions accredited for supporting the SMEs. The ultimate goals of the authorities are to support the participation of the businesses on the EU market, increase competitiveness and fully capitalize all opportunities provided by the DCFTA.

The main objectives of the analysis are:

1. Explore the situation the pandemic is creating and its influence upon small and medium-sized enterprises;
2. Asses the exports to the EU and economic impact of the Moldova–European Union Association Agreement / Deep and Comprehensive Free Trade implementation;
3. Analyze the support framework policy for the SMEs;
4. Point out recommendations to be taken by the SMEs in order to keep their businesses above the water, through consulting specialized literature.

The object of study of this analysis represent SMEs exporting goods to the EU market under the AA/DCFTA, and the consequences COVID-19 pandemic is causing to the enterprises.

1. The main indicators of SMEs sector

SMEs have a significant weigh on Republic of Moldova economy. In 2019 National Bureau of Statistics of Moldova (NBS) registered 56.7 thousand economic agents – 98.6% (55.9 thousand economic agents) constituted small and medium-sized enterprises.

SMEs consists of 3 groups – micro, small and medium-sized which differ in structure (number of employers, sales and assets of the enterprise). Small enterprises make 11.6%, medium-sized enterprises – 2.4% of SMEs (Table 1.).

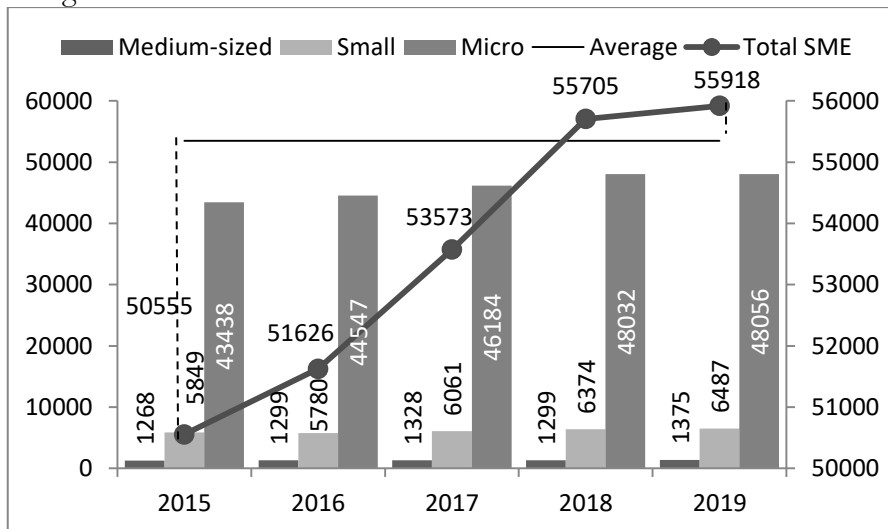
Table 1. Main indicators of SMEs sector in 2019

| Indicators | <i>Total SME</i> | Medium-sized | Small | Micro |
|--------------------------------------|------------------|--------------|--------|--------|
| Number of enterprises, unit. | 55918 | 1375 | 6487 | 48056 |
| % of Total | 98.6 | 2.46 | 11.60 | 85.94 |
| Average number of employees, persons | 336059 | 102984 | 118662 | 114413 |
| % of Total | 60.8 | 30.64% | 35.31% | 34.05% |

Source: Calculated by the authors on based on the source [5].

Before COVID-19 happened, SMEs sphere was facing slow but steady progress. Just as well as in the last years, 2019 wasn't an exception for No of SMEs going up (55.9 thousand – 2019; 55.7 thousand – 2018;).

If it were to omit the last year (2019), we can easily witness a slight growth in SMEs quantity which is frankly to the micro and medium-sized enterprises increasing, however, given the fact that these enterprises are relatively weak in terms of competitiveness, this serves as a set back for making full use of the opportunities and export capacities DCFTA is offering.

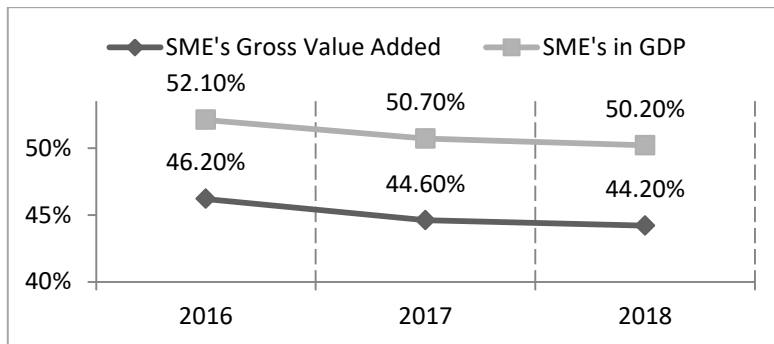


Source: Made by the authors, based on the source [5].

Figure 1. Dynamics of the number of enterprises in 2015-2019, thousand units

The GDP quota serves as a sign for quality and quantity evaluation of SMEs influence on the whole economy. Yet, in the last three years, this influence significantly weakened.

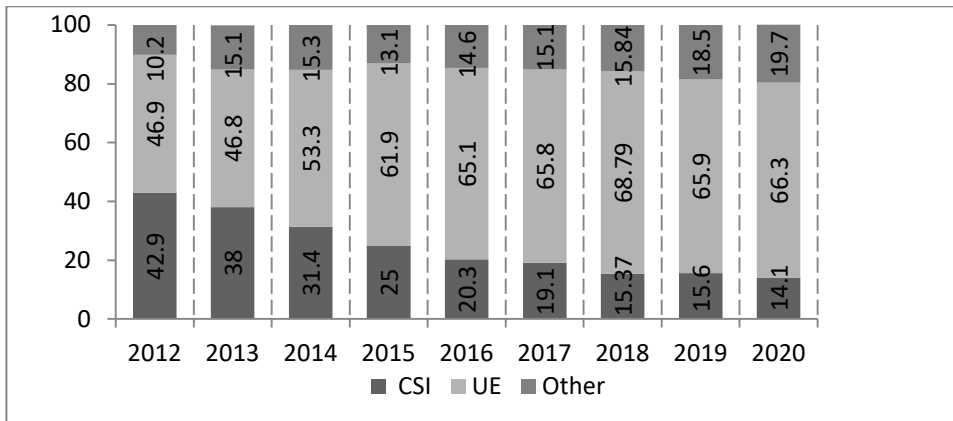
It's relevant to mention here that, according to the precedent criterion of allotment for SMEs, the contribution was not getting higher than 35%. However, SMEs in 2018 had registered a substantial increase in GDP with 50.20%. Anyway, according to the World Bank estimations [2], as a result of COVID-19 is having on export, GDP is going to drop by 6% thus cutting the incomes for SMEs.



Source: Made by the authors, based on the source [5].

Figure 2. SMEs gross value in GDP for 2016-2018,%

After 5 years of Moldova–European Union Association Agreement / Deep and Comprehensive Free Trade implementation in the Republic of Moldova, the volume of agri-food exports to the European Union market has crucially increased. In quantitative terms, the evolution of exports to the EU indicates increases by 80% of total exports, during the reference period, at lower prices. Starting with 2005, the EU becomes the most favourable economical partner for the Republic of Moldova, as the EU market has accounted for 68.79% of Moldova's total exports for 2018.



Source: Made by the authors, based on the source [4].

Figure 3. Export structure based on the group of countries, %

The comparative analysis of exports by destination countries reveals a much more stable evolution towards the EU market compared to other destinations. If we analyze the 2010 year (47.3%), prior to DCFTA, over the 2018 year (68.79%), we notice that exports to the EU have seen an upward trend of value for the entire reference period, with a 21.49% advance. For comparison, exports to the CIS during the reference period decreased from 40.5% (2010) to 15.37% (2018), while the exports to other countries slightly increased (12.2% to 15.84%). This aim could be appreciated as a positive one because it broadens the foreign market of the Republic of Moldova.

Although, with the latest COVID-19 restrictions being in force, local SMEs exporting goods to the EU market has suffered a series of difficulties.

2. Characteristics of the SME support policy in the Republic of Moldova

In the present time, the support policy for the local SMEs is being determined by the 2 legal acts:

1. The small and medium-sized enterprises act (LP 179/2016);
2. SME Development Strategy (2012-2020).

The mentioned above acts represent the overarching framework for the Republic of Moldova's policy on small and medium-sized enterprises. They are intended for improving the attitude to entrepreneurship in Moldova, simplify the normative and policy environment for local SMEs, and eliminate the lasting barriers to their further development [1].

The small and medium-sized enterprises act stipulates it's main priorities as promoting entrepreneurship, financial instruments to help them

grow, innovate and stay competitive, also highlight ways to internationalise businesses, face the existing competition, find new business companions out of the country, access foreign markets. Going on the international level increases the performance of SMEs, embraces competitiveness and supports sustainable growth. At the same time, in handy with the legal framework and DCFTA, SMEs Development Strategy (2012-2020) has designed a 13 points action plan for facilitating SMEs access to the EU market, thus, EU consolidating its position as the main foreign market for Moldova's SMEs.

3. Institutional support for SMEs

Regionally, the Organization of Small and Medium Enterprises - subordinate of the Ministry of Economy and Infrastructure is being responsible for the implementation of governmental programs aiming SMEs policy.

Under the supervision of ODIMM activates Credit Guarantee Fund, which, especially in the current COVID-19 situation is granting guarantees to the SMEs, including start-ups, extend access to loans for current business/implementing development projects, ensure the proper functioning of the "First Home", "Pare 1+1", "Women in Business" programs.

Additionally, local banks in accordance with Regulation on the treatment of banks' credit risk using standardised approach shall be assigned a risk weight of only 20% for the guarantees emitted by the ODIMM [6]. It is also worth mentioning here that ODIMM will make all the money transfers (500.000 MDL = 25.500 EUR) for the beneficiaries who have implemented eco-friendly measures for their businesses or have any kind of experience on the international arena in terms of exporting goods/services [7].

A number of state institutions are involved in the provision of certain services to local/external business, often on concessional terms. Among these are Investment Agency, The Chamber of Commerce and Industry, etc.

4. Institutional support for SMEs

In 2014, Republic of Moldova and EU signed the the Deep and Comprehensive Free Trade Agreement (DCFTA). Since it's beginning of implementation it has been offering the Republic of Moldova a distinctive opportunity to reach a more sustainable economic growth lane and after 1 year of its implementation positive balance is assessed.

A Deep and Comprehensive Free Trade Agreement (DCFTA) can not be fully compared and likened to an usual free trade agreement (FTA), which involves the scrapping of customs tariffs and quota restrictions on

trade. The ‘deep and comprehensive’ part of the DCFTA provides for the accumulation of more obligations by both sides for opening up of service sectors, elimination of technical obstacles to trade, and harmonization of regulatory regimes for domestic markets (like for financial markets, transport, environment, etc.). The partner country engages itself into introduction of convergence on EU regulations and standards in its national laws. In the vast majority of cases, the EU standards are similar to international standards, meaning that the DCFTA agreement with the EU also opens up the economy of the partner state at the global level [3].

According to Article 173 of the Association Agreement, Moldova has to take the measures needed for the steadily achievement of conformity with the EU's technical regulations, standards, metrology, accreditation, corresponding systems, and market surveillance system, and undertakes to follow the values and practices expressed in the relevant EU legislation. In order to reach this aim, Moldova is estimated to gradually incorporate the relevant EU laws into its legislation by 2018. Moldova also agreed on carrying out administrative and institutional reforms essential to provide an effective and see-through system that is required to implement the Agreement. It also committed to refrain from amending its horizontal and sector-level legislation, except for aligning such legislation progressively with the corresponding EU legislation. It is this part of the DCFTA that according to most studies will benefit most Moldovan SME.

5. Trade, business & support to SMEs

The EU-funded technical assistance project - Support to the Quality Infrastructure Framework within a DCFTA context in the Republic of Moldova (known, in short, as the QI Project) – is working with up to 75 Moldovan SMEs, providing support aimed, in part, at enhancing their capacities to export into the EU, taking advantage of the tariff benefits of DCFTA, but also helping some smaller companies expand their penetration into the domestic marketplace [1].

Conclusions

The current pandemic we are all facing nowadays has caused numerous issues to the world economy, and the Republic of Moldova wasn't an exemption. The continuous development of SMEs and boosting the export of goods are the crucial points in order to keep things on the track.

At present, local authorities are struggling to cover the losses SMEs are having, inclusively the enterprises operating internationally. Our government have announced the development and implementation of the

plan for guided economic recovery. Some of the main bullet points are: improvement of the concerned legislation - in correlation to the newly established social distancing measures; applying in response to the crisis the specially designed programmes to those hardest-hit SMEs; offering immediate borrowing options at favourable rates; keeping key interest rates at historically low levels.

Despite the difficult economic circumstances, the implementation of AA/DCFTA has had a noticeable effect on the dynamics and sustainable economic growth over time. Although, in the beginning, there were present some political concerns regarding the direction Moldova's economy should take, over time, the DCFTA implementation has been met so far all the positive expectations, thus, EU market strengthened its position as the main selling market for Moldova.

The current crisis the world is facing has harmed commercial trades of the Republic of Moldova.

If we analyze the period between 2014-2019 (the first 6 complete years of DCFTA implementation) with the similar period prior to the DCFTA (2011-2014), we notice that exports to the EU registered an upward trend in value terms for the entire reference period, with a 22% advance. For comparison, exports to CIS during the reference period decreased by 47%, while those with other countries remained relatively constant (+2.7%). At the same time, the EU share in the total Moldovan exports increased to 65.8% in 2019, compared to 53.3% from 2014. The trend was sustained, exports to the EU increased with 38.1% during the first half of the year, compared to the similar period of the previous year, while the EU market was accessed by 68.5% of the total Moldovan exports. It is worth to mention that this progress took place despite the quite tough economic and political background which hindered an even more noticeable growth of exports to the EU: political crisis, sanctions and mutual restrictions imposed by the EU and the Russian Federation, appreciation of the dollar on the international stock exchanges, adverse climatic conditions and diminishing international prices for some products.

Econometric estimates show that if we analyze the factors that influenced Moldovan exports to the EU (inertia of previous years, economic trends in the EU, domestic offer and exchange rate fluctuations of the national currency) and exclude the effect of DCFTA, these exports could be lower with about 410 million USD (367 million EUR). Over the same period, the total exports to the EU have increased almost twice (with about

746 million USD in 2014-2019 compared to 2011-2013). Therefore, a half of the increase in exports to the EU, in the period under review, was exclusively due to DCFTA, which is an obvious effect, taking into account that the assessment is performed only four years after its implementation and undoubtedly confirms the benefits of the trade liberalization with the community area.

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