Costa Rica

ECLAC estimates growth of 4.2% for the Costa Rican economy in 2016, compared to 3.7% in 2015, thanks to a recovery in agricultural and manufacturing activity after the exceptional factors acting as a drag on these sectors in 2015 eased this year, in addition to continued growth in the services sector. The consumer price index will close the year below 1% (-0.8% in 2015), still affected by the lower international fuel prices. The central government deficit will come in at between 5.2% and 5.5%, down from 5.8% in 2015, thereby breaking the upward trend of recent years. The current account deficit as a percentage of GDP narrowed for the second year running (4.2%, compared to 4.4% in 2015), on the back of a fresh gain in the terms of trade. The average national unemployment rate was 9.5%, similar to that of 2015 (9.6%).

The fiscal deficit remains the focus of economic policy debate. In 2016, the first fiscal reform bills were adopted, paving the way for cuts in public pension spending and improved State treasury management. Bills are still pending on revenue matters, particularly those to introduce a new value added tax and to reform income tax.

In the first 10 months of the year, central government total revenue was up by 9.1% in real terms, compared to the same period in 2015. Receipts from income and profit taxes were up (14.7%), thanks to administrative and technological measures implemented by the Ministry of Finance as well as to economic growth. Total central government spending rose year-on-year by 3.8% in January-October, less than in the prior-year period (9.5%). Falling interest rates in the domestic market and low inflation reduced debt-service pressure and inflation-indexed current expenditures (the latter were up year-on-year by 5.7%, compared to 8.2% in the same period in 2015). Reflecting the completion of public infrastructure work in 2015 and a gradual start to new projects in 2016, capital expenditure shrank by 19.8%.

The central government fiscal deficit was 3.4% of GDP at the end of the first three quarters of 2016 (4.2% for the prior-year period). Central government public debt stood at 43.1% of GDP, 2.6 percentage points higher than at year-end 2015. Government financing has been drawn largely from the domestic market, mainly from institutional public sector clients.

The central bank lowered the target inflation range by 1 percentage point for 2016, to 3%, with a margin of 1 percentage point on either side. This adjustment is in line with Costa Rica’s target of gradually lowering inflation over the long term, in order to converge with that of its main trade partners. After the large (350 basis points) cut in the monetary policy interest rate in 2015, in 2016 it remained unchanged at 1.75%. The transmission of these cuts to the rest of the financial system has remained gradual, however: the average lending rate fell from 15.63% at the end of January to 14.48% in November 2016, while the average gross deposit rate came down from 3.58% in January to 3.45% in November.
In September, lending to the private sector was up by a nominal 12.6% year-on-year, 1.7 percentage points more than in the same month in 2015. The percentage of foreign currency loans in the total lending portfolio continued to rise, coming to 42.0%, compared to 41.5% in September 2015.

The colon’s cumulative nominal depreciation against the dollar was 3.1% in the first nine months of the year; the real effective exchange rate index decreased by 3.7% in the same period. Under the managed float system, the central bank’s international reserves totalled US$ 7.681 billion in October, US$ 153 million less than at the close of 2015.

Negotiations on a free trade agreement between Central America and the Republic of Korea concluded in November. As regards joining the Organization for Economic Cooperation and Development (OECD), the 22 technical reviews of the accession process continued in 2016.

Goods exported showed cumulative year-on-year growth of 7.1% in the first 10 months of the year (0.7% in the same period in 2015), on the back of recovery in manufacturing and agricultural exports. On the import side, goods expanded 0.3% in the same period, compared with a 3.8% drop in 2015. Fuel imports fell (by 14.7%), but were offset by increased commodity and consumer goods inflows. Services exports continued to expand strongly, up by 12.4% year-on-year in the first half of 2016, driven by robust growth in income from tourism.

Terms of trade improved in 2016 (2.2%), chiefly as a result of the lower average fuel price. In the first half of the year, net foreign direct investment (FDI) was US$ 1.324 billion, 4.6% below the total for the first half of the previous year, owing mainly to one-off investments made in the agricultural sector in 2015.

The Costa Rican economy posted year-on-year growth of 4.3% in the first half of 2016, but this is expected to slow slightly in the second half, as external demand slackens. Services growth was driven by finance and insurance (up 12.3% year-on-year), as well as business services (8.4%), while in the manufacturing sector, which grew by 4.4%, the strongest expansion occurred in medical equipment and devices. Conversely, construction was down by 6%, as a result of the aforementioned drop in infrastructure spending. On the spending side, external demand grew strongly (9.7%), as did private consumption (4.6%), the latter driven by climbing disposable income (rising real wages, low inflation and lower fuel prices) and credit expansion.

The interannual year-on-year variation in the consumer price index returned to positive territory in July, after 12 months of negative figures. In October, it posted a year-on-year rate of 0.55%, still affected by lower international fuel prices.
In the first three quarters of 2016, the average national unemployment rate stood at 9.5%, while the average monthly wage showed a nominal increase of 3.3% year-on-year in the same period (3.9% in real terms).

ECLAC estimates real GDP expansion of 3.9% in 2017, slightly lower than in 2016, amid slacker external demand and highly uncertain international conditions. Inflation is expected to return to the central bank’s target range, at around 3%, which will result in a higher current account deficit. Should the remaining fiscal reform bills fail to prosper in the legislature, the deficit will expand again, owing to higher inflation and interest rates.