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COSTA RICA

May 2016

2016 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR COSTA RICA

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 2016 Article IV consultation with Costa Rica, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its May 16, 2016 consideration of the staff report that concluded the Article IV consultation with Costa Rica.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on May 16, 2016, following discussions that ended on March 7, 2016, 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 April 20, 2016.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- A **Statement by the Executive Director** for Costa Rica.

The documents listed below have been or will be separately released.

Selected Issues and Analytical Notes

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May 19, 2016

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IMF Executive Board Concludes Article IV Consultation with Costa Rica

On May 16, 2016, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Costa Rica.

Background

Costa Rica bounced back quickly from the 2008–09 global crisis, but growth, despite picking up in the last two years to 3.75 percent, has stayed below trend, while macro vulnerabilities, mainly from the weak fiscal position, have risen. Failure to reverse the counter-cyclical budgetary stimulus imparted in 2009, and a rising interest bill since then have pushed the deficit to about 6 percent of GDP in 2015–16. This has placed the public-debt-to-GDP ratio on an unsustainable path, which is fast approaching levels shown to increase risks of disorderly adjustment for emerging economies. Inflation, on the other hand, has been on a trend decline, and has turned negative in 2015, owing largely to lower oil prices. The current account, benefiting from the positive terms-of trade shock, has shrunk to about 4 percent of GDP and is entirely financed by Foreign Direct Investment. Continuing fast expansion of dollar-denominated credit, facilitated by a stable exchange rate, has exacerbated vulnerabilities in the financial sector, rendering further improvements in regulation and supervision even more important.

Growth is expected to accelerate to 4.25 percent in 2016 supported by the dissipation of the one-off effects arising from a withdrawal of Intel’s manufacturing operations, further terms-of-trade improvement, and current accommodative monetary policy stance. The output gap is anticipated to stabilize in 2016, and then close over the medium term. The baseline scenario contemplates fiscal consolidation measures of 2.25 percent of GDP over the medium term. The central

[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.

government overall deficit would decline moderately to 5.25 percent of GDP and the public debt ratio would reach almost 55 percent of GDP by 2021. Inflation is expected to return to the center of the new 2–4 percent target range by end-2016 and hover around that value through 2021, buttressed by continued prudent monetary policy. The current account deficit should widen slightly to 4.25 percent of GDP over the medium-term, amid gradual recovery of international commodity prices.

Risks to the outlook are tilted to the downside. Concerning external factors, in the case of faster US monetary policy normalization, slightly upside risks prevail, with a positive impact of higher US growth more than offsetting the negative influence of tighter global financial conditions in the short run. However, extreme bouts of market volatility could inflict serious damage. Continued real exchange rate appreciation can negatively affect external competitiveness. Deeper-than-expected slowdowns in the rest of the world could also hamper Costa Rica's growth. On the domestic side, the persistent large fiscal deficits could render the economy vulnerable to sudden changes in financial market conditions, necessitating an increase of domestic interest rates, which would weigh on private investment and growth. Financial stability could be jeopardized by substantial currency depreciation, mainly through higher non-performing loans.

Executive Board Assessment[2]

Executive Directors commended Costa Rica's rapid recovery from the global financial crisis. However, Directors noted that recent growth rates, while increasing over the last two years, have moderated below trend and macroeconomic vulnerabilities have increased arising mainly from the large fiscal deficits and high dollarization. They stressed the importance of a well-calibrated policy mix and broad political consensus to ensure macroeconomic and financial stability and support inclusive growth.

Directors welcomed the authorities' fiscal consolidation strategy focusing both on revenue and expenditure measures. They took positive note of the plans to increase tax collections, impose tougher sanctions against evasion, and implement the income tax reform as well as the VAT reform with targeted support to offset the impact on lower-income households. The planned reduction in the growth of current expenditures will also be important. Directors supported

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

phased adjustment over the medium term with significant frontloading to balance the objectives of maintaining growth and lending credibility to the adjustment effort. They emphasized that full implementation of the planned fiscal reforms will be critical to reducing the large budget deficit and stabilize the level of public debt over the medium term.

Directors viewed the current expansionary monetary policy stance to be appropriate and commended the progress made toward the inflation targeting regime. Welcoming the removal of the exchange rate band, they highlighted that gradual steps towards greater exchange rate flexibility would strengthen the credibility of the inflation-targeting framework and protect against shocks. Directors also saw merit in deepening of the foreign exchange market, thereby facilitating greater exchange rate flexibility.

Directors noted that while the financial system is sound, regulatory upgrades aimed at reducing dollarization and strengthening supervision will be important going forward. They encouraged the authorities to fully implement the 2008 FSAP recommendations, gradually adopt Basel III standards, and improve cross-border supervision. Directors observed that greater competition between public and private banks would help lower interest rate spreads and foster further financial deepening.

Directors called for stronger emphasis on structural reforms to boost Costa Rica's growth potential and competitiveness. They encouraged greater private sector participation in the energy sector, along with a review of the tariff-setting framework, and infrastructure upgrades, notably to ease transportation bottlenecks. They saw scope for efficiency gains and improvement in educational outcomes. Directors stressed that more efficient education and social spending would especially benefit the most vulnerable segments of the population and foster more inclusive growth.

Table 1. Costa Rica: Selected Social and Economic Indicators, Baseline Scenario 1/ 2/

Population (2014, millions)	4.8	Human Development Index Rank (2013)	68 (out of 187)
Per capita GDP (2014, U.S. dollars)	10,425	Life expectancy (2013, years)	80.0
Unemployment (2014, percent of labor force)	9.7	Literacy rate (2014, percent of people ages > 15)	98.0
Poverty (2014, percent of population)	22.0	Ratio of girls to boys in primary and secondary education (2013, percent)	103.0
Income share held by highest 10 percent of households	39.4		
Income share held by lowest 10 percent of households	1.7	Gini coefficient (2012)	48.6

				Est.	Proj.	
	2012	2013	2014	2015	2016	2017
	(Annual percentage change, unless otherwise indicated)					
Output and Prices						
Real GDP growth	5.2	1.8	3.0	3.7	4.2	4.3
Output gap (percent of potential GDP)	2.8	0.4	-0.8	-1.1	-0.9	-0.6
GDP deflator	3.9	4.2	4.7	2.2	3.4	3.2
Consumer prices (end of period)	4.6	3.7	5.1	-0.8	3.0	3.0
Money and Credit						
Monetary base	16.9	10.2	10.4	9.2	9.1	9.0
Broad money	10.7	7.7	15.4	6.6	8.6	8.3
Credit to private sector	13.4	12.2	17.5	11.8	12.1	12.0
Monetary policy rate (percent; end of period)	5.0	3.8	5.3	2.3	…	…
	(In percent of GDP, unless otherwise indicated)					
Savings and Investment						
Gross domestic investment	20.5	18.8	19.6	19.1	19.1	19.3
Gross domestic savings	15.3	13.8	14.9	15.1	14.9	15.0
External Sector						
Current account balance	-5.2	-5.0	-4.7	-4.0	-4.2	-4.3
Of which: Trade balance	-11.6	-11.3	-10.5	-10.2	-10.2	-10.4
Financial and capital account balance	9.5	6.4	4.6	6.2	5.1	5.1
Of which: Foreign direct investment	4.1	4.8	4.0	4.1	4.3	4.3
Change in net international reserves (increase -)	-2,110	-461	113	-622	-500	-500
Net international reserves (millions of U.S. dollars)	6,857	7,331	7,211	7,834	8,334	8,834
Public Finances						
Central government primary balance	-2.3	-2.8	-3.1	-3.0	-2.4	-1.5
Central government overall balance	-4.5	-5.6	-6.0	-5.8	-5.8	-5.4
Central government debt	34.3	36.0	39.3	42.4	45.0	47.3
Consolidated public sector overall balance 3/	-4.5	-5.4	-5.6	-6.0	-6.2	-5.7
Consolidated public sector debt 4/	37.6	42.0	43.2	46.0	47.9	49.6
Of which: External public debt	7.3	8.9	10.5	11.7	12.2	12.7
Memorandum Item:						
GDP (US$ billions)	46.5	49.6	49.6	52.9	56.9	60.8

Sources: Central Bank of Costa Rica, Ministry of Finance, and Fund staff estimates.

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved tax administration.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ 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).

4/ 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.

COSTA RICA

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION

April 20, 2016

KEY ISSUES

Context. Growth moderated to below trend in 2013–15. In 2015, the output gap widened notwithstanding the modest pick-up in growth to 3¾ percent. GDP is expected to return to potential over the medium-term. Inflation dove into negative territory following the sharp decline in imported oil prices, but is projected to return to the 2-4 percent target range by end-2016. The exchange rate (XR) remained stable despite the removal of the band, and reserve accumulation resumed strongly. Risks to the outlook are tilted to the downside, notably from large fiscal deficits and high dollarization.

The short-term policy mix should be characterized by the start of fiscal tightening and continuation of a supportive monetary policy. The authorities appropriately intend to begin gradual fiscal adjustment in 2016 to reduce the sustainability gap, though most of the measures require approval by the opposition-controlled Congress. The tighter fiscal stance and cyclical conditions call for a continued accommodative monetary policy, consistent with bringing inflation back to the target range.

Steady fiscal consolidation is required over the medium term. The authorities' fiscal plan, which contemplates somewhat front-loaded consolidation followed by more gradual adjustment, is appropriate to bring public debt on a sustainable footing, while maintaining robust growth. Swift adoption of fiscal reforms submitted to Congress and administratively-determined spending cuts is critical to achieve these objectives.

It is important to strengthen the monetary policy framework. Higher XR flexibility is useful to complete the transition to inflation targeting. It would be facilitated by FX market deepening. Fostering the secondary government bond market would also help.

Further improvements in financial system regulation and supervision, as well as structural reforms to stimulate inclusive long-term growth, are also needed. Additional regulatory upgrades may be necessary if recently adopted measures do not succeed in reversing the trend toward increased credit dollarization. Efforts should be undertaken to bolster consolidated and cross-border supervision, strengthen creditworthiness assessments, implement pending 2008 FSAP recommendations, and gradually adopt Basel III standards. Steps to boost potential growth include easing infrastructure and regulatory bottlenecks, increasing efficiency of education and social spending, and improving the financial architecture.

Approved By
K. Srinivasan (WHD) and M. Miyazaki (SPR)

Discussions took place in San Jose during February 23–March 7, 2016. The mission comprised L. Figliuoli (Head), V. Flamini, F. Lambert, D. Plotnikov, and J. Puig.

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OVERVIEW

1. **Having bounced back quickly from the global crisis, growth has moderated below trend and macro vulnerabilities, mainly from the weak fiscal position, are rising.** After falling modestly in 2009, real GDP surged in 2010–12. Since then, however, growth has remained below potential, with the latter also declining. Hence, structural impediments must be removed to maintain sustained rates of economic expansion. The counter-cyclical budgetary stimulus imparted in 2009 pushed the deficit above 5 percent of GDP in 2010 (mainly through a rise in wages and transfers). The deficit has crept up further to 6 percent since then, placing the public-debt-to-GDP ratio on an unsustainable upward trajectory and fast approaching levels associated with higher risks of disorderly adjustment in emerging economies. Continuing fast expansion of dollar-denominated credit, facilitated by a stable XR, exacerbates vulnerabilities in the financial sector, rendering further improvements in regulation and supervision even more important.

2. **Policy actions have been broadly consistent with past Fund advice.** The authorities submitted to Congress a fiscal reform package that is in line with staff advice, though its approval will require cooperation of opposition parties (¶22)**.** Other measures consistent with past Fund advice include: (i) the removal of the XR band in early 2015 and continued reserve accumulation (¶5), (ii) the reduction in the inflation target range in 2016 to 2–4 percent, in line with the average inflation of trading partners (¶4), and (iii) tightening of prudential requirements to discourage dollarization (¶28). The large easing of monetary policy was an appropriate response to the unexpectedly sharp decline in headline and core inflation amid low international oil prices (¶4). Additional progress is needed to implement the 2008 FSAP recommendations (¶29).

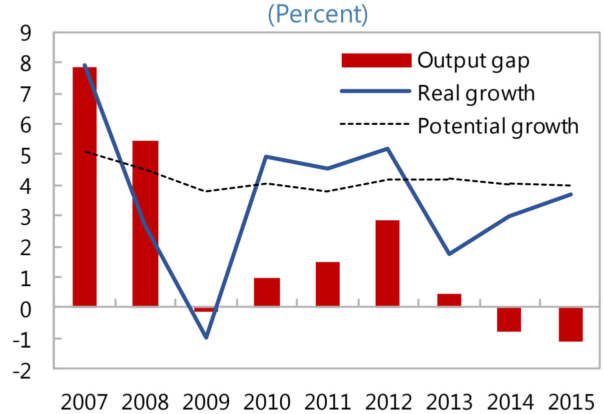
RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

A. Recent Developments

3. **A third year of growth below potential has resulted in a moderate output gap.** Having expanded by almost 5 percent annually in 2010–2012, growth slowed to 2½ percent in 2013–14. This reflected both gradual weakening of domestic demand following the rebound from the 2008–09 crisis as well as sluggish export growth, the latter mirroring the pace of the U.S. recovery. Growth picked up to 3¾ percent in 2015, as the boost to domestic demand from improved terms of trade, associated with lower commodity prices, and higher investment more than offset the drag from Intel manufacturing's closure, adverse weather conditions for the main agricultural export crops, and slightly contractionary financial conditions—the latter reflecting higher real lending rates and real

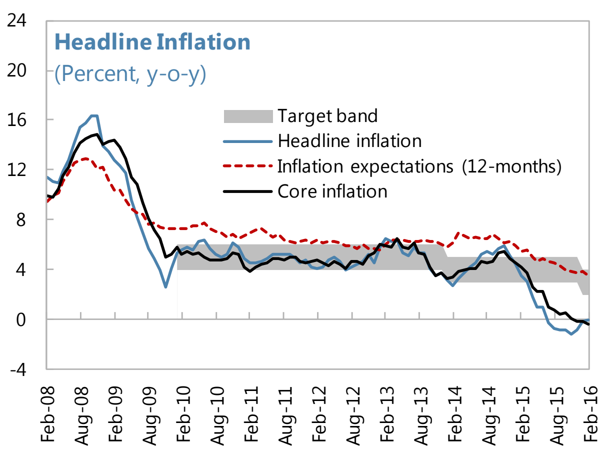
GDP growth, Potential and Output Gap

(Percent)

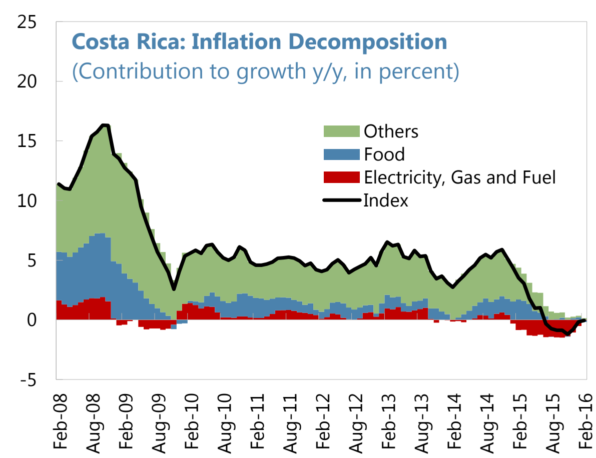


Sources: National authorities, and IMF staff estimates appreciation (¶9). Nevertheless, both private and public investment recovered significantly, the latter supported by construction of a new port terminal and public water systems. Overall, with growth below its trend rate of 4 percent during 2013-15, a negative output gap of about 1 percent of GDP has opened up (Analytical Note (AN) VIII).[1] The unemployment rate has been elevated since the crisis; its slight decline in 2015 was mainly due to lower participation from discouraged workers.

4. **The central bank took advantage of the favorable shock from lower oil prices to reduce its inflation target range.** Inflation increased sharply and breached its upper limit in 2014, owing mostly to the pass-through to domestic prices from XR depreciation in early 2014. The breach was short-lived, though, as the sharp decline in imported oil prices, tight monetary policy, and a widening output gap drove inflation into negative territory by the second half of 2015. The central bank reacted by cutting the policy rate by 350 basis points to 1¾ percent. It also availed itself of the propitious circumstances—with inflation projected to stay below the 3–5 target range until the end of 2016 and inflation expectations falling for the first time below the center of the range—to lower the target to 2–4 percent, in line with average inflation of trading partners.



Sources: Haver, BCCR and Fund staff calculations.



Sources: Haver analytics and Fund staff estimates.

5. **The exchange rate has been stable despite abandonment of the band regime, and reserve accumulation has resumed strongly.** After a short period of heightened volatility in early 2014, amid increased prospects for U.S. monetary policy normalization, the XR quickly stabilized again about 6–7 percent above the floor of the XR band, and remained there despite the early-2015 removal of the band, in line with Fund advice to strengthen the inflation targeting framework. A lower current account deficit—4 percent of GDP in 2015, driven by lower oil prices—as well as continued government Eurobond issuance, resilient FDI flows, and increased net foreign bank liabilities to meet renewed demand for credit in FX resulted in continued strong foreign reserve accumulation, in line with the authorities FX purchase program, to $7.8 bn at end-2015, above the

[1] Intel's closure resulted in both lower real GDP and lower potential output of ¾ percent of GDP in 2014-15, without any effect on the output gap in the short run.

IMF adequacy metrics.[2] Nonetheless, in December 2015 and early 2016, reserves declined somewhat, as FX demand, including by financial intermediaries, increased and the central bank accommodated it, resulting in a flat XR.

6. **The external position is close to equilibrium, with competitiveness largely unchanged in 2014–15.** In the first half of 2014, a third of the 30 percent real effective exchange rate (REER) appreciation accumulated over the last decade was undone, as nominal colón depreciation outpaced a growing inflation differential. Since then, however, the REER rose steadily until stabilizing about 5 percent above its end-2013 level. At the same time, this increase is consistent with the change in the REER equilibrium value and, as a result, competitiveness has not deteriorated (Box 1). In particular, multilaterally consistent estimates under the EBA and other regression-based approaches support this view. Nevertheless, productivity-enhancing reforms (¶32) and wage restraint are needed to maintain Costa Rica's competitiveness in world markets. Fiscal consolidation (¶18-23) would also buttress long-term external stability.

External Sustainability Assessment

Costa Rica: Implied Undervaluation ("+" = Overvaluation)

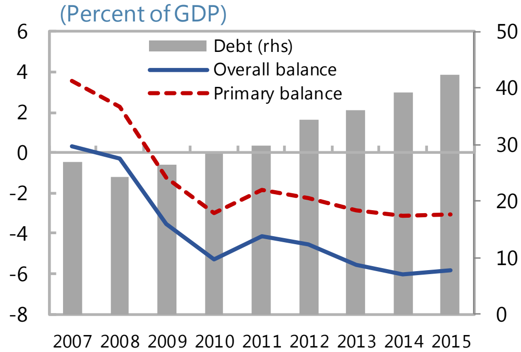
Regression-based methods	CA norm	CA projected/ cyclically-adjusted	REER gap (updated)	REER gap (2014 AIV)	REER gap (2012 AIV)
Macroeconomic Balance	-3.2	-3.9	1.9	-0.8	7.9
External sustainability (ES)	-2.4	-4.5	6.8	13.2	8.5
ES (NFA exclud. FDI)	-7.2	-4.5	-7.1	-5.9	NA
EBA					
Macroeconomic Balance	-4.7	-3.9	-2.1	-4.7	8.5
Average			-0.1	0.5	9.9

Sources: Fund staff estimates.

7. **Failure to reverse the countercyclical fiscal policies implemented during the global financial crisis put public debt on a rapid upward trend.** Attempts to curb government outlays, mainly through capital expenditure cuts in 2011, were undermined by the rising transfers (to decentralized public entities) and interest bill in 2012–2013. Tax collections, after falling from pre-crisis levels that were boosted by GDP growth well above trend, remained stagnant, with a revenue-enhancing tax reform nullified by the Constitutional Court owing to procedural irregularities in 2012. Consequently, the central government (CG) primary deficit returned to its crisis peak of around 3 percent of GDP in 2013. The new administration that came into power in mid-2014 maintained a broadly unchanged non-interest deficit, as efforts to

Central Government

(Percent of GDP)



Sources: National authorities and Fund staff estimates.

[2] After a substantial decline in 2014 reflecting in part the end of reinvestment of retained earnings by Intel, FDI remained steady in 2015, suggesting limited impact of the exit on broader FDI trends.

restrain spending and reduce tax evasion prevented a budgeted deterioration in the primary balance of more than ½ percent of GDP in 2014–15. Meanwhile, a rising interest bill has lifted the overall CG deficit to 6 percent of GDP in 2014-15, with debt exceeding 42 percent of GDP in 2015. Though the impact on domestic financing costs has been muted by the annual $1 bn external bond issuance since 2012 and aggressive monetary easing in 2015, spreads on external bonds have doubled since the 2013 tapering tantrum and the country lost its investment grade in 2014.[3]

8. **The authorities have developed a strategy for fiscal consolidation focused on strengthening revenue.** The new government initially formulated a consolidation proposal focused on reducing tax evasion and a few exemptions. Since then, a more comprehensive plan, that is broadly consistent with staff recommendations both in its size and its emphasis on revenue enhancements through tax base widening and higher rates, has been developed (¶21).

Potential Output Growth and Output Gap Estimates
(In percent)

	Potential GDP growth rate			Output Gap 1/	
	2000-08	**2009-14**	**2015**	**2014**	**2015**
Production Function	4.60	3.78	3.95	0.25	-0.36
Cycle Extraction Filters					
Hodrick-Prescott	4.60	3.74	3.85	0.46	-0.06
Butterworth	4.52	3.66	3.78	0.49	0.03
Christiano-Fitzgerald	4.53	3.52	3.99	0.42	-0.24
Baxter-King	5.23	3.76	3.80	0.16	-0.31
Univariate Kalman Filters					
Deterministic Drift	4.11	4.11	4.11	0.43	-0.33
Mean Reversion	4.51	4.60	4.60	-0.40	-1.15
Multivariate Kalman Filter					
With inflation	4.78	3.78	3.64	-0.02	-0.34
Average of All Models	**4.61**	**3.87**	**3.97**	**0.22**	**-0.35**
Macroframework 2/	**4.79**	**4.00**	**4.00**	**-0.43**	**-1.11**

Source: Fund staff estimates.
1/ Includes level effect on potential output of Intel exit, estimated at 0.2 percent of GDP in 2014 and 0.8 percent in 2015.
2/ The output gap in the macroeconomic framework is slightly different from model-based estimates, as the level of potential output for each past year in the historical series reflects the estimate available at the time.

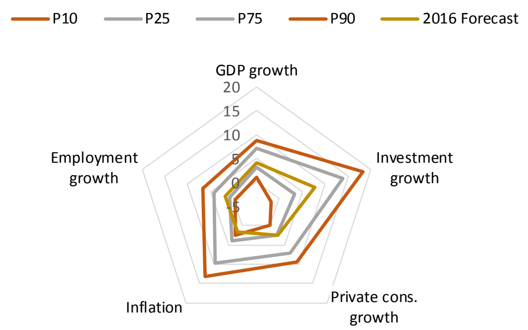
9. **The recent loosening of monetary policy is expected to bring about financial conditions more supportive of growth.** Real lending rates have been edging upwards since mid-

[3] Moody's downgraded Costa Rica's external sovereign debt by one notch in 2014 with a negative outlook on its current Ba1 rating. S&P downgraded the sovereign by one notch to BB- in 2016, while Fitch has a negative outlook on its BB+ rating since 2015.

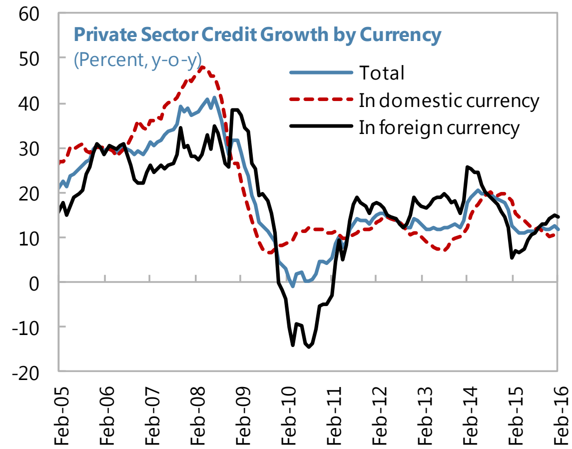
2014, as limited transmission of the large policy rate cuts to lending rates thus far has been more than offset by the fall in inflation expectations. In addition, the REER has resumed its appreciating trend and credit growth has moderated. A broad-based index (FCI) developed by staff (featuring the influence on economic activity of credit, deposits, real interest rates, REER, and house prices) suggests that financial conditions were slightly contractionary in 2015, owing to higher real interest rates and real appreciation (AN III). However, this is likely to be reversed as the lower policy rates gradually complete their pass-through. Monetary transmission, though, is hamstrung by high dollarization, segmentation of the banking system, limited capital market development (¶33 and AN V), and anticipation of forthcoming upward pressures on interest rates from large budgetary financing needs.

10. **The financial system appears sound, though profitability is low and dollarization continues to be a source of vulnerability.** Bank capital is well above regulatory requirements and liquidity indicators are robust. While non-performing loans have remained low, profitability has declined slightly in recent years, and remains below that of regional peers. Reliance on foreign funding has continued to increase, although staff analysis suggests that associated rollover risks remain manageable even under scenarios of extreme shocks in international banking systems. Moreover, macroeconomic trends are consistent with recent and anticipated credit growth and there is little evidence of financial sector risk buildup (ANs I and II). Indeed, while the depth of Costa Rica's financial system improved considerably in the past decade, it continues to lag those of comparable emerging markets as well as the degree of development implied by its macroeconomic fundamentals. In particular, credit to the private sector is still well below the estimated level consistent with fundamentals (ANs IV and V). Amid renewed exchange rate stability since late 2014, however, credit growth has again tilted toward FX, including to sectors without natural FX hedges, despite already high levels of bank loan dollarization.

Distribution of Macro Outcomes Conditional on Real Private Sector Credit Growth



Source: IMF staff estimates based on RES Macro Financial Forecast



Sources: BCCR and Fund staff calculations.

Costa Rica. Financial Soundness Indicator Heat Map

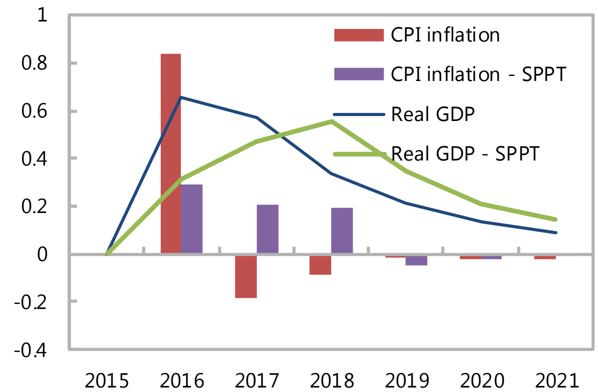
Costa Rica	2013Q2	2013Q3	2013Q4	2014Q1	2014Q2	2014Q3	2014Q4	2015Q1	2015Q2	2015
Overall Financial Sector Rating	L	L	L	M	M	M	M	L	L	L
Credit cycle	L	L	L	H	H	M	M	L	L	L
Change in credit / GDP ratio (pp, annual)	1.3	1.6	1.9	5.1	5.2	4.7	4.3	1.5	1.7	2.8
Growth of credit / GDP (%, annual)	2.7	3.3	3.9	10.5	10.6	9.6	8.4	2.7	3.1	5.2
Credit-to-GDP gap (st. dev)	1.2	1.2	1.4	1.7	1.2	0.8	0.6	-0.1	-0.4	0.6
Balance Sheet Soundness	L	L	L	L	L	L	L	L	L	L
Balance Sheet Structural Risk	M	M	M	M	M	M	M	M	M	M
Deposit-to-loan ratio	113.7	110.8	107.5	105.0	101.7	101.5	100.7	97.2	97.7	95.3
FX liabilities % (of total liabilities)	36.7	35.4	33.2	36.6	36.9	35.9	34.5	34.6	35.1	33.8
FX loans % (of total loans)	37.3	37.7	37.9	38.7	38.0	37.5	37.0	36.7	37.0	37.2
Balance Sheet Buffers	L	L	L	L	L	L	L	L	L	L
Leverage	L	L	L	L	L	L	L	L	L	L
Leverage ratio (%)	10.1	10.0	9.7	9.8	9.7	9.7	9.7	10.0	9.7	9.9
Profitability	L	L	L	L	L	L	L	L	L	L
ROA	1.3	1.1	1.2	1.5	1.3	1.2	1.1	1.1	1.0	1.0
ROE	8.6	7.5	7.9	10.7	9.5	8.4	7.6	8.0	7.4	7.4
Asset quality	L	L	L	L	L	L	L	L	L	L
NPL ratio	1.9	1.9	1.7	1.6	1.6	1.7	1.6	1.6	1.6	1.7
NPL ratio change (%, annual)	1.2	4.3	0.2	-10.6	-14.9	-12.0	-11.2	-2.0	0.7	1.6
Memo items:	**2013Q2**	**2013Q3**	**2013Q4**	**2014Q1**	**2014Q2**	**2014Q3**	**2014Q4**	**2015Q1**	**2015Q2**	**2015**
Credit-to-GDP (%)	48.7	49.4	50.8	53.4	53.8	54.1	55.1	54.9	55.5	56.7
Credit-to-GDP gap (%; HP filter)	-1.9	-1.6	-0.6	1.5	1.4	1.1	1.6	0.9	1.0	n.a
Credit growth (%; annual)	11.1	11.3	12.2	19.0	19.8	18.7	17.5	11.8	11.4	12.2
CAR (in %)	17.2	17.2	16.6	16.0	16.3	16.2	16.6	16.6	16.4	16.6
Tier 1 CAR (in %)	13.7	13.5	13.0	12.9	12.7	12.6	12.7	12.9	12.6	12.8

Sources: BIS; FSIs; IMF IFS; and national authorities.

B. Macroeconomic Outlook and Risks

11. **The joint view of staff and the authorities was that the economy will expand faster and inflation revert to the target range in 2016, with activity returning to potential over the medium term.** Growth is expected to accelerate to 4¼ percent in 2016, slightly above potential growth, supported by: (i) dissipation of the one-off effects of Intel's manufacturing withdrawal, (ii) further terms-of-trade improvement from the additional decline in international oil prices, (iii) domestic monetary stimulus—model simulations suggest that the monetary easing implemented in 2015 would boost GDP growth by ½–¾ percent of GDP in 2016, assuming full though gradual transmission from policy to lending rates—and (iv) sustained real credit expansion (estimated by staff to be consistent with projected GDP growth based on historical precedent).[4] The output gap is anticipated to stabilize in 2016, and then mostly close over the medium term. Model simulations also suggest that the monetary stimulus, together with fading base effects from the oil price decline in 2015, would also bring inflation back to the center of the new 2–4 percent target range by end-2016. Inflation is then projected to hover around that value throughout 2017–21, buttressed by continued prudent monetary policy, while still allowing for continued monetary accommodation during the initial phase of the fiscal adjustment. The current account deficit will widen slightly to 4¼ percent of GDP over the medium-term, amid gradual recovery of international commodity prices, while partial fiscal consolidation—focused on revenue measures that increase the progressivity of the tax system and with some attendant confidence effects—is not expected to have a significant negative impact on domestic demand. The staff baseline scenario, which incorporates the measures already submitted to Congress that have a higher probability of being approved, contemplates fiscal consolidation measures of 2¼ percent of GDP over the medium term. The CG overall deficit would decline slightly to 5½ percent of GDP and the public debt ratio would reach 55 percent of GDP by 2021 (¶18 and AN VI).

Real Effect of a 300bp Policy Rate Cuts with Different PT
(Percent difference from baseline)



Sources: IMF staff calculation based on RES FSGM
Note: PT=Pass-through to Lending Rates; SPPT=Slower, more persistent PT (1/3)

12. **The authorities also concurred that an alternative scenario incorporating the fiscal adjustment necessary to restore debt sustainability would yield a more favorable outlook.** According to staff analysis, a total correction of about 3¾ percent of GDP would stabilize public debt in the medium term within "safe levels," with only moderate short-term output costs (¶19). Growth would be only slightly lower in initial years and higher in outer years than in the baseline case. This is not only because of significant confidence effects but also of the more balanced macro policy mix allowed by tighter budgets consistent with restoring fiscal sustainability and reducing the current account deficit.

[4] The effect of Intel's manufacturing closure on the growth rate of potential GDP is estimated to be less than ¼ percentage points. The withdrawal is not expected to have significant impact on fiscal revenue as Intel operated in the free trade zone.

Indeed, a looser monetary stance than in the baseline would be sufficient to achieve the inflation target over the medium-term, thereby also mitigating increases in market rates associated with the normalization of U.S. monetary policy.

Costa Rica: Baseline Scenario, Partial Fiscal Adjustment 1/

(In percent of GDP, unless otherwise indicated)

	2015	2016	2017	2018	2019	2020	2021
Real GDP growth (percent)	3.7	4.2	4.3	4.4	4.3	4.0	4.0
Output gap (percent of potential GDP)	-1.1	-0.9	-0.6	-0.3	0.0	0.0	0.0
CPI (percent, end-of-period)	-0.8	3.0	3.0	3.0	3.0	3.0	3.0
Current account balance	-4.0	-4.2	-4.3	-4.2	-4.3	-4.3	-4.3
Central government fiscal balance	-5.8	-5.8	-5.4	-5.5	-5.5	-5.5	-5.3
Structural primary balance	-2.9	-2.3	-1.4	-1.1	-1.2	-1.2	-1.2
Structural overall balance	-5.7	-5.6	-5.3	-5.4	-5.5	-5.5	-5.2
Central government debt	42.4	45.0	47.3	49.4	51.3	52.9	54.4

Source: Fund staff estimates.

1/ The baseline scenario includes fiscal consolidation measures of about 2¼ percent of GDP, partly offset by a projected underlying deterioration in the primary balance mainly driven by the constitutionally mandated increase in education expenditure.

Costa Rica: Full Fiscal Adjustment Scenario 1/

(In percent of GDP, unless otherwise indicated)

	2015	2016	2017	2018	2019	2020	2021
Real GDP growth (percent)	3.7	4.2	4.2	4.6	4.5	4.2	4.3
Output gap (percent of potential GDP)	-1.1	-0.9	-0.7	-0.2	0.2	0.3	0.4
CPI (percent, end-of-period)	-0.8	3.0	3.0	3.0	3.0	3.0	3.0
Current account balance	-4.0	-4.2	-4.2	-4.1	-4.0	-3.8	-3.7
Central government fiscal balance	-5.8	-5.7	-4.4	-3.6	-3.6	-3.3	-3.2
Structural primary balance	-2.9	-2.3	-0.8	0.1	0.1	0.2	0.2
Structural overall balance	-5.7	-5.5	-4.2	-3.6	-3.6	-3.4	-3.3
Central government debt	42.4	44.9	46.2	46.1	46.0	45.7	45.5

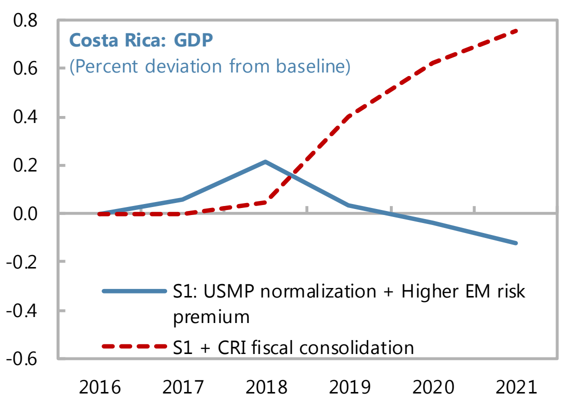
Source: Fund staff estimates.

1/ Includes measures as in the baseline scenario and additional measures of 1½ percent of GDP.

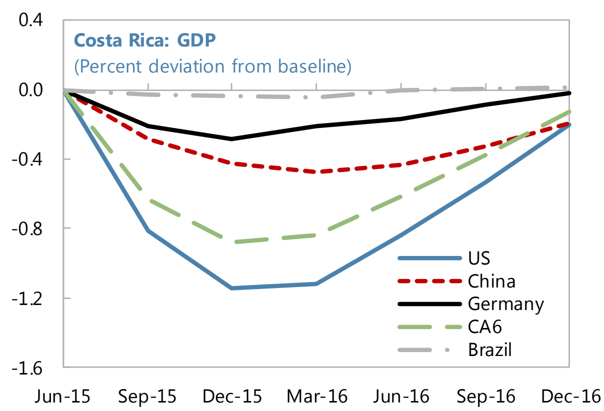
13. **The authorities agreed that risks to the outlook were tilted to the downside.** Downside risks stem from both global uncertainties and weaknesses in domestic fundamentals (as detailed in the Risk Assessment Matrix):

- **External risks.** The *normalization of* U.S. monetary policy presents moderately upside risks. Absent pronounced increases in market volatility, faster U.S. growth would have a positive impact on Costa Rican GDP, given strong trade ties, more than offsetting the negative influence of tighter global financial conditions. However, *extreme bouts of market volatility*—from a disorderly U.S. monetary policy normalization, stresses in emerging markets with high corporate leverage (including in FX), or heightened global geopolitical risks—could inflict serious damage, especially given Costa Rica's weak fiscal position, bank reliance on foreign funding, and domestic credit dollarization, with associated exposures to interest rate and exchange rate risks, the latter evident only in the event of a large depreciation (¶26 and AN I). Conversely, if the nominal effective exchange rate of the colón continues to appreciate in line with the U.S. dollar, competitiveness vis-à-vis other trading partners would be negatively affected. In addition, *deeper-than-expected slowdowns* in the rest of the world could hamper Costa Rica's growth, both in the short term—as the credit cycle matures in key emerging markets—and in the medium term, reflecting structurally weaker growth in advanced countries that have not fully addressed crisis legacies. At the same time, model simulations of the effect of slowdowns in foreign demand suggest that Costa Rica is less vulnerable to adverse developments in key emerging markets, including China and Brazil, than in the U.S., consistent with relative trade ties (AN VIII). In addition, the fact that Costa Rica does not have a significant offshore sector like other countries in the Central America-Caribbean region, and given also comparatively limited anti-money-laundering-compliance concerns (¶31), the country appears less vulnerable to *de-risking strategies by global banks*, including loss of correspondent banking services.[5] Risks from *energy prices* are balanced, with increased volatility possibly deriving from geopolitical tensions weighing on the downside, while lower-than-anticipated prices would have moderately positive effects.

Real and Financial Spillovers



Source: Staff estimates.
Note: While domestic fiscal consolidation will reduce GDP growth in the short term, a positive confidence effect is assumed to prevail in the medium to long term.



Source: Staff estimates.
Note: Effect of 1 percent lower growth in domestic demand in selected economies.

[5] The authorities and the financial community confirmed that any requests for additional information on AML/CFT procedures and readiness from correspondent banks had been satisfactorily met and that there had not been any loss of correspondent accounts. Moreover, domestic banks had remained active in monitoring possible AML/CFT activity, as demonstrated by a recent case currently under investigation raised by one of the public banks.

- **Domestic risks.** The *persistence of large fiscal deficits* and the ensuing rapid rise in the public debt ratio in a passive scenario where political support for budget consolidation falls short, could render the economy vulnerable to sudden changes in financial market conditions. Also, large government gross financing requirements could lift domestic interest rates, weighing on private investment and growth. Expectations of a pick-up in interest rates driven by the government short-term financing needs are already encouraging maintenance of excess liquidity in banks, which also limits the transmission of the monetary stimulus to lending rates—model simulations suggest that if pass-through of the policy rate cuts continued to be hindered by these concerns, the short-term boost to growth from monetary stimulus would be reduced by half (¶11 and AN I). Given *low profitability and heavy dollarization of the banking system,* financial stability could also be jeopardized by substantial currency depreciation, mainly through higher NPLs (¶26, AN I and II).

Costa Rica: Passive Scenario 1/

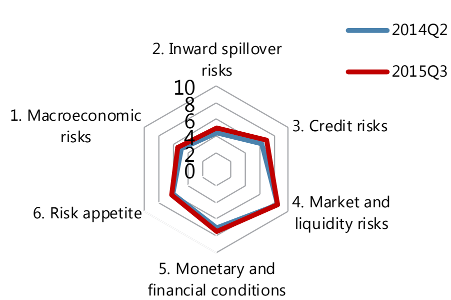
(In percent of GDP, unless otherwise indicated)

	2015	2016	2017	2018	2019	2020	2021
Real GDP growth (percent)	3.7	4.2	4.2	4.0	3.9	3.6	3.5
Output gap (percent of potential GDP)	-1.1	-0.9	-0.6	-0.6	-0.7	-1.1	-1.6
CPI (percent, end-of-period)	-0.8	3.3	3.5	3.5	3.5	3.5	3.5
Current account balance	-4.0	-4.5	-5.0	-5.8	-6.5	-6.5	-6.5
Central government fiscal balance	-5.8	-6.7	-7.3	-7.8	-8.5	-9.2	-9.6
Structural primary balance	-2.9	-3.1	-3.3	-3.3	-3.4	-3.4	-3.4
Structural overall balance	-5.7	-6.6	-7.2	-7.6	-8.4	-9.0	-9.3
Central government debt	42.4	45.9	50.1	54.4	59.1	64.0	69.1

Source: Fund staff estimates.

1/ This scenario does not include any fiscal consolidation measures, while reflecting the underlying deterioration in the primary balance mainly driven by the constitutionally mandated increase in education expenditure.

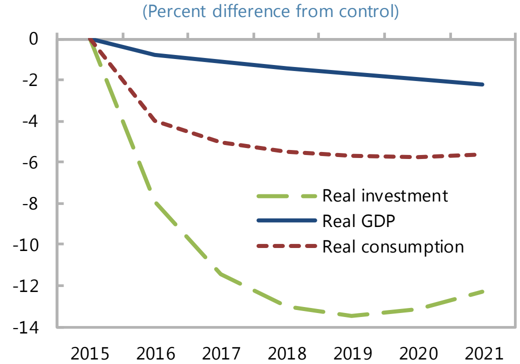
Costa Rica: Financial Stability Map



Source: Fund staff estimates.

Real Effect of a 100bp Increase in Market Interest Rates

(Percent difference from control)



Sources: IMF staff calculation based on RES FSGM

Costa Rica: Risk Assessment Matrix		
Source of Risks	**Overall Level of Concern (Scale—high, medium, or low)**	
	Relative Likelihood[2]	**Impact if Realized**
1. Slower growth in advanced and/or emerging economies.	**Low/Medium/High** • Sharper-than-expected global slowdown in the short-term, triggered by significant China slowdown (Low in the short-term, Medium thereafter), or turning credit cycle in EMs (Medium). • Protracted period of slower growth in advanced (High) and emerging economies (Medium) would reduce growth in Costa Rica, in particular, if growth in the U.S. is negatively affected.	**Medium/High** • Impact of weaker emerging markets growth in the short- or long-term would be moderate, as long as U.S. growth was relatively unaffected (Medium). • Protracted period of weaker-than-expected growth in the U.S. 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 (High).
2. Tighter or more volatile global financial conditions,	**Medium/High** • Surges in global financial market volatility—triggered by geopolitical tensions, or revised market expectations on UMP exit/emerging market fundamentals—would reduce capital flows to Costa Rica, lead to an increase in cost of government financing, as well as potentially an increase in cost of funding for the private sector (Medium). • Surge in U.S dollar prompted by improving U.S. economic prospects versus the rest of the world (High).	**High/Medium** • While orderly UMP exit with stronger U.S. growth in tandem with higher U.S. rates would on net be beneficial for Costa Rica, a decline in capital flows to emerging markets under more disorderly scenarios could disrupt foreign credit lines and reduce banking sector liquidity. If markets reassess more negatively fiscal risks in Costa Rica, the cost of external government and private sector financing could increase sharply, negatively affecting public debt dynamics and growth (High). • If the NEER continues to appreciate in line with the dollar, competitiveness vis-à-vis de rest of the world would be negatively affected. Conversely, if the local currency depreciated, the private sector (with negative foreign exchange positions) and banks would be negatively affected (through higher credit risks on unhedged borrowers, despite banks' long FX positions) (Medium).
3. Dislocation in capital and labor flows.	**Medium/High** • Reduced financial services by global/regional banks, including loss of correspondent banking services (Medium). • Increased volatility due to security dislocations in the Middle East, Africa, and Europe, leading to sharp rise in oil price volatility (High).	**Medium** • Could curtail cross-border payments, trade finance, and remittances. • Volatile oil prices could result in adverse changes in terms of trade, increase inflation, and be a drag on growth.
4. Sustained decline in energy prices.	**High** • The recent fall in oil prices could persist and deepen, with supply factors reversing only gradually.	**Low** • Persistently low oil prices would improve Costa Rica's terms of trade and counterbalance inflationary pressures, potentially yielding a modest boost to growth prospects.
5. Worse-than-anticipated impact from persistently high fiscal deficits, or higher deficits than projected in the baseline scenario.	**High** • Lack of fiscal consolidation prospects may hurt confidence. • Continued expenditure pressure and lack of tax reform could increase the fiscal deficit and public debt more than projected in the baseline scenario, which already envisages a rapid build-up of public debt.	**High** • Lower confidence or a higher government financing requirement could raise domestic interest rates further and reduce 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.

Costa Rica: Risk Assessment Matrix (concluded)

6. Larger than anticipated impact from INTEL withdrawal	**Low** • INTEL's withdrawal and external competition weighs down on FDI and leads to an increase in unemployment and a reduction in productivity growth as the enterprises with a more sophisticated export base close. An unsustainable fiscal position may exacerbate these risks.	**Low/Medium** • Depending on the size of the reduction in FDI flows, there may be low to moderate impact on short-term growth, due to lower capital accumulation and productivity growth. The impact on potential growth, however, is likely to be limited since Costa Rica has strong institutions and a well-educated workforce.

[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 focused on the policy mix appropriate for current cyclical conditions and mitigation of longer-term economic vulnerabilities.** In particular, the latter centered on how to: (i) restore fiscal sustainability; (ii) improve the monetary policy framework; (iii) further enhance financial system supervision and regulation; and (iv) boost potential and inclusive growth.

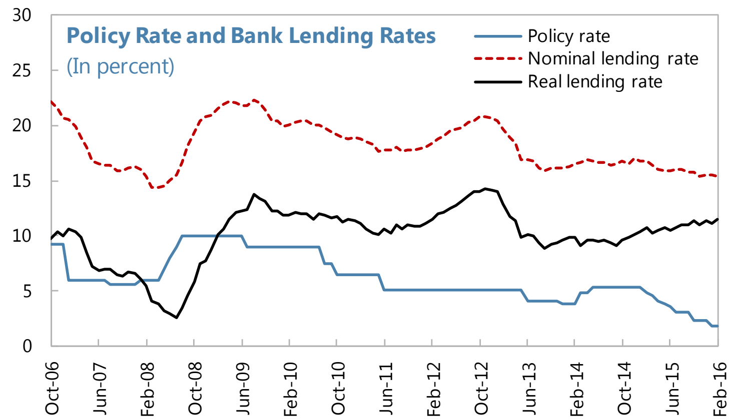
A. Near-term Policy Mix

15. **There was agreement that economic conditions call for a policy mix characterized by the start of fiscal tightening and continuation of a supportive monetary policy.** The authorities appropriately intend to begin a gradual fiscal adjustment in 2016 (¶s16, 20). With output below potential and zero inflation, a continued accommodative monetary policy stance consistent with bringing inflation back to the target range will help offset the small contractionary impact of the tighter budgetary stance in the short term.

16. **Indeed, the authorities are pursuing a sizable reduction in the deficit in 2016 as part of a gradual path toward fiscal sustainability.** Although the 2016 budget[6] envisaged the overall and primary deficits to edge up to 6½ and 3¼ percent of GDP respectively in a passive scenario, as a result mainly of constitutionally-mandated rises in education outlays and continued increases in interest payments, the government has submitted to Congress bills that could result in a correction of about ¾ percent of GDP relative to the budget. In staff's view, this correction, as part of a policy mix that takes into account the cyclical position of the economy (¶20), would be suitable. Officials were also adamant that it will be critical to implement these measures as part of a comprehensive package that delivers the total budgetary consolidation measures of 3¾ percent of GDP needed to stabilize debt over the medium-term (¶s19 and 20).

[6] Adjusted for targets in the medium-term framework (published together with the budget law) that have generally been more aligned with the authorities' intended fiscal stance.

17. **The authorities concurred that the current expansionary monetary stance is broadly adequate.** Headline inflation was negative and core inflation was below the lower bound of the 3-5 percent target range during most of 2015. Inflation is projected to return to the center of the new 2-4 percent target range by end-2016, while output remains below potential. Thus, the monetary stance—with 350 basis points in cumulative policy rate cuts to 1¾ percent, well below the estimated neutral rate of 5 percent—is appropriately expansionary (AN III). While transmission of the stimulus has been slow (¶9), domestic financial conditions are expected to gradually reflect the monetary easing, which, together with continued credit growth at a pace consistent with healthy financial deepening, should support the return of economic activity to its potential level over the medium term and of inflation within the target range in the near term (¶11). At the same time, it was noted that, if signs emerge whereby price pressures threaten to drive inflation above the mid-point of the new target range and jeopardize the still-very-recent anchoring of inflation expectations, taking into account the lags in monetary policy transmission, the central bank ought to start reversing the easing cycle. This consideration is reinforced by the prospective upward normalization of global interest rates, which could induce depreciation pressures.



Sources: National authorities, and IMF Staff estimates

Neutral Interest Rate for Costa Rica. Latest Estimates

		Expected Inflation Dic-2016	3.00
		Actual Monetary Policy Rate	1.75

Method 1/	Neutral Real Interest Rate (NRIR)	Neutral Nominal Interest Rate (NNIR)	Nominal Monetary Policy GAP (bps) 2/
Uncovered Interest Parity	1.6	4.6	283
Expected-Inflation Augmented Taylor Rule			
2006-2015	2.4	5.4	368
General Equilibrium Model			
2006-2015	2.6	5.6	381
Forward Looking Monetary Model			
1994-2015	1.8	4.8	301
QPM Model			
1996-2015	1.4	4.4	265
Average	1.9	4.9	320

Sources: National authorities and Fund staff estimates.
Notes: 1/ All units expressed as percent points unless otherwise stated. 2/ (bps): Basis points

B. Safeguarding Fiscal Sustainability

18. **The authorities viewed current fiscal trends as unsustainable in the long term.** Staff stressed that, without any policy action, the CG deficit would be above 9 percent of GDP and debt rise to almost 70 percent by 2021. Even in the baseline scenario, which incorporates a fiscal adjustment of 2¼ percent of GDP, the CG deficit would persist at about 5½ percent of GDP by 2021, owing to a mounting interest bill and constitutionally-mandated education spending. Correspondingly, CG debt would grow to 55 percent of GDP by 2021 (from 42½ percent of GDP at end-2015), further raising vulnerabilities and potentially eroding the underpinnings of macroeconomic stability.

19. **The government confirmed that a fiscal adjustment of almost 4 percent of GDP is needed to stabilize the public debt ratio.** In staff's estimates, budget retrenchment measures amounting to 3¾ percent of GDP over the medium-term would suffice to steady the share of public debt to GDP below levels which tend to weaken macro stability in emerging markets, while allowing for some desirable increases in growth-friendly capital spending (Annex III). The authorities agreed and are prepared to implement a fiscal consolidation package expected to gradually close this fiscal sustainability gap (¶21).

20. **To pace consolidation, the authorities aptly intend to maintain a balance between lowering the sustainability gap and limiting any adverse impact on growth.** The front-loaded fiscal consolidation appropriately planned by the government, with somewhat less than two-thirds of the total adjustment in 2016–17 and smaller corrections in subsequent years, would have only moderate output cost over the forecast period (¶12 and AN VI). Staff underscored that further postponing fiscal retrenchment would be costly, since, the longer the delay, the larger will be the improvement in the primary balance required to stabilize the public debt ratio. The authorities had the same concern. They asked staff to explain publicly that failing to deliver on the fiscal consolidation plan would increase the risk of an abrupt shift in investor sentiment and of acute financial market tensions, thus forcing a disorderly adjustment.

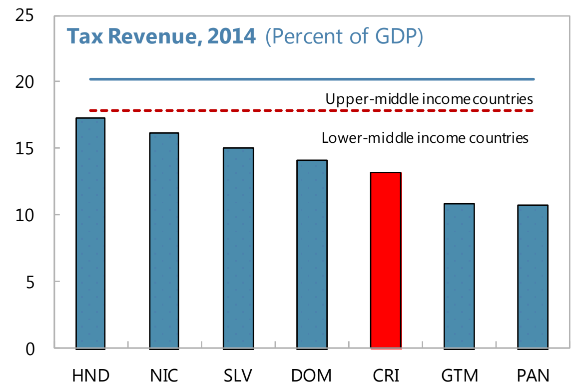
Costa Rica. Fiscal Consolidation Path

(Percent of GDP)

	2016	2017	2018	2019	2020	2021	Total
Total Adjustment	0.8	1.6	1.0	0.1	0.1	0.1	3.8
Baseline	0.8	1.1	0.4	-	-	-	2.3
Revenue	0.4	1.0	0.3	-	-	-	1.7
Expenditure	0.4	0.1	0.0	-	-	-	0.6
Additional Adjustment	-	0.6	0.7	0.1	0.1	0.1	1.5
Revenue	-	0.3	0.5		-	-	0.8
Expenditure	-	0.2	0.2	0.1	0.1	0.1	0.7

Source: Fund staff estimates.

21. **The authorities' fiscal adjustment plans adequately focus on raising revenues, with a sizable contribution from expenditures, but full implementation is critical.** The measures in the authorities' plans broadly follow staff advice, including recommendations provided in past technical assistance by the Fund and other multilaterals.



Source: WEO and Fund staff calculations.

- The government's strategy envisions about 2½ percent of GDP in higher taxes, consistent with staff's advice that about two-thirds of the adjustment should consist of increases in receipts, given Costa Rica's low revenue effort compared to other upper-middle-income countries. VAT and income tax reforms would boost collections by slightly more than 2 percent of GDP over the medium-term, and other provisions—reduced exemptions, further amendments to the corporate income tax and anti-tax evasion measures—would generate almost ½ percent of GDP. The VAT reform envisages broadening the base to include services and a gradual increase in the rate from 13 to 15 percent, starting in 2017, as well as separate increases of taxes on sales of vehicles and real estate. The bill also foresees a radical narrowing of the basic goods basket, conditional on the establishment of a transfers system that would make the VAT reform broadly revenue-neutral for lower-income households. The income tax reform introduces additional marginal rates of 20 and 25 percent on higher-income brackets, unifies the rate on capital income at 15 percent, and subjects capital gains to tax.

- Furthermore, the authorities have already identified legislative changes—including to curtail growth of pensions paid out of the budget and transfers to decentralized entities—and administrative measures that would yield the 1¼ percent of GDP of cuts in current expenditures also required to fully close the sustainability gap.

- The authorities share staff's view that only the full adjustment of 3¾ percent of GDP needed to stabilize the public-debt-to-GDP ratio would be adequate from a macro-economic perspective. Indeed, a partial fiscal adjustment as assumed in the baseline scenario—with tax reform proposals currently in Congress watered down and insufficient efforts to contain spending—would result in continued large fiscal deficits driven mainly by a mounting interest bill, and significant additional debt accumulation subject to important downside risks under less favorable macroeconomic conditions (¶11 and Annex III). This would further raise vulnerabilities and potentially erode the underpinnings of macroeconomic stability.

- The alternative full adjustment scenario assumes Congressional approval of all submitted measures, yielding 2¾ percent of GDP. Moreover, it includes administratively-determined spending cuts that would contain the growth of current spending—mostly transfers and public sector wages—to keep it throughout the medium term below the expansion of nominal GDP.

Costa Rica. Central Government. Fiscal Consolidation Measures
(in percent of GDP)

	Authorities' plans		Baseline Scenario 2/ (I)	Adjustment Scenario 3/	
	Total	Submitted to Congress, Staff Assessment 1/		Additional Measures (II)	Total adjustment (I + II)
Total adjustment	**4.0**	**2.9**	**2.3**	**1.5**	**3.8**
Revenue	2.7	2.5	1.7	0.8	2.5
Anti-tax evasion	0.5	0.2	0.2	-	0.2
VAT	1.3	1.3	0.5	0.8	1.3
Income tax	0.6	0.6	0.6	-	0.6
Corporate income tax	0.2	0.2	0.2	-	0.2
Vehicles and real estate tax	0.2	0.2	0.2	-	0.2
Expenditure	1.3	0.4	0.6	0.7	1.3
Transfers	0.4	0.4	0.4	-	0.4
Wages 4/	0.6	-	-	0.6	0.6
Miscellaneous cuts in 2016 budget	0.2	-	0.2	-	0.2
Goods and services	0.1	-	-	0.1	0.1

1/ On the revenue side, includes staff's assessment of the expected yield from revenue measures submitted to Congress. On the expenditure side, includes measures already submitted to Congress.

2/ In addition to the lower yield assumed from anti-tax evasion meaures, the difference with the authorities' plans is that it incorporates only measures that are deemed to have a higher probability of approval. The assumption in the baseline is that the proposed VAT tax rate increases will not be approved by Congress.

3/ Reflects total adjustment needed to close the sustainability gap.

4/ Includes measures to contain nominal growth of public wages, so that their share in GDP is gradually reduced. Also includes freeze in hiring outside education, and cuts to public compensation bonus schemes.

22. **The government is considering steps to ensure durable commitment to contain expenditures, thus shoring up parliamentary support for fiscal consolidation.** The executive power has a minority representation in Congress; hence approval of most budget consolidation measures requires the cooperation of opposition parties. Notwithstanding the broad consensus across the political and societal spectrum that fiscal retrenchment is needed, some opposition parties and influential lobbies have called for greater emphasis on lowering outlays. In this regard, bills currently under discussion to reform public employment conditions—thus preventing excessive automatic increases in current outlays—and a recently presented fiscal rule proposal—aimed at the preservation of government debt sustainability, broadly in line with staff advice though still

requiring greater specification of its key elements—are welcome (AN VI). An agreement is likely to require simultaneous advances on all aspects of the consolidation package. Despite promising moves toward a compromise, the process could still be derailed.

23. **The authorities agree that the pension system's financial position also has to be strengthened in the long run.** The pension plan run by the Social Security agency (CCSS) and the special regime for the judiciary are actuarially imbalanced. They are projected to turn a cash deficit over the long term due to system maturation and population aging. Preliminary projections suggest that an additional adjustment equivalent to about 1½ percent of GDP would be required at the general government level to ensure actuarial equilibrium of the CCSS for the next 50 years (AN VI). A study commissioned by the CCSS and the Superintendence of Pensions to be released in 2016 will determine the size the imbalance more precisely. The authorities have nevertheless already taken some measures, including the elimination of the early retirement option, and are considering increasing minimum contributions and gradually raising contribution rates over the medium-term above the scheduled increases already stipulated in 2005. Several legislative proposals currently in Congress also contemplate parametric adjustments to the special regime for the judiciary.

C. Improving the Monetary and Exchange Rate Policy Framework

24. **Staff commended the authorities for their achievements in lowering inflation and endorsed their decision to further lower the target range.** The central bank's monetary policy has succeeded in preventing any durable deviations from the target range since 2009 and anchoring inflation expectations to the center of the 3-5 percent target range introduced in 2014. Based on this, the staff supported the central bank's decision to take advantage of the recent sharp decline in inflation to revise the target range to 2-4 percent, in line with average inflation of trading partners. At the same time, staff emphasized, this move should be accompanied by fiscal consolidation to prevent the risk that an excessively tight monetary policy might be needed to contain inflation within the target range.

25. **The authorities have made steady progress toward full-fledged inflation targeting, but additional steps would be useful.**

- The mission underlined that removal in early 2015 of the legal constraint to exchange rate flexibility posed by the XR band is a milestone toward establishing inflation as the undisputed anchor of monetary policy and lowering XR pass-through to inflation. It also acknowledged that the authorities' preference for maintaining a significant role for active XR management, with an FX intervention rule aimed both at averting excessive volatility and at countering unwarranted deviations from medium-term fundamentals, is understandable, in light of the large financial dollarization.

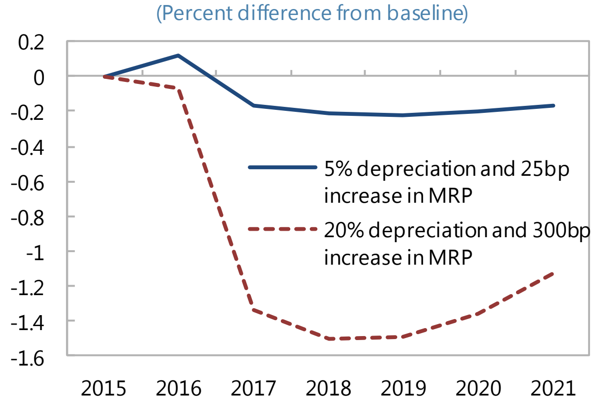
- However, staff advised that a gradual, contained increase in the flexibility of the exchange rate, in line with the stated policies of the central bank, would be important to further strengthen the credibility of the inflation-targeting framework, as well as to enhance the role of the exchange rate as a shock absorber and 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, while more generally discouraging dollarization. The latter should also be pursued with the tightening of macro-prudential norms (¶28). Moreover, the mission questioned whether the lack of transparency of the triggers for the FX-intervention-rule aimed at curbing volatility might not, under circumstances less favorable than those presently prevailing (¶4), undermine confidence in the full subordination of XR management objectives to the inflation target. The central bank agreed in principle, but emphasized that allowing more XR flexibility and more transparency about the intervention policy should proceed in parallel with the transfer of all FX transactions to the open market to make the XR less prone to speculative moves. Staff saw merit in deepening the FX market, thereby facilitating higher XR flexibility.

- Fostering growth of the underdeveloped secondary market for government securities, including through use of standardized simple instruments with conventional maturities, was also considered desirable to reinforce the effectiveness of monetary policy and enhance resilience to external financial shocks.

D. Financial Stability

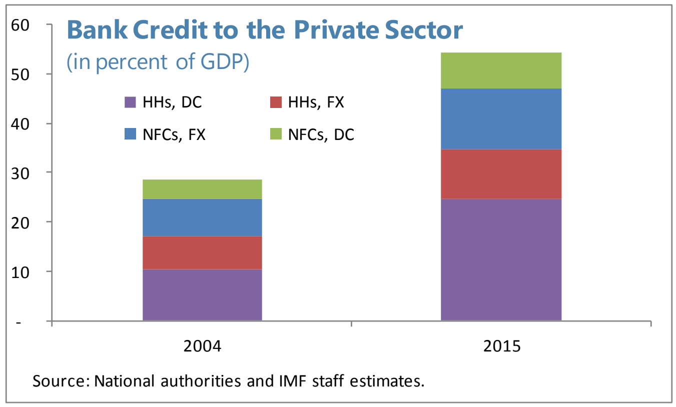
26. **The authorities acknowledge that currency mismatches in the private sector pose the key risk to financial stability.** Staff noted that Costa Rica's current level of credit and broader financial development is well below the threshold beyond which risks to stability outweigh the benefits from the positive impact on growth (AN IV). In particular, the current pace of overall credit expansion, not high by historical standards, seems consistent with continued healthy financial deepening. Moreover, a top-down stress test conducted by staff depicts a sound banking sector that could absorb a range of sizable shocks (AN II). However, large dollarization of bank loans was jointly identified as a serious and intensifying concern. Indeed, notwithstanding the overall long FX position of the banking system, a large depreciation of the colón may impact asset quality, given unhedged FX liabilities in large segments of the household and corporate sectors. In particular, staff pointed out that, according to the stress tests, the deterioration of bank capitalization, and related contingent liabilities for the sovereign, could be substantial (AN II). As for the macro impact, general equilibrium model simulations suggest that loan impairment and implied lower credit growth from, say, a twenty percent depreciation could reduce GDP growth by about 1½ percent over the medium-term (AN I).

Effect on Real GDP of Adverse Shocks on FX and NPL
(Percent difference from baseline)



Sources: IMF staff calculation based on RES FSGM
Note: NPL= Non Performing Loans; MRP= Market Risk Premium

27. **High net foreign liabilities of banks, growing household leverage, and sovereign exposures represent other vulnerabilities of the financial sector.** After a period of large bank borrowing abroad incurred to fund the rapid growth of FX credit to residents, Costa Rica is among the countries in the region with highest reliance on foreign bank funding, raising concerns about rollover risks. Indeed, staff analysis, based on network model simulations of spillovers from asset quality and capital shocks in international banks, suggests that reduced foreign bank funding could lead to a significant reduction in credit in Costa Rica (Panel 5 and AN II). While the increase in private sector debt has been limited compared to other emerging markets,[7] in Costa Rica it has been mainly concentrated in the household sector, and officials are aware that rising household leverage, not least via credit by non-bank commercial entities, could also endanger asset quality. Finally, it was observed that, though starting from the low levels prevailing before the global crisis, continuing brisk accumulation of holdings of government debt by banks, boosted by the large fiscal deficits, is an additional hazard, particularly in an environment where, over the medium term, interest rates are likely to increase. Although staff recognized that, based on its analysis, banks could currently sustain losses from a significant spike in interest rates on domestic government bonds without capital falling below regulatory requirements (AN II), it also expressed concern that risks from mark-to-market losses on bank exposures to the sovereign will mount without adequate fiscal consolidation.



28. **Supervisors recognized these risks and are taking positive steps to gradually reduce them.** Staff welcomed the recent increase in capital risk-weightings on FX loans to unhedged borrowers and the extension of reserve requirements to medium- and long-term foreign bank borrowing (in addition to the existing requirement on short-term foreign borrowing). Officials explained that additional measures to further reduce vulnerabilities are currently under consideration. These include: (i) stricter provisioning on FX loans to unhedged borrowers and household debt with income-to-debt service ratios above 30 percent; (ii) counter-cyclical provisioning; and (iii) higher risk-weightings for household mortgages with high loan-to-value and income-to-debt service ratios. The mission deemed that these steps were appropriate, but it was not possible yet to determine whether they would be sufficient to achieve substantial reductions in credit dollarization and rollover risks. Staff recommended that further tightening of provisioning on FX bank lending and of reserve requirements on FX bank borrowing (the latter requiring Congressional action) should be contemplated, if there is no evidence of a reduction in banks' FX exposures within a reasonable time frame. Additionally, the coverage of the credit bureau should be

[7] According to the October 2015 Global Financial Stability Report, private sector debt of emerging markets increased from just over 60 percent of GDP in 2005 to almost 125 percent of GDP in 2014.

extended to loans to households granted by non-bank entities to better assess household leverage and preserve asset quality.

29. **Staff urged speedier implementation of the pending 2008 FSAP recommendations.** Key points (Annex I) include empowering the Superintendence of Financial Institutions to conduct consolidated supervision, providing legal protection to bank supervisors in line with international best practice, strengthening bank resolution procedures, and broadening the supervisory perimeter to non-bank financial institutions, all of which require new legislation. The authorities remarked that advances remain slow due to the crowded legislative agenda, but also stressed that introduction of further legal protection for bank supervisors faces strong opposition and is constitutionally controversial. Staff commended the progress made towards full implementation of risk-based supervision, although efforts to bring it up to best standard should be stepped up. The FSAP update tentatively planned for 2017 will allow for a more thorough assessment of the financial system and determine the need for additional measures.

30. **Officials reiterated their support for gradual adoption of Basel III standards.** Staff concurred that it would further improve resilience of the financial system and thus welcomed the recent enactment of the Basel III Liquidity Coverage Ratio. The regulatory and risk management frameworks would also greatly benefit from introducing Basel III definitions of capital, a capital conservation buffer, and a leverage ratio. Staff analysis shows that this could be accomplished without significant detrimental effects on growth.

31. **It was agreed that further improvements in the effective supervision of cross-border financial operations are critical for stability.** Such a requirement has become more urgent because financial linkages within the region have been growing, though they are not yet fully understood, owing in part to data limitations but also to legal restrictions on information sharing. Enhancing transnational monitoring is especially important for Costa Rica, since conglomerate BCT operates in Panama and regional integration plays an important role in the transmission of financial shocks (AN I). In this respect, staff welcomed Costa Rica's participation in the system of multilateral MoUs and in the Central American Council of Banking Supervisors. In addition, strengthening the AML/CFT supervision of cross-border financial operations and implementing the recommendations of the GAFILAT mutual evaluation report would assist in safeguarding the financial sector against illicit financial flows, notably to and from higher-risk jurisdictions.[8] Swift adoption at the national level of the relevant recommendations in the WHD Cluster Surveillance Report on Financial Integration in CAPDR (Annex II) and strengthening of the national institutional framework in support of the medium-term Regional Macroprudential Policies Project for CAPDR would also help identify likely spillovers and assess joint risks.

[8] GAFILAT is the FATF-style regional body of which Costa Rica is a member.

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

Prudential Supervision and Regulation

- Amend the legal framework in order to provide protection for supervisors while performing their responsibilities in good faith.
- 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.
- Apply higher risk weight ratios to unhedged borrowers for capital adequacy purposes.
- Modify the funding arrangements for supervision, in line with international best practices.

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.
- 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.
- Improve the early warning system, to allow the adoption of remedial actions in a timely manner.
- 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.
- Establish a deposit insurance scheme, in line with international best practices.
- Amend the bank resolution legal framework to include purchase and assumption type techniques.
- Enable voluntary, extra-judicial corporate restructuring agreements.

Note: See Annex I for details on the status of implementation.

Costa Rica. Summary of Stress Test Results

	All Banks	State Owned	Domestic Private	Foreign
Summary of Results				
Solvency				
Pre-shock CAR	17.0	18.0	12.2	15.9
Impact of (percentage points of the original RWA)				
Increase in NPLs 1/	-1.7	-1.7	-1.6	-1.8
Increase in interest rates 2/	-0.1	-0.3	-0.5	0.3
Exchange rate depreciation 3/	-2.2	-2.2	-2.4	-2.2
Post-shock CAR (percent of post-shock RWA)	13.1	13.9	7.8	12.2
Change in CAR (all fundamental shocks)	-4.0	-4.1	-4.4	-3.7
Impact of interbank contagion				
Post-contagion CAR	13.1	13.9	7.8	12.2
Post-contagion CAR if profits used for defense	13.5	14.5	8.1	12.6
Liquidity 4/				
Liquid assets/total assets				
Pre-shock	22.6	22.3	19.9	23.4
Post-shock (after 5 days)	4.0	2.4	4.8	7.1
Liquid assets/short-term liabilities	0.0	0.0	0.0	0.0
Pre-shock	69.9	63.5	80.7	84.2
Post-shock (after 5 days)	36.3	16.7	106.9	117.1

Source: SUGEF; and IMF staff estimates.

1/ Assumes an increase in NPLs of 8 percent of performing loans; and a 25 percent provisioning rate. The sectoral shock to NLP assumes that 6 and 10 percent of the loan portfolio to the construction and trade sectors respectively become non-performing.

2/ Assumes a 3.5 percentage points nominal interest rate increase.

3/ Assumes a 14 percent depreciation of the FX rate, leading to 6 percent of FX loans becoming non-performing, and a 50 percent provisioning rate.

4/ Assumes a 10 and 8 percent per day withdrawal of demand deposits in domestic and foreign currency respectively; and a 5 and 3 percent per day withdrawal of time deposits in domestic and foreign currency respectively.

Figure 1. Costa Rica: Stress Test Results

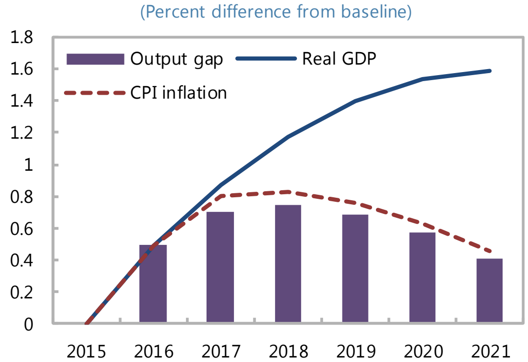
Source: SUGEF, and IMF staff estimates.

Note: The *Credit Risk* Shock assumes an increase in NPLs of 8 percent of performing loans; and a 25 percent provisioning rate. The *Interest Rate* Shock assumes a 3.5 percentage points nominal interest rate increase. The *FX Shock* assumes a 14 percent depreciation of the FX rate, leading to 6 percent of FX loans becoming NPL, and a 50 percent provisioning rate. The *Liquidity Shock* assumes a 10 and 8 percent per day withdrawal of demand deposits in domestic and foreign currency respectively; and a 5 and 3 percent per day withdrawal of time deposits in domestic and foreign currency respectively.

E. Structural Reforms

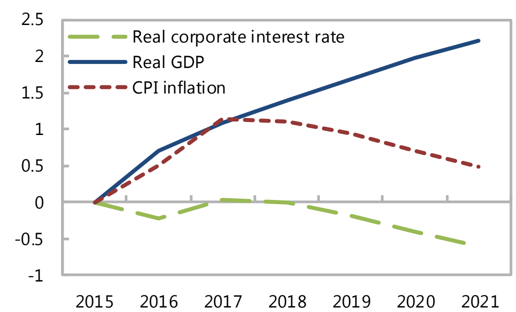
32. **Further structural reforms are needed to buttress Costa Rica's competitiveness and promote inclusive growth.** While Costa Rica ranks favorably in many business indicators and has been a regional leader in attracting foreign direct investment, further steps are needed to maintain the country's competitive edge (Box 1). Staff argued that a better separation of electricity generation from the natural monopoly element associated with electricity transmission and distribution would allow private generators to compete more effectively with the state-owned enterprise ICE, thereby increasing efficiency. Besides, revised price-setting procedures to enhance cost discipline could help bring down electricity tariffs, especially for the industrial sector. The authorities observed that the private sector already participates in electricity generation and that overall electricity provision coverage and reliability in Costa Rica are high in the region. With regards to human capital, officials deemed that there were significant margins to improve the efficiency of public social and education spending, which would help protect vulnerable groups and lift outcomes without jeopardizing the budget. Expanded child-care provision and early childhood education as well as ameliorating infrastructure, including for IT, would facilitate increased female labor force participation (AN IX).

Real Effect of Halving Collateral Requirements
(Percent difference from baseline)



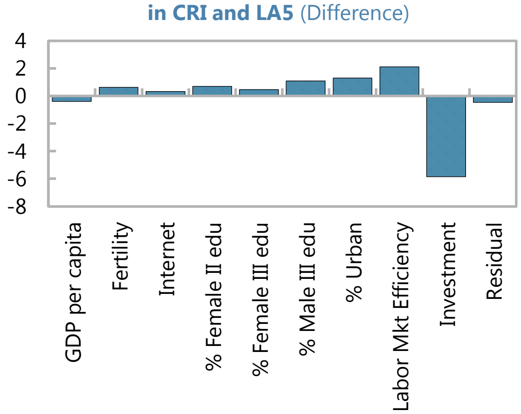
Sources: IMF staff calculation based on RES FSGM

Real Effect of Reducing Interest Rate Spreads
(Percent difference from baseline)



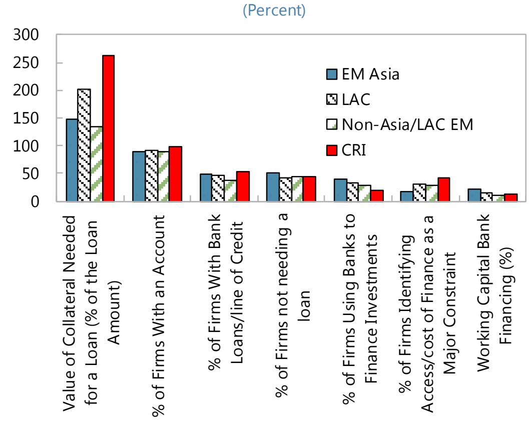
Sources: IMF staff calculation based on RES FSGM
Note: The reduction in interest rate spreads is modeled as a 100bp decrease in market risk premiums

Contribution to Female Labor Force Participation in CRI and LA5 (Difference)



Sources: ENAHO, 2012.

LAC and EMs: Enterprise Use of Financial Services
(Percent)



More generally, discussions underscored that addressing infrastructure bottlenecks, especially in the transportation sector—as the fiscal adjustment creates space for higher public investment (¶19)—and streamlining business regulations, not least to facilitate entry of new firms, would also stimulate competiveness and help accelerate potential growth.

33. **Staff analysis indicates that the financial sector remains underdeveloped**, **especially outside the banking area, relative to the country's level of income and other determinants** (¶26 and AN IV). Also, while Costa Rica ranks high for inclusion of households, that of enterprises is low relative to the country's fundamentals (AN V). It would be important to take measures to foster capital market development including through more market-friendly debt management and issuance strategies that promote larger secondary markets for government securities (¶25), as well as through better protection of investor rights and development of a larger institutional investor base. Stepping up competition among banks, refining loan-provisioning rules to avoid high collateral requirements being used as a substitute for proper credit-risk analysis, and further ameliorating the judicial enforcement of secured and unsecured claims would also help reduce financial constraints and support financial deepening. The authorities agreed that these actions should permanently lower interest rate spreads and borrowing costs, with positive effects on credit, investment and growth.

STAFF APPRAISAL

34. **Macro prospects are generally benign, though downside risks, mainly from the weak fiscal position, prevail.** Costa Rica's economy has been expanding below trend for the past three years. Despite a growth uptick in 2015, unemployment remained high and inflation sharply declined, under the combined effect of the widening output gap and the drop in oil prices. Nonetheless, the currency has been stable and reserve accumulation resumed strongly in 2015, as the current account deficit narrowed and foreign direct investment inflows remained strong. Growth is expected to pick up again in 2016, with inflation moving to the middle of the new target range by end-year. Output is anticipated to return to potential over the medium term. However, high budget imbalances cloud the horizon. The real effective exchange rate continues broadly in line with economic fundamentals.

35. **Persistence of large fiscal deficits and a growing public debt, as well as the high credit dollarization, have increased vulnerability to financial shocks**. In the absence of policy action, public debt is unsustainable in the long term and could reach close to 70 percent of GDP by 2021, with attendant funding and rollover concerns. Substantial currency depreciation would likely trigger an increase in non-performing loans given banks' sizable foreign currency lending to non-hedged private borrowers. As a small open economy, which relies on agricultural products and tourism for a third of its exports and imports all its oil, Costa Rica is also exposed to external trade shocks.

36. **Current economic conditions call for immediate fiscal tightening and the continuation of an accommodative monetary policy**. The authorities' intention to start gradually reducing the fiscal deficit from this year onward is timely. The ongoing accommodative monetary policy,

warranted by the low inflation and negative output gap, would help offsetting the short-term contractionary effects of the fiscal adjustment.

37. **A sizable fiscal correction is the key priority and there are still margins to implement it at a measured pace**. A total budgetary adjustment of 3¾ percent of GDP over the medium-term is required to stabilize the public debt ratio at a safe level. This consolidation effort is consistent with the plans announced by the government to increase revenues by about 2½ percent of GDP and decrease expenditures by around 1¼ percent of GDP. To minimize the negative impact on output and since financing is still available, the correction should be phased gradually over 2016-2020, though with a significant front-loading to lend credibility to the fiscal adjustment package.

38. **Budget consolidation should rely mainly on tax increases, given a comparatively low revenue effort, but expenditure containment is a necessary complement.** It is advisable to bring Costa Rica's tax collection closer to that of other upper-middle income countries, while increasing the progressivity of the tax system, as in the government's plan. Indeed, the announced tax measures aptly include a broadening of the base and a rate increase for the VAT, the introduction of two new brackets in the personal income tax for high earners, the reduction of tax exemptions, and a strengthening of sanctions against evasion. A refund system would compensate lower-income households for the VAT hike. A reduction in the growth of current expenditures below nominal GDP growth, in particular of public sector wages and transfers, is also necessary to fully close the fiscal sustainability gap. Current legislative proposals for public employment reform to prevent excessive automatic wage increases and for a fiscal rule to ensure public debt sustainability are useful tools to buttress longer-term fiscal discipline.

39. **The authorities have appropriately strengthened the inflation-targeting framework, but greater XR flexibility is desirable**. The central bank has managed to lower inflation and to anchor inflation expectations to the center of the 3-5 percent target range introduced in 2014, thus creating the conditions for the further downward revision of the target range in early 2016. The XR band was successfully removed in early 2015, thereby confirming inflation as the key objective of monetary policy, while maintaining XR stability, thanks partly to recurring FX interventions and a favorable external environment. However, a gradual increase in XR flexibility, which could be facilitated by a concurrent deepening of the FX market, would enhance the XR's role as a shock-absorber and encourage awareness by private agents of two-way risks in exchange markets. An improvement in the central bank's communication about FX interventions is also warranted.

40. **Regulatory upgrades should primarily aim at reducing financial dollarization, but it is important also to strengthen cross-border supervision and creditworthiness scrutiny**. FX lending, funded by foreign borrowing, is growing faster than lending in colones, despite the recent tightening of reserve requirements on bank foreign borrowing and increase in capital risk weights for foreign currency loans to un-hedged borrowers. Although staff analysis suggests that associated risks are currently manageable even under extreme stress scenarios, further strengthening of prudential measures may be necessary should this trend continue. The implementation of pending 2008 FSAP recommendations and the gradual adoption of Basel III standards, as well as

improvements in cross-country supervision, should reinforce the existing regulatory and supervisory framework. The extension of the credit bureau's coverage would facilitate credit risk monitoring and thus also support financial deepening. In addition, removing competition distortions between public and private banks would help lower interest rate spreads and improve credit supply.

41. **Boosting Costa Rica's growth potential and competitiveness requires energy sector reform, infrastructure upgrades, and education reform**. Greater private sector participation in the energy sector along with a review of tariffs would allow for a reduction in the cost of electricity for firms. An additional investment effort is needed to address infrastructure bottlenecks, in particular in the transportation sector. Sizable government education expenditures, already close to the constitutional mandate of 8 percent of GDP, should put more emphasis on early childhood and the secondary level with the goal of reducing drop-outs in secondary grades. More generally, gains in efficiency of education and social spending would especially benefit the most vulnerable segments of the population and foster more inclusive growth.

42. **It is recommended that Costa Rica remain on the standard 12-month consultation cycle.**

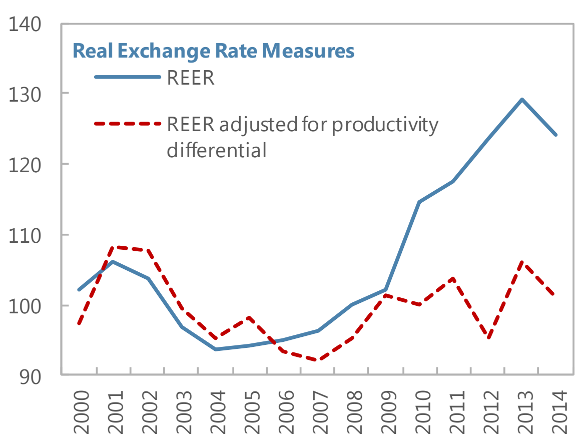
Box 1. Costa Rica: External Stability Assessment

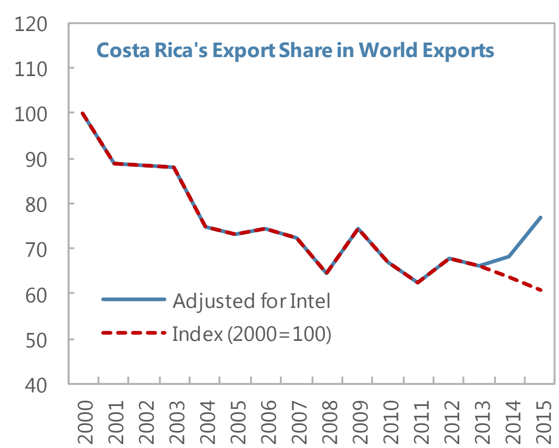
The real effective exchange rate (REER) continues to be broadly in line with fundamentals. Staff has used various approaches to assess the appropriateness of the external balance and real exchange rate. These include descriptive quantitative indicators, regression-based methods to estimate the distance of the current account (CA) balance and the REER from the values determined by their fundamentals and desirable policy settings, as well as stability conditions for net foreign assets.

The REER has been stable in 2015 and early 2016, at a level about 6 percent higher than at the beginning of 2014. In the first half of 2014, nominal depreciation outpaced a growing inflation differential with the main trading partner (USA), resulting in substantial REER depreciation that eliminated a third of the accumulated 30 percent REER appreciation since 2003. In the second half of 2014, however, the REER appreciated by 14 percent, reversing the depreciation occurred during the first half of the year. The REER adjusted for the Balassa-Samuelson effect shows that total REER appreciation since 2003 was driven by the labor productivity differential between Costa Rica and the U.S., and therefore reflects changes in fundamentals, rather than unsustainable developments.

At the same time, the CA deficit has declined and the non-Intel export market share has increased (see chart below). The CA deficit has improved reaching around 4 percent of GDP in 2015 on the back of low fuel prices and continued strong positive services balance. While the Intel exit in 2014 had a significant impact on Costa Rican exports (16 percent less cumulatively in 2014-15), it had a muted impact on the overall trade balance due to the small domestic value added of the company. At the same time, non-Intel exports have gained export market share in the world markets increasing by 3 percent relative to 2014.

The financing structure of the CA and somewhat low external liabilities mitigate risks. The CA is largely financed by FDI inflows. While the IIP is negative at almost 45 percent of GDP, FDI comprises almost 65 percent of total liabilities. The external debt profile presents no sustainability concerns, with the external debt-to-GDP ratio set to decline into the medium term and a low share of short-term debt. Net international reserves stood at 5.8 months of non-maquila imports of goods and services at end-2014 and are above the Fund's composite reserve adequacy metric.





Sources: INS; St. Louis Fed; national authorities; and Fund staff calculations.

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

IMF's multilaterally consistent estimates suggest that Costa Rica's REER is broadly in line with fundamentals and desirable policy settings both in the short term and relative to medium-term benchmarks.

- The macro-balance approach in the External Balance Assessment (EBA) estimates the sustainable CA implied by existing fundamentals and desirable policies. It points to a current account norm deficit of 4.7 percent of GDP in 2015, which is about 0.8 percent of GDP larger than the actual cyclically-adjusted deficit of 3.9 percent of GDP in 2015, implying a REER undervaluation of 3.5 percent. Identified policy gaps in Costa Rica are negative and significant at -1.7 percent of GDP, suggesting further undervaluation if corrected. Health expenditures, which are significantly higher than the world average, as well as recommended fiscal adjustment, explain 70 and 30 percent of the policy gap respectively.
- The macro-balance approach based on the CA panel regression (which relies on medium term fundamentals and assesses the medium-term current account) estimates REER overvaluation of 3.1 percent.
- The external sustainability (ES) approach, on the other hand, finds a moderate overvaluation of 6.8 percent. However, taking into account the favorable financial structure of external liabilities of Costa Rica, by excluding FDI from the stock of total liabilities, would imply an undervaluation of a similar size.

Staff views the results based on the macro-balance approaches, which both assess the external sector to be neither over- or undervalued, as the most reliable. The simple average across the different methodologies supports this assessment as well. Staff concludes that Costa Rica's REER is in line with fundamentals.

Costa Rica: Implied Undervaluation ("+" = Overvaluation)

Regression-based methods	CA norm	CA projected/ cyclically-adjusted	REER gap (updated)	REER gap (2014 AIV)	REER gap (2012 AIV)
Macroeconomic Balance	-3.2	-3.9	1.9	-0.8	7.9
External sustainability (ES)	-2.4	-4.5	6.8	13.2	8.5
ES (NFA exclud. FDI)	-7.2	-4.5	-7.1	-5.9	NA
EBA					
Macroeconomic Balance	-4.7	-3.9	-2.1	-4.7	8.5
Average			-0.1	0.5	9.9

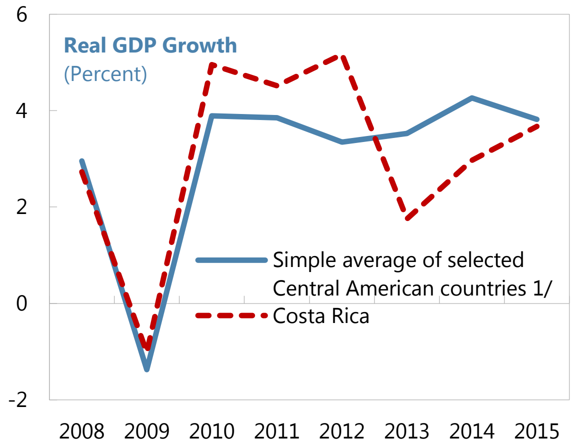
Sources: Fund staff estimates.

The recent withdrawal of Intel operations does not reflect deterioration in external competitiveness. First, the shut down operations had a very small value added. Competitiveness of Costa Rica, as a well-educated upper middle-income country, should be assessed against other middle-income countries that operate in a different market segment with a higher value added. Second, while the withdrawal had a sizable effect on total exports, non-Intel exports gained market share in 2014 and are expected to improve further in 2015. Third, Intel research operations remained in Costa Rica indicating stable demand for highly qualified labor in the country.

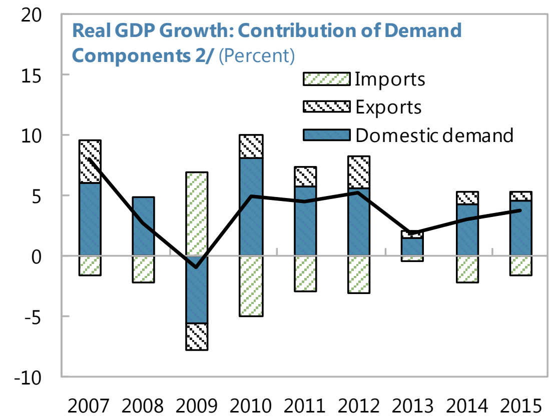
While regulatory quality and efficiency has improved, some sectors continue to weigh on overall competitiveness. Costa Rica gained 21 positions in the 2016 Doing Business Survey by the World Bank driven by improved access to credit, introduction of an electronic tax payment system, and easier access to electricity. According to the Global Competitiveness Index by the World Economic Forum, however, Costa Rica's competitiveness has remained at the same level as last year. Unsatisfactory infrastructure, concerns over inefficient government spending, and insufficient investor protection continue to weigh on competitiveness.

Figure 2. Costa Rica: Recent Developments and Prospects, Real Sector

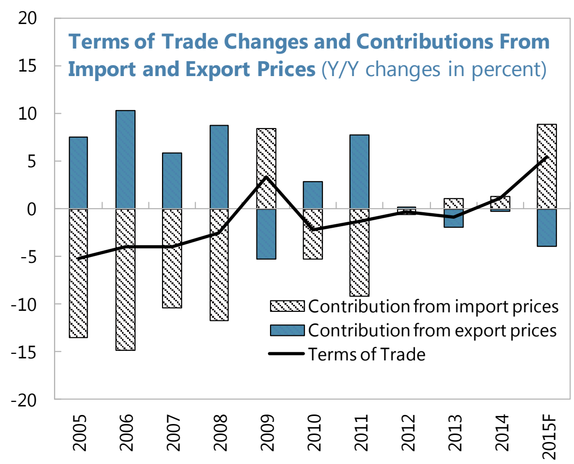
Real GDP growth has picked up over the last few years, catching up with trends in other CAPDR countries…



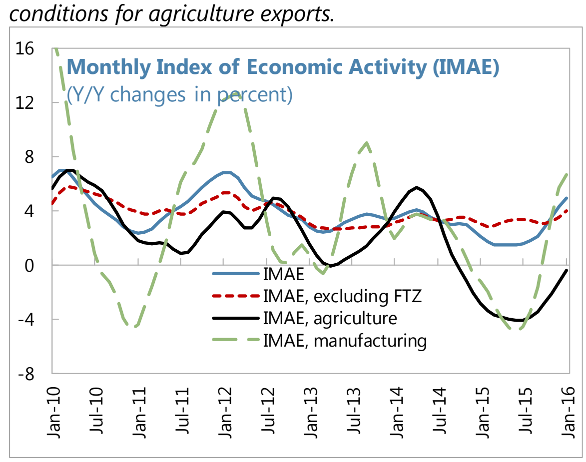
… as a result of stronger domestic demand growth, which in 2015 benefitted from…



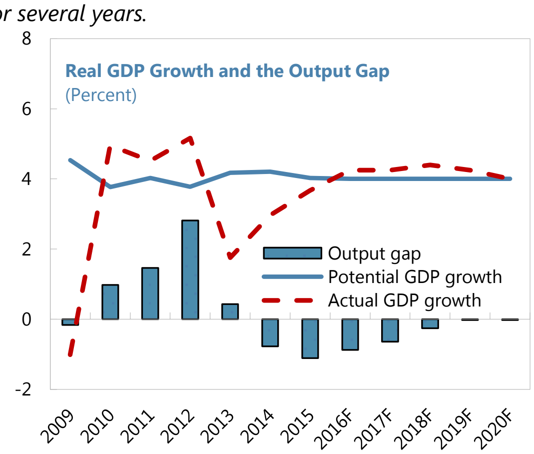
…. improved terms of trade that helped offset…



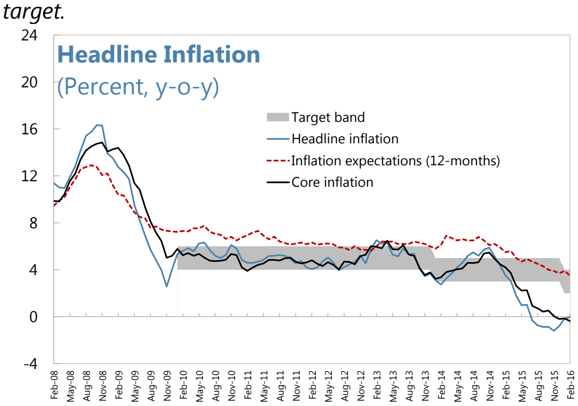
… the impact of Intel's closure and adverse weather conditions for agriculture exports.



As a result, a moderate negative output gap has opened up that is expected to persist, while gradually shrinking, for several years.



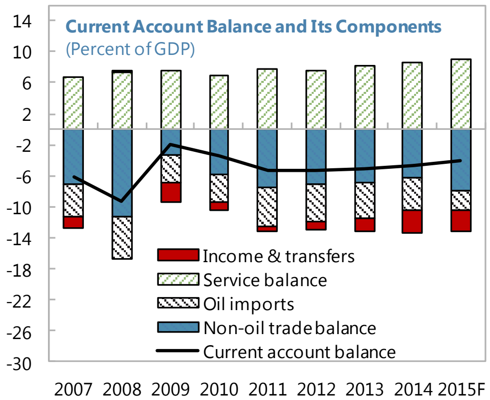
Meanwhile, inflation has turned negative, driven by lower oil prices, and inflation expectations have converged to the target.



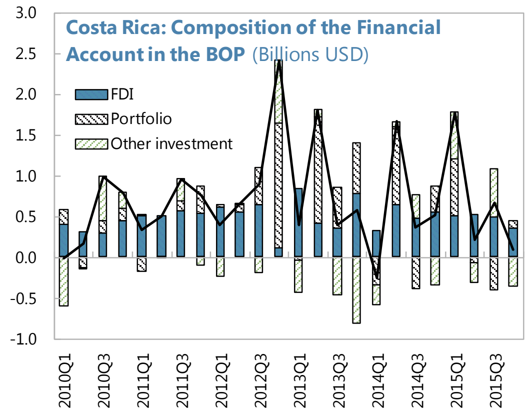
Sources: National authorities; Haver Analytics; and Fund staff calculations.

Figure 3. Costa Rica: Recent Developments, External Sector

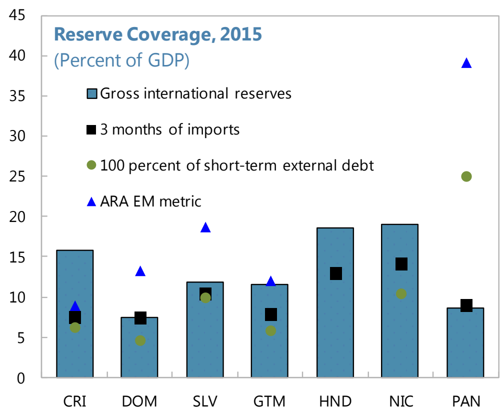
In 2015, a lower current account deficit driven mainly by lower oil prices…



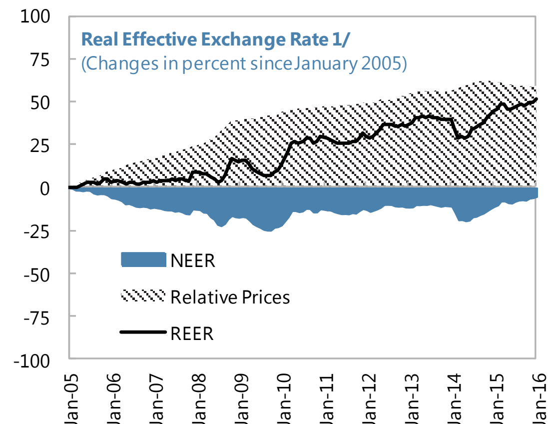
…. together with resilient FDI, new government external bond issuance, and higher bank net foreign liabilities…



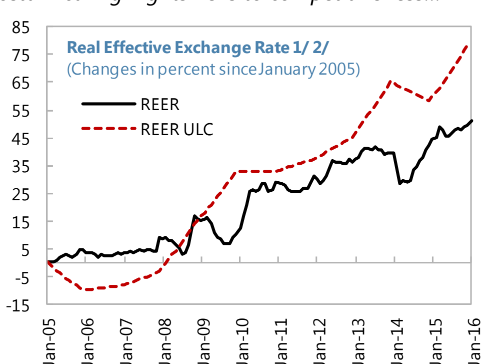
…. have resulted in strong international reserve accumulation to levels above adequacy metrics.



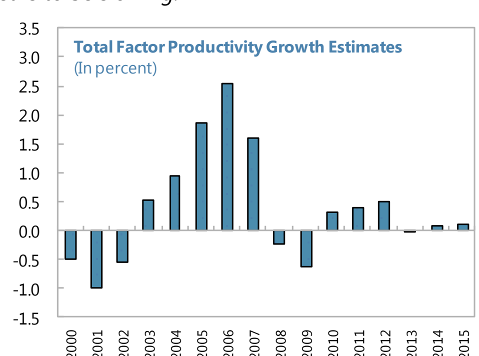
The real effective depreciation of early 2014 has been reversed driven both by nominal appreciation and inflation differentials.



While the real exchange rate is assessed to be in line with fundamentals, a ULC-based REER including public wages in Costa Rica highlights risks to competitiveness…



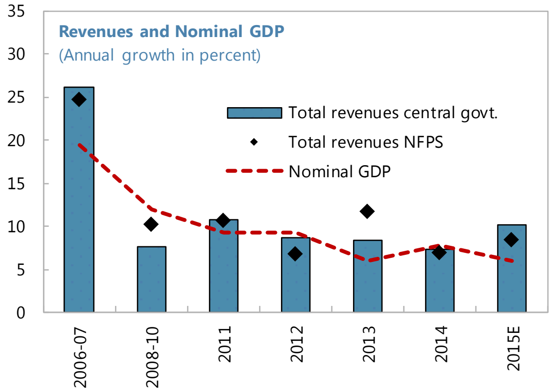
…if wages in public wage inflation were to spill over into the private sector, at a time when productivity growth appears to be slowing.



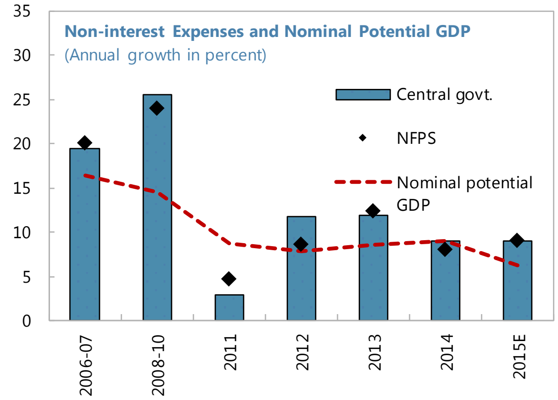
Sources: WEO; national authorities; and Fund staff calculations.
1/ Increase implies appreciation.
2/ The REER based on ULC was calculated with data for 73 percent of the trading partners. Wages are for total employment in Costa Rica and manufacturing sector in trading partners

Figure 4. Costa Rica: Recent Developments and Prospects, Fiscal Sector

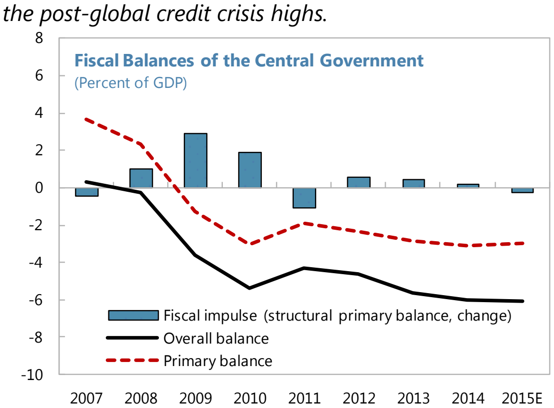
In 2015, strong revenue growth from efforts to reduce tax evasion…



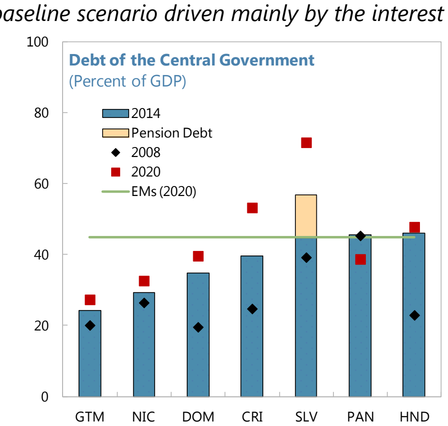
… was matched by similar growth in primary expenditure…



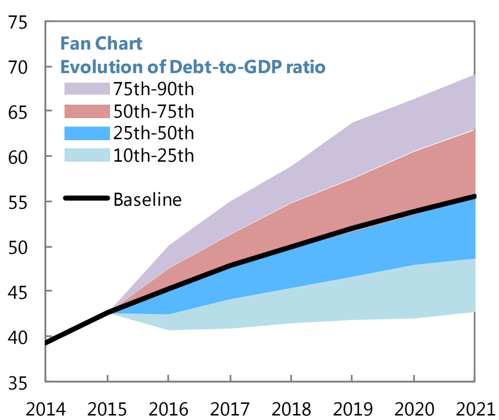
… leaving the primary and overall fiscal deficits close to the post-global credit crisis highs.



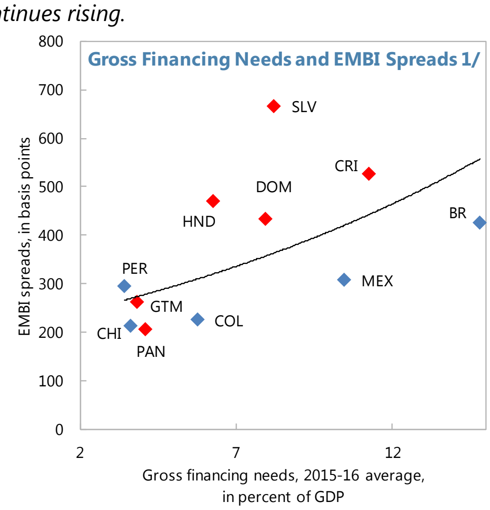
Public debt is expected to continue to rise sharply under the baseline scenario driven mainly by the interest bill…



… and risks tilted to the upside…



… plus an increasing likelihood of a debt spiral with potentially non-linear increase in financing costs as debt continues rising.

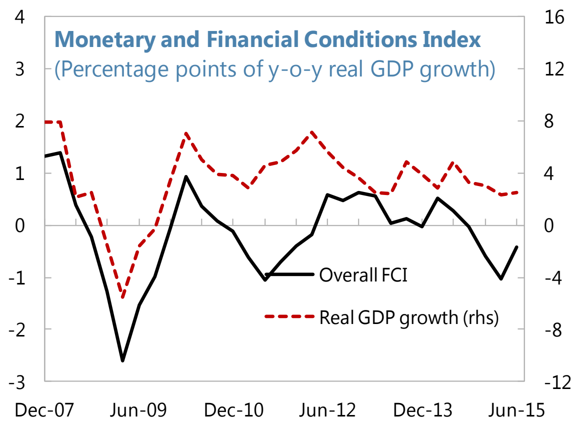


1/ Gross financing needs for LA-5 are based on data from latest Article IV reports, published in 2015.

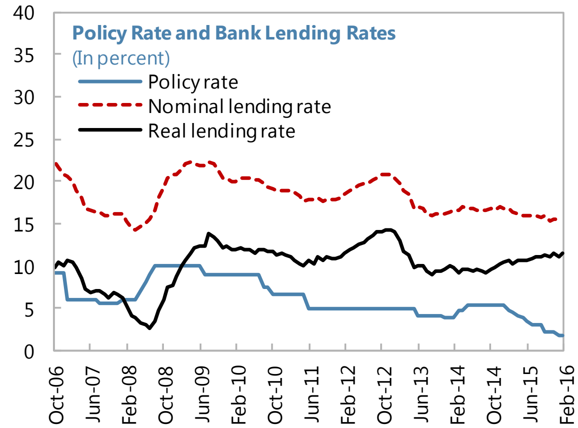
Sources: National authorities; and Fund staff estimates.

Figure 5. Costa Rica: Recent Developments, Financial Sector

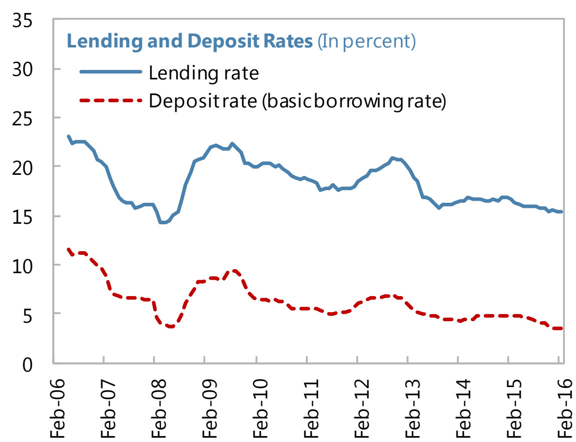
Financial conditions remain relatively tight…



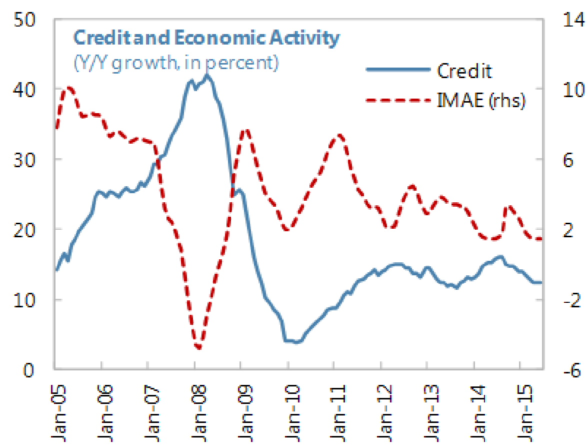
…. with real lending rates rising despite the aggressive monetary easing…



… reflecting both limited pass-through to nominal rates in the banking system and a significant decline in inflation expectations.



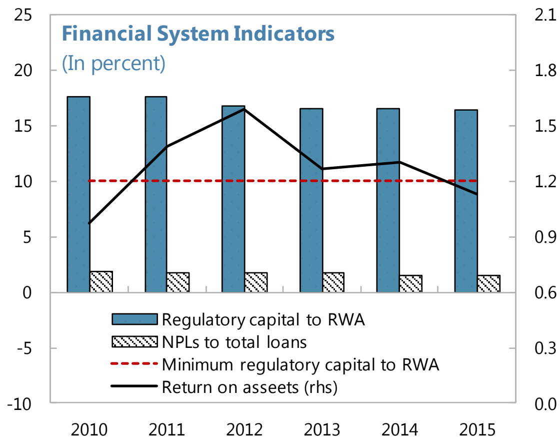
Credit growth has moderated in line with sluggish economic activity.



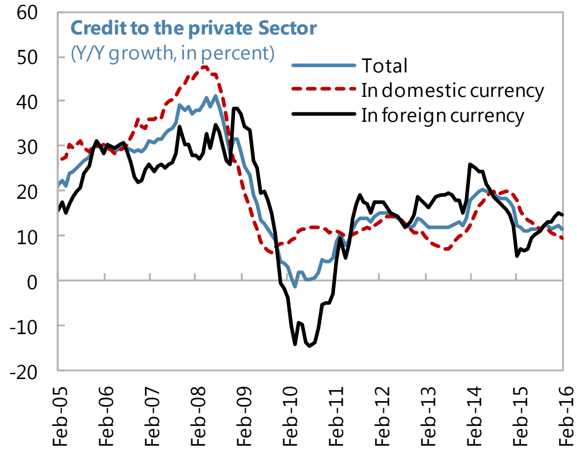
Sources: National authorities; and Fund staff estimates.

Figure 6. Costa Rica: Financial Sector Vulnerabilities

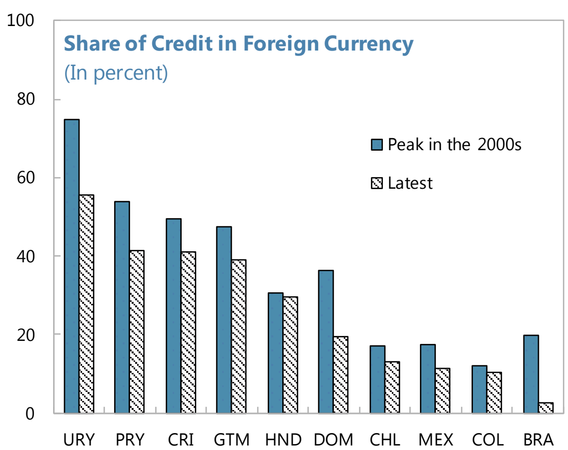
Banks are adequately capitalized and NPLs remain low, although profitability has been declining.



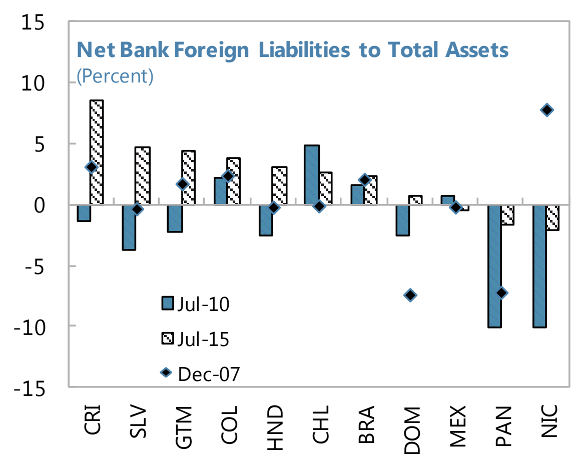
Despite the moderation in overall credit growth, credit in FX is accelerating again spurred by renewed exchange rate stability.



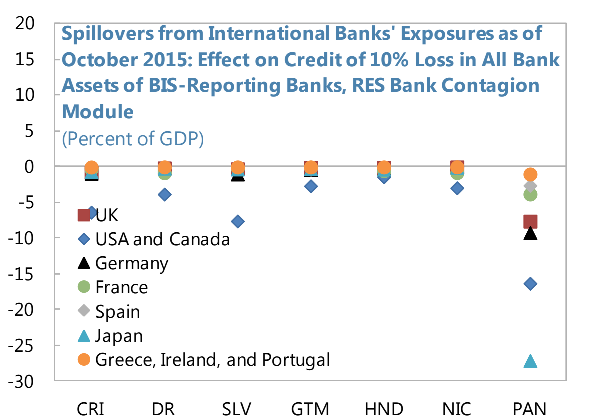
As a result, Costa Rica is one of the countries with highest credit dollarization in the region…



… and one of the most reliant on foreign financing…

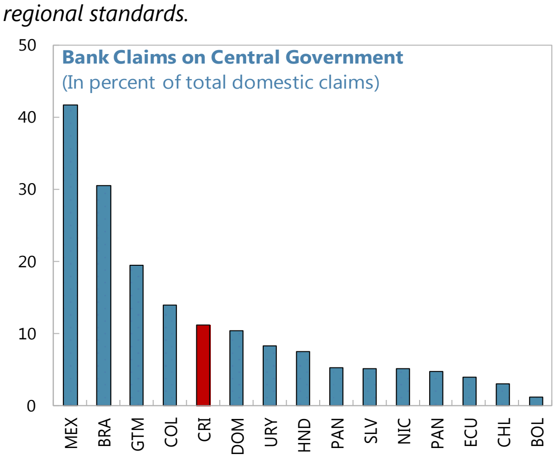


… although associated rollover risks still appear manageable.



Note: In Panama, the loss of credit includes credit by banks in the off-shore center with minimal links to the domestic economy.

Exposure to a sovereign with high and rising public debt is another area of concern, although these are still limited by regional standards.

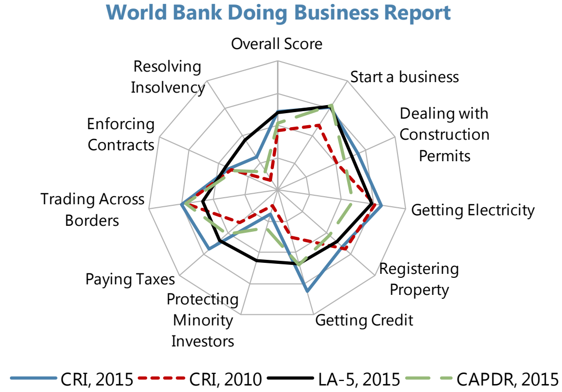


Sources: BIS; IFS; and Fund staff estimates.

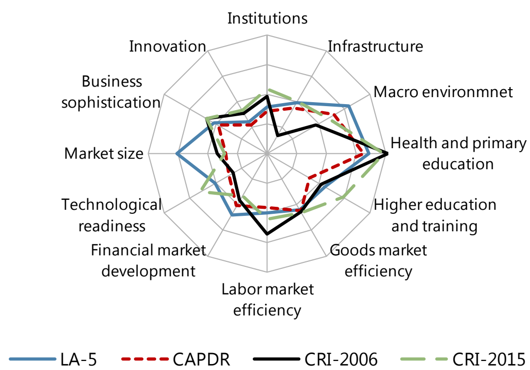
Figure 7. Costa Rica: Competitiveness and Structural Reforms

Costa Rica's competitiveness indicators have improved over the last decade, and only lag the more advanced countries in the region in a few areas, like the macroeconomic environment due to the country's unsustainable fiscal situation.

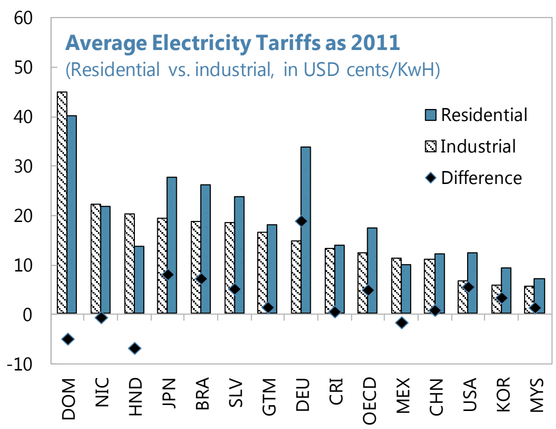
World Bank Doing Business Report



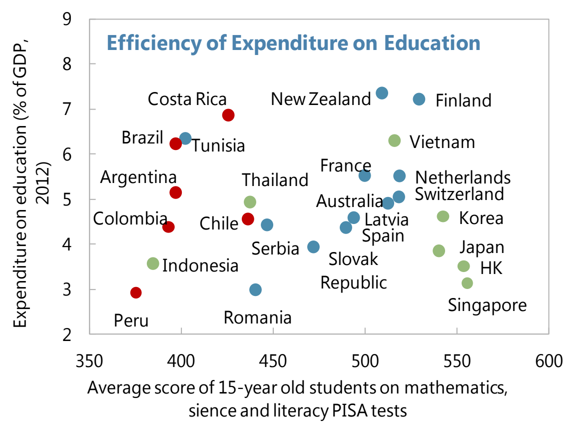
WEF Competitiveness Index



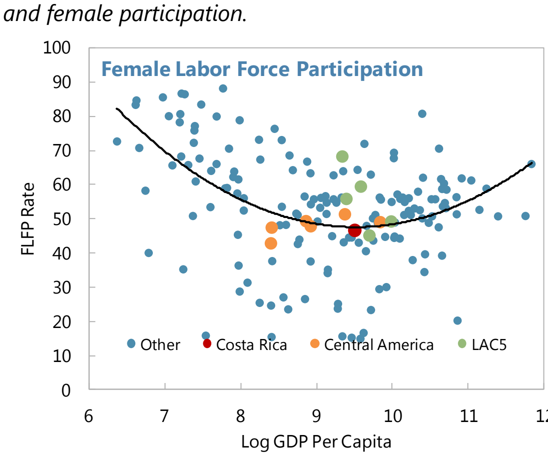
Electricity tariffs are not very high by regional standards, but Asian competitors with subsidy policies generally have lower tariffs.



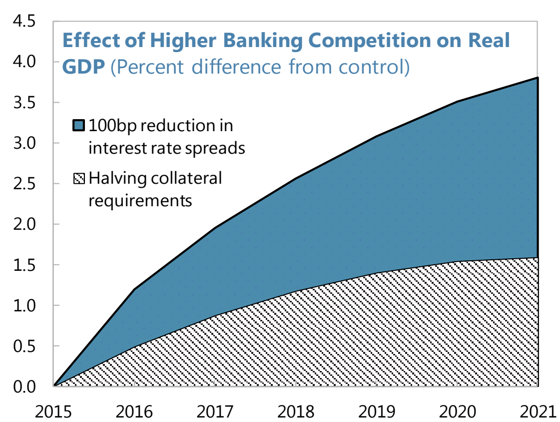
Efficiency of (high) expenditure on education, which is low compared to Asia and also to Chile, needs to be improved.



Measures are needed to take Costa Rica past the low point of the typical U-shaped relationship between development and female participation.



Increasing competition in the banking sector would provide a significant boost to the economy.



Source: World Bank, Doing Buisness Report; World Economic Forum, The Global Competitiveness Report 2015; Latin American Energy Organization (OLADE); National Center for Education Statistics, PISA tests; and Fund staff calculations based on RES FSGM.

Table 1a. Costa Rica: Selected Social and Economic Indicators, Baseline Scenario (Partial Fiscal Adjustment) 1/ 2/

Population (2014, millions)	4.8	Human Development Index Rank (2013)	68 (out of 187)
Per capita GDP (2014, U.S. dollars)	10,425	Life expectancy (2013, years)	80.0
Unemployment (2014, percent of labor force)	9.7	Literacy rate (2014, percent of people ages > 15)	98.0
Poverty (2014, percent of population)	22.0	Ratio of girls to boys in primary and secondary education (2013, percent)	103.0
Income share held by highest 10 percent of households	39.4		
Income share held by lowest 10 percent of households	1.7	Gini coefficient (2012)	48.6

				Est.	Proj.	
	2012	2013	2014	2015	2016	2017
	(Annual percentage change, unless otherwise indicated)					
Output and Prices						
Real GDP growth	5.2	1.8	3.0	3.7	4.2	4.3
Output gap (percent of potential GDP)	2.8	0.4	-0.8	-1.1	-0.9	-0.6
GDP deflator	3.9	4.2	4.7	2.2	3.4	3.2
Consumer prices (end of period)	4.6	3.7	5.1	-0.8	3.0	3.0
Money and Credit						
Monetary base	16.9	10.2	10.4	9.2	9.1	9.0
Broad money	10.7	7.7	15.4	6.6	8.6	8.3
Credit to private sector	13.4	12.2	17.5	11.8	12.1	12.0
Monetary policy rate (percent; end of period)	5.0	3.8	5.3	2.3	…	…
	(In percent of GDP, unless otherwise indicated)					
Savings and Investment						
Gross domestic investment	20.5	18.8	19.6	19.1	19.1	19.3
Gross domestic savings	15.3	13.8	14.9	15.1	14.9	15.0
External Sector						
Current account balance	-5.2	-5.0	-4.7	-4.0	-4.2	-4.3
Of which: Trade balance	-11.6	-11.3	-10.5	-10.2	-10.2	-10.4
Financial and capital account balance	9.5	6.4	4.6	6.2	5.1	5.1
Of which: Foreign direct investment	4.1	4.8	4.0	4.1	4.3	4.3
Change in net international reserves (increase -)	-2,110	-461	113	-622	-500	-500
Net international reserves (millions of U.S. dollars)	6,857	7,331	7,211	7,834	8,334	8,834
Public Finances						
Central government primary balance	-2.3	-2.8	-3.1	-3.0	-2.4	-1.5
Central government overall balance	-4.5	-5.6	-6.0	-5.8	-5.8	-5.4
Central government debt	34.3	36.0	39.3	42.4	45.0	47.3
Consolidated public sector overall balance 3/	-4.5	-5.4	-5.6	-6.0	-6.2	-5.7
Consolidated public sector debt 4/	37.6	42.0	43.2	46.0	47.9	49.6
Of which: External public debt	7.3	8.9	10.5	11.7	12.2	12.7
Memorandum Item:						
GDP (US$ billions)	46.5	49.6	49.6	52.9	56.9	60.8

Sources: Central Bank of Costa Rica, Ministry of Finance, and Fund staff estimates.

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved tax administration.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ 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).

4/ 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 1b. Costa Rica: Selected Social and Economic Indicators, Full Fiscal Adjustment Scenario 1/ 2/

Population (2014, millions)	4.8	Human Development Index Rank (2013)	68 (out of 187)
Per capita GDP (2014, U.S. dollars)	10,425	Life expectancy (2013, years)	80.0
Unemployment (2014, percent of labor force)	9.7	Literacy rate (2014, percent of people ages > 15)	98.0
Poverty (2014, percent of population)	22.0	Ratio of girls to boys in primary and secondary education (2013, percent)	103.0
Income share held by highest 10 percent of households	39.4		
Income share held by lowest 10 percent of households	1.7	Gini coefficient (2012)	48.6

				Est.	Proj.	
	2012	2013	2014	2015	2016	2017
	(Annual percentage change, unless otherwise indicated)					
Output and Prices						
Real GDP growth	5.2	1.8	3.0	3.7	4.2	4.2
Output gap (percent of potential GDP)	2.8	0.4	-0.8	-1.1	-0.9	-0.7
GDP deflator	3.9	4.2	4.7	2.2	3.6	3.1
Consumer prices (end of period)	4.6	3.7	5.1	-0.8	3.0	3.0
Money and Credit						
Monetary base	16.9	10.2	10.4	9.2	9.9	9.0
Broad money	10.7	7.7	15.4	6.6	8.9	8.2
Credit to private sector	13.4	12.2	17.5	11.8	12.4	12.9
Monetary policy rate (percent; end of period)	5.0	3.8	5.3	2.3	…	…
	(In percent of GDP, unless otherwise indicated)					
Savings and Investment						
Gross domestic investment	20.5	18.8	19.6	19.1	19.1	19.3
Gross domestic savings	15.3	13.8	14.9	15.1	14.8	15.1
External Sector						
Current account balance	-5.2	-5.0	-4.7	-4.0	-4.2	-4.2
Of which: Trade balance	-11.6	-11.3	-10.5	-10.2	-10.2	-10.3
Financial and capital account balance	9.5	6.4	4.6	6.2	5.1	5.0
Of which: Foreign direct investment	4.1	4.8	4.0	4.1	4.3	4.3
Change in net international reserves (increase -)	-2,110	-461	113	-622	-500	-500
Net international reserves (millions of U.S. dollars)	6,857	7,331	7,211	7,834	8,334	8,834
Public Finances						
Central government primary balance	-2.3	-2.8	-3.1	-3.0	-2.4	-0.9
Central government overall balance	-4.5	-5.6	-6.0	-5.8	-5.7	-4.4
Central government debt	34.3	36.0	39.3	42.4	44.9	46.2
Consolidated public sector overall balance 3/	-4.5	-5.4	-5.6	-6.0	-6.1	-4.7
Consolidated public sector debt 4/	37.6	42.0	43.2	46.0	47.7	48.4
Of which: External public debt	7.3	8.9	10.5	11.7	12.2	12.7
Memorandum Item:						
GDP (US$ billions)	46.5	49.6	49.6	52.9	57.0	60.8

Sources: Central Bank of Costa Rica, Ministry of Finance, and Fund staff estimates.

1/ Includes measures as in the baseline partial adjustment scenario, as well as administratively-determined measures to contain growth in the wage bill, and increases in the VAT rate from 2017.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ 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).

4/ 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, Baseline Scenario (Partial Fiscal Adjustment) 1/ 2/ 3/

						Est.	Projection					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						(In millions of U.S. dollars)						
Current Account	-1,281	-2,228	-2,408	-2,486	-2,340	-2,135	-2,396	-2,590	-2,759	-3,015	-3,217	-3,463
Trade balance	-3,440	-5,144	-5,375	-5,623	-5,212	-5,370	-5,807	-6,312	-6,952	-7,702	-8,394	-9,180
Export of goods (f.o.b.)	9,516	10,426	11,454	11,554	11,139	9,534	9,956	10,533	11,110	11,725	12,347	12,971
Import of goods (f.o.b.)	12,956	15,570	16,829	17,178	16,352	14,904	15,763	16,845	18,062	19,427	20,741	22,151
Services	2,537	3,182	3,436	4,030	4,302	4,603	4,956	5,433	6,030	6,662	7,306	8,004
Of which: Travel	1,575	1,747	1,884	2,225	2,491	2,669	2,779	2,918	3,082	3,248	3,408	3,574
Income	-745	-589	-801	-1,187	-1,739	-1,680	-1,822	-2,028	-2,179	-2,344	-2,524	-2,708
Current transfers	366	323	333	294	310	312	277	317	341	368	394	422
Financial and Capital Account	1,986	2,579	4,416	3,188	2,297	3,282	2,896	3,090	2,759	3,015	3,217	3,463
Public sector	615	68	1,239	1,243	1,048	703	724	860	768	774	532	782
Private sector	1,371	2,511	3,178	1,945	1,249	2,580	2,172	2,230	1,991	2,242	2,686	2,681
Foreign direct investment	1,441	2,121	1,904	2,387	1,974	2,177	2,433	2,616	2,818	3,039	3,274	3,546
Other private sector flows	-70	391	1,274	-441	-725	403	-261	-386	-827	-798	-588	-865
Errors and Omissions	-144	-218	101	-242	-70	-525	0	0	0	0	0	0
Change in International Reserves (increase -)	-561	-132	-2,110	-461	113	-622	-500	-500	0	0	0	0
						(In percent of GDP)						
Current Account	-3.4	-5.3	-5.2	-5.0	-4.7	-4.0	-4.2	-4.3	-4.2	-4.3	-4.3	-4.3
Trade balance	-9.2	-12.2	-11.6	-11.3	-10.5	-10.2	-10.2	-10.4	-10.7	-11.1	-11.3	-11.5
Export of goods (f.o.b.)	25.6	24.6	24.6	23.3	22.5	18.0	17.5	17.3	17.1	16.8	16.6	16.2
Import of goods (f.o.b.)	34.8	36.8	36.2	34.6	33.0	28.2	27.7	27.7	27.8	27.9	27.9	27.7
Of which: Oil and fuels	3.5	4.8	4.7	4.4	4.2	2.4	1.8	2.0	2.1	2.1	2.0	2.0
Services	6.8	7.5	7.4	8.1	8.7	8.7	8.7	8.9	9.3	9.6	9.8	10.0
Income	-2.0	-1.4	-1.7	-2.4	-3.5	-3.2	-3.2	-3.3	-3.4	-3.4	-3.4	-3.4
Current transfers	1.0	0.8	0.7	0.6	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.5
Financial and Capital account	5.3	6.1	9.5	6.4	4.6	6.2	5.1	5.1	4.2	4.3	4.3	4.3
Of which: Foreign direct investment	3.9	5.0	4.1	4.8	4.0	4.1	4.3	4.3	4.3	4.4	4.4	4.4
Change in International Reserves (increase -)	-1.5	-0.3	-4.5	-0.9	0.2	-1.2	-0.9	-0.8	0.0	0.0	0.0	0.0
Memorandum Items:												
Non-oil current account (percent of GDP)	0.1	-0.5	-0.5	-0.6	-0.5	-1.7	-2.4	-2.3	-2.2	-2.2	-2.3	-2.3
Terms of trade (annual percentage change)	-0.3	-3.1	-0.8	0.0	0.5	0.7	0.7	0.7	0.7	0.0	0.0	0.0
Net international reserves (millions of U.S. dollars)	4,627	4,756	6,857	7,331	7,211	7,834	8,334	8,834	8,834	8,834	8,834	8,834
-in months of non-maquila imports	4.1	3.9	5.4	5.7	5.6	5.6	5.6	5.6	5.2	5.2	5.2	5.2
-in percent short-term debt 4/	137.5	116.4	157.9	186.7	226.0	245.0	272.7	281.3	331.1	528.6	567.9	637.4
External debt (percent of GDP) 5/	25.7	26.6	31.9	35.6	38.8	38.4	36.5	34.9	32.6	30.4	28.3	26.2

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

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved tax administration.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ BOP data are reported on a fifth Balance of Payments Manual edition (BPM5) basis, with some differences of presentation relative to the data on a sixth edition (BPM6) basis disseminated by the central bank.

4/ Public and private sector external debt on remaining maturity. Includes trade credit.

5/ Includes public and private sector debt.

Table 3a. Costa Rica: Central Government Balance, Baseline Scenario (Partial Adjustment) 1/ 2/

						Est.	Projection					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
	(In billions of colones)											
Revenue	**2,591**	**2,869**	**3,118**	**3,380**	**3,625**	**3,994**	**4,433**	**5,091**	**5,622**	**6,085**	**6,541**	**7,025**
Tax revenue	2,492	2,769	3,008	3,292	3,522	3,862	4,290	4,937	5,456	5,906	6,348	6,817
Nontax revenue 3/	100	100	110	87	103	132	143	154	166	179	193	207
Expenditure	**3,623**	**3,762**	**4,178**	**4,765**	**5,230**	**5,643**	**6,194**	**6,874**	**7,554**	**8,201**	**8,805**	**9,349**
Current noninterest	2,723	2,962	3,316	3,684	3,990	4,330	4,559	4,890	5,283	5,712	6,140	6,599
Wages	1,349	1,514	1,647	1,817	1,969	2,113	2,274	2,457	2,660	2,876	3,091	3,322
Goods and services	121	136	143	158	180	194	193	208	225	243	261	281
Transfers	1,252	1,313	1,526	1,708	1,842	2,023	2,091	2,225	2,399	2,593	2,787	2,996
Interest 4/	452	497	530	681	775	787	1,027	1,303	1,511	1,668	1,782	1,802
Capital	449	304	332	400	465	526	608	681	759	821	882	948
Primary balance	**-580**	**-396**	**-529**	**-704**	**-830**	**-862**	**-733**	**-480**	**-421**	**-448**	**-481**	**-523**
Overall Balance	**-1,032**	**-893**	**-1,059**	**-1,386**	**-1,604**	**-1,649**	**-1,761**	**-1,783**	**-1,932**	**-2,116**	**-2,264**	**-2,325**
Total Financing	1,032	893	1,059	1,386	1,604	1,649	1,761	1,783	1,932	2,116	2,264	2,325
External (net)	247	-112	356	401	490	598	412	417	372	379	247	385
Domestic (net)	785	1,005	704	984	1,115	1,051	1,349	1,366	1,560	1,737	2,017	1,940
Central government debt	**5,562**	**6,382**	**8,015**	**8,932**	**10,484**	**11,984**	**13,732**	**15,532**	**17,490**	**19,640**	**21,770**	**24,072**
External	1,142	1,027	1,383	1,763	2,366	2,944	3,337	3,756	4,138	4,532	4,645	5,006
Domestic	4,420	5,355	6,632	7,169	8,118	9,040	10,395	11,776	13,352	15,109	17,126	19,065
	(In percent of GDP)											
Revenue	**13.2**	**13.4**	**13.3**	**13.6**	**13.6**	**14.1**	**14.5**	**15.5**	**15.9**	**15.9**	**15.9**	**15.9**
Tax revenue	12.7	12.9	12.9	13.3	13.2	13.7	14.1	15.1	15.4	15.4	15.4	15.4
Nontax revenue 3/	0.5	0.5	0.5	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Expenditure	**18.5**	**17.6**	**17.9**	**19.2**	**19.6**	**20.0**	**20.3**	**21.0**	**21.3**	**21.4**	**21.4**	**21.1**
Current noninterest	13.9	13.8	14.2	14.9	14.9	15.3	14.9	14.9	14.9	14.9	14.9	14.9
Wages	6.9	7.1	7.0	7.3	7.4	7.5	7.5	7.5	7.5	7.5	7.5	7.5
Goods and services	0.6	0.6	0.6	0.6	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.6
Transfers	6.4	6.1	6.5	6.9	6.9	7.2	6.9	6.8	6.8	6.8	6.8	6.8
Interest 4/	2.3	2.3	2.3	2.7	2.9	2.8	3.4	4.0	4.3	4.4	4.3	4.1
Capital	2.3	1.4	1.4	1.6	1.7	1.9	2.0	2.1	2.1	2.1	2.1	2.1
Primary balance	**-3.0**	**-1.9**	**-2.3**	**-2.8**	**-3.1**	**-3.0**	**-2.4**	**-1.5**	**-1.2**	**-1.2**	**-1.2**	**-1.2**
Overall Balance	**-5.3**	**-4.2**	**-4.5**	**-5.6**	**-6.0**	**-5.8**	**-5.8**	**-5.4**	**-5.5**	**-5.5**	**-5.5**	**-5.3**
Total Financing	**5.3**	**4.2**	**4.5**	**5.6**	**6.0**	**5.8**	**5.8**	**5.4**	**5.5**	**5.5**	**5.5**	**5.3**
External (net)	1.3	-0.5	1.5	1.6	1.8	2.1	1.4	1.3	1.0	1.0	0.6	0.9
Domestic (net)	4.0	4.7	3.0	4.0	4.2	3.7	4.4	4.2	4.4	4.5	4.9	4.4
Central government debt	**28.4**	**29.8**	**34.3**	**36.0**	**39.3**	**42.4**	**45.0**	**47.3**	**49.4**	**51.3**	**52.9**	**54.4**
External	5.8	4.8	5.9	7.1	8.9	10.4	10.9	11.4	11.7	11.8	11.3	11.3
Domestic	22.6	25.0	28.4	28.9	30.4	32.0	34.1	35.9	37.7	39.4	41.6	43.1
Memorandum items:												
Non-interest expenditure growth (percent)												
in nominal terms	23.1	3.0	11.7	12.0	9.1	9.0	6.4	7.8	8.5	8.1	7.5	7.5
in real terms	16.5	-1.8	6.9	6.4	4.4	8.1	5.3	4.7	5.3	5.0	4.4	4.3
Nominal GDP	19,581	21,392	23,371	24,781	26,703	28,279	30,495	32,804	35,437	38,312	41,183	44,263
CPI Inflation (period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved tax administration.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

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

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

Table 3b. Costa Rica: Central Government Balance, Full Fiscal Adjustment Scenario 1/ 2/

						Est.	Projection					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						(In billions of colones)						
Revenue	**2,591**	**2,869**	**3,118**	**3,380**	**3,625**	**3,994**	**4,433**	**5,202**	**5,909**	**6,396**	**6,875**	**7,383**
Tax revenue	2,492	2,769	3,008	3,292	3,522	3,862	4,290	5,049	5,743	6,216	6,682	7,176
Nontax revenue 3/	100	100	110	87	103	132	143	154	166	179	193	207
Expenditure	**3,623**	**3,762**	**4,178**	**4,765**	**5,230**	**5,643**	**6,169**	**6,649**	**7,204**	**7,778**	**8,252**	**8,827**
Current noninterest	2,723	2,962	3,316	3,684	3,990	4,330	4,559	4,821	5,142	5,520	5,893	6,289
Wages	1,349	1,514	1,647	1,817	1,969	2,113	2,274	2,408	2,554	2,723	2,885	3,057
Goods and services	121	136	143	158	180	194	193	188	189	205	220	237
Transfers	1,252	1,313	1,526	1,708	1,842	2,023	2,091	2,225	2,399	2,593	2,787	2,996
Interest 4/	452	497	530	681	775	787	1,003	1,147	1,303	1,437	1,476	1,589
Capital	449	304	332	400	465	526	608	681	759	821	882	948
Primary balance	**-580**	**-396**	**-529**	**-704**	**-830**	**-862**	**-733**	**-300**	**8**	**54**	**99**	**145**
Overall Balance	**-1,032**	**-893**	**-1,059**	**-1,386**	**-1,604**	**-1,649**	**-1,736**	**-1,447**	**-1,295**	**-1,383**	**-1,377**	**-1,444**
Total Financing	1,032	893	1,059	1,386	1,604	1,649	1,736	1,447	1,295	1,383	1,377	1,444
External (net)	247	-112	356	401	490	598	412	417	372	379	247	385
Domestic (net)	785	1,005	704	984	1,115	1,051	1,324	1,030	923	1,004	1,130	1,059
Central government debt	**5,562**	**6,382**	**8,015**	**8,932**	**10,484**	**11,984**	**13,707**	**15,171**	**16,492**	**17,907**	**19,150**	**20,570**
External	1,142	1,027	1,383	1,763	2,366	2,944	3,337	3,756	4,138	4,532	4,645	5,006
Domestic	4,420	5,355	6,632	7,169	8,118	9,040	10,370	11,415	12,354	13,375	14,506	15,564
						(In percent of GDP)						
Revenue	**13.2**	**13.4**	**13.3**	**13.6**	**13.6**	**14.1**	**14.5**	**15.8**	**16.5**	**16.4**	**16.4**	**16.3**
Tax revenue	12.7	12.9	12.9	13.3	13.2	13.7	14.0	15.4	16.1	16.0	15.9	15.9
Nontax revenue 3/	0.5	0.5	0.5	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Expenditure	**18.5**	**17.6**	**17.9**	**19.2**	**19.6**	**20.0**	**20.2**	**20.3**	**20.1**	**20.0**	**19.7**	**19.5**
Current noninterest	13.9	13.8	14.2	14.9	14.9	15.3	14.9	14.7	14.4	14.2	14.1	13.9
Wages	6.9	7.1	7.0	7.3	7.4	7.5	7.4	7.3	7.1	7.0	6.9	6.8
Goods and services	0.6	0.6	0.6	0.6	0.7	0.7	0.6	0.6	0.5	0.5	0.5	0.5
Transfers	6.4	6.1	6.5	6.9	6.9	7.2	6.8	6.8	6.7	6.7	6.6	6.6
Interest 4/	2.3	2.3	2.3	2.7	2.9	2.8	3.3	3.5	3.6	3.7	3.5	3.5
Capital	2.3	1.4	1.4	1.6	1.7	1.9	2.0	2.1	2.1	2.1	2.1	2.1
Primary balance	**-3.0**	**-1.9**	**-2.3**	**-2.8**	**-3.1**	**-3.0**	**-2.4**	**-0.9**	**0.0**	**0.1**	**0.2**	**0.3**
Overall Balance	**-5.3**	**-4.2**	**-4.5**	**-5.6**	**-6.0**	**-5.8**	**-5.7**	**-4.4**	**-3.6**	**-3.6**	**-3.3**	**-3.2**
Total Financing	**5.3**	**4.2**	**4.5**	**5.6**	**6.0**	**5.8**	**5.7**	**4.4**	**3.6**	**3.6**	**3.3**	**3.2**
External (net)	1.3	-0.5	1.5	1.6	1.8	2.1	1.3	1.3	1.0	1.0	0.6	0.9
Domestic (net)	4.0	4.7	3.0	4.0	4.2	3.7	4.3	3.1	2.6	2.6	2.7	2.3
Central government debt	**28.4**	**29.8**	**34.3**	**36.0**	**39.3**	**42.4**	**44.9**	**46.2**	**46.1**	**46.0**	**45.7**	**45.5**
External	5.8	4.8	5.9	7.1	8.9	10.4	10.9	11.4	11.6	11.7	11.1	11.1
Domestic	22.6	25.0	28.4	28.9	30.4	32.0	33.9	34.8	34.5	34.4	34.6	34.5
Memorandum items:												
Non-interest expenditure growth (percent)												
in nominal terms	23.1	3.0	11.7	12.0	9.1	9.0	6.4	6.5	7.3	7.5	6.8	6.8
in real terms	16.5	-1.8	6.9	6.4	4.4	8.1	5.3	3.4	4.1	4.3	3.7	3.7
Nominal GDP	19,581	21,392	23,371	24,781	26,703	28,279	30,549	32,832	35,780	38,892	41,941	45,177
CPI Inflation (period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes measures as in the baseline partial adjustment scenario, as well as administratively-determined measures to contain growth in the wage bill, and increases in the VAT rate from 2017.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

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

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

Table 4a. Costa Rica: Summary Operations of the Central Government, GFSM 2001 Classification. Baseline Scenario (Partial Adjustment) 1/ 2/

						Est.	Projection					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
				(In billions of colones)								
Revenue	**2,591**	**2,869**	**3,118**	**3,380**	**3,625**	**3,994**	**4,433**	**5,091**	**5,622**	**6,085**	**6,541**	**7,025**
Taxes	2,492	2,769	3,008	3,292	3,522	3,862	4,290	4,937	5,456	5,906	6,348	6,817
Other revenue 3/	100	100	110	87	103	132	143	154	166	179	193	207
Expenditure	**3,623**	**3,762**	**4,178**	**4,765**	**5,230**	**5,643**	**6,194**	**6,874**	**7,554**	**8,201**	**8,805**	**9,349**
Expense	**3,174**	**3,459**	**3,846**	**4,365**	**4,765**	**5,117**	**5,586**	**6,193**	**6,794**	**7,380**	**7,922**	**8,401**
Compensation of employees	1,349	1,514	1,647	1,817	1,969	2,113	2,274	2,457	2,660	2,876	3,091	3,322
Purchases of goods and services	121	136	143	158	180	194	193	208	225	243	261	281
Interest 4/	452	497	530	681	775	787	1,027	1,303	1,511	1,668	1,782	1,802
Of which: Adjustment for TUDES	50	48	58	50	79	-13	44	51	58	66	74	84
Social benefits	506	552	594	616	661	710	766	824	890	962	1,034	1,112
Other expense 5/	747	761	932	1,092	1,181	1,313	1,326	1,401	1,508	1,631	1,753	1,884
Net acquisition of nonfinancial assets	**449**	**304**	**332**	**400**	**465**	**526**	**608**	**681**	**759**	**821**	**882**	**948**
Gross operating balance	**-583**	**-589**	**-728**	**-985**	**-1,140**	**-1,124**	**-1,153**	**-1,102**	**-1,172**	**-1,295**	**-1,381**	**-1,376**
Net lending/borrowing	**-1,032**	**-893**	**-1,059**	**-1,386**	**-1,604**	**-1,649**	**-1,761**	**-1,783**	**-1,932**	**-2,116**	**-2,264**	**-2,325**
Net financial transactions	**1,032**	**893**	**1,059**	**1,386**	**1,604**	**1,649**	**1,761**	**1,783**	**1,932**	**2,116**	**2,264**	**2,325**
				(In percent of GDP)								
Revenue	**13.2**	**13.4**	**13.3**	**13.6**	**13.6**	**14.1**	**14.5**	**15.5**	**15.9**	**15.9**	**15.9**	**15.9**
Tax revenue	12.7	12.9	12.9	13.3	13.2	13.7	14.1	15.1	15.4	15.4	15.4	15.4
Nontax revenue 3/	0.5	0.5	0.5	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Expenditure	**18.5**	**17.6**	**17.9**	**19.2**	**19.6**	**20.0**	**20.3**	**21.0**	**21.3**	**21.4**	**21.4**	**21.1**
Expense	**16.2**	**16.2**	**16.5**	**17.6**	**17.8**	**18.1**	**18.3**	**18.9**	**19.2**	**19.3**	**19.2**	**19.0**
Compensation of employees	6.9	7.1	7.0	7.3	7.4	7.5	7.5	7.5	7.5	7.5	7.5	7.5
Purchases of goods and services	0.6	0.6	0.6	0.6	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.6
Interest 4/	2.3	2.3	2.3	2.7	2.9	2.8	3.4	4.0	4.3	4.4	4.3	4.1
Of which: Adjustment for TUDES	0.3	0.2	0.2	0.2	0.3	0.0	0.1	0.2	0.2	0.2	0.2	0.2
Social benefits	2.6	2.6	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Other expense 5/	3.8	3.6	4.0	4.4	4.4	4.6	4.3	4.3	4.3	4.3	4.3	4.3
Net acquisition of nonfinancial assets	2.3	1.4	1.4	1.6	1.7	1.9	2.0	2.1	2.1	2.1	2.1	2.1
Gross operating balance	**-3.0**	**-2.8**	**-3.1**	**-4.0**	**-4.3**	**-4.0**	**-3.8**	**-3.4**	**-3.3**	**-3.4**	**-3.4**	**-3.1**
Net lending/borrowing	**-5.3**	**-4.2**	**-4.5**	**-5.6**	**-6.0**	**-5.8**	**-5.8**	**-5.4**	**-5.5**	**-5.5**	**-5.5**	**-5.3**
Net financial transactions	**5.3**	**4.2**	**4.5**	**5.6**	**6.0**	**5.8**	**5.8**	**5.4**	**5.5**	**5.5**	**5.5**	**5.3**
Memorandum items:												
Non-interest expenditure growth (percent)												
in nominal terms	23.1	3.0	11.7	12.0	9.1	9.0	6.4	7.8	8.5	8.1	7.5	7.5
in real terms	16.5	-1.8	6.9	6.4	4.4	8.1	5.3	4.7	5.3	5.0	4.4	4.3
Primary balance												
in billions of colones	-580	-396	-529	-704	-830	-862	-733	-480	-421	-448	-481	-523
in percent of GDP	-3.0	-1.9	-2.3	-2.8	-3.1	-3.0	-2.4	-1.5	-1.2	-1.2	-1.2	-1.2
Cyclically-adjusted primary balance (percent of GDP)	-3.1	-2.0	-2.6	-2.9	-3.0	-2.9	-2.3	-1.4	-1.1	-1.2	-1.2	-1.2
Fiscal impulse (percent of GDP)	1.9	-1.0	0.6	0.3	0.1	-0.1	-0.6	-0.9	-0.2	0.0	0.0	0.0
Nominal GDP	19,581	21,392	23,371	24,781	26,703	28,279	30,495	32,804	35,437	38,312	41,183	44,263
CPI Inflation (period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved anti-tax evasion.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

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

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

5/ Includes subsidies, transfers and other expense.

Table 4b. Costa Rica: Summary Operations of the Central Government, GFSM 2001 Classification. Full Fiscal Adjustment Scenario 1/ 2/

						Est.	Projection					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
				(In billions of colones)								
Revenue	**2,591**	**2,869**	**3,118**	**3,380**	**3,625**	**3,994**	**4,445**	**5,210**	**5,920**	**6,432**	**6,929**	**7,454**
Taxes	2,492	2,769	3,008	3,292	3,522	3,862	4,301	5,056	5,753	6,251	6,733	7,244
Other revenue 3/	100	100	110	87	103	132	143	154	166	181	195	210
Expenditure	**3,623**	**3,762**	**4,178**	**4,765**	**5,230**	**5,643**	**6,176**	**6,640**	**7,218**	**7,830**	**8,331**	**8,908**
Expense	**3,174**	**3,459**	**3,846**	**4,365**	**4,765**	**5,117**	**5,566**	**5,958**	**6,456**	**7,002**	**7,438**	**7,946**
Compensation of employees	1,349	1,514	1,647	1,817	1,969	2,113	2,281	2,413	2,561	2,745	2,919	3,100
Purchases of goods and services	121	136	143	158	180	194	194	189	190	206	223	240
Interest 4/	452	497	530	681	775	787	992	1,126	1,301	1,435	1,476	1,568
Of which: Adjustment for TUDES	50	48	58	50	79	-13	44	51	56	61	66	71
Social benefits	506	552	594	616	661	710	768	826	893	970	1,047	1,128
Other expense 5/	747	761	932	1,092	1,181	1,313	1,330	1,404	1,513	1,644	1,774	1,911
Net acquisition of nonfinancial assets	**449**	**304**	**332**	**400**	**465**	**526**	**610**	**683**	**761**	**828**	**893**	**962**
Gross operating balance	**-583**	**-589**	**-728**	**-985**	**-1,140**	**-1,124**	**-1,121**	**-748**	**-537**	**-570**	**-510**	**-492**
Net lending/borrowing	**-1,032**	**-893**	**-1,059**	**-1,386**	**-1,604**	**-1,649**	**-1,731**	**-1,431**	**-1,298**	**-1,398**	**-1,403**	**-1,454**
Net financial transactions	**1,032**	**893**	**1,059**	**1,386**	**1,604**	**1,649**	**1,731**	**1,431**	**1,298**	**1,398**	**1,403**	**1,454**
				(In percent of GDP)								
Revenue	**13.2**	**13.4**	**13.3**	**13.6**	**13.6**	**14.1**	**14.5**	**15.9**	**16.5**	**16.5**	**16.5**	**16.5**
Tax revenue	12.7	12.9	12.9	13.3	13.2	13.7	14.1	15.4	16.1	16.1	16.1	16.0
Nontax revenue 3/	0.5	0.5	0.5	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Expenditure	**18.5**	**17.6**	**17.9**	**19.2**	**19.6**	**20.0**	**20.2**	**20.2**	**20.2**	**20.1**	**19.9**	**19.7**
Expense	**16.2**	**16.2**	**16.5**	**17.6**	**17.8**	**18.1**	**18.2**	**18.1**	**18.0**	**18.0**	**17.7**	**17.6**
Compensation of employees	6.9	7.1	7.0	7.3	7.4	7.5	7.5	7.4	7.2	7.1	7.0	6.9
Purchases of goods and services	0.6	0.6	0.6	0.6	0.7	0.7	0.6	0.6	0.5	0.5	0.5	0.5
Interest 4/	2.3	2.3	2.3	2.7	2.9	2.8	3.2	3.4	3.6	3.7	3.5	3.5
Of which: Adjustment for TUDES	0.3	0.2	0.2	0.2	0.3	0.0	0.1	0.2	0.2	0.2	0.2	0.2
Social benefits	2.6	2.6	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Other expense 5/	3.8	3.6	4.0	4.4	4.4	4.6	4.4	4.3	4.2	4.2	4.2	4.2
Net acquisition of nonfinancial assets	2.3	1.4	1.4	1.6	1.7	1.9	2.0	2.1	2.1	2.1	2.1	2.1
Gross operating balance	**-3.0**	**-2.8**	**-3.1**	**-4.0**	**-4.3**	**-4.0**	**-3.7**	**-2.3**	**-1.5**	**-1.5**	**-1.2**	**-1.1**
Net lending/borrowing	**-5.3**	**-4.2**	**-4.5**	**-5.6**	**-6.0**	**-5.8**	**-5.7**	**-4.4**	**-3.6**	**-3.6**	**-3.3**	**-3.2**
Net financial transactions	**5.3**	**4.2**	**4.5**	**5.6**	**6.0**	**5.8**	**5.7**	**4.4**	**3.6**	**3.6**	**3.3**	**3.2**
Memorandum items:												
Non-interest expenditure growth (percent)												
in nominal terms	23.1	3.0	11.7	12.0	9.1	9.0	6.7	6.4	7.3	8.1	7.2	7.1
in real terms	16.5	-1.8	6.9	6.4	4.4	8.1	5.6	3.3	4.2	4.9	4.1	4.0
Primary balance												
in billions of colones	-580	-396	-529	-704	-830	-862	-739	-305	3	37	73	114
in percent of GDP	-3.0	-1.9	-2.3	-2.8	-3.1	-3.0	-2.4	-0.9	0.0	0.1	0.2	0.3
Cyclically-adjusted primary balance (percent of GDP)	-3.1	-2.0	-2.6	-2.9	-3.0	-2.9	-2.3	-0.8	0.1	0.1	0.2	0.2
Fiscal impulse (percent of GDP)	1.9	-1.0	0.6	0.3	0.1	-0.1	-0.6	-1.5	-0.9	0.0	-0.1	-0.1
Nominal GDP	19,581	21,392	23,371	24,781	26,703	28,279	30,549	32,832	35,780	38,892	41,941	45,177
CPI Inflation (period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes measures as in the baseline partial adjustment scenario, as well as administratively-determined measures to contain growth in the wage bill, and increases in the VAT rate from 2017.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

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

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

5/ Includes subsidies, transfers and other expense.

Table 5a. Costa Rica: Consolidated Public Sector Operations, Baseline Scenario (Partial Adjustment) 1/ 2/ 3/

	2010	2011	2012	2013	2014	Est. 2015	Projections 2016	2017	2018	2019	2020	2021
						(In billions of colones)						
Nonfinancial public sector:												
Revenue	**4,258**	**4,715**	**5,036**	**5,627**	**6,021**	**6,529**	**7,106**	**7,966**	**8,728**	**9,443**	**10,150**	**10,904**
Tax revenue	2,526	2,807	3,049	3,342	3,575	3,917	4,350	5,001	5,525	5,981	6,429	6,904
Nontax revenue	185	225	182	257	259	309	273	293	317	343	368	396
Social security contributions	1,412	1,584	1,743	1,884	2,055	2,225	2,399	2,580	2,788	3,014	3,240	3,482
Operating balance of public enterprises	134	99	62	144	132	78	84	91	98	106	114	123
Expenditure 4/	**5,209**	**5,482**	**5,941**	**6,770**	**7,344**	**8,001**	**8,759**	**9,593**	**10,453**	**11,326**	**12,158**	**12,955**
Current noninterest	4,138	4,525	4,884	5,465	5,899	6,424	6,877	7,383	7,977	8,624	9,271	9,964
Wages	1,885	2,076	2,228	2,437	2,620	2,791	3,005	3,243	3,509	3,794	4,078	4,383
Goods and services	414	482	514	554	594	643	678	729	788	852	916	984
Transfers	1,840	1,966	2,142	2,474	2,685	2,990	3,194	3,411	3,680	3,979	4,277	4,597
Interest	432	478	506	660	740	795	1,017	1,274	1,466	1,609	1,713	1,730
Of which: Adjustment for TUDES 5/	28	26	32	27	42	-7	24	28	32	36	41	46
Capital	638	480	551	644	705	783	864	935	1,010	1,092	1,174	1,262
Primary balance	**-519**	**-289**	**-399**	**-483**	**-583**	**-677**	**-636**	**-353**	**-260**	**-274**	**-294**	**-322**
Overall Balance	**-951**	**-767**	**-905**	**-1,143**	**-1,323**	**-1,472**	**-1,653**	**-1,627**	**-1,725**	**-1,883**	**-2,007**	**-2,052**
Central government	-1,032	-893	-1,059	-1,386	-1,604	-1,649	-1,761	-1,783	-1,932	-2,116	-2,264	-2,325
Decentralized government entities	50	130	193	207	259	224	150	198	248	275	298	315
Public enterprises	31	-4	-39	34	24	-42	-42	-42	-42	-42	-42	-42
Total Financing	**951**	**767**	**905**	**1,143**	**1,323**	**1,472**	**1,653**	**1,627**	**1,725**	**1,883**	**2,007**	**2,052**
External	243	-128	338	405	505	479	427	435	390	397	283	0
Domestic	708	895	568	738	818	993	1,226	1,192	1,336	1,486	1,724	2,052
Consolidated public sector:												
Central Bank balance	-88	-126	-144	-195	-186	-219	-231	-255	-280	-305	-330	-355
Consolidated public sector balance	**-1,039**	**-893**	**-1,049**	**-1,339**	**-1,508**	**-1,687**	**-1,883**	**-1,883**	**-2,006**	**-2,188**	**-2,337**	**-2,407**
Consolidated public sector debt	**5,824**	**6,862**	**8,787**	**10,420**	**11,538**	**13,008**	**14,611**	**16,255**	**18,002**	**19,912**	**21,781**	**23,804**
						(In percent of GDP)						
Nonfinancial public sector:												
Revenue	**21.7**	**22.0**	**21.5**	**22.7**	**22.5**	**23.1**	**23.3**	**24.3**	**24.6**	**24.6**	**24.6**	**24.6**
Tax revenue	12.9	13.1	13.0	13.5	13.4	13.9	14.3	15.2	15.6	15.6	15.6	15.6
Nontax revenue	0.9	1.1	0.8	1.0	1.0	1.1	0.9	0.9	0.9	0.9	0.9	0.9
Social security contributions	7.2	7.4	7.5	7.6	7.7	7.9	7.9	7.9	7.9	7.9	7.9	7.9
Operating balance of public enterprises	0.7	0.5	0.3	0.6	0.5	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Expenditure 4/	**26.6**	**25.6**	**25.4**	**27.3**	**27.5**	**28.3**	**28.7**	**29.2**	**29.5**	**29.6**	**29.5**	**29.3**
Current noninterest	21.1	21.2	20.9	22.1	22.1	22.7	22.6	22.5	22.5	22.5	22.5	22.5
Wages	9.6	9.7	9.5	9.8	9.8	9.9	9.9	9.9	9.9	9.9	9.9	9.9
Goods and services	2.1	2.3	2.2	2.2	2.2	2.3	2.2	2.2	2.2	2.2	2.2	2.2
Transfers	9.4	9.2	9.2	10.0	10.1	10.6	10.5	10.4	10.4	10.4	10.4	10.4
Interest	2.2	2.2	2.2	2.7	2.8	2.8	3.3	3.9	4.1	4.2	4.2	3.9
Of which: Adjustment for TUDES 5/	0.1	0.1	0.1	0.1	0.2	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Capital	3.3	2.2	2.4	2.6	2.6	2.8	2.8	2.9	2.9	2.9	2.9	2.9
Primary balance	**-2.6**	**-1.4**	**-1.7**	**-1.9**	**-2.2**	**-2.4**	**-2.1**	**-1.1**	**-0.7**	**-0.7**	**-0.7**	**-0.7**
Overall Balance	**-4.9**	**-3.6**	**-3.9**	**-4.6**	**-5.0**	**-5.2**	**-5.4**	**-5.0**	**-4.9**	**-4.9**	**-4.9**	**-4.6**
Central government	-5.3	-4.2	-4.5	-5.6	-6.0	-5.8	-5.8	-5.4	-5.5	-5.5	-5.5	-5.3
Decentralized government entities	0.3	0.6	0.8	0.8	1.0	0.8	0.5	0.6	0.7	0.7	0.7	0.7
Public enterprises	0.2	0.0	-0.2	0.1	0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Total Financing	**4.9**	**3.6**	**3.9**	**4.6**	**5.0**	**5.2**	**5.4**	**5.0**	**4.9**	**4.9**	**4.9**	**4.6**
External	1.2	-0.6	1.4	1.6	1.9	1.7	1.4	1.3	1.1	1.0	0.7	0.0
Domestic	3.6	4.2	2.4	3.0	3.1	3.5	4.0	3.6	3.8	3.9	4.2	4.6
Consolidated public sector:												
Central Bank balance	-0.4	-0.6	-0.6	-0.8	-0.7	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8
Consolidated public sector balance	**-5.3**	**-4.2**	**-4.5**	**-5.4**	**-5.6**	**-6.0**	**-6.2**	**-5.7**	**-5.7**	**-5.7**	**-5.7**	**-5.4**
Consolidated public sector debt	**29.7**	**32.1**	**37.6**	**42.0**	**43.2**	**46.0**	**47.9**	**49.6**	**50.8**	**52.0**	**52.9**	**53.8**
Consolidated public sector debt, including ICE	33.0	35.3	40.7	45.3	46.8	49.6	51.6	53.0	54.0	54.9	55.5	56.2
Nominal GDP	19,581	21,392	23,371	24,781	26,703	28,279	30,495	32,804	35,437	38,312	41,183	44,263
CPI Inflation (period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved anti-tax evasion.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ 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).

4/ 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.

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

Table 5b. Costa Rica: Consolidated Public Sector Operations, Full Fiscal Adjustment Scenario 1/ 2/ 3/

						Est.	Projections					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						(In billions of colones)						
Nonfinancial public sector:												
Revenue	**4,258**	**4,715**	**5,036**	**5,627**	**6,021**	**6,529**	**7,106**	**8,077**	**9,015**	**9,753**	**10,484**	**11,262**
Tax revenue	2,526	2,807	3,049	3,342	3,575	3,917	4,350	5,113	5,812	6,291	6,762	7,262
Nontax revenue	185	225	182	257	259	309	273	293	317	343	368	396
Social security contributions	1,412	1,584	1,743	1,884	2,055	2,225	2,399	2,580	2,788	3,014	3,240	3,482
Operating balance of public enterprises	134	99	62	144	132	78	84	91	98	106	114	123
Expenditure 4/	**5,209**	**5,482**	**5,941**	**6,770**	**7,344**	**8,001**	**8,733**	**9,376**	**10,118**	**10,923**	**11,634**	**12,456**
Current noninterest	4,138	4,525	4,884	5,465	5,899	6,424	6,877	7,314	7,836	8,433	9,024	9,654
Wages	1,885	2,076	2,228	2,437	2,620	2,791	3,005	3,194	3,403	3,641	3,872	4,118
Goods and services	414	482	514	554	594	643	678	710	752	813	874	940
Transfers	1,840	1,966	2,142	2,474	2,685	2,990	3,194	3,411	3,680	3,979	4,277	4,597
Interest	432	478	506	660	740	795	992	1,127	1,272	1,397	1,436	1,540
Of which: Adjustment for TUDES 5/	28	26	32	27	42	-7	24	28	31	33	36	39
Capital	638	480	551	644	705	783	864	935	1,010	1,092	1,174	1,262
Primary balance	**-519**	**-289**	**-399**	**-483**	**-583**	**-677**	**-636**	**-173**	**169**	**228**	**286**	**346**
Overall Balance	**-951**	**-767**	**-905**	**-1,143**	**-1,323**	**-1,472**	**-1,628**	**-1,299**	**-1,103**	**-1,169**	**-1,150**	**-1,193**
Central government	-1,032	-893	-1,059	-1,386	-1,604	-1,649	-1,736	-1,447	-1,295	-1,383	-1,377	-1,444
Decentralized government entities	50	130	193	207	259	224	150	190	234	256	269	292
Public enterprises	31	-4	-39	34	24	-42	-42	-42	-42	-42	-42	-42
Total Financing	**951**	**767**	**905**	**1,143**	**1,323**	**1,472**	**1,628**	**1,299**	**1,103**	**1,169**	**1,150**	**1,193**
External	243	-128	338	405	505	479	427	435	390	397	283	0
Domestic	708	895	568	738	818	993	1,201	864	713	772	867	1,193
Consolidated public sector:												
Central Bank balance	-88	-126	-144	-195	-186	-219	-231	-255	-280	-305	-330	-355
Consolidated public sector balance	**-1,039**	**-893**	**-1,049**	**-1,339**	**-1,508**	**-1,687**	**-1,858**	**-1,555**	**-1,383**	**-1,474**	**-1,480**	**-1,548**
Consolidated public sector debt	**5,824**	**6,862**	**8,787**	**10,420**	**11,538**	**13,008**	**14,586**	**15,902**	**17,024**	**18,216**	**19,224**	**20,383**
						(In percent of GDP)						
Nonfinancial public sector:												
Revenue	**21.7**	**22.0**	**21.5**	**22.7**	**22.5**	**23.1**	**23.3**	**24.6**	**25.2**	**25.1**	**25.0**	**24.9**
Tax revenue	12.9	13.1	13.0	13.5	13.4	13.9	14.2	15.6	16.2	16.2	16.1	16.1
Nontax revenue	0.9	1.1	0.8	1.0	1.0	1.1	0.9	0.9	0.9	0.9	0.9	0.9
Social security contributions	7.2	7.4	7.5	7.6	7.7	7.9	7.9	7.9	7.8	7.7	7.7	7.7
Operating balance of public enterprises	0.7	0.5	0.3	0.6	0.5	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Expenditure 4/	**26.6**	**25.6**	**25.4**	**27.3**	**27.5**	**28.3**	**28.6**	**28.6**	**28.3**	**28.1**	**27.7**	**27.6**
Current noninterest	21.1	21.2	20.9	22.1	22.1	22.7	22.5	22.3	21.9	21.7	21.5	21.4
Wages	9.6	9.7	9.5	9.8	9.8	9.9	9.8	9.7	9.5	9.4	9.2	9.1
Goods and services	2.1	2.3	2.2	2.2	2.2	2.3	2.2	2.2	2.1	2.1	2.1	2.1
Transfers	9.4	9.2	9.2	10.0	10.1	10.6	10.5	10.4	10.3	10.2	10.2	10.2
Interest	2.2	2.2	2.2	2.7	2.8	2.8	3.2	3.4	3.6	3.6	3.4	3.4
Of which: Adjustment for TUDES 5/	0.1	0.1	0.1	0.1	0.2	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Capital	3.3	2.2	2.4	2.6	2.6	2.8	2.8	2.8	2.8	2.8	2.8	2.8
Primary balance	**-2.6**	**-1.4**	**-1.7**	**-1.9**	**-2.2**	**-2.4**	**-2.1**	**-0.5**	**0.5**	**0.6**	**0.7**	**0.8**
Overall Balance	**-4.9**	**-3.6**	**-3.9**	**-4.6**	**-5.0**	**-5.2**	**-5.3**	**-4.0**	**-3.1**	**-3.0**	**-2.7**	**-2.6**
Central government	-5.3	-4.2	-4.5	-5.6	-6.0	-5.8	-5.7	-4.4	-3.6	-3.6	-3.3	-3.2
Decentralized government entities	0.3	0.6	0.8	0.8	1.0	0.8	0.5	0.6	0.7	0.7	0.6	0.6
Public enterprises	0.2	0.0	-0.2	0.1	0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Total Financing	**4.9**	**3.6**	**3.9**	**4.6**	**5.0**	**5.2**	**5.3**	**4.0**	**3.1**	**3.0**	**2.7**	**2.6**
External	1.2	-0.6	1.4	1.6	1.9	1.7	1.4	1.3	1.1	1.0	0.7	0.0
Domestic	3.6	4.2	2.4	3.0	3.1	3.5	3.9	2.6	2.0	2.0	2.1	2.6
Consolidated public sector:												
Central Bank balance	-0.4	-0.6	-0.6	-0.8	-0.7	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8
Consolidated public sector balance	**-5.3**	**-4.2**	**-4.5**	**-5.4**	**-5.6**	**-6.0**	**-6.1**	**-4.7**	**-3.9**	**-3.8**	**-3.5**	**-3.4**
Consolidated public sector debt	**29.7**	**32.1**	**37.6**	**42.0**	**43.2**	**46.0**	**47.7**	**48.4**	**47.6**	**46.8**	**45.8**	**45.1**
Consolidated public sector debt, including ICE	33.0	35.3	40.7	45.3	46.8	49.6	51.4	51.9	50.7	49.7	48.4	47.5
Nominal GDP	19,581	21,392	23,371	24,781	26,703	28,279	30,549	32,832	35,780	38,892	41,941	45,177
CPI Inflation (period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes measures as in the baseline partial adjustment scenario, as well as administratively-determined measures to contain growth in the wage bill, and increases in the VAT rate from 2017.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ 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).

4/ 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.

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

Table 6a. Costa Rica: Summary Operations of the Consolidated Public Sector, GFSM 2001 Classification. Baseline Scenario (Partial Adjustment) 1/ 2/ 3/

						Est.			Projection		
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
					(In billions of colones)						
Nonfinancial public sector:											
Revenue	**4,258**	**4,715**	**5,036**	**5,627**	**6,021**	**6,529**	**7,106**	**7,966**	**8,728**	**9,443**	**10,150**
Taxes	2,526	2,807	3,049	3,342	3,575	3,917	4,350	5,001	5,525	5,981	6,429
Social contributions	1,412	1,584	1,743	1,884	2,055	2,225	2,399	2,580	2,788	3,014	3,240
Operating balance of public enterprises	134	99	62	144	132	78	84	91	98	106	114
Other revenue	185	225	182	257	259	309	273	293	317	343	368
Expenditure	**5,209**	**5,482**	**5,941**	**6,770**	**7,344**	**8,001**	**8,759**	**9,593**	**10,453**	**11,326**	**12,158**
Expense	**4,571**	**5,002**	**5,390**	**6,126**	**6,639**	**7,218**	**7,894**	**8,658**	**9,443**	**10,233**	**10,984**
Compensation of employees	1,885	2,076	2,228	2,437	2,620	2,791	3,005	3,243	3,509	3,794	4,078
Purchases of goods and services	414	482	514	554	594	643	678	729	788	852	916
Interest 4/	432	478	506	660	740	795	1,017	1,274	1,466	1,609	1,713
Of which: Adjustment for TUDES	28	26	32	27	42	-7	24	28	32	36	41
Other expense 5/	1,840	1,966	2,142	2,474	2,685	2,990	3,194	3,411	3,680	3,979	4,277
Net acquisition of nonfinancial assets	**638**	**480**	**551**	**644**	**705**	**783**	**864**	**935**	**1,010**	**1,092**	**1,174**
Gross operating balance	**-313**	**-287**	**-354**	**-499**	**-618**	**-689**	**-789**	**-692**	**-715**	**-790**	**-833**
Net lending/borrowing (NFPS)	**-951**	**-767**	**-905**	**-1,143**	**-1,323**	**-1,472**	**-1,653**	**-1,627**	**-1,725**	**-1,883**	**-2,007**
Net financial transactions (NFPS)	**951**	**767**	**905**	**1,143**	**1,323**	**1,472**	**1,653**	**1,627**	**1,725**	**1,883**	**2,007**
Consolidated public sector:											
Central Bank balance	-88	-126	-144	-195	-186	-219	-231	-255	-280	-305	-330
Net lending/borrowing (consolidated public sector)	**-1,039**	**-893**	**-1,049**	**-1,339**	**-1,508**	**-1,687**	**-1,883**	**-1,883**	**-2,006**	**-2,188**	**-2,337**
					(In percent of GDP)						
Nonfinancial public sector:											
Revenue	**21.7**	**22.0**	**21.5**	**22.7**	**22.5**	**23.1**	**23.3**	**24.3**	**24.6**	**24.6**	**24.6**
Taxes	12.9	13.1	13.0	13.5	13.4	13.9	14.3	15.2	15.6	15.6	15.6
Social contributions	7.2	7.4	7.5	7.6	7.7	7.9	7.9	7.9	7.9	7.9	7.9
Operating balance of public enterprises	0.7	0.5	0.3	0.6	0.5	0.3	0.3	0.3	0.3	0.3	0.3
Other revenue	0.9	1.1	0.8	1.0	1.0	1.1	0.9	0.9	0.9	0.9	0.9
Expenditure	**26.6**	**25.6**	**25.4**	**27.3**	**27.5**	**28.3**	**28.7**	**29.2**	**29.5**	**29.6**	**29.5**
Expense	**23.3**	**23.4**	**23.1**	**24.7**	**24.9**	**25.5**	**25.9**	**26.4**	**26.6**	**26.7**	**26.7**
Compensation of employees	9.6	9.7	9.5	9.8	9.8	9.9	9.9	9.9	9.9	9.9	9.9
Purchases of goods and services	2.1	2.3	2.2	2.2	2.2	2.3	2.2	2.2	2.2	2.2	2.2
Interest 4/	2.2	2.2	2.2	2.7	2.8	2.8	3.3	3.9	4.1	4.2	4.2
Other expense 5/	9.4	9.2	9.2	10.0	10.1	10.6	10.5	10.4	10.4	10.4	10.4
Net acquisition of nonfinancial assets	**3.3**	**2.2**	**2.4**	**2.6**	**2.6**	**2.8**	**2.8**	**2.9**	**2.9**	**2.9**	**2.9**
Gross operating balance	**-1.6**	**-1.3**	**-1.5**	**-2.0**	**-2.3**	**-2.4**	**-2.6**	**-2.1**	**-2.0**	**-2.1**	**-2.0**
Net lending/borrowing (NFPS)	**-4.9**	**-3.6**	**-3.9**	**-4.6**	**-5.0**	**-5.2**	**-5.4**	**-5.0**	**-4.9**	**-4.9**	**-4.9**
Net financial transactions (NFPS)	**4.9**	**3.6**	**3.9**	**4.6**	**5.0**	**5.2**	**5.4**	**5.0**	**4.9**	**4.9**	**4.9**
Consolidated public sector:											
Central Bank balance	-0.4	-0.6	-0.6	-0.8	-0.7	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8
Net lending/borrowing (consolidated public sector)	**-5.3**	**-4.2**	**-4.5**	**-5.4**	**-5.6**	**-6.0**	**-6.2**	**-5.7**	**-5.7**	**-5.7**	**-5.7**
Memorandum items:											
NFPS non-interest expenditure growth (percent)											
in nominal terms	20.6	4.8	8.6	12.4	8.1	9.1	7.4	7.5	8.0	8.1	7.5
in real terms	14.1	-0.1	3.9	6.8	3.4	8.3	6.3	4.3	4.9	5.0	7.5
NFPS primary balance											
in billions of colones	-519	-289	-399	-483	-583	-677	-636	-353	-260	-274	-294
in percent of GDP	-2.6	-1.4	-1.7	-1.9	-2.2	-2.4	-2.1	-1.1	-0.7	-0.7	-0.7

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles a estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from impro anti-tax evasion.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ The consolidated public sector balance comprises the central government, decentralized government entities, public enterprises and the Central Bank, but excludes the Instituto Costarricense de Electricida

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

5/ Includes subsidies, transfers and other expense.

Table 6b. Costa Rica: Summary Operations of the Consolidated Public Sector, GFSM 2001 Classification. Full Fiscal Adjustment Scenario 1/ 2/ 3/

						Est.	Projection					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
	(In billions of colones)											
Nonfinancial public sector:												
Revenue	**4,258**	**4,715**	**5,036**	**5,627**	**6,021**	**6,529**	**7,106**	**8,077**	**9,015**	**9,753**	**10,484**	**11,262**
Taxes	2,526	2,807	3,049	3,342	3,575	3,917	4,350	5,113	5,812	6,291	6,762	7,262
Social contributions	1,412	1,584	1,743	1,884	2,055	2,225	2,399	2,580	2,788	3,014	3,240	3,482
Operating balance of public enterprises	134	99	62	144	132	78	84	91	98	106	114	123
Other revenue	185	225	182	257	259	309	273	293	317	343	368	396
Expenditure	**5,209**	**5,482**	**5,941**	**6,770**	**7,344**	**8,001**	**8,733**	**9,376**	**10,118**	**10,923**	**11,634**	**12,456**
Expense	**4,571**	**5,002**	**5,390**	**6,126**	**6,639**	**7,218**	**7,869**	**8,441**	**9,107**	**9,830**	**10,460**	**11,194**
Compensation of employees	1,885	2,076	2,228	2,437	2,620	2,791	3,005	3,194	3,403	3,641	3,872	4,118
Purchases of goods and services	414	482	514	554	594	643	678	710	752	813	874	940
Interest 4/	432	478	506	660	740	795	992	1,127	1,272	1,397	1,436	1,540
Of which: Adjustment for TUDES	28	26	32	27	42	-7	24	28	31	33	36	39
Other expense 5/	1,840	1,966	2,142	2,474	2,685	2,990	3,194	3,411	3,680	3,979	4,277	4,597
Net acquisition of nonfinancial assets	**638**	**480**	**551**	**644**	**705**	**783**	**864**	**935**	**1,010**	**1,092**	**1,174**	**1,262**
Gross operating balance	**-313**	**-287**	**-354**	**-499**	**-618**	**-689**	**-763**	**-364**	**-93**	**-77**	**24**	**69**
Net lending/borrowing (NFPS)	**-951**	**-767**	**-905**	**-1,143**	**-1,323**	**-1,472**	**-1,628**	**-1,299**	**-1,103**	**-1,169**	**-1,150**	**-1,193**
Net financial transactions (NFPS)	**951**	**767**	**905**	**1,143**	**1,323**	**1,472**	**1,628**	**1,299**	**1,103**	**1,169**	**1,150**	**1,193**
Consolidated public sector:												
Central Bank balance	-88	-126	-144	-195	-186	-219	-231	-255	-280	-305	-330	-355
Net lending/borrowing (consolidated public sector)	**-1,039**	**-893**	**-1,049**	**-1,339**	**-1,508**	**-1,687**	**-1,858**	**-1,555**	**-1,383**	**-1,474**	**-1,480**	**-1,548**
	(In percent of GDP)											
Nonfinancial public sector:												
Revenue	**21.7**	**22.0**	**21.5**	**22.7**	**22.5**	**23.1**	**23.3**	**24.6**	**25.2**	**25.1**	**25.0**	**24.9**
Taxes	12.9	13.1	13.0	13.5	13.4	13.9	14.2	15.6	16.2	16.2	16.1	16.1
Social contributions	7.2	7.4	7.5	7.6	7.7	7.9	7.9	7.9	7.8	7.7	7.7	7.7
Operating balance of public enterprises	0.7	0.5	0.3	0.6	0.5	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Other revenue	0.9	1.1	0.8	1.0	1.0	1.1	0.9	0.9	0.9	0.9	0.9	0.9
Expenditure	**26.6**	**25.6**	**25.4**	**27.3**	**27.5**	**28.3**	**28.6**	**28.6**	**28.3**	**28.1**	**27.7**	**27.6**
Expense	**23.3**	**23.4**	**23.1**	**24.7**	**24.9**	**25.5**	**25.8**	**25.7**	**25.5**	**25.3**	**24.9**	**24.8**
Compensation of employees	9.6	9.7	9.5	9.8	9.8	9.9	9.8	9.7	9.5	9.4	9.2	9.1
Purchases of goods and services	2.1	2.3	2.2	2.2	2.2	2.3	2.2	2.2	2.1	2.1	2.1	2.1
Interest 4/	2.2	2.2	2.2	2.7	2.8	2.8	3.2	3.4	3.6	3.6	3.4	3.4
Other expense 5/	9.4	9.2	9.2	10.0	10.1	10.6	10.5	10.4	10.3	10.2	10.2	10.2
Net acquisition of nonfinancial assets	**3.3**	**2.2**	**2.4**	**2.6**	**2.6**	**2.8**	**2.8**	**2.8**	**2.8**	**2.8**	**2.8**	**2.8**
Gross operating balance	**-1.6**	**-1.3**	**-1.5**	**-2.0**	**-2.3**	**-2.4**	**-2.5**	**-1.1**	**-0.3**	**-0.2**	**0.1**	**0.2**
Net lending/borrowing (NFPS)	**-4.9**	**-3.6**	**-3.9**	**-4.6**	**-5.0**	**-5.2**	**-5.3**	**-4.0**	**-3.1**	**-3.0**	**-2.7**	**-2.6**
Net financial transactions (NFPS)	**4.9**	**3.6**	**3.9**	**4.6**	**5.0**	**5.2**	**5.3**	**4.0**	**3.1**	**3.0**	**2.7**	**2.6**
Consolidated public sector:												
Central Bank balance	-0.4	-0.6	-0.6	-0.8	-0.7	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8
Net lending/borrowing (consolidated public sector)	**-5.3**	**-4.2**	**-4.5**	**-5.4**	**-5.6**	**-6.0**	**-6.1**	**-4.7**	**-3.9**	**-3.8**	**-3.5**	**-3.4**
Memorandum items:												
NFPS non-interest expenditure growth (percent)												
in nominal terms	20.6	4.8	8.6	12.4	8.1	9.1	7.4	6.6	7.2	7.7	7.1	7.0
in real terms	14.1	-0.1	3.9	6.8	3.4	8.3	6.3	3.5	4.1	4.5	7.1	7.0
NFPS primary balance												
in billions of colones	-519	-289	-399	-483	-583	-677	-636	-173	169	228	286	346
in percent of GDP	-2.6	-1.4	-1.7	-1.9	-2.2	-2.4	-2.1	-0.5	0.5	0.6	0.7	0.8

Sources: Ministry of Finance and Fund staff estimates.

1/ Includes measures as in the baseline partial adjustment scenario, as well as administratively-determined measures to contain growth in the wage bill, and increases in the VAT rate from 2017.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ 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).

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

5/ Includes subsidies, transfers and other expense.

Table 7. Costa Rica: Public Sector Debt, Baseline Scenario (Partial Fiscal Adjustment) 1/ 2/

						Est.	Projections					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
	(In billions of colones)											
Debt issued by:												
NFPS & Central Bank (I) 3/	**7,574**	**8,961**	**11,043**	**12,774**	**14,159**	**15,888**	**17,671**	**19,542**	**21,572**	**23,795**	**25,993**	**28,362**
Nonfinancial public sector (NFPS) 3/	6,168	7,248	8,976	10,154	11,811	13,359	15,174	17,045	19,076	21,298	23,497	25,866
Central government	5,562	6,382	8,015	8,932	10,484	11,984	13,732	15,532	17,490	19,640	21,770	24,072
Rest of nonfinancial public sector 3/	605	866	961	1,222	1,327	1,376	1,442	1,514	1,586	1,658	1,726	1,794
Central Bank	1,406	1,713	2,067	2,620	2,348	2,528	2,496	2,496	2,496	2,496	2,496	2,496
Intra-public sector debt holdings (II)	**1,750**	**2,099**	**2,256**	**2,354**	**2,621**	**2,880**	**3,060**	**3,287**	**3,570**	**3,883**	**4,212**	**4,558**
CCSS 4/	1,130	1,330	1,398	1,444	1,640	1,842	1,940	2,082	2,269	2,476	2,700	2,933
Other entities of the nonfinancial public sector	604	756	848	899	969	1,026	1,106	1,190	1,285	1,390	1,494	1,606
Central Bank	15	13	10	11	12	13	14	15	16	17	18	20
Consolidated public sector debt (I-II)	**5,824**	**6,862**	**8,787**	**10,420**	**11,538**	**13,008**	**14,611**	**16,255**	**18,002**	**19,912**	**21,781**	**23,804**
External	1,363	1,330	1,711	2,201	2,812	3,319	3,724	4,164	4,568	4,984	5,116	5,495
Domestic	4,461	5,532	7,076	8,219	8,726	9,689	10,887	12,091	13,434	14,927	16,665	18,309
	(In percent of GDP)											
Debt issued by:												
NFPS & Central Bank (I) 3/	**38.7**	**41.9**	**47.2**	**51.5**	**53.0**	**56.2**	**57.9**	**59.6**	**60.9**	**62.1**	**63.1**	**64.1**
Nonfinancial public sector (NFPS) 3/	31.5	33.9	38.4	41.0	44.2	47.2	49.8	52.0	53.8	55.6	57.1	58.4
Central government	28.4	29.8	34.3	36.0	39.3	42.4	45.0	47.3	49.4	51.3	52.9	54.4
Rest of nonfinancial public sector 3/	3.1	4.0	4.1	4.9	5.0	4.9	4.7	4.6	4.5	4.3	4.2	4.1
Central Bank	7.2	8.0	8.8	10.6	8.8	8.9	8.2	7.6	7.0	6.5	6.1	5.6
Intra-public sector debt holdings (II)	**8.9**	**9.8**	**9.7**	**9.5**	**9.8**	**10.2**	**10.0**	**10.0**	**10.1**	**10.1**	**10.2**	**10.3**
CCSS 4/	5.8	6.2	6.0	5.8	6.1	6.5	6.4	6.3	6.4	6.5	6.6	6.6
Other entities of the nonfinancial public sector	3.1	3.5	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6
Central Bank	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Consolidated public sector debt (I-II)	**29.7**	**32.1**	**37.6**	**42.0**	**43.2**	**46.0**	**47.9**	**49.6**	**50.8**	**52.0**	**52.9**	**53.8**
External	7.0	6.2	7.3	8.9	10.5	11.7	12.2	12.7	12.9	13.0	12.4	12.4
Domestic	22.8	25.9	30.3	33.2	32.7	34.3	35.7	36.9	37.9	39.0	40.5	41.4
Memorandum items:												
Nominal GDP	19,581	21,392	23,371	24,781	26,703	28,279	30,495	32,804	35,437	38,312	41,183	44,263

Sources: Ministry of Finance; and Fund staff estimates.

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved anti-tax evasion.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

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

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

Table 8. Costa Rica: Monetary Survey, Baseline Scenario (Partial Adjustment) 1/ 2/

						Est.	Proj.	Proj.
	2010	2011	2012	2013	2014	2015	2016	2017
	(In billions of colones, unless otherwise indicated)							
Net foreign assets	2,485	2,567	3,612	3,799	4,038	4,413	4,792	5,195
Net international reserves	2,350	2,403	3,443	3,629	3,846	4,167	4,477	4,793
(In millions of U.S. dollars)	4,627	4,756	6,857	7,331	7,211	7,834	8,334	8,834
Net medium-term foreign assets	135	164	170	171	192	0	0	0
Net domestic assets	-1,140	-1,067	-1,858	-1,865	-1,902	-2,081	-2,247	-2,420
Net domestic credit	-926	-729	-1,303	-935	-1,019	-1,193	-1,290	-1,400
Credit to nonfinancial public sector	-288	-87	-561	-201	-65	-123	-123	-123
Credit to other depository corporations (net)	-625	-633	-733	-722	-936	-1,044	-1,141	-1,252
Credit to other financial corporations (net)	-9	-7	-7	-9	-16	-25	-25	-25
Credit to the private sector (net)	-3	-2	-2	-2	-2	-1	-1	-1
Monetary stabilization instruments (-)	-1,252	-1,588	-1,787	-2,492	-2,313	-2,491	-2,491	-2,491
Other items (net)	-319	-235	-423	-326	-421	-478	-778	-1,096
Capital account (-)	1,357	1,485	1,655	1,887	1,850	2,081	2,312	2,567
Monetary base	1,345	1,500	1,754	1,934	2,136	2,332	2,545	2,776
Currency	665	743	845	921	988	1,051	1,120	1,198
Required reserves	680	757	909	1,013	1,147	1,281	1,425	1,577
Net foreign assets	-87	-580	-1,018	-1,534	-1,716	-2,475	-3,507	-3,936
Net domestic assets	8,389	9,287	10,565	11,797	13,505	14,961	16,971	18,420
Net domestic credit	11,891	13,175	15,265	17,241	20,072	22,682	25,602	28,754
Credit to nonfinancial public sector (net)	980	1,001	1,148	1,225	1,493	1,986	2,588	3,163
Credit to nonfinancial private sector	8,645	9,832	11,145	12,507	14,701	16,440	18,435	20,646
Credit to financial corporations (net)	2,267	2,342	2,973	3,508	3,877	4,257	4,579	4,946
Other items (net)	-1,466	-1,595	-2,097	-2,526	-3,316	-4,093	-4,567	-5,437
Capital account	2,036	2,294	2,602	2,918	3,251	3,628	4,064	4,897
Liabilities to nonfinancial private sector	8,301	8,707	9,547	10,263	11,789	12,486	13,464	14,483
In national currency	4,911	5,171	6,045	6,855	7,721	8,379	9,036	9,720
In foreign currency	3,390	3,536	3,503	3,409	4,068	4,107	4,428	4,764
Of which: Deposits	8,096	8,470	9,300	9,984	11,486	12,151	13,364	14,651
Net foreign assets	2,398	1,988	2,594	2,265	2,322	1,938	1,285	1,259
Net domestic assets	7,478	8,427	8,937	10,158	12,012	13,344	15,317	16,719
Net domestic credit	9,336	10,746	11,731	13,532	16,129	18,303	20,901	23,686
Other items (net)	-1,179	-1,510	-1,847	-2,343	-2,716	-3,412	-3,831	-4,637
Capital account	680	809	947	1,030	1,401	1,547	1,753	2,330
Broad money	9,875	10,415	11,530	12,424	14,334	15,282	16,602	17,978
Memorandum Items:	(Annual percentage change)							
Monetary base	11.2	11.6	16.9	10.2	10.4	9.2	9.1	9.0
Broad money	-0.2	5.5	10.7	7.7	15.4	6.6	8.6	8.3
Credit to the private sector	4.4	13.7	13.4	12.2	17.5	11.8	12.1	12.0
Adjusted by changes in the exchange rate	8.6	13.8	13.7	12.9	14.1	11.9	12.2	11.6
	(In percent of GDP)							
Monetary base	6.9	7.0	7.5	7.8	8.0	8.2	8.3	8.5
Broad money	50.4	48.7	49.3	50.1	53.7	54.0	54.4	54.8
Of which: Deposits denominated in foreign currency	17.3	16.5	15.0	13.8	15.2	14.5	14.7	15.0
Credit to the private sector	44.1	46.0	47.7	50.5	55.1	58.1	60.5	62.9
Of which: In foreign currency	17.0	18.1	19.5	21.2	22.5	24.3	25.5	26.0
Central bank balance	-0.5	-0.6	-0.7	-0.9	0.1	-0.8	-0.8	-0.8

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

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved anti-tax evasion.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

Table 9a. Costa Rica: Medium-Term Framework, Baseline Scenario (Partial Adjustment) 1/ 2/

						Est.	Projections					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
	(Annual percentage change)											
Real GDP	5.0	4.5	5.2	1.8	3.0	3.7	4.2	4.3	4.4	4.3	4.0	4.0
Domestic demand	8.2	5.6	5.5	1.4	4.1	4.4	3.3	4.6	5.2	5.2	4.7	4.7
Consumption	2.5	3.5	8.1	2.8	3.4	4.1	2.2	4.1	4.7	4.6	4.1	4.1
Gross fixed capital formation	5.5	8.9	8.0	-1.2	2.2	8.3	7.1	6.2	7.0	7.0	6.9	6.9
Exports of goods and nonfactor services	6.0	5.6	8.1	2.2	3.1	1.9	-1.3	7.1	5.5	5.3	5.0	5.0
Imports of goods and nonfactor services	16.7	8.7	8.7	1.1	6.2	4.4	-2.9	7.9	7.6	7.9	6.8	6.8
	(Contributions to real GDP growth)											
Domestic demand	8.1	5.7	5.7	1.4	4.3	4.6	3.5	4.8	5.4	5.5	5.0	5.1
Consumption	2.1	2.9	6.5	2.3	2.9	3.4	1.9	3.5	3.9	3.8	3.4	3.4
Gross fixed capital formation	1.1	1.7	1.6	-0.2	0.4	1.7	1.5	1.3	1.5	1.6	1.6	1.6
Inventory changes	4.9	1.1	-2.5	-0.7	1.0	-0.5	0.2	0.1	0.0	0.1	0.0	0.0
Net exports	-3.2	-1.2	-0.5	0.3	-1.2	-1.0	0.7	-0.6	-1.0	-1.2	-1.0	-1.1
	(In percent of GDP)											
Savings and Investment												
Savings	20.8	22.0	20.5	18.8	19.6	19.1	19.1	19.3	19.3	19.5	19.7	19.8
Domestic savings	17.4	16.8	15.3	13.8	14.9	15.1	14.9	15.0	15.0	15.2	15.3	15.5
Private sector	19.0	18.1	16.8	15.9	17.2	17.1	17.2	16.8	16.7	16.9	17.0	17.0
Public sector	-1.6	-1.3	-1.5	-2.0	-2.3	-2.1	-2.3	-1.8	-1.7	-1.7	-1.7	-1.5
External savings 3/	3.4	5.3	5.2	5.0	4.7	4.0	4.2	4.3	4.2	4.3	4.3	4.3
Gross domestic investment	20.8	22.0	20.5	18.8	19.6	19.1	19.1	19.3	19.3	19.5	19.7	19.8
Private sector	16.6	17.1	17.4	16.2	16.2	16.4	15.8	15.7	15.7	15.7	15.8	15.8
Public sector	3.4	3.1	3.2	3.2	3.3	3.4	3.5	3.5	3.5	3.5	3.5	3.5
Inventory changes	0.8	1.9	-0.1	-0.6	0.1	-0.7	-0.2	0.0	0.1	0.3	0.4	0.4
Balance of payments												
Current account balance	-3.4	-5.3	-5.2	-5.0	-4.7	-4.0	-4.2	-4.3	-4.2	-4.3	-4.3	-4.3
Trade balance	-9.2	-12.2	-11.6	-11.3	-10.5	-10.2	-10.2	-10.4	-10.7	-11.1	-11.3	-11.5
Services	6.8	7.5	7.4	8.1	8.7	8.7	8.7	8.9	9.3	9.6	9.8	10.0
Income	-2.0	-1.4	-1.7	-2.4	-3.5	-3.2	-3.2	-3.3	-3.4	-3.4	-3.4	-3.4
Current transfers	1.0	0.8	0.7	0.6	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.5
Financial and capital account	5.3	6.1	9.5	6.4	4.6	6.2	5.1	5.1	4.2	4.3	4.3	4.3
Public sector	1.7	0.2	2.7	2.5	2.1	1.3	1.3	1.4	1.2	1.1	0.7	1.0
Private sector	3.7	5.9	6.8	3.9	2.5	4.9	3.8	3.7	3.1	3.2	3.6	3.4
Foreign direct investment	3.9	5.0	4.1	4.8	4.0	4.1	4.3	4.3	4.3	4.4	4.4	4.4
Other net private flows	-0.2	0.9	2.7	-0.9	-1.5	0.8	-0.5	-0.6	-1.3	-1.1	-0.8	-1.1
Errors and omissions	-0.4	-0.5	0.2	-0.5	-0.1	-1.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in net international reserves (increase -)	-1.5	-0.3	-4.5	-0.9	0.2	-1.2	-0.9	-0.8	0.0	0.0	0.0	0.0
Memorandum items:												
Nominal GDP (billions of colones)	19,581	21,392	23,371	24,781	26,703	28,279	30,495	32,804	35,437	38,312	41,183	44,263
GDP deflator (percent change)	8.0	4.5	3.9	4.2	4.7	2.2	3.4	3.2	3.5	3.7	3.4	3.3
Consumer prices (percent change; period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0
Consumer prices (percent change; end of period)	5.8	4.7	4.6	3.7	5.1	-0.8	3.0	3.0	3.0	3.0	3.0	3.0
Credit to the private sector (percent change)	4.4	13.7	13.4	12.2	17.5	11.8	12.1	12.0	11.6	11.6	11.3	11.2
Net international reserves (millions of U.S. dollars)	4,627	4,756	6,857	7,331	7,211	7,834	8,334	8,834	8,834	8,834	8,834	8,834

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

1/ Includes cuts in transfers of about 0.4 percent of GDP, another 0.2 percent of GDP of expenditure cuts in a 2016 supplementary budget, broadening of the VAT base and higher taxes on sales of vehicles and real estate from the last quarter of 2016, increase in marginal income tax rates on higher-income brackets from 2017, as well as further amendments to the corporate income tax and moderate gains from improved anti-tax evasion.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of

3/ External current account deficit.

Table 9b. Costa Rica: Medium-Term Framework, Full Fiscal Adjustment Scenario 1/ 2/

						Est.	Projections					
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
					(Annual percentage change)							
Real GDP	5.0	4.5	5.2	1.8	3.0	3.7	4.2	4.2	4.6	4.5	4.2	4.3
Domestic demand	8.2	5.6	5.5	1.4	4.1	4.4	4.8	4.5	5.5	5.4	4.9	4.9
Consumption	2.5	3.5	8.1	2.8	3.4	4.1	4.0	3.9	4.7	4.9	4.2	4.2
Gross fixed capital formation	5.5	8.9	8.0	-1.2	2.2	8.3	7.2	6.2	7.0	6.4	7.1	7.1
Exports of goods and nonfactor services	6.0	5.6	8.1	2.2	3.1	1.9	7.4	7.4	5.4	5.3	4.9	4.9
Imports of goods and nonfactor services	16.7	8.7	8.7	1.1	6.2	4.4	8.6	7.7	7.6	7.5	6.4	6.3
					(Contributions to real GDP growth)							
Domestic demand	8.1	5.7	5.7	1.4	4.3	4.6	5.0	4.7	5.8	5.8	5.3	5.3
Consumption	2.1	2.9	6.5	2.3	2.9	3.4	3.4	3.3	4.0	4.1	3.6	3.5
Gross fixed capital formation	1.1	1.7	1.6	-0.2	0.4	1.7	1.5	1.3	1.5	1.4	1.6	1.7
Inventory changes	4.9	1.1	-2.5	-0.7	1.0	-0.5	0.1	0.1	0.3	0.3	0.1	0.1
Net exports	-3.2	-1.2	-0.5	0.3	-1.2	-1.0	-0.8	-0.5	-1.2	-1.3	-1.0	-1.0
					(In percent of GDP)							
Savings and Investment												
Savings	20.8	22.0	20.5	18.8	19.6	19.1	19.1	19.3	20.0	20.5	20.7	20.9
Domestic savings	17.4	16.8	15.3	13.8	14.9	15.1	14.8	15.1	15.9	16.5	16.8	17.2
Private sector	19.0	18.1	16.8	15.9	17.2	17.1	17.1	15.8	15.8	16.4	16.7	16.9
Public sector	-1.6	-1.3	-1.5	-2.0	-2.3	-2.1	-2.2	-0.8	0.1	0.0	0.1	0.2
External savings 3/	3.4	5.3	5.2	5.0	4.7	4.0	4.2	4.2	4.1	4.0	3.8	3.7
Gross domestic investment	20.8	22.0	20.5	18.8	19.6	19.1	19.1	19.3	20.0	20.5	20.7	20.9
Private sector	16.6	17.1	17.4	16.2	16.2	16.4	15.8	15.7	15.6	15.3	15.3	15.4
Public sector	3.4	3.1	3.2	3.2	3.3	3.4	3.5	3.5	3.5	3.5	3.5	3.6
Inventory changes	0.8	1.9	-0.1	-0.6	0.1	-0.7	-0.2	0.0	1.0	1.7	1.8	1.9
Balance of payments												
Current account balance	-3.4	-5.3	-5.2	-5.0	-4.7	-4.0	-4.2	-4.2	-4.1	-4.0	-3.8	-3.7
Trade balance	-9.2	-12.2	-11.6	-11.3	-10.5	-10.2	-10.2	-10.3	-10.5	-10.6	-10.6	-10.6
Services	6.8	7.5	7.4	8.1	8.7	8.7	8.7	8.9	9.2	9.4	9.6	9.7
Income	-2.0	-1.4	-1.7	-2.4	-3.5	-3.2	-3.2	-3.3	-3.3	-3.3	-3.3	-3.3
Current transfers	1.0	0.8	0.7	0.6	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.5
Financial and capital account	5.3	6.1	9.5	6.4	4.6	6.2	5.1	5.0	4.1	4.0	3.8	3.7
Public sector	1.7	0.2	2.7	2.5	2.1	1.3	1.3	1.4	1.2	1.1	0.7	1.0
Private sector	3.7	5.9	6.8	3.9	2.5	4.9	3.8	3.6	2.9	2.9	3.1	2.7
Foreign direct investment	3.9	5.0	4.1	4.8	4.0	4.1	4.3	4.3	4.3	4.4	4.4	4.5
Other net private flows	-0.2	0.9	2.7	-0.9	-1.5	0.8	-0.5	-0.7	-1.4	-1.5	-1.3	-1.8
Errors and omissions	-0.4	-0.5	0.2	-0.5	-0.1	-1.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in net international reserves (increase -)	-1.5	-0.3	-4.5	-0.9	0.2	-1.2	-0.9	-0.8	0.0	0.0	0.0	0.0
Memorandum items:												
Nominal GDP (billions of colones)	19,581	21,392	23,371	24,781	26,703	28,279	30,549	32,832	35,780	38,892	41,941	45,177
GDP deflator (percent change)	8.0	4.5	3.9	4.2	4.7	2.2	3.6	3.1	4.2	4.0	3.4	3.3
Consumer prices (percent change; period average)	5.7	4.9	4.5	5.2	4.5	0.8	1.1	3.0	3.0	3.0	3.0	3.0
Consumer prices (percent change; end of period)	5.8	4.7	4.6	3.7	5.1	-0.8	3.0	3.0	3.0	3.0	3.0	3.0
Net international reserves (millions of U.S. dollars)	4,627	4,756	6,857	7,331	7,211	7,834	8,334	8,834	8,834	8,834	8,834	8,834

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

1/ Includes measures as in the baseline partial adjustment scenario, as well as administratively-determined measures to contain growth in the wage bill, and increases in the VAT rate from 2017.

2/ Data for 2012-15 reflect new nominal and real GDP data released by the authorities under new statistical standards and new base year 2012. The methodological changes resulted in an upward revision in nominal GDP of about 2½ percent in the base year, as a result mainly of a higher share of the rapidly growing services sector. Pending the release of the full new historical GDP series, nominal and real GDP prior to 2012 are staff estimates using new 2012 GDP data by component, and available past growth rates of components under the old standards.

3/ External current account deficit.

Table 10. Costa Rica: Banking Sector Indicators 1/

	2010 Dec	2011 Dec	2012 Dec	2013 Dec	2014 Dec	2015 Dec	2016 Jan
				(In percent)			
Capitalization							
Risk-adjusted capital ratio	17.3	17.3	16.8	16.6	16.7	16.2	16.2
Capital-to-assets ratio	14.8	15.0	14.8	14.5	14.1	14.1	14.2
Asset quality							
Nonperforming loans to total loans	1.8	1.7	1.7	1.7	1.5	1.6	1.7
Non-income generating assets to total assets	17.4	17.7	16.8	17.1	16.3	15.6	15.8
Foreclosed assets to total assets	0.8	0.8	1.0	1.0	1.0	0.9	0.9
Loan loss provisions to total loans	1.8	1.8	1.7	1.6	1.6	1.9	2.0
Management							
Administrative expenses to total assets	4.3	4.2	4.2	3.9	3.6	3.5	3.5
Noninterest expenses to gross income	85.0	76.5	67.4	68.1	77.7	67.6	67.4
Total expenses to total revenues	96.2	93.1	90.7	92.5	94.2	92.7	92.6
Profitability							
Return on assets (ROA)	1.2	1.3	1.5	1.2	1.2	1.0	1.0
Return on equity (ROE)	8.3	9.1	10.3	8.2	8.5	7.3	7.6
Interest margin to gross income	16.6	27.2	32.1	30.5	22.8	33.5	33.7
Liquidity							
Liquid assets to total short-term liabilities	90.1	85.1	92.6	101.2	98.7	97.8	98.5
Liquid assets to total assets	30.7	28.8	29.2	30.4	29.1	28.9	29.0
Loans to deposits	97.8	105.2	106.3	106.6	109.5	115.5	115.2
Liquid assets to deposits	43.8	42.7	44.0	47.0	45.1	46.6	46.8
Sensitivity to market risk							
Net open FX position to capital	18.8	18.8	19.1	17.8	17.4	19.9	19.9
Other							
Financial margin 1/	8.2	8.1	7.7	6.8	7.1	7.0	7.0

Source: Superintendency of Banks (SUGEF).
1/ Difference between implicit loan and deposit rates.

Annex I. Costa Rica: Financial System Assessment Program (FSAP) Main Pending Recommendations (2008)

Recommendations	Comments
A. Prudential Supervision and Regulation	
Amend the legal framework in order to provide protection for supervisors while performing their responsibilities in good faith.	Art. 28 of Insurance Law 8653 of August 7, 2008, provides legal protection to insurance supervisors. A draft bank resolution law contemplates protection for bank supervisors participating in the resolution process. A constitutional reform is necessary to establish legal protection for bank supervisors. CONASSIF has issued agreements to provide legal assistance to SUGEF senior personnel in case of judicial inquiries arising from the exercise of their functions.
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 their rapid implementation by the banking system.	The draft law that was submitted in the past has been archived by Congress. SUGEF is in the process of re-drafting a new reform bill. The strategic orientations of this bill have been defined in 2015.
Apply higher risk weight ratios to unhedged borrowers for capital adequacy purposes.	Amendment to capital adequacy regulation took effect in August 2013. This implemented gradual increases in the percentages over 18 months, to reach final levels of 125% for unhedged borrowers and 62.5% for those with residential mortgages by March 2015.[1] A normative reform that increases the generic provision for un-hedged borrowers from 0.5 to 1.5 percent is in process. Approval is expected by May 2016.
Modify the funding arrangements for supervision, in line with international best practices.	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.	With the IMF's help, SUGEF is in the process of drafting a new reform bill. The strategic orientations of this project have been defined in 2015.
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.	The authorities intend to amend the rating system once risk-based supervision is fully in place (currently expected in 2017, with major reforms to be conducted in 2015 and 2016).[1] SUGEF has been carrying pilot visits to various financial entities which will allow defining the focus of the rating system in the context of risk-based supervision.
Improve the early warning system, to allow the adoption of remedial actions in a timely manner.	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.	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. However,

Recommendations	Comments
	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.	SUGEF is working on a draft law with the assistance of the IMF's TA.
Amend the bank resolution legal framework to include purchase and assumption type techniques.	Improvements to the bank resolution framework are being developed as a complement to the deposit guarantee scheme.
Enable voluntary, extra-judicial corporate restructuring agreements.	Approval of the Law on Execution in October 2007 did not address the weaknesses of the current procedural rules.

1/ Staff's preliminary assessment based on updated information provided by the authorities.
Source: Superintendence of Financial Institutions.

Annex II. Costa Rica: Summary of Recommendations in the WHD Cluster Surveillance Report on Financial Integration in CAPDR

Micro-prudential Regulation	
Regulatory Perimeter	• Designate a Lead Supervisor in each country. • Adopt a broad definition of financial conglomerate and economic group. • Develop and periodically update a map of existing financial conglomerates. Empower supervisors to regulate holding corporations. • Agree on a common scope of supervision to minimize regulatory arbitrage.
Capital Adequacy	• Bridge existing different capital definitions across countries. • Adopt common definition of capital consistent with international best practice. • Harmonize the calculation of financial conglomerates' capital on a consolidated basis. • Adopt common loan classification criteria, at least applicable to regional entities.
Corporate Governance	• Regulate the organization structure of conglomerates to facilitate their supervision. • Reinforce legal authorities for the identification of ultimate ownership of financial conglomerates and economic groups. • Harmonize regulations on market entry and participation. • Establish minimum regional standards on risk management systems.
Credit Limits	• Adopt common thresholds on credit concentration and exposures to related parties. • Empower supervisors to inquire about ultimate owners' identities beyond financial corporations that are part of the financial conglomerates. • Grant sufficient legal protection to supervisors.
Macro-financial Regulation and Instruments	
Regional Supervision	• Implement a Regional Financial Stability Council with a broad mandate for regional financial stability, building from existing forums and Ministries of Finance. • Extend responsibility of supervising regional conglomerates to principal supervisors. • Harmonize financial data exchange in line with international accounting standards.
Macro-prudential Regulation	• Ensure full integration of systemic risk in the regulatory and supervisory frameworks. • Develop national and regional frameworks to identify SIFIs. • Calibrate micro-financial regulatory instruments to address macro-prudential risk. • Agree on a common set of macro-prudential instruments to be used to induce a reduction of systemic risk from financial conglomerates. • Reinforce regional macro-prudential surveillance, including by regional authorities.
Lender of Last Resort	• Adopt minimum country requirements on LOLR facilities. • Re-examine regulation for ring-fencing to ensure it addresses liquidity pressures transmitted across borders through financial conglomerates. • Develop macro-prudential metrics for liquidity in foreign exchange. • Reassess national frameworks on reserve requirements for foreign currency liabilities.
Remedial Actions and Resolution	• Extend legal regimes for corrective and remedial actions to non-bank financial institutions, and also specifically for SIFIs and financial conglomerates. • Adapt resolution frameworks to take into account regional implications.
Deposit Insurance	• Harmonize deposit insurance facilities. • Establish explicit coverage of deposits in off-shore banks with a specific regime.

Annex III. Costa Rica: Public Debt Sustainability Analysis (Higher Scrutiny Case)

The DSA highlights Costa Rica's unsustainable debt dynamics. The debt stock is projected to rise to 55 percent of GDP by 2021 under the baseline scenario, driven mostly by high fiscal deficits. There are substantial upside risks to the projected debt path from plausible macro shocks. Risks from relatively high financing needs are somewhat mitigated by the existence of a stable domestic investor base.

A. Key Assumptions

Debt definition. The public debt sustainability analysis focuses on the central government level where the worsening of the fiscal situation has taken place in recent years. The rest of the consolidated public sector has been broadly in balance in recent years as the cash surplus of the social security system broadly offset the small central bank deficit—resulting from its liquidity management operations—while public enterprises are broadly in balance.[1] The additional adjustment needed—about 1½ percent of GDP—to close the actuarial deficit that opens up over the medium and long-term is estimated separately.

Growth and fiscal policy assumptions. The baseline reflects the estimated growth potential of 4 percent. The baseline scenario also assumes fiscal adjustment of about 2¼ of GDP based on the staff's assessment of measures already submitted to Congress that have a higher probability of being approved. The improvement in the primary balance is smaller due to the projected deterioration in the fiscal position under a passive scenario, driven mostly by increases in expenditure on education to reach expenditure targets defined under the constitution.

Debt target. In theory it is difficult to justify a unique threshold for debt-to-GDP ratio as the government is deemed solvent if it can generate future primary surpluses sufficient to service its outstanding debt. Hence, protracted large budget deficits are not necessarily inconsistent with sustainability, provided that primary surpluses can be generated in the future. In practice, however, such an approach may require large future adjustments, which may not be feasible or desirable, economically and politically. A more operational definition of public debt sustainability offered in the 2003 WEO suggests that a given public debt level is sustainable if it implies that the government's budget constraint (in NPV terms) is satisfied without unrealistically large future corrections in the primary balance. It also emphasizes the importance of liquidity conditions, because even if a government satisfies its present value budget constraint, it may not have sufficient assets and financing available to meet or roll over its maturing liabilities. As practical guidance, empirical evidence indicates that, for emerging market economies, sustaining a debt-to-GDP ratio above 50 percent of GDP may be difficult. For example, the WEO (2003) finds that the median public debt-to-GDP ratio for emerging markets in the year before a default was about 50 percent of

[1] The basics output table for the DSA at the consolidated public sector level shows that the estimated sustainability gap in 2021 is lower than at the central government level, given lower actual and projected primary deficits and average interest rates at the consolidated level.

GDP. This study also concludes that, on average, the conduct of fiscal policy in emerging market economies is not consistent with ensuring sustainability once public debt exceeds a threshold of 50 percent of GDP. Therefore, targeting an upper bound to the public debt ratio below 50 percent of GDP or so appears justifiable in the case of Costa Rica.

B. Results and Assessment

Results. In the baseline, the headline deficit remains around 5½ percent of GDP in 2021, as the higher interest bill from rising public debt—which reaches 55 percent of GDP in 2021 and stays on an upward trajectory thereafter—largely offsets the improvement in the primary balance. The average gross financing needs would be almost 9 percent of GDP in 2016-21. In the adjustment scenario, additional measures of 1½ of GDP as part of a gradual but frontloaded consolidation plan suffice to stabilize debt by 2021 at a level below 50 percent of GDP. This outcome assumes tightening in credit spreads driven by favorable market reaction to a frontloaded adjustment plan with credible measures.

Assessment. While most standard indicators are not at "danger" levels (see heat-map), the debt and gross financing needs approach the benchmarks for medium-risk assessment under stressed scenarios, and the market perception indicators are approaching the high-risk assessment. In particular, debt rises above 65 percent of GDP under the combined macro-fiscal shock--compared to 70 percent benchmark for medium risk in the heat map—with particularly high sensitivity to growth and fiscal shocks. Debt profile indicators also highlight medium risks from relatively high spreads on external bonds, with spreads approaching the 600 basis point benchmark for upper risk assessment.

Mitigating factors. A stable investor base is an important mitigating factor. Notwithstanding the medium risk ratings for external and FX debt in the debt profile indicators heat map, the share of these types of debt are at the low end of the reference range for moderate risk countries—external and FX debt represent less than 25 and 35 percent of total debt, respectively, compared to benchmark ranges of 15 to 45 for external debt and 20 to 60 for FX debt. Moreover, about 60 percent of domestic debt is held by captive local institutional investors, including the social security system, nonfinancial public sector institutions, and banks.

Costa Rica: Central Government Debt Sustainability Analysis (DSA)—Baseline Scenario

(In percent of GDP unless otherwise indicated)

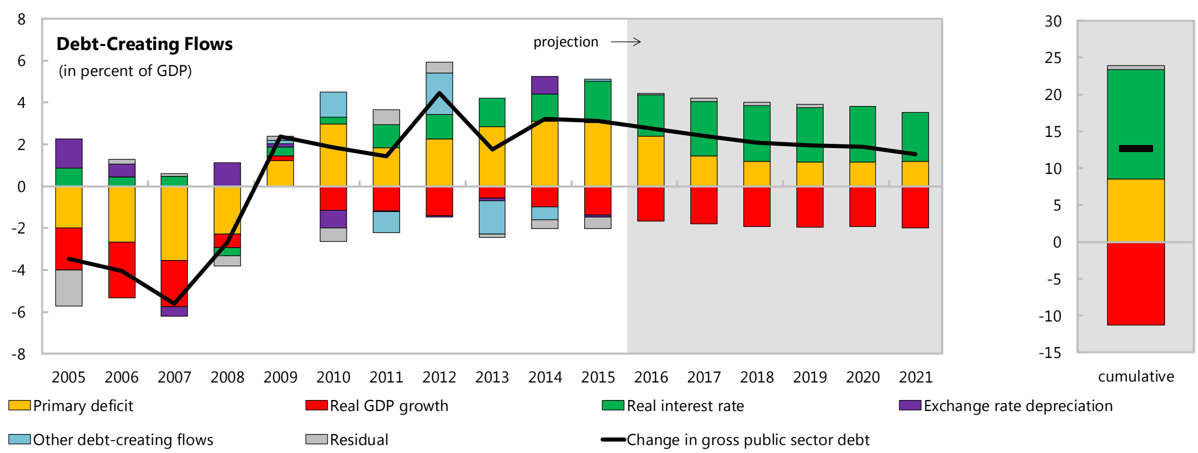
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2005-2013 [2/]	2014	2015	2016	2017	2018	2019	2020	2021
Nominal gross public debt	30.6	39.3	42.4	45.1	47.6	49.6	51.6	53.5	55.0
Public gross financing needs	12.5	10.3	9.4	9.5	9.6	9.0	8.0	8.2	7.4
Real GDP growth (in percent)	4.5	3.0	3.7	4.2	4.3	4.4	4.3	4.0	4.0
Inflation (GDP deflator, in percent)	8.0	4.7	2.2	3.4	3.2	3.5	3.7	3.4	3.3
Nominal GDP growth (in percent)	12.9	7.8	5.9	7.8	7.6	8.0	8.1	7.5	7.5
Effective interest rate (in percent) [4/]	10.7	8.7	7.5	8.6	9.5	9.7	9.5	9.0	8.2

As of March 29, 2016		
Sovereign Spreads		
EMBIG (bp) 3/		527
5Y CDS (bp)		527
Ratings	Foreign	Local
Moody's	Ba1	Ba1
S&Ps	BB-	BB-
Fitch	BB+	BB+

Contribution to Changes in Public Debt

	Actual			Projections							
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-0.4	3.2	3.1	2.8	2.4	2.1	2.0	1.9	1.5	12.7	
Identified debt-creating flows	-0.3	3.6	3.6	2.7	2.3	1.9	1.8	1.9	1.5	12.1	
Primary deficit	0.1	3.1	3.0	2.4	1.5	1.2	1.2	1.2	1.2	8.6	0.3
Primary (noninterest) revenue and grants	13.9	13.6	14.1	14.5	15.5	15.9	15.9	15.9	15.9	93.6	
Primary (noninterest) expenditure	14.0	16.7	17.2	16.9	17.0	17.1	17.1	17.1	17.1	102.1	
Automatic debt dynamics [5/]	-0.4	1.1	0.5	0.3	0.8	0.7	0.6	0.7	0.3	3.5	
Interest rate/growth differential [6/]	-0.6	0.3	0.6	0.3	0.8	0.7	0.6	0.7	0.3	3.5	
Of which: real interest rate	0.6	1.3	2.0	2.0	2.6	2.7	2.6	2.7	2.3	14.8	
Of which: real GDP growth	-1.3	-1.0	-1.4	-1.7	-1.8	-1.9	-2.0	-1.9	-2.0	-11.3	
Exchange rate depreciation [7/]	0.2	0.8	-0.1	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.1	-0.6	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (1) (e.g., drawdown of deposits) (negative)	0.1	-0.6	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2) (e.g., ESM and Euroarea loans)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	-0.1	-0.4	-0.5	0.1	0.2	0.2	0.2	0.0	0.0	0.6	



Source: Fund staff estimates and projections.

1/ Public sector is defined as central government.

2/ Based on available data.

3/ EMBIG.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

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

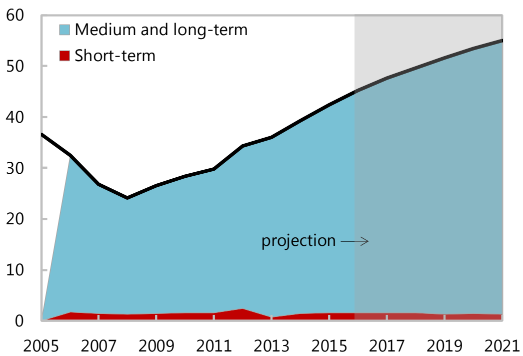
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

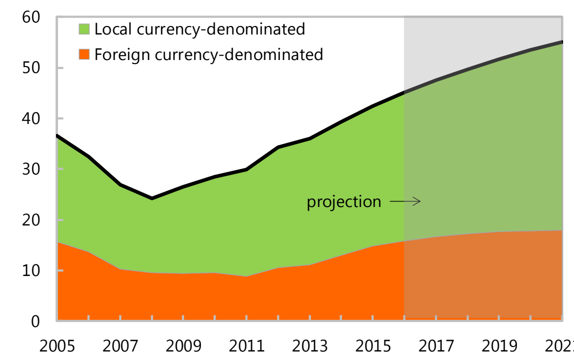
Costa Rica: Central Government DSA—Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



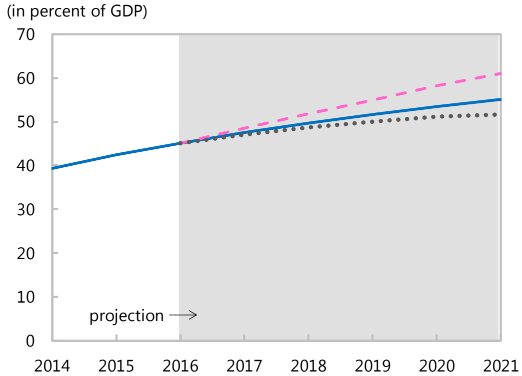
By Currency
(in percent of GDP)



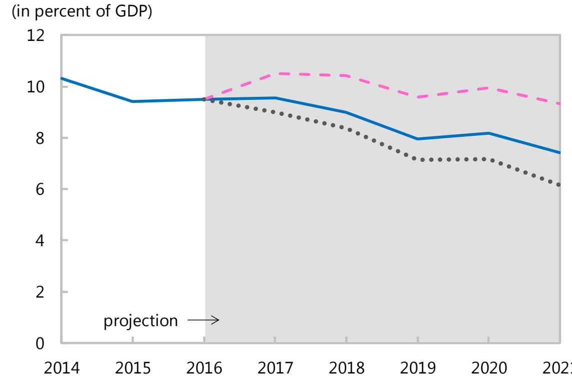
Alternative Scenarios

Baseline   Historical   Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

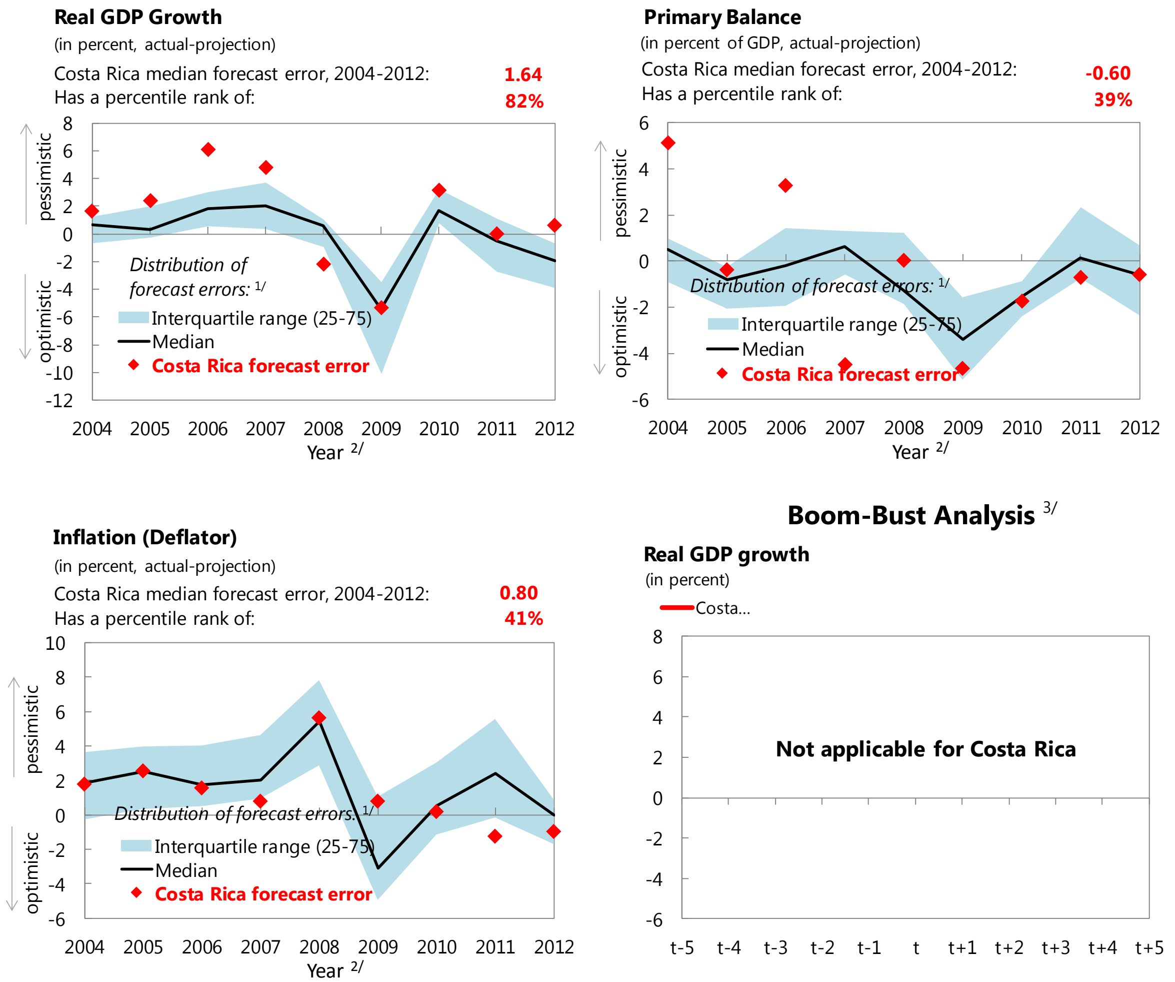
Baseline Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	4.2	4.3	4.4	4.3	4.0	4.0
Inflation	3.4	3.2	3.5	3.7	3.4	3.3
Primary Balance	-2.4	-1.5	-1.2	-1.2	-1.2	-1.2
Effective interest rate	8.6	9.5	9.7	9.5	9.0	8.2
Constant Primary Balance Scenario						
Real GDP growth	4.2	4.3	4.4	4.3	4.0	4.0
Inflation	3.4	3.2	3.5	3.7	3.4	3.3
Primary Balance	-2.4	-2.4	-2.4	-2.4	-2.4	-2.4
Effective interest rate	8.6	9.5	9.6	9.4	9.0	8.2

Historical Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	4.2	4.1	4.1	4.1	4.1	4.1
Inflation	3.4	3.2	3.5	3.7	3.4	3.3
Primary Balance	-2.4	-0.9	-0.9	-0.9	-0.9	-0.9
Effective interest rate	8.6	9.5	9.3	8.7	8.0	6.9

Source: Fund staff estimates and projections.

Costa Rica: Public DSA—Realism of Baseline Assumptions

Forecast Track Record, versus program countries



Source: Fund staff estimates and projections.

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

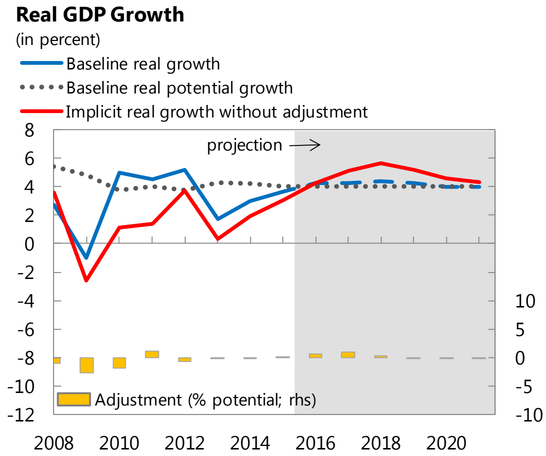
2/ Projections made in the spring WEO vintage of the preceding year

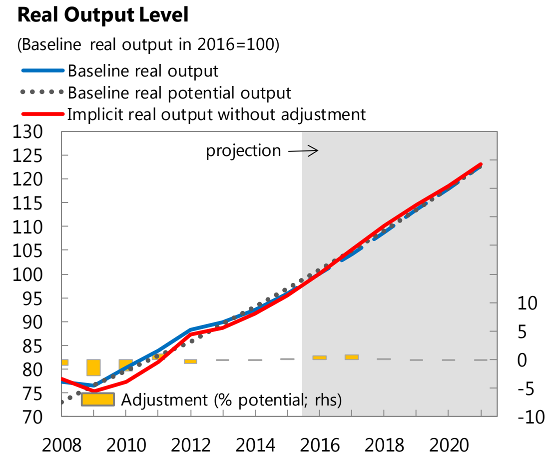
3/ Not applicable for Costa Rica, as it meets neither the positive output gap criterion nor the private credit growth criterion.

Costa Rica: Public DSA—Realism of Baseline Assumptions (concluded)

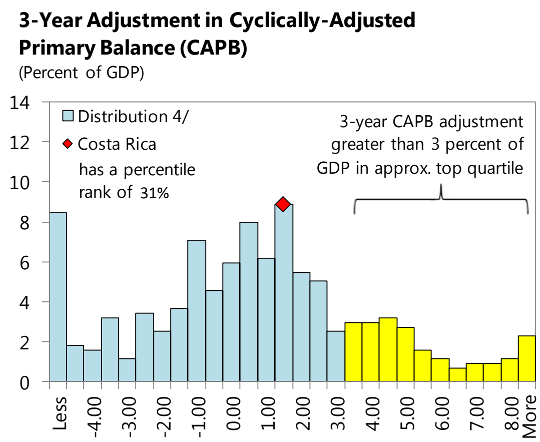
Growth and Level of Output in Absence of Fiscal Adjustment

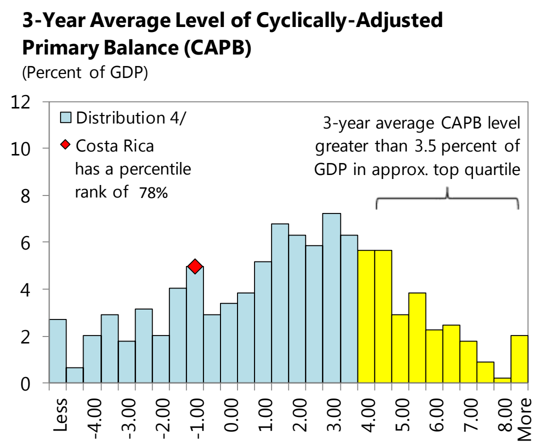
Assumed multiplier of 1, persistence of 0.6





Assessing the Realism of Projected Fiscal Adjustment





Source: Fund staff estimates and projections.

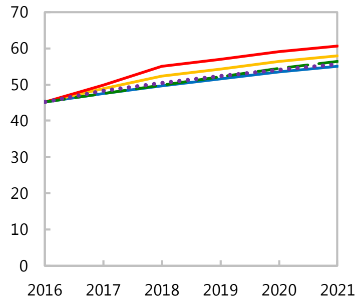
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Costa Rica: Central Government DSA—Stress Tests

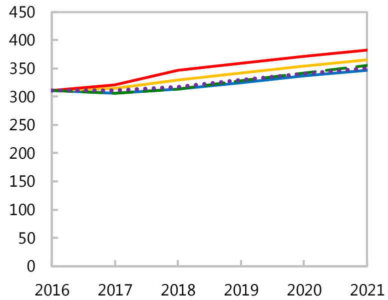
Macro-Fiscal Stress Tests

Baseline
Real GDP Growth Shock
Primary Balance Shock
Real Exchange Rate Shock
Real Interest Rate Shock

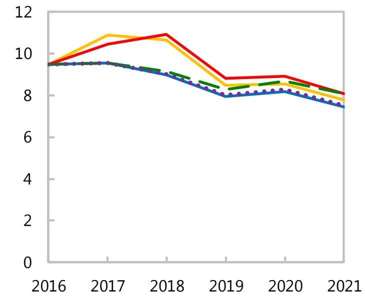
Gross Nominal Public Debt
(in percent of GDP)



Gross Nominal Public Debt
(in percent of Revenue)



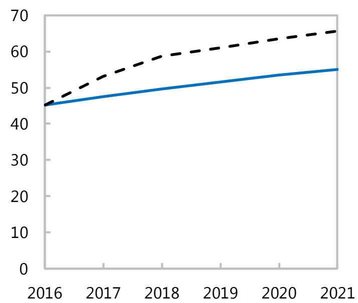
Public Gross Financing Needs
(in percent of GDP)



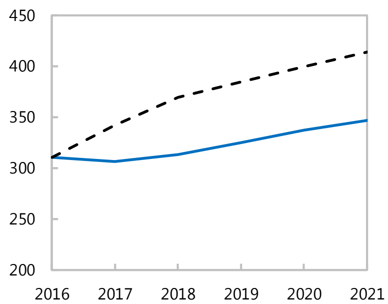
Additional Stress Tests

Baseline
Combined Macro-Fiscal Shock

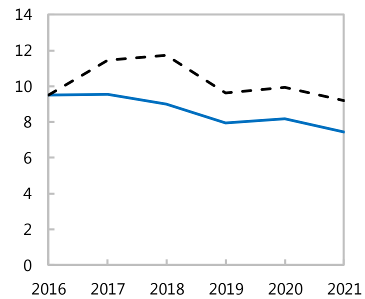
Gross Nominal Public Debt
(in percent of GDP)



Gross Nominal Public Debt
(in percent of Revenue)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions

(in percent)

Primary Balance Shock	2016	2017	2018	2019	2020	2021
Real GDP growth	4.2	4.3	4.4	4.3	4.0	4.0
Inflation	3.4	3.2	3.5	3.7	3.4	3.3
Primary balance	-2.4	-2.8	-2.5	-1.2	-1.2	-1.2
Effective interest rate	8.6	9.5	9.7	9.5	9.1	8.3
Real Interest Rate Shock						
Real GDP growth	4.2	4.3	4.4	4.3	4.0	4.0
Inflation	3.4	3.2	3.5	3.7	3.4	3.3
Primary balance	-2.4	-1.5	-1.2	-1.2	-1.2	-1.2
Effective interest rate	8.6	9.5	10.1	10.1	9.8	9.2
Combined Shock						
Real GDP growth	4.2	1.4	1.5	4.3	4.0	4.0
Inflation	3.4	2.5	2.8	3.7	3.4	3.3
Primary balance	-2.4	-2.8	-2.5	-1.2	-1.2	-1.2
Effective interest rate	8.6	9.9	9.9	10.0	9.8	9.2

Real GDP Growth Shock	2016	2017	2018	2019	2020	2021
Real GDP growth	4.2	1.4	1.5	4.3	4.0	4.0
Inflation	3.4	2.5	2.8	3.7	3.4	3.3
Primary balance	-2.4	-2.1	-2.4	-1.2	-1.2	-1.2
Effective interest rate	8.6	9.5	9.7	9.5	9.1	8.3
Real Exchange Rate Shock						
Real GDP growth	4.2	4.3	4.4	4.3	4.0	4.0
Inflation	3.4	7.0	3.5	3.7	3.4	3.3
Primary balance	-2.4	-1.5	-1.2	-1.2	-1.2	-1.2
Effective interest rate	8.6	9.9	9.6	9.4	9.0	8.2

Source: Fund staff estimates and projections.

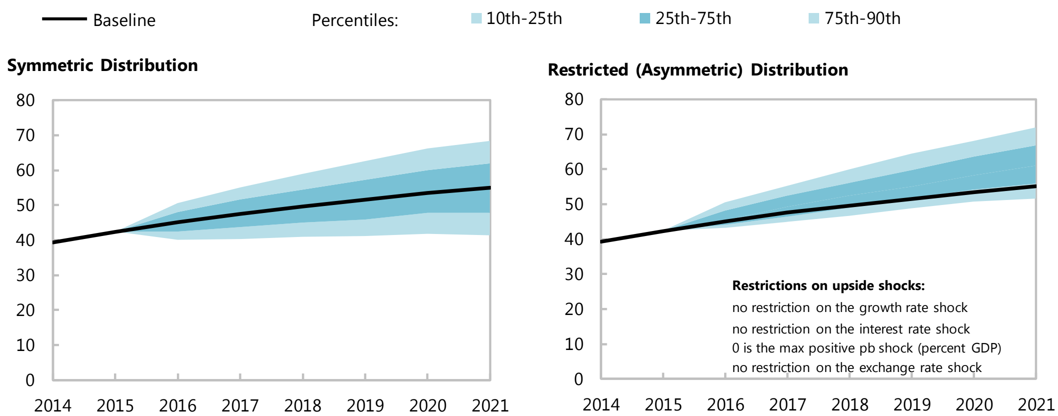
Costa Rica: Central Government DSA Risk Assessment

Heat Map

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

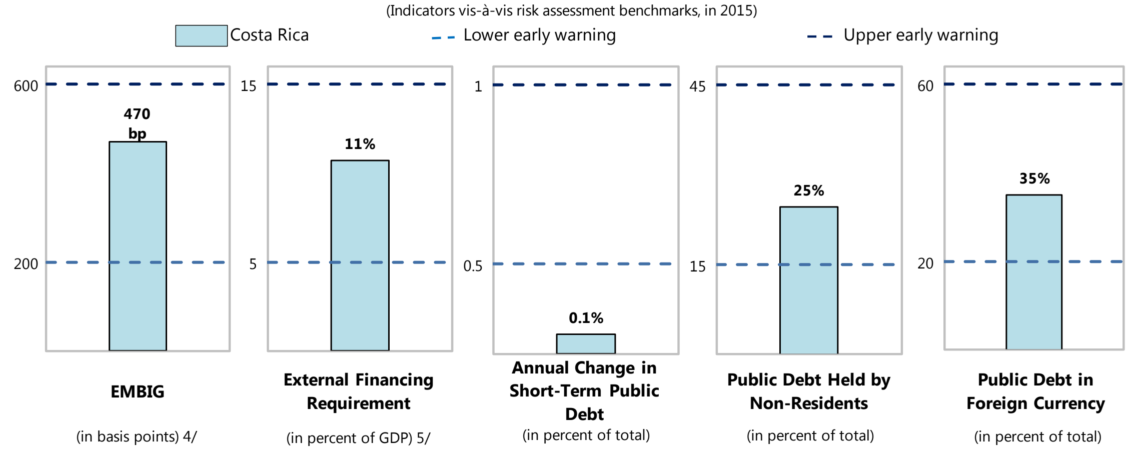
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2015)



Source: Fund staff estimates and projections.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

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

Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ EMBIG, an average over the last 3 months, 30-Dec-15 through 29-Mar-16.

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

Costa Rica: Consolidated Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

(In percent of GDP unless otherwise indicated)

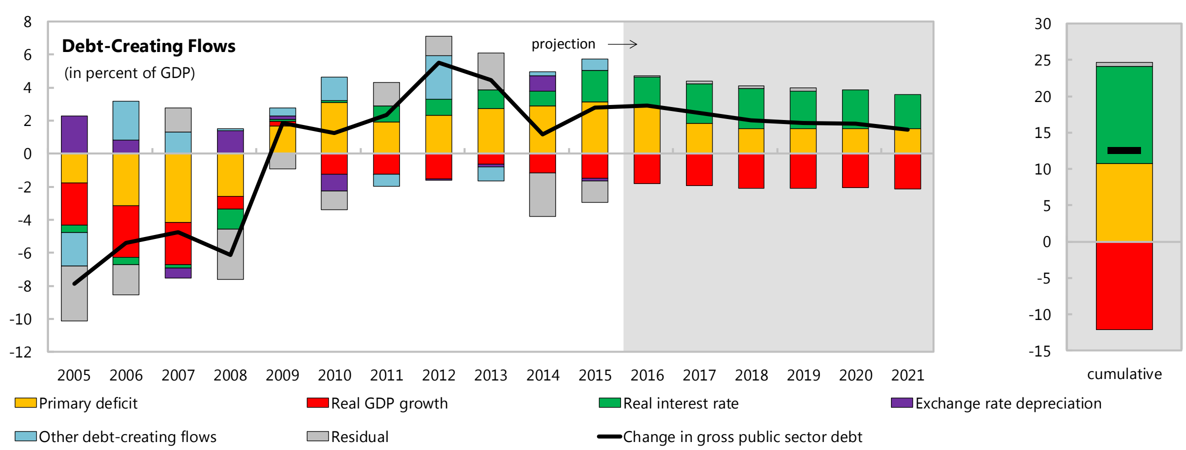
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2005-2013 [2/]	2014	2015	2016	2017	2018	2019	2020	2021
Nominal gross public debt	34.4	43.2	46.0	48.9	51.4	53.4	55.3	57.1	58.5
Public gross financing needs	5.0	10.0	10.1	10.0	9.9	9.3	8.2	8.4	7.6
Real GDP growth (in percent)	4.5	3.0	3.7	4.2	4.3	4.4	4.3	4.0	4.0
Inflation (GDP deflator, in percent)	8.0	4.7	2.2	3.4	3.2	3.5	3.7	3.4	3.3
Nominal GDP growth (in percent)	12.9	7.8	5.9	7.8	7.6	8.0	8.1	7.5	7.5
Effective interest rate (in percent) [4/]	8.8	7.1	6.9	7.8	8.5	8.7	8.5	8.1	7.4

As of March 29, 2016		
Sovereign Spreads		
EMBIG (bp) 3/		527
5Y CDS (bp)		527
Ratings	Foreign	Local
Moody's	Ba1	Ba1
S&Ps	BB-	BB-
Fitch	BB+	BB+

Contribution to Changes in Public Debt

	Actual			Projections							
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-1.0	1.2	2.8	2.9	2.5	2.0	1.9	1.8	1.5	12.6	
Identified debt-creating flows	-0.5	3.8	4.1	2.8	2.3	1.8	1.7	1.8	1.5	12.0	
Primary deficit	0.0	2.9	3.2	2.8	1.9	1.5	1.5	1.5	1.5	10.8	-0.1
Primary (noninterest) revenue and grants	22.1	22.5	23.1	23.3	24.3	24.6	24.6	24.6	24.6	146.1	
Primary (noninterest) expenditure	22.1	25.4	26.2	26.1	26.1	26.2	26.2	26.2	26.2	156.9	
Automatic debt dynamics [5/]	-1.1	0.7	0.3	0.0	0.4	0.3	0.2	0.3	-0.1	1.2	
Interest rate/growth differential [6/]	-1.4	-0.3	0.4	0.0	0.4	0.3	0.2	0.3	-0.1	1.2	
Of which: real interest rate	0.1	0.9	1.9	1.8	2.4	2.4	2.3	2.4	2.1	13.3	
Of which: real GDP growth	-1.5	-1.2	-1.5	-1.8	-1.9	-2.1	-2.1	-2.1	-2.1	-12.1	
Exchange rate depreciation [7/]	0.3	1.0	-0.1	...	...	...	...	...	...	...	
Other identified debt-creating flows	0.5	0.2	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (1) (e.g., drawdown of deposits) (negative)	0.5	0.2	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2) (e.g., ESM and Euroarea loans)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	-0.4	-2.6	-1.3	0.1	0.2	0.2	0.2	0.0	0.0	0.6	



Source: Fund staff estimates and projections.

1/ Public sector is defined as consolidated public sector.

2/ Based on available data.

3/ EMBIG.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

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

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Annex IV. Costa Rica: External Debt Sustainability Analysis

	Actual		Est.	Projections							
	2013	2014	2015	2016	2017	2018	2019	2020	2021		**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	35.6	38.8	38.4	**36.5**	**34.9**	**32.6**	**30.4**	**28.3**	**26.2**		**-4.8**
Change in external debt	3.7	3.2	-0.4	-1.9	-1.5	-2.4	-2.2	-2.1	-2.1	0.0	
Identified external debt-creating flows (4+8+9)	-2.4	0.3	-2.9	-3.2	-2.8	-2.8	-2.6	-2.5	-2.5	0.0	
Current account deficit, excluding interest payments	4.2	3.7	3.0	3.2	3.2	3.1	3.2	3.2	3.3	4.8	
Deficit in balance of goods and services	3.2	1.8	0.0	0.0	0.0	-0.1	0.0	0.0	0.0		
Exports	35.5	35.3	32.2	31.6	31.7	31.7	31.8	31.7	31.5		
Imports	38.7	37.2	32.2	31.7	31.7	31.7	31.8	31.7	31.5		
Net non-debt creating capital inflows (negative)	-5.4	-4.4	-4.5	-4.7	-4.7	-4.7	-4.8	-4.8	-4.8	-4.8	
Automatic debt dynamics 1/	-1.2	1.0	-1.4	-1.7	-1.3	-1.2	-1.0	-0.9	-0.9	0.0	
Contribution from nominal interest rate	0.8	1.0	1.0	1.0	1.0	1.1	1.1	1.1	1.1	1.0	
Contribution from real GDP growth	-0.5	-1.1	-1.3	-1.5	-1.5	-1.4	-1.3	-1.1	-1.1	-1.0	
Contribution from price and exchange rate changes 2/	-1.5	...	...	...	...	...	...	...	...		
Residual, incl. change in gross foreign assets (2-3) 3/	6.0	2.9	2.5	1.3	1.2	0.4	0.4	0.4	0.4	0.0	
External debt-to-exports ratio (in percent)	100.3	109.8	119.2	115.4	110.3	102.6	95.6	89.3	83.3		
Gross external financing need (in billions of US dollars) 4/	6.8	6.3	5.8	5.8	5.8	5.8	5.8	4.9	5.0		
in percent of GDP	13.8	12.6	10.9	10.2	9.5	9.0	8.4	6.6	6.3		
Scenario with key variables at their historical averages 5/				**34.9**	**32.4**	**29.4**	**26.5**	**23.8**	**21.3**		**-6.6**
Key Macroeconomic Assumptions Underlying Baseline										For debt stabilization	
Real GDP growth (in percent)	1.8	3.0	3.7	4.2	4.3	4.4	4.3	4.0	4.0	4.0	
GDP deflator in US dollars (change in percent)	4.9	-2.8	2.9	3.2	2.4	2.5	2.7	2.9	3.3	3.3	
Nominal external interest rate (in percent)	2.8	2.8	2.8	2.8	3.0	3.4	3.8	3.9	4.0	4.0	
Growth of exports (US dollar terms, in percent)	3.9	-0.5	-2.7	5.6	6.9	7.2	7.2	6.8	6.7		
Growth of imports (US dollar terms, in percent)	1.7	-4.0	-7.7	5.9	6.7	7.1	7.4	6.7	6.8		
Current account balance, excluding interest payments	-4.2	-3.7	-3.0	-3.2	-3.2	-3.1	-3.2	-3.2	-3.3		
Net non-debt creating capital inflows	5.4	4.4	4.5	4.7	4.7	4.7	4.8	4.8	4.8		

Source: National authorities and Fund staff estimates.

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.

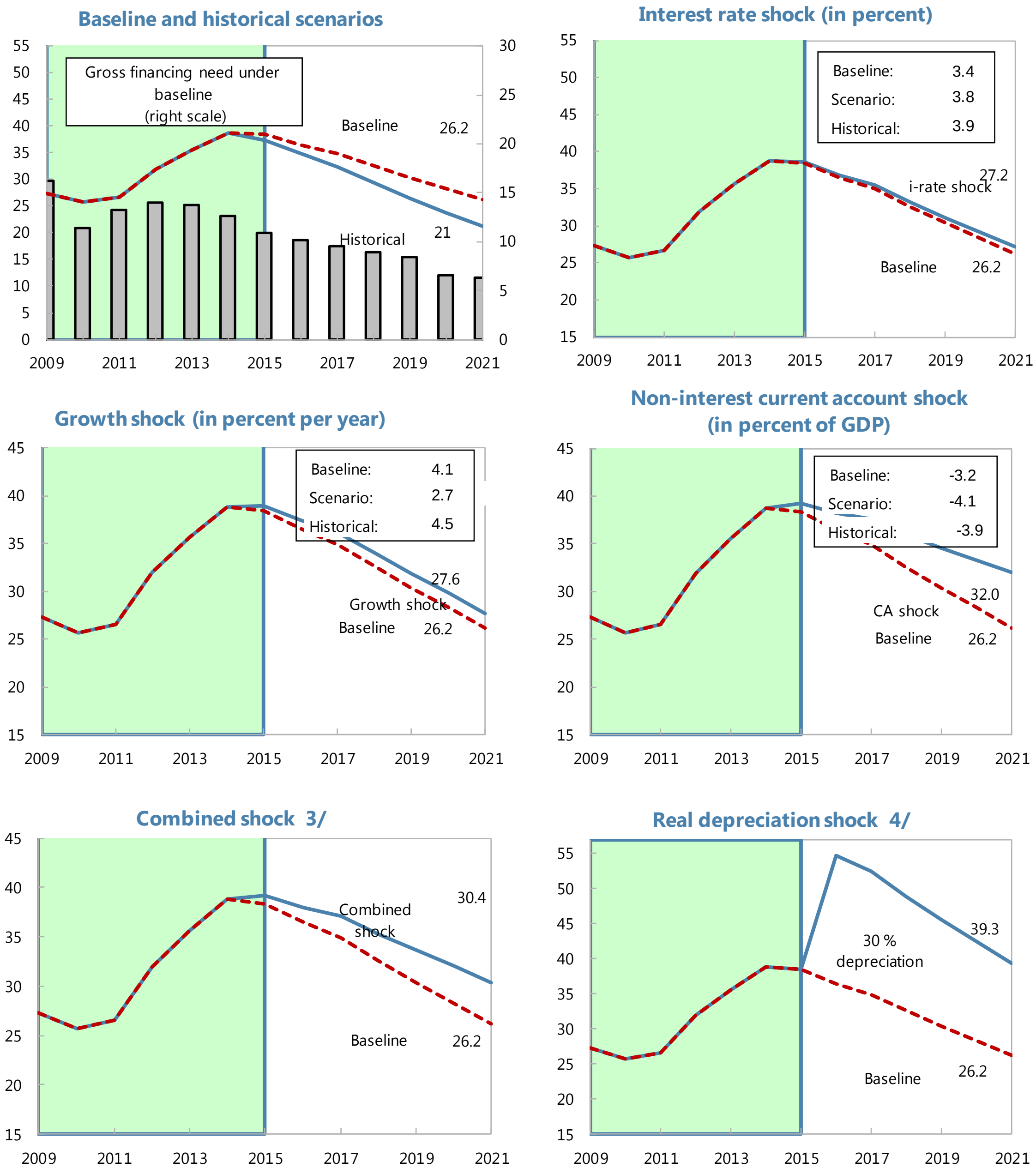
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

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.

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.

4/ One-time real depreciation of 30 percent occurs in 2016.

INTERNATIONAL MONETARY FUND

COSTA RICA

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

April 20, 2016

Prepared By: The Western Hemisphere Department

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FUND RELATIONS

(As of February 29, 2016)

Membership Status: Joined: January 8, 1946

General Resources Account:	**SDR Million**	**% Quota**
Quota	369.40	100.00
Fund holdings of currency	298.07	80.69
Reserve Tranche Position	71.34	19.31

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	156.53	100.00
Holdings	85.09	54.36

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**			
		2016	2017	2018	2019
Principal	0.00	0.00	0.00	0.00	0.00
Charges/Interest	0.00	0.03	0.05	0.05	0.05
Total	**0.00**	**0.03**	**0.05**	**0.05**	**0.05**

Exchange Rate Arrangement. Costa Rica's de jure current exchange rate arrangement classification is "managed float," (previously classified as a crawling band arrangement) while the de facto current exchange rate arrangement is classified as "stabilized." The former was established on February 2, 2015. The central bank committed to allow the exchange rate to be freely determined by foreign currency supply and demand, but reserved the right to participate in the market in order to meet its own foreign currency requirements and those of the nonbank public sector and, at its discretion, to prevent sharp fluctuations in the exchange rate. In 2015, the exchange rate deviated less than 1 percent from its mean value against the U.S. dollar, mostly because the Central Bank maintained significant active role in exchange rate management to avert excessive volatility in light of the large financial dollarization of the financial system. 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 January 31, 2015 (Country Report No. 15/29).

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	November 2014	Quarterly national accounts
Real Sector	January 2015	Source data – quarterly construction survey
	February 2015	Quarterly national accounts
	March 2015	Financial account – flow of funds table
	May 2015	Quarterly national accounts
	May 2015	National accounts – projections with I-O tables indices
	July 2015	National accounts – source data (survey and directories)
	August 2015	Quarterly national accounts
	August 2015	Annual national accounts (agriculture)
	December 2015	Quarterly national accounts
External Sector	February 2015	Balance of payments statistics and IIP
	March 2015	Topics of the financial account
	August 2015	Balance of payments statistics – external debt
	September 2015	Balance of payments and IIP statistics
MCM, CAPTAC-DR	November 2014	Macroeconomic analysis and projection
	November 2014	Capacity building of the division of financial stability
	January 2015	Building a model to analyze regional policy transmission mechanisms
	January 2015	Implementation of risk-based securities supervision
	March 2015	Improve operational framework of exchange rate policy
	March 2015	Minimum capital requirements for market risk
	April 2015	Implementation of risk-based securities supervision
	April 2015	Corporate governance
	April 2015	Capital market risk
	April 2015	Development model dynamic stochastic general equilibrium
	May 2015	Monetary and exchange rate policy
	July 2015	Capacity building of regional convergence analysis
	July 2015	Corporate governance follow-up
	August 2015	Bank supervision & regulations
	August 2015	Regulation of liquidity risk
	September 2015	Capacity building for financial stability analysis
	September 2015	Regulation and supervision of credit risk
	October 2015	Interest rates behavior and financial sector demand for medium-term government
	November 2015	Banking supervision
	November 2015	Regulation and supervision of credit risk
	January 2016	Accounting standardization
	January 2016	Improve capabilities for analyzing financial stability/stress testing
	February 2016	Macroprudential
	February 2016	Capacity building projection and macroeconomic analysis of BCCR
	March 2016	Strengthening capacities for macroeconomic analysis-Central American
	March 2016	Regulation and supervision of credit risk
	March 2016	Corporate governance – review of draft rules and laws

FAD, CAPTAC-DR	November 2014 January 2015 February 2015 February 2015 February 2015 April 2015 April 2015 June 2015 June 2015 August 2015 August 2015 October 2015 October 2015 November 2015 February 2016 March 2016 March 2016	Customs administration Tax Administration Tax Administration Public financial management Customs administration Customs administration Tax administration Paper "Grado de madurez" Customs administration Custom administration Strengthening the integral IVA credit Management indicators Customs administration Improvement of mass audit implementation Customs administration Information crossed Matrix risk construction
LEG	September 2014 November 2014 December 2014 March 2015 May 2015 July 2015 September 2015	Formulate a National AML/CFT Strategy Formulate a National AML/CFT Strategy Formulate a National AML/CFT Strategy Formulate a National AML/CFT Strategy Formulate a National AML/CFT Strategy Formulate a National AML/CFT Strategy Deposit Insurance Scheme and Banking Resolution

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

PAST FUND STAFF RECOMMENDATIONS AND IMPLEMENTATION

2014 Article IV Staff Recommendation	Implementation
Fiscal Policy	
• Fiscal adjustment of 3¾ percent of GDP is needed to stabilize the debt-to-GDP ratio over the medium term below levels which are shown to pose risks for macro stability in emerging markets. In the longer-term, parametric adjustments would also be needed to remedy the actuarial imbalance of the pension system. • Start fiscal adjustment in 2015 as a first critical step to reduce the sustainability gap, while also mitigating risks of higher inflation, widening external imbalances and possible adverse financial market reactions.	• In 2015, the new administration that came into power in mid-2014 presented tax and expenditure reform proposals to Congress that could yield about 2¾ percent of GDP, although none of the measures have yet obtained Congressional approval. The administration has also identified administratively-determined expenditure cuts that would yield the additional 1 percent of GDP needed to fully close the sustainability gap. The authorities have also started to take measures to remedy the actuarial imbalance of the pensions system, including the elimination of the early retirement option, and are considering raising minimum contributions and gradually raising contribution rates over the medium term. • The new administration has maintained a broadly

	unchanged non-interest deficit, with efforts to restrain spending and reduce tax evasion preventing a budgeted deterioration in the primary balance of more than ½ percent of GDP in 2014-15.
Monetary and Foreign Exchange Policy	
• Stand ready to raise rates if inflation does not decline to the target range once pass-through from exchange rate depreciation in the first half of 2014 is completed. • Allow more XR flexibility to help establish inflation as the undisputed monetary anchor, as well as to discourage dollarization. Take advantage of current absence of pressures on the exchange rate to abandon the XR band. Continued FX intervention to reduce volatility and strengthen the NIR position can be warranted as long as inflation target is not jeopardized. Improve transparency of the FX-intervention-rule.	• Inflation declined sharply to -1¼ percent toward the end of 2015, from almost 6 percent a year earlier, driven by low oil prices. The authorities reacted by adopting an appropriately accommodative stance with policy rate cuts of 350 basis points to 1¾ percent. The central bank took advantage of the fall in inflation to lower the target range to 2-4 percent, in line with average inflation of trading partners. • The authorities removed the XR band in early 2015 in line with Fund advice, while maintaining their FX intervention policy, including an undisclosed rule to dampen volatility and a general policy of preventing excessive deviations from fundamentals. • A lower current account deficit from lower oil prices, continued Eurobond issuance, resilient FDI, and increase net foreign bank liabilities resulted in strong reserve accumulation during 2015, in line with the authorities' FX purchase program, while the exchange rate remained stable.
Financial Sector	
• Implementation of the 2008 FSAP recommendations should be accelerated. • The authorities should strive to introduce risk-based supervision and improve supervision of cross-border financial operations. Existing capital quality should be firmed up and liquidity and capital requirements increased in line with Basel III standards. • Reduce vulnerabilities stemming from currency mismatches in the private sector and high bank net foreign liabilities.	• Progress on introducing FSAP recommendations has been mixed. Critical legislation to enhance consolidated supervision and strengthen bank resolution remains to be approved. • Measures have been enacted to move towards full implementation of risk-based supervision. Basel III Liquidity Coverage Ratio was introduced in 2015. • Capital risk-weightings on FX loans to unhedged borrowers have been increased, and reserve requirements were extended to medium- and long-term foreign bank borrowing (in addition to the existing requirement on short-term foreign borrowing). Additional measures are currently under consideration, including: (i) stricter provisioning on FX loans to unhedged borrowers and household debt with income-to-debt service ratios above 30 percent; (ii) counter-cyclical provisioning; and (iii) higher risk-weightings for household mortgages with high loan-to-value and income-to-debt service ratios.

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

1. **The IMF's Costa Rica team led by Mr. Figliuoli (mission chief) has met on various occasions with the World Bank's Costa Rica team led by Mr. Calvo-Gonzalez (lead economist and PREM sector leader)** to discuss macroeconomic challenges, identify macro-critical 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. **Based on the shared assessment of macroeconomic challenges, the teams identified four structural reform areas as macro-critical:**

- *Fiscal consolidation.* The fiscal consolidation strategy should comprise both revenue and expenditure components, with a slant towards revenue enhancement. The adjustment plan laid out by the authorities is appropriate, but full implementation is critical. Key elements include raising revenues through fiscal reforms already submitted to Congress that adequately focus on broadening the base for the VAT, increasing VAT rates and marginal income tax rates on high earners, with an additional sizeable contribution from mostly administratively-determined measures aimed at gradually reducing expenditures as a share of GDP.

- *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.

- *Productivity.* 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 maintain Costa Rica's growth of knowledge-intensive exports. 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), though these will require vigilance to avoid undue contingent liabilities.

4. **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 seek opportunities to 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. The authorities have requested an FSAP update for next fiscal year.

- Productivity. 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), a catastrophe draw down deferred option (approved in March 2009) and a health operation (approved in March 2016). The government has also requested technical assistance from IFC Advisory services to improve the investment climate.

5. **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. Timing: when milestones are reached (and at least semi-annually).

6. **The table below lists the teams' separate and joint work programs for 2015.**

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	Good Practices in Development Finance Fiscal Management in Central America AAA (P151829)	May 2016	Completed (final delivery March 2016) Final delivery December 2016
IMF Work Program	Staff visit Regional Conference Technical assistance: National Accounts and Price Statistics Monetary and FX Operations Banking Supervision and Regulation Fiscal Revenue and Expenditure Management	November, 2016 November, 2016 2016	November, 2016 November, 2016

7. **The attached table summarizes the financial relations between Costa Rica and the World Bank (in million U.S. dollars).**

Table 2. Costa Rica and the World Bank: Financial Relations

Project Name	Total loan	Undisbursed through FY16	Projected disbursements in FY17
Higher Education Improvement Project	200	171.5	10
Catastrophe Deferred Draw Down Option	65	31	0
Strengthening Universal Health Insurance	420	420	0

RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

1. **Recent activities**. The IBD´s loan portfolio in Costa Rica has 11 sovereign guaranteed operations in execution and two programs pending ratification, with an approved amount of US$ 2.046,18 million. The available amount for disbursements is US$ 1.312,15 million (64% of the approved), and is concentrated in the areas of Transportation (44,5%), Energy (34,2%), Education (8,2%) and Reform and Modernization of the State (6,5 %). The average age of the operations is 2.1 years. Disbursements of sovereign guaranteed operations during 2016 are expected to reach around US$146,9 million, concentrated in the areas of Transportation (27.4%), Energy (26,2%) and Reform and Modernization of the State (23,8%).

2. **Future plans**. During 2016, the IDB expects to implement the 2015-2018 Country Strategy for Costa Rica, focused on the areas of Infrastructure and Logistics, Innovation and Competitiveness, Energy, Education and Public Finances. In 2016 the IDB expects to approve two Sovereign Guarantee loans for a total amount of US$140 million on Integrated urban consolidation and the Cantonal road network.

Loan Disbursements (Sovereign Guaranteed Operations)

(In millions of U.S. dollars)

	2009	2010	2011	2012	2013	2014	2015	2016*
Disbursements	40,6	55,7	121,0	86,9	131,3	209.9	173.4	146.9
Amortization	45.1	44.6	46.6	44.7	36.2	31.9	38.5	55.1
Interest and charges	11.8	11.4	10.3	9.3	9.6	10.2	12.8	19.7
Net cash flow	-18.2	-0.3	62	31.0	84	165.7	120.4	70.2

* Projections (February 2016)

Lending Program for 2016 (tentative)

(In millions of U.S. dollars)

Projects	Amount
Integrated Urban Consolidation - Bonos Comunales	50
Cantonal Road Network Program	90
Total	140

Sovereign Guaranteed Operations (as of February 29, 2015)
(In millions of U.S. dollars)

	Approved	Disbursed	Obligated	Available
Loans in execution	**2.046,2**	**734,0**	**146.90**	**1.312,15**
Sustainable Development of the Binational Watershed Rio Sixaola	9,22	9,22	0,0	0,0
Tourism Program in Protected Areas	19,0	11,36	7.64	7,64
First Electric Power Sector Development Program 2008-2011	250,0	232,54	17.46	17,46
First Road Infrastructure Program	300,0	286,67	13.32	13,32
Cantonal Road Network Program	60,0	25,86	15.00	34,14
Water and Sanitation Program	73,0	5,07	6.23	67,93
Violence Prevention and Social Inclusion Promotion Program	132,4	41,93	35.00	90,51
Innovation and Human Capital for Competitiveness Program	35,0	9,01	8.50	25,99
Power Sector Development Program 2012–16 (Reventazon Hydroelectric Project)	250,0	97,23	21.00	152,77
Education Infrastructure Construction and Equipment Program	167,52	15,13	10.75	152,39
Infrastructure Transport Program	450	0,0	12.00	450
Border Integration Program of Costa Rica*	100	0,0	0,0	100
First Renewable Energy, Transmission and Distribution of Electricity Program*	200	0,0	0,0	200
Nonreimbursable Technical Cooperations	**19,6**	**9,7**	**0,0**	**9,9**
Total	**2065,78**	**743,72**	**146,9**	**1322.05**

*Pending ratification

STATISTICAL ISSUES

(As of April, 2016)

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 2008 (SNA 2008). The Central Bank disseminated the annual national accounts data for the years 2012-2015, with 2012 as the new base year of the system. The full transition including release of the rebased historical data is scheduled for completion by September 2016. Estimation of real estate housing including owner-occupied housing has been improved: the housing stock of the base year (2012) has been estimated at the most detailed level according to the 2011 Census, at national, provincial, canton and district level. To calculate subsequent years, the rental item of the CPI is used as the price indicator, and the volume is extrapolated from the statistics of houses built with residential purposes obtained from the construction industry. Accounting depreciation is used instead of estimating consumption of fixed capital. In the new system, double deflation method is applied to obtain annual value added in constant prices; whereas single extrapolation is used for quarterly volume estimates using output volume indicators. Appropriate price indices are used to derive current value estimates. Changes in inventories are obtained following the 2008 SNA recommendations for those products for which enough information is available. This includes the most important agricultural and livestock products. The proportional Denton method is applied for benchmarking quarterly national accounts series to their annual counterpart. The informal activity of households as producers of goods and services is included in GDP level (but not separately estimated) thanks to the elaboration of employment and remuneration matrices.

Price statistics: The compilation of the consumer price index (CPI) employs concepts and definitions from the last international CPI manual. Its structure, scope, and coverage have been recently updated. The CPI weights are based on the 2012/2013 Income and Expenditure Survey, and the index covers the national urban and mixed households, which comprise approximately 73 percent of the total population and 82 percent of the total consumption expenditures of Costa Rica. Atypical movements in the data are investigated and corrected when necessary.

The PPI is compiled based on concepts and definitions from the 1993 SNA and the international PPI Manual, and is calculated both by product and economic activity (manufacture and services activities). The base year of the PPI for domestic manufacture, transportation, tourism services and professional services is 2012, whereas PPI for electricity and sales hydrocarbons, and the export and import price index (that is not yet available) are calculated following a moving-base approach.

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. 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. Annual data for the *GFS Yearbook* are reported on a regular basis, most recently for 2014. 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 and Financial Statistics: Central Bank of Costa Rica (CBCR) reports the Standardized Report Forms (SRFs) 1SR for CBCR, 2SR for the other depository corporations (ODCs), and 5SR for monetary aggregates for publication in the IMF's *International Financial Statistics (IFS)* on a monthly basis with a lag of two months. The reported monetary statistics are broadly in line with the methodology of the *Monetary and Financial Statistics Manual* (*MFSM*). The classification of financial instruments and economic sectors follows the *MFSM* with some exceptions. Accrued interest is not classified together with underlying instruments, as recommended the *MFSM*. The CBCR is working for expanding the coverage of the monetary statistics including short term funds as ODCs and investment funds and pension funds as other financial corporations.

Financial sector surveillance: Costa Rica reports all core financial soundness indicators (FSIs) and one of the 13 encouraged FSIs for deposit takers on a monthly basis for posting on the IMF's FSI website with less than one quarter lag. The authorities are planning to expand the reported FSIs of the encouraged set for deposit takers.

External sector statistics: The Central Bank of Costa Rica (BCCR) compiles and disseminates quarterly balance of payments and international investment position (IIP) statistics, which are produced on a sixth edition of the Balance of Payments and International Investment Position Manual (BPM6) basis. Source data are generally adequate and derived from sound collection programs and work is still ongoing to improve the coverage of financial transactions of the nonfinancial private sector (such as those related to trade credit and advances), and remuneration of employees. Transfer prices in some cases are not converted to market prices.

The BCCR also monthly compiles and disseminates the Data Template on International Reserves and Foreign Currency Liquidity, reports semi-annual data to the Coordinated Portfolio Investment Survey (CPIS) and annual data to the Coordinated Direct Investment Survey (CDIS), and submits quarterly external debt statistics to the Quarterly External Debt Statistics (QEDS) database.

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 March 24, 2016)

	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	Mar 16	Mar 16	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Mar 16	Mar 16	D	D	D		
Reserve/Base Money	Feb 16	Feb 16	D	D	D	O, LO, LO, LO	O, O, O, LO, O
Broad Money	Feb 16	Feb 16	M	M	M		
Central Bank Balance Sheet	Feb 16	Feb 16	M	M	M		
Consolidated Balance Sheet of the Banking System	Feb 16	Feb 16	M	M	M		
Interest Rates[2]	Mar 16	Mar 16	D	D	D		
Consumer Price Index	Feb 16	Mar 16	M	M	M	O, LO, O, O	LO, O, LO, LO,O
Revenue, Expenditure, Balance, and Composition of Financing[3]– Central Government	Dec 15	Feb 15	M	M	M	LO, LNO, LO, LO	LO, O, O, LO, O
Stocks of Central Government and Central Government-Guaranteed Debt[4]	Dec 15	Feb 15	M	M	M		
External Current Account Balance	Sep 15	Jan 16	Q	Q	Q	O, LO, O, LO	LO, O, LO, O, LNO
Exports and Imports of Goods and Services	Sep 15	Jan 16	Q	Q	Q		
GDP/GNP	Sep 15	Jan 16	Q	Q	Q	O, LO, LNO, O	LO, O, LNO, O, LO
Gross External Debt	Sep 15	Jan 16	Q	Q	Q		
International Investment Position	Sep 15	Jan 16	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, 2012, 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 6, 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.

Statement by Mr. Jimenez Latorre, Executive Director for Costa Rica and Mr. Pacheco, Senior Advisor to the Executive Director
May 16, 2016

The Costa Rican authorities appreciate the constructive and transparent dialogue with staff and broadly concur with its assessment and key recommendations.

Economic outlook

Costa Rica has continued growing at an accelerating rate during the last three years. As a small open economy, the country is exposed to a variety of shocks such as commodity prices volatility, international financial conditions and main trade partners' growth, besides its high exposure to natural disasters. Thanks to an increasingly diverse economy, adverse weather conditions for main agricultural exports were compensated by dynamic export of services and lower import commodity prices, especially oil during 2015. Exports supply has widen, medical devices—the main export product— continued to perform strongly while services grew 8.4 percent in 2015 reaching all-time records driven by tourism, IT, information, medical and other business services. FDI also grew in 2015 and is expected to continue financing a sustainable current account deficit. The central bank's growth projection for 2016 rose to 4.3 percent after closing at 3.7 percent in 2015. The combined effect from improved external demand, stability in main macro variables and lower interest rates have contributed to accelerate the rate of growth which raised to 5.4 percent y-o-y as of February 2016.[1]

Overall, the economy is expected to continue growing above 4 percent in the medium term in the midst of a fiscal consolidation process and propelled by a loose monetary policy stance, if price pressures do not arise. Even though some risks in the financial sector have build up, the sector remains sound and resilient and the authorities have put in place a number of measures and stand ready to take further actions to keep strengthening the financial system and maintaining it in a growth-friendly development stage.

[1] Measured by the monthly index of economic activity (IMAE).

Fiscal Policy

The government has put in place many administrative measures and a technological revamp to improve tax management. The start up of a new virtual tax administration system eased significantly the administrative cost for taxpayers and digitalized all relevant information to tighten controls. A special strategy to closely monitor large taxpayers was put in place which, combined with other efforts, has helped increase the number of income tax files by 21 percent and income tax revenue by 14.3 percent during 2015. Consequently, the revenue effort climbed to 13.7 percent of GDP in 2015 from 13.2 percent in 2014.

On the spending side, the government has continued working to reduce the growth rate of the wage bill and other current outlays. Latest figures show that the Q1 2016 wage bill grew 3.4 percent compared to the same period last year, while the average growth rate on the first quarter of the last four years was 9.9 percent. In the same vein, purchases of goods and services decreased 28 percent during the first quarter compared to the same period last year. Even though it is too early in the year for conclusions, the government is showing its commitment to hold up current expenditure. In fact, salary increases during the last semesters have been almost negligible for professional central government servants.

With regard to fiscal reform, the government has sent to congress a comprehensive package of law initiatives,[2] nine law proposals, to address both the revenue and the expenditure sides of the balance. The broad part of the adjustment is expected to come from the reform to VAT and income tax which were submitted to Congress last year. In the current VAT setup, services—the most dynamic sector of the economy—are exempted. Thus, the proposal amends these leaks while regressivity concerns have been tackled by exonerating the population below the last 4 deciles of the income distribution. The Anti-smuggling law was approved by congress as expected and it is already under execution.

In the case of the Anti-tax evasion initiative,[3] its approval has taken longer than expected because the government managed to include the foundation of a business ownership registry, including information of final beneficiaries. This goes in line with OECD, G-20 and G-5 recent initiatives to allow for future automatic exchange of information. In the meantime, the corporate tax law is advancing properly in congress; its final approval is expected soon.

On May 1, 2016 a coalition of parties that control congress directorate agreed on promoting a fiscal reform agenda tilted to the expenditure side. They are proposing to approve a comprehensive set of expenditure measures before approving VAT and income tax reforms. Since many of the coalition measures were already contemplated in the government package (see footnote 2), the authorities have taken this as an opportunity to speed up fiscal reform and negotiations are currently underway.

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[2] The package presented by the government is composed by the following law proposals: reforms to the VAT and income tax, anti-evasion, anti-smuggling (already approved), corporate tax, reforms to improve the treasury single account, reform to improve public servants evaluation, reforms to control pensions paid out of the budget and the fiscal rule (to be sent in the next days).

[3] This law proposal is intended to strengthen tax controls and enforce collection.

Monetary Policy, Exchange Rate Policy and Financial Sector

The central bank has continued working on strengthening its monetary policy framework in order to have inflation as the undisputable anchor, including the successfully surrender of the XR band in early 2015. Also, it has succeeded in anchoring inflation expectations, allowing the recent revision of the inflation target range to 2-4 percent (from 3-5 percent), in line with average inflation of main trading partners.

So far three particular characteristics of the economy have shaped the current FX intervention rule aiming at countering deviations from medium-term fundamentals as well as from excessive volatility. First, the high level of dollarization is making the bank more vigilant of financial sector vulnerabilities. Second, the FX market lags competition since it is dominated by few large players. Finally, since the inception of the new XR regime, the FX market has been largely on surplus which would have induced even larger real exchange rate appreciation in the short run.[4] The staff has seen merit on this explanation and the central bank is working on a new set of rules that would increase competition and deepen the FX market. More XR flexibility and communication on the intervention policy would flow as these measures are put in place.

The authorities concur with staff that the dollar-denominated credit has been growing faster than desirable and, as recognized in the report, they have come up with a series of measures to address this common concern. They already increased capital risk-weightings for dollar denominated credit to unhedged borrowers and set up a 15 percent reserve requirement to medium- and long-term new foreign bank borrowing (this requirement on short-term foreign borrowing was already in place). However, the authorities' efforts have not stopped there. They are also working on a new proposal to further increase capital provisions for dollar denominated credit and preparing a law proposal to allow increases above 15 percent to the reserve requirements on FX bank borrowing. The authorities are determined to end up this trend and do not rule out additional measures, if required.

Structural Reforms

The authorities recognize the importance of improving the business climate and competitiveness overall. Last year relevant reforms were approved on access to credit, easiness to pay taxes and access to electricity, which allowed the country to gain 21 positions in the 2016 World Bank Doing Business report.[5]

[4] Even though REER has appreciated recently, as confirmed by staff, there is no evidence that it has deviated from fundamentals so far.

[5] The main reforms were: a new secured transaction law that broadens the kind of assets that could be used as collateral on financial transactions, the implementation of an electronic filing system for income and sales taxes and the reduction of the time that takes a business to get electricity.

In order to address infrastructure gaps, large projects are under execution and many more are in the pipeline thanks to a wide variety of financing sources. The construction of a mega-port in the Caribbean coast awarded to the Dutch based, APM Terminals,[6] advances as programmed and is expected to be operational in 2018. A new highway—in the north part of the Inter-American highway, key for trade and tourism—is almost ready and will come into operation next month. Major projects to revamp the capital beltway are currently under execution with some sections projected to open this year. Other key routes, including connections to the new port, will begin major overhauling next year using already secured funding from China, multilaterals and a novel figure through bank trusts.[7]

Costa Rica's environmental friendly policies are deeply entrenched in the population. Electricity generation is an example where 97 percent was produced from renewable sources during 2016 first quarter, following the same pattern of 2015. Most of them, 65 percent, came from hydroelectric power plants, while 16 percent from wind, 14 percent from geothermal and two percent from biomass. Solar energy represents a fraction but its participation would probably increase. The system delivers a high quality service and network coverage is very high compared to regional standards. In line with its ambitious environmental goals a wastewater treatment plant, financed through Japan's cooperation agency, was inaugurated last year which would duplicate the percentage of treated water in the short-run and, as the sewerage network is developed, it would initially take the water treated percentage up to 27 percent of the population.

The authorities are committed to further strengthening the policy mix to preserve macroeconomic and financial stability as these are key to maintain Costa Rica's strong structural features such as high income per capita, social development and governance indicators, which are also supporting the process to become an OECD member.

[6] APM Terminals is an independent business unit within the Danish-based Maersk Group.

[7] There is one project using this financial model already approved by congress. Predefine future tolls would be securitized to finance the road construction.