



Study supporting the ex-post evaluation on Macro- Financial Assistance operations to the Eastern Partnership countries of Moldova, Georgia and Ukraine (2017-2020)

Final Report

19 April 2024

Submitted to:

Directorate-General for Economic and Financial Affairs (ECFIN)



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A report submitted by [ICF S.A.](#)

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List of abbreviations

AA	Association Agreement
ACN	Anti-Corruption Network
ADA	Austrian Development Agency
ADB	Asian Development Bank
AEO	Authorised Economic Operator
AfD	Agence Française de Développement
AIIB	Asian Infrastructure Investment Bank
ALMP	Active Labour Market Policies
AML	Anti-Money Laundering
AMLD	EU Anti-Money-Laundering Directive
ANRE	National Energy Regulatory Agency
BEPS MLI	Multilateral Convention to Implement Tax Treaty Related Measures to Prevent
CARA	Criminal Assets Recovery Agency
CFT	Counter-Terrorist Financing
CoA	Court of Accounts
CRD	EU Capital Requirements Directive
CRF	Crisis Recovery Facility
CRR	EU Capital Requirements Regulation
CSO	Civil Society Organisation
DCFTA	Deep and Comprehensive Free Trade Agreement
DG	Directorate-General
DG GROW	Directorate-General for Growth
DG JUST	Directorate-General for Justice and Consumers
DG NEAR	Directorate-General for Neighbourhood and Enlargement Negotiations
DPL	Development Policy Loan
DSA	Debt Sustainability Analysis
EaP	Eastern Partnership
EBRD	European Bank for Reconstruction and Development
ECA	European Court of Auditors

ECFIN	Directorate-General for Economic and Financial Affairs
EEA	European Economic Area
EEAS	European External Action Service
EFC	Economic and Financial Committee
EFF	Extended Fund Facility
EIB	European Investment Bank
EnC	Energy Community
ENP	European Neighbourhood Policy
ENPARD	European Neighbourhood Programme for Agriculture and Rural Development
EP	European Parliament
ESRA	Economic Stimulation in Rural Areas
EU	European Union
EUACI	EU Anti-Corruption Initiative
EUR	Euro
FATF	Financial Action Task Force
FDI	Foreign Direct Investment
FSDPL	Financial Sector Development Policy Loan
GDP	Gross Domestic Product
GEL	Georgian Lari
GIZ	Gesellschaft für Internationale Zusammenarbeit
GNI	Gross National Income
GRECO	Group of States against Corruption
HACC	High Anti-Corruption Court of Ukraine
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IFI	International Financing Institution
IMF	International Monetary Fund
KfW	Kreditanstalt für Wiederaufbau
MDL	Moldovan Leu
MFA	Macro-Financial Assistance

MoU	Memorandum of Understanding
MP	Member of Parliament
MPTL	Motor Third Party Liability Insurance Law
NABU	National Anti-Corruption Bureau
NAPC	National Agency for Prevention of Corruption
NAPR	National Agency of Public Registry
NASC	National Complaints Settlement Agency
NBG	National Bank of Georgia
NBM	National Bank of Moldova
NBU	National Bank of Ukraine
NCFM	National Commission for Financial Markets
NCTS	New Computerized Transit System
NGO	Non-Governmental Organisation
NHSU	National Health Service of Ukraine
NIA	National Integrity Authority
NIAS	National Integrity and Anticorruption Strategy
NPL	Non-Performing Loan
NQF	National Qualifications Framework
OA	Operational Assessment
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OLAF	European Anti-Fraud Office
PAR	Public Administration Reform
PAS	Party of Action and Solidarity
PEFA	Public Expenditure and Financial Accountability
PES	Public Employment Service
PFM	Public Finance Management
PPP	Public-Private Partnership
RCF	IMF Rapid Credit Facility
RFI	IMF Rapid Financing Instrument

SAPO	Specialised Anti-Corruption Prosecutor's Office
SBA	IMF Stand-by Arrangement
SBA	Stand-By Agreement
SDR	Special Drawing Rights
SFS	State Fiscal Service
SIA	Social Impact Analysis
SMEs	Small and Medium-sized Enterprises
SOE	State-Owned Enterprise
TFEU	Treaty on the Functioning of the European Union
ToC	Theory of Change
UAH	Ukrainian Hryvnia
UBO	Ultimate Beneficiary Owner
UHC	Universal Healthcare System
UNDP	United Nations Development Programme
UNM	United National Movement
US	United States
USAID	United States Agency for International Development
USD	US Dollars
USSR	Union of Soviet Socialist Republics
VET	Vocational Education Training
VLAP	Visa Liberalisation Action Plan
WB	World Bank

1 Introduction

This is the Final Report for an independent, external ex-post evaluation on the Macro-Financial Assistance (MFA) operations to the Eastern Neighbourhood Countries of Moldova, Georgia and Ukraine (2017-2020).

This evaluation covers three MFA operations¹ to Eastern Neighbourhood countries, namely:

- MFA II operation to Moldova (Decision (EU) 2017/1565);
- MFA III operation to Georgia (Decision (EU) 2018/598);
- MFA IV operation to Ukraine (Decision (EU) 2018/947).

The Final Report provides a comprehensive and separate analysis for each country covered under the evaluation criteria, as well as standalone analyses (Social Impact Analysis (SIA), Debt Sustainability Analysis (DSA)). It is complemented by a cross-country analysis that examines the three operations comparatively, and a regional analysis. It is accompanied by a standalone annex report.

1.1 Structure of the report

The Final Report is structured as follows:

- Section 2 provides an overview of the key economic and political developments in Moldova, Georgia and Ukraine during the period leading up to the MFA requests and during and after the European Union (EU) MFAs were implemented. It also provides a detailed description of the main characteristics of the MFA operations;
- Sections 4, 5 and 6 present the evaluation findings for Moldova, Georgia and Ukraine, respectively;
- Section 7 describes the comparative assessment and the regional analysis;
- Section 8 presents conclusions and lessons.

The report is supported by several annexes:

Part A: Procedural annexes

- Annex 1 Procedural information
- Annex 2 Methodologies of data collection and analysis, limitations and challenges
- Annex 3 Synopsis report
- Annex 4 Evaluation framework
- Annex 5 References

Part B: Standalone analytical outputs

- Annex 6 Indicators database
- Annex 7 Background information
- Annex 8 Detailed description of the macroeconomic outcomes
- Annex 9 Debt sustainability analysis (DSA)
- Annex 10 Social impact analysis (SIA)
- Annex 11 Case studies
- Annex 12 Detailed comparison of MFA, International Monetary Fund (IMF) and World Bank (WB) conditionalities
- Annex 13 Classification of MFA conditions and condition-by-condition tables
- Annex 14 Cost-benefit analysis (CBA)

¹ The name/ numbering of the operations do not reflect the full history of MFA operations – there were previous MFA operations in these three countries.

2 Rationale and background to the intervention

This section presents the political and economic context for the MFA operations in Georgia, Moldova, and Ukraine.

2.1 Political and economic context for the MFA operations

Political context

Launched in 2009, the **Eastern Partnership (EaP)** is a joint policy initiative that aims to deepen and strengthen relations between the EU, its Member States, and its six Eastern neighbours: **Armenia, Azerbaijan, Belarus², Georgia, Moldova and Ukraine**. The EaP is underpinned by a shared commitment to international law and fundamental values (democracy, rule of law, respect for human rights and fundamental freedoms) and to the market economy, sustainable development, and good governance.

The EaP has since evolved. In 2014, '**Association Agreements**' and '**Deep and Comprehensive Free Trade Areas**' (AAs/DCFTAs) were concluded between the EU and the so-called '**Association Trio**' of **Georgia, Moldova, and Ukraine**. The agreements aimed to bring about strengthened political association and economic integration. More recently, in May 2021, the three countries signed a **Memorandum of Understanding (MoU)** between their Ministries of Foreign Affairs to further dialogue on matters of common interest, notably their joint advancement towards EU membership. The Trio also committed to working collaboratively on transport, digital transformation, green energy/economy, justice and home affairs, strategic communications, and healthcare.

Apart from their desire to mutually support and coordinate their work on European integration, the three countries share another important commonality – **unresolved/ongoing territorial conflict with Russia** (see Box 2.1). Only Ukraine is currently involved in an active military conflict with Russia.

Box 2.1 Territorial disputes with Russia



The roots of the Russia-Georgia conflict go back to the early 1990s, when both Russia and Georgia were newly independent nations after the dissolution of the Union of Soviet Socialist Republics (USSR). Civil war erupted within Georgia when two provinces – South Ossetia in eastern Georgia, and Abkhazia, on the north-western coast – sought to declare their own independence. Conflict in the breakaway regions of Abkhazia and South Ossetia was largely backed by Russia. Following the 1991-1992 South Ossetia War, South Ossetia unilaterally declared independence from Georgia on 29 May 1992. Abkhazia declared its independence after its war with Georgia in 1992-1993. Its constitution was adopted on 26 November 1994. In the years that followed, neither Abkhazia nor South Ossetia was recognised as an independent country, with tensions between Russia and Georgia remaining high (notably in Abkhazia and South Ossetia). These tensions were further heightened when President Mikheil Saakashvili came to power in Georgia in 2004 and vowed to regain control of the separatist regions of Abkhazia and South Ossetia.

In 2008, war broke out involving Russian and Georgian forces in South Ossetia. The legacy of this short war – lasting just five days – also had a profound impact on the unresolved Georgian-Abkhaz conflict. In the aftermath, Russia and several other nations officially recognised both Abkhazia and South Ossetia as independent states. Russia also stationed military bases in both territories. In

² In June 2021, Belarus unilaterally suspended its participation in the EaP.

addition, Russia is pursuing the tactics of ‘borderisation’ or ‘creeping occupation’ of the Georgian territories by moving demarcation lines along disputed borders deeper inside Georgian territory³.

Moldova

The breakaway region of Transnistria is a post-Soviet ‘frozen conflict’ zone. With Russian backing, Transnistria fought a war against Moldova in the early 1990s. The war has left Transnistria with de facto independence and a permanent Russian garrison. It remains an unrecognised breakaway state (and is still internationally recognised as part of Moldova). Russian state media – widely available in Transnistria – is believed to have played a significant role in cementing pro-Russian attitudes in the enclave, while Moldova continues its shift towards the West under the leadership of its current liberal/pro-EU president.

Ukraine

Russia's hybrid warfare against Ukraine has been ongoing since February 2014. Incursions into Ukrainian territory ultimately led to Russia's annexation of Crimea in March 2014, followed shortly afterwards by the beginning of the war in the Donbas region between Russian-backed separatists and Ukrainian state forces. Over the years, the conflict was accompanied by several naval incidents, cyberwarfare, and heightened political tensions. Throughout 2021, bilateral tensions rose due to Russian military build-up around Ukrainian territory. On 24 February 2022, Russia invaded Ukraine. This caused Europe's largest refugee crisis since World War II, with millions of Ukrainians fleeing the country and one-third of the population being displaced.

Macroeconomic context

Economic context before the MFA operations (2014-2016)

In the wake of Russia's illegal annexation of Crimea in 2014 and the subsequent military conflicts in Eastern Ukraine, the Eastern Partnership countries—Moldova, Georgia, and Ukraine—faced profound economic shocks that reverberated through the region. These events marked a significant geopolitical shift, exacerbating existing vulnerabilities and introducing new economic challenges that would shape the trajectory of these nations' relationships with the European Union and their broader economic policies.

For Ukraine, the annexation of Crimea and the conflict in the east had direct and severe economic repercussions. The nation experienced a sharp depreciation of the Ukrainian hryvnia, which in turn fuelled rampant inflation. This inflation was not only a result of the currency's fall but also due to hikes in administrative prices, including for essential utilities like gas and heating. The ongoing conflict and the perceived instability of Ukraine's investment climate led to a significant reduction in foreign direct investment, further straining the country's economic resources.

Moldova faced a series of economic setbacks during this period, notably from 2014 to 2016. A trade ban imposed by Russia from 2013 to 2015 and a major bank fraud scandal in 2014 severely hampered economic growth and stability. These events undermined trust in Moldova's financial institutions and economic governance, complicating its path toward economic recovery.

Georgia felt the ripple effects of regional instability, through the depreciation of lari (GEL) (inflating its foreign-dominated external debt). This underscored the fragility of its economic

³ Parliamentary Assembly of the Organization for Security and Co-operation in Europe (OSCEPA), ‘Human rights leaders deeply concerned about the continued “borderisation” process in Georgia and its impact on local residents, Press release, 22 August 2019, <https://www.oscepa.org/en/news-a-media/press-releases/press-2019/human-rights-committee-leaders-deeply-concerned-about-the-continued-borderization-process-in-georgia-and-its-impact-on-local-residents>

recovery and the necessity of robust support from international partners, including the EU, to safeguard against external economic pressures.

The MFA operations subsequently launched by the EU were a response to these crises. Box 2.2 presents the key macroeconomic developments observed in the three countries from 2010-2016.

Box 2.2 Macroeconomic developments observed in the three countries

		
Georgia	Moldova	Ukraine
<ul style="list-style-type: none"> ■ Between 2010 and 2013, real GDP growth recorded for Moldova and Georgia was almost on par, averaging almost 6.0% <ul style="list-style-type: none"> ➢ Tourism inflows and high levels of public investment contributed to renewed economic growth in Georgia, while in Moldova, a strong rebound in agriculture and related industries, private consumption, and exports contributed to its initial recovery ■ However, neither country was able to sustain the rapid growth experienced in the mid 2010s <ul style="list-style-type: none"> ➢ In Georgia, weaker private investment (reflecting increased business/investor uncertainty ahead of the October 2012 parliamentary elections) reduced FDI, and lower government spending contributed to a slowdown in growth. Real GDP grew by an average of 3.4% during the period 2014-2016. ➢ In Moldova, output growth started to moderate from 2014 onwards, averaging around 3.0%. This was mainly due to a slowdown in agriculture and related industries and weaker economic activity in main trading partners (particularly Russia and Ukraine). Additionally, over the period 2014-2016, Moldova's current account deficit widened to about 6.0% of GDP⁴, driven by a slowdown in export growth and a decline in remittances 	<p>The situation in Ukraine became significantly more critical compared to its neighbours after 2014 due to geopolitical tensions.</p> <ul style="list-style-type: none"> • severe GDP contraction: The Ukrainian economy faced dramatic declines, with GDP dropping by 6.6% in 2014 and further plummeting to 9.8% in 2015. • impact of conflict: These declines were largely a result of the annexation of Crimea by Russia and the ongoing armed conflict in the eastern regions. • industrial production slowdown: Industrial sectors such as metallurgy, chemicals, and machine building experienced substantial slowdowns, exacerbating the economic downturn. • fiscal and monetary challenges: The period was also marked by reduced government spending and a tighter monetary policy enforced by the National Bank of Ukraine (NBU), which contributed to the economic strain. • inflation and currency volatility: The conflict and political instability led to significant inflation and depreciation of the Ukrainian hryvnia, further destabilizing the economy. • decrease in foreign investment: The uncertain security and economic environment resulted in a notable reduction in foreign direct investment, impacting economic recovery prospects. 	

⁴ World Bank data, <https://data.worldbank.org/indicator/BN.CAB.XOKA.GD.ZS?locations=MD>

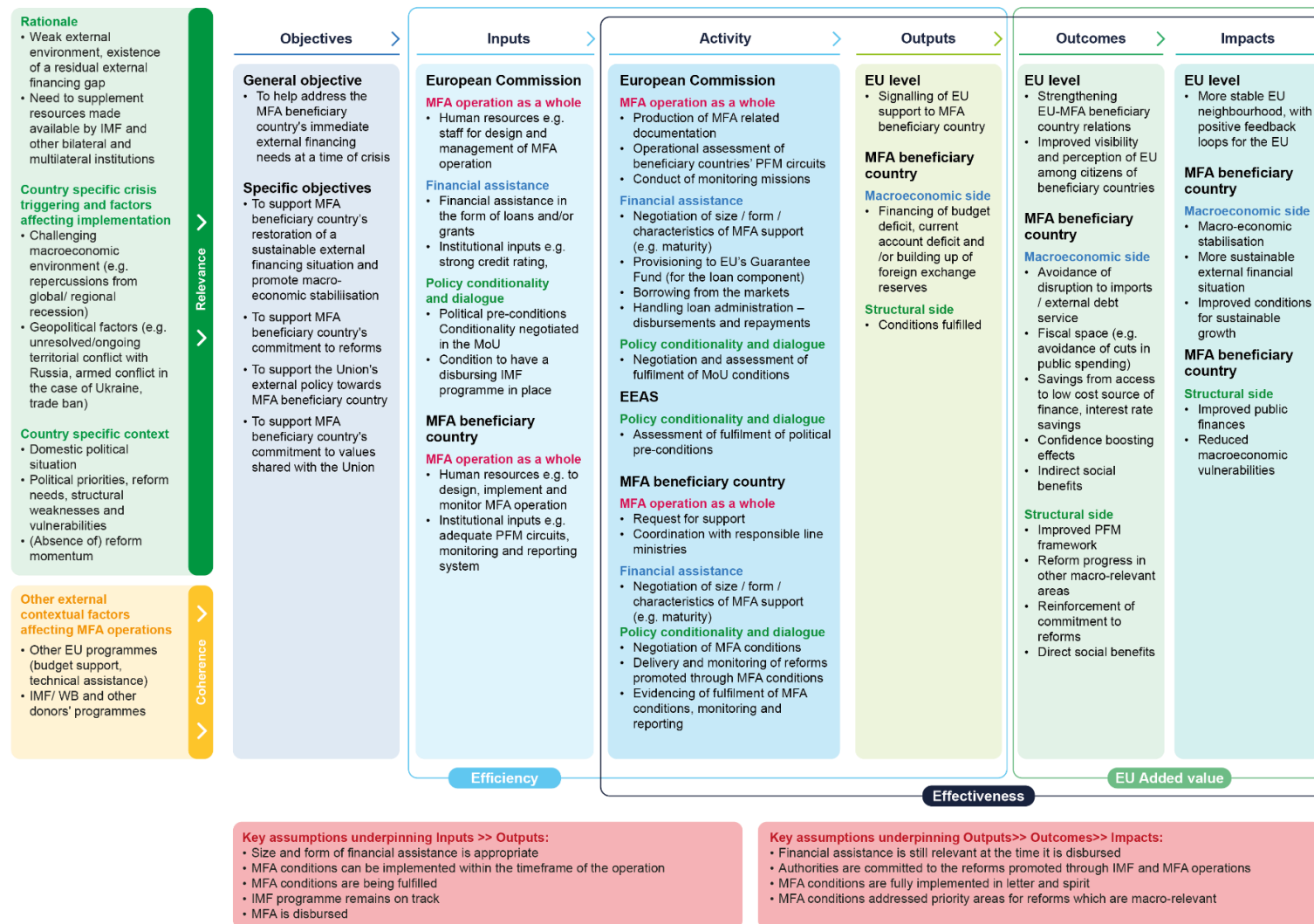
2.2 Design and implementation of the MFA operations to the EaP countries of Moldova, Georgia and Ukraine (2017-2020)

Theory of change for the MFA instrument

The theory of change (ToC) in Figure 2.1 illustrates the mechanics of the MFA instrument as a whole and displays how these MFA operations were expected to: (i) support the restoration of sustainable external financing for MFA beneficiary countries (in conjunction with resources made available under the concurrent disbursing IMF programme); and (ii) support the national authorities' reform programme. It shows the expected outcomes and impacts from MFA operations for the beneficiary country and also at EU level. It clearly identifies key underlying assumptions and other external factors potentially influencing the direction and scale of changes.

The ToC does not, however, depict the logic behind the concrete design choices for each of the three operations (e.g. size, form, specific conditions). A high-level mapping of individual conditions' intervention logic is presented separately for each country/operation in the following sub-sections.

Figure 2.1 Theory of change for the MFA instrument



Source: ICF elaboration

Moldova

MFA II design

Following a request by the Republic of Moldova and following lengthy initial discussions, on 13 January 2017, the European Commission adopted a proposal for an MFA programme (MFA II) of up to EUR 100 million, of which up to EUR 40 million would be provided in grants and up to EUR 60 million in loans. MFA II represents an important moment in which the EU provided support to a neighbouring country left reeling after a major bank scandal. The beginnings of the operation were compromised by the cancellation of the mayoral elections in the capital city Chisinau and the first instalment of EUR 30 million was released only in October 2019. The second instalment of EUR 30 million was released in July 2020. The third and final instalment of the programme was cancelled, as the availability period of the programme ended in July 2020.

All disbursements under MFA programmes are tied to political preconditions of respect for democratic mechanisms, the rule of law and human rights, as well as to the beneficiary country's track record under the IMF programme and the fulfilment of the specific policy conditions laid down in the MoU. Here, these political preconditions were paid particular attention in the evaluation, as their non-fulfilment put the operation on hold twice.

The 28 conditions of MFA II (a large number for an operation of its size) reflected political processes on the EU side and recognised that the granting of the MFA assistance was not an obvious choice and safeguards were required. Somewhat unusually, the first instalment was contingent on conditions being met. The 28 MFA conditions emphasised stabilising and improving the banking system, improving public administration and the judiciary system, unbundling the energy sector so as to mitigate social damage, and battling corruption through better laws, law-making processes, procurement processes, public participation, and e-government.

Table 2.1 presents the expected outputs and outcomes from Moldova's MFA conditions, by reform area.

Table 2.1 Expected outputs and outcomes of Moldova's 28 conditions, by reform area

Input: conditions as per the MoU, by reform area	Output	Outcome
Public sector governance (five conditions: #1, #2, #3, #4, #13)	<ol style="list-style-type: none"> 1. New Law on Government adopted by the parliament (#1) 2. New National Complaints Settlement Agency adequately resourced (#2) 3. New Law on State and Municipal Enterprises adopted by the parliament (#3) 4. New law on the Court of Accounts adopted by the parliament (#4) 5. Public Accounts Committee created within the parliament (#4) 6. Amendments to the Law on Public Procurement, the law on Public-Private Partnerships (PPPs) and the Law on Utility Companies submitted to parliament (#13) 	<ol style="list-style-type: none"> 7. Rationalisation of the central public administration (#1) 8. Increased effectiveness of public procurement system (#2) 9. Increased transparency and accountability in state-owned enterprises (SOEs) (#3) 10. Increased independence of the Supreme Audit Institution (#4) 11. Increased parliamentary oversight of the government's budget execution (#4) 12. Better regulation of the concessions, PPPs and procurement by utility companies (#13)
Fight against corruption and	<ol style="list-style-type: none"> 13. New Law on the Prevention of Money Laundering and Counter Terrorism 	<ol style="list-style-type: none"> 21. Appropriate regulatory and institutional framework for an effective fight against

Input: conditions as per the MoU, by reform area	Output	Outcome
<p>money laundering (six conditions: #5, #6, #7, #14, #22, #23)</p>	<p>Financing adopted by the parliament (AML/CTF) (#5)</p> <p>14. Office for the Prevention and Fight against Money Laundering (#5)</p> <p>15. Resourcing the National Integrity Authority adequately resourced (#6)</p> <p>16. Criminal Asset Recovery Office set up and adequately resourced (#7)</p> <p>17. Regulation clarifying the methodology for the verification of asset declarations and conflicts of interest adopted by the National Integrity Authority (NIA) (#14)</p> <p>18. Operational asset declaration and verification system (#14)</p> <p>19. Actions foreseen for 2017 in the Action Plan accompanying the National Integrity and Anticorruption Strategy (NIAS) implemented (#22)</p> <p>20. Progress report on the implementation by the authorities of the asset recovery strategy submitted to parliament (#23)</p>	<p>money laundering and terrorism financing (#5, #6, #7, #14, #22)</p> <p>22. Recovery of the funds from banking fraud scandal (#23)</p>
<p>Energy sector (five conditions: #8, #15, #16, #24, #25)</p>	<p>23. New Law on Energy adopted by the parliament (#8)</p> <p>24. New Law on Energy Efficiency submitted to parliament (#15)</p> <p>25. Tender organised for the selection of a general contractor for the construction of the Ungheni-Chisinau gas pipeline (#16)</p> <p>26. Revised eligibility criteria for the Ajutor Social and Heating Allowance programmes and adequate resourcing (#24)</p> <p>27. Progress in implementation of the Action Plan for the legal and functional unbundling of the three system operators in the gas sector (#25)</p>	<p>28. Strengthening the governance and regulatory framework of the energy sector (#8)</p> <p>29. Pursuing energy efficiency objectives (#15)</p> <p>30. Diversification of Moldova's gas supplies and promotion of energy interconnectivity with the EU (#16)</p> <p>31. Protection of the most vulnerable households from the adjustment in energy tariffs (#24)</p> <p>32. Development of competitive and open electricity and gas markets (#25)</p>
<p>Business climate and DCFTA implementation (seven conditions: #9, #10, #17, #18, #26, #27, #28)</p>	<p>33. Nomenclature reviewed by the Ministry of Economy; reduced number of required permits and licences (#9)</p> <p>34. New Customs Service Law adopted by the parliament (#10)</p> <p>35. Revised criteria for the selection and the promotion of judges (#17)</p> <p>36. Amendments to the law of Disciplinary Liability of Judges adopted by the parliament (#18)</p> <p>37. Amendments to the Law on Competition (to include media sector) proposed by the government (#26)</p> <p>38. New Customs Code, consistent with the EU Customs Code, adopted by the parliament (#27)</p> <p>39. Primary and secondary legislation to strengthen the position of the Superior Council of Magistracy (SCM) adopted by the parliament (#28)</p>	<p>40. Reduction in the administrative burden of starting and operating a business (#9)</p> <p>41. Strengthening customs system (#10, #27)</p> <p>42. Increased competition (#26)</p> <p>43. Strengthening effectiveness, independence and accountability of judiciary system (#17, #18, #28)</p>
<p>Financial sector governance (five conditions: #11, #12, #19, #20, #21)</p>	<p>44. New Law on Banking Activity and Prudential Supervision of Banks and Investment Firms adopted by the parliament and substantial progress towards the adoption of secondary legislation (#11)</p> <p>45. Action Plan for the audit of all insurance companies and for the identification of ultimate beneficiary owners (UBOs) of</p>	<p>49. Alignment of the regulatory framework for banks with international and EU standards and promotion of financial stability (#11)</p> <p>50. Enhancement of the governance and shareholder transparency in the insurance and banking sectors (#12, #19)</p>

Input: conditions as per the MoU, by reform area	Output	Outcome
	<p>qualified shareholders in all insurance companies adopted by the National Commission for Financial Markets (NCFM) (#12)</p> <p>46. Identification of UBOs of qualified shareholders completed by the National Bank of Moldova (NBM), diagnostic analyses of related party lending concluded in all banks and recommendations of these diagnostic analyses followed up (#19)</p> <p>47. Amendments to the Deposit Insurance Law strengthening the deposit insurance system adopted by the parliament (#20)</p> <p>48. Law on non-bank credit organisations submitted to parliament (#21)</p>	<p>51. Strengthening the deposit insurance system (#20)</p> <p>52. Sound development of the non-banking financial sector (#21)</p>

Notes: #XX refers to the condition number set in the MoU linked to the **first instalment**, **second instalment**, or **third instalment**.

Implementation timetable

Figure 2.2 presents the timeline and main milestones of MFA II, alongside other key developments (political/economic developments, other MFA operations, IMF assistance). Moldova officially requested financial assistance twice, first in August 2015 and again in March 2016. The MFA II was approved by the European Parliament (EP) and the Council in September 2017, after a time lag of more than a year⁵. On the EU side, the scale of the operation and reform needs, the poor implementation track record, and, above all, concerns about financial governance of the country were the main factors slowing the decision-making process. As such, the adoption of MFA II came five years after the fulfilment of the previous programme (MFA I). The Loan Agreement and MoU⁶ were signed in November 2017 and ratified by the national authorities in January 2018.

Political preconditions were unfulfilled several times during implementation, with the operation repeatedly put on hold. The first hold occurred in July 2018, meaning it took almost two years from signature of the MoU for the first disbursement of EUR 30 million to be made (in October 2019). The second hold occurred two months later, in December 2019. Eight actions were subsequently defined in Spring 2020 to unblock the operations (see Box 2.3).

Box 2.3 Political short-term actions 2020

Action 1 - Setting up an international joint investigation team to recover the assets from the banking fraud

Action 2 - Formally joining the Organisation for Economic Co-operation and Development (OECD) anti-corruption network (ACN) peer-to-peer monitoring programme, and formally participating in the 'EU for Integrity' regional programme

Action 3 - Adoption of the Law on Anti-Money Laundering sanctions by the parliament, in line with EU directives and Moneyval recommendations

⁵ Decision (EU) 2017/1565 of the European Parliament and of the Council of 13 September 2017 on providing macro-financial assistance to the Republic of Moldova, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32017D1565>

⁶ MoU between the EU and the Republic of Moldova for Macro-Financial Assistance of up to EUR 100 million, https://economy-finance.ec.europa.eu/international-economic-relations/candidate-and-neighbouring-countries/neighbouring-countries-eu/neighbourhood-countries/moldova_en

Action 4 - Extending the moratorium on the Citizenship for Investment programme until the provisions on programme in the Law of Citizenship are repealed. Committing publicly to repeal the programme

Action 5 - Launching a step-by-step consultation among political parties and other stakeholders to prepare a clear strategic concept on necessary changes in the judicial sector

Action 6 - Adopting the Draft Law on Non-Commercial Organisations in the version registered by the government, without the problematic provisions on limiting foreign funding and political activities and on government control over the functioning of civil society organisations (CSOs) introduced by parliament

Action 7 - Launch independent peer reviews (independent audits) of the activity in the last two years of the Audio-visual Council and the Competition Council

Action 8 - Amending the Law on the Superior Council of Magistracy in line with European standards, the Council of Europe's anti-corruption body, Group of States against Corruption (GRECO) reports, and Venice Commission recommendations. Pause the selection of lay members of the Superior Council of Magistracy and introduce sufficient safeguards in the selection process to ensure transparent, credible and non-partisan selection of lay members

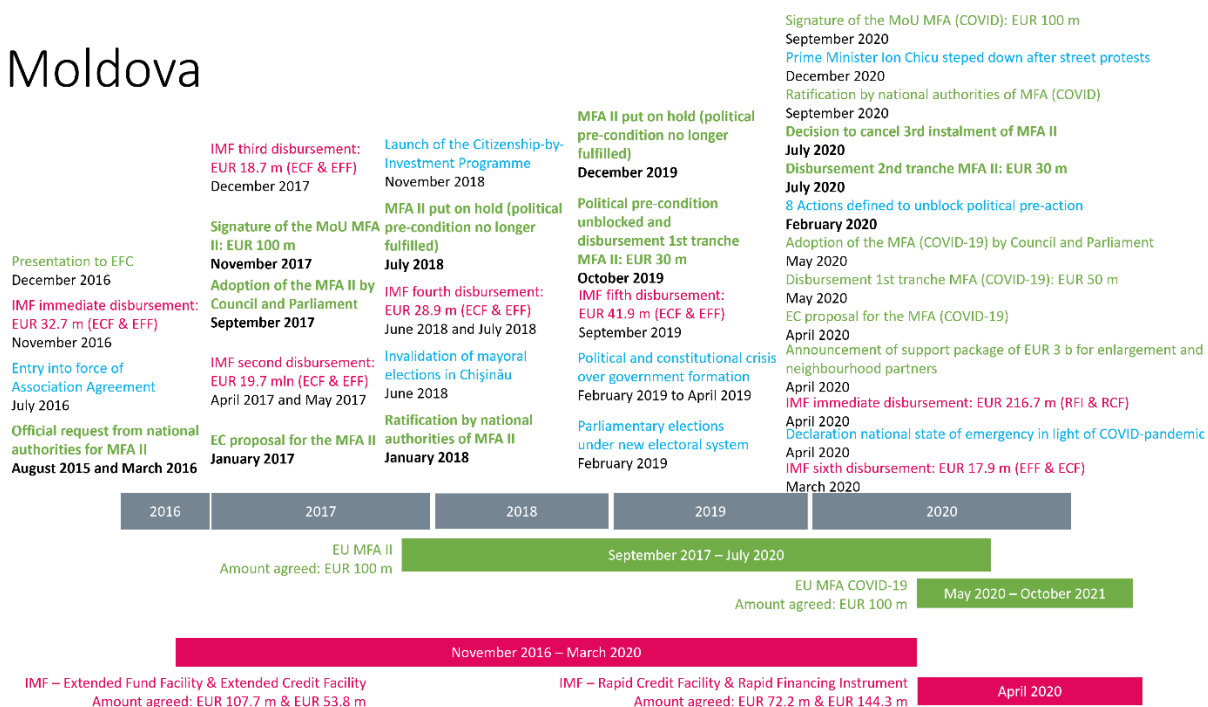
Moldova's successful compliance with the short-term actions allowed the second disbursement (EUR 30 million) to be released in early July 2020. The third and final disbursement was cancelled by the European Commission after the expiry of the availability period at the end of the same month (July 2020), leaving EUR 40 million undisbursed. While when the first tranche was put on hold in 2018, the IMF also halted disbursements, IMF support continued during the second interruption 2019-2020, resulting in a certain desynchronisation of the programmes. None of the interviewees (Commission or government) noted any related issues, however.

An MFA in the context of the COVID-19 pandemic was approved in May 2020, overlapping with available period of MFA II by six months. MFA COVID-19 falls outside the scope of this evaluation. As part of that package, the EU agreed on an MFA programme of EUR 100 million to Moldova. The first instalment of EUR 50 million was disbursed on 25 November 2020. The second and final instalment was disbursed on 8 October 2021, successfully completing the programme.

A new MFA programme (ongoing) was requested by the authorities in 2021. Initially amounting to EUR 150 million, the Commission has proposed that this MFA programme be augmented as part of an effort to help Moldova to address its urgent financing needs stemming from the heavy economic impact of Russia's war of aggression against Ukraine and the ongoing energy crisis since October 2021. The EU proposed to increase the MFA operation for Moldova by EUR 145 million, of which EUR 100 million would be disbursed in loans on concessional terms and EUR 45 million in grants. It would be disbursed in two additional instalments subject to new policy conditions being added to the MoU. The first additional instalment was disbursed in October 2023, while the second additional disbursement has not yet taken place as of the date of publication.

Figure 2.2 Implementation timeline for Moldova

Moldova



Source: ICF elaboration

Progress with reforms

Box 2.4 summarises the Moldovan authorities' progress in implementing MFA II conditionalities. It is derived from documents provided by the European Commission's Directorate-General for Economic and Financial Affairs (DG ECFIN) and insights from interviews. Annex 13 provides a more detailed overview of implementation status, by condition.

Box 2.4 Progress on reforms

Of the conditions, 24 out of 28 were considered fulfilled within the agreed timeframe. There was significant progress in various sectors of Moldova's governance and economy. In the financial sector, reforms such as the enactment of the Law on Banking Activity and amendments to the Law on Capital Markets strengthened prudential supervision and risk management. Efforts by the NCFM saw Moldova's banking sector align with EU standards, enhancing its stability. In terms of public sector governance, reforms include the establishment of the National Complaints Settlement Agency (NCSA), adoption of laws governing state and municipal enterprises, and improvements in the organisation of the Court of Accounts. However, some challenges remain, including issues with staffing levels in the NCSA and public administration reforms.

Efforts to combat corruption and money laundering advanced, with the implementation of laws and action plans. Nevertheless, technical deficiencies persist, particularly in due diligence processes. The establishment of the Criminal Assets Recovery Agency faced resource constraints. Asset recovery tied to the 2014 banking fraud was not possible.

In the energy sector, laws were enacted to improve efficiency and infrastructure, although challenges regarding regulatory independence persist, as noted by the 2021 Energy Community (EnC) implementation report. A tender was also organised for the Chisinau-Ungheni pipeline. The

unbundling of the three primary gas system operators was not completed, although *Vestmoldtransgaz* was privatised and sold to a Romanian operator.

Business climate reforms led to a reduction in permits and licences and the introduction of the successful One Stop Shop mechanism. However, further legislative action is needed, such as adopting a Customs Code consistent with EU standards and enacting laws to limit membership terms in judicial bodies. Moldova also adopted the Customs Service Law in December 2017, providing the legal foundation for improving the Customs Service's human resource management and administrative capacity. The parliament has yet to adopt a Customs Code consistent with the EU Customs Code.

Georgia

MFA design

MFA III to Georgia constitutes the third operation since the military conflict with Russia in August 2008. The first two operations were implemented between 2009-2010 and 2015-2017, respectively, having been pledged by the EU at the International Donors' Conference in Brussels in October 2008.

The third operation was requested in June 2017, one month after the last disbursement under MFA II and several months after the agreement with the IMF on a three-year Extended Fund Facility (EFF) (dating from April 2017). All MFA operations to Georgia were broadly the same size (EUR 45 million for MFA III, EUR 46 million for each of the first two). MFA III prioritises the loan element (EUR 35 million) while MFA I was solely grants and MFA II was half-loan, half-grants. This reflected Georgia's recent graduation from concessional financing.

The main triggers of MFA III were Georgia's persisting exposure to geopolitical instability and its weak external environment. As per the Commission proposal⁷, Georgia's external financing gap was attributable to three main factors: a relatively large current account deficit (due to reduced exports and remittances); insufficient foreign exchange reserves in light of increasing reserve needs (IMF metric); and high external debt and significant expected debt amortisation requirements.

In addition to supporting Georgia's economic stabilisation, MFA III aimed to support Georgia's substantive reform agenda and its efforts to adapt to the requirements of the DCFTA.

MFA III consisted of EUR 45 million (EUR 10 million in grants) disbursed in two instalments, each consisting of a loan and a grant element. The operation was fully disbursed.

The MoU with the authorities included 11 MFA conditions in the following reform areas:

- Public Finance Management (PFM);
- Financial sector;
- Social and labour market policies;
- Business environment.

Table 2.2 presents the expected outputs and outcomes from Georgia's MFA conditions linked to the second instalment.

⁷ Proposal for a decision of the European Parliament and of the Council providing further macro-financial assistance to Georgia, COM/2017/0559 final/2.

Table 2.2 Expected outputs and outcomes from Georgia's 11 conditions linked to the second MFA instalment

Input: conditions as per the MoU, by reform area	Output	Outcome
PFM (three conditions: #1, #2, #3)	53. Unit responsible for public investments at the Ministry of Finance appropriately resourced and in function (#1) 54. Draft Law on PPP adopted by the parliament (#2) 55. PPP unit and fiscal risk unit at Ministry of Finance appropriately resourced and in function (#2) 56. Public procurement secondary legislation revised by Georgian authorities (#3) 57. Revised legal framework for dispute resolution body drafted by Georgian authorities (#3)	58. Sound project selection framework and administrative capacities (#1) 59. Sound regulatory framework for PPP (#2) 60. Reduced proportion of direct procurement to ensure it is competitive, transparent, and offers value-for-money; independent dispute resolution body (#3)
Financial sector (two conditions: #4, #5)	61. Motor Third Party Liability Insurance Law adopted by the parliament (#4) 62. Offsite inspection manual adopted by the Insurance State Supervision Service and inspections launched (#4) 63. Regulation on sound risk management adopted by National Bank of Georgia (#5)	64. Development of the domestic Insurance and capital markets (#4) 65. Improved resilience of the financial sector and management of dollarisation-related risks by the National Bank of Georgia (#5)
Social and labour market policies (three conditions: #6, #7, #8)	66. Pilot project on selective contracting extended by the Social Services Agency, to costly medical treatment other than maternity care (#6) 67. Labour Market Strategy and Action Plan adopted and implemented by Georgian authorities (#7) 68. Vocational Education Training (VET) Law adopted by the parliament (#8)	69. Sustainability of Universal Health Care system (#6) 70. Higher employment and increase the matching of demand and supply in the labour market (#7) 71. High-quality VET to help address the skills mismatch (#8)
Business environment (three conditions: #9, #10, #11)	72. At least 500,000 plots registered according to simplified procedure and action plan to increase land registration adopted by National Agency of Public Registry (NAPR) (#9) 73. Draft Law on Entrepreneurs submitted to parliament (#10) 74. Improved judicial system (all rulings of supreme and appeal court published, cases randomly allocated and statistical data on disciplinary procedures published) (#11)	75. Creation of functioning land market to increase agricultural productivity (#9) 76. Increased transparency in the governance of enterprises (#10) 77. Increased independence and quality of the judicial system and improved business environment (#11)

Notes: #XX refers to the condition number in the MoU linked to the second instalment.

Implementation timetable

Figure 2.3 presents the timeline and main milestones of MFA III, alongside other key developments (political/economic developments, other MFA operations, IMF assistance).

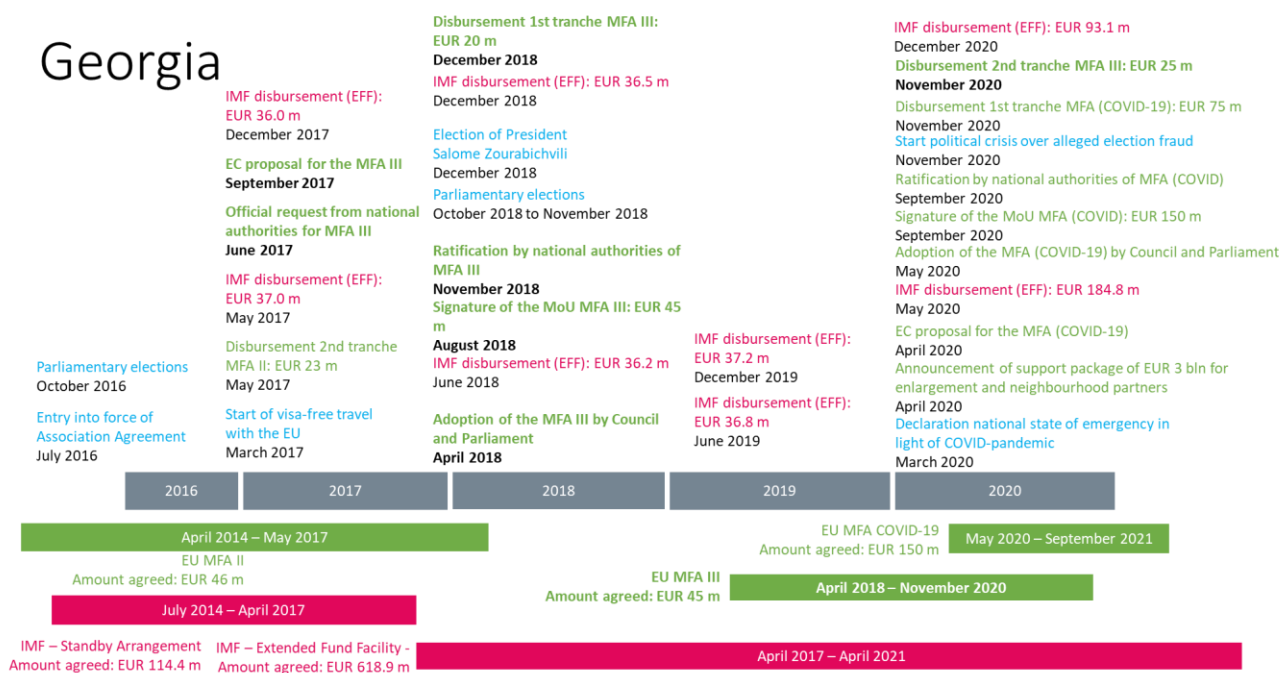
Georgia officially requested MFA III in June 2017, only two months after disbursement of the last tranche of the previous programme (MFA II). The European Commission proposal was put forward in September 2017 and MFA III was approved by the EP and the Council in April

2018⁸. It took then two months for the Loan and Grant Agreements and the MoU⁹ to be signed (August 2018). The documents were ratified by the Georgian national authorities within another two months (November 2018), allowing the first disbursement of EUR 20 million to be made in December 2018. The disbursement of the second tranche (EUR 25 million) was withheld until November 2020, after the fulfilment of one outstanding condition requesting the submission of the Law on Entrepreneurs to the national parliament. Nevertheless, implementation was relatively smooth overall.

MFA III was linked to the IMF EFF agreed in 2017, initially foreseen for a duration of three years and initially amounting to Special Drawing Rights (SDR) 201.4 million or 100% of Georgia's quota (approximately EUR 257 million). In view of the COVID-19 pandemic, the programme was then extended by one year and augmented to SDR 484 million or 230% of Georgia's quota (approximately EUR 619 million).

In 2020, as MFA III was ongoing, Georgia was covered by MFA COVID-19 (EUR 150 million). The first disbursement of EUR 75 million was paid in November 2020 (at the same time as the MFA III second tranche). The Commission then cancelled the second instalment due to unfulfilled conditions relating to the judicial system and absence of a request for disbursement from Georgia. MFA COVID-19 is outside the scope of this evaluation.

Figure 2.3 Implementation timeline for Georgia



Source: ICF elaboration

Progress on reforms

Box 2.5 summarises Georgia's progress in implementing MFA III conditionalities, based on documents provided by DG ECFIN and insights from interviews. Annex 13 provides a more detailed overview of implementation status, by condition.

⁸ Decision (EU) 2018/598 of the European Parliament and of the Council of 18 April 2018 providing further macro-financial assistance to Georgia, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32018D0598>

⁹ MoU between the EU and Georgia, https://economy-finance.ec.europa.eu/international-economic-relations/candidate-and-neighbouring-countries/neighbouring-countries-eu/neighbourhood-countries/georgia_en

Box 2.5 Overview of Georgia's implementation of MFA III conditions

All conditions except one were considered fulfilled within the agreed timeframe.

A waiver was granted for condition four, as the first part of the condition (parliamentary adoption of the Motor Third Party Liability Insurance Law) was not met. The Draft Law was approved by the government and submitted to parliament in December 2018. The entry into force of the law would have imposed an additional cost (mandatory insurance premium) on all drivers of domestic vehicles. The reform lacked public acceptance and the law remained at parliament throughout 2019. Following the outbreak of COVID-19, the momentum to implement this reform was lost. The Commission assessed it as possibly economically counterproductive to implement it at the time, as many companies and individuals were already losing part of their income, and waived the condition. As of 2023, the law has not been passed but remains on the government's agenda.

Another reason for withholding disbursement of the second tranche was the delay in fulfilling condition 10, on the submission to parliament of a new Law on Entrepreneurs. The delay appeared technical in nature, entailing a long preparatory process, including time to consult beyond the coordinating Ministry of Justice (with other ministries, Members of Parliament (MPs), lawyers, business associations, civil society, other stakeholders) and to produce a Regulatory Impact Assessment and an external legal analysis confirming that it adequately approximated the EU Company Law Directive. The government adopted and submitted the Draft Law to the Parliament in September 2020. Its adoption by the parliament was part of the MFA COVID-19 conditions.

Ukraine

MFA design

MFA IV to Ukraine succeeds three previous MFA operations in Ukraine. The first two (amounting to EUR 1.6 billion) were launched in early 2014 as part of a wider support package for Ukraine¹⁰ announced by the Commission in response to the crisis following the illegal annexation of Crimea and the subsequent conflict in the east of the country. The Commission was also responding to the reform aspirations expressed by Ukraine's citizens during the Revolution of Dignity, which led to a change of government in early 2014.

MFA III (EUR 1.8 billion) was adopted in 2015 when the conflict in the east of the country intensified and the economic situation worsened. MFA III set out an ambitious reform agenda with 36 specific conditions in six areas. It expired on 13 January 2018 without the third and final disbursement (EUR 600 million), given the lack of progress on the implementation of some conditions¹¹. The Commission approved the non-disbursement in the Cancellation Decision of 18 January 2018.

In hindsight, as reflected in the ex-post evaluation of MFA III, there were too many conditions in MFA III, especially given the timeline of the operation. Some conditions were also seen to

¹⁰ European Commission, 'European Commission's support to Ukraine', Press release, 5 March 2014, https://ec.europa.eu/commission/presscorner/detail/en/IP_14_219

¹¹ **Measure 5** - requiring the set-up of an electronic asset declaration system for public officials, including a verification mechanism. **Measure 6** – linked to the set-up of an online database on beneficial ownership of companies and requiring putting in place mechanisms to verify the accuracy of information provided. **Measure 17** – refraining from introducing new trade-restricting or trade-distorting measures, in line with Ukraine's World Trade Organization (WTO) obligations. **Measure 21** – the establishment of a Central Credit Registry.

have a high level of ambition, with stakeholders suggesting they could have been broken into smaller concrete steps to make them achievable¹².

Ukraine requested a new MFA programme in November 2017 to help to cover its external financing needs. The Decision on the MFA IV programme (in the amount of EUR 1 billion) was adopted on 4 July 2018 by the EP and the Council. MFA IV was divided into two tranches (EUR 500 million each), with conditions attached to both.

The design of MFA IV was informed by the lessons of MFA III. Firstly, the number of conditions was decreased (18, compared to the previous 36). There was an attempt to define each condition more clearly, ensuring that it remains ambitious but also sets achievable targets within the time period envisaged.

The MoU with the authorities included conditions in four main reform areas:

- PFM;
- Good governance and fight against corruption;
- Sector reforms and state-owned enterprises;
- Social policies.

A Joint Statement by the EP, the Council and the Commission was attached to the Decision on MFA IV. In view of the unfulfilled conditions under MFA III, the Statement underscored the political importance of fulfilling the newly agreed conditions. It highlighted the particular importance of conditions linked to the verification system for asset declarations, verification of companies' beneficial ownership, the establishment of a well-functioning Anti-Corruption Court, and combating money laundering and tax avoidance. The Statement asked for the Commission to share publicly its assessment of the fulfilment of all conditions on disbursement, which it did.

MFA IV's first tranche included most of the unfulfilled conditions from MFA III, particularly those related to anti-corruption efforts. An exception was one of the unfulfilled conditions linked to trade restrictions (Measure 17 under MFA III). Going forward, Ukraine's export ban on unprocessed wood was instead addressed via a dispute settlement mechanism set-up under the EU-Ukraine AA¹³.

Table 2.3 Expected outputs and outcomes from Ukraine's MFA conditions

Input: conditions as per the MoU, by reform area	Output	Outcome
PFM (four conditions: #1, #1, #2, #3)	<p>78. At least seven general tax consultations on the practical application of tax legislation issued by the Ministry of Finance in the third quarter of 2018 (#1)</p> <p>79. Medium-term reform plan for the tax and customs administration adopted by the Cabinet of Ministers of Ukraine (#1)</p> <p>80. (a) changes to the Customs Code adopted (b) draft law on the implementation in the national legislation of key provisions of international conventions regarding trade in goods submitted to the parliament (#2)</p> <p>81. Multilateral Convention to Implement Tax Treaty- Related measures to Prevent Base</p>	<p>82. Improved predictability of the tax environment for businesses (#1)</p> <p>83. Improved domestic revenue mobilisation (#1)</p> <p>84. Better balance between customs control and trade facilitation (#2)</p> <p>85. Improved framework for fighting tax evasion (#3)</p>

¹² European Commission, *Ex post evaluation of Marco-Financial Assistance operation to Ukraine over the period 2015-2017, 2020*, https://commission.europa.eu/about-european-commission/departments-and-executive-agencies/economic-and-financial-affairs/evaluation-reports-economic-and-financial-affairs-policies-and-spending-activities/ex-post-evaluation-mfa-operations-ukraine_en

¹³ European Commission, *Ukraine wood export ban*, 2019, https://policy.trade.ec.europa.eu/enforcement-and-protection/dispute-settlement/bilateral-disputes/ukraine-wood-export-ban_en

Input: conditions as per the MoU, by reform area	Output	Outcome
<p>Good governance and fight against corruption (six conditions: #2, #3, #4, #4, #5, #6)</p>	<p>Erosion and Profit Shifting submitted to the parliament and ratified (#3)</p> <p>86. a) electronic asset declarations' verification module upgraded and operational, b) automatic data exchange between the verification module and relevant state registers (#2)</p> <p>87. Company registration process amended so as to require – whenever a legal entity seeks to register or change its entry – additional information on beneficial ownership (#3)</p> <p>88. High Anti-Corruption Court of Ukraine (HACC) appropriately resourced (#4)</p> <p>89. Processes launched for the selection of members of the Public Council of International Experts and of judges of the HACC (#4)</p> <p>90. At least 1,000 declarations of high-level officials verified as per corresponding verification decisions (#4)</p> <p>91. Key milestones achieved for selection of qualified and independent judges for the HACC (#5)</p> <p>92. Resourcing of the HACC (#5)</p> <p>93. Anti-Money Laundering Law adopted (#6)</p>	<p>94. Fully functional automated verification system for electronic asset declarations of persons authorised to perform functions of the state and local self-government (#2, #4)</p> <p>95. Verification of information on companies' beneficial ownership (#3)</p> <p>96. Effective and independent functioning of the HACC (#4, #5)</p> <p>97. Improved framework for fighting and preventing money laundering (#6)</p>
<p>Sector reforms and state-owned enterprises (five conditions: #5, #6, #7, #8, #9)</p>	<p>98. a) independent members of the supervisory board of Ukrenergo (electricity transmission operator) selected and nominated, so that the supervisory board becomes operational in its new composition, and (b) selection process for independent supervisory board members started in at least three other large SOEs (#5)</p> <p>99. At least 200 small state-owned objects put up for sale through electronic auction in the ProZorro.Sale system (#6)</p> <p>100. Resolution on the management of non-performing assets in banks developed by the NBU (#7)</p> <p>101. Public reporting on asset recovery in state-owned banks and action through the courts where appropriate (#7)</p> <p>102. Amendments on state-owned banks under the Law on Banks and Banking Activities adopted by the parliament (#8)</p> <p>103. Ukrenergo prepared for certification as an independent transmission operator; and control over power generation and power transmission separated (#9)</p>	<p>104. Improved corporate governance in SOEs, with supervisory boards becoming operational (#5, #8)</p> <p>105. Privatisation plans implemented (#6)</p> <p>106. Reduced level of non-performing loans (NPLs) (#7)</p> <p>107. Progress on asset recovery (#7)</p> <p>108. Progress with implementation of Electricity Market Law (#9)</p>
<p>Social policies (three conditions: #10, #11, #12)</p>	<p>109. Key milestones achieved for reform of healthcare financing, including at least 600 contracts signed between the National Health Service of Ukraine and relevant providers for the provision of primary healthcare (#10)</p> <p>110. Resolution No 329 of the Cabinet of Ministers of Ukraine on improved targeting of Household Utility Subsidies effectively implemented (#11)</p> <p>111. Process of monetisation of subsidies at household level launched through a pilot project (#11)</p> <p>112. Action Plan on the implementation of the Strategy of Integration of Internally Displaced Persons adopted (#12)</p>	<p>113. Adequate healthcare cover at sustainable cost (#10)</p> <p>114. Improved targeting, efficiency and fairness of social benefits to the advantage of those most in need (#11)</p> <p>115. Better integration of internally displaced persons (#12)</p>

Notes: #XX refers to the condition number in the MoU linked to the first instalment or second instalment.

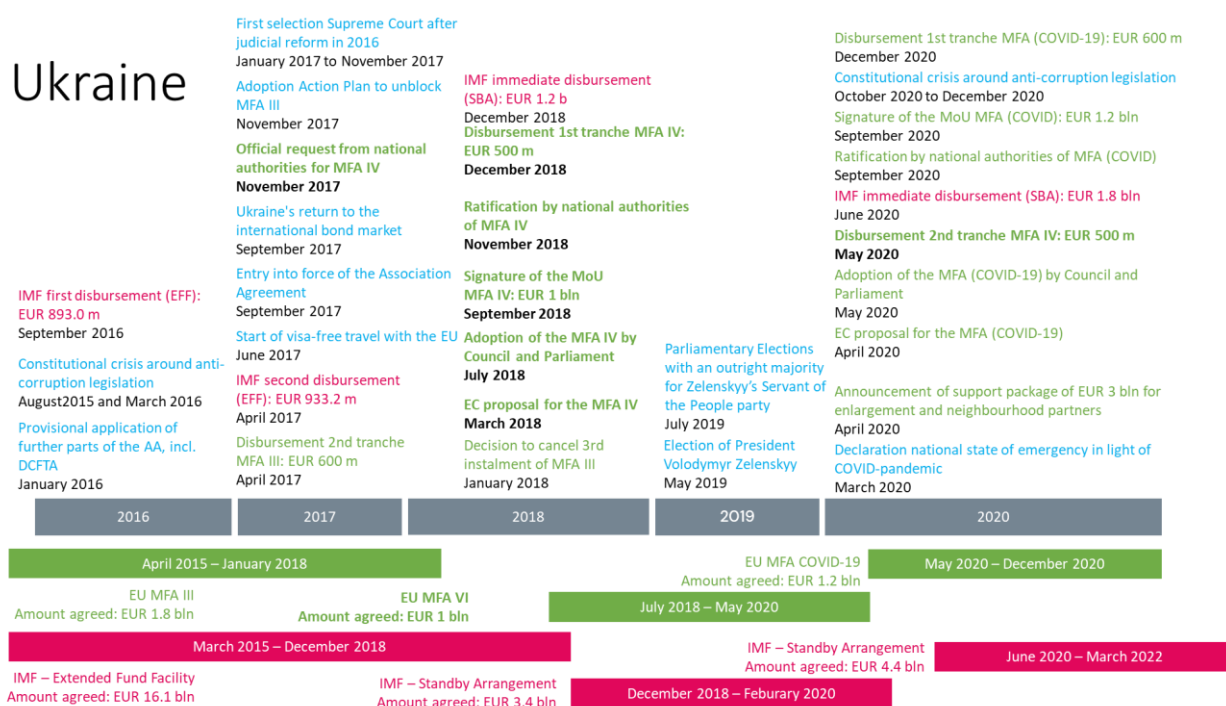
Implementation timetable

Figure 2.4 presents the timeline and main milestones of MFA IV, alongside other key developments (political/economic developments, other MFA operations, IMF assistance).

The MFA IV was proposed in March 2018, two months after the cancellation of the third tranche under MFA III. MFA IV was approved by the EP and the Council in July 2018¹⁴. It took then two months for the Loan Agreement and the MoU¹⁵ to be signed (September 2018). The documents were ratified by the Ukrainian national authorities in November 2018, which, together with its compliance with the conditions attached to the first tranche, allowed the first disbursement of EUR 500 million in December 2018. The disbursement of the second and final tranche (EUR 500 million) took place in 2020, after the single outstanding action from the new IMF Stand-By Agreement (SBA) programme was implemented. The MFA IV implementation period overlapped with three different IMF programmes (2015-2018 EFF programme; 2018-2020 SBA programme and 2020-2022 SBA programme).

MFA COVID-19 was approved in May 2020, occurring back-to-back with MFA IV, but falls outside the scope of this evaluation.

Figure 2.4 Implementation timeline for Ukraine



Source: ICF elaboration

Progress on reforms

Box 2.6 summarises the Ukrainian authorities' progress in implementing the MFA IV conditions, based on documents provided by DG ECFIN and insights from the scoping

¹⁴ Decision (EU) 2018/947 of the European Parliament and of the Council of 4 July 2018 providing further macro-financial assistance to Ukraine, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32018D0947&qid=1530869453198&from=EN>

¹⁵ MoU between the EU and Ukraine for Macro-Financial Assistance to Ukraine of up to EUR 1 billion, https://economy-finance.ec.europa.eu/document/download/c2c108ba-8455-47cb-8a44-75287558fc20_en?filename=mou_protocol_version_eu.pdf

interviews. Annex 13 provides a more detailed overview on implementation status, by condition.

Box 2.6 Overview of implementation of MFA IV conditions by the Ukrainian authorities

All conditions were considered met.

The finalisation of conditions under the first instalment saw progress on conditions that remained unfulfilled under MFA III, including the verification of asset declarations of public officials and progress on the establishment of the new HACCC. The first disbursement under MFA IV was made in December 2018, following fulfilment of the conditions tied to the first instalment.

Two conditions under the second instalment were considered 'broadly met' (#6 and #9). Condition #6, on the adoption of an Anti-Money Laundering Law, was considered broadly met because the new law was adopted largely in line with the EU's fourth Anti-Money-Laundering Directive (AMLD). Despite discrepancies, the new law was seen as an important step forward. Similarly, for condition #9, on the implementation of the Electricity Market Law, the Commission concluded that significant improvements had been made, even if some challenges persisted. Accordingly, the second instalment was disbursed in May 2020.

2.3 Key political and economic developments in the period during and after MFA implementation

Political developments

During the MFA implementation period, in addition to ongoing conflict with Russia, member countries of the Trio were mired in **local political tensions**. **Georgia** has been undergoing a **serious political crisis** since the last parliamentary elections, which were held between October and November 2020. At the time, the opposition (led by the United National Movement (UNM) party) accused the ruling Georgian Dream party of election fraud and did not recognise the results. The crisis was defused in April 2021, with an accord brokered by European Council President Charles Michel. Yet, the situation was not completely resolved. The opposition continued to demand new elections and the governing party pulled out of the EU-brokered agreement in July 2021. The situation worsened in October 2021 after local elections were again dominated by the Georgian Dream party. The opposition claimed that the elections were rigged, sparking fresh protests in the streets. Today, Georgia's political setting remains dominated by aggressive campaigning between Georgian Dream and the UNM. The country continues to face a crisis of polarisation, with its two main political parties locked in a fierce power struggle and little scope for new opposition/political voices to emerge.

Moldova faced a **serious electoral crisis** in 2018, following the invalidation of the Chisinau mayoral elections. The opposition candidate, seen as pro-West, had secured a clear victory. However, the courts, believed to be influenced by the ruling party, overturned the results. This sparked mass protests and outrage from the international community, particularly the EU, who questioned Moldova's commitment to democracy and froze MFA and budget support disbursements¹⁶. The crisis highlighted a deeper issue of oligarchic control over Moldovan institutions, raising concerns about the future of fair elections in the country.

This electoral crisis was followed by a serious constitutional crisis following its parliamentary elections in 2019. This resulted from the incumbent Democratic Party refusing

¹⁶ European Parliament resolution of 5 July 2018 on the political crisis in Moldova following the invalidation of the mayoral elections in Chişinău (2018/2783(RSP))

to step down, despite failing to secure a majority of the popular vote in the elections. The United States (US), EU and Russia all called for the Democratic Party, led by Vladimir Plahotniuc, to step down and engage in a transfer of power to the legitimately elected government. In the wake of this constitutional crisis, a temporary coalition was formed between the pro-EU and reform-oriented party (PAS) and the pro-Russian party, Party of Socialists of Republic of Moldova. Maia Sandu, the leader of PAS, was appointed the Prime Minister of Moldova. This coalition did not last, given the clear ideological and conceptual divergences. As a result, the Party of Socialists of Republic of Moldova together with the Democratic Party dismissed the Maia Sandu Government and, on 14 November 2019, formed the Ion Chicu Government. Following the Presidential elections in 2020, where Maia Sandu won over Igor Dodon, the PAS obtained a majority in the parliament after the 2021 elections. This enabled a pro-EU and reformist government that benefits from major support from EU, US and international development partners.

After the European Council granted EU candidate status to Moldova and Ukraine in June 2022¹⁷, in November 2023, the European Commission recommended opening formal accession negotiations with both countries. In June 2022, the European Council concluded that it was ready to grant the status of candidate country to Georgia once the priorities specified in the Commission's opinion were addressed, and, in December 2023, it did so.

Economic developments during the period of implementation (2017-2020)

Economic developments spanning 2010-2016 differed somewhat across the three countries. However, **from 2017-2019, all three countries achieved stable economic growth.**

In Moldova, growth was back on track from 2016 onwards. Financial assistance from international partners helped to foster the implementation of appropriate reforms to address financial vulnerabilities, restore macroeconomic sustainability, and boost economic growth and resilience. Consumption and investment also constituted crucial drivers of economic growth over the period 2017-2019, during which real GDP growth averaged 4.2%.

In Georgia, real GDP growth increased to 4.8% in 2017 and 2018, respectively. This acceleration was supported by increased domestic and external demand. Several factors and notably the currency crisis in Turkey, one of Georgia's foremost trading partners, and an anticipated drop in tourism inflows, following Russia's ban on flights to Georgia, resulted in the depreciation of the Georgian lari (GEL) (by 7.3% against the US dollar¹⁸) and an inevitable rise in inflation. However, rising private consumption, net exports and public investments meant that the Georgian economy remained resilient. Real GDP rose to 5.0% in 2019.

In Ukraine, adequate policy measures (including fiscal consolidation, increased efficiency of the tax system and reform of the banking sector), along with a more favourable external environment, allowed the Ukrainian economy to grow at an average of 3.0% over the period 2017-2019.

Despite their improved macroeconomic performances, Moldova, Georgia and Ukraine all faced severe economic hardship in the wake of the COVID-19 pandemic. By the end of 2020, real GDP had contracted by nearly 7.0% in Georgia on account of weakened domestic and external demand (notably for tourism and related services). As a result, its current account deficit widened, driven by lower export revenues. However, the effects of the

¹⁷ European Council conclusions on Ukraine, the membership applications of Ukraine, the Republic of Moldova and Georgia, Western Balkans and external relations, 23 June 2022.

¹⁸ Institute for Economic Research and Policy Consulting, Overview of macroeconomic trends in Georgia, Moldova, and Ukraine under the Association Agreements since 2014, 2020.

pandemic could have proven more detrimental were it not for strong fiscal stimulus, substantial bank lending, and better-than-expected remittances performance. In addition to the pandemic, Moldova faced a severe drought, which significantly impacted agricultural production/output. This, coupled with the lockdown measures that halted trade, and the decline in household consumption and investment, led to a reduction in real GDP of 8.3% in 2020. A similar picture was observed in Ukraine, which saw its economy shrink by 3.8% in 2020. The government's decision to close/lock down much of the economy, as well as the decision to reshuffle its Cabinet (removing key reformers from senior positions) had a significant negative bearing on growth. Nevertheless, these impacts were to a certain extent offset by a more favourable external environment. Ukraine's international currency reserves increased to USD 29.0 billion¹⁹, the highest level since 2011 (when they were USD 31.8 billion). The growth in currency reserves was the result of an improvement in Ukraine's terms of trade in 2020. The price of primary exports (agricultural goods, iron ore, and steel) increased, while the price of energy imports fell. This allowed Ukraine, whose current account had persistently been in deficit between the period 2016 to 2019 to reach a surplus to 3.4% in 2020²⁰.

Economic developments post-MFA (2021-present)

Signs of recovery were observed in 2021 in all three countries. Vaccination rollout and the removal/relaxation of COVID-19-related restrictions bolstered economic activity. Although recovery gained momentum in the three countries, inflation was rampant because of utility price increases and higher global commodity and food prices. Strong growth in remittances, resilient exports, and a pick-up in tourism supported economic recovery in Georgia, with the economy growing by 10.5% in 2021. Similarly, a robust economic rebound was observed in Moldova, driven by increased aggregate demand (brought about by high credit and wage growth) and strong remittance inflows. Real GDP grew by 13.9% in 2021. Growth also resumed in Ukraine. As of 2021, the economy had grown by 3.4%. This was well below growth figures observed in Georgia and Moldova, likely due to prolonged lockdown measures in Ukraine and weakened market sentiment in the face of ongoing tensions with Russia.

In 2022, Russia's war of aggression against Ukraine brought Ukraine's economic recovery to an abrupt halt. The war has put Ukraine's economy under enormous strain, with heavy devastation of infrastructure and production capacities. Real GDP dropped by 30.3% in 2022 due to temporary occupation of territories by Russia, difficult logistics, blackouts following the destruction of about 80% of energy infrastructure in Ukraine, and blockage of exports through sea ports. Growth increased by only 2% in 2023 from an already low base.²¹ Logistics remains a challenge for Ukrainian companies, which also experience difficulties in operating due to shelling by the Russian army.

In the context of the increasing geopolitical tensions in early 2022 and following Russia's full-scale invasion of Ukraine in February 2024, the Commission launched a number of exceptional MFA operations to Ukraine, summarised in the box below. These have been subsequently replaced by a new Ukraine Facility, of up to EUR 50 billion, approved in early 2024, aimed at ensuring consistent and transparent approach to funding to Ukraine through a unified instrument. The Ukraine Facility includes MFA type loans and grants under pillar I,

¹⁹ World Bank data, <https://data.worldbank.org/indicator/FI.RES.TOTL.CD?end=2021&locations=UA&start=2013>

²⁰ World Bank data (see: <https://data.worldbank.org/indicator/BN.CAB.XOKA.GD.ZS?locations=UA>)

²¹ IMF World Economic Outlook

but is enhanced through funds dedicated to technical assistance (pillar III) and investment support (pillar II).²²

Overview of MFA support to Ukraine since February 2022²³

- **Emergency MFA**, February – May 2022 (EUR 1.2 billion in loans, disbursed in two instalments)
- **Exceptional MFA**, July – December 2022 (up to EUR 9 billion announced in March 2022)
 - EUR 1 billion disbursed in the form of highly concessional long-term loans, in August 2022
 - EUR 5 billion disbursed across October – December 2022
- **MFA+**, December 2022 – October 2023 (up to EUR 18 billion in loans announced)
 - EUR 3 billion disbursed in January 2023
 - EUR 1.5 billion disbursed in October 2023
- **Ukraine Facility**, 2024-2027 (up to EUR 50 billion), including:
 - grants and loans (pillar I),
 - Ukraine Investment Framework (pillar II),
 - technical assistance and other supporting measures (pillar III)

In March 2023, the IMF also provided Ukraine with a full-scale programme (EFF) of USD 15.6 billion, with the IMF Board changing its policies to do so. The programme is presented as part of a USD 115 billion support package, which includes official assistance and debt restructuring.

Spillovers from Russia's war of aggression against Ukraine were expected to weigh heavily on Georgia's and Moldova's economic. In Georgia's case, the country performed much better than expected, posting a growth of 10.1% in 2022, mainly due to an influx of migrants and remittances from Russia, strong rebound in tourism and external trade (e.g. export growth of 33% was largely driven by Commonwealth of Independent States (CIS) partner countries)²⁴. In 2023, growth stood at 6.2%.

By contrast, Moldova experienced a decline (-5% in 2022). Negative factors included spillovers from the war, rising global energy prices, a gas and electricity crisis related to overdependence on Russian energy supplies and a large fall in agricultural output/production owing to drought. After the outbreak of Russia's war of aggression against Ukraine, almost 700,000 Ukrainian refugees crossed the border into Moldova. About 100,000 chose to stay, which, in a nation of 2.6 million, was the highest per capita influx to any neighbouring country²⁵.

²² For more information on the Ukraine Facility, see:

https://ec.europa.eu/commission/presscorner/detail/el/qanda_23_3353

²³ For an overview of all MFA operations to Ukraine since 2014, see: https://economy-finance.ec.europa.eu/international-economic-relations/candidate-and-neighbouring-countries/neighbouring-countries-eu/neighbourhood-countries/ukraine_en

²⁴ International School of Economics at TSU (ISET), 'Georgian Economy and one year of Russia's war on Ukraine: trends and risks', Policy brief, 2023, <https://iset-pi.ge/en/publications/policy-briefs/3281-georgian-economy-and-one-year-of-russias-war-in-ukraine-trends-and-risks>

²⁵ Directorate-General for European Civil Protection and Humanitarian Aid Operations (ECHO), "Moldova joins the EU Civil Protection Mechanism", 2023. https://civil-protection-humanitarian-aid.ec.europa.eu/news-stories/news/moldova-joins-eu-civil-protection-mechanism-2023-09-29_en

3 Evaluation findings: Moldova

3.1 Was the intervention relevant? [Related evaluation criterion to assess: *relevance*]

Question: *To what extent was the MFA operation design (including adequateness of financing envelope, focus of conditionality) appropriate in relation to the outputs to be produced and objectives to be achieved?*

In answering this question, four essential issues are considered: (i) adequacy of the size of the financial assistance, (ii) appropriateness of the form of financial assistance, and (iii) design and (iv) focus of conditionality.

Issue 1: Size of the financial assistance

Size of the financial assistance vs expectations

In his first letter requesting the opening of MFA negotiations to Commissioner Moscovici in August 2015, Moldovan Prime Minister Strelt did not specify the exact amount requested. Rather, this was elaborated in the second letter from the Filip government in March 2016. With an ongoing programme with the IMF which had started in November 2016, the door was opened for an MFA and increased collaboration with other donors. Initially, an MFA of maximum EUR 150 million was envisaged²⁶, but, ultimately, the proposed size of the assistance was smaller (EUR 100 million), in anticipation of difficult negotiations in the aftermath of the 2014 banking fraud scandal. The amount that was ultimately agreed corresponded to the European Commission proposal.

Size of the financial assistance vs financing gap and burden-sharing considerations

According to the European Commission proposal, MFA II to Moldova was initially projected to be fully disbursed by 2018 and was to be divided into three tranches, the first being disbursed in 2016. Considering the residual financing gap at the time, as assessed by the IMF, MFA II was envisioned to cover approximately 25% of the residual financing gap by 2018. Other donors were to cover up to 50% of the financing gap, with main contributions from the WB Development Policy Loans (DPLs) and bilateral aid from Romania. The renewed use of the EU budget support modality, which had been frozen since 2015 due to concerns with rule of law developments in the country, was also expected to contribute to closing the financing gap.

Prolonged negotiations in the EP, together with domestic events, meant that disbursements were significantly delayed. MFA II made no contribution to closing the 2016-2018 gap, with the first tranche released in October 2019 instead of 2016, as originally planned. Actual MFA contribution took place over 2019-2020 and accounted for 15% of the financing gap for these two years (a more modest contribution than planned given the size of the gap for 2020, unexpectedly high given the pandemic, at EUR 355 million)²⁷. The third tranche of MFA II was ultimately cancelled, as the timeline for the operation had expired.

²⁶ As per 2016 Note for the Alternates of the Economic and Financial Committee.

²⁷ Financing gap as per IMF Country Report No. 22/1, page 43, converted to EUR using InfoEuro rates for January of corresponding year

MFA II and the estimated financing gap, 2016-2018

USD Million	2016	2017	2018	Total 2016-2018
1. Current account balance*	-238	-358	-417	-1,013
2. Capital and financial account balance**	429	503	522	1,454
3. Overall balance (1+2)	191	146	105	442
4. Reserves ('-' indicates increase)	-318	-358	-205	-881
5. Overall external financing gap	-127	-212	-100	-439
6. Exceptional financing by the IMF and the WB				
Net IMF disbursements	-42	-45	-21	-108
Disbursements by the WB DPLs	45	30	30	105
7. Residual financing gap	-124	-227	-91	-442
Financing of the gap				
EU MFA	0	66	44	110
EU budget support grants	56	66	44	166
Romanian loan	66	100		166
Total identified sources	122	232	88	442
Total MFA as % of residual gap 2016-2018				24.9%

Source: IMF projections, as quoted in the Note for the Alternates of the Economic and Financial Committee, attached to the MFA II proposal. Total calculated for the years MFA was planned to be disbursed.

Notes: *Excludes official grants in the form of policy-based budgetary support; **Includes exceptional financing.

Size of financial assistance in absolute terms

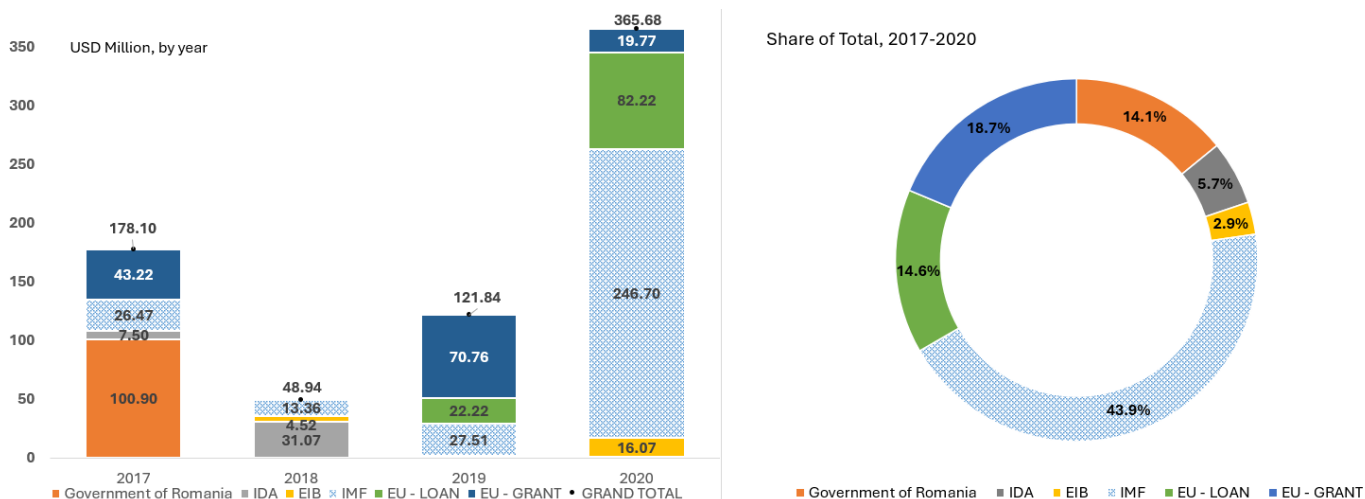
The size of the MFA, first set at EUR 100 million, is close to the average size of operations between 2009-2020 (excluding the amounts granted to Ukraine).

Size of financial assistance in relative terms

MFA II disbursements remained modest, relative to the scale of the economy, accounting for approximately 0.1-0.2% of GDP.

Relative to other donors, MFA disbursements (loans and grants), together with EU budget support (grants only), amounted for 33.3% of total budget support to Moldova over the period 2017-2020 (see Figure 3.1). Only the IMF provided more assistance (at 43.9%) and that aid was mostly disbursed in 2020 at the start of the COVID-19 crisis.

Figure 3.1 MFA II and other budgetary support, 2017-2020, USD million



Source: Ministry of Finance, Moldova.

Notes: Budget support from international financial institutions (IFIs) and donors other than the EU consist of loans only.

Issue 2: Form of the financial assistance

In adherence to the guidelines outlined in the 2013 Joint Declaration, MFA structures typically involve a loan mechanism designed to address immediate and transitory financial challenges. However, under specific conditions, a recipient nation may be eligible for either outright grants or a combination of grants and loans. The determination of a full grant or a blended MFA predominantly relies on two key factors: the level of economic and social progress in the recipient country, and its capacity to sustain and repay the debt. This approach retains a certain level of flexibility, guided by robust indicators that provide valuable insights without rigidly dictating decisions, allowing for a nuanced and individualised approach.

Box 3.1 Main factors influencing the form of MFA instrument

Case Study 1 Criterion 1: Level of economic and social development

The level of economic and social development is typically assessed based on the Gross National Income (GNI) per capita and poverty level indicators. GNI per capita is the essential indicator that determines the income category of the WB classification. For a country to be eligible for a grant, it needs to be in the lower middle-income category or below²⁸. Indicators of poverty level (as per WB data²⁹) usually complement the income category data.

Criterion 2: Debt sustainability and repayment capacity

Debt sustainability (public and external) and repayment capacity is an essential factor influencing decisions about the form of the MFA. Assessing debt sustainability and repayment capacity is a complex process that uses various indicators. These typically include: *External debt over GDP/GNI*; *External debt over exports*; *Net present value of external debt over GNI*; *External debt service ratio (debt service over exports)*; *Public debt over GDP*; *Public external debt over GNI*; *Public debt service*

²⁸ World Bank data, 2023, <https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups>

²⁹ World Bank, Poverty data, 2015, http://data.worldbank.org/topic/poverty#boxes-box-topic_cust_sec

to tax revenue. This list is not exhaustive and may be extended by liquidity indicators or other information, e.g. DSA by the IMF and WB³⁰.

Case Study 2 Additional criteria: treatment by other international donors and EU budgetary constraints

Final steps to refine the analysis include:

- Cross-checking the results of the initial analysis under criteria 1 and 2 against the status that *other international donors* grant to the country (whether the country in question is eligible to concessional finance, such as the WB's International Development Association (IDA));
- Taking into account the *EU's budgetary constraints*, i.e. the limited availability of funds under the macroeconomic assistance line of the EU budget.

The decision to provide assistance to Moldova partially through grants for MFA II can be justified based on several factors. Firstly, Moldova was categorised at the time as a lower middle-income country³¹ with a comparatively low per-capita GNI according to the WB³² (among its peers, only Armenia reported a lower GNI³³). This economic classification highlighted the country's vulnerability and limited financial resources, making grants a more suitable form of assistance to ensure effective support. Secondly, although the IMF deemed Moldova's public debt dynamics to be sustainable, the country had experienced significant increases in public debt ratios following the banking crisis and the depreciation of the Moldovan leu (MDL). Grant assistance could alleviate the pressure on Moldova's fiscal position, allowing the government to address critical priorities without further burdening its debt obligations. Thirdly, Moldova qualified for concessional financing from institutions such as the IMF's Poverty Reduction and Growth Trust and the WB's IDA. This eligibility underscored the need for assistance in the form of grants, as concessional financing ensures favourable terms and conditions tailored to the country's economic circumstances.

While grants were deemed necessary to support Moldova through MFA II, the inclusion of loans can be attributed to several factors. Firstly, constraints within the EU budget played a significant role, with limited uncommitted budget allocations available. In 2017, only a small amount (EUR 6 million) remained unallocated (see Annex 14). Despite progress in governance reforms, concerns about financial governance lingered, prompting a cautious stance.

Using both loans and grants in the proposed operation thus allowed a balanced approach to address Moldova's needs while considering budgetary constraints and governance concerns. The Commission's proposal to provide the majority of MFA II in the form of medium-term loans ensured favourable terms, including long maturities, grace periods of up to 15 years, and low interest rates, leveraging the EU's triple-A credit rating in international capital markets. This blend of loans and grants maximised the effectiveness of the assistance while managing fiscal and governance considerations.

³⁰ European Commission, *Criteria for determining the Use of Loans and Grants in EU Macro-Financial Assistance*, 2011, <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52011SC0874&from=EN>

³¹ WB data, 2023, <https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups>

³² WB, 2015. Poverty data, 2015, . Available at: http://data.worldbank.org/topic/poverty#boxes-box-topic_cust_sec

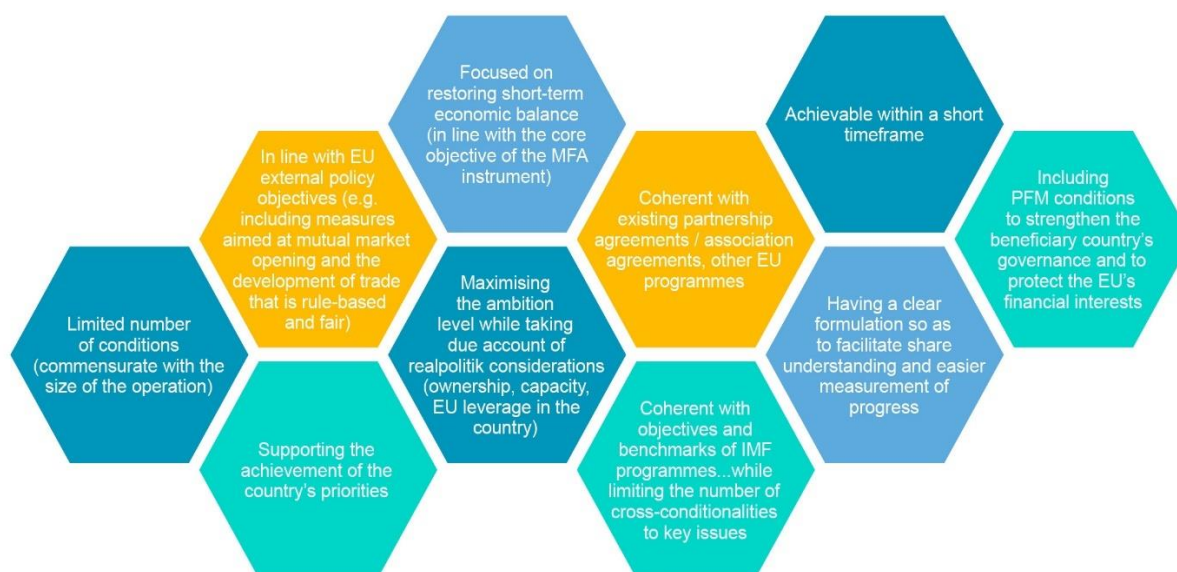
³³ WB, GNI, Atlas method (current US\$) - Ukraine, Moldova, Georgia, Belarus, Armenia, Azerbaijan data, 2023, <https://data.worldbank.org/indicator/NY.GNP.ATLS.CD?end=2022&locations=UA-MD-GE-BY-AM-AZ&start=2017&view=chart>

Issue 3: Focus of conditionality

High-level analysis

The MFA instrument was created to help to address the immediate external financing needs of a beneficiary country. This EU assistance to third countries is guided by a set of principles that informs the design and selection of MFA conditionality (see Figure 3.2). These include the expectation that the structural conditions should remain limited in number and focused on reforms related to the core objective of the MFA instrument (restoring short-term economic balance). MFA conditionality should also be consistent with the existing agreements between the EU and the beneficiary country (in the case of Moldova, the AA).

Figure 3.2 Guiding principles for MFA instrument



Source: Authors' elaboration.

When discussing the relevance of MFA II for Moldova, stakeholders often stressed the importance of the reform conditions over the financial assistance itself. It provided an agenda for the reform debate within the Moldovan government, parliament and society at large, as well as for dialogue with the EU.³⁴

Extent to which conditionality was in line with the core objectives of MFA II and EU priorities

The 28 conditions agreed in the MoU were grouped into five reform areas:

- Public sector governance;
- Fight against corruption and money laundering;
- Financial sector governance;
- Energy sector reforms;
- Business climate and DCFTA implementation.

³⁴ Interview with the European External Action Service (EEAS).

The conditionality framework reflected the EU’s ambition to ensure that the financial support would effectively benefit the Moldovan economy and population, while addressing the systemic causes of the crisis.

The crisis to which MFA II was responding had been triggered by the banking scandal, which was enabled and allegedly covered up by widespread corruption at top state function levels. The extensive anti-corruption conditions were therefore directly in line with the goal of achieving long-term macro-financial stability in Moldova.

EU stakeholders noted that a more political aim of MFA II was to support the forces within the Moldovan political system that supported greater orientation towards the EU. Linked to this aim were the reforms in the energy sector, which were designed to reduce Moldova’s extreme dependence on Russian gas and oil imports.

Many of the conditions also served the parallel aim of promoting harmonisation of the Moldovan legislative framework with the EU *acquis*.

In addition to the conditions agreed in the MoU, the eight **short-term political actions** required of the Moldovan government to restore confidence in Moldovan democracy – which had suffered a blow with the cancellation of the 2018 elections in Chisinau – were particularly important. The somewhat vaguely formulated political precondition gave the EU enough leeway to react to political developments that could not be foreseen at the time of negotiations³⁵.

The short-term political actions gave additional weight to the MFA programme, which was no longer seen as an ordinary MFA. Together with the more ‘political’ conditions in the MoU, they added value to the conditionalities put in place by the IMF and WB³⁶. EU stakeholders perceived the additional actions as designed to be effective and substantial, yet achievable within a very brief timeline.

Number of conditions and scope of conditionality

The scope and depth of conditionality considers the time needed to complete reforms, as well as the specific characteristics of the MFA instrument. In practice, this means that, given the relatively short-term nature of MFA and the need for rapid action by the recipient country, the number and ambition of conditions should be limited and feasible within a window of 6-12 months, or 30 months maximum.

The high number of conditionalities attached to the planned disbursements under MFA II in Moldova was exceptional among the three operations under review. It is even higher if including the list of eight short term actions operationalising the political preconditions. Among all pre-COVID MFA operations since 2009, it was surpassed only by the third MFA package extended to Ukraine. The first MFA to Moldova was accompanied by 12 conditions.

Table 3.2 Conditions, assistance and ratio of assistance to condition, pre-COVID-19 MFA operations, 2009-2020

Countries/operations		Total number of conditions	Amount of MFA in EUR million	Amount of MFA per condition in EUR million
By operation	Ukraine III	36	1,800	50
	Moldova II	28	100	4

³⁵ Interview with DG ECFIN.

³⁶ Interviews with DG ECFIN and EEAS.

Ukraine I	25	610	24
Ukraine IV	18	1,000	56
Tunisia II	15	500	33
Lebanon	13	40	3
Moldova I	12	90	8
Georgia III	11	45	4
Ukraine II	11	1,000	91
Serbia	11	200	18
Jordan II	11	200	18
Georgia II	11	46	4
Bosnia and Herzegovina	10	100	10
Tunisia I	9	300	33
Jordan I	9	180	20
Armenia	9	100	11
Georgia I	8	46	6
Kyrgyzstan	7	30	4
Median	11	140	14.5

Source: ICF analysis of MFA MoUs 2009-2020.

The size of the assistance also affects the EU's leverage in demanding reforms. While the number of conditions was high in proportion to the assistance, a much more stringent and comprehensive conditionality framework was perceived as necessary to convince EU decision-makers of a second MFA programme against the backdrop of the prevailing governance issues in the country.

The number of conditions, in addition to the short-term political actions committed to in 2019, in itself presented a challenge to the Moldovan administrations. The study team understands, however, that no issue was raised ex ante from the Moldovan side on the number of conditions or feasibility of the reforms, because of strong political will and the need to rapidly receive an endorsement from the EU.

The conditions were considered significant in their substance by both Moldovan and EU stakeholders. Many related to the adoption of laws by the parliament. At the same time, they were generally seen as necessary, balanced and appropriate to address the governance issues that were prevalent at the time. The challenges in meeting the conditions would have been higher had many of the reforms not already been on the path to implementation or in the government's plans.

While four conditions were not fulfilled by the time of expiry of the operation in July 2020, EU and Moldovan stakeholders attribute this to political instability and the resulting delayed timeline. Exceptions were condition #23, on asset recovery, and condition #Nr. 25, on the unbundling of energy SOEs, which were described as unattainable within the timeframe, even by some EU stakeholders.

As a result of the delayed disbursements, some of the conditions were perceived as outdated and less relevant than foreseen at the time of negotiation. However, in view of the relative

rigidity of the MFA process (which requires consent from the EU co-legislators), it was deemed impracticable to revise those conditions³⁷.

Complementarity/cross-conditionality with other EU and IFI programmes

See Section 1391714960.653 on coherence.

Extent to which the operation addressed priority areas for reform, relevance of specific reform areas, and conditions

The conditions attached to the previous MFA 2010-2012 targeted areas more directly related to macroeconomic and financial stability, with nine actions addressing public finances and the financial sector and three actions promoting legislative and regulatory convergence with the EU.

The incisive event of the 2014 banking fraud, however, exposed pervasive governance issues that reached far beyond the financial sector and required more comprehensive reforms. This was reflected in the MoU on MFA II, whose 28 conditions aimed to improve the integrity, transparency and accountability of Moldovan public institutions.

The 28 conditions finally agreed in the MoU built on a rich reform agenda, including existing national government action plans, WB and IMF conditionalities, the EU-Moldova Association Agenda, commitments under the Energy Community Treaty, and recommendations from international organisations such as the Council of Europe (GRECO, Moneyval).

The reform areas addressed in the MoU were outlined in the comprehensive Association Agenda adopted by the EU-Moldova Association Council in August 2017, but the MoU conditionality addressed a selected subset of those issues that can be broadly described as financial-economic issues on the one hand and issues related to governance and the rule of law on the other hand.

The heavy and comprehensive conditionality reflects the lesson of the banking fraud that the country's economic and financial performance and stability could not be divorced from the prevailing governance issues. Despite the large number of conditions, each of the actions was relevant to the overarching objective of enabling sustainable growth through the establishment of a rule-based and competitive economic order.

In parallel, the conditionality was designed to promote measures under the EU-Moldova AA and regulatory convergence and economic integration with the EU more generally. Accordingly, the EU *acquis* served as benchmark for the actions requiring legislative changes such as anti-money laundering or energy legislation.

The predominant challenge identified in the ex-ante evaluation was governance and stability in the Moldovan financial sector. This was addressed in the MoU through five actions required for the disbursement of the second and third tranches.

Interviews repeatedly stressed that another key challenge to reform in Moldova was (and still is) the lack of independence and effectiveness of the judiciary in enforcing the law.³⁸ The Moldovan judiciary has been described as 'one of the weakest in the world in terms of independence from the political elite'³⁹, with the importance of the issue recognised in the

³⁷ Interview with EEAS.

³⁸ Interviews with stakeholders from the EU, national authorities, and IFIs.

³⁹ GAN integrity, *Moldova risk report*, 2020, <https://www.ganintegrity.com/country-profiles/moldova/>

design of the conditionality⁴⁰. While the issue was addressed in three of the conditions, there was some sentiment among EU-side interviewees that the conditionality could have been strengthened somewhat.

Given the controversial nature of MFA II, design of the conditionality was lengthy and subject to numerous iterations between and within the EU institutions. One IFI interviewee noted that this led to a delay between problem assessment, design and the formal adoption of the MoU, by which time several conditions were well on course to being fulfilled and were therefore less pertinent. This was the case for conditions #1, #8 and #9, where the required (legislative) measures had already been taken.

Box 3.2 Public sector governance

Viewed as a prerequisite for reforms in other sectors, an overarching **Public Administration Reform Strategy** had been developed by the Moldovan government in 2016, in collaboration with the OECD Sigma initiative and the international donor community. Given the scarce human and budgetary resources, the Strategy aimed to reduce unnecessary overlaps between competences while improving the quality, accountability and efficiency of public services. Despite the relevance of these wider objectives, interviewees pointed out that the specific configuration of ministries, including the role of state secretaries, targeted by the MFA condition was of lower broader relevance as it often changes, reflecting the political conditions and governmental needs at each juncture.

A perennial problem for the public sector in Moldova is the inability to attract and retain sufficient numbers of suitably qualified staff. Factors include a lack of skilled talent, low salaries, disproportionate entry barriers, and unattractive working conditions, sometimes including exposure to undue pressures and influences on officials' decision-making. The aim of the Law on Government Reform, supported by condition #1, was thus to **restructure the central government** so as to separate more clearly the service and control functions and to free up resources that could be used to increase salaries.

The other main sub-area of reform addressed by the MoU was the **governance of state and municipal enterprises**. The reforms aimed to ensure that SOEs, at the time responsible for nearly 27% of GDP,⁴¹ were run efficiently and to the benefit of the general public.

The government had put forward a Strategy for the Development of the **Public Procurement System** in Moldova for 2016-2020, under which a new independent agency was set up to settle complaints related to SOEs. Condition #2 was to ensure its effective functioning. To increase the **accountability and transparency of SOEs**, condition #3 required the introduction of statutory audits in line with the EU *acquis*. This was also part of the IMF EFF/ECF, as well as the WB development policy operation (DPO) reform agenda.

Better alignment with EU standards was envisaged in the areas of **public procurement, PPPs, and concessions in the utilities sector**. Corresponding commitments under the DCFTA were reinforced by the MFA conditionality.

To ensure that the audit of SOEs, and public finances in general, would be carried out effectively and without interference, the MoU required the parliament to adopt a law establishing the financial, operational and functional independence of the **Court of Accounts** and to establish parliamentary oversight in a special committee.

Box 3.3 Fight against corruption and money-laundering

⁴⁰ European Commission, Annex to the Ex-ante evaluation statement Accompanying the document Proposal for a Decision providing macro-financial assistance to the Republic of Moldova, SWD/2017/012 final - 2017/07 (COD), 2017.

⁴¹ IMF data.

Moldova has long suffered from pervasive corruption at lower and higher levels of administration, to the point of being diagnosed with 'state capture' by Transparency International in 2017, meaning that its political, judiciary and economic spheres were shaped by a powerful circle of individuals, notably one specific person, Vladimir Plahotniuc, then-leader of the ruling Democratic Party⁴². A significant influence of vested interests over state institutions was also identified by the EEAS in the ex-ante evaluation.

Based on Transparency International's 2014 integrity system assessment of Moldova, the government formulated the National Integrity Strategy 2017-2020, comprising 130 actions across six focus areas. The last MFA tranche's disbursement was conditional on 'substantial progress' on this agenda.

One of the key priorities, both domestically and on the EU side, was to contain the financial consequences of the bank fraud and to address the enabling factors. This was required politically in the first instance, to convince the co-legislators that the Moldovan government was willing to reform. It later emerged that key political decision makers in the Democratic Party – who were among the interlocutors for the MFA operation – were themselves entangled in the scandal.

The **recovery of assets** stolen in the context of bank fraud was addressed in two MFA conditions: condition #7 required the parliament to allocate sufficient staff and budget for the effective functioning of the newly established Criminal Assets Recovery Agency (CARA), while condition #23 required, somewhat vaguely, 'substantial progress' in the implementation of the recovery strategy.

In addition to banking fraud, Moldova was one of the main theatres of the so-called 'Russian laundromat' between 2010 and 2014, during which an estimated USD 20-80 billion was siphoned out of Russia, making it one of the 'world's biggest and most elaborate money-laundering scheme[s]'⁴³. To address the **anti-money laundering/counter-terrorist financing (AML/CFT) vulnerabilities** exposed, the government brought in a law to align the country's regulatory framework with EU and international standards (Moneyval). The MFA and IMF packages supported this initiative by including it in the conditionality of each operation.

The establishment of a new system for the **declaration and verification of assets and interests** of public officials was an important achievement in anti-corruption policy since 2014. The MFA conditionality supported that system by aiming to ensure the independent functioning of the new National Integrity Agency, as well as the practical functioning of the electronic asset declaration system.

Box 3.4 Energy sector reforms

Moldova became a Contracting Party to the Energy Community Treaty in 2010, making a legally binding commitment to adopt core EU legislation in the energy field. In 2016, Moldova requested and received an audit review from the EnC Secretariat of the **National Energy Regulatory Agency** (ANRE), which found an urgent need to strengthen ANRE's independence. An action plan was drawn up to address the shortcomings identified, while the MFA conditionality backed the EnC's recommendations (condition #8), although the Law on Energy had already been adopted prior to the MoU signature⁴⁴.

⁴² Rahman, K., 'Moldova: Overview of corruption and anti-corruption with a focus on the healthcare and procurement sectors', *U4 Expert Answer*, 2017, p. 3.

⁴³ The Herald, 'Scots shell companies used to launder £4 billion out of Russia', News, 27 March 2017, <https://www.heraldsotland.com/news/15183346.scots-shell-companies-used-launders-4-billion-russia/>

⁴⁴ Government of Republic of Moldova, Law on Energy, <http://lex.justice.md/index.php?action=view&view=doc&lang=1&id=371969>.

Reducing energy consumption by increasing **energy efficiency** was part of the seven goals of the National Development Strategy (NDS), 'Moldova 2020' adopted by the Moldovan parliament in 2012. The MoU required the government to submit legislation approximating the EU *acquis*.

In the gas sector, Moldova was almost entirely dependent on Russia, importing 99% of its gas from Russia in 2016⁴⁵. To mitigate this dependency, the construction of a **new gas pipeline** was planned with financial assistance from the European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB) and EU grants, and the MFA conditionality integrated this target. In addition, the MoU required the **unbundling of gas system operators** to comply with EnC *acquis*, for which an action plan was drawn up, in collaboration with the EnC Secretariat and international partners.

Energy tariffs set by the Moldovan Energy Regulator were well below cost-recovery levels, preventing energy companies from being financially viable and prices from incentivising energy efficiency. To enable readjustment of energy tariffs while protecting vulnerable households from fuel poverty, the MoU provided for the strengthening of two **social assistance** programmes that were assessed by the WB as relatively well-targeted.

Box 3.5 Business climate and DCFTA implementation

As part of the AA, Moldova and the EU established a bilateral DCFTA in 2014, facilitating trade between the two partners and committing Moldova to regulatory convergence. Following certain reforms, by 2017 Moldova ranked 44th in the WB's Ease of Doing Business ranking, up from 81st in 2011, and ahead of several EU Member States (such as neighbouring Romania or Italy) and Ukraine, but below Georgia, which ranked 9th⁴⁶.

In the National Development Strategy Moldova 2020 (NDS), developed in collaboration with the United Nations Development Programme (UNDP), the parliament set targets to **decrease the number of permits and licences** required for operating a business in Moldova. The MFA conditionality took up this target in condition #9, but a number of reforms had already been implemented by the time the MoU was signed, and the condition was assessed as fulfilled.

Customs administration was characterised by 'burdensome and non-transparent formalities, procedures and rules', according to the NDS, and was a major forum for rent-seeking, with one-third of businesses reporting having paid bribes to customs officials⁴⁷. The MoU conditionality required two legislative reforms to address these issues, approximating the legislative framework to the EU *acquis*, in line with the AA.

Another measure to promote legislative convergence was included in the area of competition and specifically aimed to improve diversity in the media sector, which was dominated at the time by oligarch and Democratic Party leader Vlad Plahotniuc, who owned an estimated 70% of the market⁴⁸.

In the **justice sector**, low levels of trust in courts and the judicial system have long undermined the performance of businesses⁴⁹. The Moldovan judiciary has been described as 'one of the weakest in the world in terms of independence from the political elite'.⁵⁰ Reforms in the judiciary were named as the first priority in the 2017 Association Agenda and assessed as the most problematic of the eight

⁴⁵ EnC Secretariat, *Annual Implementation Report*, 2016, p. 104.

⁴⁶ WB, *Doing Business 2018 – Full Report*, 2018, p. 4.

⁴⁷ Transparency International, *Sociological Study - Corruption in Republic of Moldova: Perceptions vs. Personal Experiences of Business People and Households*, 2015, https://www.transparency.md/wp-content/uploads/2017/06/TI_Moldova_Sociological_Survey_2015.pdf

⁴⁸ Freedom House, *Moldova's Media Struggle to Shake Off Political Influence - The fate of press freedom in the country is closely tied to the success of its democracy*, 2017, <https://freedomhouse.org/article/moldovas-media-struggle-shake-political-influence>

⁴⁹ WB, *Moldova – Paths to Sustained Prosperity – A Systematic Country Diagnostic*, Report No. 107502-MD, 2016, p. 48.

⁵⁰ GAN integrity, *Moldova risk report*, 2020, <https://www.ganintegrity.com/country-profiles/moldova/>

reform priorities in the NDS⁵¹. The EU had previously provided funds to support reforms, but a third disbursement worth EUR 28 million was cut in October 2017 due to ‘insufficient commitment to reforming the justice sector’⁵².

The MFA conditionality addressed the pressing issue from two angles, requiring Moldova to establish procedures to ensure that the selection and promotion of judges, as well as disciplinary accountability, are based on objective and transparent criteria. In addition, a condition was included to strengthen the position of the Superior Council of Magistracy, while enhancing its independence from undue external influence.

Box 3.6 Financial sector reforms

Confidence in the Moldovan financial sector collapsed as a result of the involvement of Moldovan banks in the year-long money laundering scheme known as the ‘Russian laundromat’ and the 2014 ‘billion-dollar fraud’, which led to the liquidation of three Moldovan banks, at a public cost equivalent to 10% of Moldova’s GDP⁵³. A report investigating the circumstances of the 2014 fraud found evidence that the fraud had been concealed in a coordinated effort by actors within the three banks⁵⁴. Three further banks were put under special supervision by the NBM in 2015 due to their opaque ownership structure.

The IMF addressed many of the issues in the financial sector through a detailed and concrete action plan, as a condition of its USD 180 million EFF/ECF arrangements approved in late 2016.

One of the core issues that facilitated the 2014 fraud was the **lack of shareholder transparency** in the Moldovan financial sector, which allowed a small number of individuals to gain control over nearly 80% of the banking sector and 70% of the non-banking sector⁵⁵. The MFA conditionality aimed to address this vulnerability by encouraging, together with the IMF, the identification of UBOs of existing shareholders in the banking sector and in the insurance sector. In addition, the NBM was to carry out a diagnostic analysis of related party lending, another mechanism used in the bank fraud.

In parallel, the Law on Banking Activity (also a prior action in the WB DPO) and accompanying NBM regulation was to strengthen internal **bank governance**, including through more transparent and competent supervisory boards. The law was also to enhance the resilience of the banking system through new **capital adequacy** requirements in line with the EU’s Capital Requirements Directive IV(CRD IV)/ Capital Requirements Regulation (CRR) package.

Convergence with EU standards was also expected through amendments to the **Deposit Insurance Law**, which was to help to restore public confidence in the banking system by increasing individual coverage levels and extending the scope of protection to non-financial corporates and small and medium-sized enterprises (SMEs). The non-banking financial sector was considered underregulated and the conditionality was to promote legislation to develop the sector, while controlling associated risks by ensuring proper regulation by the NCFM, in particular of microfinance institutions and leasing companies.

⁵¹ Expert Grup, *Mid-term evaluation of National Development Strategy ‘Moldova 2020’ – Key Findings*, 2017, p. 5.

⁵² EEAS, *Moldova: EU cuts budget support programme for justice reforms*, 2017, https://www.eeas.europa.eu/node/33723_en

⁵³ IMF, *Country Report No. 16/343*, 2016, p. 4.

⁵⁴ Kroll Consultancy, *Project Tenor – Scoping Phase*, Final Report prepared for the National Bank of Moldova, 2015, p. 9.

⁵⁵ WB, *Moldova – Paths to Sustained Prosperity – A Systematic Country Diagnostic*, Report No. 107502-MD, 2016, p. 49.

3.2 To what extent was the intervention successful and why? [Related criteria to assess: effectiveness, efficiency, coherence]

Evaluation criterion: *Effectiveness*

Part 1: assessment of the macroeconomic role of MFA II

Examining the observed macroeconomic outcomes over the MFA disbursement period (2018-20)

During the MFA II disbursement, Moldova's economy saw a slight decline, averaging -0.2% in 2018-2020, which was entirely driven by the huge recession in 2020 (8.3% GDP contraction) the country experienced due to the COVID-19 pandemic. This contrasted with earlier growth in 2016-2017 driven by infrastructure and private investment, rising incomes, and improved bank lending. However, already in 2019, lower-than-planned infrastructure spending and tighter monetary policy led to a slower growth. Swift responses to the COVID-19 pandemic, including increased healthcare spending and IMF assistance, facilitated a strong 2021 rebound (13.9% growth), but recovery waned in 2022 (negative 5%) and 2023 (2%) amid overlapping crises.

Inflation fluctuated but was maintained its peak at 13.5% in 2015 during the banking crisis. Inflation briefly dropped to 0.9% in 2018 due to cuts in energy tariffs, lower food prices, and currency appreciation, with effects waning in 2019 (7.5%). Correspondingly, the NBM initially tightened, then eased monetary policy. Despite inflation remaining above target, the NBM reduced its base rate from 7.5% to 5.5% in December 2019, anticipating lower food prices and subdued demand. This move was seen as 'premature' by the IMF, but inflation fell as expected, to 6.9% in January 2020.

Moldova maintained historically low unemployment rates, averaging 4.8% between 2010 and 2023, with the lowest at 3.1% in 2018. However, this positive indicator is accompanied by an extremely low labour force participation rate, currently around 45%. Structural challenges persisted, including job supply and workforce skills mismatches, limiting comprehensive reforms in business, governance, and human capital quality.

Moldova saw a decrease in gross government debt from 42.4% in 2015 to 28.8% in 2019 and a slight increase to 36.6% in 2020. Key factors were nominal exchange rate appreciation in 2017 (11.3%) and under-execution of spending. The overall risk of total debt distress remained moderate despite the disruptions caused by the COVID-19 pandemic, which resulted in a fiscal deficit of 5.3% of GDP (compared to a 2010-2019 average of 1.6%). Moldova's public debt decreased again in 2021.

The overall profile of gross financing needs from 2016 to 2022 was relatively flat, averaging 8.5% of GDP. The lowest value of 4.3% was in 2018, and the highest value was 12% in 2020, from the COVID-19 crisis. Overall, the gross financing needs of Moldova remained below the 15% indicative benchmark identified by the IMF as suggesting debt burdens of heightened risk,⁵⁶ even during periods of negative external shocks to the economy.

Moldova maintained a B3 credit rating since the 2010s, facing fluctuations in outlook. In January 2017, Moldova returned from a negative to a stable outlook, reflecting improved institutional strength and political stability, with affirmations in 2018 and 2020. Despite

⁵⁶ IMF. 2013. 'Staff guidance note for public debt sustainability analysis in market-access countries'. Available here: [link](#).

continuous improvements, Moldova's ratings were constrained by reliance on external financing, limited economic base, elevated poverty, weak institutions, and political risks.

Moldova's external sector experienced shifts over the years. In 2016, the current account deficit reached a historic low of 3.6% of GDP, attributed to enhanced export performance, a stable foreign exchange market, controlled import growth, and strong remittances. However, in 2018, the external sector deteriorated, with the deficit increasing to 10.8% of GDP due to strong domestic demand and real exchange rate appreciation. By 2020, there was a slow improvement, with the deficit reducing to 7.7% of GDP, influenced by lower energy prices and reduced domestic demand offsetting lower exports, but the trend reversed again in 2021 and 2022, with the current account deficit worsening to 12.4% and 15.8%, respectively.

Despite recent reforms, challenges persist, with a lack of qualified labour, ongoing emigration, global economic uncertainty during the pandemic, and structural issues such as corruption and governance hindering investment attractiveness. Moldova is experiencing challenges in attracting FDI. Inflows.

After the 2014 banking sector crisis, Moldova's financial system demonstrated resilience and substantial progress on oversight reforms. Its banks maintained robust capital buffers that exceeded required minimums. Following a long period of significant improvement, the capital adequacy ratio fell from 31% in 2017 to 25.3% in 2019 and 27.1% in 2020. NPLs decreased from a period high in 2017 (18.25%) to 6.44% in 2022, indicating progress following the introduction of new prudential norms. The return on equity improved overall but dropped to 9.6% in 2020 due to the COVID-19 pandemic. Challenges included a high loan-to-deposit ratio, excess liquidity, dollarisation, and rising risks in the non-bank financial sector. Efforts to reduce dollarisation showed some success, but risks in the non-bank sector increased. Regulatory and structural challenges persisted, including limited financial market depth, a small banking sector, and underdeveloped capital markets. Although there was a partial recovery in assets in 2020 after the crisis-induced contraction, concerns lingered regarding oversight of the non-bank financial sector, political interference, and deficiencies in the AML/CFT framework.

Table 3.3 Evolution of key macroeconomic indicators, Moldova, 2017-2021

Indicator	2017	2018	2019	2020	2021
GDP, current prices (USD billion)	9.5	11.3	11.7	11.5	13.7
Real GDP growth (%)	4.2	4.1	3.6	-8.3	13.9
Inflation, average consumer prices (%)	6.5	3.6	4.8	3.8	5.1
Inflation, end of period consumer prices (%)	7.3	0.9	7.5	0.4	13.9
Unemployment, % of labour force	4.1	3.1	5.1	3.8	3.3
General government net lending/borrowing (% of GDP)	-0.7	-0.9	-1.5	-5.3	-2.6
General government gross debt (% of GDP)	34.9	31.8	28.8	36.6	32.6
Gross external debt (USD million)	6,804.2	7,163.1	7,182.6	8,088.3	8,740.9
Gross external debt (% of GDP)	72.8	67.6	65.1	73.5	64.2*
FDI (inflows) (USD million)	149,520	293,790	507,170	157,790	391,310
FDI (inflows) (% of GDP)	1.6	2.6	4.3	1.4	2.9
Gross international reserves (USD million)	-531	-236	-60	-637	-206
Gross international reserves, months of imports	5.3	5.4	6.2	5.7	4.9*

Sources: IMF, WB, NBM.

Notes: *Estimated.

Assessing the role and contribution of MFA II to observed outcomes

The four scenarios are follows:

1. What would have happened without the first tranche of the MFA II, disbursed in 2019 (Alternative A: no MFA first tranche);
2. What would have happened without the second tranche of the MFA II, disbursed in 2020 (Alternative B: no MFA second tranche);
3. What would have happened if the cancelled third tranche of the MFA II was disbursed as originally planned in 2020 (Alternative C: additional MFA third tranche);
4. What would have happened in the absence of both MFA II and IMF assistance (Alternative D: no MFA or IMF).

Alternative A: No disbursement of the first MFA III tranche in 2018

Alternative B: No disbursement of the second MFA II tranche in 2020

In a scenario where the MFA II tranche was not to be disbursed in 2019 or 2020, Moldova would have faced challenges addressing the financing gap. With relatively modest tranches (EUR 30 million each), the impact on macroeconomic stability and debt sustainability would likely have been limited. The absence of the first and second tranches might have increased political and financial pressures, leading to necessary budget cuts. While domestic borrowing was plausible due to robust liquidity in 2019 and 2020, high rates made it unattractive and less likely. In less favourable international markets, Moldova's lack of credibility would result in even higher costs and challenges in securing external financing. Seeking additional support from donors – a historical practice – could encounter challenges due to governance issues and political instability, limiting donor readiness and availability. The most plausible scenario would involve further fiscal adjustments, with cuts in social spending and COVID-19-related support due to challenges in raising taxes and limited external financing. This is all the more likely that there is evidence that the actual MFA disbursement led to increase in social spending.

Alternative C: Disbursement of the cancelled third MFA II tranche in 2020

In the context of the COVID-19 crisis, the EUR 40 million from the cancelled third MFA II tranche could have been crucial for Moldova, addressing challenges particularly in health and social welfare. Moldova's pandemic-related spending needs were substantial, estimated at around EUR 90 million (USD 106 million). However, disparities between planned and actual external funding impeded the implementation of planned government measures to address pandemic challenges. The additional funds from the cancelled tranche could have enabled higher-social spending. The most plausible options would have involved potential policy actions that could have been financed to counter the impacts of the pandemic such as targeted cash transfers or tax deferrals for companies, coupled with additional spending on health and social welfare.

Alternative D: No EU (MFA) and IMF support

In Alternative D, the most hypothetical scenario, without support from the EU (MFA) and the IMF, Moldova would have faced severe consequences, resulting in a substantial financing gap of at least EUR 436.5 million from 2016 to 2020. The effect of the lack of EU and IMF support, pivotal in restoring investor confidence and stabilising sovereign risk ratings, is

exacerbated by existing constraints such as the inability to issue Eurobonds.⁵⁷ While domestic financing through securities issuance could have been an option, high rates relative to EU/IMF lending would have been less fiscally sustainable. Without these key supports, Moldova's borrowing capacity would have been unpredictable and diminished. EU and IMF support, instrumental in prompting corrective policy actions and stimulating Western donor assistance, would be, by design, non-existent under Alternative D. Considering alternative financing from Russia and China becomes a plausible but likely less advantageous option, given the informal and untransparent conditions tied to such assistance. This was evident in the Russian loan in 2020 that was initially ratified but ultimately rejected on constitutional grounds, as well as China's involvement in the 'One Belt, One Road' programme⁵⁸. In the absence of EU and IMF support, likely actions would involve a mix of high-rate domestic borrowing, donor financing potentially tied to Russia and/or China, and fiscal adjustments, including cuts in social programs and COVID-19-related measures. Anticipated budget cuts would likely cancel programmes like the Heating Allowance and Ajutor Social, social infrastructure and service sector investments, and salary increases for doctors and teachers. The failure to secure EU/IMF funding could have led to both economic and political instability, given the substantial (symbolic) importance of these operations in maintaining low debt levels and restoring Moldova's international and domestic standing after the 2014 banking scandal-induced turmoil.

Choice of the most plausible counterfactual scenario(s)

The table below presents our conclusions on the most plausible counterfactual alternative(s), that feed into the rest of the analysis.

Table 3.4 Most plausible counterfactual scenario(s)

Moldova	
Alternative A: Absence of MFA first tranche : absence of EUR 30 million in October 2019.	
Alternative financing	Probably not available.
Direct implications	Budget cuts to make up for the absence of the tranche.

⁵⁷ Despite discussions in 2020 about involving Moldova in Eurobond issuance with assistance from a major international bank, it lacks credibility to attract external financing and capacity to absorb funds due to governance issues, corruption, and slow reform.

⁵⁸ Centre for Eastern Studies, *Russian loan is a threat to Moldova*, 2020, <https://www.osw.waw.pl/en/publikacje/analyses/2020-04-28/russian-loan-a-threat-to-moldova>; Sirbu, S., Notification no. 56a of 23 April 2020 on constitutional review of the Agreement between the Government of the Republic of Moldova and the Government of the Russian Federation on granting the Government of the Republic of Moldova a state financial loan, 2020, <https://www.constcourt.md/ccdocview.php?tip=sesizari&docid=1262&l=ro?tip=sesizari&docid=1262&l=ro>; Butmalai, I., Lariusin, T. and Preasca, I., *Study summary: Russian Economic Footprint in Moldova*, 2020, <https://corrosiveconstructivecapital.cipe.org/wp-content/uploads/2021/04/Russian-Economic-Footprint-in-Moldova-Study.pdf>; Grant Thornton, *Belt and Road opportunities*, 2018, <https://www.grantthornton.global/en/insights/articles/Belt-and-Road-opportunities/>

	Moldova
Alternative B: Absence of MFA second tranche : absence of EUR 30 million in July 2020.	
Alternative financing	Probably not available.
Direct implications	Budget cuts to make up for the absence of the tranche.
Alternative C: Additional tranche for Moldova : disbursement of EUR 40 million in July 2020	
Alternative financing	NA
Direct implications	Additional budget support for health and social welfare.
Alternative D: No MFA or IMF support: absence of EUR 437 million over 2016-2020	
Alternative financing	Probably not available.
Direct implications	More severe budget cuts.

Debt Sustainability Analysis (DSA)

The objective of the DSA was to evaluate the contribution of MFA II (2019-2020) and IMF support to Moldova's debt sustainability in terms of public debt and gross financing needs. DSA involves modelling the key debt burden indicators and macroeconomic variables that affect the path of a country's debt and its ability to manage its debt sustainability. To assess the contributions of the MFA support to Moldova's debt sustainability, the main debt sustainability indicators (baseline) are compared to hypothetical outcomes in four alternative scenarios (counterfactuals).

In developing these counterfactuals, experts were consulted on the most likely courses of action in the absence of support, enabling different scenarios of plausible actions (variants) to be defined. The scenarios were then modelled in the IMF DSA tool for each counterfactual, including, where applicable, estimates and assumptions on how borrowing costs might have changed and how GDP would have been affected. The consequent evolution of the main DSA indicators was assessed, shedding light on the macro-fiscal contribution of MFA II and IMF support.

Moldova: Alternative A – no MFA first tranche

Without the first MFA tranche, worth EUR 30 million and disbursed in October of 2019, Moldova would most likely have resorted to cuts in government spending. Covering the outstanding financing gap through lower government spending would have had implications for GDP, with an expected reduction of 0.2% compared to the 2019 baseline. In this

situation, Moldova would have seen small changes to its main debt sustainability indicators, but its broad macroeconomic outlook would have remained unchanged.

Moldova: Alternative B – no MFA second tranche

Without the second MFA tranche, worth EUR 30 million and disbursed in July of 2020, Moldova would again have likely relied on cuts to government spending. This follows a similar rationale as for Alternative A, given that this second disbursement was executed nine months after the first. Covering the outstanding financing gap through government spending would have had negative effects on GDP, with an expected reduction of 0.3% compared to the baseline. In this situation, Moldova would again have seen small changes in its main debt sustainability indicators, and its broad macroeconomic outlook would have remained unchanged.

Moldova: Alternative C – additional MFA third tranche

The third MFA tranche was worth EUR 40 million and planned to be disbursed in July of 2020. Moldova's potential policy actions with these funds could have included more assistance in the form of higher health and social welfare spending. Overall, additional government spending tends to raise economic activity, leading to higher GDP. In this case, the third tranche could have increased GDP slightly, by 0.3% compared to the baseline. Gross public debt as a ratio to GDP would have increased accordingly, by approximately 0.5 pp.

Given the comparable size of the planned third tranche to the first two, the effects of incurring additional debt in 2020 for Moldova would likely have been negligible in terms of overall debt sustainability, while possibly increasing GDP and growth outlook slightly, along with possible positive social impacts, depending on how the money was spent.

Moldova: Alternative D – no MFA and no IMF

Without MFA II and IMF support, worth a total of EUR 437 million and disbursed over 2016-2020, Moldova would likely have relied on severe cuts to government spending. Cuts to social programmes and capital/infrastructure investment were likely options.

Covering the financing gap through lower government spending would have lowered GDP, with an average expected reduction of 0.3% compared to the baseline each year between 2016 and 2020, peaking in 2020 with a 0.8% reduction. This reduction might have been amplified by interaction with the COVID-19 crisis, potentially resulting in further severe GDP reductions.

The absence of both IMF and MFA support would likely have had been more material for Moldova. While the extent of these effects is hard to estimate precisely, given the uncertainties and extreme nature of the counterfactual, had Moldova had to enact drastic fiscal consolidation, while financial sustainability ratios may have improved somewhat, this would have taken place against a much more challenging backdrop of lower economic growth. Had there been stronger exchange rate responses, debt sustainability would have also been more problematic.

Part 2: Assessment of the effectiveness of MFA conditionality

Of the MFA conditions, 24 of 28 were met by the end of the implementation period. This is generally seen as a positive outcome, given the political turmoil experienced by Moldova between 2017 and 2020, with three different governments in power, each with very different positions on the reforms.

While the effective implementation of structural reforms is a significant challenge in Moldova and has been undermined by a lack of real commitment to reform, particularly under the Democratic Party's government (see Section Evaluation criterion: Efficiency), the MFA

conditionality nevertheless played an important role in establishing a capable legislative and institutional framework on which more progressive forces can build.

Reforms in the banking sector have been particularly effective and impactful. Given the collapse of Moldova's banking system after 2014, its restoration was high on the agenda, and reforms under MFA – as well as IMF conditionalities – succeeded in clearing the sector of illicit actors and bringing much-needed transparency to ownership structures, while achieving some convergence with the EU *acquis*.

Energy sector reforms were less immediately effective but no less significant, helping to lay the groundwork for the country's eventual move away from near-total dependence on Russian natural gas imports. The Ungheni-Chisinau pipeline, which became operational in late 2022, shields Moldova from Russian blackmail attempts, although the contribution of MFA II appears limited compared to the direct financial support from the EU and other donors (notably, EIB and EBRD). The timetable for unbundling the gas system operators proved too ambitious to be completed within the MFA implementation period, but was finally achieved in 2023.

Several of the actions devised under the conditionality aimed to support the effectiveness of regulatory reforms through the establishment of specialised institutions or the promotion of their operability and independence. This approach likely reflects scepticism towards the reform ownership of certain government actors and the history of widespread influence of vested interests in Moldova (see case study on corruption in the Annex).

Some success was achieved in allocating sufficient budgetary resources to the relevant authorities during the implementation period, although in some cases this required the intervention of international observers (e.g. the Council of Europe, in the case of CARA) or budget cuts were made after 2020 (in the case of the NIA). Several institutions faced challenges to their independence, indicating the continued presence of forces that resist effective reform.⁵⁹

An example of how the effectiveness of some formally compliant reforms could be undermined in practice is the Law on the Organisation and Functioning of the Court of Accounts (CoA), which in itself was deemed sufficient to safeguard the Court's independence, but was then undermined by subsequent legislation requiring the Court's budget to be approved by the government.

A striking issue affecting the ability of all public institutions to function effectively is the acute inability to attract and retain sufficient talent. Few government agencies are operating at or near full capacity, with one experiencing crippling staff turnover rates of almost 50% within a year (National Complaints Settlement Agency, NASC). Stakeholders attribute this to a number of factors, including uncompetitive salaries, a shortage of skilled talent in the wider labour market, a lack of protection from external pressures on civil servants (including arbitrary judgements and threats to physical integrity), work culture, and/or disproportionate barriers to entry. Some also pointed to a lack of political will.

The problem is well known and there have been efforts to remedy it, for instance by streamlining recruitment procedures (e.g. NIA). The government's Public Administration Reform Strategy increased the salaries of civil servants in central government, but overall,

⁵⁹ For instance, the independence of the energy regulator ANRE has been put questioned in several EnC implementation reports; the Court of Accounts' independence was found to be lacking by a 2023 OECD-SIGMA report; the independence of judges and prosecutors was disputed by large parts of respondents to a survey among Moldovan lawyers, prosecutors and judges; and the anti-corruption agencies NIA and NACC were allegedly weaponised against opponents of the Plahotniuc network. See Annexes A11.2 (Overarching case study on anti-corruption) and A13.2 (Condition tables) for detail.

and particularly in the agencies, salaries are still below market rates and other efforts have yet to pay off.

Another recurring theme was the obstacle to reform posed by a lack of enforcement – or even allegations of active obstruction, according to CSO and IFI interviewees – by the Moldovan judiciary. Important structural reforms were implemented under MFA conditionality to establish objective standards for the selection, promotion and accountability of judges, but their impact is expected to be felt only in the longer term. In the meantime, stakeholders across the board (EU, Moldovan authorities, civil society) perceive the role of the judiciary as an inhibitor rather than an enabler of reform in Moldova.

Beyond progress on advancing structural reforms in the MoU, the MFA contributed positively to the satisfaction of the political preconditions prior to the disbursement of funds.

Box 3.7 Public sector governance

Results in the public sector were mixed, with formal compliance with all conditions, but implementation often lacking immediate effectiveness in practice.

While the **Public Administration Reform Strategy** was duly implemented through the new Law on Government (even before the MoU adoption), central aspects such as the reduction and restructuring of ministries, or the introduction of non-political state secretaries were reversed/changed by subsequent governments. Both the ministerial structure and the role of the state secretaries proved too politicised to withstand the volatile changes in government.

In an important step to increase the attractiveness of civil service positions, central government salaries were improved significantly in recent years, but resulting wage asymmetries with other public authorities risk cannibalising the potentially positive effects.

In **public procurement**, comprehensive legislative reforms were envisaged as part of the conditionality and successfully delivered by 2020. As a result, the Moldovan regulatory framework is now largely in line with EU *acquis*, and rules are effectively enforced. The NASC is operational, with some delay, since 2017, although it, too, has suffered from the same issues relating to staff shortages, combined with extremely high staff turnover (almost 50% in 2022). The NASC's budget increased steadily between 2019 and 2022.

For **SOEs**, IFI interviewees noted that the major public interest entities were generally compliant with audits, although it appears that compliance (or capacity) with requirements to publish audit reports was low, especially among smaller enterprises. The effectiveness of auditing requirements is diminished by sub-par accounting standards. There are signs that corporate governance is improving in the sector, but change is slow and difficult.

Box 3.8 Fight against corruption and money laundering

In each of the three sub-areas of anti-corruption reforms covered by MFA conditionality, legislative/regulatory reforms were coupled with efforts to establish specialised, independent, operational public agencies.

In the field of anti-money laundering and CFT, a law was introduced that put Moldova on an equal legal footing with EU Member States, strengthening banks' customer due diligence requirements and introducing a register of UBOs. The latter reform addressed a deficiency in shareholder transparency that had contributed to the 2014 bank fraud. At the same time, the Moldovan Financial Intelligence Unit became operationally independent, and the NBM was awarded additional supervisory powers. As a result of reforms in the area, Moldova's ratings for compliance with the Financial Action Task Force (FATF) recommendations were improved in 15 areas and lowered in four.

Another focal point of reforms was the **declaration of assets and conflicts of interest**. The introduction of an electronic system is widely considered an important step forward, enabling ordinary citizens to verify the declarations of any public servants. Deficiencies remain in relation to assets

abroad, posing a serious challenge given the dual citizenship of large parts of the Moldovan population, many of whom own assets in other countries.⁶⁰

In parallel with the development of the e-integrity platform for asset declarations, the MFA conditionality aimed to secure operational **independence and effectiveness of the NIA**, responsible for verification of the declarations. While the budget allocated to NIA was deemed acceptable at the time (an assessment likely partly motivated by government promises to increase the budget over time), this did not materialise, and the budget was significantly cut in 2021. In addition, persistent staffing shortages seriously limit the NIA's capacity to verify declarations and fulfil other important tasks. Nevertheless, the NIA has had some success in enforcing conflict of interest rules, although critics note its ineffectiveness in delivering more high-profile cases. Its role is further limited by the judiciary, which has struck down many of its decisions.

Little progress was made in the **recovery of assets** siphoned out of Moldova as a result of the bank fraud, likely due to the influence of the actors involved. The process was opaque and any such recovery during the MFA implementation phase appeared limited to funds generated by the liquidation of banks bailed out by the state. A dedicated agency for asset recovery (CARA) was set up, but was provided with adequate resourcing only after international pressure.

Box 3.9 Energy sector reforms

Regulatory reforms in the energy sector are among the most impactful measures under the MFA conditionality, although not all were equally effective and one was not implemented until 2023.

The adoption of the Law on Energy and the Law on Energy Efficiency led to further **alignment with the EU energy acquis**. Beyond legislative convergence, the expected improvements in energy efficiency are expected to contribute to Moldova's efforts to become less dependent on external energy supplies, namely from Russia.

In terms of **energy independence**, one of the most important reforms cited was the construction of a gas pipeline between Moldova and Romania, giving Moldova access to the European gas market and thus market leverage over Russia, which in the past had repeatedly sought to exploit Moldova's near-total dependence on Russian natural gas for political gain. The MFA conditionality contributed to an intermediate step in this process by requiring the organisation of a tender for the construction of the pipeline.

Less success was achieved in the **independence of the Moldovan energy regulator**, ANRE. Although condition #8 was considered fulfilled, the EnC Secretariat consistently criticised the lack of de facto independence of ANRE. A particularly problematic law was passed in 2021, against the advice of the Secretariat, allowing for the dismissal of ANRE board members for 'unsatisfactory performance of duties'.

The **unbundling of the state-owned gas system operator**, *Moldovagaz*, was not achieved within the planned timeframe, which was in fact perceived as overly ambitious by EU, government and donor interviewees. However, it was implemented in 2023 and is expected to bring benefits to Moldovan consumers by enabling a more competitive market.

Box 3.10 Business climate and DCFTA implementation

Tangible improvements were achieved under the MFA conditionality in reducing the **administrative burden placed on entrepreneurs** by reducing the number of permits necessary to operate businesses as well as of competent inspection authorities. These improvements were reflected in improved scores on the WB Ease of Doing Business index, including on the components dealing with construction permits, enforcing contracts, getting electricity, paying taxes, registering property.⁶¹

⁶⁰ Interview with national authority.

⁶¹ See <https://databank.worldbank.org/reports.aspx?source=doing-business>.

Important reforms were also implemented in the judiciary where the procedure for the **selection of judges** was amended, and for the first time periodic, transparent competitions were held in Spring 2019, hailed by a CSO interviewee as a step forward from previous *ad hoc* competitions for individual openings. Moreover, rules on disciplinary action against judges were overhauled and transparency was improved with procedural documentation published online. On the other hand, a CSO report criticised the reform for making the procedure more complicated rather than simplifying it.

A **reform of the Superior Council of Magistracy (SCM)**, the judiciary's self-governing body, had been committed to in the MoU but was not satisfactorily implemented in time. More recently, however, promising developments have been noted by CSO interviewees as well as in the Council of Europe Group of States against Corruption (GRECO) 2023 compliance report, noting that half of its members will now be judges elected by their peers and the exclusion of ex officio members like the Minister of Justice and Prosecutor General. As noted above, however, broader reform efforts in the judiciary are yet to bear concrete results in rendering the system more independent and effective.

The **media sector** was brought under the supervision of the Competition Council in 2018; however, the authority has been found by the NGO Freedom House to be ineffective in preventing or addressing dominant positions on the media market. Challenges persist also according to CSO interviewees with regard to media independence, citing the importance of supporting media's financial independency and sustainable financial revenue flows. Still, the departure of media magnate Vladimir Plahotniuc resulted in a certain diversification of ownership in the market (although not attributable to MFA).

Efforts to draft and adopt a **new Customs Code** in line with EU standards have been underway; albeit at a slow pace such that the action was completed only after the MFA II timeframe (as part of the COVID-19 MFA agenda). Recent legislative approximation to EU *acquis* is expected to increase trade with the EU by reducing administrative burdens and enhancing the predictability of customs procedures.

Box 3.11 Financial sector governance

Alongside the energy sector reforms, measures in the financial sector were frequently brought up by stakeholders (EU and national authorities) as among the reforms bringing the most immediate benefits. Measures spearheaded by the IMF but also supported by the MFA (and WB) conditionality succeeded in creating better ownership structures and establishing more transparency.

The adoption of the **Law on Banking Activity** in October 2017 and of subsequent secondary legislation, capital adequacy and risk-weighted ratio in the bank sector were improved, contributing to an overall improved resilience of the sector.

The National Bank of Moldova (NBM) supported this by **investigating Ultimate Beneficial Owners (UBOs)** of Moldovan banks and sanctioning non-compliant shareholders. All three major Moldovan banks (MAIB, Moldindconbank, and Victoria Bank) were acquired by international owners by 2020. A 2019 Moneyval assessment acknowledged improvements of the licensing framework for financial institutions.⁶²

Governance and transparency were also improved in the insurance sector, where the National Commission for Financial Markets (NCFM) implemented an action plan **to identify UBOs** and established a framework for **external audits of insurance companies**.

A **law on non-banking credit institutions** was passed in March 2018, and amended according to IMF and EU recommendations in February 2020, requiring organisations within that ambit to register and placing the sector under the supervision of the NCFM.

⁶² <https://rm.coe.int/moneyval-2019-6-5th-round-mer-repmoldova/168097a396>.

Social impact analysis (SIA)

The overarching aim of the SIA was to use evidence from social indicators and primary data to assess the impacts of MFA II on the social situation in Moldova. The analysis considered both direct impacts of policies specified in the MFA conditionalities and indirect impacts of wider macroeconomic stability across a range of social indicators. The full findings are presented in Annex 10.

Key findings of the SIA in Moldova include:

- **Inconclusive impacts on social assistance targeting.** Evidence on the number of beneficiaries and amounts disbursed by assistance programmes aimed at alleviating the burden of heating expenses for vulnerable households indicate some possible positive social impacts in that the number of beneficiaries declined while average payments increased, suggesting somewhat improved targeting. However, more granular evidence on the types of households receiving the payments is needed for a clearer assessment of the social effects.
- **Some adverse social impacts associated with no first tranche MFA (Alternative A).** In Alternative A, fiscal consolidation was thought likely in the absence of MFA, with social programmes among those likely to see budget cuts. Consequently, there may have been some (though perhaps limited) negative impacts on socioeconomic conditions. For example, total and average payments under the heating allowance programmes may have been reduced in the absence of the first MFA tranche, leaving vulnerable households worse off.
- **Some adverse social impacts associated with no second tranche MFA (Alternative B).** Given that the scale of alternative financing needed and the ability to access these alternatives was similar to Alternative A, the impacts on socioeconomic conditions are likely to be similar under Alternative B. However, unlike at the time of the first MFA tranche, Moldova was facing additional challenges posed by the pandemic and a severe drought at the time of the disbursement of the second MFA tranche, worsening the social and economic climate. In this context, any additional funds may have proven a welcome remedy.
- **Likely positive social impacts associated with third tranche MFA (Alternative C).** In a situation in which the third MFA tranche was disbursed, some positive social impacts might have occurred. Although small, the additional support could have been helpful during the COVID-19 pandemic to maintain or expand social assistance to vulnerable households. In relation to the conditionality linked to the third tranche, the state might have increased the funds available for the heating allowance programme, had the MFA support been made available. Depending on the extent to which the existing programme was/was not providing adequate resources to the intended recipients, there might have been scope to provide further targeted payments to households.
- **Severe deterioration in socioeconomic conditions in the absence of MFA and IMF support (Alternative D).** Socioeconomic outcomes stemming from the absence of any support from IMF and MFA operations would likely have been much more severe. A large financing gap and few alternative sources available for Moldovan authorities would have led to a need for substantial fiscal adjustments, with spending cuts to social programmes and capital/infrastructure investment. Considering the timing of events, with the COVID-19 pandemic and then Russia's war of aggression against Ukraine, the country would have been further burdened. Overall, Alternative D would likely have lowered growth prospects, with indirect adverse effects on employment and a deterioration of socioeconomic conditions through (required) reduced social spending.

Evaluation criterion: Efficiency

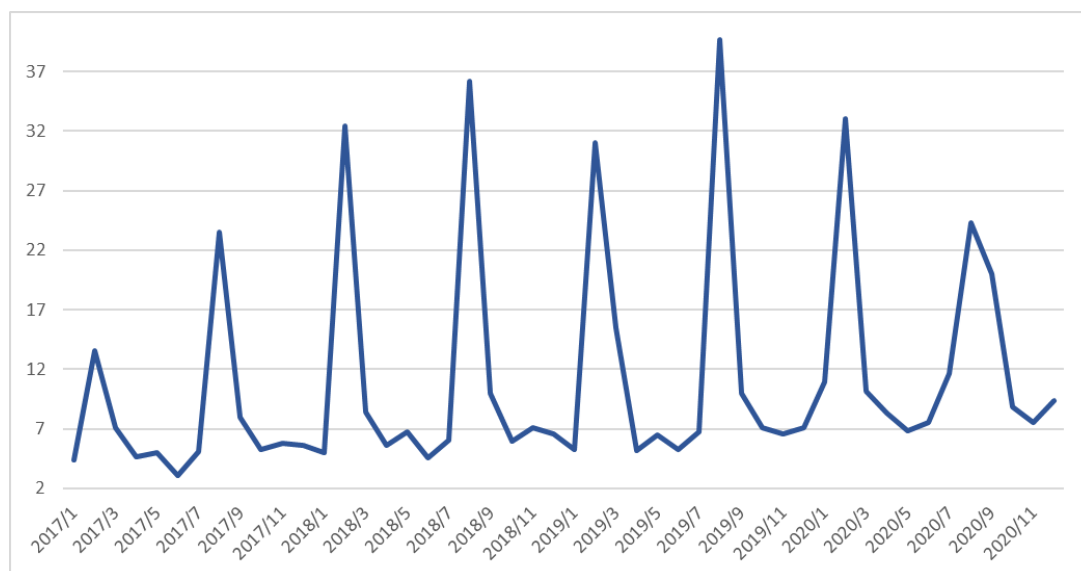
Question: Was the disbursement of the financial assistance appropriate in the context of the prevailing economic and financial conditions in the beneficiary country?

Moldova's economic conditions were challenging at the time of the first disbursement in 2019, given the widening current account deficit (-9% to -11% in 2018-2019, compared to -6% in 2017). Moldova remains unable to issue Eurobonds, limiting its avenues for raising external funds and increasing its reliance on international financial assistance to address its pressing fiscal needs. In terms of debt repayment obligations, Moldova did not face a specific peak in debt repayment obligations over the MFA implementation period and there was a continuous decrease in public debt from 2015 to 2019 (see Figure 4.1).

The disbursement period was relatively calm compared to 2015-2016 when the MFA II was being negotiated. In fact, some local stakeholders noted that the aid would have been even more timely if disbursed before 2017, when the country was facing the worst financial conditions. At that time, there was a more urgent need for external financial capital, caused by the banking fraud uncovered in 2014 and the ensuing high inflation rate. Despite the dire need, however, the political conditions were not met to disburse the MFA earlier: the negotiations for MFA II took longer than usual on the EU side and, once the MFA decision was adopted and conditions were met for the first disbursement to take place, there were other issues with the non-observance of the political preconditions, linked to the invalidation of the mayoral elections in Chisinau. According to economists in Moldova, the delayed disbursement of the first two tranches led to a higher-than-expected execution deficit in 2017 and 2018, when the disbursements were originally scheduled. The government however managed to keep the budget almost in balance, with a deficit of less than 1% in 2017-2018, by cutting some expenditure (executed budget less than planned budget) and resorting to domestic borrowing on relatively unfavourable terms (rates of ~20%).

The second tranche was disbursed in July 2020 and was comparatively timelier, coming amid the COVID-19 crisis, when the need for support was significantly higher.

Figure 4.1. Total external debt repayment obligations, 2017-2020, by month, USD million



Source: Moldovan Ministry of Finance data.

Question: To what extent did the MFA operation design enable the intervention to be carried out efficiently? In what way has the design of the MFA assistance conditioned the performance of the operation in respect to its cost and its objectives?

Several other issues are also worth considering:

Issue 1: Ownership of the programme by the authorities

Under MFA II, national ownership was driven by the urgent need for financing after the 2014 banking fraud and the requirement to attract investment and signal the country's credibility, both internally and externally.

Throughout the period, Moldova experienced fluctuations in its governments' pro-Russia and pro-EU orientations. The association of the Pavel Filip government with oligarchs (as it later emerged) closely linked to the 2014 bank fraud scandal raised doubts about the government's commitment to implementing crucial anti-corruption reforms and ensuring effective asset recovery.

The cancellation of the Chisinau mayoral elections in 2018 (under the Filip government) marked an instance of serious democratic backsliding that knocked the implementation of the MFA II operation off track. After the collapse of the Sandu government in November 2019, which had been perceived as pro-reform, the continuation of the dialogue on the ongoing MFA operation with the ensuing Chicu government was conditional on the fulfilment of eight short-term political actions, required by the EU to reinforce the new government's commitment to democratic principles.

Local civil society and EU interviewees highlighted a gap between the formal adoption of legislative and institutional reforms and their effectiveness in practice. That effectiveness is particularly hampered by the lack of staff in newly established government agencies and the lack of enforcement by the judiciary, which is perceived as a strong obstacle to reform.

At all times, however, Moldova's authorities maintained significant efforts to satisfy the MFA conditionality, driven by the realisation that public perception and political popularity were increasingly tied to adherence to EU-mandated reforms. The consultations showed that the conditions, together with those of other donors, directly determined the policy priorities of all three governments in office during the period of MFA II⁶³. However, the extent to which the required reforms were pursued with real determination by the Moldovan side varied between governments and between reform areas. According to some interviewees, anti-corruption reforms were reportedly treated as a mere box-ticking exercise between 2016 and 2019, when the oligarch, Plahotniuc was leader of the Democratic Party.

As successive governments adopted a more pro-European stance, ownership of the reform programme became instrumental in positioning Moldova as a candidate for EU accession.

Issue 2: Capacity to effectively implement the programme

The Moldovan government's capacity to drive reforms was under close scrutiny from donors. MFA II aimed to contribute by inserting relevant conditions on public administration reform. However, the substantial number of conditions – 28 reforms – contributed to donors' scepticism about Moldova's capability to fulfil all requirements.

Ultimately, the government successfully executed most reforms, with the exception of unbundling energy provider operators and asset recovery. Some EU stakeholders attribute the challenges in energy reform to time constraints, given that the unbundling reform was only implemented in 2023. As a result of the delays in disbursing the first and second tranche, the MFA availability period expired before the third and final tranche could be disbursed.

Despite the achievements, a recurring concern among EU stakeholders is the shortage of adequately trained personnel to staff national institutions and oversight bodies created by these reforms, including the Public Property Agency, Court of Accounts, and NIA. This

⁶³ Interviews with high-level adviser's mission.

significant human resources capacity gap is preventing reforms from delivering the expected benefits.

Issue 3: Liaison and monitoring processes

From the very beginning, it was made clear that the Moldovan operation would be closely monitored. Negotiations on the EU side were very difficult, and a Joint Statement by the EP, the Council and the Commission was attached to the MFA Decision, reiterating the importance of the political preconditions and the need to respect effective democratic mechanisms. It emphasised that the Commission and the EEAS would monitor the fulfilment of this precondition throughout the lifecycle of the MFA. Indeed, utmost attention was paid to this issue, with the EEAS producing several assessments throughout MFA II. The decisions to put the operation on hold were made when the political preconditions were assessed as unmet. Several EU stakeholders (including the Directorate-General for Neighbourhood and Enlargement Negotiations (DG NEAR), EEAS and Directorate-General for Justice and Consumers (DG JUST)) were mobilised to work with the Moldovan side to define and agree the concrete actions that needed to be taken to ensure that MFA assistance could resume.

Another crucial aspect for MFA II was to mitigate the risks of fraudulent use of the funds. The risk was seriously considered in the ex-ante evaluation⁶⁴, given the 2014 banking fraud. To ensure the integrity of its funds, the EU could rely on several safeguarding provisions and monitoring measures typically deployed for MFA operations and with additional importance in this case. In accordance with the Financial Regulation requirements, the Commission services commissioned an operational assessment (OA) of Moldova's financial and administrative circuits. Received in February 2016, the final report acknowledged that the status of administrative and financial circuits was broadly adequate to manage an MFA (although significant weaknesses persisted). MFA conditions and budget support assistance were also used to enhance Moldova's PFM systems, with strong support from other donors. Ongoing monitoring, including through progress reports on PFM reforms by the EU Delegation in Chisinau, closely followed progress on addressing those weaknesses. Both the Loan and Grant Agreements comprised provisions on inspection, fraud prevention, audits, and the recovery of funds in cases of fraud or corruption, while the assistance was subject to verification, control, and auditing procedures under the responsibility of the Commission, including oversight by the European Anti-Fraud Office (OLAF) and the European Court of Auditors (ECA).

To monitor progress with structural reforms, in addition to the standard processes, the DG ECFIN team also benefitted from the presence of Moldovan high-level advisors from the EU on the ground, enhancing specialisation on various sectoral issues. The EU Delegation maintained positive relations with Moldovan authorities throughout the operation and DG ECFIN could rely on its expertise, including leveraging the expertise of other DGs where needed.

Issue 4: Adjustments to implementation in light of unforeseen external events

MFA II implementation was uneven. Given the long negotiation period, some conditions were outdated by the time the MoU entered in force. However, many other conditions remained relevant and there was consensus that the best way forward was to proceed with the agreed MoU. This was not seen as undermining the leverage of the instrument.

With MFA II to Moldova, the MFA as an instrument proved it had the flexibility to be put on hold in light of unforeseen worrying events, e.g. in July 2018, when the Chisinau mayoral

⁶⁴ European Commission, Ex-ante evaluation statement accompanying the document Proposal for a decision of the European Parliament and of the Council providing macro-financial assistance to the Republic of Moldova, SWD/2017/012 final, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD:2017:12:FIN>

elections were invalidated, thus failing to respect the political preconditions. The assistance was successfully resumed once the preconditions were met.

The delays in the planned timeline and non-fulfilment of four conditions triggered the cancellation of the third and final tranche at the end of MFA II availability period. Despite the challenging macroeconomic conditions at the time, amid the COVID-19 pandemic, there is no evidence that the cancellation decision was perceived negatively in Moldova. The decision was largely attributed to political instability, even though four conditions remained unmet and some EU stakeholders deemed some conditions (conditions #23 and #25, on asset recovery and energy sector reforms) unattainable within the original timeframe. The parallel initiation of the EU's MFA COVID-19 operation indicated that the relationship remained unaffected, mitigating concerns.

Issue 5: Visibility and public ownership

Stakeholders underscored the EU's notable standing in Moldova, particularly in recent times. The aspiration to join the EU and be perceived as progressing towards accession has become a matter of paramount public interest, acting as a pivotal metric against which the popularity of governments is measured. The developments around MFA II in Moldova (when it was blocked / unblocked) were closely followed by CSOs and in the media and became a benchmark for government performance domestically.

General EU support to Moldova is widely acknowledged and appreciated. According to the 2018 EU Neighbours East Opinion Poll⁶⁵, a significant 87% of Moldovans are aware of the EU's financial support, marking an 8% increase from 2017 and surpassing the regional average by a considerable margin. There has been a notable 18% rise in those who perceive EU support as effective, reaching 55%. In another recent poll, the EU was chosen as the country's most important economic partner by 72% of participants and as the most important political partner by 67% of participants⁶⁶. CSOs and the general public in Moldova are aware of the reform agenda promoted by the EU. CSOs actively publish reports on various reform areas, aligning with Moldova's commitments under the AA and its obligation to transpose EU directives. Overall, there is strong support for reforms aimed at advancing Moldova's EU integration aspirations, indicating a very positive sentiment towards the country's European path. Stakeholders however noted a need for better communication of the benefits of EU support among the rural population, which tends to be more open to pro-Russian narratives.

Evaluation criterion: Coherence

Question: *To what extent was the MFA II operation in line with key principles, objectives and measures taken in other EU external action towards Moldova in the context of the European Neighbourhood Policy?*

Policy framework and principles

Moldova first entered into a formal Partnership and Cooperation Agreement (PCA) with the EU in 1994⁶⁷.

⁶⁵ EU Neighbours East, *Opinion Survey 2018: Regional Overview*, 2018, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2018-regional-overview/>

⁶⁶ CISR/IPSOS, *Public Opinion Survey*, 2021, https://www.iri.org/wp-content/uploads/2021/04/new_iri_march_21_slide_deck_descriptive_public_release_2.pdf

⁶⁷ Partnership and Cooperation Agreement between the European Communities and their Member States and the Republic of Moldova, <https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A21998A0624%2801%29>

From 2004, Moldova benefitted from a strategic partnership with the EU as part of the European Neighbourhood Policy (ENP)⁶⁸. This political framework complemented the legal relationship under the PCA in the form of individual action plans devising economic, political, and social reforms with short and medium-term priorities that were reviewed in Commission progress reports and evaluation by local experts⁶⁹. The launch of the EaP in 2009 was intended to deepen this partnership and included reinforced commitments to *'the principles of international law and to fundamental values, including democracy, the rule of law and the respect for human rights and fundamental freedoms, as well as to, market economy, sustainable development and good governance'*⁷⁰.

In the energy sector, Moldova has been a member of the EnC since 2009⁷¹. In acceding to the Energy Community Treaty⁷², it committed to the transposition of EU legislation into Moldovan law and to certain measures to permit the operation of the cross-border 'single energy market'. Under the Treaty, Moldova and all other Contracting Parties commit to implement a list of Community *acquis* on energy, environment, competition and renewables (last updated in 2021).

In the so-called Visa Liberalisation Dialogue with the EU, through which Moldovan nationals gained visa-free access to the Schengen area in 2014⁷³, Moldova committed to fulfil and maintain standards related to document security, border management, migration and asylum, public order and security, and external relations and fundamental rights.

Replacing the old PCA concluded in the nineties, Moldova signed an AA⁷⁴ with the EU in 2014, involving comprehensive commitments to gradually align its legislative framework with the EU *acquis*. As part of the AA, Moldova gained access to the single market by becoming part of the bilateral (European Economic Area (EEA)--Moldova) DCFTA. Moldova also made concrete commitments to approximate more than 300 pieces of legislation in the trade sector⁷⁵.

After the Council granted EU candidate status to Moldova (and Ukraine) in June 2022⁷⁶, in November 2023, the Commission recommended opening formal accession negotiations with Moldova.

Moldova

28 November 1994 – Conclusion of the EU-Moldova PCA

⁶⁸ European Neighborhood Policy (ENP), https://neighbourhood-enlargement.ec.europa.eu/european-neighbourhood-policy_en

⁶⁹ Chirila, V., 'New Opportunities for Moldova', *IPG*, Vol. 3, 2011, p. 109.

⁷⁰ Joint Declaration of the Prague Eastern Partnership Summit, 8435/09 (Presse 78), Paragraph 1.

⁷¹ Decision of the Ministerial Council of the Energy Community of 7th MC/18/12/09-Annex 8 on the accession of the Republic of Moldova to the Energy Community Treaty of 27 October 2009, https://energy-community.org/dam/jcr:c5335e2d-aaa9-45ef-8fce-50d3dd535a8c/MC122009_Annex8.PDF

⁷² Treaty Establishing the Energy Community, <https://www.energy-community.org/legal/treaty.html>

⁷³ European Commission, 'Commissioner Malmström on visa-free travel for the citizens of the Republic of Moldova', Press release, 27 April 2014, https://ec.europa.eu/commission/presscorner/detail/en/STATEMENT_14_137

⁷⁴ Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and the Republic of Moldova, of the other part, *OJ L 260, 30.8.2014*, pp. 4-738.

⁷⁵ Centre for European Policy Studies (CEPS), *Ex-post evaluation of the implementation of the Deep and Comprehensive Free Trade Area between the EU and its Member States and Moldova*, Final Report, 2022, pp. 26 ff.

⁷⁶ European Council conclusions on Ukraine, the membership applications of Ukraine, the Republic of Moldova and Georgia, Western Balkans and external relations, 23 June 2022.

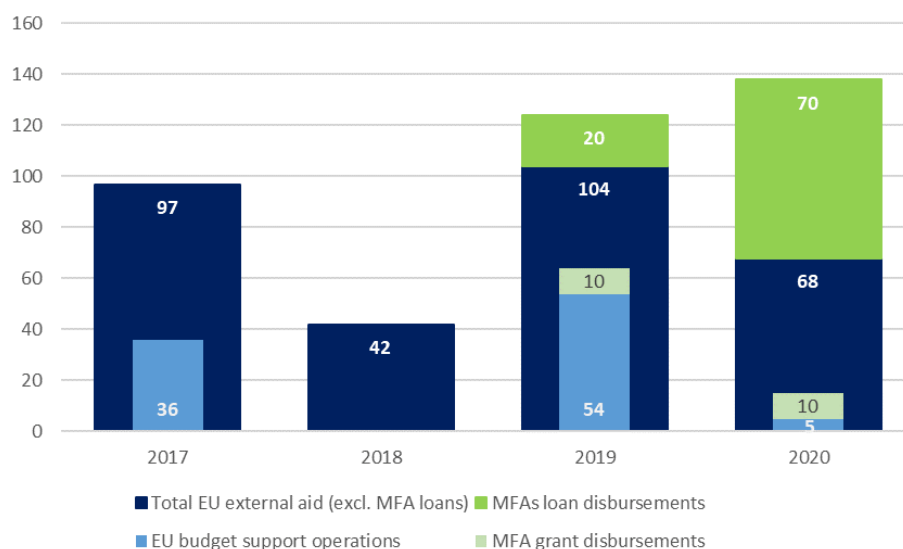
- 29 September 2004** – ENP instrument launched by Commission
- 7 May 2009** – Joint Declaration of the Prague Eastern Partnership Summit
- 27 October 2009** – Accession to the Energy Community Treaty
- 28 April 2014** – Visa-free access to Schengen-area for Moldovans
- 27 June 2014** – Signature of the AA, including creation of bilateral DCFTA
- 23 June 2022** – Moldova receives EU candidate status
- 8 November 2023** – EU Commission recommends opening formal accession negotiations with Moldova

EU assistance to Moldova

Overview of assistance provided via budget support programmes (grants) and MFA assistance (grants/loans)

Figure 3.3 shows MFA loan and grant disbursements compared to total EU external aid and EU 'budget support' assistance over the 2017-2020 period. Moldova experienced large variations in the provision of EU budget support grants. In 2018, both budget support grants and MFA II were put on hold. In 2019, disbursements resumed and those under budget support programmes far exceeded MFA disbursements. The MFA instrument was particularly important in 2020, where disbursements were made under both MFA II and MFA COVID-19 operations. MFA disbursements of EUR 70 million (EUR 80 million including MFA grants) exceeded total EU external aid assistance, and only EUR 5 million was received in the form of budget support grants in that year.

Figure 3.3 EU external aid to Moldova, by type, and MFA 2017-2020, EUR million



Source: Annual reports on the implementation of the EU's instruments for financing external actions; Annual reports on the implementation of macro-financial assistance to third countries (2017-2020); Budget support. Trends and results reports;

Notes: Data refer only to external aid financed through the EU budget and do not include bilateral aid from Member States or financing from the EIB.

Coherence with other EU programmes and initiatives

MFA II versus previous MFA

MFA II might not be considered a linked or follow-on programme to MFA I 2010-2012, which differed in both structure and substance: EUR 90 million, all grants, with only eight conditions. Given the time that elapsed between the two operations and the dynamic political events preceding MFA II, the two programmes are not readily comparable (despite some thematic continuity). This report does not compare in detail the conditions of both operations, as there is no expectation that reform needs and EU priorities would have remained similar.

In brief, the three reform areas in MFA I were public finances and PFM reform, financial sector reform, and legislative and regulatory convergence with the EU, while MFA II focused on public sector governance, financial sector governance, fight against corruption and money laundering, energy sector reforms, and business climate and DCFTA implementation. Looking more closely at both MoUs, there is substantial thematic coherence, particularly in public procurement, financial sector reform, and strengthening the capacity of the NBM. MFA II, however, reflects the dynamics in the Moldovan political situation necessitating an increased focus on governance and combating corruption after the bank scandal.

MFA II operations in the context of the overall EU budget support package

For the MFA II period, 2017-2020, the EU Single Support Framework for Moldova, totalling some EUR 300 million had several key sectors:

- Economic development and market opportunities, including sustainable and inclusive economic growth;
- Strengthening institutions and good governance, including the rule of law and security;
- Connectivity, energy efficiency, environment and climate change;
- Mobility and people-to-people contacts;
- Complementary support for capacity development, institutional and civil society development, and strategic communication.

The MFA II reform areas map directly to sectors 1 and 2 in the Single Support Framework. However, there is only limited overlap with the specific objectives under Sector 1, where the MFA conditionality targeted the financial sector and was thus more complementary. The strongest alignment was with sector 2, particularly with these objectives:

- To prevent and fight corruption, conflicts of interest and fraud (specific objective 1);
- To strengthen independence, accountability, efficiency, transparency and professionalism of the judiciary (specific objective 3);
- To support the independence of the media and increase access to balanced and reliable news reporting for citizens (specific objective 6).

There was also some alignment with sector 4, on the specific goals of promoting energy efficiency and energy sector reforms.

EU budget support programmes targeted several reform areas in 2017 (Economic Stimulation in Rural Areas (ESRA), the European Neighbourhood Programme for Agriculture and Rural Development (ENPARD), Public Finance Policy Reform, and Vocational Education Training)⁷⁷. Some of these had links to MFA II (e.g. public finances). Disbursements under EU budget support programmes were frozen in the same way as MFA II disbursements in 2018-2019, due to concerns over the country's deteriorating rule of law. In 2019, the newly

⁷⁷ IPN, 'EU disburses budget support assistance to Moldova under four programmes', News, 10 January 2017, <https://www.ipn.md/en/economie/81427#!>

installed government made significant progress on reforms, leading the EU to conclude that conditions had been met to resume budget support to the country in July of that year⁷⁸.

Technical assistance

There was close coordination between DG ECFIN and the high-level advisory mission to Moldova. High-level advisors were involved in discussions at different stages of the programme and directly contributed to the selection of conditions, both in the MoU and the short-term political actions required to unlock the second MFA tranche in 2019. They also helped to monitor the implementation of actions, as well as providing technical assistance to advance the reforms.

Stakeholders explicitly noted the complementarity of EU and other technical assistance on the ground with the MFA reform agenda.

IMF and WB programmes

The stakeholder interviews emphasised the level of collaboration and complementarity with the IMF and WB. There was particularly strong complementarity on SOE reform, customs reform, and strengthening financial sector governance.

The EU was alone in targeting the areas of justice/judiciary reform and business climate, although other donors such as the United States Agency for International Development (USAID) were also active in business climate reform. Table 3.5 outlines the cross-conditionality with the IMF and the WB.

Table 3.5 Detailed cross-conditionality with the IMF/WB

Area	Condition	Donors Involved
FIRST INSTALMENT		
Public sector governance	Public administration reform	EU only
	New independent National Complaints Settlement Agency (NCSA)	EU only
	New Law on State and Municipal Enterprises regarding audits and publishing records online	EU only; IMF and WB doing different work with SOEs
	New law on the Court of Accounts	EU only
	New law on the Prevention of Money Laundering and Counter-Terrorism Financing	EU only
Fight against corruption/money laundering	Selection of President and Vice-President of the National Integrity Authority (NIA) by Council	EU only
	New Criminal Assets Recovery Agency (CARA)	EU only
	New Law on Energy; independence of the National Energy Regulatory Agency	EU, IMF

⁷⁸ EU Monitor, 'The EU resumes budget support assistance to the Republic of Moldova', Press release, 23 July 2019, https://www.eumonitor.eu/9353000/1/j9vvik7m1c3gyxp/vl0fgnxdnmtp?ctx=vqaxlcr1jzkn&start_tab0=10

Business climate and DCFTA implementation	Reducing regulations, permits, licences	EU only
	New Customs Service Law	EU and IMF
SECOND INSTALMENT		
Financial sector governance	Banking Activity and Prudential Supervision secondary legislation regarding Basel, capital adequacy, etc.	EU, IMF
	NCFM Action Plan for insurance companies	EU, IMF
Public sector governance	Concessions, PPPs, procurement for energy companies	EU and WB (WB involved in improving procurements for state-owned companies including energy companies)
Fight against corruption and money laundering	Asset declaration and verification	EU
Energy Sector reforms	Energy Efficiency Law	EU, IMF
Energy sector reforms	Tender for the construction of the Chisinau-Ungheni pipeline.	EU only
Business climate and DCFTA implementation	Criteria for the selection and the promotion of judges	EU only
	Disciplinary liability of judges	EU only
THIRD INSTALMENT		
Financial sector governance	NBM identification of UBOs of qualified shareholders	EU, IMF
	Deposit insurance	EU, IMF
	Non-bank credit organisations	EU, IMF
Fight against corruption and money laundering	National Integrity and Anti-corruption Strategy (NIAS) for 2017-2020	EU only
	Implementation of asset recovery strategy	EU, IMF
Energy sector reforms	Social assistance programmes related to energy tariff adjustments, in particular the Ajutor Social and Heating Allowance programmes	EU, IMF
	Unbundling of the three system operators in the gas sector	EU, IMF
Business climate and DCFTA implementation	Amendments to the Law on Competition	EU and WB (WB efforts on competition were conditional in an earlier operation in 2015-2016)
	New Customs Code consistent with the EU Customs Code	EU only (WB active in customs area.)

Adopt primary and secondary legislation to strengthen the position of the Superior Council of Magistracy	EU only
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Source: ICF review of documentation.

3.3 How did the EU intervention make a difference and to whom? [Related criterion to assess: EU added value]

3.3.1.1 Financial added value

Moldova's limited access to capital markets in the aftermath of the 2014 banking fraud, coupled with its inability to issue Eurobonds, exacerbated liquidity challenges at the time. The MFA assistance provided to Moldova was not merely symbolic: alongside IMF budget support, MFA II played a crucial role in closing the budget gap and maintaining the balance of payments. Nevertheless, additional assistance would have been beneficial, particularly in early 2020 when the COVID-19 pandemic struck the economy, with individuals with modest incomes bearing the brunt of the impact. A COVID-MFA package was ultimately signed in May 2020 for this purpose.

However, the financial benefits of MFA II to Moldova extend beyond the amount of the assistance. The backing from the EU and the extension of the IMF programme were crucial in helping Moldova to weather the COVID-19 crisis in 2020 and ensuring ongoing support. MFA II also stood out as a 'blended' operation, i.e. including a (relatively uncommon) grant component. The actual MFA loan / grant split was EUR 40 million / EUR 20 million, the concessionality of the different MFA disbursements can be estimated to be higher, worth about EUR 40 million, using the IMF calculation of grant element tool⁷⁹.

Table 3.6 MFA Concessionality results

Disbursement	MFA loan/grant split (in EUR million)	Concessionality	
		Grant element (%)	Grant equivalent (in EUR million explicit grant)
MFA II -first tranche	20/10	66.55%	19.97
MFA II – second tranche	20/10	66.55%	19.97
MFA II - total	40/20	66.55%	39.94

Source: authors' calculations

The value of MFA assistance also lay in its terms and conditions (see Table 3.7). In the case of MFA, the grace period for repayment is longer than that provided by all other donors, with repayment occurring in a bullet format at maturity. Typically, the grace period lasts around five years, with repayments starting after approximately one-third of the loan duration has passed. The interest rate for this MFA operation (2017-2020) is also lower compared to other donors, at 0.125-0.20% (IDA interest rates: 0.75-2.0%).

Table 3.7 Average terms and conditions of budgetary support assistance to Moldova, 2017-2020

Average terms and conditions of assistance disbursed over 2017-2020

⁷⁹ Calculation of grant element. (2022, February 10). IMF. <https://www.imf.org/en/GECalculator>

	Amount disbursed over 2017-2020 (USD million)	Interest rate	Maturity (years)	Grace period (years)
MFA II loan	43	0.125-0.20%	15	15
EU budget support grants	133.7	N/A		
Government of Romania	100.9	N/A		
IMF EFF	314.04	1.1%	10	4.5
IMF ECF			10	5.5
IMF RFI			10	4.5
IMF RCF			10	5.5
IDA	40.8	0.75-2.0%	20-30	5-10
EIB	20.6	0.305-1.566%	25	5

Source: Moldovan Ministry of Finance data and ICF calculations.

3.3.1.2 Non-financial added value

Signalling effect to civil society and the general population

Given the damaged credibility of domestic institutions among the Moldovan population, and because of its broader political dimension compared to the IMF programme, the EU's MFA support acquired a certain symbolic status as a benchmark for government performance domestically. When the first and second disbursements were put on hold due to non-compliance with the political precondition, this strongly reverberated in the domestic political space.

Apart from its economic implications, the freeze was perceived by many as a confirmation of the government's lack of commitment to democratic values. On the other hand, when discussions resumed after the election of a new government, this was seen as a sign of support from the EU.

An interviewee from a national authority also pointed to the role of EU MFA, particularly its political dimension, in tilting the balance between the competing pro-Western and pro-Russian narratives in Moldova. This was particularly important in living up to expectations placed on the EU as a force for reform at a time when it emerged that the leadership of the Democratic Party had been involved in the bank fraud. However, Moldovan interviewees emphasised the need to improve communication on the benefits of EU assistance, particularly in the more rural and Russian-speaking communities.

Confidence-boosting effects

Together with the other assistance packages provided to Moldova during the period, MFA II helped to regain investor confidence after the shock of the bank fraud crisis in 2014. In 2017, when the MFA II MoU was signed, Moody's improved Moldova's rating outlook from 'negative' to 'stable', while confirming the B3 rating that the country had held since 2010. More recently, however, the country's investment climate has been dominated by exogenous risks related to Russian aggression in the region⁸⁰. Moldova's reliance on EU support is also heightened because, unlike other European countries, it cannot issue Eurobonds. Despite discussions in 2020 about involving Moldova in Eurobond issuance with assistance from a major international bank, it lacks credibility to attract external financing and capacity to absorb funds due to governance issues, corruption, and slow reform.

Reinforcing Moldova's call for reform and conditionality design

The consultations confirmed that the financial and political weight of the MFA operation, as well as other conditionalities related to financial assistance, led to a clear prioritisation of the associated reforms.

EU Commission interviewees noted that regardless of the success of conditionality, the mere fact that an issue was on the agenda meant it provided an opportunity for political dialogue. From the Moldovan perspective, including an issue from the government's agenda as a condition could help to overcome internal resistance.

In Moldova's politically volatile context, with three different governments during the MFA implementation period, the reform conditionality represented a common thread for reforms, as all governments attached high importance to it, irrespective of their political leanings.

Despite some doubts about the ownership of some of the structural reforms implemented under the MFA conditionality (among certain political actors) and their effectiveness in practice, the package helped Moldova to achieve a more modern legislative and institutional framework, supporting the efforts of the strong forces in the country committed to a more competitive, democratic and rule-based order.

4 Evaluation findings: Georgia

4.1 Was the intervention relevant? [Related criterion to assess: relevance]

Question: *To what extent was the MFA operation design (including adequateness of financing envelope, focus of conditionality) appropriate in relation to the outputs to be produced and objectives to be achieved?*

Four essential issues will be considered here: (i) adequacy of the size of the financial assistance, (ii) appropriateness of the form of financial assistance, and (iii) design, and (iv) focus of conditionality.

Issue 1: Size of the financial assistance

Size of the financial assistance vs expectations

All three MFA operations to Georgia since the military conflict with Russia in August 2008 were broadly the same size (EUR 45 million for MFA III, EUR 46 million for the first two). In its request for further MFA support, the government of Georgia did not specify the amount it

⁸⁰ Interview with Moldovan authority.

was expecting. The final size of the operation approved by the co-legislators corresponded to the amount proposed by the European Commission.

Size of financial assistance vs financing gap and burden-sharing considerations

According to the European Commission proposal, MFA III to Georgia was expected to be disbursed in full in 2018 or split between 2018 and 2019. Given the size of the residual financing gap estimated by the IMF at the time, this meant that MFA III was designed to make a significant contribution: 53% of the 2018 residual financing gap, or 35% of the 2018-2019 residual financing gap. Full disbursement in 2018 would have exceeded the indicative ceiling as defined by the Council in 2002 of one-third of the residual external financing gap (for countries that do not have candidate status and potential candidate countries)⁸¹. The most likely outcome, however, was that disbursements would be spread over time (the Commission put MFA III in perspective with the residual gap for 2017-2020 in its proposal). Indeed, MFA III actual disbursements were spread over a longer period of time (2018-2020) and the actual EU contribution was more diluted than expected (see Table 4.1). One ex-ante justification for covering a large share of the residual financing gap (slightly more than one-third of the 2018-2019 gap) was to reward Georgia for its good reform track record, in line with the 'more for more' principle⁸².

At the same time, the stated objective was to remain proportionate. MFA III was calibrated to constitute 12% of the estimated total financing gap and was commensurate with IMF contribution (82% of 2018-2019 IMF *net* disbursements). Other major IFIs and donors were expected to make significant contributions, namely the WB (expected to contribute as much as the IMF and the EU jointly) and the Asian Development Bank (see Table 4.1).

Table 4.1 MFA and the estimated financing gap, 2018-2019

USD million	2018	2019	Total 2018-2019
1. Current account balance	-1,849	-1,836	-3,685
2. Capital and financial account balance	1,942	2,076	4,018
3. Overall balance (1+2)	93	240	333
4. Reserves ('-' indicates increase)	-315	-423	-738
5. Overall external financing gap	-222	-183	-405
6. Exceptional financing by IMF and WB			
Net IMF disbursements	27	34	61
Disbursements by WB	100	100	200
7. Residual financing gap	-95	-49	-144
Financing of the gap			
MFA III	50		50
Asian Development Bank	50	50	100
Total identified sources	50	50	100
Total MFA as % of residual gap 2018-2019			35%

⁸¹ This indicative ceiling is still referenced in practice, despite more recent principles being available. The Joint Declaration of 12 August 2013 of the Parliament and the Council on Macro-Financial Assistance no longer specifies indicative ceilings.

⁸² Note for the Alternates of the Economic and Financial Committee, attached to the 2017 MFA III proposal.

includes disbursements under budget support programmes (all grants); ** Includes IMF disbursements directed to budget support and directed to reserves. Only EUR 181 million was recorded as budget support in 2020 in Ministry of Finance data.

Issue 2: Form of the financial assistance

In its proposal, the European Commission explained that Georgia still qualified for a grant component.

At the time, in 2017, Georgia was still classified by the WB as a lower middle-income country (it moved sustainably to the upper middle category in 2018). The incidence of poverty was assessed as quite high, including by regional standards (25.3% of population living below relative poverty line, as per latest (2014) WB data). Levels of public debt and external debt were presented as sustainable but increasing (reaching 45% and 112% of GDP, respectively, at the end of 2016), thus a source of vulnerability, given the high dollarisation (average dollarisation ratio of the total non-bank deposits 67-70% in 2015-2016).

However, given Georgia's recent graduation from IMF or WB concessional financing (Georgia was eligible to receive IDA resources until the fiscal year 2014), the loan element was prioritised (22% of the proposed assistance in grants under MFA III, compared to 50% under MFA II and full grant MFA I).

Despite comprising both grants and loans, the ex-post evaluation of MFA II confirmed that the gradual transition to MFA provided as loans was broadly coherent with the improvement of the situation in Georgia. It noted that the terms of MFA II remaining very favourable and estimated it to have contributed to significant fiscal savings (amounting to EUR 31 to EUR 34 million or 0.3% of GDP) compared to market-based alternatives⁸⁴. Fiscal savings from lower borrowing costs as a result of MFA III loans were estimated to be similar, at around EUR 29 million (roughly corresponds to an additional tranche) (see section on Debt Sustainability Analysis).

Annex 14 presents an indication of the uncommitted budget allocations for MFA grants. In 2018 and 2019, when the commitment for the MFA III was meant to materialise, EUR 31 million and EUR 17 million, respectively, remained uncommitted. EU budgetary constraining was not the main limiting factor explaining the reduction in the share of the grant component for MFA III (another EUR 10-15 million in grants could have been accommodated from a budgetary perspective).

Issue 3: Focus of conditionality

High-level analysis

The design of the MFA conditions was inspired by – and will be assessed against - the general principles summarised in Figure 3.2. The evaluation of MFA II to Georgia completed in 2019 had not flagged any particular lesson on how the design of MFA conditions could be improved in its case, with the design considered solid overall. At the time of the MoU negotiations for MFA II in 2014, the Commission proposal for MFA to Georgia was 'taken hostage' by the co-legislators for several years, thus conditions were designed to allow rapid disbursement and most were met before the signature of the MoU. Under MFA III, there was no comparably strong focus on actions that could be met quickly. Indeed, some implementation challenges were experienced in relation to some of the conditions.

⁸⁴ European Commission, Evaluation of Decision No 778/2013/EU of the European Parliament and of the Council of 12 August 2013 providing further macrofinancial assistance to Georgia, SWD(2019) 447 final.

Extent to which conditionality was in line with core objectives of the operation and EU priorities

MFA III to Georgia included 11 conditions in the following reform areas: (i) PFM; (ii) financial sector; (iii) social and labour market policies; (iv) business environment.

Broadly speaking, many of these reform areas had a link either to the objectives of the MFA instrument (PFM, financial sector) and/or EU external policy objectives (business environment). All supported the association process with the EU (notably in relation to the judiciary). Very strong alignment with both EU budget support programmes and programmes of other donors and IFIs stood out in MFA III to Georgia. The choice of the conditions seems to have been dictated by this willingness to push for reforms already being promoted via other EU instruments. The aim was to unblock/accelerate progress or capitalise on the option under the MFA instrument to include less specific/detailed indicators in the pursuit of broader objectives (compared to how indicators need to be defined under budget support operations).

It was understood that because Georgia had already progressed on many macro critical issues typically addressed by MFAs (e.g. resilience of the financial sector, basic PFM reforms), the MFA conditions could address less macro significant topics that were nevertheless important in Georgia (e.g. Motor Third Party Liability Insurance (MPTL) Law, PPP legal framework).

Number of conditions and scope of conditionality

The number of conditions increased slightly between MFA II and III, from eight to 11. The number of conditions was not raised as an issue by any stakeholder. Rather, there was an understanding on the part of the national authorities that the reform agenda was 'homegrown' and the reform process mostly driven by the government of Georgia.

For the more challenging conditions (condition #4, on the adoption of the MPTL Law, which required a waiver, and condition #10 on the Law on Entrepreneurs, which delayed the second disbursement), no particular issue was raised in relation to their ambition. In the case of the MPTL Law, it matched a parallel commitment under an EU budget support programme. In the case of the Company Law, the first draft was submitted for finalisation to the Ministry of Justice in 2016 and the Regulatory Impact Assessment had been completed by October 2017⁸⁵. The MFA III condition only required submission of the law to the parliament.

Complementarity/cross-conditionality with other EU and IFI programmes

See discussion in Section Evaluation criterion: Coherence.

Extent to which MFA III addressed priority areas for reforms, relevance of specific reform areas, and conditionalities

Many of the MFA III conditions supported the national reform agenda, the so-called 'Four Point Reform Plan 2016-2020'⁸⁶, focused on improving the business environment, education and public administration, as well as investment in infrastructure. As the country's reform agenda was underpinned by its commitment to the implementation of the AA/ DCFTA, it also corresponded to EU priorities. Other IFIs/ donors were aligned with the same reform priorities.

⁸⁵ ISET, *Regulatory Impact Assessment (RIA) of the Draft Law of Georgia on Entrepreneurs*, 2017, <https://iset-pi.ge/en/publications/ria/1829-regulatory-impact-assessment-ria-of-the-draft-law-of-georgia-on-entrepreneurs>

⁸⁶ Government of Georgia, *Government platform*, November 2016, https://www.gov.ge/files/41_61087_816118_GoG_Platform_LKF_19_05_2017.pdf

Even if many conditions targeted areas with historically strong domestic ownership of reform, MFA III did not focus exclusively on simpler reforms. The most difficult reforms contained in the MoU, as assessed ex-ante, were linked to public procurement and the judiciary.

In the case of PFM, Georgia had championing PFM reform for many years, adopting successive reforms plans (Public Finance Management Reform Policy Vision 2009-2013, Public Finance of Georgia Management Reform Strategy 2014-2017) and orchestrating continuous technical assistance from the EU, WB and IMF. Within the broad PFM field, the MFA focused on specific aspects with identified weaknesses, as per the OA of Georgia's financial and administrative circuits in September 2017, conducted as part of preparing the Commission proposal on MFA III. It included some more difficult conditions on public procurement and procurement complaints management, where a lot of work was needed to turn the existing Dispute Resolution Council into an impartial and independent body, in compliance with the AA.

Similarly, in relation to business environment, Georgia was highly regarded in terms of ease of doing business, thanks to its rather favourable tax regime, access to simple e-services, and earlier reforms to eliminate petty corruption. The MFA conditions focused on the more challenging aspects, such as judicial reform, where a lot of work was needed to approximate EU legislation. Previous efforts under a sectoral budget support programme had brought mixed results.

Other conditions considered politically easier to implement addressed priority needs, e.g. de-dollarisation of the economy and skills mismatch in the Georgian labour market.

As to whether the MFA could potentially have focused on more pressing weaknesses, it seems that a good balance was struck overall, but some would have expected a focus on the reform of SOEs (improving their corporate governance as in the subsequent MFA COVID-19 package or, from a PFM point of view, improving oversight of aggregate fiscal risks from SOEs).

Box 4.1 PFM

Given the nature of MFA assistance, PFM is often systematically targeted by MFA conditions. Georgia is at the forefront on many PFM aspects and in the 2018 PEFA assessment, the Ministry of Finance and the Government of Georgia were praised for having implemented PFM reforms for more than 10 years⁸⁷. In the Open Budget Survey (OBS) published in 2022, Georgia ranked first on 'Transparency', which takes into account the online availability, timeliness, and comprehensiveness of eight key budget documents, using 109 equally weighted indicators. It was already classified among the most transparent countries in previous editions (ranked fifth in the global ranking in 2017 and 2019)⁸⁸.

Yet some gaps remained to be addressed and Georgia was at the time preparing for the implementation of its third Public Financial Management Strategy, 2018-2022⁸⁹.

MFA III conditions focused on issues of public investment: public investment management (PIM), i.e. the selection of projects for public investment (condition #1) and the way public investment is carried out, notably by means of PPP (condition #2) and public procurement (condition #3). This focus reflected the planned increase in public investment, as per Georgia's 2017 Four Point Reform Plan⁹⁰ (with a target spending rate on public investment of 8% of GDP over the 2017-2020 period).

⁸⁷ PEFA, Georgia 2018, <https://www.pefa.org/node/276>

⁸⁸ Open Budget Survey, Georgia country assessment, 2021, <https://internationalbudget.org/sites/default/files/country-surveys-pdfs/2021/open-budget-survey-georgia-2021-en.pdf>

⁸⁹ Ministry of Finance, Public Financial Management Strategy to 2018-2022, <https://www.mof.ge/5189>

⁹⁰ Government of Georgia, *Government platform*, November 2016, https://www.gov.ge/files/41_61087_816118_GoG_Platform_LKF_19_05_2017.pdf

It was areas where Georgia was performing less well according to the PEFA assessment (with scores ranging from B to D depending on the issue)⁹¹, even if progress was noted before the start of MFA III. In the OA conducted in 2017 ahead of MFA III (updating the 2011 assessment), the consultants noted enhanced analysis and disclosure of fiscal risks and the transparent nature of Georgia's e-procurement system. Further progress was still required, however. Most of the specific MFA (sub-)conditions featured among the OA's identified priority areas for action: implementation of the recently adopted PIM guidelines, reduction in the use of emergency and single source procedures for public tenders, remedying the lack of impartiality and independence of the Dispute Resolution Council (also required by the AA).

The PPP Law had recently been submitted to the parliament as per an IMF requirement. In addition to donor coordination aspects, the rationale in including it under MFA III was to ensure that it would align with relevant EU rules/AA (e.g. concessions).

Box 4.2 Financial sector

The banking sector in Georgia is generally described as profitable and healthy, if quite concentrated – it exhibits large capital and liquidity buffers and NPLs consistently remain at low levels (see also Annex 8). The National Bank of Georgia (NBG), working with the IMF and other central banks, has acquired a strong reputation. It was described in the 2017 OA as able to retain skilled staff, and also holds a seat on the International Operational Risk Working Group, sharing best practices on risk management and governance with other central banks within and outside the region⁹².

The high level of dollarisation remained a challenge and made the sector vulnerable to potential exchange rate volatility. Condition #5 aimed to support the NBG in its efforts to improve banking supervision (Pillar 2 of the Basel III framework), in line with the recommendations of the 2017 OA, and to promote better corporate governance and better management of dollarisation risks across the financial sector as a whole.

The non-bank segment and insurance market are very underdeveloped by comparison (holding no more than 8% of the total financial sector assets, according to the EFC note). Car insurance is not mandatory and road safety is a major problem in Georgia. Accidents, deaths, injuries and damage create a social burden for those having to pay liabilities, and victims are not always adequately compensated.

Extending the mandatory character of third-party liability insurance to domestic vehicles had been on the agenda for several years. The ambition was to ensure gradual alignment with EU and United Nations (UN) insurance standards and facilitate Georgia's membership in the International Motor Insurance (Green Card) System. It was also part of the budget support programme, Economic and Business Development in Georgia, 2019-2022, designed in parallel with MFA III.

Box 4.3 Social and labour market policies

Before MFA III, Georgia had recently emerged from a period of strong deregulation in its social and labour market sector.

A Universal Healthcare System (UHC) was introduced in 2013 to tackle poor access to healthcare and extremely high levels of out-of-pocket expenditure for healthcare services. Healthcare became a top priority for the government following the election in 2012, which led to the launch of the UHC in 2013⁹³. Ensuring its sustainability then became a priority, due to the significant benefits it generated (increased access to healthcare, reduced out-of-pocket payments). Selective contracting in the UHC was piloted by the Ministry of Internally Displaced Persons, Labour, Health and Social Affairs in March 2017.

⁹¹ PEFA, Georgia 2018, <https://www.pefa.org/node/276>

⁹² IMF, *Reining in risk to enhance financial stability in Georgia*, n.d., https://www.imf.org/external/np/ins/english/capacity_countries_mfs_georgia.htm

⁹³ Ecorys, *Ex-post evaluation of Macro-Financial Assistance to Georgia*, 2019.

Condition #6 focused on the extension of selective contracting to medical treatments, other than maternity care, covered by the UHC. It aimed to improve the sustainability of the UHC system by controlling costs while ensuring higher quality of services. This was important because, following the introduction of the UHC, the government was consistently overspending on healthcare, increasing by 3% between 2015-2017, for example.

Georgia's labour market policies were heavily deregulated before the change in government in 2012. A state employment service and labour inspection service began to be developed in 2015, with improvements in labour market regulations becoming a priority. Following a series of highly publicised workplace deaths, the Prime Minister raised the need to reactivate the labour inspection system. Similarly, the reestablishment of the public employment service (PES) was in development in Georgia since before MFA III. Georgia's commitment through the AA had an important role in enabling reform progress (e.g. the Association Agenda for 2014-2016 contained a direct reference to the need to establish a labour inspection service).

In the years preceding 2017, there was increased focus and financing of VET, following recognition of an oversupply of highly educated workers in the Georgian economy, but insufficient availability of vocational skills. In 2016, education, including the introduction of VET, was highlighted in the Government's Four-Point Reform Plan⁹⁴. A Strategy for VET reform covering 2013-2020 was also prepared (with EU technical support)⁹⁵ and adopted. Several international donors, including the WB, were involved in promoting VET reform before MFA III. However, some stakeholders highlighted that Georgian society's prioritising of higher education mean that VET tended to be less scrutinised by the government and society.

Condition #7 focused on developing a new labour market strategy and action plan, including the introduction of a PES, labour inspection system, employment-related legal framework, and system for labour market analysis and forecasting. Unemployment in Georgia was relatively high and persistent, driven by structural issues such as limited labour mobility and skills mismatches. There was also a relatively high rate of workplace accidents and deaths in Georgia (by international standards), leading on several occasions to public unrest and demonstrations. In targeting skills mismatches within the Georgian economy and labour force, condition #8 centred on the improvement of the VET offer through the adoption of the VET Law.

Box 4.4 Business environment

Overall, the business environment in Georgia was very favourable, with Georgia ranking seventh among 190 countries in the WB 2020 Doing Business Index⁹⁶. However, the specific areas targeted by MFA III created challenges.

For example, condition #9 targeted the registration of 500,000 plots of land according to the temporary rule for simplified registration, as well as the adoption of an action plan to roll out systematic registration. Following the collapse of the Soviet Union, land reform was implemented to privatise land previously owned by the state. However, initial land registration processes suffered from technical issues, leading to incomplete and inaccurate records. This condition aimed to develop a functioning land market in Georgia, building on the introduction of the Law on the Special Rule for Systemic and Sporadic Registration of Land Parcels within the State Project and Improvement of Cadastre Data, that simplified the land registration process in 2016 and launched a process of sporadic land registration. The aim was also to build on the Justice Budget Support Programme 2015-

⁹⁴ WB, *Second Programmatic Private Sector Competitiveness Development Policy Operation Programme Document*, 2017, <https://documents1.worldbank.org/curated/en/478801501725663367/pdf/Georgia-Private-Sector-Competitiveness-Development-Policy-Operation.pdf>

⁹⁵ Unified Strategy for Education and Science for 2017-2021, chrome-extension://mhnlakgilnojmhinhkckjpnpcpbhabphi/pages/pdf/web/viewer.html?file=https%3A%2F%2Fplanipolis.iiep.unesco.org%2Fsites%2Fdefault%2Ffiles%2Fressources%2Fgeorgia_unified_strategy_of_education_and_science_2017-2021_0.pdf

⁹⁶ Agenda, 'Georgia is 7th among 190 states in the World Bank Doing Business 2020 ranking', News release, 24 October 2019, <https://agenda.ge/en/news/2019/2857#:~:text=Georgia%20has%20ranked%207th%20among,the%20UK%2C%20Norway%20and%20Sweden.>

2017, where slower than planned progress had been made. Land registration was high on the government agenda since before MFA III – it was referenced in the national government program and is also covered by the 2030 Vision for Georgian Development⁹⁷ and in the 2017 Four-Point Plan. Other donors, notably the WB, were active in promoting reform in this area, including supporting systematic registration pilot projects since 2016.

Georgia's Law on Entrepreneurs was adopted in 1994. In 2008, large-scale legislative changes were made to allow for deregulation and flexibility for corporations, the objectives of which later failed, requiring further changes to the law. Condition #10 targeted revisions to the law to enable it to meet modern requirements and align with EU law by incorporating several relevant directives, in line with the requirements of the AA. Changes, such as developing a legal base that would facilitate entrepreneurship, was also one of the key pillars in Georgia's Four-Point Plan for national structural reform⁹⁸.

MFA III targeted reform within Georgia's judicial system. Condition #11 aimed to increase the independence and quality of Georgia's judiciary by ensuring the publication of all court rulings, the proper implementation of the system of random allocation of cases, and the publication of statistical data on disciplinary procedures against judges. While Georgia had been successful in implementing reforms to eliminate petty corruption, trust and the independence of its judiciary remained a challenge. This was high on the government agenda since 2013, when the first wave of large-scale reforms were implemented. In fact, condition #11 focused on improving reforms that had already been introduced by authorities in Georgia in 2017 (to introduce random electronic allocation of cases and an institution of disciplinary inspectors, as well as mandating the publication of court judgments).

4.2 To what extent was the intervention successful and why? [Related criteria to assess: effectiveness, efficiency, coherence]

Evaluation criterion: *Effectiveness*

Part 1: assessment of the macroeconomic role of MFA III

Examining observed macroeconomic outcomes over the MFA disbursement period (2018-2020)

The MFA III operation came at a time of severe regional disruptions that adversely impacted Georgia and neighbouring countries. Persistent exposure to geopolitical instability and a weak external environment contributed to sluggish growth. Over the period 2015-2017, Georgia posted slower growth (compared to previous years), which averaged to about 4.0% yearly. However, improved economic dynamics in the region, a rebound in demand and consumption, supportive fiscal spending, and strong policy efforts boosted economic activity and output growth in the years that followed. Georgia was significantly affected by the COVID-19 crisis, when the economy shrank by almost 7%. On the back of depressed demand, food and commodity prices fell considerably. This helped to rein-in inflation, which had been persistently high since 2017 (except in 2018), averaging about 7% in 2017 and 2019. High inflation in those years was explained by an increase in excise taxes by the Georgian government in 2017. The currency crisis in Turkey, one of Georgia's foremost trading partners, and a ban on flights to Georgia by

⁹⁷ Government of Georgia, *Development Strategy of Georgia - Vision 2030*, 2022, <https://leap.unep.org/en/countries/ge/national-legislation/development-strategy-georgia-vision-2030>

⁹⁸ Ministry of Finance, *Georgia Reforms to Development*, 2017 https://www.mof.ge/images/File/BROSHURA/2017/Georgia%E2%80%93Reforms_to_Development.pdf

Russian authorities in 2019 reducing tourism inflows also caused the Georgian lari (GEL) to depreciate and the price of imported goods and services to go up. Despite having receded in the previous decade, unemployment remained high and was well above average unemployment levels observed in the other EaP countries. Between 2018 and 2020, Georgia's unemployment rate averaged about 18%, explained by deep-seated structural problems in the labour market, notably an underutilisation of labour resources and, in 2020, the COVID-19 pandemic, which triggered a jobs crisis.

Mounting fiscal pressure prompted the Georgian government to embark on an ambitious fiscal consolidation programme from the mid-2010s. Tighter control of government spending (other than social and education spending) and higher fiscal revenue, supported by improved economic activity, helped to narrow the fiscal deficit. By 2018, the fiscal deficit had fallen to 0.8% of GDP from a yearly average of 1.2% recorded over the 2014-2017 period. A small contraction in government debt was noted in 2018, when it reached 38.9% of GDP (compared to 39.4% in 2017). The 2019 budget allowed for higher social spending, along with continued investments in infrastructure and education, and the implementation of targeted public sector wage increases for some public sector workers. The fiscal deficit increased to 1.8%, while government debt rose to 40.4% (within the acceptable limit of 45% of GDP set by Georgian authorities as part of its fiscal consolidation efforts). The fiscal deficit widened further during the COVID-19 pandemic owing to the substantial (financial) support offered by the Georgian government to vulnerable households and businesses, additional spending to support economic activity, and emergency healthcare expenditure (personal protective equipment (PPE), quarantine hotels, etc.). Georgia recorded a high fiscal deficit for 2020, at almost 10.0% of GDP. Similarly, the government debt-to-GDP ratio rose to 60.2% that year (slightly surpassing the Georgian government's debt ceiling, mandated at 60% of GDP under the 2011 Organic Law of Georgia on Economic Freedom).

Rapid and sustained growth in exports, tourism receipts and remittances helped to improve Georgia's external position from the mid-2010s. By 2018, the current account deficit had fallen to 6.8% of GDP, further receding in 2019 to a historic low of 5.9% of GDP. This was mostly driven by a stronger goods trade balance, largely driven by motor car re-exports, whose share grew from 9.9% of total exports in 2017 to 14% and 20% in 2018 and 2019, respectively (according to the NBG). These improvements were short-lived, however. The COVID-19 pandemic brought about a deterioration in Georgia's external position due to its devastating economic consequences for the tourism sector. As a result, the current account deficit surged to its highest level of the decade, reaching 12.5% of GDP in 2020. In contrast, the trade deficit (pertaining to the trade of goods) narrowed slightly following decreases in both domestic and external demand. It reached 20.0% of GDP in 2020 (from 25.4% and 21.7% in 2018 and 2019, respectively), the lowest level observed in a decade.

FDI inflows were severely adversely impacted by the COVID-19 pandemic. They (more than) halved in 2020, reaching 3.5% of GDP (compared to 7.9% of GDP in 2019)⁹⁹. The main reasons for the decline were the COVID-19 pandemic, transfer in ownership of several companies from non-residents to residents, and the completion of a large-scale investment project¹⁰⁰. Georgia's external debt was already elevated before the pandemic (averaging 94% over the 2010-2017 period, and 104% over 2018-2019), and grew further,

⁹⁹ Macrotrends, Georgian Foreign Direct Investment 1993-2024, n.d., <https://www.macrotrends.net/countries/GEO/georgia/foreign-direct-investment>

¹⁰⁰ World Trade Organization, Trade policy review Georgia, 2021, https://www.wto.org/english/tratop_e/tpr_e/s420_e.pdf.

reaching 129.8% of GDP in 2020, reflecting the Georgian government turning to outside sources to finance various stimuli measures to aid the economy.

Up to and including 2017, gross financing needs represented less than 5% of GDP. However, that ratio then increased, to just over 6% in 2018 and 6.5% in 2019. Gross financing needs increased substantially in 2020 and 2021, to around 15%, the threshold above which the IMF considers market-access countries to be at risk of unsustainable debt. These outcomes were in the context of MFA III and other assistance, and the counterfactual analysis will consider whether such outcomes might have been worse in the absence of such support.

Table 4.2 Evolution of key macroeconomic indicators, Georgia

Indicator	2017	2018	2019	2020	2021
GDP, current prices (USD billion)	16.2	17.6	17.5	15.8	18.6
Real GDP growth (%)	4.8	4.8	5.0	-6.8	10.5
Inflation, average consumer prices (%)	6.0	2.6	4.9	5.2	9.6
Inflation, end of period consumer prices (%)	6.7	1.5	7.0	2.4	13.9
Unemployment, % of labour force	21.6	19.2	17.6	18.5	20.6
General government balance (% of GDP)	-0.5	-0.8	-1.8	-9.3	-6.0
General government gross debt (% of GDP)	39.4	38.9	40.4	60.2	49.7
Gross external debt (USD billion)	17.3	17.9	18.9	20.9	n/a
Gross external debt (% of GDP)	119.3	100.3	106.6	129.5	n/a
FDI (inflows) (USD billion)	2.0	1.4	1.4	0.6	1.3
FDI (inflows) (% of GDP)	11.9	7.4	7.9	3.5	n/a
Gross international reserves (USD billion)	3.0	3.3	3.5	3.9	n/a
Gross international reserves, months of imports	3.4	3.6	3.8	5.2	n/a

Sources: IMF, WB, National Statistics Office of Georgia, NBG.

Assessing the role and contribution of MFA III to observed outcomes

We assess the role and contribution of MFA III by looking at three scenarios:

1. What would have happened without the first tranche of the MFA III, disbursed in 2018 (Alternative A: no MFA first tranche);
2. What would have happened without the second tranche of the MFA III, disbursed in 2020 (Alternative B: no MFA second tranche);
3. What would have happened in the absence of MFA III and without IMF assistance (Alternative D: no MFA and no IMF).

In developing these counterfactuals, experts were consulted on the most likely course of action in the absence of support and different plausible scenarios were defined. These are presented here, alongside our conclusion on the most likely scenario.

Alternative A: No disbursement of the first MFA III tranche in 2018

Without the first MFA III tranche, worth EUR 20 million and disbursed in December 2018, borrowing on domestic financial markets (as opposed to international markets) would have been feasible for Georgian authorities. It would have been relatively easy, given the high level of liquidity in the markets at the time. The high liquidity in domestic markets and the increasing issuance of treasury bills and bonds would have also made domestic financing a feasible option. However, resorting to domestic financing on its own would likely not have

sufficed, as open market operations, such as T-bill and bond auctions, were increasingly conducted on a smaller scale. It also has its downsides in terms of deepening the ties between the sovereign and banking sectors, with the risk that an increase in sovereign affects the banks' balance sheets and lending appetite.

The Georgian authorities would likely have had recourse to other or additional sources of financing to address the financing gap caused by the absence of MFA III. Georgia had received a substantial amount of external aid from bilateral and multilateral donors for many years. In the absence of the MFA III disbursement in 2018, the Georgian authorities could have sought additional financial support, which would have likely been easily and readily extended (facilitated by its good relationship with the donor community).

As Georgia was outperforming on the revenue collection side, the taxation revenue (in excess of the conservative projections) could also have been used to help to address the financing gap entailed by the absence of MFA III in 2018.

Alternative B: No disbursement of the second MFA III tranche in 2020

Amid the COVID-19 pandemic, Georgia's domestic financial market remained resilient, characterised by robust capital, liquidity, and credit growth. The government was able to step up its borrowing (mostly) to finance healthcare and stimulus spending. This suggests that raising financing on the domestic market would have been a plausible option for the Georgian government had the second MFA III tranche not been disbursed in 2020. Conversely, on the international front, financial conditions tightened considerably and accessing funds on the international financial markets could have proved a very costly alternative to MFA III and thus an unlikely alternative route for financing.

In the wake of the pandemic, international aid continued to pour into Georgia. Seeking additional multilateral and/or bilateral support would likely have constituted another feasible, potentially preferable, option for Georgian authorities.

Other forms of alternative financing would have been fiscal adjustments, probably in the form of cuts in capital spending rather than tax increases. This is because it would not have been possible to raise additional taxes owing to declining incomes and legal restrictions (i.e. 2011 Economic Liberty Act).

Alternative D: No MFA or IMF support

In the absence of both EU and IMF support, the Georgian government would likely have resorted to increased borrowing on the domestic market rather than international financial markets, since its access to international markets would have been greatly reduced. IMF support is instrumental in restoring investor confidence and lowering sovereign risk premia and in its absence, Georgia would not have enjoyed the same borrower status. Even though domestic markets provided high liquidity, under this extreme situation, restricted capacity would likely have emerged from the uncertainty and lack of confidence arising as a result of the withdrawal of EU and IMF support. Similarly, additional/increased support from the donor community would have been unlikely. EU and IMF support is generally accompanied by a set of corrective policy actions and signals that appropriate policies are being put in place. In their absence, donors and development partners could have been reluctant to offer financial support.

One plausible course of action would have been the privatisation of state-owned assets, the proceeds of which could have helped to address the shortfall, based on experience of successful past operations. In 2020 alone, the Georgian government privatised 100 state buildings, gaining over EUR 40 million in proceeds. Privatisation on its own would likely not

have sufficed and additional sources of financing would have had to be considered, such as fiscal adjustments. For instance, the Georgian government could have considered the reprioritisation of spending by reducing capital expenditures and the scope of COVID-19-related fiscal measures, while preserving social spending.

Choice of the most plausible counterfactual scenario(s)

Table 4.3 presents our conclusions on the most plausible counterfactual alternative(s), that feed into the rest of the analysis.

Table 4.3 Most plausible counterfactual scenario(s)

Georgia	
Alternative A: Absence of MFA first tranche : absence of EUR 20 million in December 2018.	
Alternative financing	Domestic financing and donor support.
Direct implications	No direct implications, as the extra revenue actually collected during the period could have covered the missing tranche.
Alternative B: Absence of MFA second tranche : absence of EUR 25 million in November 2020	
Alternative financing	Donor support.
Direct implications	Possibly postponement of capital expenditure.
Alternative D: No MFA or IMF support: absence of EUR 545 million over 2018-2020	
Alternative financing	Some scope for domestic market financing
Direct implications	More severe budget cuts.

Debt Sustainability Analysis (DSA)

The objective of the DSA was to evaluate the contribution of MFA III (2018-2020), and IMF support to Georgia's debt sustainability in terms of public debt and gross financing needs. DSA involves modelling the key debt burden indicators and macroeconomic variables that affect the path of a country's debt and its ability to manage its debt sustainability. To assess the contributions of the MFA support to Georgia's debt sustainability, the observed main debt sustainability indicators (baseline) are compared to hypothetical outcomes in three alternative scenarios (counterfactuals).

The scenarios presented in Table 4.3 were modelled in the IMF DSA tool for each counterfactual, including, where applicable, estimates and assumptions on how borrowing costs might have changed and how GDP would have been affected. The consequent evolution of the main DSA indicators was assessed to shed light on the macro-fiscal contribution of MFA III and IMF support.

Georgia: Alternative A – no MFA first tranche

Relying on alternative financing, such as domestic markets or multilateral and bilateral support, would have come at higher borrowing costs due to both direct and indirect effects. The direct effect would arise as a result of increases in interest payments on debt compared to those under MFA III. The indirect effect would be the increased cost of borrowing from private investors resulting from lower investor confidence in the absence of MFA support. Overall, covering the financing gap using alternative financing would have increased gross financing needs and gross public debt modestly, by 0.25 pp and 0.2 pp, respectively, in order to maintain the same levels of government operations as was observed.

Overall, Georgia would have seen small changes to its main debt sustainability indicators, but its overall outlook would have remained largely unchanged (with future stress still showing, as suggested in the baseline). In the absence of the support, a total cost of EUR 15 million would have been incurred as a result of higher borrowing costs (2018-2022).

Georgia: Alternative B – no MFA second tranche

As with Alternative A, relying mostly on alternative financing, such as multilateral/bilateral aid, would have come at higher borrowing costs due to direct and indirect effects. The direct effect would arise as a result of increases in interest payments on debt compared to those available under MFA. The indirect effect represents the increased cost of borrowing from private investors resulting from lower investor confidence in the absence of MFA support. Overall, covering the financing gap mostly using alternative financing would have increased gross financing needs and gross public debt slightly (as a ratio to GDP) by around 0.1 pp in both cases.

Overall, as in Alternative A, Georgia would have seen small changes to its main debt sustainability indicators, and the overall outlook would have remained largely unchanged. In the absence of support, a total cost of EUR 14 million would have been incurred as a result of higher borrowing costs (2018-2022).

Georgia: Alternative D – no MFA and no IMF

Covering the outstanding financing gap largely through lower government spending would have had a substantial negative effect on GDP, ranging from a 1.3% reduction in 2017 to a 9.8% reduction in 2020. This would likely have been exacerbated by any interaction with the COVID-19 crisis, resulting in further and even more severe GDP reductions.

Absent IMF and MFA support, there would likely have been considerable repercussions for Georgia. While the extent of these effects is hard to specify, given the uncertainties and extreme nature of the counterfactual, the results nevertheless suggest that, had Georgia opted for more drastic fiscal consolidation, financial sustainability ratios might have improved somewhat, but this would have taken place against a substantial challenging backdrop of lower economic growth. Had there been stronger exchange rate responses, debt sustainability would also have been even more problematic.

Part 2: Assessment of the effectiveness of MFA conditionality

The general view is that there was satisfactory progress on the various sectoral reforms during the MFA-III implementation period.

Significant changes were initiated under MFA III and followed up with the subsequent MFA COVID-19 package. This included setting up the Dispute Resolution Council, the Law on Entrepreneurs and the offering of employment services, where the MFA COVID-19 package requested the parliamentary passage of the corresponding laws. These are all examples of changes where reforms brought about meaningful changes, with the legal frameworks now closer to the EU *acquis*.

In other areas, progress constituted incremental improvements rather than step changes, e.g. in relation to PIM or to PPPs.

Despite steps to improve labour market policies, the problems of skills mismatch and high (youth) unemployment largely persisted but these were long-standing, largely systemic, issues (e.g. absence of unemployment benefits and minimum wage), which could not have reasonably been expected to be fully resolved within the MFA timeframe.

It is hard to disentangle the specific role of MFA III, given the government's strong ownership of the reforms and the large IFI/donor support provided in parallel. In general, in the many areas where this applied, the common ground between MFA and other EU support tools (notably budget support, but also technical assistance) gave the EU greater leverage in promoting reforms. Stalled reforms, or reforms that had been progressing slower than planned, began to move again or more quickly once introduced under MFA. This was the case for land registration, the VET Law and the Law on Entrepreneurs (whose technical complexity delayed the disbursement of the second tranche for several months). Overall, the EU had a clearer political and operational reinforcing effect in promoting reforms that were on the Association Agenda (e.g. Dispute Resolution Council, Law on Entrepreneurs, amendments to the Labour Code).

Not all MFA-promoted reforms were successful. The passing of the MPTL Law remains pending, confirming that a waiver may have been required even in the absence of the COVID-19 pandemic. The difficulties in passing this law were not anticipated from the beginning of the operation. They are linked to general political economy considerations and difficulties with implementing reforms that impose a cost burden on a large segment of the population.

In the judiciary, *stricto sensu*, the conditions were considered fulfilled. However, several substantial limitations persisted. For example, a change in the treatment of personal data meant that the publication of lower court case rulings was suspended following MFA III. The system of random allocation of cases to judges was heavily criticised for being exposed to undue influence. EU assessments are that the legal framework has improved following four consecutive waves of reform prior to 2022, but overall progress is assessed as limited¹⁰¹. EU stakeholders and CSOs from Georgia shared concerns about the independence and quality of the judicial system and flagged perceptions of backpedalling on areas of judicial reform following MFA III. The second instalment of MFA COVID was cancelled by the Commission not only following the decision of Georgia to refrain from requesting it, but also in view of the non-fulfilment of an important policy condition related to the judicial system¹⁰².

More generally – and increasingly since the 2020 parliamentary elections – calls are made to “refrain from actions that could further deepen the political tensions and hamper the country's

¹⁰¹ European Commission, *Georgia 2023 Report*, SWD(2023) 697 final.

¹⁰² https://economy-finance.ec.europa.eu/international-economic-relations/candidate-and-neighbouring-countries/neighbouring-countries-eu/neighbourhood-countries/georgia_en

reform agenda¹⁰³. CSOs report some signs of democratic backsliding¹⁰⁴ and persistently high political tensions. While Georgia was initially considered a leader in the EaP region in terms of implementing reforms, approximating EU standards, economic development, and democratisation efforts, concerns are increasingly raised about media freedom, NBS governance, and judicial reform. This translated into Georgia being granted EU candidate status later than Ukraine and Moldova, on the understanding that it will take the relevant steps set out in a Commission recommendation¹⁰⁵. The EU recently recalled “the importance to guarantee NBS’s independence and credibility”¹⁰⁶. The IMF also expressed concerns about the recent changes at the NBS (management structure; decision on amendments to the sanctions regulation), which delayed the second review of the ongoing SBA programme that authorities treat as precautionary¹⁰⁷. In parallel, the EU in its report on Georgia of November 2023 and many IFIs and donors¹⁰⁸ noted and welcomed the continuous (though somewhat slower) progress with various sectoral reforms.

Box 4.5 PFM

PFM has seen continuous progress during the MFA implementation period, building on past achievements. 2022 Public Expenditure and Financial Accountability (2022 PEFA) scores¹⁰⁹ improved on most of the dimensions linked to the MFA conditions, compared to the situation in 2018. The most significant changes related to public procurement, notably procurement complaints procedures.

- Indicator PI-11 (assesses the economic appraisal, selection, costing, and monitoring of **public investment** projects by the government) improved from C to A between 2018 and 2022;
- Indicator PI-10.3 (assesses fiscal risks, i.e. reporting of contingent liabilities and other fiscal risks, including from **PPPs**) improved from B to A;
- Indicator PI-24.4 (**procurement complaints management**) is now at A, while it was still highlighted as a weakness (D) in 2018;
- Indicator PI-24.2 (actual **use of open and competitive means**/methods) was the only indicator downgraded, from A to B. This may mask some objective reasons, such as the prevalence of non-competitive purchases linked to the COVID-19 pandemic and the level at which the threshold is set (very low compared to other countries, and now smaller in real terms than in 2010 when it was set).

Georgia’s PFM systems were assessed as resilient during the COVID-19 pandemic, despite the challenges and constraints of the time. Georgia is pursuing further progress in this area, together with the international partners and donors who are coordinated via the PFM Council, in the direction set in its new Public Finance Management Strategy 2023-2026¹¹⁰.

¹⁰³ Council of the EU, Georgia, <https://www.consilium.europa.eu/en/press/press-releases/2024/02/21/joint-press-statement-following-the-8th-association-council-meeting-between-the-eu-and-georgia/>

¹⁰⁴ For instance, while Georgia’s ‘democracy percentage’ at the beginning of the MFA III operation was 40%, it has now decreased to 34% (Freedom House, Georgia, <https://freedomhouse.org/country/georgia/nations-transit/2023>)

¹⁰⁵ Council of the EU, Georgia, <https://www.consilium.europa.eu/en/policies/enlargement/georgia/>

¹⁰⁶ Council of the EU, Georgia, <https://www.consilium.europa.eu/en/press/press-releases/2024/02/21/joint-press-statement-following-the-8th-association-council-meeting-between-the-eu-and-georgia/>

¹⁰⁷ IMF, ‘IMF concludes virtual visit to Georgia’, Press release No 23/271, 21 July 2023, <https://www.imf.org/en/News/Articles/2023/07/21/pr23271-georgia-imf-staff-concludes-virtual-visit>; Civil, ‘IMF stand-by arrangement delayed, not suspended’, News, 4 October 2023, <https://civil.ge/archives/562046>

¹⁰⁸ See, for example, EBRD, *Country strategy 2021-2026: Georgia*, <https://www.ebrd.com/georgia-strategy.pdf>

¹⁰⁹ <https://www.pefa.org/node/5197>

¹¹⁰ Georgian Ministry of Finance, Public Financial Management Reform Strategy 2023-2026, n.d., https://www.mof.ge/images/File/strategia/2023/30-06-2023/2023-2026%20PFM%20Reform%20Strategy%20_ENG.pdf

MFA conditions appeared to have most weight in relation to the setting up of the institutionally independent Dispute Resolution Council. The MFA COVID-19 followed the MFA III condition, asking for the parliamentary passage of the law, the Directorate-General for Growth (DG GROW) provided advice and guidance on the technical aspects, and, overall, the MFA conditions were seen as helpful in overcoming internal resistance to change.

Box 4.6 Financial sector

There were mixed results in the financial sector.

In relation to the MFA condition *stricto sensu*, the NBG continued to progress, incorporating the implementation of the new Code of Corporate Governance for Commercial Banks¹¹¹ into its supervision processes. It continued its efforts to reduce dollarisation, with some visible impacts in terms of reducing the share of loans and deposits denominated in foreign currency. The MFA role in promoting progress here was considered rather limited.

In relation to NBG governance, however, wider developments raised concerns among EU stakeholders, who feared that recent amendments to the Law on NBG undermined the institution's independence¹¹².

There was no substantial progress in the insurance sector. The MTPL Insurance Law, whose adoption was waived during the COVID-19 pandemic, has still not been adopted as of early 2024. The reform is still on the agenda and discussions are underway.

Box 4.7 Social and labour market policies

Progress on social and labour market policies was achieved through the reforms targeted. However, the extent to which these were sustained, or realised tangible benefits, varied.

All three conditions were satisfied with no delays. Selective contracting was expanded to several additional services (e.g. intensive care, emergency services, heart disease). Between 2019 and 2020, Georgia established and/or strengthened a National Strategy of Labour and Employment Policy 2019-2023 and associated action plan, as well as a new State Employment Support Agency, labour market information management system and Labour Inspection Service. It also adopted a new Law on Occupational Safety, and a new Labour Code and legislation. Finally, the VET Law was adopted, unlocking additional support from international donors and enabling the achievement of several initiatives (e.g. adoption of a National Qualifications Framework (NQF)).

Progress towards achieving selective contracting is still ongoing, after having been put temporarily on hold during the COVID- pandemic. It is one of priorities of the National Health Strategy for 2022-2030 endorsed by the government in May of 2022. National authorities confirmed that selective contracting has been extended to further service, new quality related criteria had been introduced for primary care providers across the country and international accreditation will be a requirement for participation in the State Funded health programs from 2025. Wider stakeholders however expressed concerns that selective contracting in healthcare was not being pursued by the government actively enough, due to the political risks of dissatisfaction among healthcare providers, which were generally resistant to reforms, given the high profitability of the sector. In fact, since MFA III, it was felt that the UHC service quality overall had worsened, despite ongoing reform efforts. Overall, there was a reduction in out-of-pocket payments, but these seem more closely related to the introduction of the UHC rather than MFA reforms.

Concerns were raised about the effectiveness and efficiency of the State Employment Support Agency and Labour Inspection Service. Further alignment with the EU *acquis* in labour law was called

¹¹¹ Code of Corporate Governance for Commercial Banks, https://www.nbg.gov.ge/uploads/legalacts/fts/eng/215_04_eng.pdf

¹¹² European Commission, *Georgia 2023 Report*, SWD(2023) 697 final.

for, notably for the directives applicable to specific sectors and gender-responsive family policies^{113,114}. Notwithstanding assessment difficulties given the effects of the COVID-19 pandemic, these reforms did not appear to translate into significant improvements in the labour market. The number of workplace-related accidents and deaths remained relatively high, albeit decreasing.

Finally, despite the adoption of the VET law, the lack of funding for VET colleges, poor wages for VET teachers and poor institutional management were cited as reasons for questioning the quality, capacity and capability of the current VET offer. In fact, until 2018 the number of VET students fell below government targets¹¹⁵, with the number of graduates and VET institutions falling over time.

Box 4.8 Business environment

Reforms targeting improvements in Georgia's business environment showed mixed results.

Reforms in land registration made good progress. By April 2020, the NAPR had exceeded its target for sporadic registration, having registered 780,000 plots of land according to the simplified registration rule. They are on track to complete this process by the end of 2024 (as set out in the Action Plan¹¹⁶). Currently, over 80%¹¹⁷ of land is registered (and checked for accuracy) in Georgia. Although it is too early to identify tangible benefits, stakeholders noted an increase in the number of transactions involving mortgages, i.e. increased the use of land as collateral.

The condition on the Law on Entrepreneurs was also met, with the draft law submitted to parliament in September 2020, promising several benefits to the business environment, including further alignment with EU acquis. However, it took longer than expected, due in part to the complexity of the process of developing the law, delaying the disbursement of the second tranche of MFA III. The European Commission's the 2023 Georgia report highlighted that it was only partially aligned with EU acquis on company law¹¹⁸, with authorities awaiting final confirmation of the law's full alignment with EU directives. Finally, whereas the law entered into force in 2022, companies have until 2025 to comply, thus expected benefits are yet to materialise.

Whereas condition #11, on judiciary reforms was considered met in MFA III, it was the most controversial reform area, due to perceptions of backpedalling by Georgian authorities since 2020. A dedicated website for the publication of court rulings was upgraded, a system of random allocation of cases was operationalised, and statistical data on disciplinary proceedings against judges were published. However, some stakeholders criticised the system of random allocation of cases for having numerous exceptions to the rule.

According to data provided by the High Council of Justice, in 2023, 68.4%¹¹⁹ of cases were allocated using the automated case management system, with the rest distributed manually. There are a number of reasons put forward to justify the manual distribution: when there is only one judge available (e.g., only one judge in the respective municipality/city, or with the relevant specialisation on duty); and when the case is an additional/related case to one previously assigned randomly to a judge, it would be reallocated to that same judge. The EU¹²⁰ and CSOs however considers that the exceptions expose allocations to undue influence.

¹¹³ European Commission, *Georgia 2023 Report*, SWD(2023) 697 final.

¹¹⁴ Ibid.

¹¹⁵ European Commission, *Evaluation of the EU's cooperation with Georgia*, 2022.

¹¹⁶ Agenda, 'Systemic land registration in Georgia to be completed in 2024, Justice Minister says', News, 16 December 2022, <https://agenda.ge/en/news/2022/4912>

¹¹⁷ Confirmed by the NAPR in interview. According to the NAPR statistics, 62.7% of land was registered in 2022, <https://slr.napr.gov.ge/statistics>

¹¹⁸ European Commission, *Georgia Report 2023*, DG NEAR, 2023.

¹¹⁹ Social Justice Centre, *Electronic System of Case Distribution in Courts 2020-2021 Assessment*, 2022, https://socialjustice.org.ge/uploads/products/pdf/Electronic_System_of_Case_Distribution_in_Courts_ENG_16571_14427.pdf

¹²⁰ European Commission, *Georgia Report 2023*, DG NEAR, 2023.

Considering the cases where there is an Independent Inspector's report on initiating disciplinary proceedings against the judge, the number of disciplinary proceedings resolved in line with the recommendations of the Independent Inspector remained relatively low¹²¹, at 30% in 2023¹²². Finally, a Constitutional Court decision in 2019 affected the treatment of personal data in court decisions, with the publication of lower court decisions suspended (expected to resume shortly)¹²³. Despite the strong legal framework in Georgia, stakeholders noted concerns about the extent to which the judiciary was subject to informal influences in practice. In fact, some believed that challenges around the fulfilment of reform conditions in this area affected Georgia's decision not to request the second disbursement of MFA IV (MFA COVID-19). The non-fulfilment of an important policy condition related to the judicial system clearly played a role in the EU's cancellation decision. More recently, in December 2023, Georgia was granted EU candidate status, on the understanding that the relevant steps set out in the Commission recommendation of 8 November 2023¹²⁴ are taken, including those related to judiciary reform.

Social Impact Analysis (SIA)

The overarching aim of the SIA was to use evidence from social indicators and primary data to assess the impacts of MFA III on the social situation in Georgia. The analysis considered direct impacts of policies specified in the MFA conditionalities and indirect impacts of wider macroeconomic stability across a range of social indicators. The full findings are presented in Annex 10.

Key findings of the SIA in Georgia include:

- **Enhanced coverage of universal healthcare.** Evidence indicates that healthcare reforms implemented in the last 10 years substantially reduced out-of-pocket expenditure for households. The share of private expenditure fell from 70% in 2013 to 47% in 2020. However, the specific contribution of MFA III is not easily discerned, given the timing of reforms (with the initial changes pre-dating the MFA). The outturn data for the MFA period suggest a continuation of reform efforts established prior to the implementation phase, with the range of healthcare services gradually expanded. Selective contracting implemented after 2018 seems to have somewhat expanded the variety of services offered, in line with the MFA conditionality;
- **Unclear impacts on labour market and education indicators.** As yet, existing data do not indicate clear impacts of reforms relating to employment and education. While various institutions and laws aimed to improve the registration of jobseekers and vacancies, as well as enhancing the quality of VET, their social effects may take longer to materialize. It is possible that these effects will only be visible in future data releases (and may even then be confounded by COVID-19 pandemic and conflict effects). In general, it seems that efforts to support employment creation through active labour market policies (ALMP) increased following MFA III, with a strong focus on employment in the public sector for the most vulnerable people (those receiving targeted social assistance);
- **Limited social impacts associated with no first tranche of MFA (Alternative A).** The likely social impacts of Alternative A were limited, as the assumed alternative sources of finance did not involve government spending cuts (Georgia would have been able to seek

¹²¹ Ibid.

¹²² The High Council of Justice of Georgia agreed with the conclusion of the Independent Inspector in 10 cases out of 31 cases where there was an Independent Inspector's report on initiating disciplinary proceedings against the judge. Source: Office of Independent Inspector, *Statistical Report of Activities*, 2023, p. 14, <https://dis.court.ge/wp-content/uploads/2023/05/First-Quarter-2023.pdf>

¹²³ Constitutional Court of Georgia, <https://constcourt.ge/en/judicial-acts?legal=1268>

¹²⁴ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Communication on EU Enlargement Policy, COM(2023) 690 final.

financing from alternative sources if needed). No social conditionalities were attached to the first MFA tranche and any impacts would therefore have been limited to potentially minor increases in inflation and slight impacts on real household incomes;

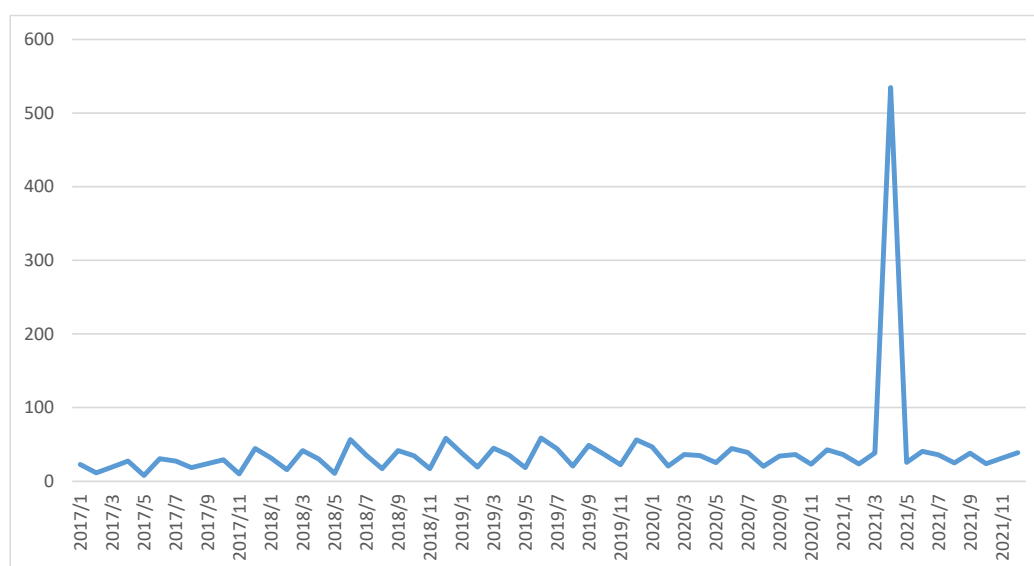
- **Limited social impacts associated with no second tranche of MFA (Alternative B).** Given that the scale of alternative financing needed and the ability to access these alternatives was similar to Alternative A, the impact on socioeconomic conditions was, again, likely limited. Social reforms conditional on the second tranche, such as those aimed at raising employment and improving skills matching, were assessed as not highly dependent on receiving MFA support, i.e. they might have taken place anyway. Broader effects might have been harder to discern over the period of interest, for similar reasons as above;
- **Deterioration of socioeconomic conditions in the absence of MFA and IMF support (Alternative D).** Outcomes stemming from the absence of any support from IMF and MFA operations would likely have been detrimental to the social situation in Georgia. Macroeconomic impacts of failing to fill the resulting finance gap would likely have exacerbated the already severe labour market situation.

Evaluation criterion: Efficiency

Question: Was the disbursement of the financial assistance appropriate in the context of the prevailing economic and financial conditions in Georgia?

By the time of the first disbursement at the end of 2018, the Georgian economy had begun to regain momentum, recovering from its weak growth rates and large current account deficits, and exceeding IMF expectations¹²⁵. Some key vulnerabilities and downside risks remained, however. IMF support was drawn upon to build up reserves, while MFA III was used to create fiscal buffers. In 2019, there was no MFA disbursement because of slow progress with several conditions, but this did not create any issue from an economic or financial point of view. No significant peaks in debt repayment obligations were observed in Georgia over the MFA implementation period (see Figure 4.2). The USD 500 million Eurobonds issued in 2011 were to be repaid in April 2021. These were successfully refinanced on the market at a low coupon rate (2.75% for five-year maturity).

Figure 4.2 Total external debt repayment obligations, by month, USD million



¹²⁵ IMF, *Country Report No. 18/373*, 2018.

Source: Georgian Ministry of Finance, Public Debt Management Department.

In 2020, the pandemic and strict anti-COVID-19 measures took a heavy toll on Georgia's tourism-reliant economy and led the government to adopt a comprehensive anti-crisis plan. Georgia recorded a fiscal deficit of almost 10% of GDP¹²⁶, thus the need for MFA support was greater at the time of the second disbursement in November 2020. Massive donor support was mobilised. As part of this wider package of assistance directed to the budget (including a specific EU COVID-19 resilience contract for Georgia), MFA III's second tranche (0.2% of 2020 GDP) made a small contribution to Georgia's overall fiscal response. The fiscal response represented approximately 3.8% and 2.9% of GDP in 2020 and 2021, respectively, of spending on measures to support the health sector, vulnerable households, and viable businesses. It allowed the government to:

- Support the health sector with an increase in the number of beds in intensive care units (to 1,400 beds);
- Provide social assistance to more than 78,000 vulnerable households and around 45,000 people with disabilities;
- Provide support to companies to preserve jobs (over 400,000 companies)¹²⁷.

Although it was not raised as a major limitation of MFA III support, it could have been helpful if the 2020 second tranche disbursement had been made earlier. The assistance reportedly reached vulnerable households and employees with some delays, although not all delays were attributed to a shortage of funds but rather to difficulties identifying recipients (COVID-19 support was not universal and required identification of employees and self-employed people who had lost their jobs/incomes). The submission of the Law on Entrepreneurs to the parliament held up the disbursement of the second tranche (until September 2020).

Question: To what extent did the MFA operation design enable the intervention to be carried out efficiently? In what way has the design of the MFA assistance conditioned the performance of the operation in respect to its cost and its objectives?

In addition to the disbursement schedule assessed above, a number of specific issues should be considered.

Issue 1: Ownership of the programme by the authorities

Georgia is consistently assessed as strongly committed to reform. This was reiterated recently in an evaluation of the EU's cooperation with Georgia¹²⁸ and is also evidenced by the wide use of the budget support modality in Georgia. The main factors promoting national ownership under MFA III included the conditions drawing on the national reform agenda and bringing Georgia closer to European standards, in line with its AA/DCFTA commitments.

According to EU stakeholders, a good sense of ownership was maintained throughout the implementation period. Changes on the political side of the government did not impede commitment to reforms. However, it gradually became clear that there were delays in fulfilling several conditions. The most substantial delays were in relation to the MPTL Law and the Law on Entrepreneurs, but, by mid-2019, five other conditions had some minor steps outstanding, according to a DG ECFIN mission report. This confirmed the absence of a sense of urgency on the macroeconomic front and illustrated that the main motivation behind fulfilling MFA III conditions was the government's willingness to demonstrate its ability to deliver EU-agreed reforms (rather than a pressing need for funds).

Issue 2: Capacity to effectively implement the programme

¹²⁶ IMF, World Economic Outlook data.

¹²⁷ European Commission, *Budget support: trends and results 2021*, September 2021.

¹²⁸ European Commission, *Evaluation of the EU's cooperation with Georgia*, 2022.

Georgia has two decades' experience implementing wide-ranging political and economic reforms, since the 2003 so-called 'Rose Revolution'. In some respect, Georgia is considered a leader and shares its experience of reforms with its neighbours/peers (e.g. e-procurement system, PIM).

The Ministry of Finance in Georgia was described as very competent to promote reforms and fulfil its coordination role under MFA III. No specific capacity issue was reported as impeding the fulfilment of the MFA conditions.

In general, Georgia actively seeks to engage with donors to support the implementation of its homegrown reform agenda. Capacity-building activities, twinning opportunities and advisory services seemed to be offered to Georgia where needed (see Section Evaluation criterion: Coherence¹³⁹1714960.653) and played a role in fulfilling the condition on public procurement, for example, in relation to the Dispute Resolution Council.

IFIs and donors noted that results can be achieved where there is strong political will. Existing forums, such as the Investors Council or PFM Council, were described as effective mechanisms to coordinate and mobilise line ministries where needed. The extent to which existing (donor) coordination mechanisms existed varied by sector. Inter-ministerial coordination could generally be improved, according to a 2018 OECD report¹²⁹.

The Investors Council¹³⁰ is 'an independent platform of public-private dialogue chaired by the Prime Minister of Georgia, with the objective of promoting dialogue between the business community, international financial institutions, donors and the Government of Georgia with the objective of promoting business and investment climate in Georgia'.

This donor-funded initiative was implemented through the EBRD with the support of the government of Georgia in 2015. It has been involved in discussions on the reforms promoted under MFA III, including the MPTL Law, the Law on Entrepreneurs, and financial sector and business environment reforms more generally.

The PFM Inter-Agency Council (PFM Council) was set up in 2010 to approve and monitor progress on PFM strategies and action plans. Chaired by the Minister of Finance, it includes representatives of line departments and relevant agencies (State Audit Office, State Procurement Agency) and parliament committee members (Budget and Finance Committee). It is open to CSOs and the international community, and thus also serves as a coordination platform. The PFM Council meets quarterly and its reports are publicly available online.

Issue 3: Liaison and monitoring processes

Meetings between the EU and the Georgian authorities were generally described as having a cooperative and constructive spirit. Good communication channels remained open throughout the operation. Beyond the MFA exchanges, EU-Georgia AA Subcommittee meetings were described as an additional forum to obtain information on MFA-relevant topics.

Given that the MFA conditions were very much aligned with the government's own priorities, there was a sense among EU stakeholders that implementation of the MFA conditions would be smooth and rapid. In that context, the delays in meeting the conditions arose somewhat unexpectedly. Authorities remained open to discuss relevant steps already taken, outstanding actions, and reasons for slow progress, and provided further information and data where needed.

¹²⁹ OECD, *Georgia Baseline Measurement report*, 2018, <https://www.sigmaweb.org/publications/Baseline-Measurement-Report-2018-Georgia.pdf>; more recent assessment is not yet available but CSOs report slow progress, https://idfi.ge/en/idfi_and_gyla_joint_statement_oecd-sigma

¹³⁰ Investors' Council, <https://investorscouncil.ge/>

To follow up specific sectoral issues, the DG ECFIN team drew on the expertise of the EU Delegation (in areas where projects/budget support programmes existed) and colleagues from other DGs (e.g. DG GROW, on public procurement, DG JUST, on justice conditions). This was deemed very useful in successfully concluding negotiations and carrying out independent assessments of needs/progress beyond national authorities' compliance reports. For Georgia, this internal expertise also came from the EC and EEAS headquarters, as there is no equivalent the Support Group for Ukraine (SGUA) or high-level advisor in the country, and thus less specialisation on sectoral issues.

Issue 4: Adjustments to implementation in light of unforeseen external events

Under MFA III, one waiver was granted to Georgia to allow for the disbursement of the second tranche despite the non-adoption of the MPTL Law. The waiver was granted in the context of the COVID-19 pandemic. The success of a reform is also a matter of timing and the pandemic was, rather unanimously, considered to be an unsuitable time to introduce legislation that would impose a new cost on motorists. There were doubts, however, as to whether the condition would have been met anyway. The reform lacked public acceptance even before the outbreak of COVID-19 and had been sitting at the parliament since its submission in December 2018. Despite Georgia's rather rapid COVID-19 recovery, the MPTL Law has yet to be adopted (as of early 2024).

At the time, the EU's flexible stance and its decision to disburse the second tranche under MFA III was consistent with its other efforts to maximise its support to Georgia. The fixed tranches of different budget support programmes were reportedly frontloaded, a new budget support operation was approved (EUR 75 million grant, 'COVID-19 Resilience Contract for Georgia'¹³¹, designed to support the Georgian government's anti-COVID-19 crisis efforts) and the MFA COVID-19 package was launched (with EUR 150 million earmarked for Georgia) in parallel to MFA III implementation.

The EU's flexibility was also consistent with the approach taken by other donors, with the IMF prolonging and augmenting its existing EFF programme, helping Georgia to secure more donor funding.

Issue 5: Visibility and public ownership

There was a consensus among focus group participants and civil society interviewees that general EU support to Georgia was visible and well known. In the 2018 Opinion Poll¹³², 67% of Georgian citizens (who have heard of the EU) declared that they knew the EU provides financial support to their country. The share had increased to 71% by 2020 (although Georgia still lagged behind Moldova on awareness of EU financial support)¹³³.

CSOs and the general public also know about the reform agenda promoted by the EU. CSOs published shadow association implementation reports and followed many of the reform areas promoted through MFA III (e.g. labour market, VET, justice). Many of Georgia's reform efforts were associated with its commitments under the AA and its obligation to transpose EU directives. In this context, public awareness of the reforms implemented through MFA III was estimated to be high, and the EU's role in supporting these changes was considered likely to be known.

¹³¹ EEAS, 'EU and Georgia sign financing agreements for COVID-19 recovery worth €129 million', Press release, 29 September 2020, https://www.eeas.europa.eu/delegations/georgia/eu-and-georgia-sign-financing-agreements-covid-19-recovery-worth-%E2%82%AC129-million_en

¹³² EU Neighbours East, *Opinion Survey 2018: Regional Overview*, 2018, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2018-regional-overview/>

¹³³ EU Neighbours East, *Opinion Survey 2020: Regional Overview*, 2020, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2020-regional-overview/>

Overall, there is strong support for reforms supporting Georgia on its EU path. In a recent poll, a majority of Georgians (56%) said that their government is either not doing enough or is doing nothing to ensure EU membership¹³⁴.

However, in normal circumstances, the visibility of the MFA was typically considered low, both among the public and among more specialised experts in Georgia. Those who knew about MFA support were unlikely to know the details of the MoU, e.g. which reforms were promoted via MFA. EU assistance is often promoted as a whole for the general public. Given the extensive use of budget support and the successive MFA operations, there were specific efforts from the EU Delegation to raise awareness and understanding of this type of assistance.

The visibility of the MFA instrument increased in 2021-2022 when the second tranche of the MFA COVID-19 package was not disbursed. The media investigated the case¹³⁵, reviewing conditions that were not satisfied from the EU perspective, despite official government communication that there was no economic need for the second disbursement. The non-disbursement became associated with the lack of progress with judiciary reform and created political embarrassment.

Evaluation criterion: Coherence

Question: *To what extent was the MFA II operation in line with key principles, objectives and measures taken in other EU external action towards Georgia in the context of the European Neighbourhood Policy?*

Policy Framework and Principles

A PCA between the EU and Georgia was formally signed in April 1996, following a period of intensive cooperation after the EU's recognition of Georgia's independence in 1992¹³⁶.

Since 2008, an EU Monitoring Mission has operated in the vicinity of the administrative boundary lines with Georgia's breakaway regions of Abkhazia and South Ossetia. The EU remains committed to supporting Georgia's territorial integrity¹³⁷.

In 2009, Georgia joined the EaP, the Eastern regional dimension of the ENP, launched in 2004 to deepen strategic partnership with the EU. It aimed to strengthen the political and economic relations between the EU and partner countries¹³⁸, and was based on a shared

¹³⁴ National Democratic Institute (NDI), Taking Georgians' pulse: Findings from December 2022 face to face survey, 2023,

https://www.ndi.org/sites/default/files/NDI%20Georgia_December%202022%20poll_public%20version_ENG_vf.pdf

¹³⁵ See, for example, Mandaria, T., 'Georgia turns down 75 million euros from the EU', Eurasianet, 1 September 2021, <https://eurasianet.org/georgia-turns-down-75-million-euros-from-the-eu>; Georgia Today, 'Georgian Dream refuses EU financial aid, EU Reps: Georgia didn't deserve it anyway', 2 September 2021,

<https://georgiatoday.ge/georgian-dream-refuses-eu-financial-aid-eu-reps-georgia-didnt-deserve-it-anyway/>

¹³⁶ Government of Georgia, Partnership and Cooperation Agreement, https://smr.gov.ge/uploads/prev/2_Partner_cce01fcf.pdf

¹³⁷ Delegation of the European Union to Georgia, *The European Union and Georgia*, 2023, https://www.eas.europa.eu/georgia/european-union-and-georgia_en?s=221

¹³⁸ European Commission, European Neighbourhood Policy and Enlargement Negotiations, n.d., [https://neighbourhood-enlargement.ec.europa.eu/european-neighbourhood-policy/eastern-partnership_en#:~:text=The%20European%20Neighbourhood%20Policy%20\(ENP,closeset%20Eastern%20and%20Southern%20neighbours.](https://neighbourhood-enlargement.ec.europa.eu/european-neighbourhood-policy/eastern-partnership_en#:~:text=The%20European%20Neighbourhood%20Policy%20(ENP,closeset%20Eastern%20and%20Southern%20neighbours.)

commitment to international law, fundamental values, the market economy, sustainable development, and good governance¹³⁹.

In June 2014, Georgia signed an AA with the EU and its Member States, which entered into force in July 2016. This was an outcome of the ENP and, together with the DCFTA, built a foundation for far-reaching Georgian political and economic integration with the EU¹⁴⁰. This enabled Georgian citizens to access visa-free travel to the Schengen area from March 2017. Key ambitions for Georgia included ever-increasing democracy and rule of law, human rights, good governance, and economic development¹⁴¹.

Georgia applied for EU membership in March 2022. The EU, however, advised that Georgia defer its candidacy as significant reforms to the judiciary, electoral system and press still needed to be carried out. In September 2022, the EU reiterated its support for Georgia and encouraged advancements towards EU integration. In light of its achievements since June 2022, in November 2023, the European Commission recommended that the Council grant Georgia the status of candidate country, on the understanding that it complete the nine steps set out in the Commission's Report on Georgia¹⁴².

Georgia

22 April 1996 – EU-GE PCA Agreement signed in Luxembourg

29 September 2004 – ENP instrument launched by Commission

7 May 2009 – Joint Declaration of the Prague Eastern Partnership Summit

1 July 2016 – Entry into force of the AA, including creation of bilateral DCFTA

28 March 2017 – Visa-free access to Schengen-area for Georgians

3 March 2022 – Georgia applies for membership of the EU

23 June 2023 – European Council recognises the European perspective for Georgia and sets out 12 priorities to address before granting candidate status

8 November 2023 – European Commission recommends that the Council grants Georgia candidate country status

14-15 December 2023 – the Council grants Georgia candidate status, on the understanding that it takes the relevant steps as set out in the Commission recommendation

¹³⁹ Joint Declaration of the Prague Eastern Partnership Summit, 8435/09 (Presse 78), Paragraph 1.

¹⁴⁰ Delegation of the European Union to Georgia, *The European Union and Georgia*, 2023, https://www.eeas.europa.eu/georgia/european-union-and-georgia_en?s=221

¹⁴¹ Delegation of the European Union to Georgia, *The European Union and Georgia*, 2023, https://www.eeas.europa.eu/georgia/european-union-and-georgia_en?s=221

¹⁴² Delegation of the European Union to Georgia, Communication on EU Enlargement Policy, 2023, https://www.eeas.europa.eu/delegations/georgia/2023-communication-eu-enlargement-policy-extract-about-georgia_en

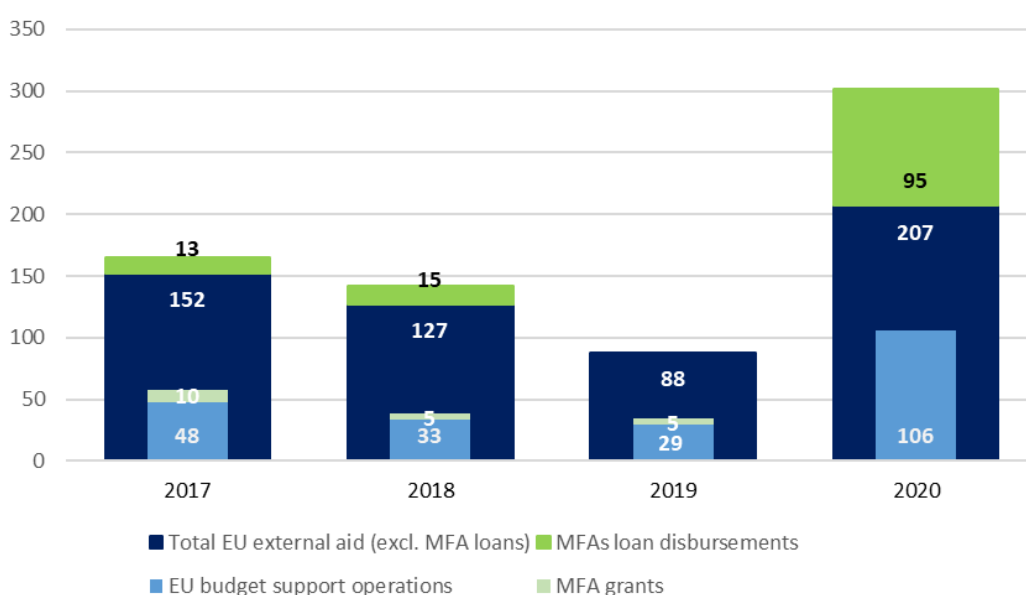
EU assistance to Georgia

Overview of assistance provided via budget support programmes (grants) and MFA assistance (grants/loans)

Figure 4.3 presents MFA loan and grant disbursements compared to total EU external aid and EU budget support assistance exclusively received by Georgia over the 2017-2020 period.

MFA disbursements in Georgia were relatively modest, compared to the EU support package and provision of budget support programmes. The amounts disbursed and relative importance of MFA was higher in 2020, when MFA loan disbursements (EUR 96 million under both MFA III and MFA COVID-19) were almost on par with disbursements under budget support programmes (EUR 106 million), themselves at a record high that year.

Figure 4.3 EU external aid to Georgia, by type, and MFA, 2017-2020, EUR million (disbursement data)



Source: Annual reports on the implementation of the EU's instruments for financing external actions; Annual reports on the implementation of macro-financial assistance to third countries (2017-2020); Budget support: Trends and results reports;

Note: Data refer only to external aid financed through the EU budget and do not include bilateral aid from Member States or financing from the EIB.

Coherence with other EU programmes and initiatives

MFA III versus previous MFA operation

Table 4.4 shows that MFA III focused on the same reform area as MFA II in three instances (risk management at the NBG, health sector, public procurement). There was no evidence of direct continuation in the pursuit of the same reform efforts, but MFA III focused on complementary aspects.

Some reform areas were no longer addressed as part of MFA III (external audit, trade conditions in the implementation of DCFTA, financial sector legal reforms, regulation, and

supervision), while some new areas were introduced (labour market, business environment including judiciary reform, assessment of fiscal risk public investment projects and PPPs).

The main reason behind this progressive change in reform focus was that MFA III conditions, negotiated in 2018, were developed quite some time after the MFA II conditions, which were negotiated in 2014. MFA III conditions were logically designed to reflect the priorities of the time and those of ongoing/upcoming parallel budget support programmes. In addition, while there was an intention to opt for conditions permitting rapid disbursement under MFA II (after the MFA Decision had been blocked for more than two years between 2011 and 2013), there was no reason for such a strong focus on rapid disbursement under MFA III.

Comparatively, there was more continuation with the MFA COVID-19 package, which followed up a number of MFA III conditions, on public procurement, PES, company law, justice sector (e.g. requiring that laws that had been submitted to the parliament under MFA III be adopted under the MFA COVID-19 package).

Table 4.4 Mapping of conditions: MFA II vs MFA III

	MFA II	MFA III
Areas with complementarities		
Public procurement	Training on public procurement legislation and procedures	Reduction of the proportion of direct procurement - Dispute Resolution Council
Risk management at the NBG	Establishment of Centralised Risk Management Department	Regulation on sound risk management, including management of dollarisation-related risks
Health sector	Health Utilisation and Expenditure Survey	Selective contracting
Areas with no complementarities		
External audit	x	
Implementation of DCFTA	x	
Financial sector legal reforms, regulation, and supervision	x	
Business environment, including judicial system		x
Labour market		x

MFA III operations in the context of the overall EU budget support package

All reforms areas promoted through MFA III had links to past/ongoing sectoral EU budget support programmes or programmes being negotiated at the time. The aim was to use the MFA leverage to incentivise the Georgian authorities to pursue their efforts in areas where there had been delays, and to ensure reform progress on commitments made through other budget support programmes and more generally as per AA/DCFTA obligations.

The most relevant budget programmes with synergies with MFA III were:

- EU 4 Economic Governance and Fiscal Accountability, 2019-2021;
- Skills Development and Matching for Labour Market Needs, 2018-2023;
- Economic and Business Development in Georgia, 2019-2022, which also covers the justice sector.

These programmes were in the pipeline at the same time as the MFA III operations (they were presented in the 2017¹⁴³ or 2018¹⁴⁴ annual work programmes). Most built on earlier work in this domain (Skills4jobs phase 1, PFM 2014-2017, justice sectoral budget support programme 2015-2017).

Examining the cross-conditions and complementarities using the budget support programmes' results' matrices reveals that MFA conditions on the adoption of the VET Law¹⁴⁵ and land registration¹⁴⁶ were specifically designed to address aspects that had posed challenges under past budget programmes. Some MFA conditions (PIM, MPTL Law) corresponded to the exact same performance indicators under parallel budget support programmes (cross-conditions). Other MFA conditions (company law, justice) targeted complementary aspects addressed through technical assistance projects.

Table 4.5 Detailed cross-conditionality and complementarity with EU budget support programmes

Area	Condition	EU budget support programme
PFM	#1 Public investment	Improved governance and accountability in PIM was one focus of the 2019-2021 PFM budget support programme. Same indicators on need to conduct economic analysis of investment projects (target date: end 2020) NB: predecessor PFM programme (2014-2017) not focused on PIM
	#2 PPP	Related indicators on the need to report PPP-related fiscal risks in the 2019-2021 PFM budget support programme (target date: end-2020).
Financial sector	#3 Public procurement	-
	#4 Insurance sector	Same indicator on adoption of the legal framework (MPTL Law) as part of the Economic and Business Development in Georgia programme (target date: end-2019)
	#5 NBG	-
Social sector	#6 Healthcare	-
Labour market	#7 Labour market	Indicators on availability of labour market analysis and forecasting, functioning of the PES and participation in VET/VET qualification (i.e. elements to be covered by the new labour market strategy) were included among performance indicators for the disbursement of variable tranches under the 2018-2023 Skills4jobs programmes
	#8 Vocational training	In 2017, the review of the Skills4jobs (phase 1) had showed that one performance indicator (revision of NQF) was not fulfilled, as the new NQF remained in draft, pending adoption of the new VET Law

¹⁴³ European Commission, Commission Implementing Decision of 11.12.2017 on the Annual Action Programme 2017 in favour of Georgia to be financed from the general budget of the Union, C(2017) 8575 final

¹⁴⁴ European Commission, Commission Implementing Decision of 28.11.2018 on the Annual Action Programme in favour of Georgia for 2018 C(2018) 8064 final

¹⁴⁵ European Commission, *Review of Sector Reform Contract on Employment and Vocational Education and Training (EVET)*, 2017.

¹⁴⁶ European Commission, *Evaluation of the EU's cooperation with Georgia*, 2022.

Area	Condition	EU budget support programme
		MFA III pushed for the adoption of the law and the subsequent Skills4jobs (phase 2) programme included a range of indicators on quality of VET system, transition from VET to employment, social partnership, awareness of VET
Business environment	#9 Land market	Following the Justice Budget Support Programme 2015-2017, which contained one set of indicators on introducing systemic land registration in the country In its 2017 Compliance Assessment of General and Specific Conditions, the EU Delegation found the government non-compliant with specific indicators on land registration EU + GIZ project on private and administrative law reform, touching on land registration
	#10 Governance of companies	Economic and Business Development in Georgia 2018-2021 focused on the adoption of the complementary Insolvency Law Complementary/other support was provided in relation to the company law (e.g. expert advice for the finalisation (approximation), in partnership with GIZ)
	#11 Judicial system	Focus in the Economic and Business Development in Georgia 2019-2021 was on enforcement of judicial proceedings Technical assistance provided under the EU4 Justice programme

Source: ICF review of documentation.

EU technical assistance

The strong alignment of MFA conditions with ongoing budget support programmes meant that technical assistance was available to Georgian authorities in the targeted reform fields. For all MFA-related budget support programmes reviewed, a substantial share of the EU budget contribution was directed to complementary support in the form of technical assistance, especially in areas where Georgia was less advanced (e.g. lower budget in the PFM field). The EU-funded technical assistance, touching on the same MFA conditions in some cases (MPTL Law, company law, justice sector), was implemented by relevant partners with the technical expertise, including the WB and GIZ.

Technical assistance was also provided outside the framework of budget support programmes, e.g. in the field of public procurement via the EU Twinning Project for Strengthening Public Procurement Practices in Georgia and policy advice by DG GROW¹⁴⁷.

Technical assistance linked to budget support programmes

Programme	Amounts	Focus of EU-funded technical assistance and implementing partners
EU 4 Economic Governance and Fiscal Accountability, 2019-2021	- EUR 15 million for budget support	<i>Donors involved in MFA-related areas:</i> WB through the Europe 2020 Programmatic Trust Fund, focusing on improving fiscal

¹⁴⁷ European Union for Georgia, *Strengthening public procurement practices in Georgia*, n.d., <https://eu4georgia.eu/projects/eu-project-page/?id=320>

Programme	Amounts	Focus of EU-funded technical assistance and implementing partners
	- EUR 3.64 million for complementary support	governance and strengthening the independence and capacity of external audit
Skills Development and Matching for Labour Market Needs, 2018-2023	- EUR 30 million for budget support - EUR 15.1 million for complementary support - EUR 3.75 million for specific actions in Abkhazia	<p><i>Types of technical assistance to follow implementation of MFA conditions</i></p> <ul style="list-style-type: none"> - Technical assistance and twinning projects targeting beneficiary line ministries and relevant agencies - Grant scheme open for the private sector, non-governmental actors and various service providers in education and training, employment and youth; aimed at enhancing the employability of target groups <p><i>Other technical assistance</i> Specific support to Abkhazia implemented through the UNDP</p>
Economic and Business Development in Georgia, 2019-2022, which also covers the justice sector	- EUR 21.25 million for budget support - EUR 26.4 million for complementary and other support	<p><i>Donors involved in MFA-related areas:</i></p> <ul style="list-style-type: none"> - WB is supporting reforms aimed at introducing a mandatory MTPL Insurance Law and strengthening the legal and supervision capacities of Georgia's State Insurance Supervision Service. - GIZ supports achievement of major objectives, including ensuring fairer and faster litigation for businesses through streamlining judicial proceedings, implementation of the new company law, strengthening rehabilitation-oriented insolvency proceedings, and enhancing enforcement of judicial decisions <p><i>Other donors involved in other areas:</i> UNDP, ADA, EBRD</p>
EU4Justice programme 2015-2018	- EUR 30 million for budget support - EUR 20 million for complementary support	<p><i>MFA-related:</i> Technical assistance consisted of the delivery of capacity-building activities to ensure fair and prompt judicial trials for all people (continued under Economic and Business Development in Georgia 2019-2022, under EU4Justice Judiciary Support Project)</p> <p>Focused on designing modern electronic tools of management and case allocations, reasoning and accessibility of decisions, issues of judicial discipline</p> <p><i>Other:</i> Focus on criminal justice</p>

Source: ICF review of annual work programmes for 2017¹⁴⁸ and 2018¹⁴⁹.

IMF and WB programmes

MFA III to Georgia was conditional on the approval of IMF three-year EFF (2017-2020), initially agreed in April 2017, two months before Georgia requested MFA support, and augmented in light of the COVID-19 pandemic. The aim of the EFF programme was to support Georgia's efforts to implement an economic reform programme, reduce its economic vulnerabilities, and promote higher and more inclusive economic growth. The IMF EFF programme was fully disbursed (with eight reviews completed and programme objectives largely achieved)¹⁵⁰.

There were two cross-conditions between MFA III and the IMF EFF programme, related to PFM and fiscal transparency. More specifically, these required Georgia to secure resources and adopt an internationally recognised methodology for assessing PPP projects and public investment projects. In other PFM areas there were examples of conditions building on each other's achievements, such as the PPP Law, where the EFF first required submission of the law to the parliament and then the adoption of the implementing decrees, while the MFA pushed for parliamentary adoption of the law. Other PFM sub-themes were divided between MFA (public procurement) and EFF (further fiscal transparency, budgetary processes, value-added tax (VAT) refunds). In the financial sector domain, both the MFA and EFF had complementary conditions on the framework for central bank operations (with the MFA more focused on the risk framework) but the IMF was generally more involved here. In other areas, there was more of a division of labour, with one or other institution involved (e.g. social and labour market conditions for MFA; pension reforms, civil service reform and reforms of SOEs for the IMF).

The WB is another IFI heavily involved in the development, growth, and modernisation of Georgia's economy. Over the MFA implementation period, the WB strategy in Georgia shifted in focus from an infrastructure-heavy programme under the Y14–FY17 Country Partnership Strategy (CPS) to one that emphasises human capital under the Country Partnership Framework (CPF) for FY19–FY22¹⁵¹.

The two main DPOs during the MFA implementation period were:

- Second Programmatic Inclusive Growth DPO – EUR 47.2 million approved in April 2017: targeting improvements in the public sector (increased fiscal oversight of public investments and SOEs, improved coverage and quality of social services, strengthened monitoring of outcomes);
- Second Private Sector Competitiveness DPO – EUR 44.6 million approved in July 2017: aimed to increase private sector competitiveness (through business environment reforms, financial sector deepening, developing insurance markets, increasing firms' capacity to innovate and export).

Both DPOs had links with MFA conditions, especially with the first reform areas, PFM and the financial sector. Other specific reforms promoted via MFA in the other areas (social and

¹⁴⁸ European Commission, Commission Implementing Decision of 11.12.2017 on the Annual Action Programme 2017 in favour of Georgia to be financed from the general budget of the Union, C(2017) 8575 final

¹⁴⁹ European Commission, Commission Implementing Decision of 28.11.2018 on the Annual Action Programme in favour of Georgia for 2018 C(2018) 8064 final

¹⁵⁰ IMF, Country Report No. 21/79, 2021.

¹⁵¹ WB, *Country Partnership Framework for Georgia*, Report No. 121853-GE, 2018, <https://documents1.worldbank.org/curated/en/588751525364587100/pdf/WBG-Georgia-CPF-FINAL-4-25-04302018.pdf>

labour market reform area, business environment) were more EU-only reforms, as other IFIs, when involved, focused on different sub-themes.

The WB was also involved in MFA-relevant fields, as an implementer of EU-funded technical assistance (see Table 4.7).

Table 4.7 Detailed cross-conditionality with the IMF/WB

Area	Condition	Donors involved
PFM	#1 Public investment	Cross-condition with IMF and WB Follow up WB PIM technical assistance project (2016-2017; EUR 0.83 million)
	#2 PPP	Cross-condition/complementary with IMF (IMF asked for submission of the law to parliament)
	#3 Public procurement	WB also involved in this area (legal framework)
Financial sector	#4 Insurance sector	IMF and WB also pursuing financial sector deepening/development of insurance markets, focusing on other aspects, e.g. deposit insurance vs MTPL Insurance Law for MFA III WB involved in MTPL Law through EU-funded technical assistance
	#5 NBG	Complementary conditions from IMF on framework on central bank operations; shared objective to support de-dollarisation
Social sector	#6 Healthcare	WB active on enhanced obstetric and neonatal care
Labour market	#7 Labour market	EU only
	#8 Vocational Training	EU only (no other conditionality or structural benchmark in this field)
Business environment	#9 Land market	EU (with WB IDA financing pilot land registration project)
	#10 Governance of companies	EU only (IMF and WB active in relation to SOEs)
	#11 Judicial system	EU only

Source: ICF review of documentation.

Other IFI assistance

Several multilateral and bilateral development agencies have delivered operations and budgetary support programmes to Georgia since 2017. In the period between 2017 and 2020, EU support represented 17% of total assistance received in the form of budget support or directed to reserves (see Figure 4.1). In addition to the IMF and WB, budget support was provided by other institutions, including the ADB, AfD and KfW. The focus of their support can be summarised as follows:

- The ADB has supported Georgia’s development since 2007, mainly in the form of sovereign loans and direct non-sovereign loans¹⁵². It prioritises support to sectors such as transport, water supply and sanitation, energy, public sector management and finance;
- The AfD has supported Georgia’s commitment to climate change, fair and inclusive transition, and convergence with the EU since 2012, focusing on sectors such as regional connectivity, energy, agriculture, water resource management and human development¹⁵³;
- KfW has been active in Georgia since 1993 on behalf of the German federal government, supporting areas such as sustainable economic development, training and employment, with a particular focus on modernising the VET system, climate and energy, sustainable urban development, and the protection of natural resources¹⁵⁴.

Other donors from the EU are also involved in Georgia. The EIB has been active in providing loans to Georgia since 2010, mainly funding infrastructure projects and the development of local private sector and climate action investments¹⁵⁵. Similarly, the EBRD has provided investments in projects in Georgia, with a focus on those supporting private and financial sector development and inter-regional connectivity through investments under PPPs¹⁵⁶. The EBRD is also involved in policy dialogue. GIZ was a main implementing partner for EU-funded technical assistance in areas related to MFA III.

In 2020, several donors, such as the Asian Infrastructure Investment Bank (AIIB), provided additional emergency budgetary support to the government of Georgia’s response to the COVID-19 pandemic. The AIIB provided two loans to Georgia under its COVID-19 Crisis Recovery Facility (CRF), co-financed by the WB and aiming to enhance inclusive growth and competitiveness, build resilience, diversify sources of financing, and improve the education system¹⁵⁷.

4.3 How did the EU intervention make a difference and to whom? [Related criterion to assess: EU added value]

4.3.1.1 Financial added value

Financial added value from MFA III to Georgia did not primarily come from the size of the operation. Rather, it came from the terms and conditions of the MFA assistance.

In the case of MFA III, the operation was a ‘blended’ operation, including a grant component, unlike the other assistance (budget support). While the actual MFA loan / grant split was EUR 35 million / EUR 10 million, the concessionality of the different MFA disbursements can be estimated to be higher, worth about EUR 25 million, using the IMF calculation of grant element tool¹⁵⁸.

Table 4.8 MFA Concessionality results

Disbursement	Concessionality
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¹⁵² Asian Development Bank, *Georgia and ADB*, n.d., <https://www.adb.org/where-we-work/georgia>

¹⁵³ AfD, *AfD and Georgia*, n.d., <https://www.afd.fr/en/ressources/afd-group-and-georgia>

¹⁵⁴ KfW, *Georgia*, n.d., <https://www.kfw-entwicklungsbank.de/International-financing/KfW-Development-Bank/Local-presence/Europe/Georgia/>

¹⁵⁵ EIB, *The EIB in Georgia*, 2019, <https://www.eib.org/en/publications/the-european-investment-bank-in-georgia>

¹⁵⁶ EBRD, *The EBRD in Georgia*, n.d., <https://www.ebrd.com/georgia.html>

¹⁵⁷ AIIB, ‘AIIB approves EUR 45 million loan to Georgia for COVID-19 crisis mitigation’, Press release, 21 July 2020, <https://www.aiib.org/en/news-events/news/2020/AIIB-Approves-EUR45-Million-Loan-to-Georgia-for-COVID-19-Crisis-Mitigation.html>

¹⁵⁸ *Calculation of grant element*. (2022, February 10). IMF. <https://www.imf.org/en/GECalculator>

	MFA loan/grant split (in EUR million)	Grant element (%)	Grant equivalent (in EUR million explicit grant)
MFA III – first tranche	15/5	52.84%	10.57
MFA III – second tranche	20/5	58.60%	14.65
MFA III - total	35/10	56.04%	25.22

Source: authors' calculations

Terms and conditions of the loan component (interest rate, maturity) generally matched those of the other supports provided (the larger IMF support was however estimated to be more expensive). The grace period applicable in the case of MFA is longer (bullet repayment at maturity), while the others (except the International Bank for Reconstruction and Development (IBRD)) had grace periods typically ranging between three and six years (repayments starting once about one-third of loan duration elapsed).

Table 4.9 Average terms and conditions of budgetary support assistance to Georgia, 2018-2020

	Amount disbursed 2017-2020 (EUR million)	Average terms and conditions of assistance, 2018-2020		
		Interest rate	Maturity (year)	Grace period (year)
MFA III (loan component)	35	0.61%	14	14
MFA III (grants)	10	Not applicable		
Other MFA loans (MFA II, MFA Covid first tranche)	88	Not available		
Other MFA grants	10	Not applicable		
EU budget support grants	216	Not applicable		
IMF EFF	618	2.3%	10	5
ADB	90	0.32%	14	4
AfD	401	0.44%	20	6
AIIB	75	0.25%	12	3
WB	197	1.39%	25	14
KfW	389	0.61%	14	4

Source: ICF, based on Georgian Ministry of Finance data; EU-related support uses European Commission data (to avoid discrepancies in relation to exchange rate conversion and include budget support provided in the form of grants).

Notes: Except for MFA and IMF, terms and conditions applied to committed amounts. Average interest rates estimated based on historic Euribor-12 month rate (where applicable) and based on weighted averages; IMF interest rate based on historic SDR interest rate, a margin (currently 100 basis points), surcharges, which depend on the amount and time that credit is outstanding and service charge of 50 basis points is applied on each amount drawn; MFA III rate is the actual rate (weighted average of the interest rate of the two tranches).

4.3.1.2 Non-financial added value

Signalling effect to civil society and the general population

Georgian citizens share strong European aspirations. They tend to have positive (or neutral) perceptions of the EU, with only 5% expressing a negative attitude towards the EU¹⁵⁹. Recurring polls show unwavering support for EU membership, with 75-83% supporting the government's stated goal of joining the EU since 2018, across the political spectrum¹⁶⁰. In this context, there is a high expectation that the EU will step in at times of crisis, especially in unprecedented crises, such as the COVID-19 pandemic.

The study consultations suggested that the visibility of the MFA itself remained low and there was little evidence that MFA conditions were used as leverage externally to advance specific reform agendas. Instead, CSOs publicly referred to European values and standards in general and Georgia's commitments under the AA/ DCFTA as a driver for reforms (rather than MFA III, but MFA conditions are aligned with the Association Agenda).

Greater visibility of MFA support and the specific reform conditions could be helpful for advocacy purposes, while greater visibility of the achievements could contribute to strengthening relationships with the EU.

Confidence-boosting effects

MFA III came at a time when Georgia was starting to regain investor confidence. Since 2016, with its de-dollarisation programme, the NBG had taken steps to limit Georgia's heavy reliance on debt creating external financing. Georgia's issuer ratings at leading international credit rating agencies were being upgraded (e.g. to Ba2 by Moody's in September 2017). Closer ties with the EU and ongoing alignment with EU norms through the AA/DCFTA were one of the factors expected to further strengthen Georgia's economy and increase its resilience to shocks. There was an explicit understanding that these agreements would mean that Georgia would be provided with EU technical and financial support¹⁶¹.

MFA III was provided in this context. Many other donors were active in Georgia over the 2017-2020 period and provided assistance in the form of budget support. Together with the rest of the assistance package, MFA III signalled that Georgia continued to be on the right track and helped to sustain market confidence. The 'EU stamp', together with the extension of the IMF programme, helped in the context of COVID-19 in 2020 to secure more support. The increased confidence ultimately translated into the decrease of a risk premium and lower borrowing costs, as illustrated by the conditions obtained by Georgia when refinancing its Eurobonds in April 2021.

Approximation with the EU laws and standards in general and some individual MFA conditions were also expected to boost competitiveness, notably the Law on Entrepreneurs, adopted in 2021, which approximated the EU standards and modernised the regulations on the legal forms of companies, the procedures for their establishment and functioning, as well as the 2020 law setting up the Dispute Resolution Council.

4.3.1.3 Reinforcing Georgia's call for reform and conditionality design

¹⁵⁹ EU Neighbours East, *Opinion Survey 2018: Regional Overview*, 2018, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2018-regional-overview/>

¹⁶⁰ NDI, Taking Georgians' pulse: Findings from December 2022 face to face survey, 2023, https://www.ndi.org/sites/default/files/NDI%20Georgia_December%202022%20poll_public%20version_ENG_vf.pdf

¹⁶¹ Agenda, 'Global ratings agency Moodys upgrades Georgia's credit rating', News, 12 September 2017, <https://agenda.ge/en/news/2017/1954>

The main added value from the MFA programme was to provide the 'EU stamp' on the authorities' reform programme and signal that Georgia was advancing towards convergence with the EU.

The MFA conditions were also helpful to overcome internal resistance or inertia in areas where ownership was not necessarily lacking, but progress was slow (e.g. land registration, VET, company law). The MFA instrument was seen as a powerful tool, able to 'unblock' some files where other instruments (bilateral meetings, statements, budget support programmes) might have shown less progress. Under MFA operations, conditions can be formulated as higher-level goals and the fact that all conditions need to be met for the disbursement to take place (no possibility of partial disbursement) gives the instrument more weight compared to budget support programmes.

For the reforms to be successful, ownership is key and is typically a prerequisite. There are limits to the MFA leverage and extent to which reforms can be imposed from the outside. The success factor of this MFA operation from Georgia's point of view was that it promoted a home-grown reform agenda, anchored in the AA /DCFTA commitments. The Ministry of Finance, as the coordinating agent, was able to liaise with line ministries and agencies to identify areas where their planned reforms needed some 'backing', e.g. reforms needing buy-in from a wide range of stakeholders.

In pushing for more difficult reform, it was a useful lesson for the EU that in-house ownership can play an important role and the push for reform is more successful when it builds on internal expertise /technical know-how. This was illustrated during DG GROW involvement in public procurement reform in Georgia.

5 Evaluation findings: Ukraine

5.1 Was the intervention relevant? [Related criterion to assess: relevance]

Question: *To what extent was the MFA operation design (including adequateness of financing envelope, focus of conditionality) appropriate in relation to the outputs to be produced and objectives to be achieved?*

In answering this question, four essential issues are considered, namely: (i) adequacy of the size of the financial assistance, (ii) appropriateness of the form of financial assistance, and (iii) design, and (iv) focus of conditionality.

Issue 1: Size of the financial assistance

Size of the financial assistance vs expectations

Since MFA I, all subsequent MFA operations to Ukraine have sought to address the country's significant external financing needs and support its economic stabilisation and reform efforts in the face of external conflicts and instability. Each successive MFA intervention has increased in size and/or form¹⁶². In the request seeking further MFA assistance, the Ukrainian government did not detail the desired funding amount. The final size of the assistance, as determined by the legislative authorities, aligned with the sum suggested by the European Commission and IMF projections.

¹⁶² A first MFA of EUR 610 million, second MFA of up to EUR 1 billion, a third MFA of up to EUR 1.8 billion, and a fourth MFA of up to EUR 1 billion in loans.

Size of financial assistance vs financing gap and burden-sharing considerations

As reflected in the European Commission proposal, MFA IV to Ukraine was tailored to align with the ongoing IMF programme's timeframe, which was set to conclude in March 2019. Given the timeframe, the MFA operation was limited to two instalments, focusing on mitigating Ukraine's residual external financing needs for 2018 and 2019, in conjunction with the ongoing IMF programme¹⁶³. These financing needs were estimated at about USD 4.5 billion, in addition to the USD 40 billion financing requirement identified by the IMF in 2015¹⁶⁴, which the EU had already partially addressed through MFAs I to III. The primary goal of MFA IV was to contribute to Ukraine's economic stability and support its continuing reform efforts, as part of the EU's broader commitment to the country's financial health and reform processes.

A revised IMF assessment in December 2017 projected Ukraine's external financing requirements for 2018-2019 at USD 16.1 billion, with the larger portion, USD 10.5 billion, needed in 2018¹⁶⁵. Part of this financing gap was also considered to be due to the non-disbursement of the amounts envisaged by the IMF's EFF. The projection was based on Ukraine's anticipated borrowing from international debt markets and the need to accumulate substantial international reserves, as per the IMF's standards (USD 11.6 billion). The balance of payments deficit, primarily driven by slower private capital inflows and strong domestic demand, accounted for the remaining financing need of USD 4.5 billion. This financing gap of USD 4.5 billion (EUR 3.8 billion) was considered even after IMF's contribution for 2018-2019. For this reason, and to remain proportionate, the EU's proposed MFA IV of EUR 1 billion aimed to cover 26.5% of this gap and 32% post-consideration of the WB's prospective USD 800 million policy-based guarantee. This projection was also based on the assumption that Ukraine would be able to secure funding from the international markets in 2018 and 2019 of up to USD 2 billion annually. Other major contributions were expected from international donors, notably the WB and the US (see Table 5.1).

Table 5.1 MFA and the estimated financing gap, 2018-2019, USD billion

	2018	2019	Total 2018-2019
1. Financing gap	10.5	5.6	16.1
Reserve accumulation	9.5	2.1	11.6
Underlying balance-of-payments gap	1.1	3.4	4.5
2. Identified financing	7.3	4.4	11.7
Bilateral and multilateral	5.3	3.3	8.6
IMF	5.3	3.3	8.6
3. Debt operations	2.0	1.1	3.1
4. Remaining gap, of which	3.3	1.2	4.5
MFA	0.6	0.6	1.2
WB	0.8		0.8

¹⁶³ European Commission, Ex-ante evaluation statement on EU macro-financial assistance to Ukraine, 2018, <https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1520603877743&uri=SWD:2018:66:FIN>

¹⁶⁴ IMF, *Country report No 15/69*, 2015, https://www.imf.org/-/media/Websites/IMF/imported-full-text-pdf/external/pubs/ft/scr/2015/_cr1569.ashx

¹⁶⁵ European Commission, *Ex-ante evaluation statement on EU macro-financial assistance to Ukraine*, SWD/2018/066 final.

	2018	2019	Total 2018-2019
Other sources, to be identified	1.9	0.6	2.5

Source: IMF projections (European Commission, Ex-ante evaluation statement on EU macro-financial assistance to Ukraine, SWD/2018/066 final).

A portion of the gap, USD 2.5 billion, had yet to be identified. Qualitative evidence from stakeholder interviews indicates similar perspectives on the adequacy of MFA IV. One highlighted its positive contribution to the country's budget and overall economic health, emphasising the limited FDI and the significant support provided by IFIs and commercial partners. Others noted that the MFA constituted a substantial amount of external financing in 2018 and 2020, although diminishing in 2020, attributing to favourable GDP growth.

Size of financial assistance in absolute terms

In absolute terms, and compared to other operations, MFA IV represented a significant allocation, in line with the trend of substantial support to Ukraine in previous MFAs. Its size was smaller than MFA III, but the needs in Ukraine were less dire than in 2014-2015.

Size of financial assistance in relative terms

The financial disbursements under MFA IV were relatively small in proportion to the overall scale of the Ukrainian economy, representing about 0.5% and 0.4% of annual GDP (current prices) for 2018 and 2020, respectively, or 2.8% and 2.0% of gross international reserves for each year. The scale of MFA IV disbursements was notably less than the funds provided by the IMF under the Standby Arrangement Facility in Ukraine during the same period, with disbursements amounting to EUR 1.2 billion and EUR 1.8 billion in 2018 and 2020, respectively.

Issue 2: Form of the financial assistance

MFA is typically structured as a loan to address immediate and temporary financial challenges. However, under specific circumstances, the recipient nation may qualify for grants alone or for a mix of grants and loans. The criteria for receiving a full grant or a combined MFA primarily hinge on two factors: economic and social progress in the receiving country, and its ability to sustain and repay debt.

As of 2017, Ukraine was classified by the WB as a lower middle-income country¹⁶⁶. Its GNI was the highest among its Eastern European neighbours, at an estimated USD 100,202 billion¹⁶⁷, making it the largest country in the EaP by a considerable margin¹⁶⁸. An additional factor identified in the ex-ante evaluation was that the structure of MFA IV aligned with the

¹⁶⁶ WB data, <https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups>

¹⁶⁷ WB data, GNI Atlas method, <https://data.worldbank.org/indicator/NY.GNP.ATLS.CD?end=2022&locations=UA-MD-GE-BY-AM-AZ&start=2017&view=chart>

¹⁶⁸ Armenia trails Ukraine, with a GNI of approximately USD 11.621 billion, indicative of a much smaller economic footprint. Azerbaijan's GNI at USD 40,496 billion, while substantial, is less than half of Ukraine's, reflecting a smaller yet sizable economy. Belarus is closer to Ukraine in economic terms, with a GNI of USD 50,355 billion, suggesting a relatively robust economic structure, albeit still not on par with Ukraine. Georgia and Moldova, with GNI of USD 15,049 billion and USD 9,105 billion, respectively, are at the lower end of the economic spectrum within this regional group.

approach taken in the previous three MFA initiatives (2014-2017). This method of support corresponded to the kind of assistance extended to Ukraine by the WB and IMF¹⁶⁹.

The analysis of EU budgetary room (as shown in Annex 14 on uncommitted budget allocations for MFA grants between 2017-2020) shows that there may have been scope to provide an additional EUR 10-15 million to Ukraine in the form of grants. However, compared to the size of the Ukrainian economy, these additional funds and very small grant component might not have made a significant difference.

Issue 3: Focus of conditionality

High-level analysis

In addition to the general principles informing the focus of conditionality (see Figure 3.2), the design of conditionalities attached to MFA IV was very much informed by the experience and lessons of MFA III in relation to the focus, scope and number of conditions.

With the decision not to disburse the last tranche of MFA III due to Ukraine's non-fulfilment of certain conditions, including in the area of combating corruption, there was a perceived need for Ukraine to show progress in this area. A Joint Statement was attached to the decision on MFA IV, whereby the EP, the Council and the Commission underlined that further MFA would be conditional on progress in the fight against corruption in Ukraine. The Joint Statement specifically highlighted the importance of the asset verification system, the operationalisation of the HAAC, and verification of companies' beneficial ownership data, as well as conditions linked to combating anti-money laundering and tax avoidance. The Joint Statement, while not legally binding, informed the negotiation of the MoU with the Ukrainian authorities. In that context, the MFA IV maintained some of the core objectives of the previous operation and helped to reflect the EU's overall priorities in its relationship with Ukraine.

Extent to which conditionality was in line with core objectives of the operation and EU priorities

The MFA operation focused on the following four reform areas: 1) PFM, 2) governance and fight against corruption, 3) sector reforms and SOEs, 4) social policies. A number of the conditionalities followed-up MFA III.

Among others, the conditions aimed to contribute to several outcomes:

- Improved PFM framework (tax and customs reform);
- Reinforcement of commitments to reform (anti-corruption, anti-money laundering, corporate governance in SOEs, privatisation, reforms in the banking sector, electricity market law);
- Social benefits (e.g. healthcare reform, social benefits, internally displaced persons).

Many of these outcomes had a clear and direct link either to the objectives of the MFA operation (macroeconomic stability) and/or EU external policy objectives, including under the AA. For example, reforms in customs and trade facilitation measures were expected under the AA, as was the adoption of a new anti-money laundering law. Anti-corruption reform and the creation of an anti-corruption framework composed of professional and independent institutions (National Anti-Corruption Bureau (NABU), Specialised Anti-Corruption

¹⁶⁹ European Commission, *Ex-ante evaluation statement on EU macro-financial assistance to Ukraine*, SWD/2018/066 final.

Prosecutor's Office (SAPO), National Agency for Prevention of corruption (NAPC), HACC) remains at the core of the EU's support to Ukraine, as well as that of other donors (e.g. IMF).

The relevance of the attached conditionalities was also achieved through the close involvement of technical experts (including from DG NEAR's Support Group for Ukraine, as well as the EU's Anti-Corruption Initiative (EUACI) programme based in Kyiv) in the design of MFA IV conditionalities. A number of EU-level stakeholders (DG ECFIN, DG NEAR, EU Delegation and EEAS) emphasised that this level of cooperation improved during MFA IV compared to previous or subsequent MFA operations and resulted in the design of targeted, technical conditions – especially in the area of anti-corruption or customs. This was seen to have helped to ensure that the conditions were designed in line with wider EU priorities and the reform efforts supported by other EU programmes, thereby ensuring their relevance. The stakeholder consultation suggested that this level of cooperation was lost during the COVID-19 pandemic and due to later changes in personnel within the European Commission.

Number of conditions and scope of conditionality

The number and scope of conditions under MFA IV was informed by the experience and lessons of MFA III. The overall aim was to make the conditions more focused and concrete (thus more easily measurable), while reducing the overall number compared to the previous MFA operation. This resulted in 18 conditions (compared to 36 previously), with the first six attached to the first tranche.

No stakeholder disagreed with the number of conditions set. The Ukrainian authorities cited some challenges in meeting the conditions attached to the first tranche, given the short timeframe available, but they were all successfully implemented ultimately and the first tranche was duly disbursed. This was considered an important political precondition at EU level, considering the non-fulfilment of conditions attached to the previous MFA operation.

The scope of the different conditions and their level of ambition varied. Some went into a considerable level of technical detail to support the operationalisation of existing systems and infrastructures (e.g. asset verification). Others remained broader and harder to measure in terms of impact (e.g. adoption of reform/action plans for customs/tax or internally displaced persons).

The majority of conditions (eight out of 18) fell within the last category and constituted a follow-up to previous legislative or institutional changes, forming part of a longer/ongoing reform process. This was understandable, given the EU's support for Ukraine's reform efforts since 2014, including via previous three MFA operations. Most were attached to good governance and the fight against corruption, underscoring the importance of reforms in the context of EU-Ukraine relations. The social policy conditions also all fell into this category.

One-third (six out of 18) of the conditions form actions that are part of a longer reform process but can be viewed as an initial stepping stone. These include the adoption of medium-term reform plans for the tax and customs administration, amendments to existing legislation and/or ratification of international conventions in the tax or customs fields, as well as selection of members of supervisory boards of SOEs. Impact in this category can be harder to measure, as follow-up falls outside the scope of the MFA operation and relies on the (political) will of national stakeholders.

Two of the conditions attached to the first tranche fell within the last category of conditionalities, defined by the study team as Type A: concrete measures with no immediate impact. They included specific measures, such as the issuance of general tax consultations or the sale of state-owned assets. They were formulated to be very specific and implementable within the short timeframe envisaged for the first tranche. Both supported

ongoing reform efforts in a concrete way, without necessarily foreseeing subsequent follow-up.

For two specific reform priorities (operationalisation of the asset verification system; HAAC), MFA IV developed sequential conditions for each tranche, helping to break down the expected reform into more concrete follow-up steps.

Complementarity/cross-conditionality with other EU and IFI programmes

See discussion in Section Evaluation criterion: Coherence.

Extent to which MFA IV addressed priority areas for reforms, relevance of specific reform areas, and conditionalities

Discussions with key EU stakeholders showed an overall consensus on the relevance of the conditions. There was an understanding that the final selection represented a cross-section of the most important reforms across the key priority areas. The close involvement of technical experts in the design of MFA IV conditions also played a role in ensuring their relevance.

Box 5.1 PFM

PFM is usually at the core of MFA conditionality. Under MFA IV, the focus was on improving revenue mobilisation, as well as trade facilitation via tax and customs reforms.

PFM reform was a priority area for the Ukrainian government. Ukraine had a PFM Strategy (2017-2021) with four key objectives: 1) to maintain overall fiscal discipline in the medium term; 2) to improve resource allocation efficiency at the level of government policy-making; 3) to ensure efficient budget implementation; and 4) to improve the level of transparency and accountability in PFM. At the time, the action plan for the implementation of the Strategy was assessed by the Commission as overly optimistic, while other areas lacked progress¹⁷⁰. The Ukrainian Ministry of Finance stressed the need for regular technical assistance to help with the implementation of the reforms in the Strategy.

Ukraine's tax and customs authorities had long suffered from low levels of public trust. The tax authorities, in particular, were viewed as an instrument used to pressure businesses or provide unequal advantages to others. The complexity of the tax legislation created space for varying interpretations of tax law due to many contradictory provisions, leading to lack of transparency for businesses and, at times, unexpected fiscal pressure.

Understanding the need for a deep and comprehensive reform of the tax and customs administrations, in 2018, both the EU and IMF set out conditions linked to the need to reform the State Fiscal Service (SFS), which at the time comprised both tax and customs. The Ukrainian authorities also set the reform of the SFS as a priority, recognising the need to improve public trust, provide more transparency, and improve the service-oriented nature of the Service, which in turn would help to improve domestic tax compliance and increase government revenue. The SFS was split into separate State Tax and State Customs Services in 2019 as part of the reform. This issue gained in importance, especially in the context of Russia's war of aggression against Ukraine in 2022. A detailed case study on reforms of the SFS is included in Annex 11.3.

Additional conditions related to PFM tackled more concrete measures, including the issuance of tax consultations by the Ministry of Finance, to address inconsistent interpretations of the tax legislation (and create more clarity for businesses in certain areas). Other conditions helped to support the adoption/ratification of international conventions, facilitating further reforms (e.g. implementing OECD standards in fighting tax evasion; customs and common transit procedures).

¹⁷⁰ DG ECFIN, *Operational assessment of the financial circuits and procedures in Ukraine*, August 2018.

Box 5.2 Good governance and fight against corruption

Anti-corruption efforts have been at the core of international donor support to Ukraine since 2014¹⁷¹. Without tackling the issue, progress in the country (including macroeconomic improvements) would be limited in the long-term¹⁷². Call to root out endemic corruption was at the heart of citizens demands during the Revolution of Dignity in 2014. The Ukrainian government has since been under close scrutiny, including from civil society, to show concrete progress in moving away from the post-Soviet era legacy.

Anti-corruption reform was part of all previous MFA operations and IMF programmes to Ukraine. Reforms tackling corruption were also central to a number of other EU-led processes, including the Visa Liberation Action Plan for Ukraine. Given the Ukrainian authorities' uneven ownership of reform in this area, continued focus by local civil society and international donors maintained momentum and helped to move reforms forward.

Since 2014, Ukraine made significant progress on establishing a wide array of new anti-corruption institutions. MFA IV conditions were particularly focused on operationalising existing reforms, such as the newly created HAAC, and addressing existing shortcomings in existing reforms (e.g. improving the asset declarations verification system). Some aspects, such as the adoption of a revised anti-money laundering law were also closely linked to the AA.

Ukrainian authorities pointed to the complexity of implementing conditions where there was no agreed EU-standard, e.g. on beneficial ownership, which created uncertainty for local authorities and required input from Commission and Member State experts. They also noted that conditions should be worded so as to fully consider the local legal context in order to avoid later legal challenges (as was the case for some new anti-corruption institutions).

Box 5.3 Sector reforms and SOEs

Sectoral reforms played a pivotal role in MFA packages, as evidenced in the case of MFA IV for Ukraine, where they spanned two tranches. Enhancing how SOEs are managed was crucial for solving major related problems, including ineffective management practices that created a build-up of financial risk for the government. Issues such as corruption and political meddling created unfair advantages, disrupting fair competition for other businesses, with action seen as vital to improve overall performance and fairness in the sector.

The first tranche of conditions primarily focused on the need for corporate governance reforms within SOEs. The Ukrainian authorities took decisive action, including the appointment of independent members to supervisory boards in institutions such as Ukrenergo, Ukrzaliznytsia, Naftogaz, UkrPoshta, Ukrainian Sea Ports Authority, and Boryspil airport. Conditions focused on fixing problems related to poor management, financial risk, widespread corruption, and undue political influence. A key element was choosing independent members for the companies' supervisory boards, greatly increasing transparency and effectiveness.

The privatisation of small state-owned assets emerged as a critical step in reducing government influence, facilitating funding, and advancing managerial practices. This was accomplished through the utilisation of electronic auctions on the ProZorro.Sale platform, which enabled Ukraine to offer numerous small state-owned assets for sale. The initiative placed 300 assets up for sale and sold 67, signalling a clear shift towards an open market and inviting additional investment in the economy. The outcome was enhanced transparency and increased operational efficiency.

In the second tranche of conditions, the focus shifted to the banking sector, particularly addressing NPLs. The NBU took steps to manage these loans and recover assets in state-owned banks, promoting financial stability and growth. Corporate governance reforms within state-owned banks also played a pivotal role, leading to profitability and a substantial contribution to the banking sector's success. Lastly,

¹⁷¹ Kaleniuk, D., 'Tough anti-corruption conditions are essential', *Kyiv Post*, 11 July 2017, <https://archive.kyivpost.com/article/opinion/op-ed/daria-kaleniuk-tough-anti-corruption-conditions-essential.html>

¹⁷² IMF, *Government of Ukraine report on diagnostic study of governance issues pertaining to corruption, the business climate and the effectiveness of the judiciary*, 2014, <https://www.imf.org/external/pubs/ft/scr/2014/cr14263-a.pdf>

Ukraine's commitment to the implementation of the Electricity Market Law paved the way for a liberalised electricity market. The separation of power generation and transmission, along with Ukrenergo's certification as an independent transmission operator, enhanced market presence, transparency, and pricing mechanisms, benefitting consumers and attracting investment in sustainable energy practices.

These reforms led to improved corporate governance in SOEs, increasing transparency and investor trust while fostering efficient privatisation processes that reduce government interference and bolster managerial practices. Ukraine not only enhanced its economic governance but also curtailed opportunities for corruption and mismanagement, making SOEs more appealing to potential investors.

Box 5.4 Social policies

Conditions related to social policy reforms focused on ensuring sustainable healthcare financing, enhancing the targeting and efficiency of household utility subsidies, and adopting a comprehensive action plan for the integration and support of internally displaced persons until 2020.

In 2017, Ukraine initiated patient-centred healthcare financing reform, anchored by a substantial law (in October 2017), and creating a patient-oriented healthcare system. The National Health Service of Ukraine (NHSU) played a pivotal role, contracting healthcare providers for primary healthcare services. Restructuring state-owned medical institutions into municipal non-profit entities simplified the process, incentivising reform and aligning healthcare with patient preferences.

By March 2020, 1,539 contracts had been concluded, benefiting 71% of Ukrainians. Nearly 29.8 million citizens were free to choose their primary care providers, in line with the patient-centred approach. The eHealth system allowed real-time health analysis and efficient budget allocation. Ongoing establishment of interregional NHSU departments highlight commitment to widespread benefits despite political challenges.

Another condition aimed to improve the targeting, efficiency, and fairness of social benefits in Ukraine, particularly within the Housing and Utility Subsidy (HUS) programme, which aimed to assist households with energy bills. The condition was driven by the need to enhance targeting precision, given that nearly 50% of the HUS budget was allocated to households with above-average incomes. Resolution No 329, enacted in April 2018, established stricter eligibility criteria and thorough verification to combat fraud. It also introduced monetisation at household level to promote energy savings by directly providing subsidies to eligible households. Implementation efforts streamlined subsidy allocation, reducing the number of eligible households and the total subsidy amount, aligning with the goal of enhancing the programme's relevance and effectiveness. The Ministry of Social Policy gradually expanded subsidy monetisation, ensuring direct cash payments to households.

One condition stood out as lacking a clear link to macroeconomic stability (thus potentially being less relevant) – the condition linked to internally displaced persons. This was also mentioned as an atypical condition during the evaluation of MFA III. However, it was emphasised that it was politically important for the EU to show continued commitment toward enhancing the rights and integration of internally displaced persons and to build on similar conditionality included under the previous MFA operations, especially as further progress in this area was needed.

5.2 To what extent was the intervention successful and why? [Related criteria to assess: effectiveness, efficiency, coherence]

Evaluation criterion: *Effectiveness*

Part 1: assessment of the macroeconomic role of MFA IV

Examining the observed macroeconomic outcomes over the MFA disbursement period (2018-2020)

MFA IV was initiated amid a complex backdrop of geopolitical tensions, regional conflicts, and economic challenges. Prior to MFA IV, Ukraine struggled with the impacts of the global financial crisis, followed by political upheaval and military conflicts, including the illegal annexation of Crimea by Russia and the conflict in Eastern Ukraine since 2014. These events significantly hampered its economic progress, leading to a stark economic contraction of the economy in 2014, at 6.6%, and a further decline of 9.8% in 2015, exacerbated by severed economic ties with conflict-affected regions.

Between 2017 and 2020, Ukraine's economy showcased modest economic recovery followed by setbacks due to external shocks like the COVID-19 pandemic. The country experienced a **positive GDP growth trajectory**, supported by agricultural bounties, increased fixed investment, and reforms aimed at stabilizing the economy and fostering growth. Notably, GDP grew by 2.4% in both 2016 and 2017, reflecting the effectiveness of policy measures and international aid. This growth continued into 2018 and 2019 with real GDP increases of 3.5% and 3.2%, respectively, driven by improved political stability and economic reforms. Investment also saw a notable uptick, reflecting renewed confidence in the Ukrainian economy. However, the outbreak of the COVID-19 pandemic in 2020 posed new challenges, causing a significant economic downturn, with GDP contracting by 3.8%. The situation deteriorated further in 2022 due to Russia's war of aggression against Ukraine, leading to a devastating economic collapse, with a 29.1% drop in GDP. This period marked one of the most challenging phases in Ukraine's recent economic history, characterised by widespread infrastructural damage, disruption of economic activities, and massive displacement of people.

Inflation in Ukraine throughout the decade was marked by significant volatility, influenced by external and internal factors. The early part of the decade saw controlled inflation, but by 2015, it had rose to 43.3% due to currency devaluation and increased energy costs, amid geopolitical turmoil. In subsequent years, inflation rates fluctuated, with the government implementing various measures to stabilise prices.¹⁷³ By 2022, inflation surged to 26.6%, fuelled by global economic conditions, energy price fluctuations, and the impacts of Russia's war of aggression against Ukraine. **The labour market in Ukraine also underwent significant changes during this period.** Unemployment rates, initially decreasing post-financial crisis, escalated to 9.5% by 2016 due to the combined effects of economic turmoil and conflict. A modest recovery in 2019 was short-lived, as the COVID-19 pandemic and war in 2022 exacerbated unemployment challenges. The labour market faced particular difficulties in relation to women and young people, with rising unemployment rates and a widening gender pay gap, indicating structural imbalances and sector-specific vulnerabilities.

Prior to 2017, Ukraine experienced a series of fiscal fluctuations. The early 2010s were marked by stability, with **government revenue** stable at around 43% of GDP, signalling recovery from the global financial crisis. However, by late 2013, fiscal stability was

¹⁷³ [Changes are Possible: Which Reforms does Ukraine Need Now? \(worldbank.org\)](https://www.worldbank.org/)

compromised due to policy missteps and isolation from international capital markets. This situation worsened after Ukraine declined an EU Association Agreement for a \$3 billion loan from Russia. The annexation of Crimea and conflict in Eastern Ukraine in 2014 further strained fiscal resources, necessitating budget cuts and impacting revenue, particularly with the loss of the economically significant Donbas region.

In response, Ukraine implemented significant fiscal measures, including tax reforms and spending cuts, leading to a gradual reduction in government spending as a percentage of GDP. The fiscal policy was central to the IMF programme initiated in 2014 to stabilise the economy. By 2015, the government had successfully lowered spending to 43% of GDP, a testament to the stringent fiscal discipline adopted during this period. **Government debt** in Ukraine followed a fluctuating trajectory. Before 2013, it remained below the budget code threshold of 60% of GDP, but surged due to the economic downturn, currency depreciation, and the need for significant public sector recapitalisation. Ukraine embarked on a comprehensive restructuring of its external public debt in 2015, which was instrumental in bringing the debt level down to 71.6% in 2017 from 79.5% in the previous year.

During MFA IV, Ukraine witnessed a decrease in general government gross **debt as a percentage of GDP**, with a decline from 60% of GDP to 50% in 2019. This period was marked by prudent fiscal management and strategic debt restructuring, contributing to a consistent debt level around or below the 60% mark. Fiscal balance also saw some deterioration in the following years, with slight increases in government spending are observed during the period of MFA IV by about 4.6% despite insignificant changes in government revenue. The increased spending was allocated towards social services, housing, utility subsidies, and defence, reflecting the dual needs of addressing the COVID-19 pandemic and supporting economic recovery.

Ukraine's gross financing needs as a percentage of GDP has tended to be relatively high, raising concerns about instability. Over 2016-20, Ukraine's gross financing needs to GDP averaged 12%. In 2020 gross financing needs increased to 15%, bringing this indicator to a level typically considered to be of some concern with respect to debt sustainability; a situation which continued into 2021. Gross financing needs increased further in 2022, to 25% of GDP. The economy was thus increasingly under stress.

Ukraine's **external sector and balance of payments** position also experienced significant shifts. The early 2010s were characterised by current account deficits, impacted by unstable capital investments, reduced demand for exports, and high energy import costs. However, a surplus emerged in 2015, driven by agricultural growth and increased investment inflows. In 2020, Ukraine experienced a significant increase in its current account due to substantial grant support from international partners. Goods trade consistently registered deficits, highlighting challenges in expanding the export base and balancing imports. The services trade, a strength for Ukraine, also experienced a deficit in 2022. Amongst other reasons, this deficit was partly due to the Russian aggression disrupting foreign trade and closing key export routes, coupled with economic contraction and sanctions on Russia.¹⁷⁴ The displacement of millions of people within Ukraine further disrupted local demand for services, contributing to the deficit.¹⁷⁵

Current transfers, including remittances and international aid, played a crucial role in supporting Ukraine's economy, especially in 2022, with a significant surge in international support. Income from abroad showed resilience, with notable surpluses, reflecting stable remittances and strategic management of outbound investment payments.

¹⁷⁴ [World Bank: Ukraine economy to shrink by almost half in 2022 | World Economic Forum \(weforum.org\)](https://www.weforum.org/news/world-bank-ukraine-economy-to-shrink-by-almost-half-in-2022)

¹⁷⁵ [Services Barometer Template June 2022.xlsx \(wto.org\)](#)

In the **banking sector**, Ukraine's regulatory capital to risk-weighted assets ratio illustrated the sector's resilience. The ratio was high at the start of the decade but declined through 2015, indicating stress due to economic downturns and increased loan defaults. Post-2015, the ratio improved, surpassing the 2010 level by 2020, signifying recovery and the impact of regulatory reforms. The NPL ratio, initially high due to banking sector challenges, reaching a peak of 54.5% of total gross loans in 2017 and decreased significantly 41% in 2020, demonstrating effective resolution processes and stabilisation of the loan portfolio.

In summary, Ukraine's economic landscape during MFA IV was shaped by a series of profound challenges, including geopolitical conflicts, and the COVID-19 pandemic. Nevertheless, the country exhibited remarkable resilience, underpinned by strategic economic reforms, fiscal discipline, and international support. The fluctuations in GDP, inflation rates, labour market dynamics, and public debt levels underscored the country's ongoing efforts to stabilise and grow its economy amid persistent external and internal pressures.

Table 5.2 Evolution of key macroeconomic indicators, Ukraine

Indicator	2017	2018	2019	2020	2021
GDP, current prices (USD billion)	112.1	130.9	154.0	156.6	199.8
Real GDP growth (%)	2.4	3.5	3.2	-3.8	3.4
Inflation, average consumer prices (%)	14.4	10.9	7.9	2.7	9.4
Inflation, end of period consumer prices (%)	13.7	9.8	4.1	5.0	10.0
Unemployment, % of labour force	9.7	9.0	8.5	9.2	9.8
General government structural balance (% of GDP)	-1.8	-2.5	-1.7	-5.1	-3.3
General government gross debt (% of GDP)	71.6	60.3	50.4	60.5	48.9
Gross external debt (USD billion)	115,451	114,710	121,739	125,682	129,713
Gross external debt (% of GDP)	103.0	87.6	79.1	80.2	64.9
FDI (inflows) (USD billion)	3,680	4,975	5,796	304	7,954
FDI (inflows) (% of GDP)	3.3	3.8	3.8	0.2	4.0
Gross international reserves (USD billion)	18,808	20,820	25,302	29,133	30,941

Sources: IMF, WB, National Statistics Office of Ukraine, NBU.

Assessing the role and contribution of MFA IV to observed outcomes

To assess the contributions of MFA IV support to Ukraine's debt sustainability, the observed main debt sustainability indicators (baseline) are compared to hypothetical outcomes in three alternative scenarios (counterfactuals). The three scenarios are as follows, of which just the first two were modelled:

1. What would have happened without the first tranche of the MFA IV, disbursed in 2018 (Alternative A: no MFA first tranche);
2. What would have happened without the second tranche of the MFA IV, disbursed in 2020 (Alternative B: no MFA second tranche);
3. What would have happened in the absence of MFA IV and without IMF assistance (Alternative D: no MFA and no IMF).

Alternative A: No disbursement of first MFA IV tranche in 2018

Without this disbursement, Ukraine might have resorted to borrowing from high-interest domestic markets or the costly international financial markets. The country would likely have turned to domestic financial markets for borrowing, despite high interest rates. Alternatively,

Ukraine might have sought funding from international markets, but this would have been expensive, given the high yields on Eurobonds at that time. Ukraine would likely also have looked for increased assistance from multilateral and bilateral donors, although this approach would have been constrained by the prevailing political and economic conditions. Fiscal adjustments, potentially in the form of improved tax collection or spending cuts, would have been on the table. However, making significant changes in this direction would have been difficult due to the political climate, particularly with upcoming presidential and parliamentary elections (in 2019) and the need for social stability.

Alternative B: No disbursement of the second MFA IV tranche in 2020

The absence of this tranche during the COVID-19 pandemic would have led Ukraine to rely on domestic borrowing, despite high costs. The global economic downturn caused by the pandemic would have made international borrowing a very costly and potentially unsustainable option. Seeking additional multilateral and bilateral support would have become necessary to fill the funding gap, especially for healthcare and pandemic response. Fiscal adjustments would have been likely, with the government prioritising spending cuts in areas deemed less critical, such as infrastructure, to allocate more resources to urgent healthcare needs. In the context of MFA IV to Ukraine, Alternative C does not apply here.

Alternative D: No MFA and IMF support

This scenario would have significantly strained Ukraine's financial resources. The absence of support would have dramatically increased borrowing costs and reduced market access, both domestically and internationally. High domestic borrowing rates, reflecting the country's economic fragility, would have become more pronounced. The situation would have been exacerbated in the international financial market, where Ukraine's ability to secure funding at reasonable rates would have been severely hampered. This scenario would have necessitated stringent fiscal adjustments, with the government likely implementing substantial spending cuts across various sectors. Debt restructuring might have been considered a way to alleviate the financial burden, but this would have carried risks for Ukraine's long-term financial reputation and the perception of its creditworthiness in international markets.

For each of these scenarios, the absence of MFA IV and IMF support would have put Ukraine's financial stability and economic growth at significant risk, especially during the COVID-19 pandemic. The Ukrainian government would have had to navigate a delicate balance between addressing immediate financial challenges and ensuring long-term fiscal health.

Choice of the most plausible counterfactual scenario(s)

The table below presents our conclusions on the most plausible counterfactual alternative(s), that feed into the rest of the analysis.

Table 5.3 Most plausible counterfactual scenario(s)

Ukraine	
Alternative A: Absence of MFA first tranche : absence of EUR 500 million in December 2018.	
Alternative financing	International and/or domestic market. Fiscal adjustments (improved tax collection or spending cuts).

Ukraine	
Direct implications	Either external borrowing at higher interest rates, or cut in government spending.
Alternative B: Absence of MFA second tranche : absence of EUR 500 million in May 2020	
Alternative financing	Probably not available.
Direct implications	Budget cuts and possible reduction/postponement of capital expenditure.
Alternative D: No MFA or IMF support: absence of EUR 4 billion over 2018-2020	
Alternative financing	Limited scope for borrowing from domestic markets.
Direct implications	More severe budget cuts, with heightened implications for economic stability and debt sustainability.

Debt Sustainability Analysis (DSA)

The objective of the DSA was to evaluate the contribution of MFA IV (2018-20), and IMF support to Ukraine's debt sustainability in terms of public debt and gross financing needs (including as ratios to GDP). DSA involves modelling the key debt burden indicators and macroeconomic variables that affect the path of a country's debt and its ability to manage its debt sustainability. The full DSA is presented in Annex 9.

In developing these counterfactuals, experts were consulted on the most likely courses of action in the absence of support, and different scenarios of plausible action were defined. The scenarios were then modelled in the IMF DSA tool for each counterfactual, including, where applicable, estimates and assumptions on how borrowing costs might have changed and how GDP would have been affected. The consequent evolution of the main DSA indicators was assessed, shedding light on the macro-fiscal contribution of MFA IV and IMF support.

Ukraine: Alternative A – no MFA first tranche

Without the first MFA tranche, worth EUR 500 million and disbursed in December 2018, Ukraine would likely have relied on borrowing from domestic and/or international markets, at higher interest rates. This might have been paired with some (limited) cuts to government spending but heavier borrowing was thought to be the predominant response.

Relying mainly on alternative financing would have come at higher borrowing costs due to both direct and indirect effects. The direct effect would arise as a result of increased interest payments on debt compared to the MFA conditions. The indirect effect represents the increased cost of borrowing from private investors resulting from lower investor confidence in the absence of MFA support. Overall, covering the financing gap fully using alternative financing would have increased gross financing needs and gross public debt slightly, by 0.2 pp and 0.1 pp, respectively.

Ukraine would have seen changes to its main debt sustainability indicators and its outlook would have been slightly worsened, but the situation was already quite challenging. Gross financing needs would have continued to have exceeded the 15% threshold at which countries might be at increasing risk of unsustainable debt.¹⁷⁶ There would also have been large implications for the economic growth outlook, given that, in the absence of this support, GDP would have been lower.

Ukraine: Alternative B – no MFA second tranche

Without the second MFA tranche, worth EUR 500 million and disbursed in May of 2020, government spending cuts and postponement of capital expenditure were much more likely in Ukraine. Covering the outstanding financing gap through government spending would have had negative effects on GDP. Ukraine would have seen overall mild changes to its main debt sustainability indicators and its outlook would have been somewhat worse than the already-challenging situation. Gross financing needs would however have continued to be at levels of concern. There would also have been significant implications for the economic growth outlook, given that GDP would have been lower.

Ukraine: Alternative D- no MFA and no IMF

Without MFA IV and IMF support, worth a total of EUR 4 billion and disbursed from 2018-2020, Ukraine would have faced a highly constrained financial environment. The dependence on external funding, particularly low-interest options like MFA support, was a cornerstone of its financial strategy. The absence of support would have significantly increased borrowing costs and reduced market access. Additionally, the decrease in donor support would likely not be confined to the EUR 1.4 billion of MFA and IMF loans. The IMF support was considered essential to restoring investors' confidence and improving credit ratings. Without this support, investors' confidence and Ukraine's outlook would have been much worse. There would have been considerable risk that other donors would withdraw their support.

The potential implications of this scenario seem severe. Further evaluation of the impacts of a potential default on Ukraine's economy, for example, would be purely speculative due to the level of uncertainty. Accordingly, the scenario is not analysed any further using the DSA framework.

Part 2: Assessment of effectiveness of MFA conditionality

The following sub-sections summarise the effectiveness of MFA IV conditions linked to the different thematic areas: PFM reform; good governance and fight against corruption; sector reforms; and social policies. A more detailed analysis of each condition, its implementation and measurable benefits is presented in Annex 13.3.

Overall, progress was made in all areas, with all conditions implemented successfully. Some conditions were defined more specifically and aimed to tackle technical issues, while some were worded quite broadly (e.g. the adoption of reform/action plans). Broader conditions were sometimes criticised for not having a direct impact yet were also understood to have a wider signalling effect in relation to reform.

The need for wider EU-level support in implementation, including the presence of technical assistance projects, was highlighted as crucial to the effectiveness of MFA conditionality. Technical assistance projects supported reforms in the area of anti-corruption (EUACI) and PFM (EU4PFM) and continue to do so today, including conditions specifically tackled by MFA IV (tax, customs, asset verification, HAAC). In the context of the adoption of the Anti-

¹⁷⁶ IMF. 2013. 'Staff guidance note for public debt sustainability analysis in market-access countries'. Available [here](#); [link](#).

Money Laundering Law – which faced strong opposition in the parliament due to MPs concerns about disclosure of their business interests – the role of the EU Delegation and IMF in supporting the adoption of the law was highlighted by Ukraine’s Ministry of Finance.

Some EU-level stakeholders noted that MFA IV was announced shortly after the decision not to disburse the last tranche of MFA III. For some, this diluted the impact of the non-disbursement decision, and MFA IV was seen as indirect compensation for that decision. At the same time, others felt that the decision not to disburse MFA III’s last tranche sent a strong signal on the need to uphold and implement conditionality under MFA IV and, in that context, helped to strengthen effective implementation of that conditionality. Some stakeholders also pointed to the fact that MFA III was overly ambitious, while MFA IV sought a better balance between maintaining the overall ambition of the attached conditionality, while ensuring that conditions were realistic and achievable. The challenge was to ensure that the ambition level was sufficiently high, while setting realistic targets. Lastly, some emphasised that the decision not to follow up MFA III with another MFA operation would have undermined the EU-Ukraine relationship in the long-term.

Discussions with stakeholders show that the context has changed quite significantly since MFA IV, taking into account the COVID-19 pandemic, Russia’s war of aggression against Ukraine since February 2022, as well as Ukraine’s progress on its path toward the EU. These factors all played a role in shaping the continuation of some of the reform efforts initiated or supported under MFA IV. Some long-term developments and progress cannot be divorced from the changing context, making it more difficult to judge the direct effectiveness of MFA IV conditionality alone. Clearly, there was significant progress by the Ukrainian authorities (including in the past two years) to align legislation with the EU *acquis* (notably in the area of customs). At the same time, the government has had to operate in an increasingly complex environment, despite losing important human resources (staff leaving for the war, or the EU), further limiting the capacity needed to continue implementing reforms.

Box 5.5 PFM reform

PFM reform in the context of MFA IV focused on improving revenue mobilisation and trade facilitation. The MFA IV conditionality tackled a number of issues, with varying degrees of complexity and specificity. This prompted some discussion about the effectiveness of conditions that are quite broad vs conditions that are very specific but tackle a narrower area.

A number of stakeholders pointed to the general/broad nature of conditionality that foresaw the adoption of a medium-term reform plan for the SFS, noting the difficulty in fully attributing impact or effectiveness of such MFA conditionality to any subsequent specific reforms. Broad conditionality can also hinder implementation as there may be different understandings and expectations on each side. At the same time, MFA conditionality (jointly with IMF structural benchmarks in this area) were seen to send an important signal of the need to systematically reform the tax and customs administrations and ensure improved revenue mobilisation.

Given the complexity of the institutional reform, it was seen as a stepping stone toward initiating medium-term reforms. Stakeholders noted that the presence of technical assistance projects was central to ensuring some progress of reform within the SFS (e.g. EU4PFM, IMF supporting the restructuring of the service and further internal capacity-building). The process of reform is ongoing, with gradual improvements in the functioning of both tax and customs administrations, accompanied by repeated calls for further reform. The Ukraine case study in Annex 11 gives a more detailed assessment of the effectiveness of this conditionality.

Additional PFM conditions were more targeted and specific, addressing technical reforms and legislative changes. Significant progress was noted in the area of customs and the introduction of the Authorised Economic Operator (AEO) programme, as well as joining the Common Transit Convention and the

introduction of a new computerised transit system (NCTS). EU4PFM, as well as the Reform Support Team within the Ministry of Finance, played an important role in supporting the implementation of both AEO and NCTS. As these reforms are closely linked to the AA, it is possible that they would have been eventually implemented also without MFA conditionality. However, stakeholders emphasised previous delays with the adoption of the relevant legislation (e.g. linked to AEO), suggesting that MFA conditionality provided an impetus for more rapid reform.

Progress in customs reform, supported by the EU, contributed to Ukraine making a good level of preparations on customs unions (as assessed by the Commission in 2023)¹⁷⁷. The introduction of the AEO and NCTS, both supported via MFA IV conditionality, were important trade facilitation measures, with clear impact on Ukrainian businesses.

Reforms linked to the implementation of OECD standards on tax evasion were important. Here, MFA conditionality was seen (including by the OECD and Ministry of Finance) to have contributed to the process of the ratification of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BESP MLI)¹⁷⁸, an important step forward in limiting opportunities for tax avoidance by multinational enterprises. Further progress was supported via capacity-building by the OECD and EU4PFM (ongoing).

Since 2020, it has been understood that effective revenue mobilisation will play a crucial role in Ukraine's future reconstruction. The reform of both tax and customs are ongoing, with further reform targets set under Ukraine's new Revenue Strategy (with inputs from international donors) in 2023.

Box 5.6 Good governance and fight corruption

Good governance and the fight against corruption was a key conditionality across all previous MFA operations, as well as IMF programmes. Since 2014 Ukraine has made substantial progress through the creation of a vast array of new anti-corruption institutions. However, given the uneven reform ownership of Ukrainian authorities - especially in the area of anti-corruption – it was considered important to attach conditionality that would build on previous MFA operations and support progress on reforms already implemented.

MFA IV conditionality was focused on further operationalising existing reforms, such as the HACC, and addressing existing shortcomings in implemented reforms (e.g. improving the asset declarations verification system). Some aspects, such as the adoption of an anti-money laundering law, were also closely linked to the AA.

The conditions were all quite specific and well defined, making it easier to measure their implementation and impact. The exception was the condition linked to disclosure of beneficial ownership, where the lack of clearly defined EU standards required Ukrainian authorities to seek additional clarity from the Commission. In such instances, it may be preferable to have more clarity in the wording of the original condition to avoid uncertainty.

MFA IV made effective use of the fact that the same condition was attached to both tranches. This was used to break the specific conditions around the HACC and the asset declaration system into smaller steps, making them easier to implement and allowing for more targeted follow-up.

¹⁷⁷ European Commission, *Analytical Report following the Communication from the Commission to the European Parliament, the European Council and the Council Commission Opinion on Ukraine's application for membership of the European Union*, (SWD(2023) 30 final), https://neighbourhood-enlargement.ec.europa.eu/system/files/2023-02/SWD_2023_30_Ukraine.pdf

¹⁷⁸ OECD, *Multilateral Convention to implement tax treaty-related measures to prevent BEPS*, n.d., <https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beeps.htm>

Given the difficulties faced in the adoption of the HACC law, additional conditions linked to its budget and selection of judges aimed to ensure that the reform success would not later be undermined. Since its establishment, the HACC has been viewed as an effective and independent institution, contributing meaningfully to the fight against corruption in the country.

The necessary information technology (IT) upgrades to the asset declaration and verification system, allowing for automated checks of data, helped to improve the overall effectiveness of the system and prioritise declarations for verification. The target of verifying 1,000 declarations of high-level officials was met. However, the system continued to face different legal challenges (see Annex 13.3), highlighting the difficulty in ensuring the sustainability of implemented reforms.

Finally, Ukraine continued to build on other reforms linked to MFA IV conditionality, including the disclosure of beneficial ownership of companies, and anti-money laundering legislation.

Box 5.7 Sector reforms and SOEs

Conditions on sector reforms and SOEs enabled significant improvements in addressing multiple aspects of economic and governance inefficiency. The condition targeting the privatisation of state-owned assets ensured that numerous state-owned objects were put up for sale through electronic auctions, aligning with the government's privatisation strategy. The successful sale of these assets reduced government influence over the economy and sent encouraging signals to potential investors. Another noteworthy aspect was the focus on improving corporate governance within state-owned banks. The enactment of Law No 2491-VIII and the appointment of independent members to supervisory boards marked significant progress. That transition to greater independence resulted in enhanced bank performance and profitability, as well as instilling confidence in the financial sector and its governance.

Addressing the high levels of NPLs in Ukraine's banking sector was a priority. This condition prompted the NBU to develop a resolution on NPL management, emphasising asset recovery and reporting transparency. The subsequent reduction in NPLs substantially improved financial sector stability, promoting a healthier banking environment. The condition on the implementation of reforms in the electricity market – notably the certification of Ukrenergo and the separation of power generation and transmission – were crucial achievements, aligning Ukraine's electricity market with EU standards, enhancing market efficiency, transparency, and market-driven operations.

Despite these achievements, stakeholders acknowledged certain persistent challenges. For example, while the revenue generated from the sale of state-owned assets exceeded initial expectations, it was relatively modest in absolute terms. There is a need to address challenges related to marketing, auctioning, and deal closures. In the banking sector, continuous monitoring and addressing legacy NPLs are imperative to maintain the stability of state-owned banks. Additionally, sustaining the independence of supervisory boards and upholding positive changes in corporate governance requires ongoing vigilance.

Box 5.8 Social policies

The condition on healthcare financing reform was effective in improving the quality and efficiency of healthcare services in Ukraine. The implementation of the 'money follows the patient' principle, and the signing of contracts between the NHSU and providers of primary healthcare significantly improved service delivery, while the creation of the eHealth system enhanced data analysis and resource allocation. The targeting, efficiency, and fairness of social benefits were addressed, with the HUS programme restructured. Tighter eligibility criteria and verifications led to better targeting, reducing the number of eligible households and subsidies paid. Monetisation of subsidies at household level was initiated, providing direct support to beneficiaries.

Finally, a proactive approach was taken to the integration of internally displaced persons. The approval of an Action Plan to implement the Internally Displaced Persons Integration Strategy until 2020 signified a commitment to address the needs of this vulnerable population. Measures to ease payment of social

benefits and provide compensation for property damage reflected the government's dedication to supporting internally displaced persons.

Social Impact Analysis (SIA)

The overarching aim of the SIA was to use evidence from social indicators and primary data to assess the impacts of MFA IV on the social situation in Ukraine. The analysis considered both direct impacts of policies specified in the MFA conditionalities and indirect impacts of wider macroeconomic stability across a range of social indicators. The full findings are presented in Annex 10.3.

Key findings of the SIA in Ukraine include:

- **While not expressly the aim, healthcare reform may have improved future resilience (e.g., for the subsequent COVID-19 pandemic and war).** While reform efforts did not (as yet) result in clear reductions in the contribution of out-of-pocket expenditure on healthcare, the analysis suggests that actions taken may have facilitated more resilient service provision in critical times. The new law contributed to a substantial increase in the number of contracts between health authorities and service providers. Experts highlighted the role of such reform action in enabling the organisation and financing of healthcare services during the pandemic and the war;
- **Some low-income households may have been negatively affected by changes in social assistance targeting.** In relation to energy cost assistance to vulnerable households, Ukrainian authorities' targeting efforts may have been effective in reducing the number of beneficiaries, but it is less clear whether, in doing so, the distribution of the subsidies favoured vulnerable households more than before. Some evidence suggests that the reduction in the number of beneficiaries was broad based, meaning that poor households may also have been cut off from the subsidies;
- **No clear impacts on the situation of internally displaced persons.** Ukrainian authorities implemented an action plan to improve the integration of internally displaced persons. While various measures facilitating social benefits payments or providing affordable housing were enacted or prepared, the social impacts remained limited, with no noticeable change in the number of beneficiaries or average monthly payments;
- **Some potential for negative impacts on the social situation associated with no first tranche MFA (Alternative A).** In the absence of the first MFA tranche of EUR 500 million, Ukrainian authorities would probably have resorted to alternative, and more expensive, funding options which would likely have incurred some negative social implications. Some fiscal adjustment, especially in the form of VAT increases, may also have been considered in the absence of this MFA tranche, which would have eroded household real incomes. However, the feasibility of this tax option would have likely been limited due to political cycle considerations;
- **Clearer deterioration in the social situation due to cuts to social spending associated with no second tranche MFA (Alternative B).** In the absence of the second MFA tranche in 2020, Ukraine's options for filling the funding gap would have been more constrained, given the challenging economic backdrop at the time. The country would likely have had to resort to extensive spending cuts in addition to those already implemented in education and social spending. The government's response to the COVID-19 pandemic would also have been more limited. Funds available to social programmes, such as those linked to reforms conditional on MFA IV, might have been reduced, with clear and negative direct socioeconomic consequences. However, results from the expert assessments were inconclusive on the dependence of these reforms on the disbursement of the MFA specifically. Lower overall public

spending may also have led to lower economic activity, indirectly affecting social outcomes through lower employment;

- Severe deterioration of socioeconomic conditions in the absence of MFA and IMF support (Alternative D).** The impact on socioeconomic conditions in Ukraine in the absence of any support from IMF and MFA operations would likely have been severe. While default would have been unlikely, the finance gap would have been large enough to require considerable cuts to governments spending, including in social areas, as well as debt restructuring. The social situation in Ukraine would have been negatively impacted directly via this reduced government assistance and indirectly through substantially impaired economic growth. It is reasonable to think that this alternative would likely have resulted in lower employment and real disposable incomes of households, as well as rising poverty and inequality.

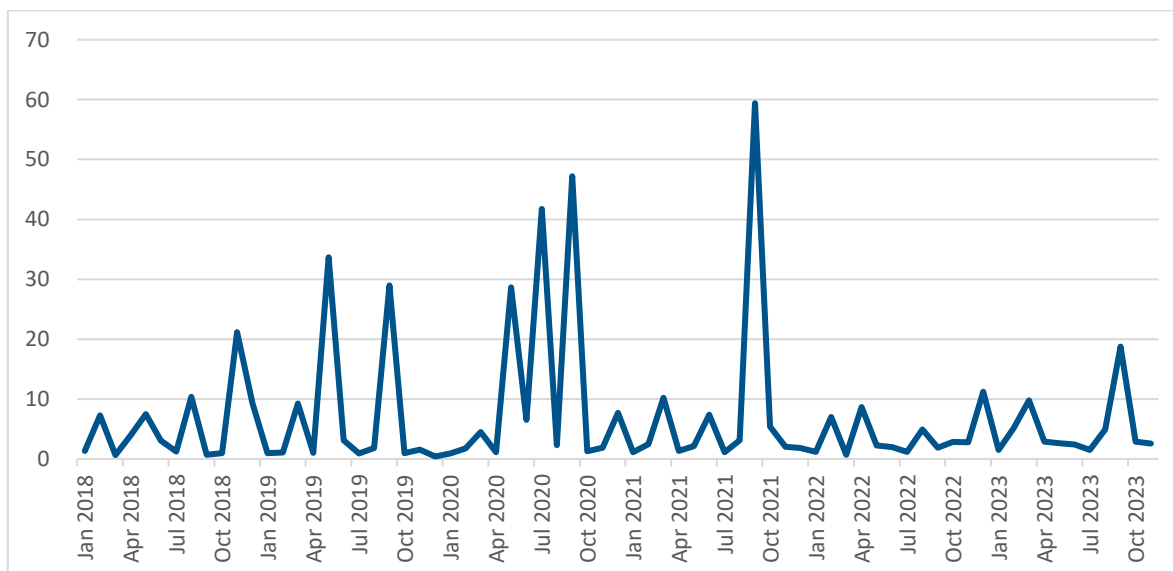
Evaluation criterion: Efficiency

Timing of the disbursement of financial assistance

Question: Was the disbursement of the financial assistance appropriate in the context of the prevailing economic and financial conditions in Ukraine?

Examining the macroeconomic context and trends in Ukraine during the disbursement period of MFA IV, the assistance clearly played a pivotal role in the nation's economic stability. Against a backdrop of geopolitical tension and economic challenges, MFA IV came at a time when Ukraine was just beginning to emerge from a significant recession, with an economy deeply affected by conflict and political turbulence. Notwithstanding some monthly fluctuations and occasional spikes in Ukraine's debt repayments obligations, the overall trend shows a commitment to meeting debt obligations (see Table 5.4).

Table 5.4 Total external debt repayment obligations, state budget, by month, UAH billion



Source: Ukrainian Ministry of Finance data.

The first tranche of MFA in 2018 was timely, with stakeholders noting that it provided much-needed stability and reinforcing confidence amid delays in IMF support. It was crucial, given the vulnerabilities that persisted despite a recovering economy. The pattern of external debt repayment obligations (see Table 5.4) did not display any significant peaks, indicating that the MFA did not coincide with any immediate large-scale repayment pressures, allowing the

assistance to contribute more broadly to economic stabilisation and reform efforts rather than merely serving immediate debt obligations.

By 2020, the COVID-19 pandemic had placed severe strain on the Ukrainian economy, exacerbating the need for external financial support. The second tranche of MFA, disbursed in November 2020, was critical, supplementing other donor efforts and directly supporting the government's fiscal capacity to manage the crisis's impact. It facilitated essential reforms and bolstered investor confidence during a period marked by increased borrowing costs and the potential for austerity measures that could have hindered the economic response to the pandemic.

Design of MFA assistance and efficiency of implementation

Question: To what extent did the MFA operation design enable the intervention to be carried out efficiently? In what way has the design of the MFA assistance conditioned the performance of the operation in respect to its cost and its objectives?

In addition to the disbursement schedule, a number of other specific issues are worth considering.

Ownership of the programme by the Ukrainian authorities

All EU and international stakeholders pointed to **uneven reform ownership** by Ukrainian authorities, often citing a 'two steps forward, one step back' approach. Both President Poroshenko and President Zelenskyy (pre-2022) showed strong commitment to reform in the early years of their presidencies, with set-ups and gradual decline/push-back later on. As such, stakeholders emphasised the need for continuous follow-up and engagement of international donors, local civil society and other experts to ensure that reform momentum was maintained.

The **reform commitment differed between ministries and institutions**, and **shifted with changes in key personnel**. For example, the appointment of reform-oriented heads of the state tax and customs services in 2019 (Verlanov and Nefyodov) was seen as positive signals for the reforms of the two institutions, but both were dismissed after a short six-month tenure, bringing uncertainty about the progress of their reform efforts and overall reform commitment of the new government under Zelenskyy¹⁷⁹.

A number of external commentators pointed to **better reform ownership within newly created institutions** (e.g. anti-corruption bodies such as NABU, HACC) versus older institutional structures (law enforcement bodies, judiciary), as they often benefit from a transparent recruitment facilitated by external partners and local experts. Even here, however, the performance of new institutions is not always guaranteed and their success depends on their set-up and the selection processes behind key managerial staff. This issue was exemplified by the need to reboot the NAPC (in 2019) and the ongoing discussions around the early need to reboot the recently created Bureau of Economic Security (in 2021) to ensure transparent selection of its new leadership¹⁸⁰ (part of IMF's structural benchmarks in 2023¹⁸¹). In the meantime, the strong involvement of international experts in the set-up and

¹⁷⁹ Dickinson, P., 'Zelenskyy changes course with government reshuffle', *Atlantic Council*, 5 March 2020, <https://www.atlanticcouncil.org/blogs/ukrainealert/zelenskyy-changes-course-with-government-reshuffle/>

¹⁸⁰ The creation of a new Bureau of Economic Security in 2021 was anticipated to be a 'ground-breaking' new institution, yet it was initially led by a former head of the SFS (who was seen as part of the older, unreformed generation), <https://www.atlanticcouncil.org/blogs/ukrainealert/old-problems-threaten-ukraines-new-bureau-of-economic-security/>

¹⁸¹ Interfax Ukraine, 'Updated memorandum with IMF contains 12 new structural benchmarks – MP', *Ukraine News Agency*, 12 December 2023, <https://en.interfax.com.ua/news/economic/953604.html>

appointments of judges to the HAAC were seen to have contributed to the Court's independence and effectiveness.

The **fragility of existing reforms** is evident in the asset verification system, which was a key condition under MFA III and MFA IV. While seen as an important reform helping to enhance transparency and accountability within Ukraine's civil service, it nevertheless faced a number of legislative efforts to undermine its functioning. With the fulfilment of MFA IV-linked conditions, Ukraine implemented a verification system for electronic asset declaration to facilitate the effective verifications of submitted declarations, thereby achieving the condition of verifying 1,000 declarations. However, in October 2020, the Constitutional Court (CC) adopted a decision that invalidated the criminal responsibility for failure to submit an asset declaration or for filling inaccurate asset declarations, calling into question the effectiveness of the overall system. Following pressure from local civil society and the international community, President Zelenskyy subsequently submitted legislative amendments (adopted in June 2021) to address the impact of the CC's decision. Following Russia's war of aggression against Ukraine in February 2022, the asset declaration system was fully suspended. In 2023, the parliament aimed to reinstate the declarations, but keep the disclosures closed to the public for an additional year. This legislative proposal was eventually vetoed by the President in September 2023. Although the system has now been restored, the Commission noted in its 2023 report that there may be potential weaknesses in the current verification powers of the NAPC and the data to be verified. Thus, reforms that are considered to have been successfully implemented may still be undermined at a later stage.

The various vested interests operating within a number of institutions and the parliament cannot be underestimated, often posing additional roadblocks to government-initiated reforms. Commentators pointed to the infighting between the 'old guard' in certain institutions and new reformist heads/leadership trying to implement structural reforms, which can slow reform or create set-backs, even where there is reform ownership.

It is not possible to draw a simple conclusion on the reform ownership of the Ukrainian authorities. Interviews with EU and international stakeholders suggested that the ownership is there, but it shifts with changes in the political environment. Even where there is a will to reform, this can be undermined by the efforts of different interest groups, making reform and the institutional environment complex and difficult to unpack. Nevertheless, since 2014 Ukraine has made progress in implementing extremely complex reforms, including creating a vast array of new institutions and bodies. While that progress may not have been uniform, it was acknowledged by EU and international stakeholders.

Capacity for reform

Ukraine has consistently been ranked relatively low on the WB's Governance Effectiveness Indicator (quality of public service provision, quality of bureaucracy, competence of civil servants, independence of civil service from political pressures, credibility of government's commitment to policies)¹⁸². Reform ownership and capacity for reform were not uniform across all institutions and were not helped by the constant changes in leadership.

None of the interviewees pointed to delays in specific reform efforts that would stem from low capacity. At the same time, Ukraine's lack of sufficient capacity across all institutions was noted, together with its inability to attract talent, which has only worsened since Russia's war of aggression. The importance of ensuring that reforms are supported by technical assistance projects was emphasised by a large number of EU and international

¹⁸² WB, Worldwide Governance Indicators, <https://www.worldbank.org/en/publication/worldwide-governance-indicators>

stakeholders, underlining the need for additional support on internal capacity-building in Ukraine's institutions.

Liaison with Ukrainian authorities

Both EU-level and Ukrainian stakeholders rated the communication between the Ukrainian and EU authorities very positively. The general perception was that there was a good working relationship and understanding in place as a result of the previous three MFA operations. As such, the key stakeholders understood the processes, with no surprises or issues highlighted by either side.

As in previous MFA operations, the dialogue was led by DG ECFIN, supported by the EU Delegation in Kyiv. The Delegation was large, with sufficient capacities to provide the necessary support.

The capacity of the Ukrainian Ministry of Finance to coordinate the process was also rated positively. Some challenges were reported in ensuring buy-in from other Ukrainian institutions for the implementation of reforms under the responsibility of other ministries that were less engaged in the MFA process.

As a number of conditions flowed directly from MFA III, there were no surprises or disagreements over the conditions set. Rather, there was an appreciation that important lessons from MFA III were incorporated, including reducing the overall number of conditions and ensuring clearer scope.

Adjustments to implementation in light of unforeseen external events

There were no specific waivers required under MFA IV. This can be partly attributed to the impact of the decision not to disburse the last tranche of MFA III and the political statement attached to the MFA IV operation emphasising the need to ensure implementation of all conditions. It can also be attributed to the fact that the conditions were designed to be achievable and realistic within the given timeframe in order to avoid a repeat of the situation at the end of MFA III.

The only condition with a slight deviation in implementation was on the adoption of the anti-money laundering law (condition #6, second instalment). The draft law was adopted, with the final adopted version found to largely comply with the EU's fourth AMLD. There were some discrepancies related to the size of fines for financial institutions, in particular banks. Nevertheless, as the newly adopted maximum fines were 5,000 times higher than the fines under the previous Ukrainian AML legislation, the Commission considered the law a significant step forward in terms of the dissuasive effect of financial sanctions. The Commission stressed that the difference in fines should not be perceived as a critical issue, particularly given that all other provisions of the Directive were properly implemented and that the final version adopted was the maximum possible compromise that could be achieved. Finally, the threshold of fines in the AMLD does not correspond to the economic and political realities of Ukraine. Citing Article 249 of the Treaty on the Functioning of the European Union (TFEU), the Commission noted that directives establish a general framework and leave each country room for its own implementing policy actions.

Visibility of MFA IV

The evaluations of previous MFA operations to Ukraine (I-III) highlighted their lack of visibility, which was also true of MFA IV. The IMF's financial support continues to be much more visible and talked about in Ukraine.

None of the reforms supported by MFA IV conditions experienced public resistance (as was the case under MFA III conditions on the ban on exports of wood, which was highly politicised and criticised). Civil society and local experts generally agreed with the reform priorities supported by MFA IV.

Civil society organisations previously referred to MFA/IMF conditions in their advocacy work¹⁸³, in particular in the fight against corruption. In 2017, a leading anti-corruption non-governmental organisation (NGO) in Ukraine (ANTAC) created a website detailing the conditions set by the EU and IMF in the area of anti-corruption and Ukraine's progress on its implementation. It can be filtered by the source (IMF/MFA/SBC/VLAP) and status of implementation (implemented/serious risk/not implemented/roll-back). It also includes the conditionality of MFA IV and notes some of the progress made. The website does not seem to have been updated for some time (with the last weekly anti-corruption updates published in the summer of 2021).

While there may be some knowledge/understanding of EU's MFA among the expert community, this does not appear to extend to the general public. Experts consulted for this study often did not have a detailed awareness of the MFA operation or its overarching conditionality, but, rather, a more general awareness or knowledge of specific conditions relevant to their work. Previous evaluations of MFA I and II, which included media content analysis, showed the limited coverage and visibility of those operations in the country. This could be due to the overall amounts of MFA support pre-2020 (especially compared to the IMF).

According to annual Open Neighbourhood surveys, in 2018, around 60% of citizens were aware of the financial support provided by the EU to Ukraine (with the most well-known EU-financed programmes relating to education), a 7% increase compared to 2017¹⁸⁴. In 2020, that figure rose to 62%¹⁸⁵. Some EU staff noted that the support provided by the EU to Ukraine was already significant pre-2020, considerably higher than many other EaP countries, even before Russia's war of aggression against Ukraine in 2022. The lack of overall awareness could reflect a need to improve the efficiency of the EU's communication campaigns.

The number of people aware of the EU's financial support to Ukraine had risen significantly by 2023, given the EU's support to Ukraine following Russia's war of aggression since February 2022. This included an overall increase in reported levels of trust in the EU and positive attitudes toward the EU¹⁸⁶. National stakeholders and experts interviewed tended to have higher levels of awareness of recent EU support to Ukraine, including a more detailed overview of the discussions around the Ukraine Facility¹⁸⁷ (planned support, EU 50 billion). This change reflects the overall higher amounts provided by the EU to Ukraine since 2022, as well as the close and growing relationship between Ukraine and the EU (including the opening of accession negotiations).

¹⁸³ ANTAC, Anti-corruption website, <https://antac.org.ua/en/news/anticorruption-conditionalities-as-miracle-makers-for-ukrainian-reformers/>

¹⁸⁴ EU Neighbours East, *Opinion Survey 2018: Ukraine*, 2018, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2018-ukraine/>

¹⁸⁵ EU Neighbours East, *Opinion Survey 2020: Ukraine*, 2020, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2020-ukraine/>

¹⁸⁶ EU Neighbours East, *Opinion Survey 2023: Ukraine*, 2023, <https://euneighbourseast.eu/news/publications/annual-survey-2023-ukraine/>

¹⁸⁷ European Commission, Ukraine Facility, https://ec.europa.eu/commission/presscorner/detail/el/ganda_23_3353

Evaluation criterion: Coherence

Question: *To what extent was the MFA IV operation in line with key principles, objectives and measures taken in other EU external action towards Ukraine in the context of the European Neighbourhood Policy?*

Policy framework and principles

Ukraine is a priority partner for the EU, with EU–Ukraine cooperation underpinned by the ENP¹⁸⁸. The ENP promotes the deepening of political and economic relations between the EU, its Member States and partner countries, including via bilateral and multilateral tracks, such as the EaP¹⁸⁹.

The previous legal basis for EU-Ukraine relations was the EU-Ukraine PCA signed in 1994, which focused on economic and social ties.

The negotiation of an AA, including a DCFTA, took place in 2007-2011. In December 2012, the Council of the EU adopted its Conclusions on Ukraine, affirming its commitment to signing the Agreement subject to Ukraine showing progress in three specific areas¹⁹⁰. While the negotiations were complete, preparations for AA signature were then suspended by the administration of President Yanukovich in 2013.

Following the Revolution of Dignity in 2013-2014, the EU and Ukraine signed the political provisions of the AA in March 2014. The remaining provisions were signed in June 2014. This led to the provisional application of parts of the agreement from September 2014. The provisional application of the DCFTA started in January 2016.

On 11 July 2017, the Council adopted a decision to conclude the AA with Ukraine, which was the final step of the ratification process, with the AA fully implemented as of 1 September 2017¹⁹¹. The AA constitutes the legal framework informing EU-Ukraine relations, promoting deeper political ties, stronger economic links, and respect for common values. Importantly, it contains comprehensive commitments by Ukraine to gradually align its legislative framework with the EU *acquis*. The DCFTA offers a framework for modernising Ukraine's economy and trade relations¹⁹².

Visa-free travel for Ukrainian citizens with biometric passports entered into force in 2017, enabling Ukrainian citizens with a biometric passport to enter the Schengen Area for a period of stay of 90 days in any 180-day period¹⁹³.

On 28 February 2022, Ukraine submitted its application for EU membership. On 17 June 2022, the European Commission delivered its opinion, which was subsequently endorsed on

¹⁸⁸ EEAS, European Neighbourhood Policy, 2021, https://www.eeas.europa.eu/eeas/european-neighbourhood-policy_en

¹⁸⁹ Ibid.

¹⁹⁰ Council of the EU, Council conclusions on Ukraine, 3209th Foreign Affairs Council Meeting, 2012, https://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/foraff/134136.pdf

¹⁹¹ Association Agreement between the European Union and its Member States, of the one part, and Ukraine, of the other part, [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22014A0529\(01\)](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22014A0529(01))

¹⁹² Council of the EU, EU relations with Ukraine, 2023, <https://www.consilium.europa.eu/en/policies/eastern-partnership/ukraine/>

¹⁹³ European Commission, Visa liberalisation with Moldova, Ukraine and Georgia, Directorate-General for Migration and Home Affairs, n.d., https://ec.europa.eu/home-affairs/what-we-do/policies/international-affairs/eastern-partnership/visa-liberalisation-moldova-ukraine-and-georgia_en

23 June 2022 by the European Council, granting candidate status to Ukraine¹⁹⁴. In November 2023, the Commission recommended opening formal accession negotiations with Ukraine¹⁹⁵.

Ukraine
<p>14 June 1994 – EU-Ukraine PAC signed</p> <p>1 March 1998 – EU-Ukraine PAC entered into force</p> <p>29 September 2004 – ENP instrument launched by Commission</p> <p>7 May 2009 – Joint Declaration of the Prague Eastern Partnership Summit</p> <p>30 March 2012 – EU-Ukraine AA initialled in Brussels</p> <p>21 March 2014 – Political part of the AA signed by Ukraine Prime Minister Yatseniuk</p> <p>27 June 2014 – Economic part of the AA signed by Ukraine President Poroshenko</p> <p>1 January 2016 – Provisional entry into force of the DCFTA</p> <p>11 June 2017 – Visa-free access to Schengen Area for Ukrainians</p> <p>1 September 2017 – AA fully implemented</p> <p>28 February 2022 – Ukraine applies for membership of the EU</p> <p>23 June 2022 – Ukraine is granted candidate status</p> <p>8 November 2023 – European Commission recommends opening formal accession negotiations with Ukraine</p> <p>14-15 December 2023 – European Council adopts conclusions on Ukraine, opening accession negotiations with Ukraine and inviting the Council to adopt the negotiation framework once the relevant steps set out in the Commission’s 8 November 2023 report are taken</p>

The EU’s MFA to Ukraine continues to be informed by the wider policy context of its relationship with the country, and is in line with the ENP, EaP and AA. Overall, the MFA aims to address both the economic weaknesses in Ukraine and the reform commitments undertaken in the AA.

The close involvement of technical experts in the design of the conditions (including from DG NEAR - SGUA and EUACI based in Kyiv) helped to ensure the coherence of the conditions with the overall policy context, including the ENP, the AA and the overarching reforms supported by the EU in Ukraine.

Comparing the AA implementation reports for 2017¹⁹⁶ (prior to MFA IV) and 2022 (post-MFA IV), both highlight many of the same themes that featured prominently in the MFA IV conditions, including:

- Fight against corruption
- Corporate governance of SOEs
- Financial sector

¹⁹⁴ Council of the EU, European Council conclusions on Ukraine, the membership applications of Ukraine, the Republic of Moldova and Georgia, Western Balkans and external relations, 23 June 2022, <https://www.consilium.europa.eu/en/press/press-releases/2022/06/24/european-council-conclusions-23-24-june-2022/>

¹⁹⁵ Council of the EU, Ukraine, n.d., <https://www.consilium.europa.eu/en/policies/enlargement/ukraine/>

¹⁹⁶ European Commission, *Association Implementation Report on Ukraine*, SWD(2017) 376 final, https://www.eeas.europa.eu/sites/default/files/association_implementation_report_on_ukraine.pdf

- Tax reform
- Customs reform
- Privatisation of small assets
- Public health system
- Internally displaced persons (more prominent in 2017-2018 than 2022)

This illustrates the alignment of the MFA with the policy context and underscores the importance of achieving further reforms in these areas. While progress has been achieved, further progress is clearly required, with these reform areas remaining high on the Association Agenda.

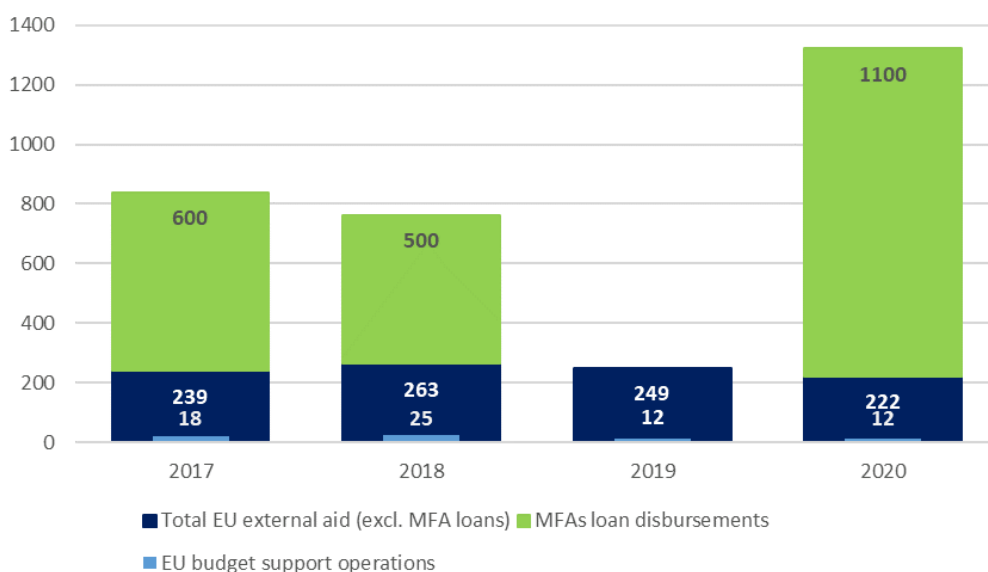
EU assistance to Ukraine

Overview of assistance provided via budget support programmes (grants) and MFA assistance (loans)

Figure 5.1 shows MFA loan disbursements compared to total EU external aid and EU budget support assistance exclusively received by Ukraine over the 2017-2020 period.

Throughout the implementation period, budget support operations were at a rather low level, at EUR 67 million over four years, 7% of total external assistance. In contrast, MFA loan disbursements amounted to EUR 2.2 billion, including the second tranche of MFA III in 2017 and the first MFA COVID-19 tranche at end-2020. This highlights the importance of the MFA instrument in the EU support package to Ukraine.

Figure 5.1 EU external aid to Ukraine, by type, and MFA, 2017-2020, EUR million



Source: Annual reports on the implementation of the EU's instruments for financing external actions; Annual reports on the implementation of macro-financial assistance to third countries (2017-2020), Budget support: Trends and results reports.

- Note: Data refer only to external aid financed through the EU budget and do not include bilateral aid from Member States or financing from the EIB.

Coherence with other EU programmes and initiatives

MFA IV versus previous MFA III operation

Table 5.5 highlights the links between MFA IV and MFA III. MFA IV represented a notable shift from MFA III in terms of number of conditions, but the focus on key reform areas was maintained throughout both operations.

One of the key links between the two MFAs was the continued emphasis on addressing corruption and promoting good governance. MFA IV pushed for unmet MFA III conditions (implementation of an automated verification system for electronic asset declarations; verification of beneficial ownership information). It also retained the focus on building the institutional framework. However, the focus under MFA IV shifted to full operationalisation of the HAAC, where MFA had targeted the NABU, NAPC and SAPO.

In the energy sector, the focus was on implementing the Electricity Market Law, which was amended as part of MFA III. Finally, there was a focus on implementing the strategy of integration of internally displaced persons.

Given the more targeted approach under MFA IV, certain fields were no longer addressed (e.g. internal/external audit, public administration, fiscal governance/policy, trade).

Table 5.5 Mapping of conditions – MFA III vs MFA IV

	MFA III	MFA IV
Areas with complementarities		
Good governance and fight against corruption	Set up NABU, SAPO, NAPC Specific conditions on asset disclosure/asset recovery	Allocation of a financial envelope in the 2019 budget for the HAAC and full operationalisation Set up and operation of an automated verification system for electronic asset declarations Ensure effective verification of information on companies' beneficial ownership
Sector reforms and SOEs	Amend Electricity Market Law	Significant progress in implementing Electricity Market Law
Social policies	Effective provision of social benefits and services to internally displaced persons Evaluation of social services for internally displaced persons	Improved targeting, efficiency, and fairness of social benefits Adoption of Action Plan on the implementation of the strategy of integration of internally displaced persons
Areas with no complementarities		
Internal/external audit	x	
Public administration	x	
Fiscal governance/policy	x	
Trade	x	
Financial sector and NBU		x

MFA IV operations in the context of the overall EU budget support package

Reform measures in Ukraine were promoted via ongoing EU budget support programmes, including in the fields of energy, administration, and governance.

Table 5.6 EU budget support programmes to Ukraine

Year	Contracts signed	Thematic focus
2017	3	Agriculture, rural development and food security; energy; governance
2018	2	Administration and energy
2019	2	Administration and energy
2020	1	Administration and energy

Source: Budget support: Trends and results, 2017 to 2020.

Technical assistance

The role of technical assistance projects was highlighted as crucial in supporting implementation of the reforms promoted via MFA IV. While MFA conditionality set a general direction of reform (e.g. adoption of a reform plan, ratification of specific legislation), the reform was less likely to be initiated if there was no follow-up, nor would its achievements be sustained in the medium and long-term. Technical assistance projects thus helped to maintain momentum by ensuring sufficient technical know-how was provided to the local authorities implementing complex reforms.

In the context of MFA IV conditionality, the most important EU projects were the **EUACI**, which already existed prior to MFA IV, and **EU4PFM**, which was set-up in 2018.

EUACI¹⁹⁷ has long been a flagship project supporting anti-corruption reforms in Ukraine, working closely with the newly created anti-corruption institutions. It also played an important role in defining the technical conditionality related to the asset verification system (condition #2, first tranche) and then in supporting Ukrainian authorities to implement the technical modules.

EU4PFM¹⁹⁸ has supported reforms in the areas of customs and tax¹⁹⁹, including wider reforms within the SFS (business processes, human resources, etc.) (condition #1, second tranche). Other EU4PFM that complemented MFA IV were support with the implementation of AEO or NCTS for customs (condition #2, second tranche) and support with implementation of the BEPS Action Plan together with the OECD (condition #3, second

¹⁹⁷ EUACI, Components, n.d., <https://euaci.eu/what-we-do/components/>

¹⁹⁸ EU4PFM, Components and objectives, n.d., <https://eu4pfm.com.ua/components-and-objectives/revenue-mobilization-horizontal-functions-and-governance/?mi=5590>

¹⁹⁹ Among its priorities, it aimed to strengthen capacities of both tax and customs by reviewing and helping to adapt business processes; helping to introduce and implement a new tax compliance strategy and developing a compliance measurement framework; strengthening capacities in broadening Ukraine's tax base; strengthening capacities in the legal approximation of customs law and regulations with the EU *acquis* and international best practice and its implementation; strengthening capacities of tax and customs administrations to counter tax avoidance and implement trade facilitation measures.

tranche). The experts seconded to the Ministry of Finance's Reform Support Team were another key support to tax and customs reform (support team financed by the EBRD)²⁰⁰.

Other donors' technical assistance programmes included technical assistance provided by both the OECD and IMF in the area of tax. OECD assistance focused on supporting the Ukrainian authorities to align their tax legislation with OECD standards, as well as the area of BEPS (linked to condition #3, second tranche). The IMF supported the overarching reforms of the SFS (linked to condition #1, second tranche).

IMF and WB programmes

During the MFA implementation period, Ukraine received IMF support, first in the form of a four-year (2015-2019) EFF (SDR 12.348 billion, about USD 17.5 billion, 900% of quota)²⁰¹. That programme aimed to address Ukraine's economic challenges, including high inflation, fiscal imbalances, and geopolitical tensions. Delays in reform progress meant that only three reviews were completed under the EFF instead of the 15 originally planned. The EFF was cancelled in 2018 and replaced with a 14-month SBA in December 2018 (SDR 2.8 billion, about USD 3.9 billion, 139% of quota)²⁰². In June 2020, the IMF approved another 18-month SBA (SDR 3.6 billion, about USD 5 billion or 179% of quota) to help Ukraine to cope with COVID-19²⁰³, after which Ukraine transitioned to an EFF arrangement to continue its reform efforts and economic stabilisation.

IMF and MFA IV conditions had a strong focus on anti-corruption institutions (particularly the selection of judges to the newly created HAAC), reform of the SFS, and improving corporate governance of state-owned banks. These commonalities indicated a coordinated approach to tackling corruption issues, enhancing transparency of existing institutions and improving revenue mobilisation, highlighting the alignment between MFA IV and IMF SBA/EFF conditions.

The WB also supported Ukraine's economic and institutional reforms between 2014 and 2020 through various DPLs and investment projects. The DPLs and FSDPLs provided financial resources and technical assistance to help Ukraine to improve governance, transparency, accountability, stability, and efficiency in the public sector and the financial sector. The investment projects aimed to improve the quality and relevance of healthcare, education, power transmission, and renewable energy services in selected regions of Ukraine. The WB's commitment to supporting Ukraine's reform agenda amounted to approximately USD 5.5 billion over the period²⁰⁴.

Across both IMF and WB conditions, the links with MFA IV are most apparent around good governance and fight against corruption (see Table 5.7). A more detailed coherence assessment is presented in Annex 12.

²⁰⁰ Foundation for Support of Reforms in Ukraine, Reform Support Teams, n.d., <https://fsr.org.ua/en/page/reform-support-teams>; Ministry of Finance of Ukraine, Reform Support Team Project Management Office, n.d., <https://mof.gov.ua/en/ofis-pidtrymky-reform>

²⁰¹ IMF, 'IMF Executive Board approves four-year US\$17.5 billion Extended Fund Facility for Ukraine, US\$5 billion for immediate disbursement,' Press release No. 15/107, 11 March 2015.

²⁰² IMF, 'Request for SBA and cancellation of arrangement under the EFF,' Press release No. 18/843, 2018.

²⁰³ IMF, 'IMF Executive Board approves 18-month US\$ 18 billion Stand-By Arrangement for Ukraine,' Press release No. 20/239, 9 June 2020.

²⁰⁴ WB, Projects, n.d., https://projects.worldbank.org/en/projects-operations/projects-list?lang=en&countrycode_exact=UA&os=20

Table 5.7 Detailed cross-conditionality with the IMF/WB

Area	Condition	Donors involved
First disbursement		
PFM	#1 Issue of at least seven general tax consultations on the practical application of tax legislation	EU only - IMF and WB focused on VAT related issues
Good governance and fight against corruption	#2 Set up and operation of an automated verification system for electronic asset declarations	EU, WB (WB programmes focused on adaptation of law setting up external verification of financial disclosures of public officials)
	#3 Ensure effective verification of information on companies' beneficial ownership	EU, WB
	#4 Allocation of financial envelope in the 2019 budget for the HAAC and its full operationalisation	EU only - IMF (IMF focused on NABU)
Sector reforms and SOEs	#5 Improvement of corporate governance in SOEs	EU, IMF
	#6 Following the government's privatisation plan, put at least 200 small state-owned assets for sale via electronic auction	EU, IMF
Second disbursement		
PFM	#1 Improvement of corporate governance in SOEs	EU, IMF (IMF focus on privatisation /restructuring)
	#2 Better balance between customs control and trade facilitation	EU, IMF
	#3 Fighting tax evasion	EU only
Good governance and fight against corruption	#4 Progress on automated verification system for electronic asset declarations	EU, WB (WB focused on adaptation of law setting up external verification of financial disclosures of public officials)
	#5 Progress on HAAC	EU, IMF (selection of anti-corruption judges)
	#6 Adoption of an anti-money laundering law	EU, IMF
Sector reforms and SOEs	#7 Reduction of high level of NPLs, including in state-owned banks	EU only
	#8 Improvement of governance in state-owned banks	EU, IMF

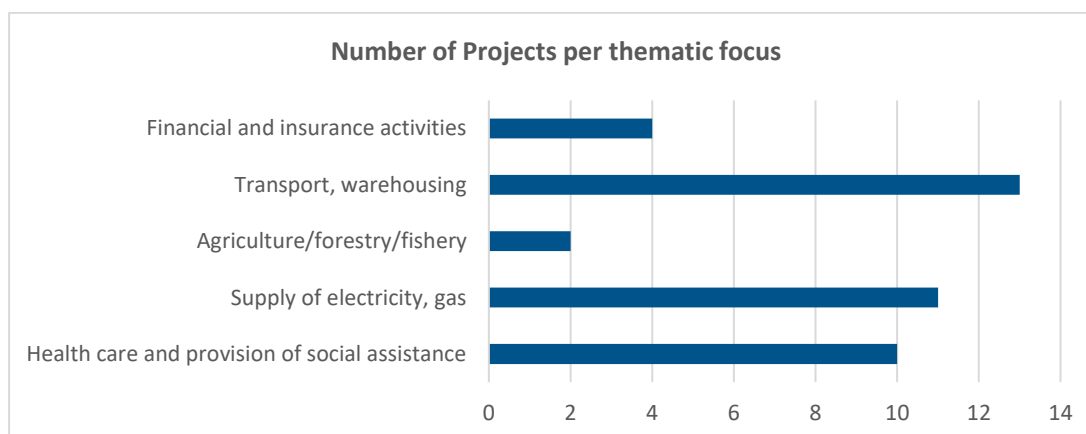
Area	Condition	Donors involved
	#9 Significant progress in implementing Electricity Market Law	EU, WB (WB involved in energy sector regulation)
Social policies	#10 Implementation of the reform of healthcare financing	EU only
	#11 Improvement of targeting, efficiency and fairness of social benefits	IMF and WB involved in other social reforms
	#12 Adoption of the Action Plan on the implementation of the strategy of integration of internally displaced persons	EU only

Source: ICF review of documentation.

Other IFI assistance

EU funding represented about 24% of the total amount of IFI assistance to Ukraine between 2017 and 2020 (See Figure 5.2). In terms of synergies with relevant budget support programmes, during the period the EIB invested significantly in the construction sector, allocating EUR 640 million to two projects. The IBRD also funded a single project within this sphere, contributing to the sector’s overall growth. In water supply, sewage, and waste management, KfW committed EUR 21.55 million to one project. The EIB and IBRB funded three educational projects, totalling EUR 58 million. The IBRD was also involved in 10 healthcare and social assistance projects, with an allocation of EUR 250 million. In the electricity and gas supply sector, EUR 967 million was invested across 11 projects.

Figure 5.2 IFI projects, by thematic area, 2017-2020



Source: ICF review of documentation.

Across thematic areas, the transport and warehousing sector had the highest number of IFI projects, followed by the supply of electricity and gas. This suggests a significant focus on Ukraine’s infrastructure and energy sectors. Healthcare and provision of social assistance also had a notable number of projects. Agriculture/forestry/fishery and financial and insurance activities had fewer projects, suggesting that these areas might be more specialised or may have received lump-sum investments in fewer, larger-scale projects.

5.3 How did the EU intervention make a difference and to whom? [Related criterion to assess: EU added value]

Financial added value

MFA IV served as a progression from MFA III. The macroeconomic analysis underscored that Ukraine's economy had achieved stability following the previous MFA. Although the collective assistance from MFA IV and the IMF SBA appeared larger than past interventions (filling a gap of EUR 4 billion over 2018-2020), the MFA IV package was relatively modest in relation to Ukraine's economy (combined with the IMF intervention, totalling EUR 1.7 billion in 2018, about 1.53% of 2018 GDP; EUR 2.3 billion in 2020, roughly 1.84% of 2020 GDP). In this scenario, the primary financial benefit of MFA IV to Ukraine was not related to the operation's size.

During the MFA IV period (2017-2020), other donors were also contributing to Ukraine. financing needs EU institutions were among the leading providers of financial assistance to Ukraine during that time. Donors offered aid in the form of budget and project support. The MFA package, coupled with the IMF programme extension, provided an 'EU stamp' that stimulated investor confidence and donor involvement. This was particularly beneficial in the context of COVID-19, helping to secure additional support in 2020. Apart from the 'EU stamp', the financial benefit also stemmed from the MFA assistance's terms and conditions. For MFA IV, the operation primarily consisted of a loan component, with exceptional terms compared to the assistance provided as budget support. The loan component's terms and conditions generally aligned with other support at the time.

Non-financial added value

Signalling effect to civil society and the general population

As also noted in the evaluations of previous MFA operations in Ukraine, the AA, established between the EU and Ukraine, created an expectation within Ukrainian civil society and the general population that the EU would offer support during times of crisis. However, in view of the decision not to disburse the last tranche of MFA III, there were some concerns regarding the EU's commitments. The initiation of the MFA IV programme was interpreted as a reaffirmation of the EU's commitment to Ukraine. This reinforcement signalled to Ukrainian civil society and the general population that the EU remained dedicated to supporting Ukraine despite the challenges faced during the MFA III disbursement.

Opinion polls from 2020 showed that, at the time, the EU was the most trusted international institution (66% of Ukrainians expressed trust towards the EU). In addition, 64% of Ukrainians believed that relations with the EU were good, and 51% had a positive image of the EU²⁰⁵. However, that image of the EU was fluctuating, with only 56% of people reporting having had a positive image of the EU in the preceding year²⁰⁶. Overall Ukrainians' perceptions of the EU could not solely be attributed to the MFA but may have played a role in how the EU was perceived overall.

While the visibility of the MFA operation remained low overall, civil society used the conditions to support the fight against corruption in their own advocacy work. Both the EU

²⁰⁵ EU Neighbours East, *Opinion Survey 2020: Ukraine*, 2020, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2020-ukraine/>

²⁰⁶ EU Neighbours East, *Opinion Survey 2019: Ukraine*, 2019, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2019-ukraine/>

and IMF played an important role in supporting local-level efforts to advance specific reform agendas (albeit not in all sectors equally).

Confidence-boosting effects

Since 2014, Ukraine has been the recipient of an unparalleled level of MFA support, marking it the highest recipient of EU MFA ever granted to a non-EU country within such a condensed timeframe. In line with its predecessors (MFA I, II, III), the impact of MFA IV on private sector confidence was not distinctly discernible. Despite the inability to quantify the extent of the confidence boost effect triggered by MFA IV, a political signalling effect was evident in the political pre-conditions attached to each financial disbursement. This effect, in conjunction with the IMF package, served as a form of endorsement. Consultations with stakeholders did not provide specific evidence documenting the tangible impact of MFA IV on the business environment and investor confidence, but most interviewees underscored the significance of the 'EU stamp' in enhancing confidence and facilitating reform implementation.

An examination of the foreign exchange rate trends from 2017 to 2020 does not permit the attribution of specific movements to the two MFA IV disbursements. The exchange rate between the euro (EUR) and Ukrainian hryvnia (UAH) from 2017 to 2020 showed an overall depreciation of the UAH against the EUR. In 2017, the UAH began to weaken, aligning with an average exchange rate of approximately 30 UAH for 1 EUR²⁰⁷. This depreciation trend persisted through 2018 and 2019, potentially indicative of inflationary pressures in Ukraine, economic uncertainties, or a comparatively stronger economic performance in the Eurozone. By 2020, an increase in volatility was observed, potentially attributable to the global economic repercussions of the COVID-19 pandemic. This suggests that MFA IV, in tandem with the IMF programme, did not contribute significantly to the appreciation of the Ukrainian hryvnia.

Credit ratings issued by leading credit rating agencies (Moody's, S&P, Fitch) are closely monitored by the private sector and have a direct and substantial impact on business confidence. As outlined in the macroeconomic analysis (see Annex 8), Ukraine's credit rating progressively improved during this period, transitioning from Caa3 with a stable outlook in mid-2017 to B3 by 2020. This upward trajectory in credit ratings was indicative of the successful execution of structural reforms, an improved external financial position following the initiation of both the MFA IV and the IMF SBA, as well as substantial progress in anti-corruption efforts. The ratings upgrade not only signalled an enhanced credit profile but also reflected growing confidence in Ukraine's economic stability. Beyond the financial aspects, certain individual conditions were noted, during the stakeholder consultation²⁰⁸, to have had positive effects on the business community and alignment with international agreements. These encompassed (i) conditions on tax reforms, and (ii) good governance and anti-corruption related conditions, fostering improved transparency in the long-term.

Reinforcing call for reform and conditionality design

MFA conditionality was found to be beneficial in reinforcing reform commitments already made by the government. Some international stakeholders highlighted that, even in areas where the Ministry of Finance (or other institutions) wish to push through reforms, they may face strong opposition from the existing vested interests. Having MFA conditionality can help to act as an additional impetus towards facilitating progress in key reforms. The Ministry of Finance reported, for example, that MFA conditionality was key in helping to move the ratification of BEPS MLI forward in parliament (condition #3, second tranche).

²⁰⁷ XE, Euro to Ukrainian hryvnia exchange rate chart, n.d., <https://www.xe.com/currencycharts/?from=EUR&to=UAH&view=10Y>

²⁰⁸ ICF interviews with relevant stakeholders

MFA conditionality can also reinforce or speed-up reforms envisaged under the Association Agreement, by setting clear targets and dates for adoption. This can help to maintain momentum of reforms even in the face of changing leadership in key institutions. Here, for example, the MFA supported the adoption of the new anti-money laundering law and the launch of the AEO programme.

One lesson in the context of Ukraine is the need to make sure that conditionality is clearly defined and informed by inputs of technical experts with strong knowledge of the local context.

6 Comparative exercise and regional-level analysis

6.1 Cross-country comparison

The design and implementation of each operation contained certain specificities (see Figure 6.1). These are examined in detail in the following sections.

Figure 6.1 Analysis of the specificities of each operation



Source: ICF, review of MFA documentation.

Relevance of the operations: from comparative perspective

The form and size of assistance varied across the three countries but were found to be relevant overall, although not as significant as IMF support.

In terms of the financing gap covered by the MFA operations, in Ukraine MFA IV aimed to cover 26.5% of the financing gap and 32% post-consideration of the WB's prospective

USD 800 million policy-based guarantee. The projection was based on the assumption that Ukraine would be able to secure funding from the international markets in 2018 and 2019 of up to USD 2 billion annually. In Moldova, MFA II aimed to maintain proportionality by constituting 24.9% of the estimated total financing gap, aligning with contributions from other major IFIs. In Georgia, MFA III, despite being the smallest operation, was initially designed to make a more significant contribution to a comparatively smaller financing gap: 53% of the 2018 residual financing gap, or 35% of the 2018-2019 residual financing gap. The comparatively larger contribution of the MFA appeared to reflect an intention to reward Georgia for its good reform track record, in line with the 'more for more' principle²⁰⁹, rather than a more dire economic situation. Ultimately, MFA III disbursements were spread over a longer period of time (2018-2020) than originally expected (2018-2019) and the actual EU contribution was thus more diluted.

Typically, MFA operations are structured as loans to address immediate and temporary financial challenges. While this was true in Ukraine, both Moldova and Georgia's MFA operations included a grant component. This was because of their economic and social progress level (in line with the criteria informing the form of MFA assistance). Given Georgia's progress on the previous MFA operations, the loan element was prioritised (22% of the proposed assistance in grants under MFA III, compared to 50% under MFA II and full grant under MFA I). The decision to grant only loans to Ukraine reflected previous MFA operations in the country and also took into account GNI, which was the highest among its Eastern European neighbours²¹⁰. Ukraine is the largest economy among the EaP nations²¹¹. Grant operations tend to be smaller given EU budgetary constraints, and Ukraine required bigger financing, proportionate with its size and needs.

In absolute terms, the Ukrainian operation was significantly larger than the other two (EUR 1 billion), reflecting the overall size of the country, compared to EUR 100 million in Moldova and EUR 45 million in Georgia. In all three countries, however, MFA disbursements were relatively small compared to the scale of the economy. In Moldova, MFA II disbursements remained modest, accounting for approximately 0.1-0.2% of GDP. In Georgia, MFA III disbursements were also modest, representing 0.1-0.2% of annual GDP, or 0.6-0.7% of annual public spending (depending on the year). In Ukraine, the financial disbursements under MFA IV were relatively small compared to the overall scale of the Ukrainian economy, representing about 0.5% and 0.4% of annual GDP (current prices) for 2018 and 2020, respectively, or 2.8% and 2.0% of gross international reserves for each year.

Compared to the other two operations, the design of the MFA in Georgia appeared more standard. By contrast, the design of the operation in Moldova was influenced by concerns about financial governance, while intermittent issues with the fulfillment of the political preconditions impeded smooth implementation. In Ukraine, the design of MFA IV was influenced by the cancellation of the third tranche of MFA III. In both Moldova and Ukraine, specific reform conditions were attached to the disbursement of the first tranche of the MFA, despite the anti-crisis nature of the MFA instrument typically seeing the first tranche released with no specific reform conditions attached, shortly after the signature and ratification of the

²⁰⁹ Note for the Alternates of the Economic and Financial Committee, attached to the 2017 MFA III proposal.

²¹⁰ WB, GNI, Atlas method (current US\$) - Ukraine, Moldova, Georgia, Belarus, Armenia, Azerbaijan data, <https://data.worldbank.org/indicator/NY.GNP.ATLS.CD?end=2022&locations=UA-MD-GE-BY-AM-AZ&start=2017&view=chart>

²¹¹ Armenia trails Ukraine, with a GNI of approximately USD 11,621 billion, indicative of a much smaller economic footprint. Azerbaijan's GNI at USD 40,496 billion, while substantial, is less than half of Ukraine's, reflecting a smaller yet sizable economy. Belarus is closer to Ukraine in economic terms with a GNI of USD 50,355 billion, suggesting a relatively robust economic structure, albeit still not on par with Ukraine. Georgia and Moldova, with GNIs of USD 15,049 billion and USD 9,105 billion, respectively, are at the lower end of the economic spectrum within this regional group.

relevant MoU and associated loan/grant agreements, and provided that the IMF programme is on track.

There was a limited use of conditions requiring the adoption of concrete measures (see Table 6.1). Instead, actions forming part of a longer reform process were targeted in the first instance. There appeared to be differences depending on the country: the focus in Ukraine was on pushing for implementation, given the implementation deficit concerns in previous MFA evaluations; in Moldova, 11 of the 28 conditions required legislative changes (including nine conditions related to the parliamentary passage of new laws) (in Ukraine, the adoption of the new anti-money laundering law was the sole such condition); the Georgian MoU contained an equal mix of the various condition types.

Table 6.1 Classification of MFA conditions

	Type A - concrete measures		Type B - actions forming part of a longer reform process			Total number of conditions
	Immediate benefits	No immediate benefits	Stepping stone	New legislative/ institutional change	Follow-up on legislative/ institutional change	
Georgia III	1		4	3	3	11
Moldova II	2		6	11	9	28
Ukraine IV	1	1	6	2	8	18

Source: ICF elaboration.

Overall, all three were shaped by the particular context in which they arose and thus reflected the specific (political and economic) needs at the time.

Outcomes and impacts of the three operations

Macroeconomic performance

The outturn macroeconomic outlook over 2016-2019 was relatively stable for all three countries. Their GDP growth averaged 5%, without any major deviations from the trend. There were, however, some concerns about fluctuating and high inflation levels, especially in Ukraine over 2016-2018 (see Annex 7).

In all countries, the macroeconomic situation deteriorated in 2020. GDP declined, with fallen FDI and worsening debt sustainability. Despite the deterioration of the economic situation, unemployment did not deviate much from previous years' trends. In 2021, recovery was apparent in all countries, with GDP growing once more. In 2022, the start of Russia's war of aggression against Ukraine negatively affected the macroeconomic performance of both Ukraine and Moldova, while Georgia remained largely unaffected and even benefitted from the relocation of Russians and dramatically increased remittances (boosting aggregate demand).

Debt sustainability differed slightly across countries. Over 2016-2019, Moldova's gross public debt was on a downward trajectory but it was followed by an 8 pp increase in 2020, to 36% of GDP. Georgia had a stable debt-to-GDP ratio over 2016-2019, slightly higher (6 pp) than Moldova's, at about 40% over 2016-2019. It experienced a larger increase in 2020 (20 pp). Ukraine saw far higher levels of gross public debt over the entire period, averaging 66%.

In the absence of MFA, the macroeconomic situation would likely have only been slightly worse for Moldova and Georgia (with their outturn/baseline profiles broadly stable). The

difference for Ukraine would have been somewhat larger given the greater stress in its economy.

In Moldova's no MFA scenarios, any financing gaps would likely have been closed by cuts to government spending, coupled with limited increases in domestic borrowing. Depending on the specific allocation across the options, lower GDP as a result of cuts to government spending and an increase in borrowing costs due to alternative financing would have emerged, but not at any concerning scale. Its debt sustainability profile would have remained largely the same.

Georgia's no MFA scenarios show similar results to those of Moldova, but with slightly smaller impacts given the corresponding smaller size of the MFA. Georgia would have similarly relied on a combination of fiscal adjustments and alternative financing, including domestic market borrowing and multilateral/bilateral support, resulting in similar effects to Moldova and, overall, negligible implications for the DSA outlook compared to the baseline.

By contrast, the absence of the MFA would have had more substantial effects in Ukraine. Not only was the support provided to Ukraine substantially larger than that of Moldova and Georgia, but the macroeconomic situation in Ukraine was also more unstable, making the effects of any alternative financing and cuts to government spending greater in absolute terms. Under these scenarios, it is estimated that Ukraine would have seen higher borrowing costs, of EUR 363 million and EUR 225 million in the two no-MFA counterfactuals, respectively (Alternatives A and B), far higher than that of the other countries. Overall gross financing needs and gross public debt were not affected as much as ratios to GDP, suggesting that the debt sustainability profile was unlikely to be improved or impaired much more than the already challenging situation; however, the size of the additional spending supported might have been material to Ukraine's macroeconomic performance.

The combined effect of no MFA and no IMF would have had more severe consequences for all countries' economies. A range of views was elicited regarding the hypothetical no-MFA and no-IMF scenarios, but their estimation was highly speculative given the magnitude of the impacts. For Moldova, the likely course of action would have been severe government spending cuts, coupled with some borrowing from domestic markets at higher interest rates. Relying mainly on alternative financing would have cost Moldova an additional EUR 175 million, together with, on average, 1.4 pp and 2 pp increases in gross public debt and gross financing needs as ratios to GDP each year. Relying mainly on government spending cuts would have improved sustainability ratios at the cost of a reduction in GDP of 0.3% each year compared to the baseline over 2016-2020, with a peak of -0.8% in 2020. The effects would likely have been worsened by the COVID-19 crisis.

In Georgia, the authorities would likely have implemented severe government spending cuts, potentially some privatisation of state-owned assets, and borrowing from domestic markets at high rates. Even though domestic markets were quite liquid, the removal of MFA and IMF support would likely have resulted in a drop in investor confidence, pushing up borrowing costs. Regardless of the combination of responses to cover the financing gap, Georgia's macroeconomic performance would have worsened. Relying on government spending cuts might have improved sustainability ratios but at a substantial GDP cost, ranging from a 1.3% reduction in 2017 to a 9.8% reduction in 2020. Conversely, relying on alternative financing would have increased gross financing needs and gross public debt by 0.6 pp and 0.7 pp on average each, with an additional EUR 227 million in borrowing expenses. Overall, compared to Moldova, macroeconomic performance would have been more severely affected, especially if more weight was placed on government spending cuts.

Ukraine would have faced a highly constrained financial environment and severe repercussions to macroeconomic performance. The dependence on external funding, particularly low-interest options like MFA support, was a cornerstone of its financial strategy.

The absence of this support would have significantly increased borrowing costs and reduced market access. The IMF support was considered essential to restoring investors' confidence and improving credit ratings. Without that support, investors' confidence and Ukraine's outlook would have been far worse, with considerable potential for other donors to have withdrawn their support as well. Overall, even though this counterfactual was not explicitly modelled due to the high uncertainty involved, evidence suggests a major deterioration of Ukraine's macroeconomic performance, be more substantial than that of Moldova and Georgia.

Social impact of the MFA operations

The three MFA operations included conditionalities intended to have direct impacts on the social situation in each country by influencing social/social policy outcomes. MFA IV for Ukraine contained a measure to improve the efficiency of the healthcare sector through contracting, which bore some similarities to conditionality in MFA III for Georgia. For Moldova, under MFA II, there was a measure to improve the targeting of social assistance, albeit for energy, rather than health. Other conditionalities (relating to subsidies for internally displaced persons in Ukraine, and to labour market and VET in Georgia) were specific to individual countries.

Progress was made in the practical implementation of the various conditions, but in some cases, it is too soon to assess whether their final objectives were achieved, given a lack of relevant data or the need for more time for certain impacts to manifest. For example, social assistance programmes may have improved (operationally) in both Moldova and Ukraine in terms of fewer beneficiaries and higher average payments, but the available data do not necessarily show if the subsidies reached the most vulnerable households, i.e. if targeting unambiguously improved. In Georgia, reductions in out-of-pocket expenditure coincided most visibly with the creation of the UHC rather than MFA III. This makes precise attribution difficult, although the implementation of selective contracting does seem to have increased the availability of health services for the population. Labour market and VET reforms in Georgia will need a longer timeframe to assess whether they have led to increased employment and reduced skills mismatches. However, on more of an input basis, it seems that ALMPs are slowly reaching an increasing number of jobseekers. If effective, the benefits should come in due course.

The absence of the first or second tranche of the MFA programmes would likely have had limited impact in Georgia due to the availability of funding in the form of alternative borrowing. In Moldova and Ukraine, however, the population might have suffered from cuts to public spending and/or higher taxation needed to compensate for the loss of MFA funding, especially in the context of the COVID-19 pandemic in 2020 and the resulting weaker economies and health systems. In Ukraine, the lack of the second MFA IV tranche might have entailed a reduction in anti-COVID-19 measures and possibly a delay in the implementation of healthcare reforms.

The simultaneous absence of MFA and IMF programmes would have had severe consequences, with lower economic growth, higher inflation, and large fiscal adjustments to compensate for the missing funds. Real incomes in the three countries would likely have been affected by higher inflation, cuts to social assistance (especially in Moldova and Ukraine), higher tax rates (in Georgia, to some extent), and lower expenditure on infrastructure, all leading to longer-term challenges. Debt restructuring might have been necessary in the case of Ukraine, and, in Georgia, the challenging labour market situation would likely have worsened.

Structural reforms

In all three countries, reform progress was generally seen as successful, despite delays in the implementation of some conditions in Moldova (later met) or backsliding in some reform areas in Georgia in recent years.

The design of the three operations was informed by the different political contexts in each country. As a result, each tackled a variety of structural reforms (e.g. anti-corruption in Ukraine, following MFA III; financial governance in Moldova).

Evaluation of the MFA operations in all three countries highlights the difficulties in attributing direct impact to their effectiveness for certain conditions. This is partially because all three countries were beneficiaries of wider donor support (including from the IMF), which also impacted reform progress. The Association Agreements also helped to shape and inform progress in some of the areas tackled via MFA conditionality. Accordingly, MFA conditionality was rather a tool to reinforce or speed up ongoing reform efforts.

When discussing the effectiveness of MFA across the three countries, the advantages and disadvantages of specific or vague conditionality attached to the operations were discussed and conclusions are presented in the conclusions section.

The successes and reform failures across all three countries tended to differ, in view of their varying contexts. Overall, Georgia's reform efforts were seen as quite successful, given the high ownership of the authorities at the time, with step changes completed in the public procurement field. Despite the inability to recoup any of the funds lost in the banking scandal, the most meaningful reform achieved in Moldova under MFA II was linked to banking sector reform (in the wake of the 2014 banking fraud scandal). Conditionality in the Ukrainian context was more operational, focusing on the operationalisation of ongoing reform efforts.

Some similarities are evident across all three operations, especially in relation to the focus on anti-corruption reform in Moldova and Ukraine. Moldova has begun to implement some of the anti-corruption reforms initiated in Ukraine since 2014 (asset verification system, discussions about a new anti-corruption court), building on the lessons learned from Ukraine. Georgia focused on addressing corruption earlier in the aftermath of the Rose Revolution and its legal and institutional framework is assessed as adequate overall.

Similarly, reforms to the judiciary continue to be a priority for all three countries, even if not directly tackled by each of these MFA operations. In both Georgia and Moldova, stakeholders pointed to the difficulties in achieving effective reforms in the area. While conditions were met in both countries linked to judicial reform and accountability of judges, the assessment shows that limitations persist. In Georgia, stakeholders highlighted perceptions of backpedalling on areas of judicial reform following MFA III. In Moldova, the judiciary was identified as an inhibitor to reform overall. Similarly, while reform of the judiciary was not part of MFA IV to Ukraine specifically, the judiciary was identified as an inhibitor to progress, particularly anti-corruption reforms. This led to the identified need to set-up a separate, independent, anti-corruption court, the HAAC (now successfully achieved, with the help of EU and IMF conditions)²¹². Judicial reform continues to be an important element of reform in all three countries, with the scale and scope of change impossible to finalise during the lifespan of one MFA operation.

MFA conditionality appeared particularly effective in setting up new institutions, safeguarding their operationalisation, and helping to overcome internal resistance to change. In Georgia,

²¹² U4 Anti-Corruption Resource Centre (CRI), *Launching an effective anti-corruption court: lessons from Ukraine*, 2021, See: <https://www.u4.no/publications/launching-an-effective-anti-corruption-court>; Halushka, O., 'The fight against courtroom corruption continues in wartime Ukraine', *Atlantic Council*, 1 June 2023, <https://www.atlanticcouncil.org/blogs/ukrainealert/the-fight-against-courtroom-corruption-continues-in-wartime-ukraine/>

the Dispute Resolution Council was considered a success, achieved with the help of technical assistance provided by DG GROW. In Ukraine, MFA IV was particularly successful in helping to operationalise the HAAC by focusing on the allocation of a sufficient budget and the independent selection of its judges. This helped to create the perception of the Court as an independent and effective institution. In Moldova, however, the newly set up institutions (NASC, for public procurement; CARA, for asset recovery) were not considered properly functional as yet.

The MFA to Moldova showed that formal compliance with conditionality does not always translate into effectiveness in practice, with human capital, funding, and political influence all proving key inhibitors. MFA IV to Ukraine can serve as a good example of conditionality being used to follow-up the implementation of previous reforms. It was specifically broken into successive concrete steps (first and second tranches), allowing for clearer follow-up. Similarly in Georgia, MFA III was later followed-up more closely with MFA COVID-19.

One of the lessons learnt of all three operations is that complex reforms require the engagement of multiple stakeholders and long-term support to ensure that progress does not subsequently stall or reverse. All three countries highlighted the importance of safeguarding progress already achieved from the possibility of back-sliding or reversals. This suggests that MFA conditionality is not definitive in itself. Rather, reforms need to be followed-up via additional instruments (e.g. technical assistance projects) and implementation and progress should be systematically monitored post-MFA to assess whether follow-up conditionality may be needed to ensure progress is maintained.

Factors affecting effectiveness (coherence, efficiency)

All three MFA operations aligned strongly with the EU Association Agreements or other EU budget support objectives (particularly Georgia). The enlargement agenda closely informed the design of MFA operations for the three EaP countries and is likely to continue to do so as they progress towards EU membership.

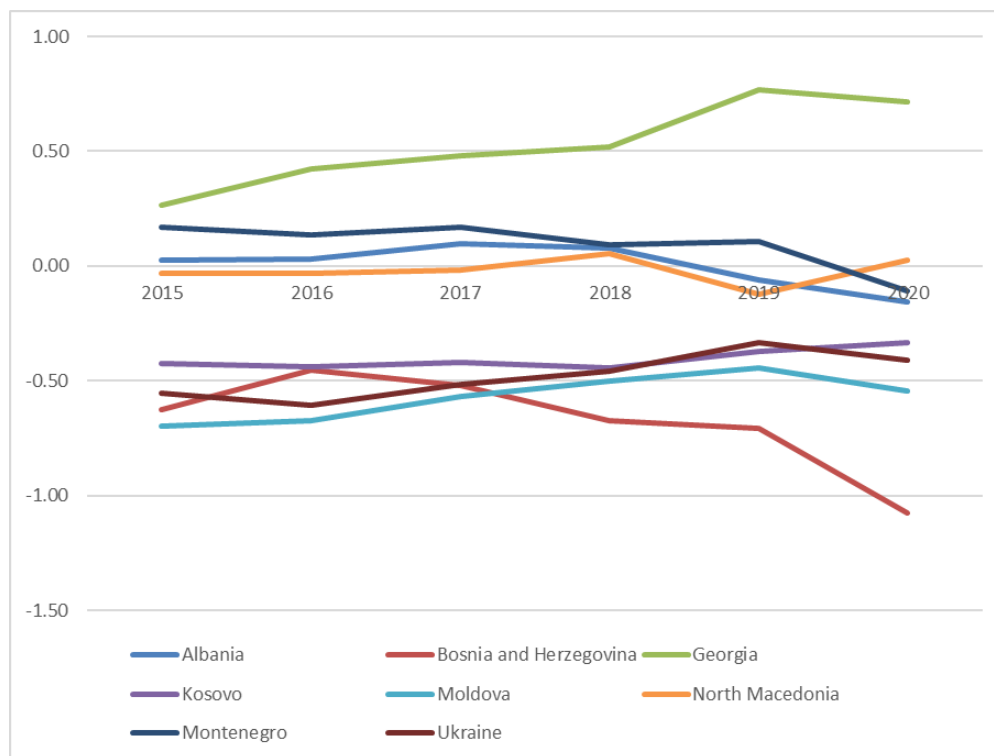
MFA IV to Ukraine was launched very closely after the MFA III operation (and the decision not to disburse the last tranche) and built directly on the reforms initiated under that earlier operation. By contrast, the MFAs to both Georgia and Moldova had a time lag and were not closely aligned to previous operations. In Georgia, this was because the preceding MFA II was specifically designed to allow for quick disbursement after the decision on the Commission proposal for a MFA Framework Regulation was blocked. In Moldova, the conditions for MFA II were very much defined by the 2014 bank fraud scandal, thus requiring a far larger scope than the previous operation.

All three operations were aligned to some degree with IMF conditionality, showing complementarity of donor support across all three countries. While joint conditionality was not always linked to the most strategic issues, it was seen as a means of signalling donor coordination overall.

All three countries benefitted from significant **donor support**, including via budget support programmes. The EU institutions were an unmatched provider of official development assistance (ODA) support, representing close to half of the flows (without including bilateral assistance from EU Member States). Despite this heavy international donor engagement, Moldova was the only country where this reportedly led to a heavy cumulative burden for the local administration in fulfilling both IMF and MFA conditions. This can also be traced to the high number of conditions attached to MFA II in Moldova (compared to the operations in Georgia and Ukraine at the time), as well as the limited administrative capacities in Moldova, especially compared to Georgia (see Figure 6.2).

Overall, reform ownership and the administrative capacity to implement reforms varied across the three countries. Georgia was consistently ranked higher than Ukraine and Moldova on the WB Governance Effectiveness Indicator (see Figure 6.2), which considers the quality of public service provision, quality of bureaucracy, competence of civil servants, independence of civil service from political pressures, and credibility of the government's commitment to policies)²¹³. The Georgian public administration was considered significantly more effective and modern than the other two, with an associated higher capacity to implement reforms. Moldova suffered from widespread capacity issues (e.g. within the Public Property Agency and Court of Accounts), with newly created institutions unable to function properly. Ukraine's public administration showed a more mixed performance, differing by institution, but, overall, rating only marginally better than Moldova. It was difficult to draw direct comparisons between the three countries, given their different political contexts. In Moldova and Ukraine, stakeholders also noted the difficulties faced by local public administrations in attracting and retaining talent, with limited capacity potentially hindering more complex reform efforts.

Figure 6.2 WB Governance Effectiveness Indicator, 2015-2020



Source: WB, *Worldwide Governance Indicators, 2015-2020*.

All three countries saw changes in government during the three MFA operations. Nevertheless, reform ownership was maintained within the new administrations, potentially highlighting the political importance of maintaining EU backing (in Moldova, the wish to retain EU support was reportedly high, ensuring reform ownership despite the change in government). Reform ownership may also have been maintained through the alignment of all three operations with the existing Association Agreements, whose implementation was important in all three countries.

²¹³ WB, *Worldwide Governance Indicators*, <https://www.worldbank.org/en/publication/worldwide-governance-indicators>

In terms of **overall implementation**, Moldova stood out as a particularly difficult operation. Issues with the fulfillment of the political preconditions repeatedly put the operation on hold and the last tranche was eventually canceled. By contrast, implementation performance was satisfactory in both Georgia and Ukraine (with Georgia requiring some flexibility and one waiver being granted in the context of COVID-19). However, Moldova also had to deal with the highest number of conditions (28) compared to the other two, making implementation more complex, particularly in a country with more limited administrative capacity. Comparisons can be drawn to the preceding operation in Ukraine (MFA III, with 36 conditions), which also faced implementation issues, leading to a non-disbursement decision at the end (similar to Moldova's MFA II). MFA IV in Ukraine drew on the lessons learned of MFA III by decreasing the number (and complexity) of conditions to 18, which was welcomed by Ukraine as part of a smoother operation.

In Ukraine, stakeholders noted that institutional memory and capacity developed over three previous consecutive MFA operations was an important factor favorably impacting the efficiency of the operation. Overall communication and coordination between the EU and Ukraine were well developed, with a strong understanding of how MFA works on the side of Ukrainian institutions. This was seen to have contributed to smooth implementation, highlighting the importance of understanding the knowledge and capacities of the receiving country. In Moldova, political instability during the MFA II implementation period likely creates challenges in capitalising on lessons learned. In Georgia, this learning factor was not highlighted, with stakeholders suggesting that its receipt of considerable donor support had developed capacity in terms of managing these kinds of programmes.

All three operations had **low visibility** among the wider public. This was often explained by the higher support provided by the IMF, which thus tended to garner wider public attention. While this can be easily understood in the context of Moldova and Georgia, a number of EU-level stakeholders noted that the amounts provided to Ukraine are already more substantial, and despite MFA still being lower than IMF support overall (and smaller in the context of the overall size of the economy), there should nevertheless be room for the EU to improve its communications.

Awareness of EU financial assistance was highest in Moldova. In a 2018 Opinion Poll²¹⁴, 87% of Moldovans reported being aware of EU financial assistance, significantly higher than the regional average of 57%. In Georgia, awareness of EU financial assistance²¹⁵ was at 67% and in Ukraine at 60%²¹⁶. While there were slight changes by 2020, Moldova continued to lead the other two countries by some distance²¹⁷.

Interestingly, In Ukraine, civil society reportedly used MFA and IMF conditionality in their advocacy work (particularly as relates to anti-corruption), which did not seem to be the case in Georgia and Moldova. The reasons were unclear, but closer engagement between EU stakeholders and civil society in recipient countries could help to promote similar engagement elsewhere.

²¹⁴ EU Neighbours East, *Opinion Survey 2018: Moldova*, 2018, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2018-republic-of-moldova/>

²¹⁵ EU Neighbours East, *Opinion Survey 2018: Regional Overview*, 2018, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2018-regional-overview/>

²¹⁶ EU Neighbours East, *Opinion Survey 2018: Ukraine*, 2018, <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2018-ukraine/>

²¹⁷ With 82% of citizens reporting awareness of EU financial support in Moldova in 2020, ; 71% of citizens in Georgia and 62% in Ukraine (. See: EU Neighbours East, *EIGHBOURSEAST (2020), Opinion Survey 2020: Regional Overview*, 2020, report in English. Available at: <https://euneighbourseast.eu/news/opinion-polls/opinion-survey-2020-regional-overview/>

EU added value of the three operations

Financial added value

The three evaluations highlighted that the financial added value of MFA operations did not always come solely from the disbursed amounts. Often the MFA operations were only one element of wider donor support. At the same time the 'EU stamp', together with IMF support, played an important role in signalling to other donors and investors, making it easier for beneficiary countries to access additional financial support, boost investments, or borrow on international markets. In Ukraine, for example, without MFA IV, it would likely have been harder for the government to borrow elsewhere, at interest rates almost certainly higher.

Financial added value also came from the terms and conditions of MFA assistance. For Georgia and Moldova, the MFA operations included a grant component, reflecting the economic situation in both countries. While Ukraine received MFA support solely in the form of loans, the conditions under the MFA instruments were considered very concessional and on par with or even more favourable than those from other donors (especially in terms of the grace period, as evidenced by data from Georgia).

Non-financial added value

The visibility of all MFA operations was relatively low. However, in Moldova, given the political situation, the MFA support was seen as providing an important reform benchmark for the government, with delays in disbursements (due to non-compliance) closely watched in the domestic political space. Ukraine was the only country where civil society used MFA conditions in their advocacy work, including monitoring and reporting on its implementation (and unexpected roadblocks). This could serve as an interesting example for the other countries in the region. In Georgia, the MFA instrument operated in a more stable environment and CSOs were more likely to refer to Georgia's wider commitments under the AA/DCFTA as a driver for specific reforms.

In all three countries, MFA operations were seen to have played a role in ensuring investor confidence, even if indirectly. This was especially noticeable in Moldova, given the unstable political situation prior to the operation. Moldova's ratings outlooks improved in 2017 when the MFA MoU was signed. In Ukraine, any such effect was less discernible. Nevertheless, stakeholders underscored the significance of the 'EU stamp' in enhancing confidence and facilitating reform implementation. Similarly in Georgia, the country was already progressively regaining investor confidence, in part due to growing alignment with the EU *acquis*, and, as such, MFA was further confirmation. In Georgia and Ukraine, stakeholders acknowledged the impact of MFA on maintaining those positive trends, suggesting that a no-MFA decision might have been damaging to all three.

Overall, MFA conditionality was beneficial in reinforcing reforms to which governments had already committed, particularly in helping to overcome internal resistance and speed up processes. Given that MFA conditionality in all three countries was aligned with the wider Association Agenda, the MFA instrument was seen to support the advancement of wider EU-led reform efforts.

Notwithstanding that doubts could be raised about the longevity of the effectiveness of some conditions, the fact that the issue is a priority on the political agenda was seen as positive (e.g. in Moldova, where MFA conditions helped to maintain continuity of the European spirit of the reforms during three changes of government). The requirement that all conditions must be met for the disbursement to happen was seen to add weight to the instrument. In Ukraine, conditionality (both EU and IMF – both pre- and post-MFA IV) played an important role in

maintaining reform momentum in the anti-corruption agenda, where internal resistance and vested interests were strongest.

Some conditions aimed at boosting competitiveness in the three countries improved the wider business environment and thus indirectly helped to boost economic growth. In Georgia, the Law on Entrepreneurs, adopted in 2021, approximated EU standards and modernised the regulations on the legal forms of companies, as well as procedures for their establishment and functioning, while the 2020 law set up the public procurement Dispute Resolution Council. In Ukraine, conditions attached to reforms in the areas of tax and customs also aimed to improve the business climate.

6.2 Regional analysis

MFA operations are bilateral forms of support and pursue objectives at national level. The MFAs under consideration were not meant to address a regional crisis; rather, the triggers were country-specific. Moldova, Georgia and Ukraine share many common challenges and reform priorities as well as a common EU ambition, but there are also marked differences between the three countries (see Section 2).

The EaP region covers a heterogeneous group of countries, with Belarus, Moldova and the Ukraine to the east, and Armenia, Azerbaijan, and Georgia to the southeast. EaP is not a regional classification typically used by IFIs. The three countries are often understood as belonging to different regions, e.g. with Moldova and Ukraine classified as 'emerging European economies' or 'Eastern Europe' and Georgia falling under 'Caucasus and Central Asia', as per the IMF regional classification.

This section explores the history of MFA/IMF/wider donor support in the region. The extent to which Moldova, Georgia, Ukraine, and the rest of the Eastern Neighbourhood countries (ENCs) are exposed to the same sources of growth spillovers/vulnerabilities is then analysed, looking at trade and financial integration and the repercussions of Russia's war of aggression against Ukraine.

MFA operations and wider donor support in the Eastern Neighbourhood

Eastern Neighbourhood countries have traditionally been among the main recipients of MFA assistance, a trend that has increased in the recent past. Between 2006 and 2020, the Eastern Neighbourhood received 72% of the amounts disbursed as MFA or about EUR 5 billion²¹⁸. This was driven by successive large operations to Ukraine, which absorbed EUR 4.3 billion between 2014 and 2020²¹⁹. Ukraine, suffering from Russia's hybrid warfare and fighting Russia-backed separatists since 2014, was heavily economically impacted in the years preceding MFA IV (especially 2014-2015).

Like Ukraine, Moldova and Georgia are democratizing countries that share a European agenda and suffer from frozen conflicts with Russia. Their economies had suffered from the aftermath of the global financial crisis, but growth had resumed in the years that followed.

²¹⁸ European Commission, Commission Staff Working Document, Background Analysis per beneficiary country accompanying the document Report from the commission to the European parliament and the council on the implementation of macro-financial assistance to third countries in 2020, SWD (2021) 178 final.

²¹⁹ Excludes EUR 110 million from MFA I based on the 2002 package, the second disbursement under the MFA COVID-19 package (EUR 600 million) and the 2022 operations (Emergency MFA of EUR 1.2 billion and New Exceptional MFA of up to EUR 9 billion).

The involvement of the IMF in the region has followed a similar pattern, with several successive programmes in Moldova, Georgia, and Ukraine (see Annex 7).

Of the six EaP countries, Georgia and Moldova are most dependent on ODA, which represented 4.3% and 3.5% of their annual GNI, on average, over 2017-2020 (see Table 6.2). In Ukraine and Armenia, ODA flows had a lower macroeconomic importance (around 2% of GNI). In Belarus and Azerbaijan, ODA flows were not macroeconomically significant (less than 0.5 % of GNI).

In absolute terms, Ukraine has been by far the largest recipient of ODA from EU institutions, followed by Georgia and then Moldova, i.e. the countries that signed AAs and DCFTAs with the EU. Per inhabitant, Georgia and Moldova received however more than Ukraine. By contrast, in the EaP region, Belarus and Azerbaijan received less support from the EU institutions, both in absolute terms and compared to the assistance from other donors. Armenia received average EU support.

Table 6.2 ODA in the EaP countries

Recipients	ODA from EU institutions (yearly average 2017-2020), disbursement data in constant prices (2021 USD million)	ODA from EU institutions as share of total ODA received 2017-2020	ODA from EU institutions (yearly average 2017-2020) divided by average Population (2017 – 2020) ²²⁰	ODA as percentage of GNI, 2017-2020 average ²²¹
Ukraine	741	47%	16.65	1.96%
Georgia	312	45%	83.77	4.27%
Moldova	179	48%	66.53	3.45%
Belarus	92	38%	9.76	0.43%
Armenia	86	33%	30.40	2.05%
Azerbaijan	25	21%	2.51	0.28%

Source: OECD, Aid (ODA) disbursements to countries and regions [DAC2a].

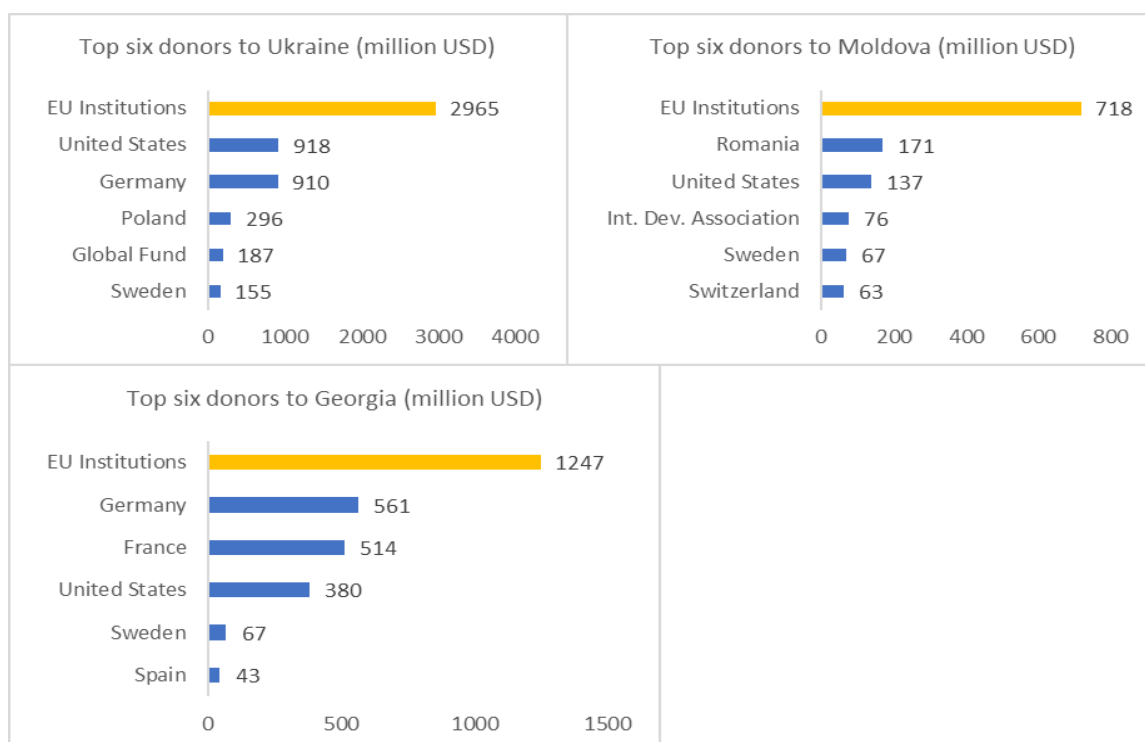
Note: ODA from EU institutions refers to ODA from the European Commission and the EIB. It does not include ODA from Member States.

EU institutions top the ranking of donors for all three EaP countries, with a total disbursement amount of almost USD 5 billion over four years. US ODA comes second in Ukraine, third in Moldova and fourth in Georgia, totaling close to USD 1.5 billion. Germany's ODA disbursements to Ukraine (USD 910 million) and Georgia (USD 561 million) match or exceed those from the US. In Moldova, Romania is the second largest ODA donor, at USD 171 million.

²²⁰ Population data from WB data, <https://data.worldbank.org/indicator/SP.POP.TOTL?locations=UA-GE-MD-BY-AM-AZ>

²²¹ WB data, https://data.worldbank.org/indicator/NY.GNP.ATLS.CD?most_recent_year_desc=true&view=chart

Figure 6.3 Top providers of ODA to Moldova, Georgia, Ukraine, 2017-2020, USD million



Source: OECD, Aid (ODA) disbursements

to countries and regions [DAC2a].

Note: ODA from EU institutions refers to ODA from the European Commission and the EIB. It does not include ODA from Member States; Includes bilateral and multilateral inflows. Projects executed by multilateral organisations on behalf of donor countries are classified as bilateral flows, as it is the donor country that controls the use of the funds. This explains the low presence of multilateral organisations in the top six here. Only aid activities financed from multilateral organisations' regular budgets are recorded under their own name.

Importance of Georgia, Moldova and Ukraine for the macroeconomic stability of the Eastern Neighbourhood region and evidence of regional spillovers/economic linkages

Collectively, Georgia, Moldova, and Ukraine in 2023 accounted for more than half (56%) of the total output produced by the ENC. Ukraine is the largest contributor (almost 45% of total output²²²), while Georgia and Moldova are smaller economies, accounting for about 8% and 4% of total GDP²²³, respectively. In the period preceding the COVID-19 pandemic, real GDP growth was highest in Georgia (yearly average of 5.0%), followed by Armenia (4.5%) and Moldova (4.2%)²²⁴. Ukraine, by contrast, showed modest growth year-on-year. As such, output grew by a yearly average of 0.5% over the 2010-2019 period, which also saw the

²²² IMF, World Economic Outlook, 2023.

²²³ Ibid.

²²⁴ Ibid.

illegal Russian annexation of Crimea and the City of Sevastopol, and the loss of government control over further territories^{225,226}.

The COVID-19 pandemic entailed a significant contraction in output across all ENCs in 2020, the most severe being Moldova (at -8.3%), followed by Armenia (-7.2%) and Georgia (-6.8%)²²⁷. The slowdown experienced in the rest of the ENCs was less pronounced, including in Ukraine, where the economy contracted by 3.8%. While the pandemic persisted into 2021, the economies of the Eastern Neighbourhood rebounded and experienced significant positive growth: most recorded larger growth in 2021 than the corresponding contraction in 2020, notably Moldova (+13.9%), and Georgia (+10.5%)²²⁸.

Following the outbreak of Russia's war of aggression against Ukraine in early 2022, recovery in the region was expected to stall. However, the evidence suggests limited adverse spillovers on most neighboring countries e.g. Azerbaijan. Growth in Georgia and Armenia even unexpectedly reached double digits in 2022 on the back of buoyant tourism, a surge in war-related migrant and financial inflows. The emergence of intermediated trade also played a role – meaning an increase in Western exports to Caucasus and Central Asia countries accompanied by an increase in exports from these countries to Russia. In the case of countries part of the Eurasian Customs Union²²⁹ like Armenia, EBRD analysis suggests that this intermediated trade could be suggestive of circumvention of trade sanctions - to some extent, equivalent to 5% of the reduction in direct exports to Russia, as the redirection of trade flows was much more likely to concern sanctioned or similar goods. In the case of Georgia, re-exports to Russia increased significantly but no such pattern emerged²³⁰. Despite positive growth in these countries since the start of the war in 2022, the prevailing uncertain domestic and external environment warrants continued policy prudence and reform efforts.

By contrast, the war has weighed heavily on Moldova. In 2022, the Moldovan economy contracted by 5% following multiple headwinds, including the energy crisis and other spillovers from the war, record high inflation, and a drought²³¹. Modest recovery was expected in 2023, supported by strong agricultural production and a rebound in consumption and investment. In Ukraine, the war has had a devastating economic and humanitarian impact. Output fell by nearly 30% in 2022. Ukrainian authorities introduced measures to maintain macroeconomic and financial stability, while continuous external support/financing has helped to keep the economy afloat²³².

Belarus has been directly impacted by the war. In view of its involvement in Russia's military activities in Ukraine, several Western countries, including the EU, have imposed sanctions on Belarus, including individual and economic sanctions, restrictions on trade, banking

²²⁵ Eurostat, European Neighbourhood Policy - East - economic statistics, 2023, https://ec.europa.eu/eurostat/statistics-explained/index.php?title=European_Neighbourhood_Policy_-_East_-_economic_statisticshttps://ec.europa.eu/eurostat/statistics-explained/index.php?title=European_Neighbourhood_Policy_-_East_-_economic_statistics

²²⁶ It is important to note that GDP for Ukraine has been adjusted to account for the loss of Crimea. This means that the GDP figures from 2010 to 2013 do not include the value added that was generated in Crimea. It is not adjusted to account for the loss of government control in Eastern Ukraine to Russia.

²²⁷ IMF, World Economic Outlook, 2023.

²²⁸ Ibid.

²²⁹ Belarus, Kazakhstan, Kyrgyzstan, and Armenia.

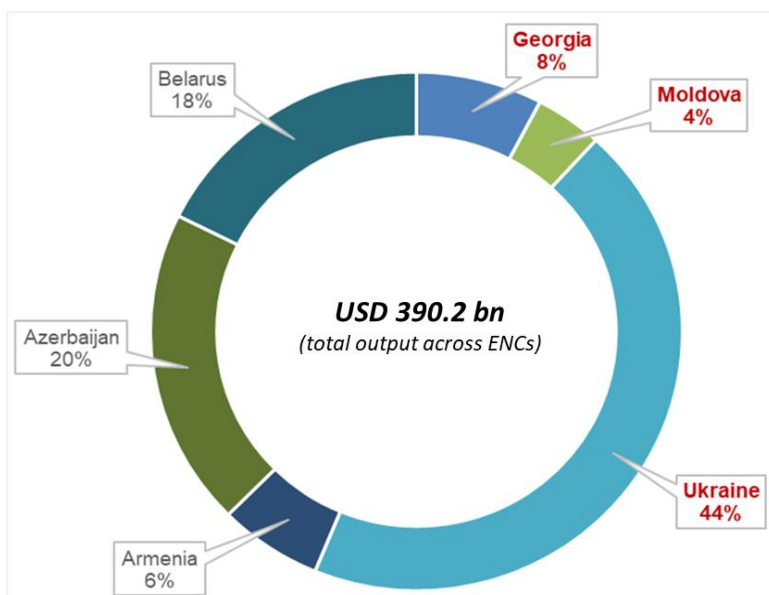
²³⁰ Chupilkin, Maxim, Beata Javorcik and Alexander Plekhanov, 2023, "The Eurasian roundabout: Trade flows into Russia through the Caucasus and Central Asia", EBRD Working Paper 276.

²³¹ IMF, Staff Report for the 2023 Article IV Consultation, 2023, <file:///C:/Users/N116712/Downloads/1MDAEA2023004.pdf>

²³² IMF, 2023 Article IV Consultation, 2023, <file:///C:/Users/N116712/Downloads/1UKREA2023003.pdf>

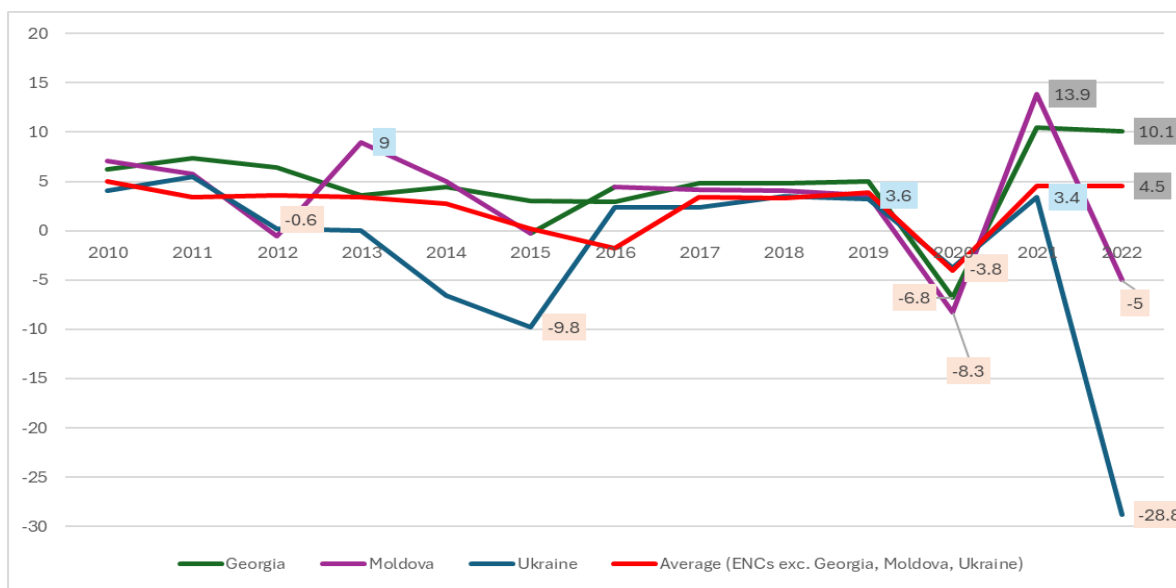
activities and financial inflows. The Belarusian economy contracted by almost 4% in 2022²³³, owing to these sanctions and the recession in Russia, its main trading partner.

Figure 6.4 Estimated Economic output of Georgia, Moldova, Ukraine as share of overall output of ENCs, 2023 (%)



Source: IMF, World Economic Outlook, 2023 (estimates from October 2023)

Figure 6.5 Real GDP growth (%) in Georgia, Moldova, Ukraine vs remaining ENCs, 2010-



2022

Source: IMF, World Economic Outlook, 2023

Trade linkages

There are trade linkages between Georgia, Moldova, Ukraine and the remaining ENCs (see Table 6.3). Over the years, however, bilateral trade concentration among ENCs/within the

²³³ IMF, World Economic Outlook, 2023.

region has been on a downward trend. As such, most of the ENCs increasingly trade with the EU, US, China, India, Turkey, and other Middle Eastern and Central Asian countries.

In theory, these linkages could have been important in channelling spillovers from the ongoing war in Ukraine. The evidence suggests that the war has had limited impact on most of the ENCs. Armenia and Georgia, for instance, experienced an inflow of foreign exchange, migrants, and businesses, notably from Russia, which helped to boost economic activity and aggregate income. Additionally, with sanctions restricting Russia's ability to trade with the EU and the US, neighbouring countries in the region have benefitted from a ramp-up in their trade activities with the West. Georgia, for example, has seen an increase in revenue from surging transit demand as international shippers choose to avoid traditional routes across Russia. The war has had a limited impact on Azerbaijan's real economy, while non-oil growth has remained strong.

Conversely, Belarus and Moldova have been more severely impacted. Belarus was hit with punitive sanctions for lending support to Russia in its war of aggression against Ukraine, and has had to reorient its foreign trade from the EU and Ukraine to Asia, Africa and Russia. It also lost access to important trade routes, such as the Lithuanian ports, making it even more reliant on Russian markets.

Moldova has also been severely affected by the war in Ukraine due to proximity and a heavier reliance (compared to the other ENCs) on commodity imports from both Ukraine and Russia. Given that the energy infrastructure in Ukraine and Moldova is interlinked, the latter experienced multiple blackouts when Russia attacked Ukraine's energy grid. This, along with Gazprom (Russia's state-owned natural gas supplier) reducing its gas deliveries to Moldova by 51%, led to a sevenfold increase in the price of natural gas in Moldova and quadrupled the price of electricity. Since Russia's war of aggression against Ukraine, Moldova has dealt with energy disruption, massive inflation, trade disruption and thousands of Ukrainian refugees, while managing tense relations with its breakaway province of Transnistria, where approximately 1,500 Russian troops are stationed.

Table 6.3 Trade ties: Georgia, Moldova, Ukraine

Country	Value of world exports, yearly average 2017-2020	Value of world imports, yearly average 2017-2020	Exports going to the EU-27, yearly average 2017-2020	Imports originating from the EU-27, yearly average 2017-2020	Exports going to the ENCs, yearly average 2017-2020	Imports originating from the ENCs, yearly average 2017-2020	Exports going to Russia, yearly average 2017-2020	Imports originating from Russia, yearly average 2017-2020
Georgia	USD 3.3 billion	USD 8.7 billion	21.8%	25.0%	28.3%	16.0%	13.4%	10.3%
Moldova	USD 2.6 billion	USD 5.5 billion	64.2%	47.6%	7.2%	11.5%	9.1%	11.8%
Ukraine	USD 47.1 billion	USD 55.0 billion	39.5%	40.3%	6.3%	7.3%	7.2%	12.2%

Source: IMF trade statistics, 2023.

Financial linkages

The majority of FDI in Georgia, Moldova and Ukraine appear to come from outside the Eastern Neighbourhood. Georgia attracted a total of USD 5.3 billion in FDI over the period 2017-2020²³⁴. In recent years, the top five investor countries were: the US, the United Kingdom (UK), the Netherlands, Turkey and China. For Moldova, FDI inflows totalled about USD 1.1 billion over the period 2017-2020²³⁵. The majority came from neighbouring European countries, particularly Romania, which accounted for 34.6% of total FDI in 2020²³⁶. Other important investors were Cyprus, Russia and Ukraine. Prior to Russia's war of aggression against Ukraine in 2022, total FDI inflows in Ukraine reached about USD 14.4 billion²³⁷. Most investments were in the manufacturing, wholesale and retail trade, mining, financial services and real estate sectors. The main investors in Ukraine seemed to be from Cyprus, the Netherlands, Switzerland, the UK, and Germany²³⁸; numbers however include round tripping transactions routed through these countries especially for Cyprus, the Netherlands and Switzerland²³⁹. Russia's war of aggression against Ukraine deeply impacted the investment climate: insecurity, political and economic uncertainty, supply chain disruptions and infrastructure destruction resulted in considerable capital flight. There is, however, little evidence captured so far that the slowdown in Ukraine (and Russia) channelled significant negative spillovers (e.g. investment cutbacks, reduced investor sentiment) in the region.

Conclusions on linkages

Overall, the evidence points to some trade ties, but weaker financial ties, among the ENC. Over the last decade, the ENCs (except Belarus, which remained heavily reliant on Ukraine and Russia) have become increasingly open to foreign trade and investment, reducing the extent of intraregional dependence.

The economic shock brought about by Russia's war of aggression in Ukraine in 2022 had limited regional effects (except in Moldova), in view of lower bilateral trade concentration (among ENCs/in the region), well-developed trade and financial links with Western and Asian economies, access to new export markets, continued international donor funding/support to the region, and prudent macroeconomic policies and reforms.

In this context, and given the limited size of the MFA operations compared to the size of the beneficiary countries' respective economies, the MFA operations in Georgia, Moldova and Ukraine are unlikely to have had sizeable direct macroeconomic impacts on the other ENCs and/or the wider region.

Had support from the EU and the IMF not been made available, however, shocks of a large magnitude could have arisen, increasing the probability of negative spillovers onto neighbouring countries. Again, low intraregional integration could have helped to contain these negative spillovers, as evidenced by the rather limited regional repercussions of Russia's war of aggression against Ukraine. However, the extent to which shocks become

²³⁴ National Statistics Office of Georgia, <https://www.geostat.ge/en/modules/categories/191/foreign-direct-investments>

²³⁵ United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2022*, United Nations, 2022, https://unctad.org/system/files/official-document/wir2022_en.pdf

²³⁶ Lloyds Bank, Foreign direct investment (FDI) in Moldova, 2022, <https://www.lloydsbanktrade.com/en/market-potential/moldova/investment>

²³⁷ United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2022*, United Nations, 2022, https://unctad.org/system/files/official-document/wir2022_en.pdf

²³⁸ NBU, 2021 (Lloyds Bank, Foreign direct investment (FDI) in Ukraine, 2022, <https://www.lloydsbanktrade.com/en/market-potential/ukraine/investment>).

²³⁹ https://bank.gov.ua/admin/uploads/article/FDI_round_triping_ICL-DFS_pr_eng.pdf?v=4

regional shocks are hard to predict. Other factors play a role in the region e.g. the dynamics of the oil prices. In 2014, Georgia's macroeconomic stability was affected by Russia's illegal annexation of Crimea and the subsequent conflict in the east of Ukraine, through the depreciation of lari (GEL) (inflating its foreign-dominated external debt). Concomitantly the prices of the prices of Brent crude oil were declining, reaching their second lowest point between 2014-2023 excluding the COVID-19 period in 2020. In 2022-2023, Georgia was less affected than initially projected.

Indirect impacts of MFA operations in the EaP region/beyond borders

Beyond direct transmission channels, other channels existed for the MFAs to have impacts in the region/beyond borders.

Firstly, the MFA operations may have sent signals beyond borders.

- The MFA operations were approved in the context of strengthening relations between the EU and the three countries. That (along with other budgetary/ donor support) signalled stability and helped to restore/increase investor confidence (in addition to the macroeconomic reforms attached to these individual support packages). Together, this would have had a stabilising effect on Georgia, Moldova and Ukraine, and potentially on neighbouring countries. Greater confidence would have been crucial for attracting tourism and investment flows into the region;
- A potential demonstration effect of disbursements and non-disbursements was also noted. Neighbouring countries tend to monitor how much support was received, noting greater support for those countries that are progressing with reforms and meeting political preconditions. In isolation, it would not be sufficient to bring a country closer to the EU, but it can demonstrate the positive effects of reforms. Conversely, cancellation of tranches may have sent signals with disciplinary effects beyond borders, highlighting that the EU was unwilling to compromise on crucial reform requirements (e.g. anti-corruption efforts or judiciary reform).

Secondly, the reforms in question could be expected to have some impacts across borders. This could be indirectly, e.g. via an improved business climate or a fair public procurement system, which positively impacts the main business partners in the medium term. In Georgia, there was evidence that the MFA (among others) contributed to the development of best practices in terms of fiscal/PPP legal framework, and these practices were then shared with other countries from the Caucasus region and beyond.

Conclusions on regional analysis

There is no conclusive evidence that the MFA operations had direct economic impact in the region or across borders. However, indirectly and through 'soft' transmission channels, MFA operations may have had some impact, e.g. signalling or demonstration effects on other ENC's in the region.

MFA operations could have wider regional impacts if the main trigger had a regional dimension (i.e. an MFA intended to help a country to address a crisis of a regional nature). This was not the case for the three operations under consideration.

7 Conclusions and lessons from the evaluation

Overall, the evaluation confirmed the relevance, coherence, effectiveness, efficiency and added value of the three MFA operations, though to varying degrees, considering the different contexts in all three countries under evaluation. Moreover, the evaluation has helped in the formulation of a number of lessons learnt and recommendations for the future.

As highlighted across the evaluation, all three MFA operations were designed in response to the specific context of the three countries at the time. As such, they also differed significantly in terms of their size, focus of conditionality and number of conditions attached.

Nevertheless, all three operations were found to have been **relevant**, in terms of the size and form of the assistance provided. The amounts varied significantly, also in view of the different needs of each country and different size of their economies. Overall, while the MFA disbursements were relatively small compared to the scale of the three economies, they still played a significant role, also from a burden-sharing perspective.

Evidence has also shown that these operations are facilitated when they are anchored in a clear policy framework, as was the case for all three operations. Each was strongly aligned with the countries' respective Association Agreement's in place, thus there was a shared reform agenda in place for reference. The EU has more leverage in these three countries of the Eastern Neighbourhood, whose clear EU orientation facilitated the implementation of shared reforms. This also helped ensure the **relevance and coherence** of the attached conditions to all three MFA operations with the EU's policy priorities in the region, as well as with other international donor support.

As regards the **efficiency** criteria, in all three countries, the need for disbursement was larger during the second tranche (2020), due to the unexpected impact of the COVID-19 pandemic. This timing of disbursements enhanced the **social impact** of the three operations. For the first disbursements, the need was higher in both Moldova and Ukraine in 2018. In Georgia, the economy was performing better than expected at that time.

The **Debt Sustainability Analysis** and **Cost Benefit Analysis** conducted as part of this assignment confirmed that benefits outweigh costs to the EU budget, which remain limited in light of the prioritisation of the loan element. From the perspective of the MFA beneficiary countries, concessionality of MFA assistance remains high despite the loan format of the assistance, given terms and conditions reflect those that the EU can obtain on the market as an issuer. MFA terms and conditions are on par or compare well with those of other donors (e.g. longer grace periods). Compared to the IMF, MFA terms and conditions are more preferential, once taking into account of all fees, margins and surcharges that can apply, depending on programme type and quota's utilisation rate. IMF rates are on average higher (1.1% to 2.7% vs 0.2% to 0.7% for MFA), for a shorter maturity. The grant element of the provided assistance was found to range between 44% (for Ukraine) and 67% (for Moldova). In terms of quantifiable benefits, they are estimated to take different forms depending on the most plausible counterfactual alternative (what would have happened in the absence of the assistance). In case budgetary cuts were a likely alternative option (like for Moldova or Ukraine's second tranche), the benefit of the assistance was to provide additional fiscal space (equivalent to assistance provided, minus cost of servicing MFA loan). In case alternative borrowing was a likely alternative (i.e. for Georgia and Ukraine's first tranche), the MFA assistance was found to generate significant fiscal savings (EUR 29 million for Georgia's two tranches and EUR 454 million for Ukraine's first tranche).

Beyond financial added value, other elements of **EU added value** came from the 'EU stamp' and its signalling role towards the markets, but also towards the citizens especially in the case of Moldova, as a sign of credibility. MFA conditionality as well as political preconditions were beneficial in reinforcing commitments to EU oriented reforms.

When considering the factors impacting on the **effectiveness and efficiency** of structural reforms supported via all three MFA operations, it should be mentioned that in all three countries, reform progress under these operations was generally seen as successful, even though implementation capacities differed. Some broader challenges were raised in each country. The below summarises some key considerations that emerged as impacting the effectiveness of supported structural reforms, including the role of political preconditions and design of attached conditionality.

Political preconditions

The recent meta-evaluation found little evidence of the impact of the political preconditions on the outcomes, efficiency and effectiveness of the MFA operations. This was often the case, as political preconditions were generally met and did not play an important role in the implementation of the operations.

In the case of MFA II to Moldova, however, the political preconditions played an important role. The programme was seen as impactful and successful because of the political preconditions, which provided a useful safeguard when the elections of the Chisinau mayor were invalidated. The fact that the political preconditions were formulated in broad terms (respect effective democratic mechanisms, including a multi-party parliamentary system; respect the rule of law and human rights) was helpful. Once the operation was suspended, however, the EU's clear specification of the conditions to be met for the assistance to resume was helpful. This happened twice during the Moldovan operation. In 2018, the focus was on calling for the February 2019 parliamentary elections be held in a credible, inclusive and transparent manner, with a new government that represented the results of the election and did not rely on support from members prosecuted for the 2014 bank fraud. In 2020, eight short-term actions were negotiated with the Moldovan authorities, related to anti-corruption, reforms in the justice sector, and investigation of the 2014 bank fraud.

Stakeholders, including in Moldova, generally believed that the EU was right in adopting a firm stance and putting the operation on hold, as it helped to rectify the deterioration of democratic standards, maintain Moldova on its EU path, and keep the focus on AA-related reforms. The fact that this ultimately contributed to the operation being cancelled without the third disbursement was not viewed negatively.

MFA conditions in the MoU

Reform challenges, ownership, capacity and broader geopolitical and economic context vary, even within one region or within the same country at different points in time. This was reflected in the design of the MFAs operations evaluated here. Setting conditionality and assessing implementation should always remain context-specific, but general considerations must also be built-in, in line with the guiding principles for setting MFA conditions (see Figure 3.2).

Prudent use of conditionality

In Georgia and Ukraine, the number and ambition level of conditions was seen as appropriate overall. A waiver was required in the case of Georgia (adoption of the MPTL Law), but this was in the context of COVID-19 and the evaluation concluded that it did not reflect an overly ambitious reform condition.

The Moldovan operation, to which 28 conditions were attached initially, with eight short-term political actions added in 2020, was very different in design. The atypical attachment of conditions to the disbursement of the first tranche for both Moldova and Ukraine was seen as justified, given their specific contexts. The conditions in the Moldovan MoU reflected concerns about the financial governance of the country and were seen as necessary to convince the co-legislators on the EU side. While the choices made were seen as somewhat inevitable, some specific conditions (especially in relation to energy reform) were considered

overly ambitious for the timeframe and would have benefitted from being broken into smaller, more realistic steps. The study team understands that the Moldovan side raised no issue ex-ante about the feasibility of these reforms, but this may have been due to the strong will to rapidly receive an endorsement from the EU.

Clear, measurable conditions vs more broad conditions

The EU *acquis* was a useful reference for many reform areas in the three countries, e.g. in the fields of energy, customs, public procurement, and company law. It helped to clarify the ultimate objectives of the conditions. One condition that was seen as problematic was the beneficial ownership condition in Ukraine. This followed an MFA III condition, and, despite being more clearly spelled out than before, the authorities in Ukraine still lacked clarity on its implementation. There is no EU *acquis* in this domain and EU Member States themselves lacked experience of implementing such systems. Member States were consulted while the operation was ongoing to define the precise steps needed to put such a system in place.

More generally, to compensate for the fact that MFA conditions cannot be renegotiated without amending the MoU and going through the whole decision-making process again, there can be a tendency to formulate somewhat broad conditions (e.g. 'make substantial progress towards'). This comes with certain advantages – it ensures that conditions do not become outdated too quickly if the decision-making process takes time, and gives the Commission more room to assess whether the conditions have been fulfilled in letter and in spirit. It can also give more flexibility during implementation to adjust the EU stance to the evolving political and economic situations (and avoid a non-disbursement decision later). This approach can work for reform areas that are unlikely to be controversial and where government ownership is a priori high, as assessed ex ante. In some spheres, broad conditionality may be preferred and can encourage reforms without being too prescriptive. At the same time, as raised by some stakeholders, broad conditionality also makes it more difficult to confirm implementation has been successful or to measure impact.

In allowing flexibility to recipient countries, there is also the option to grant waivers, thus avoiding vague conditions. Hindsight showed that in the Moldovan MoU, several conditions were insufficiently precise. For instance, condition #22, on the fight against corruption, stated that 'substantial progress should be made'. The vague wording made it challenging to assess the fulfilment of this condition accurately, with disagreements between two ministries as to its fulfilment, as well as uncertainty about when implementation could be considered complete. Condition #9, on improving the business climate, mandated the reduction of permits required to start a business without providing specific guidance (the wording used was 'reduce their number accordingly').

There were no such examples of overly broad conditions in Ukraine, as MFA IV conditions were written on the basis of the MFA III experience and consisted of smaller steps. However, some conditions related to the adoption of plans could be considered vague (e.g. in the absence of detailed specifications on what should be in the reform plan). In Georgia, clarity came from the fact that MFA III conditions mirrored pre-existing and parallel commitments under AA and budget support programmes. However, in both countries, local experts also agreed that it was best to avoid vagueness and try to ensure a shared understanding of what exactly was meant in each case. In Georgia, the risk of vagueness leading to differences in views of whether or not conditions were met was raised (referring to the MFA COVID-19 experience). In Ukraine, the argument was that vagueness makes it more complicated for external stakeholders to follow progress on MFA implementation. Civil society organisations in Ukraine noted that they found it harder to monitor and report on the implementation of vague/broad conditionality for advocacy purposes, as they did not know the exact criteria against which fulfilment of the conditions would be assessed. The IMF was seen as setting a good example on how to develop more specific detailed conditionality (and providing broader explanations in accompanying reports).

In some cases, defining precise targets may mean that quantitative targets are inserted within the conditions. This was the case for conditions on land registration in Georgia and verification of asset declaration in Ukraine. A quantitative target may help even if the same objectives have already been announced by the government, to make sure the agreed plans are implemented.

Specifying the conditions more precisely does not necessarily mean that they should address more technical (quantitatively measurable) issues. Some conditions could remain high level or broad, with the MoU accompanied by a document detailing the baseline and expectations.

The availability of in-house technical expertise on the EU side was highlighted as key to derive more specific conditions and closely follow progress.

For all three operations, DG ECFIN, which led the negotiation/monitoring welcomed detailed technical inputs from other colleagues (Commission; EEAS). In the Ukraine MFA IV operation, a number of EU-level stakeholders praised the close involvement of technical experts from DG NEAR, the EU Delegation in Kyiv, and technical assistance projects (e.g. EUACI) in helping to define targeted conditionality (especially in the area of anti-corruption). The study team believes that these consultations on the EU side could usefully be organised in a more systematic manner at the negotiation stage and throughout implementation to ensure that they are part of the standard process, irrespective of the person in charge of the operations. Ensuring close coordination across relevant EU and international stakeholders could also be crucial in ensuring that targeted conditionality is sufficiently adapted to the local context. During any such consultation, attention should be paid to avoiding the insertion of a disproportionate number of conditions, instead focusing on better chosen and specified conditions.

Results-oriented conditions

In addition to being specific, ensuring shared understanding, and inserting measurable targets, there is a need to ensure that conditions are results-oriented and designed to make a meaningful difference. This may mean inserting conditions that follow up the implementation of reforms, e.g. making sure that the newly adopted law is actually enforced and that the newly established institutions have the mandate and capacity to act. In MFA IV to Ukraine, there were many such conditions (particularly in relation to the operationalisation of the newly created HAAC, or improvement of the functioning of the asset verification system). The relevance of these types of conditions increases progressively once the legal and institutional framework is put in place.

To facilitate the achievement of actual benefits, areas where the EU is widely engaged should be targeted. These might be areas where technical expertise is made available, such as to help develop and/or implement reform plans or strategies (e.g. Ukraine's tax and customs reform) and/or where other EU policy instruments are likely to follow up on subsequent steps (e.g. via budget support operations, as in the case of Georgia's labour market and VET reforms).

Visibility and communication issues

The assessment found that the lack of visibility of the MFA instrument was frequently reported, most importantly in Ukraine and Georgia. Comparing the three operations, there was a missed opportunity in Georgia especially, where CSOs and experts were unaware of the details of the MFA operations and were thus unable to use MFA leverage in their activities (unlike in Ukraine).

While in Ukraine, civil society had made use of MFA (and IMF) conditionality to report on the government's progress in key reform areas, the overall visibility of the instrument was still low. Given the overall high amounts of EU assistance to the country, stakeholders pointed out that more could have been done to strengthen the EU's strategic communications.

Overall, communicating the specifics of the MFA operation with an informed audience should be part of the standard process. The lessons learnt that this may be easier in specific political climates. For example, in Moldova, the overall visibility and higher public awareness of the EU's MFA support at the time can be understood in the careful scrutiny of government actions by political and civil society actors at the time, following the banking fraud scandal. This also likely made EU assistance in such a context, as well as the EU supported reforms via the MFA instrument, more visible and relevant in the eyes of the public.

For the wider audience, MFA support could be communicated more broadly, alongside the wider EU support. The focus should be on communicating the (expected) benefits of the assistance and the specific measures supported²⁴⁰.

Sustainability of reforms

The evaluation has shown that ensuring tangible benefits from implemented conditions cannot always be guaranteed, given changing political context, as well as increasingly more challenging geopolitical situation in the region. Moreover, reform ownership is not always uniform across all national stakeholders, the spirit of the condition is not necessarily adhered to and implementation capacities can also be limited at national level.

To help maintain reform momentum, the evaluation has highlighted the important role of technical assistance projects in supporting local stakeholders with the implementation of attached conditionality in the long-term. The presence of such projects also helps move initiated reforms further. But technical experts can also play a key role at design stage, to ensure conditions are relevant and achievable.

The close alignment of MFA conditionality with the EU and national policy priorities also helps ensure greater ownership and supports implementation and longevity of initiated reform efforts.

Lastly, MFA operations that follow each other can build on previous MFA operations and help add momentum to previously supported reform efforts. In this regard, the example of Ukraine stands out the most, given that the MFA IV package was closely following the preceding three MFA operations and was able to successfully build on previous reform achievements, but also set new reform targets.

²⁴⁰ See for instance the factsheet produced in the Covid context: https://eu4georgia.eu/wp-content/uploads/Factsheet_Covid_Eng-2-1.pdf

