

COSTA RICA

1. General trends

The Costa Rican economy grew by 5.1% in 2012, compared with 4.2% in 2011, driven by robust growth in external demand (8.5%) and gross fixed capital investment (8.1%). Domestic demand also expanded, but at a slower pace (4.3%).

Unemployment stood at 7.8% (7.7% in 2011), while year-on-year inflation was 4.6% at December 2012 (4.7% at December 2011), within the target range set by the central bank for 2012 (5.0% \pm 1 percentage point).

The central government fiscal deficit came to 4.4% of GDP, against 4.1% the previous year. The deficit of the narrowly defined global public sector—which includes the central government, the central bank and the non-financial public sector—was 5.0% of GDP, compared with 5.6% the previous year. The widening fiscal deficit and greater liquidity absorption undertaken by the central bank pushed public debt up to 51.3% of GDP at December 2012, against 44.6% in 2011.

The current account ended 2012 with a deficit of 5.2% of GDP, down from the 5.4% posted in 2011, largely as a result of a narrowing goods balance deficit and a services account surplus in line with the 2011 figure (7.8% of GDP).

During 2012, significant progress was made towards signing an association agreement between Central America and the European Union.

In the first quarter of 2013, the monthly index of economic activity (IMAE)—trend-cycle adjusted—posted a year-on-year variation of 3.9%, lower than in the year-earlier period (7.2%). ECLAC estimates growth of 3.5% in 2013. The fiscal deficit is expected to remain at current levels, owing to the difficulty in containing the growth of current expenditure and the absence of a comprehensive fiscal reform that would boost tax revenues. The current account deficit is expected to remain high.

2. Economic policy

(a) Fiscal policy

Despite efforts to curb public spending and strengthen tax administration, the central government fiscal deficit came to 4.4% of GDP, 0.3% higher than the previous year. The fiscal deficit of the narrowly defined global public sector—which includes the central government, the central bank and the non-financial public sector—amounted to 5.0% of GDP, as compared with 5.6% the previous year. This reduction is mainly attributable to the rest of the narrowly defined non-financial public sector, which more than compensated for the deterioration in central government accounts by moving from a deficit of 0.9% of GDP in 2011 to a surplus of 0.1% of GDP in 2012.

The widening of the central government deficit is due to both mounting current expenditure and a slowdown in tax revenues. Current expenditure expanded by 10.6% in 2012, against 8.9% in 2011, with continued growth in components such as public-sector transfers (19.4%) and wages (8.8%), although the latter rose by less than in 2011 (12.2%). Notable expenditure on current transfers included resources for

social programmes such as *Avanceamos*, run by the Fund for Social Development and Family Allowances (FODESAF), and commitments made to public universities through the Special Fund for State Higher Education (FEES). Slower wage bill growth is the result of presidential directive 13-H, which froze the creation of new jobs in the public sector, and a lower salary increase for public employees. Capital expenditure posted 9.1% growth on the back of higher spending on education infrastructure and repairs to the road network, among other areas.

Tax revenues increased by 8.7%, after a rise of 11.1% the previous year. This trend reflects both slower growth in indirect tax revenues (7.4% in 2012 against 12.6% in 2011) and stagnant revenues from taxes on imports. This trend was partly offset by an increase in direct tax revenues (11.1% in 2012 compared with 8.4% in 2011).

Total gross public debt stood at 51.1% of GDP at December 2012, a 6.5-percentage-point rise on the previous year, prompted by the widening of the fiscal deficit in 2012 which required more funding from the central government and greater monetary absorption by the central bank. The central government funded around 70% of this increase (4.5 percentage points of GDP) by stepping up bond placements on both the domestic and international markets. The central bank contributed public debt equivalent to one additional percentage point of GDP. In 2012, domestic public debt reached 38.8% of GDP, a 4.8-percentage-point increase over the previous year; external public debt totalled 12.3% in 2012, a rise of 1.7 percentage points compared with 2011.

In the first quarter of 2013, the narrowly defined global public sector ran a deficit equivalent to 1.7% of GDP, rising by 0.1 percentage points on the same period the previous year. This trend is the result of 8.7% growth in total revenues in the first quarter of 2013 compared with the first quarter of 2012, while total expenditure jumped by 10.4%.

Projections for 2013 are for continued pressure on the fiscal accounts, given the difficulty in further reining in fiscal expenditure and the absence of a comprehensive tax reform that would boost revenues.

(b) Monetary and exchange-rate policies

In 2012, the central bank fulfilled its commitment to maintain the existing exchange-rate band parameters and to gradually transition towards a flexible exchange rate regime. The central bank's currency board approved an international reserves accumulation programme for 1 February to 31 December 2012, with the aim of buying US\$ 1.50 billion.

The main monetary and credit aggregates showed no signs of aggregate demand pressures until August 2012. In this context, monetary indicators performed in keeping with the level of economic activity and inflation targets. However, the last four months of the year an unforeseen inflow of external resources resulting from the spread between dollar and colón interest rates, coinciding with a seasonal peak in foreign-currency generation, led to a situation of excess liquidity linked to foreign-exchange purchases by the central bank. This increased the pressure on the colón and led the central bank to intervene more frequently and rigorously to protect the floor of the exchange-rate band, mostly in the last four months of the year. Dollar purchases in 2012 therefore totalled US\$ 1.369 billion, of which 82.6% was executed in the closing four months of the year.

September 2012 saw the enactment of Law No. 9070, which authorizes the Ministry of Finance to issue up to US\$ 4.0 billion (US\$ 1.0 billion annually) in securities on the international market over the next 10 years, with the aim of converting domestic bonded debt into external debt or repaying external

debt. The Ministry of Finance placed the first US\$ 1.0 billion in November 2012 and another US\$ 1.0 billion in April 2013. The latter included US\$ 500 million at a fixed rate of 4.5% maturing in 12 years, and the remaining US\$ 500 million at a fixed rate of 5.75% maturing in 30 years.

Domestic credit grew by 5.2% in nominal terms in 2012, compared with 12.8% the previous year. This trend mainly reflects a sharp 46.6% fall in lending to the public sector (having soared by 37.1% in 2011), as a result of the 2012 bond issue by the Ministry of Finance. Private-sector lending grew by 13% in 2012, slightly slower than in 2011 (13.2%). However, lending patterns differed significantly depending on the currency. Loans denominated in foreign currency swelled by 17.8% in 2012, while colón-denominated ones did so by 11.4%. This was due to the interest-rate spread and the fact that the exchange rate was very close to the floor of the band for much of the year. As a result, dollar loans accounted for 79% of the total credit portfolio of private banks, while for State-owned banks and non-bank depositary corporations the figure was 30.5% and 9.0%, respectively.

The substantial rise in dollar lending and the implicit exchange-rate risk in lending to borrowers with income sources denominated in the local currency, together with the difficulties in neutralizing excess liquidity using conventional monetary policy instruments, led the central bank to adopt a series of measures to curb the excessive growth in credit, especially in foreign currency.

On 30 January 2013, the board of directors of the central bank set an overall limit of 9% on the cumulative growth, between 1 February and 31 October 2013, of the outstanding portfolio of loans to and investments in the non-financial private sector by financial intermediaries subject to oversight by the General Financial Institute Audit Bureau. The overall limit for foreign currency was set at 6% of cumulative growth over the same period. In the first quarter of 2013, growth in private-sector credit slowed sharply as a result of the central bank board resolution to this effect. Total lending grew by 1.3% in this period (1% in local currency and 1.7% in foreign currency). The board of the central bank also submitted a bill to the Legislative Assembly containing measures to discourage external capital inflows.

The monetary policy rate remained at 5%, since inflation indicators, the output gap and inflation expectations were all in line with the inflation target range set by the central bank.

In 2012, the monetary base grew faster than nominal GDP (16.9% compared with 11.6% in 2011), mainly as a result of the central bank's dollar purchases and, to a lesser degree, its net interest payments on government bonds denominated in colones. This monetary expansion was partially offset by a net placement of monetary stabilization bonds, an increase in the balance of electronic term deposits, and other central bank operations.

The central bank's international reserves rose by US\$ 2.1 billion to US\$ 6.857 billion at December 2012, which equates to 1.8 times the monetary base and to more than six months of imports.

(c) Trade policy

Trade policy continued to be aimed at creating the conditions to facilitate export diversification, while at the same time consolidating, broadening and rationalizing the foreign trade platform. In terms of Central American economic integration, in May 2013, when it first came up for debate, the Legislative Assembly approved the association agreement between Central America and the European Union aimed at facilitating and consolidating Costa Rica's access to the European market. The third negotiating round for a free trade agreement between Central America and the European Free Trade Association (EFTA)

commenced in August 2012. This group of European countries consists of Iceland, Liechtenstein, Norway and Switzerland; the Central American participants are Costa Rica, Guatemala, Honduras and Panama.

June 2012 saw the launch of negotiations on a free trade agreement between Costa Rica and Colombia, with the aim of strengthening trade and investment relations between the two countries. The agreement with Peru is awaiting legislative approval.

3. The main variables

(a) The external sector

The current account posted a deficit of 5.2% of GDP in 2012, trimming 0.2 percentage points from the 2011 figure. This change is attributable to a 0.8-percentage-point narrowing of the goods balance deficit (11.8% of GDP in 2012 against 12.6% in 2011), largely offset by the income account deficit, which rose by 0.6 percentage points (2.0% of GDP in 2012 against 1.4% in 2011), reflecting a US\$ 266 million increase in interest, profits and dividends paid. Surpluses in both the services account (7.8% of GDP) and the transfers account (0.7% of GDP) followed trends similar to 2011.

The goods balance deficit was driven down by a significant weakening of import growth, from 19.5% in nominal terms in 2011 to 8.4% in 2012. There was a marked deceleration in imports of both consumer goods (12.8%, against 19.7% in 2011) and capital goods (11.6%, against 18.9% in 2011). Imports of intermediate goods saw the most drastic change, plummeting 20.0% in 2012 after climbing 19.7% in 2011. Exports grew by 10.0% in nominal terms, slightly down on the 2011 figure (10.2%), fuelled by sales of goods manufactured under special regimes (12.4%), particularly electronic microcomponents, microprocessors and medical devices. Sales of IT services stood out, delivering 18.2% growth.

The current account deficit was financed by a hefty increase in debt securities, which totalled US\$ 1,920 billion in 2012 (4.3% of GDP). This increase is the result of the aforementioned US\$ 1 billion bond issue carried out by Ministry of Finance, and higher external borrowing by the banking sector. Foreign direct investment (FDI) amounted to US\$ 2.265 billion in 2012 (5.0% of GDP) and also helped to fund the current account deficit. The main FDI destination sectors were services (40.2%), manufacturing (25.4%) and real estate (19.1%).

International reserves added US\$ 2.110 billion in 2012 and closed the year with a balance of US\$ 6.857 billion, equivalent to more than six months of imports and to 1.8 times the monetary base.

In the first quarter of 2013, Costa Rica's trade deficit was US\$ 1.303 billion, down US\$ 128 million on the deficit posted in the first quarter of 2012. This trend is basically due to rising exports of products made by companies operating under special trade regimes, particularly electronic components and microprocessors.

(b) Economic growth

The 5.1% growth posted in 2012, which overshot expectations, was mainly driven by an 8.5% increase in external demand. However, the Costa Rican economy performed inconsistently over the course of 2012: growth was 6.2% in the first semester and 3.7% in the second.

In 2012, growth was led by manufactured goods (6.3%), business services (9.6%), transport, storage and communications (5.9%) and construction (5.7%). Strong performance in the manufacturing sector reflects increased activity by companies operating under special regimes, especially those involved in the production of electronic microcomponents and medical equipment parts. However, like the national economy, this sector also showed major variations over the year, with 10.5% growth in the first semester falling to just 1.8% in the second. Growth in the business-services sector was spurred by increased call-centre, cost-centre and software exports. The transport, storage and telecommunications sector expanded on the back of greater demand for mobile telephony and Internet services, cargo transport and tourism-related activities. Lastly, the rebound in construction, after a three-year downturn in activity, was fuelled by growth in commercial and residential private construction, and, to a lesser extent, by public building projects.

In the first quarter of 2013, the monthly index of economic activity, trend-cycle adjusted, posted year-on-year variation of 3.9%, down from 7.2% in 2012. This slowdown was primarily the result of lower growth in the production of goods for export, as well as falling domestic demand in various sectors, namely manufacturing, transport, agriculture and storage and communications.

(c) Inflation, wages and employment

Headline inflation, measured by variation in the consumer price index (CPI), was 4.6% at December 2012 (4.7% at December 2011), within the target range set by the central bank for the year (5.0% \pm 1 percentage point). Alcoholic beverages and cigarettes, rent and housing services and education all saw prices rising faster than the CPI. In the alcoholic beverages and cigarettes category, prices soared by 48.6% following the entry into force of the General Law for the Control of Tobacco and its Harmful Effects on Health, in March 2012. Despite this sharp increase, these products accounted for only 5.3% of total variation in the CPI, given their low weighting in the basket of goods and services. The other three categories accounted for 63.5% of cumulative variation in the CPI. This can be explained by price adjustments for regulated services, water (64.1%) and electricity (7.8%). The price of basic and higher education rose by 9.7% and 8.2% respectively.

The open unemployment rate remained virtually unchanged, edging up from 7.7% in 2011 to 7.8% in 2012 as a result of falls of equal magnitude in the participation and employment rates.

Table 1
COSTA RICA: MAIN ECONOMIC INDICATORS

	2004	2005	2006	2007	2008	2009	2010	2011	2012 a/
	Annual growth rates b/								
Gross domestic product	4.3	5.9	8.8	7.9	2.7	-1.0	5.0	4.4	5.1
Per capita gross domestic product	2.4	4.1	7.0	6.2	1.2	-2.5	3.5	3.0	3.7
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	0.7	4.3	12.7	5.6	-3.2	-2.8	6.7	1.1	3.5
Mining and quarrying	7.7	7.6	25.7	-1.5	-5.6	-14.2	-7.1	-3.2	5.3
Manufacturing	4.0	10.8	10.8	7.0	-3.7	-3.9	4.0	4.2	6.3
Electricity, gas and water	4.0	5.9	6.1	2.3	-0.6	3.3	2.7	2.8	3.8
Construction	6.3	-0.2	18.2	21.3	14.6	-3.0	-4.1	-3.8	5.7
Wholesale and retail commerce, restaurants and hotels	3.9	4.0	4.8	6.6	3.4	-6.0	4.2	4.2	4.2
Transport, storage and communications	12.0	9.6	10.5	9.8	7.6	3.0	6.9	7.7	5.9
Financial institutions, insurance, real estate and business services	6.6	5.4	11.1	9.3	8.5	5.6	6.5	7.0	7.2
Community, social and personal services	1.4	3.3	2.3	3.4	4.5	5.2	4.2	2.4	2.2
Gross domestic product, by type of expenditure									
Final consumption expenditure	2.9	3.9	5.4	6.9	3.5	2.3	4.5	4.0	4.2
Government consumption	1.3	0.2	2.9	2.3	4.4	6.7	4.7	1.5	1.7
Private consumption	3.1	4.4	5.7	7.5	3.4	1.7	4.5	4.3	4.5
Gross capital formation	10.9	11.3	13.9	-1.2	20.2	-34.7	33.4	13.0	4.8
Exports (goods and services)	8.2	12.8	10.3	9.9	-2.0	-6.0	5.5	6.1	8.5
Imports (goods and services)	9.1	12.4	8.1	4.3	6.5	-18.9	16.5	9.5	7.0
Investment and saving c/	Percentajes of GDP								
Gross capital formation	23.1	24.3	26.4	24.7	27.6	16.3	20.6	21.6	21.2
National saving	18.9	19.4	21.9	18.4	18.2	14.3	17.1	16.2	16.0
External saving	4.3	4.9	4.5	6.3	9.3	2.0	3.5	5.4	5.2
Balance of payments	Millions of dollars								
Current account balance	-791	-981	-1 023	-1 646	-2 787	-576	-1 281	-2 203	-2 341
Goods balance	-1 421	-2 159	-2 727	-2 985	-5 013	-2 039	-3 440	-5 151	-5 309
Exports, f.o.b.	6 370	7 099	8 102	9 299	9 555	8 838	9 516	10 383	11 442
Imports, f.o.b.	7 791	9 258	10 829	12 285	14 569	10 877	12 956	15 534	16 752
Services trade balance	857	1 116	1 351	1 734	2 201	2 188	2 537	3 193	3 525
Income balance	-440	-209	4	-865	-417	-1 084	-745	-567	-886
Net current transfers	212	270	349	470	442	359	366	323	329
Capital and financial balance d/	872	1 374	2 053	2 794	2 439	836	1 842	2 335	4 451
Net foreign direct investment	733	904	1 371	1 634	2 072	1 339	1 441	2 098	1 839
Other capital movements	139	470	682	1 160	367	-503	401	237	2 612
Overall balance	80	393	1 031	1 148	-348	260	561	132	2 110
Variation in reserve assets e/	-80	-393	-1 031	-1 148	348	-260	-561	-132	-2 110
Other external-sector indicators									
Real effective exchange rate (index: 2005=100) f/	99.4	100.0	99.6	97.4	93.9	92.8	82.4	79.4	76.5
Terms of trade for goods (index: 2005=100)	104.0	100.0	97.1	96.1	92.5	95.6	91.8	88.4	87.9
Net resource transfer (millions of dollars)	432	1 166	2 058	1 929	2 022	-247	1 097	1 768	3 565
Total gross external debt (millions of dollars)	5 766	6 763	7 191	8 444	9 105	8 238	9 189	10 714	14 473
Employment g/	Average annual rates								
Labour force participation rate	54.4	56.8	56.6	57.0	56.7	60.4	59.1	60.7	60.1
Open unemployment rate	6.7	6.9	6.0	4.8	4.8	8.5	7.1	7.7	7.8
Visible underemployment rate	14.4	14.6	13.5	11.5	10.5	13.5	11.2	13.4	13.8

Table 1 (concluded)

	2004	2005	2006	2007	2008	2009	2010	2011	2012 a/
Prices	Annual percentages								
Variation in consumer prices (December-December)	13.1	14.1	9.4	10.8	13.9	4.0	5.8	4.7	4.5
Variation in industrial producer prices (December-December)	17.7	12.1	13.7	14.6	23.5	-1.2	4.5	7.4	3.5
Variation in nominal exchange rate (annual average)	10.0	9.1	7.0	1.0	1.9	8.9	-8.3	-3.8	-0.5
Variation in average real wage	-2.6	-1.9	1.6	1.4	-2.0	7.7	2.1	5.7	1.3
Nominal deposit rate h/	11.5	12.1	11.4	7.1	5.4	8.6	6.1	5.3	6.5
Nominal lending rate i/	23.4	24.0	22.7	17.3	16.7	21.6	19.8	18.1	19.5
Central government	Percentajes of GDP								
Total revenue	13.6	13.9	14.2	15.5	15.9	14.0	14.3	14.6	14.4
Tax revenue	13.3	13.6	14.0	15.2	15.6	13.8	13.3	13.7	13.6
Total expenditure	16.3	16.0	15.3	14.9	15.7	17.4	19.5	18.7	18.8
Current expenditure	15.2	14.9	14.3	13.6	13.5	15.6	17.2	17.2	17.4
Interest	4.1	4.1	3.8	3.1	2.2	2.1	2.1	2.2	2.1
Capital expenditure	1.1	1.1	0.9	1.3	2.2	1.8	2.4	1.5	1.5
Primary balance	1.4	2.0	2.7	3.7	2.4	-1.3	-3.1	-1.9	-2.3
Overall balance	-2.7	-2.1	-1.1	0.6	0.2	-3.4	-5.2	-4.1	-4.4
Central government public debt	41.0	37.5	33.3	27.6	24.9	27.4	29.2	30.8	35.3
Domestic	27.5	25.1	22.9	19.2	17.6	21.6	23.2	25.9	29.2
External	13.5	12.3	10.4	8.3	7.3	5.8	6.0	5.0	6.1
Money and credit	Percentages of GDP, end-of-year stocks								
Domestic credit	44.7	43.3	42.9	44.5	47.8	48.5	45.3	48.0	46.9
To the public sector	9.7	7.4	5.1	2.7	2.6	3.9	3.7	4.5	2.8
To the private sector	32.0	35.6	37.9	44.3	50.5	49.2	45.3	47.4	49.2
Others	2.9	0.3	0.0	-2.4	-5.2	-4.6	-3.6	-3.9	-5.1
Monetary base	5.9	6.4	6.7	7.6	7.3	7.2	7.0	7.2	7.7
Money (M1)	48.7	53.1	54.0	55.1	56.0	56.4	50.2	49.6	50.2
M2	26.6	30.2	32.5	36.5	34.5	33.4	32.2	32.1	34.0
Foreign-currency deposits	22.2	22.9	21.5	18.7	21.6	23.1	18.0	17.5	16.2

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 1991 prices.

c/ Based on values calculated in national currency and expressed in current dollars.

d/ Includes errors and omissions.

e/ A minus sign (-) indicates an increase in reserve assets.

f/ Annual average, weighted by the value of goods exports and imports.

g/ Nationwide total. New measurements have been used since 2009; the data are not comparable with the previous series.

h/ Average local-currency deposit rate in the financial system.

i/ Average system lending rate in local currency.

Table 2
COSTA RICA: MAIN QUARTERLY INDICATORS

	2011				2012				2013	
	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2 a/
Gross domestic product (variation from same quarter of preceding year) b/	2.9	4.3	5.0	5.6	7.7	5.7	3.8	3.4	1.2	...
Goods exports, f.o.b. (millions of dollars)	2 508	2 728	2 565	2 608	2 944	2 992	2 731	2 791	2 875	1 996 c/
Goods imports, c.i.f. (millions of dollars)	3 859	3 883	4 230	4 248	4 380	4 244	4 324	4 630	4 375	3 040 c/
Gross international reserves (millions of dollars)	4 642	4 843	4 763	4 756	4 745	4 870	5 140	6 857	6 937	7 885 c/
Real effective exchange rate (index: 2005=100) d/	78.8	80.0	80.0	78.9	78.7	76.5	75.6	75.3	74.1	73.2 c/
Consumer prices (12-month percentage variation)	4.6	5.2	5.2	4.7	4.2	4.6	4.5	4.5	6.2	5.3 c/
Wholesale prices (12-month percentage variation)	7.5	9.2	9.5	7.4	4.2	2.8	4.0	3.5	3.6	3.1 c/
Average nominal exchange rate (colones per dollar)	503	503	507	510	510	504	499	499	501	500
Nominal interest rates (annualized percentages)										
Deposit rate e/	5.5	5.4	5.1	5.2	6.0	6.5	6.8	6.7	5.8	5.1 c/
Lending rate f/	18.7	17.9	17.8	17.8	18.4	19.4	20.1	20.8	19.6	17.7 c/
Interbank rate	4.6	4.9	5.1	4.7	4.6	5.2	5.2	4.7	4.8	4.8
Monetary policy rates	6.5	6.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
International bond issues (millions of dollars)	-	-	-	250	-	250	-	1 000	-	1 500 c/
Stock price index (national index to end of period, 31 December 2005 = 100)	117	134	132	121	123	123	127	129	154	172
Domestic credit (variation from same quarter of preceding year)	9.7	9.9	13.8	16.2	13.4	13.4	12.7	7.6	8.4	...
Non-performing loans as a percentage of total credit	1.9	2.1	2.1	1.8	1.9	1.9	1.8	1.8	1.8	2.1 c/

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 1991 prices.

c/ Figures as of May.

d/ Quarterly average, weighted by the value of goods exports and imports.

e/ Average local-currency deposit rate in the financial system.

f/ Average system lending rate in local currency.