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REPUBLIC OF SAN MARINO

2014 ARTICLE IV CONSULTATION—STAFF REPORT; PRESS RELEASE; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE REPUBLIC OF SAN MARINO

April 2014

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 2014 Article IV consultation with San Marino, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on April 23, 2014, following discussions that ended on February 7, 2014, with the officials of San Marino on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on March 24, 2014.
- An **Informational Annex** prepared by the IMF.
- A **Press Release** summarizing the views of the Executive Board as expressed during its April 23, 2014 consideration of the staff report that concluded the Article IV consultation with San Marino.
- A **Statement by the Executive Director** for San Marino.

The publication policy for staff reports and other documents allows for the deletion of market-sensitive information.

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REPUBLIC OF SAN MARINO

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION

March 24, 2014

KEY ISSUES

Context: The global crisis and tense relations with Italy triggered a 30 percent GDP contraction since 2008 and a sea change in San Marino's off-shore banking model. The banking system has undergone deep restructuring, with several banks intervened and the largest bank requiring large injections of public capital. The economic downturn and bank recapitalization needs have put significant pressure on public finances. Nevertheless, the very recent exit from the Italy's tax black list should facilitate the recovery and the transition to a new growth model.

Challenges: Lay foundations for sustainable growth by advancing the cleanup of the banking system, realign fiscal policy with new economic realities, and integrate into international markets.

Key policy recommendations:

- ***Financial sector policy***. Complete recapitalization of the largest bank, diluting shareholders unconditionally and taking control of the board and management. For all banks, step up on-site supervisions to ensure adequate provisioning, and undertake an external asset-quality review coupled with appropriate contingency plans if capital needs are identified.

- ***Fiscal policy.*** Further consolidation of 3 percent of GDP is needed over the medium term to put public debt on a sustainable path and rebuild buffers.

- ***Structural policy***. Stay committed to openness and transparency to fully normalize relations with the international community; improve nonprice competitiveness to facilitate the reallocation of resources to the nonbanking sector.

Traction of past Fund advice: The authorities have recognized plausible losses in the largest bank in line with Fund advice, but the modalities of public recapitalization remain problematic. The 2014 budget delivers significant savings, consistent with past Fund advice.

Approved By
Aasim M. Husain and Peter F. Allum

Discussions for the 2014 Article IV consultation were held in San Marino during January 29−February 7, 2014. The mission comprised Messrs. Miniane (head), Gracia, and Lanau (all EUR), and Parker (MCM). Ms. Spinella (OED) joined the meetings. The mission met with Minister of Finance Felici, Minister of Foreign and Political Affairs Valentini, Minister of Industry Arzilli, Minister of Labor Belluzzi, Central Bank President Clarizia, Central Bank Director General Giannini, other senior public officials, and representatives from parliament, the private sector, and civil society.

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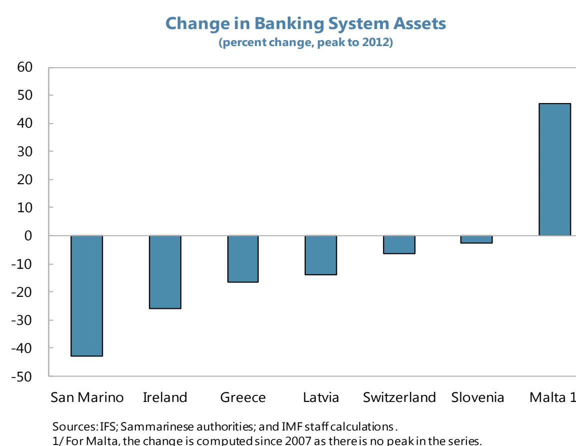
CONTEXT, OUTLOOK, AND RISKS

1. **Since 2008, GDP in San Marino has fallen by a cumulative 30 percent**. The decline encompassed all key sectors including banking, manufacturing, and construction. As a result, the unemployment rate has jumped from 3 percent five years ago to around 9 percent now, while employment has declined 10 percent. Three key factors combined to cause the economic crisis in San Marino:

- A 2009 fiscal amnesty in Italy led to the outflow of 60 percent of nonresident deposits held in Sammarinese banks, or 40 percent of total deposits.
- In 2010, Italy imposed higher reporting requirements on Italian businesses dealing with countries on the tax black list, including San Marino. The Bank of Italy also limited transactions between Italian and Sammarinese financial institutions.
- The economic downturn in Europe reduced demand for tourism and Sammarinese exports.

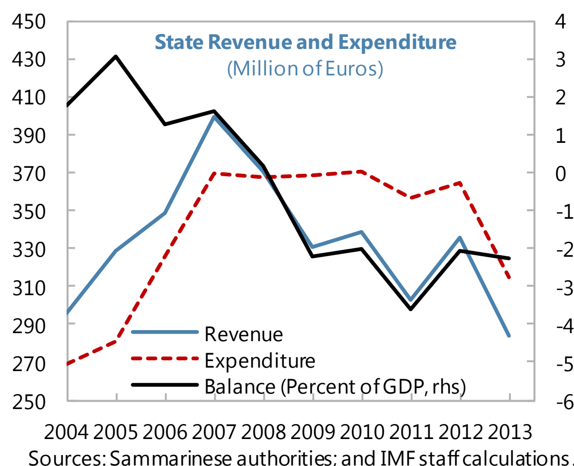
2. **The financial sector has undergone sharp adjustment.** High liquidity in the system allowed banks to withstand the shock to deposits. However, several bank and nonbank financial institutions became insolvent, prompting a major consolidation in the sector. Total assets fell from €11.5 billion in 2008 to €6 billion in 2012. Similarly, assets under management of fiduciary companies have fallen by 90 percent to less than €500 million.



3. **Cassa di Risparmio della Repubblica di San Marino (CRSM), the largest bank, has required 13 percent of GDP in public support**. CRSM's assets accounted for 37 percent of the system and 240 percent of GDP in 2008. Recapitalization needs resulted from large losses on its investment in the Italian Delta group (intervened by Italian supervisors in 2009 and put under compulsory administration). Going forward, further capital needs cannot be ruled out (see below).

4. **The deep recession and bank recapitalization costs are weighing heavily on public finances.** Despite some consolidation measures—notably an extraordinary income tax surcharge, and a temporary real estate tax—the central government balance shifted from a surplus of some 2–3 percent of GDP before the crisis to deficits of 2–3 percent of GDP. This, together with bank recapitalization costs has tripled central government debt to 30 percent of GDP, while simultaneously exhausting precrisis cash buffers of 15 percent of GDP. The crisis is also having a negative impact on public pensions. Precrisis forecasts projected deficits in the pay-as-you-go system to occur sometime around 2030; such deficits could now materialize in a few years.

5. The baseline forecast is for a modest recovery. Both banking system deposits and assets have been relatively stable since their trough in late 2012, industrial production saw positive (albeit small) y/y growth in 2013, and industrial employment appears to have stabilized too. In addition, the recovery in Europe should stimulate external demand going forward. However, important sectors like construction are still contracting sharply, and fiscal consolidation envisaged in the 2014 budget and beyond (see below) could weigh on activity. All in all, staff project a modest recovery to start in the second half of the year, implying a 1 percent contraction for the full 2014 (a significant improvement over last year's estimated -5 percent) and 1 percent growth next year.



Sources: Sammarinese authorities; and IMF staff calculations.

6. Upside risks to the baseline are significant and stem from San Marino's recent exit from Italy's black list (see Appendix I). Following ratification in late 2013 of a landmark bilateral double taxation treaty, incorporating a legal framework for the exchange of tax information, Italy removed San Marino from its tax black list in February. Concretely, Italian firms dealing with Sammarinese counterparts will no longer be subjected to additional reporting requirements to prove they are not evading VAT. Greater ease of doing business could provide a jolt to the recovery in San Marino, though the impact is difficult to quantify at this stage. On the downside, San Marino remains exposed to the risk of slower than projected growth in Europe, particularly Italy, and to further bank capital shortfalls domestically that could undermine public finances and deepen GDP losses.

7. San Marino faces daunting medium-term challenges. Sustaining growth and job creation will require diversifying away from banking, and integrating more fully into neighboring Emilia-Romagna—as well as Europe and the world. The exit from the black list eliminates a key roadblock to this process, but the process will still be long and arduous. Even if upside risks to short term growth materialize, precrisis GDP levels will remain well out of reach; a significant share of the GDP decline is permanent after the demise of the old economic/banking model.

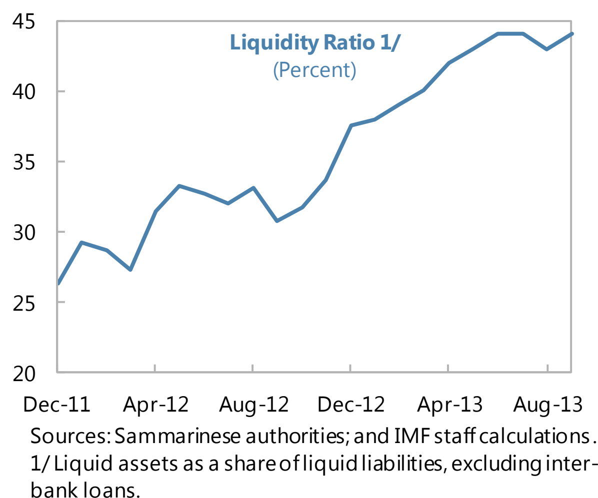
Authorities' views

8. The authorities agreed that economic activity will remain weak in 2014, but believe that exiting the black list would boost economic confidence and, eventually, growth. At the same time, they emphasized that the exit from the black list, which they see as proof of their commitment to openness and transparency, should not be used as an excuse to avoid deep reforms needed to return to sustained growth.

POLICY DISCUSSIONS

A. Financial Sector

9. The deposit base has stabilized, and liquidity buffers are now comfortable. Deposits have been stable since early 2012, after falling by close to €600 million in 2011 and €2.5 billion in 2009–10. This stabilization, together with limited demand for loans, has given banks breathing room to replenish their liquid assets. As a result, the coverage of short-term liabilities has improved and is now over 45 percent for the banking system as a whole.[1] More important given that resident deposits have proved very stable, liquid assets now cover about 140 percent of short-term nonresident liabilities. In the case of CRSM, immobilized assets in Italy related to the Delta restructuring are slowly being repatriated as part of the creditors' agreement, boosting liquidity.



Sources: Sammarinese authorities; and IMF staff calculations.
1/ Liquid assets as a share of liquid liabilities, excluding inter-bank loans.

10. System wide buffers also include contingent credit lines at the central bank and a few private banks. The credit line allows the Central Bank to repo ECB-acceptable securities for cash with a solid foreign private counterpart on a three to twelve month maturity, which it can then use to inject liquidity if needed. Some of the largest banks have similar lines available to them on a bilateral basis. Generally, liquidity risks appear low, reflecting the high liquidity ratio of Sammarinese banks and the central bank's contingent credit line (the counterparty to which, in turn, has access to LOLR facilities).

11. While liquidity risks have abated, capitalization concerns remain present. Under pressure from supervisors, CRSM significantly increased its provisions against losses on its Delta exposure in the first half of 2013 (recorded in the final 2012 accounts). The bank's capital adequacy fell to 6 percent, well below the 11 percent prudential requirement. Given that the bank is of systemic importance and that current shareholders have no means to recapitalize it, state intervention was justified and necessary. This led parliament to approve in late 2013 a €85 million public capital injection, on top of the €95 million provided in late 2012 and early 2013 (see Box 1). Total public support to date amounts to 13 percent of GDP. Given the government's limited access to financing other than the domestic banking system, the latest recapitalization will be implemented by issuing a ten year, zero-coupon bond subscribed by CRSM with an implied return of 1.43 percent. This interest rate is well below indicative benchmarks (e.g., the 10-year Italian sovereign rate) and could impair the bank's future profitability.

[1] This excludes interbank loans within San Marino.

Box 1. CRSM: Past Recapitalizations

CRSM's capital buffers were not enough to absorb the losses from its Delta and non-Delta investments. Given that the bank is systemic, and that its shareholders had limited means to recapitalize it, the best approach would have been to nationalize it, with full dilution of shareholders and state control of management and board. This would have (i) respected the tenet that shareholders should be the first to bear losses; (ii) protected taxpayers' interests, by giving them a claim on future profits commensurate with the risk they are bearing; and (iii) ensured a meaningful change in the bank's business model to give it a realistic chance to return to profitability.

Fearing a negative public reaction to nationalization, the government and parliament decided instead in late 2012 to recapitalize the bank by extending a low interest loan to the shareholders in the amount of €60 million, which the shareholders then injected as their own capital (together with €20 million of their own funds). With this, they retained their equity stake in the bank. In exchange, the government obtained some concessions, such as the possibility to name the chairman of the bank's board and two other board members.

Subsequently, in early 2013 the bank issued subordinated debt in the amount of €40 million, €35 million of which were subscribed by the social security fund. This was the second instance of public recapitalization with no dilution of shareholders and limited or no conditionality.

12. Staff warned that the modalities of the recapitalization plan continue to fall well short of international best practice. As part of the recapitalization process, the state and bank shareholders have entered into a provisional agreement on the modalities and conditionality of the latest recapitalization tranche. Staff argued that, ideally, shareholders should have been fully diluted and the state should have become the sole owner of the bank (see box). Hence, the partial dilution of shareholders contemplated under the agreement is not ideal, but it still represents progress relative to past practice of no dilution. It is also positive that the state will now get to nominate six of the nine board members, giving it better control over the bank's restructuring process. Still, various aspects of the agreement remain highly problematic and should be reconsidered:

- *Shareholder dilution will not be upfront and unconditional.* According to the agreement, the public funds injected will be converted into equity capital (diluting existing shareholders) only if the central bank approves CRSM's financial forecasts as providing a good basis for compliance with prudential requirements in coming years. (This is viewed as a safeguard by the government for its investments.) This role for the central bank potentially jeopardizes its independence, in that to achieve a best practice outcome for shareholder dilution, it may have to compromise its standards in assessing CRSM's financial strategy (which appears to involve optimistic assumptions).

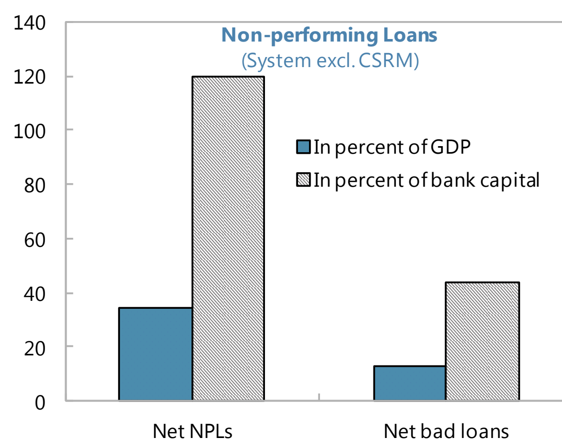
- *Shareholder dilution will be capped by an unrealistically high valuation of the bank.* The provisional agreement appears to set an unrealistically high value for the bank, based on generous assumptions on goodwill and limited consideration of current and future profitability. In turn, this high value would result in a correspondingly lower stake accruing to the state, now estimated at just 46 percent even if the full €85 million are converted into equity.

- *The agreement should not give current shareholders a disproportionate say on decisions.* In the current agreement, the state cannot sell its stake in the bank without the approval of the current shareholders. This is in violation of the state's right to decide what is best for itself and the country.

13. Further capital needs in CRSM cannot be ruled out. Capital injections so far will result in a capital adequacy ratio of 10 percent, below the 11 percent minimum. More generally, losses on Delta or other assets could exceed current provisions, while CRSM's profitability will remain constrained since about half of its assets do not earn any interest.[2] With this in mind, staff urged the central bank to assign a full time on-site examiner at CRSM.

14. The viability of CRSM will depend on the design and execution of a credible restructuring plan. While the bank has taken some measures to reduce costs, it is still missing a pluriannual plan that assesses what the sustainable size of the balance sheet could be, what the bank's comparative advantage is in the new San Marino context, and what the resource implications to operationalize this comparative advantage are. With the state now due to appoint six of the nine members of CRSM's board, staff urged the government to pick highly qualified turnaround experts that will be able to design and execute a proper restructuring plan.

15. The rest of the banking system meets minimum capital ratios, but risks remain there as well. All other banks have capital above 11 percent, with the two largest banks after CRSM at 16.6 and 13.7 percent, respectively.[3] However, the crisis has brought about high nonperforming loans. In the system excluding CRSM, the gross NPL ratio stands at 24 percent of total loans, while the NPL ratio net of provisions accounts for 120 percent of banks' capital and 34 percent of GDP. Thus, capital buffers could prove insufficient outside of CRSM as well, although it should be noted that several banks have proven capable of raising private capital in recent times.



Sources: Sammarinese authorities and IMF staff estimates.

[2] As part of the Delta creditor's agreements, CRSM holds a credit over four finance companies in Italy, which repay CRSM as they recover their own assets. This credit does not earn interest.

[3] These two banks account for about 50 percent of banking system assets.

16. Ensuring adequate provisioning will be key. The crisis has impaired profitability, reducing incentives for provisioning. At the same time, regulations in San Marino provide banks with significant discretion in this area, as banks have to provision on the basis of *expected* losses over the entire life of the asset. To compound the problem, resources that the central bank can devote towards supervision have been reduced, resulting in less frequent than ideal on-site supervisions, even as off-site supervision and monitoring continues. At prima facie, the current provisioning rate does seem on the low side, being at 40.2 percent for all NPLs and 54.3 percent for bad loans (loans to insolvent borrowers, the worst category of NPLs). Staff thus called for increased resources for and a stricter regime of on-site supervisions, to ensure that banks are promptly identifying and tackling any emerging pressure point, that they are properly classifying NPLs, and that they are adequately provisioning for losses. The CBSM could also consider more stringent provisioning requirements, albeit gradually.

17. An external asset quality review in line with those to be conducted elsewhere in Europe could help increase confidence in the banking system. The exercise could sharpen clarity about the true state of the banks. It would also force the banks to recognize losses now, avoiding an evergreening of dubious assets that would delay the needed restructuring in the system. Responses to any capital shortfalls identified by the exercise should first and foremost be market-based, including injections by current shareholders as has happened recently outside CRSM. Still, the government should have contingency plans ready beforehand, including a public backstop if needed.[4]

18. The bank resolution framework should be amended, to give the central bank better tools for speedy and least cost resolution. At present, there is no special bank resolution regime separate from general bankruptcy law. Although the Banking Law grants the central bank special corrective powers, it is possible for the courts to reverse some central bank decisions. The Banking Law should ideally be amended to introduce a special bank resolution regime administered by the central bank; the law should legislate, at a minimum, that no court can reverse central bank decisions. Moreover, early intervention measures and other resolution tools (e.g., purchase and assumption and bridge bank) should be introduced, together with a "least-cost" test for bank resolution, so as to comply with the Financial Stability Board's Key Attributes for Effective Financial Institution Resolution. As part of the bank resolution framework, the deposit insurance fund with up to €50,000 coverage is a key tool, but staff recommended moving gradually to a fully ex-ante funded model in line with the draft EU directive on deposit insurance.

Authorities' views

19. The authorities noted that significant steps have been taken to address CRSM, and agreed that an external asset quality review could be beneficial. The revocation of the law protecting the foundation's majority stake in CRSM was an important political achievement, paving the way for the dilution of current shareholders and for a proper restructuring of the bank. They

[4] As discussed below, realistic fiscal consolidation would give the Senate room for significant further public recapitalization if needed, still keeping debt on a sustainable path.

emphasized that the agreement between the state and the foundation is provisional, leaving room to revisit its key clauses. They added that most decisions at the bank's board are taken by simple majority, hence the ability to nominate six board members (for which they will seek highly qualified candidates) will give the state de facto control over the bank. Outside of CRSM, they concurred with staff on the need to ensure proper provisioning and ensure that banks not evergreen dubious loans, and will consider an external asset quality review.

B. Public Finances

20. The 2014 budget contains welcome savings of about 1 percent of GDP, though not all of high quality. In December, parliament approved a major reform of direct taxation. The reform increases efficiency by broadening the base and lowering marginal rates, and results in an estimated gross yield of about 1¼ percent of GDP. Net revenue gains in the budget will be only about 0.3 percent of GDP, however, because the real estate tax and the extraordinary surtax on income introduced during the crisis were eliminated. On the expenditure side, the budget contemplates difficult but needed cuts in wages, though with some protections for lowest earners. These cuts are complemented with incentives for early retirement and a 25 percent replacement ratio in order to facilitate a reduction in the size of the public service. Other measures, such as the decision to lower transfers to the social security fund, are not sustainable in the long term and only result in lower central government deficit at the expense of lower social security surpluses.

21. Despite progress, staff argued that significant additional budgetary savings will need to be found over the medium term. As recent experience shows, San Marino's inherent vulnerabilities as a very small and open economy argue in favor of having ample fiscal buffers. While public debt is not very high at present, it will continue to increase under the baseline even without further bank recapitalizations (see Appendix II). A consolidation of 3 percentage points of GDP (€35–40 million) over the next few years is needed to put debt on a downward path and clear space for possible bank recapitalization needs. Consolidation would also help limit future financing needs, an important consideration given limited financing options at present. If exit from the black list leads to a stronger than expected recovery, the need for consolidation could fall to around 2 percent of GDP, but it would not disappear altogether (see Box 2).

22. The ongoing spending review will help increase public spending efficiency and identify areas of savings. The review, which was launched in 2013 and is being complemented with Fund technical assistance, is appropriately focusing on the following:

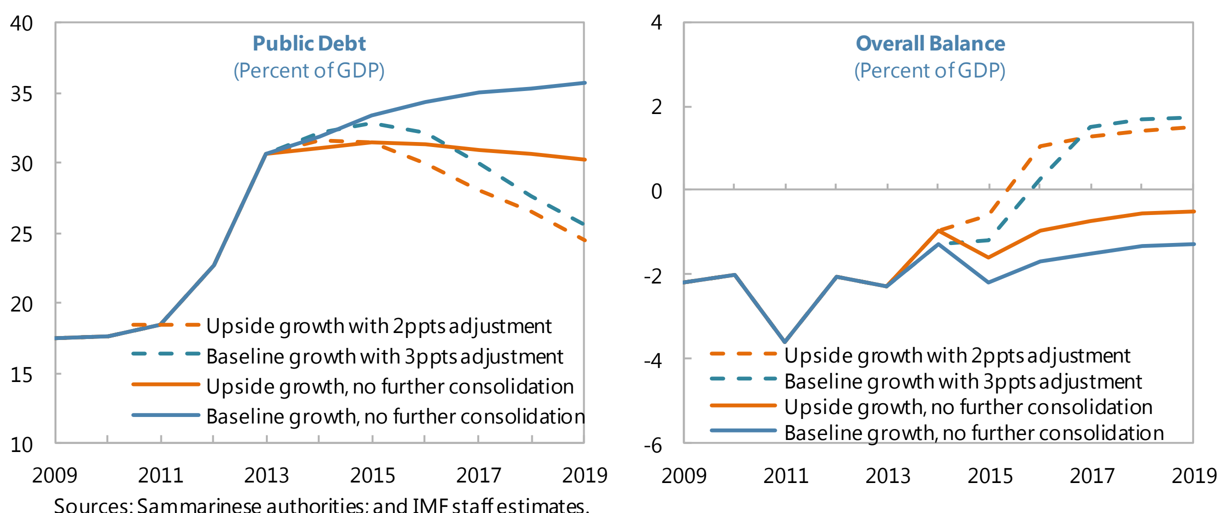
- *Wages.* Public sector wages are about 10 percent higher than in the private sector, with the gap increasing with seniority. In addition, special allowances and indemnities, unrelated to merit, account for a large share of public wages. Some caps have been introduced in the 2014 budget.

- *Health benefits.* Spending in this area has increased in recent years despite the state's reduced means, reflecting strong demand for service in the absence of co-payments and other rationing devices. Also, capacity utilization, measured by hospital occupancy rates, is low. Any reform in this area has to account for the country's size and need to import some of its care.

- *Public pensions.* The system is no longer financially viable due to high replacement ratios (over 80 percent), low contribution rates of some 20 percent, and low effective retirement age partly because of early retirements (including seniority pensions not based on actuarially fair rules).

Box 2. Adjustment Needs Under an Upside Scenario

The exit from Italy's black list could result in higher GDP and hence less fiscal adjustment needs. If the upside scenario results in 6 percent higher GDP by 2019 (commensurate with average annual growth over 2014–19 that is 1 percentage points higher than the 0.8 percent assumed in the baseline), debt would stabilize around 30 percent instead of increasing towards 35 percent by 2019 as in the baseline. Moreover, a 2 percent of GDP cumulative adjustment would be enough to put debt on a downward trajectory, and would build up comparable space for potential recapitalization needs as the 3 percent adjustment under the baseline GDP path.



23. There is room to further increase the tax intake and improve the efficiency of the tax system. The reform of indirect taxation, to be presented for discussion mid-year, would replace the current tax on imports with a full VAT system. Introducing a VAT in such a small country will be technically challenging but, if properly executed, it can deliver significant efficiency and revenue gains relative to the current monofase tax.[5] Separately, the real estate tax should be reinstated as it is a relatively un-distortive source of revenue. An alternative would be to increase the yield from imputed rents, which are included as part of taxable personal income, but this would require updating cadastral values.

[5] The yield from indirect taxes including the monofase amounts to 10 percent of GDP, versus 12 percent in Italy and some 12½ percent on average across Europe.

24. Financing pressures are manageable, but the growing fiscal-financial nexus needs to be tackled by seeking external market access. With a liquid banking system and moderate financing needs, funding will not be a problem in the short term. However, the combination of rising debt and financing needs financed entirely via domestic banks, together with bank recapitalization happening mostly via unfunded government bonds, is creating a closed loop between banks and the government. In this context, external financing should be sought even if the terms are initially less attractive, as this would result in a more diversified funding pool, lesser concentration of government securities on bank's balance sheets, and external discipline to fiscal performance.

Authorities' views

25. The authorities recognized the need for additional fiscal consolidation. They expressed concern about the rising trend in debt and financing needs, and pledged to use the upcoming expenditure review and reform of indirect taxation to gradually move towards fiscal surpluses. At the same time, they pointed to significant public opposition to the recent tax reform, and the challenge of implementing fiscal adjustment when public opinion perceives little "concrete gains" from these sacrifices. They noted that they had sought external financing, but had been deterred by the higher cost. However, they are considering renewing these efforts now that San Marino has exited the black list, expecting costs to be lower.

C. Structural Issues

26. The key structural challenge facing San Marino is to develop new growth sectors that make up for the demise of the old economic model. Some stakeholders in the financial industry see a future centered on asset management, an activity that in principle carries fewer risks to the sovereign than traditional banking. However, positioning San Marino as an asset management hub will take time and considerable resources as the needed expertise is not developed yet, nor is the legal, administrative, or IT infrastructure. Extending traditional banking activities beyond surrounding regions is also being considered, though this should be based on San Marino's own expertise and not on any regulatory arbitrage. Beyond banking, deepening economic ties with neighboring Emilia-Romagna, one of the most dynamic regions in Italy[6], presents an important opportunity for growth. Indeed, manufacturing and trade links used to be the drivers of the Sammarinese economy before off-shore banking took over. In this context, San Marino's low tax rates represent a competitive advantage.

27. Continued commitment towards openness and transparency is a sine qua non condition for a successful diversification. San Marino will not be able to rebuild its economy on new foundations without a full normalization of its international relations. In this regard, the recent exit from Italy's black list is key, as are other achievements:

[6] For instance, GDP has been roughly flat in Emilia-Romagna over the last four years, compared with a *circa* 3½ percent contraction in the rest of Italy. Unemployment at less than 9 percent is also some 4 percentage points lower than in the rest of Italy.

- *Monetary agreement with the EU, signed in 2012.* San Marino has committed to transpose into its law EU requirements in the fields of banking and financial supervision (including Basel III core principles) as well as the prevention of money laundering. Separately, San Marino has been accepted into the Single Euro Payments Area.

- *Progress in strengthening the AML/CFT framework and its enforcement,* as recognized by MONEYVAL. The authorities are working to remedy remaining shortcomings ahead of the next assessment. There is also willingness to put in practice a national risk assessment strategy, a longstanding IMF recommendation, despite considerable resource constraints.

28. Other initiatives in the transport and industrial areas have the potential to support growth. The agreement on the Rimini-San Marino airport signed in September will give the country management rights over a significant part of the airport's infrastructure. The medium-term goal is to develop refueling and cargo services that serve Italian and international clients. Progress on a science and technology park, which is about to launch with a dozen companies at the incubator phase, is also positive.

29. Further measures are needed to help reallocate resources towards new growth sectors and lower the wage gap with Italy. In particular:

- *Facilitate the hiring of skilled non-resident workers.* Lack of skills is typically an important bottleneck in any economy the size of San Marino's. The current process for hiring skilled nonresidents should be reformed, as it is slow, cumbersome, and imposes de facto quantitative limits.

- *Vocational training.* Current services are too limited in scope and should be expanded to provide workers with the skills to integrate in the regional Italian supply chain.

Sources: Sammarinese authorities; and IMF staff estimates.
1/ Average of three industrial sectors.
2/ A posititive number means Sammarinese wages are higher than Italian wages.

- *Business environment.* Despite a low tax environment, San Marino ranks a disappointing 81st in the World Bank Doing Business survey. For instance, it takes longer than in OECD countries on average to start a business, register property or obtain construction permits.

Authorities' views

30. The authorities affirmed San Marino's commitment to openness and transparency, and expressed satisfaction that their efforts were translating into concrete results. They agreed with the need to diversify their economy and integrate more deeply with surrounding regions and beyond, taking advantage of San Marino's location and competitive tax system. In this regard, they pointed to the various initiatives underway, not least efforts to develop tourism as another growth sector. They also expressed confidence that the tender for the Rimini-San Marino airport would

attract well qualified international bidders, and that a joint venture would be signed before the end of the year. Regarding labor market reforms, these are still at a preliminary stage and it is too early to presume the outcome.

D. Data Issues

31. There are some data gaps which are not uncommon for a small country like San Marino. In particular, national accounts and fiscal statistics lack the detail required by international standards and are produced with significant delay. There are also inconsistencies between GDP data and other real sector indicators such as the industrial production index, which are difficult to reconcile. Balance of payments data are not currently available, but San Marino has received Fund technical assistance to compile these data. Of note, banking sector data are quite comprehensive, a key consideration given the importance of the sector within the economy. On balance, the data are of sufficient quality for surveillance purposes, but further efforts and greater resources are needed to improve both their coverage and quality.

STAFF APPRAISAL

32. Over the last twelve months, San Marino has managed important achievements. The recent exit from Italy's black list has paved the way for a normalization of bilateral relations; deposits in the banks have stabilized and even increased in some cases, meaning that banks now have comfortable liquidity; and parliament recently passed an important tax reform.

33. Still, the challenges remain daunting. The economy is estimated to have suffered a *circa* 5 percent contraction last year, as many firms continued to suffer from the effects of the black list and weak external demand. While there are tentative signs of stabilization in a few sectors, persistent weaknesses in the banking system and needed cuts in public sector wages will continue to weigh on the recovery. More generally, San Marino faces the task of rebuilding the economy on new foundations after the demise of the old economic model. The recent exit from Italy's black list is an important achievement that will facilitate the transition process, but a substantial share of the 30 percent drop in GDP over the last five years appears permanent at this stage.

34. An immediate priority is to properly resolve CRSM. Recapitalizing the bank was important, as CRSM is a cornerstone of the financial system and the economy at large. Now that legal provisions protecting the foundation's majority stake in the bank have been removed, the state should dilute shareholders upfront and unconditionally, and demand a controlling majority stake commensurate with its capital contributions—something that has not happened thus far. This would protect taxpayers' interests, in line with best international practices. Moreover, members representing the state at the bank's board should be appointed primarily on the basis of their banking expertise, so that the board can develop and execute a credible plan to turn around the bank's fortunes and minimize future capital needs. A permanent on-site inspector at CRSM would also help protect the state's investment, by monitoring asset quality on a daily basis.

35. The crisis has also put significant pressures on other banks in the system, necessitating increased vigilance. While these banks meet prudential requirements, nonperforming loans will continue to put pressure on their capital bases. The central bank needs appropriate resources to scale up its on-site supervisions to ensure banks are identifying and tackling any emerging troubles and provisioning adequately for losses. In addition, an external review of banks' asset quality, in line with what is being done in other European countries, could enhance the confidence of potential external investors in the soundness of the Sammarinese banking system. Given the potential for recapitalization needs that might be uncovered by the exercise, the authorities need to prepare a credible backstop plan, even if any need should first and foremost be filled by existing shareholders or other private sector participants. The bank resolution framework also needs to be improved to allow for quicker, more transparent, and least cost resolutions.

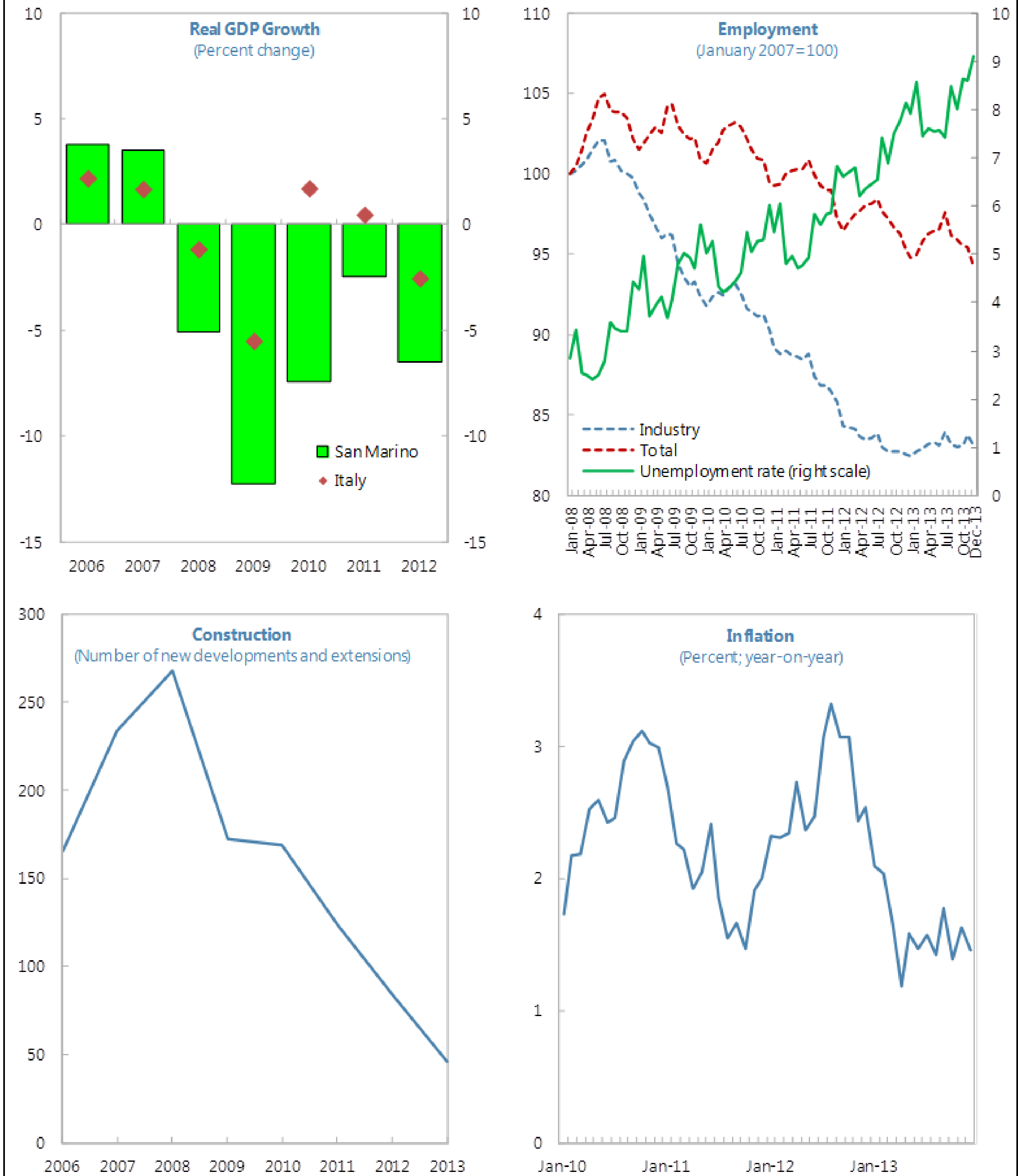
36. The 2014 budget contains good measures that deliver significant savings. The recent tax reform makes the system more efficient by reducing exemptions, and is expected to generate more revenue for the state despite lower nominal tax rates. Furthermore, the budget contemplates significant cuts in public sector wages, with welcome progressivity. All in all, the central government deficit should fall from -2.3 percent of GDP in 2013 to -1.3 percent this year.

37. However, further fiscal consolidation will be required to change current debt dynamics and create fiscal space for potential negative shocks, all the more given limited access to foreign financing. The government must aim to gradually move towards a 2–2½ percent of GDP surplus over the next 3–4 years, equivalent to €35–40 million in additional savings. Should exit from the black list provide a stronger than expected jolt to the recovery, these needs could fall to €25 million, but would not disappear altogether.

38. The ongoing expenditure review and upcoming reform of indirect taxation provide opportunities to move towards this goal. The spending review rightly focuses on the areas of public wages, pensions, and health and social benefits. Attention will need to be paid to ensure that cuts are well targeted and equitable. The reform of indirect taxation should seek to improve tax efficiency but also increase the revenue intake, and any introduction of a VAT should follow best international practice by aiming at a uniform rate with as limited exemptions as possible. Separately, the real estate tax should be reinstated, as it provides a relatively un-distortive source of revenue.

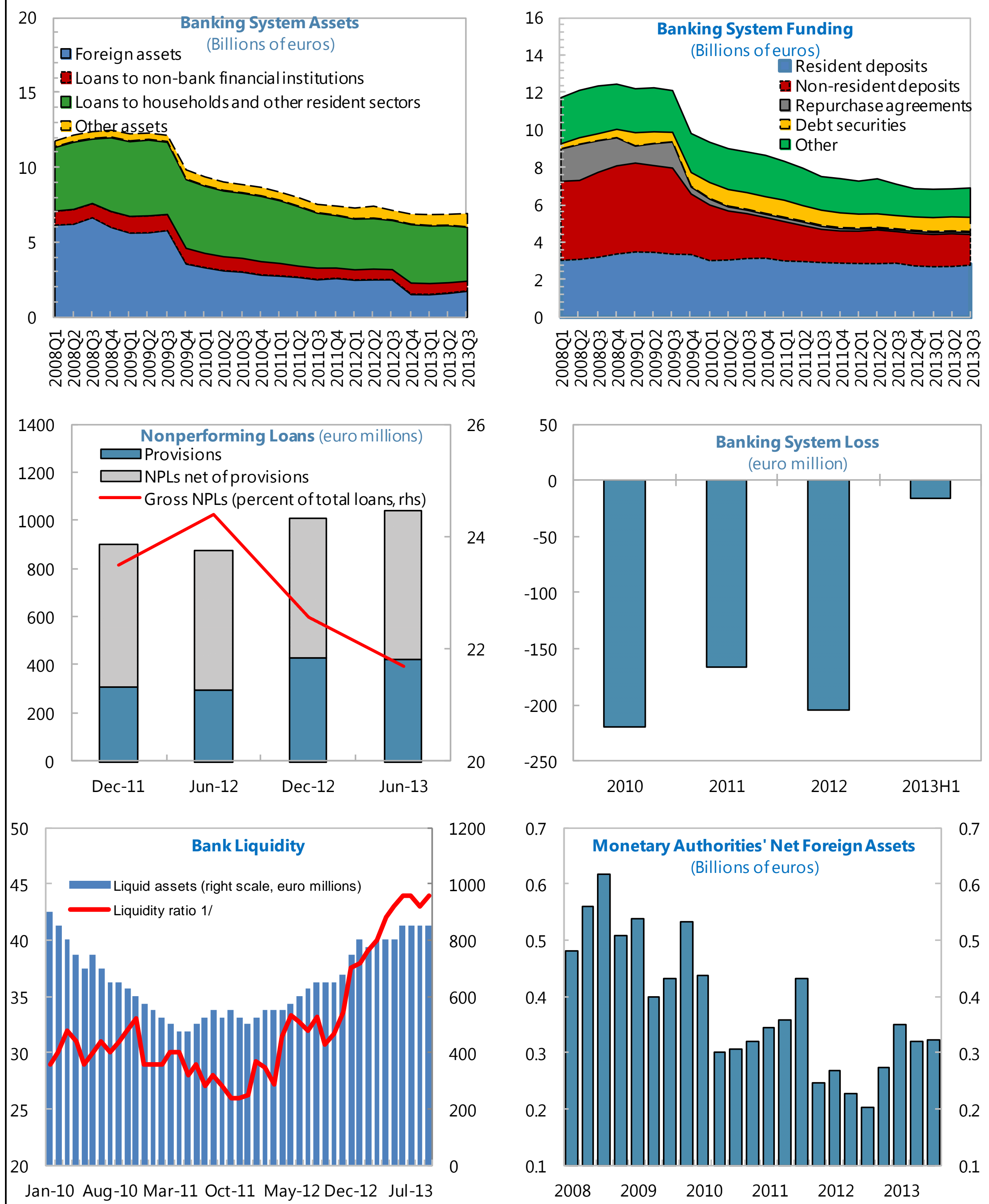
39. San Marino has made important strides in moving away from the old economic model. Future growth lies in diversifying beyond banking, and in integrating more deeply with Emilia Romagna—one of the most dynamic regions in Italy—and with Europe and the world. Continued actions that underscore San Marino's commitment to openness and transparency, which have facilitated the recent exit from Italy's black list, will remain key. In parallel, the government's efforts to open up new opportunities for the private sector, coupled with San Marino's competitive tax environment, bode well for the long and arduous process of rebuilding the economy on new foundations.

40. It is recommended that the next Article IV consultation with the Republic of San Marino be held on the current 12-month cycle.



Source: CBSM; IMF, International Financial Statistics; UPECEDS; and IMF staff calculations .

Figure 2. San Marino: Financial Sector Indicators, 2008-13



Sources: CBSM; IMF, International Financial Statistics; UPECEDS; and IMF staff calculations.

1/ Liquid assets as a share of liquid liabilities, excluding inter-bank loans.

Table 1. San Marino: Selected Economic and Social Indicators, 2007-14

GDP per capita (2011): 63,650 U.S. dollars — Life expectancy at birth (2010): 83.2 years
Population (December 2011): 32,166 persons — Literacy, adult (2008): 96 percent

						Estimate	Projection	
	2007	2008	2009	2010	2011	2012	2013	2014
Activity and Prices								
Real GDP (percent change)	3.5	1.7	-12.8	-4.6	-9.5	-7.5	-4.5	-1.0
Domestic demand	..	1.1	-11.4	-7.8	-9.1	-4.6	...	...
Final consumption	..	2.9	1.4	-3.4	-5.4	0.0	...	...
Fixed investment	..	5.6	-19.6	-19.0	-15.6	-13.0	...	...
Net exports (contribution to growth)	..	0.8	-4.3	1.2	-2.8	-4.1	...	...
Exports	..	6.0	-18.0	-9.2	-15.5	-9.8	...	...
Imports	..	6.3	-18.1	-11.1	-16.3	-8.9	...	...
Employment (percent change)	3.2	3.5	-0.3	-0.8	-2.2	-1.0	...	...
Unemployment rate (average; percent)	3.0	3.1	4.5	4.9	5.5	6.9	8.0	...
Inflation rate (average; percent)	2.5	4.1	2.4	2.6	2.0	2.8	1.3	1.0
Nominal GDP (millions of euros)	1817.5	1878.6	1700.8	1615.3	1477.5	1401.5	1357.1	1357.0
Central Government Operations (percent of GDP) 1/								
Revenues	22.0	19.7	19.5	20.9	20.5	24.0	20.9	21.2
Expenditure	20.3	19.6	21.7	22.9	24.1	26.0	23.2	22.4
Overall balance	1.6	0.2	-2.2	-2.0	-3.6	-2.0	-2.3	-1.3
Government debt	11.4	13.5	17.5	17.6	18.4	22.6	30.7	31.9
Loans	3.6	3.5	3.7	3.5	3.2	7.1	14.6	15.9
Net account payables	7.9	10.0	13.8	14.1	15.2	15.5	16.0	16.0
Government deposits (millions of euros)	214.4	263.9	256.9	218.2	154.1	72.9	55.9	55.9
Money and Credit								
Deposits (percent change)	...	16.1	-18.7	-18.0	-12.5	-1.6	...	...
Private sector credit (percent change)	13.6	12.2	-5.5	-6.6	-20.0	-13.3	...	...
Net foreign assets (percent of GDP)	39.3	29.2	9.2	25.4	46.4	37.6	...	...
Commercial banks	15.1	2.1	-22.0	5.7	29.8	21.4	...	...
Central bank	24.2	27.0	31.2	19.7	16.6	16.1	...	...
External Accounts (percent of GDP)								
Balance of goods and services	25.1	24.6	25.5	26.3	24.4	21.6	...	...
Exports	211.6	222.4	205.7	197.5	184.8	178.7	...	...
Imports	186.4	197.8	180.2	171.2	160.4	157.1	...	...
Gross international reserves (millions of U.S. dollars)	647.8	706.8	790.3	449.2	341.9	308.6	...	...
Exchange Rate (average)								
Euros per U.S. dollar	0.73	0.68	0.72	0.76	0.72	0.78	0.75	...
Real exchange rate	100.5	102.0	103.2	99.4	99.4	97.6	99.2	...
Financial Soundness Indicators (percent) 3/								
Regulatory capital to risk-weighted assets	17.5	16.9	16.9	15.6	14.1	8.8	9.7	...
Bad loans to total loans	n.a.	n.a.	2.9	5.9	10.1	10.6	11.7	...
Loan loss provision to total loans 2/	4.3	2.6	3.9	6.3	10.5	13.3	12.1	...
Return on equity (ROE)	12.1	10.0	-14.4	-24.4	-24.4	-21.1	...	...
Liquid assets to short-term liabilities	...	...	...	...	...	37.9	46.1	...

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

1/ Does not include possible costs of future bank recapitalization beyond the €85 million recently decided for CRSM.
2/ Based on total loan loss provision, which covers nonperforming and performing loans.
3/ Data as of June for 2013

Table 2. San Marino: Financial Soundness Indicators, 2007-13

	2007	2008	2009	2010	2011	2012	2013 1/
Capital adequacy ratios (percent)							
Regulatory capital to risk-weighted assets	17.5	16.9	16.9	15.6	14.1	8.8	9.7
Capital to assets	10.8	10.7	11.1	9.9	9.6	8.2	7.4
Asset quality ratios (percent)							
Bad loans to total loans	...	...	2.9	5.9	10.1	10.6	11.7
Nonperforming loans to total loans	...	4.2	8.5	15.0	23.5	22.6	21.7
Bad loans net of provision to capital	...	...	7.2	17.6	28.6	41.3	58.0
Nonperforming loans net of provision to capital	...	...	22.9	52.5	77.3	82.4	102.2
Loan loss provision to total loans 2/	4.3	2.6	3.9	6.3	10.5	13.3	12.1
Earning and profitability (percent)							
Return on assets (ROA) 3/	1.2	0.8	-1.4	-2.7	-6.6	-10.9	...
Return on assets (ROA) 4/	1.3	1.1	-1.6	-2.6	-2.4	-6.9	...
Return on equity (ROE) 3/	10.7	7.6	-13.1	-25.2	-67.9	-121.5	...
Return on equity (ROE) 4/	12.1	10.0	-14.4	-24.4	-24.4	-77.0	...
Interest margin to gross income	81.2	100.9	51.4	49.0	65.8	51.9	...
Non-interest expenses to gross income	36.7	45.2	52.2	68.5	83.2	88.7	...
Trading income to gross income	-7.8	-29.1	11.0	1.3	-7.0	8.7	...
Administrative expenses to non-interest expenditures	84.0	83.5	51.3	61.9	69.2	69.7	...
Liquidity (percent)							
Liquid assets to total assets	37.2	38.3	25.5	17.1	15.0	16.1	16.5
Liquid assets to short-term liabilities	...	...	...	...	...	37.9	46.1
Loans to deposits	77.1	75.2	88.5	101.4	91.6	108.7	111.4
Interest rates (basis points)							
Spread between lending and deposit rates	496	567	478	468	484	520	...

Sources: CBSM; IMF, International Financial Statistics; and IMF staff calculations.

1/ As of June 2013

2/ Based on total loan loss provision, which also covers problem loans and performing loans.

3/ Before extraordinary items and taxes.

4/ After extraordinary items and taxes, and before provision to fund for general banking risk.

Table 3. San Marino: Central Government Operations, 2008-15

(Percent of GDP)

						Projection		
	2008	2009	2010	2011	2012	2013	2014	2015
Revenue	19.7	19.5	20.9	20.5	24.0	20.9	21.2	20.9
Taxes	15.9	15.0	16.2	15.3	18.8	15.6	16.6	16.3
Income Taxes	6.2	6.0	6.9	6.5	6.4	6.7	7.3	6.9
Non-income taxes	9.7	9.1	9.4	8.8	12.4	8.9	9.3	9.5
Taxes on international trade and transactior	6.8	6.1	6.6	6.3	8.0	5.7	5.7	5.7
Other taxes	3.0	2.9	2.8	2.5	4.4	3.1	3.6	3.8
Non-tax revenue	3.8	4.5	4.7	5.2	5.2	5.3	4.6	4.6
Expenditure	19.6	21.7	22.9	24.1	26.0	23.2	22.4	23.1
Expense	18.0	20.2	22.1	23.1	25.1	22.3	21.3	22.0
Compensation of employees	6.0	6.8	7.3	7.7	8.0	8.4	8.0	7.9
Use of goods and services	1.5	1.8	1.8	2.0	2.1	2.1	2.4	2.4
Interest	0.2	0.1	0.1	0.1	0.1	0.1	0.4	0.4
Grants to other government units	8.9	10.5	10.5	10.2	10.0	10.4	9.4	10.1
Current	7.4	8.4	8.7	8.6	9.3	9.7	8.9	9.6
Capital	1.5	2.1	1.7	1.5	0.7	0.7	0.5	0.5
Other expenses (including subsidies)	1.4	1.0	2.5	3.1	4.9	1.2	1.1	1.1
Net acquisition of non-financial assets	1.6	1.5	0.8	1.0	0.9	0.9	1.1	1.2
Asset purchase	1.7	1.5	0.8	1.0	0.9	0.9	1.1	1.2
Asset sale	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross Operating Balance	1.8	-0.7	-1.2	-2.5	-1.1	-1.4	-0.1	-1.0
Net lending (+)/borrowing (-) (fiscal balance) 1/	0.2	-2.2	-2.0	-3.6	-2.0	-2.3	-1.3	-2.2
Net financial worth, transactions 1/	0.0	-2.4	-2.3	-3.9	-5.7	-2.3	-1.3	-2.2
Net acquisition of financial assets	1.0	-5.9	-4.1	-5.6	-1.2	5.0	0.0	0.0
Currency and deposits	2.6	-0.4	-2.4	-4.3	-5.8	-1.3	0.0	0.0
Other accounts receivable	-1.7	-5.5	-1.7	-1.3	0.3	0.0	0.0	0.0
Investment in CRSM					4.3	6.3	0.0	0.0
Net incurrence of liabilities	1.0	-3.6	-1.7	-1.7	4.5	7.3	1.3	2.2
Loans	-0.1	-0.1	-0.1	-0.2	4.7	7.3	1.3	2.2
Other accounts payable	1.0	-3.5	-1.6	-1.5	-0.3	0.0	0.0	0.0
	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Consolidated Budgetary Central Government and Social Security Fund								
Total revenue (consolidated)	29.4	30.7	32.4	33.6	37.5	35.6	35.3	34.6
Total expenditure (consolidated)	29.4	32.9	34.5	38.0	40.9	39.7	38.9	38.5
Overall balance (consolidated BCG and SSF)	0.0	-2.2	-2.1	-4.4	-3.4	-4.1	-3.6	-4.0
	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items								
Public debt	13.5	17.5	17.6	18.4	22.6	30.7	31.9	33.4
Loans	3.5	3.7	3.5	3.2	7.1	14.6	15.9	17.7
Net accounts payable	10.0	13.8	14.1	15.2	15.5	16.0	16.0	15.7
Government deposits	14.0	15.1	13.5	10.4	5.2	4.1	4.1	4.0
Nominal GDP (in millions of euros)	1878.6	1700.8	1615.3	1477.5	1401.5	1357.1	1357.0	1386.6

Sources: Sammarinese authorities; and IMF staff calculations and projections.

1/ Bank recapitalizations are only recorded as financing operations.

Appendix I. Risk Assessment Matrix[1]

Risk	Relative likelihood	Impact if realized
***Upside risk:* exit from the black list leads to stronger than expected recovery**	**Medium**	**High** Exit is now official. By facilitating business between Sammarinese firms and their Italian counterparts, the exit could provide a stronger than expected jolt to the recovery.
Financial stress in the euro area re-emerges (triggered by stalled or incomplete delivery of national and euro area policy commitments).	**Medium**	**High** Given extensive financial and real links with Italy, the impact on the economy would be direct.
Continued stress in the banking system.	**Medium**	**High** Continued stress would impair credit provision, impact confidence, and possibly have a bearing on public finances.
Failure to enact fiscal consolidation.	**Medium**	**Medium** Public debt would remain on an upward trend, and there would be limited fiscal space to absorb further shocks from the financial system.
Protracted period of slower European growth (larger than expected deleveraging or negative surprise on potential growth).	**High**	**Medium** Given links to Italy, this would likely entail slow growth in San Marino as well.

[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 of risks listed is the staff's subjective assessment of the risks surrounding the baseline. The RAM reflects staff views on the source of the risks and overall level of concern as of the time of the discussion with the authorities.

Appendix II. Public Debt Sustainability Analysis

1. San Marino's debt (central government level) is in a difficult trajectory. Before the crisis, gross debt was below 15 percent of GDP, and most of it was in the form of unclaimed tax refunds rather than actual borrowing. Since then, the sharp decline in revenues has turned budget surpluses into deficits, and the largest bank has required some 13 percent of GDP in public support.[1] This has brought debt to 30 percent of GDP, and the increase would have been greater had the government not largely used its large cash buffers to finance its needs (cash buffers have gone from more than 15 percent of GDP in 2009 to 4 percent of GDP in 2013). Barring fiscal adjustment beyond what is already incorporated in the 2014 budget, the combination of primary deficits between 1–2 percent of GDP over the medium term together with sluggish growth will mean that debt will continue to increase and reach close to 36 percent by 2019. The government will also face significant gross financing needs in 2017 (11 percent of GDP), when it has to repay the first loan used to recapitalize CRSM.[2]

2. The possible need for further bank capital support represents the main risk to public finances and debt sustainability. An extreme, albeit unlikely, scenario where further recapitalization needs amount to up to 15 percent of GDP—either from further losses from CRSM's Delta assets, or a combination of capital needs from CRSM and other banks—would place debt in an steep trajectory, reaching 55 percent of GDP in 2019. These adverse debt dynamics would hardly be sustainable in a country with still difficult access to external financing.

3. Debt dynamics highlight the need for fiscal adjustment. A gradual adjustment of 1 percent of GDP per year over 2015–17 would put debt on a downward trend if no contingent liabilities materialize, and by 2019 debt would end up some 10 percent of GDP below the baseline. Gross financing needs would also be commensurately smaller. In addition, consolidation would free up fiscal space for contingent liabilities: should these materialize, the debt path would be significantly more favorable than under no adjustment scenario (see chart).

[1] 11 percent was provided by the central government and 2 percent by the social security institute.

[2] Note: the increase in gross financing needs in 2013 is an artificial by-product of the DSA template, given that the bond used to recapitalize CRSM was not funded but was rather issued to the bank in exchange for capital.

Figure A2.1. San Marino: Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(in percent of GDP unless otherwise indicated)

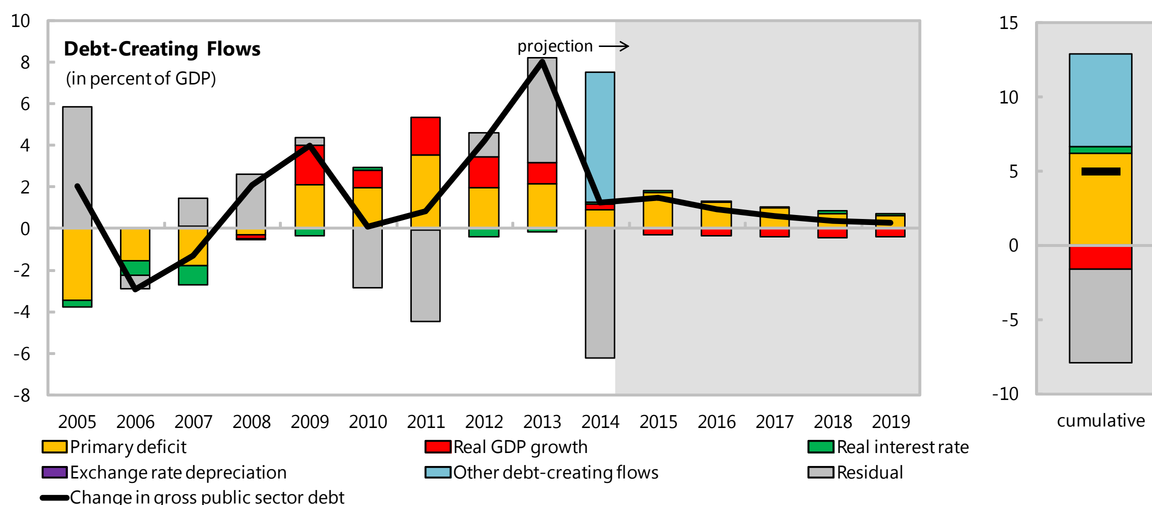
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2003-2011 [2/]	2012	2013	2014	2015	2016	2017	2018	2019
Nominal gross public debt	15.2	22.6	30.7	31.9	33.4	34.4	35.0	35.4	35.7
Public gross financing needs	-0.4	1.4	1.5	3.4	4.9	5.4	10.6	7.4	7.6
Real GDP growth (in percent)	-2.9	-7.5	-4.5	-1.0	1.0	1.1	1.2	1.3	1.3
Inflation (GDP deflator, in percent)	4.3	2.6	1.4	1.0	1.2	1.3	1.4	1.5	1.6
Nominal GDP growth (in percent)	1.4	-5.1	-3.2	0.0	2.2	2.4	2.6	2.8	2.9
Effective interest rate (in percent) [4/]	1.1	0.4	0.6	1.3	1.4	1.4	1.5	1.8	1.9

As of January 00, 1900		
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	n.a.	n.a.

Contribution to Changes in Public Debt

	Actual			Projections							
	2005-2011	2012	2013	2014	2015	2016	2017	2018	2019	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	0.7	4.2	8.0	1.3	1.5	0.9	0.6	0.4	0.3	5.0	-0.3
Identified debt-creating flows	0.4	3.0	3.0	7.5	1.5	0.9	0.6	0.4	0.3	11.3	
Primary deficit	0.1	2.0	2.1	0.9	1.7	1.3	1.0	0.7	0.6	6.2	
Primary (noninterest) revenue and gra	20.6	24.0	20.9	21.2	20.9	21.2	21.2	21.2	21.1	126.9	
Primary (noninterest) expenditure	20.7	25.9	23.0	22.0	22.7	22.5	22.2	21.9	21.7	133.1	
Automatic debt dynamics [5/]	0.3	1.1	0.9	0.4	-0.2	-0.3	-0.4	-0.3	-0.3	-1.2	
Interest rate/growth differential [6/]	0.3	1.1	0.9	0.4	-0.2	-0.3	-0.4	-0.3	-0.3	-1.2	
Of which: real interest rate	-0.3	-0.4	-0.2	0.1	0.1	0.0	0.0	0.1	0.1	0.4	
Of which: real GDP growth	0.6	1.5	1.1	0.3	-0.3	-0.4	-0.4	-0.4	-0.4	-1.6	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	0.0	6.3	0.0	0.0	0.0	0.0	0.0	6.3	
Contingent liabilities	0.0	0.0	0.0	6.3	0.0	0.0	0.0	0.0	0.0	6.3	
Residual, including asset changes [8/]	0.3	1.2	5.0	-6.3	0.0	0.0	0.0	0.0	0.0	-6.3	



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.

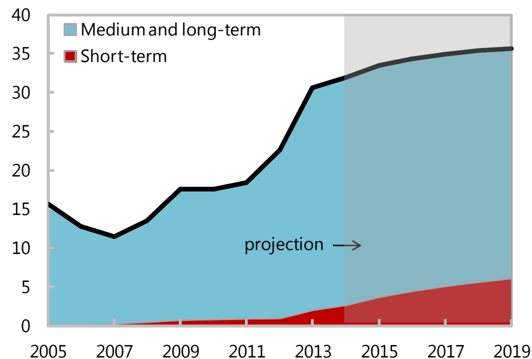
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure A2.2. San Marino: Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

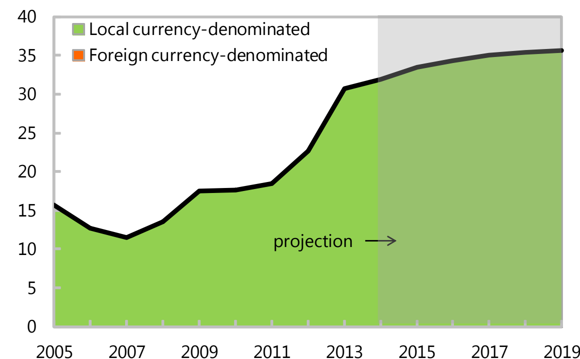
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

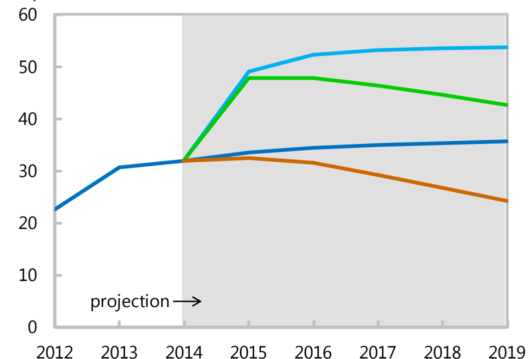


Alternative Scenarios

Baseline
Contingent Liability Shock
Contingent Liability Shock+Adj
Baseline+Adjustment

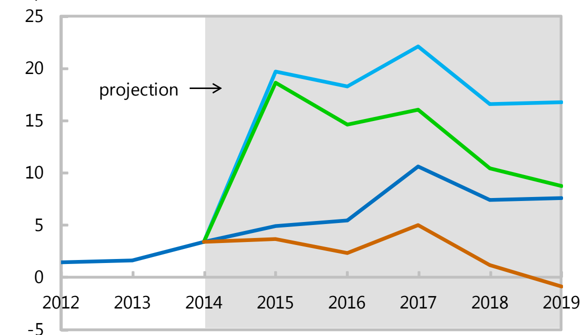
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	-1.0	1.0	1.1	1.2	1.3	1.3
Inflation	1.0	1.2	1.3	1.4	1.5	1.6
Primary Balance	-0.9	-1.7	-1.3	-1.0	-0.7	-0.6
Effective interest rate	1.3	1.4	1.4	1.5	1.8	1.9
Constant Primary Balance Scenario						
Real GDP growth	-1.0	1.0	1.1	1.2	1.3	1.3
Inflation	1.0	1.2	1.3	1.4	1.5	1.6
Primary Balance	-0.9	-0.9	-0.9	-0.9	-0.9	-0.9
Effective interest rate	1.3	0.5	0.9	0.9	1.4	1.4
Contingent Liability Shock+Adj						
Real GDP growth	-1.0	-1.0	-0.9	-0.8	-0.7	-0.7
Inflation	1.0	1.2	1.3	1.4	1.5	1.6
Primary Balance	-0.9	-15.7	0.7	2.0	2.3	2.4
Effective interest rate	1.3	0.5	2.0	1.8	1.9	1.9

Historical Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	-1.0	-3.8	-3.8	-3.8	-3.8	-3.8
Inflation	1.0	1.2	1.3	1.4	1.5	1.6
Primary Balance	-0.9	-0.2	-0.2	-0.2	-0.2	-0.2
Effective interest rate	1.3	0.5	0.5	0.5	0.5	0.5
Contingent Liability Shock						
Real GDP growth	-1.0	-1.4	-1.3	1.2	1.3	1.3
Inflation	1.0	0.6	0.7	1.4	1.5	1.6
Primary Balance	-0.9	-16.7	-1.3	-1.0	-0.7	-0.6
Effective interest rate	1.3	0.6	3.4	2.2	2.3	2.1
Baseline+Adjustment						
Real GDP growth	-1.0	0.0	0.1	0.2	0.3	0.3
Inflation	1.0	1.2	1.3	1.4	1.5	1.6
Primary Balance	-0.9	-0.7	0.7	2.0	2.3	2.4
Effective interest rate	1.3	0.5	0.9	0.8	1.1	0.9

Source: IMF staff.

INTERNATIONAL MONETARY FUND

REPUBLIC OF SAN MARINO

March 24, 2014

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By
European Department
(In consultation with other departments)

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FUND RELATIONS

(As of March 14, 2014)

Membership Status
Joined: September 23, 1992; Article VIII

General Resources Account	**SDR Million**	**Percent of Quota**
Quota	22.40	100.00
Fund holdings of currency	16.95	75.67
Reserves tranche position	5.45	24.34

SDR Department	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	15.53	100.00
Holdings	15.46	99.52

Outstanding Purchases and Loans: None

Latest Financial Arrangements: None

Projected Payments to the Fund: None

Implementation of HIPC Initiative: Not applicable

Implementation of Multilateral Debt Relief Initiative: Not applicable

Implementation of Post-Catastrophe Debt Relief: Not applicable

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]

[1] EU Regulations are not directly applicable to San Marino as a result of 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

(continued)

Article IV Consultation

San Marino is on a 12-month cycle. The previous Article IV consultation discussions took place during February 21–March 5, 2013, and the consultation was concluded on May 17, 2013 (Country Report No. 13/122).

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

Resident Representative: None

Italy, acting on behalf of the European Union, or as a result of the monetary agreement signed between San Marino and the European Union.

STATISTICAL ISSUES

(As of March 14, 2014)

Data Provision
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. In January 2007, in view of their intention to participate in the GDDS, the authorities named two national GDDS coordinators and announced their objective to increase the frequency of website updates in order to improve data dissemination. As of March 2012, national and fiscal accounts, as well as monetary and financial sector data are compiled according to international standards, but some key statistics (such as real and fiscal data) are available only with delay and, in many cases, are at a lower than standard frequency and detail.

Real Sector Statistics
National accounts data for 1995 onward have been calculated in accordance with ESA95 and data are compiled annually based on the income approach with about ten months delay. The authorities have also calculated sectoral contribution. However, as part of ongoing STA technical assistance on national accounts statistics, production and expenditure approaches are adopted instead. Consumer prices and employment data are available monthly with short delay. An industrial production index based on electricity consumption, launched in 2000, became available monthly in 2009. Consumption and business sentiment indexes have been compiled starting 2007 based on annual household and business surveys.

Government Finance Statistics
The authorities have provided data for the central government, state-owned enterprises, and social security fund for 2004–12, as well as the budget for 2013–15. However, some of the data have not been compiled in accordance with IMF standards. Financing items, such as amortization, are included as expenditures while "borrowing requirement" is included among the revenues.

Monetary and Financial Statistics
Since 1997, the authorities have provided balance sheet data on the commercial banks and the monetary authorities to STA database. These data are provided on a quarterly basis, with approximately a six-week reporting lag. The authorities have introduced laws and took some measures to improve coverage and timeliness of banks' reporting. The CBSM has improved sectorization and expanded data collection to cover the offshore asset management activities of banks. The breakdown of deposits (and other assets and liabilities) between residents and nonresidents and the breakdown of short-term credit by public and private sector components are also available. However, there is no broad money survey. Data on nonbank financial intermediaries are also lacking.

External Sector Statistics

Starting in 2008, trade statistics have been released quarterly with a lag of about six months.
San Marino does not publish balance of payments accounts, but the authorities have received Fund technical assistance on BOP statistics and are in the process of compiling them.

San Marino: Table of Common Indicators Required for Surveillance

(As of March 14, 2014)

	Date of latest observation	Date received	Frequency of Data[5]	Frequency of Reporting[5]	Frequency of Publication[5]
Exchange Rates	3/28/14	3/28/14	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Q3 2013	Feb 2014	Q	Q	Q
Reserve/Base Money	Q3 2013	Feb 2014	Q	Q	Q
Broad Money	Q3 2013	Feb 2014	Q	Q	Q
Central Bank Balance Sheet	Q3 2013	Feb 2014	Q	Q	Q
Consolidated Balance Sheet of the Banking System	Q3 2013	Feb 2014	Q	Q	Q
Interest Rates[2]	Q3 2013	Feb 2014	Q	Q	Q
Consumer Price Index	Dec 2013	Feb 2014	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	Q4 2013	Feb 2013	A	A	A
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	Q4 2013	Feb 2014	A	A	A
Stocks of Central Government and Central Government-Guaranteed Debt	Q4 2013	Feb 2014	A	A	A
External Current Account Balance	NA [6]				
Exports and Imports of Goods and Services	2012	Feb 2014	A	A	A
GDP/GNP	2012	Feb 2014	A	A	A
Gross External Debt	NA [6]				
International Investment Position	NA [6]				

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, 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] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).
[6] Lack of capacity precludes the compilation of balance of payments data at present. Fund technical assistance in this area is ongoing.

Press Release No. 14/185
FOR IMMEDIATE RELEASE
April 29, 2014

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2014 Article IV Consultation with the Republic of San Marino

On April 23, 2014, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with San Marino.

The global crisis and difficult relations with Italy have led to the demise of the off-shore banking model, and resulted in a 30 percent GDP contraction since 2008. The banking sector has undergone deep restructuring, with several banks intervened and sizeable public support for the largest bank. The country's recent exit from Italy's tax black list should facilitate the recovery and the transition to a new growth model.

Bank deposits have now stabilized and liquidity buffers are comfortable. While liquidity risks have abated, capitalization concerns remain against the background of thin capital buffers, high non-performing loans, and relatively low provisioning.

The economic downturn and bank recapitalization needs have put pressure on public finances, with public debt increasing significantly over the last five years. The 2014 budget contains savings of about 1 percent of GDP, and is an important first step towards putting debt on a sustainable path and rebuilding buffers. The upcoming reform of indirect taxation, together with the ongoing expenditure review, will help improve efficiency and identify further savings.

In addition to the recent exit from Italy's black list, important steps have been taken to normalize international relations and rebuild the economy on new foundations. These include the monetary agreement with the EU signed in 2012, the recent inclusion of San Marino in the Single Euro Payments Area, good progress in strengthening the Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) framework as noted by MONEYVAL, and important projects jointly with Italy.

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[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.

Executive Board Assessment

The Executive Directors noted that while the economy is pointing to a modest recovery, San Marino is facing significant challenges in transitioning to a new growth model. To lay the foundations for sustainable growth, Directors encouraged the authorities to persist with the restructuring of the banking system and to continue to implement fiscal and structural reforms. The recent exit from Italy's tax black list should facilitate the process of recovery. Directors emphasized that continued commitment to openness and transparency will be essential to fully normalize relations with the international community.

Directors were encouraged by stable deposits in the banking system and related improvements in banks' liquidity position. They urged the authorities to promptly address Cassa di Risparmio della Repubblica di San Marino's (CRSM) financial situation in line with international best practice through an upfront and unconditional dilution of shareholders equity by converting injected public funds to equity capital. The authorities should also take control of the bank's management and board so as to execute a credible restructuring plan.

Directors underscored the need to monitor the banking system closely in light of high nonperforming loans and relatively low provisioning ratios. In general, they considered that intensified on-site supervisions in all banks should help in this regard. Directors pointed out that an external review of banks' asset quality could sharpen clarity about the true state of the system. They recommended that any capital shortfalls uncovered by the review should be filled first by shareholders and other private investors, and that the authorities should also have backstop plans ready. Amending the bank resolution framework to give the central bank better tools for speedy and least-costly resolution will also be important.

Directors commended the authorities for the savings contained in the current budget, and noted that the recent tax reform would improve the efficiency of the tax system and help strengthen revenues. However, to put public debt on a sustainable path and rebuild buffers, Directors saw need for further fiscal consolidation. They agreed that the upcoming reform of indirect taxation, and the ongoing expenditure review focusing on wages, pensions, and social benefits, would provide opportunities to move in this direction. Directors underscored that cuts should be well targeted and equitable.

Directors noted that San Marino had made tangible progress in normalizing international relations. They encouraged the authorities to press ahead with structural reforms to facilitate opportunities for private investment, diversifying the economy beyond banking, and integrating it more deeply with Europe and the rest of the world. Continued commitment to openness and transparency, including further progress in strengthening the AML/CFT framework, will be key to achieving durable growth.

San Marino: Selected Economic and Social Indicators, 2007-14

GDP per capita (2011): 63,650 U.S. dollars | Life expectancy at birth (2010): 83.2 years

Population (December 2011): 32,166 persons | Literacy, adult (2008): 96 percent

	2007	2008	2009	2010	2011	Estimate 2012	Projection 2013	2014
Activity and Prices								
Real GDP (percent change)	3.5	1.7	-12.8	-4.6	-9.5	-7.5	-4.5	-1.0
Domestic demand	..	1.1	-11.4	-7.8	-9.1	-4.6	...	...
Final consumption	..	2.9	1.4	-3.4	-5.4	0.0	...	...
Fixed investment	..	5.6	-19.6	-19.0	-15.6	-13.0	...	...
Net exports (contribution to growth)	..	0.8	-4.3	1.2	-2.8	-4.1	...	...
Exports	..	6.0	-18.0	-9.2	-15.5	-9.8	...	...
Imports	..	6.3	-18.1	-11.1	-16.3	-8.9	...	...
Employment (percent change)	3.2	3.5	-0.3	-0.8	-2.2	-1.0	...	...
Unemployment rate (average; percent)	3.0	3.1	4.5	4.9	5.5	6.9	8.0	...
Inflation rate (average; percent)	2.5	4.1	2.4	2.6	2.0	2.8	1.3	1.0
Nominal GDP (millions of euros)	1817.5	1878.6	1700.8	1615.3	1477.5	1401.5	1357.1	1357.0
Central Government Operations (percent of GDP) 1/								
Revenues	22.0	19.7	19.5	20.9	20.5	24.0	20.9	21.2
Expenditure	20.3	19.6	21.7	22.9	24.1	26.0	23.2	22.4
Overall balance	1.6	0.2	-2.2	-2.0	-3.6	-2.0	-2.3	-1.3
Government debt	11.4	13.5	17.5	17.6	18.4	22.6	30.7	31.9
Loans	3.6	3.5	3.7	3.5	3.2	7.1	14.6	15.9
Net account payables	7.9	10.0	13.8	14.1	15.2	15.5	16.0	16.0
Government deposits (millions of euros)	214.4	263.9	256.9	218.2	154.1	72.9	55.9	55.9
Money and Credit								
Deposits (percent change)	...	16.1	-18.7	-18.0	-12.5	-1.6	...	...
Private sector credit (percent change)	13.6	12.2	-5.5	-6.6	-20.0	-13.3	...	...
Net foreign assets (percent of GDP)	39.3	29.2	9.2	25.4	46.4	37.6	...	...
Commercial banks	15.1	2.1	-22.0	5.7	29.8	21.4	...	...
Central bank	24.2	27.0	31.2	19.7	16.6	16.1	...	...
External Accounts (percent of GDP)								
Balance of goods and services	25.1	24.6	25.5	26.3	24.4	21.6	...	...
Exports	211.6	222.4	205.7	197.5	184.8	178.7	...	...
Imports	186.4	197.8	180.2	171.2	160.4	157.1	...	...
Gross international reserves (millions of U.S. dollars)	647.8	706.8	790.3	449.2	341.9	308.6	...	...
Exchange Rate (average)								
Euros per U.S. dollar	0.73	0.68	0.72	0.76	0.72	0.78	0.75	...
Real exchange rate	100.5	102.0	103.2	99.4	99.4	97.6	99.2	...
Financial Soundness Indicators (percent) 3/								
Regulatory capital to risk-weighted assets	17.5	16.9	16.9	15.6	14.1	8.8	9.7	...
Bad loans to total loans	n.a.	n.a.	2.9	5.9	10.1	10.6	11.7	...
Loan loss provision to total loans 2/	4.3	2.6	3.9	6.3	10.5	13.3	12.1	...
Return on equity (ROE)	12.1	10.0	-14.4	-24.4	-24.4	-21.1	...	...
Liquid assets to total assets	...	...	...	...	...	11.9	...	...
Liquid assets to short-term liabilities	...	...	...	...	...	37.9	46.1	...

Sources: IMF; International Financial Statistics; Sammarinese authorities; World Bank; and IMF staff calculations.
1/ Does not include possible costs of future bank recapitalization beyond the €85 million recently decided for CRSM.
2/ Based on total loan loss provision, which covers nonperforming and performing loans.
3/ Data as of June for 2013

Statement by Mr. Andrea Montanino, Executive Director for the Republic of San Marino and Ms. Marta Spinella, Advisor to Executive Director
April 23, 2014

The authorities thank staff for the far-reaching and open discussions held during the Article IV consultations. They are in broad agreement with the reasoned and comprehensive analysis reflected in the report; moreover, they will continue to draw on the Fund's valued advice and, where necessary and feasible, on the IMF/WB technical assistance in the ongoing reform process to stabilize and diversify the economy of San Marino.

Overview

Starting from the financial crisis in 2008, the Sammarinese economy has undergone a remarkable adjustment necessitated by the convergence of profound shocks in the financial sector, a reduction of the demand for tourism and Sammarinese exports, and emerging tensions in the international community due to the country's "tax-haven" image and an unfavorable lack of transparency. The effects of the crisis exacted a toll of a cumulative 30 percent GDP contraction since 2008 and a sizeable banking consolidation; a significant part of these effects is expected to be permanent. Notwithstanding the described difficult scenario and the inherent complexity of intervening on a very small, highly specialized, open economy such as the Sammarinese, the authorities at first drew heavily on the existing large fiscal buffers to respond to the emergency, and then started a profound reform process, carrying out unpopular and rough measures when necessary.

At this juncture, even though the country still faces potentially relevant downsize risks and future developments warrant a vigilant and pro-active approach, the situation is moving towards an improved outlook, thanks to several initiatives in the pipeline and to the much sought and awaited exit from the Italian fiscal "black list"[1], a fundamental prerequisite to boost business with the neighboring Italian counterparts and the international community as a whole.

[1] The double taxation agreement (DTA) between Italy and San Marino entered into force on October 3, 2013, and paved the way for San Marino to be taken off the "black list" of countries that Italy considers to be "tax havens". The exit was ratified on February 12, 2014. The DTA, signed in 2002, and the Amending protocol thereto, aligning the provisions on exchange of tax information with the 2005 OECD standards, were ratified in June 2012. San Marino's Government has, for some time, been working to reduce the evasion of Italian taxes through its territory and has irrevocably chosen the path of international tax transparency and collaboration. DTAs or tax information exchange agreements (TIEAs) were also signed with a number of other countries, including, most recently, Singapore and Greece (DTAs) and India and China (TIEAs).

The authorities share the staff view that much still needs to be done to reform the business model of the country, pinpointing and pursuing new sustainable sources of income and growth and re-designing the financial sector structure. In the same vein, they are focused on identifying medium term expansionary projects and enhance San Marino's openness and transparency also by promoting active participation in international fora to boost opportunities and partnerships. Furthermore, the authorities are committed to the adoption of international best practices in the banking and financial sectors and to a coherent transposition of the EU requirements. It is relevant to highlight that San Marino has been accepted into the Single Euro Payment Area (SEPA)[2], that the efforts of the authorities in addressing the main weaknesses of the anti-money laundering framework have been acknowledged by MONEYVAL[3] in its periodic reviews of the country's compliance with the FATF requirements. Moreover, the EU Commission acknowledged the country's legal framework compliance with the European AML/CFT Directives and regulation.

Macroeconomic Outlook

The baseline scenario presented by staff, though still weak, accounts for a better trend, registering a positive industrial growth and a marginal upturn of GDP in the second half of 2014, which will result in a 1 percent growth in 2015. Despite being coupled by a still very high level of unemployment (around 9 percent) these figure depicts a much better development than expected, as last year's estimate projected growth at a disappointing -5 percent. Furthermore, the recent exit from Italy's "black list" is a concrete upside risk since it will entail, as a direct consequence, that Italian firms doing business with Sammarinese partners will not be obliged anymore to comply with additional and costly paperwork connected with the difficulty for the Italian authorities to evaluate their compliance with VAT obligations and, therefore, will be more willing to engage in new activities and exchanges.

Having said that, the authorities are cognizant that the progression to broaden the economy's scope and boost confidence in potential investors will need time and unrelenting efforts. Meanwhile, they remain committed to an ambitious reform agenda and to maintaining the momentum for greater openness and transparency.

Fiscal Policy

The important budget measures, affecting both the revenue and the expenditure side, generated a saving of 1 percent of GDP. San Marino's Parliament approved in December a far-reaching

[2] SEPA is a payment-integration scheme of the European Union to harmonize and increase the simplicity and reliability of bank transfers denominated in euro. As of February 2014, SEPA consists of the 28 EU member states, the four members of the EFTA (Iceland, Liechtenstein, Norway and Switzerland), Monaco and San Marino.

[3] MONEYVAL is the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism of the Council of Europe.

reform of direct taxation, aimed at expanding the tax base while reducing marginal rates. The tangible effect is estimated in additional gross proceeds of 1¼ percent of GDP. Despite having repealed the extraordinary surtax on income introduced during the crisis and the real estate taxes, savings were generated by the necessary, if socially controversial, remuneration reductions, which only spared the lowest wages. The authorities are aware of the need to further consolidate; at the same time, they need to consider the burden imposed over the population and dilute the necessary cuts and tax increases in such a way as not to impinge too drastically on the citizens' standard of living and avoid strong and persistent public opposition. The fiscal package already includes incentives for early retirement to be substituted with a contained 25 percent replacement ratio. The objective of this measure is twofold: downsize the public service sector and reduce its cumulative wages, as senior workers enjoy a higher average salary. At this juncture, some fringe benefits have already been reduced and more savings are expected to result from the spending review currently underway – with the help of TA from the IMF – focusing on wages and benefits, health costs and the public pension scheme.

With a view to restoring the country's eroded fiscal buffers, having in mind that San Marino is still exposed to high vulnerabilities, the government, in the second semester of 2014, will start discussing the scope and terms to substitute the current levy on imports with a complete VAT regime. The authorities concur with staff that the technical implementation might prove challenging but will further reinforce credibility in the Sammarinese reform process.

The authorities are also prepared to start considering a painstaking pension reform aimed at ensuring the viability of the public pay-as-you-go pension system as long as possible and guaranteeing generational fairness. The authorities are conscious that the existing system is very generous and cannot be financed in the long term due to the after crisis reduced fiscal buffers; forthcoming actions will redefine the replacement ratio, the contribution rates and the prospective pension age. The reform is complex and sensitive and will need a high level of political consensus. In the meantime, the Parliament adopted a decision to cap the highest public pensions and impose – on the existing ones that exceed the cap – a solidarity subsidy in favor of the unemployed.

Financial sector

The banking sector shows positive signs of stabilization, with deposits remaining stable since early 2012 and liquidity buffers being back to a reassuring magnitude. The negative trend of little credit demand contributed to help the banks to restock their assets and coupled with the contingent credit lines at the central bank brought the liquidity risk to a comfortable low level. Capital requirements are largely met by all the banks, with the exception of Cassa di Risparmio della Repubblica di San Marino (CRSM). Nevertheless, the authorities are conscious that the crisis reduced profitability and left a heritage of high nonperforming loans; they agree on the opportunity to require higher resources against NPLs and to a revision of the provisioning mechanism. Moreover, the authorities are considering the suggested possibility of conducting an external asset quality review.

The recapitalization of Cassa di Risparmio della Repubblica di San Marino (CRSM), the largest systemic bank of the country, still poses relevant risks on the national accounts and therefore calls for replenishing the fiscal buffers and enhancing the economy resilience to negative shocks.

Despite the sizeable public contribution in 2012 and at the beginning of 2013, in the second half of 2013 parliament approved another injection of 85 million euro, driving total public support to 13 percent of GDP. The latest capitalization has been realized by means of a zero-coupon bond underwritten by CRSM. Despite not having yet completely resolved the intricate CRSM issue, much has been accomplished over the last year. The law protecting the foundation's majority stake in CRSM was waived[4], a difficult and important attainment that the authorities consider a milestone to the gradual dilution of the current shareholders of the bank. Indeed, the covenant between the financing state and the foundation is still undergoing negotiations and the final agreement to be reached will devise the best feasible arrangements to safeguard the injected public resources. The state is already nominating six board members out of nine, and being the CRSM governed by simple majority, it is effectively controlling the bank's strategy and future development. The authorities are committed to recruit highly qualified experts with the clear mandate to restructure and revamp the bank's business.

The authorities appreciated the fruitful discussions with staff aimed at improving the banking resolution framework and the supervisory requirements. The necessary improvements will need careful planning and major legal amendments; as a consequence, a medium term approach is warranted, also considering the current resource constraints and the challenging structural reforms underway.

Structural reforms

San Marino embarked on a cycle of comprehensive and ambitious reforms to profoundly revise and re-launch its business model. The founding scheme is to reinforce the credibility, openness and transparency of the country, at the same time developing a series of services and niche activities to attract foreign investment, tourism and specialized businesses.

Consequently, the starting point was to reform the tax system and exit from the Italian "black list", simultaneously embarking in the spending review, budget consolidation and restructuring of the labor market.

In the meantime, a recovery plan based on the development of new activities and an upswing of selected tourism is underway. In particular, reinforcing the ties with neighboring Italian regions, first among all lively Emilia-Romagna, will offer the financial sector a great opportunity to provide services outside of the narrow country borders.

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[4] In 2013, the law allowing the injection of new public capital into the bank also disciplined that, as a consequence, the State could be assigned the majority stake of CRSM.

The advantageous Sammarinese tax system should be a key brick to attract investments and partnerships finalized to the development of several initiatives: the Rimini-San Marino airport, especially devoted to cargo services and touristic itineraries; a scientific and technological park, financed by high-innovative businesses and connected to researchers and universities; telecommunications and media.