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**The present form of the study is transitional. It contains information collected by the author so far during the fellowship program. No chapter included in this draft can be considered as final form.**

# **TOBACCO POLICY IN MOLDOVA AND THE ROLE OF CIVIL SOCIETY**

## **INTRODUCTION**

According to the data of the National Centre for Preventive Medicine smoking is rather widespread in Moldova: 46.2% of adult men and 6.2% of women, 11.6% of boys and 3.2% of girls of school age smoke. Cardio vascular diseases are the leading cause of death in the country. Thus, 212709 of patients with cardio vascular diseases were registered in 2000 and 22732 deceased in the result of these diseases. The epidemic of tobacco smoking began in the country 5-7 years ago.

Approximately 3 years ago Moldovan market was invaded by aggressive tobacco advertising, which slightly decreased in 2001 when parliament adopted the law on tobacco providing certain limitations on tobacco advertising. BAT attempted to organize the first educational campaign targeted at youth in 2001. Hot debates in parliament and press about tobacco industry became frequent recently, which is connected with the upcoming privatization of the largest tobacco producer of Moldova – “Tutun CTC”. Monitoring of press publications about tobacco which has been conducted by the author of the project during the last 2 years clearly demonstrates the existence of tobacco lobby, which in most cases has been successful in preventing tobacco control policy initiatives.

Government and parliament occupy a “two faced” position regarding tobacco control issue. On the one hand, tobacco industry is one of the few industries still functioning in the country, and all efforts should be done to support it. On the other hand, Moldova is striving for becoming a full member of the EU, which imposes certain limitations and requirements to introduce tobacco control measures and tobacco import control. Hence, the law on tobacco is also “two faced”. For instance, the law prohibits street, radio and TV tobacco advertising, but advertisements in press are legal. Moldova takes part in the discussions of the Framework Convention on Tobacco Control. Although the country occupies a “waiting” position preferring not to express any opinion, by the time of the treaty signing Moldova will have to make a choice.

Research of the tobacco policy in Moldova will cover the following directions: study of public documents of the parliament (verbatim records of parliamentary sessions and special committees meetings, history of the revision of legislative initiatives, adopted tobacco related laws), monitoring of publications about tobacco in the 18 leading newspapers of the country; establishing of contacts with NGOs advocating tobacco free society or able to advocate, establishing of contacts with medical institutions, whose direct duty is health advocacy among population including antismoking advocacy; survey conducted among representatives of the above mentioned institutions and journalists writing on economy and health. Such a survey will help to learn their opinion about tobacco control policy and governmental activity in this area.

The main goal of the research is to analyze peculiarities of elaboration of tobacco policy in Moldova, to evaluate the sincerity of governmental declaration of the intention to control tobacco, to investigate supporters and opponents of tobacco control policy, to establish the role of foreign tobacco producers, particularly BAT, in the formation of this policy and public opinion about it.

Knowledge of these issues will let us elaborate recommendations on participation of various governmental institutions and NGOs in tobacco control policy advocacy in the country.

### COUNTRY BACKGROUND

**Geography and climate.** Moldova is one of the newly independent European states. Situated between the Danube, Prut and Dnestr rivers, Moldova occupies a territory of approximately 33,800 square kilometers. It borders Romania in the west and Ukraine in the north, east and south. Its central region is the Bessarabian Plateau with forested and mountainous highlands up to 400 meters in elevation. The principal rivers in Moldova are the Dnestr and the Prut. The country has a temperate continental climate similar to Western Europe. Black soil rich in humus predominates in the country. An extremely favorable combination of climate and soil creates necessary conditions for high crops of cereals, grapes, tobacco, fruit and vegetables.

**Population.** Moldova is one of the most densely populated European countries (about 127 pers./sq.km). As of January 1, 1999, Moldova's population was estimated at approximately 4, 3 million. Approximately 65 per cent. of the population is Moldovan, with other ethnic groups comprising a substantial proportion of the population. These include ethnic Ukrainians (approximately 14 per cent. of the population), ethnic Russians (13 per cent.) and the Gagauzi (a Christian Turkic ethnicity) (3.5 per cent.). The official language is Moldovan, which is identical to Romanian, although Russian is also widely spoken.

Moldova has 60 cities and towns and more than 1,600 villages. More than 33 per cent of the urban population is concentrated in the capital of Chisinau.



***Political situation.*** Moldova is, after Armenia, the smallest former Soviet republic in terms of territory. Throughout its history it was subject to frequent invasions and changes, but the Republic's core is the territory between the Prut and Dneestr rivers, with the historical name of Bessarabia. The medieval principality of Moldavia, large parts of which are now incorporated into Romania and Ukraine, was for much of its history under Austro-Hungarian or Lithuanian rule. In the course of the 16th century, it fell under Turkish suzerainty but was eventually annexed by Russia in 1812. After Russia's defeat in the Crimean War, part of Moldova's territory, southern Bessarabia, was lost to Romania, but Russia recovered it again at the Congress of Berlin in 1878. In 1918, Russia lost Bessarabia to Romania, and in 1924 the Soviet Union formed the Moldavian Autonomous Socialist Republic on the eastern side of the Dneestr (which was at the time populated mainly by ethnic Ukrainians) and refused to recognize Romania's claim to Bessarabia.

The Republic of Moldova proclaimed its independence on August 27, 1991. During eight years of independence the political situation has remained stable. On July 29, 1994 the Constitution of the Republic of Moldova was adopted. This was a major historic step for the Republic. It placed the country on the road to democracy and free market economy. The Constitution stipulates that the guideline for the country economy “is a market economy, socially oriented, based on both private and public ownership, involved in free competition”.

On March 2, 1992, the Republic of Moldova joined the United Nations Organization as a full member. The same year, Moldova joined the International Monetary Fund and the World Bank Group. On March 16, 1994, it signed the NATO initiative “Partnership for Peace”. The Partnership and Cooperation Agreement (PCA) between the Republic of Moldova and the European Communities, on the one hand, and its Member States, on the other hand, came into force on July 1, 1998.

***Economic policy.*** After the break-up of the Soviet Union, Moldova was affected by a sharp deterioration of the external trade, loss of traditional markets, disruption in payments and trade relations. The 1992 and 1994 droughts and the Transnistrian conflict in 1992 compounded the adverse effects on output. As a result, the real GDP declined by more than 50% between 1991 and 1994.

The main change in the economic policy of Moldova has taken place after 1993. This year marked the borderline between the state-dominated and market oriented economy. This period followed after the important events of 1990-1992: liberalization of prices, commerce and enterprise operations, adoption of the first set of laws establishing the market economy (laws regarding ownership, privatization, Land Code, etc.), entry into new markets.

The “big bang” in the transition from one model of social, political and economic development to another was marked during 1993-1995. This was the period when the mass privatization program was implemented, the National Bank of Moldova initiated credit auctions, the new national currency was introduced and its stability maintained. The situation of the economy in 1996/97 could be described as a “stable depression” which, under the impact of external and internal pressures, led to a crisis.

The pace of structural reform implementation was slowed down and an economic growth did not occur (in 1995 the GDP fall reached 1.4%, in 1996 – 7,8%). A modest increase in the output was recovered in 1997 (+1,6%), for the first time since independence. After Russia’s 1998 crisis, Moldovan export to CIS countries dropped more than twice and consequently, the GDP decreased 8,6% in 1998. Real GDP continues to decline in 1999 as well. With a GDP of 1440 USD per capita

according to PPP, the Republic of Moldova became one of the poorest countries in Europe. The UNDP Human Development Index ranked Moldova on 104th place among all 174 countries.

The Ranking List of the World Bank posted Moldova on the 94th place amongst 133 countries in terms of GDP per capita, including it in the group of 63 “low-income economies”. According to the evaluation presented in the UNDP Human Development Report (1999) about 90% of the population of Moldova have incomes less than US\$ 2 per day, whereas the income discrepancy between the wealthiest 10% and the poorest 10% reached 15.4-fold (in 1993 7.0-fold).

The average inflation rate was reduced from 1184% in 1993 to 30% in 1995, 24% in 1996, 12% in 1997 and 7.7% in 1998. As a consequence of Russia’s financial collapse of 1998, the average inflation rate has reached 35-40% in 1999 and it is estimated to be around 13-15% in 2000.

## **STATE OF MARKET DEVELOPMENT**

**Level of foreign trade liberalization.** Moldova has a liberal trade regime with a low import tariff (6,8% in 1997, 4,3% in 1998, 4,2% in 1999 and an offer to join WTO - 8,8%). Imports of machinery and equipment for production purposes are tax exempted as well as exports of goods and services. In Moldova there are no quantitative restrictions and licensing on export-import transactions. The country trade policy is based on the “small open economy” principle. Moldova has taken a number of steps to improve its trade regime and to facilitate international trade by developing trade relations with Europe and North America. European Union has granted privileges to Moldova which are described in GSP (Generalized System of Preferences). The United States has granted the most-favored-nation status for Moldova. It has moved to strengthen trade relations with its traditional trading partners by signing free trade agreements with Romania and former SU countries, including Russia.

In addition, as a member of the International Monetary Fund, Moldova has been operating according to Article 8 of the IMF Article of Agreement, allowing full current account convertibility. There are no controls on the repatriation of dividends and profits, though registration for the export of currency is required.

***Market entry/exit barriers.*** In the Republic of Moldova there are favorable conditions for the local and foreign companies’ establishment and operation. The Moldovan Law “On foreign investments” is one of the most progressive among transition countries, according to expert assessments. The main obstacle to establish and operate both local and foreign companies is the high level of bureaucracy, corruption and shadow economy. According to “Transparency International Report” the corruption index for Moldova reached 7 (max-8). In the mentioned report, the Republic of Moldova has the same index like Bulgaria, and are ranked after Romania, followed by the Ukraine. The average for EU varies around 2,5.

The high level of corruption leads to the growth of the black market. The black market index (Heritage Foundation) is varying from min. (1) to max. (5). The black market index for Moldova as well as Bulgaria, Latvia and Lithuania equals 4.

The high level of bureaucracy conditions an aspiration to regulate various spheres of economic activity. The Law "On Licensing of Activity" provides for licensing of 106 kinds of activity. 21 public administration bodies and mayoralities of municipalities, cities, and villages issue such licenses. The number of kinds of activity for regulation and the bodies issuing licenses should be reduced.

The yearly research of the Heritage Foundation (USA) shows that the Index of Economic Freedom (IEF) for Moldova significantly improved in the first half of the '90s (price and trade liberalization, quality of monetary policy, openness of the country to foreign investments, etc.). The rating of the country rose from the 148<sup>th</sup> to the 96<sup>th</sup> place among 156 reviewed countries. However, during the recent three years, the IEF has remained unchanged – 3.35.

Starting from the spring of 1999, the young reformers – liberals, who have to carry out an open, transparent and understandable program of reforms, are trying to make a U-turn in improving conditions for establishing and operating of business.

**Privatization.** Since the beginning of the '90s, three privatization programs were adopted and implemented. The first one – based on National Patrimonial Bonds (NPB) - in 1993-1994, the second - mixed privatization for Bonds and cash - in 1995-1996, and, finally, privatization for cash exclusively in 1997-1999. At present, the last program has been extended till 2001. “Moldova implemented one of the most rapid and comprehensive mass privatization schemes in the former Soviet Union” (Transition Report, EBRD).

Enterprise privatization in Moldova has taken place through a variety of methods: mass privatization against NPB, cash privatization of small-scale enterprises and cash privatization of middle and large-scale enterprises, including sale by tender of large companies. Privatization in the first two categories has been very rapid and has been completed by now. As a result, the private sector in GDP grew from 30% in 1995 to 45% in 1998. The private sector then accounted for 70% of the retail trade and services, 60% of industrial output, and 44% of construction and transport activity. The private sector's share in the employed varied from 50% to 80% across sectors (Transition Report, EBRD).

To speed-up privatization, on August 2nd, 1999, the Government of Moldova, announced an open international tender for the privatization of electricity distribution companies. Also, the Government is preparing papers to privatize strategically important sectors of telecommunication, wine and tobacco production.

The first stage consists of a simultaneous privatization of the electricity distribution companies and it should be completed by the end of 1999, while the second stage consists of a simultaneous privatization of the combined heat and power production plants to be finished by March 2000. The privatization tender shall provide for 100% transfer of shares of the distribution companies. The controlling portfolio of the privatized combined heat and power production plants shall be determined by the auction committee but shall not be less than 50% +1 of the total shareholders' portfolio of these companies. Privatization of the telecommunication, wine and **tobacco production** plants should be completed by the end of 2000.

## **POLITICAL DEVELOPMENT**

In spite of the slow progress of the democratic transformations in the Republic of Moldova, its political institutions have had a positive evolution. The European and international observers have not remarked serious deviations from the norms and standards of a democratic society. In July 1994, the Parliament of the Republic of Moldova adopted the new Constitution of the country that establishes a semi-parliamentary regime of governing, appropriate as a form of the majority of the semi-parliamentary regimes. The Venice Commission gave a positive assessment of the new Constitution text and of the functioning of the political institutions from the Republic of Moldova. The evaluation given by Strasbourg at the moment of Moldova's adherence to the Council of Europe on July 13, 1995, could serve as a good example in this respect.

As regards the problem of ethnical minorities, the Republic of Moldova is a rare exception from the South-Eastern Europe. It has not been cited in a negative context at European institutions (Council of Europe, OSCE), even though the minority population represents 35% of the country's population. The inter-ethnic conflict from the south of the Republic of Moldova that began in 1989 was completely solved in 1994 through granting a large autonomy to the Gagauz minority. Besides, the transnistrean conflict is a conflict that has been qualified as a geopolitic conflict. Some issues concerning the Bulgarian minority appeared at the end of 1998. Bulgarian communities were reluctant to be included in the Cahul County, demanding to establish a separate ethnic county - Taraclia.

However, there are issues concerning the respect of human rights and functioning of the independent judiciary system. The Council of Europe has contacted Chisinau several times concerning the respect of some commitment made in this relation at the moment of the Republic of Moldova's admission to the Council of Europe. Some of the issues were the maintaining of the state prosecution and the modification of the Civil and Criminal Codes. The human rights issues are in most cases raised in the context of the serious social and economic situation in the country (salaries and pensions arrears, penalties for non-payment of utilities in the conditions of the non-payment of salaries and others). ODILL has also raised the issue concerning the situation of the detainees and police actions.

In spite of all these facts, the Republic of Moldova, on the general background of the East-European and South-East European context, has had incomparably fewer human rights and minority issues raised by European and international bodies, as well as issues related to the functioning of political and judiciary institutions.

**Civil Society: current state.** Civil Society, the sphere of local initiative, social movements, non-governmental organizations, is an arena for civic virtue. This sphere is crucial for the stability and consolidation of a new democratic state as it promotes liberty and responsibility, generates alternative political options and information processes, produces new leaders etc.

The right of association represents one of the basic human rights stipulated in the Universal Declaration of Human Rights (1948), the International Pact on Civil and Political Rights (1966) and European Convention of Human Rights (1950). The Republic of Moldova has subscribed to all these international treaties, assuming the obligation to guarantee this right to all its citizens. Unfortunately, the right to associate in voluntary organizations, distinct from political ones, (that is socio-political associations and trade unions) is not stipulated in the Moldovan Constitution. According to Article 4, the state only ensures the creation of conditions suitable for the establishment and operation of NGOs.

The civil society in Moldova has insufficient practice of self-organization due to the long tradition of totalitarian administration. The current and future challenges for the NGO sector in Moldova are to overcome the funding dependency, to decrease the urban concentration and to strengthen the sector internally and externally.

In Moldova, there are around 1300 registered NGOs. Less than a third of them carry out concrete activities, most of them exist just nominally. Almost 75% - 80% of all registered NGOs are capital-based. Although the number of NGOs established in the rural areas has increased in the last year. The awareness of the role of NGOs among population is low - the larger part of citizens knows almost nothing about civil society. The impact of the NGO sector on the society is still insignificant.

The government does not provide enough effort and willingness for co-operation with NGOs, although promises were given at the highest level. The relationship NGO - business is sporadic and almost unknown to the public.

**Source: Republic of Moldova: National Strategy for South East Europe. Chisinau, 1999**

## **TOBACCO CULTIVATION AND CIGARETTE PRODUCTION IN MOLDOVA: BRIEF OVERVIEW**

The agricultural policy is of great concern for Moldova, the country with a high level of agricultural production and food industry (about 40% of GDP). 54% of the population live in rural areas and more than 40% of human resources are involved in the agricultural sector. Aspiring to integrate into the EU, the Republic of Moldova should develop an agricultural policy in correspondence with the EU Common Agricultural Policy.

The main objectives of Moldovan Agricultural Policy are:

- increasing competitiveness internally and externally
- ensuring food safety and food quality, which are both fundamental obligations towards consumers;
- ensuring a fair standard of living for the agricultural community and contributing to the stability of farm incomes;
- promotion of sustainable agriculture and the integration of environmental goals;
- creation of alternative job and income opportunities for farmers and their families.

Prior to the implementation of a new agricultural policy, the transfer of agrarian land into the private ownership should be completed. This process has been recently activated thanks to the USAID technical assistance and within a year it will be practically finished. In addition a clear and transparent system of state subsidies to the agricultural sector should be adopted pursuing the EU countries' experience.

**Tobacco Leaf and Tobacco Fermentation.** Moldova has a long tradition of producing semi-oriental tobacco, the basic ingredient used in the production of "American blend" type of cigarettes. Under the FSU, Moldova's tobacco was produced mainly by the kolkhozes; according to the Ministry of Agriculture, there were some 450 farms involved in tobacco cultivation, about half the total number of kolkhozes. Cigarette production first began in Moldova in the 1920s, with the creation of *Tutun* factory in Chisinau. The introduction of industrial fermentation processes in the 1970s, which replaced seasonal fermentation, led to a significant increase in the output of tobacco leaf and fermented tobacco, and made Moldova the largest supplier of tobacco in the FSU, with about one-third of total output by the early 1980s. By then, Moldova was selling more than three-quarters of its fermented tobacco to the rest of the USSR. *Tutun* cigarette factory also underwent rapid growth in the late 1970s, when Philip Morris was invited to bring in new technology and equipment. Cooperation with Philip Morris, which last until the early 1980s, resulted in better quality brands, improved packaging and the introduction of Virginia and Burley varieties of tobacco and flue-curing barns. As a result of these developments, Moldovan tobacco and cigarettes had an excellent market throughout the USSR.

Tobacco has consequently been a very significant activity in the Moldovan economy. By the middle of the 1980s, Moldova was using 77,000 hectares to produce some 120,000 tons of semi-oriental tobacco. At that time, approximately one-quarter of Moldova's population was earning at least some of its income from the sector; and tobacco provided almost 20% of government revenue

and the export of fermented tobacco and cigarettes made up a significant share of the republic's sales to the rest of the USSR. However, the industry began to lose ground in the late 1980s, and by 1990, tobacco leaf production had halved, to 66,000 tons, wholly because of a fall in acreage.

Since Independence in 1991, tobacco production has declined dramatically, falling to less than 20,000 tons in 1996, although Moldova remains the third largest (behind Kyrgyzstan and Azerbaijan) producer of leaf tobacco within the former SU. The decline of production was caused mainly by the break-down of the former production and marketing arrangements resulting from the dismantling of the USSR, and was accentuated by the sluggish and ineffective reforms in the agricultural sector between 1991 and 1995, rising costs of energy, reductions in the use of fertilizers and pesticides, and farm gate prices for tobacco leaf that were well below world prices. The decline in tobacco production was somewhat more severe than the overall decline in agricultural output, which is estimated to have fallen by 56% between 1990 and 1996.

Since 1996, production of tobacco has arrested the decline and begun to recover slowly. However, with the end of the protected market that Moldova enjoyed within the USSR, profit rates for tobacco leaf are now under pressure from competitors in such countries as China, Philippines, Azerbaijan and Italy that have entered the regional market in recent years and are able to offer similar tobacco at comparable prices. In 1998, the government adopted a Program for Development of the Tobacco Sector for 1998-2003 designed to increase output of tobacco to 80,000 tons by 2003. The Ministry of Agriculture planned to create a development fund to finance investments in seed production and drying and to finance pre-cultivation expenses of farmers, in the expectation that some 140 million lei would be available under the 2001 budget for the tobacco sector. In the middle of 2002 it became clear that the program was failed and the Parliament entrusted the Government with elaboration of a new Program for Development of the Tobacco Sector for 2003-2010.

Major Indicators of Tobacco Production, 1990-2000

Year	Cultivated Area ('000 ha)	Output ('000 tons)	Yield (q. per ha)
1990	32.1	66.4	20.6
1991	31.5	65.0	20.0
1992	28.1	45.0	15.1
1993	31.2	50.0	16.1
1994	28.4	42.0	14.9
1995	20.0	25.0	12.6
1996	16.3	19.0	11.4
1997	17.2	24.0	13.7
1998	21.8	24.0	11.2
1999	18.5	21.0	11.4
2000			10.2

While tobacco production has begun to recover gradually, the first-level of tobacco processing, fermentation, has experienced deteriorating circumstances over the past years. In part, the fortunes of the fermentation plants have declined along with the production of tobacco, but their performance has worsened as a result of the break-up of the vertically-integrated industry in 1998. When the individual fermentation plants were corporatized in 1998, it does not appear that they were furnished with sufficient working capital for them either to pre-finance farmers for cultivation of tobacco or to purchase the tobacco crop. Moreover, prior to the break-up of the industry, the fermentation plants were having their output marketed for them, but following the split-up in 1998, there had to develop their own export marketing strategies. In 1999 the fermentation plants, which employed some 1,500 workers, had approximately 82,000 tons of nominal capacity. In addition, private sector fermentation enterprises appeared to be emerging, in the form of small factories that



have been licensed to introduce an alternative drying/fermenting technology that uses less energy, developed by the Institute of Tobacco.

**Cigarette Production.** Cigarette production in Moldova has varied between 7 billion and 10 billion sticks over the past decade. Almost all the production has been from *Tutun Cigarette Plant*, which has always been able to finance from retained earnings sufficient supplies of domestic tobacco and imported tobaccos<sup>1</sup>. However, *Orhei Fermentation Plant* also has some capacity to make cigarettes, which was installed in 1992 and consists of *Skoda* machines able to make about 1 billion sticks per annum. The plant procured new equipment for cigarette production, as part of its joint venture with a Cyprus-based company, with the intention of producing low-cost brands for the domestic market.

Cigarette Production, 1992-2000 (billion sticks)

	Unit	1992	1993	1994	1995	1996	1997	1998	1999	2000
Tutun CTC	b. sticks	8.5	8.8	8.1	7.1	9.7	9.5	7.5	8.7	
O/w for export	m. sticks							144.0	84.0	
Orhei plant	m. sticks	n.a.	n.a.	n.a.	n.a.	0.0	0.0	0.0	45.4*	
TOTAL										

\* Orhei restarted cigarette production, after a hiatus of three years, in September 1999, and sold 45.4 million sticks in the four months, earning 1.4 million lei.

Cu privire la activitatea industriei Republicii Moldova în ianuarie-mai 2003\*

În perioada de raport s-au înregistrat creșteri ale volumului producției industriale față de ianuarie-mai 2002 la întreprinderile cu următoarele activități:  
fabricarea produselor de tutun (cu 11%);

Volumul producției în prețuri curente, mil. lei	Indicii volumului producției, %: ianuarie-mai 2003 față de ianuarie-mai 2002 în prețuri:		Informativ: ianuarie-mai 2002 în % față de ianuarie-mai 2001 în prețuri medii ale anului precedent			
	curente	medii ale anului precedent				
Fabricarea produselor de tutun		158,7		128	111	60

<http://www.statistica.md/statistics/?g=388&id=227>

**Tobacco Exports.** Over the last decade, tobacco has continued to be a significant earner of foreign exchange for Moldova, in spite of the decline in production and the loss of traditional business partners after the dismantling of the FSU. The share of production exported has varied annually between 60% and 95%.

Tobacco Exports, 1994-2000

	Units	1994	1995	1996	1997	1998	1999	2000
Total Exports	m. \$	565.5	745.5	801.6	874.1	632.1	471.4	

<sup>1</sup> The factory has imported between 1,500 and 3,000 tons of aromatized tobacco used for local blends. It also has its own fermentation plant, and has been able to finance production and procurement of all the domestic tobacco it needs for its own cigarette production.

Agricultural exports	m. \$	391.7	538.8	593.0	641.4	466.6	307.7	
Tobacco exports	m. \$	25.9	22.0	27.1	23.8	28.5	33.7	13.1
	Tons	30,694	25,560	20,878	14,190	16,236	21,891	9,180
	Price (\$ per ton)	844.6	862.0	1,298.4	1,679.4	1,757.4	1,539.0	1,431.5
	% of agricultural exports	7.0	4.0	5.0	4.0	6.0	11.0	
	% of total exports	5.0	3.0	3.0	3.0	5.0	7.0	
Tobacco exports to CIS	m. \$	21.2	18.7	18.6	17.5	26.9		
	Tons	24,829	21,148	14,825	10,230	15,260		
	Price (\$ per ton)	852.3	882.8	1,252.6	1,715.4	1,764.3		
Tobacco exports to other countries	m. \$	4.8	3.4	8.5	6.3	1.6		
	Tons	5,865	4,412	6,053	3,960	976		
	Price (\$ per ton)	811.9	762.2	1,410.7	1,586.1	1,649.6		

By 1999, benefiting from a substantial and sustained increase in average export price<sup>2</sup>, it was the third largest agricultural sub-sector in terms of exports, behind beverages and processed vegetables and fruits. By far the largest market for Moldovan tobacco has continued to be Russia, which bought some 88% of all tobacco exported by Moldova in 1999. Some of the exports are in the form of fermented tobacco, but a significant amount is exported as unprocessed tobacco. This is because; although far more fermentation capacity exists than is required at current levels of tobacco production, the fermentation plants simply do not have the financial ability to finance the purchase of the entire crop. In addition, the existence of the excise tax may have persuaded some farmers to sell their tobacco leaf elsewhere.

***Cigarette Markets and Consumption.*** Domestic consumption of cigarettes is reported to have been approximately 5 billion sticks (250 million packs) per annum over the past five years. Aggregate consumption has remained fairly stable because falls in disposable income have resulted in consumers generally switching to cheaper brands rather than reducing their smoking. While the trends in disposable income have resulted in a surge in the sales of cheap local brands, such as “Jok”, in which *Tutun* has had a strong market position, in the long term the market is moving towards the imported “American blend” brands. According to *Tutun*, it sells between 3.5 billion and 4 billion sticks on the domestic market, including its own new “American blend” brands that it has introduced in the recent past. This means that imports account for the other 1 billion to 1.5 billion sticks, and currently it is estimated that almost all of the imported cigarettes on offer in Moldova are smuggled. This also means that some 4-5 billion sticks are exported by *Tutun*, mainly to Russia and Ukraine, but also in increasing amounts to Romania.

The trends towards cheaper brands in the past few years conceal a longer-term trend away from such brands, not only in Moldova but also in Moldova’s export markets. The opening of markets in the FSU to international brands and the purchase of cigarette plants in neighboring countries by the large global producers, like British American Tobacco (BAT) and Philip Morris will change both

<sup>2</sup> Reflecting an increase in the international demand for semi-oriental tobacco that is used for production of American-blend cigarettes, the highest growth segment of the industry.

the market into which Moldovan cigarettes are sold and also the extent and nature of competition for the market. These developments will lead to greater pressure to tighten specifications for nicotine and tar content in tobacco, provide products that meet the international industry standards and to constantly reduce production costs and increase efficiency. Whether or not the Moldovan tobacco industry is to be privatized, it is now a player in an international market.

**Ownership and Privatization Developments.** The tobacco sector has experienced a substantial amount of institutional change and restructuring since 1991, including various privatization proposals. Prior to independence, the tobacco sector in Moldova had operated a vertically-integrated system under state control. Beginning in 1991, the early attempts at land reform and farm restructuring began to break up this system. Between 1991 and 1995, there was slow progress in privatizing land and agriculture, but the pace accelerated dramatically after January 1996, when the constitutional court ruled that various Land Code provisions were unconstitutional, thereby clearing the way for faster privatization. By the end of 1997, the state owned only 18% of agricultural land, compared to 100% before independence, and most of its holding was in the Reserve Fund

Production of tobacco leaf has already been privatized in Moldova to the largest extent. With the break-up of the kolkhoz and distribution of land, tobacco is now being produced primarily on private farms. Typically, tobacco is grown on corporate farms which produce numerous other crops, since tobacco needs to be cultivated as part of a multi-year crop rotation in view of its effect on soil fertility. According to statistics quoted by the National Agency for Tobacco Development at the end of December 2002, there are just under 196 farms currently growing tobaccos.

By contrast, the eight fermentation plants and the cigarette plant have remained predominantly state-owned. All these enterprises went through the voucher privatization program in 1992-1994, and as a result, between 3 and 9% of their shares are now in the hands of management and workers. The voucher privatization was meant to be a first step in the overall transformation of ownership and restructuring of the industry. In 1993, *Tutun S.A.*, the national tobacco monopolist, started looking for joint ventures or other forms of cooperation with international firms. Initial attempts were made to re-establish cooperation with Philip Morris, but it was reported that the company was not interested, and approaches were made by *Tutun* to BAT and Reemtsma<sup>3</sup>. In July 1995, the Parliament approved a plan for the reorganization and privatization of the tobacco industry, which provided for the establishment of a joint venture with foreign participation, corporatization of the tobacco enterprises and their privatization through an international tender. Subsequently, the government transformed the tobacco enterprises into a joint-stock company named *Tutun S.A.*

In 1996, an international tender was issued, inviting proposals for the purchase of a 60% stake in the *Tutun* cigarette factory and all the fermentation plants as one unit. Two bidders, BAT and Reemtsma, responded. Details of exactly what happened are skimpy, but it has been reported that Reemtsma was initially selected on the basis of an offer to invest \$59 million. After BAT made a counteroffer of \$61 million, the government annulled the agreement with Reemtsma, and invited further bids after indicating that it might be prepared to divide up the enterprises into various lots. It has been reported that BAT subsequently raised its bid to \$71 million, but that negotiations broke down, after the government's tender committee introduced new conditions. In February 1998, the government approved a Program for Development of the Tobacco Sector for 1998-2003. The overall objective of the program was to increase tobacco output to 80,000 tons by 2003, with government providing financial assistance for seed production and improved drying. This program provided for:

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<sup>3</sup> In May 1994, a joint venture agreement between Reemtsma and Tutun was announced, involving a \$40 million investment in cigarette manufacturing and tobacco cultivation, but it never materialized.

- Split-up of *Tutun* S.A. into separate companies;
- Corporatization of the companies;
- Development of new individual projects for privatization of the companies;
- Prohibition of the export of non-fermented tobacco; and
- Introduction of an upper limit for the price of fermented tobacco at 120% of the price on unfermented tobacco.

By the end of 1998, the split-up of *Tutun* and corporatization of the newly established companies was completed. In early 2000, the government introduced a proposal to sell all the remaining state-owned shares in the fermentation plants and *Tutun*. This proposal was rejected by Parliament. Subsequently, a group of parliamentary deputies have reformulated the proposal; the modified proposal envisages the sale of 51% of the shares in each enterprise to a strategic investor and the sale of further shares to workers and management up to a limit of 15%, with the state retaining ownership of the remaining 34%.

During next two years Parliament and Government changed the conditions of tobacco industry privatization several times. This entailed very serious consequences for relationship between Moldova and Monetary Fund.

Meanwhile, the governance of these plants has become increasingly problematical for the government. In 2000 the WB mission, on the basis of the information that it collected during its visit, concluded that governance of the processing enterprises was a major problem in Moldova. In WB experts' opinion, "the fact that the tobacco sector remains, even at its historically depressed levels of output and sales, a significant generator of cash has led to a wide range of activities and behaviors that can be captured under the term "corruption". Although the state is the major shareholder in *Tutun CTC* and the fermentation plants, it does not appear that the government can impose its authority easily on the enterprises". In support of such conclusion the experts provided the example of *Tutun CTC*: "...first, it has been reported that the financial accounts for 1999 are incomplete and that there are no audited accounts for the enterprise for 1998, and no action has been taken on the State Audit Office's findings of irregularities in audits of earlier years' accounts; second, while the mission was in Chisinau, the factory reported in the press that it was establishing a joint venture with *Seita*, a French company, apparently without informing its Board; third, there are regular reports that both inputs and outputs for cigarette production are channeled through intermediary companies, owned by political groups and other individuals, presumably with the intention of siphoning off the company's cash; and fourth, the tax payments made to the budget by *Tutun* seem to be determined by negotiations between the factory and the Ministry of Finance rather than in accordance with the tax code".

In WB experts' opinion, "the end-product of this process of politicization and corruption will inevitably be the impoverishment of the industry and the enrichment of those individuals and groups who now exercise effective control; eventually, the government can look forward to being handed an "empty shell" with few assets and many liabilities. This process, which has been seen to varying extents in many transitional economies, has been aptly summarized as "privatization of profits, socialization of losses". That is why the experts supposed that "privatization of the industry, and installation of owners who are risking their own money, could put an end to the activities described above".

The tobacco industry privatization has his supporters and opponents. This problem is not solved till now and from time to time a flow of denunciations and exposes befalls to the readers from Moldavian mass media.

**Source: Republic of Moldova. World Bank Supervision Mission. Tobacco Sector Aide-Memoire. Chisinau, 2000**