INTERNATIONAL MONETARY FUND

IMF Country Report No. 13/79

COSTA RICA

2012 ARTICLE IV CONSULTATION

March 2013

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2012 Article IV consultation with Costa Rica, the following documents have been released and are included in this package:

- **Staff Report** for the 2012 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on December 11, 2012, with the officials of Costa Rica on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on February 5, 2013. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF..
- **Informational Annex** dated February 5, 2013
- **Staff Statement** of February 22, 2013
- **Public Information Notice** (PIN) summarizing the views of the Executive Board as expressed during its February 22, 2013 discussion of the staff report that concluded the Article IV consultation.
- **Statement by the Executive Director** for Costa Rica.

The document listed below has been or will be separately released.

Selected Issues Paper

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

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INTERNATIONAL MONETARY FUND

COSTA RICA

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION

February 5, 2013

KEY ISSUES

Context. The economy recovered quickly from the global crisis of 2008-09, with low inflation, and healthy growth is expected to continue. However, risks to the outlook are tilted to the downside. Absent consolidation, large fiscal deficits would make public debt dynamics unsustainable in the long-run. Moreover, current policies could result in overheating, a risk that has been heightened by surging capital inflows.

The short-term policy mix should be adjusted. A tighter fiscal stance would mitigate risks of rising inflation and external imbalances. The authorities should also stand ready to increase interest rates and allow greater exchange rate flexibility if signs of inflationary pressure emerge. In the absence of fiscal adjustment, bolder monetary policy action may be required to ensure price stability.

Steady fiscal consolidation is required over the medium term. The threat of unsustainable public debt dynamics calls for corrective action. The authorities' intention to renew tax reform efforts and implement other fiscal consolidation measures is a welcome first step. A moderately front-loaded adjustment would strike the appropriate balance between achieving fiscal sustainability and maintaining robust growth. Postponing fiscal consolidation further could endanger macroeconomic stability.

It is important to strengthen the monetary policy framework, by increasing exchange rate flexibility and completing the transition to inflation targeting. This would permit consolidating gains in lowering inflation made in recent years.

Further improvements in financial system regulation and supervision as well as structural reforms to stimulate potential growth are desirable. Deepening consolidated and risk-based supervision as well as gradually adopting Basel III capital and liquidity standards would further buttress financial system soundness. Efficiency-enhancing measures to fuel competition and eliminate red-tape would help boost growth and bolster external competitiveness.

Approved By
Miguel Savastano (WHD)
and
Masato Miyazaki (SPR)

Discussions took place in San José during November 28-December 11. The mission comprised Lorenzo Figliuoli (Head), Pablo Morra, Yulia Ustyugova, M. Belén Sbrancia (all WHD), and Fernando Delgado (Regional Resident Representative). José Rojas and Luis Cosenza (OED) participated in the closing meeting.

BOXES

FIGURES

TABLES

OVERVIEW

1. **Costa Rica was resilient to the 2008-09 financial crisis and recovered quickly.** In response to the downturn, the authorities increased public expenditure and entered in a high-access precautionary Stand-By Arrangement with the Fund (that ended in mid-2010), while depreciation of the colón facilitated external adjustment. Macroeconomic and financial stability were maintained. After falling modestly in 2009, real GDP grew strongly in 2010-12, with low inflation. As global economic conditions improved, private capital inflows resumed and the nominal exchange rate returned to pre-crisis levels, reaching the floor of the exchange rate band by end-2010.

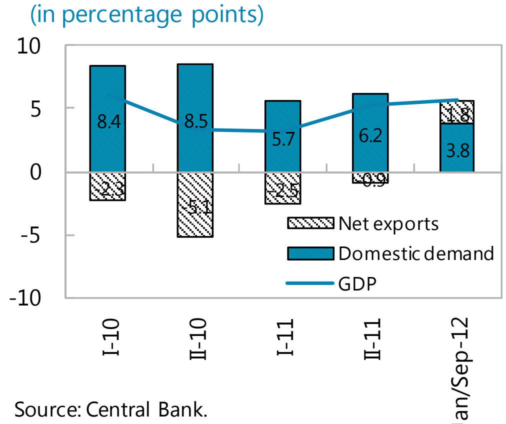
2. **However, the fiscal situation deteriorated markedly and attempts to correct it have encountered strong headwinds.** The budgetary stimulus imparted in 2009, mainly through a rise in wages and transfers, was not reversed when the economy improved and a new government took office. The increase in public expenditure combined with an endogenous fall in revenue (which was above trend in 2008) pushed the fiscal deficit above 5 percent of GDP by 2010—from near balance in 2008. While the authorities curbed expenditure growth in 2011-12, the budgetary position improved only moderately and public sector debt kept on climbing. A revenue-enhancing tax reform aimed at placing the public sector balance on a sustainable path was voided in 2012.

RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

A. Recent Developments

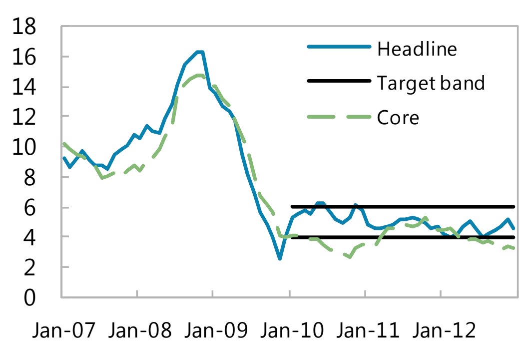
3. **Growth picked up in 2012, with inflation well within the policy limits.** Real GDP grew by about 5 percent in 2012 (up from an average of 4½ percent during 2010-11), buoyed by strong investment and exports, especially in manufacturing. As a result, the negative output gap that arose during the downturn is estimated to have almost closed. By year-end, headline inflation stood at 4.6 percent, comfortably within the 4-6 percent official target range, and core and producer price inflation were also subdued. At a historical low of 5.7 percent in December, twelve-month inflation expectations were anchored within the target range.

Real GDP growth and contributions to growth
(in percentage points)



Source: Central Bank.

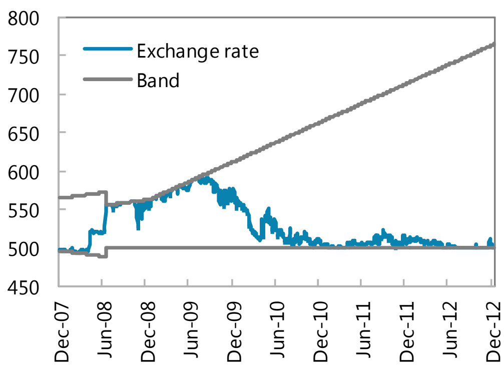
Headline and core inflation
(percent y/y)



Source: Central Bank.

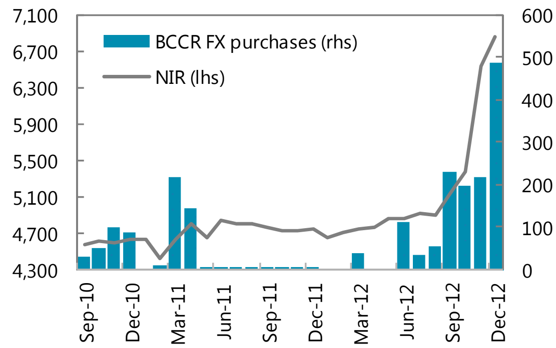
4. **A significant rise in capital inflows more than offset a modest increase in the external current account deficit and placed strong appreciating pressure on the colón.** Robust foreign direct investment (FDI), higher public and private external borrowing, and, since late August 2012, a rise in net portfolio inflows increased the financial and capital account surplus. The rise in private capital inflows kept the colón at the bottom of the exchange rate band, and prompted the central bank to step up its foreign exchange purchases. As a result, net international reserves (NIR) at end-2012 rose to US$6.9 billion, close to adequacy metrics (Box 1).

Exchange rate
(colones per US$)



Source: Central Bank.

Net international reserves and central bank foreign exchange purchases
(millions of US$)

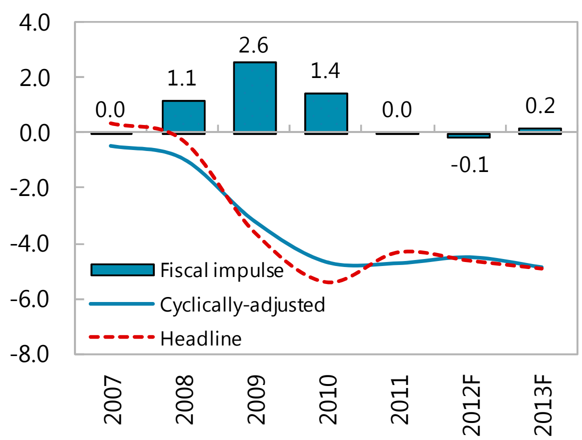


Source: Central Bank.

5. **Competitiveness has eroded and may not be adequate to ensure long-term external stability.** Since 2005, the real effective exchange rate (REER) has appreciated by over 30 percent, largely due to high inflation differentials. Multilaterally consistent estimates under the EBA and CGER approaches suggest that the current account deficit is above medium-term fundamentals-based levels (Box 1) and point to moderate REER overvaluation. Productivity-enhancing reforms (¶ 27) and wage restraint would help restore competitiveness. Fiscal consolidation (¶ 19) would also support long-term external stability.

6. **While public expenditure growth was contained, the fiscal deficit remained large and the public debt ratio kept rising.** During 2011-2012, the authorities slammed the brakes on the rapid swelling of public expenditure of 2008-10 by freezing public sector vacancies, containing wage growth, rationalizing outlays on goods and services, and postponing non-priority public investment projects. These efforts helped reduce the fiscal deficit to an estimated 4½ percent of GDP in 2011 and 2012, from a peak of 5½ percent of GDP in 2010. However, they did not prevent a

Headline Fiscal Balance, Cyclically-adjusted Balance and Fiscal Stimulus (percent of GDP)

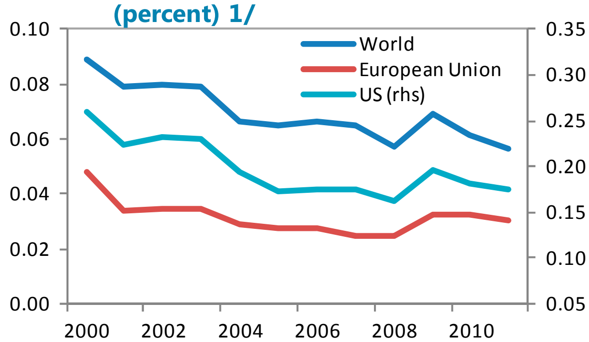


Source: IMF staff estimates.

Box 1. Costa Rica: External Stability Assessment

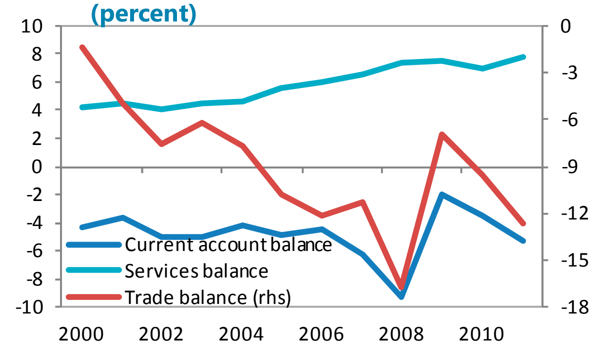
Costa Rica's share in global merchandise trade fell in the last decade, but the export-oriented services sector is growing rapidly. Costa Rica's share in total world trade has decreased mostly driven by a lower contribution of traditional exports. This decline and the significant widening observed in the merchandise trade deficit, however, were partly offset by a steady increase in the surplus of the real services balance.

Costa Rica: Export market shares (percent) 1/



Sources: International Financial Statistics and Fund staff calculations.
1/ Computed as Costa Rica's exports to the World, the EU and the US in percent of total World, EU and US imports from the World respectively.

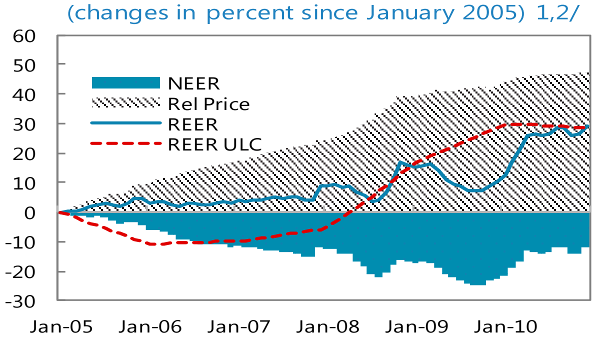
Costa Rica: External current account (percent)



Sources: Central Bank , Fund staff calculations

Survey-based indicators of competitiveness highlight some key challenges. Costa Rica's ranking in the 2012-2013 Global Competitiveness Index improved to the 57th position (out of 144 countries), from 61st in the previous survey. However, inadequate infrastructure and excessive government bureaucracy continue to weigh on the country's competitiveness. The country also stands low in the Doing Business Index, ranking in the 110th position out of 185 countries.

Costa Rica: Real effective exchange rate (changes in percent since January 2005) 1,2/



Source: National authorities and Fund staff calculations.
1/ Increase implies appreciation.
2/ The REER based on ULC was calculated with data for 73 percent of the trading partners.

The real effective exchange rate has appreciated significantly in recent years. Driven to a large extent by the inflation differential vis-à-vis trading partners, the real effective exchange rate (REER) has risen by more than 30 percent since 2005. Using unit labor costs, the REER measure rose by about the same magnitude, though at a much slower rate since 2009.

Multilaterally-consistent estimates suggest that Costa Rica's REER is moderately overvalued, and that a narrower current account deficit would be warranted over the medium term.

External balance assessment (EBA) estimates rely on econometric analysis to gauge the values of key indicators of external sustainability implied by fundamentals and desirable policies:

Box 1. Costa Rica: External Stability Assessment (concluded)

- The current account regression-based approach points to a sustainable cyclically-adjusted current account deficit of about 2.7 percent of GDP, which is 2 percentage points below the current cyclically-adjusted level. The gap reflects in part the effect of the large fiscal deficit and generous social protection policies that reduce the need for precautionary saving.
- Preliminary estimates under the REER regression-based approach point to an overvaluation of about 25 percent. This result, however, should be interpreted with caution. While it is driven in part by identifiable factors—notably, again, by the country's fiscal policies and high social spending— it is also characterized by a large regression residual.
- Under the external sustainability approach, the net foreign asset (NFA) position would stabilize at the benchmark level of 26 percent with a current account deficit of 1.9 percent. This suggests that the REER gap is about 23 percent. However, if alternative estimates for the NFA position are used,[1] the NFA-stabilizing current account deficit widens to 3.5 percent and the estimated REER overvaluation drops to 12 percent.

Methodologies developed by the IMF's *Consultative Group on Exchange Rate Issues (CGER)* also suggest that the real exchange rate is moderately overvalued: three different approaches produce a deviation from fundamentals-based values in the range of 7.9 to 14.6 percent.

Estimates of Competitiveness Using EBA Methodologies 1/
(Deviation from norms implied by fundamentals and desirable policies)

Methodology	
CA regression-based approach: CA gap (percent of GDP)	-2.0
CA regression-based approach: CA norm (percent of GDP)	-2.7
ES approach: CA gap (percent of GDP)	-3.6
ES approach: CA norm (percent of GDP)	-1.9
REER regression-based approach: REER gap (percent)	25.2

Source: IMF staff estimates
1/ EBA (External Balance Assessment). CA gaps: negative gap implies REER overvaluation.

Estimates of Competitiveness Using CGER Methodologies 1/
(REER deviation from levels implied by medium-term fundamentals)

Methodology	
Macroeconomic balance (MB) approach	7.9
ES approach	8.5
Equilibrium REER approach	14.6

Source: IMF staff estimates
1/ CGER (Consultative Group on Exchange Rate Issues). Plus indicates overvaluation. International Monetary Fund, 2008, "Exchange Rate Assessments: CGER Methodologies" (available at www.imf.org)

While Costa Rica's current account deficit appears elevated, its financing structure mitigates risks. The current account deficit is mostly financed by FDI inflows, which have hovered at about 5 percent of GDP per year since 2005. As a result, Costa Rica's net international investment position is negative, with more than 60 percent of the external liabilities are comprised of FDI liabilities. Such financing structure makes the external accounts less vulnerable to sudden changes in global financial conditions.

The level of net international reserves (NIR) is somewhat below the composite adequacy metric. According to staff's estimates, Costa Rica's NIR stand at about 95 percent of the reserve adequacy metric that captures countries' vulnerabilities based on their exports and asset-liability structure, as well as the risk of related outflows.[2]

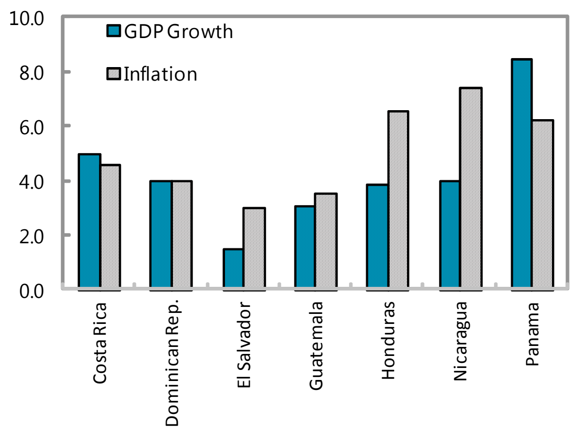
[1] Philip R. Lane and Gian Maria Milesi-Ferretti, 2006, "The External Wealth of Nations Mark II: Revised and Extended Estimates of Foreign Assets and Liabilities, 1970–2004", IMF Working Paper 06/69.

[2] See "Assessing reserve adequacy", 2011, Policy Paper, International Monetary Fund.

further rise in the public debt-to-GDP ratio, which is expected to have reached 38 percent of GDP at end-2012 (including external debt placed in late 2012 to pre-finance 2013 borrowing requirements, ¶ 7).

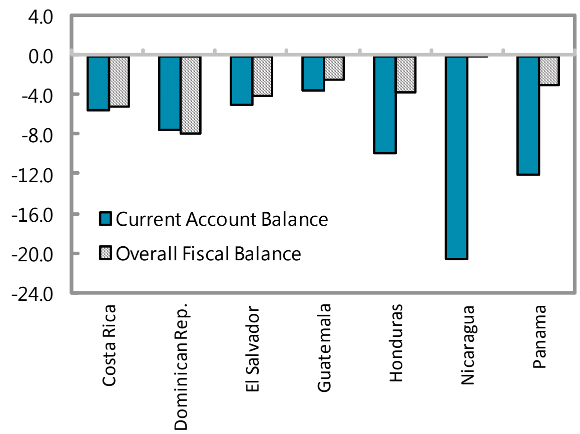
Costa Rica's GDP growth and fiscal deficit are higher than the CAPDR average, while inflation and the current account deficit are lower than the regional average

CAPDR: GDP growth and inflation (2012F)
(percent)



Source: National authorities.

CAPDR: Current account and fiscal deficit (2012F)
(percent of GDP)



Source: National authorities.

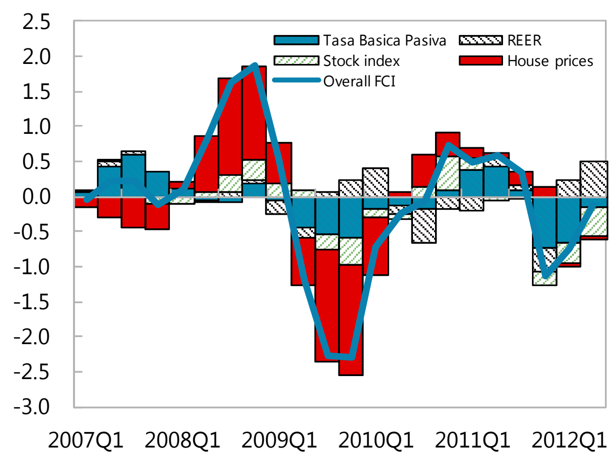
7. **The Supreme Court voided a revenue-enhancing tax reform.** As discussed in the staff report for the 2011 Article IV consultation, a tax reform aimed at increasing public revenues by 1½-2 percentage points of GDP (by broadening the tax base and turning the sales tax into a full-fledged value-added tax) was the cornerstone of the government's fiscal consolidation strategy. In March 2012, Congress approved the bill but a month later the Supreme Court nullified it, citing procedural irregularities in its legislative approval. Since then, the authorities' fiscal policy strategy focused on containing expenditure, strengthening tax administration, and reducing borrowing costs by tapping international capital markets. The government placed US$1 billion Eurobonds in late 2012 and is planning to place an additional US$3 billion in the coming years.

8. **Domestic financial conditions tightened during 2012.** Although the monetary policy rate has remained at 5 percent since mid-2011, other interest rates rose significantly, especially during the first half of the year, driven by large government borrowing and buoyant private sector credit demand. Interest rates declined somewhat late in the year, but remained above the previous year's level. A broader-based index developed by staff (comprising variables such as interest rates, the REER, and house prices) also pointed to tighter financial conditions (Box 2). Despite this tightening, credit expansion to the private sector was slightly higher than nominal GDP growth.

Box 2. Costa Rica: Financial Conditions

A Financial Conditions Index (FCI) was developed for Costa Rica. Financial conditions can be defined as the current state of financial variables that influence economic activity. The FCI seeks to summarize the information contained in key financial variables and capture the link between them and economic activity. A VAR analysis was used to decompose the contribution of various financial indicators to real GDP growth. The FCI was built as the sum of the cumulative impulse responses of real GDP to each of the relevant financial variables. The financial variables used included a summary measure of interest rates (the basic passive rate or "tasa basica pasiva"), the real effective exchange rate, the stock market index, and a house price index (proxied by rental prices as measured in the consumer price index). The period of estimation was 1991-2012, and the frequency of the data was quarterly. The impulse responses were standardized so that a change in each FCI component by one unit can be interpreted as an (annualized) change in real GDP growth by 1 percentage point. Hence, a change in the value of the overall FCI reflects the total contribution of financial conditions to GDP growth.

Monetary and Financial Conditions Index
(percentage points of y/y real GDP growth)



Source: Fund staff estimates.

The estimated FCI suggests that financial conditions tightened in 2012. The rise in the basic passive interest rate and a weaker stock market during the first half of the year were the main drivers of the tightening in the FCI. Financial conditions eased somewhat during the second half of the year, partly driven by a decline in the basic passive interest rate in the fourth quarter. However, considering the year as a whole, financial conditions in 2012 were on average tighter than in 2011. Tighter financial conditions may have been a drag on growth, which showed slowing signs in the second half of the year.

9. **The financial system remained sound, though dollarization continues to be a source of vulnerability.** Capital adequacy stood well above regulatory requirements and liquidity remained robust. Profitability was stable, albeit somewhat below that of regional peers, and non-performing loans are at manageable levels. Reliance on foreign funding is small and exposure to foreign assets modest. Staff analysis suggests that a potential intensification of sovereign and banking strains in advanced countries would not have a large direct impact on credit or the financial system in Costa Rica (Box 3). Stress test exercises conducted by bank supervisors in 2012 yielded similar results. Although the banking sector has a long open foreign exchange position, a large depreciation of the colón may impact asset quality, given large unhedged liability dollarization of households and corporations.

Financial Soundness Indicators *(in percent)* 1/

	Costa Rica	Guatemala	El Salvador	Honduras	Dominican Republic	Panama	CAPDR 2/	LA6 3/
Regulatory Capital to Risk-Weighted Assets	17.4	14.6	17.4	14.9	15.7	16.0**	15.7	15.4
Capital to Assets Ratio	15.1	9.5*	13.9*	11.0	9.9	11.7**	11.2	10.1
Nonperforming Loans to Total Loans Ratio	1.8	1.5	3.3*	2.6	3.2	0.9**	2.3	2.6
Return on Assets	1.5	1.9*	1.6	2.5	2.3	1.8**	2.0	2.1
Return on Equity	10.3	19.6*	11.7*	25.2	23.2	7.3**	17.4	20.1

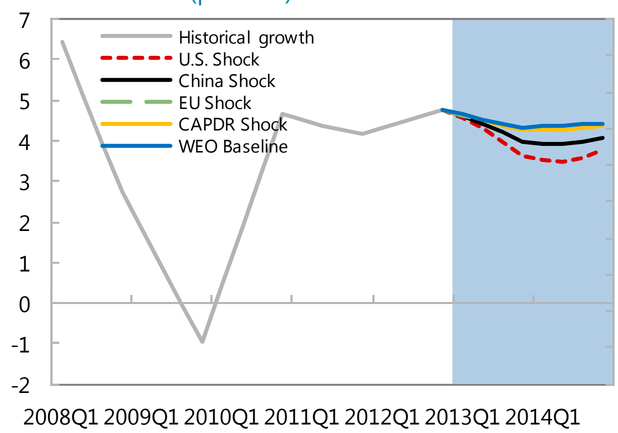
Source: FSI tables, October 2012, IMF, http://fsi.imf.org/fsitables.aspx.
1/ As of July, 2012 unless otherwise noted.
* As of August, 2012; ** as of June, 2012.
2/ Comprises Guatemala, El Salvador, Honduras, Panama, and the Dominican Republic.
3/ Comprises Brazil, Chile, Colombia, Mexico, Peru, and Uruguay.

Box 3. Costa Rica: Cross-Border Spillovers[1]

Strong trade and financial linkages make Costa Rica particularly sensitive to shocks emanating from the United States (U.S.). The U.S. is Costa Rica's main trading partner, the destination of over a third of its merchandise exports and the source of almost 40 percent of its merchandise imports. Financial linkages also are strong, with a large share of external assets and liabilities of Costa Rica's banks concentrated in the U.S. In addition, the bulk of foreign direct investment flows comes from the U.S. (64 percent of the total FDI stock is of U.S. origin).

Risks stemming from a growth slowdown in the U.S. are significantly higher than those from lower growth in other trading partners. Results from multi-country VAR analysis suggests that an adverse shock of ½ standard deviation in U.S. growth could lower Costa Rican GDP growth by ⅓ percentage points in 2013 and ¾ percentage points in 2014. A U.S. growth shock would propagate to Costa Rica both directly and indirectly through its negative impact on other Central American countries. In comparison, a shock of a similar size in China would lower growth by ⅕ and ⅖ percentage points in 2013 and 2014, respectively, while growth shocks in Europe and the rest of Central America would have very modest effects.

Costa Rica: Growth Forecast and Simulation, 2008-2014 (percent)



Sources: OECD, Poirson and Weber (2011), World Economic Outlook, and Fund staff calculations.

Fiscal adjustment in the U.S. could have comparatively significant but still limited effects on Costa Rica. Simulations suggest that each percentage point of GDP of fiscal adjustment in the United States would reduce Costa Rican growth by about 0.1 percentage points.

Though the presence of foreign banks is important, the direct effects of banking stress spillovers on the Costa Rican economy do not seem large. As of end-2012, the market share of international banks subsidiaries was about a third of the banking sector's total assets. The private and public sectors also have been actively involved in direct cross-border borrowing from international banks. The associated rollover risks, however, appear to be moderate, as the upstream exposure of Costa Rica to all BIS reporting banks does not exceed 13 percent of total credit.[2]

- The analysis of various stress scenarios based on the RES/MFU Bank Contagion Module suggests that the impact of large haircuts in the sovereign debt of some European countries on international banks lending to Costa Rica would be close to zero. This is due to the limited sovereign exposure of these banks to the euro area periphery countries.
- The estimates also indicate that the direct impact on lending to Costa Rican residents from a 10-percent decline in value in European assets (both sovereign and non-sovereign) held by international banks lending to Costa Rica would not exceed 3 percent of GDP.

Box 3. Costa Rica: Cross-Border Spillovers (concluded)

Spillovers to Costa Rica from International Banks' Exposures as of March 2012

	Shock Originating From Magnitude 1/	Impact on claims on CRI borrowers (percent of GDP) 2/
Greece	30	0.0
Greece, Ireland, and Portugal	30	-0.1
Italy	10	0.0
Spain	10	-0.1
France	10	-0.3
Germany	10	-1.0
Netherlands	10	-0.3
Austria	10	0.0
UK	10	-1.2
Selected European Countries 3/	10	-2.9
Canada and US	10	-3.7

Source: RES/MFU Bank Contagion Module based on BIS, ECB, and IFS data.
1/ Magnitude denotes the percent of on-balance sheet claims (all borrowing sectors) that lose value.
2/ Reduction in foreign banks credit to Costa Rica due to the impact of the analyzed shock on their balance sheets, assuming a uniform deleveraging across domestic and external claims.
3/ Austria, Greece, Ireland, Portugal, Italy, Spain, France, Germany, Netherlands, and UK.

[1] See Analytical Note 1 (AN 1).

[2] Total credit to the non-bank sectors in Costa Rica is calculated by adding IFS local (both domestic and foreign owned) banks' claims on non-bank borrowers and BIS reporting banks' direct cross-border claims on non-bank sectors (BIS Locational Banking Statistics Table 6B).

B. Macroeconomic Outlook and Risks

10. **Both authorities and staff project growth to decelerate in 2013, with inflation and the current account deficit remaining broadly stable.** Real GDP growth would ease to 4¼ percent largely on account of a lower contribution from net exports and a somewhat slower expansion in domestic demand. On the supply side, the bulk of the slowdown would come from manufacturing after an exceptionally strong performance in 2012. With output still slightly below potential, inflation is projected to stay within the target range and the current account deficit would not change materially. The overall balance of payments would remain strongly in surplus, amid continuing large FDI and portfolio inflows, leading to further substantial NIR rise.

11. **Staff's medium-term baseline scenario envisages continuing growth but a modest deterioration in fundamentals.** This central setting contemplates no fiscal consolidation over the forecast period (given uncertainties surrounding passage of the tax reform, ¶ 21), and projects the output gap to close by 2014, after which growth would converge to a steady-state potential rate of

4½ percent. The overall fiscal deficit would increase to about 7½ percent of GDP by 2018, and the public debt ratio would rise steadily to about 50 percent of GDP. With prudent monetary policy, inflation is projected to hover around 5 percent, though the current account deficit increases to about 6 percent of GDP.

Costa Rica. Baseline Scenario
(in percent of GDP, unless otherwise stated)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Real GDP growth (percent)	2.7	-1.0	4.7	4.2	5.0	4.2	4.4	4.5	4.5	4.5	4.5
Output gap (percent of potential GDP)	3.5	-1.6	-1.0	-1.0	-0.1	-0.1	0.1	0.2	0.2	0.2	0.2
Consumer prices (percent)	13.9	4.0	5.8	4.7	4.6	5.0	5.0	5.0	5.0	5.0	5.0
Current account balance	-9.3	-2.0	-3.5	-5.3	-5.5	-5.4	-5.5	-5.7	-5.8	-6.0	-6.0
Consolidated fiscal balance	0.2	-4.0	-5.5	-4.3	-4.4	-4.9	-5.9	-6.3	-6.6	-7.1	-7.4
Structural primary balance 1/ 2/	1.7	-0.9	-2.3	-2.3	-2.2	-2.3	-2.7	-2.7	-2.7	-2.7	-2.7
Structural overall balance 1/ 2/	-0.9	-3.2	-4.7	-4.7	-4.5	-4.8	-5.7	-6.0	-6.4	-6.7	-7.0
Consolidated public sector debt	27.3	29.2	30.6	33.2	38.1	39.5	41.2	43.6	45.8	47.9	50.1

Sources: National authorities, and IMF staff estimates
1/ Central government.
2/ The structural fiscal balance in 2010 and 2011 was adjusted taking into consideration the timing of a large public investment project.

12. **An alternative scenario that incorporates the authorities' fiscal consolidation intentions yields a stronger outlook**. The authorities aim to start a process of adjustment as well as adopt monetary and exchange rate policies that would keep the economy on a robust growth path, while alleviating lingering vulnerabilities. This scenario would have inflation gradually declining to trade partners' levels and would improve prospects for long-term external and fiscal sustainability (¶s 5 and 19). According to staff analysis, the authorities' plans would have only moderate short-term output costs and help lower inflation and the current account deficit over the forecast period.

Costa Rica. Fiscal Consolidation Scenario
(in percent of GDP, unless otherwise stated)

	2012	2013	2014	2015	2016	2017	2018
Real GDP growth (percent)	5.0	4.2	4.0	3.8	4.2	4.5	4.5
Output gap (percent of potential GDP)	-0.1	-0.1	-0.3	-0.9	-0.6	-0.3	0.0
Consumer prices (percent)	4.6	5.0	5.3	5.0	4.5	4.0	4.0
Current account balance	-5.5	-5.4	-4.8	-4.8	-4.9	-4.9	-4.9
Consolidated fiscal balance	-4.3	-4.4	-4.8	-5.0	-3.8	-3.6	-3.5
Structural primary balance 1/	-2.2	-2.3	-1.8	-0.3	-0.2	0.0	0.1
Structural overall balance 1/	-4.5	-4.8	-4.9	-3.6	-3.4	-3.3	-3.1
Consolidated public sector debt	38.1	39.5	40.5	40.7	40.3	39.4	38.4

Sources: National authorities, and IMF staff estimates
1/ Central government.

13. **Risks to the outlook are tilted to the downside.** Downside risks stem from both external and domestic sources. While deviations from the assumed baseline for each of the risk factors listed below could occur in either direction, the probability of downside occurrences is deemed prevalent.

- *Weaker global growth* would reduce the demand for Costa Rican exports and FDI flows, weakening domestic activity. Costa Rica would be particularly sensitive to a worsening in the U.S. growth outlook, given close trade and financial links.
- *Higher global risk aversion* would ease the pressures stemming from large capital inflows but, if extreme, could impair access to international capital markets and bank lending, with adverse implications for growth, the balance of payments, and the fiscal accounts.
- *Inflation shocks* could stem from an increase in commodity prices, stronger-than-expected price pressures from current policies, or inability to manage large private capital inflows.
- *The persistence of a large fiscal deficit*, and the ensuing rise in the public debt ratio, could render the economy vulnerable to sudden changes in financial market conditions, and reduce the authorities' policy space to respond to adverse shocks. Also, large government financing requirements could raise domestic interest rates, and weigh on private investment and growth.
- *A large depreciation of the colón* (in the event of an adverse balance of payments shock) *could weaken the balance-sheets of corporate and households*, given their negative foreign exchange positions, raising credit risks for banks, hurting economic activity.

Costa Rica: Risk Assessment Matrix[1]
(Scale—high, medium, or low)

Source of Risks	Overall Level of Concern	
	Relative Likelihood[2/]	**Impact if Realized**
1. Weaker global growth, especially slowdown in the U.S.	**Low** • Shocks affecting global economic growth, and in particular U.S. growth, would lower growth in Costa Rica.	**High** • Weaker-than-expected U.S. growth would lower export demand and significantly weigh on activity and tax revenues. A shock could have a more severe impact than in 2008-09, as fiscal buffers have been drawn down.
2. Higher global risk aversion.	**Medium** • Heightened financial stress in Europe could increase global risk aversion and reduce global growth. It could also reduce capital flows to emerging markets.	**Medium** • The direct trade impact would be modest. The indirect impact would depend on how much the shock affects U.S. growth. • A decline in capital flows to emerging markets would ease pressure from large capital inflows but, if extreme, could disrupt foreign credit lines and reduce banking sector liquidity.
3. Higher inflation, including from adverse global oil and food price shock or larger capital inflows.	**Low/Medium** • A supply shock could raise world food and oil prices. • With rising capital inflows, there is a risk that domestic policies prove too loose to prevent a rise in inflation.	**Medium** • Higher food and oil prices would increase inflation, widen the current account deficit, and adversely affect growth.
4. Worse-than-anticipated impact from persistently high fiscal deficits, or higher deficits than projected in the baseline scenario.	**Medium** • Lack of fiscal consolidation prospects may hurt confidence. • Continued expenditure pressure could increase the fiscal deficit and public debt above the projections in the baseline scenario.	**High** • Lower confidence or a higher government financing requirement could raise domestic interest rates and lower investment and growth. • Lower growth or a higher fiscal deficit would exacerbate fiscal sustainability risks, increasing the economy's vulnerability and reducing the government's ability to respond to adverse shocks. • Alternatively, even if confidence remained strong and financing were available, a looser fiscal stance could result in overheating.
5. Sudden unraveling of balance-sheet foreign exchange imbalances.	**Low** • Balance sheets of corporate and households are exposed to a depreciation of the local currency, given their negative foreign exchange positions. • While the banking sector holds a large open position in foreign currencies, it is also exposed to foreign exchange risk through its loan portfolio.	**Medium** • Bank loan availability would be curtailed, impacting economic activity and worsening the fiscal position. • Depending on the magnitude of the depreciation, balance sheet deterioration may affect some financial institutions.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path discussed in this report (which is the scenario most likely to materialize in the view of the staff). The RAM reflects staff's views on the source of risks and overall level of concerns as of the time of discussions with the authorities. The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding this baseline.

[2] In case the baseline does not materialize.

POLICY DISCUSSIONS

14. **Discussions centered on how to maintain macroeconomic stability and reduce vulnerabilities, while taking actions to spur potential growth and boost competitiveness.** In the near term, tighter fiscal and monetary policies may be necessary to maintain macroeconomic stability. In addition, fiscal consolidation is necessary to place public finances on a long-term sustainable path, the monetary policy framework should be further improved to maintain low inflation, financial sector supervision and regulation should be further enhanced, and structural reforms are needed to boost the growth potential of the economy and bolster competitiveness.

A. Near-term Policy Mix

15. **Staff cautioned about inflationary risks.** Though inflation has stayed subdued since 2009, risks of an uptick stem from: (i) continued capital inflows in the context of a lax global financial environment and a rigid exchange rate system; (ii) potential second round effects from higher global food prices (deserving special attention in light of their elevated pass-through in the past); and (iii) the imminent closure of the output gap. While agreeing with this assessment, the authorities highlighted that inflation expectations have recently fallen and are well-anchored within the target range.

16. **There was agreement that a tighter policy stance would help safeguard macro stability, but the authorities indicated that major fiscal adjustment was not possible in 2013.**

- Staff argued that a tighter fiscal stance in 2013 would contribute to mitigate risks of inflation and a wider external imbalance. It would also represent a step towards ensuring long-term sustainability (¶ 19). In staff's assessment, a fiscal correction of about 1-1½ percent of GDP in 2013 would be appropriate, taking into consideration inflation and fiscal sustainability concerns as well as the cyclical position of the economy (¶ 20 and AN 3). The authorities noted that, while administrative efforts to contain expenditure and improve tax collections would continue and result in some decline of the fiscal deficit, a correction of the magnitude recommended by staff would require passage of fiscal measures, notably tax reform, through Congress, which the authorities considered unlikely to be enacted before 2014 owing to the parliamentary calendar.

- The authorities indicated readiness to tighten monetary policy if signs of inflationary pressure emerge. Staff highlighted that, in the absence of fiscal adjustment, actions may be required to keep inflation within the target range. The central bank indicated that, to prevent a resurgence of inflation, it would consider raising the policy rate and allowing greater exchange rate flexibility, probably coupled with adoption of capital flows management measures.

B. Safeguarding Fiscal Sustainability

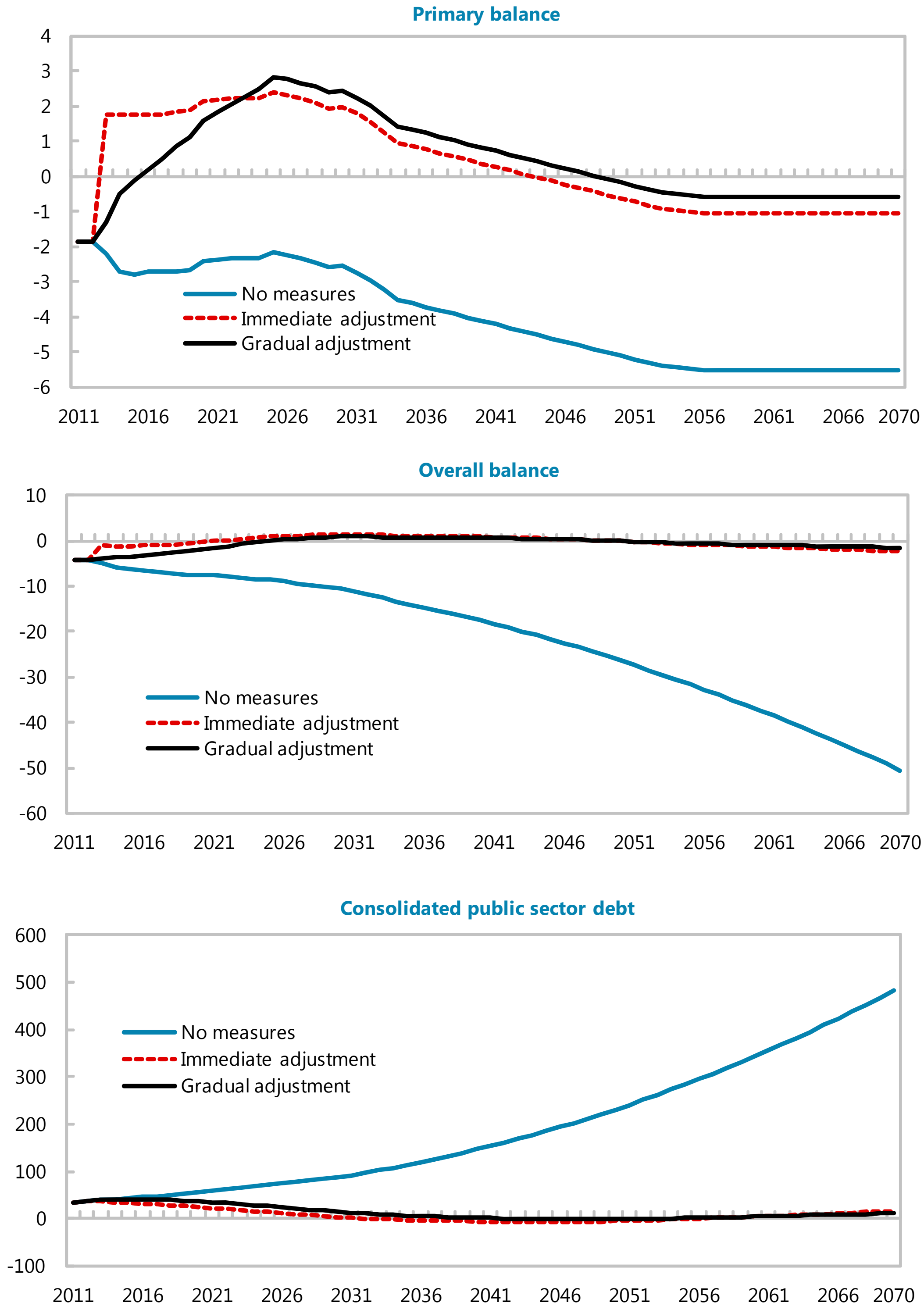
17. **The authorities concurred that current fiscal trends are unsustainable in the long-term.** While efforts made in 2011-12 to contain expenditure yielded important results (¶ 6), the fiscal deficit remains well above debt-stabilizing levels. Moreover, in the absence of measures, the consolidated public sector deficit would rise to about 7½ percent of GDP by 2018, driven by higher education and investment spending and a mounting interest bill. This would increase public sector debt to about 50 percent of GDP by 2018 (from 33 percent of GDP at end-2011). The authorities acknowledged that a rise in debt of that magnitude would raise vulnerabilities and erode the underpinnings of macroeconomic stability.

18. **The authorities also acknowledged that the pension system's financial position has to be strengthened.** The Old Age, Disability and Survivor insurance plan run by the Social Security agency (Caja Costarricense de Seguro Social or CCSS) as well as the pension funds of the judicial system and teachers are actuarially imbalanced. They are projected to turn a cash deficit over the medium and long term due to system maturation and population aging (AN 3). Preliminary projections suggest that an adjustment equivalent to about 1½ percent of GDP would be required to ensure actuarial equilibrium of all pension systems for the next 100 years. The authorities indicated that a joint study (by the CCSS and the Superintendence of Pensions) would allow determining more precisely the size of the imbalance. Based on the results from the study, gradual corrective measures (in the form of higher contributions, lower replacement rates, an increase in the retirement age, or a combination of measures) would be considered.

19. **The authorities agreed that substantial improvement in the primary balance was necessary to attain fiscal sustainability.** Staff noted that a permanent improvement in the primary balance of 2½-3 percent of GDP was necessary to stabilize the public debt ratio, and that the improvement would have to be 1½ percentage points of GDP higher to remedy the actuarial imbalance of the pension system (¶ 18), with the long-term fiscal sustainability gap thus totaling 4-4½ percentage points of GDP. Staff also argued that, beyond stabilizing the public debt ratio, it might be prudent to rebuild the budgetary buffers heavily eroded during 2009-10, considering the high sensitivity of public debt dynamics to shocks and the substantial risks to the outlook. Attaining this goal would require an additional improvement in the primary balance of about 1 percent of GDP.

Costa Rica: Long-Term Fiscal Sustainability, 2011-2070

(Percent of GDP)



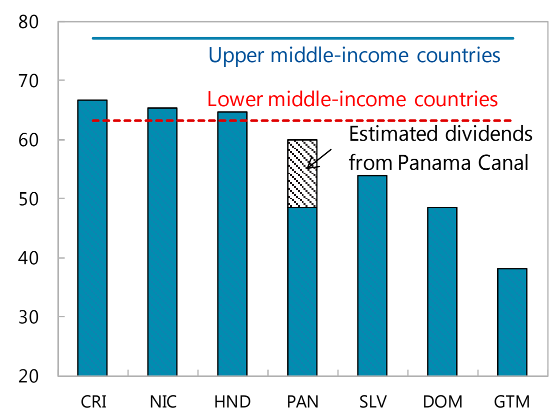
Source: IMF staff estimates.

20. **It was recognized that the pace of fiscal consolidation had to strike a balance between lowering the sustainability gap and limiting the adverse impact on growth.** While cyclical considerations (output is close to potential) and the rapid pace at which public debt is growing call for significant upfront fiscal tightening, the overall adjustment needed to achieve sustainability should be adopted gradually. Staff analysis suggests that a reasonable balance would be attained by undertaking about one third of the fiscal consolidation in 2013 (or at the latest in 2014) followed by smaller steps in subsequent years (AN 3). With a fiscal multiplier of about 0.3 (multipliers tend to be small when the output gap is virtually closed), consistent with the authorities' own estimates, the proposed adjustment path would be expected to have a small output cost over the forecast period. At the same time, staff cautioned against further postponing fiscal adjustment, emphasizing that the longer the delay, the larger will be the improvement in the primary balance required to stabilize the public debt ratio. Postponing fiscal consolidation would also increase the risk that currently favorable financial conditions reverse, which would precipitate a disorderly adjustment.

21. **The authorities favor a fiscal consolidation strategy with both revenue and expenditure components.**

- Recognizing Costa Rica's low tax effort, the authorities saw significant scope to increase public revenues. They remained convinced that a tax reform similar to the one they had proposed in 2011-12 had to be the cornerstone of the fiscal consolidation strategy. For this reason, the authorities considered that their plan to resubmit a tax reform proposal to Congress was an important step, as it would allow consensus to be built before a new administration takes office in May 2014. Staff agreed and welcomed new legislation approved in 2012 to strengthen revenue administration.

Tax Effort in the Region (Actual/Potential Tax Revenues), 2010 (percent)



Source: Country authorities; and IMF staff estimates.

- Efforts to contain the growth of current expenditure, particularly wages and transfers, should continue. In this connection, staff welcomed the bill submitted by the government to make the rigid public wage adjustment system more flexible as well as decisions to freeze vacancies and prioritize operational spending.

Costa Rica. Main Elements of the Authorities Fiscal Consolidation Plan

Area	Main Measures	Possible yield (percent of GDP)
Revenue	Submit new tax reform to Congress aimed at: Increasing tax base Reducing exemptions Redesigning value-added tax system Strengthen tax administration	**2½-3**
Expenditure	Reform public employees compensation regime Align wage adjustments with expected inflation and productivity growth Rationalize and streamline additional compensation schemes Enhance efficiency of spending, especially in health and education	**½**
Public Debt Management	Increase use of external debt to reduce cost of public debt	

Source: IMF staff based on national authorities.

C. Upgrading the Monetary and Exchange Rate Policy Framework

22. **Staff commended the authorities for having lowered inflation to single digits.** Having posted double-digit inflation for almost 30 years, Costa Rica has managed to lower it to 4-6 percent since 2009. This achievement has been underpinned by continued efforts by the central bank to improve monetary control and strengthen its monetary operations framework, notably through the establishment of a corridor for short-term interest rates and the launch of a policy interest rate in 2011. Inflation, nonetheless, remains above that of trading partners. The authorities reaffirmed their goal to reduce inflation to trading partners' levels (about 3 percent) over the medium term.

23. **However, the monetary policy framework still presents weaknesses.** Staff argued that the continued adherence to the exchange rate band was undermining the hard-won gains in lowering inflation, and the central bank's ability to anchor inflation expectations. With the exchange rate at the bottom of the band and persistent appreciating pressures, the central bank has thus far reconciled monetary and exchange rate policy objectives by sterilizing foreign exchange purchases. However, the risk is high that sterilization costs will increase, widening the central banks' deficit, particularly if capital inflows rise further. Clinging to the rigidity of the current exchange rate band could then lead to higher inflation. The central bank recognized these risks and indicated that, should conflicts arise, the inflation target would take precedence over other objectives.

24. **The authorities reiterated their commitment to adopt full inflation targeting, but are concerned that removal of the band would result in abrupt colón appreciation.** To protect macroeconomic stability, staff repeated the advice given in past Article IV consultations of eliminating the exchange rate band and establishing the inflation target as the undisputed anchor of monetary policy. This would allow greater use of the exchange rate as a shock absorber. A more flexible exchange rate regime would also make market participants more cognizant of two-way risks in exchange markets, promoting the development and use of hedging facilities and the reduction of foreign currency mismatches. The authorities concurred in principle, but they saw a serious risk of a large appreciation of the colón at the present juncture. To mitigate the latter, the authorities noted that they may consider the adoption of capital flow management measures (CFMs). Staff noted that the elimination of the band would not preclude the central bank from engaging in foreign exchange market interventions to smooth out exchange rate fluctuations as long as these do not undermine the inflation target. At the same time, it stressed that CFMs cannot replace fiscal and monetary policies as the key levers for preventing excessive REER appreciation over the medium term.

D. Financial Stability

25. **The authorities are working to implement pending recommendations from the 2008 FSAP update.** Progress in implementation has been slow, largely due to a crowded legislative agenda**.** Key pending steps include empowering the Superintendence of Financial Institutions to conduct consolidated supervision, providing adequate protection to bank supervisors, strengthening bank resolution procedures, and broadening the supervisory perimeter to non-bank financial institutions, all of which require passage of new legislation. On the supervisory front, staff welcomed progress in establishing risk-based supervision, and advised the authorities to step up efforts for its full implementation.

Costa Rica. Financial System Assessment Program (FSAP) Main Recommendations (2008)

Recommendations	Status 1/	Comments
A. Prudential Supervision and Regulation		
Amend the legal framework in order to provide protection for supervisors while performing their responsibilities in good faith.	NI	Art. 28 of Insurance Law 8653 of August 7, 2008, provides legal protection to insurance supervisors. The draft bank resolution law contemplates protection for bank supervisors participating in the resolution process.
Introduce pertinent laws for the Superintendency of Banks (SUGEF) to be able to supervise banking groups (including offshore structures) on a consolidated basis. Upon the approval of such laws the SUGEF should issue without delay operational regulations to ensure its rapid implementation by the banking system.	PL	
Apply higher risk weight ratios to unhedged borrowers for capital adequacy purposes.	NI	Under consideration by the authorities.
Modify the funding arrangements for supervision, in line with international best practices.	NI	A draft legislation to recapitalize the central bank also addresses the increase in the financing share of the industry.
B. Crisis Management and Bank Crisis Resolution Framework		
Amend article 155 of the Central Bank law in order to grant the SUGEF an appropriate range of supervisory tools to require a bank to take prompt remedial action and to impose penalties in accordance with the gravity of a situation.	PL	
Amend the rating system for prompt corrective actions, to include new directives that allow the SUGEF to take an appropriate range of remedial actions and supervisory decisions.	PI	The authorities intend to amend the rating system once risk-based supervision is fully in place.
Improve the early warning system, to allow the adoption of remedial actions in a timely manner.	PI	The authorities will review the possibility of taking a broader range of remedial actions within the scope of the existing law.
Eliminate the emergency loan window and improve the design and operational arrangements of the ordinary rediscount window, including by establishing prudential limits in terms of regulatory capital.	PI	The emergency line introduced during the 2008-09 crisis was discontinued and two high-access rediscount windows were created in 2011: (i) using bonds already included in the money market collateral pool; and (ii) using commercial credit portfolio as collateral (with strict rules on quality and haircuts). Both lines are available in US dollars and in colones.

Costa Rica. Financial System Assessment Program (FSAP) Main Recommendations (2008) (concluded).

		However, the rediscount windows are activated only when a central bank committee considers that there is a systemic risk; operational procedures need to be further streamlined; and repo operations are still to be linked to prudential limits in terms of regulatory capital
Establish a deposit insurance scheme, in line with international best practices.	PL	
Amend the bank resolution legal framework to include purchase and assumption type techniques.	PL	
Enable voluntary, extra-judicial corporate restructuring agreements.	NI	Approval of the Law on Execution on October 2007 did not address the weaknesses of the current procedural rules.
1/ FI: fully implemented; PI: partially implemented; PL: pending legislation; NI: Not implemented. Source: Superintendence of Financial Institutions.		

26. **Staff supported the gradual adoption of Basel III standards to improve further the resilience of the financial system.** It noted that implementation of Basel III standards should be tailored to the characteristics of the Costa Rican financial system. Staff argued that the regulatory and risk management frameworks would benefit from firming up capital quality and increasing liquidity and capital requirements in line with Basel III standards. In particular, it advised introducing Basel III definitions of capital, a capital conservation buffer, and a leverage ratio. Supervisors agreed and confirmed that a coverage ratio conforming to Basel III will be introduced shortly. Staff estimates that adopting Basel III capital requirements would have a negligible negative growth impact (AN 4).

E. Structural Reforms

27. **There was agreement that Costa Rica needs structural reforms to boost potential growth and buttress competitiveness.** Staff recommended lifting competition in the banking sector (including by removing legal and regulatory differences between private and public banks), fostering the development of the domestic capital market, addressing infrastructure bottlenecks, and streamlining business regulations. According to staff estimates, efficiency gains from these measures could increase potential growth by up to 2 percentage points over the long run, although these are subject to a considerable degree of uncertainty. The authorities underlined the need to increase investment in infrastructure and noted ongoing projects in this area. They also pointed out progress in increasing competition in the insurance sector, which is expected to contribute to financial deepening.

Reforms to Boost Long-term Growth and Bolster Competitiveness

Reforms	Goals
Eliminate/reduce existing weaknesses in transport infrastructure and logistics Improve the operation of ports in the Atlantic coast Increase private sector participation in the provision of infrastructure services Speed up border checkpoints Increase security in highways	Reduce transportation costs
Promote investment in power generation Review tariff and subsidies to residential consumers Increase private sector participation in the energy sector	Ensure adequate electricity provision
Improve education Enhance the secondary education system Increase student financial aid for higher education	Boost human capital
Streamline business regulations Reduce the number of procedures to start a business Simplify the procedures to obtain constructuction permits Decrease the number of documents required for external trade	Reduce the cost of doing business
Support financial deepening Remove regulatory asymmetries between public and private banks Facilitate the collateral repossession process Redesign development finance system Promote the development of derivatives market Increase competition in the securities market and the insurance sector	Increase access to finance

Source: World Bank; and Fund staff.

STAFF APPRAISAL

28. **Having recovered fast from the global crisis of 2008-09, Costa Rica is well placed to maintain vigorous growth, but external and domestic strains loom large**. The output gap that emerged during 2008-09 has almost closed, while inflation is well within the target range and projected to remain stable. However, risks to the outlook are tilted to the downside. On the external front an adverse shock in the U.S. would have a significant impact on growth. As for domestic risks, the current policy mix may not be conducive to lasting macroeconomic stability, and may result in overheating. Surging capital inflows, amidst lax global financial conditions, increase this risk. At the same time, continuing sizable fiscal deficit could hurt confidence and raise borrowing costs.

29. **To lessen risks for macroeconomic stability, the fiscal deficit should be reduced and monetary policy prepared for tightening.** While spending growth has been contained in the last two years, the fiscal deficit remains large, and public sector debt is rising. With a closing output gap, an early fiscal correction of about 1-1½ percent of GDP would contain the risk of an acceleration of domestic demand, which could stir up price pressures and external imbalances. Such an adjustment would also make an important contribution toward stabilizing the public debt-to-GDP ratio. The monetary policy stance appears conducive to stable inflation. However, risks that inflation may turn higher than anticipated persist. Accordingly, interest rates should be raised and greater exchange rate flexibility allowed, if there is evidence on an inflation uptick.

30. **Ambitious fiscal consolidation should be sustained over the medium term.** The current fiscal path, with continuously rising government debt, is untenable in the long-term and exacerbates macroeconomic fragilities. The authorities should thus seek to stabilize the public-debt-to-GDP ratio, which would require a permanent improvement in the primary balance of about 2½-3 percentage points of GDP. Additional adjustment (of about 1½ percentage points of GDP) would be necessary to bring the pension system to actuarial equilibrium. The pace of fiscal consolidation should balance the objectives of lowering the sustainability gap and limiting the adverse short-term impact on growth, which is quite feasible, since fiscal multipliers are low when the output gap is small. Reducing gradually the public debt ratio is also desirable to increase fiscal policy buffers.

31. **Fiscal consolidation should include both revenue and expenditure measures.** The size of the fiscal adjustment required to ensure sustainability calls for a multi-pronged strategy. There is significant scope to increase public revenues, since Costa Rica's tax effort is low for an upper-middle-income country. In this connection, the intention of the government to seek parliamentary approval of a new version of the tax reform is welcome. In addition, revenue administration should be further strengthened. At the same time, current expenditure growth, which greatly outstripped nominal GDP growth during 2008-10, should be restrained, including through efficiency gains, as planned by the authorities.

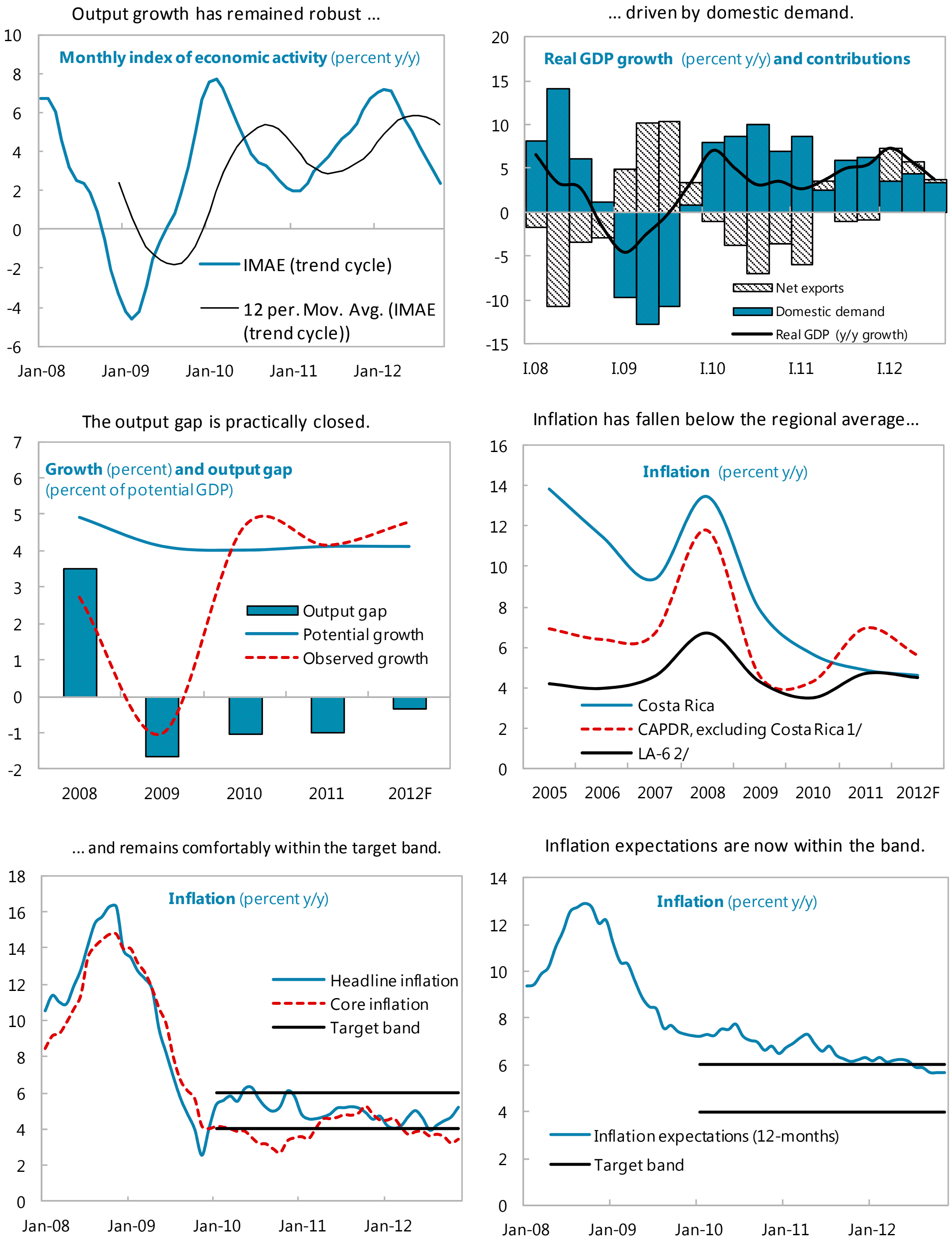
32. **The monetary policy framework should be strengthened by moving to inflation targeting and allowing greater exchange rate flexibility.** Continued adherence to the exchange rate band system may imperil the low inflation achieved in recent years, in light of the strong appreciating pressures exacerbated by the large capital inflows. Sterilization of foreign exchange purchases will become increasingly costly and ultimately compel the central bank to allow higher inflation. To protect macroeconomic stability, the authorities should phase out the exchange rate band and establish the inflation target as the sole nominal anchor of the economy. Foreign exchange market interventions by the central bank to smooth out exchange rate fluctuations and strengthen the NIR position would still be possible insofar as these do not undermine the inflation target. If necessary, these policies, along with appropriate fiscal and monetary policies, could be complemented for a limited period by macro-prudential and other capital flow management measures.

33. **Further improvements in regulation and supervision of the financial system are desirable.** The risk of a sharp deterioration of the bank loan portfolio following a large depreciation of the colon (given that a sizable share of dollar-borrowers does not generate significant earnings in foreign currency) is of particular concern. To mitigate this and other vulnerabilities, measures recommended in the 2008 FSAP update but still not implemented should be adopted. On the supervisory front, full-fledged introduction of risk-based supervision should be a priority. In addition, the regulatory and risk management frameworks would benefit from firming up the existing capital quality and increasing liquidity and capital requirements in line with Basel III standards.

34. **Structural reforms should be pursued to boost potential growth.** Measures to lift competition in the banking sector (including by promoting higher private sector participation), foster the development of the domestic capital market, reduce infrastructure bottlenecks, and streamline business regulations are especially important.

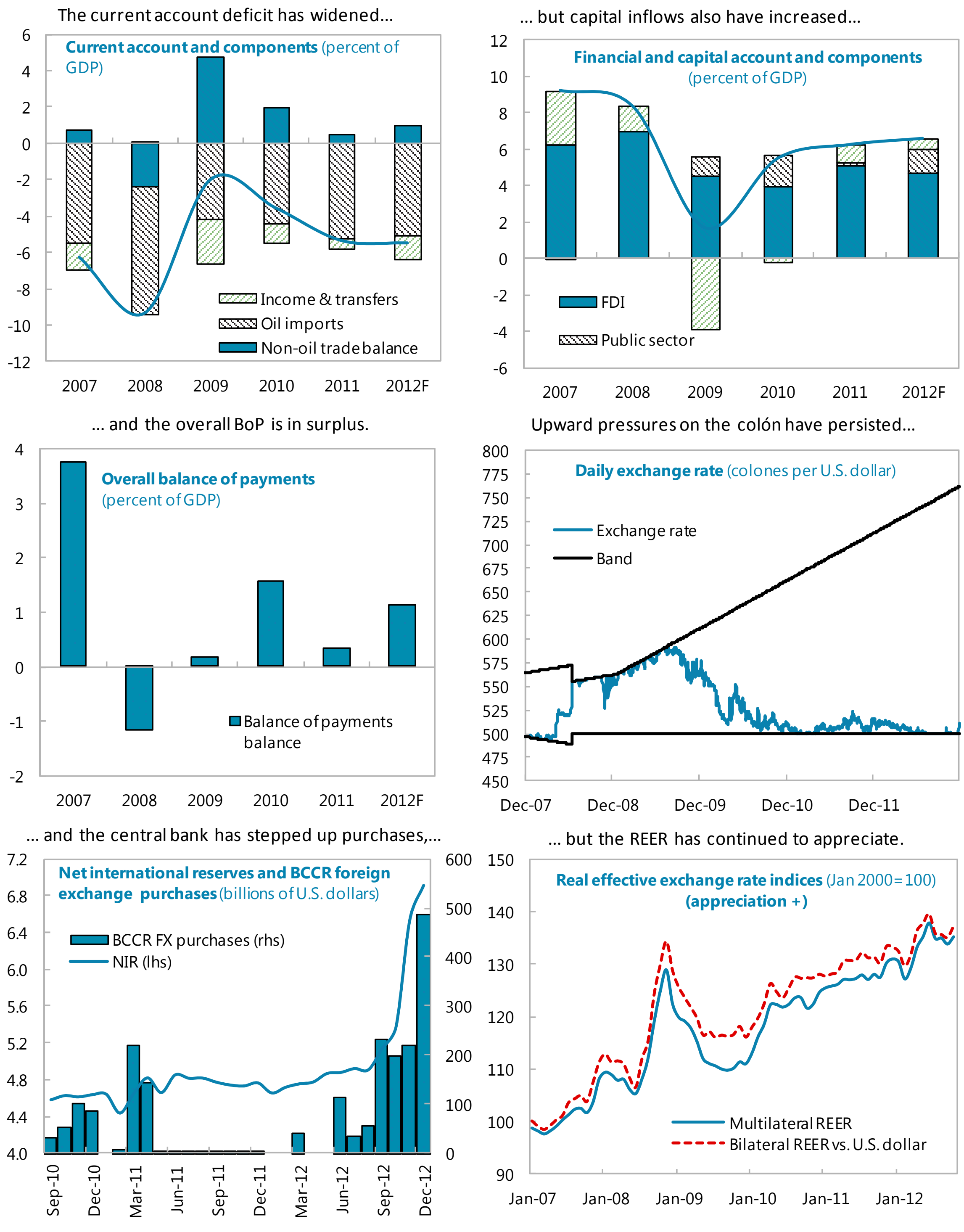
35. **It is recommended that the next Article IV consultation be held on the standard 12-month cycle.**

Figure 1. Costa Rica: Growth & Inflation



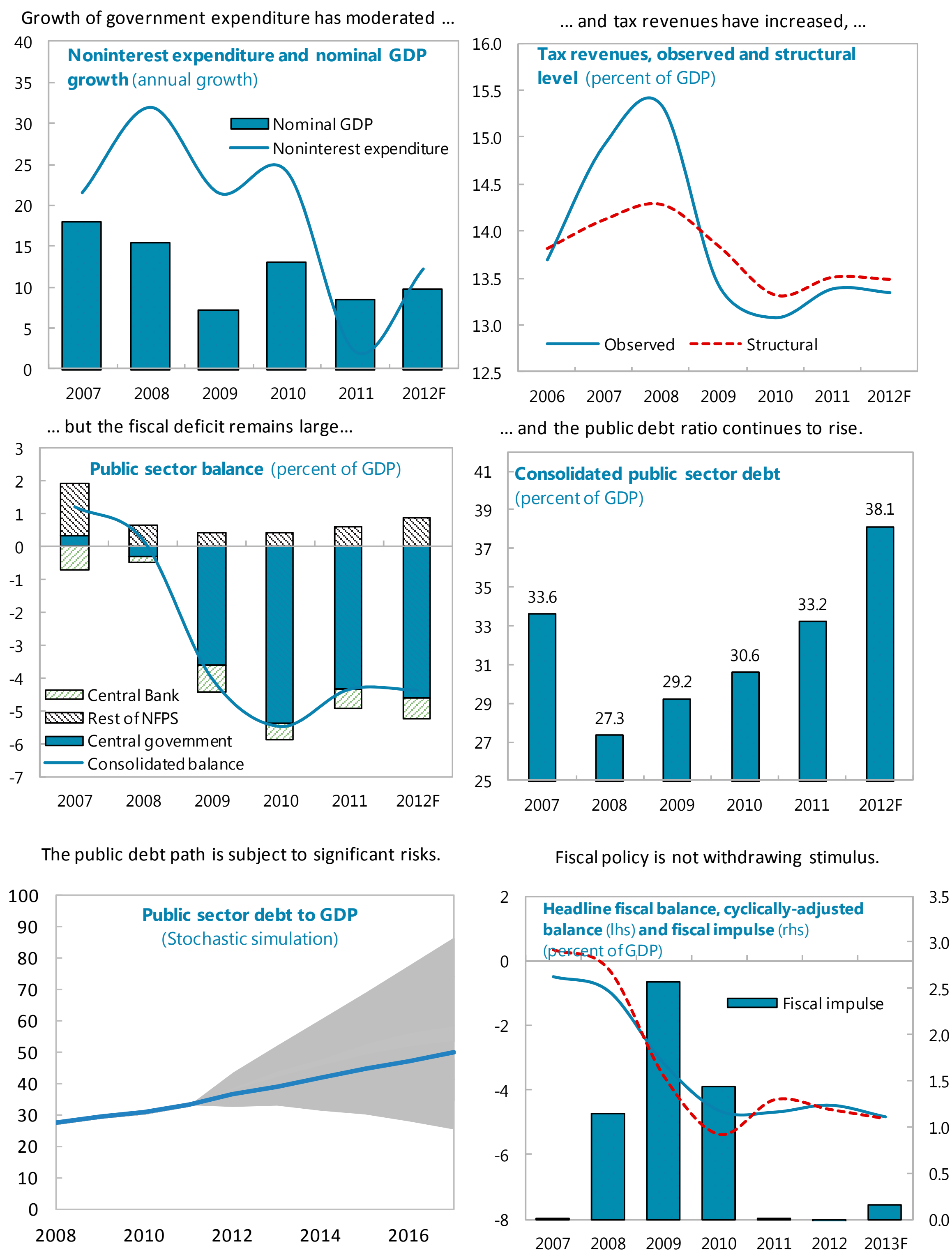
Sources: Country authorities and IMF staff calculations.
1/ CAPDR excluding Costa Rica comprises Dominican Rep, El Salvador, Guatemala, Honduras and Panama.
2/ LA-6 comprises Brazil, Chile, Colombia, Mexico, Peru and Uruguay.

Figure 2. Costa Rica: External Sector



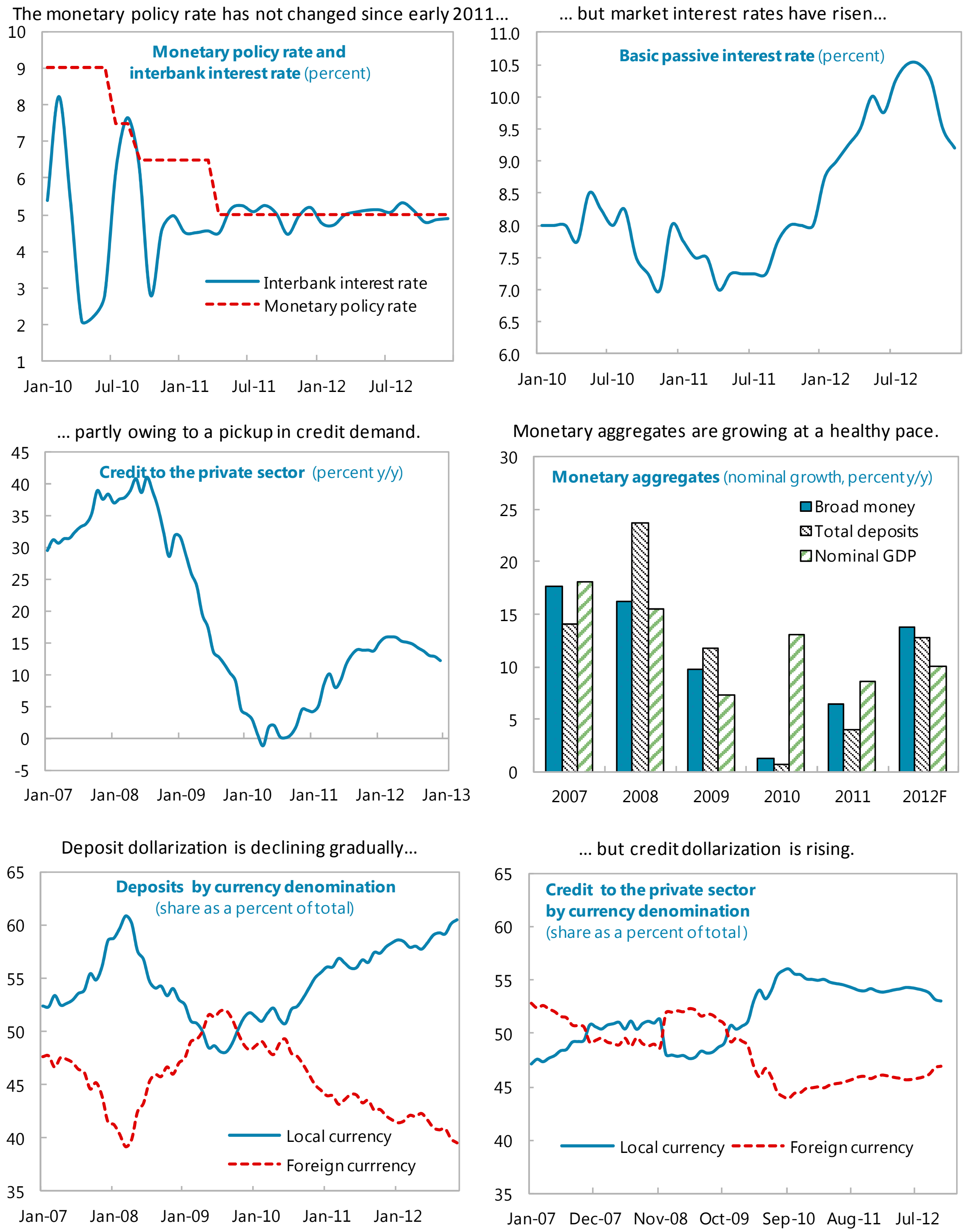
Sources: Country authorities and IMF staff calculations.

Figure 3. Costa Rica: Fiscal Developments



Source: Country authorities and IMF staff calculations.

Figure 4. Costa Rica: Money and Credit



Source: Country authorities and IMF staff calculations.

Table 1. Costa Rica: Selected Social and Economic Indicators

Population (2011, millions)	4.7	Human Development Index Rank (2011)	70 (out of 187)
Per capita GDP (2011, U.S. dollars)	10,591	Life expectancy (2009, years)	79.1
Unemployment (2011, percent of labor force)	7.7	Literacy rate (2009, percent of people ages > 15)	96.0
Poverty (2010, percent of population)	24.2	Ratio of girls to boys in primary and secondary education (2010, percent)	102.0
Income share held by highest 10 percent of households	39.4		
Income share held by lowest 10 percent of households	1.7	Gini coefficient (2009)	51.0

					Est.	Proj.	
	2008	2009	2010	2011	2012	2013	2014
	(Annual percentage change, unless otherwise indicated)						
Output and Prices							
Real GDP growth	2.7	-1.0	4.7	4.2	5.0	4.2	4.4
Output gap (percent of potential GDP)	3.5	-1.6	-1.0	-1.0	-0.1	-0.1	0.1
GDP deflator	12.4	8.4	8.0	4.1	4.5	5.1	5.2
Consumer prices (end of period)	13.9	4.0	5.8	4.7	4.6	5.0	5.0
Money and Credit							
Monetary base	11.9	5.1	11.2	11.6	10.1	9.9	9.8
Broad money	16.1	9.7	1.2	6.4	11.1	11.7	11.6
Credit to private sector	31.8	4.5	4.4	13.7	12.7	12.6	11.3
Monetary policy rate (percent; end of period)	…	…	…	5.5	5.5	…	…
	(In percent of GDP, unless otherwise indicated)						
Savings and Investment							
Gross domestic investment	27.6	16.3	20.1	20.6	20.8	20.5	20.7
Gross domestic savings	18.2	14.3	16.6	15.3	15.3	15.0	15.2
External Sector							
Current account balance	-9.3	-2.0	-3.5	-5.3	-5.5	-5.5	-5.6
Of which: Trade balance	-16.8	-6.9	-9.5	-12.6	-12.6	-12.6	-12.6
Financial and capital account balance	8.3	1.7	5.5	6.3	10.1	8.5	7.4
Of which: Foreign direct investment	6.9	4.6	4.0	5.1	5.0	4.8	4.5
Change in net international reserves (increase -)	348	-51	-561	-132	-2,101	-1,500	-1,000
Net international reserves (millions of U.S. dollars)	3,799	4,066	4,627	4,756	6,857	8,357	9,357
Public Finances							
Central government primary balance	2.4	-1.3	-3.0	-1.9	-2.3	-2.4	-2.7
Central government overall balance	-0.3	-3.6	-5.4	-4.3	-4.6	-4.9	-5.7
Central government debt	24.8	27.2	29.2	30.9	34.8	35.9	37.3
Consolidated public sector overall balance 1/	0.2	-4.0	-5.5	-4.3	-4.4	-4.9	-5.9
Consolidated public sector debt 2/	27.3	29.2	30.6	33.2	38.1	39.5	41.2
Of which: External public debt	8.6	7.2	7.2	6.4	7.8	9.3	10.4
Memorandum Item:							
GDP (millions of U.S. dollars)	29,838	29,383	36,218	40,870	45,103	49,778	54,523

Sources: Central Bank of Costa Rica; Ministry of Finance; and Fund staff projections.

1/ The consolidated public sector balance comprises the central government, decentralized government entities, public enterprises, and the central bank, but excludes the Instituto Costarricense de Electricidad (ICE).

2/ The consolidated public debt nets out central government and central bank debt held by the Caja Costarricense del Seguro Social (social security agency) and other entities of the nonfinancial public sector.

Table 2. Costa Rica: Balance of Payments

					Est.	Projection					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
					(In millions of U.S. dollars)						
Current Account	-2,787	-576	-1,281	-2,185	-2,469	-2,738	-3,027	-3,429	-3,806	-4,222	-4,621
Trade balance	-5,013	-2,039	-3,440	-5,151	-5,684	-6,262	-6,879	-7,717	-8,426	-9,217	-10,074
Export of goods (f.o.b.)	9,555	8,838	9,516	10,383	11,111	11,638	12,379	13,290	14,454	15,712	16,966
Import of goods (f.o.b.)	14,569	10,877	12,956	15,534	16,795	17,900	19,258	21,006	22,879	24,929	27,040
Services	2,201	2,188	2,537	3,210	3,719	4,171	4,624	5,167	5,679	6,235	6,841
Of which: Travel	1,689	1,448	1,575	1,747	1,994	2,261	2,542	2,852	3,087	3,351	3,634
Income	-417	-1,084	-745	-567	-847	-979	-1,148	-1,327	-1,529	-1,733	-1,907
Current transfers	442	359	366	323	343	332	376	448	471	494	520
Financial and Capital Account	2,487	498	1,986	2,557	4,569	4,238	4,027	4,229	4,006	4,272	4,671
Public sector	11	302	615	53	813	995	990	1,020	640	722	721
Private sector	2,476	196	1,371	2,505	3,757	3,243	3,037	3,209	3,366	3,550	3,950
Foreign direct investment	2,072	1,339	1,441	2,099	2,251	2,371	2,464	2,561	2,727	2,982	3,263
Other private sector flows	404	-1,143	-70	406	1,505	872	573	648	639	568	688
Errors and Omissions	-48	129	-144	-239	0	0	0	0	0	0	0
Change in International Reserves (increase -)	348	-51	-561	-132	-2,101	-1,500	-1,000	-800	-200	-50	-50
					(In percent of GDP)						
Current Account	-9.3	-2.0	-3.5	-5.3	-5.5	-5.5	-5.6	-5.7	-5.8	-6.0	-6.0
Trade balance	-16.8	-6.9	-9.5	-12.6	-12.6	-12.6	-12.6	-12.9	-12.9	-13.1	-13.2
Export of goods (f.o.b.)	32.0	30.1	26.3	25.4	24.6	23.4	22.7	22.2	22.2	22.3	22.2
Import of goods (f.o.b.)	48.8	37.0	35.8	38.0	37.2	36.0	35.3	35.1	35.1	35.3	35.3
Of which: Oil and fuels	7.0	4.2	4.4	5.3	5.0	4.6	4.3	4.2	4.0	4.0	4.0
Services	7.4	7.4	7.0	7.9	8.2	8.4	8.5	8.6	8.7	8.8	8.9
Income	-1.4	-3.7	-2.1	-1.4	-1.9	-2.0	-2.1	-2.2	-2.3	-2.5	-2.5
Current transfers	1.5	1.2	1.0	0.8	0.8	0.7	0.7	0.7	0.7	0.7	0.7
Financial and Capital account	8.3	1.7	5.5	6.3	10.1	8.5	7.4	7.1	6.1	6.0	6.1
Of which: Foreign direct investment	6.9	4.6	4.0	5.1	5.0	4.8	4.5	4.3	4.2	4.2	4.3
Change in International Reserves (increase -)	1.2	-0.2	-1.5	-0.3	-4.7	-3.0	-1.8	-1.3	-0.3	-0.1	-0.1
Memorandum Items:											
Non-oil current account (percent of GDP)	-2.3	2.3	0.9	-0.1	-0.5	-0.9	-1.3	-1.6	-1.8	-2.0	-2.0
Terms of trade (annual percentage change)	-1.1	4.9	-0.3	-3.1	-0.8	0.0	0.5	0.7	0.7	0.7	0.7
Net international reserves (millions of U.S. dollars)	3,799	4,066	4,627	4,756	6,857	8,357	9,357	10,157	10,357	10,407	10,457
-in months of non-maquila imports	6.7	6.1	5.5	5.2	6.9	7.8	8.0	8.0	7.5	7.5	7.5
-in percent short-term debt 1/	88.4	141.3	139.7	137.1	172.8	184.1	177.1	164.8	188.6	169.6	153.3
External debt (percent of GDP) 2/	30.5	27.8	25.2	25.2	27.8	29.8	32.4	34.6	35.8	36.6	37.2

Sources: Central Bank of Costa Rica; and Fund staff estimates.

1/ Public and private sector external debt on remaining maturity. Includes trade credit.
2/ Includes public and private sector debt.

Table 3. Costa Rica: Central Government Balance

					Est.		Projection				
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
					(In billions of colones)						
Revenue	**2,490**	**2,363**	**2,617**	**2,869**	**3,147**	**3,510**	**3,890**	**4,264**	**4,684**	**5,156**	**5,670**
Tax revenue	2,409	2,262	2,492	2,767	3,028	3,380	3,747	4,107	4,512	4,967	5,462
Nontax revenue 1/	81	101	125	102	119	130	143	157	172	189	208
Expenditure	**2,536**	**2,970**	**3,649**	**3,765**	**4,195**	**4,729**	**5,445**	**6,078**	**6,782**	**7,582**	**8,465**
Current noninterest	1,776	2,275	2,748	2,965	3,306	3,670	4,086	4,485	4,924	5,410	5,947
Wages	857	1,115	1,349	1,513	1,661	1,819	1,998	2,193	2,408	2,646	2,909
Goods and services	88	106	121	136	159	199	218	240	263	289	318
Transfers	832	1,054	1,278	1,316	1,486	1,652	1,869	2,052	2,253	2,475	2,721
Interest 2/	415	393	452	497	527	628	814	994	1,202	1,456	1,721
Capital	344	302	449	304	363	431	544	599	656	716	797
Primary balance	**370**	**-213**	**-580**	**-400**	**-522**	**-590**	**-740**	**-820**	**-897**	**-970**	**-1,074**
Overall Balance	**-46**	**-606**	**-1,032**	**-896**	**-1,049**	**-1,218**	**-1,555**	**-1,814**	**-2,099**	**-2,426**	**-2,795**
Total Financing	46	606	1,032	896	1,049	1,218	1,555	1,814	2,099	2,426	2,795
External (net)	-49	-186	247	-112	498	531	518	594	346	325	330
Domestic (net)	95	793	785	1,008	551	687	1,037	1,220	1,753	2,101	2,465
Central government debt	**3,891**	**4,587**	**5,562**	**6,382**	**7,904**	**8,923**	**10,180**	**11,995**	**14,140**	**16,619**	**19,472**
External	1,138	976	1,142	1,027	1,492	2,031	2,553	3,147	3,539	3,917	4,305
Domestic	2,753	3,611	4,420	5,355	6,412	6,893	7,627	8,848	10,601	12,702	15,167
					(In percent of GDP)						
Revenue	**15.9**	**14.0**	**13.7**	**13.9**	**13.9**	**14.1**	**14.3**	**14.2**	**14.2**	**14.3**	**14.3**
Tax revenue	15.3	13.4	13.1	13.4	13.3	13.6	13.7	13.7	13.7	13.7	13.8
Nontax revenue 1/	0.5	0.6	0.7	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Expenditure	**16.1**	**17.6**	**19.2**	**18.2**	**18.5**	**19.0**	**20.0**	**20.3**	**20.6**	**21.0**	**21.3**
Current noninterest	11.3	13.5	14.4	14.3	14.6	14.8	15.0	15.0	15.0	15.0	15.0
Wages	5.5	6.6	7.1	7.3	7.3	7.3	7.3	7.3	7.3	7.3	7.3
Goods and services	0.6	0.6	0.6	0.7	0.7	0.8	0.8	0.8	0.8	0.8	0.8
Transfers	5.3	6.3	6.7	6.4	6.6	6.7	6.9	6.9	6.9	6.9	6.9
Interest 2/	2.6	2.3	2.4	2.4	2.3	2.5	3.0	3.3	3.7	4.0	4.3
Capital	2.2	1.8	2.4	1.5	1.6	1.7	2.0	2.0	2.0	2.0	2.0
Primary balance	**2.4**	**-1.3**	**-3.0**	**-1.9**	**-2.3**	**-2.4**	**-2.7**	**-2.7**	**-2.7**	**-2.7**	**-2.7**
Overall Balance	**-0.3**	**-3.6**	**-5.4**	**-4.3**	**-4.6**	**-4.9**	**-5.7**	**-6.1**	**-6.4**	**-6.7**	**-7.0**
Total Financing	**0.3**	**3.6**	**5.4**	**4.3**	**4.6**	**4.9**	**5.7**	**6.1**	**6.4**	**6.7**	**7.0**
External (net)	-0.3	-1.1	1.3	-0.5	2.2	2.1	1.9	2.0	1.1	0.9	0.8
Domestic (net)	0.6	4.7	4.1	4.9	2.4	2.8	3.8	4.1	5.3	5.8	6.2
Central government debt	**24.8**	**27.2**	**29.2**	**30.9**	**34.8**	**35.9**	**37.3**	**40.0**	**43.0**	**46.0**	**49.0**
External	7.3	5.8	6.0	5.0	6.6	8.2	9.4	10.5	10.8	10.8	10.8
Domestic	17.5	21.4	23.2	25.9	28.3	27.7	27.9	29.5	32.2	35.2	38.2
Memorandum items:											
Non-interest expenditure growth (percent)											
in nominal terms	31.9	21.5	24.1	2.2	12.3	11.8	12.9	9.8	9.8	9.8	10.1
in real terms	16.3	12.7	17.4	-2.5	7.4	6.8	7.5	4.6	4.5	4.6	4.8
Cyclically-adjusted primary balance (percent of GDP)	1.7	-0.9	-2.3	-2.3	-2.2	-2.3	-2.7	-2.7	-2.7	-2.7	-2.7
Fiscal impulse (percent of GDP)	1.1	2.6	1.4	0.0	-0.1	0.2	0.4	0.0	0.0	0.0	0.0

Sources: Ministry of Finance; and Fund staff estimates.

1/ Transfers to the Social development and Family Transfers Fund (FODESAF) are recorded in net terms.

2/ The inflation adjustment of the principal of TUDES (inflation indexed bonds) was recorded as interest expenditure.

Table 4. Costa Rica: Summary Operations of the Central Government, GFSM 2001 Classification

					Est.	Projection					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
					(In billions of colones)						
Revenue	**2,490**	**2,363**	**2,617**	**2,869**	**3,147**	**3,510**	**3,890**	**4,264**	**4,684**	**5,156**	**5,670**
Taxes	2,409	2,262	2,492	2,767	3,028	3,380	3,747	4,107	4,512	4,967	5,462
Other revenue 1/	81	101	125	102	119	130	143	157	172	189	208
Expenditure	**2,536**	**2,970**	**3,649**	**3,765**	**4,195**	**4,729**	**5,445**	**6,078**	**6,782**	**7,582**	**8,465**
Expense	**2,191**	**2,668**	**3,200**	**3,461**	**3,833**	**4,298**	**4,901**	**5,479**	**6,126**	**6,867**	**7,668**
Compensation of employees	857	1,115	1,349	1,513	1,661	1,819	1,998	2,193	2,408	2,646	2,909
Purchases of goods and services	88	106	121	136	159	199	218	240	263	289	318
Interest 2/	415	393	452	497	527	628	814	994	1,202	1,456	1,721
Of which: Adjustment for TUDES	75	33	50	47	58	64	69	76	88	106	127
Social benefits	372	445	506	552	606	663	729	800	878	965	1,060
Other expense 3/	460	609	772	764	880	989	1,141	1,252	1,375	1,511	1,661
Net acquisition of nonfinancial assets	**344**	**302**	**449**	**304**	**363**	**431**	**544**	**599**	**656**	**716**	**797**
Gross operating balance	**299**	**-305**	**-583**	**-593**	**-686**	**-788**	**-1,011**	**-1,215**	**-1,442**	**-1,711**	**-1,998**
Net lending/borrowing	**-46**	**-606**	**-1,032**	**-896**	**-1,049**	**-1,218**	**-1,555**	**-1,814**	**-2,099**	**-2,426**	**-2,795**
Net financial transactions	**46**	**606**	**1,032**	**896**	**1,049**	**1,218**	**1,555**	**1,814**	**2,099**	**2,426**	**2,795**
					(In percent of GDP)						
Revenue	**15.9**	**14.0**	**13.7**	**13.9**	**13.9**	**14.1**	**14.3**	**14.2**	**14.2**	**14.3**	**14.3**
Tax revenue	15.3	13.4	13.1	13.4	13.3	13.6	13.7	13.7	13.7	13.7	13.8
Nontax revenue 1/	0.5	0.6	0.7	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Expenditure	**16.1**	**17.6**	**19.2**	**18.2**	**18.5**	**19.0**	**20.0**	**20.3**	**20.6**	**21.0**	**21.3**
Expense	**14.0**	**15.8**	**16.8**	**16.7**	**16.9**	**17.3**	**18.0**	**18.3**	**18.6**	**19.0**	**19.3**
Compensation of employees	5.5	6.6	7.1	7.3	7.3	7.3	7.3	7.3	7.3	7.3	7.3
Purchases of goods and services	0.6	0.6	0.6	0.7	0.7	0.8	0.8	0.8	0.8	0.8	0.8
Interest 2/	2.6	2.3	2.4	2.4	2.3	2.5	3.0	3.3	3.7	4.0	4.3
Of which: Adjustment for TUDES	0.5	0.2	0.3	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Social benefits	2.4	2.6	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
Other expense 3/	2.9	3.6	4.1	3.7	3.9	4.0	4.2	4.2	4.2	4.2	4.2
Net acquisition of nonfinancial assets	2.2	1.8	2.4	1.5	1.6	1.7	2.0	2.0	2.0	2.0	2.0
Gross operating balance	**1.9**	**-1.8**	**-3.1**	**-2.9**	**-3.0**	**-3.2**	**-3.7**	**-4.1**	**-4.4**	**-4.7**	**-5.0**
Net lending/borrowing	**-0.3**	**-3.6**	**-5.4**	**-4.3**	**-4.6**	**-4.9**	**-5.7**	**-6.1**	**-6.4**	**-6.7**	**-7.0**
Net financial transactions	**0.3**	**3.6**	**5.4**	**4.3**	**4.6**	**4.9**	**5.7**	**6.1**	**6.4**	**6.7**	**7.0**
Memorandum items:											
Non-interest expenditure growth (percent)											
in nominal terms	31.9	21.5	24.1	2.2	12.3	11.8	12.9	9.8	9.8	9.8	10.1
in real terms	16.3	12.7	17.4	-2.5	7.4	6.8	7.5	4.6	4.5	4.6	4.8
Primary balance											
in billions of colones	370	-213	-580	-400	-522	-590	-740	-820	-897	-970	-1,074
in percent of GDP	2.4	-1.3	-3.0	-1.9	-2.3	-2.4	-2.7	-2.7	-2.7	-2.7	-2.7
Cyclically-adjusted primary balance (percent of GDP)	1.7	-0.9	-2.3	-2.3	-2.2	-2.3	-2.7	-2.7	-2.7	-2.7	-2.7
Fiscal impulse (percent of GDP)	1.1	2.6	1.4	0.0	-0.1	0.2	0.4	0.0	0.0	0.0	0.0

Sources: Ministry of Finance; and Fund staff estimates.

1/ Transfers to the Social development and Family Transfers Fund (FODESAF) are recorded in net terms.

2/ The inflation adjustment of the principal of TUDES (inflation indexed bonds) was recorded as interest expenditure.

3/ Includes subsidies, transfers and other expense.

Table 5. Costa Rica: Consolidated Public Sector Operations 1/

					Est.	Projection					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
					(In billions of colones)						
Nonfinancial public sector:											
Revenue	**3,700**	**3,808**	**4,258**	**4,640**	**5,084**	**5,632**	**6,221**	**6,822**	**7,492**	**8,242**	**9,043**
Tax revenue	2,437	2,289	2,526	2,798	3,062	3,418	3,788	4,152	4,561	5,021	5,502
Nontax revenue	161	218	185	269	295	323	355	389	428	470	516
Social security contributions	1,057	1,227	1,412	1,532	1,682	1,842	2,023	2,221	2,438	2,679	2,945
Operating balance of public enterprises	46	75	134	41	45	50	55	60	66	72	79
Expenditure 2/	**3,640**	**4,343**	**5,209**	**5,410**	**5,928**	**6,655**	**7,623**	**8,496**	**9,414**	**10,485**	**11,630**
Current noninterest	2,755	3,469	4,138	4,391	4,853	5,384	5,969	6,551	7,193	7,904	8,688
Wages	1,201	1,545	1,885	2,051	2,251	2,465	2,708	2,972	3,263	3,586	3,941
Goods and services	355	387	414	446	499	571	628	689	756	831	914
Transfers	1,199	1,537	1,840	1,894	2,103	2,348	2,634	2,890	3,174	3,487	3,833
Interest 3/	383	381	432	509	563	662	861	1,050	1,261	1,517	1,778
Of which: Adjustment for TUDES 3/	41	18	28	26	32	35	38	42	49	58	70
Capital	503	493	638	510	513	608	792	895	959	1,065	1,164
Primary balance	**443**	**-154**	**-519**	**-260**	**-281**	**-360**	**-541**	**-624**	**-660**	**-726**	**-809**
Overall Balance	**60**	**-535**	**-951**	**-769**	**-844**	**-1,022**	**-1,402**	**-1,674**	**-1,921**	**-2,243**	**-2,587**
Central government	-46	-606	-1,032	-896	-1,049	-1,218	-1,555	-1,814	-2,099	-2,426	-2,795
Decentralized government entities	101	73	50	131	190	235	261	274	299	323	377
Public enterprises	4	-2	31	-4	14	-41	-109	-134	-120	-140	-170
Total Financing	**-60**	**535**	**951**	**769**	**844**	**1,022**	**1,402**	**1,674**	**1,921**	**2,243**	**2,587**
External	-54	-188	243	4	477	533	532	608	360	342	347
Domestic	-6	723	708	765	367	490	870	1,066	1,561	1,901	2,241
Consolidated public sector:											
Central Bank balance	-29	-138	-88	-126	-142	-182	-203	-225	-257	-308	-355
Consolidated public sector balance 1/	**31**	**-673**	**-1,039**	**-896**	**-987**	**-1,205**	**-1,605**	**-1,899**	**-2,177**	**-2,551**	**-2,942**
Consolidated public sector debt 1/	**4,292**	**4,925**	**5,824**	**6,862**	**8,650**	**9,822**	**11,237**	**13,064**	**15,060**	**17,320**	**19,903**
					(In percent of GDP)						
Nonfinancial public sector:											
Revenue	**23.6**	**22.6**	**22.4**	**22.5**	**22.4**	**22.7**	**22.8**	**22.8**	**22.8**	**22.8**	**22.8**
Tax revenue	15.5	13.6	13.3	13.5	13.5	13.8	13.9	13.9	13.9	13.9	13.9
Nontax revenue	1.0	1.3	1.0	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
Social security contributions	6.7	7.3	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
Operating balance of public enterprises	0.3	0.4	0.7	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Expenditure 2/	**23.2**	**25.8**	**27.4**	**26.2**	**26.1**	**26.8**	**27.9**	**28.4**	**28.6**	**29.0**	**29.3**
Current noninterest	17.5	20.6	21.7	21.2	21.4	21.7	21.9	21.9	21.9	21.9	21.9
Wages	7.6	9.2	9.9	9.9	9.9	9.9	9.9	9.9	9.9	9.9	9.9
Goods and services	2.3	2.3	2.2	2.2	2.2	2.3	2.3	2.3	2.3	2.3	2.3
Transfers	7.6	9.1	9.7	9.2	9.3	9.5	9.7	9.7	9.7	9.7	9.7
Interest 3/	2.4	2.3	2.3	2.5	2.5	2.7	3.2	3.5	3.8	4.2	4.5
Of which: Adjustment for TUDES 3/	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2
Capital	3.2	2.9	3.4	2.5	2.3	2.4	2.9	3.0	2.9	2.9	2.9
Primary balance	**2.8**	**-0.9**	**-2.7**	**-1.3**	**-1.2**	**-1.4**	**-2.0**	**-2.1**	**-2.0**	**-2.0**	**-2.0**
Overall Balance	**0.4**	**-3.2**	**-5.0**	**-3.7**	**-3.7**	**-4.1**	**-5.1**	**-5.6**	**-5.8**	**-6.2**	**-6.5**
Central government	-0.3	-3.6	-5.4	-4.3	-4.6	-4.9	-5.7	-6.1	-6.4	-6.7	-7.0
Decentralized government entities	0.6	0.4	0.3	0.6	0.8	0.9	1.0	0.9	0.9	0.9	0.9
Public enterprises	0.0	0.0	0.2	0.0	0.1	-0.2	-0.4	-0.4	-0.4	-0.4	-0.4
Total Financing	**-0.4**	**3.2**	**5.0**	**3.7**	**3.7**	**4.1**	**5.1**	**5.6**	**5.8**	**6.2**	**6.5**
External	-0.3	-1.1	1.3	0.0	2.1	2.1	1.9	2.0	1.1	0.9	0.9
Domestic	0.0	4.3	3.7	3.7	1.6	2.0	3.2	3.6	4.7	5.3	5.6
Consolidated public sector:											
Central Bank balance	-0.2	-0.8	-0.5	-0.6	-0.6	-0.7	-0.7	-0.8	-0.8	-0.9	-0.9
Consolidated public sector balance 1/	**0.2**	**-4.0**	**-5.5**	**-4.3**	**-4.4**	**-4.9**	**-5.9**	**-6.3**	**-6.6**	**-7.1**	**-7.4**
Consolidated public sector debt 1/	**27.3**	**29.2**	**30.6**	**33.2**	**38.1**	**39.5**	**41.2**	**43.6**	**45.8**	**47.9**	**50.1**
Consolidated public sector debt, including ICE	30.8	33.3	34.0	36.6	41.2	42.7	44.4	46.8	49.0	50.9	52.8

Sources: Ministry of Finance; and Fund staff estimates.

1/ The consolidated public sector balance comprises the central government, decentralized government entities, public enterprises and the Central Bank, but excludes the Instituto Costarricense de Electricidad (ICE).

2/ Expenditure was adjusted downward in 2010 and upward in 2011 by ½ percent of GDP to reflect a capital project recorded in 2010 but undertaken in 2011.

3/ The inflation adjustment of the principal of TUDES (inflation indexed bonds) was recorded as interest expenditure.

Table 6. Costa Rica: Summary Operations of the Consolidated Public Sector, GFSM 2001 Classification 1/

					Est.	Projection					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
					(In billions of colones)						
Nonfinancial public sector:											
Revenue	**3,700**	**3,808**	**4,258**	**4,640**	**5,084**	**5,632**	**6,221**	**6,822**	**7,492**	**8,242**	**9,043**
Taxes	2,437	2,289	2,526	2,798	3,062	3,418	3,788	4,152	4,561	5,021	5,502
Social contributions	1,057	1,227	1,412	1,532	1,682	1,842	2,023	2,221	2,438	2,679	2,945
Operating balance of public enterprises	46	75	134	41	45	50	55	60	66	72	79
Other revenue	161	218	185	269	295	323	355	389	428	470	516
Expenditure	**3,640**	**4,343**	**5,209**	**5,410**	**5,928**	**6,655**	**7,623**	**8,496**	**9,414**	**10,485**	**11,630**
Expense	**3,138**	**3,850**	**4,571**	**4,899**	**5,415**	**6,046**	**6,830**	**7,601**	**8,454**	**9,420**	**10,466**
Compensation of employees	1,201	1,545	1,885	2,051	2,251	2,465	2,708	2,972	3,263	3,586	3,941
Purchases of goods and services	355	387	414	446	499	571	628	689	756	831	914
Interest 2/	383	381	432	509	563	662	861	1,050	1,261	1,517	1,778
Of which: Adjustment for TUDES	41	18	28	26	32	35	38	42	49	58	70
Other expense 3/	1,199	1,537	1,840	1,894	2,103	2,348	2,634	2,890	3,174	3,487	3,833
Net acquisition of nonfinancial assets	**503**	**493**	**638**	**510**	**513**	**608**	**792**	**895**	**959**	**1,065**	**1,164**
Gross operating balance	**563**	**-42**	**-313**	**-259**	**-331**	**-414**	**-610**	**-779**	**-962**	**-1,178**	**-1,424**
Net lending/borrowing (NFPS)	**60**	**-535**	**-951**	**-769**	**-844**	**-1,022**	**-1,402**	**-1,674**	**-1,921**	**-2,243**	**-2,587**
Net financial transactions (NFPS)	**-60**	**535**	**951**	**769**	**844**	**1,022**	**1,402**	**1,674**	**1,921**	**2,243**	**2,587**
Consolidated public sector: 1/											
Central Bank balance	-29	-138	-88	-126	-142	-182	-203	-225	-257	-308	-355
Net lending/borrowing (consolidated public sector)	**31**	**-673**	**-1,039**	**-896**	**-987**	**-1,205**	**-1,605**	**-1,899**	**-2,177**	**-2,551**	**-2,942**
					(In percent of GDP)						
Nonfinancial public sector:											
Revenue	**23.6**	**22.6**	**22.4**	**22.5**	**22.4**	**22.7**	**22.8**	**22.8**	**22.8**	**22.8**	**22.8**
Taxes	15.5	13.6	13.3	13.5	13.5	13.8	13.9	13.9	13.9	13.9	13.9
Social contributions	6.7	7.3	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
Operating balance of public enterprises	0.3	0.4	0.7	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Other revenue	1.0	1.3	1.0	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
Expenditure	**23.2**	**25.8**	**27.4**	**26.2**	**26.1**	**26.8**	**27.9**	**28.4**	**28.6**	**29.0**	**29.3**
Expense	**20.0**	**22.9**	**24.0**	**23.7**	**23.9**	**24.3**	**25.0**	**25.4**	**25.7**	**26.1**	**26.4**
Compensation of employees	7.6	9.2	9.9	9.9	9.9	9.9	9.9	9.9	9.9	9.9	9.9
Purchases of goods and services	2.3	2.3	2.2	2.2	2.2	2.3	2.3	2.3	2.3	2.3	2.3
Interest 2/	2.4	2.3	2.3	2.5	2.5	2.7	3.2	3.5	3.8	4.2	4.5
Other expense 3/	7.6	9.1	9.7	9.2	9.3	9.5	9.7	9.7	9.7	9.7	9.7
Net acquisition of nonfinancial assets	**3.2**	**2.9**	**3.4**	**2.5**	**2.3**	**2.4**	**2.9**	**3.0**	**2.9**	**2.9**	**2.9**
Gross operating balance	**3.6**	**-0.2**	**-1.6**	**-1.3**	**-1.5**	**-1.7**	**-2.2**	**-2.6**	**-2.9**	**-3.3**	**-3.6**
Net lending/borrowing (NFPS)	**0.4**	**-3.2**	**-5.0**	**-3.7**	**-3.7**	**-4.1**	**-5.1**	**-5.6**	**-5.8**	**-6.2**	**-6.5**
Net financial transactions (NFPS)	**-0.4**	**3.2**	**5.0**	**3.7**	**3.7**	**4.1**	**5.1**	**5.6**	**5.8**	**6.2**	**6.5**
Consolidated public sector: 1/											
Central Bank balance	-0.2	-0.8	-0.5	-0.6	-0.6	-0.7	-0.7	-0.8	-0.8	-0.9	-0.9
Net lending/borrowing (consolidated public sector)	**0.2**	**-4.0**	**-5.5**	**-4.3**	**-4.4**	**-4.9**	**-5.9**	**-6.3**	**-6.6**	**-7.1**	**-7.4**
Memorandum items:											
NFPS non-interest expenditure growth (percent)											
in nominal terms	29.9	21.6	20.6	2.6	9.5	11.7	12.8	10.1	9.5	10.0	9.8
in real terms	14.6	12.8	14.1	-2.2	4.8	6.7	7.5	4.9	4.3	4.8	4.6
NFPS primary balance											
in billions of colones	443	-154	-519	-260	-281	-360	-541	-624	-660	-726	-809
in percent of GDP	2.8	-0.9	-2.7	-1.3	-1.2	-1.4	-2.0	-2.1	-2.0	-2.0	-2.0

Sources: Ministry of Finance; and Fund staff estimates.

1/ The consolidated public sector balance comprises the central government, decentralized government entities, public enterprises and the Central Bank, but excludes the Instituto Costarricense de Electricidad (ICE).

2/ The inflation adjustment of the principal of TUDES (inflation indexed bonds) was recorded as interest expenditure.

3/ Includes subsidies, transfers and other expense.

Table 7. Costa Rica: Public Sector Debt

	2008	2009	2010	2011	Est. 2012	Projection 2013	2014	2015	2016	2017	2018
	(In billions of colones)										
Debt issued by:											
NFPS & Central Bank (I) 1/	**5,659**	**6,443**	**7,574**	**8,961**	**10,964**	**12,398**	**14,107**	**16,244**	**18,574**	**21,194**	**24,191**
Nonfinancial public sector (NFPS) 1/	4,137	5,018	6,168	7,248	8,792	9,864	11,185	13,063	15,277	17,827	20,752
Central government	3,891	4,587	5,562	6,382	7,904	8,923	10,180	11,995	14,140	16,619	19,472
Rest of nonfinancial public sector 1/	246	431	605	866	888	940	1,005	1,069	1,137	1,208	1,280
Central Bank	1,522	1,425	1,406	1,713	2,173	2,534	2,922	3,180	3,298	3,368	3,439
Intra-public sector debt holdings (II)	**1,367**	**1,519**	**1,750**	**2,099**	**2,315**	**2,576**	**2,870**	**3,179**	**3,515**	**3,875**	**4,288**
CCSS 2/	889	987	1,130	1,330	1,471	1,653	1,856	2,066	2,292	2,531	2,811
Other entities of the nonfinancial public sector	458	514	604	756	829	908	998	1,095	1,203	1,321	1,452
Central Bank	20	18	15	13	14	15	17	18	20	22	25
Consolidated public sector debt (I-II)	**4,292**	**4,925**	**5,824**	**6,862**	**8,650**	**9,822**	**11,237**	**13,064**	**15,060**	**17,320**	**19,903**
External	1,353	1,207	1,363	1,330	1,763	2,300	2,832	3,436	3,843	4,241	4,651
Domestic	2,939	3,717	4,461	5,532	6,887	7,522	8,405	9,628	11,217	13,079	15,252
	(In percent of GDP)										
Debt issued by:											
NFPS & Central Bank (I) 1/	**36.0**	**38.3**	**39.8**	**43.4**	**48.3**	**49.9**	**51.7**	**54.2**	**56.5**	**58.7**	**60.9**
Nonfinancial public sector (NFPS) 1/	26.3	29.8	32.4	35.1	38.8	39.7	41.0	43.6	46.5	49.3	52.2
Central government	24.8	27.2	29.2	30.9	34.8	35.9	37.3	40.0	43.0	46.0	49.0
Rest of nonfinancial public sector 1/	1.6	2.6	3.2	4.2	3.9	3.8	3.7	3.6	3.5	3.3	3.2
Central Bank	9.7	8.5	7.4	8.3	9.6	10.2	10.7	10.6	10.0	9.3	8.7
Intra-public sector debt holdings (II)	**8.7**	**9.0**	**9.2**	**10.2**	**10.2**	**10.4**	**10.5**	**10.6**	**10.7**	**10.7**	**10.8**
CCSS	5.7	5.9	5.9	6.4	6.5	6.7	6.8	6.9	7.0	7.0	7.1
Other entities of the nonfinancial public sector	2.9	3.1	3.2	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7
Central Bank	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Consolidated public sector debt (I-II)	**27.3**	**29.2**	**30.6**	**33.2**	**38.1**	**39.5**	**41.2**	**43.6**	**45.8**	**47.9**	**50.1**
External	8.6	7.2	7.2	6.4	7.8	9.3	10.4	11.5	11.7	11.7	11.7
Domestic	18.7	22.1	23.4	26.8	30.4	30.3	30.8	32.1	34.1	36.2	38.4
Memorandum items:											
Debt issued by ICE	3.4	4.1	3.4	3.4	3.1	3.2	3.2	3.2	3.2	3.0	2.7
Consolidated public sector debt including ICE	30.8	33.3	34.0	36.6	41.2	42.7	44.4	46.8	49.0	50.9	52.8

Sources: Ministry of Finance; and Fund staff estimates.

1/ Excludes the debt issued by the Instituto Costarricense de Electricidad (ICE).

2/ Caja Costarricense del Seguro Social (social security agency).

Table 8. Costa Rica: Monetary Survey

					Est.	Projection	
	2008	2009	2010	2011	2012	2013	2014
	(In billions of colones, unless otherwise indicated)						
Central Bank							
Net foreign assets	2,178	2,413	2,485	2,567	3,637	4,376	4,896
Net international reserves	2,090	2,272	2,350	2,403	3,469	4,198	4,715
(In millions of U.S. dollars)	3,799	4,066	4,627	4,756	6,857	8,357	9,357
Net medium-term foreign assets	89	141	135	164	167	178	182
Net domestic assets	-1,027	-1,203	-1,140	-1,067	-1,984	-2,560	-2,903
Net domestic credit	-547	-790	-926	-729	-1,275	-1,173	-1,368
Monetary stabilization instruments (-)	-1,513	-1,414	-1,407	-1,812	-2,155	-2,520	-2,912
Other items (net)	-186	-265	-153	-3	-174	-668	-627
Capital account (-)	1,219	1,266	1,346	1,477	1,619	1,801	2,004
Monetary base	1,151	1,210	1,345	1,500	1,653	1,816	1,993
Currency	575	613	665	743	812	887	966
Required reserves	576	597	680	757	840	929	1,028
Other Depository Institutions							
Net foreign assets	-420	-20	-87	-580	-920	-1,018	-1,119
Net domestic assets	7,840	8,325	8,389	9,287	10,393	11,389	12,511
Net domestic credit	10,160	11,194	11,897	13,206	15,038	16,754	18,706
Credit to nonfinancial public sector (net)	412	693	980	1,001	1,145	1,244	1,505
Credit to nonfinancial private sector	7,925	8,281	8,645	9,832	11,079	12,471	13,883
Credit to financial corporations (net)	1,823	2,221	2,273	2,373	2,813	3,039	3,319
Other items (net)	-722	-1,039	-1,473	-1,625	-2,200	-2,608	-3,138
Capital account	1,597	1,829	2,036	2,294	2,445	2,757	3,056
Liabilities to nonfinancial private sector	7,420	8,305	8,301	8,707	9,473	10,370	11,392
In national currency	4,080	4,461	4,911	5,171	5,932	6,554	7,198
In foreign currency	3,341	3,844	3,390	3,536	3,541	3,878	4,288
Of which: Deposits	7,255	8,111	8,096	8,470	9,239	10,115	11,138
Consolidated Financial System							
Net foreign assets	1,758	2,393	2,398	1,988	2,717	3,358	3,777
Net domestic assets	7,059	7,282	7,393	8,426	8,853	9,564	10,638
Net domestic credit	8,317	8,923	9,336	10,746	11,706	13,873	15,679
Other items (net)	-879	-1,077	-1,253	-1,503	-2,027	-3,353	-3,989
Capital account	378	564	690	817	826	956	1,052
Broad money	8,818	9,675	9,791	10,414	11,570	12,922	14,415
Memorandum Items:	(Annual percentage change)						
Monetary base	11.9	5.1	11.2	11.6	10.1	9.9	9.8
Broad money	16.1	9.7	1.2	6.4	11.1	11.7	11.6
Adjusted by changes in the exchange rate	10.2	13.4	5.5	2.8	12.0	10.6	11.6
Credit to the private sector	31.8	4.5	4.4	13.7	12.7	12.6	11.3
Adjusted by changes in the exchange rate	23.7	8.7	9.3	9.5	13.8	11.1	11.4
	(In percent of GDP)						
Monetary base	7.3	7.2	7.1	7.3	7.3	7.3	7.3
Broad money	56.2	57.4	51.4	50.4	51.0	52.0	52.8
Of which: Deposits denominated in foreign currency	21.3	22.8	17.8	17.1	15.6	15.6	15.7
Credit to the private sector	50.5	49.2	45.4	47.6	48.8	50.2	50.9
Of which: In foreign currency	22.4	20.9	17.5	18.7	19.6	20.5	20.7
Central bank balance	-0.2	-0.3	-0.4	-0.6	-0.6	-0.7	-0.7

Sources: Central bank of Costa Rica; and Fund staff estimates.

Table 9. Costa Rica: Medium-Term Framework

					Est.	Projection					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
	(Annual percentage change)										
Real GDP	2.7	-1.0	4.7	4.2	5.0	4.2	4.4	4.5	4.5	4.5	4.5
Domestic demand	7.7	-8.1	9.1	6.1	5.5	4.5	5.0	5.0	5.0	4.9	4.9
Consumption	3.5	2.3	4.6	4.2	4.4	4.1	4.1	4.2	4.2	4.3	4.3
Gross fixed capital formation	11.0	-11.1	4.1	8.3	7.1	6.7	10.1	7.6	6.5	7.0	6.7
Exports of goods and nonfactor services	-2.0	-6.0	4.9	6.7	8.8	5.3	6.3	5.8	5.8	5.7	4.7
Imports of goods and nonfactor services	6.5	-18.9	14.0	10.6	9.9	5.8	7.4	6.6	6.7	6.4	5.3
	(Contributions to real GDP growth)										
Domestic demand	7.4	-8.1	8.4	5.9	5.4	4.4	5.0	5.0	5.0	4.9	4.9
Consumption	2.5	1.6	3.4	3.1	3.3	3.0	3.0	3.1	3.1	3.1	3.1
Gross fixed capital formation	2.5	-2.7	0.9	1.8	1.6	1.5	2.4	1.9	1.7	1.8	1.8
Inventory changes	2.3	-7.0	4.1	0.9	0.6	-0.1	-0.4	0.0	0.2	0.0	0.0
Net exports	-4.6	7.1	-3.7	-1.7	-0.4	-0.2	-0.6	-0.5	-0.5	-0.4	-0.4
	(In percent of GDP)										
Savings and Investment											
Savings	27.6	16.3	20.1	20.6	20.8	20.5	20.7	20.9	21.1	21.3	21.5
Domestic savings	18.2	14.3	16.6	15.3	15.3	15.1	15.2	15.3	15.3	15.3	15.6
External savings 1/	9.3	2.0	3.5	5.3	5.5	5.4	5.5	5.7	5.8	6.0	6.0
Gross domestic investment	27.6	16.3	20.1	20.6	20.8	20.5	20.7	20.9	21.1	21.3	21.5
Private sector	19.6	18.4	16.4	16.3	16.5	16.4	16.4	16.5	16.7	17.0	17.2
Public sector	4.0	3.6	3.5	3.4	3.1	3.0	3.6	3.7	3.6	3.6	3.6
Inventory changes	4.0	-5.8	0.2	1.0	1.2	1.1	0.8	0.7	0.8	0.7	0.7
Balance of payments											
Current account balance	-9.3	-2.0	-3.5	-5.3	-5.5	-5.4	-5.5	-5.7	-5.8	-6.0	-6.0
Trade balance	-16.8	-6.9	-9.5	-12.6	-12.6	-12.3	-12.3	-12.3	-12.2	-12.1	-11.9
Services	7.4	7.4	7.0	7.9	8.2	8.3	8.2	8.1	8.0	7.8	7.7
Income	-1.4	-3.7	-2.1	-1.4	-1.9	-2.0	-2.1	-2.2	-2.3	-2.4	-2.3
Current transfers	1.5	1.2	1.0	0.8	0.8	0.7	0.7	0.7	0.8	0.7	0.6
Financial and capital account	8.3	1.7	5.5	6.3	10.1	8.4	7.4	7.0	6.1	6.1	6.0
Public sector	0.0	1.0	1.7	0.1	1.8	2.0	1.8	1.7	1.0	1.0	0.9
Private sector	8.3	0.7	3.8	6.1	8.3	6.4	5.5	5.3	5.1	5.1	5.1
Foreign direct investment	6.9	4.6	4.0	5.1	5.0	4.8	4.5	4.3	4.2	4.2	4.3
Other net private flows	1.4	-3.9	-0.2	1.0	3.3	1.6	1.0	1.0	1.0	0.8	0.8
Errors and omissions	-0.2	0.4	-0.4	-0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in net international reserves (increase -)	1.2	-0.2	-1.5	-0.3	-4.7	-3.0	-1.8	-1.3	-0.3	-0.1	-0.1
Memorandum items:											
Nominal GDP (billions of colones)	15,702	16,845	19,044	20,666	22,683	24,841	27,290	29,952	32,885	36,134	39,719
GDP deflator (percent change)	12.4	8.4	8.0	4.1	4.5	5.1	5.2	5.0	5.1	5.1	5.2
Consumer prices (percent change; period average)	13.4	7.8	5.7	4.9	4.5	4.7	5.0	5.0	5.0	5.0	5.0
Consumer prices (percent change; end of period)	13.9	4.0	5.8	4.7	4.6	5.0	5.0	5.0	5.0	5.0	5.0
Net international reserves (millions of U.S. dollars)	3,799	4,066	4,627	4,756	6,857	8,357	9,357	10,157	10,357	10,407	10,457

Sources: Central Bank of Costa Rica; and Fund staff estimates.
1/ External current account deficit.

Table 10. Costa Rica: Banking Sector Indicators

	2008 Dec	2009 Dec	2010 Dec	2011 Dec	2012 Nov
			(In percent)		
Capitalization					
Risk-adjusted capital ratio	15.1	16.0	17.3	17.3	17.2
Capital-to-assets ratio	13.3	13.9	14.8	15.0	15.1
Asset quality					
Nonperforming loans to total loans	1.5	2.0	1.8	1.7	1.7
Non-income generating assets to total assets	18.2	18.6	17.4	17.7	17.2
Foreclosed assets to total assets	0.3	0.6	0.8	0.8	1.0
Loan loss provisions to total loans	1.8	1.9	1.8	1.8	1.7
Management					
Administrative expenses to total assets	4.4	4.1	4.3	4.2	4.2
Noninterest expenses to gross income	79.3	76.8	85.0	76.5	68.9
Total expenses to total revenues	92.5	95.2	96.2	93.1	91.0
Profitability					
Return on assets (ROA)	1.8	1.1	1.2	1.3	1.5
Return on equity (ROE)	14.3	8.7	8.3	9.1	10.3
Interest margin to gross income	20.8	20.7	16.6	27.2	31.3
Liquidity					
Liquid assets to total short-term liabilities	83.0	93.4	90.1	85.1	92.4
Liquid assets to total assets	27.7	30.6	30.7	28.8	28.9
Loans to deposits	109.7	98.9	97.8	105.2	106.4
Liquid assets to deposits	42.1	43.9	43.8	42.7	43.4
Sensitivity to market risk					
Net open FX position to capital	20.4	25.4	18.8	18.8	19.1
Other					
Financial margin 1/	7.9	7.7	8.2	8.1	7.8

Source: Superintendency of Banks (SUGEF).

1/ Difference between implicit loan and deposit rates.

Table 11. Costa Rica: Medium-Term Framework Under Fiscal Consolidation Scenario

					Est.	Projection					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
	(Annual percentage change)										
Real GDP	2.7	-1.0	4.7	4.2	5.0	4.2	4.0	3.8	4.2	4.5	4.5
	(In percent of GDP)										
Savings and Investment											
Savings	27.6	16.3	20.1	20.6	20.8	20.5	20.2	20.3	20.6	20.7	20.9
Domestic savings	18.2	14.3	16.6	15.3	15.3	15.0	15.4	15.5	15.6	15.8	16.0
External savings 1/	9.3	2.0	3.5	5.3	5.5	5.5	4.9	4.8	4.9	4.9	4.8
Gross domestic investment	27.6	16.3	20.1	20.6	20.8	20.5	20.2	20.3	20.6	20.7	20.9
Private sector	19.6	18.4	16.4	16.3	16.5	16.4	16.4	16.5	16.7	16.9	17.1
Public sector	4.0	3.6	3.5	3.4	3.1	3.0	3.6	3.7	3.6	3.7	3.7
Inventory changes	4.0	-5.8	0.2	1.0	1.2	1.1	0.3	0.1	0.2	0.1	0.1
Public Finances											
Central government primary balance	2.4	-1.3	-3.0	-1.9	-2.3	-2.3	-1.8	-0.2	-0.1	0.0	0.1
Central government overall balance	-0.3	-3.6	-5.4	-4.3	-4.6	-4.8	-4.8	-3.5	-3.4	-3.3	-3.1
Central government debt	24.8	27.2	29.2	30.9	34.8	35.9	36.6	37.2	37.6	37.7	37.6
Consolidated public sector overall balance	0.2	-4.0	-5.5	-4.3	-4.4	-4.8	-5.0	-3.8	-3.6	-3.5	-3.3
Consolidated public sector debt	27.3	29.2	30.6	33.2	38.1	39.5	40.5	40.7	40.3	39.4	38.4
Balance of payments											
Current account balance	-9.3	-2.0	-3.5	-5.3	-5.5	-5.5	-4.9	-4.8	-4.9	-4.9	-4.8
Trade balance	-16.8	-6.9	-9.5	-12.6	-12.6	-12.6	-12.0	-12.1	-12.4	-12.5	-12.5
Services	7.4	7.4	7.0	7.9	8.2	8.4	8.6	8.8	9.0	9.1	9.2
Income	-1.4	-3.7	-2.1	-1.4	-1.9	-2.0	-2.1	-2.3	-2.3	-2.4	-2.4
Current transfers	1.5	1.2	1.0	0.8	0.8	0.7	0.7	0.8	0.9	0.8	0.8
Financial and capital account	8.3	1.7	5.5	6.3	10.1	8.5	6.3	5.8	5.2	5.0	4.9
Public sector	0.0	1.0	1.7	0.1	1.8	2.0	1.7	1.3	0.7	0.3	0.2
Private sector	8.3	0.7	3.8	6.1	8.3	6.5	4.6	4.5	4.5	4.7	4.7
Foreign direct investment	6.9	4.6	4.0	5.1	5.0	4.8	4.5	4.5	4.5	4.6	4.7
Other net private flows	1.4	-3.9	-0.2	1.0	3.3	1.8	0.2	0.1	0.1	0.1	0.0
Errors and omissions	-0.2	0.4	-0.4	-0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in net international reserves (increase -)	1.2	-0.2	-1.5	-0.3	-4.7	-3.0	-1.5	-1.0	-0.3	-0.1	-0.1
Memorandum items:											
Nominal GDP (billions of colones)	15,702	16,845	19,044	20,666	22,683	24,818	27,126	29,510	32,213	35,239	38,537
GDP deflator (percent change)	12.4	8.4	8.0	4.1	4.5	5.0	5.1	4.8	4.8	4.7	4.7
Consumer prices (percent change; period average)	13.4	7.8	5.7	4.9	4.5	4.7	5.1	5.1	4.7	4.2	4.0
Consumer prices (percent change; end of period)	13.9	4.0	5.8	4.7	4.6	5.0	5.3	5.0	4.5	4.0	4.0
Net international reserves (millions of U.S. dollars)	3,799	4,066	4,627	4,756	6,857	8,357	9,157	9,757	9,957	10,007	10,057

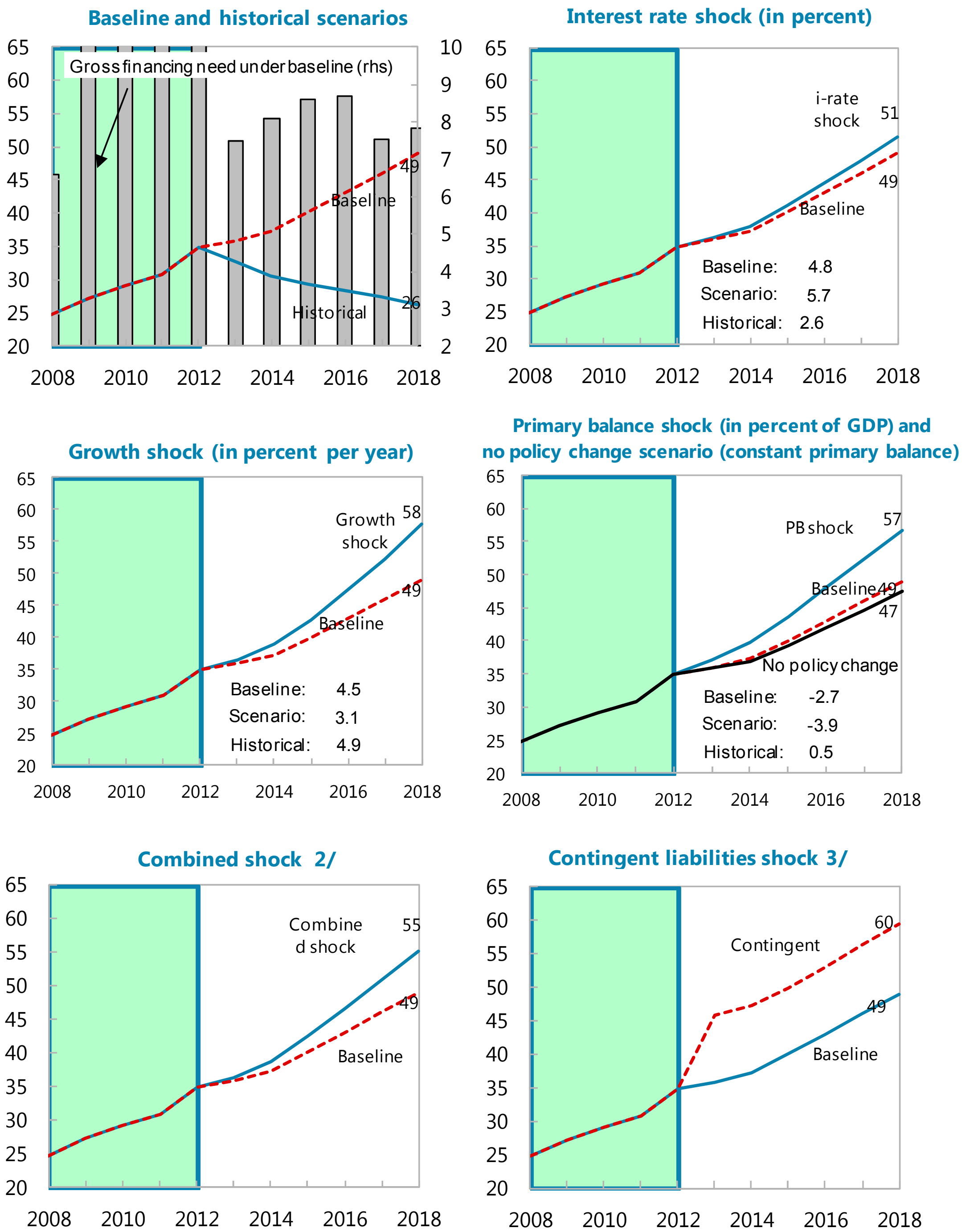
Sources: Central Bank of Costa Rica; and Fund staff estimates.
1/ External current account deficit.

Table 12. Costa Rica: Central Government Debt Sustainability Framework, 2010-2018
(In percent of GDP, unless otherwise indicated)

	Actual		Est.	Projections						
	2010	2011	2012	2013	2014	2015	2016	2017	2018	
				I. Baseline Projections						Debt-stabilizing primary balance 7/
Public sector debt 1/	**29.2**	**30.9**	**34.8**	**35.9**	**37.3**	**40.0**	**43.0**	**46.0**	**49.0**	**0.4**
o/w foreign-currency denominated	9.9	9.2	11.1	12.6	13.8	15.2	15.9	16.5	16.9	
Change in public sector debt	2.0	1.7	4.0	1.1	1.4	2.7	3.0	3.0	3.0	
Identified debt-creating flows (4+7+12)	2.7	1.0	4.0	1.1	1.4	2.7	2.9	3.0	3.0	
Primary deficit	3.0	1.9	2.3	2.4	2.7	2.7	2.7	2.7	2.7	
Revenue and grants	13.7	13.9	13.9	14.1	14.3	14.2	14.2	14.3	14.3	
Primary (noninterest) expenditure	16.8	15.8	16.2	16.5	17.0	17.0	17.0	17.0	17.0	
Automatic debt dynamics 2/	-1.6	0.1	-0.6	-0.5	-0.2	0.0	0.2	0.3	0.3	
Contribution from interest rate/growth differential 3/	-0.8	0.1	-0.4	-0.5	-0.2	0.0	0.1	0.2	0.2	
Of which contribution from real interest rate	0.4	1.2	1.0	0.8	1.2	1.5	1.7	1.9	2.1	
Of which contribution from real GDP growth	-1.1	-1.1	-1.4	-1.3	-1.4	-1.5	-1.6	-1.8	-1.9	
Contribution from exchange rate depreciation 4/	-0.8	0.0	-0.1	...	...	...	...	...	...	
Other identified debt-creating flows	1.2	-1.1	2.2	-0.8	-1.1	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Change in government deposits	1.2	-1.1	2.2	-0.8	-1.1	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3)	-0.7	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	212.6	222.5	251.2	254.2	261.7	281.3	301.9	322.3	343.4	
Gross financing need 5/	16.0	16.0	10.2	7.5	8.1	8.6	8.7	7.5	7.8	
in billions of U.S. dollars	5.8	6.5	4.6	3.7	4.4	5.2	5.7	5.3	6.0	
Key Macroeconomic and Fiscal Assumptions										Projected Average
Real GDP growth (in percent)	4.7	4.2	5.0	4.2	4.4	4.5	4.5	4.5	4.5	4.5
Average nominal interest rate on public debt (in percent) 6/	9.9	8.9	8.3	7.9	9.1	9.8	10.0	10.3	10.4	9.9
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	1.8	4.8	3.7	2.9	3.9	4.7	5.0	5.2	5.2	4.8
Nominal appreciation (increase in US dollar value of local currency, in percent)	10.2	0.2	2.8	-0.4	-0.2	0.0	-1.4	-1.4	-1.4	-0.9
Inflation rate (GDP deflator, in percent)	8.0	4.1	4.5	5.1	5.2	5.0	5.1	5.1	5.2	5.1
Growth of real primary spending (deflated by GDP deflator, in percent)	14.9	-1.8	7.4	6.3	7.3	4.5	4.5	4.4	4.7	5.1
Primary deficit	3.0	1.9	2.3	2.4	2.7	2.7	2.7	2.7	2.7	2.7

Source:
1/ Central government debt.
2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = 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).
3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.
4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).
5/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.
6/ Derived as nominal interest expenditure divided by previous period debt stock.
7/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 5. Costa Rica: Central Government Debt Sustainability: Bound Tests 1/ (debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and Fund staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.
3/ Ten percent of GDP shock to contingent liabilities occurs in 2009.

Table 13. Costa Rica: Consolidated Public Sector Debt Sustainability Framework, 2010-2018

(In percent of GDP, unless otherwise indicated)

	Actual		Est.	Projections						
	2010	2011	2012	2013	2014	2015	2016	2017	2018	
				I. Baseline Projections						**Debt-stabilizing primary balance 7/**
Public sector debt 1/	**30.6**	**33.2**	**38.1**	**39.5**	**41.2**	**43.6**	**45.8**	**47.9**	**50.1**	**-0.7**
o/w foreign-currency denominated	11.3	10.9	12.5	13.9	15.0	16.3	16.9	17.4	17.8	
Change in public sector debt	1.3	2.6	4.9	1.4	1.6	2.4	2.2	2.1	2.2	
Identified debt-creating flows (4+7+12)	2.1	3.0	4.9	1.4	1.6	2.4	2.2	2.1	2.2	
Primary deficit	3.2	1.9	1.9	2.2	2.7	2.8	2.8	2.9	2.9	
Revenue and grants	22.4	22.5	22.4	22.7	22.8	22.8	22.8	22.8	22.8	
Primary (noninterest) expenditure	25.5	24.3	24.3	24.9	25.5	25.6	25.6	25.7	25.7	
Automatic debt dynamics 2/	-2.1	0.0	-0.6	-0.6	-0.4	-0.2	0.1	0.2	0.3	
Contribution from interest rate/growth differential 3/	-1.1	0.1	-0.5	-0.6	-0.4	-0.2	-0.1	0.1	0.2	
Of which: contribution from real interest rate	0.1	1.2	1.0	0.8	1.2	1.5	1.7	2.0	2.1	
Of which: contribution from real GDP growth	-1.2	-1.2	-1.5	-1.5	-1.6	-1.7	-1.8	-1.9	-2.0	
Contribution from exchange rate depreciation 4/	-1.0	0.0	-0.2	...	...	...	...	...	...	
Contribution from exchange rate depreciation 4/	-1.0	0.0	-0.2	0.1	0.0	0.0	0.1	0.1	0.1	
Denominator = 1+g+p+gp	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	
Other identified debt-creating flows	1.0	1.1	3.7	-0.2	-0.7	-0.2	-0.7	-1.0	-1.1	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net public sector asset changes 5/	1.0	1.1	3.7	-0.2	-0.7	-0.2	-0.7	-1.0	-1.1	
Residual, including asset changes (2-3)	-0.8	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio	136.8	147.9	170.1	174.4	180.6	191.5	201.0	210.1	220.1	
Gross financing need 6/	16.2	16.2	10.1	7.5	8.3	9.0	9.0	7.9	8.2	
in billions of U.S. dollars	5.9	6.6	4.5	3.7	4.5	5.4	5.8	5.6	6.3	
Key Macroeconomic and Fiscal Assumptions										Projected Average
Real GDP growth (in percent)	4.7	4.2	5.0	4.2	4.4	4.5	4.5	4.5	4.5	4.5
Average nominal interest rate on public debt (in percent) 7/	8.8	8.7	8.2	7.7	8.8	9.3	9.7	10.1	10.3	9.6
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	0.8	4.6	3.7	2.6	3.5	4.3	4.6	4.9	5.1	4.5
Nominal appreciation (increase in US dollar value of local currency, in percent)	10.2	0.2	2.8	-0.4	-0.2	0.0	-1.4	-1.4	-1.4	-0.9
Inflation rate (GDP deflator, in percent)	8.0	4.1	4.5	5.1	5.2	5.0	5.1	5.1	5.2	5.1
Growth of real primary spending (deflated by GDP deflator, in percent)	9.8	-0.8	4.8	6.7	7.2	4.9	4.3	4.9	4.6	5.2
Primary deficit	3.2	1.9	1.9	2.2	2.7	2.8	2.8	2.9	2.9	2.8

Source:

1/ Consolidated public sector debt.

2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = 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).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.

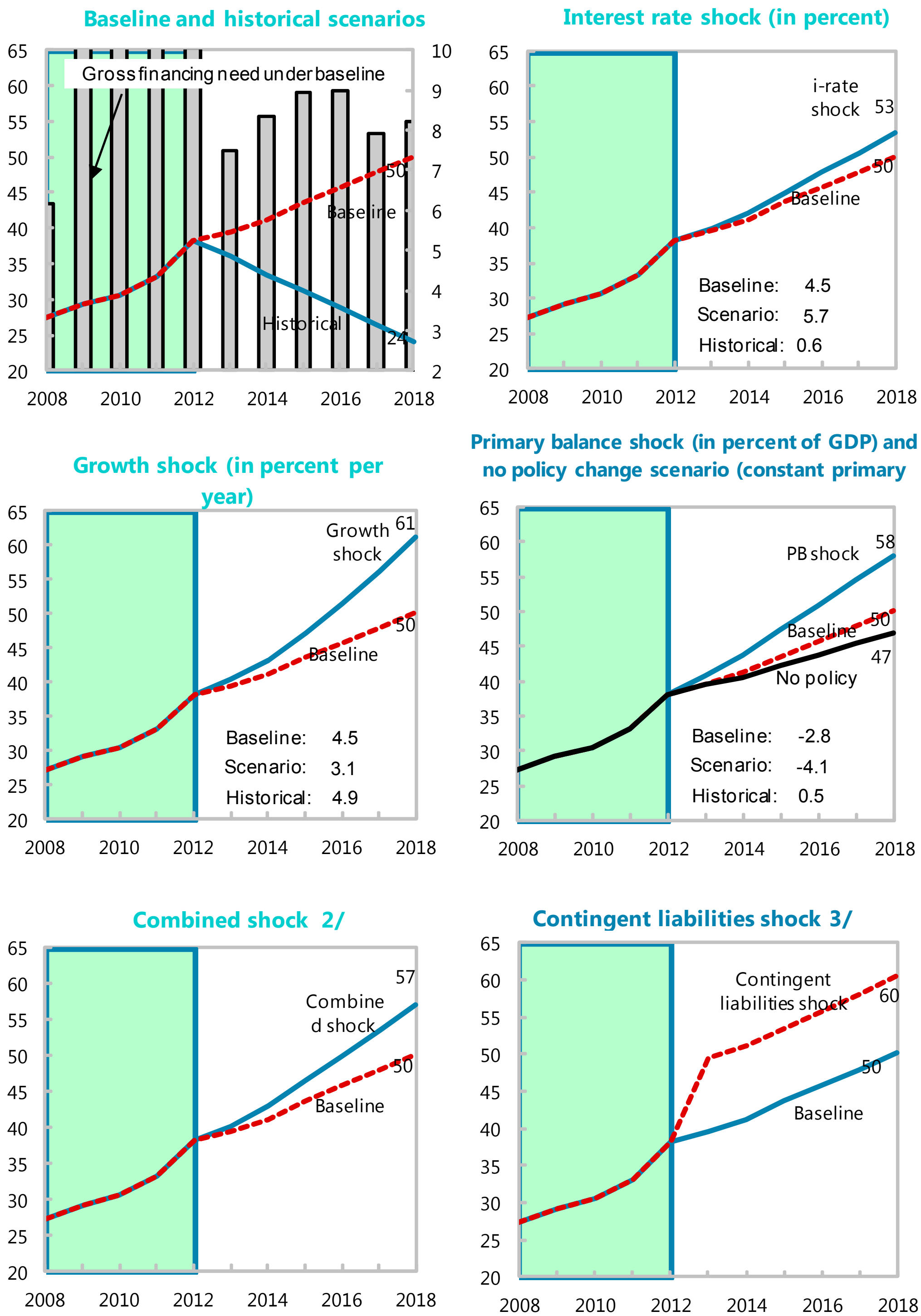
4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

5/ Comprises pre-financing, net purchases of private sector assets by the social security agency and issuance of monetary sterilization bonds.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ Derived as nominal interest expenditure divided by previous period debt stock.

Figure 6. Costa Rica: Public Debt Sustainability: Bound Tests 1/
(Public debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and Fund staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.
3/ Ten percent of GDP shock to contingent liabilities occurs in 2009.

Table 14. Costa Rica: Consolidated Public Sector Debt Sustainability Framework (Under Fiscal Consolidation Scenario), 2010-2018

(In percent of GDP, unless otherwise indicated)

	Actual		Est.	Projections						
	2010	2011	2012	2013	2014	2015	2016	2017	2018	
						I. Baseline Projections				**Debt-stabilizing primary balance 7/**
Public sector debt 1/	**30.6**	**33.2**	**38.1**	**39.5**	**40.5**	**40.7**	**40.3**	**39.4**	**38.4**	**-0.9**
o/w foreign-currency denominated	11.3	10.9	12.5	13.9	15.0	16.0	16.2	16.2	16.1	
Change in public sector debt	1.3	2.6	4.9	1.4	1.0	0.1	-0.4	-0.9	-1.0	
Identified debt-creating flows (4+7+12)	2.1	3.0	4.9	1.4	1.0	0.2	-0.4	-0.8	-1.0	
Primary deficit	3.2	1.9	1.9	2.1	1.8	0.3	0.1	0.0	0.0	
Revenue and grants	22.4	22.5	22.4	22.7	23.5	25.0	25.0	25.1	25.0	
Primary (noninterest) expenditure	25.5	24.3	24.3	24.8	25.3	25.3	25.2	25.1	25.0	
Automatic debt dynamics 2/	-2.1	0.0	-0.6	-0.6	-0.1	0.2	0.1	0.1	0.1	
Contribution from interest rate/growth differential 3/	-1.1	0.1	-0.5	-0.6	-0.1	0.2	0.1	0.0	0.0	
Of which: contribution from real interest rate	0.1	1.2	1.0	0.9	1.3	1.6	1.6	1.6	1.6	
Of which: contribution from real GDP growth	-1.2	-1.2	-1.5	-1.5	-1.4	-1.4	-1.6	-1.7	-1.6	
Contribution from exchange rate depreciation 4/	-1.0	0.0	-0.2	...	...	...	...	...	...	
Other identified debt-creating flows	1.0	1.1	3.7	-0.2	-0.7	-0.4	-0.7	-0.9	-1.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net public sector asset changes 5/	1.0	1.1	3.7	-0.2	-0.7	-0.4	-0.7	-0.9	-1.0	
Residual, including asset changes (2-3)	-0.8	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio	136.8	147.9	170.1	174.2	172.2	162.7	160.9	157.2	153.3	
Gross financing need 6/	16.2	16.2	10.1	7.4	7.5	6.5	6.0	4.4	4.2	
in billions of U.S. dollars	5.9	6.6	4.5	3.7	4.1	3.8	3.8	3.0	3.2	
Key Macroeconomic and Fiscal Assumptions										Projected Average
Real GDP growth (in percent)	4.7	4.2	5.0	4.2	4.0	3.8	4.2	4.5	4.5	4.2
Average nominal interest rate on public debt (in percent) 7/	8.8	8.7	8.2	7.7	8.9	9.4	9.4	9.3	9.4	9.3
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	0.8	4.6	3.7	2.7	3.8	4.6	4.6	4.7	4.7	4.5
Nominal appreciation (increase in US dollar value of local currency, in percent)	10.2	0.2	2.8	-0.4	-0.4	0.0	-0.9	-0.5	-0.5	-0.4
Inflation rate (GDP deflator, in percent)	8.0	4.1	4.5	5.0	5.1	4.8	4.8	4.7	4.7	4.8
Growth of real primary spending (deflated by GDP deflator, in percent)	9.8	-0.8	4.8	6.3	6.4	3.7	3.6	4.3	4.1	4.4
Primary deficit	3.2	1.9	1.9	2.1	1.8	0.3	0.1	0.0	0.0	0.5

Source:

1/ Consolidated public sector debt.

2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = 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).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

5/ Comprises pre-financing, net purchases of private sector assets by the social security agency and issuance of monetary sterilization bonds.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ Derived as nominal interest expenditure divided by previous period debt stock.

Table 15. Costa Rica: External Debt Sustainability Framework, 2010-2018

(In percent of GDP, unless otherwise indicated)

	Actual		Est.	Projections						
	2010	2011	2012	2013	2014	2015	2016	2017	2018	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	25.2	25.2	27.9	**29.8**	**32.4**	**34.6**	**35.9**	**36.6**	**37.2**	**-4.7**
Change in external debt	-2.6	0.0	2.6	2.0	2.5	2.3	1.2	0.8	0.6	
Identified external debt-creating flows (4+8+9)	-5.8	-2.8	-2.0	-2.0	-1.7	-1.5	-1.3	-1.1	-1.1	
Current account deficit, excluding interest payments	2.7	4.7	4.8	4.8	4.8	4.9	4.9	4.9	4.9	
Deficit in balance of goods and services	2.5	4.7	4.4	4.2	4.1	4.3	4.2	4.2	4.2	
Exports	38.2	37.6	37.1	35.9	35.3	35.0	35.0	35.2	35.2	
Imports	40.7	42.4	41.5	40.1	39.4	39.2	39.2	39.4	39.4	
Net non-debt creating capital inflows (negative)	-4.0	-5.3	-5.1	-4.9	-4.6	-4.4	-4.3	-4.3	-4.3	
Automatic debt dynamics 1/	-4.4	-2.2	-1.7	-2.0	-1.8	-2.0	-1.9	-1.7	-1.7	
Contribution from nominal interest rate	0.8	0.6	0.6	0.7	0.8	0.8	1.0	1.1	1.1	
Contribution from real GDP growth	-1.1	-0.9	-1.1	-1.1	-1.2	-1.3	-1.4	-1.5	-1.5	
Contribution from price and exchange rate changes 2/	-4.2	-1.9	-1.2	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	3.1	2.8	4.6	4.0	4.2	3.8	2.5	1.9	1.7	
External debt-to-exports ratio (in percent)	65.9	67.1	75.0	83.1	91.7	99.1	102.5	104.2	105.8	
Gross external financing need (in billions of US dollars) 4/	0.0	5.5	5.9	6.7	7.6	8.6	9.8	11.0	12.2	
in percent of GDP	0.0	13.5	13.2	13.5	13.9	14.4	15.0	15.5	15.9	
Scenario with key variables at their historical averages 5/				**29.8**	**31.0**	**31.7**	**31.1**	**29.8**	**28.5**	**-6.8**
Key Macroeconomic Assumptions Underlying Baseline										
Real GDP growth (in percent)	4.7	4.2	5.0	4.2	4.4	4.5	4.5	4.5	4.5	
GDP deflator in US dollars (change in percent)	17.8	8.3	5.1	5.9	4.9	4.9	4.3	3.7	3.7	
Nominal external interest rate (in percent)	3.7	2.9	2.7	2.6	2.8	2.9	3.0	3.2	3.4	
Growth of exports (US dollar terms, in percent)	11.3	11.1	9.0	6.7	7.7	8.6	9.0	9.0	8.5	
Growth of imports (US dollar terms, in percent)	20.0	17.5	8.1	6.7	7.7	9.1	8.9	8.9	8.5	
Current account balance, excluding interest payments	-2.7	-4.7	-4.8	-4.8	-4.8	-4.9	-4.9	-4.9	-4.9	
Net non-debt creating capital inflows	4.0	5.3	5.1	4.9	4.6	4.4	4.3	4.3	4.3	

Source:

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

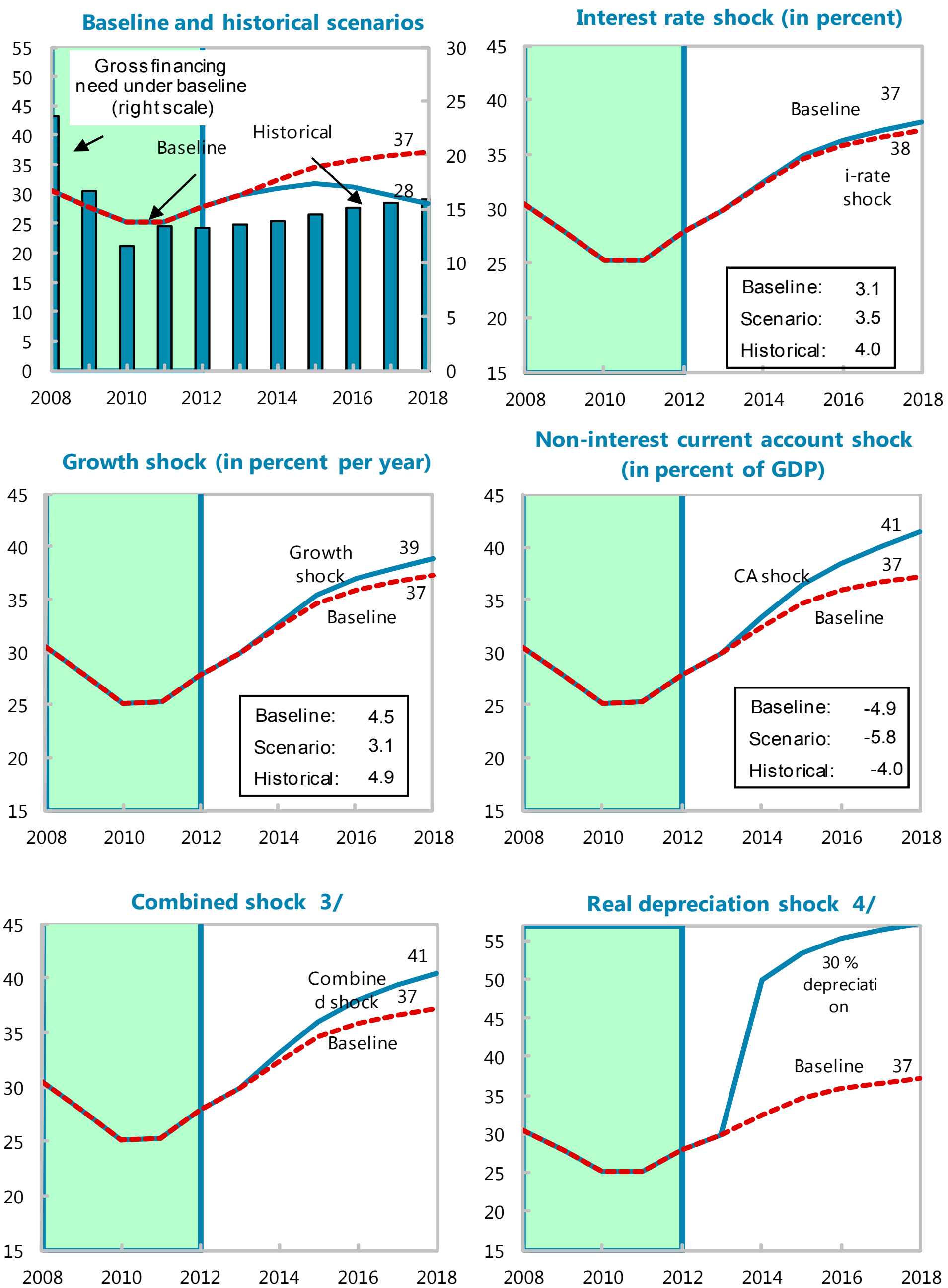
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 7. Costa Rica: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

INTERNATIONAL MONETARY FUND

COSTA RICA

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

February 5, 2013

Prepared By: The Western Hemisphere Department

CONTENTS

FUND RELATIONS

(As of November 30, 2012)

Membership Status: Joined: January 08, 1946

General Resources Account:	**SDR Million**	**% Quota**
Quota	164.10	100.00
Fund holdings of currency	144.09	87.81
Reserve Tranche Position	20.02	12.20

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	156.53	100.00
Holdings	132.58	84.70

Outstanding Purchases and Loans:

None

Latest Financial Arrangements:

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
Stand-By	04/11/2009	07/10/2010	492.30	0.00
Stand-By	11/29/1995	02/28/1997	52.00	0.00
Stand-By	04/19/1993	02/18/1994	21.04	0.00

Projected Payments to Fund
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Overdue	**Forthcoming**			
		2012	2013	2014	2015
Principal	0.00	0.00	0.00	0.00	0.00
Charges/Interest	0.00	0.11	0.11	0.11	0.11
Total	**0.00**	**0.11**	**0.11**	**0.11**	**0.11**

Exchange Rate Arrangement. Costa Rica's de jure exchange rate arrangement is classified as a "crawling band," while the de facto exchange rate arrangement is classified as a "stabilized arrangement." Since October 2006, the de jure exchange rate arrangement has been a crawling band with an increasing width. The ceiling and floor of the band have been adjusted several times, most recently in January 2009, when the crawl rate of the band's ceiling has been set at 0.20 colones (previously 0.06 colones) a business day. The floor of the band has been flat since July 2008. As of January 23, 2013, the intervention buying and selling exchange rates were 500 and 765.25 colones per U.S. dollar respectively. Costa Rica maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions.

Article IV Consultation. The last Article IV consultation was concluded on May 25, 2011 (Country Report No. 11/161).

FSAP participation and ROSCs. The FSAP took place in 2001, and was updated in 2008. A data ROSC took place in 2001 with a reassessment in 2009. A fiscal ROSC took place in 2006.

Technical Assistance.

Department	Time of Delivery	Purpose
STA, CAPTAC-DR	August 2011	Producer price index
	November 2011	Export-import price indices
	2011 and 2012	National accounts statistics
	2011 and 2012	Regional project for harmonization of external sector statistics
	January/May 2012	Regional project for harmonization of monetary and financial statistics
	April 2012	Government finance statistics
MCM, CAPTAC-DR	August 2011	Liquidity management
	November 2011	Construction of a general equilibrium model for the Costa Rican economy
	March 2012	Adoption of International Financial Reporting Standards
	April 2012	Measuring the equilibrium exchange rate
	August 2012	Macro-prudential policy and modeling
	September 2012	Stress tests of the banking system
	September 2012	Formulation of rules to facilitate liquidity risk management and supervision
	December 2012	Methodology and information system for cross-border and consolidated supervision
	December 2012	Modernizing internal audit, risk management and the accounting framework at the central bank
FAD, CAPTAC-DR	2011 and 2012	Internal revenue and customs administration
	February 2012	Measurement of non-compliance and tax expenditure
	June 2012	Plan to strengthen tax and custom administration
	November 2012	Implementation of International Public Sector Accounting Standards
	December 2012	Implementing a medium-term expenditure framework

Resident Representative: Fernando Delgado (based in Guatemala) is the regional resident representative for Central America, Panama and the Dominican Republic.

PAST FUND STAFF RECOMMENDATIONS AND IMPLEMENTATION

2011 Article IV Staff Recommendation	Implementation
Fiscal Policy	
• Rebuild fiscal buffers that were used to contain the impact of the global crisis. Moreover, fiscal consolidation is needed to safeguard fiscal sustainability over the medium and long term. More ambitious fiscal consolidation targets than those envisioned by the authorities would be advisable. • The consolidation strategy should center on both revenue enhancing measures and expenditure restraint. Planned efforts to strengthen tax administration are also appropriate.	• The fiscal deficit has remained high, although the authorities have contained somewhat expenditure growth since 2011 • The tax reform proposed by the authorities in 2011 was void by the Supreme Court in early 2012 due to procedural irregularities. Since then, the authorities have shifted their fiscal adjustment efforts to containing expenditure pressures, strengthening tax administration, and reducing borrowing costs by tapping international markets. The authorities intend to resubmit a tax reform to congress.
Monetary Policy	
• The near-term risks to the inflation outlook stem from possible second-round effects from higher commodity prices and sustained capital inflows. The authorities should stand ready to increase interest rates if signs of inflationary pressures emerge. • Upgrading the monetary policy framework should receive higher priority. Exchange rate flexibility should be raised and the interest rate corridor narrowed to enhance monetary control. • Speed up the transition toward inflation targeting. Too long a transition may compromise the central bank's credibility.	• Inflation has fallen to historically lows, partially in response to the authorities' continued efforts to strengthen the monetary operations framework, notably through establishment of a corridor for short-term interest rates and the launch of a policy interest rate in 2011. • The authorities have reiterated their intentions to move to a more flexible exchange rate system, although the band system is still in place and the exchange rate remains at the appreciated end of the band.
Financial Sector	
• Implementation of the 2008 FSAP recommendations should be accelerated. • Congressional approval should be sought for legislation to enhance consolidated supervision, establish a deposit insurance system and strengthen the bank resolution framework. • The authorities should continue working to introduce risk-based supervision.	• Progress on introducing FSAP recommendations has been mixed. • Critical legislation to enhance consolidated supervision and strengthen bank resolution remains to be approved. • By end-2012, implementation of a risk-based supervision methodology had been largely completed, but more work needs to be done to make it fully operational.

RELATIONS WITH THE WORLD BANK AND BANK-FUND COLLABORATION UNDER THE JOINT MANAGEMENT ACTION PLAN (JMAP)

1. **In November 2012, the IMF's Costa Rica team led by Mr. Figliuoli (mission chief) met with the World Bank's Costa Rica team led by Mr. Calvo-Gonzalez (lead economist and PREM sector leader) to discuss macroeconomic challenges, identify macrocritical structural reforms, and coordinate the two teams' work.**

2. **The teams agreed that Costa Rica's main macroeconomic challenges are to safeguard fiscal sustainability, increase the effectiveness of monetary policy, maintain financial sector stability and enhance competitiveness.**

3. **The teams also discussed the risks to Costa Rica's inflation outlook stemming from large capital inflows, high commodity prices and closing of the output gap.**

4. **Based on the shared assessment of macroeconomic challenges, the teams identified four structural reform areas as macrocritical:**

- Fiscal consolidation. The fiscal consolidation strategy should comprise both revenue and expenditure components. On the revenue side, consensus should be sought to enact a tax reform along the lines of the 2011-12 proposal. On the expenditure side, the focus should be to contain the pace of growth of current expenditure, including wages and transfers. In addition, the authorities should continue working on strengthening revenue administration.

- Monetary policy framework. The transition to inflation targeting and greater exchange rate flexibility should be accelerated in order to lock in low inflation achieved in recently years.

- Financial sector stability. Progress has been made in adopting risk-based financial supervision. Looking ahead, approval of legislation on consolidated supervision, deposit insurance and banking resolution will be critical to bring the regulatory framework up to international best practices.

- Competitiveness. The country is making progress in addressing issues of universal coverage and quality in secondary education, and is seeking to develop its scientific and technological capabilities, which would help position Costa Rica as a knowledge economy. There is also strong commitment to improving the business environment and removing burdensome red tape. Given the sizable investments required to upgrade infrastructure and the tight fiscal situation, the government is seeking to create the institutional conditions to engage the private sector in financing, construction and management of infrastructure projects (public-private partnerships). The government has already begun to open the insurance, electricity and telecommunication sectors to private investment.

5. **The teams agreed the following division of labor:**

- Fiscal consolidation. The IMF (the Fund) will continue to provide policy recommendations on macro-fiscal issues, including the overall strategy of fiscal consolidation and the tax reform. The World Bank (the Bank) will provide technical assistance to support the use of public-private partnerships as a vehicle to finance key infrastructure projects. The government also requested assistance to improve financial management, service delivery, and sustainability of its social security system.

- Monetary policy framework. The Fund will continue to provide policy recommendations regarding the transition to inflation targeting and a more flexible exchange rate regime.

- Financial sector stability. The Bank and the Fund will cooperate as necessary in assisting the country in implementing the FSAP recommendations.

- Competitiveness. The Bank will continue to provide policy recommendations in key areas. In terms of lending, the government is being supported by a project in higher education (approved in September 2012). The government has also requested technical assistance from IFC Advisory services to improve the investment climate.

6. **The teams have the following requests for information from their counterparts:**

- The Fund team requests to be kept informed of progress in the above macro-critical structural reform areas. Timing: when milestones are reached (and at least semi-annually).

- The Bank team requests to be kept informed of the Fund’s assessments of macroeconomic policies and prospects.

7. **The attached table lists the teams' separate and joint work programs for 2013.**

Table 1. World Bank and IMF Planned Activities in Macro-Critical Structural Reform Areas

Title	Products	Provisional Timing of Missions	Expected Delivery Date
World Bank Work Program	Conference: Logistics in Central America a Way to Competitiveness	February 8, 2013	February 8, 2013
	Costa Rica: Development of capital markets (technical assistance)	TBC	Final delivery April 2013
	Financial crisis simulation program (technical assistance)	TBC	Final delivery April 2013
	Costa Rica health (technical assistance)	February, 2013	Final delivery January 2014
IMF Work Program	Regional Conference	July 2013	July 2013
	Staff visit	September 2013	September 2013
	Technical assistance:	2013	
	Internal revenue and customs administration		
	Liquidity management, macro forecasting models		
	Macro-prudential legal framework		
	Central bank accounting		
	Improvement in monetary and financial statistics as part of regional project		
	Improvement in external sector statistics as part of regional project		

RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

8. **Recent activities**. The IBD´s loan portfolio in Costa Rica has 11 sovereign guaranteed operations in execution, with an approved amount of US$1,360.7 million. The available amount for disbursements is US$1,069.8 million (80.1% of the approved), and is concentrated in the areas of Energy (32.5%), Transportation (26.3%), Education (15.6%) and Reform and Modernization of the State (12.9 %). The average age of the operations is 4 years. The IDB still has three operations pending legislative ratification: Water and Sanitation Program, an Innovation and Human Capital for Competitiveness Program and an Education Infrastructure Construction and Equipment Program. Disbursements of sovereign guaranteed operations during 2012 are expected to reach around US$94.2 million, concentrated in the areas of Energy (69.7%), Reform and Modernization of the State (15.0%) and Transportation (12.8%).

9. **Future plans**. During the 2013 the IDB expects to continue the implementation of its 2011-2014 Country Strategy for Costa Rica, focused on the areas of Transportation, Energy, Citizen Security, Early Childhood Development, Health and Innovation. In 2013 the IDB expects to approve two Sovereign Guarantee loans for a total amount of US$338.0 million on Transportation and Logistics/Regional Integration.

Loan Disbursements (Sovereign Guaranteed Operations)

(In millions of U.S. dollars)

	2007	2008	2009	2010	2011	2012*
Disbursements	12.9	18	40.6	55.7	121.0	94.2
Amortization	81.4	289.3**	46.0	45.3	47.0	61.4
Interest and charges	23.6	24.1	13.8	11.4	10.4	17.1
Net cash flow	-92.1	-295.4	-19.2	-1.0	61.5	14.3

* Projections (December 2012).

**Includes an anticipated repayment of US$200 million

Lending Program for 2013 (tentative)

(In millions of U.S. dollars)

Projects	**Amount**
Border Crossing	40.0
Second Road Infrastructure Program	298.0
Total	338.0

Sovereign Guaranteed Operations (as of December 03, 2012)

(In millions of U.S. dollars)

	Approved	Disbursed	Obligated	Available
Loans in execution	**1360.7**	**270.1**	**20.7**	**1069.8**
Cadaster and Registry Regularization	65.0	59.1	0.0	5.9
Sustainable Development of the Binational Watershed Rio Sixaola	9.2	0.9	0.0	8.3
Tourism Program in Protected Areas	19.0	0.0	0.0	19.0
First Electric Power Sector Development Program 2008-2011	250.0	131.6	20.7	97.7
First Road Infraestructure Program	300.0	66.6	0.0	233.4
Cantonal Road Network Program	60.0	12.0	0.0	48.0
Water and Sanitation Program	73.0	0.0	0.0	73.0
Violence Prevention and Social Inclusion Promotion Program	132.4	0.0	0.0	132.4
Innovation and Human Capital for Competitiveness Program	35.0	0.0	0.0	35.0
Power Sector Development Program 2012-16 (Reventazon Hydroelectric Project)	250.0	0.0	0.0	250.0
Education Infrastructure Construction and Equipment Program	167.0	0.0	0.0	167.0
Nonreimbursable Technical Cooperations	**15.5**	**6.5**	**0.5**	**8.6**
Total	**1376.2**	**276.6**	**21.2**	**1078.4**

STATISTICAL ISSUES

(As of January 2013)

General: Data provision is broadly adequate for surveillance. The quality of macroeconomic data has continued to improve in recent years. This was confirmed by a reassessment of the Data Module Report on the Observance of Standards and Codes (ROSC) that was published in February 2010. Further statistical improvements are being pursued, including in the real, monetary, fiscal and balance of payments sectors. The Central Bank, the Ministry of Finance, and the National Institute of Statistics and Census make data available to the public through regular official publications on their websites (www.bccr.fi.cr, www.hacienda.go.cr, and www.inec.go.cr).

National accounts: National accounts are compiled generally in accordance with the System of National Accounts 1993 (SNA 1993). However, the reference year 1991 for the series at constant prices is outdated. Estimation of rentals for owner occupied dwellings should be improved. Accounting depreciation is used instead of estimating consumption of fixed capital. Double deflation method is not applied. Changes in inventories are obtained as residuals and the Chow Lin (without indicator) method is applied for benchmarking quarterly value added of activities, comprising a third of GDP. Non-observed/informal activities are not properly covered. The Central Bank started a project for changing the base year to 2012 and implementing the recommendations of the System of National Accounts 2008 (2008 SNA) that are relevant for the Costa Rican economy.

Price statistics: The compilation of the consumer price index (CPI), in general, employs concepts and definitions from the 1993 SNA and the international CPI manual. However, the CPI lacks a market basket component to measure the cost of owner-occupied housing. Also, the index only covers urban households located in greater San Jose, which comprise approximately 46 percent of the total population and 72 percent of the urban population of Costa Rica. Individual price index data are not generally verified against similar data from other databases such as the producer price index (PPI) and agricultural price indices. Nevertheless, atypical movements in the data are investigated and corrected when necessary.

Except for being compiled only by product aggregations and not by economic activity as well, the PPI is compiled based on concepts and definitions from the 1993 SNA and the international PPI Manual. However, the weights, the establishment sample, and the product sample for the PPI that were introduced in 2000 are based on 1997 sales data. Therefore, the index needs updating. A comprehensive assessment of the source data is being carried out, and this is guiding the production of new source data to update the PPI and the national accounts. The export and import and import price indices as well as the PPI are currently being updated.

Government finance statistics: The concepts and definitions used in compiling GFS generally follow the guidelines of the GFSM 1986. However, financing data and government debt, which use national concepts that combine instruments and holders, are not in accordance with international standards. A migration path to the GFSM 2001 has been adopted in the context of the GFS harmonization project for Central America, Panama, and the Dominican Republic. Monthly fiscal statistics are only compiled and disseminated for budgetary central government, while annual statistics are compiled and disseminated for the entire public sector and its subsectors. The place of issue (Costa Rica or abroad) criterion is followed to classify domestic and foreign debt, instead of the internationally recommended residency criterion. Fiscal data discrepancies among national compilers on particular items are not regularly reconciled, although large fluctuations or discrepancies are investigated. Fiscal statistics are not regularly reconciled with monetary statistics, or other macroeconomic statistics.

Monetary Statistics: Costa Rica's monetary statistics are broadly in line with the methodology of the MFSM. Classification/sectorization follows the MFSM with some exceptions. The social security system accounts are not presented within the central government, but aggregated with other public sector accounts. Some financial assets and liabilities are not disaggregated by economic sector. Accrued interest is not classified together with its underlying instrument.

Balance of Payments: The balance of payments statistics broadly follow the concepts and definitions in the BPM5. While generally adequate and derived from sound collection programs, source data are incomplete to compile some services in the current account, financial transactions of the nonfinancial private sector, and remuneration of employees. Foreign direct investment transactions and positions are valued on a cash basis instead of the recommended accrual basis. Services are recorded at the time the service is provided. While other income transactions are recorded on an accrual basis, interest on public external debt is recorded on the due date; no adjustment is made to convert interest to accrued values. Transfer prices in some cases are not converted to market prices.

Data Standards and Quality: Costa Rica is in observance with the Special Data Dissemination Standards (SDDS). Data Module Report on the Observance of Standards and Codes (ROSC) was published in February 2010.

Costa Rica: Table of Common Indicators Required for Surveillance

(As of January 10, 2013)

	Date of latest observation	Date received	Frequency of Data[5]	Frequency of Reporting[5]	Frequency of Publication	Memo Items: Data Quality – Methodological soundness[6]	Memo Items: Data Quality – Accuracy and reliability[7]
Exchange Rates	Jan 13	Jan 13	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Jan 13	Jan 13	D	D	D		
Reserve/Base Money	Dec 12	Jan 13	D	D	D	O, LO, LO, LO	O, O, O, LO, O
Broad Money	Dec 12	Jan 13	M	M	M		
Central Bank Balance Sheet	Sep 12	Jan 13	M	M	M		
Consolidated Balance Sheet of the Banking System	Nov 12	Jan 13	M	M	M		
Interest Rates[2]	Jan 13	Jan 13	D	D	D		
Consumer Price Index	Dec 12	Jan 13	M	M	M	O, LO, O, O	LO, O, LO, LO,O
Revenue, Expenditure, Balance, and Composition of Financing[3]– Central Government	Dec 12	Jan 13	M	M	M	LO, LNO, LO, LO	LO, O, O, LO, O
Stocks of Central Government and Central Government-Guaranteed Debt[4]	Dec 12	Jan 13	M	M	M		
External Current Account Balance	Sep 12	Jan 13	Q	Q	Q	O, LO, O, LO	LO, O, LO, O, LNO
Exports and Imports of Goods and Services	Nov 12	Jan 13	Q	Q	Q		
GDP/GNP	Oct 12	Jan 13	Q	Q	Q	O, LO, LNO, O	LO, O, LNO, O, LO
Gross External Debt	Sep 12	Jan 13	Q	Q	Q		
International Investment Position	Sep 12	Jan 13	Q	Q	Q		

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discounts rates, money market rates, rates on treasury bills, notes, and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] Including currency and maturity composition.
[5] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).
[6] Reflects the assessment provided in the data ROSC, published in February, 2010 and based on the findings of the mission that took place in April, 2009, for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).
[7] Same as footnote 7, except referring to international standards concerning source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

Staff Statement by the Staff Representative on Costa Rica
February 22, 2013

1. This statement provides additional information that has become available since the staff report was issued. It does not alter the thrust of the staff appraisal.

2. **Headline inflation has risen and interest rates have fallen.**

- Annual headline inflation climbed to 5.7 percent in January, from 4.6 percent in December, owing to important increases in the education, entertainment, and alcohol and tobacco components of the consumer price index. Nevertheless, headline inflation remained within the 4-6 percent official target range. Core inflation stayed at 3.3 percent (y/y), the same as in December.

- A key interest rate, the basic passive rate (BPR), declined to 7.8 percent as of February 14. The BPR has declined steadily since October, reflecting the increased liquidity brought about by large capital inflows and more reliance on external financing by the government. The sharp increase in the BPR observed in the first half of 2012 has almost fully reversed.

3. **The authorities announced their intention to adopt macro-prudential and capital flow management measures (CFMs) to stem the increase in private capital inflows.** They submitted to congress a bill proposing: (i) a surtax—of up to 30 percentage points over the regular income tax rate—for interest, dividends, and capital gains from investment by non-residents (excluding foreign direct investments); and (ii) the application of a reserve requirement on the same investments. At the same time, the central bank introduced temporary limits on credit growth by banks.

4. **As noted in the staff report (SM/13/36), staff thinks that CFMs are not a substitute for the adjustments in macro policies that Costa Rica needs**. Those adjustments include reducing the fiscal deficit, standing ready to tighten monetary policy, if needed, and allowing greater exchange rate flexibility by removing the band. CFMs may be a useful transitory complement to these measures, which are needed to alter the "pull factors" behind the recent surge in capital inflows.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 13/25
FOR IMMEDIATE RELEASE
March 1, 2013

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

IMF Executive Board Concludes 2012 Article IV Consultation with Costa Rica

On February 22, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Costa Rica.[1]

Background

Costa Rica's economy has proven resilient to the adverse shocks of recent years. A proactive policy response, supported by a high-access precautionary Stand-By arrangement with the Fund (that expired in mid-2010), allowed to maintain macroeconomic and financial stability and mitigate the effects of the global financial crisis of 2008-09. After falling by 1 percent in 2009, output recovered quickly. Real GDP grew at an average pace of 4½ percent per annum in 2010-12, while inflation stood within the 4-6 percent official target range.

[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. 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 summing ups can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

A sizable rise in capital inflows more than offset a modest increase in the current account deficit (estimated at about 5½ percent of GDP in 2012). The resulting balance of payments surplus placed strong appreciating pressure on the local currency. Net international reserves rose to US$6.9 billion at end-2012 (from US$4.8 billion at end-2011), reflecting large foreign exchange purchases by the central bank and the government's placement of a US$1 billion bond in international capital markets in late 2012. This notwithstanding, competitiveness, which eroded significantly in recent years, may pose a risk to external stability in the long term. The reversion of this tendency requires enhancing productivity while improving fiscal sustainability and maintaining prudent monetary and exchange rate policies.

The overall public sector deficit stayed broadly unchanged at about 4½ percent of GDP in 2012. Efforts to contain expenditure growth and strengthen tax administration continued, while enactment of an ambitious tax reform approved by Congress was voided by the Constitutional Court owing to procedural problems. The consolidated public sector debt rose to 38 percent of GDP at end-2012, up from 27 percent of GDP at end-2008. The authorities are preparing a fiscal consolidation plan that will be discussed with all sectors of society. Once consensus is reached, the plan would be submitted to Congress aiming for approval before the next administration takes office in May 2014.

Financial sector indicators remained healthy, with adequate levels of liquidity and capitalization. Although the authorities maintained the policy rate unchanged, other interest rates rose significantly, particularly during the first half of 2012. Financial conditions began to ease toward the end of year. Credit to the private sector increased by about 13 percent (y/y) in nominal terms, with stronger growth in the foreign-currency denominated segment.

Real GDP growth is expected to slow from about 5 percent in 2012 to about 4¼ percent in 2013 and hover at around its estimated potential rate of 4½ percent over the medium term. In the absence of significant fiscal consolidation, inflation is projected to remain above that of trading partners, at about 5 percent, while the external current account deficit is anticipated to rise to about 6 percent of GDP through 2018.

The economic outlook is generally positive, but the balance of risks is tilted to the downside amid external uncertainties and domestic policy challenges. Weaker-than-expected growth in the United States, a global financial shock, or a rise in world oil prices are the main sources of external risk. Risks also arise from an eventual resumption of large private capital inflows, which would call for a combination of tighter fiscal and monetary policies and greater exchange rate flexibility to avoid overheating. Finally, lack of fiscal consolidation would lead to a steady rise in public debt, which would increase vulnerabilities and may erode the underpinnings of macroeconomic stability.

Executive Board Assessment

Directors welcomed Costa Rica’s strong economic recovery since the global financial crisis and the continued favorable outlook for growth. In light of the risks posed by the external and internal challenges, Directors emphasized that policies should be geared towards maintaining macroeconomic stability, reducing vulnerabilities, and boosting growth potential and competitiveness.

Directors underscored the importance of preserving fiscal and debt sustainability and commended the authorities’ efforts to enhance revenues and contain expenditures. However, additional measures will be necessary to reduce the large deficits and the public debt-to-GDP ratio. In this context, Directors welcomed the authorities’ intention to resubmit to congress a tax reform proposal which aims at broadening the tax base, reducing tax exemptions, and strengthening revenue administration, with a view to have it approved by May 2014 when the new administration takes office. Directors also highlighted the importance of keeping current expenditure growth in check, especially on public sector wages and transfers, while improving its quality in the social sectors. Strengthening the pension system should be a priority as well.

Directors recognized that the current fiscal trend is unsustainable in the long run and therefore welcomed the authorities’ commitment to fiscal consolidation. Most Directors agreed that a moderately front-loaded adjustment would strike an appropriate balance between addressing Costa Rica’s fiscal challenges and maintaining robust growth. Some Directors were of the view that adjustment efforts should be considered in light of the political economy situation and should also not jeopardize the success of the Costa Rican social-economic model.

Directors commended the authorities for strengthening the monetary framework and bringing inflation down to single digits. However, given the risks posed by the rigid exchange rate regime and continued capital inflows, they called for further action to upgrade the monetary and exchange rate policy framework. Directors noted the authorities' concern about exchange rate flexibility, but generally recommended increasing exchange rate flexibility as it would allow greater use of exchange rate as a shock absorber. In general, Directors also saw merit in establishing an inflation target as the anchor of monetary policy to protect macroeconomic stability. Directors were generally of the view that appropriate fiscal and monetary policies could be complemented, for a limited period, by capital flow management measures and that these should not be a substitute for needed macroeconomic adjustment.

Directors recommended further strengthening of the supervision and prudential regulations of the financial system, and stressed the importance of implementing pending recommendations of the 2008 Financial System Assessment Program's update. They also underlined that full implementation of risk-based supervision and gradual adoption of Basel III capital and liquidity standards would further buttress financial sector stability.

Directors encouraged the authorities to continue advancing their structural reform agenda to raise potential growth and bolster competitiveness. In this regard, addressing infrastructure bottlenecks and streamlining business regulation should be key priorities.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Costa Rica: Selected Economic Indicators

Population (2011, millions)	4.7	Poverty (2010, percent of population)	24.2
Per capita GDP (2011, U.S. dollars)	9,596	Life expectancy (2009, years)	79.1
Unemployment (2011, percent of labor force)	7.7	Literacy rate (2009, percent of people ages > 15)	96.0

	2008	2009	2010	2011	Est. 2012	Proj. 2013
	(Annual percentage change, unless otherwise indicated)					
Output and Prices						
Real GDP growth	2.7	-1.0	4.7	4.2	5.0	4.2
GDP deflator	12.4	8.4	8.0	4.1	4.5	5.1
Consumer prices (end of period)	13.9	4.0	5.8	4.7	4.6	5.0
Money and Credit						
Monetary base	11.9	5.1	11.2	11.6	10.1	9.9
Broad money	16.1	9.7	1.2	6.4	11.1	11.7
Credit to private sector	31.8	4.5	4.4	13.7	12.7	12.6
	(In percent of GDP, unless otherwise indicated)					
Savings and Investment						
Gross domestic investment	27.6	16.3	20.1	20.6	20.8	20.5
Gross domestic savings	18.2	14.3	16.6	15.3	15.3	15.0
External Sector						
Current account balance	-9.3	-2.0	-3.5	-5.3	-5.5	-5.5
Of which: Trade balance	-16.8	-6.9	-9.5	-12.6	-12.6	-12.6
Financial and capital account balance	8.3	1.7	5.5	6.3	10.1	8.5
Of which: Foreign direct investment	6.9	4.6	4.0	5.1	5.0	4.8
Change in net international reserves (increase -)	348	-51	-561	-132	-2,101	-1,500
Net international reserves (millions of U.S. dollars)	3,799	4,066	4,627	4,756	6,857	8,357
Public Finances						
Central government overall balance	-0.3	-3.6	-5.4	-4.3	-4.6	-4.9
Consolidated public sector overall balance 1/	0.2	-4.0	-5.5	-4.3	-4.4	-4.9
Central government debt	24.8	27.2	29.2	30.9	34.8	35.9
Consolidated public sector debt 2/	27.3	29.2	30.6	33.2	38.1	39.5

Sources: Central Bank of Costa Rica; Ministry of Finance; and IMF staff projections.

1/ The consolidated public sector balance comprises the central government, decentralized government entities, public enterprises, and the central bank, but excludes the Instituto Costarricense de Electricidad (ICE).

2/ The consolidated public debt nets out central government and central bank debt held by the Caja Costarricense del Seguro Social (social security agency) and other entities of the nonfinancial public sector.

Statement by Mr. Rojas and Mr. Cosenza Jimenez on Costa Rica
February 22, 2013

On behalf of our Costa Rican authorities, we would like to thank staff for a well-written set of papers on the Costa Rican economy. The Article IV report adequately reflects the constructive dialogue between our authorities and staff during the consultation process in December, and is a good indication of the collaborative relationship between Costa Rica and the Fund. As a small and highly integrated economy, Costa Rica has a significant stake on an environment that promotes a well-functioning global economy. My authorities see their productive engagement with the Fund as part of their contribution to that environment.

Background

In 2012 Costa Rica grew 5.1 percent (yoy), compared to an average growth of 4.7 percent in 2010-11. Most industries were more dynamic in 2012 compared to 2011, including manufacturing, services, commerce, construction and agriculture. The expansion in economic activity was also supported by buoyant credit, which grew at 14.4 percent, though dollar-denominated credit grew at a much higher rate of 19 percent.

Costa Rica has managed to lower its inflation rate to 4-6 percent since 2009, after posting double-digit inflation for almost 30 years. This achievement was underpinned by the strengthening of the Central Bank's operational framework. The authorities are committed to adopt a full inflation targeting framework once economic conditions are appropriate. Concerns remain that the removal of the exchange rate band may result in abrupt appreciation of the colón as long as international interest rates in developed countries remain at historic lows and keep appreciation pressures on an already overvalued exchange rate.

Owing to a dynamic private sector and strong public sector financing requirements, pressure on domestic interest rates increased steeply during the first quarter of 2012 and persisted through the third quarter. Net external public financing was negative during this period as external debt amortization surpassed new external borrowing, adding to pressures on the domestic credit market. In this context, the Costa Rican Congress approved a new international bond issuance program for up to US$4 billion over a 10-year period with a maximum amount of US$1 billion per year. The Government placed $1 billion (2.2 percent of GDP) in November 2012 after nearly eight years of absence in the international bond markets. This bond placement, together with significant private capital inflows and coordinated action by Treasury and Central Bank to reduce public sector competition for funds in the credit market, contributed to a sizable decline in domestic interest rates (400 basis points on 10-year local currency Government bonds), compared to 2011.

The Central Government deficit in 2012 was 4.4 percent of GDP, lower than originally envisaged at the beginning of the year, due to the combination of current expenditure contention policies and the strong effort by domestic tax and customs administrations to curb evasion and smuggling. Additionally, the 10-year US$1 billion international bond placement at 4.25 percent interest, the lowest rate ever for a Costa Rica sovereign, has allowed the authorities to improve the profile of Costa Rica's debt.

Monetary Policy

Along with the international bond placement in November 2012, private portfolio inflows surged from September 2012 to January 2013, putting appreciation pressure on the exchange rate and complicating the conduction of monetary policy. The Central Bank made significant purchases of foreign exchange to defend the exchange rate band, well exceeding foreign exchange purchases scheduled for 2012. Aside from the impact of these operations on monetary aggregates and associated sterilization costs, the authorities were particularly concerned over the volatile nature of such inflows and their potentially destabilizing impact on prices and on the financial sector. Furthermore, the current monetary imbalance coupled with a high interest rate differential posed a significant challenge for monetary authorities.

As a result, the authorities decided to seek approval from Congress for expanded powers in order to impose temporary measures (six months, but renewable if conditions so require) and only in the context of an external disequilibrium produced by portfolio inflows. Such powers would allow authorities to increase the tax rate on bond interest paid to non-residents and to impose non-remunerated deposits on foreign capital inflows directed toward the purchase of bonds placed in the Costa Rican market. Since the draft law was submitted to Congress four weeks ago, portfolio inflows have receded and Central Bank foreign exchange purchases have practically ceased. The draft law will not impact international bond placements by non-financial public institutions and will preserve the rules of the game for investors that made domestic bond purchases before changes in such tax rates or non-remunerated deposits take place.

Fast growth in private sector credit during 2012 increased inflationary risks and its dollar-denominated component heightened the risks faced by unhedged borrowers, whose capacity to pay may be impacted by exchange rate depreciation. As a result, the Central Bank has imposed a temporary ceiling on dollar-denominated and total credit growth. These ceilings are consistent with 9 percent and 12.2 percent annualized growth rates in dollar-denominated and total credit, respectively, and with the economy's projected nominal growth of about 11 percent in 2013.

The Central Bank is prepared to tighten monetary policy in the event that inflationary pressures arise, as long as this does not trigger a new surge in capital inflows. Through successful negotiations with state banks and weekly open market operations, in February the Central Bank withdrew a large fraction of the excess liquidity that resulted from foreign exchange purchases over the past three months.

Fiscal Policy

Despite efforts to enhance revenue and contain expenditures, ongoing since 2010, the authorities recognize the need for additional efforts to reduce the fiscal deficit, now over 4 percent of GDP, to levels that are sustainable over the medium term. The Government considers that a fiscal consolidation effort of about 2.5 percent of GDP is required over the period 2014-18, and should include measures on both the revenue and expenditure sides.

A key element of this strategy is tackling the public sector's structural challenges in expenditure and financing. The government is already analyzing how to improve the compensation system for public employees in order to make it more equitable and efficient, as well as how to optimize resource management in the entire state apparatus and contain interest payments. By accessing the international market and extending maturities of new debt in the domestic market, the Government is improving its liquidity management and debt structure.

The fiscal consolidation program will be developed in three stages. The starting point will be the tax reform agreements reached over the past two years in the context of the tax reform that was voided by the Constitutional Tribunal in 2012. This will need to be supplemented with additional initiatives arising from meetings with think tanks, social sectors, the media and political parties in the first stage, which will conclude by June 2013 with the publication of a proposal that will be the centerpiece of a National Dialogue in a second stage. The document will include policy actions both on structural spending, improvements to minimize tax evasion and fraud, and tax reform.

During the second stage, the Government will engage all sectors of society to improve the proposal. At this point, the participation of the presidential candidates of the major political parties would be sought. Once a consensus is reached on the fiscal proposal, the Government will present it to Congress in the form of one or several draft laws aiming for Congress approval before the new government takes office in May 2014.

As in many other developing and developed countries, demographic changes are likely to strain the public pension system in the long term and will require parametric adjustments either in pension contributions, pension benefits or retirement age. The Costa Rican authorities are already looking into the issue and are in the process of undertaking an actuarial study that may determine the real size of the actuarial deficit over the long term, the effectiveness of alternative measures and adequate timing to deal with the issue.

Our authorities strongly believe that guaranteeing Public Sector solvency is an issue of national interest that goes beyond any particular government. They see the 2013-14 electoral process as an opportunity for the government, political parties, and all sectors of the economy to seek and agree on a comprehensive and balanced solution safeguarding the sustainability of Costa Rica's public policies in the long run.

Financial Sector Issues

The Superintendence of Financial Institutions (SUGEF) has set as a strategic goal the implementation of risk-based supervision, which would start operating in 2014. The authorities will proceed, in line with the recommendations of the 2008 FSAP update, with the modification of existing prudential legal framework for the effective implementation of this approach, together with the final drive for the approval of two projects already submitted to Congress and which seek to strengthen the financial framework and disciplinary penalties.

The authorities are committed to a gradual transition to Basel III, centered on the issues of liquidity and prudential regulations. Given the current situation in terms of capital inflows to the country, SUGEF proposed to the National Supervisory Council of the Financial System, CONASIF, stricter rules on currency matching and maturity, as well as strengthening criteria on risk evaluation for dollar-denominated credits. The CONASIF is expected to approve the measures in the following weeks.

Finally, in November 2011 CONASSIF created the Macroprudential Surveillance Committee in order to strengthen the financial system's ability to identify and mitigate potential systemic risks. In 2012, the committee held, in coordination with the other regulators, a stress exercise of the financial system that was conceived as a pilot for both regulatory bodies and supervised entities, and which will be repeated periodically. This test identified weaknesses in terms of conceptual, methodological consistency, communication and coordination issues that will be shared with the financial entities shortly.