

GREEN/20/18

March 23, 2020

**Green Statement from Mr. Lischinsky and Mr. Corvalan on the
Republic of San Marino—2020 Article IV Consultation (SM/20/63)**

We thank staff for the informative report on the Republic of San Marino.

The offshore banking model is no longer functioning and the process towards more transparency and enhanced integrity in the global financial sector is pushing the authorities to reshape the sector to adapt it to the new environment. Since the Global Financial Crisis (GFC) around one-third of the output was lost and is categorized as one of the deepest and longest recessions in Europe. The outbreak of COVID-19 is putting more strain on the already troubled economy through tourism, supply chains, and confidence in the financial system.

Banking sector adaptation to the new environment is taking place. The authorities are fully aware of the situation and they concurred with staff's advice on the need to speed up the balance sheets repair process. Capitalization of viable banks are urgent as well as cleaning up NPLs. Nevertheless, due to insufficient policy implementation on this front, plus some concerns on the accuracy of the financial system asset quality, the level of confidence is deteriorating. Financial outflows might continue creating severe liquidity stress on the system. We encourage the authorities to speed up the financial clean-up process and to offer the CBSM with the necessary legal power and tools to do so.

Fiscal sector fragility needs quick fixes. We encourage the authorities to reconsider tapping external markets to support liquidity or enhance resilience to shocks. Because of the financial crisis, fiscal liabilities increased dramatically over the last decade, raising the public debt-to-GDP ratio from 20 to 86 percent. The last figure includes liabilities such as tax credits, CRSM legacy losses, and BCIS bailout. The debt-to-GDP ratio at this level is categorized as unsustainable. Therefore, emphasis on revenue mobilization and improvements in the composition of government expenditure are appropriate and urgently needed. On the former, we were surprised by the authorities' divergences of views on the capacity for VAT to increase revenues. *We would appreciate staff's assessment of this issue.* On the latter, we fully agree that creating budget rigidities with current expenditures is not a growth-friendly fiscal strategy to follow.

Strengthening labor supply, rethinking the current benefits, and investing in infrastructure might alleviate the one-third loss of output observed since the GFC. It is

striking to observe the youth unemployment rate at around 25 percent. This figure clearly shows the crisis denting the economy and the need to reallocate the workforce in the new economy model. We found Annex IV of the report interesting on how to tackle these bottlenecks and unleash the economic potential to promote inclusive growth for the medium term.

With these comments, we wish the people of San Marino every success in their future endeavors in these difficult times.