Implementing the DCFTA in the context of state capture: assessing the position of Small and Medium Enterprises

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Abstract

The implementation of the DCFTA in the Republic of Moldova is an ongoing process, its ultimate objective being the modernisation of the Moldovan economy, broad prosperity and the creation of an open society. By using conditionality, the EU is banking on public and private actors aligning to European norms and practices. This article focuses on the position of SMEs and their interactions with the DCFTA. The overall argument posited is that the condition of 'state capture', twinned with a disadvantageous business climate serve as structural impediments to the full implementation of the DCFTA and to the capacity of the SME sector to benefit.

Keywords: Moldova, Small and Medium Enterprises, DCFTA, SMEs Eastern Partnership, State Capture, Corruption

1. Introduction

In 2014, the Republic of Moldova and the European Union set out to deepen their relationship by adopting the Association Agreement (AA) in the context of the Eastern Partnership (EaP). This agreement recognised the extent to which Moldova had already travelled some way down the European path, that previous agreements had run their course and crucially, that a deeper, more dynamic and ambitious framework was now needed. It is also important to recall that the EaP, when established in 2009, was a response to the intensifying geopolitical conflict in the region, which also had relevance for Moldova (Prague Eastern Partnership Summit, 2009).

A sizable portion of the EU-Moldova Association Agreement is devoted to 'Trade and Trade Related Matters', in other words the Deep and Comprehensive Free Trade Agreement (Official Journal of the European Union, 2014). This is Title Five of the AA and comprises the densest and arguably most detailed set of

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all provisions. There is a lot to say about the DCFTA and its short and long-term aspirations and objectives, but it suffices to say at this point that, as well as boosting two-way trade, its rationale is all about enhancing the positive interplay between sustainable domestic political change and economic reform, building prosperity and anchoring Moldova into the EU's orbit.

The Association Agreement undoubtedly represents a milestone in the process of rolling out the EU's neighbourhood policies and the DCFTA has already started to yield positive outcomes in the form of more trade and by providing footholds for further political and socio-economic reforms in Moldova. However, at the same time, this is still just the beginning of the story for both the EU and Moldova. The AA and its DCFTA component are elements of the EU's normative clout and are thus related to the process and transformation of the Moldovan political, economic and social landscape rather than quick fixes. Ultimately, the measure of the project will be whether it can bond Moldova to the EU, benefit Moldovan society and nurture the country's security and wellbeing.

There are a number of useful analytical studies that have sought to gauge the extent to which the DCFTA is fairing. A snapshot from a current vantage point gives a decent image – though the most astute commentary points to the deleterious effects of Moldova's 'state capture' and its effects on the long term success of EU initiatives. Subsequently, there is a lot of scholarship on the domestic state of affairs in Moldova and consideration of the combined effects of corruption, a crisis of identity, tough economic contexts, politicised national institutions, dominant personalities and geopolitical fragility and other ways in which the specific 'Moldovan reality' affects the way that EU policies are received and implemented (Tudoroiu, 2015; Socor, 2015; Cenusa, 2016).

This paper aims to build upon existing scholarship by looking at the domestic factors that relate to and mediate the implementation of the DCFTA. Another reason for taking such an approach is that the academic commentary in the field of International Relations on the subject tends to focus on the big picture of the European Neighbourhood Policy (ENP) and the Eastern Partnership (EaP) with less attention on or acknowledgement of the vital importance of specific domestic contexts, capacities and actors other than national governments. The paper also seeks to build upon the argument that Moldova's 'problem' is not simply geopolitical, involving a conflict between pro-Russian and pro-European tendencies and visions, but it has also to do with being a weak state, with profound corruption and low domestic trust in political institutions and national elites – either pro-EU or pro-Russian (Peleshuk, 2016). With this thought in mind, the paper will contend that the prevailing domestic context of state capture in Moldova does not augur well for the DCFTA in meeting its medium and long-term objectives of transformation.

To advance this general assertion about domestic factors mattering a little further, the paper will hone in on issues to do with the local business environment and the position and role of Small and Medium Enterprises (SMEs) in Moldova. The creation of the Eastern Partnership in 2009 recognised the significance of SMEs to the development paths of the partner countries and their importance in realising the full potential of the DCFTAs. It was also recognition of the fact that whilst SMEs were abundant across most of the region, their input into national GDPs was quite low. The growth of ‘grey’ or ‘informal’ economies and the resulting negative effects this was having on tax income for states was a further factor behind the EU’s renewed efforts vis-à-vis SMEs and its support for entrepreneurship. Finally, with a lack of employment opportunities for educated and skilled young people in most EaP states, which resulted in high levels of economic migration, the support for the SME sector was aimed at stemming the brain-drain by creating a generation of entrepreneurs engaged in building up domestic economies. Consequently, and often in partnership with other international organisations, the EU has upped its support to private enterprises and entrepreneurs. For example, together with the EBRD and SIMEST, the EU provides direct financial support to SMEs to improve their access to finance by providing guarantees schemes and technical assistance for DCFTA-aligned investment, capacity building and modernization.

The paper’s main hypothesis is that there is a palpable mismatch of expectations and realities between the provisions and opportunities in the DCFTA and the capacities of Moldovan SMEs as key stakeholders to optimally engage with and potentially benefit from the agreement. The paper holds that whilst an increase in the volume and value of trade flows between EU states and Moldova is a vital indicator of success, appraising the DCFTA only by metrics is a method that only reveals part of the evolving picture. There are a host of reasons why such an avenue of enquiry is worthwhile. Moldovan SMEs are, or at least should be considered, key stakeholders in the implementation of the DCFTA. This line of thought is vital to acknowledge since the Eastern Partnership and its capacity to deliver on medium and long-term objectives rests, to a very large extent, on strong local ownership by private and public actors. Equally, if Moldova is to go beyond a model of growth based on domestic consumption to one premised on innovation, investment and internationalisation, changes in context and opportunity structures for SMEs need to be consistently revitalised and sustained through international intervention.

2. Transitions and open societies - why are Small and Medium Enterprises important?

In the context of transition states and developing countries, SMEs are strongly associated with sustainable development and the creation of business environments characterised by openness and transparency. The logic is that an environment where SMEs can freely flourish helps to bring about a deconcentration and positive dispersal of political and economic power involving multiple stakeholders who can then promote open societies, sustainability and also lessen dependence on international donors or remittances. SMEs in private hands also enrich democratisation since entrepreneurs tend to be more positively disposed towards democratic reforms and the liberalisation of economies (European Bank for Reconstruction and Development, 2015). Crucially, in transition economies and at times when new trade opportunities are emerging, as is the case for Moldova, SMEs can be critical agents of change. SMEs are also important points of resilience in transition economies since they are close to the market and their customer base and can therefore gauge changing demands and expectations with relative ease; they are usually hardy and determined to survive since they are often family businesses and the only income source for the owner. SMEs are also relatively nimble and sufficiently flexible to adjust and adapt to external changes, shocks and new circumstances. In the shifts from command economies to liberal market-driven economies, SMEs can help counteract unemployment problems, which inevitably result from downsizing the monopolistic public sector industries by providing new opportunities for employment, entrepreneurship and income for those affected by economic transitions. The post-communist economic transformation of Central Europe confirms these assumptions. The 1990's witnessed the rise of SMEs led by entrepreneurs who readily latched on to new market opportunities and consequently became motors for economic change which helped to erode monopolies and state-controlled industries. Subsequently, SMEs became important stakeholders developing foreign trade, domestic market growth and diversification, all of which contributed to getting states ready for EU accession in economic, political and social terms. In Poland, for example, small enterprises emerged in their legions after the collapse of the command economy and by around 2000 SMEs accounted for over 90% of total enterprises and around one third of Polish exports (Myant and Cox, 2008). The Central European example is certainly illustrative, but there are defining differences between Central Europe in the 1990s and contemporary Eastern Europe. Operating in an oligarchic system with weak formal governance means that SMEs have little leverage and power to shape the political and economic environments in which they operate. In addition, SMEs, especially the small ones, do not have sufficient resources, intellectual or financial, to identify and efficiently respond to opportunities such as the DCFTA and despite their capacity for flexibility, it may be more difficult for them to ride out some types of shocks, such as foreign export embargoes. But there is another salient factor at play here in the shape of the EU as 'context'. The economic transformations in post 1989 Central Europe were spurred on by the prospect of EU membership and underwritten by the development of low risk environments, which served to attract plenty of Foreign Direct Investment. Crucially, this context provided footholds for reformers and the business sector to carry out painful and demanding reforms necessary to get closer to the EU; this was backed by strong domestic consensuses on EU membership. The prospect of membership is not on the table for Moldova and crucially, the Eastern Partnership and DCFTA still have an ambiguous end-goal. Moreover, adhesion to EU standards places huge demands and burdens on domestic actors to modernise, the benefits of which are mostly not instantly tangible (Expert Grup, 2016).

3. Moldova's DCFTA: bearing fruit but with limitations?

What can be said about the DCFTA so far? The implementation of the Association Agreement and DCFTA has been subject to on going monitoring, with measures of progress being relatively open to public and expert scrutiny. A lack of transparency had been one of the chief criticisms brought to previous EU-Moldova negotiations by the civil society sector. In addition, there have been a number of quality research projects, which have analysed the interim results of the agreement, which this paper will draw from (Emerson and Cenusa, 2016; the Government of Moldova, 2016).

The DCFTA text itself is a legal document and is a sizable portion of the Association Agreement. The AA is premised on 'common values and strong links' and 'a common desire to 'further develop, strengthen and extend' relations between Moldova and the EU'. Furthermore, the agreement acknowledges the 'European aspirations and the European choice of the Republic of Moldova', leaving open 'the way for future progressive developments in the EU-Republic of Moldova relations'. The scope and ambition of the AA/DCFTA is immense, recalling the overall scope of European integration, it pledges to

> contribute to the political and socioeconomic development of the Republic of Moldova, through wide-ranging cooperation in a broad spectrum of areas of common interest, including in the field of good governance, freedom, security and justice, trade integration and enhanced economic cooperation, employment and social policy, financial management, public administration and civil service reform, civil society participation, institution building, reduction of poverty, and sustainable development…(Moldova-EU Association Agreement, 2014)

Research suggested that by joining a DCFTA, Moldova would be able to grow its exports to the EU by some 11-16%, and to boost GDP by 5.4 - 6% annually (Radeke, 2012). Such figures though were constructed on the assumption that necessary reforms were carried out not only to prepare the technical landscape for enhanced trade, but also to align to EU norms and to create fundamental underpinnings of good governance and a conducive environment to enable domestic businesses, especially SMEs to flourish and facilitate an inflow of FDI.

What of progress? Since September 2015, the EU has almost completely opened its markets for imports from Moldova, unencumbered by tariffs. Consequently, export opportunities for Moldovan producers to access and sell their products to the EU market have grown exponentially. At the same time, Moldovan producers are afforded cushioning in the form of the staggered opening of the Moldovan market with a regime for only the gradual removal of tariffs on EU imports to protect the domestic market from sudden shocks and tough competition. What have the effects been so far? In return for export opportunities, the DCFTA lays out strict and closely monitored conditions relating to the modernisation towards EU-standards of the Moldovan economy, production methods and practices, health and safety standards, hygiene and phyto-sanitary rules and so on. Moreover, the DCFTA aims to fundamentally re-shape the local business environment – where there is vast room for improvement.

The introduction of the DCFTA did not result in a huge overall rise in the level of Moldovan exports to the EU. 2014-2015 rather witnessed a slight decrease of 1.4% (6.9% for non-food exports) on bilateral trade between Moldova and the EU (Botan et al., 2015). Notwithstanding this change, the EU market is the most stable area of growth for Moldovan export products and by adopting European standards Moldovan producers have also started to find their feet in other markets beyond. Moreover, despite the modest dip, the first years of DCFTA have seen certain products, such as sugar, honey, barley, wheat, dried fruit and some fresh fruit, being exported to the EU at five times the amounts as before. The implementation of the DCFTA has also helped Moldovan exporters to diversify their markets and to compensate for the losses in the CIS markets, brought on by Russian embargoes and declining demand. In this sense, the DCFTA is already helping Moldova consolidate its strategy of trade diversification and desire for stable markets. Around 62% of Moldovan exports end up in the EU and whilst Romania remains the key largest destination, the overall number of EU states buying Moldovan produce is palpably growing – especially when it comes to key agricultural goods (European Commission, 2016). Agriculture and agri-food sectors are already Moldova's most important export areas, but restrictions that limit the country's capacity to export more quantity and a wider selection of products (most notably dairy, meat and eggs) remain in place. To be able to produce quality and competitively priced goods, Moldova has to continue on the path of approximating to and fully implementing EU standards. However, adopting such EU-standards takes time, effort, and sizable investment, whose positive consequences are not necessarily felt very quickly, whilst the costs of modernisation and adaptation to producers can be immense. Meanwhile, there is opposition from various domestic and foreign stakeholders who would rather refer to the former and less demanding Soviet 'GOST' standards (Emerson and Cenusa, 2016, p. 5), with a view towards re-capturing the CIS and Russian export markets in the new context of the Eurasian Economic Union.

An interim conclusion is that the DCFTA remains work in progress and that it is not, as already noted by Cenusa and Emerson, a 'magic wand' with which Moldova's multiple political and economic ills can be cured. The Association Agreement and DCFTA insist upon comprehensive EU 'normative alignment' from Moldova, which ultimately requires a thorough transformation, not just of technical standards, but of governance – understood in its widest sense (Emerson and Cenusa, 2016, p. 5). All evaluations of Moldova so far tend to back this claim, by pointing to barriers in the DCFTA implementation and the limited realisation of benefits that will continue if the country's macro political, economic and social problems are not dealt with. The unstable political system, corruption, highly politicised institutions, a disenfranchised civil society and lack of trust in public institutions as well as legislation lacking in core spheres, such as the judiciary and media ownership thwart Moldova's capacities. In response to this, the government in Chisinau defined a Priority Reform Action Roadmap (DCFTA, 2016), comprising a list of measures, stakeholders' engagement and a time frame to try to meet the problems identified in the European Union Foreign Affairs Council of February 2016, as well as by other international donors and stakeholders, such as the IMF. At the time of writing, it appears that progress has been made and has eventually been rewarded with a positive response from the IMF, which had held back financial support until the country demonstrated the capacity to address weak governance and banking problems (International Monetary Fund, 2016). At the same time, the conduct and outcome of the Presidential election of November 2016 suggests that any baby steps that have been taken forward could easily be pushed back and that the Moldovan trajectory of positive change is rarely linear.

4. The notion of state capture as Moldova's defining feature

It was asserted earlier that a nuanced understanding of Moldova's predicament and seeming incapacity to achieve sustainable transformation is best reached if the analysis focuses on domestic contextual factors and structures and not just on geopolitical competition.

The concept of 'state capture' implies systemic and widespread political corruption, a situation where the private interests of individual oligarchs or small groups palpably influence a state's institutional set up and decision-making structures to their own political or economic advantage. Crucially, this is manifest in discrete and hidden manoeuvres and deals within or amongst all organs of government across the executive, ministries, legislative and judiciary. Needless to say, such a context does not bode well for the implementation of EU-style norms and guidelines or for the creation of an investment-friendly business environment for SMEs to prosper.

Leitner and Meissner provide a useful overview of Moldova as a captured state. For them, Moldovan life and politics suffer from the persistence of informal practices, which act as 'compensatory mechanisms', regulating normal ways of life and bypassing official rules, laws and principles. This, they argue, is due to the fact that the state is weak in its capacities to provide for the welfare of its citizens and secondly, that is not able to reward rule conformity or punish rule breaking. As a consequence, key public institutions, such as schooling and education, the judiciary, police, healthcare and the mass media tend to function according to 'principles other than those stated in law, which contributes to the spread and perpetuation of corruption (Leitner and Messner, 2016). Needless to say, the toxic blend of oligarchy, weak public institutions and 'informality as default' tends to stymie the implementation of EU policies, which necessitate the rule of law, an accountable public administration and an open and permissive business environment. The reality seems to be that although tackling corruption remains a national priority supported by the EU and other international donors, the persistence of a specific oligarchic structure blocks the necessary fundamental tectonic changes.

The oligarchic situation in Moldova is different from that in states such as Ukraine or Russia, where there is a plurality of oligarchs. The omnipresence of Vladimir Plahotniuc as Moldova's only true oligarch is significant and runs counter to transformational processes in a number of ways. He has the capacity to reach and the ability to define many aspects of high and low politics, the media, as well as finance and banking and crucially, there is no competition or counter balance as such from other oligarchs to his hegemony. Moreover, Plahotniuc's means and influence is such that he can restrain, discredit and destroy his opponents with relative ease. A study of the Polish Eastern Studies Institute dissected Plahotniuc's power into four reinforcing elements, the first being the tightness of his entourage and clan-like support network, often based on family ties. Next comes his substantial business and financial power, which sets him above and beyond his closest business competitor. Third is his noted control over the judiciary and justice system, which has proven to be a very effective way of controlling individuals and setting comfortable conditions for pursuing his own business and political interests. Finally, there is his media power, which is a further enabling factor to assure his oligarchy (Calus, 2016). Crucially, since Plahotniuc's power derives from the control he exerts over national institutions, he has no interest in any profound transformation or EU-inspired reforms, such as those entailed in the AA and DCFTA, since this would undermine his position and dislodge his capacity to profit from the status quo.

But there is more to say about the consequences of this oligarchic monopole. Even if Maia Sandu had won the Presidential election of November 2016, she would have faced enormous challenges and obstacles when tackling corruption. Her success at gathering 47% of the vote is a sign that an ever larger sector of the population is in favour of fundamental change, it also suggests that the choices voters make are not solely determined by a binary pro-Europe or pro-

Russia preference as international reporting often concludes, but it rather has to do with pro-reform versus anti-reform. However, the main point to make here is that any reform agenda for Moldova will be stymied by prevailing realities and the structural corruption that results from oligarchy and state capture. Recent times have seen an apparent consolidation of Vladimir Plahotniuc's international profile. By travelling as part of the official delegation to the United States in 2016, by meeting Victoria Nuland and by writing in reputable Western publications, he has been able to legitimise his position abroad.

Attempts to confront structural corruption and to improve the local business environment have to also deal with the realities of Moldova as a fractured state. The persistence of Transnistria is a demonstration of the problematic nature of the Moldovan national identity, patchwork of allegiances and the long-term geopolitical fall out from the Soviet Union's demise. The continued stationing of Russian troops in Transnistria, subsidies from Moscow that keep the region afloat and local stakeholders with strong business and political interests in keeping the status quo provide formidable distractors against fundamental change and conflict resolution (Calus, 2016). The economic effects of this protracted conflict are evolving, not least since the DCFTA offers prospects for Transnistrian businesses to export to the EU, based on the conditionality aimed at strengthening the Moldovan economy and its viability and at raising production standards in Transnistria in line with those of the EU.

The notion that Moldova is a captured state is a compelling one. The consequences are broad and far-reaching and as briefly mentioned already, the negative effects on the overall implementation of the DCFTA are palpable. For the purposes of this paper, the main consequences can be described as

(i) A local business and economic environment characterised by a relatively high level of risk;

(ii) Low levels of Foreign Direct Investment (FDI): FDI flows into Moldova constitute just 2.5% of national GDP, which is below the levels of Azerbaijan, Georgia and Armenia (OECD, 2016, p. 305);

(iii) A local business environment not conducive for entrepreneurship to flourish and for SMEs to develop, both in size and scope;

(iv) A large and expanding grey economy which starves the economy of tax income and workers' access to social protection and so on;

(v) A shrinking population, due to mass migration and huge reliance on remittances, which generally then remain in private hands;

(vi) The persistence of informal and irregular practices and transactions, including bribery;

(vii) Inconsistent performance and effectiveness of bodies set up to advise SMEs and entrepreneurs in a DCFTA context.

5. Considerations and consequences for SMEs and DCFTAs

The effects of state capture, weak regulation and corruption are acutely felt by SMEs. Despite their small size and flexibility supposedly being a source of strength in the context of economic transitions, they are the businesses that are the most vulnerable to corruption. Moreover, accepting that SMEs are important drivers of development, the effects of corruption can be overwhelming for fragile and poor states, such as Moldova.

There are a number of structural reasons as to why SMEs are susceptible to and victims of corruption. First, as small concerns and often based around a family, informality is the modus operandi in the work place, which can mean that corrupt practices are overlooked or simply regarded as the norm. Second, SMEs as businesses generally have short-term horizons and, in the case of Moldova, tend to be about subsistence and survival, thus managers and workers cannot afford to think about the long-term consequences of engaging in corrupt activities, concentrating instead on the immediate business gains from corruption. SMEs will, in effect, opt for the path of least resistance. Linked to this is the fact that SMEs are in weak positions vis-à-vis corrupt public institutions and officials in the sense that they do not hold much bargaining power nor are they likely to have their own 'connections' to influence corruptible decision makers and power brokers. Third, soft-corruption can become the norm for SMEs, in the form of nepotism or gift giving to smooth business relations and acquire short-term advantages. Next, the prevalence of corruption in the business environment has limiting effects on development efforts amongst SMEs and entrepreneurs. Moldovan SMEs have, for instance, actively chosen not to expand the size and scope of their enterprises because they are aware that they will have to pay more bribes so as to render investment and the efforts involved not worth it.[1]

Compounding the damaging effects of corruption is the conscious choice often taken by SMEs to operate within the informal or grey economy. This reality is a direct challenge to DCFTAs which, above all else, require 'norm alignment', the verification of which requires regulations within an open economy. For SMEs in EaP states, which are generally small or even micro in nature, the financial costs of regulatory compliance and of dealing with bureaucracies are too weighty. For a country whose future economic welfare is premised on association with the European Union, a situation where SMEs feel discouraged from entering the formal economy does not augur well for the DCFTA.

To sum up, the mismatch between DCFTA-related requirements and conditions and the state of the SME sector in EaP states is explained by the following factors and contexts: (i) SMEs are small and often involve intensive

[1] Interview with an official working on DCFTA implementation, Chisinau, Moldova, August 2016.

labour production of low-value goods (ii) SMEs often lack modern methods and technological know-how which means that they require significant investment starting from scratch (iii) Barriers to entering the formal economy are sizable, costly and often perceived to be unfair, disadvantageous to SMEs and riddled with a lack of transparency and corruption.

6. The SME landscape in Moldova

The diversity of contexts and local situations of SMEs across the Eastern Partnership region suggests that a one-size-fits-all approach from the side of international donors is not appropriate and that assistance needs to be tailored to national and sub-national contexts and realities. For Moldova, getting the SME sector fit for the DCFTA has brought together a multitude of international and national efforts to improve contextual regulatory conditions, financial opportunities, human capital, training and education for the labour markets and also competitivity and 'innovation spirit' (the Government of Moldova, 2016). Efforts have been made as much about setting up financial opportunities and technical assistance as about changing cultural practices and business norms amongst SMEs, which tend to be reliant on informal practices, soft-corruption and activities based within or on the borders of the grey economy.[2] The Moldovan 'SME Sector Development Strategy 2012-2020' attempts to create better conditions for SMEs and to get them prepared to be able to profit individually and collectively from DCFTA opportunities and in so doing, to get them to play an incisive role in the country's regional, economic and social development (the Government of Moldova, 2016). The national strategy is backed by EU and EBRD schemes, which are angled at comparative objectives.

The various propositions mentioned above regarding the importance of SMEs in transition economies and potential positive effects vis-à-vis democracy, sustainable development and open societies, have huge resonance in the case of Moldova, given that SMEs define the structure of the commercial sector. 99% of private Moldovan businesses are SMEs and almost 60% of the working population is employed in one. Still, as already mentioned, there are specific factors at play in Moldova that complicate and intervene in the capacity of SMEs to play a role in domestic transitions and in advancing adherence to EU conditionality in the context of the DCFTA. Crucially, aside from the implications of state capture, the inherent nature and character of SMEs in Moldova is not suited to positive interaction with the DCFTA. Above all else, adjustment to the DCFTA requires modernisation, which in turn assumes investment, an intellectual capacity to understand new rules of production and of doing business, openness for

[2] Interview with SME Business Advisor, Chisinau, August 2016.

internationalisation, an appetite for entrepreneurship and growth and a willingness and ability to accept short term transition costs in favour of long term benefits.

In relation to their numbers, SMEs in Moldova have not generated substantial wealth creation; Moldovan SMEs only contribute 28% to national GDP (the EU average is 58%) (the Government of Moldova, 2016). What partially explains this is inefficiency and lack of modernisation in production terms. Furthermore, the current evolution of the SME sector in Moldova is not necessarily leading to a parallel rise in employment or salaries nor is it entailing the creation of a more sophisticated or diversified job market. An interim conclusion to be made here is that for SMEs to deliver on their potential as drivers of economic transitions and national resilience structured external assistance and support, aimed at both contextual transformation and individual empowerment and opportunity creation for SMEs, is a necessity.

The small size of SMEs in Moldova is of consequence. 80% of Moldovan SMEs are 'micro' in nature, meaning that they are made up of ten people or less and are most likely family concerns. Moreover, such enterprises tend to reside in lower added-value sectors in labour intensive fields and represent necessity or survival entrepreneurship rather than opportunity entrepreneurship (EC, 2016). Current trends see a winding down of medium and larger SMEs towards a burgeoning number of micro enterprises of the type mentioned above. As entities become micro, they can get lost amidst the already large informal or grey economic sector, which of course means that they are probably not declaring income and capital, paying taxes to the state, nor providing social security for their employees. Going informal, whether by design or not, also heightens the prospect of corruption and bribes being used to secure short-term gains and also reduces the chances that an enterprise would think of its business in terms of investment and long-term strategy.[3]A SWOT analysis of the Moldovan SME landscape suggests the following (Longhurst, 2016):[4]

[3] Interview with SME business advisor, Chisinau, August 2016.

[4] Author's own findings and adapted from Eastern Partnership Small and Medium Enterprises Flagship Paper, http://ec.europa.eu/enlargement/neighbourhood/pdf/riga/20150518_flagship_sme.pdf
Managing Authority Ministry of Regional Development and Public Administration Joint Operational Programme Romania – Republic of Moldova 2014-2020 (Draft) May 2015 www.ro-ua-md.net/wp.../Proiect-Program-ROMD-2014-2020.doc.

STRENGTHS	WEAKNESSES
- SME-friendly national regulatory Frameworks are being put in place - National development strategies are in line with those of the EU and other IOs - Favourable pro-EU domestic environment; DCFTA - Tailored financing schemes for SMEs needs are in place - IOs support local banks for lending to SMEs - Well educated national population with good language skills - Positive cultural attitude to setting up a business - Close to EU and CIS markets[5] - Small SMEs can adapt to market changes and shocks - Mobile and aspirational population - Strength in fields of agriculture and wines - Cheap labour force - EU markets completely open and quota-free for large range of product exports - A small country; borders with the EU - Strong on the ground presence of International Organisations - Very fast internet connection	- Inconsistent implementation of regulatory frameworks, laws and norms - Geo-political problems in the near neighbourhood - Corruption of economic and political systems - Prevalence of micro and small SMEs - Lack of business links and collaboration between small and larger SMEs - SMEs are not integrated into European or international supply chains and produce mainly for domestic markets - Monopolisation of national economy sectors and unfair competition due to ‘state capture’ - Underdeveloped infrastructure for supporting businesses and capital markets - Low level of business culture and vocational training (VET) - Low level of competitiveness; production inefficiencies - Low levels of FDI; investors are cautious - Uneven distribution of enterprises around the country - Low value products and inefficient methods of production - Huge reliance on remittances and international donors - Road and rail networks in need of updates
OPPORTUNITIES	**THREATS**
- International Organisations provide support for SME development - Expanded opportunities for registering and setting up an SME - Opening of EU market for trade via DCFTA - Facilitation of accessing funds for entrepreneurship and investment	- Territorial conflict and proximity to Russia - Instable domestic political system and low public faith in élites - Russian economic and political interference, such as export bans and embargoes

[5] Though currently embargoes are in place.

- Harnessing skills of returning emigrant workers / ploughing remittances into businesses and investments - Improving the positive image of the country EU consumers becoming positively disposed towards Moldova - Growing attention of the state towards problems and needs of the SME sector - Development of investments in public- private partnership - Constant development of internationalisation of the SMEs sector - Development of cluster policies - Constant reform of educational system in the sphere of business and vocational training	- Potential for weakening of pro-EU national development vector - Weak independent media; ownership by oligarch - Brain-Drain of young people; low level of returning emigrants - Growth of the shadow economy - Energy dependence - Slow development of Public-Private partnerships - Slow adaptation of the national educational system to market demands for labour; - Instability of legislative framework and susceptibility to corruption - Fragmented civil society with limited impact on formal politics - Unresolved banking crisis

Source: own representation.

This SWOT analysis issues a complex overall picture and a situation that is very much in transformation and flux. For every strength, there is an almost equal number of weaknesses and though many opportunities are apparent, there are numerous parallel threats and risks.

Accordingly, Moldova’s strength in terms of SME potential is substantial. Crucially, and at least in theory, it has in place the regulatory frameworks and funding mechanisms including access to financial support for SMEs to create a conducive environment. The DCFTA provides for stable market access into the EU for an extremely wide range of Moldovan products without quotas. The detail of the DCFTA also provides a blueprint for enterprises on how to meet EU standards, which in turn will help to ensure their sustainability, boost efficiency and capacity to play a role in Moldova’s transition. Further positive synergy is created by the fact that Moldovan national development strategies dovetail neatly with the visions of the EU and other International Organisations. Indeed, the Association Agreement with the EU and the DCFTA are cross-referenced in national strategies. That Moldova is a small state bordering directly with the EU bodes well for export potential and easy logistics. Meanwhile, the fact that there is a well-educated and relatively cheap work force in place implies that SMEs could become more sophisticated in nature and move into more specialised, high-tech and added value industries. Countering these strengths, there are multiple weaknesses that revolve around corruption and the prevalence of informal practices that cast doubt on the actual implementation of regulations in a systematic fashion. Furthermore, though the country does have decent connectivity, the road and rail networks are in need of modernisation so as to begin to get Moldova linked to European and International transport and supply chains (East Invest, 2016).

In terms of opportunity, the most crucial remains the potential offered by the DCFTA. The agreement provides the script and directions for Moldovan stakeholders to engage, and there is plenty additional support (financial and technical) for SMEs to rise to the occasion. Indeed, since 2009 SMEs have gained significantly more attention from international donors and the Moldovan government in the context of the Eastern Partnership, its flagship initiative and 'East Invest'. Alongside the domestic reform agenda aimed at improving the local business environment, there have been efforts to overcome the apparent miss-match between education, both formal and non-formal, and the immediate and projected needs of the job market. Higher Education provision and VET (vocational education and training) have been largely incompatible with the emerging needs of the job market and manifestly so in relation to the implications for the employment sector stemming from the DCFTA and Association Agreement.[6] A disconnection between the needs of the job market and importance of capacity building in the SME sector and the skills and attributes of young people presents a sizable source of threat to the potential of SMEs (and public sector organisations) and to the implementation of the DCFTA.

7. Conclusion: time for a re-focusing of priorities

The fundamental argument of this paper is that the implementation of EU policies and specifically the DCFTA in the Republic of Moldova is set back by the domestic political, economic and social conditions equivalent to 'state capture'. Second, it was asserted that SMEs are prime stakeholders in the DCFTA but their chances of benefitting are hindered not just by problems at the macro level, but also by the very nature and character of the sector. Despite a combination of national and international efforts to lever SMEs into the DCFTA, it is apparent that such strategies are not yet bearing fruit. This is vital to note since, as the recent Presidential election has demonstrated, the political conditions in Moldova are always on the move, the European path of development should not be taken for granted and critically, that oligarchs will retain a firm grip on national life. By way of a conclusion, the paper will present ideas for a re-focusing of SME policies.

[6] Interview with employment and training expert, Chisinau, August 2016.

Encouraging Ways Out of the Grey Zone

Lowering the entry and, just as importantly, re-entry costs and associated burdens for SMEs of going formal, streamlining tax and customs procedures for inexperienced entrepreneurs, reducing the time and simplifying the procedures involved in setting up a business and providing more generous and empathetic 'second chance' opportunities for people who failed or went bankrupt after their first business endeavour should be key priorities. Equally, micro SMEs that opted to join or just fell into the grey zone need to be incentivised to move into the formal business arena - this is essential if they are to participate in the DCFTA in terms of modernisation and trade as well as to contribute to the national economy. Of course, the question of finance is always pertinent. However, evidence suggests that it is not a question of finance per se, but rather of 'access to finance'. The financial resources are in place, but getting access to them is where the problem rests. Small and micro SMEs, in particular, do not normally have the financial literacy and capacity to apply for loans. Neither do they necessarily have a positive disposition towards the very idea of taking out credit, nor a belief that they should have an investment strategy. Stronger efforts and hands-on mentoring by IOs, but also local entrepreneurs can build capacity in this vital area.

Constructive Use of Remittances

The better or more constructive use of remittances sent by Moldovans working abroad is already being promoted. It is mostly the case that remittances stay in private hands and get ploughed into building houses, kept for daily expenses or saved up in private accounts for rainy days. Declaring remittances, paying taxes on them and, most importantly, investing into domestic businesses should be encouraged more fiercely by international financial institutions as a means to enrich local SMEs and create more of a sense of responsibility for strengthening Moldova's overall economic welfare on the part of migrant workers. Such a transformation will only occur if generous incentives, such as co-financing and guarantees, are laid out and if migrant workers believe that the country is a good investment, that the banking sector is sound and that they will not just be throwing good money away.

More Clustering and Cooperation

Small and micro SMEs are the most numerous in Moldova, but are the least blessed with substantial investment potential, know-how or capacity to benefit from economies of scale. The Government and international organisations already actively encourage businesses to collaborate, to create shared capacities or 'clusters' for production and storage, for example, with the effect of reducing the costs associated with investment and DCFTA-relevant modernisation. Such efforts need to multiply, as without effective clustering, the SME sector will neither be able to latch on to new opportunities for trade, modernise, nor encourage FDI. A related area that needs to be addressed is that of intra-sectoral cooperation. As already noted, evidence suggests that there is a lack of cooperation between smaller and larger SMEs, to the detriment of the sector and its potential as a whole. Efforts should be placed on nurturing links, which will ensure that small and micro SMEs have a better chance at internationalisation and at becoming a part of new trade opportunities.

The Question of Entrepreneurship and Labour Resources

As to whether an entrepreneurship spirit or culture exists in post-communist Moldova and whether it can flourish independently of external stimuli and support still remains an open debate that needs further substantiation. It was mentioned above that the EU and other IOs also have a keen eye on employment, especially youth employment and the nexus with the education system at all levels: from school, to VET and formal Higher Education. Evidence points to the need to prioritise around the issue of human resources and to ensure that 'employability' is secured as an integral aspect of the learning curricula (European E-Competence Framework, 2016). More specifically, there is a need for business and entrepreneurship training at all levels of the education system so that a generation of young people equipped with knowledge and expertise could be able strengthen the Moldovan SME sector and consequently, the sustainable development of the country and national resilience. A first priority should be to align VET priorities and qualifications with national reform strategies, the provisions of the EU Association Agreement and the DCFTA. By doing this, a work force able to help with the implementation of such policies in practical and technical terms can be created.

All in all, as long at the Republic of Moldova remains straightjacketed by 'state capture', the fundamental reforms needed for the full implementation of the DCFTA will be elusive. Ultimately, it is the persistence of a monopolistic oligarchy, which perpetuates structural corruption, weak government and politicised institutions that runs against the efficient and sustained absorption of EU norms and regulations (Sekarev, Antsu and Maniokas, 2016). Theory and history shows us that SMEs play a vital role in the creation of open societies and the breaking down of Soviet style structures but, for a multitude of reasons discussed in this paper, Moldovan SMEs are not yet able to perform such a role. The upshot of this is that the implementation of the DCFTA will continue to be limited.

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