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August 9, 1983

To: Members of the Executive Board

From: The Acting Secretary

Subject: Costa Rica - Use of Fund Resources - Compensatory Financing Facility

Attached for consideration by the Executive Directors is a paper on a request expected to be received from Costa Rica for a purchase equivalent to SDR 18.6 million under the compensatory financing facility. A draft decision appears on page 14.

This subject will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Kaibni, ext. 74162.

Att: (1)

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INTERNATIONAL MONETARY FUND

COSTA RICA

Use of Fund Resources--Compensatory Financing Facility

Prepared by the Research Department and the Western Hemisphere Department

(In consultation with the Exchange and Trade Relations, Legal, and Treasurer's Departments)

Approved by Wm. C. Hood and Eduardo Wiesner

August 8, 1983

The Managing Director has been informed that the Costa Rican authorities will shortly request a purchase of SDR 18.6 million (30 percent of quota) under the compensatory financing decision. The request is being made with respect to a shortfall in merchandise exports for the 12 months ended February 1983. Costa Rica has made two previous purchases under the compensatory financing decision: SDR 20.5 million in October 1979 and SDR 30.1 million in June 1981. If approved, the member's new purchase would raise outstanding purchases under the decision from 70 percent of quota to 100 percent of the present quota, and the total outstanding purchases by Costa Rica from 213 percent to 243 percent of quota. A waiver of the limitation of Article V, Section 3(b)(iii) of the Fund's Articles of Agreement would be required and is being proposed.

This paper, which is being circulated in advance of the formal request from Costa Rica, is presented in five sections and an annex. The sections deal with: (1) the balance of payments position and cooperation with the Fund; (2) estimation of the export shortfall; (3) causes of the shortfall and export prospects; (4) repurchase; and (5) staff appraisal and proposed decision. The relations of Costa Rica with the Fund are summarized in the annex.

1. Balance of payments position and cooperation with the Fund

a. Balance of payments position

In recent years, Costa Rica has been experiencing serious balance of payments difficulties. Following several years of surplus, the overall balance of payments swung into deficit in 1978 and the deficit rose sharply in each of the following four years (Table 1). Over the period 1978-82, the cumulative overall balance of payments deficit amounted to SDR 1.13 billion.

Table 1. Costa Rica: Balance of Payments, 1978-83

(In millions of SDRs)

	1978	1979	1980	1981	1982	Proj. 1983
A. Current account	-290.0	-432.4	-509.9	-361.7	-218.3	-261.5
Trade balance	-241.3	-352.0	-404.0	-178.7	14.9	--
Exports, f.o.b.	(690.0)	(729.2)	(768.7)	(850.4)	(793.8)	(831.8)
Imports, c.i.f.	(-931.3)	(-1,081.2)	(-1,173.1)	(-1,029.1)	(-778.9)	(-831.8)
Net services	-62.0	-89.8	-116.6	-205.9	-263.9	-303.1
Net transfers	13.3	9.4	11.1	22.9	30.7	41.6
B. Capital account (net)	258.2	368.6	159.9	-32.9	-73.3	261.5
Private capital 1/	77.5	28.2	-138.8	-54.5	-14.2	23.1
Official capital 2/	180.7	340.4	298.7	21.6	-59.1	238.4
C. Overall balance (A+B)	-31.8	-63.8	-350.0	-394.6	-291.6	--
D. Arrears (net)	--	--	217.4	304.3	417.8	-54.5 3/
E. Changes in net official reserves of the Central Bank (increase -)	31.8	63.8	132.6	90.3	-126.2	54.5
Memorandum items:						
Gross official reserves of the Central Bank (year-end)						
Outstanding amount	166.8	119.1	175.3	124.6	238.3	347.0 4/
Equivalent months of imports	2.1	1.3	1.8	1.5	3.7	5.0 4/
Current account balance in percent of GDP	-10.3	-13.9	-14.4	-11.7	-9.6	-9.7

Sources: Central Bank of Costa Rica; and staff estimates.
1/ Includes net errors and omissions.
2/ Includes SDR allocation and gold revaluation.
3/ Includes a reduction of arrears (-) equivalent to SDR 1,000 million and new financing (-) of SDR 946 million, involving rescheduling of debt, conversion of CDs, and a trade credit facility.
4/ As of end-June 1983.

As of December 31, 1982, net international reserves amounted to negative SDR 1.09 billion, including SDR 1 billion in payments arrears. Gross official reserves amounted to SDR 238 million as of that date, or the equivalent of 3 1/2 months of 1982 imports. However, much of these reserves were held in the form of illiquid assets.

The current account deficit in percent of GDP, which rose from 10 1/2 percent in 1978 to a peak of 14 1/2 percent in 1980, declined sharply to 10 percent in 1982. This improvement, however, was due largely to the foreign exchange crisis and the consequent sharp decline in imports. Although exports also declined, imports fell more rapidly, and the trade balance in 1982 registered a small surplus. This surplus, however, was offset by sharply increasing interest payments. The capital account, which began to deteriorate in 1980, recorded a net outflow in 1981 and 1982, reflecting both private and official capital movements. Debt service payments, which were suspended in August 1981 because of an acute foreign exchange shortage, were partially resumed in July 1982, and negotiations for the rescheduling of external public debt were reopened.

In 1983, equilibrium in the overall balance is projected, mainly on the strength of a marked improvement in the capital account. The current account deficit is expected to deteriorate somewhat in nominal terms, but to remain virtually unchanged from 1982 in terms of GDP. Exports are projected to increase moderately largely because of higher prices of bananas and sugar and a larger volume of fresh meat exports. Imports should also rise moderately, reflecting the improved foreign exchange situation. The services account will continue to deteriorate as a result of larger interest payments on external debt. The capital account is expected to register a net inflow of about SDR 260 million, owing largely to increased official loans from the United States, a reflow of private capital, and debt relief resulting from rescheduling of external debt. A rescheduling agreement with Costa Rica's bilateral official creditors was signed in January 1983 under the aegis of the Paris Club, and an agreement with foreign commercial banks is expected to be finalized shortly. 1/ Gross official reserves as of June 30, 1983 amounted to SDR 347 million, equivalent to five months of projected 1983 imports; however, a large portion of the reserves continued to be held in the form of illiquid assets. Net international reserves, taking into account payment arrears, were negative to the extent of 16 months of imports.

b. Cooperation with the Fund

The proposed purchase would raise Costa Rica's outstanding CF purchases to 100 percent of quota, and, consequently, the Fund must be satisfied that Costa Rica has been cooperating with the Fund in an effort to find, where required, appropriate solutions to its balance of payments difficulties.

1/ For a detailed description of the rescheduling agreements, see SM/83/150 (7/5/83), p. 61.

Costa Rica's external position has encountered a series of difficulties in the past several years. In an effort to overcome these difficulties, Costa Rica entered into a one-year stand-by arrangement with the Fund in December 1982 (EBS/82/214, 11/29/82). Costa Rica has complied with all the performance criteria under the current stand-by arrangement and has made three drawings as scheduled under the program. The Article IV consultation and the mid-term review of the stand-by arrangement were completed by the Executive Board on July 18, 1983 (EBS/83/127, 6/20/83, and SM/83/150, 7/5/83). Costa Rica maintains multiple currency practices consisting of a multiple exchange rate system, mixing rates, and the imposition of an exchange tax on exports; it also has exchange restrictions arising from external payments arrears. The Fund granted approval for the retention of these practices and restrictions until December 19, 1983 (EBM/83/104, 7/18/83). At present, a Fund resident representative is stationed in San Jose, and a fiscal advisor has been assisting the Costa Rican authorities in the formulation of the public sector budgets. The staff is satisfied that the requirement of cooperation relating to the proposed purchase is met.

2. Estimation of the export shortfall

The authorities of Costa Rica have requested that the 12 months ended February 1983 be treated as the shortfall year. Final data have been provided for the first eight months, and the staff, in collaboration with the authorities, has estimated exports for the final four months (November 1982-February 1983). 1/

After averaging SDR 791 million a year during the two pre-shortfall years, the value of exports in the shortfall year ended February 1983 is estimated to have declined to SDR 764 million--3 percent below the average of the two pre-shortfall years. Earnings are projected to recover gradually, averaging SDR 812 million per year in the two post-shortfall years--6 percent higher than in the shortfall year. On the basis of these movements, the export shortfall is estimated at SDR 30.2 million, which is 60 percent larger than the amount of the proposed purchase of SDR 18.6 million (Table 2).

1/ These estimates are largely based on detailed export data for the four months described by the authorities as preliminary export data. Export earnings in the first eight months of the shortfall year averaged SDR 63 million compared with SDR 72 million in the corresponding months of the previous year. In the remaining four months, earnings are estimated to have averaged SDR 65 million, compared with SDR 67 million in the corresponding months of the previous year.

Table 2. Costa Rica: Calculation of the Export Shortfall

(In millions of SDRs)

	Years Ending February			Projected 1/	
	1981	1982	1983 2/	1984	1985
Total exports	740.9	844.3	763.6	806.7	817.8
Shortfall			30.2		
Proposed purchase			18.6		

1/ Based on judgmental forecast of earnings given in Table 3.
2/ Data for final four months (November 1981-February 1982) are preliminary.

3. Causes of the shortfall and export prospects

The estimated shortfall of SDR 30 million reflects to a large extent the difficulties Costa Rica faced in export markets for its manufactured goods, particularly as a result of the low level of economic activity in the Central American Common Market; manufactured exports registered a shortfall of SDR 14 million. Shortfalls are also estimated for fresh meat (SDR 13 million), sugar (SDR 6 million), and "other" agricultural and food products (SDR 5 million). The shortfall in fresh meat largely resulted from marketing difficulties in the United States; the shortfall in sugar from low international prices; and the shortfall in "other" products from weak external demand. The two largest individual commodity components of export earnings--bananas and coffee, registered excesses: SDR 2 million for bananas and SDR 12 million for coffee (Tables 3 and 4).

a. Agricultural and food products

Despite increases in earnings from both coffee and bananas, the value of agricultural and food exports fell by 3 percent in the shortfall year because of lower earnings from fresh meat, sugar, and "other" agricultural exports. This reduction followed an increase in the previous year of over 13 percent. For the two post-shortfall years, increases at 7 percent per annum are projected on average for agricultural and food exports. The largest increases are projected for bananas, fresh meat, and sugar.

(1) Coffee

Costa Rica is an important producer of mild arabica coffee. Except for the shortfall year and for 1975, when earnings from banana exports were greater, coffee has been the largest single source of export

Table 3. Costa Rica: Export Earnings and Shortfalls by Major Commodities

	Years Ending February								Shortfall	
	1978	1979	1980	1981	1982	1983	1984	1985	Geometric	Arithmetic
					(In millions of SDRs)					
Total exports	717.0	680.4	744.7	740.9	844.3	763.6	806.7	817.8	30.2	31.1
Agricultural and food products	517.2	497.7	538.3	475.3	538.4	521.8	574.5	576.3	14.1	15.5
Coffee	290.9	238.8	255.5	171.1	204.5	212.9	205.7	215.2	-11.7	-11.0
Bananas	130.3	134.8	150.9	162.7	197.9	216.1	263.1	244.2	-2.3	0.7
Fresh meat	36.7	54.6	66.7	50.1	64.3	38.1	48.0	57.0	12.6	13.4
Sugar	14.8	12.6	14.9	37.8	25.4	17.8	20.8	21.2	5.9	6.8
Other 1/	44.5	56.9	50.3	53.6	46.3	36.9	36.9	38.7	5.1	5.6
Manufactured goods	199.8	182.7	206.4	265.6	305.9	241.8	232.2	241.5	14.3	15.6
				(Percentage change)						
Total exports		-5	9	-1	14	-10	6	1		
Agricultural and food products		-4	8	-12	13	-3	10	--		
Coffee		-18	7	-33	20	4	-3	5		
Bananas		3	12	8	22	9	22	7		
Fresh meat		49	22	-25	28	-41	26	19		
Sugar		-15	18	154	-33	-30	17	2		
Other 1/		28	-12	7	-14	-20	0	5		
Manufactured goods		-9	13	29	15	-21	-4	4		

1/ Adjusted to exclude re-exports.

Table 4. Costa Rica: Value, Volume, and *Unit Value Indices by Major Commodities*

(1983=100; in terms of SDRs)

	Value Share in Total Exports in 1983 (In percent)	Years Ending February 1978	1979	1980	1981	1982	1983	1984	1985	Shortfall in Percent of Level in Shortfall Year
Value	63.5	98	91	101	87	102	100	111	111	1.8
Coffee	27.9	137	112	120	80	96	100	97	101	-5.5 (excess)
Bananas	28.3	60	62	70	75	92	100	122	113	-1.0 (excess)
Fresh meat	5.0	96	143	175	131	169	100	126	150	33.1
Sugar	2.3	83	71	84	212	143	100	117	119	33.4
Volume		96	108	109	91	107	100	102	103	0.5
Coffee		74	94	102	73	98	100	100	100	-6.5 (excess)
Bananas		103	105	105	98	103	100	101	101	0.6
Fresh meat		167	196	171	132	188	100	120	130	31.1
Sugar		125	116	110	137	101	100	89	89	1.9
Unit value		101	84	92	95	95	100	109	108	1.2
Coffee		184	119	118	111	98	100	97	101	1.3
Bananas		58	59	67	77	89	100	120	111	-1.8 (excess)
Fresh meat		58	73	102	99	90	100	105	115	1.5
Sugar		67	61	76	155	141	100	131	134	30.9

earnings for Costa Rica since the early 1950s. The contribution of coffee to export earnings was particularly large in the late 1970s, when high world prices prevailed.

As an exporting member of the 1976 International Coffee Agreement, Costa Rica became subject to export quotas introduced under the Agreement in October 1980. The large coffee crop in 1980/81 (October/September) provided exportable production considerably in excess of the quota assigned to Costa Rica for exports to importing members of the Agreement, and large stocks were accumulated by Costa Rica. With the small harvest in 1981/82, an "off" year in the two-year coffee production cycle, and with sizable sales to nonquota markets at prices much lower than those for sales to quota markets, stocks were reduced. For the 1982/83 coffee year, a record crop of 138 thousand tons has been estimated, and even with sizable sales to nonquota markets, stocks are expected to increase from 17 thousand to nearly 50 thousand tons by the end of the quota year (October/September). In the shortfall year ended February 1983, exports to quota markets were 69 thousand tons and exports to nonquota markets were 28 thousand tons, the latter at prices roughly one half those obtained in quota markets. Earnings were 4 percent above the previous year, attributable to a 2 percent increase in volume and an increase of 2 percent in unit values.

Although the production of coffee in the 1983/84 coffee year is expected to be lower than in 1982/83 at around 125 thousand tons because 1983/84 is an "off" year in the production cycle, the carryover from the 1982/83 crop will provide sufficient supplies to maintain exports at the level of the shortfall year. Production in the following year is expected again to be high. Consequently, the volume of exports will be constrained by quotas and by the demand situation in nonquota markets. The volume of exports is projected in both post-shortfall years to equal that in the shortfall year, with the same distribution between quota and nonquota markets. Export unit values are projected to fall by 3 percent in the first post-shortfall year, but to increase by 4 percent in the second. These projections are based on the downward movements of the world prices of "other mild" coffees in recent months and on the expectation that the prices of "other mild" coffees will recover gradually, so that the price differential between "other mild" and robusta coffees, which has become very narrow in recent months, would return to a traditional level. An excess of SDR 12 million is calculated for coffee on the basis of these projections.

(2) Bananas

Bananas, usually the second largest single source of export earnings for Costa Rica, provided the largest earnings in the shortfall year, over 28 percent of the total. The volume of banana exports by Costa Rica has been relatively stable at about 1 million tons in recent years, and increases in earnings have resulted mainly from price increases. Earnings in the shortfall year were 9 percent above those in the previous year, with the volume of exports showing a decrease of 3 percent and unit values an increase of 12 percent. Extensive storm damage in a number of producing countries contributed to an increase in international prices in the latter part of the shortfall year.

Production and export volumes in the two post-shortfall years are projected to be similar to those in recent years. World market prices of bananas during March-July 1983 have been more than one third higher than the average for the shortfall year because of the effects of continuing supply difficulties in Central and South America. On the expectation that prices will settle at a level somewhat lower than the prices in recent months, an increase of 20 percent is projected for export unit values of bananas during the first post-shortfall year, to be followed by a decrease of 8 percent during the second; the projected decline in prices is based on the assumption that more normal supply conditions will prevail. An excess of SDR 2 million is calculated for bananas.

(3) Fresh meat

Fresh meat, mostly beef, is exported almost entirely to the United States. Earnings from these exports have varied considerably from year to year because of the beef production cycle in Costa Rica and changes in market conditions in the United States. Earnings tended to increase throughout the 1970s, with a sharp rise in calendar year 1979 on the occasion of an increase by 35 percent in beef prices in the United States. In 1980/81, earnings fell by 25 percent, chiefly because of a decline in the volume of exports, which was in part related to the occurrence of a low point in the beef production cycle and in part to a weakening competitive position in export markets. In the following year earnings increased by 28 percent, despite a decline of 9 percent in export unit values. The major currency devaluation during the course of that year provided incentives to exporters, resulting in an exceptionally large increase of 42 percent in export volume.

In the shortfall year, earnings fell by 41 percent. The volume of exports declined by 47 percent, but the effect of this decline was partly offset by an increase in unit values of 11 percent. The sharp decline in export volume from 35 thousand tons to 19 thousand tons was primarily due to difficulties encountered in the U.S. market. As a result of a quality control problem, certain meat packing plants in Costa Rica were "delisted" by the U.S. authorities, and this action effectively placed an embargo on imports from Costa Rica. Subsequently, the Costa Rican authorities and the United States Department of Agriculture agreed on sanitation and labeling procedures to correct the problem, limiting adverse effects on exports. This problem coincided with large shipments of meat from Australia to the United States, following a severe drought in Australia which necessitated a reduction in livestock numbers; these shipments led to lower prices in July and August 1982, which created difficulties for other exporters in the U.S. market. A subsequent agreement on voluntary quotas between the United States and its major suppliers enabled some recovery of prices in September.

In the post-shortfall years, improved demand conditions in the U.S. market are expected to have a favorable impact on the beef export earnings of Costa Rica. The expansion of economic activity is expected to increase demand for beef, and, barring drought or other factors leading to unusually large slaughterings in major exporting countries, export unit values are projected to increase by 5 percent in the first post-shortfall year and 10 percent in the second. The resulting unit values would still be below the record annual average attained in 1979. The sanitary and labeling arrangements reached between Costa Rica and the United States should help Costa Rica increase the volume of exports. An increase of 20 percent in the volume of exports is projected for the first post-shortfall year and an increase of 8 percent for the second. On the basis of these projections, a shortfall of SDR 13 million is projected for fresh meat.

(4) Sugar

Costa Rica's sugar production averaged around 200 thousand tons throughout the 1970s but fell to around 175 thousand tons in 1981/82 and 1982/83. With domestic consumption rising steadily as population increased, and with poor crops in recent years, exports declined from around 100 thousand tons in the early 1970s to around 75 thousand tons at the end of the 1970s, and subsequently declined even further to 55 thousand tons in calendar year 1982.

Costa Rica is a member of the 1977 International Sugar Agreement (ISA) with a basic export tonnage of 102 thousand tons and a quota in effect for 1982 of 86 thousand tons. In July 1982, Costa Rica fulfilled its minimum stocking obligation of 1,968 tons under the Agreement and is obligated to accumulate additional stocks of 2,953 tons by December 31, 1983. Almost all of Costa Rica's sugar exports have traditionally been shipped to the United States, and since May 1982 these shipments have been subject to quota limitations. The quota allocation for Costa Rica in the U.S. market for the 1982/83 year (October/September) is 38.1 thousand tons.

Earnings from sugar in the two pre-shortfall years were boosted by high world market prices. In the year ended February 1981 (1980/81), earnings from sugar were one and one half times larger than those of the previous year, with a 25 percent increase in the volume exported adding to the effect of a doubling of the average price received. Earnings fell by one third in 1981/82 on account of both lower volume and lower unit values; however, earnings remained well above those in the other years since 1975, when high world sugar prices also prevailed. The lower volume of exports was related to lower production than expected; the fulfillment of export contracts necessitated the import of sugar for domestic consumption during the last months of 1981 to supply the domestic market.

In the shortfall year (1982/83), earnings fell further by 30 percent because of much lower prices. Owing to the relatively poor crops in 1981 and 1982, the maintenance of export volume resulted in shortages in the domestic market, and stocks fell to very low levels by the end of 1982. Some imports of sugar were again required in November and December in 1982 for domestic consumption. Sugar prices in the U.S. market fell to an average of 17 cents per pound in March 1982, compared with an average of 30 cents per pound in 1980/81. However, following the imposition of country-specific quotas in May 1982, prices rose above 20 cents a pound and remained at that level for the remainder of 1982. The export unit values received by Costa Rica averaged 15 cents per pound in the shortfall year (1982/83), compared with 23 cents per pound in 1981/82. This reduction occurred largely because in the first four months of 1982/83, the average unit value was relatively low at 12 cents per pound.

The United States has announced a reallocation of sugar quotas for Central American countries to become effective October 1, 1983; this reallocation will effectively increase the quota for Costa Rica by 38 percent above its current level if the import quota for all countries combined remains unchanged. The 1983 crop is expected to be sufficient to fill the quota allocation in the U.S. market, to build up stocks to more normal levels, including fulfillment of ISA stocking obligations, and to enable some recovery in domestic consumption. This would permit exports by Costa Rica at levels equivalent to about 89 percent of those in the shortfall year. An increase of 31 percent in unit values is projected for the first post-shortfall year, in line with prices prevailing in the U.S. market, to be followed by an increase of 2 percent for the second. On the basis of these projections, a shortfall of SDR 6 million is estimated for sugar.

(5) "Other" agricultural and food products

"Other" products include cocoa, rice, cassava, planting material, vegetables, fruit, live cattle, and shrimp. Their major export market is the Central American Common Market (CACM) countries. After averaging SDR 50 million per year during the pre-shortfall period, export proceeds from "other" agricultural and food products declined to SDR 37 million in the shortfall year. The sizable negative growth in the CACM countries and the low level of economic activity in most other markets for these products largely accounted for the decline. No improvement is projected for the first post-shortfall year, as the effects of the economic improvement in the United States, also an important market, are expected to be offset by continued low level of demand from the CACM countries. For the second post-shortfall year, a modest growth rate of 5 percent is projected. On the basis of these projections a shortfall of SDR 5 million is calculated for "other" agricultural and food products.

b. Manufactured goods

Exports of manufactured goods grew at a rapid rate, averaging 20 percent per annum over the period from the early 1960s to the early 1980s; consequently, Costa Rica now has sizable exports of manufactured goods. In the two pre-shortfall years, these exports averaged in excess of 35 percent of total export earnings. In recent years, approximately two thirds of these exports--a somewhat lower proportion than in the 1960s and 1970s--have been shipped to the countries of the CACM; the next largest market is the United States. The largest component of manufactured exports is chemicals, mainly chemical fertilizer, and other important groups are machinery and equipment, textile and leather goods, paper and printing, and wood products.

In the shortfall year the value of exports of manufactured goods declined by 21 percent. The fall was particularly marked in the CACM markets (27 percent), but was also large (12 percent) in other markets. This decline was related to a sharp downturn in the level of economic activity in the CACM countries and a worldwide economic recession (Table 5). Continued decline is projected in exports to the CACM in both post-shortfall years, 11 percent in the first (that is, less than one half that of the shortfall year) and 4 percent in the following year on the assumption that the economies of these countries become somewhat stabilized in that year. The value of exports to non-CACM countries are projected to rise by 5 percent in each of the two post-shortfall years on the strength of the improved world economic outlook. This expansion should be facilitated by a US$25 million World Bank loan to Costa Rica, approved in May 1983, to establish a revolving Export Financing Fund to help ensure adequate

Table 5. Costa Rica: Exports of Manufactures and Underlying Factors

	Years Ending February				
	1979	1980	1981	1982	1983 1/
	(Annual percentage change)				
Total value (SDR terms)	-9	13	29	15	-21
Exports to CACM countries	-8	5	39	3	-27
Exports to others	-9	30	11	41	-12
Real GNP 2/	3	-3	2	1	-3
CACM countries 2/	2	-5 3/	3	1	-4
United States	5	3	0	2	-2

1/ Partly estimated.
2/ Weighted on the basis of exports by Costa Rica; for preceding calendar years.
3/ Reflects a large decline in Nicaragua.

access of exporters to foreign exchange for imported inputs and to strengthen the export promotion program. On the basis of these assumptions, earnings from manufactures by Costa Rica are projected to fall by 4 percent in the first post-shortfall year, but to increase by 4 percent in the second. A shortfall of SDR 14 million is estimated for manufactured goods.

4. Repurchase

In accordance with paragraph 7 of the compensatory financing decision, the authorities of Costa Rica are expected to represent that they will make a prompt repurchase in respect of any outstanding part of this purchase, if the amount purchased on the basis of partly estimated data (i.e., estimates for the four-month period November 1982 to February 1983) exceeds the amount that could have been purchased on the basis of actual data for the entire shortfall year.

5. Staff appraisal and proposed decision

The authorities of Costa Rica are expected to request a purchase equivalent to SDR 18.6 million under the compensatory financing decision, in respect of a shortfall of SDR 30 million in merchandise exports estimated for the year ended February 1983. The proposed purchase is equivalent to 30 percent of quota and would raise the member's purchases under the compensatory financing facility to 100 percent of quota. Data for the last four months of the shortfall year are partly estimated and, in accordance with paragraph 7 of the compensatory financing decision, the request is expected to include a representation that Costa Rica will make a prompt repurchase of the amount, if any, by which the proposed purchase exceeds the amount that could have been purchased on the basis of actual, rather than estimated, data for the entire shortfall year.

While Costa Rica has been experiencing balance of payments difficulties since 1978, the problems became particularly serious in 1981, when debt service payments were suspended because of acute foreign exchange shortages. In 1982, the overall balance of payments position continued to be weak. Despite a considerable reduction in the current account deficit, the overall deficit remained large and additional payments arrears were accumulated. In 1983, the balance of payments is expected to improve somewhat on the strength of favorable developments on the capital account, reflecting mainly a large inflow of foreign aid and rescheduling of Costa Rica's outstanding payments arrears. Although as of June 30, 1983, the gross official reserves were equivalent to five months of imports, they were held mostly in the form of illiquid assets, while net international reserves, taking into account payments arrears, were negative to the extent of the equivalent of about 16 months of imports. The staff considers that the balance of payments need of Costa Rica justifies the proposed purchase.

The staff also considers that the requirement of cooperation with the Fund is met for a compensatory financing purchase above 50 percent of quota. In December 1982, Costa Rica entered into a one-year stand-by arrangement with the Fund. In the discussion of the 1983 Article IV consultation and the mid-term review of the stand-by arrangement at the meeting of the Executive Board on July 18, 1983, it was noted that Costa Rica had been in compliance with the performance criteria of the stand-by program and had made significant progress in areas of inflation, exchange rate management, and rescheduling of external public debt. The request for a compensatory financing purchase is expected to include a representation by Costa Rica that the member will cooperate with the Fund in efforts to find, where required, appropriate solutions to its balance of payments difficulties.

Export earnings in the shortfall year ended February 1983 are estimated to have fallen 3 percent below the average for the two pre-shortfall years and to be 6 percent lower than the average projected for the two post-shortfall years. The overall shortfall of SDR 30 million reflects largely the shortfall in manufactured exports (SDR 14 million) and in fresh meat (SDR 13 million). The shortfall in manufactured exports relates to a large degree to the weak external demand for these goods in the Central American Common Market and the United States. The shortfall in the earnings from fresh meat arises from problems of quality control encountered in marketing fresh meat in 1982 and to low demand in major markets, especially in the United States. Smaller shortfalls are estimated for sugar (SDR 6 million) and for "other" agricultural and food exports (SDR 5 million), whereas the largest commodity exports, bananas and coffee, both recorded excesses (SDR 2 million and SDR 12 million, respectively). The increases in earnings in the two post-shortfall years arise largely from bananas, sugar, and fresh meat. While earnings from exports of manufactured goods are projected to decline further in the first post-shortfall year, a recovery to the level of the shortfall year is projected for the second. The staff believes that the circumstances leading to the shortfall in Costa Rica's exports in the year ended February 1983 were mainly attributable to world market conditions and therefore largely beyond the member's control. The staff further believes that, in view of the projected recovery, the shortfall is temporary in character.

The staff considers that the request by Costa Rica under the compensatory financing decision will meet all the requirements set forth in the decision. Accordingly, the following draft decision is proposed for adoption by the Executive Board, after a duly authenticated request has been received:

1. The Fund has received a request by the Government of Costa Rica for a purchase of SDR 18.6 million under the Decision on Compensatory Financing of Export Fluctuations (Executive Board Decision No. 6224-(79/135), adopted August 2, 1979).

2. The Fund notes the representations of Costa Rica and approves the purchase in accordance with the request.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Costa Rica--Relations with the Fund
(As of July 31, 1983)

Date of membership: January 8, 1946

Status: SDR 61.5 million

Quota: Present SDR 61.5 million
Proposed SDR 84.1 million (consent granted)

Fund holdings of Costa Rica colones:

	Millions of SDRs	Percent of Quota
Total	195.1	317.2
Of which:		
Credit tranche	(34.7)	(56.4)
Extended Fund facility	(11.3)	(18.3)
Supplementary financing facility	(16.4)	(26.6)
Enlarged access	(25.8)	(41.9)
Compensatory financing facility	(45.5)	(73.9)
Oil facility	(--)	(--)

SDR Department:

		Percent of Allocation
Net cumulative allocation	SDR 23.7 million	100.0
Holdings	SDR 4,282	0.01

Gold distribution: 27,387 fine ounces.

Direct distribution of profits from gold sales: US$5.1 million.

Exchange rate: A multiple exchange rate system consisting of three separate rates: an official rate, a banking rate, and a free rate. As of June 30, 1983 the exchange rates for the colon (buying) were ₡ 20 per U.S. dollar in the official market, ₡ 41.00 per U.S. dollar in the banking market, and ₡ 43.10 per U.S. dollar in the free market. The representative rate for valuation of the Fund's holdings of colones is the banking rate.

Exchange practices subject to Article VIII:	Costa Rica does not maintain unapproved exchange practices and restrictions.
Last consultation (Article IV):	Last consultation discussions were held in April-May 1983, and completed by the Executive Board on July 18, 1983 (EBM/83/104).
Technical assistance:	A panel expert from FAD is assigned to the Ministry of Finance.