INTERNATIONAL MONETARY FUND

IMF Country Report No. 20/93

REPUBLIC OF SAN MARINO

2020 ARTICLE IV CONSULTATION—PRESS RELEASE AND STAFF REPORT

April 2020

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2020 Article IV consultation with the Republic of San Marino, the following documents have been released and are included in this package:

- A **Press Release**.
- A **Staff Supplement** updating information on recent developments.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse-of-time basis. The staff report reflects discussions with the Sammarinese authorities in January 2020 and is based on the information available as of January 31, 2020. It focuses on San Marino's near- and medium-term challenges and policy priorities and was prepared before COVID-19 became a global pandemic and resulted in unprecedented strains in global trade, commodity, and financial markets. It, therefore, does not reflect the implications of these developments and related policy priorities. The outbreak has greatly amplified uncertainty and downside risks around the outlook. Staff is closely monitoring the situation and will continue to work on assessing its impact and the related policy response in San Marino and globally.
- An **Informational Annex** prepared by the IMF staff.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

PRESS RELEASE

PR20/126

IMF Executive Board Concludes the 2020 Article IV Consultation with the Republic of San Marino

FOR IMMEDIATE RELEASE

WASHINGTON, DC – **April 2, 2020** On March 27, 2020 the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with the Republic of San Marino and considered and endorsed the staff appraisal without a meeting on a lapse-of-time basis[2] (see below an important note on the timing of the report which precedes the outbreak of COVID-19).[3]

San Marino is now facing very significant challenges owing to the recent COVID-19 outbreak, which has taken a heavy toll on local population and businesses. The authorities' near-term efforts are rightly focused on limiting and containing the adverse social and economic effects, including by re-directing resources to the health system.

Medium-term growth prospects are projected to remain weak as tight credit conditions and a substantially weaker external environment will constrain the recovery. The high uncertainty around the extent and length of the COVID-19 spread, the current lack of external market access, and the limited central bank liquidity buffers suggest that the balance of risks is heavily tilted to the downside. San Marino's key medium term challenge is to address the elevated macro-financial vulnerabilities emanating from the weak banking system liquidity and capital positions, poor asset quality, and high cost-to-income ratios as well as low government's liquidity buffers and an excessive accumulation of fiscal liabilities.

Executive Board Assessment

In concluding the Article IV consultation with the Republic of San Marino, Executive Directors endorsed the staff's appraisal as follows:

Banking sector weaknesses continue to pose stability risks and hinder economic recovery. Significant deposit outflows and weak risk management have left the banking system with low liquidity, poor asset quality, and considerable recapitalization needs, while multiple bank failures and continued state support to the banking system have eroded government liquidity buffers and led to an excessive and unsustainable accumulation of the implicit public debt. Absent a significant policy change, growth prospects are projected to remain subdued over the medium term with risks heavily tilted to the downside. The recent outbreak of COVID-19 in

---

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] The Executive Board takes decisions under its lapse-of-time procedure when it is agreed by the Board that a proposal can be considered without convening formal discussions.

[3] The staff report reflects discussions with the Sammarinese authorities in January 2020 and is based on the information available as of January 31, 2020. It focuses on San Marino's near- and medium-term challenges and policy priorities and was prepared before COVID-19 became a global pandemic and resulted in unprecedented strains in global trade, commodity, and financial markets. It, therefore, does not reflect the implications of these developments and related policy priorities. The outbreak has greatly amplified uncertainty and downside risks around the outlook. Staff is closely monitoring the situation and will continue to work on assessing its impact and the related policy response in San Marino and globally.

San Marino and Italy has significantly increased uncertainty. The external position is weaker than implied by fundamentals and desirable policy setting.

A comprehensive and credible stabilization plan is urgently needed. Shifting the economy to a higher medium-term growth path requires implementation of a coherent and credible strategy that restores banking system viability, ensures fiscal sustainability, and addresses structural impediments. The recent general elections and establishment of a four-party coalition government provides an opportunity to build a broad consensus for the necessary reforms.

Sustained efforts are needed to increase banking system liquidity and boost CBSM reserves. The CBSM should further enhance its liquidity management, including by aligning the ELA framework with international best practice, and restrict budget financing to only exceptional needs and on a temporary basis. Attracting bank ownership participation by reputable banking groups and selling non-performing loans (NPLs) and banks' real estate portfolios to strategic investors would also support liquidity in the system.

A deep banking system restructuring is critical to restore its profitability and sustainability. Banks' capital shortfalls should be promptly addressed, following a fresh asset quality review and upfront loss-recognition while laws that allow banks to spread losses over time should be repealed. The CBSM should quickly intervene in undercapitalized banks that fail to raise capital while state support should be provided only to systemically-important and viable banks, following burden sharing. Reducing banks' high operating costs by rationalizing the oversized branch network and staffing levels, and increasing the share of income-generating assets, including by converting the tax credits into coupon-bearing assets, would improve their profitability. Accelerating NPL resolution by strengthening supervisory oversight and streamlining judicial procedures should support these efforts. Plans to establish an AMC should be carefully considered to avoid potential risks to public finances and delayed recognition of bank losses.

Strengthening the CBSM institutional framework and mitigating financial integrity risks would support financial stability. Bank supervisors need adequate resources and sufficient powers to monitor systemic risks, carry out frequent bank inspections, and promote compliance with regulations. Reviewing the CBSM law with a view to enhance its institutional and financial independence would increase its effectiveness as a supervisory authority. Continued efforts to strengthen the anti-money laundering framework, including in the context of the ongoing preparations of the second National Risk Assessment and Moneyval review, are welcome.

Undertaking a credible and ambitious fiscal consolidation and restricting state support to the banking system would safeguard public finances. Putting public debt on a downward and sustainable path requires an implementation of VAT and pension reforms along with measures to rationalize the tax exemptions, better target social benefits, and increase spending efficiency. Limiting state contributions to bank recapitalization is also necessary. The government's plan to access external markets and increase liquidity should take into account debt sustainability considerations and be accompanied by development of debt and cash management capacity.

Steps to remove supply-side bottlenecks and increase economic integration would promote sustained growth. Addressing the lingering distortions in the labor market and mitigating the skill mismatch are necessary to promote job seeking and efficient allocation of labor while improving the business climate and closing the infrastructure gaps would help attract foreign investment, boost productivity, and increase external competitiveness. Concluding the association agreement with the EU would simplify procedures for domestic firms and support their expansion into new markets.

Efforts to improve data reporting and provision should continue. San Marino’s adherence to the IMF’s e-GDDS is an important step in improving data dissemination. Further steps to improve data quality, coverage, and reporting frequency, including by allocating additional resources to the Statistical Office, would support policy-making process.

INTERNATIONAL MONETARY FUND

REPUBLIC OF SAN MARINO

March 24, 2020

STAFF REPORT FOR THE 2020 ARTICLE IV CONSULTATION—SUPPLEMENTARY INFORMATION

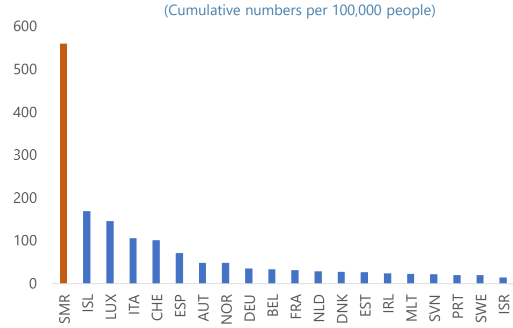
Prepared by | European Department (In consultation with other departments)

This supplement provides information that became available after the staff report was issued on March 9, 2020.

A. Developments Related to COVID-19

1. **San Marino has been severely hit by the Covid-19 outbreak.** As in other neighboring regions in Italy, the number of Covid-19 cases in San Marino has risen rapidly since mid-February, inflicting detrimental human and economic cost. As of March 23, 187 people have contracted the virus, resulting in 67 hospitalizations and 20 reported deaths. About 425 people are in active quarantine, including vital health and law enforcement personnel. With its small population (33,000), San Marino has become the country with the highest rate of infection and deaths per capita.

COVID-19 Confirmed Cases, Mar. 23, 2020
(Cumulative numbers per 100,000 people)



Sources: Johns Hopkins University; Haver Analytics; and IMF staff.

2. **The authorities moved quickly to implement containment measures.** The authorities adopted a first set of containment measures on March 8 by imposing a lockdown on the entire territory of San Marino, ordering schools, universities, and some public offices to close while allowing selected services to remain open, subject to some restrictions. These restrictions, which followed the Italian authorities' response to the outbreak, were further expanded by a March 14 Decree Law, which prohibited social gathering and events in public places and suspended all construction and retail activities except for essential services related to the provision of food and health. Moreover, other private businesses, including in the manufacturing sector, were required to reduce the number of active employees by 50 percent, and encourage employees to work from home where possible.

3. In addition, the authorities adopted a set of measures to provide economic relief. The supplemental wage mechanism for temporary lay-offs was expanded to include reduction of the workforce related to containment measures while payments of taxes, utility bills, sanctions and other administrative deadlines have been postponed, and wages of public sector employees have been temporary curtailed to re-direct more resources to the health sector. Some commercial banks have granted temporary suspension of existing mortgage and loan instalments to further support the liquidity of families and firms.

4. While the thrust of staff's appraisal remains unchanged, staff strongly supports the authorities' response to the ongoing health crisis. The authorities' near-term efforts are rightly focused on limiting and containing the adverse social and economic effects of the COVID-19 outbreak.

INTERNATIONAL MONETARY FUND

REPUBLIC OF SAN MARINO

STAFF REPORT FOR THE 2020 ARTICLE IV CONSULTATION

March 9, 2020

KEY ISSUES

The Staff Report was prepared by a staff team of the IMF for the Executive Board's consideration on March 27 on a lapse of time basis. The staff report reflects discussions with the Sammarinese authorities in January 2020 and is based on the information available as of January 31, 2020. It focuses on San Marino's near- and medium-term challenges and policy priorities and was prepared before COVID-19 became a global pandemic and resulted in unprecedented strains in global trade, commodity, and financial markets. It, therefore, does not reflect the implications of these developments and related policy priorities. The outbreak has greatly amplified uncertainty and downside risks around the outlook. Staff is closely monitoring the situation and will continue to work on assessing its impact and the related policy response in San Marino and globally.

Context: Banking system vulnerabilities pose considerable stability risks and hinder economic recovery. Significant deposit outflows have left the banking system with low liquidity, while persistent bank losses, poor asset quality, sizable capital shortfalls, led to multiple bank failures in recent years. Recent bank interventions largely relied on regulatory forbearance and state support, which widened fiscal deficits, eroded fiscal buffers, and increased the implicit public debt to unsustainable levels. The elevated risks, and a shared recognition that a broad coalition is critical to advance the necessary reforms, triggered snap elections in early-December—two years ahead of schedule—and the establishment of a four-party coalition government.

Outlook and risks: With no credible measures to restore banking system health and in the face of a continued weak external environment, economic growth is projected to remain subdued in the coming years. Slow progress in repairing the banking system and failure to restore fiscal sustainability are the key and material risks. The recent outbreak of COVID-19 in San Marino and Italy has significantly increased uncertainty.

Main policy recommendations: Urgently develop a stabilization plan that safeguards financial stability, restores fiscal sustainability, and removes supply-side bottlenecks to sustained growth:

- **Financial sector:** Safeguard the central bank's liquidity buffers and develop a credible strategy to secure banks' viability and sustainability through upfront loss recognition, recapitalization with burden sharing, deep restructuring with significant reduction in non-performing loans and operating costs, and improvement of financial sector governance and oversight.

- **Fiscal policy:** Put public finances on a sustainable path and gradually rebuild fiscal buffers, including by restricting state support to the banking system and implementing an ambitious fiscal adjustment that relies on both revenue and expenditure measures. Urgently reform the pension system and reduce fiscal risks through diversification of sovereign financing sources and enhancement of debt and cash management capacity.
- **Structural reforms:** Strengthen labor supply, including by further relaxing hiring of nonresidents, rationalizing the social benefits system, and mitigating skill mismatch. Further improve the business climate and address infrastructure gaps to advance economic integration.

Approved By
Mahmood Pradhan (EUR) and Yan Sun (SPR)

Discussions were held in San Marino on January 22–31, 2020. The team comprised Messrs. Klein (head), Dell'Erba, Muraki (all EUR), Kaffo (SPR), and Leonovich (MCM). Mr. Spadafora (OED) participated in the discussions. Mr. Pradhan (EUR) and Mr. Fanizza (OED) met with the authorities and attended some meetings. The team met with the heads of state, Secretary of State for Finance and Budget, Central Bank President, other cabinet members and central bank officials, private sector representatives, and social partners. Ms. Burova and Mr. Velazquez-Romero (both EUR) assisted the mission from headquarters.

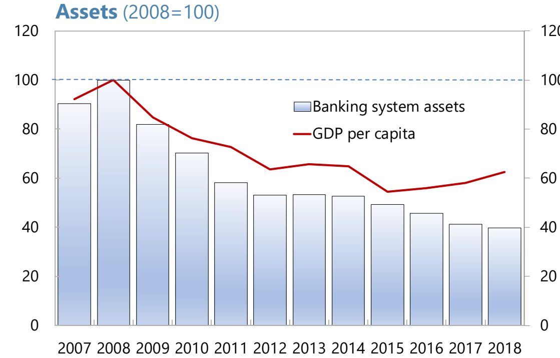
CONTENTS

ANNEXES

CONTEXT

1. **San Marino's economy experienced a deep contraction, from which it struggles to recover**. San Marino's offshore banking model, which largely benefitted from banking secrecy, collapsed due to enhanced transparency and anti-tax evasion measures. Bank balance sheets shrank significantly owing to sizable deposit outflows and deleveraging, while poor risk management resulted in a considerable deterioration of banks' asset quality and persistent losses. The financial contraction, coupled with feeble external demand, contributed to a deep and prolonged recession, from which the economy bottomed out in 2015. Yet, the recovery remained weak with GDP-per-capita well below its pre-crisis level.

San Marino: GDP Per Capita and Banking System Assets (2008=100)



Sources: WEO and IMF staff.

2. **Banking sector weaknesses threaten financial stability and fiscal sustainability.** The banking system's low liquidity, high non-performing loans (NPLs), and large recapitalization needs have left the banking system highly vulnerable to shocks while re-current state support to banks—though not properly recognized—led to persistent fiscal deficits and an increase of the implicit public debt to unsustainable levels. The weak fiscal position together with the lack of market access and limited central bank of San Marino's (CBSM) liquidity buffers significantly constrain the authorities' policy options if faced by adverse economic conditions.

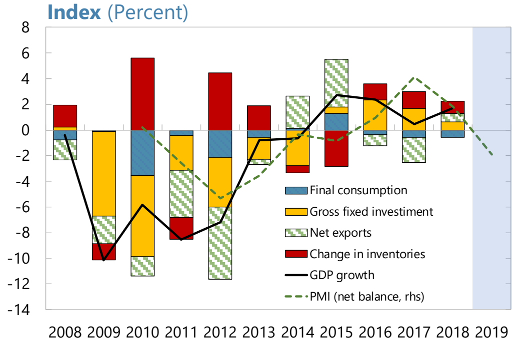
3. **A new government took office in early January with the goal of reviving economic activity.** The Christian Democrats emerged from December elections as the largest party and established a four-party coalition government. The coalition's platform centers on stimulating growth, including by developing technology-based sectors, improving the business environment, and adopting a national strategy for NPL resolution. Priority is also given to ensure public debt sustainability, including by containing current expenditure, modernizing public administration, and reforming the tax system.

RECENT DEVELOPMENTS AND POLICY PRIORITIES

4. **Economic activity remained subdued, keeping the unemployment rate elevated.** Real GDP growth accelerated to 1.7 percent in 2018 from 0.4 percent in 2017 as investment and net exports growth more than offset the contraction of consumption. For 2019, high frequency indicators are inconclusive: while exports of services remained strong and the number of enterprises grew following a prolonged contraction, employment growth, which was mostly driven by non-residents, decelerated up to September and increased only in the last quarter, imports growth moderated, and manufacturing Purchasing Managers Index further weakened. Unemployment rate modestly declined to 7.7 percent from 8 percent in 2018 but remained well above its pre-crisis

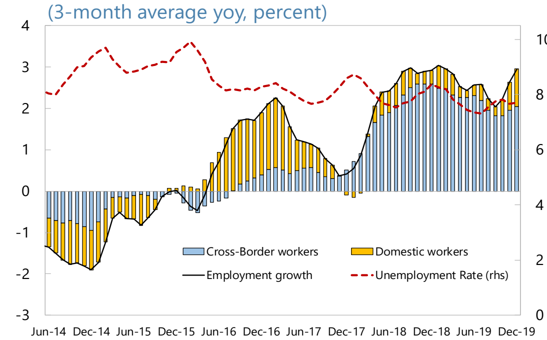
levels. Despite modest improvements in firms' repayment capacity—owing to prolonged deleveraging—the corporate sector remained largely vulnerable with low profitability and high leverage, thus weighing on economic recovery (Annex I).

Real GDP Growth and Purchasing Managers Index (Percent)



Sources: Sammarinese authorities and IMF staff.

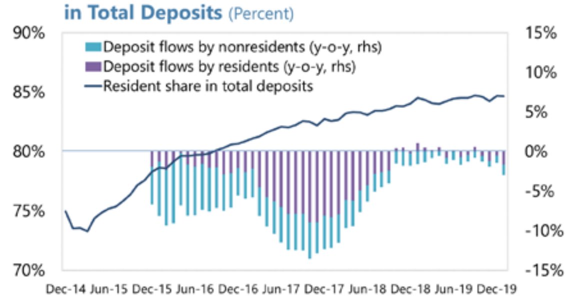
Unemployment Rate and Employment Growth (3-month average yoy, percent)



Sources: Sammarinese authorities and IMF.

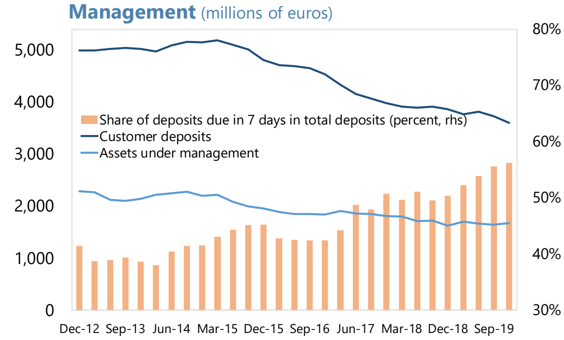
5. Banking system liquidity remained broadly stable in 2019, but at low levels. Bank deposits declined slightly in 2019 and they are now at about 30 percent below their 2014 level. Liquidity risks in the banking system are high as the share of short-term deposits (due in seven days) increased to more than half of total deposits, and seven-day liquidity coverage ratios remained at about 30 percent. CBSM reserves increased to €385 million at end-2019 from €223 million at end-2018, mainly due to a temporary shift of part of pension fund deposits from banks into the CBSM, CBSM's divestment of illiquid securities, and the sale of Delta sub-portfolio by the state-owned bank, Cassa di Risparmio della Repubblica di San Marino (CRSM), which contributed to an increase of its deposits at the CBSM. Nevertheless, CBSM's capacity to withstand sizable deposits withdrawals is still constrained as reserves remain inadequate (Annex II).

Deposit Flows by Residency and Resident Share in Total Deposits (Percent)



Note: Customer deposits include certificates of deposits (CDs). In 2019, deposit increases/decreases related to the sales of the Delta subportfolio, reallocation of pension fund deposits between banks and the CBSM, and Banca CIS resolution are excluded from deposit flow data.
Sources: Sammarinese authorities and IMF staff.

Banking System Deposits and Assets under Management (millions of euros)

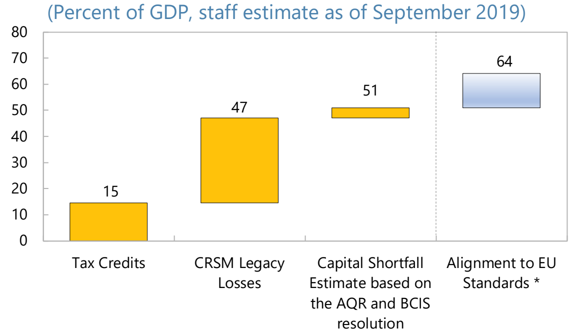


Note: Customer deposits include certificates of deposits (CDs).
Sources: Sammarinese authorities and IMF staff.

6. The banking system recapitalization needs are sizable, and the recent bank resolution suggests a potential underestimation. The estimated capital shortfalls, which are based on the 2017 Asset Quality Review (AQR) update, stand at 51 percent of GDP, and mostly concentrated in

CRSM, which, in 2017, the government committed to recapitalize gradually over 25 years. Banks were required to incorporate the AQR findings in their capital calculations for the 2019 financial statements and they are currently evaluating ways to address their capital shortfalls. However, with AQR results becoming outdated, there is a risk that the capital needs are under-estimated.

San Marino: Banking System Recapitalization Needs
(Percent of GDP, staff estimate as of September 2019)

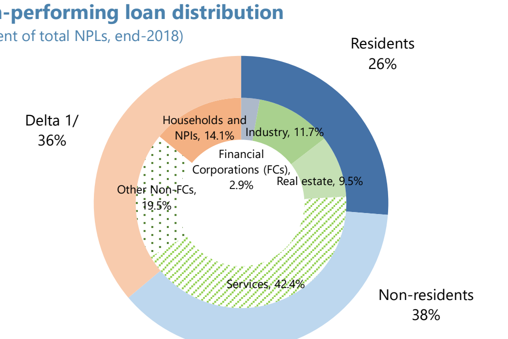


* Higher capital levels will be required under the application of the EU standards.
Sources: Sammarinese authorities and IMF staff.

7. A new bank resolution law was enacted and immediately applied to resolve a failed bank (Box 1). The law, which increases the CBSM's intervention powers, was adopted to support BCIS' resolution. While equity and a small part of uninsured deposits were written-off, the resolution of BCIS also entailed a bailout. The bank's insured deposits, pension fund deposits, a small portion of NPLs, and all performing loans were transferred to other entities, while the remaining structure—renamed as Banca Nazionale Sammarinese (BNS)—was nationalized and recapitalized by converting CBSM Emergency Liquidity Assistance (ELA) claims into equity. A new management team was appointed and the bank has retained its banking license. Nevertheless, BNS has recently halted banking operations and its business model is expected to be re-defined in the coming weeks as most of its assets are not generating income.

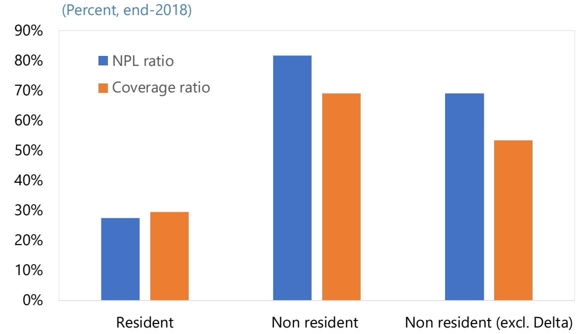
8. Banking system NPLs increased further, accounting for more than half of banks' total loans. The NPL ratio increased further to about 57 percent in November 2019 from 53 percent at end-2018, primarily due to reclassification of BCIS' loan portfolio during its resolution process. Yet, reported NPLs are understated as they do not include NPLs of failed banks that are kept off-balance sheet (in closed funds) and—considering the large volume of ageing NPLs and the significant difficulties in cross-border enforcement of collaterals—they are likely to be under-provisioned. The authorities are planning to speed up NPL resolution through stricter supervisory requirements and creation of an Asset Management Company (AMC) that will manage and recover NPLs.

Non-performing loan distribution
(precent of total NPLs, end-2018)



1/ Delta was an Italian financial company that was owned by CRSM, before liquidated due to anti-money laundering concerns.
Sources: Sammarenise authorities and IMF staff

NPL and Coverage Ratios by Residency/1
(Percent, end-2018)



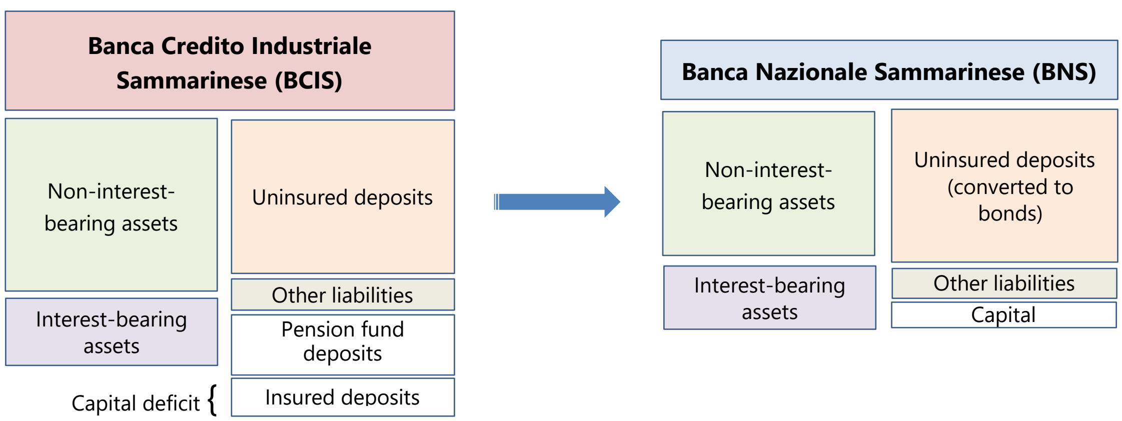
1/ NPLs figure indicates the pre-AQR ratio.
Source: Sammarinese authorities and IMF staff.

Box 1. The Bank Resolution Law and Its Application to BCIS

A bank resolution law was enacted in June 2019. Recognizing the limitations of the resolution regime, which only allowed liquidation of an insolvent bank, the authorities adopted a new framework, which significantly expanded their powers and tools to resolve failing banks. The new law provides the resolution authorities with early intervention powers against banks that suffer losses and do not have prospects of meeting the minimum capital requirements as well as the ability to transfer the assets and liabilities to third parties, establish a bridge institution, and provide state support. The new resolution law protects all but a limited category of uninsured deposits, thereby restricting the scope of bail-in on top of loss absorption by shareholders' equity, hybrid capital instruments, and subordinated debt. Protected uninsured deposits can be converted into senior bonds with longer maturity.

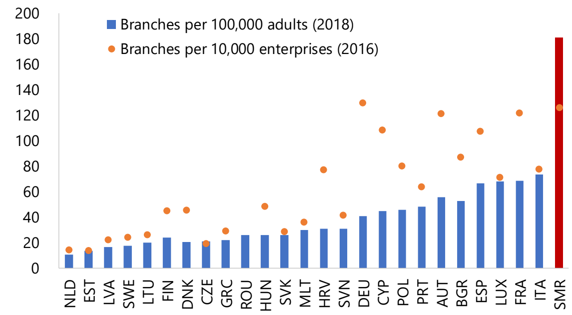
The failed BCIS was subsequently resolved. Shareholders' equity was wiped out and a small amount (estimated at €16 million) of uninsured deposits were written off. The remaining balance sheet was split into three parts, based on the liabilities' characteristics:

- Insured deposits were transferred to three private banks, along with performing loans and NPL fund ("Odisseo") shares.
- The capital shortfall and a small portion of the bank's NPL book were transferred to a newly-created public entity alongside pension funds' deposits (about €100 million, 7 percent of GDP), which the state committed to repay over a period of 8–10 years.
- The rest of the bank was nationalized and renamed as BNS. Its assets largely consist of NPLs and tax credits that do not generate income, while a high share of its liabilities are uninsured deposits that were converted into bonds to mitigate immediate liquidity pressures.



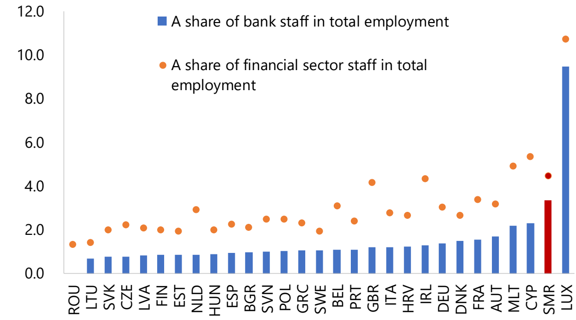
9. The banking system's unviable cost and income structure resulted in persistent losses. Owing to exceptionally high cost-to-income ratios, the banking system is estimated to have registered a loss in 2019—the tenth year in a row—reflecting sizable additional provisions made in BCIS resolution. Income generation continues to be constrained by a high share of non-income bearing assets such as NPLs and tax credits as well as limited fee and commission income, while high funding cost and large inefficiencies—partly reflecting the oversized branch network and high concentration of employment in the banking sector—keep the banks' costs elevated.

Number of branches per 100,000 adults and 10,000 enterprises



Sources: ECB, Eurostat, IMF Financial Access Survey, CBSM, and IMF staff

Share of bank and financial sector staff in total employment (Percent, 2018)



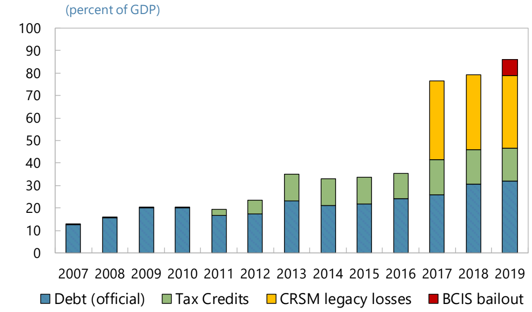
Sources: ECB, Eurostat, CBSM, and IMF staff

10. The fiscal position further weakened. The 2019 fiscal deficit is estimated at 2.5 percent of GDP—well above the balanced budget target—largely due to CRSM recapitalization for its 2018 loss and capital spending increase, which more than offset one-off revenue related to confiscation of money-laundering-suspected deposits. Government liquidity buffers stood at €32 million at end-2019, limiting its ability to repay its expiring CBSM loans (€55 million). The fiscal deficit and the BCIS bailout are projected to have increased the already unsustainable implicit public debt to 86 percent of GDP at end-2019 (Box 2).

Box 2. Public Debt: The Official vs. the Implicit Level

The official public debt—estimated at 32 percent of GDP at end-2019—does not fully report the entire fiscal liabilities. It excludes the government's commitment to cover CRSM's losses and repay pension funds' deposits following BCIS resolution, as well as the banking system tax credits, which were given to banks to cover the asset-liability gap when they absorbed failed ones. The overall size of the implicit fiscal liabilities amounts to about 54 percent of GDP, resulting in an implicit public debt of 86 percent of GDP:

Public Debt: Official and Implicit Levels
(percent of GDP)



Sources: Sammarinese authorities and IMF staff.

- **CRSM legacy losses**. In 2017, the government committed to amortize the CRSM legacy losses over 25 years. The remaining losses as of end-2019 stood at €455 million (32 percent of GDP).

- **Banking system tax credits**. They amount to €209 million (15 percent of GDP) and account for a significant part of banks' assets. Staff consider these tax credits as legitimate fiscal costs that need to be explicitly recognized as they are not realizable in the foreseeable future and are part of the bank recapitalization cost given their detrimental impact on banks' profitability and sustainability.

- **BCIS' pension fund deposits**. As part of the recent BCIS' bailout, the government committed to repay €100 million (7 percent of GDP) of pension fund deposits at BCIS over 8–10 years.

11. The external position is considered as weaker than implied by fundamentals and desired policy settings (Annex II). The 2019 current account balance is estimated to have shifted to a slight surplus of 0.7 percent of GDP from a deficit of 1.6 percent in 2018 as income balance improved, while preliminary estimates suggest that the net international investment position modestly decreased to 244 percent of GDP from 247 percent of GDP in 2018 as banks continued to liquidate foreign portfolio investment and further reduce their loan exposure to non-residents. The real effective exchange rate (REER) remained broadly stable in 2019, yet staff's analysis—which warrants caution given data weaknesses—points to an over-valuation.

OUTLOOK AND RISKS

12. Banking sector weaknesses are projected to continue to weigh on the economy. Staff's baseline assumes an unsustainable muddle-through scenario wherein banking sector vulnerabilities are not fully addressed, and financial and economic conditions gradually worsen. In this scenario, which also considers Italy's weak growth outlook, GDP growth is projected to decelerate over the medium term to around 0.5 percent, primarily reflecting lower investment growth and weaker net exports.[1] The current account is projected to remain broadly balanced, while inflation, which is largely driven by external prices, is set to slightly increase. Continued moderate capital outflows, including from the banking system, are projected to gradually drive CBSM's reserves down.

San Marino: Macro Projections 2018–25

		Projection						
	2018	2019	2020	2021	2022	2023	2024	2025
Activity and Prices (percentage change)								
Real GDP	1.7	1.1	0.7	0.8	0.7	0.6	0.5	0.5
Domestic demand	1.4	0.2	0.2	0.6	0.6	0.6	0.6	0.6
Final consumption	-1.0	-0.4	-0.2	0.1	0.1	0.1	0.1	0.1
Fixed investment	3.1	3.5	1.2	1.7	1.7	1.7	1.7	1.7
Exports	1.3	2.2	1.8	1.6	1.6	1.5	1.5	1.5
Imports	1.0	1.9	1.8	1.6	1.7	1.7	1.7	1.7
Employment (percent change)	2.4	2.6	1.0	0.8	0.7	0.3	0.3	0.2
Unemployment	8.0	7.7	7.8	7.8	7.8	7.8	7.8	7.8
Inflation rate (average)	1.8	1.0	1.2	1.4	1.5	1.6	1.6	1.6
Current account (percent of GDP)	-1.6	0.7	0.3	0.0	-0.1	-0.2	-0.1	-0.1

Sources: IMF; International Financial Statistics; Sammarinese authorities; and IMF staff.

13. The outlook is clouded by significant downside risks (Risk Assessment Matrix, Annex III). Given the CBSM's limited liquidity buffers, the key domestic risk is a resurgence of acute deposit outflows, which could increase liquidity pressures, disrupt the payment system, and undermine financial stability. An insufficient banking system restructuring would increase bank recovery costs over time, erode confidence, and further weaken financial intermediation with adverse growth implications. While households' debt is low and their NPLs account for only 14 percent of total NPLs, lower growth and a higher unemployment rate would exacerbate their vulnerability with negative feedback effects to the banking system. A full bank bailout by the government and a slow fiscal consolidation would amplify the already high fiscal risks, increase debt service payments, and crowd-out important productive spending. Weaker-than-expected growth in key trading partners and wider spread of COVID-19 in San Marino and Italy would have adverse effects on growth prospects through reduced flows of trade and tourism and lower consumption and investment, as well as fiscal costs of response to the virus.

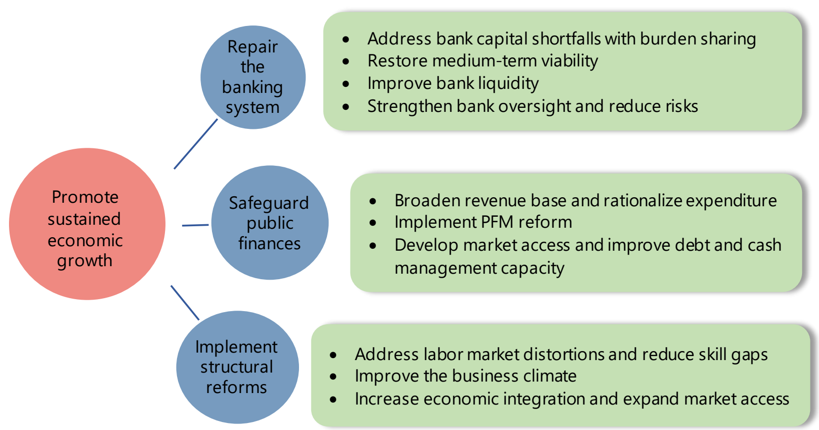
[1] The 2020 growth projection assumes that the COVID-19 outbreak will be contained in the first half of the year.

Authorities' Views

14. The authorities broadly concurred with staff's risk assessment and agreed that the current piecemeal approach to reforms is unsustainable. They shared staff's view on the need for a comprehensive strategy to restore the banking sector viability and re-establish trust as well as to safeguard public finances. They stressed the recent progress in enhancing supervisory powers and highlighted that the ongoing efforts to develop a stabilization plan would support financial stability. They acknowledged the fiscal risks emanating from a slow fiscal consolidation and underscored their intent to carryout fiscal reforms to contain future increases in public debt. The authorities were confident that structural reforms aimed at improving external competitiveness will promote exports and growth. Following the spread of the COVID-19 in San Marino and Italy, they noted plans to provide temporary support to hard-hit sectors, as needed.

POLICY AGENDA

15. San Marino's key challenges are to address banking sector vulnerabilities, safeguard public finances, and shift the economy to a high medium-term growth path. This requires a comprehensive strategy that restores banking system viability, including through upfront recapitalization and deep restructuring; reduces fiscal risks and ensures fiscal sustainability; and introduces structural reforms to strengthen the labor market as well as improve infrastructure and business climate.



A. Repairing the Banking System and Safeguarding Financial Stability

Addressing Capital Shortfalls and Improving Liquidity

16. Addressing banks' capital shortfalls is critical to enhance their resilience to shocks and improve confidence. The following measures should be implemented in sequence:

- **Upfront loss-recognition following a fresh AQR.** A new prudent AQR and solvency stress test should be carried out to quantify bank cleanup costs using loan classification and loss estimation that are consistent with international standards. Regulatory forbearance, including on capital calculations, should be avoided and laws that allow spreading losses over time be repealed.

- **Consolidation through resolution.** The CBSM should intervene in banks that fail to deliver a credible capital management plan. To restore viability and efficiency, resolved banks need to be consolidated by transferring the good assets into a bridge bank while leaving the non-core assets behind in a liquidation entity.

- **Recapitalization with burden sharing**. Given limited fiscal space, banks' recapitalization should involve burden sharing with a wider coverage than in the current bank resolution law. Only systemically-important and viable banks should receive restricted public support following agreement on a restructuring plan.

17. Increasing banking system liquidity and preserving CBSM liquidity buffers are critical to safeguard financial stability. Priority should be given to aligning the ELA framework with international best practice, including by restricting it to fully-collateralized loans to solvent banks, contingent on credible plans to repay loans at maturity. Limiting CBSM's budget financing to only exceptional needs and on a temporary basis is also essential. Attracting bank ownership participation by reputable banking groups and selling NPLs and banks' real estate assets portfolios to strategic investors would also support liquidity in the system.

Restoring Medium-Term Viability

18. San Marino's banking system requires deep restructuring to increase efficiency and restore profitability. The CBSM is currently reviewing banks' industrial plans to ensure that they contain credible measures to return to profitability. Priority should be given to reducing banks' high operating costs, including by rationalizing the oversized branch network and staffing levels, and increasing the share of income-generating assets, including through addressing CRSM's legacy losses and converting banking system tax credits into coupon-bearing assets (e.g. government bonds). The law that allows the volume of tax credits to increase as recoveries from NPLs of failed banks decline should be repealed as it introduces moral hazard and increases fiscal costs over time. Continued CBSM ownership of the newly-created BNS presents a significant conflict of interest and poses risks to CBSM's financial autonomy. Furthermore, BNS is currently unviable as a bank given that most of its assets do not generate income, thus its banking license needs to be quickly revoked, as currently envisaged.

19. Accelerating NPL resolution would also support these efforts. A speedy resolution of NPLs would reduce the significant burden on banks and, over the medium term, free up resources for new lending. The recent liberalization of the real estate market, removal of the cap on tax deductibility for loan-loss provisions, and the CBSM's ongoing efforts to set strict supervisory requirements on the adequacy of loan-loss provisioning, timeliness of write-offs, and development of decisive NPL reduction strategies are steps in the right direction. Streamlining the judicial processes with a view to expediting insolvency and enforcement procedures is also a priority.

20. Plans to establish an AMC to tackle banking system NPLs should be carefully considered given the potential risks involved (Box 3). The authorities are considering establishing a centralized vehicle for NPL resolution, possibly by transforming BNS into an AMC.

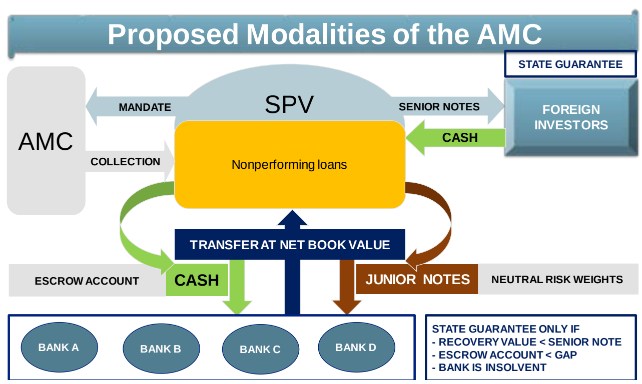
While the final modalities of the AMC are still being discussed with key stakeholders, the new entity is expected to manage and recover banking system NPLs that will be purchased—through a state-owned special purpose vehicle—at net book value, partly by issuing state-guaranteed senior bonds to foreign institutional investors. As not all the banks expressed an intention to offload the entirety of their NPLs to the vehicle, the effectiveness of the AMC remains unclear. Furthermore, sufficient write-downs on the NPLs by banks, preferably through a new AQR, and an application of a market-based transfer pricing are needed to reduce risks to public finances and delayed recognition of bank losses, while strong governance structure and a sunset clause for the AMC operations are critical to limit political interference and facilitate a speedy NPL recovery. In addition, the operating cost structure of the AMC, including managing servicing fee and interest payments to senior bonds, should be carefully weighed against their benefits as higher operating cost would inevitably reduce final payouts to banks. Involving foreign special servicers with the needed expertise and efficiency would help attract foreign NPL investors.

Box 3. The Proposed Asset Management Company (AMC)

The authorities are considering transforming BNS into an AMC to tackle the system-wide NPLs. While the timeline and final modalities are still under discussion, the key elements of the proposed AMC are:

- **Governance:** A Special Purpose Vehcile (SPV) that will be established for the securitization of the NPLs is assumed to be fully state-owned and managed locally by a Board of Directors appointed by the parliament. The AMC/BNS will be owned by local banks and tasked to manage and recover NPLs, potentially in partnership with a reputable foreign servicer.

- **Funding:** The SPV will be established to purchase NPLs from banks. The SPV will issue state-guaranteed senior bonds to foreign investors for funding.



Source: Central Bank of San Marino.

- **Transfer pricing:** The transfer of the NPLs will be at their net book value (NBV). The price will be paid to orginator banks partly by cash, received from the subscribers of the senior bonds, and partly by issuing junior bonds to the originating banks. A part of the cash will be kept in an escrow account, and be paid to the originator banks only at the expiration of the senior bonds.

- **Risk sharing hierarchy:** Cashflows of every individual NPL will be tracked and losses related to NPL recovery will be absorbed in the first instance by the junior bonds held by banks that sold the particular loss-making NPLs, and—if insufficient—by the reserves of the bank held in the escrow accounts, with potential additional contributions requested from the banks. The state is assumed to be the final backstop in case these measures are not sufficient to repay the senior bonds.

Strengthening Bank Oversight and Reducing Risks

21. Enhancing banking sector oversight and governance would help reduce financial stability risks. Steps are needed to enhance the CBSM’s crisis response capacity, including by overhauling lender-of-last-resort facilities and strengthening contingency plans. Moreover, financial sector regulators and supervisors, including for anti-money laundering (AML) and countering the financing of terrorism (CFT), need adequate resources and sufficient powers to monitor systemic risks, carry out regular bank inspections, and promote compliance with regulations. Plans to adopt a "Fit and Proper" regulation in the coming weeks would improve banks' corporate governance.

22. Strengthening CBSM' independence, decision-making structure, and resources is needed to support these efforts. Priority should be given to reviewing the CBSM law with a view of clarifying its mandate and responsibilities of decision-making bodies, as well as strengthening its institutional and financial independence, including by setting limits on government financing. Applying stronger eligibility and dismissal criteria to Governing Council members, enhancing their autonomy, and allocating more resources to supervisory activities are also critical.

23. Continuous efforts are needed to mitigate financial integrity risks. The authorities are continuing efforts to enhance financial integrity framework, including through conducting a second National Risk Assessment, rolling out AML/CFT inspections to designated non-financial professions and businesses as required under the Financial Action Task Force (FATF), legislating to address implementation of the targeted financial sanctions, and expanding corporate governance guidelines which include the voluntary establishment of AML committees by reporting entities. Concurrently, they are preparing for the Moneyval on-site visit, which will focus both on technical compliance and AML/CFT effectiveness. The authorities' risk-based supervision and inspection ultimately resulted in sizable seizure and confiscation of assets. However, allocating more human and financial resources to Financial Intelligence Agency and enhancing banks' customer due diligence and suspicious transaction reporting would support further reduction of financial integrity risks.

Authorities' Views

24. The authorities agreed that addressing vulnerability of the banking system is an utmost priority. They realized that a comprehensive strategy that includes bank recapitalization and restoration of profitability is critically needed and committed to developing such a strategy as soon as possible. The authorities underlined their ongoing efforts to enhance bank oversight, including by requiring banks to make an upfront capital deduction of the 2017 AQR findings and submit plausible business plans to return to profitability. The CBSM also stressed recent improvement of its liquidity position while agreeing that there is scope for further enhancing its liquidity buffers. The authorities expressed the importance of advancing the plan for establishing an AMC to remove and manage NPLs that are plaguing bank balance sheets. They committed to further strengthen the AML/CFT framework by developing an action plan that is based on the second national risk assessment.

B. Putting the Public Finances on a Sustainable Path

25. The 2020 budget deficit is set to widen significantly. The 2020 budget targets a deficit of 1.2 percent of GDP, excluding CRSM recapitalization for its 2019 loss and a partial repayment of pension fund deposits following BCIS' resolution. Considering these factors, and applying a more conservative revenue projection, staff project the 2020 fiscal deficit to double relative to the 2019 level and stand at 5 percent of GDP. With government's low liquidity buffers, the financing of the deficit will be challenging, especially given the heavy reliance on the domestic market.

San Marino: Fiscal Projections, 2018–25

Percent of GDP	2018	2019 Est.	Proj. 2020	2021	2022	2023	2024	2025
Revenues	23.0	21.6	20.2	19.9	20.0	20.1	20.1	20.1
Expenditures	24.5	24.1	25.3	25.2	25.2	25.4	25.3	25.3
of which bank support	3.1	2.3	2.2	2.0	1.8	1.6	1.5	1.3
Overall Balance	-1.6	-2.5	-5.0	-5.3	-5.1	-5.3	-5.2	-5.1
Primary Balance	-1.2	-2.1	-4.6	-4.6	-4.3	-4.4	-4.2	-4.0
Primary Balance, net of bank support	1.9	0.3	-2.4	-2.7	-2.5	-2.7	-2.7	-2.7
Public debt (official)	30.3	32.0	34.4	39.0	43.3	47.7	52.0	56.2
Implicit public debt /1	78.8	85.8	86.9	88.9	90.8	92.9	95.0	97.1

Source: IMF staff.

1/ Official public debt plus tax credits, CRSM legacy losses, and commitments related to BCIS resolution.

Medium-Term Fiscal Sustainability

26. Ensuring fiscal sustainability requires an ambitious adjustment strategy that is supported by burden sharing. An upfront loss-recognition and a full bank recapitalization by the state would increase public debt to about 87 percent of GDP in 2020, which would substantially increase financing risks given San Marino's lack of market access, low revenue base, and weak debt management capacity (Annex VI). Staff consider public debt of about 50 percent of GDP and government deposits covering at least two months of spending as adequate medium-term fiscal anchors that can be achieved by limiting state contributions to bank recapitalization and applying a frontloaded fiscal adjustment that would be sustained over the medium term. Specifically, staff consider increasing the primary fiscal surplus, net of bank support, to 2.5 percent of GDP from 0.3 percent of GDP in 2019 as a feasible adjustment that can be supported by both revenue and expenditure measures:[2]

- **Revenue:** Replacing the single-stage import tax with a VAT would support revenue mobilization, provided it is designed with sufficiently-high rates and limited exemptions and is implemented on a timeline that is consistent with the tax administration capacity.[3] Reforming the regressive consumption allowance and repealing the discounts on petroleum products and other wasteful rebates should also play a pivotal role in broadening the tax base and boosting revenue.

Proposed Fiscal Adjustment Relative to 2019 1/

% of GDP	2020-2025
Tax Increase	**1.5**
VAT	0.6
SMAC rebate	0.6
Petroleum rebate	0.3
Spending Cuts	**1.6**
Pension reform	0.6
Reduction in transfers to other government units	1.0
Total Net Adjustment 2/	2.2

1/ In net terms, cumulative

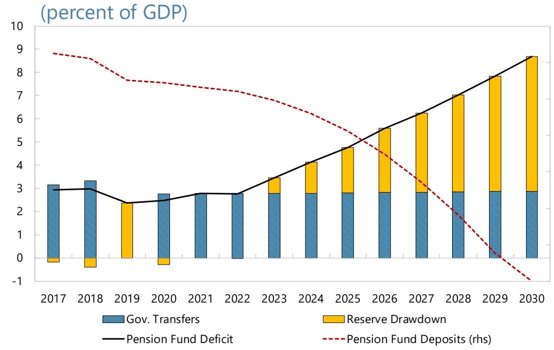
2/ Net of the impact of automatic stabilizers

[2] Additional measures would be needed to reverse the fiscal relaxation in 2020.

[3] The VAT modalities are under discussion, Staff recommended a three rates structure: a standard rate of 15 percent, with reduced rates of 10 percent for most services and 5 percent for food and other basic goods.

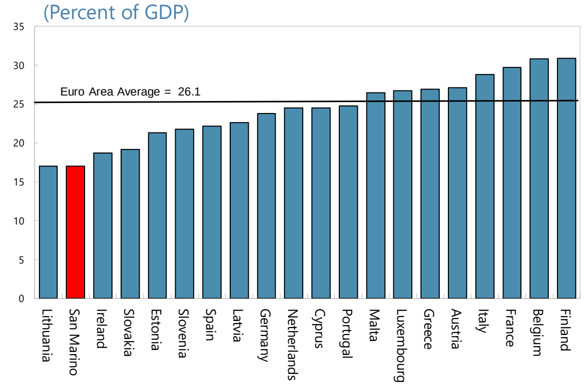
- **Expenditure:** The pension system is unsustainable and its annual deficit, currently at 2.5 percent of GDP, is projected to rapidly increase over the medium term on account of a rising old-age dependency ratio, thus further draining government resources and significantly reducing the pension funds' liquid assets.[4] Reforming the pension system by delaying retirement age, increasing contribution rates, and rationalizing existing benefits is urgently needed to reduce its systemic imbalance over time. Increasing spending efficiency by conducting spending reviews across public sector units and reforming the social safety-nets could yield further savings.

Estimated Pension Fund Deficit and Financing
(percent of GDP)



Sources: Sammarinese authorities and IMF staff.

Tax Revenue, 2018
(Percent of GDP)



Public Financial Management (PFM) Reforms

27. The authorities' plan to modernize their PFM framework and diversify financing options is welcome. The draft PFM law, which is currently discussed with key stakeholders, includes measures to unify and align public sector accounting framework to international standards while enhancing budget planning, management, reporting, and controls. The government is also considering diversifying financing sources to reduce its reliance on domestic investors and increase system-wide liquidity. To reduce fiscal risks, the government strategy to broaden financing sources should take into account debt sustainability and cost-risk considerations and be accompanied by development of debt and cash management capacity and a broad fiscal strategy. Given the limited resources, careful prioritization is needed.

Authorities' Views

28. The authorities agreed that fiscal reforms should complement banking system restructuring to achieve public debt sustainability. They agreed that both revenue and expenditure measures should contribute to fiscal consolidation. While supporting the introduction of the VAT, they noted the limited tax administration capacity as well as the need for a careful evaluation of its economic impact and considered implementation at mid-legislature as a realistic timeline. They also stressed that due to the structure of the Sammarinese economy, the VAT might not raise additional significant revenue, and saw scope to also reform the direct taxation system, including by rationalizing tax incentives. Additionally, they noted their intent to introduce e-

[4] See Annex VI, Staff Report for San Marino's 2019 Article IV Consultation. .

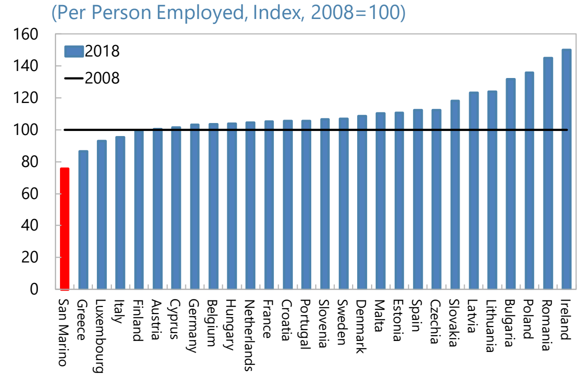
invoicing to boost tax collection. The authorities recognized that a pension reform is critical for fiscal consolidation given that the structural deficit of the pension fund is set to widen and noted that the dialogue with social parties has already started, though the final modalities have yet to be defined. They also argued that the planned public accounting reform would strengthen controls and increase digitalization of public sector services, thus increasing spending efficiency and reducing operating costs. While the system of social security has served the country well, the authorities saw scope to improve targeting of specific benefits and allow private sector participation in the provision of health services. Lastly, the authorities noted that tapping external markets would support liquidity and enhance their resilience to shocks.

C. Promoting Sustainable Growth

29. Structural reforms would strengthen external competitiveness, improve productivity, and promote sustained economic growth. Attention should be given to:

- **Labor market.** While labor markets have been partially liberalized, there are still lingering distortions, which hinder job search, prevent efficient allocation of labor, and undermine labor productivity growth (Annex IV). Further relaxing hiring processes, including of nonresidents, revisiting the supplemental wage for temporary layoffs, and rationalizing the duration of unemployment benefits would promote job seeking and unlock resources for high-productivity sectors. As finding of well-trained workforce is seen by many firms as a key challenge, revamping vocational training programs would help mitigate the skill mismatch and reduce the unemployment rate.

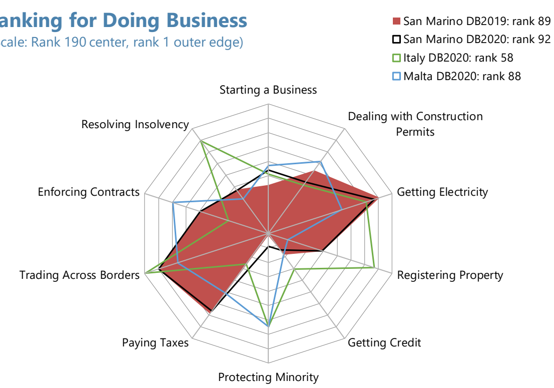
Real Labor Productivity, 2008 vs. 2018
(Per Person Employed, Index, 2008=100)



Sources: Eurostat and IMF staff.

- **Business climate.** San Marino' ranking (92 out of 190) in the World Bank's Doing Business is lagging many of its EU peers. While the authorities have advanced computerization, instituted self-certification, and reduced the number of permits required for certain procedures, further efforts are needed to support business environment, including in areas of starting a business, obtaining construction permits, protecting minority investors, and speeding up contract enforcement.

Ranking for Doing Business
(Scale: Rank 190 center, rank 1 outer edge)



Source: World Bank, Doing Business.

- **Economic integration.** Sustained efforts are needed to increase economic integration and expand market access, including by concluding the EU association agreement, which is expected to simplify procedures for domestic exporting firms. Investment in infrastructure, particularly in the areas of telecommunication and transportation, remains essential to allow firms to expand into higher value-added sectors.

Authorities' Views

30. The authorities broadly concurred with the importance of addressing structural bottlenecks to promote sustainable growth. They agreed that skill mismatch is a critical structural issue and expressed their intension to provide better trainings to residents, including by enhancing cooperation between universities and industries. They also emphasized the importance of attracting foreign investment and stressed their commitment to address infrastructure gaps and improve the ease of doing business, including through reducing red tape, expediting judicial processes, and streamlining regulations. The authorities reiterated their plans to conclude the Association Agreement with the EU, while also strengthening the relationship with Italy to further advance economic integration. Encouraged by recent positive trends in tourism, they are working to promote San Marino as an attractive tourism destination and are exploring ways to upgrade accommodations as well as hosting cultural events and conferences in partnership with the private sector.

DATA

31. Data reporting and provision have improved but more needs to be done. In 2018, the authorities started to produce balance of payment and IIP statistics annually and are making efforts to improve data dissemination, including by implementing the recommendations of the IMF's Enhanced General Data Dissemination System (e-GDDS) and publishing critical data through the National Summary Data Page in January 2020. While data provision is broadly adequate for surveillance, further steps to improve data quality, coverage, and reporting frequency, including by providing greater resources to the Statistical Office, would support policy-making process.

STAFF APPRAISAL

32. Banking sector weaknesses continue to pose stability risks and hinder economic recovery. Significant deposit outflows and weak risk management have left the banking system with low liquidity, poor asset quality, and considerable recapitalization needs, while multiple bank failures and continued state support to the banking system have eroded government liquidity buffers and led to an excessive and unsustainable accumulation of the implicit public debt. Absent a significant policy change, growth prospects are projected to remain subdued over the medium term with risks heavily tilted to the downside. The recent outbreak of COVID-19 in San Marino and Italy has significantly increased uncertainty. The external position is weaker than implied by fundamentals and desirable policy setting.

33. A comprehensive and credible stabilization plan is urgently needed. Shifting the economy to a higher medium-term growth path requires implementation of a coherent and credible strategy that restores banking system viability, ensures fiscal sustainability, and addresses structural impediments. The recent general elections and establishment of a four-party coalition government provides an opportunity to build a broad consensus for the necessary reforms.

34. Sustained efforts are needed to increase banking system liquidity and boost CBSM reserves. The CBSM should further enhance its liquidity management, including by aligning the ELA framework with international best practice, and restrict budget financing to only exceptional needs and on a temporary basis. Attracting bank ownership participation by reputable banking groups and selling non-performing loans (NPLs) and banks' real estate portfolios to strategic investors would also support liquidity in the system.

35. A deep banking system restructuring is critical to restore its profitability and sustainability. Banks' capital shortfalls should be promptly addressed, following a fresh asset quality review and upfront loss-recognition while laws that allow banks to spread losses over time should be repealed. The CBSM should quickly intervene in undercapitalized banks that fail to raise capital while state support should be provided only to systemically-important and viable banks, following burden sharing. Reducing banks' high operating costs by rationalizing the oversized branch network and staffing levels, and increasing the share of income-generating assets, including by converting the tax credits into coupon-bearing assets, would improve their profitability. Accelerating NPL resolution by strengthening supervisory oversight and streamlining judicial procedures should support these efforts. Plans to establish an AMC should be carefully considered to avoid potential risks to public finances and delayed recognition of bank losses.

36. Strengthening the CBSM institutional framework and mitigating financial integrity risks would support financial stability. Bank supervisors need adequate resources and sufficient powers to monitor systemic risks, carry out frequent bank inspections, and promote compliance with regulations. Reviewing the CBSM law with a view to enhance its institutional and financial independence would increase its effectiveness as a supervisory authority. Continued efforts to strengthen the anti-money laundering framework, including in the context of the ongoing preparations of the second National Risk Assessment and Moneyval review, are welcome.

37. Undertaking a credible and ambitious fiscal consolidation and restricting state support to the banking system would safeguard public finances. Putting public debt on a downward and sustainable path requires an implementation of VAT and pension reforms along with measures to rationalize the tax exemptions, better target social benefits, and increase spending efficiency. Limiting state contributions to bank recapitalization is also necessary. The government's plan to access external markets and increase liquidity should take into account debt sustainability considerations and be accompanied by development of debt and cash management capacity.

38. Steps to remove supply-side bottlenecks and increase economic integration would promote sustained growth. Addressing the lingering distortions in the labor market and mitigating the skill mismatch are necessary to promote job seeking and efficient allocation of labor while improving the business climate and closing the infrastructure gaps would help attract foreign investment, boost productivity, and increase external competitiveness. Concluding the association agreement with the EU would simplify procedures for domestic firms and support their expansion into new markets.

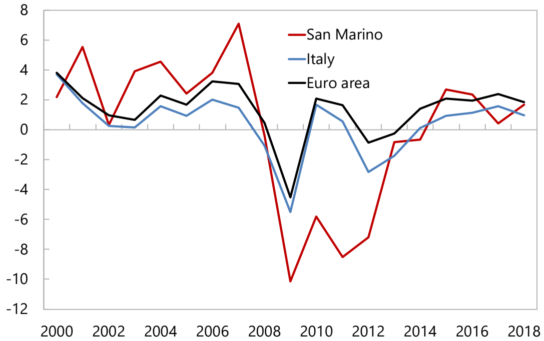
39. Efforts to improve data reporting and provision should continue. San Marino's adherence to the IMF's e-GDDS is an important step in improving data dissemination. Further steps to improve data quality, coverage, and reporting frequency, including by allocating additional resources to the Statistical Office, would support policy-making process.

40. Staff propose that the next Article IV consultation with the Republic of San Marino follows a standard 12-month cycle.

Figure 1. San Marino: Macroeconomic Developments

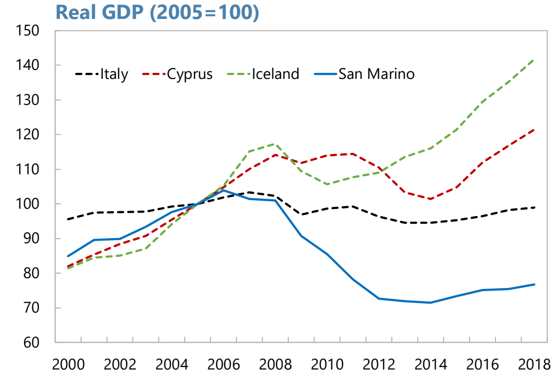
Economic activity has recovered from a prolonged and deep recession…

Real GDP Growth (Percent)



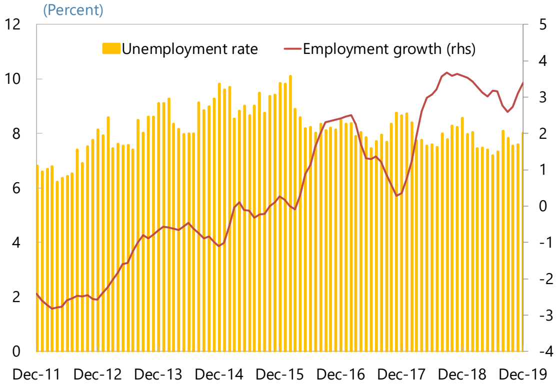
…yet real GDP remains well below its pre-crisis levels.

Real GDP (2005=100)



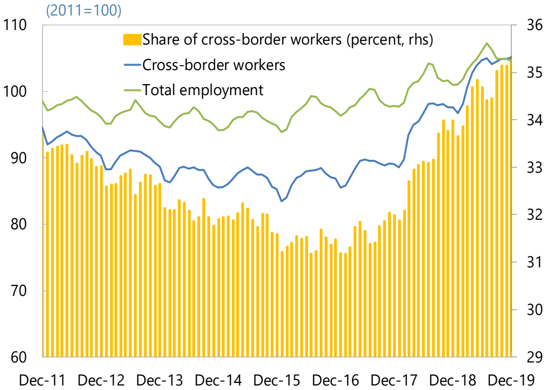
Unemployment rate remained elevated at just below 8 percent despite recent increases of employment, …

Unemployment Rate and Employment Growth
(Percent)



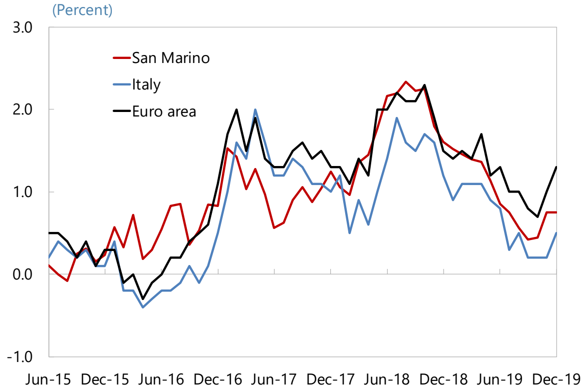
…which largely reflect a rising share of cross-border workers

Employment and Cross Border Workers
(2011=100)



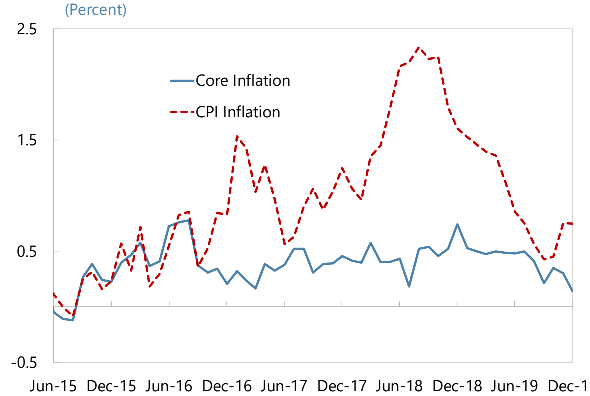
Headline inflation increased in the last quarter of 2019 following a deceleration in previous quarters…

CPI Inflation
(Percent)



…while core inflation further declined.

CPI and Core Inflation
(Percent)

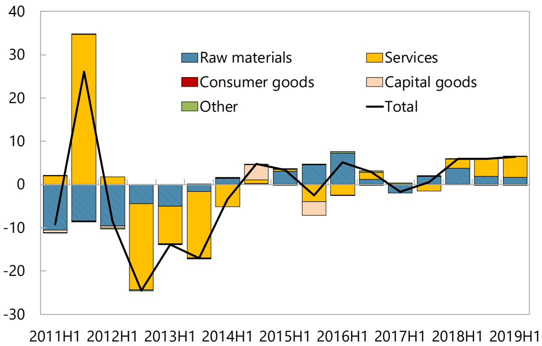


Source: World Economic Outlook, Sammarinese authorities, and IMF staff.

Figure 2. San Marino: High Frequency Indicators

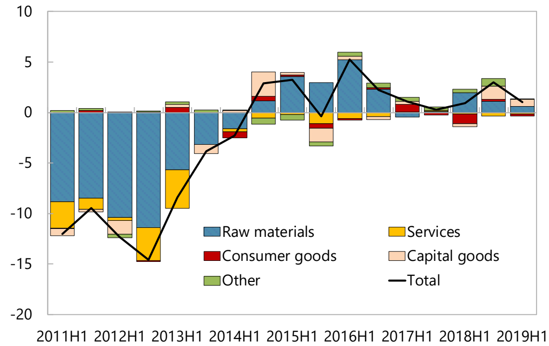
Exports growth remained strong as exports of services increased…

Exports: Contribution to Growth
(Percent)



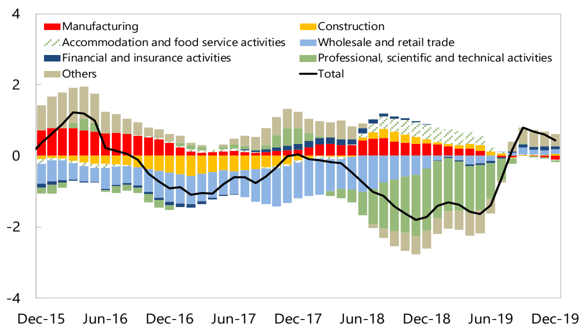
…While imports growth moderated, partly due to lower growth of capital goods and raw materials

Imports: Contribution to Growth
(Percent)



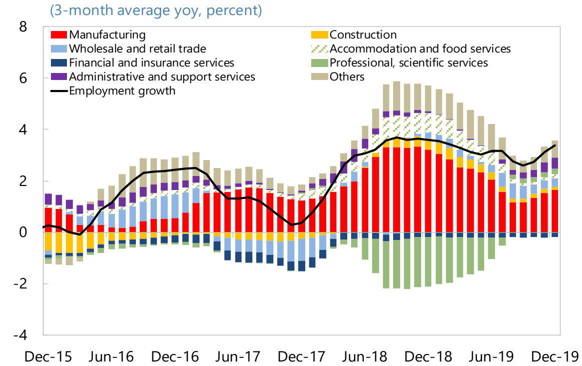
The number of enterprises slightly increased following a prolonged contraction

Number of Enterprises
(Percent, contribution to growth in 3-month average)



Employment growth was largely driven by manufacturing

Sectoral Contributions to Private Employment Growth
(3-month average yoy, percent)

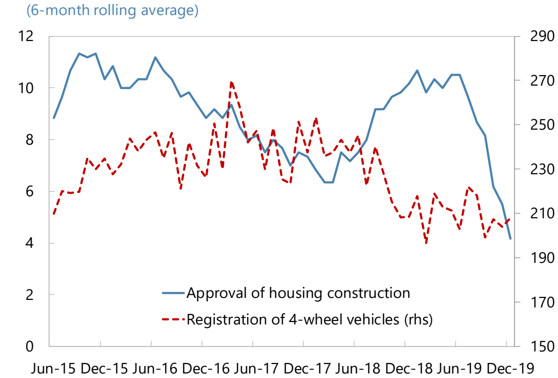


Tourism arrivals and hotel stays rebounded strongly at end-2019, though exhibiting a highly volatile growth

Tourism
(yoy growth rate in 3-month average)

Approvals of housing construction declined sharply while car registration remained broadly stable

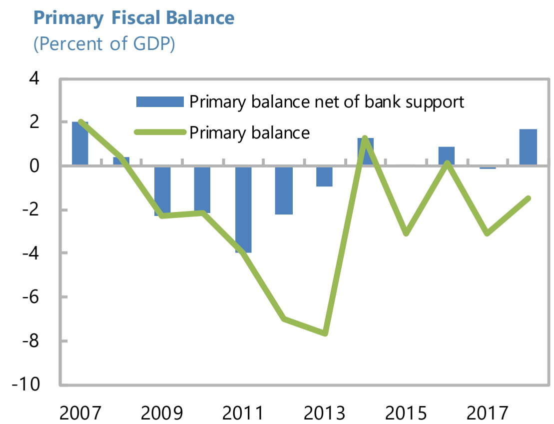
Housing and Durable Consumption
(6-month rolling average)



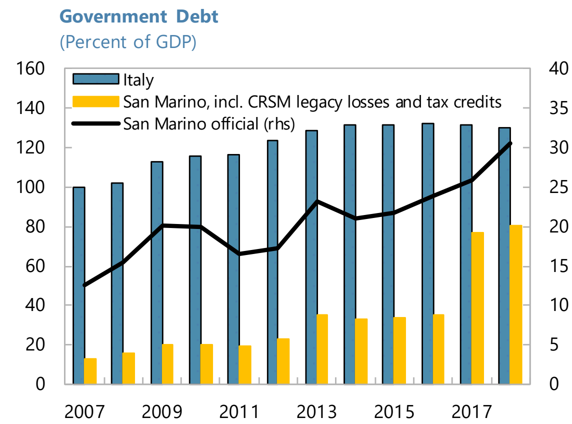
Source: Sammarinese authorities and IMF staff.

Figure 3. San Marino: Fiscal Developments

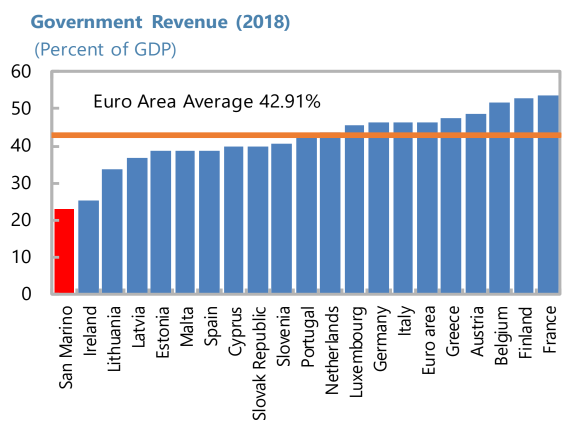
Public interventions in the banking sector have contributed to a deterioration of the primary fiscal balance...



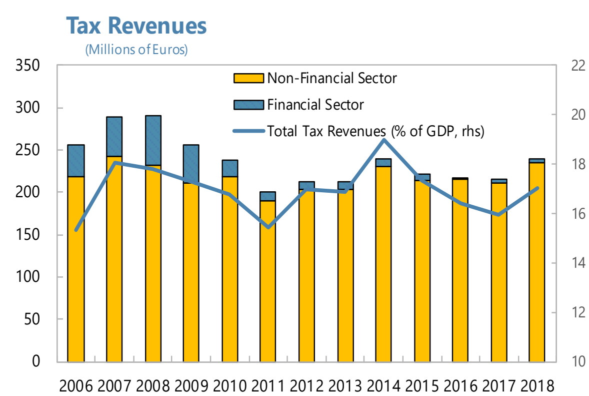
...resulting in a rapid increase in public debt, from a low level



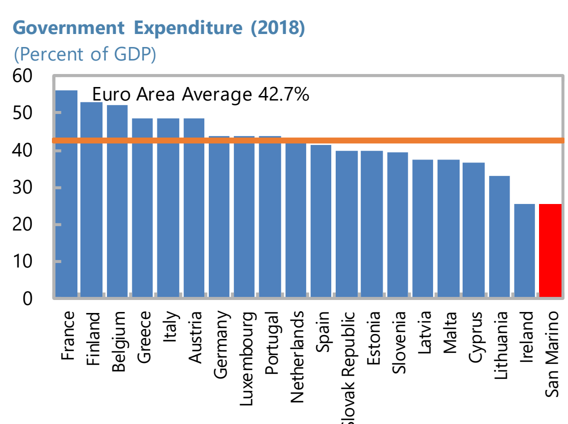
Government revenues are below euro area average...



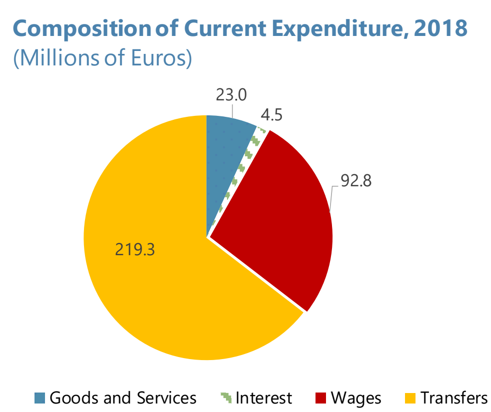
...while tax revenue losses from the financial sector have been significant



While the size of government is small...



... spending is rigid, and mostly on social transfers and wages.

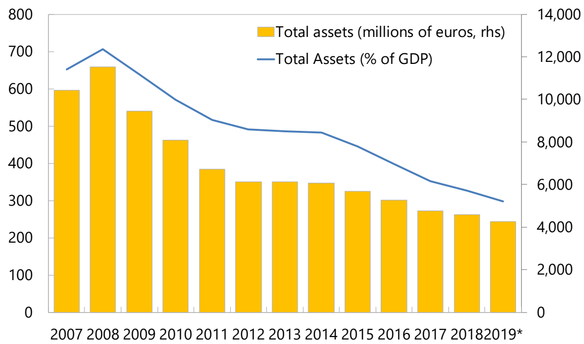


Source: Sammarinese authorities and IMF staff.

Figure 4. San Marino: Financial Sector

Downsizing of the Sammarinese banking sector has continued since the global financial crisis….

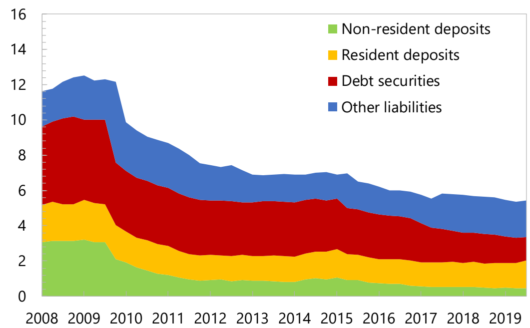
Banking System Assets



*As of Nov 2019.

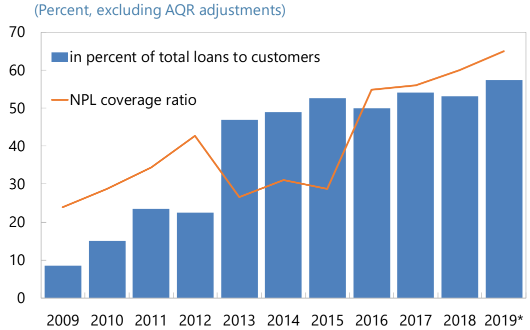
…due to outflows of deposits and certificates of deposit (CDs), largely by non-residents

Banking System Funding
(Billions of euros)



NPLs continue to be high, and the loan provision coverage is likely insufficient given a large volume of ageing NPLs

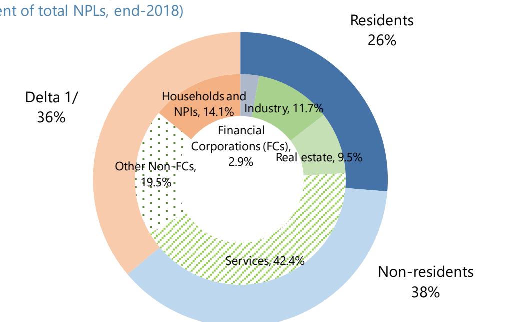
Banking Sector's Non-Performing Loans
(Percent, excluding AQR adjustments)



*As of Nov 2019. 2019 Nov data reflected the adjustments made related to Banca CIS resolution.

NPLs are distributed more towards non-residents and service sector

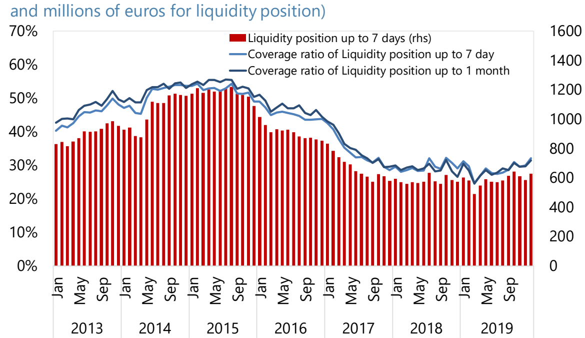
Non-performing loan distribution
(precent of total NPLs, end-2018)



1/ Delta was an Italian financial company that was owned by CRSM, before liquidated due to anti-money laundering concerns.
Sources: Sammarenise authorities and IMF staff

Liquidity situation has deteriorated since 2015 due to deepening banking sector uncertainties

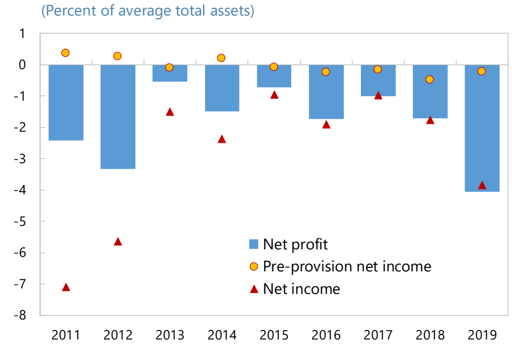
Banking Sector Liquidity (percent for coverage ratios and millions of euros for liquidity position)



Note: Coverage ratios are liquid position (liquid assets plus net interbank loans up to 7 days/1 month) as a share of customer deposits and financial instruments up to 7 days/1 month.

Banks continue to report losses, reflecting high operational cost and high NPLs

Banking Sector's Profitability
(Percent of average total assets)



*As of Nov 2019. The 2019 Nov data include losses made by the failed Banca CIS.

Source: Sammarinese authorities and IMF staff.

Table 1. San Marino: Selected Economic and Social Indicators, 2017–25

GDP per capita (2018): 45,670 U.S. dollars — Life expectancy at birth (2018): 86.6 years
Population (2018): 33,419 persons — Literacy, adult (2015): 96 percent

	2017	2018	2019	2020	2021	2022	2023	2024	2025
			Projection						
Activity and Prices									
Real GDP (percent change)	0.4	1.7	1.1	0.7	0.8	0.7	0.6	0.5	0.5
Domestic demand	3.2	1.4	0.2	0.2	0.6	0.6	0.6	0.6	0.6
Final consumption	-1.0	-1.0	-0.4	-0.2	0.1	0.1	0.1	0.1	0.1
Fixed investment	8.8	3.1	3.5	1.2	1.7	1.7	1.7	1.7	1.7
Net exports	-2.0	0.6	0.9	0.6	0.4	0.3	0.1	0.1	0.0
Exports	-1.2	1.3	2.2	1.8	1.6	1.6	1.5	1.5	1.5
Imports	-0.1	1.0	1.9	1.8	1.6	1.7	1.7	1.7	1.7
Contribution to GDP	0.4	1.7	1.1	0.7	0.8	0.7	0.6	0.5	0.5
Domestic demand	1.3	0.1	0.6	0.1	0.4	0.4	0.4	0.4	0.4
Final consumption	-0.6	-0.5	-0.2	-0.1	0.1	0.1	0.1	0.1	0.1
Fixed investment	1.8	0.7	0.8	0.2	0.4	0.4	0.4	0.4	0.4
Inventories	1.0	0.9	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Net exports	-1.8	0.6	0.9	0.6	0.4	0.3	0.1	0.1	0.0
Employment (percent change)	1.1	2.4	2.6	1.0	0.8	0.7	0.3	0.3	0.2
Unemployment rate (average; percent)	8.1	8.0	7.7	7.8	7.8	7.8	7.8	7.8	7.8
Inflation rate (average; percent)	1.0	1.8	1.0	1.2	1.4	1.5	1.6	1.6	1.6
Nominal GDP (millions of euros)	1353.1	1401.7	1430.3	1457.6	1490.9	1523.8	1556.1	1587.8	1619.4
Public Finances (percent of GDP) 1/									
Revenues	22.3	23.0	21.6	20.2	19.9	20.0	20.1	20.1	20.1
Expenditure	25.7	24.5	24.1	25.3	25.2	25.2	25.4	25.3	25.3
Overall balance	-3.4	-1.6	-2.5	-5.0	-5.3	-5.1	-5.3	-5.2	-5.1
Government debt (official)	25.9	30.3	32.0	34.4	39.0	43.3	47.7	52.0	56.2
Implicit public debt /2	76.6	78.8	85.8	86.9	88.9	90.8	92.9	95.0	97.1
Money and Credit 3/									
Deposits (percent change)	3.3	1.3	4.2	...	...	...	...	...	...
Private sector credit (percent change)	1.1	-7.0	-3.1	...	...	...	...	...	...
Net foreign assets (percent of GDP)	138.1	125.0	121.8	...	...	...	...	...	...
Commercial banks	117.8	105.7	92.5	...	...	...	...	...	...
Central bank	20.3	19.3	29.4	...	...	...	...	...	...
External Accounts (percent of GDP)									
Current Account	-0.1	-1.6	0.7	0.3	0.0	-0.1	-0.2	-0.1	-0.1
Exports	159.5	161.2	161.1	160.0	159.5	159.4	159.4	159.5	160.1
Imports	151.8	153.3	153.3	153.5	153.5	153.5	153.5	153.5	153.9
Gross international reserves (millions of euros)	252.7	248.1	410.6	...	...	...	...	...	...
Financial Soundness Indicators (percent) 4/									
Regulatory capital to risk-weighted assets	13.7	12.3	9.2	...	...	...	...	...	...
NPL ratio 5/	54.0	53.0	57.4	...	...	...	...	...	...
NPL coverage ratio 5/	56.0	59.9	65.0	...	...	...	...	...	...
Return on equity (ROE)	-10.1	-16.1	-79.3	...	...	...	...	...	...
Liquid assets to total assets	18.6	22.8	19.4	...	...	...	...	...	...
Liquid assets to short-term liabilities	33.3	41.2	32.8	...	...	...	...	...	...

Sources: International Financial Statistics; IMF Financial Soundness Indicators; Sammarinese authorities; World Bank; and IMF staff.
1/ For the central government.
2/ Official public debt plus tax credits, CRSM legacy losses, and commitments related to BCIS resolution.
3/ 2019 data are as of Sept 2019.
4/ 2017-19 data do not reflect 2017 AQR results. Latest NPL ratio and NPL coverage ratio are as of Nov 2019 and the others are as of Sept 2019.
5/ CBSM supervisory data. Latest data reflect changes related to Banca CIS resolution. Supervisory data, as opposed to FSI data, reflect retrospective revisions made by banks in their annual financial statements. Loans and NPLs to banks are excluded in calculating each indicator.

Table 2a. San Marino: Statement of Operations for Budgetary Central Government, 2017–25

(Millions of euros)

						Proj.			
	2017	2018	2019	2020	2021	2022	2023	2024	2025
Revenue	302.1	321.7	309.6	295.1	297.1	305.2	313.3	319.8	326.2
Taxes	215.4	239.0	222.2	228.4	228.8	235.5	242.1	247.1	252.0
Income Taxes	112.8	126.8	117.5	119.7	117.3	119.9	122.5	125.0	127.4
Non-income taxes	102.6	112.1	104.7	108.7	111.5	115.5	119.6	122.1	124.6
Taxes on international trade	66.3	56.7	64.8	68.0	69.9	73.0	76.2	77.9	79.4
Other taxes	36.3	55.5	39.9	40.7	41.6	42.5	43.4	44.3	45.2
Non-tax revenue	86.6	82.7	87.5	66.7	68.2	69.8	71.2	72.7	74.1
Expenditure	347.7	343.5	345.1	368.7	376.2	383.3	395.1	402.3	409.1
Current Expenditure	345.5	340.9	324.9	365.7	373.1	380.2	391.9	399.0	405.8
Compensation of employees	94.8	92.8	95.0	96.8	99.0	101.2	103.4	105.5	107.6
Use of goods and services	26.1	23.0	25.9	26.4	27.0	27.6	28.1	28.7	29.3
Interest	4.0	4.5	5.6	7.1	10.0	11.9	13.6	15.9	17.8
Transfers	217.4	217.4	194.1	231.1	232.9	235.1	242.3	244.4	246.5
To other general government units	148.7	154.9	139.7	177.4	181.2	185.0	193.7	197.3	200.9
To the banking sector	40.0	44.1	33.5	31.5	29.5	27.5	25.5	23.5	21.5
To other private sector entities	28.8	18.4	20.9	22.3	22.2	22.7	23.2	23.6	24.1
Other expenses (including subsidies)	3.2	3.1	4.2	4.3	4.3	4.4	4.4	4.5	4.6
Net acquisition of non-financial assets	2.2	2.6	20.3	3.0	3.1	3.1	3.2	3.3	3.3
Overall Balance	-45.7	-21.8	-35.5	-73.6	-79.1	-78.1	-81.8	-82.5	-83.0
Memorandum items									
Pension Funds Balance (net of gov. transfers)	-35.9	-43.9	...	...	...	...	...	...	...
Primary Balance	-41.7	-17.3	-29.9	-66.5	-69.1	-66.2	-68.2	-66.6	-65.2
Primary Balance net of bank support	-1.7	26.9	3.6	-35.0	-39.6	-38.7	-42.7	-43.1	-43.7
Public debt (official)	351.1	425.0	458.0	501.9	581.1	659.7	742.3	826.0	910.6
Implicit public debt /1	1037.1	1104.1	1226.5	1266.2	1325.1	1383.5	1445.5	1508.9	1573.0
Nominal GDP (in millions of euros)	1353.1	1401.7	1430.3	1457.6	1490.9	1523.8	1556.1	1587.8	1619.4

Sources: Sammarinese authorities; and IMF staff.

1/ Official public debt plus tax credits, CRSM legacy losses, and commitments related to BCIS resolution.

Table 2b. San Marino: Statement of Operations for Budgetary Central Government, 2017–25

(Percent of GDP)

						Proj.			
	2017	2018	2019	2020	2021	2022	2023	2024	2025
Revenue	22.3	23.0	21.6	20.2	19.9	20.0	20.1	20.1	20.1
Taxes	15.9	17.0	15.5	15.7	15.3	15.5	15.6	15.6	15.6
Income Taxes	8.3	9.0	8.2	8.2	7.9	7.9	7.9	7.9	7.9
Non-income taxes	7.6	8.0	7.3	7.5	7.5	7.6	7.7	7.7	7.7
Taxes on international trade and transactions	4.9	4.0	4.5	4.7	4.7	4.8	4.9	4.9	4.9
Other taxes	2.7	4.0	2.8	2.8	2.8	2.8	2.8	2.8	2.8
Non-tax revenue	6.4	5.9	6.1	4.6	4.6	4.6	4.6	4.6	4.6
Expenditure	25.7	24.5	24.1	25.3	25.2	25.2	25.4	25.3	25.3
Current Expenditure	25.5	24.3	22.7	25.1	25.0	25.0	25.2	25.1	25.1
Compensation of employees	7.0	6.6	6.6	6.6	6.6	6.6	6.6	6.6	6.6
Use of goods and services	1.9	1.6	1.8	1.8	1.8	1.8	1.8	1.8	1.8
Interest	0.3	0.3	0.4	0.5	0.7	0.8	0.9	1.0	1.1
Transfers	16.1	15.5	13.6	15.9	15.6	15.4	15.6	15.4	15.2
To other general government units	11.0	11.1	9.8	12.2	12.2	12.1	12.4	12.4	12.4
To the banking sector	3.0	3.1	2.3	2.2	2.0	1.8	1.6	1.5	1.3
To other private sector entities	2.1	1.3	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Other expenses (including subsidies)	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Net acquisition of non-financial assets	0.2	0.2	1.4	0.2	0.2	0.2	0.2	0.2	0.2
Overall Balance	-3.4	-1.6	-2.5	-5.0	-5.3	-5.1	-5.3	-5.2	-5.1
Memorandum items									
Pension Funds Balance (net of gov. transfers)	-2.7	-3.1	...	...	...	...	...	...	...
Primary Balance	-3.1	-1.2	-2.1	-4.6	-4.6	-4.3	-4.4	-4.2	-4.0
Primary Balance net of bank support	-0.1	1.9	0.3	-2.4	-2.7	-2.5	-2.7	-2.7	-2.7
Public debt (official)	25.9	30.3	32.0	34.4	39.0	43.3	47.7	52.0	56.2
Implicit public debt /1	76.6	78.8	85.8	86.9	88.9	90.8	92.9	95.0	97.1
Nominal GDP (in millions of euros)	1353.1	1401.7	1430.3	1457.6	1490.9	1523.8	1556.1	1587.8	1619.4

Sources: Sammarinese authorities; and IMF staff.

1/ Official public debt plus tax credits, CRSM legacy losses, and commitments related to BCIS resolution.

Table 3. San Marino: Balance of Payments, 2017–25

	2017	2018	2019	2020	2021	2022	2023	2024	2025
		Est.	Projections						
	(In millions of euros)								
Current account balance	-0.8	-22.2	10.0	4.9	0.0	-2.3	-3.5	-1.6	-1.2
Balance of goods and services	104.9	109.8	112.2	95.2	90.4	90.1	92.6	95.6	100.2
Goods balance	117.4	142.4	126.3	115.7	113.9	114.7	117.6	120.8	125.3
Exports	1,581.5	1,638.7	1,687.6	1,709.9	1,742.1	1,778.9	1,816.9	1,854.7	1,898.8
Imports	1,464.1	1,496.3	1,561.4	1,594.2	1,628.2	1,664.2	1,699.4	1,734.0	1,773.4
Services balance	-12.6	-32.7	-14.1	-20.5	-23.5	-24.6	-25.0	-25.2	-25.1
Exports	577.2	620.3	616.7	622.5	636.6	650.0	663.9	677.7	693.8
Imports	589.8	653.0	630.8	643.0	660.1	674.6	688.9	703.0	719.0
Primary income balance	-95.2	-121.0	-92.8	-80.7	-80.3	-81.8	-85.1	-85.7	-89.5
Credit	99.9	100.5	101.8	101.7	101.6	101.5	101.4	101.3	101.2
Debit	195.1	221.5	194.7	182.4	181.9	183.3	186.5	186.9	190.7
Secondary income balance	-10.5	-11.0	-9.3	-9.7	-10.1	-10.6	-11.0	-11.5	-11.9
Capital account balance	3.1	3.0	18.0	3.1	3.2	3.2	3.3	3.4	3.5
Financial account balance	-15.2	-1.1	29.6	7.9	3.5	1.3	0.2	2.1	2.2
Direct investments	-26.6	8.5	6.4	7.0	7.0	7.6	6.3	7.0	7.6
Portfolio investments	22.2	-29.7	-113.9	3.1	4.7	6.2	6.1	3.1	0.8
Other investments	116.6	24.7	-25.4	12.8	6.8	2.5	2.7	7.0	7.8
Change in reserve assets (increase = +)	-127.5	-4.6	162.5	-15.0	-15.0	-15.0	-15.0	-15.0	-14.0
Net errors and omisions	-17.6	18.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	(In percent of GDP)								
Current account balance	-0.1	-1.6	0.7	0.3	0.0	-0.2	-0.2	-0.1	-0.1
Balance of goods and services	7.8	7.8	7.8	6.5	6.1	5.9	5.9	6.0	6.3
Goods balance	8.7	10.2	8.8	7.9	7.6	7.5	7.6	7.6	7.9
Exports	116.9	116.9	118.0	117.3	116.8	116.7	116.8	116.8	119.6
Imports	108.2	106.7	109.2	109.4	109.2	109.2	109.2	109.2	111.7
Services balance	-0.9	-2.3	-1.0	-1.4	-1.6	-1.6	-1.6	-1.6	-1.6
Exports	42.7	44.3	43.1	42.7	42.7	42.7	42.7	42.7	43.7
Imports	43.6	46.6	44.1	44.1	44.3	44.3	44.3	44.3	45.3
Income balance	-7.0	-8.6	-6.5	-5.5	-5.4	-5.4	-5.5	-5.4	-5.6
Credit	7.4	7.2	7.1	7.0	6.8	6.7	6.5	6.4	6.4
Debit	14.4	15.8	13.6	12.5	12.2	12.0	12.0	11.8	12.0
Secondary income balance	-0.8	-0.8	-0.6	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7
Capital account balance	0.2	0.2	1.3	0.2	0.2	0.2	0.2	0.2	0.2
Financial account balance	-1.1	-0.1	2.1	0.5	0.2	0.1	0.0	0.1	0.1
Direct investments	-2.0	0.6	0.4	0.5	0.5	0.5	0.4	0.4	0.5
Portfolio investments	1.6	-2.1	-8.0	0.2	0.3	0.4	0.4	0.2	0.1
Other investments	8.6	1.8	-1.8	0.9	0.5	0.2	0.2	0.4	0.5
Change in reserve assets (increase = +)	-9.4	-0.3	11.4	-1.0	-1.0	-1.0	-1.0	-0.9	-0.9
Net errors and omisions	-1.3	1.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items									
Nominal GDP (in millions of euros)	1,353.1	1,401.7	1,430.3	1,457.6	1,490.9	1,523.8	1,556.1	1,587.8	1,619.4
GIR (in millions of euros)	252.7	248.1	410.6	395.6	380.6	365.6	350.6	335.6	321.6
GIR in months of imports	1.5	1.4	2.2	2.1	2.0	1.9	1.8	1.7	1.5

Sources: San Marino Statistical Office and IMF staff.

Table 4. San Marino: Financial Soundness Indicators, 2012–19

	2012	2013	2014	2015	2016	2017	2018	2019. Sept
Capital adequacy ratios (percent) 1/								
Regulatory capital to risk-weighted assets	8.8	13.6	11.4	12.7	11.5	13.7	12.3	9.2
Capital to assets	6.3	7.3	6.2	6.9	6.2	6.5	6.2	4.8
Asset quality ratios (percent) 1/ 2/								
Bad loans to total loans	10.6	15.4	18.2	20.8	18.3	20.5	20.4	26.2
Nonperforming loans to total loans	22.6	47.0	48.8	52.6	50.0	54.0	53.0	57.4
Bad loans net of provision to capital	58.7	54.6	70.1	79.6	73.8	78.6	90.6	101.2
Nonperforming loans net of provision to capital	164.3	289.3	332.1	340.0	224.4	250.1	249.9	234.2
NPL coverage ratio	42.6	26.5	31.1	28.7	54.8	56.0	59.9	65.0
Earning and profitability (percent) 1/								
Return on assets (ROA)	-2.2	-0.6	-1.8	-0.7	-1.0	-0.7	-1.2	-4.6
Return on equity (ROE)	-22.5	-7.8	-21.4	-9.0	-13.2	-10.1	-16.1	-79.3
Interest margin to gross income	58.5	46.1	32.1	37.3	39.0	42.4	50.3	37.4
Non-interest expenses to gross income	69.7	81.2	50.7	62.3	72.4	66.9	74.3	58.7
Trading income to gross income	11.7	13.3	13.9	1.9	3.0	4.1	-17.4	2.0
Personnel expenses to non-interest expenditures	55.7	59.5	61.7	60.9	61.4	57.0	58.9	58.9
Liquidity (percent)								
Liquid assets to total assets	18.9	21.8	24.0	23.6	23.7	18.6	22.8	19.4
Liquid assets to short-term liabilities	39.6	44.7	48.4	46.5	44.8	33.3	41.2	32.8
Loans to deposits	91.8	86.7	80.0	165.0	153.8	141.4	125.6	114.5
Memo items								
Banking system assets (millions of euros) 2/	6122.1	6141.1	6081.9	5692.0	5279.8	4763.6	4576.1	4252.2
percent of GDP	490.1	486.0	482.9	444.9	398.0	352.0	326.5	297.3

Sources: Sammarinese authorities; IMF International Financial Statistics; and IMF staff.

1/ 2017-19 data do not reflect 2017 AQR results, while 2019 data reflect changes related to Banca CIS resolution

2/ CBSM supervisory data. Latest data are as of Nov 2019. Supervisory data, as opposed to FSI data, reflect retrospective revisions made by banks in their annual financial statements. Loans and NPLs to banks are excluded in calculating each indicator.

Table 5. San Marino: Depository Corporate Survey, 2012–19 1/

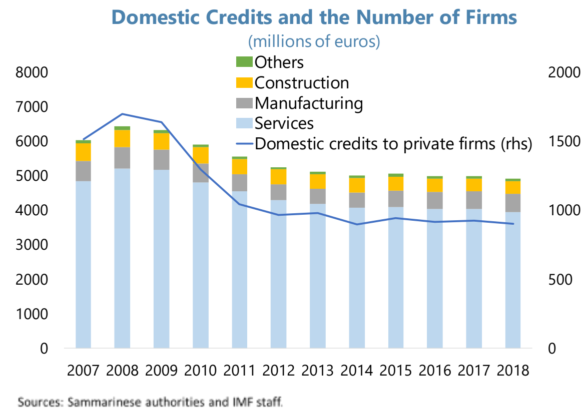
	2012	2013	2014	2015	2016	2017	2018	2019. Sept
	(In Millions of euros, end of period)							
Net foreign assets	2600.1	2643.5	2512.2	2340.4	2136.5	1868.3	1752.2	1742.8
Claims on nonresidents	3938.9	3864.1	3801.2	3433.9	3054.8	2612.8	2393.3	2347.1
Central Bank	267.5	367.7	298.0	321.5	401.2	274.7	270.6	420.4
Other Depository Corporations	3671.4	3496.4	3503.2	3112.4	2653.7	2338.1	2122.7	1926.7
Liabilities to Nonresidents	-1338.8	-1220.6	-1288.9	-1093.5	-918.4	-744.4	-641.1	-604.3
Central Bank	0.0	0.0	0.0	0.0	-0.1	-0.2	-0.2	-0.1
Other Depository Corporations	-1338.8	-1220.6	-1288.9	-1093.5	-918.2	-744.2	-640.9	-604.2
Net domestic assets	1455.0	1557.5	1693.7	1323.4	1382.5	1122.4	1125.9	1052.0
Net Claims on Central Government	200.9	229.4	202.9	-8.8	-35.1	-234.8	-256.3	-189.1
Claims on State and Local Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Claims on Public Nonfinancial Corporations	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Claims on NBFIs	799.7	690.7	625.9	485.0	381.6	263.0	242.6	232.4
Claims on private sector	1506.3	1535.2	1656.2	1547.1	1468.6	1485.3	1381.8	1339.6
Corporates	965.5	980.0	898.7	945.3	914.2	925.9	859.5	847.2
Households	540.8	555.1	757.5	601.8	554.3	559.4	522.3	492.4
Capital and Reserves	590.4	599.6	544.7	519.7	471.5	419.8	388.6	333.3
Other items, net	461.5	298.2	246.7	180.3	-39.0	-28.7	-146.4	-2.4
Broad Money	1472.8	1539.1	1635.1	1430.0	1466.7	1441.6	1459.6	1598.1
Currency in Circulation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Transferable Deposits	1334.7	1385.8	1449.7	1340.5	1372.2	1370.5	1398.5	1444.7
Other Deposits	138.2	153.4	185.4	89.4	94.5	71.1	61.1	153.4
Securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Long-term securities excluded from Broad Money	2582.2	2661.8	2570.8	2233.8	2052.3	1549.1	1418.5	1196.7
	(Annual percentage change)							
Net foreign assets	-18.4	1.7	-5.0	-6.8	-8.7	-12.6	-6.2	-0.5
Net domestic assets	42.2	7.0	8.7	-21.9	4.5	-18.8	0.3	-6.6
Claims on private sector	-2.2	1.9	7.9	-6.6	-5.1	1.1	-7.0	-3.1
Corporates	-7.4	1.5	-8.3	5.2	-3.3	1.3	-7.2	-1.4
Households	8.7	2.6	36.4	-20.5	-7.9	0.9	-6.6	-5.7
Broad Money	-0.1	4.5	6.2	-12.5	2.6	-1.7	1.2	9.5

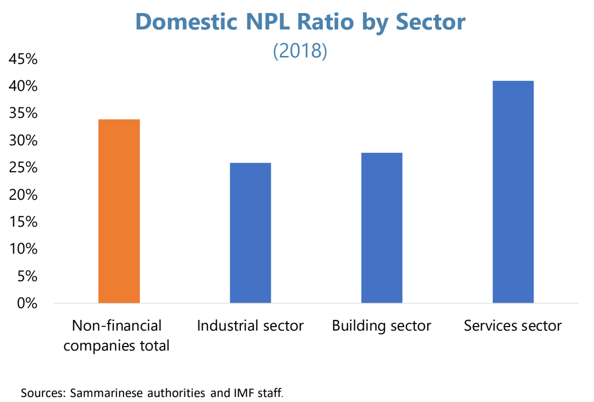
Sources: International Financial Statistics and IMF Staff.

1/ Data beginning in June 2015 accord to the IMF's monetary and financial statistics methodology, and are not strictly comparable to earlier periods.

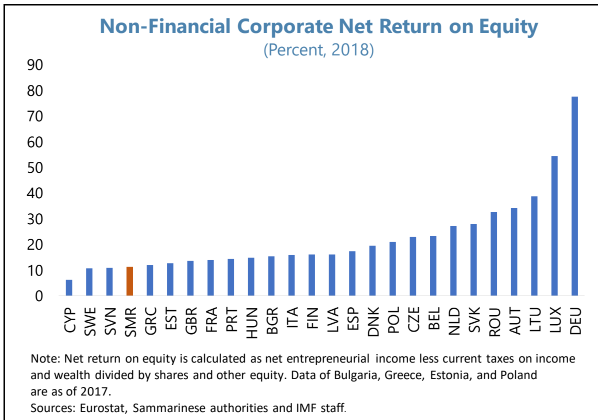
Annex I. Corporate Vulnerability in San Marino

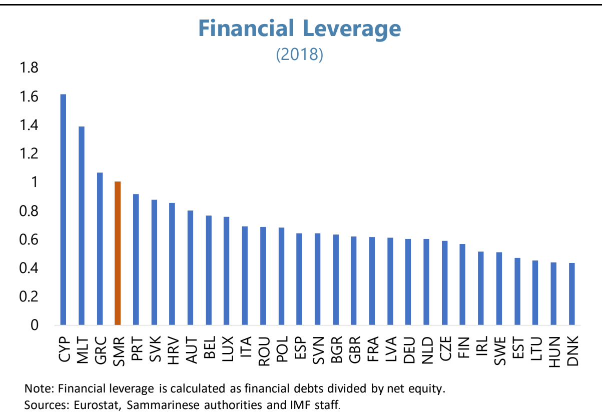
1. The corporate sector in San Marino was hit hard by the prolonged economic contraction. San Marino experienced one of the deepest and longest recessions in Europe with an output loss of about one-third in the last decade. The number of firms has shrunk significantly by about one quarter compared with the 2008 level, reflecting firms' liquidation rate of about 5 percent per annum. Domestic corporate NPLs increased sharply and remained elevated, especially in the service sector.





2. The corporate sector's profitability is low and its debt burden is high. Firms' net return on equity stands around 10 percent, among the lowest in the EU countries, suggesting that firms are still suffering from low profitability on average, partly owing to the anemic recovery of key trading partners[1]. The low profitability, together with firms' high financial leverage ratio may indicate that firms face difficulties in servicing their debt.

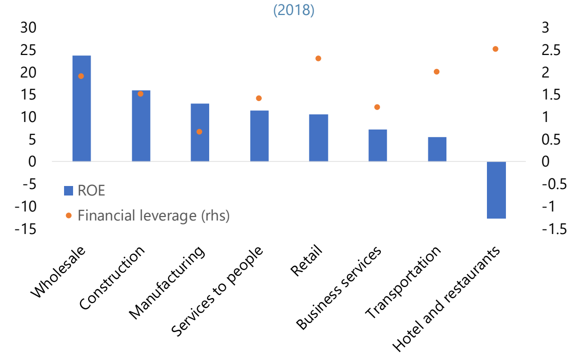




[1] The average return on total assets (ROA) in San Marino stood at around 4 percent in 2012–18, well below that of the EU.

3. The service sector, in particular the food and accommodation sector, is facing significant challenges. With the exception of the wholesale sector, the service sector generally shows low profitability and high financial leverage. In particular, hotels and restaurants have continuously made losses while carrying the highest debt burden. This, together with the fact that the decline in the number of firms in hotel and restaurant sector (8 percent) is much smaller than the total (24 percent), may suggest that many firms in this sector are struggling to service their debt without exiting the market, contributing to banks' slow NPL resolution.

ROE and Financial Leverage by Sector
(2018)

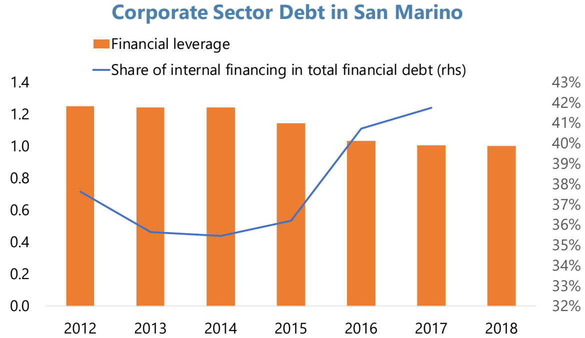


Sources: Sammarinese authorities and IMF staff.

4. The stress in the domestic banking sector has affected firms' financing structure. Reflecting the gradual deleveraging process of Sammarinese banks, and the difficulties in securing cross-border financing from banks in other EU countries, surviving firms reduced their leverage while using other financing sources. In this context, many firms turned to internal resources as a source for investment, resulting in increasing share of shareholder loans and group company loans in total financial debt to 42 percent in 2017 compared with 36 percent in 2013.

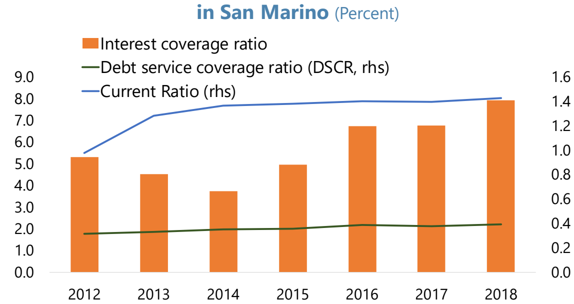
5. Debt repayment capacity has recently improved but is still a source of concern. Firms' ability to service debt has improved due to declining interest payments and accumulated liquidity assets. However, though it can partially be mitigated by sizable shareholder/group companies funding, their high reliance on short-term debt (60 percent of total financial debt), together with still elevated debt level, represents a significant repayment risk, particularly if banks will not be able to rollover existing loans due to ongoing liquidity pressure.

Corporate Sector Debt in San Marino



Note: Financial leverage is defined as financial debt per net capital. Internal financing include loans from shareholders and group companies.
Sources: Sammarinese authorities and IMF staff.

Debt Servicing Capacity of the Corporate Sector in San Marino (Percent)



Note: Interest coverage ratio is calculated as earnings before interest and tax (EBIT) divided by interest expense. Debt service coverage ratio is calculated as EBITDA divided by debt service cost within on year (i.e. interest payment + short-term debt). Current ratio is current assets per current liabilities.
Sources: Sammarinese authorities and IMF staff.

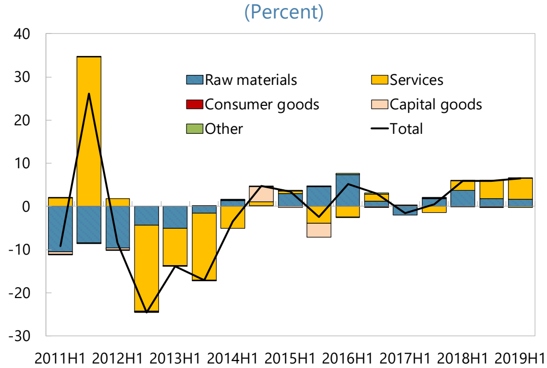
Annex II. External Sector Assessment and Reserve Adequacy for San Marino

A. External Sector Assessment

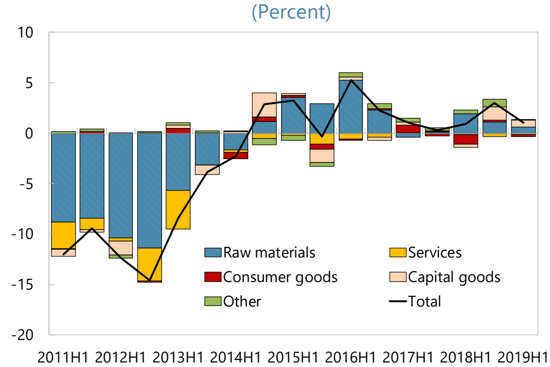
The external position of the Republic of San Marino in 2019 was weaker than implied by fundamentals and desirable policy settings. While significant data weaknesses call for caution, both the current account (CA) gap and real effective exchange rate (REER) Index models suggest an overvaluation, albeit with different magnitude. [1] *These findings, which largely reflect structural impediments, suggest that improving external competitiveness remains a key challenge for San Marino.*

1. The 2019 current account is estimated to be broadly balanced while financial account outflows moderated. While data weaknesses call for caution, the 2019 current account balance is estimated to have shifted to a slight surplus of 0.7 percent of GDP from a deficit of 1.6 percent in 2018, largely due to an improvement in the income balance. Gross international reserves are estimated to have increased to €416 million at end-2019 from €249 million in 2018, largely reflecting the divestment of CBSM's illiquid securities, and a shift of the pension fund bank deposits into the CBSM. Preliminary estimates suggest that the net IIP remained high, although moderating to 244 percent of GDP in 2019 from 247 percent of GDP in 2018 due to continued liquidation of foreign portfolio investments by banks as well as a sustained decline—though at a slower pace—in domestic banks' loans to nonresidents.

Exports: Contribution to Growth
(Percent)



Imports: Contribution to Growth
(Percent)



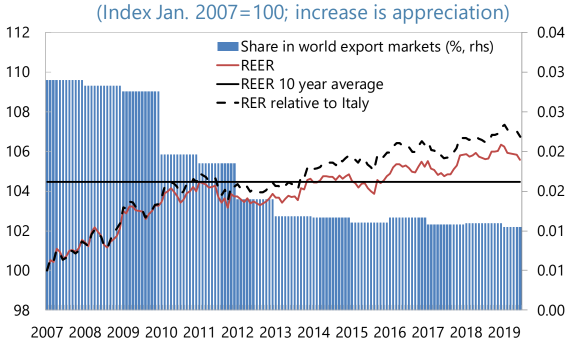
2. San Marino's market share declined considerably in recent years. The country lost about two-thirds of its world export market share compared to the pre-crisis period due to a weak recovery in Italy, which contributed to a significant reduction in exports of goods, including manufacturing. The loss in export market share occurred simultaneously with a prolonged appreciation of the REER due to a persistent and widening positive inflation differential vis-à-vis Italy. This, along with other structural impediments, suggests that improving competitiveness remains a key challenge for San Marino. Indeed, in recent years labor productivity declined and unit

[1] San Marino recently started to produce balance of payment and IIP statistics.

labor costs increased significantly compared to that in neighboring Italian regions. Moreover, San Marino continues to lag its peers on regulations for starting a business, enforcing contracts and resolving insolvency, protecting minority investors and dealing with construction permits.

CPI-Based REER and Export Market Share

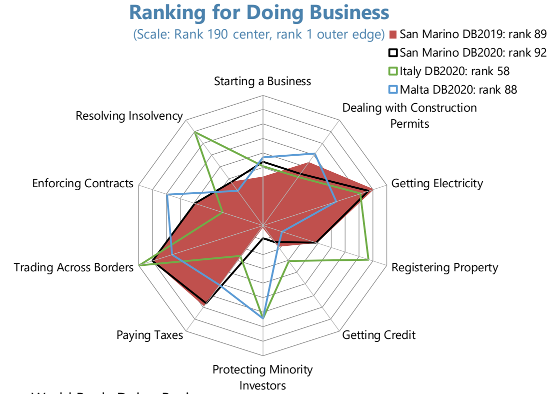
(Index Jan. 2007=100; increase is appreciation)



Sources: Haver, IFS, San Marino authorities and IMF staff.

Ranking for Doing Business

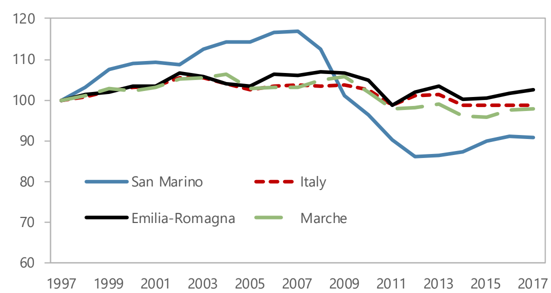
(Scale: Rank 190 center, rank 1 outer edge)



Source: World Bank, Doing Business.

GDP per Employed

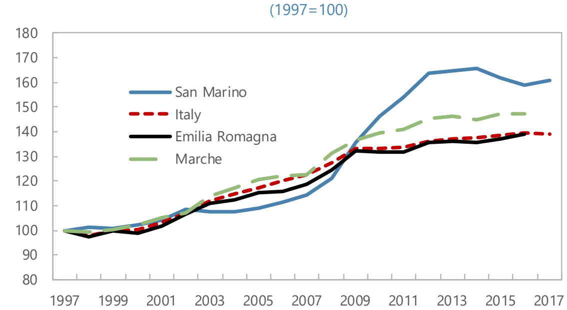
(1997=100)



Sources: Sammarinese authorities, Italian authities, and IMF staff.

Unit Labor Cost

(1997=100)



Sources: Sammarinese authorities, Italian authities, and IMF staff.

3. Both the current account (CA) and REER index models point to an REER overvaluation, although the models' fit for San Marino is poor.

- **Current account (CA) approach:** Based on the revised EBA-lite approach, the estimated 2019 CA norm and the implied REER gap, stood at about 11 percent and 9 percent of GDP, respectively. The high CA norm and large REER overvaluation primarily reflect the relatively high net foreign asset position[2] of the economy relative

San Marino: External Balance Assessment, 2019

	CA-Actual	0.7%
a	Cyclically adjusted CA	0.9%
b	Multilaterally Consistent Cyclically adjusted CA Norm	10.8%
c	**CA-Gap = [a]-[b]**	**-9.9%**
	of/which Policy gap	3.2%
d	Elasticity	-1.2
e	**REER Gap = [c]/[d]**	**8.6%**
f	CA-Fitted	13.0%
g	Residual = [a]-[f]	-12.3%

[2] The stock of NIIP stood at 244 percent of GDP as of end-2019, of which 45 percent was related to banks and 47 percent attributable to other financial and nonfinancial corporations, households, and Nonprofit Institutions Serving Households (NPISHs). In this assessment, the NIIP stock was deflated to account for the fact that about 80 percent of loans to non-residents are non-performing.

to its key trading partners, yet these estimates, which suggests that the policy gap is relatively small, should be taken with caution given the model's poor fit for San Marino, and data weaknesses, which limit the ability to assess the REER elasticity with high confidence.

- **REER index model:** Consistent with the CA gap approach, the REER appears to be overvalued by about 11 percent, suggesting that the REER is stronger than implied by fundamentals. However, the REER deviation from its equilibrium is not explained by a policy gap and mostly reflects large residuals (8 percent).

4. Staff judge San Marino's external position as weaker than implied by fundamentals and desirable policy settings. Staff cannot exclusively rely on the two EBA-Lite approaches given their poor fit for San Marino and the persistence of significant data weaknesses. Nonetheless, given the strong need for fiscal consolidation, reserves accumulation (see below), and burden sharing for bank recapitalization, staff view the REER as overvalued and the external position as weaker than implied by fundamentals and desirable policy settings. This assessment is also supported by the recent erosion of external competitiveness and the significant reduction of exports' market share.

B. Reserve Adequacy for San Marino

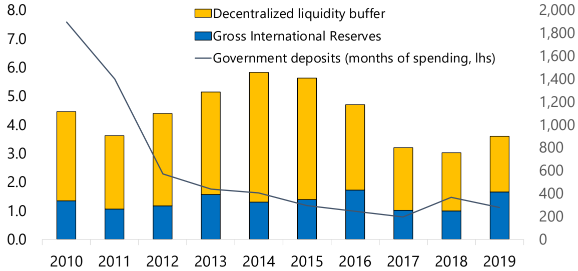
5. San Marino's system-wide liquidity buffers have declined considerably in recent years. The aggregate liquidity buffers—comprised of international reserves and the decentralized liquidity buffer held by commercial banks outside the CBSM—have fallen sharply in 2015–17 on the back of significant deposits outflows, withdrawal of government deposits, and CBSM liquidity support to the banking system and the government. Overall liquidity has improved since end-2018, but still stood around 60 percent of the liquidity buffers in 2014.[3]

6. Some standard metrics still indicate that international reserves are below levels that are considered as adequate.[4] While the ratio of reserves to broad money and the ratio of reserves to short-term external debt suggest that San Marino's international reserves are at comfortable levels, the imports coverage ratio indicates that international reserves are insufficient. Moreover, the Fund's ARA EM metric—a composite metric designed to better capture a range of capital outflow risks—shows that the international reserves amount to 71 percent of the metric, below the range which is generally considered to be adequate (100–150 percent).

[3] The improvement in liquidity in 2019 relative to end-2018 was mainly driven by one-off factors, including divestment of illiquid securities by the CBSM, a shift in pension fund bank deposits into the CBSM, and CRSM's sale of the sub-delta portfolio, the proceeds of which were mostly deposited at the CBSM.

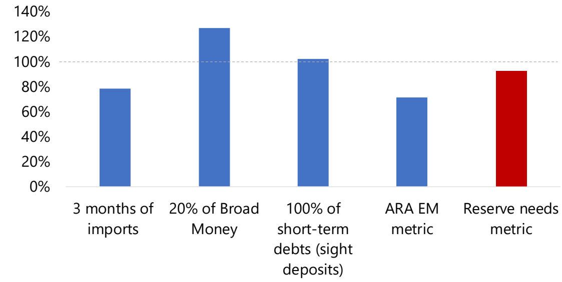
[4] See Guidance note on the assessment of reserve adequacy and related considerations (IMF, 2016).

Liquidity Buffers
(millions of euros)



Sources: CBSM, MoF and IMF staff.
Note: Decentralized liquidity buffer includes cash, deposits and loans available within 7 days, and securities that can be readily converted to cash but does not include deposits at CBSM and Sammarinese banks.

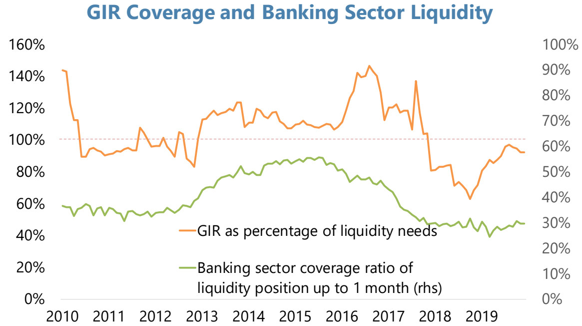
Reserve Coverage Metrics
(as of end 2019)



Note: ARA EM metric is defined as 10% of exports of goods and services, 30% of non-resident sight deposits, 20% of other liabilities to non-residents, and 10% of broad money.
2019 import/export is an esimate. Broad Money and other liablity data are as of Sept-2019.
Sources: CBSM, IMF Monetary and Financial Statistics, and IMF staff.

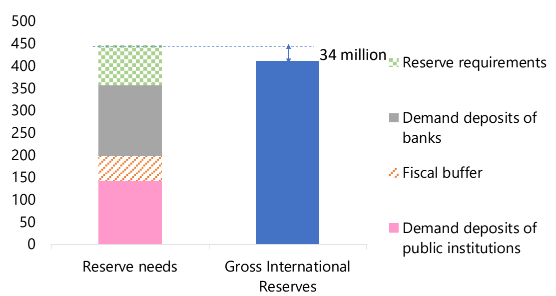
7. **San Marino's reserve needs metric, which consider liquidity risks in the banking system and the public sector, shows an improvement, yet international reserves are below "safe" levels.**[5] As a fully euroized economy that does not have access to external markets, San Marino's international reserves play a critical role as a buffer against shocks. Staff's developed metric, which takes into account system-wide liquidity risks, suggests that the reserve gap is estimated to have declined to 8 percent (i.e. €34 million) at end-2019 from 28 percent at end-2018, mainly owing to termination of credit lines to banks and divestments of illiquid securities. Despite recent improvements, the CBSM may need to hold a higher buffer than the minimum level if further liquidity support to banks and the government becomes likely.

GIR Coverage and Banking Sector Liquidity



Note: Reserve coverage is defined as gorss international reserves as a share of the reserve needs. The latter is the sum of (1) reserve requirements, (2) sight deposits (excl. the government deposits), (3) fiscal buffer, and (4) credit lines (expected loans) to banks and the government.
Sources: CBSM and IMF staff calculations.

Reserve Needs
(millions of euros, end-2019)



Note: Demand deposits of public institutions exclude the government deposits at the CBSM for liquidity buffer purpose.
Sources: CBSM, IMF Monetary and Financial Statistics, and IMF staff.

[5] See Annex III of Republic of San Marino: 2019 Article IV Consultation Staff Report.

Annex III. Risk Assessment Matrix[1]

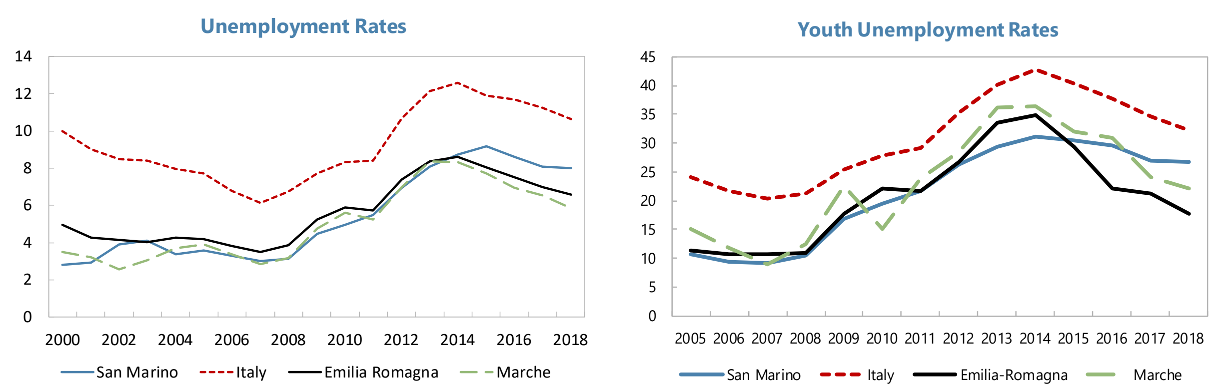
Source of Risks	Impact if Realized	Policy Response
High **Weaker-than-expected growth in the euro area.** Weak foreign demand or an unanticipated Brexit outcome delays investment, reduces private consumption, and strains banks. With limited policy space, the region enters a prolonged period of anemic growth and low inflation.	High With extensive financial and real links with Italy and advanced Europe, the impact on the Sammarinese economy would be large and direct.	• Ease the pace of the fiscal adjustment and reevaluate periodically; • Address financial sector vulnerabilities; • Proceed with fiscal and structural reforms; and • Further diversify trade and financing options.
Medium **Sharp rise in risk premia.** An abrupt reassessment of market fundamentals triggers widespread risk-off events that expose financial vulnerabilities that have been building in a period of low interest rates and a search for yield. Higher risk premia generate debt service and refinancing difficulties; stress on leveraged firms, households, and vulnerable sovereigns; and capital outflows.	Medium Tighter global financial conditions may lead to large financial outflows and could result in higher borrowing costs for some firms that operate in San Marino, and therefore to lower investment and growth. This could also affect public finances, especially if the sovereign seeks external financing.	• Carefully assess alternative options in seeking external financing; • Address financial sector vulnerabilities; and • Apply liquidity safeguard measures on an "as needed" basis.
Medium **Coronavirus outbreak** causes widespread and prolonged disruptions to economic activity and global spillovers through tourism, supply chains, containment costs, and confidence effects on financial markets and investment.	High The spread of the outbreak in Europe, including in San Marino and Italy, would have adverse effects on growth through reduced flow of trade and tourism, factory closures, travel restrictions, and lower consumption and investment. This would also affect public finances directly through containment and mitigation costs.	• Ease the pace of fiscal adjustment to accommodate the urgent spending needs; • Provide temporary support to hard-hit sectors; and • Increase collaboration with international agencies to improve containment and mitigation.
High **Slow banking system repair,** including addressing recapitalization needs and cleaning up bank balance sheets.	High Insufficient implementation of measures to restructure the banking sector will lead to a deterioration of confidence accompanied by significant financial outflows, higher liquidity pressures in the banking system, and retrenchment of credit with adverse growth implications.	• Extend central bank powers and tools for tackling failing banks; • Apply bank resolution tools and liquidity safeguard measures on an "as needed" basis; and • Accelerate the implementation targets in a financial sector strategy and strengthen the CBSM-government coordination.
High **Slow fiscal consolidation and delays in implementing fiscal reforms.**	High High level of public debt and a narrow tax base will increase vulnerabilities and limit the government's ability to respond to shocks. A sustained level of high debt service would also crowd out productive spending, thus undermining growth prospects.	• Advance fiscal reforms, develop debt management capacity, and establish a Treasury department; • Diversify financing options; and • Seek technical support as needed.
Medium **Loss of cross-border electronic payment services:** Failure of one or more banks to meet their gross settlements obligations would significantly curtail cross-border payments.	High Disruptions of retail and wholesale electronic payment services leads to an abrupt adjustment in consumption and trade. A sudden shift to cash may cause short-term currency shortages.	• Take immediate steps to improve liquidity in the central bank; and • Apply liquidity safeguard measures to restore the payment system.
Low **Tensions with neighboring Italy resurface.**	High Persistent tensions would dissuade Italian corporates and banks from doing business with San Marino, thus affecting growth.	• Build fiscal buffers and pursue structural reforms; • Enhance international relations; • Further diversify trade.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities.

Annex IV. Social Benefits and Labor Market Outcomes

Recent Developments in the Labor Market

1. **San Marino's economy is recovering from a deep economic contraction.** Since the global financial crisis, the country has lost more than 30 percent of its output, resulting in a steady and persistent increase in unemployment from about 4 percent to a peak of 9 percent in 2015. Although in recent years the unemployment rate has somewhat stabilized to about 8 percent, it remains elevated and above those in neighboring regions.[1] A similar trend was observed among the youth, whose unemployment rate tripled during the crisis and has only modestly recovered in the recent period.



Sources: UPECEDS, ISTAT.

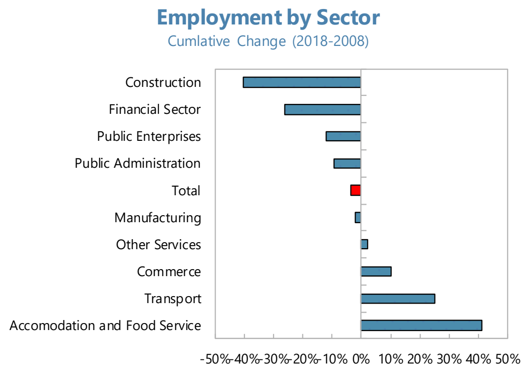
2. **The crisis has led to a reallocation of workforce in the economy.** Since 2008, the overall level of employment (excluding self-employment) has declined by 4 percent.[2] At the sectoral level, the largest decline has been observed in construction (40 percent), finance (26 percent), public enterprises (12 percent) and public administration (9 percent). The financial sector is likely to face further downsizing over the next years, due to the need to regain profitability, while the public sector employment remains constrained by a significant erosion of the fiscal space and the need for fiscal consolidation.[3] Manufacturing, on the other hand, continues to be the economy's largest employer. Additionally, sectors like transport, commerce, accommodation and food services and especially other professional services have become more relevant in the economy, accounting for more than 40 percent of total employment, compared to 30 percent in 2002.

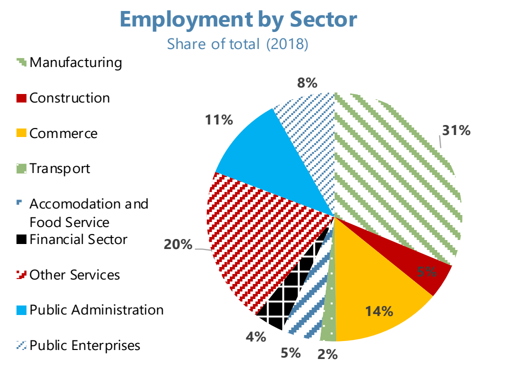
---

[1] The magnitude of the economic contraction did not translate into a significantly higher increase in unemployment partly due to the wage supplementation system given to companies in economic distress.

[2] Considering the number of self-employed, total employment declined by about 6 percent since 2008.

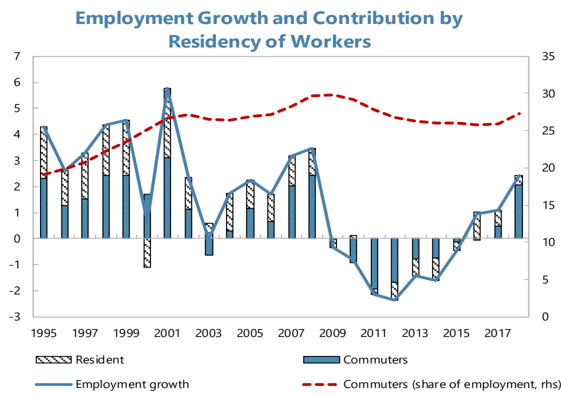
[3] The share of public sector workers in total dependent employment has been instead on a declining trend, reaching 19 percent in 2018 compared with 30 percent in the 1990s.





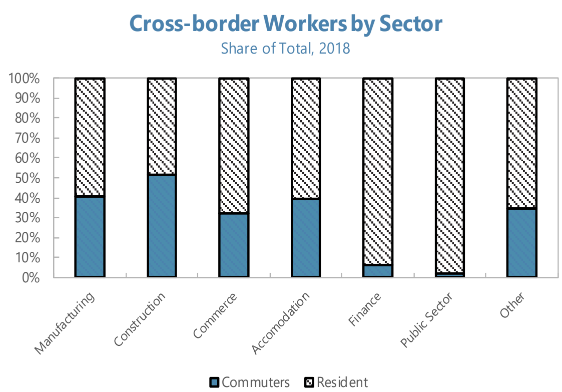
Note: The figures exclude self-employment.
Sources: UPECEDS, IMF staff elaborations.

3. The shift in the sectoral composition of the workforce has been supported by inflows of cross-border workers. The share of cross-border workers (predominantly employees from neighboring Italian regions) in total employment has increased steadily over the years, reaching 30 percent in 2008. Since 2017, employment growth has been for the most part driven by the hiring of cross-border workers, a process facilitated by the partial liberalization of the labor markets introduced with the 2017 "Development Law" (Box AIV.1).



Sources: UPECEDS and IMF staff.

4. Cross-border workers remain more predominantly employed in lower paying economic sectors. Over the years, Sammarinese workers have been predominantly employed in high paying sectors such as the financial sector and public administration. On the other hand, cross-border workers are more prevalent in lower paying sectors, like manufacturing, construction, commerce, accommodation and food service. The average salary in the public sector is about 30 percent higher than that of an average private sector employee, while in the finance sector the average wage is 80 percent higher.[4] While these wage differentials can be partly explained by higher education of the workforce, as in the case of the public sector, it has been argued that such differentials create incentives for people to remain unemployed (Box AIV.2).[5, 6]



Sources: UPECEDS and IMF staff.

---

[4] The hourly wage figures, which might be a better indicator, are not available.

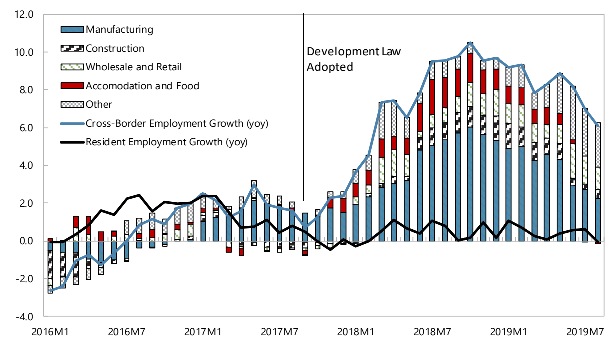
[5] Only 6.8 percent of the private sector workforce has a university degree, compared to about 22 percent in the public sector.

[6] See Burda, Michael 1988, "Wait Unemployment' in Europe." Economic Policy, vol. 3, no. 7, pp. 393–425, and 1996 IMF staff report SM/96/165 (7/3/96) for an examination in the case of San Marino.

Box AIV.1. Cross-Borders Workers and the 2017 "Development Law"

The hiring process in San Marino is centralized, managed by both the Labor Office and the Office for Active Labor Market Policies. A job seeker needs to be registered on the centralized employment registry, which provides a prospective employer information about education level, skills, and targeted sector of the job seekers. Job seekers on this list are ranked according to their needs (family size, and length of unemployment) and their qualifications. In the previous regime, the matching between supply and demand for labor was done by the Labor Office, which provided prospective employers candidates based on their ranking on the list. Only after it was concluded that all the interviewed candidates were not qualified for the jobs, employers could search openly, either among people already employed, or among cross-border workers, subject to approval from the Labor Office. The "Development Law"—adopted in 2017—has partly liberalized this process. Employers can now choose between two channels for hiring. They can follow the old regime and recruit from the employment registry, or they can hire directly cross border workers, by paying a surcharge (4.5 percent additional contribution rate, earmarked to finance the Office for Active Labor Market Policies). Another important aspect of the Development law has been the equalization of status between cross-border workers and people on the employment registry. Since September 2017, cross-border workers can also be hired with open-ended contracts, a feature which in the old regime was allowed only after the workers had been employed for at least seven years.

Cross Border Employment Growth and Sectoral Contributions

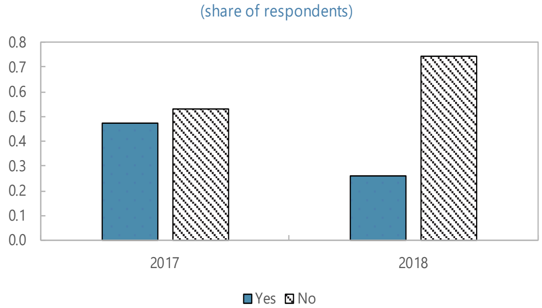


Sources: UPECEDS and IMF staff.

8. Recent surveys suggest that firms look for qualified candidates abroad because of a skills gap. While some domestic workers might be unwilling to fill jobs in lower-paying sector, some firms, particularly in the manufacturing sector, face the emergence of a skill gap. According to the survey on employers' occupational needs, performed by the *Ufficio per le Politiche Attive del Lavoro* (UPAL), about one in two firms reported difficulties in finding qualified local candidates in 2017, largely due to unavailability of the needed skills. Following the adoption of the Development law, the situation has somewhat eased, yet remained prominent, as one in four firms lamented difficulties in hiring. In San Marino the skill shortage seems to be more acute among firms that look for skilled industrial and construction trades workers. Firms in services sectors also have difficulties in hiring candidates and look abroad for workers with marketing, accounting and sales experience—profiles which are not readily available in San Marino.

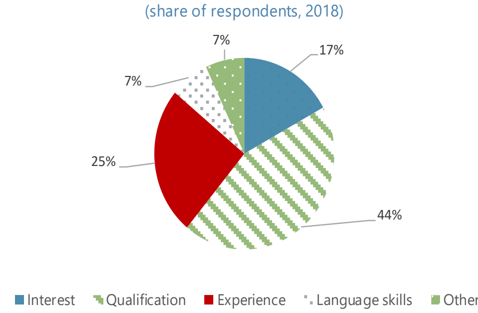
Firms Facing Hiring Challenges

(share of respondents)



Hiring Difficulties Experienced Due to Lack of:

(share of respondents, 2018)

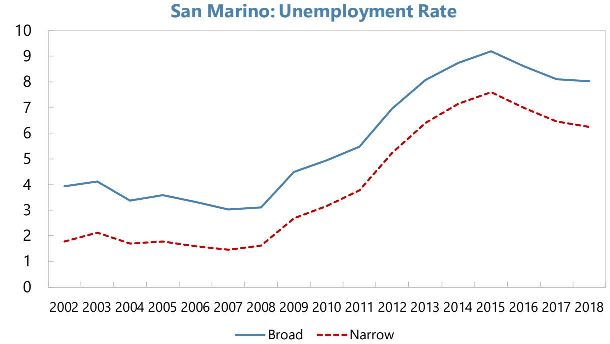


Sources: UPAL

Box AIV.2. Measuring Unemployment Rates

The Statistical Office of San Marino (UPECEDS) publishes two series of unemployment rates. The first series, the "overall" unemployment rate, considers as unemployed those people registered on the employment list. The second series, called the "narrow" unemployment rate, excludes from the calculation those people who are seeking either a fixed term or part-time employment. The UPECEDS does not consider this group of people "immediately" employable, as they are not willing to accept any job. Therefore, they consider the narrow definition as the true rate of unemployment. The difference between these two series is constant throughout the years and did not increase significantly after the crisis. This group of "voluntary" unemployed people are predominantly women (85 percent).

San Marino: Unemployment Rate

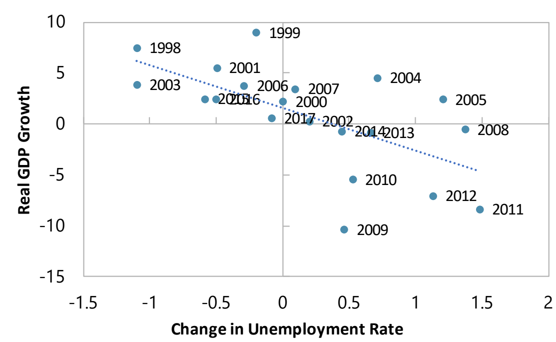


Sources: UPECEDS.

Options for Reforms

9. Promoting growth remains key for employment creation. As the economy is going through a structural transformation, it is important to support firms' demand for labor. The centralized hiring process imposed significant cost for firms, and the recent decision to allow them to directly search the employment registry without the intermediation of the labor office is a step in the right direction. However, reforms that further streamline the hiring process will, over time, reduce the search costs for firms and speed up job creation. The surcharge on direct hiring of cross-border workers should be discontinued, as it impacts negatively on firms' ability to expand their activity, especially those facing skills gap in the domestic market. Reducing unemployment and addressing the skills gap requires interventions that affect incentives on both the supply and demand of labor.

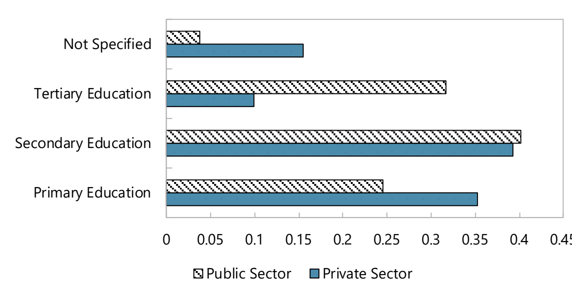
Okun's Law



Sources: IMF staff.

7. Labor market policies should strive to reduce the incidence of frictional unemployment. The existence of frictional unemployment (Box AIV.2), can be addressed through several initiatives. First, a better understanding of the profiles of the workforce registered on the employment list is needed; second, lowering the hourly wage differentials between the private and public sectors can strengthen labor market participation. At the same time, it can improve productivity in the economy by ensuring that a higher educated workforce is also employed in the public sector.

Share of Workforce by Level of Education



Sources: UPECEDS.

8. Addressing the skills gap will require investment in training and education. San Marino has two centers in charge of Active Labor Market Policies (ALMP), the UPAL, overseeing tasks such as job placement services and counseling, and the *Centro per la Formazione Professionale* (CFP) which oversees training. San Marino also provides tax incentives for firms that expand their workforce by hiring through the employment list, and for hiring disadvantaged workers.[7] The international evidence shows that such schemes can be costly to run, while the evidence on their effectiveness is mixed.[8] For a country in need of fiscal consolidation like San Marino, it is important to subject ALMP to rigorous cost-benefit analysis and continuously monitor their supposed impact. As an example, providing tax incentives to hire workers on the employment list appears wasteful. To improve employability, it can be more effective to bolster existing incentives for training at the firm level. Going forward, to increase the level of competencies and skills of the local workforce, the UPAL can play a coordinating role between firms, schools, and universities to better match labor demand and supply.

9. The social protection system can be rationalized to promote job search. San Marino provides different type of financial support for the unemployed. The cost of unemployment benefits remains relatively contained in percent of GDP, similar to those in other countries, also in terms of generosity.[9] Nonetheless, attention should be given to:

- **Wage supplementation system (CIG)**. This financial assistance, which is meant to be provided only for temporary shocks, is also used for prolonged economic downturn and corporate restructuring, thereby suppressing unemployment figures. This system may prevent de facto reallocation and reorganization of labor during downsizing and structural changes. In such cases, consideration should be given to provide workers with a standard unemployment benefit, conditioned on active job search and training.

- **Duration of unemployment benefits**. The maximum duration of the unemployment benefits is 24 months, even for those that only worked for 6 months continuously. Linking the duration of unemployment benefits to employment period will reduce abuse and support more active job search.[10]

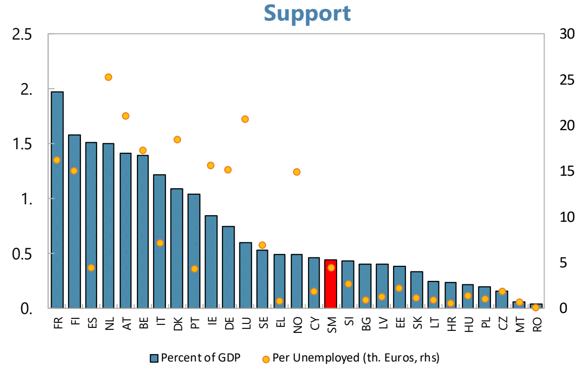
[7] Apprenticeships policies are also available to support young workers.

[8] Vooren, M., Haelermans, C., Groot, W. and Maassen van den, Brink, H., 2019, "The Effectiveness of Active Labor Market Policies: A Meta—Analysis". Journal of Economic Surveys, 33: 125–149.

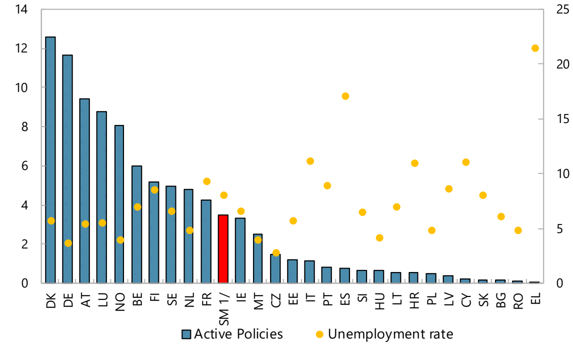
[9] A comparison in purchasing power standard is not available for San Marino.

[10] The *Indennita economica speciale* (IES), which is granted to workers unemployed because of company closure is normally given for 12 months, although they are benefiting from priority in their ranking on the employment list.

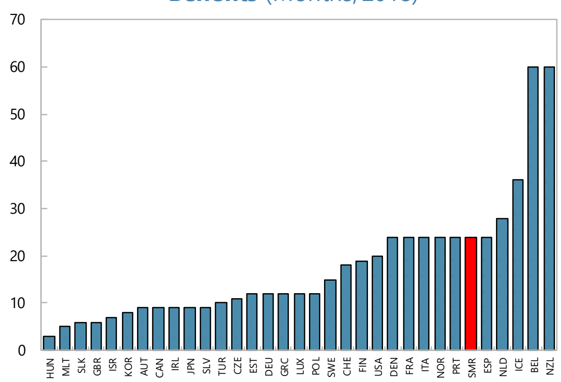
Expenditure on Out of Work Income Support



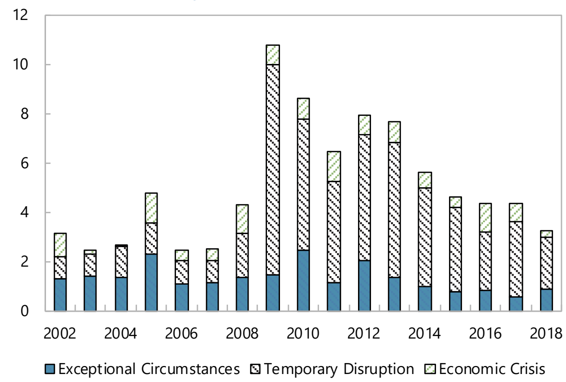
Spending on Labor Market Services, Training (per unemployed, th. euros)



Maximum Duration of Unemployment Benefits (Months, 2018)



Expenditure on CIG (by motivation, Euro Mil)



Sources: OECD, UPECEDS, Institute for Social Security, Eurostat, UPAL.

1/ For San Marino, spending on labor market services and training is indicative, as it is the total budget allocated to OALMP, thus likely an over-estimate the actual spending on ALMP.

Annex V. Implementation of Past IMF Recommendations

IMF Policy Advice from 2019 Consultation	Authorities' Action
Financial Sector Policy	
• Safeguard central bank liquidity buffers through aligning the ELA to international best practices and restricting the central bank's budget financing. • Restructure banking system through recapitalization, cost reduction, and NPL resolution. Convert tax credits into government bonds. • Enhance the central bank's powers and strengthen its capacity to oversee the banking system. Review the central bank law to increase its accountability, governance, and independence, • Further contain financial integrity risks.	• The CBSM reserve gap narrowed in 2019 due to divestment of illiquid securities and termination of credit lines to banks. The government continues to rely on CBSM's financing, and the maturity of expired loans were extended. • The CBSM requested banks to incorporate the 2017 AQR findings and submit a capital plan to fill capital shortfalls. No action has been taken so far to address the large recapitalization needs of CRSM or to convert tax credits into government bonds. To support NPL resolution, the authorities have liberalized the real estate market and removed the cap on tax deductibility for loan-loss provisions. They are also considering an AMC to further facilitate NPL resolution. • The authorities passed a new resolution law that granted the CBSM wider tools and powers to intervene and resolve failing banks with a limited scope of burden sharing. They are also planning to introduce a "fit and proper" rule to enhance governance of banks. • The authorities are undertaking a second National Risk Assessment, to be completed in 2020.
Fiscal Policy	
• Contain the government's contribution to banks' recapitalization and develop a fiscal consolidation strategy, which should rely on: o Reform indirect taxes by introducing a Value Added Tax (VAT); o Rationalize tax rebates; o Improve spending efficiency and adopt a pension reform; and o Strengthen debt management capacity • Diversify financing options.	• Public debt further increased in 2019, partly due to CRSM losses and BCIS' bailout. • The 2020 budget is expansionary and lacks significant consolidation measures. VAT implementation is likely to be postponed to 2022 while discussions on the pension reforms are ongoing. • The government initiated a spending review by mandating cost reduction across the public administration and public agencies. • The authorities are planning to introduce a PFM reform, which includes measures to unify and align the public sector accounting framework to international standards while enhancing budget planning, management, reporting and controls.
Structural Reforms and Data Provision	
• Address structural impediments, expand market access, close infrastructure gap. • Continue to engage in international cooperation and improve transparency. • Strengthen data provision.	• The government continued efforts to decrease red tape, including by introducing self-certification for selected bureaucratic procedures. • Following an IMF TA mission (October 2019), the authorities implemented the recommendations of the IMF's Enhanced General Data Dissemination System (e-GDDS) by publishing critical data through the National Summary Data Page.

Annex VI. Debt Sustainability Analysis

Recent bank interventions have increased the implicit public debt to unsustainable levels. Staff's baseline scenario, which incorporates the government's excessive commitments to banking system and the pension funds, indicates that public debt increased to 85.8 percent of GDP in 2019 from 78.8 percent of GDP in the previous year mainly due to the recent bailout of BCIS. In the absence of durable fiscal adjustment and in the face of subdued growth prospects, the implicit public debt is projected to climb to 97.1 at the end of the forecast horizon. These levels, which are unsustainable for San Marino given its lack of market access and limited domestic financing sources, underscore the urgent need for an ambitious fiscal consolidation, stronger public debt management, and private sector contributions to banking system recapitalization. While data weaknesses call for caution, persistent capital outflows are projected to set the external debt, which is estimated at 67 percent of GDP in 2019, on a downward trajectory over the medium term.

1. **Public debt, adjusted to include government's commitments to the banking sector and the pension funds, increased further in 2019**. Public debt increased in 2019 to 85.8 percent of GDP from 78.8 percent of GDP in 2018, mainly owing to the recent BCIS bailout. Going forward, public debt is projected to increase further to 97.1 percent of GDP by 2025 on the back of persistent fiscal deficits and weak growth (Figure AVI.1). The 2020 gross financing needs are projected to increase significantly to about 10.6 percent of GDP from 3.7 percent in 2019 due to a larger fiscal deficit and the repayment of a government loan from the CBSM,[1] and—while declining in 2021—they are projected to remain on an upward path throughout the projection period and reach 11.9 percent of GDP in 2025, partly due to re-current state recapitalization of CRSM, which will facilitate a gradual recognition of public debt and thus increase interest payments.

2. **The unsustainable level of implicit public debt calls for an ambitious fiscal adjustment and a restricted public sector contribution to bank recapitalization.** The elevated public gross financing needs pose significant financing risks, given the lack of market access, limited domestic financing sources, and weak debt management capacity. Adverse economic conditions will further amplify these risks (see adverse scenarios below and Figure AVI.3). This underscore the urgent need for an ambitious and durable fiscal consolidation, stronger public debt management capacity, and careful design of a banking sector recapitalization strategy to limit future incurrences of public debt.

3. **The sustainability of public debt is assessed via several adverse scenarios**. The analysis suggests that public debt remains highly vulnerable to negative shocks to GDP growth, the materialization of contingent liabilities, and a set of combined macro-fiscal shocks. In particular:

- *Real growth shock.* Real GDP growth rate is assumed to decline by one-standard deviation below the baseline during 2021–22. Under this scenario, the public debt ratio would increase to 101.4 percent of GDP by 2022, and to 107.5 percent of GDP by 2025.

[1] In the projection, we assume the short-term loan from CBSM is repaid in 2020 by issuing a new 10-year bond with 2 percent interest rate.

- *Primary balance shock.* The primary balance is assumed to decline by half of its standard deviation in both 2021–22. The public debt is expected to increase to 100 percent of GDP by 2025.

- *Real interest rate shock.* The interest rate is expected to increase by 300 basis points by 2021. Under this scenario, public debt is projected to increase to 99 percent of GDP by 2025.

- *Combined macro-fiscal shock.* Under this scenario, which is a combination of the above shocks, the public debt will reach 104 percent of GDP by 2022, and then gradually increase to 112 percent of GDP by 2025.

- *Contingent liability customized shock.* This scenario envisages new intervention in the banking sector, equal to 10 percent of GDP. This shock is accompanied by an interest rate increase of 50 basis points, and a real growth shock as the one above (growth declining by one standard deviation in 2021–22). Under this scenario, public debt reaches 118 percent of GDP by 2025.

4. San Marino's gross external debt is set to decline on the back of continued, albeit more moderate, capital outflows. San Marino's gross external debt stood at 76 percent of GDP in 2018, where deposit liabilities of deposit-taking corporations accounted for the largest component. With continued capital outflows, including from the banking system, gross external debt is estimated to have declined to 67 percent of GDP in 2019 and projected to remain on a downward trajectory over the medium term, reaching a level of 49 percent of GDP at the end of the forecast horizon. All else equal, lower growth, a deterioration in the current account, and a slower price growth relative to that in key trading partners (real exchange rate depreciation) would result in a higher trajectory of external debt relative to the baseline.

5. The analysis is subject to several caveats reflecting limited data availability. First, due to lack of data, gross external debt does not include FDI debt instrument liabilities and, as a result, gross financing needs may be underestimated. In addition, the limited availability of external sector historical data (only two data points) requires making assumptions about averages and standard deviations of key variables, such as the non-interest current account balance, export and import growth, and non-debt creating capital flows, that are used for the stress tests.

Figure AVI.1. San Marino: Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

(In percent of GDP unless otherwise indicated)

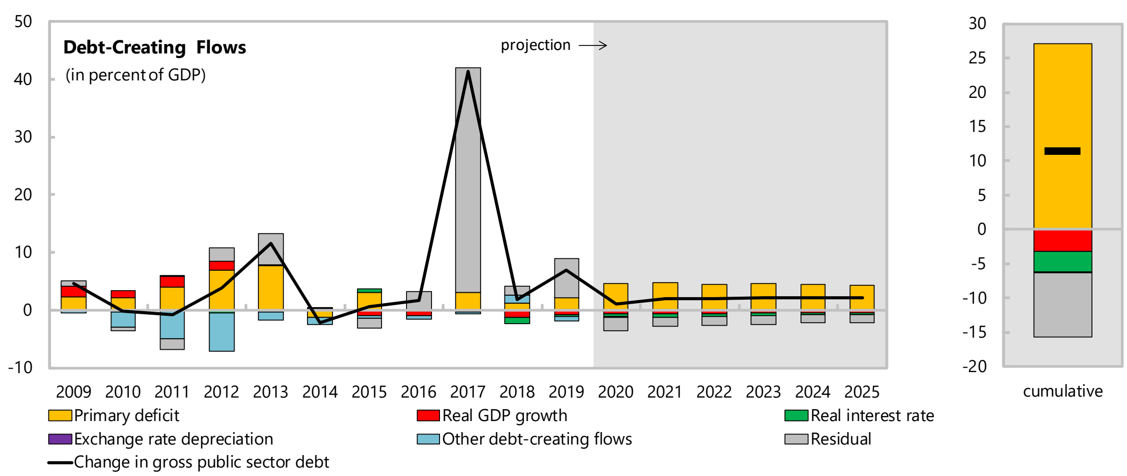
Debt, Economic and Market Indicators [1]

	Actual			Projections					
	2009-2017 [2]	2018	2019	2020	2021	2022	2023	2024	2025
Nominal gross public debt	33.4	78.8	85.8	86.9	88.9	90.8	92.9	95.0	97.1
Public gross financing needs	4.0	2.7	3.7	10.6	8.2	8.8	10.1	11.0	11.9
Real GDP growth (in percent)	-3.1	1.7	1.1	0.7	0.8	0.7	0.6	0.5	0.5
Inflation (GDP deflator, in percent)	1.2	1.9	0.9	1.2	1.5	1.5	1.5	1.5	1.5
Nominal GDP growth (in percent)	-2.0	3.6	2.0	1.9	2.3	2.2	2.1	2.0	2.0
Effective interest rate (in percent) [4]	0.6	0.4	0.5	0.6	0.8	0.9	1.0	1.1	1.2

As of December 30, 2018		
Sovereign Spreads		
EMBIG (bp) 3/		n.a.
5Y CDS (bp)		n.a.
Ratings	Foreign	Local
Moody's	n.a.	n.a.
S&Ps	n.a.	n.a.
Fitch	BBB-	BBB-

Contribution to Changes in Public Debt

	Actual			Projections							
	2009-2017	2018	2019	2020	2021	2022	2023	2024	2025	cumulative	debt-stabilizing primary balance [9]
Change in gross public sector debt	6.7	1.8	7.0	1.1	2.0	1.9	2.1	2.1	2.1	11.4	
Identified debt-creating flows	1.5	0.3	0.2	3.3	3.5	3.4	3.5	3.5	3.5	20.7	
Primary deficit	3.1	1.2	2.1	4.6	4.8	4.5	4.5	4.4	4.2	27.1	-0.8
Primary (noninterest) revenue and grants	22.8	23.0	21.6	20.2	19.9	20.0	20.1	20.1	20.1	120.6	
Primary (noninterest) expenditure	25.9	24.2	23.7	24.9	24.7	24.5	24.7	24.5	24.4	147.7	
Automatic debt dynamics [5]	0.5	-2.3	-1.2	-1.1	-1.3	-1.1	-1.0	-0.9	-0.8	-6.1	
Interest rate/growth differential [6]	0.5	-2.3	-1.2	-1.1	-1.3	-1.1	-1.0	-0.9	-0.8	-6.1	
Of which: real interest rate	-0.1	-1.1	-0.3	-0.5	-0.6	-0.5	-0.5	-0.4	-0.3	-2.9	
Of which: real GDP growth	0.6	-1.3	-0.8	-0.6	-0.7	-0.6	-0.5	-0.4	-0.4	-3.2	
Exchange rate depreciation [7]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	-2.1	1.4	-0.7	-0.2	0.0	0.0	0.0	0.0	0.0	-0.2	
Deposit Drawdown (+) (negative)	-2.1	1.4	-0.7	-0.2	0.0	0.0	0.0	0.0	0.0	-0.2	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8]	5.2	1.6	6.8	-2.2	-1.5	-1.5	-1.4	-1.4	-1.4	-9.3	



Source: IMF staff.

1/ Public sector is defined as central government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

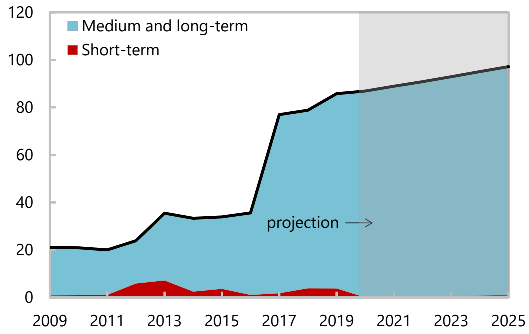
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

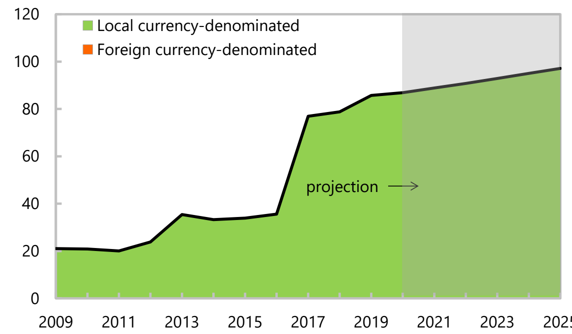
Figure AVI.2. San Marino: Public DSA—Composition of Public Debt and Alternate Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



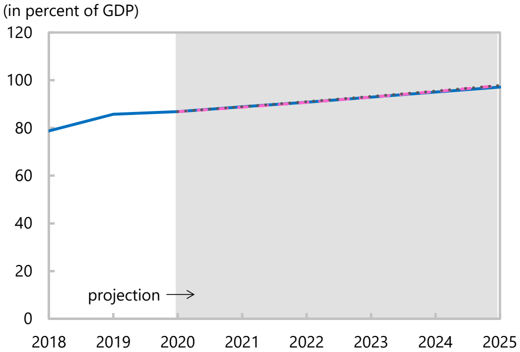
By Currency
(in percent of GDP)



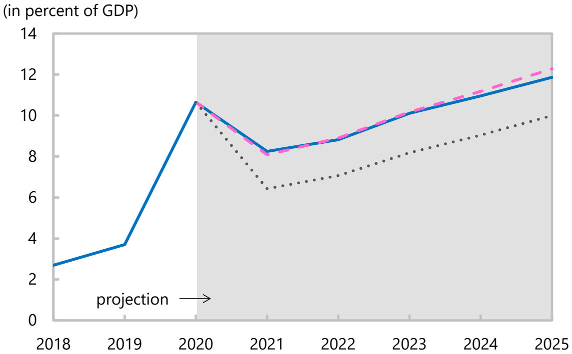
Alternative Scenarios

Baseline   Historical   Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

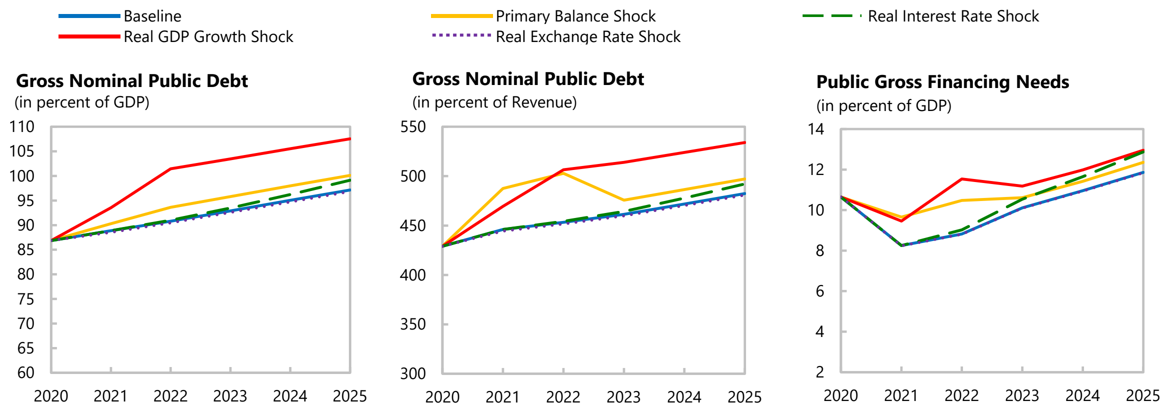
Baseline Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	0.7	0.8	0.7	0.6	0.5	0.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary Balance	-4.6	-4.8	-4.5	-4.5	-4.4	-4.2
Effective interest rate	0.6	0.8	0.9	1.0	1.1	1.2
Constant Primary Balance Scenario						
Real GDP growth	0.7	0.8	0.7	0.6	0.5	0.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary Balance	-4.6	-4.6	-4.6	-4.6	-4.6	-4.6
Effective interest rate	0.6	0.8	0.9	1.0	1.1	1.2

Historical Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	0.7	-1.5	-1.5	-1.5	-1.5	-1.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary Balance	-4.6	-2.9	-2.9	-2.9	-2.9	-2.9
Effective interest rate	0.6	0.8	0.9	0.9	1.0	1.1

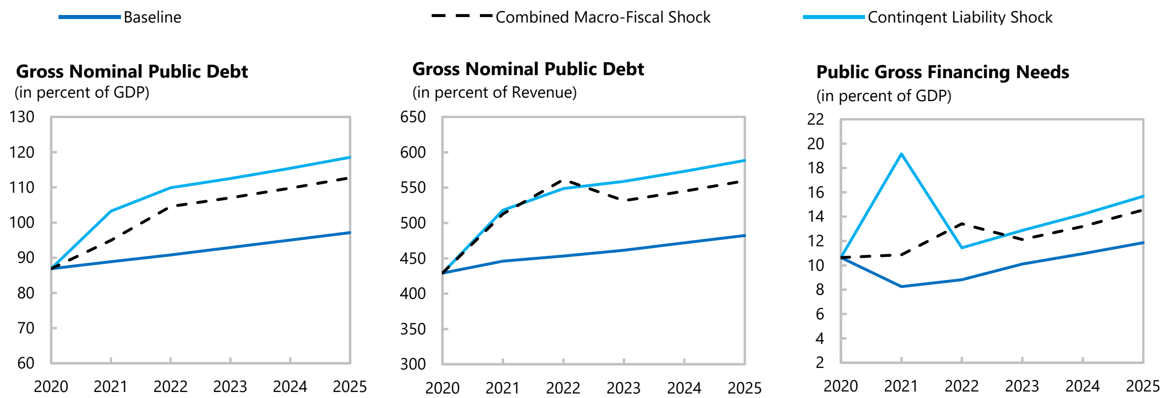
Source: IMF staff.

Figure AVI.3. San Marino: Public DSA—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(in percent)

Primary Balance Shock	2020	2021	2022	2023	2024	2025
Real GDP growth	0.7	0.8	0.7	0.6	0.5	0.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary balance	-4.6	-6.2	-5.9	-4.5	-4.4	-4.2
Effective interest rate	0.6	0.8	1.0	1.1	1.2	1.2
Real Interest Rate Shock						
Real GDP growth	0.7	0.8	0.7	0.6	0.5	0.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary balance	-4.6	-4.8	-4.5	-4.5	-4.4	-4.2
Effective interest rate	0.6	0.8	1.1	1.4	1.8	2.0
Combined Shock						
Real GDP growth	0.7	-3.3	-3.5	0.6	0.5	0.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary balance	-4.6	-7.2	-8.1	-4.5	-4.4	-4.2
Effective interest rate	0.6	0.8	1.2	1.6	1.9	2.2

Real GDP Growth Shock	2020	2021	2022	2023	2024	2025
Real GDP growth	0.7	-3.3	-3.5	0.6	0.5	0.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary balance	-4.6	-5.8	-6.7	-4.5	-4.4	-4.2
Effective interest rate	0.6	0.8	1.0	1.2	1.2	1.3
Real Exchange Rate Shock						
Real GDP growth	0.7	0.8	0.7	0.6	0.5	0.5
Inflation	1.2	1.9	1.5	1.5	1.5	1.5
Primary balance	-4.6	-4.8	-4.5	-4.5	-4.4	-4.2
Effective interest rate	0.6	0.8	0.9	1.0	1.1	1.2
Contingent Liability Shock						
Real GDP growth	0.7	-3.3	-3.5	0.6	0.5	0.5
Inflation	1.2	1.5	1.5	1.5	1.5	1.5
Primary balance	-4.6	-15.5	-4.5	-4.5	-4.4	-4.2
Effective interest rate	0.6	0.8	1.5	1.8	2.1	2.3

Source: IMF staff.

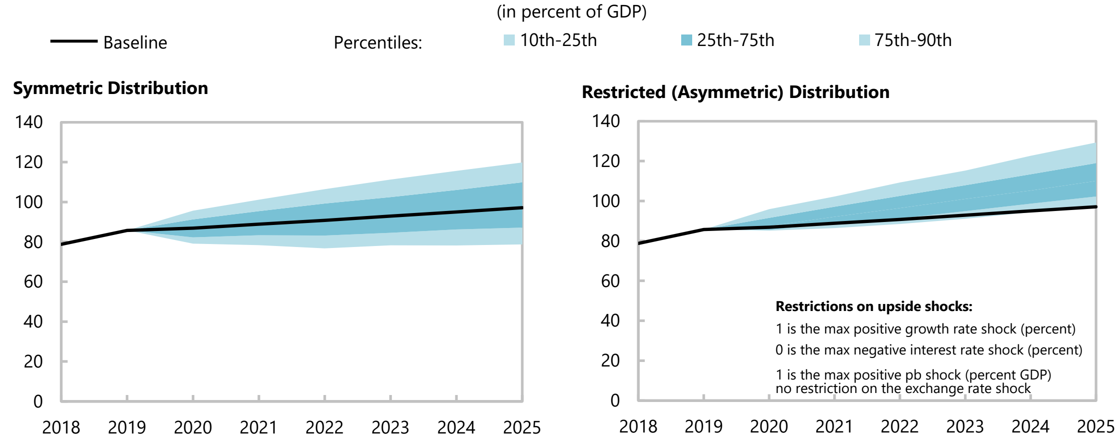
Figure AVI.4. San Marino: Public DSA—Risk Assessment

Heat Map

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

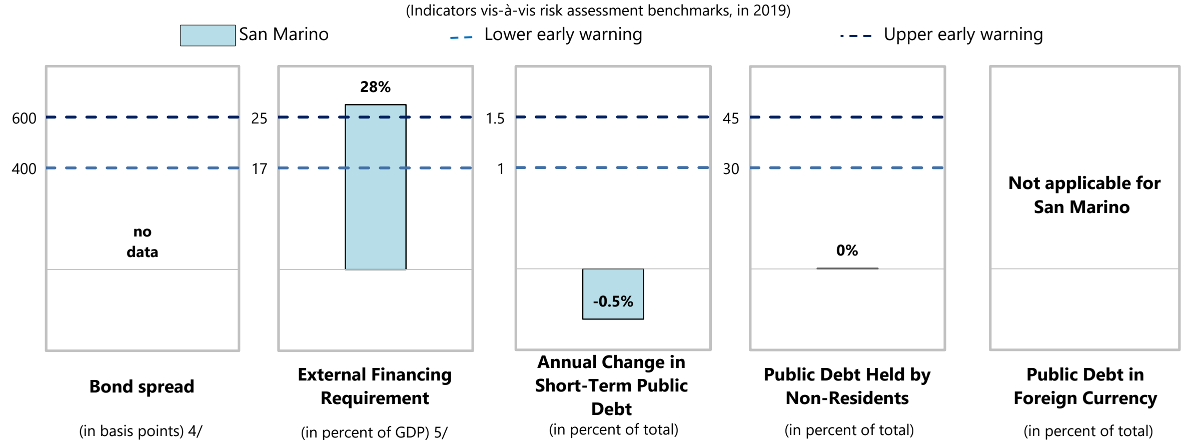
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2019)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 85% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 20% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.

Lower and upper risk-assessment benchmarks are:

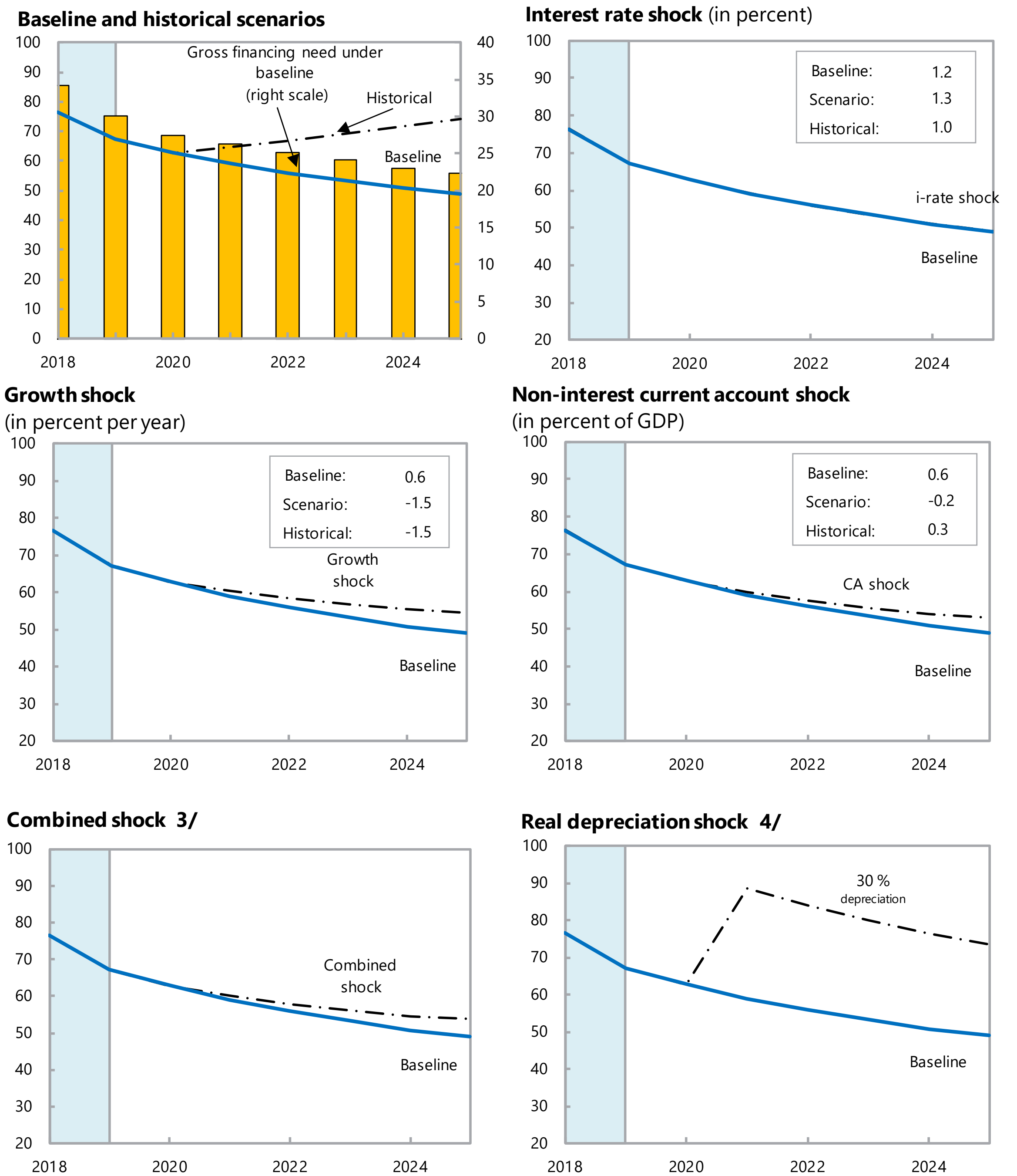
400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents.

4/ Long-term bond spread over German bonds, an average over the last 3 months, 01-Oct-18 through 30-Dec-18.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure AVI.5. San Marino: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2020.

Table AVI.1. San Marino: External Debt Sustainability Framework, 2017–24

(In percent of GDP unless otherwise indicated)

(In percent of GDP, unless otherwise indicated)

	Actual 2017	2018	2019	10-Year Historical Average	10-Year Standard Deviation	Projections 2020	2021	2022	2023	2024	2025	Debt-stabilizing non-interest current account 6/
1 **Baseline: External debt**	89.4	76.4	67.2			**63.0**	**59.2**	**56.1**	**53.5**	**51.0**	**49.1**	**0.3**
2 Change in external debt	-16.9	-13.0	-9.2			-4.2	-3.8	-3.1	-2.6	-2.5	-1.9	
3 Identified external debt-creating flows (4+8+9)	-7.6	-9.8	4.5			0.3	0.6	0.8	0.8	0.8	0.8	
4 Current account deficit, excluding interest payments	0.0	0.8	-1.5			-1.1	-0.7	-0.6	-0.5	-0.6	-0.6	
5 Deficit in balance of goods and services	-7.8	-7.8	-7.8			-6.4	-5.9	-5.6	-5.6	-5.6	-5.7	
6 Exports	159.5	161.2	161.1			157.4	154.5	152.3	150.5	148.7	148.5	
7 Imports	151.8	153.3	153.3			150.9	148.6	146.6	144.9	143.1	142.8	
8 Net non-debt creating capital inflows (negative)	-1.9	0.5	0.4			1.1	1.1	1.0	0.9	0.9	0.9	
9 Automatic debt dynamics 1/	-5.7	-11.2	5.6			0.3	0.2	0.3	0.4	0.4	0.4	
10 Contribution from nominal interest rate	0.9	0.7	0.8			0.8	0.7	0.7	0.7	0.6	0.6	
11 Contribution from real GDP growth	-0.4	-1.3	-0.9			-0.5	-0.5	-0.4	-0.3	-0.2	-0.2	
12 Contribution from price and exchange rate changes 2/	-6.2	-10.6	5.7			...	...	...	...	...	...	
13 Residual, incl. change in gross foreign assets (2-3) 3/	-9.3	-3.2	-13.7			-4.5	-4.4	-3.9	-3.4	-3.3	-2.6	
External debt-to-exports ratio (in percent)	56.1	47.4	41.7			40.0	38.3	36.8	35.6	34.3	33.1	
Gross external financing need (in billions of US dollars) 4/	0.0	0.6	0.5			0.5	0.5	0.5	0.5	0.5	0.5	
in percent of GDP	0.0	34.1	30.0			27.6	26.4	25.2	24.2	23.1	22.4	
Scenario with key variables at their historical averages 5/						**63.0**	**64.9**	**66.8**	**69.0**	**71.4**	**73.5**	**5.1**
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	0.4	1.7	1.1	-1.5	4.1	0.7	0.8	0.7	0.6	0.5	0.5	
GDP deflator in US dollars (change in percent)	6.2	13.4	-6.9	-3.6	13.2	3.4	3.9	3.6	3.4	3.6	2.0	
Nominal external interest rate (in percent)	0.9	0.9	1.0	1.0	0.0	1.2	1.2	1.2	1.2	1.2	1.3	
Growth of exports (US dollar terms, in percent)	--	9.5	-2.6	3.5	8.5	1.7	2.8	2.8	2.8	2.9	2.4	
Growth of imports (US dollar terms, in percent)	--	9.5	-2.6	3.4	8.5	2.5	3.1	2.9	2.8	2.8	2.3	
Current account balance, excluding interest payments	0.0	-0.8	1.5	0.3	1.6	1.1	0.7	0.6	0.5	0.6	0.6	
Net non-debt creating capital inflows	1.9	-0.5	-0.4	-0.5	0.1	-1.1	-1.1	-1.0	-0.9	-0.9	-0.9	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

INTERNATIONAL MONETARY FUND

REPUBLIC OF SAN MARINO

STAFF REPORT FOR THE 2020 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

March 9, 2020

Prepared by European Department

CONTENTS

FUND RELATIONS

(As of January 31, 2020)

Membership Status: Joined September 23, 1992; Article VIII

General Resources Account	**SDR Million**	**Percent of Quota**
Quota	49.20	100.00
Fund holdings of currency	37.05	75.30
Reserves tranche position	12.15	24.70

SDR Department	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	15.53	100.00
Holdings	8.88	57.17

Outstanding Purchases and Loans
None

Latest Financial Arrangements
None

Projected Obligations to Fund 1/
(SDR Million; based on existing use of resources and present holdings of SDRs)

	Forthcoming				
	2020	**2021**	**2022**	**2023**	**2024**
Principal					
Charges/Interest	0.05	0.05	0.05	0.05	0.05
Total	0.05	0.05	0.05	0.05	0.05

1/ When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Arrangements:
Prior to 1999, the currency of San Marino was the Italian lira. Since January 1, 1999, San Marino uses the euro as its official currency. The central monetary institution is the Central Bank of San Marino (CBSM). Foreign exchange transactions are conducted through commercial banks without restriction at rates quoted in Italian markets. There are no taxes or subsidies on purchases or sales of foreign exchange. San Marino's exchange system is free of restrictions on the making of payments and transfers for current international transactions, except for those maintained solely for the preservation of national or international security and which have been notified to the Fund pursuant to Executive Board Decision No. 144-(52/51).[1] The current classifications of San Marino's de jure and de facto exchange rate arrangements are "no separate legal tender".

[1] EU Regulations are not directly applicable to San Marino due to Article 249 of the Treaty Establishing the European Community, but they may well be applied as a result of the legal relationship between San Marino and the EU, including the Monetary Agreement.

Latest Article IV Consultation:
San Marino is on a 12-month cycle. The previous Article IV consultation discussions took place during January 23–February 1, 2019, and the consultation was concluded on March 20, 2019 (IMF Country Report No. 19/85).

FSAP Participation:
A review under the Financial Sector Assessment Program (FSAP) was completed in 2010.

Technical Assistance:

Year	Department/Purpose
1997	STA Multi-sector assistance
2004	STA Monetary and financial statistics
2005	MFD Deposit insurance
2008	STA GDDS metadata development
2009	LEG AML/CFT
2011	STA National accounts statistics
2012	STA Government finance statistics
2012	STA Monetary and Financial Statistics
2013	STA Balance of Payments Statistics
2014	FAD Expenditure Policy
2016	MCM Cassa di Risparmio Bank Restructuring
2018	FAD Foundations for a Value Added Tax
2018	FAD VAT Administrative Readiness Assessment
2018	STA Balance of Payments statistics
2019	LEG Enterprise Restructuring and Individual Over-indebtedness
2019	STA Enhanced General Data Dissemination System (E-GDDS)

Resident Representative: None

STATISTICAL ISSUES

(As of January 31, 2020)

Assessment of Data Adequacy for Surveillance
General: Data provision is broadly adequate for surveillance, but data gaps exist. Progress has been made since San Marino's participation in the IMF's General Data Dissemination System (GDDS) on May 16, 2008, but important weaknesses in the statistical database remain, mainly due to resource constraints. National accounts as well as monetary and financial sector data are compiled according to international standards, but some key statistics (in real and fiscal sectors) are available only with delays and, in many cases, are at a lower-than-standard frequency and level of detail. Following technical assistance provided by the IMF Statistics Department, San Marino started compiling balance of payments and international investment position (IIP) in 2018.
National Accounts: National accounts data for 2007 onward have been calculated in accordance with ESA95, and data are compiled annually based on production and expenditure approach, albeit with about 10 months delay. Methodological improvements starting 2015 lead to historical series revision. Employment data are available monthly. An industrial production index based on electricity consumption, launched in 2000, became available monthly in 2009 but has been discontinued. A purchasing managers' index has been compiled starting in 2010.
Price Statistics: Consumer prices data are available monthly.
Government Finance Statistics: The authorities have provided data for the central government, state-owned enterprises, and social security fund for 2004–18, and preliminary data for 2019. However, some of the data have not been compiled in accordance with IMF standards. Financing items, such as amortization, are included as expenditures while "financing needs" are included among revenues. The authorities report annually fiscal data in the GFS Yearbook, revenues, expenses and stock of assets and liabilities for the General Government in the format of the GFSM2014, the last year reported is 2018.
Monetary and Financial Statistics: In 2018, the Central Bank of San Marino began using the standardized Report Forms to submit Monetary and Financial Statistics to the Fund for use in surveillance and for dissemination in *International Financial Statistics*. Data for Other Financial Corporations are not available. There is a need for improving the classification of commercial bank assets/liabilities.
Financial Sector Surveillance: The authorities regularly report financial soundness indicators (FSIs). Eleven out of twelve core and five out of thirteen encouraged FSIs for deposit takers are disseminated on a quarterly basis. FSIs for other financial corporations, nonfinancial corporations, and households are not reported. The authorities should shift to a timelier provision of quarterly FSI data to the Fund with a time lag of no more than four months.
External Sector Statistics: In 2018, San Marino started compiling balance of payments and IIP. Frequency, coverage and reporting should be improved. Data are reported once a year and with a long lag. In addition, there are several data gaps in the balance of payments, IIP, and external debt components. Going forward, the authorities should sustain efforts to improve the frequency, coverage, and reporting of relevant statistics.

San Marino: Common Indicators Required for Surveillance
(As of January 31, 2020)

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	Jan 2020	Jan 2020	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Sept 2019	Jan 2020	M	M	M
Reserve/Base Money	Sept 2019	Jan 2020	M	M	M
Broad Money	Sept 2019	Jan 2020	M	M	M
Central Bank Balance Sheet	Sept 2019	Jan 2020	M	M	M
Consolidated Balance Sheet of the Banking System	Sept 2019	Jan 2020	M	M	M
Interest Rates[2]	Sept 2019	Jan 2020	M	M	M
Consumer Price Index	Dec 2019	Jan 2020	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]—General Government[4]	2018	Sep 2019	A	A	A
Revenue, Expenditure, Balance and Composition of Financing[3]—Central Government	2018	Sep 2019	A	A	A
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2019	Jan 2020	A	A	A
External Current Account Balance	2018	Nov 2019	A	A	A
Exports and Imports of Goods and Services	June 2019	Nov 2019	M	M	M
GDP/GNP	2018	Nov 2019	A	A	A
Gross External Debt	2018	Nov 2019	A	A	A
International Investment Position [6]	2018	Nov 2019	A	A	A

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[2] Deposit and lending rates.

[3] Foreign, domestic banks, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).