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**Statement by Mr. Palei and Mr. Tolstikov on Republic of San Marino  
(Preliminary)  
Executive Board Meeting  
November 15, 2021**

We thank staff for the informative paper and Mr. Fanizza and Mr. Spadafora for their helpful Buff statement.

**San Marino's response to the pandemic was timely and effective.** The authorities adopted a comprehensive policy package to boost the health sector and support employment, providing targeted relief to households and businesses. They also implemented an effective vaccination campaign – one of the fastest in Europe. These measures limited the impact of the COVID-19 crisis and laid the groundwork for future recovery. At the same time, the authorities have taken decisive steps in addressing vulnerabilities in the banking system, recapitalizing it through a large-scale public borrowing.

**A sharp increase of the public debt poses new challenges for the authorities' fiscal policies.** After recapitalizing the state-owned CRSM bank and acquiring the BNS liabilities, the official public debt increased to 105 percent of GDP in July 2021, from 32 percent of GDP at end-2019. The new three-year, 27 percent of GDP Eurobond creates a substantial refinancing risk in 2024. Staff propose to substitute the current short-term debt with the new one, in order to maintain a high level of fiscal liquidity ahead of the 2024 debt repayment and preserve market confidence. We wonder why it has to be done now and not later, if needed, closer to the debt repayment peak? *Staff comments are welcome.*

**Taking into account a heavy debt burden, prudent fiscal policies are essential.** To ensure the declining path of the public debt, the authorities should aim at ambitious primary balance targets in the near future. To achieve fiscal consolidation, measures on both revenue and expenditure sides are needed. We, therefore, welcome the authorities' commitment to

growth-friendly fiscal reforms, including introduction of VAT. On the spending side, reforms should include the rationalization of social benefits and better targeting of social programs. Restoring sustainability of the pension system cannot be delayed. The need to enhance the debt management capacity is also becoming more urgent.

**The bailout of the banking system was done at huge costs to taxpayers.** The recapitalization of the CRSM bank at 47 percent of GDP is the costliest banking crisis in history, especially if the resolution of the BNS at 21 percent of GDP is added. Have these operations restored the viability of the banking system? Were the private lenders and depositors of the CRSM fully bailed out? Were haircut options for the private creditors considered? With an extraordinarily high NPL level (63 percent of loans and 150 percent of GDP) the comprehensive program to address this issue is needed. We welcome the establishment of the asset management company. Revamping the outdated insolvency framework should also be a priority.

**The fiscal and financial sector reforms should be complemented by structural policies aimed at supporting long-term growth.** We welcome the work on a comprehensive reform of the labor market to increase its flexibility and enhance training and re-training opportunities. We note that the negotiations of the association agreement with the EU are advancing. *Could staff comment on why San Marino, despite being de-facto fully integrated into the Italian economy, prefers to maintain its status outside the EU, especially after the collapse of its offshore banking economic model?*