EXECUTIVE BOARD MEETING

SM/21/76

May 19, 2021

To: Members of the Executive Board

From: The Secretary

Subject: **Principality of Andorra—Staff Report for the 2021 Article IV Consultation**

Board Action:	Executive Directors' **consideration** (Formal)
Tentative Board Date:	**Monday, June 7, 2021**
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Questions:	Ms. Mitra, EUR (ext. 37056) Ms. Lariau, EUR (ext. 35779) Ms. Tejada, EUR (ext. 38927) Mr. Ishikawa, STA (ext. 38977)

***Unless an objection from the authorities is received prior to the conclusion of the Board's consideration, the document will be published.**

INTERNATIONAL MONETARY FUND

PRINCIPALITY OF ANDORRA

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION

May 18, 2021

KEY ISSUES

Context. Andorra, the IMF's newest member since October 2020, participated in its first Article IV consultation with a commitment to further enhance transparency. Tourism and banking-related services dominate economic activity in the euroized economy. The country enjoys long-standing political stability, a good track-record of fiscal discipline, a gender-balanced work force, and internationally competitive ski resorts.

COVID-19. The authorities are managing the pandemic well with universal testing and expanded hospital capacity that kept fatality rates very low despite high case-loads. The testing strategy helped Andorra implement more targeted internal restrictions than in neighboring countries. At the same time, emergency fiscal measures stabilized real incomes and supported firms.

Outlook and risks. Real GDP growth is projected to rebound this year in line with the region, amid huge uncertainty, and risks are tilted to the downside in the near-term. Slower than planned vaccination rates in Andorra and neighboring countries is one of the main risks. Over the medium term, GDP growth is expected to converge to regional averages, given comparable per capita incomes.

Policy recommendations aim to support a lasting recovery. Emergency ***fiscal*** support should remain in place until a recovery has set in. Increasing public investment would strengthen the recovery and contribute to higher long-term growth while maintaining debt at manageable levels. The fiscal authorities would also need to build up international reserves gradually. In the ***financial sector***, bank capital appears adequate to absorb the pandemic shock but the full impact of the crisis should be carefully evaluated as the policy measures expire. In the medium-term, bank capital buffers should be re-assessed in light of risks associated with large domestic exposures to a few clients, related party lending, and a sizeable nonresident deposit base. Building on important efforts, further improving the effectiveness of ***anti-money laundering*** supervision would strengthen financial stability. Disseminating official ***statistics*** according to international standards will enhance transparency and aid policy-making and surveillance.

Approved By
Mahmood Pradhan (EUR) and Gavin Gray (SPR)

Discussions were held virtually on March 19–April 8, 2021. The staff team comprised Srobona Mitra (head), Ana Lariau, Michelle Tejada, Jenny Lee (all EUR), Joji Ishikawa (STA), and Arz Murr (LEG). Maksym Markevych (LEG) attended some meetings. Dries Cools (OED) participated in the discussions. Mahmood Pradhan (EUR) and Paul Hilbers (OED) met with the authorities. Dilcia Noren (EUR) supported the mission. The team met with the Minister of Finance, the Secretary of State for International Financial Affairs, the Minister of Presidency, Economy & Business Affairs, the Minister of Foreign Affairs, the Minister of Tourism, the Minister of Social Affairs, Housing & Youth, and the Minister of Civil Service and Reform of the Administration; the Director of Andorran Financial Authority; banks and various other government and private sector representatives; economists and academia.

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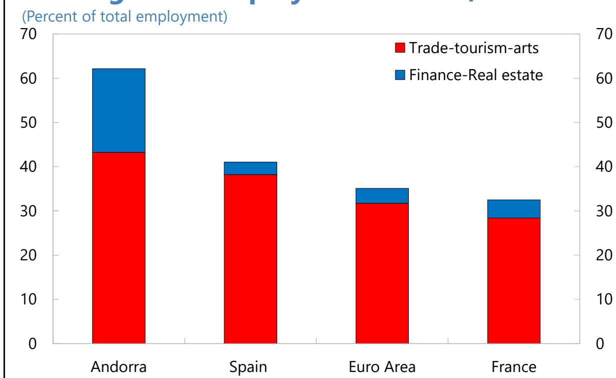
MACROECONOMIC BACKGROUND

1. **The Principality of Andorra, the IMF's newest member since October 2020, participated in its first Article IV consultation.** The authorities are committed to further enhance transparency as they integrate into the international financial community. A coalition government took office in April 2019 with Prime Minister Xavier Espot Zamora from the Democrats for Andorra at the helm. The country enjoys political stability and has a good track-record of fiscal discipline, a gender-balanced work force, and ski resorts not dependent on air travel. The authorities successfully tested the appetite of foreign investors through successful private debt placements in 2020 and issued its first public international bond in late April 2021.

2. **Banking services and tourism dominate economic activity and employment.** With consolidated bank assets over 500 percent of GDP, jobs in finance and real estate comprise 20 percent of employment, a disproportionate size compared to the region (Figure 1). Trade and tourism activity, accounting for a fifth of the economy's gross value added (GVA) and 40 percent of employment, is comparable to Spain's. However, with various other sectors connected to tourism, the share of the latter could be more than half of the economy.

Figure 1. Employment Shares, 2019



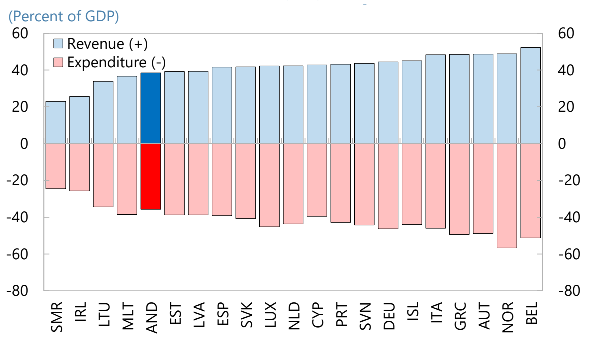
Sources: Govern d'Andorra, Eurostat, and IMF staff estimates.

3. **The euro has served well as a monetary anchor as the economy trades extensively with the eurozone, especially Spain.** The formal use of the euro is enshrined in a Monetary Agreement with the EU—that allows for a limited circulation of euro coins with Andorran themes in exchange for strict laws against counterfeiting and money-laundering, and for full adoption of EU's financial sector legislations—while Andorra negotiates an Association Agreement to gain full access to the EU's single market (Annex I). The economy imports two thirds of the value of goods from Spain, ranging from food to electricity. Spaniards accounted for half of the 8.2 million people visiting Andorra in 2019, followed by the French. Reflecting the close integration, annual GDP growth since 2013 has averaged 1.5 percent, similar to that of the euro area. Inflation is in line with neighbors', not only in the headline rate but also in tourism-related services. The unemployment rate is the lowest in the region—averaging 3.4 percent in 2013–2019—and cross-border workers from France and Spain help meet the high demand for labor during the busy tourist season.

4. **Fiscal policy, the main lever in the euroized country without a central bank, is prudent and anchored in a medium-term framework.** The size of the general government seems small by European comparisons, with both expenditure and revenue below 40 percent of GDP in 2019 (Figure 2). Refinancing needs have been high, averaging 13 percent of GDP in 2018–19, with average maturity of debt falling over the years, reaching 2½ years by end-2019. The authorities have stayed

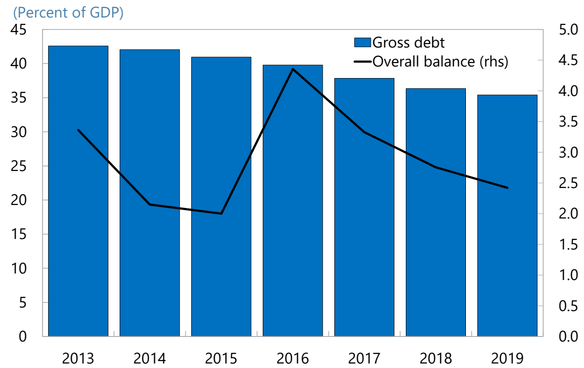
within the remit of the "fiscal rule"—limits on debt, deficit, current spending and revenue—since its inception in 2014 (Annex II). The central government has been running primary surpluses, averaging 0.7 percent of GDP in 2015–2019. With interest payments averaging 0.6 percent of GDP during this period, the overall deficit and debt were well within the fiscal rule limits. Since the local government also ran surpluses, the general government had positive overall balances in the past seven years (Figure 3).

Figure 2. Size of the General Government, 2019



Sources: Eurostat, Haver Analytics, Govern d'Andorra Department of Statistics, and IMF staff calculations.
Note: San Marino numbers reflect central government revenue and expenditure.

Figure 3. General Government Debt and Overall Balance, 2013–19

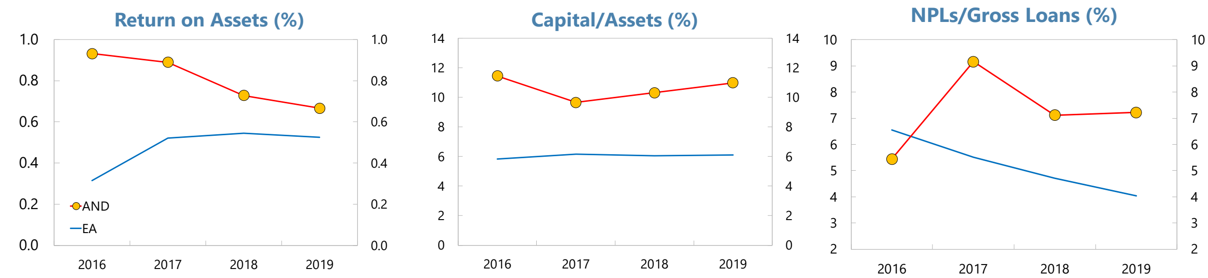


Sources: Govern d'Andorra Department of Statistics and IMF staff calculations.

5. The broader public sector operates well and a reform of the pensions system is about to begin. The two largest state-owned enterprises (SOEs)—the electricity company (FEDA) and Andorra Telecom—are profitable with investment strategies mostly financed from retained earnings. The SOEs have a revenue-sharing policy with the central government. The Andorran social security fund—under the mandatory "first pillar" defined contribution pension system—is, however, in need of reform as a depletion of the reserves fund by 2038 is projected in the latest actuarial study. The government has announced a public consultation aiming to enact a new law within a year to restore the pension fund to long-term sustainability.

6. Banks entered the pandemic with high reported capital and profits, but with increasing nonperforming loans. The banking system—four Andorran banks and one Spanish subsidiary—is diversified both geographically and in income models. Almost 60 percent of assets operate in 13 other countries—including Spain and Luxembourg—and almost 80 percent of income is based on non-interest income sources, which is typical in private banking. The diversification has served the sector well, delivering higher profits than in eurozone banks (Figure 4). Capitalization has grown over time, partly due to falling private sector loans due to domestic deleveraging. Nonperforming loans (NPLs) are, however, high—partly due to a large stock of legacy NPLs from a bank undergoing resolution after an anti-money laundering (AML)/Countering Financing of Terrorism (CFT) breach—and projected to increase further as the pandemic-related policies expire.

Figure 4. Banking Sector—Profitability, Capitalization, and Nonperforming Loans

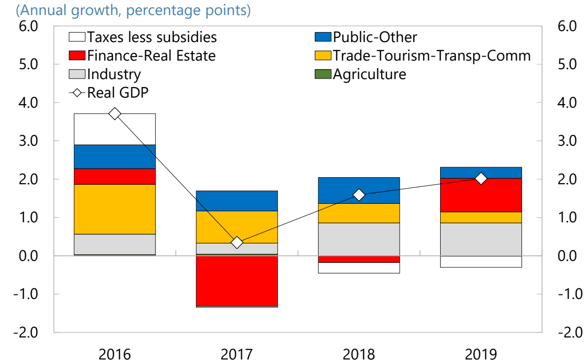


Sources: Fitch Ratings, Andorran authorities, and IMF staff estimates.
Note: The euro area (EA) aggregate is weighted average of large euro area banks supervised by the European Central Bank.

7. On the eve of the COVID-19 pandemic, economic growth bucked regional trends. Real GDP grew by 2 percent in 2019 even as growth in the euro area and Spain slowed. On the production side, services contributed significantly, particularly in the financial sector that recovered after two years of declining performance, and construction continued to contribute sizably to the growth in industry (Figure 5). While data on real expenditure components are not available, nominal growth seemed to have been broad-based. Private consumption, in particular, grew with higher minimum and real public sector wages, and was supported by bank credit. However, staff estimates in the absence of data show that private investment seems to have fallen along with banks' business lending (Tables 2 and 3). Even though the stock of domestic private sector credit is high, at 136 percent of GDP in 2019, banks cited lack of demand from firms as the main reason for low credit growth.

Figure 5. Real Economic Activity in Andorra

(Annual growth, percentage points)



Sources: Govern d'Andorra Department of Statistics and IMF staff calculations.

8. The current account surplus is estimated to be large. The Statistical agency started producing balance of payments data with technical assistance from IMF's Statistics Department. The estimates show that the current account balance was close to 18 percent of GDP in 2019, with net exports and net investment income contributing almost equally (see Selected Issues Paper (SIP): *Current Account Balance and External Competitiveness*). While not all components are available for earlier years, net exports had remained stable from 2018. In line with the current account surplus in 2019 and historically large surpluses in net exports, staff estimates of the international investment position shows a positive net asset position, but with a fairly high gross other investment liabilities stemming from banks' dependence on foreign depositors.

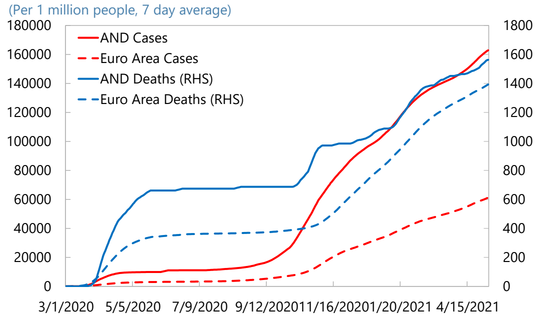
IMPACT OF THE PANDEMIC

9. Andorra has been hit hard by the pandemic, but the authorities managed the health crisis well with universal testing and revamped hospital capacity. Tourism and domestic services fell with the stringency of containment measures in the first half of 2020 but rebounded strongly during the summer with the arrival of tourists and a temporary ease of stringency (Figure 6 and Annex III). With French and Spanish borders closed until recently, especially during the height of the ski season in the first quarter of 2021, hotels and ski resorts have already lost a major share of their annual revenue. In comparison to neighboring regions though, universal testing might have enabled more targeted containment measures (Annex III). Despite the very high prevalence of COVID-19 cases per capita (Figure 6), fatality rates are among the lowest in the world as hospital capacity and protective equipment were quickly scaled up in response to the pandemic. So far, the pace of vaccination has been comparable to that of EU countries facing similar problems of supply, and doses for half the population have arrived. About 35 percent of the population have received at least one dose so far [May 12].

Figure 6. The Impact of the Pandemic and Lockdowns on Health and Activity

Case-fatality rates are low, despite high number of cases.

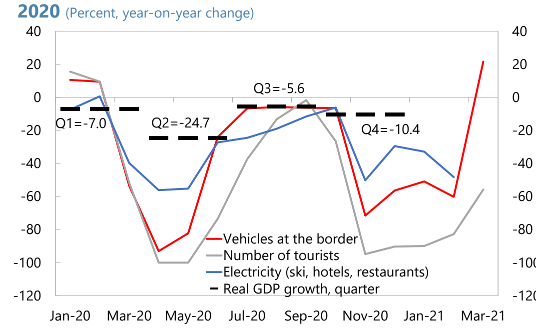
COVID-19 Indicators
(Per 1 million people, 7 day average)



Sources: Bloomberg Finance L.P., Blavatnik School of Government at University of Oxford, Our World in Data, and IMF staff calculations.

Activity rebounded strongly when lockdowns were lifted.

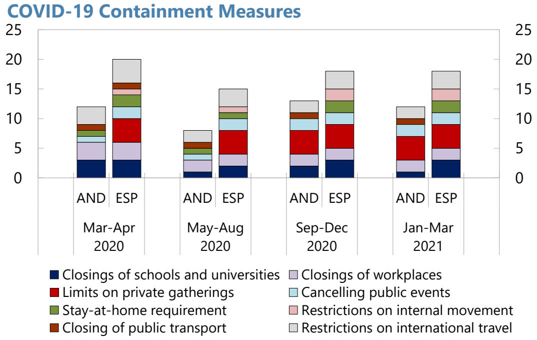
Andorra: Output, Electricity, Tourists, Border Vehicles, 2020 (Percent, year-on-year change)



Sources: Govern d'Andorra Department of Statistics and IMF staff calculations.

Containment measures were fewer and more targeted...

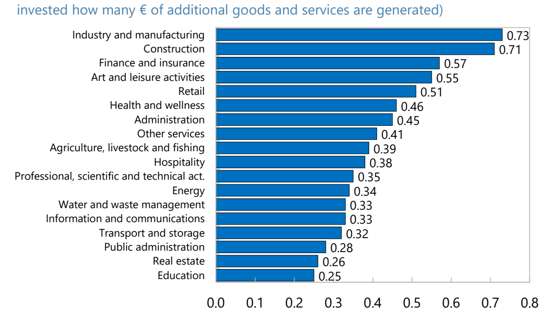
COVID-19 Containment Measures



Source: Oxford COVID-19 Government Response Tracker, Blavatnik School of Government.

...using information on sectoral multipliers on output.

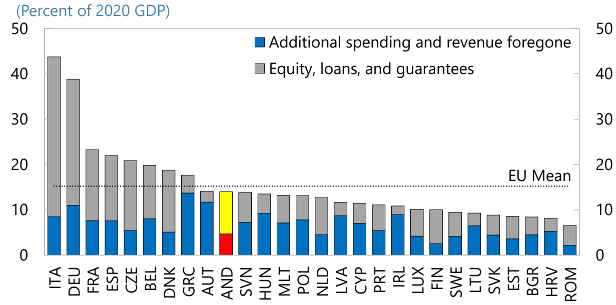
Andorra: Additional Goods and Services Generated in Other Sectors through Supply Chain Effects (Ranking by sectors: For each € invested how many € of additional goods and services are generated)



Sources: Andorran authorities and PricewaterhouseCoopers.

10. In response to the outbreak, the authorities undertook mitigating fiscal measures anchored in their medium-term framework. Expenditure measures worth 2.2 percent of GDP and revenue measures worth 0.4 percent of GDP were lower than neighbors owing to fear of financing constraints during the pandemic's first wave (Figure 7). The measures included healthcare spending and financial support for pandemic-affected sectors and households (Table 1). In addition, government guarantees worth 9 percent of GDP were made available for bank loans to liquidity-strapped companies. A 60 percent take-up of guarantees enabled a sharp increase of bank credit to firms by about 11½ percent y/y in 2020:Q2 but offset by a decline in credit to households and the public sector, as the central government diverted to other funding sources later in the year (Figure 8). The COVID-related measures and lower revenues reduced the central government balance to -4.3 percent of GDP in 2020. The measures provided about one percentage point boost to GDP growth last year, assuming an average multiplier of one across COVID-related spending categories.

Figure 7. Fiscal Response to COVID-19, in Comparison to EU



Sources: IMF Database of Country Fiscal Measures in Response to the COVID-19 Pandemic (April 2021); Andorran authorities, and IMF staff estimates.
Note: The timeframe for the announced measures is country-specific, but the bulk of the measures announced so far are short-term crisis-response measures implemented in 2020 and planned for 2021.

Table 1. Andorra: 2020–21 COVID-19 Fiscal and Financial Measures

FISCAL MEASURES

		2020		2021	
		€ million	% of GDP	€ million	% of GDP
Central Government		**65.0**	**2.6**	**37.5**	**1.4**
Revenue	Relaxation of tax obligations for households and corporations	9.1	0.4	0.0	0.0
Expenditure	Increased healthcare spending *Acquisition of tests, vaccines, and medical supplies, transfers to the healthcare system*	15.2	0.6	16.7	0.6
	Financial assistance to households *Unemployment benefits, subsidies to self-employed*	11.7	0.5	11.2	0.4
	Financial assistance to corporations *ERTO, social security contributions, rent/mortgage support 1/*	29.0	1.2	9.6	0.4
Public Enterprises	Direct support and discounts on the telecommunications and electricity bills of firms	**5.1**	**0.2**	**6.0**	**0.2**
Loan Guarantees	Government guarantees for new bank loans to businesses 2/	**135.8**	**5.5**	**94.2**	**3.6**

MONETARY AND MACRO-FINANCIAL MEASURES

Moratoria to provide repayment relief
- Legislative moratoria approved by the government (April 18th, 2020), guidelines from the European Banking Authority
- Non-legislative sector-wide moratoria approved by the Andorran Banking Association (June 11th, 2020), with application deadline extended until March 31st, 2021

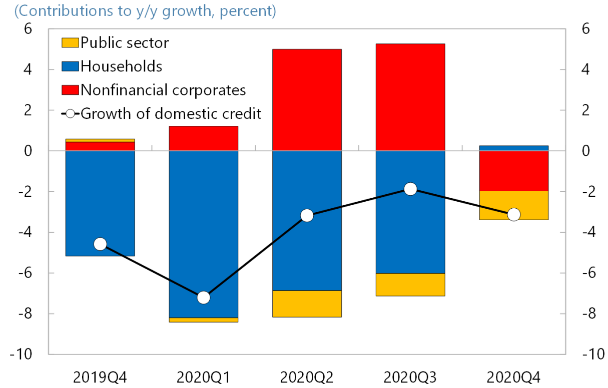
Supervisory, regulatory and macroprudential policy action by the Andorran Financial Authority
- Limit onsite examinations and postpone the non-priority ones to 2021
- Postpone stress tests to 2021 if conditions allow
- Postpone the requirement for banks to establish a capital buffer for systemic risks
- Recommend banks to not distribute dividends
- Extend the deadline for banks to report on their audited balance sheets

1/ ERTO stands for 'temporary employment regulation' and comprises the temporary suspension of work contracts and the reduction of working hours.
2/ In 2020, the government made available €230 million (equivalent to 9 percent of GDP) of loan guarantees to businesses. The table shows the amount taken up in 2020, and the amount that remains available from the total envelope in 2021 (the actual takeup could be lower).

11. Inflation moved into negative territory in mid-2020 as the unemployment rate increased. Sharp declines in energy prices led to negative inflation in transport and recreation sectors that account for a third of the weight in the consumer price index (CPI) (Figure 9). Moreover, restrictions on services activities and social distancing further slowed inflation in restaurants and hotels through the end of 2020. Meanwhile, the unemployment rate increased to 3.2 percent in 2020:Q4, a sharp increase over 2019 but was buffered by the introduction of job retention schemes ("ERTO"). Even though the ERTO benefitted 10,181 workers in May-December, employment in hospitality and personal services sectors declined by 7.3 percent in 2020.

Figure 8. Bank Credit Growth to Domestic Nonfinancial Sector

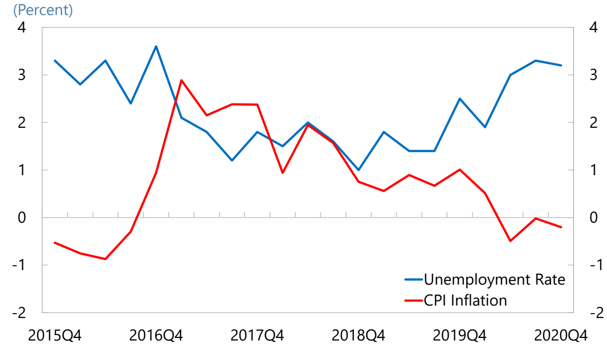
(Contributions to y/y growth, percent)



Sources: Andorran authorities and IMF staff calculations.

Figure 9. Inflation and Unemployment Rate

(Percent)



Sources: Andorran authorities, Govern d'Andorra Department of Statistics, and IMF staff calculations.

OUTLOOK AND RISKS

12. **In the near-term, despite the projected rebound, economic activity is likely to remain subdued and well below 2019 levels.** Under staff's baseline, real GDP is projected to rise by 5.8 percent in 2021, from an estimated drop of 11.8 percent in 2020 (Table 2). Private consumption will recover as lockdowns ease and vaccinations for more than half of the Andorran population reduces local transmission by mid-2021. Furthermore, higher minimum wages announced for 2021 and the availability of unemployment benefits and salary support at least until June will stabilize real incomes despite record-high unemployment. Tourism, and thus net exports, are projected to recover sooner than in other countries once mobility at the borders is fully restored, since most tourists do not travel to Andorra by air. Pent-up demand for tourism and ski vacations is expected to add back to tourism receipts later this year. But, the lasting effects of the reduction in public investment in 2020, together with the planned rollback of some COVID-19 measures after June 2021, will work toward a slightly slower recovery in GDP growth than its neighbors (Table 2). Real GDP is projected to remain almost 7 percent below 2019 levels in 2021.

Table 2. Andorra: IMF Baseline Forecasts

		Estimate	Projections					
	2019	2020	2021	2022	2023	2024	2025	2026
Real GDP growth (percent)	2.0	-11.8	5.8	4.1	3.6	2.8	1.5	1.5
Nominal GDP growth (percent)	3.4	-11.9	6.5	5.3	5.0	4.6	3.2	3.2
			(contribution to nominal GDP growth, percent)					
Consumption	2.5	-3.5	4.5	3.5	3.2	3.0	1.9	1.9
Private	1.6	-5.7	3.4	2.8	2.7	2.6	1.5	1.5
Public	1.0	2.2	1.2	0.7	0.5	0.5	0.4	0.4
Investment	1.8	-3.9	0.2	0.5	0.5	0.4	0.4	0.4
Private 1/	*1.6*	*-2.5*	*-0.8*	*0.4*	*0.4*	*0.3*	*0.2*	*0.2*
Public	0.2	-1.4	1.0	0.1	0.1	0.2	0.2	0.2
Net exports of goods and services	-1.0	-4.5	1.7	1.3	1.3	1.1	0.9	0.9
Exports	1.1	-6.8	4.5	4.0	3.7	3.1	2.3	2.3
Imports	2.0	-2.3	2.8	2.7	2.3	2.0	1.4	1.4
CPI inflation (percent, period average)	0.7	0.3	0.5	0.9	1.3	1.6	1.7	1.7
Unemployment rate (percent)	1.8	2.9	3.0	2.4	2.0	1.8	1.7	1.7
Central government overall balance (percent of GDP)	0.2	-4.3	-3.3	-1.4	-0.1	0.5	0.9	1.1
Current account balance (percent of GDP)	18.0	14.2	15.5	16.4	17.3	18.0	18.5	19.1
Memorandum items								
Euro Area real GDP growth (percent)	1.3	-6.6	4.4	3.8	1.9	1.6	1.4	1.3
Euro Area inflation (percent, period average)	1.2	0.3	1.4	1.2	1.4	1.6	1.7	1.8
Spain real GDP growth (percent)	2.0	-11.0	6.4	4.7	2.8	2.4	1.4	1.4

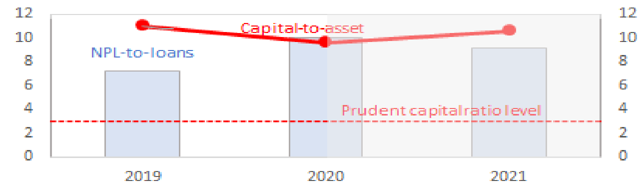
Sources: Govern d'Andorra Department of Statistics, and IMF staff calculations.

1/ The contribution of private investment is derived as a residual. Since the fiscal accounts are covered at the general government level, investments of state-owned enterprises are subsumed under private investment.

13. Banks are expected to be resilient in the baseline, supporting credit growth, although they face risks. On the credit supply side, even though bank profitability initially is expected to fall due to higher loan-loss provisions and lower noninterest earnings through 2021, reducing banks' ability to grow capital organically, banks would remain sufficiently capitalized to continue lending. However, beyond the immediate liquidity needs of some nonfinancial corporates, firms' credit demand for private investment is likely to remain lackluster. Under staff's baseline, NPLs are expected to grow to about 9 percent of loans due to the pandemic (Figure 10). This baseline assessment is, however, subject to considerable risks (see below and policy section).

Figure 10. Capital and Nonperforming Loans

(IMF Baseline Projections; percent)



Source: Andorran Authorities; IMF staff estimates.
Note: Impact of GDP growth, unemployment rate and NPL projection on capital-to-assets via impact on return-on-assets is based on IMF European Departmental Paper "COVID-19--How will European Banks Fare?" Since policy measures are in place, the trough in capital ratio and the peak in the NPL ratio could occur later in 2021 or beyond. The leverage ratio (proxied by the capital-to-asset ratio) floor of 3 percent--even though it is not applicable for Andorra as yet--has been taken as the "prudent level".

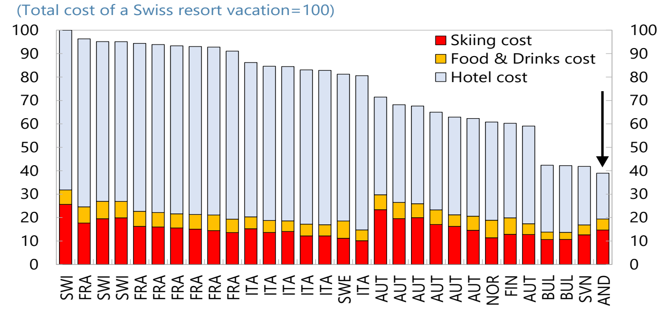
14. In the medium-term, under significant uncertainty, GDP growth is expected to converge to the euro area average by 2026. Growth is projected to remain strong as the world economy recovers fully from the pandemic and consumer confidence continues to improve with lower unemployment. In keeping with its per capita income higher than the eurozone average, Andorran growth is expected to eventually converge near the euro area's by 2026. Inflation is projected to remain subdued, slowly rising toward EA levels by 2026.

15. The current account balance seems to have moderated slightly in 2020 but is expected to rise to pre-pandemic levels by 2026. The current account surplus—based on newly produced statistics by the Andorran authorities—was 18 percent of GDP in 2019 (see SIP: *Current Account Balance and External Competitiveness*). High frequency indicators show that while the number of tourists fell by almost 40 percent in 2020, the large share of imported food and other necessity items, including medical supplies, have kept imports persistently high, reducing the current account balance to about 14.2 percent of GDP in 2020. With a full resumption of tourism, and a fairly flat demand for imports of necessary goods, the current account surplus is projected to increase to 19.1 percent of GDP by 2026.

16. The tourism sector in Andorra is competitive, especially in skiing. While a norm for the current account cannot be established, various measures of the real exchange rate suggest that Andorra fares well in external competitiveness, with low relative prices of exportable services and rising export market shares of tourism. A new index, developed by staff, shows that the relative price of a ski vacation in

Figure 11. "1-Week Cost of Ski Vacation" Index, 2019

(Total cost of a Swiss resort vacation=100)



Sources: UK Post Office Travel Money Ski Resort Report 2019; US Department of State; and IMF staff estimates.
Note: See SIP: *Current Account Balance and External Competitiveness.*

Andorra is on the lower side among European peers (Figure 11). The ongoing increase in higher minimum wages and plans to create luxury ski-tourism products are not expected to reduce the competitiveness of this sector over the medium-term.

17. Risks to the outlook are substantially skewed to the downside in the near-term (Annex IV):

- **Resurgence of the virus.** Vaccination efforts may falter with inadequate supply of doses or if the number of new cases and strains exceeds the vaccination rate in Andorra and its neighbors. These possibilities would entail protracted lockdowns in 2021 and a slower economic recovery in the region and in tourism. Increased firm bankruptcies and unemployment in the retail and tourism sectors would lead to additional scarring in the medium term.

- **Banking stress.** Banks' capitalization could come under intense pressure as loan and insolvency moratoria are lifted, and fiscal measures in the corporate sector expire to reveal sizeable loan losses for banks. While banks are assumed to weather losses well using analysis based on euro area loan-loss sensitivities of capital, these sensitivities could be more acute in Andorra due to its structural features (see policy section). Sizeable increases in NPLs in the banking sector and reduced capital buffers could make banks reluctant to lend sufficiently for recovery in private domestic demand.

- **Sovereign stress.** Most debt is short-term and gross financing needs are high in the near-term (see policy section). Increasing stress in the real sector could entail a large call on government guarantees, substantially increasing gross financing needs in 2021 (Annex V). Moreover, banking sector stress could further increase contingent liabilities of the government—due to the systemic nature of banks and absence of lender of last resort facilities—and could raise the risk of sharply higher refinancing costs for the private and public sectors. Sudden increases in gross financing needs could put temporary stops to government programs leading to a weaker recovery.

18. Upside risks are related to both Andorra and the region. A successful deployment of vaccines covering the entire adult population in Andorra and neighbors is a clear upside risk. Moreover, policies that lead to a more rapid recovery in the eurozone and Spain would help Andorran GDP growth through a stronger rebound in tourism.

Authorities' Views

19. The authorities broadly shared staff's views on the economic outlook and balance of risks. While their forecast for 2021 is more pessimistic than staff's, they are currently assessing the full outturn of the first quarter of 2021 and might revise their projections accordingly. They are optimistic about another summer rebound in tourism as they expect that 60–70 percent of the Andorran as well as the regional population (as projected by the EU authorities) will be vaccinated by the summer.

POLICIES: FROM PANDEMIC SUPPORT TO STEERING THE NEW ECONOMY

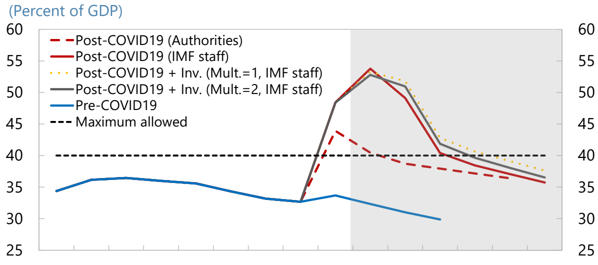
A. Fiscal Policy

Staff supports the fiscal rule as a medium-term anchor. However, the authorities' ambitious consolidation plans could be costly for the recovery. The fiscal measures related to the pandemic provided strong support to household incomes and firms' liquidity, while maintaining debt sustainability. Public support will need to continue until the recovery firmly sets in, and public investment, at least on maintenance projects, could increase while the authorities diversify funding sources. Investing in tourism, electricity, and environmentally-sustainable projects will not only lift growth but also boost private investment while bringing the unemployment rate half-way down to 2019 levels. Andorran public debt would remain sustainable in such a higher-public-investment scenario. In the medium-term, as primary fiscal balances turn positive, the authorities will need to build international reserves on a precautionary basis.

20. Public debt increased beyond the fiscal rule limit in 2020 but remains sustainable. The worsening of the fiscal balance and large debt repayments resulted in gross financing needs of the central government of 18 percent of GDP in 2020. The gross financing needs are lower for the general government since the local government and the social security administration run surpluses. To cover these needs, but also as a pre-financing strategy partly to cover large amortizations due in 2022, the central government issued new debt accessing both domestic and external sources. As a result, central government debt increased to 48.4 percent of GDP in 2020 (Figure 12), supported by activation of the escape clause embedded in the fiscal rule (Annex II). Higher revenues during the recovery and roll-back of COVID-19 measures will lead to primary surpluses from 2023 (Figure 13). Furthermore, the 10-year maturity of the €500 million Eurobond issuances will reduce debt service substantially in the short-to-medium term. The combined effects will see debt reaching the fiscal rule target of 40 percent of GDP by 2024.

Figure 12. Central Government Debt

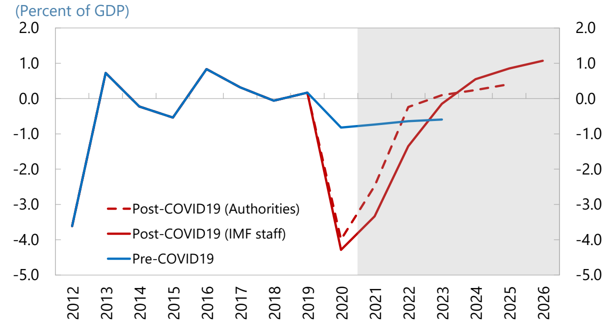
(Percent of GDP)



Source: Andorran authorities, 2020 and 2021 Budgets, and IMF staff calculations.
Note: The 'Pre-COVID19' scenario is based on the 2020 Budget. The 'Post-COVID19 (Authorities)' scenario is based on the 2021 Budget and discussions with the auhotirities. The 'Post-COVID19 (IMF staff)' scenario is the staff's baseline. The 'Post-COVID19+Investment' scenario assumes that public investment increases by 1 percent of GDP per year in 2021-23 relative to the baseline, and it is financed with an additional €100 million Eurobond issuance in 2022. The 'Maximum allowed' corresponds to the fiscal rule target of 40 percent of GDP.

Figure 13. Central Government Balance

(Percent of GDP)

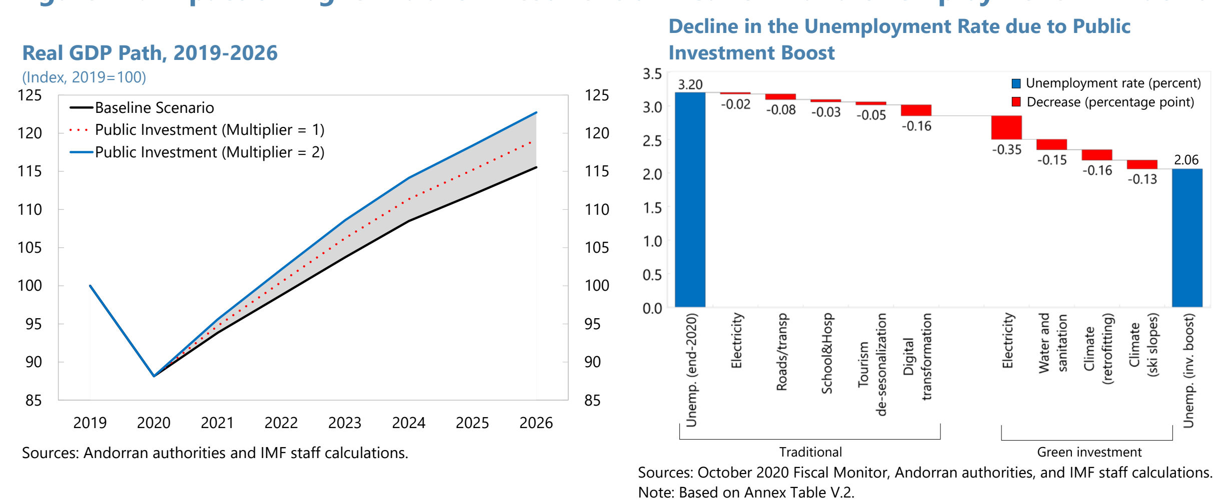


Sources: Andorran authorities, 2020 Budget and IMF staff calculations.
Notes: The 'Pre-COVID19' scenario is based on the 2020 Budget. The 'Post-COVID19 (Authorities)' scenario is based on the 2021 Budget. The 'Post-COVID19 (IMF staff)' scenario is the staff's baseline.

21. **In the near-term, fiscal policy should evolve in line with the demands of the pandemic, and the authorities should not prematurely withdraw stimulus.** The authorities are planning to maintain the healthcare spending to finance the purchase of vaccines and tests, and the operation of the COVID Office (Table 1). They are also keeping in place most support measures to households, while those to firms—particularly ERTO—are being rolled back as the economy is projected to recover. The risk of renewed lockdowns and uncertainty with various virus strains call for maintaining emergency lifelines, particularly for firms. These could only be rolled back gradually, reducing the coverage and generosity of programs if local transmission is low and activity has begun to normalize. Acquisition of vaccines for the entire population is necessary.

22. **The scaling back of public investment in 2020 could hurt the recovery and should be reversed as soon as feasible.** Planned public investment spending was cut back by about 0.4 percentage points of GDP in 2020, while it increased on average in the EU (See SIP: *Public Investment to Catalyze Andorra's Recovery*). Even though there were some offsetting investments in digital and sustainable-energy infrastructure, the cuts in a few construction projects could reduce growth prospects assuming reasonable multiplier effects (October 2020 IMF *Fiscal Monitor*). Furthermore, in the 2021 budget, public investment is projected to stall in 2021–2023, which could significantly drag down medium-term growth. Staff analysis shows that a modest increase in public investment—around 1 percent of GDP per year in 2021–23, financed by issuing €100 million extra debt—could raise real GDP level by 3 to 6 percent in the medium-term, compared to staff's baseline projections (Figure 14). Moreover, greater job-creating capacities of climate-mitigating green investments—such as adopting renewable energy sources and retrofitting buildings—would enable a faster return to the precrisis unemployment rate (Figure 14 and SIP: *Public Investment to Catalyze Andorra's Recovery*), while boosting private investment. Public debt is expected to remain sustainable in this higher public investment scenario (Annex V).

Figure 14. Impact of Higher Public Investment on Real GDP and Unemployment in Andorra



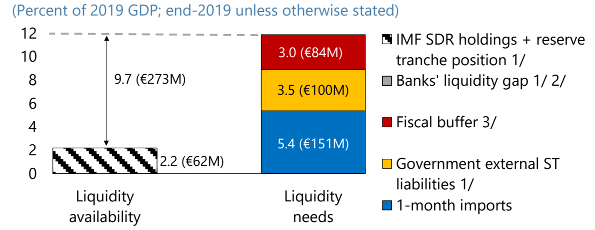
23. In the medium-term, more infrastructure spending could increase long-term growth by strengthening Andorra's position in tourism and adapting to climate change. The authorities already have plans to diversify the tourism season by offering varied summer activities. While planned investments in climate mitigation are welcome, the authorities will need to adapt to climate change as ski slopes become warmer. Additional investments in artificial snow-making machines—either directly or through incentivizing private investment—could help Andorra's competitiveness in tourism even further and lead to more sustainable fiscal revenues. Moreover, the authorities have been weighing the costs and benefits of train connections with Barcelona and French cities as a form of green investment. The authorities should continue to carefully assess the viability of these investment strategies along with costs and ensure proper governance arrangements on public procurement.

24. The authorities should continue diversifying funding sources and lengthening debt maturities. In the midst of the pandemic, the authorities borrowed externally for the first time in 2020, with Spanish and French banks as lenders and as intermediaries for private debt placement, which was oversubscribed. The government is also trying to secure long-term financing from multilateral banks such as the European Investment Bank and the Council of Europe Development Bank. Importantly, the government successfully floated Andorra's first international bond on April 27, with a rating of BBB+ (Fitch) and BBB (S&P), worth €500 million with a maturity of 10 years. At a yield of 1.25 percent, this bond was oversubscribed.

25. Over time, the fiscal authorities will need to build international reserves to cover their liquidity needs on a precautionary basis. Staff assesses such reserves needs to be about 12 percent of GDP or €334 million in the baseline scenario (Figure 15 and SIP: *Gross International Reserves*), provided that the banking system is liquid and its liquidity risks are well supervised. Using detailed bank-by-bank data on liquidity, staff assessed the liquidity gap to be zero based on the definition of liquidity coverage ratio (LCR) adopted from EU regulations. According to this metric, high-quality liquid assets are more than sufficient to cover net outflows of liabilities over a 30-day period. Against the government's liquidity needs, available reserve assets with the IMF amount to 2 percent of GDP, equivalent to €62 million. The "shortfall" of €273 million could be built up over time. The allocation of IMF Special Drawing Rights (SDRs), expected later this year, would increase available reserves by almost 4 percentage points of GDP.

Figure 15. International Reserves

(Percent of 2019 GDP; end-2019 unless otherwise stated)



Sources: Andorran authorities and IMF staff calculations.
1/ As of end-2020.
2/ The banks' liquidity gap is the difference between the banks' liquidity buffer and the net liquidity outflows in a 30-day stress period under a more adverse scenario. The net outflows are calculated by subtracting haircut-adjusted liquidity inflows from gross liquidity outflows. The gross outflows correspond to the available stock of funding sources multiplied by their corresponding outflow rates in a 30-day stress period. The baseline scenario assumes that the eligibility of liquid assets for the buffer, the haircuts on 30-day inflows and the 30-day outflow rates are consistent with the LCR regulation. In such scenario, the liquidity buffer exceeds the net outflows and there is no liquidity gap.
3/ The fiscal buffer is equivalent to one month of total government spending.

26. Different options are available for accumulating reserves, which need to meet certain qualifications. The government could increase the contribution rate to the compensation account under the fiscal rule, save all future fiscal surpluses starting in 2023, or issue debt. To qualify as international reserves, these assets need to be under the legal and managerial control of the central government and invested abroad in highly liquid assets (SIP: *Gross International Reserves*).

Authorities' Views

27. The authorities broadly agreed with the assessment and policy recommendations on the fiscal front. They reiterated their commitment to fiscal discipline and to bring the debt level below their fiscal debt limits, while taking advantage of the favorable financial conditions and exploring alternatives to build international reserves. The authorities highlighted that the COVID-related measures limited the loss in households' income and businesses' bankruptcies. The authorities welcomed staff assessment on the need to boost public investment to support the economic recovery and aid the economic transformation. They noted that, despite the investment cuts in 2020–21, the government has well-developed public investment plans for the coming years that can be fast-tracked. However, they would like to balance the implementation pace with their medium-term fiscal goals. They also noted that the public investment multiplier in Andorra could be lower than in peer countries given the small size and openness of the economy.

B. Financial Sector Policies

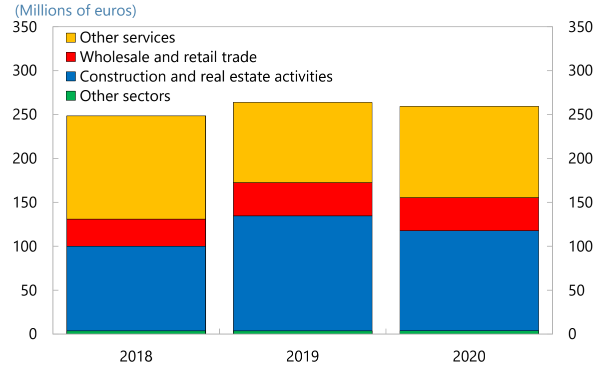
Banks have weathered the pandemic well so far, with high levels of profitability and capital buffers and pandemic policies in place. However, reliance on foreign deposit funding, loans to banks' own shareholders and other related parties, as well as large exposures to the domestic economy carry substantial risks. The Andorran Financial Authority (AFA) should carefully assess the capital needs in light of the structural risks and the impact of the policy measures adopted during the pandemic. Technical assistance from IMF's Monetary and Capital Markets Department will take a close look at the structural risks and provide detailed recommendations on bank supervision later this year.

28. The banking sector seems to be weathering the pandemic well, while fiscal and financial sector policies are still in place, amid a lack of credit demand for investment purposes. The emergency fiscal measures are providing substantial support to household incomes and firms' expenses during the pandemic. Still, borrowers took up the offer of moratoria on about 8 percent of GDP worth of loans. Similarly, firms have accessed credit from banks using loan guarantees from the government to tide over liquidity needs. However, in such an uncertain environment, businesses—especially in the tourism sector—are reluctant to borrow more for investment purposes. Bank capital has been holding up well so far due to very few loan losses in the pandemic and the presence of the insolvency moratoria.

29. The stock of NPLs remains high and is concentrated in the services sector. The high ratio of NPLs is partly due to legacy loans from *Banca Privada d'Andorra*, which is under resolution since 2015 after an AML/CFT breach. When adjusted for these legacy assets, the NPL ratio is close to 3 percent of gross loans, and near the regional average. Part of the recent increase in NPLs is also due to the adoption of new regulation that modified the classification of such loans. The nominal stock of NPLs remain concentrated in services and construction/real estate sectors and a market for NPLs do not exist (Figure 16). The NPLs usually are resolved by prolonged work-outs.

Figure 16. Stock of Nonperforming Loans

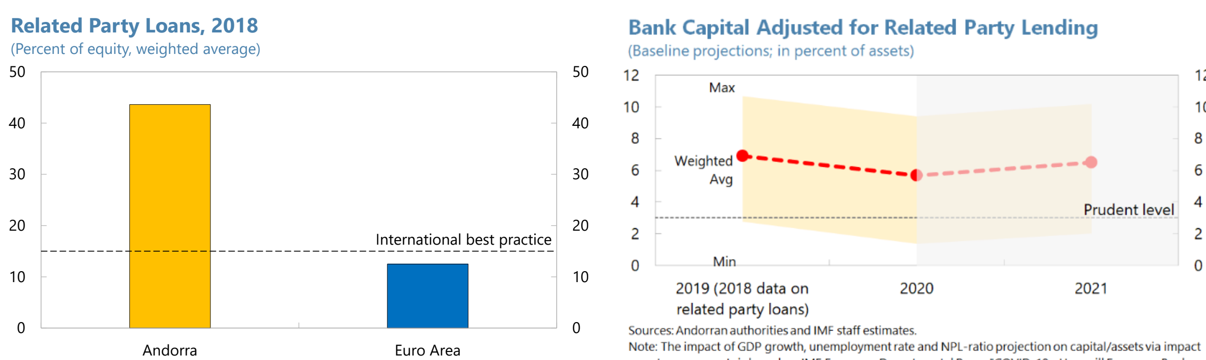
(Millions of euros)



Source: Andorran authorities.

30. Banks' capital adequacy needs to be assessed in light of related party lending and large exposures. As in many small countries with a non-diversified economic base and large banking sector, Andorran banks are exposed to domestic credit risks from large exposures to a few clients. These features could lead to a higher sensitivity of loan losses to the economic downturn. Moreover, a considerable share of loans goes to banks' "related parties" such as shareholders (Figure 17). This poses risks to the measurement of bank capital, which needs to be adjusted for such transactions. To illustrate the issue, staff analysis shows that deducting the full amount of related party loans from total capital would reduce the capital-to-asset ratio by almost 3 percentage points. This adjustment would decrease the projected capital-to-asset ratio of a portion of the banking sector below the 3 percent threshold—used in the illustrative analysis as a proxy for the leverage ratio floor—exposing a capital ratio gap of about 2 percent of GDP.

Figure 17. Banking Sector—Related Party Loans and Bank Capital



Sources: FitchConnect and IMF staff estimates.
Note: "Euro Area" includes large euro area banks with total assets of EUR10 trillion included in the analysis. Data on some banks are from 2017.

Sources: Andorran authorities and IMF staff estimates.
Note: The impact of GDP growth, unemployment rate and NPL-ratio projection on capital/assets via impact on return-on-assets is based on IMF European Departmental Paper "COVID-19--How will European Banks Fare?" The dashed red line is based on an adjustment of capital for related party loans. The yellow shaded area represents the maximum and the minimum capital ratios of Andorran banks. The leverage ratio (proxied by the capital-to-asset ratio) floor of 3 percent--even though it is not applicable for Andorra as yet--has been taken as the "prudent level".

31. Banks remain highly liquid, but dependence on foreign funding requires continuous vigilance. Due to the adoption of the EU's bank liquidity rules, Andorran banks need to have an LCR of 100 percent since January 2021. Against this requirement, Andorran banks have an LCR close to 200 percent, assuming liquidity outflows specified in the regulation and consistent with regional crisis scenarios. Staff's liquidity stress test based on detailed bank-by-bank data suggests, however, that banking system's liquidity gap could go up to 6.8 percent of GDP in an extremely adverse scenario where liquidity outflows of stable and unstable deposits occur at up to thrice the rate assumed in the baseline. The Andorran Financial Authority (AFA) will need to monitor the liquidity situation very closely, paying special attention to banks that are most exposed to this risk.

32. In the near-term, the AFA should assess the impact of the pandemic on bank capital. The temporary moratoria on debt service might have made bank balance sheets less transparent, even though the take-up was limited, and AFA should ensure that loan classifications and provisioning are continuing in a proper manner. Good provisioning practices are also needed in the absence of an NPL resolution market since banks would eventually need to mostly absorb the cost through write-offs. If the economic outlook worsens, loan moratoria should only be extended by banks on a case-by-case basis to eligible clients. Borrowers would seem to meet loan commitments if the fiscal support to households and firms is extended. Blanket moratoria would reduce bank income prospects and regulatory forbearance on loan classification would obscure bank balance sheets.

33. In the medium-term, AFA needs to manage three key risks. First, it needs strengthened rules on related party lending aiming to disincentivize banks from such loans. It could consider additional capital in the form of "Pillar II" on related party exposures of specific banks. Second, it needs to continue vigilance on liquidity risks to ensure an adequate level of liquid assets to meet short-term runs from foreign depositors. Third, the authorities should strengthen the monitoring of cross-border flows, including through cooperation with foreign counterparts, and continue deepening the understanding of money-laundering risks.

Authorities' Views

34. The authorities concurred with the assessment of the financial sector risks highlighted by staff and offered important nuances. The AFA closely monitors loans to related parties and acknowledged that an increase in capital requirements might be necessary to mitigate the associated risk. The supervisor stressed that NPLs declined in 2020 and that it did not expect them to increase when the COVID measures are lifted, arguing that most firms faced liquidity issues but not solvency problems. On NPL resolution, the AFA explained that there is a good share of restructuring to support the companies' deleveraging process and that, as a result, foreclosures are not usual. And, even when these happen, it is easy and profitable to sell a foreclosed property, given the current conditions in the real estate market. They attributed falling corporate credit growth over the years to low demand, and the reluctance of firms to accumulate debt in an uncertain environment, and instead preferring to use their own resources to finance investments.

C. Governance and Transparency

Indicators of government effectiveness, such as voice and accountability, rule of law, and political stability, compare or exceed those in the region. But Andorra is yet to ratify the United Nations convention against corruption. The authorities should build on the important progress made on the production of balance of payments statistics to close remaining data gaps.

Governance

35. **Further efforts to improve good governance are encouraged.** While a reform of the public procurement framework is underway, information on the beneficial ownership of entities—that were awarded contracts, including COVID-related ones—should be collected and published to increase transparency and accountability of public spending. In the absence of an anti-corruption strategy, the authorities should further strengthen the coordination of measures to combat corruption and identify areas for priority action. Andorra should ratify the United Nations Convention against Corruption (UNCAC) and adopt the bills on asset declaration and public access to information.

36. **The effectiveness of the AML/CFT framework needs to build on the important progress made so far.** Since 2018, the understanding of ML risks in the banking sector has been improving. An update of the national risk assessment is being finalized. UIFAND's AML/CFT supervision is risk-sensitive, but it mostly focuses on risks related to crimes committed in Andorra. To deepen the understanding of ML risks, the monitoring of cross-border flows, including through cooperation with foreign counterparts, should be further developed. Moreover, focusing the allocation of resources to higher risk areas would increase the effectiveness of AML/CFT supervision.

Data Gaps

37. **Closing data gaps and publishing statistics according to international standards are key to achieving transparency.** There is room for improving Andorra's statistical system in several dimensions. Various data gaps need to be closed, including in real expenditure components of GDP, international investment position, and data on financial soundness for banks and the private sector (see *Informational Annex*). Preparing an advance release calendar containing release dates for major macroeconomic statistics would also help transparency and surveillance. The authorities may benefit from using the Enhanced General Data Dissemination System (e-GDDS), which is the first tier of IMF data sharing standard for macroeconomic data essential for policy making and surveillance, to further develop Andorra's statistical system and improve data transparency. The IMF can provide technical assistance on the various areas if requested.

Authorities' Views

38. **The authorities consider the risk of corruption in Andorra to be moderate.** They also concur with the view that the publication of information on beneficial ownership of entities that were awarded procurement contracts would strengthen transparency. AML/CFT supervisors agree

that the understanding of ML/TF risks of cross-border flows in banking sector need to be properly evaluated.

39. The authorities plan to continue working with the IMF in further developing Andorra's statistical system and to participate in e-GDDS. They are interested in requesting further technical assistance from the IMF to improve their data transparency.

STAFF APPRAISAL

40. The pandemic has taken a considerable economic toll but the authorities managed the health crisis well. Universal testing and expanded hospital capacity kept fatality rates very low despite a high number of cases. This strategy helped Andorra implement more targeted internal restrictions than the neighboring countries. At the same time, emergency fiscal measures stabilized real incomes and supported firms. The authorities are highly engaged in transitioning to a green and digitalized economy and more diversified tourism services.

41. Fiscal policy should remain supportive in the near-term and allow for higher public investment in the medium-term. The fiscal rule has served well as a medium-term anchor and offers space for a slower consolidation than the authorities' plans. The risk of renewed lockdowns and uncertainty with various virus strains call for maintaining emergency lifelines. These should only be rolled back gradually, reducing the coverage and generosity of programs if local transmission is low and activity begins to normalize. Some of the planned investments in digital technologies and in climate adaptation and mitigation could be brought forward in 2021 to support the recovery. Frontloading the planned public investment could boost private investment in tourism-related sectors, which are reluctant to invest during uncertain times.

42. Over time, the fiscal authorities will need to build international reserves to cover their liquidity needs in the event of future crises. IMF staff assess such reserves needs to be about 12 percent of GDP, which would be sufficient to cover one month of imports, fiscal revenue fluctuations, and short-term external debt service. Against these liquidity needs, the currently available liquidity is limited to the reserve assets with the IMF, worth two percent of GDP at this stage. Various options are available to build up the remaining 10 percent of GDP over time. Bank liquidity risks need to be intensely supervised to make sure reserve needs of the government do not rise.

43. AFA should ensure banks' sound health in the near-term and manage three structural risks in the medium-term. The supervisors should assess the impact of the pandemic on bank capital so that banks are strong enough to support the recovery and respond to increased demand for credit. Moratoria should be extended only to eligible clients, if needed. In the medium-term, AFA needs to consider stronger rules against related party lending and additional capital in the form of "Pillar II" on related party exposures of specific banks. It should continue to ensure that there are no liquidity gaps in banks. Moreover, the authorities should strengthen the monitoring of cross-border flows and continue deepening the understanding of money-laundering risks.

44. The authorities should develop a strategy to increase the effectiveness of measures to counter corruption. To strengthen the anti-corruption legal framework, Andorra should ratify the UNCAC, establish an assets declaration framework for politically exposed persons, and ensure appropriate public access to information in line with the UNCAC.

45. The authorities already recognize the importance of publishing statistics according to international standards. They are making rapid strides in further developing more comprehensive data on Andorra’s economy to help policy-making and to improve surveillance. They produced balance of payments statistics, with support from the IMF, within a few months of membership. Other external, real, fiscal, and financial sector statistics need to be compiled and reported according to international standards. The authorities plan to work with the IMF in this area and participate in the Enhanced General Data Dissemination System.

46. It is recommended that the next Article IV consultation take place on the standard 12-month cycle.

Table 3. Andorra: Selected Economic and Financial Indicators

I. Social Indicators

Population (2019)	77,543	Poverty Rate (percent, 2019)	13
Per capita income (2019, euros)	36,335	Human Development Index Rank (2019)	36 (out of 189)
Gini Index (2019)	35	Life expectancy at birth (2011)	81.9

II. Economic Indicators

				Estimate	Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
NATIONAL ACCOUNTS AND PRICES	(annual change, percent, unless otherwise indicated)									
Real GDP	0.3	1.6	2.0	-11.8	5.8	4.1	3.6	2.8	1.5	1.5
Nominal GDP	1.5	2.6	3.4	-11.9	6.5	5.3	5.0	4.6	3.2	3.2
GDP deflator	1.1	1.0	1.4	-0.1	0.6	1.1	1.4	1.7	1.7	1.7
	(contribution to nominal GDP growth, percentage points)									
Consumption	...	3.4	2.5	-3.5	4.5	3.5	3.2	3.0	1.9	1.9
Private	...	1.8	1.6	-5.7	3.4	2.8	2.7	2.6	1.5	1.5
Public	...	1.6	1.0	2.2	1.2	0.7	0.5	0.5	0.4	0.4
Investment	...	2.3	1.8	-3.9	0.2	0.5	0.5	0.4	0.4	0.4
Private 1/	...	1.8	1.6	-2.5	-0.8	0.4	0.4	0.3	0.2	0.2
Public	...	0.5	0.2	-1.4	1.0	0.1	0.1	0.2	0.2	0.2
Net exports of goods and services	...	-3.0	-1.0	-4.5	1.7	1.3	1.3	1.1	0.9	0.9
Exports	...	0.8	1.1	-6.8	4.5	4.0	3.7	3.1	2.3	2.3
Imports	...	3.8	2.0	-2.3	2.8	2.7	2.3	2.0	1.4	1.4
Prices										
Inflation (percent, end of period)	2.6	1.3	0.7	0.3	0.5	0.9	1.3	1.6	1.7	1.7
Inflation (percent period average)	2.4	0.8	1.0	-0.2	0.6	1.1	1.3	1.6	1.7	1.7
Unemployment rate (percent)	1.7	1.5	1.8	2.9	3.0	2.4	2.0	1.8	1.7	1.7
EXTERNAL SECTOR	(percent of GDP, unless otherwise indicated)									
Current account	...	...	18.0	14.2	15.5	16.4	17.3	18.0	18.5	19.1
Balance on goods and services	14.2	10.9	9.6	5.8	7.1	8.0	8.9	9.6	10.1	10.7
Exports of goods and services	76.6	75.4	74.0	76.3	75.9	75.9	75.8	75.5	75.4	75.2
Imports of goods and services	62.4	64.6	64.4	70.5	68.8	68.0	67.0	65.9	65.2	64.6
Primary income, net	...	...	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7
Secondary income, net	...	...	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Capital account	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	...	...	18.1	14.2	15.5	16.4	17.3	18.0	18.5	19.1
Errors and omissions	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross international reserves (millions of euros)	...	...	0.0	61.6	61.6	61.6	61.6	61.6	61.6	61.6
FISCAL SECTOR	(percent of GDP, unless otherwise indicated)									
General Government 2/										
Revenue	38.0	38.5	38.0	41.1	38.4	38.6	38.7	38.8	39.0	39.1
Expenditure	34.6	35.7	35.6	44.0	40.8	38.0	36.7	36.1	35.9	35.6
Interest	0.7	0.6	0.5	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Primary balance	4.0	3.4	2.9	-2.3	-1.7	1.2	2.6	3.3	3.8	4.1
Net lending/borrowing (overall balance)	3.3	2.8	2.4	-2.9	-2.3	0.6	2.0	2.7	3.2	3.5
Public debt	37.8	36.3	35.4	51.5	56.7	51.9	43.0	41.0	39.5	38.1
Central Government 3/										
Revenue	19.6	19.6	19.5	20.6	18.8	19.2	19.3	19.4	19.5	19.6
Expenditure	19.3	19.7	19.3	24.9	22.1	20.5	19.4	18.9	18.7	18.5
Interest	0.5	0.5	0.4	0.5	0.6	0.5	0.4	0.4	0.4	0.4
Primary balance	0.8	0.4	0.6	-3.8	-2.8	-0.9	0.3	1.0	1.3	1.5
Net lending/borrowing (overall balance)	0.3	-0.1	0.2	-4.3	-3.3	-1.4	-0.1	0.5	0.9	1.1
Public debt	34.3	33.2	32.7	48.4	53.8	49.1	40.4	38.4	37.1	35.7
BANKING SECTOR	(percent, unless otherwise indicated)									
Regulatory capital to risk-weighted assets	...	20.4	21.8	21.7	...	...	...	...	...	...
Nonperforming loans to total gross loans	...	7.1	7.3	6.1	...	...	...	...	...	...
Credit to nonfinancial private sector										
Level (percent of GDP)	...	147.9	135.9	151.4	...	...	...	...	...	...
Corporates	...	72.0	70.3	76.5	...	...	...	...	...	...
Households	...	75.9	65.6	74.8	...	...	...	...	...	...
Growth (nominal)	...	...	-5.0	-1.8	...	...	...	...	...	...
Corporates	...	...	0.9	-4.0	...	...	...	...	...	...
Households	...	...	-10.6	0.6	...	...	...	...	...	...
Credit to public sector										
Level (percent of GDP)	...	7.5	7.5	6.2	...	...	...	...	...	...
Growth (nominal)	...	...	3.0	-27.2	...	...	...	...	...	...
Memorandum items										
Exchange rate (€/USD, period average)	0.89	0.85	0.89	0.88	0.82	0.81	0.81	0.81	0.81	0.81
Nominal GDP (millions of euros)	2,656	2,725	2,818	2,484	2,645	2,784	2,924	3,058	3,155	3,256

Sources: Govern d'Andorra Department of Statistics, Andorran authorities, Eurostat, and IMF staff calculations.

1/ The contribution of private investment is derived as a residual. Since the fiscal accounts are covered at the general government level, investments of state-owned enterprises are subsumed under private investment.

2/ The general government comprises the central government, local governments and the social security fund.

3/ The central government The central government comprises Govern d'Andorra, as well as non-market public corporations and nonprofits.

Table 4. Andorra: General Government Operations

				Estimate	Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
	(millions national currency)									
Revenue	1,008.5	1,048.6	1,071.4	1,021.8	1,016.9	1,075.6	1,131.3	1,187.5	1,231.4	1,273.2
Tax Revenue	398.2	409.1	416.3	359.4	383.5	416.7	441.0	464.6	482.5	500.4
Income	71.2	84.3	88.0	96.3	81.4	89.1	93.7	98.2	102.0	105.3
Goods and services	135.1	128.5	132.9	107.7	117.9	128.3	136.0	143.5	149.0	154.8
International trade	154.0	156.2	150.9	108.1	133.2	145.0	153.7	162.2	168.4	174.8
Other	37.8	40.2	44.5	47.4	51.1	54.3	57.5	60.7	63.0	65.5
Social Contributions	249.9	263.9	274.2	269.0	268.4	277.7	289.4	302.7	312.4	322.4
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Revenue	360.4	375.6	381.0	393.4	364.9	381.3	400.9	420.2	436.5	450.5
Expenditure	920.1	973.6	1,003.2	1,093.2	1,078.4	1,057.8	1,071.7	1,105.2	1,131.5	1,160.1
Current expenditure	799.5	839.7	863.7	960.5	938.6	923.6	932.8	962.1	985.1	1,008.7
Wages and salaries	212.3	219.4	226.8	236.0	240.1	247.8	252.6	257.5	262.4	267.5
Goods and services	127.5	136.6	138.4	156.2	164.5	164.8	165.7	166.5	167.3	168.2
Subsidies and transfers	441.5	467.3	485.0	553.7	517.9	494.1	496.8	519.6	536.2	553.3
Interest	18.0	16.4	13.6	14.5	16.0	16.9	17.7	18.5	19.1	19.7
Net acquisition of non-financial assets	120.6	133.9	139.5	132.7	139.8	134.2	138.9	143.2	146.4	151.4
Net acquisition of fixed assets	66.9	80.1	88.2	62.8	78.6	80.2	82.2	85.1	88.0	91.1
Capital transfers	53.8	53.8	51.3	69.9	61.2	54.0	56.7	58.1	58.4	60.2
Primary balance	106.4	91.4	81.8	-56.8	-45.5	34.7	77.4	100.8	119.0	132.8
Net lending/borrowing	88.4	75.1	68.2	-71.3	-61.5	17.8	59.7	82.2	99.9	113.1
Financing										
Net acquisition of financial assets	...	...	...	210.4	158.0	-37.2	-126.1	76.4	94.1	107.3
Domestic	...	...	...	210.4	158.0	-37.2	-126.1	76.4	94.1	107.3
External	...	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	...	...	...	281.7	219.5	-55.1	-185.8	-5.8	-5.8	-5.8
Domestic	...	...	...	169.7	-180.5	-655.1	-185.8	-5.8	-5.8	-5.8
New Issuances	...	...	...	515.5	15.5	15.5	15.5	15.5	15.5	15.5
Amortizations	...	...	...	345.8	196.0	670.6	201.3	21.3	21.3	21.3
External	...	...	...	112.0	400.0	600.0	0.0	0.0	0.0	0.0
New Issuances	...	...	...	112.0	500.0	600.0	0.0	0.0	0.0	0.0
Amortizations	...	...	...	0.0	100.0	0.0	0.0	0.0	0.0	0.0
	(percent of GDP)									
Revenue	38.0	38.5	38.0	41.1	38.4	38.6	38.7	38.8	39.0	39.1
Tax Revenue	15.0	15.0	14.8	14.5	14.5	15.0	15.1	15.2	15.3	15.4
Income	2.7	3.1	3.1	3.9	3.1	3.2	3.2	3.2	3.2	3.2
Goods and services	5.1	4.7	4.7	4.3	4.5	4.6	4.7	4.7	4.7	4.8
International trade	5.8	5.7	5.4	4.4	5.0	5.2	5.3	5.3	5.3	5.4
Other	1.4	1.5	1.6	1.9	1.9	1.9	2.0	2.0	2.0	2.0
Social Contributions	9.4	9.7	9.7	10.8	10.1	10.0	9.9	9.9	9.9	9.9
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Revenue	13.6	13.8	13.5	15.8	13.8	13.7	13.7	13.7	13.8	13.8
Expenditure	34.6	35.7	35.6	44.0	40.8	38.0	36.7	36.1	35.9	35.6
Current expenditure	30.1	30.8	30.6	38.7	35.5	33.2	31.9	31.5	31.2	31.0
Wages and salaries	8.0	8.1	8.0	9.5	9.1	8.9	8.6	8.4	8.3	8.2
Goods and services	4.8	5.0	4.9	6.3	6.2	5.9	5.7	5.4	5.3	5.2
Subsidies and transfers	16.6	17.1	17.2	22.3	19.6	17.8	17.0	17.0	17.0	17.0
Interest	0.7	0.6	0.5	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Net acquisition of non-financial assets	4.5	4.9	5.0	5.3	5.3	4.8	4.8	4.7	4.6	4.6
Net acquisition of fixed assets	2.5	2.9	3.1	2.5	3.0	2.9	2.8	2.8	2.8	2.8
Capital transfers	2.0	2.0	1.8	2.8	2.3	1.9	1.9	1.9	1.9	1.9
Primary balance	4.0	3.4	2.9	-2.3	-1.7	1.2	2.6	3.3	3.8	4.1
Net lending/borrowing	3.3	2.8	2.4	-2.9	-2.3	0.6	2.0	2.7	3.2	3.5
Financing										
Net acquisition of financial assets	...	...	...	8.5	6.0	-1.3	-4.3	2.5	3.0	3.3
Domestic	...	...	...	8.5	6.0	-1.3	-4.3	2.5	3.0	3.3
External	...	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	...	...	...	11.3	8.3	-2.0	-6.4	-0.2	-0.2	-0.2
Domestic	...	...	...	6.8	-6.8	-23.5	-6.4	-0.2	-0.2	-0.2
New Issuances	...	...	...	20.8	0.6	0.6	0.5	0.5	0.5	0.5
Amortizations	...	...	...	13.9	7.4	24.1	6.9	0.7	0.7	0.7
External	...	...	...	4.5	15.1	21.6	0.0	0.0	0.0	0.0
New Issuances	...	...	...	4.5	18.9	21.6	0.0	0.0	0.0	0.0
Amortizations	...	...	...	0.0	3.8	0.0	0.0	0.0	0.0	0.0
Memorandum items										
Gross Financing Needs (millions of euros)	...	...	...	417.2	357.5	652.8	141.7	0.0	0.0	0.0
Percent of GDP	...	...	...	16.8	13.5	23.5	4.8	0.0	0.0	0.0
Public Debt (millions of euros)	1,004.6	990.5	997.7	1,279.4	1,498.9	1,443.8	1,258.0	1,252.2	1,246.4	1,240.6
Percent of GDP	37.8	36.3	35.4	51.5	56.7	51.9	43.0	41.0	39.5	38.1
Nominal GDP (in millions of euros)	2,655.8	2,725.3	2,818.4	2,484.2	2,644.7	2,783.6	2,923.5	3,057.5	3,155.2	3,256.3

Sources: Govern d'Andorra Department of Statistics, Andorran authorities and IMF staff calculations.

Note: The general government comprises the central government, local governments and the social security fund.

Table 5. Andorra: Central Government Operations

				Estimate	Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
(millions national currency)										
Revenue	519.9	533.9	549.6	511.6	497.5	534.1	564.0	593.1	616.0	637.8
Tax Revenue	364.2	372.6	375.1	306.5	334.7	361.8	382.9	403.3	418.8	434.3
Income	71.3	84.4	88.1	87.7	80.5	85.2	89.6	93.9	97.6	100.7
Goods and services	135.1	128.5	132.9	107.7	117.7	128.1	135.8	143.3	148.8	154.5
International trade	154.0	156.2	150.9	108.1	133.2	145.0	153.7	162.2	168.4	174.8
Other	3.8	3.6	3.3	3.1	3.3	3.5	3.7	3.9	4.1	4.2
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Revenue	155.7	161.3	174.5	205.1	162.8	172.3	181.1	189.8	197.2	203.5
Expenditure	511.5	535.6	544.9	618.2	585.7	571.7	568.4	576.4	589.2	603.0
Current expenditure	462.9	487.8	487.0	549.3	515.2	514.1	510.4	523.6	534.6	546.5
Wages and salaries	159.7	165.6	170.3	176.1	178.3	182.5	186.0	189.6	193.2	197.0
Goods and services	88.3	95.3	92.3	95.4	108.2	102.8	100.7	101.0	101.5	102.0
Subsidies and transfers	201.0	213.7	212.0	264.6	214.1	214.9	210.5	220.1	227.2	234.5
Interest	13.8	13.1	12.5	13.2	14.7	13.9	13.2	12.8	12.6	13.0
Net acquisition of non-financial assets	48.6	47.8	57.8	68.9	70.5	57.6	58.0	52.8	54.6	56.5
Net acquisition of fixed assets	42.4	40.5	47.9	37.4	37.2	40.9	43.4	45.1	46.7	48.3
Capital transfers	6.2	7.4	9.9	31.4	33.3	16.7	14.6	7.6	7.9	8.1
Primary balance	22.3	11.5	17.2	-93.3	-73.5	-23.7	8.8	29.6	39.5	47.9
Net lending/borrowing	8.5	-1.7	4.8	-106.5	-88.2	-37.6	-4.4	16.8	26.9	34.9
Financing										
Net acquisition of financial assets	…	…	…	175.2	131.3	-92.7	-190.2	11.0	21.1	29.1
Domestic	…	…	…	175.2	131.3	-92.7	-190.2	11.0	21.1	29.1
External	…	…	…	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	…	…	…	281.7	219.5	-55.1	-185.8	-5.8	-5.8	-5.8
Domestic	…	…	…	169.7	-180.5	-655.1	-185.8	-5.8	-5.8	-5.8
New Issuances	…	…	…	515.5	15.5	15.5	15.5	15.5	15.5	15.5
Amortizations	…	…	…	345.8	196.0	670.6	201.3	21.3	21.3	21.3
External	…	…	…	112.0	400.0	600.0	0.0	0.0	0.0	0.0
New Issuances	…	…	…	112.0	500.0	600.0	0.0	0.0	0.0	0.0
Amortizations	…	…	…	0.0	100.0	0.0	0.0	0.0	0.0	0.0
(percent of GDP)										
Revenue	19.6	19.6	19.5	20.6	18.8	19.2	19.3	19.4	19.5	19.6
Tax Revenue	13.7	13.7	13.3	12.3	12.7	13.0	13.1	13.2	13.3	13.3
Income	2.7	3.1	3.1	3.5	3.0	3.1	3.1	3.1	3.1	3.1
Goods and services	5.1	4.7	4.7	4.3	4.5	4.6	4.6	4.7	4.7	4.7
International trade	5.8	5.7	5.4	4.4	5.0	5.2	5.3	5.3	5.3	5.4
Other	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Revenue	5.9	5.9	6.2	8.3	6.2	6.2	6.2	6.2	6.3	6.3
Expenditure	19.3	19.7	19.3	24.9	22.1	20.5	19.4	18.9	18.7	18.5
Current expenditure	17.4	17.9	17.3	22.1	19.5	18.5	17.5	17.1	16.9	16.8
Wages and salaries	6.0	6.1	6.0	7.1	6.7	6.6	6.4	6.2	6.1	6.0
Goods and services	3.3	3.5	3.3	3.8	4.1	3.7	3.4	3.3	3.2	3.1
Subsidies and transfers	7.6	7.8	7.5	10.7	8.1	7.7	7.2	7.2	7.2	7.2
Interest	0.5	0.5	0.4	0.5	0.6	0.5	0.4	0.4	0.4	0.4
Net acquisition of non-financial assets	1.8	1.8	2.1	2.8	2.7	2.1	2.0	1.7	1.7	1.7
Net acquisition of fixed assets	1.6	1.5	1.7	1.5	1.4	1.5	1.5	1.5	1.5	1.5
Capital transfers	0.2	0.3	0.4	1.3	1.3	0.6	0.5	0.3	0.3	0.3
Primary balance	0.8	0.4	0.6	-3.8	-2.8	-0.9	0.3	1.0	1.3	1.5
Net lending/borrowing	0.3	-0.1	0.2	-4.3	-3.3	-1.4	-0.1	0.5	0.9	1.1
Financing										
Net acquisition of financial assets	…	…	…	7.1	5.0	-3.3	-6.5	0.4	0.7	0.9
Domestic	…	…	…	7.1	5.0	-3.3	-6.5	0.4	0.7	0.9
External	…	…	…	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	…	…	…	11.3	8.3	-2.0	-6.4	-0.2	-0.2	-0.2
Domestic	…	…	…	6.8	-6.8	-23.5	-6.4	-0.2	-0.2	-0.2
New Issuances	…	…	…	20.8	0.6	0.6	0.5	0.5	0.5	0.5
Amortizations	…	…	…	13.9	7.4	24.1	6.9	0.7	0.7	0.7
External	…	…	…	4.5	15.1	21.6	0.0	0.0	0.0	0.0
New Issuances	…	…	…	4.5	18.9	21.6	0.0	0.0	0.0	0.0
Amortizations	…	…	…	0.0	3.8	0.0	0.0	0.0	0.0	0.0
Memorandum items										
Gross Financing Needs (millions of euros)	…	…	…	452.4	384.2	708.2	205.7	4.5	0.0	0.0
Percent of GDP	…	…	…	18.2	14.5	25.4	7.0	0.1	0.0	0.0
Public Debt (millions of euros)	911.8	904.0	920.8	1,202.5	1,422.0	1,367.0	1,181.2	1,175.4	1,169.6	1,163.8
Percent of GDP	34.3	33.2	32.7	48.4	53.8	49.1	40.4	38.4	37.1	35.7
Nominal GDP (in millions of euros)	2,655.8	2,725.3	2,818.4	2,484.2	2,644.7	2,783.6	2,923.5	3,057.5	3,155.2	3,256.3

Sources: Govern d'Andorra Department of Statistics, Andorran authorities and IMF staff calculations.

Note: The central government comprises Govern d'Andorra, as well as non-market public corporations and nonprofits.

Table 6. Andorra: Balance of Payments

				Estimate	Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
	(millions national currency)									
Current account	...	...	507.6	353.9	409.7	455.7	504.7	549.4	585.0	621.6
Balance of goods and services	376.7	296.6	270.5	144.9	187.2	221.5	258.8	292.2	319.5	347.6
Imports of goods	1,242.7	1,292.6	1,316.5	1,310.6	1,355.2	1,408.0	1,455.9	1,500.1	1,534.3	1,570.9
Exports of goods	106.3	112.3	116.1	142.9	122.0	128.4	132.9	137.3	141.6	146.1
Imports of services	415.5	466.8	498.8	439.8	465.4	484.4	501.9	516.1	523.8	531.5
Exports of services	1,928.5	1,943.7	1,969.6	1,752.4	1,885.7	1,985.5	2,083.7	2,171.1	2,236.0	2,304.0
Primary income, net	...	...	274.4	241.9	257.5	271.0	284.6	297.7	307.2	317.0
Secondary income, net	...	...	-37.3	-32.9	-35.0	-36.8	-38.7	-40.5	-41.7	-43.1
Capital account	...	...	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	...	...	509.2	353.9	409.7	455.7	504.7	549.4	585.0	621.6
Direct investment, net	...	...	-286.1	...	...	...	...	...	...	...
Portfolio investment, net	...	...	83.8	...	...	...	...	...	...	...
Financial derivatives, net	...	...	N.A.	...	...	...	...	...	...	...
Other investment, net	...	...	711.6	...	...	...	...	...	...	...
Reserve assets	...	...	N.A.	...	...	...	...	...	...	...
Errors and omissions	...	...	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	(in percent of GDP)									
Current account	...	...	18.0	14.2	15.5	16.4	17.3	18.0	18.5	19.1
Balance of goods and services	14.2	10.9	9.6	5.8	7.1	8.0	8.9	9.6	10.1	10.7
Imports of goods	46.8	47.4	46.7	52.8	51.2	50.6	49.8	49.1	48.6	48.2
Exports of goods	4.0	4.1	4.1	5.8	4.6	4.6	4.5	4.5	4.5	4.5
Imports of services	15.6	17.1	17.7	17.7	17.6	17.4	17.2	16.9	16.6	16.3
Exports of services	72.6	71.3	69.9	70.5	71.3	71.3	71.3	71.0	70.9	70.8
Primary income, net	...	...	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7
Secondary income, net	...	...	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Capital account	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	...	...	18.1	14.2	15.5	16.4	17.3	18.0	18.5	19.1
Direct investment, net	...	...	-10.2	...	...	...	...	...	...	...
Portfolio investment, net	...	...	3.0	...	...	...	...	...	...	...
Financial derivatives, net	...	...	...	...	...	...	...	...	...	...
Other investment, net	...	...	25.2	...	...	...	...	...	...	...
Reserve assets	...	...	...	...	...	...	...	...	...	...
Errors and omissions	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items										
Nominal GDP (in millions of euros)	2,656	2,725	2,818	2,484	2,645	2,784	2,924	3,058	3,155	3,256
Gross international reserves (in millions of euros)	...	0.0	0.0	61.6	61.6	61.6	61.6	61.6	61.6	61.6
Gross international reserves (in months of imports)	...	0.0	0.0	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Total external debt (in millions if euros)	5,343	4,977	4,251	...	...	...	...	...	...	...
of which: Short term (in millions of euros)	3,511	3,370	3,134	...	...	...	...	...	...	...

Source: Andorran authorities and IMF staff calculations.

Table 7. Andorra: Financial Soundness Indicators

(in percent)

	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
Core FSIs for Deposit takers									
Regulatory capital to risk-weighted assets	20.4	20.1	20.4	19.9	21.8	20.3	21.3	20.9	21.7
Regulatory Tier 1 capital to risk-weighted assets	20.1	19.8	20.0	19.1	21.0	19.4	20.4	20.0	20.8
Nonperforming loans net of provisions to capital	21.6	21.2	23.4	23.2	21.4	20.7	19.6	19.7	18.4
Nonperforming loans to total gross loans	7.1	7.1	7.6	7.0	7.3	6.3	6.5	5.9	6.1
Sectoral distribution of loans to total loans									
Residents	62.0	63.7	59.4	58.3	61.8	55.3	58.3	52.7	55.8
Deposit-takers	1.0	1.6	1.6	3.7	3.0	2.2	2.0	3.1	1.8
Central bank	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other financial corporations	1.2	1.4	1.2	1.2	1.8	1.5	2.0	1.6	2.6
General government	2.9	3.0	3.0	2.7	3.0	2.7	2.3	1.9	2.0
Nonfinancial corporations	27.8	27.0	24.8	23.9	28.0	25.4	27.4	24.4	25.0
Other domestic sectors	29.2	30.6	28.8	26.9	26.1	23.5	24.7	21.7	24.5
Nonresidents	35.4	36.0	39.6	41.7	38.2	44.7	41.7	47.3	44.2
Return on assets	0.7	0.2	0.3	0.3	0.7	0.2	0.4	0.5	0.5
Return on equity	7.1	2.1	2.6	3.3	6.0	2.2	3.3	4.3	4.4
Interest margin to gross income	22.9	20.4	22.2	23.5	21.6	19.9	21.2	22.0	21.2
Noninterest expenses to gross income	76.1	71.1	78.4	80.6	74.6	65.8	71.0	76.2	75.2
Liquidity coverage ratio (LCR) 1/ 2/	235.9				223.0				187.1
Liquid assets to short-term liabilities 2/	23.2	24.2	21.6	21.8	15.0	22.4	17.5	20.0	14.4
Net open position in foreign exchange to capital	0.0	73.0	5.3	13.5	0.9	4.9	0.0	0.0	0.0
Encouraged FSIs for Deposit takers									
Capital to assets	10.3	10.6	10.4	10.5	11.0	10.7	11.2	10.8	11.5
Large exposures to capital	137.0	133.7	140.1	140.0	134.0	142.9	132.8	147.1	104.7
Gross asset position in financial derivatives to capital	8.9	8.1	8.9	9.3	8.7	16.5	14.6	14.2	13.5
Gross liability position in financial derivatives to capital	12.7	12.3	12.3	13.3	10.9	18.7	16.6	16.7	13.4
Trading income to total income	10.2	12.3	10.0	11.4	10.8	4.0	14.7	14.2	13.9
Personnel expenses to noninterest expenses	48.1	46.5	46.3	46.1	48.8	49.6	47.8	48.4	48.9
Customer deposits to total (noninterbank) loans	146.5	149.0	148.2	149.3	149.2	154.7	152.8	153.8	150.7
Foreign-currency-denominated loans to total loans	0.0	0.1	0.0	1.2	0.1	0.8	0.0	0.0	0.0
Foreign-currency-denominated liabilities to total liabilities	18.2	16.0	21.4	23.8	22.6	23.8	24.5	24.0	21.6

Source: Andorran authorities.

1/ The LCR is defined as the ratio between high-quality liquid assets and net liquidity outflows in a 30-day stress period.

2/ The definition of liquid assets has changed in 2019 from including all exchange-traded securities to including only those financial assets that are held for trading.

Annex I. Arrangements with the European Union

Monetary Agreement

The agreement permits the Banque de France (BdeF) and Banco de España (BdeE) to issue low-denomination euro coins on Andorra's behalf since 2012. In return, Andorra has committed to adopt all EU banking and financial sector directives and regulations within a 10-year horizon. It has also committed to prevent counterfeiting and to address AML/CFT risks. Banking supervisors are eligible for technical assistance from the ECB under this agreement.

Andorra adopted Basel III capital rules through the EU's Capital Requirements Directive (CRD IV) and Regulation (CRR) in 2019, phasing in a proportionate set of rules for its banks and investment firms through 2022. Most of the other legislations have already been transposed. The legal text of the agreement makes it clear that the eurosystem will not deal with or accept Andorran securities for eurozone monetary policy purposes.

A Joint Committee for the Monetary Agreement—comprising representatives from Andorra, the European Commission (EC), the European Central Bank (ECB), BdeF, and BdeE—meets once a year. The Andorran delegation is represented by the Ministries of Finance, Foreign Affairs, and Justice and Interior; Andorran Financial Authority (AFA), which is the single supervisor for all financial institutions; Agència Estatal de Resolució de Entitats (AREB) which is the bank resolution authority, and Unitat d'Intellingencia Financera d'Andorra (UIFAND) which is in charge of AML/CFT supervision and enforcement. The Committee assesses Andorra's progress on adopting financial sector legislations and decides on the maximum amount of issuance of euro coins for Andorra.

Association Agreement

Andorran authorities have been discussing progressive access to the EU internal market since December 2014. The aim of this agreement is to enable small states such as Andorra to participate in the EU's single market while respecting their specificities, in line with the Declaration 3 of Article 8 of the Treaty of the Functioning of the European Union. Their level of market access should, in due course, be comparable to that enjoyed by the European Economic Area Members—EU member states, and Iceland, Liechtenstein and Norway.

The Andorran government views the Association agreement as an opportunity to diversify the economy and considers it to be a priority. In return, Andorra is fully committed to the international standards of transparency and exchange of information. In this regard, the Andorran authorities have committed to improve their legal framework according to the international standards while ensuring a level playing field. So far, the EU and the Andorran authorities have been able to agree on the institutional framework and the free movement of goods (among the four freedoms of goods, services, capital, and labour enshrined in the EU Treaty).

Annex II. Fiscal Rule

A set of rules ensure fiscal discipline and sustainability in Andorra since 2014 after the Global Financial Crisis. The law (Law 32/2014), and subsequent modifications, introduced a multi-annual budget framework that covers the four-year central and local governments' mandates and is updated every year. It sets limits to debt, deficit, current spending, and revenue. The Court of Auditors is responsible for controlling the compliance with the obligations established by the Law.

Items	Limits under the Law
Debt	
General government 1/	55 percent of nominal GDP
Central government 2/	40 percent of nominal GDP
Public or para-public institutions associated with the central government	50 percent of each institution's own equity
Local government (incl. public and para-public institutions associated with the local government)	200 percent of the average budgeted revenues in the preceding 3 years
Deficit	
Overall deficit of the central government 2/	1 percent of nominal GDP
Overall deficit of the local government (incl. public and para-public institutions associated with the local government)	No limit, as long as the local government complies with the debt limit
Current Spending	
Growth of current primary spending of the general government 1/ 3/	Up to the nominal GDP growth if positive, or zero otherwise; the limit does not apply to the local government if its debt (incl. public and para-public institutions associated with the local government) is below 180 percent of the average budgeted revenue in the preceding three years
Revenue	
Direct Taxes	40 percent of total tax collection (excluding taxes from international trade)

1/ For the purpose of this annex, the general government includes the central and local governments and excludes the pension fund.
2/ The central government, for the purpose of this annex, corresponds to Govern d'Andorra and any public or para-public institutions associated with it.
3/ Current primary spending is defined as the sum of wages and salaries, goods and services and current transfers.

The fiscal framework includes an escape clause, which was activated in 2020 due to the fiscal impact of the COVID-19 pandemic. The debt and spending limits associated with the central government can only be exceeded under extraordinary circumstances, comprising natural disasters, serious emergencies, and extraordinary events, including those of economic nature. When this happens, the General Council of the Parliament should approve: (i) an extraordinary budget that exceeds the debt and spending limits established by the Law; and (ii) a plan that sets the path to return to compliance with the debt and spending limits within six years. To finance the extraordinary expenses, the Law creates a structural fund ('*compte de compensació*') that should be endowed with an amount equivalent to 0.1 percent of the total budgeted expenses of the central and local governments. The escape clause does not apply to the local governments, which should always comply with the limits established by the Law. If under exceptional circumstances the budget allocation for the local governments is not enough, the extraordinary need should be covered by the central government.

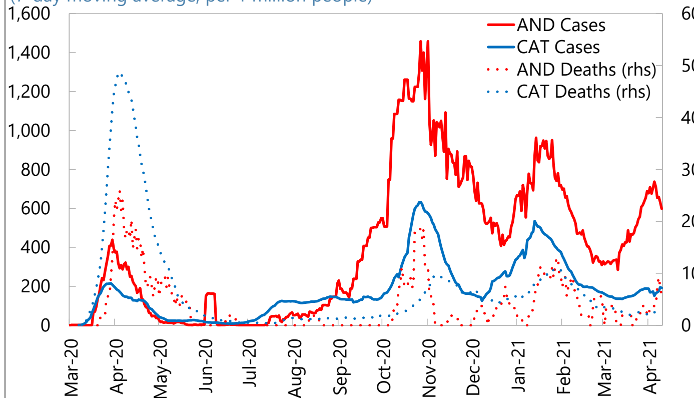
Annex III. COVID-19 Cases and Economic Impact: is Universal Testing Helping Andorra?[1]

Andorra was hit hard by COVID-19, but universal testing allowed the country to adopt less stringent measures than Spain. Compared to the neighboring Spanish region, Catalonia, Andorran activity was recovering better, while the neighbors had their borders open, with contained death rates.

Universal testing partly explains the high number of confirmed cases in Andorra. The authorities made testing the centerpiece of their prevention strategy. Andorra has among the highest rates of testing in Europe, with about 2.5 tests per person on average, while Catalonia's rate is only one test per person. The phased reopening that started in May 2020 was accompanied by widespread testing, with enough tests for the entire Andorran population. The strategy for the winter season involved regular screenings in schools, long-term care, and healthcare facilities, and in retail and tourism firms. In addition, three rapid, self-administered antigen tests were distributed for free to all residents over the age of six to prevent the spread of the disease during the winter holidays.

COVID-19 New Confirmed Cases and Deaths

(7-day moving average; per 1 million people)

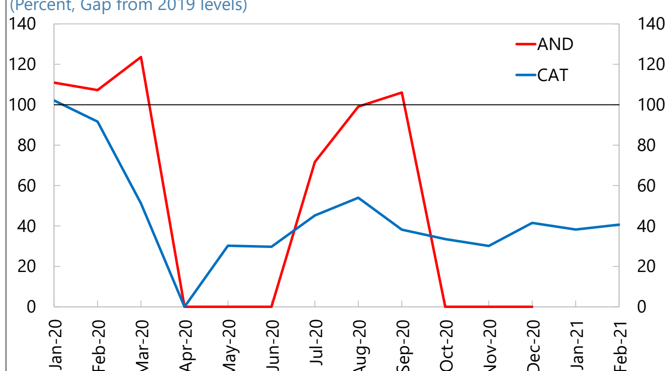


Sources: Bloomberg Finance L.P., Generalitat de Catalunya, Statistical Institute of Catalonia, and IMF staff calculations.

Large testing efforts with data-driven policy decisions, as well as the spillovers from higher stringency in the neighboring countries, allowed Andorra to adopt less stringent containment measures (Figure 6). An analysis of linkages between economic sectors informed the authorities' decisions during the reopening phase to focus on those sectors that are more connected to the rest of the economy and that have a high impact on employment. Furthermore, Doorley et al. (2021), as part of a joint project between Andorra's Innovation Hub and MIT, find that the spread of the virus was highly correlated with inter-parish transmission and with crowding episodes, and less related to tourism. These findings may have been used by the government to promote the arrival of tourists under strict health protocols during the summer and to limit social gatherings and other spreading events

Hotel Occupancy

(Percent, Gap from 2019 levels)



Sources: Statistical Institute of Catalonia, Hotel Union of Andorra, and IMF staff calculations.

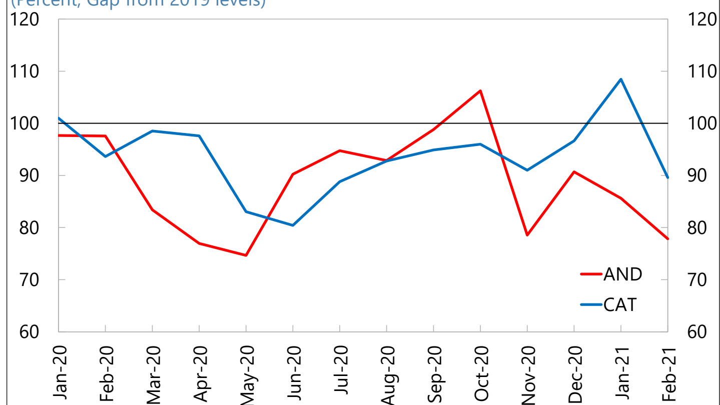
[1] Prepared by Ana Lariau (EUR).

to control the sharp increase in cases since September. In addition, analysis of high-frequency health data not only supported an active communication campaign but also helped the authorities to make quick decisions on the relaxation or tightening of containment measures.

High frequency indicators show that Andorra's economy suffered less than Catalonia when borders were open. More widespread and rapid testing, while increasing the statistics on cases, can help contain the spread of the virus and cushion the economic shock ([Dizioli, Andrle, and Bluedorn, 2020)](). While hotel occupancy in April 2020 was zero in both Andorra and Catalonia, Andorra's occupancy rate quickly recovered to pre-crisis levels during the summer season (keeping death/cases low) but Catalonia's remained subdued, at about half the levels observed in previous years. In September, electricity consumption in Andorra had already caught up to 2019 levels, while Catalonia's was still 5 percent short. These trends reversed since October 2020 due to France and Spain's decision to close their borders until early-April, amid the several waves of infections. While tourism in Andorra has been completely disrupted—including during the peak of the ski season in the first quarter of 2021—Catalonia's economy was supported by internal tourism.

Electricity Consumption

(Percent, Gap from 2019 levels)



Sources: Statistical Institute of Catalonia, Statistics Department of Andorra, and IMF staff calculations.

Annex IV. Risk Assessment Matrix[1]

Sources of Risk	Likelihood of Risk (High, Medium, Low)	Expected Impact of Risk (High, Medium, Low)	Policy Responses
Conjunctural Risks			
Unexpected shift in the Covid-19 pandemic	Medium **Downside.** The disease proves harder to eradicate, requiring costly containment efforts and prompting persistent behavioral changes rendering many activities unviable. Prolonged support is needed to cushion the economy but exacerbates stretched asset valuations, fueling financial vulnerabilities. **Upside.** Pandemic is contained faster than expected due to the rapid production and distribution of vaccines.	High **Downside.** Protracted containment measures and a slower reactivation of the tourism sector would delay the recovery and produce greater scarring effects. Deterioration in banks' asset quality would lead to capital shortfalls and limit the lending channel. Prolonged fiscal support and lower revenues would put further pressure on fiscal accounts and debt. **Upside.** Faster-than-expected recovery would boost confidence and economic activity, though some scarring effects would remain.	• Scale up measures already in place. • Realign policy support measures towards incentivizing reallocation of resources while supporting affected workers during the transition. • Ensure the financial sector's capacity to support the real economy through credit growth. • Accelerate the unwinding of rescue measures, while ensuring that it does not disrupt the recovery process.
Sharp rise in global risk premia	Medium. A reassessment of market fundamentals (e.g., in response to adverse Covid-19 developments) triggers a widespread risk off event, exposing financial and fiscal vulnerabilities.	High. Higher risk premia could generate financing difficulties for firms and households, and a wave of bankruptcies could erode banks' capital buffers. Government financing may become scarcer and more costly as the government accesses international markets for the first time. Bank profitability—given the private banking model—could come under pressure.	• Continue to diversify the government's financing base and reducing gross financing needs. • Build reserve assets to cushion for possible liquidity shortages faced by the government.
Structural Risks			
Higher frequency and severity of natural disasters related to climate change	Medium. Higher frequency and severity of natural disasters related to climate change cause severe economic damage to smaller economies susceptible to disruption.	High. Climate change is affecting Andorra's ski slopes. An increase in temperatures reduce the amount of snow, leading to shorter skiing seasons and negatively impacting the Andorran tourism-based economy.	• Adopt policies to adapt to climate change while transitioning to greener goals. • Provide targeted support to most vulnerable sectors, particularly tourism.
Domestic Risks			
Higher-than-expected call on government guarantees	Medium. Increasing stress in the real sector could impose a larger call on government guarantees.	High. A sudden increase of the government's gross financing needs, without a well-diversified funding base, could require temporary stops to government funding/transfer programs leading to an even weaker recovery.	• Maintain fiscal sustainability by continuing to adhere to the fiscal rule. • Continue diversifying the government's funding base and reducing gross financing needs.
Excessive stress on the banking sector	Medium. The lifting of loan and insolvency moratoria, as well as the expiration of fiscal measures in the corporate sector, may reveal large loan losses for banks. Sizeable gross external liabilities would pose systemic liquidity risks.	High. Increase in capital needs of banks. Due to the size and systemic nature of banks, this could increase contingent liabilities of the government and lead to higher funding costs for the private and public sectors.	• Assess bank capital needs • Strengthen bank supervision to reduce related party risks and liquidity risks.
Setbacks in closing AML/CFT gaps	Medium. Delays in aligning the Andorran AML/CFT legal framework with FATF standards.	High. Reputational damage, reduced external funding and access to international financial services, higher borrowing costs, and increased scrutiny of Andorran entities.	• Strengthen AML/CFT risk-based supervision, the sanctioning of ML activities and the recovery of proceeds of crime.

[1] The Risk Assessment Matrix shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of the staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline. "Low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability of 30 percent or more.

Annex V. Public Debt Sustainability Assessment

Andorran public debt remains sustainable under the baseline scenario and under a high public investment scenario. Debt increased beyond the fiscal debt limits in 2020 reflecting the deterioration of the primary balance, the accumulation of debt repayments, and the authorities pre-financing strategy. Starting in 2022, the debt ratio is set to decline rapidly to pre-pandemic levels, a sizable but credible consolidation effort supported by the authorities track-record of prioritizing fiscal discipline. With careful consideration of gross financing needs and projects' soundness, the authorities have adequate space to increase infrastructure spending beyond the baseline levels, while also building fiscal buffers. However, a negative shock to real GDP growth or a sharp increase in contingent liabilities could slow the consolidation pace and worsen debt dynamics even though debt remains sustainable under such scenarios.

A. Background

This DSA is produced in the context of Andorra's first Article IV Consultation. The DSA covers the general government debt, encompassing the central government debt, and the local government debt, and social security funds.[1] Over 90 percent of the public debt is owed by the central government. Central government guarantees of up to €230 million are not included in the baseline scenario, but a contingent liability shock—based on calls on guarantees—has been included as part of the analysis. The Law 32/2014, and subsequent modifications, aimed at ensuring fiscal discipline in Andorra sets limits to the debt of general government (excluding pension fund) and the central government at 55 and 40 percent of GDP, respectively, among other fiscal rules (Annex II). These limits can be exceeded only under extraordinary circumstances by activating an escape clause. This happened in 2020 due to the fiscal impact of the COVID-19 pandemic but the authorities aim to be below the limit within three years.

Public debt levels prior to the pandemic remained well below the debt limits imposed by the fiscal rule, reflecting Andorra's strong fiscal position. The general government debt stock averaged 39.2 percent of GDP in 2010–2018, reaching a peak of 42.5 percent of GDP in 2013 and gradually declining to 35.4 percent of GDP in 2019. However, debt rose sharply in 2020 to 51.5 percent of GDP reflecting the deterioration of the primary balance amidst the COVID-19 crisis, the accumulation of debt repayments; as well as part of the authorities' pre-financing strategy that leads to a large but temporary increase in net acquisition of financial assets to be used for future debt service.

However, due to the short maturity of debt, gross financing needs have been relatively high historically, despite the government efforts to persistently sustain primary surpluses. Historical debt stocks consisted primarily of domestic bonds with average maturity of about three years which

[1] Historical data on debt stocks and flows are preliminary at this stage. The mission is working closely with the authorities to verify the composition of the debt stocks and flows by instrument, and to incorporate data on net acquisition of financial assets and other debt-creating flows.

were typically rolled over at the time of maturity. These dynamics, while not substantially increasing public debt over time, resulted in average annual gross financing needs of 8.8 percent of GDP in 2010–2019.

B. Baseline Scenario

Public debt is projected to increase further in 2021—due to the authorities pre-financing strategy—and to decline rapidly afterwards. The authorities issued Eurobonds worth €500 million in 2021, with a maturity of 10 years, as part of a program totaling €1.2 billion over 2021–22. Such a debt reprofiling would help to diversify founding sources and lower annual gross financing needs in coming years, while taking advantage of favorable market conditions. Even though this strategy increases central government's debt by 10 percentage points of GDP to 56.7 percent of GDP in 2021, the debt service will decline significantly from 2023 onwards, freeing fiscal resources for other needs including for the gradual buildup of fiscal buffers. Moreover, the positive impact on revenue of the recovery of economic activity, coupled with the rollback of the COVID-19 related measures, will lead to general government primary surpluses starting from 2022, and central government primary surpluses starting from 2023. The combined effect of improved fiscal balances and lower debt service is expected to put debt on a declining path, reaching the fiscal rule target of the general government by 2022 and of the central government by 2024. Under the baseline scenario, gross general government debt is expected to reach 38.1 percent by 2026 and continue its declining path over the long-term.

Underlying Assumptions and Realism of Projections

Although with high uncertainty, the baseline scenario assumes significant scarring in the medium-term and convergence to the Euro Area (EA) average GDP growth rate by 2025. Following an estimated fall of 11.8 percent in 2020, real GDP is projected to recover by 5.8 percent in 2021, remain strong in 2022 as the world economy recovers fully from the pandemic, and eventually converge to the EA average by 2026. Higher revenues during the recovery and the roll-back of COVID-19 measures will lead to primary surpluses from 2022 in line with the authorities' plan to rapidly consolidate and reduce its public debt stock. Inflation for 2021 is estimated at 0.3 percent, and projected to remain subdued in the short-term, only slowly rising toward EA levels by 2025. Sovereign borrowing spreads are assumed to be uniformly 147 bps above German yields for all maturities in line with the actual yield on privately placed external bonds in April 2021.

Assessing the realism of projections, cross-country experience suggests that Andorra's projected adjustment is credible yet sizable. The projected adjustment and level of the cyclically-adjusted primary balance (CAPB) are below the threshold that would cast doubt on the feasibility of the adjustment, based on high-debt country experienced.[2] The near-term adjustment in the CAPB is large compared with cross-country experience but reflect the sizable but temporary COVID-19 measures, which are largely assumed to expire in 2021 followed by rapid consolidation and decline

[2] In the absence of potential output estimate due to data constraints, it is not possible to estimate the CAPB. The current estimate reflects the actual primary balance.

in gross financing needs. The credibility of the consolidation effort is also supported by the authorities track-record of staying within the broad parameters of their medium-term fiscal framework, which prioritizes debt sustainability.

Stress Tests and Alternative Scenarios

Standard stress tests' scenarios suggest that a shock to real GDP growth would significantly worsen debt dynamics, slowing debt consolidation and increasing gross financing needs.[3] Under this scenario: (i) public debt declines only to 51.2 by 2026 (compared to 38.1 under the baseline); (ii) gross debt in percent of revenue declines from 147.4 in 2021 to 131 in 2026, instead of 97.5 percent under the baseline; and (iii) gross financing needs peak at 27.4 percent of GDP in 2022, compared to 23.7 under the baseline scenario. Alternatively, shocks to the primary balance, the real exchange rate, or the real interest rate do not lead to significant deviations from the baseline.

Moreover, an alternative scenario of a contingent liability shock would also result in higher debt ratios and gross financing needs. The contingent liability shock assumes a one-time increase in non-interest expenditures equivalent to 1 percent of banking sector assets leading to a real GDP growth shock. This represents a call on 25 percent of €135 million worth of outstanding public guarantees provided for bank loans to liquidity-strapped companies as part of the COVID-19 related measures, and additional 2 percent of GDP for the case of an adverse shock in the banking sector. Under this scenario, gross financing needs peak at 30.8 percent of GDP in 2022. This is 7.1 percentage points higher than the baseline, of which 5.1 percentage points of GDP result from the outstanding public guarantees.

In contrast, a modest increase in public investment financed with new debt could support the economic recovery and would not lead to significant increases in public debt. Assuming an increase of around 1 percent of GDP in 2021–2023—financed by issuing €100 million extra long-term debt—would keep debt ratios close to the baseline scenario as the positive impact on GDP growth outweighs the burden of the additional cost (see main text, Figure 12). If carefully selected, public investment projects could support the economic recovery as the fiscal multiplier of investment and job-creating potential are assumed to be high in the post-pandemic recovery phase, and improved infrastructure would in turn positively affect long-term potential growth and strengthen the resilience and sustainability of the country.

[3] The shock to real GDP growth assumes that real GDP growth in 2021 and 2022 is lower than in the baseline by one standard deviation; which in turn leads to lower inflation (0.25 percentage points per 1 percentage point decrease in GDP growth), and the deterioration in primary balance lead to higher interest rate.

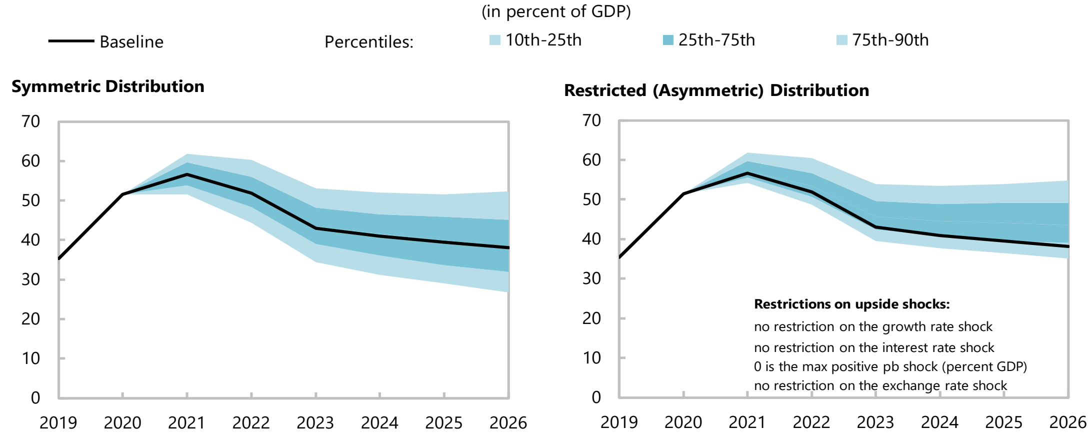
Annex Figure V.1. Andorra: Public DSA Risk Assessment

Heat Map

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

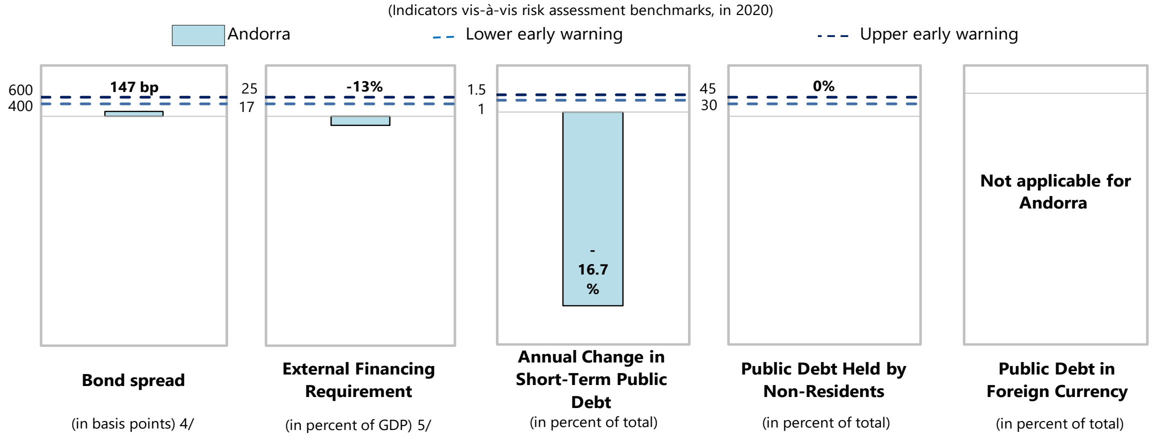
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2020)



Source: IMF staff.

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

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

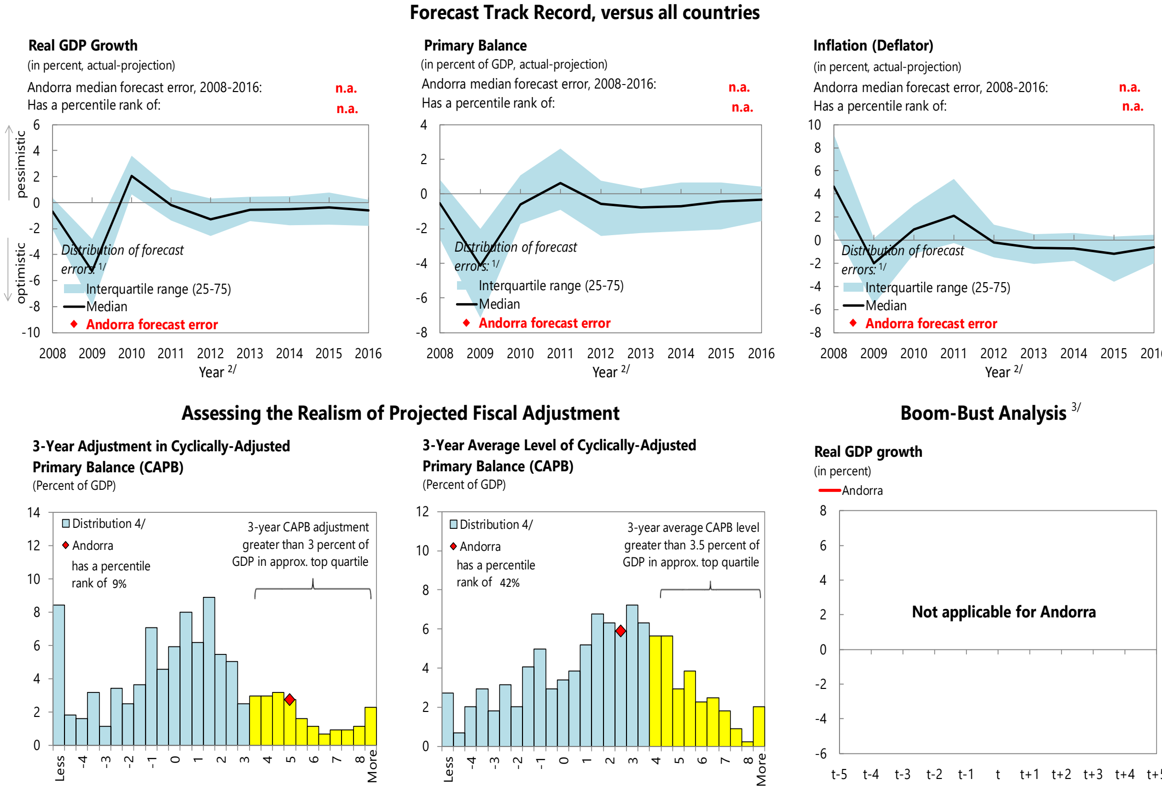
3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant,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

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

4/ Long-term bond spread over German bonds, an average over the last 3 months, 02-Feb-21 through 03-May-21.

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

Annex Figure V.2. Andorra: Public DSA—Realism of Baseline Assumptions



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Andorra, as it meets neither the positive output gap criterion nor the private credit growth criterion.

4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Annex Figure V.3. Andorra: Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

(in percent of GDP unless otherwise indicated)

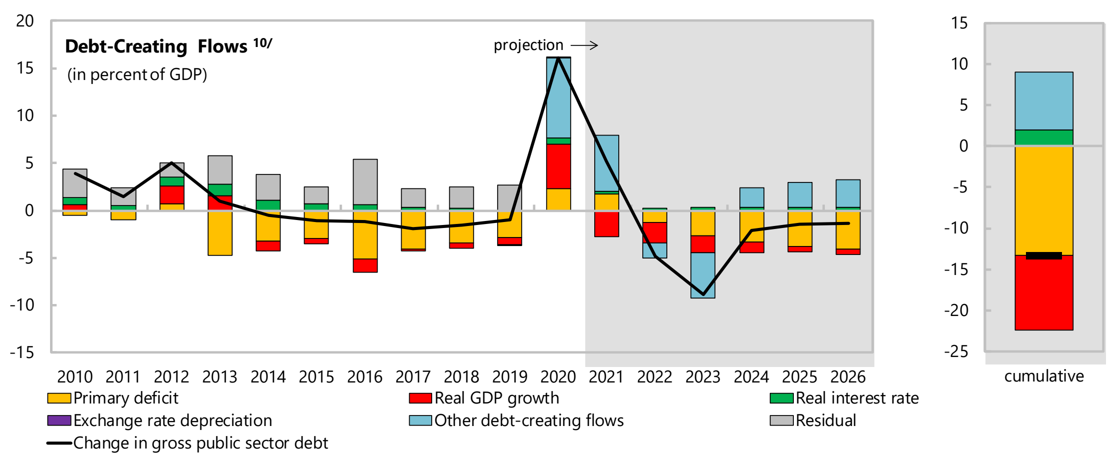
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2010-2018 [2/]	2019	2020	2021	2022	2023	2024	2025	2026
Nominal gross public debt	39.2	35.4	51.5	56.7	51.9	43.0	41.0	39.5	38.1
Public gross financing needs	8.6	10.1	16.8	13.5	23.7	5.3	-1.5	-2.0	-2.4
Real GDP growth (in percent)	-0.1	2.0	-11.8	5.8	4.1	3.6	2.8	1.5	1.5
Inflation (GDP deflator, in percent)	0.5	1.4	-0.1	0.6	1.1	1.4	1.7	1.7	1.7
Nominal GDP growth (in percent)	0.4	3.4	-11.9	6.5	5.3	5.0	4.6	3.2	3.2
Effective interest rate (in percent) [4/]	2.3	1.4	1.5	1.3	1.5	2.2	2.6	2.6	2.7

As of May 03, 2021		
Sovereign Spreads		
EMBIG (bp) 3/		147
5Y CDS (bp)		95
Ratings	Foreign	Local
Moody's	n.a.	n.a.
S&Ps	BBB	BBB
Fitch	BBB+	BBB+

Contribution to Changes in Public Debt

	Actual			Projections							
	2010-2018	2019	2020	2021	2022	2023	2024	2025	2026	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	0.6	-0.9	16.1	5.2	-4.8	-8.8	-2.1	-1.4	-1.4	-13.4	
Identified debt-creating flows	-2.0	-3.6	16.1	5.2	-4.8	-8.8	-2.1	-1.4	-1.4	-13.4	
Primary deficit	-2.7	-2.9	2.3	1.7	-1.2	-2.6	-3.3	-3.8	-4.1	-13.3	2.7
Primary (noninterest) revenue and grants	34.3	38.0	41.1	38.4	38.6	38.7	38.8	39.0	39.1	232.8	
Primary (noninterest) expenditure	31.6	35.1	43.4	40.2	37.4	36.1	35.5	35.3	35.0	219.4	
Automatic debt dynamics [5/]	0.7	-0.7	5.3	-2.5	-2.0	-1.4	-0.8	-0.2	-0.2	-7.1	
Interest rate/growth differential [6/]	0.7	-0.7	5.3	-2.5	-2.0	-1.4	-0.8	-0.2	-0.2	-7.1	
Of which: real interest rate	0.7	0.0	0.6	0.3	0.2	0.4	0.3	0.4	0.4	2.0	
Of which: real GDP growth	0.0	-0.7	4.7	-2.8	-2.2	-1.8	-1.2	-0.6	-0.6	-9.1	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	8.5	6.0	-1.6	-4.8	2.0	2.5	2.9	7.1	
Net acq. of financial assets (negative)	0.0	0.0	8.5	6.0	-1.6	-4.8	2.0	2.5	2.9	7.1	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	2.6	2.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	



Source: IMF staff.

1/ Public sector is defined as general 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.

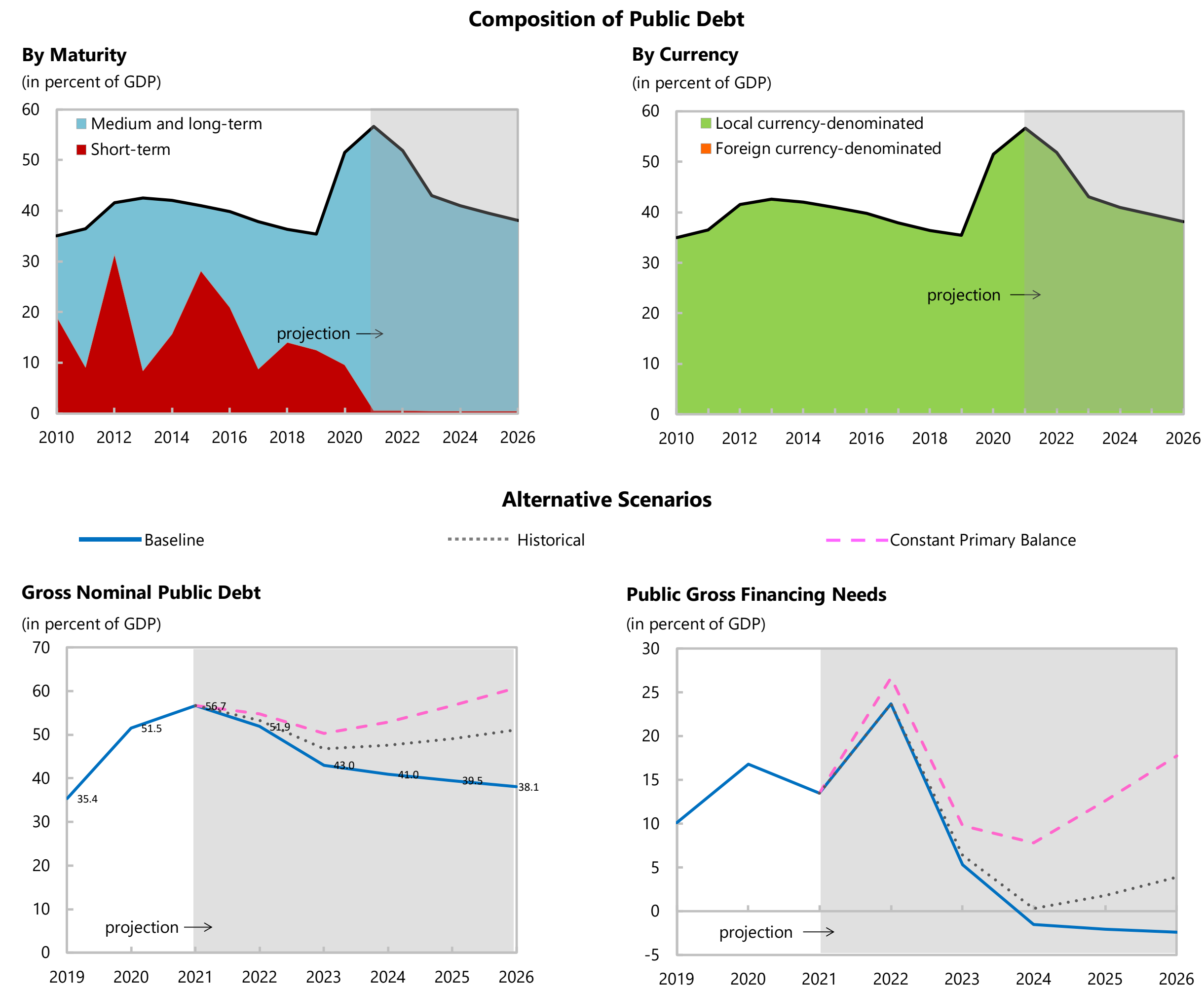
7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

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.

10/ Historical data on net acquisition of financial assets and other debt-creating flows prior to 2020 are not included, resulting in a relatively large residual.

Annex Figure V.4. Andorra: Public DSA—Composition of Public Debt and Alternative Scenarios



Underlying Assumptions

(in percent)

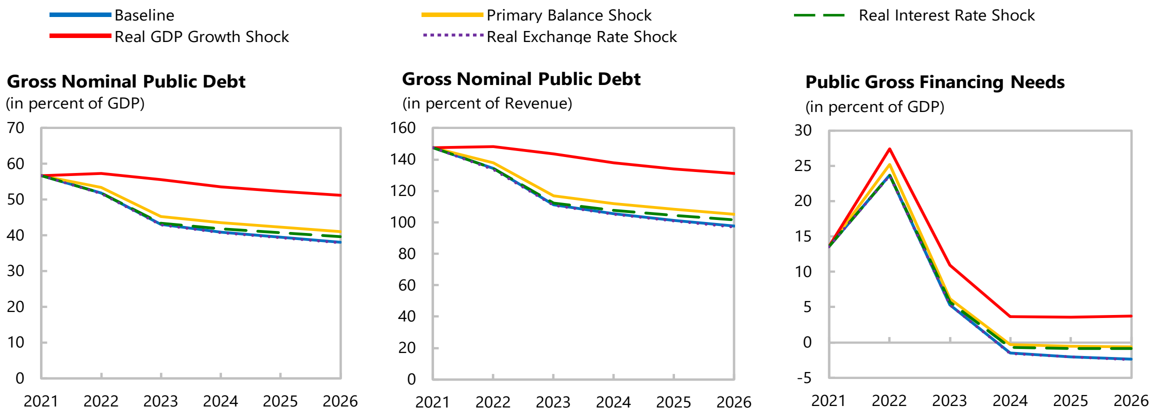
Baseline Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	5.8	4.1	3.6	2.8	1.5	1.5
Inflation	0.6	1.1	1.4	1.7	1.7	1.7
Primary Balance	-1.7	1.2	2.6	3.3	3.8	4.1
Effective interest rate	1.3	1.5	2.2	2.6	2.6	2.7
Constant Primary Balance Scenario						
Real GDP growth	5.8	4.1	3.6	2.8	1.5	1.5
Inflation	0.6	1.1	1.4	1.7	1.7	1.7
Primary Balance	-1.7	-1.7	-1.7	-1.7	-1.7	-1.7
Effective interest rate	1.3	1.5	2.1	2.3	2.2	2.1

Historical Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	5.8	-0.9	-0.9	-0.9	-0.9	-0.9
Inflation	0.6	1.1	1.4	1.7	1.7	1.7
Primary Balance	-1.7	2.4	2.4	2.4	2.4	2.4
Effective interest rate	1.3	1.5	2.5	2.9	2.9	2.9

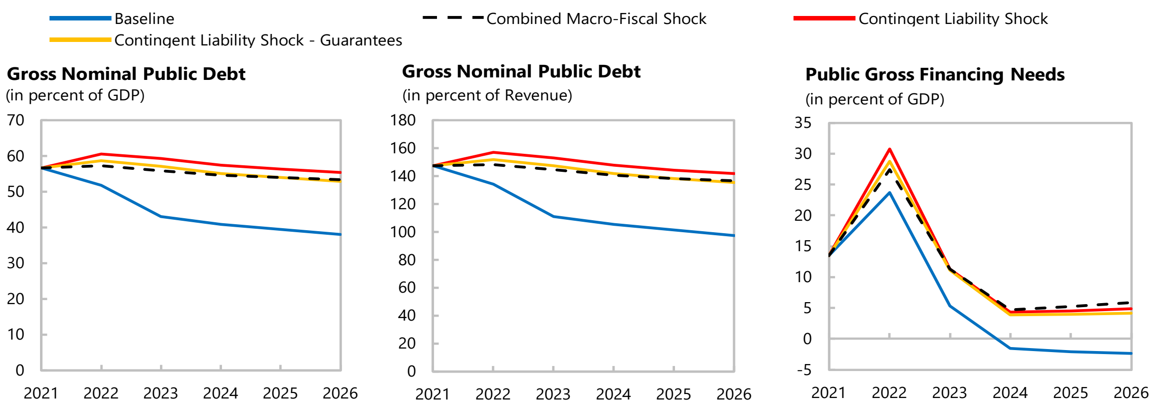
Source: IMF staff.

Annex Figure V.5. Andorra: Public DSA—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests [1/]



Underlying Assumptions
(in percent)

Primary Balance Shock	2021	2022	2023	2024	2025	2026
Real GDP growth	5.8	4.1	3.6	2.8	1.5	1.5
Inflation	0.6	1.1	1.4	1.7	1.7	1.7
Primary balance	-1.7	-0.2	1.9	3.0	3.5	3.9
Effective interest rate	1.3	1.5	2.3	2.7	2.7	2.8
Real Interest Rate Shock						
Real GDP growth	5.8	4.1	3.6	2.8	1.5	1.5
Inflation	0.6	1.1	1.4	1.7	1.7	1.7
Primary balance	-1.7	1.2	2.6	3.3	3.8	4.1
Effective interest rate	1.3	1.5	3.0	3.5	3.6	3.6
Combined Shock						
Real GDP growth	5.8	-0.6	-1.1	2.8	1.5	1.5
Inflation	0.6	-0.1	0.2	1.7	1.7	1.7
Primary balance	-1.7	-1.0	-1.8	3.0	3.5	3.9
Effective interest rate	1.3	1.5	3.0	3.3	3.4	3.4
Contingent Liability Shock - Guarantees						
Real GDP growth	5.8	-0.6	-1.1	2.8	1.5	1.5
Inflation	0.6	-0.1	0.2	1.7	1.7	1.7
Primary balance	-1.7	-2.4	-1.8	3.3	3.8	4.1
Effective interest rate	1.3	1.5	2.5	2.8	2.8	2.8

Real GDP Growth Shock	2021	2022	2023	2024	2025	2026
Real GDP growth	5.8	-0.6	-1.1	2.8	1.5	1.5
Inflation	0.6	-0.1	0.2	1.7	1.7	1.7
Primary balance	-1.7	-1.0	-1.8	3.3	3.8	4.1
Effective interest rate	1.3	1.5	2.4	2.6	2.6	2.7
Real Exchange Rate Shock						
Real GDP growth	5.8	4.1	3.6	2.8	1.5	1.5
Inflation	0.6	1.5	1.4	1.7	1.7	1.7
Primary balance	-1.7	1.2	2.6	3.3	3.8	4.1
Effective interest rate	1.3	1.5	2.2	2.6	2.6	2.7
Contingent Liability Shock						
Real GDP growth	5.8	-0.6	-1.1	2.8	1.5	1.5
Inflation	0.6	-0.1	0.2	1.7	1.7	1.7
Primary balance	-1.7	-4.4	-1.8	3.3	3.8	4.1
Effective interest rate	1.3	1.6	2.8	3.0	3.0	3.0

Source: IMF staff.

1/ The "contingent liability shock" assumes the combination of a one-time increase in non-interest expenditures equivalent to 1.02% of banking sector assets (25% of €135 million outstanding with public guarantees plus 2% of GDP) and a standard real GDP shock, in which real GDP growth is reduced by 1 standard deviation for 2 consecutive years; revenue-to-GDP ratio remains the same as in the baseline; level of non-interest expenditures is the same as in the baseline (plus the contingent liability); deterioration in primary balance lead to higher interest rate; decline in growth leads to lower inflation (0.25 percentage points per 1 percentage point decrease in GDP growth). The "contingent liability shock - guarantees" assumes the combination of a one-time increase in non-interest expenditures equivalent only to the public guarantees portion and a standard real GDP shock.

PRESS RELEASE

PR[21/XX]

Appendix I. Draft Press Release

IMF Executive Board Concludes 2021 Article IV Consultation with Andorra

[FOR IMMEDIATE RELEASE]

Washington, DC – June 7, 2021: The Executive Board of the International Monetary Fund (IMF) concluded the first Article IV consultation[1] with Andorra.

The COVID-19 pandemic has hit Andorra's society and economy severely following a broad-based, job-rich growth in 2019. Tourism and domestic services fell with the stringency of containment measures in the first half of 2020 but rebounded strongly during the summer with the arrival of tourists and a temporary ease of stringency. With French and Spanish borders closed until recently, especially during the height of the ski season in the first quarter of 2021, hotels and ski resorts have already lost a major share of their annual revenue.

Universal testing might have enabled more targeted containment measures compared to the region. Despite the very high prevalence of COVID-19 cases per capita, fatality rates are among the lowest in the world as hospital capacity and protective equipment were quickly scaled up in response to the pandemic. So far, the pace of vaccination has been comparable to that of EU countries, and about a third of the population have received at least one dose so far [April 30].

In response to the virus outbreak, the authorities undertook mitigating fiscal and financial sector measures. Expenditure measures worth 2.2 percent of GDP and revenue measures worth 0.4 percent of GDP included healthcare spending and financial support for pandemic-affected sectors and households. In addition, government guarantees worth 9 percent of GDP were made available for bank loans to liquidity-strapped companies. In the financial sector, debt moratoria provided relief to private sector borrowers. The COVID-related measures and lower revenues reduced the central government balance to -4.3 percent of GDP and increased government debt to about 48 percent of GDP in 2020.

Activity is estimated to have fallen by about 12 percent in 2020 and, under a baseline scenario without new widespread containment measures, is projected to partially recover by about 6 percent in 2021. The

[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.

recovery rests on a strong rebound in private consumption and return of tourism. Government debt is expected to rise further to about 54 percent of GDP in 2021, before descending to the fiscal rule limit of 40 percent of GDP in the medium-term. The outlook is highly uncertain, with risks heavily tilted to the downside in the near-term and will crucially depend on the containment of the waves of infections in Andorra and the region; as well as on the success of policy measures to mitigate the scarring effects of the crisis.

Executive Board Assessment[2]

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[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

Andorra: Selected Economic and Financial Indicators

I. Social Indicators

Population (2019)	77,543	Poverty Rate (percent, 2019)	13
Per capita income (2019, euros)	36,335	Human Development Index Rank (2019)	36 (out of 189)
Gini Index (2019)	35	Life expectancy at birth (2011)	81.9

II. Economic Indicators

				Estimate			Projections			
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
NATIONAL ACCOUNTS AND PRICES				(annual change, percent, unless otherwise indicated)						
Real GDP	0.3	1.6	2.0	-11.8	5.8	4.1	3.6	2.8	1.5	1.5
Nominal GDP	1.5	2.6	3.4	-11.9	6.5	5.3	5.0	4.6	3.2	3.2
GDP deflator	1.1	1.0	1.4	-0.1	0.6	1.1	1.4	1.7	1.7	1.7
				(contribution to nominal GDP growth, percentage points)						
Consumption	...	3.4	2.5	-3.5	4.5	3.5	3.2	3.0	1.9	1.9
Private	...	1.8	1.6	-5.7	3.4	2.8	2.7	2.6	1.5	1.5
Public	...	1.6	1.0	2.2	1.2	0.7	0.5	0.5	0.4	0.4
Investment	...	2.3	1.8	-3.9	0.2	0.5	0.5	0.4	0.4	0.4
Private 1/	...	1.8	1.6	-2.5	-0.8	0.4	0.4	0.3	0.2	0.2
Public	...	0.5	0.2	-1.4	1.0	0.1	0.1	0.2	0.2	0.2
Net exports of goods and services	...	-3.0	-1.0	-4.5	1.7	1.3	1.3	1.1	0.9	0.9
Exports	...	0.8	1.1	-6.8	4.5	4.0	3.7	3.1	2.3	2.3
Imports	...	3.8	2.0	-2.3	2.8	2.7	2.3	2.0	1.4	1.4
Prices										
Inflation (percent, end of period)	2.6	1.3	0.7	0.3	0.5	0.9	1.3	1.6	1.7	1.7
Inflation (percent period average)	2.4	0.8	1.0	-0.2	0.6	1.1	1.3	1.6	1.7	1.7
Unemployment rate (percent)	1.7	1.5	1.8	2.9	3.0	2.4	2.0	1.8	1.7	1.7
EXTERNAL SECTOR				(percent of GDP, unless otherwise indicated)						
Current account	...	...	18.0	14.2	15.5	16.4	17.3	18.0	18.5	19.1
Balance on goods and services	14.2	10.9	9.6	5.8	7.1	8.0	8.9	9.6	10.1	10.7
Exports of goods and services	76.6	75.4	74.0	76.3	75.9	75.9	75.8	75.5	75.4	75.2
Imports of goods and services	62.4	64.6	64.4	70.5	68.8	68.0	67.0	65.9	65.2	64.6
Primary income, net	...	...	9.7	9.7	9.7	9.7	9.7	9.7	9.7	9.7
Secondary income, net	...	...	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Capital account	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	...	...	18.1	14.2	15.5	16.4	17.3	18.0	18.5	19.1
Errors and omissions	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross international reserves (millions of euros)	...	...	0.0	61.6	61.6	61.6	61.6	61.6	61.6	61.6
FISCAL SECTOR				(percent of GDP, unless otherwise indicated)						
General Government 2/										
Revenue	38.0	38.5	38.0	41.1	38.4	38.6	38.7	38.8	39.0	39.1
Expenditure	34.6	35.7	35.6	44.0	40.8	38.0	36.7	36.1	35.9	35.6
Interest	0.7	0.6	0.5	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Primary balance	4.0	3.4	2.9	-2.3	-1.7	1.2	2.6	3.3	3.8	4.1
Net lending/borrowing (overall balance)	3.3	2.8	2.4	-2.9	-2.3	0.6	2.0	2.7	3.2	3.5
Public debt	37.8	36.3	35.4	51.5	56.7	51.9	43.0	41.0	39.5	38.1
Central Government 3/										
Revenue	19.6	19.6	19.5	20.6	18.8	19.2	19.3	19.4	19.5	19.6
Expenditure	19.3	19.7	19.3	24.9	22.1	20.5	19.4	18.9	18.7	18.5
Interest	0.5	0.5	0.4	0.5	0.6	0.5	0.4	0.4	0.4	0.4
Primary balance	0.8	0.4	0.6	-3.8	-2.8	-0.9	0.3	1.0	1.3	1.5
Net lending/borrowing (overall balance)	0.3	-0.1	0.2	-4.3	-3.3	-1.4	-0.1	0.5	0.9	1.1
Public debt	34.3	33.2	32.7	48.4	53.8	49.1	40.4	38.4	37.1	35.7
BANKING SECTOR				(percent, unless otherwise indicated)						
Regulatory capital to risk-weighted assets	...	20.4	21.8	21.7	...	...	...	...	...	...
Nonperforming loans to total gross loans	...	7.1	7.3	6.1	...	...	...	...	...	...
Credit to nonfinancial private sector										
Level (percent of GDP)	...	147.9	135.9	151.4	...	...	...	...	...	...
Corporates	...	72.0	70.3	76.5	...	...	...	...	...	...
Households	...	75.9	65.6	74.8	...	...	...	...	...	...
Growth (nominal)	...	...	-5.0	-1.8	...	...	...	...	...	...
Corporates	...	...	0.9	-4.0	...	...	...	...	...	...
Households	...	...	-10.6	0.6	...	...	...	...	...	...
Credit to public sector										
Level (percent of GDP)	...	7.5	7.5	6.2	...	...	...	...	...	...
Growth (nominal)	...	...	3.0	-27.2	...	...	...	...	...	...
Memorandum items										
Exchange rate (€/USD, period average)	0.89	0.85	0.89	0.88	0.82	0.81	0.81	0.81	0.81	0.81
Nominal GDP (millions of euros)	2,656	2,725	2,818	2,484	2,645	2,784	2,924	3,058	3,155	3,256

Sources: Govern d'Andorra Department of Statistics, Andorran authorities, Eurostat, and IMF staff calculations.

1/ The contribution of private investment is derived as a residual. Since the fiscal accounts are covered at the general government level, investments of state-owned enterprises are subsumed under private investment.

2/ The general government comprises the central government, local governments and the social security fund.

3/ The central government The central government comprises Govern d'Andorra, as well as non-market public corporations and nonprofits.