DOCUMENT OF INTERNATIONAL MONETARY FUND
AND NOT FOR PUBLIC USE

FOR AGENDA

EBS/83/127
Supplement 1

CONFIDENTIAL

July 13, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Costa Rica - Staff Report for the 1983 Article IV Consultation and Review Under the Stand-By Arrangement

The attached supplement to the staff report for the 1983 Article IV consultation with Costa Rica and review under the stand-by arrangement has been prepared on the basis of additional information. Revised proposed decisions appear on pages 3 and 4.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Bonangelino, ext. 74328.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

COSTA RICA

Staff Report for the 1983 Article IV Consultation and Review Under the Stand-By Arrangement--Latest Developments

Prepared by the Western Hemisphere Department

(In consultation with the Exchange and Trade Relations and Legal Departments)

Approved by Joaquin Ferran and Manuel Guitian

July 13, 1983

The Costa Rican authorities have recently informed the staff of various new measures adopted in the areas of exchange rate, fiscal, and monetary policies, which are summarized below.

1. Exchange rate policy

Since the end of June 1983, the spread between the banking and the free market exchange rates has been reduced from 9 per cent to less than 5 per cent. The narrowing of this spread, which is in accordance with the stand-by program's exchange rate unification guidelines, was the result of a 2 per cent decline in the free market exchange rate and a 2 per cent upward adjustment of the banking rate by the Central Bank. The banking exchange rate is at present ₡ 41 per U.S. dollar (buying) while the free market exchange rate is ₡ 43.10 per U.S. dollar (buying).

In addition, effective June 28, 1983, the surrender requirement of export proceeds at the banking exchange rate was reduced from 99 per cent to 98 per cent, and 1 per cent of export proceeds were permitted to be sold at the free market. As indicated in the staff report (EBS/83/127), 1 per cent of the export proceeds is surrendered at the official exchange rate of ₡ 20 per U.S. dollar. The Costa Rican authorities may in the future make further shifts of transactions from the banking market to the free market with the view to promoting the unification of the exchange rates, which is an objective of the program.

A revised proposed decision reflecting the above change in the exchange system is attached.

2. Fiscal policy

a. Import surcharge

On June 28, 1983 the existing temporary surcharge on imports from outside Central America and Panama, the payment of which is made at the free market exchange rate, was raised by 2-1/2 percentage points to a level of 3-1/2 per cent. This measure was adopted for fiscal reasons and it is estimated to yield about ₡ 100 million this year.

b. Tariffs of public enterprises

Electricity rates and oil prices have been reduced in the last two months. The electricity rates charged by the Costa Rican Electricity Institute (ICE) were rolled back on June 15, 1983 to their December 1982 level. Previously, ICE had revoked the last phased increase of 13 per cent in electricity rates which had become effective in April 1983 (EBS/83/127). These government actions represent a reversal of cumulative increases in electricity rates of 59 per cent and involve a total revenue loss for ICE during 1983 of about ₡ 550 million. In addition, in early June the domestic prices of most oil derivatives, other than gasoline, sold by RECOPE were reduced to reflect part of this year's drop in the import price of crude. This adjustment of oil prices, which was mentioned as a possibility in the staff report (EBS/83/127), represents a weighted average reduction of about 3-1/2 per cent. The revenue loss to RECOPE is estimated at about ₡ 300 million in 1983. The authorities have informed the staff that efforts will be made to compensate for the revenue losses from the described measures through adjustment in expenditures.

3. Monetary policy

In a move to strengthen monetary control and to stimulate the growth of long-term time deposits with the banking system, the Monetary Board of the Central Bank decided to increase the reserve requirements on shorter-term deposits. Effective June 28, 1983, the legal reserve requirement on term deposits of less than 30 days was increased from 27 per cent to 32 per cent, and on term deposits of 30 days to less than 180 days was increased from 10 per cent to 40 per cent. Legal reserve requirements on term deposits of 180 days and over remained unchanged at 10 per cent, but now are to be met in the form of cash or deposits at the Central Bank instead of with bonds.

Proposed Decisions

The following revised decisions are proposed for adoption by the Executive Board:

A. 1983 Consultation

1. The Fund takes this decision relating to Costa Rica's exchange measures subject to Article VIII, Sections 2 and 3, in light of the 1983 Article IV consultation with Costa Rica conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance Over Exchange Rate Policies).

2. Costa Rica maintains multiple currency practices and restrictions on payments and transfers for current international transactions described in EBS/82/213, EBS/83/127, and EBS/83/127, Supplement 1. In light of the continuing implementation by Costa Rica of policies for balance of payments adjustment, which are supported by a stand-by arrangement, the Fund grants approval for the retention of these multiple currency practices and restrictions until the termination of the stand-by arrangement on December 19, 1983.

B. Review Under the Stand-By Arrangement

1. The Fund and Costa Rica have concluded the review pursuant to paragraph 4(c) of the stand-by arrangement for Costa Rica (EBS/82/214, Supplement 1).

2. Subparagraph 4 (d)(ii) of the stand-by arrangement shall read: "introduces any new multiple currency practices, or modifies the existing multiple currency practice other than as described in paragraph 13 of the attached letter and in EBS/83/127, Supplement 1; or"

3. The Fund finds that no further understandings are necessary.