Costa Rica

The Costa Rican economy is expected to grow at a rate of 3.8% in 2011, against 4.2% in 2010. This slowdown is attributable chiefly to slackening external demand and falling agricultural output owing to adverse weather events. Inflation in December will be about 5%, which is within the central bank's target range (5% with a margin of 1 percentage point on either side). The current account deficit will widen to 5% of GDP (2010: 3.6%) because of a steep rise in imports and a loss of momentum in exports. The central government deficit will close the year equivalent to about 5% of GDP (as against 5.2% in 2010) and with a fiscal reform package yet to be approved. The urban open unemployment rate edged up from 7.1% in 2010 to 7.7% in 2011.

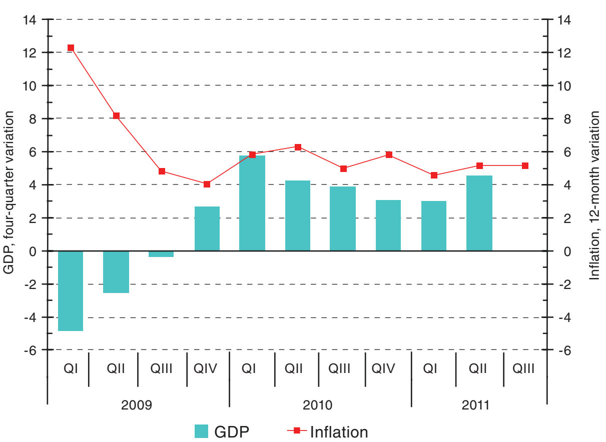
In October 2011, the executive branch presented a new fiscal reform proposal, replacing the one submitted in late 2010 that was rejected by the Legislative Assembly in the first half of 2011. The new proposal continues to focus on modifying income and sales taxes, in particular, by generalizing the sales tax on goods and services and converting it into a value added tax. If adopted, the reform would bring in additional annual resources for the central government equivalent to about 2.1% of GDP.

In 2011, total central government spending grew at a rate similar to that of revenues (9.2% and 9.1% in real terms, respectively, in the first nine months of the year) but significantly slower than the 24% posted in the same period in 2010, as a result of measures to curb spending. The deficit was financed primarily by issuing domestic debt. In September, total public debt stood at 43% of GDP, 1.9 percentage points higher than for the same month in 2010.

In 2011, the central bank continued to pursue a gradual transition towards a flexible exchange rate and an inflation-targeting regime. The exchange market was relatively stable compared with the two previous years. In the first four months of the year, the exchange rate stayed close to or at the floor of the band (500 colones to the dollar); it started to pull up in May and since then has hovered around 510 colones to the dollar. The real effective exchange rate appreciated by 2.8% in the first 10 months of 2011. Between January and April, the central bank intervened in the exchange market to protect the floor of the band, thus accumulating US$ 370 million in international reserves. In the months that followed, reserves declined slightly to total US$ 4.733 billion at the end of October, in comparison with US$ 4.627 billion at the end of 2010.

The monetary policy rate was lowered by 150 basis points in June, resulting in an annual rate of 5%, as pressure on prices eased. The real base deposit rate was 2.9% in October, while the real average lending rate of the financial system was 15%. Credit to the private sector rebounded significantly, with year-on-year nominal growth of 13.1% in the first 10 months of the year. Lower rates on foreign currency and relative exchange-rate stability have contributed to a shift from deposits in dollars to deposits in colones.

COSTA RICA: GDP AND INFLATION



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

In September, a reserve requirement was introduced on short-term external borrowing in foreign currency, for macroprudential purposes.

In terms of trade policy, the association agreement with the European Union that was signed in May 2010 is currently going through the European Union ratification process. Once it has been ratified, it will be sent to the Legislative Assembly of Costa Rica for adoption. The government continued its efforts to diversify the country's trade relations: in May it signed a bilateral trade agreement with Peru, and in August an agreement with China entered into force. In November, a single free trade agreement was signed between Mexico and Central America to converge existing separate bilateral agreements.

In 2011 total consumption grew at pace similar to 2010 as private consumption picked up slightly and public consumption slowed. Gross fixed investment expanded at a higher rate than in 2010, driven by the recovery of the construction industry. The monthly index of economic activity reflected slower growth in the first three quarters of 2011, with an annual average growth rate of 3.8% versus 5.7% in the same period in 2010. Agricultural production plummeted owing to adverse weather events, while manufacturing slumped as a result of sagging external demand. By contrast, services performed robustly, particularly the communications, transport, and other business services sectors. Construction expanded after contracting for two years.

Year-on-year growth in the consumer price index in November stood at 4.6%. The absence of domestic demand pressures and the stability of the exchange rate have contributed to this price pattern, while higher international commodity and fuel prices have not generated extraordinary pressures. National household survey findings show an increase in the open unemployment rate, even though the country's solid economic performance led to a rise in the employment rate from 54.8% in 2010 to 56.0% in 2011.

The wider current account deficit is attributable above all to the burgeoning merchandise trade deficit. Exports saw moderate 7.2% growth in the first nine months; imports surged by 19.4% in the same period as domestic demand revived and international commodity prices climbed. Services exports rose by 16.5% in the first half of the year, driven in particular by business services, thus continuing to mitigate the merchandise trade deficit. Revenues from remittances and tourism went up slightly.

COSTA RICA: MAIN ECONOMIC INDICATORS

	2009	2010	2011 [a]
	Annual growth rates		
Gross domestic product	-1.3	4.2	3.8
Per capita gross domestic product	-2.6	2.8	2.4
Consumer prices	4.0	5.8	4.6 [b]
Real average wage [c]	7.7	2.1	4.5 [d]
Money (M1)	-0.2	20.9	6.6 [b]
Real effective exchange rate [e]	-0.4	-10.8	-3.3 [f]
Terms of trade	3.3	-3.9	-3.7
	Annual average percentages		
Urban unemployment rate	8.5	7.1	7.7
Central government overall balance / GDP	-3.4	-5.2	-5.0
Nominal deposit rate [g]	8.6	6.1	5.3 [h]
Nominal lending rate [i]	21.6	19.4	17.6 [h]
	Millions of dollars		
Exports of goods and services	12 499	13 812	15 092
Imports of goods and services	12 350	14 725	17 090
Current account balance	-576	-1 291	-2 521
Capital and financial balance [j]	836	1 852	2 627
Overall balance	260	561	106

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Preliminary estimates.
[b] Twelve-month variation to November 2011.
[c] Average wages declared by workers covered by social security.
[d] Estimate based on data from January to October.
[e] A negative rate indicates an appreciation of the currency in real terms.
[f] January to October average, year-on-year variation.
[g] Average deposit rate in the financial system.
[h] January-November average.
[i] Average lending rate in the financial system.
[j] Includes errors and omissions.

Foreign direct investment totalled US$ 2.2 billion at the end of the year —50% higher than the figure for 2010. Manufacturing and telecommunications services account for the bulk of these inflows; both sectors have been spurred by opening up to foreign investment.

ECLAC forecasts that Costa Rica will see economic activity grow at the rate of 3.5% in 2012. This moderate expansion is likely to be associated with sluggish external demand in an international environment clouded by the economic woes of Europe and the United States. With the fiscal reform approved, the central government deficit should be around 3.5% of GDP next year. However, the chances of meeting the central bank's inflation target of 4%, with a margin of 1 percentage point on either side, could be jeopardized by the effects of the fiscal reform. The current account deficit will once again widen in 2012, edging over 5% of GDP.