FOR AGENDA

EBS/88/133

CONFIDENTIAL

July 11, 1988

To: Members of the Executive Board

From: The Secretary

Subject: Costa Rica - Review Under Stand-By Arrangement

Attached for consideration by the Executive Directors is the staff report on the second review under the stand-by arrangement for Costa Rica, which will be brought to the agenda for discussion on a date to be announced.

No decision proposing completion of the review has been included in the report at this time. A supplement will be issued prior to the Executive Board meeting proposing a course of action regarding the completion of the second review.

Mr. Linde (ext. 8500) or Mr. DeMilner (ext. 8502) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

COSTA RICA

Review Under Stand-By Arrangement

Prepared by the Western Hemisphere Department

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

Approved by S. T. Beza and Eduard Brau

July 8, 1988

Page

Text Tables

Appendices

Chart

I. Introduction 1/

A 17-month stand-by arrangement for Costa Rica in an amount of SDR 50 million (42 percent of quota on an annual basis) was approved by the Executive Board on October 28, 1987. No purchase was made upon approval of the arrangement, and since certain end-December performance criteria were not met, the purchase that was to be available at the end of January 1988 also was not made.

In the first program review, which was concluded by the Executive Board on April 4, 1988, the authorities proposed additional measures to achieve the program objectives for 1988 and to correct part of the deviation that occurred in 1987. At that meeting, the size of total access under the arrangement was reduced to SDR 40 million. At the time of the review the authorities emphasized that they wished to establish a track record of performance before making their first purchase. Under the amended arrangement the first purchase of SDR 10 million was to become available upon observance of the end-March performance criteria, and subsequent quarterly purchases for the same amount would be available with the observance of the corresponding performance criteria as well as upon completion of the second program review, which is to assess external financing arrangements with commercial banks and official bilateral creditors, and the progress made in the implementation of program policies. At the conclusion of the arrangement, assuming full use by Costa Rica of the resources available thereunder, total Fund credit outstanding to Costa Rica would be just under SDR 89 million, or nearly 106 percent of quota (Table 1).

The main objectives of the adjustment program for 1988 are an improvement in the net official reserve position of about US$60 million and the elimination of all external payments arrears while maintaining a moderate rate of output growth and bringing about a further reduction of inflation. 2/ To achieve these objectives the principal policy initiatives adopted for 1988 were: (1) a 6 percent real effective depreciation of the colon, which was to be achieved through an initial devaluation followed by crawling peg adjustments sufficient to maintain the targeted level of the real effective rate; (2) ceilings to limit banking system credit expansion to the private sector during 1988 to 10 percent; (3) adjustment of fiscal policies to achieve a combined public sector

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1/ A staff mission visited San José in the period April 25 - May 12 in conjunction with the second review of the stand-by arrangement. The staff met with the Minister of Finance and the Executive President of the Central Bank and senior officials of these and other public institutions. The staff representatives were Armando S. Linde (Head), Julian Berengaut, Lawrence DeMilner, (all WHD), Karnit Flug (ETR), and Marta Araya (Secretary-EXR). The mission was assisted by Ignacio Tampe, the Fund resident representative in San José. Mr. Edgar Ayales, Advisor to the Executive Director for Costa Rica, participated in the main policy discussions.

2/ Other projections under the 1988 program are shown in Table 2.

Table 1. Costa Rica: Position with the Fund During Period of Arrangement

	Outstanding May 31, 1988	1988 June	1988 July-Sept.	1988 Oct.-Dec.	1989 Jan.-Mar.
	(In millions of SDRs)				
Transactions under tranche policies (net)		-8.9	14.4	1.2	5.9
Purchases 1/		--	20.0	10.0	10.0
Repurchases		-8.9	-5.6	-8.8	-4.1
Ordinary resources		-5.0	-3.6	-3.5	-2.1
Enlarged access resources		-2.5	-2.0	-5.3	-2.0
Supplementary financing facility		-1.4	--	--	--
Transactions under special facilities (net) 2/		-2.3	-2.3	--	--
Purchases		--	--	--	--
Repurchases		-2.3	-2.3	--	--
Total Fund credit outstanding (end of period)	80.9	69.7	81.8	83.0	88.9
Under tranche policies 3/	76.2	67.4	81.8	83.0	88.9
Special facilities 2/	4.7	2.3	--	--	--
	(As percent of quota)				
Total Fund credit outstanding (end of period)	96.2	82.8	97.3	98.7	105.8
Under tranche policies 3/	90.6	80.1	97.3	98.7	105.8
Special facilities 2/	5.5	2.8	--	--	--

Source: IMF Treasurer's Department.

1/ From ordinary resources only.
2/ Includes compensatory financing facility.
3/ Includes outstanding use under EAR, SFF, and EFF.

Table 2. Costa Rica: Selected Economic Indicators

	1983	1984	1985	1986	Prel. 1987	Proj. 1988
(Annual percent change, unless otherwise specified)						
National income and prices						
GDP at constant prices	2.9	8.0	0.7	5.5	3.9	2.4
Nominal GDP	32.6	26.1	21.4	25.2	14.2	13.8
Consumer prices (end of period)	10.7	17.3	10.9	15.4	16.4	10.0
(average)	32.6	12.0	15.0	11.8	16.8	14.8
External sector (on the basis of U.S. dollars)						
Total exports, f.o.b.	-2.0	17.0	-5.9	15.6	2.6	5.7
Total imports, c.i.f.	11.1	11.0	0.8	4.7	19.1	-5.4
Non-oil imports, c.i.f.	14.8	16.0	0.6	12.3	19.2	-6.0
Export volume	2.1	14.4	-7.3	-6.3	13.4	-0.7
Import volume	19.1	12.8	7.4	7.7	13.0	-10.1
Terms of trade (deterioration -)	2.9	4.0	8.2	26.9	-14.2	1.2
Real effective exchange rate (end of period; depreciation -)	-3.3	4.2	-9.4	-3.8	-17.4	-6.0
Central administration						
Revenue and grants	52.7	26.1	18.5	18.8	17.0	16.3
Total expenditure	50.7	22.8	12.4	28.7	8.8	14.7
Banking system						
Net domestic assets 1/2/	31.6	8.6	10.4	16.2	23.3	8.7
Of which: public sector 1/3/	0.9	-1.7	0.8	-1.6	-1.0	-3.0
private sector	51.7	17.9	16.1	17.4	23.7	9.3
Central Bank losses (cash basis)1/	...	6.8	24.0	6.6	2.1	23.7
Liabilities to private sector	30.3	10.5	12.9	22.2	18.4	12.9
Interest rate (annual rate for six-month deposits, end of period)	22.0	20.0	22.5	21.5	23.0	...
(In percent of GDP)						
Combined public sector deficit	-8.0	-6.2	-7.0	-5.4	-3.2	-3.0
Nonfinancial public sector deficit	-3.1	-1.9	-1.8	-1.7	-0.2	0.8
Changes in floating debt and interest arrears	-5.3	1.5	-1.3	1.1	-0.7	-1.0
Domestic financing	11.1	-0.8	-0.3	-0.8	0.5	-0.7
External financing	-2.7	1.2	3.4	1.4	0.4	0.9
Central Bank losses (commitment basis)	-4.9	-4.3	-5.2	-3.7	-3.0	-3.8
Nonfinancial public sector savings	3.1	4.3	3.9	4.4	4.9	7.2
Central administration	0.4	0.3	1.0	0.5	0.3	1.0
Rest of public sector	2.7	4.0	2.9	3.9	4.6	6.2
Central administration deficit	-3.6	-3.0	-1.9	-3.3	-2.1	-2.0
Gross domestic investment	22.5	21.1	20.6	21.7	20.3	20.2
Gross national savings	11.4	13.4	12.2	17.6	11.1	14.3
Trade balance 4/	-4.9	-3.2	-5.0	-2.1	-7.1	-3.3
Current account balance (excluding official transfers for balance of payments support)4/	-11.1	-7.7	-8.4	-4.1	-9.2	-4.9
External debt (including use of Fund credit)4/	118.0	109.0	107.1	102.9	102.5	99.4 5/
(In percent of exports of goods and nonfactor services)						
Debt service ratio 6/	55.2	53.6	53.8	49.2	54.0	51.0
Interest payments 7/	28.6	24.5	22.9	19.9	19.5	18.1
(In millions of U.S. dollars)						
Overall balance of payments	-800	-128	194	-81	-165	330
Gross official reserves	307	441	513	553	501	...
Gross official reserves (months of imports)8/	3.7	4.8	5.5	5.7	4.3	...
External debt payments arrears outstanding	40	215	46	180 9/	255 9/	--

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

1/ In relation to the stock of liabilities to the private sector at the beginning of the period.
2/ Excludes counterpart of external payments arrears included in net international reserves of the Central Bank.
3/ Excludes increases in credit arising from the assumption by the Central Bank of part of the external debt of the public sector.
4/ GDP in colones has been converted into U.S. dollars using a constant real exchange rate between the colon and the U.S. dollar at the 1988 level.
5/ Includes expected exceptional financing.
6/ Before rescheduling. Includes Fund charges and repurchases, interest on short-term debt, unpaid interest and amortization, and interest on resources to cover the financing gap in 1987 and 1988.
7/ Before rescheduling. Includes Fund charges, interest on short term debt, unpaid interest, and interest on resources to cover the financing gap in 1987 and 1988.
8/ A substantial portion consists of nonliquid reserve assets, mainly claims against other Central American central banks.
9/ Excludes revolving credit facility in arrears, which is treated as a renewable credit line in the net official reserves of the Central Bank. Also excludes arrears accumulated in 1987 that are refinanceable.

deficit of no more than 3 percent of GDP; and (4) reduction in net domestic assets of the Central Bank by 9 1/2 percent. Achievement of the fiscal objective was predicated on the revenue generated by the tax package passed in November 1987, adjustments of public sector prices and prices of energy products, and the reduction or removal of subsidies for major food crops.

The Costa Rican authorities also were undertaking a series of measures to address the structural problems constraining economic growth. Thus, the levels and dispersion of import tariffs were to be reduced and the incentive scheme for exports to third markets was to be improved. The financial system was being strengthened and made more efficient by measures aimed at increasing competition and improving the regulatory and supervisory framework. Support prices for producers of basic grains were being reduced toward international levels and consumer subsidies on these items were being removed. These structural reforms were expected to be supported by a second structural adjustment loan from the World Bank.

Information relevant to the program performance in 1987 and the revision of the program for 1988 was included in the Staff Report for the 1987 Article IV Consultation and first review under the stand-by arrangement (EBS/88/60). Accordingly, this report reviews the 1988 performance to date, discusses policies for the remainder of the program period, and describes the latest developments on financing arrangements with external creditors.

II. Review of the Program

The end-March 1988 performance criteria for net international reserves, the stock of payment arrears, and net domestic assets of the Central Bank were met, but the limits on central government expenditure and banking system credit to the public sector were exceeded, albeit by moderate amounts. The first quarter performance is summarized in Table 3.

In other developments, the rate of inflation in the first quarter of 1988 was quite rapid. Producer prices rose by 8 percent and the index of consumer prices by 7 1/2 percent during the first three months of the year, largely reflecting adjustments to administered prices for public services, major food crops (as a number of subsidies were removed or reduced) and refined petroleum products. Wholesale prices decelerated sharply in April and May, as did consumer prices in May. Both price indexes have increased 10 percent during the first five months of 1988.

Table 3. Costa Rica: Performance Under Stand-By Arrangement
(March 1988)

Target	Program	Outcome	Margin
(In millions of U.S. dollars)			
1. Net international reserves	-300	-286	14
2. Stock of external payments arrears	260	255	5
(In millions of colones)			
3. Net domestic assets of the Central Bank	39,500	39,089	411
4. Cumulative government expenditure (1/87-3/88)	63,780 1/	64,202	-422
5. Net domestic credit to the nonfinancial public sector	34,489 2/	34,749	-260

1/ Adjusted (+ ₡ 400 million) for overperformance of central government revenue.
2/ Adjusted (- ₡ 2,211 million) for increase in government bonds held in the private sector.

1. Monetary policy developments

The program target for net domestic assets of the Central Bank in March 1988 was met without difficulty, and contributed to the overperformance on the net international reserves target (Table 4). However, banking system credit to the nonfinancial public sector exceeded the ceiling by a moderate amount. This deviation from the program target corresponds roughly to a larger than expected net investment of surplus funds (some ₡ 450 million) by certain institutions in the public sector (mainly the social security agency) in financial institutions outside the consolidated banking system. 1/

Although the performance in respect of the credit limits was substantially in line with the program, a number of developments in addition to the rapid rate of inflation in the first months of 1988 have raised concerns about the adequacy of existing credit policies for the achievement of the targets during the remaining period of the program.

1/ Because of delays in the availability of these data and questions about their coverage, they were not included in the program definition of net credit to the public sector.

Table 4. Costa Rica: Summary Operations of the Banking System

	December 31								March 31	
	(₡ 45/US$1)		(₡ 50/US$1)		(₡ 56.5/US)		(₡ 63/US$1)		(₡ 76/US$1)	
	1983	1984	1984	1985	1985	1986	1986	1987	1987	1988
I. Central Bank										
(In millions of colones)										
Net international reserves	-5,994	-11,800	-13,111	-3,317	-3,747	-8,202	-9,146	-18,980	-10,365	-21,729
Official reserves	-4,180	-2,030	-2,256	-1,022	-1,154	1,979	2,207	-2,587	1,567	-2,319
Payments arrears	-1,814	-9,770	-10,855	-2,295	-2,593	-10,181	-11,353	-16,393	-11,932	-19,410
Net domestic assets	14,942	21,685	22,996	16,573	17,003	25,509	26,453	38,450	25,878	39,089
Public sector credit (net) 1/	29,328	30,339	31,874	32,896	34,244	44,712	48,061	42,932	53,727	43,725
Rest of banking system credit (net)	-7,537	-9,597	-10,454	-11,108	-12,443	-11,106	-12,072	-6,093	-14,606	-9,709
Government trust funds	-1,098	-4,478	-4,478	-10,985	-10,985	-18,263	-18,263	15,676	-18,154	-19,227
Counterpart arrears	1,814	8,588	9,542	2,295	2,593	10,165	11,334	16,223	11,538	19,410
Operational losses (cash basis)	18,781	22,523	22,523	37,359	37,359	42,118	42,118	44,013	43,338	46,928
Medium- and long-term foreign liabilities	-66,845	-69,125	-76,806	-83,171	-93,983	-102,979	-114,826	-112,867	-136,011	-129,337
Stabilization bonds	-5,041	-4,895	-4,895	-4,900	-4,900	-5,079	-5,079	-7,815	-5,219	-10,294
Other accounts net	45,540	48,330	55,690	54,187	65,118	65,941	75,180	77,733	91,265	97,593
Of which: valuation adjustments	20,756	20,756	28,118	28,118	38,050	38,050	47,289	47,289	65,702	65,702
Currency issue	8,948	9,885	9,885	13,256	13,256	17,307	17,307	19,470	15,514	17,360
II. Banking System										
Net international reserves	-3,415	-10,328	-11,475	-1,331	-1,504	-4,761	-5,309	-14,802	-4,794	-16,266
Net foreign assets	-1,601	-558	-620	964	1,089	5,420	6,044	1,591	7,138	3,145
Payment arrears	-1,814	-9,770	-10,855	-2,295	-2,593	-10,181	-11,353	-16,393	-11,932	-19,410
Net domestic assets	58,407	71,109	73,354	71,205	73,223	92,419	95,044	120,647	99,011	134,657
Public sector credit (net) 1/	27,098	25,444	26,985	23,848	26,161	35,690	38,956	33,290	42,515	36,002
Of which: Adjusted net credit 2/	17,508	16,549	17,073	17,578	26,161	25,038	38,956	40,084	42,515	36,002
Credit to private sector 3/	27,541	32,470	32,490	37,733	38,183	44,824	45,081	56,800	47,542	58,430
Medium- and long-term foreign liabilities	-68,716	-71,825	-79,806	-86,881	-98,181	-104,209	-116,198	-114,307	-137,672	-131,343
Other accounts (net) 4/	72,484	85,020	93,685	96,505	107,060	116,114	127,205	144,864	146,626	171,568
Liabilities to private sector 4/	54,992	60,781	61,879	69,874	71,719	87,658	89,735	105,846	94,216	118,392
Money	22,481	25,710	25,710	28,970	28,970	39,901	39,901	40,225	37,616	37,954
Quasi-money	32,511	35,071	36,169	40,904	42,749	47,757	49,833	65,621	56,600	80,438
(Annual percentage change)										
Net domestic assets 5/6/		8.6		8.2		16.2		22.9		29.9
Public sector credit 2/5/		-3.0		0.8		-1.6		1.3		-6.9
Credit to private sector		17.9		16.1		17.4		26.0		22.9
Liabilities to private sector		10.5		12.9		22.2		18.0		25.7
(In percent of GDP) 7/										
Credit to private sector		18.4		18.2		17.1		18.0		18.1
Central Bank losses (cash basis)		2.3		7.7		2.0		0.7		1.2
Liabilities to private sector		35.5		34.2		32.9		34.6		36.3
Money		14.8		14.2		14.2		14.2		12.9
Quasi-money		20.7		20.0		18.7		20.4		23.4

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

1/ Includes counterpart of external debt assumed during the year.
2/ For program purposes, excludes counterpart of external debt assumed during the year.
3/ Includes rest of financial system.
4/ Includes Government trust funds, counterpart arrears, and Central Bank operational losses.
5/ In relation to the initial stock of liabilities to the private sector.
6/ Excludes counterpart of external payments arrears.
7/ *Average of the stocks at the beginning and end of year* in relation to the GDP of the same year, except for the Central Bank losses for which the numerators of the ratios are yearly flows. The calculation for March 1988 is based on a weighted average of 1987 GDP and the projected GDP for 1988.

Commercial bank credit to the private sector exceeded the Government's guidelines for the first quarter by one percentage point and contributed to a faster than expected increase in imports during the first three months of 1988. In addition, there was some delay in the Government's program to sterilize the surpluses of two major public enterprises that was in part a response to concerns over liquidity of the financial system following the insolvencies of a number of finance companies in late 1987 and January 1988.

The authorities' concern over the threat to confidence in the financial system posed by the insolvencies was reflected in their action in early February of this year to reduce temporarily the reserve requirement on six-month deposits from 10 percent to 6 percent, with the released funds (estimated at ₡ 1,200 million) to be made available for lending to troubled private commercial banks, or to regulated financial intermediaries, as well as to borrowers of these institutions in order to facilitate the orderly recovery of loans. The additional credit expansion was to be accommodated within the announced credit ceilings. Since these measures were adopted, the situation has stabilized and the atmosphere of crisis in the private financial sector seems to have subsided. The planned step-wise restoration of the reserve requirement on six-month deposits will take place on schedule beginning in July and will be completed by October.

The growth in credit to the private sector in the first quarter also reflects to a certain extent new activities undertaken by the two largest banks in the country. These banks have begun to offer a repurchase agreement by which government bonds in the banks' portfolio were sold to large private depositors on an overnight or very short-term basis. The transaction provide these banks with liquidity by attracting resources from other banks without increasing reserve requirements, thus avoiding penalties on noncompliance. 1/

As discussed with the authorities during the January 1988 staff visit, the Central Bank had reached accords with the state oil refinery (RECOPE) requiring it to utilize its surplus to retire its debt with the Central Bank, and with the social security agency (CCSS) to sterilize some of its surpluses through the purchase of central bank stabilization bonds. However, there was a delay in the signing and implementation of these accords with the result that no effect was given to this agreement in the first quarter. This situation has now been rectified and the process of sterilization began in the second quarter. The bond purchases by CCSS and debt amortization by RECOPE for 1988 as a whole would total ₡ 7 1/2 billion (or 2 1/2 percent of GDP).

1/ It should be noted that this measure is equivalent to a further reduction in reserve requirements.

With the passing of the liquidity difficulties of the banks, the authorities have initiated additional measures to bring about a tightening of credit conditions in order to ensure attainment of program targets during the rest of the program. The interest rate on three-month stabilization bonds was raised from 17 to 20 percent in April, and to 22 percent in May. The authorities also have confirmed their intent to raise the reserve requirement on demand deposits in the banking system from 35 to 37 percent. This move, which is expected to occur shortly, will result in an absorption of about 1/2 percent of banking system liabilities to the private sector.

2. Fiscal developments

The fiscal program for 1988 envisaged an improvement in the overall position of the consolidated nonfinancial public sector from a deficit of 0.3 percent of GDP in 1987 to a surplus of 0.8 percent of GDP in 1988 (Table 5). Given the projection of a rise in the losses of the Central Bank from 3.1 percent of GDP in 1987 to 3.8 percent in 1988, the overall deficit of the combined public sector would decline to 3 percent of GDP in 1988. Central administration expenditures under the program for 1988 are projected to increase by no more than 15 percent; this limit could be adjusted upwards (by up to ₡ 2 billion) in case that actual revenue collections would exceed projected amounts by a sufficient margin.

Data for the first quarter of 1988 indicate that cumulative central government expenditures exceeded the program limits by a small margin because of certain emergency expenditures in connection with extensive flooding in the Atlantic coast regions in February 1988. For the same reason, the Housing Mortgage Bank (BANHVI), the National Institute for Urban Housing (INVU), and the National Commission for Emergencies extended emergency financing for housing reconstruction. Additional spending overruns stemmed from a judicial decision in late 1987 that modified the methodology for calculating pension levels.

With respect to prospects for the rest of 1988, the authorities reaffirmed their commitment to the programmed spending targets. It was their view that the application of strict discipline over expenditures, including restraint in the adjustment of public sector wages (discussed below), would restore observance of the spending target starting at midyear.

Central administration revenues for the first quarter of 1988 amounted to ₡ 14.2 billion, or some ₡ 2 billion higher than the program projection and 40 percent above the level in the first quarter of 1987. Revenues in April were 29 percent above a year earlier; this slowing was anticipated and still leaves revenue ahead of projections thus far in 1988. 1/ The effects of the November 1987 package of tax measures were on balance broadly as expected, but income tax receipts

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1/ Revenue growth for 1988 as a whole is projected at 16 percent.

Table 5. Costa Rica: Operations of the Nonfinancial Public Sector 1/

	1983	1984	1985	1986	1987 Actual	1988 Program
	(In millions of colones)					
Central administration	-4,627	-4,966	-3,941	-8,245	-5,714	-6,000
Revenue	21,417	27,012	32,005	38,030	44,642	51,750
Expenditures	26,044	31,978	35,946	46,275	50,356	57,750
Current	20,953	26,586	30,144	36,858	43,629	50,625
Fixed capital formation	2,931	3,662	3,390	2,834	2,395	2,750
Other capital and net lending	2,160	1,730	2,412	6,583	4,332	6,375
Less: safeguard adjustment	--	--	--	--	--	2,000
Rest of general government 2/	2,393	1,870	2,704	3,534	3,472	4,798
Revenue	12,628	15,176	19,336	24,774	28,378	36,593
Current	12,082	14,909	18,765	24,292	28,080	35,548
Capital	546	267	571	483	298	1,045
Expenditures	10,235	13,306	16,632	21,240	24,906	31,796
Current	10,190	11,916	14,535	18,783	21,764	26,500
Fixed capital formation	335	219	474	1,150	985	1,743
Other capital and net lending 2/	-290	1,171	1,623	1,307	2,157	3,552
Public enterprises	-1,783	7	-2,479	642	1,379	3,662
Revenue	28,473	34,152	36,950	43,269	47,450	62,320
Current	27,879	33,860	36,659	41,621	46,543	60,967
Capital	594	292	291	1,648	907	1,353
Expenditures	30,256	34,145	39,429	42,627	46,071	58,658
Current	26,230	30,217	35,065	37,358	40,612	51,068
Fixed capital formation	3,408	3,811	4,414	5,523	5,967	7,533
Other capital and net lending	618	117	-50	-254	-508	57
Current account deficit (-)	4,005	7,062	7,685	10,943	13,260	22,073
Central Administration	464	426	1,861	1,172	1,013	3,125
Rest of general government	1,892	2,993	4,230	5,508	6,316	9,048
Public enterprises	1,649	3,643	1,594	4,263	5,931	9,900
Overall deficit (-) 2/	-4,017	-3,089	-3,716	-4,069	-862	2,460
Change in floating debt and interest arrears	-6,850 3/	2,425	-2,536	2,597	-1,105	-2,960
Of which: interest on foreign debt	-7,290 3/	1,589	-1,959	801	1,373 4/	-3,460
Net financing requirements	10,867	664	6,251	1,472	1,967	500
External (net)	-3,540	1,971	6,730	3,338	528	2,775
Disbursements	4,981	4,343	7,405	8,187	4,681	7,258
Amortization due	-5,322	-2,884	-6,706	-10,253	-10,433	-11,195
Principal in arrears (net change)	-6,476 3/	512	-1,136	2,044	5,820	-10,373
Debt relief	3,277	--	7,167	3,360	460	...
Expected rescheduling	--	--	--	--	--	17,085 5/
Domestic	14,407 3/	-1,307	-479	-1,866	1,439	-2,275
Bank credit (net)	13,889 3/	-959	505	-1,123	-798	-3,325
Other (net)	518	-348	-984	-743	2,237	1,050
	(In percent of GDP)					
Current account deficit (-)	3.1	4.3	4.0	4.5	4.9	7.2
Central Administration	0.4	0.3	1.0	0.5	0.4	1.0
Rest of general government	1.5	1.8	2.2	2.3	2.3	2.9
Public enterprises	1.3	2.2	0.8	1.8	2.2	3.2
Fixed capital formation	5.2	4.7	4.3	3.9	3.5	3.9
Overall deficit (-) 5/	-3.1	-1.9	-1.9	-1.7	-0.3	0.8
Central Administration	-3.6	-3.0	-2.0	-3.4	-2.1	-2.0
Rest of general government 5/	1.8	1.1	1.4	1.5	1.3	1.6
Public enterprises	-1.4	--	-1.3	0.3	0.5	1.2
Changes in floating debt and interest arrears	-5.3	1.5	-1.3	1.1	-0.4	-1.0
External financing	-2.7 3/	1.2	3.5	1.4	0.2	0.9
Domestic financing	11.1 3/	-0.8	-0.2	-0.8	0.5	-0.7

Sources: Ministry of Finance; and Fund staff estimates.

1/ Reduced coverage of the nonfinancial public sector for program purposes.
2/ Includes statistical discrepancies arising from reporting on an accrual and cash basis, from reporting periods that differ from the calendar year, and from public sector operations not included in this consolidation.
3/ Includes the effect of the assumption by the Central Bank of part of the external debt of the nonfinancial public sector in connection with the 1983 rescheduling agreement with foreign commercial banks.
4/ Includes expected rescheduling of current amortization and interest payments as well as rescheduling of arrears; derived from balance of payments data.
5/ Includes interest payments to commercial banks to be covered by rescheduling agreement expected to be concluded in 1988.

were sharply higher than projected, on the strength of administrative improvements that permitted a speeding up of mailings of tax notices. In addition, the collection of sales and consumption taxes improved sharply following the introduction of a computerized unified registry of businesses subject to taxation, which permitted the rapid identification and elimination of tax arrears. Export tax receipts fell short of budgeted amounts because of continuing low international prices of coffee, but higher than projected imports resulted in higher tariff revenues.

In discussing the prospects for the rest of 1988, the authorities emphasized that several of the factors that accounted for the better than expected revenue performance were of a nonrecurrent nature, and thus to avoid the incentive for higher spending, they were inclined to maintain the original program projections.

Outside the central administration, the program envisaged improvements in the financial position of (1) the social security agency (CCSS) primarily because of a broadening of its coverage to include additional wage earners, (2) the state oil refinery (RECOPE) as a result of price adjustments, and (3) the national grain marketing agency (CNP) following the elimination of subsidies. Complete data on the operation of decentralized entities and public enterprises through the first quarter are not yet available, but on the basis of partial information it would appear that the financial results so far have been broadly in line with the program.

Since inflation in the early months of 1988 exceeded the official projection, the formula for the determination of public sector wage adjustments introduced in 1986 1/ calls for a reopening of wage negotiations with the Government in July. The authorities observed that they intended to adopt a conservative position in these discussions so that the resulting wage adjustments would be consistent with the fiscal objectives of the program, and with the limits on central administration expenditure.

3. External policies

Although the end-March targets for net international reserves and arrears were met with some margin, the performance of the external sector was mixed; both exports and imports were somewhat higher than expected, and the trade deficit was some US$5 million higher than projected. The higher level of exports seems to have reflected mostly a change in the timing of shipments; as a result, the projection for total exports for the year as a whole remains unchanged. Higher imports might

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1/ Under the formula, whose general objective is to maintain public sector base wages broadly constant in real terms, wages are raised at the beginning of a year and at midyear by amounts related to the projected inflation rate with a possibility of readjustment of the midyear increase in the event that actual inflation exceeds projections.

have been related to the greater than programmed expansion of credit to the private sector and to increased capital inflows. Private capital inflows (including errors and omissions) were larger than expected by some US$20 million, and contributed to an overall balance of payments surplus that was slightly higher than projected.

The balance of payments projections for 1988 as a whole made at the time of the first review are still broadly consistent with the policies outlined below (Table 6). While the current account is expected to remain roughly unchanged from the earlier projection, in the capital account reduced disbursements on public sector loans are expected to be offset by more debt relief. The downward revision of official capital inflows is due to a change in the phasing of the World Bank's SAL-II disbursements and the associated Japanese cofinancing (these disbursements in 1988 are now expected to amount to US$80 million instead of US$100 million assumed earlier). However, the bilateral rescheduling recently signed with Mexico provides more debt relief than had been assumed in the program, and certain certificates of deposit held by Japan are now expected to be covered by the Paris Club rescheduling. These latter developments helped to reduce nonreschedulable arrears and thus to meet the arrears target with somewhat lower cash payments than envisaged in the program.

Regarding exchange rate policy, following the 6 percent step devaluation in January 1988, there was an acceleration of domestic price increases, which together with the modest size of biweekly crawling peg adjustments, resulted in an erosion of the effect of the step devaluation on the real effective exchange rate (Chart 1). Thus, the real effective exchange rate at the end of April 1988 was only 1 percent lower than the level at end-1987.

The authorities recognized the desirability of regaining the level of competitiveness reached by the January step devaluation. While the rapid increase in prices at the beginning of the year was a factor in the decision to proceed slowly with crawling peg adjustments after the step devaluation, the authorities noted the healthy performance of nontraditional exports and the attainment of the net international reserves target as factors that gave them some room in the execution of exchange rate policy. With the deceleration of prices in April and May following the absorption of changes in administered prices, the authorities have followed up on their intention to undertake somewhat larger adjustments of the crawling peg.

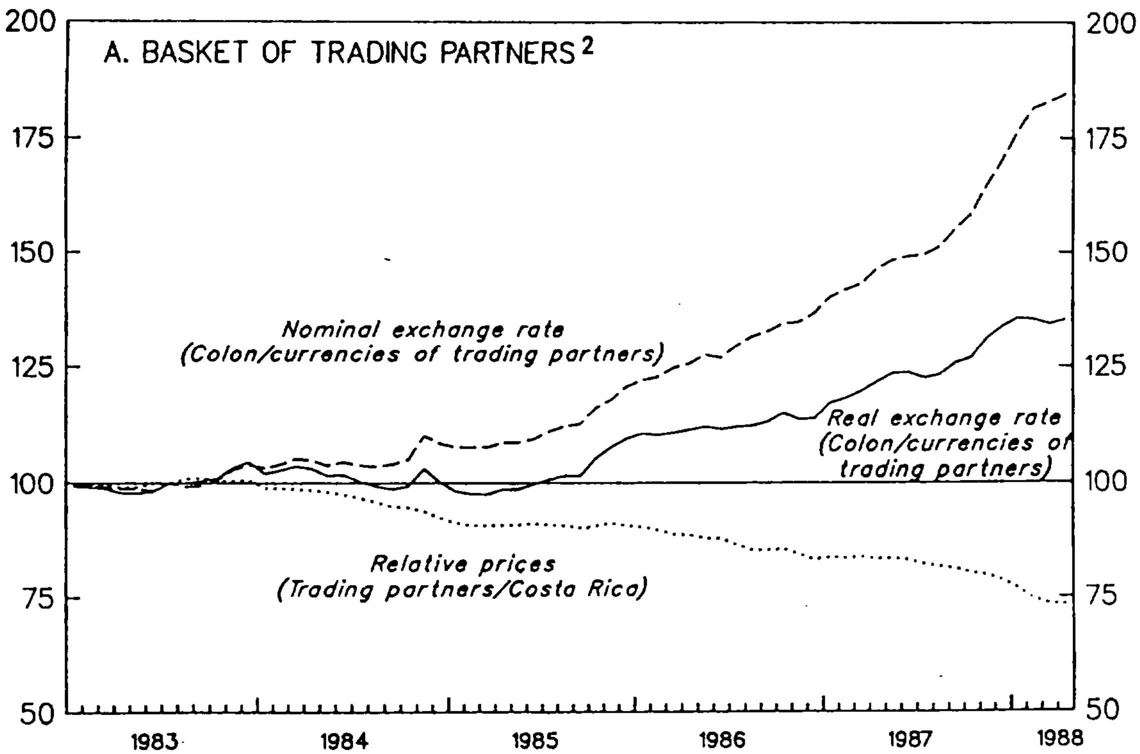
Table 6. Costa Rica: Medium-Term Balance of Payments and External Debt Projections

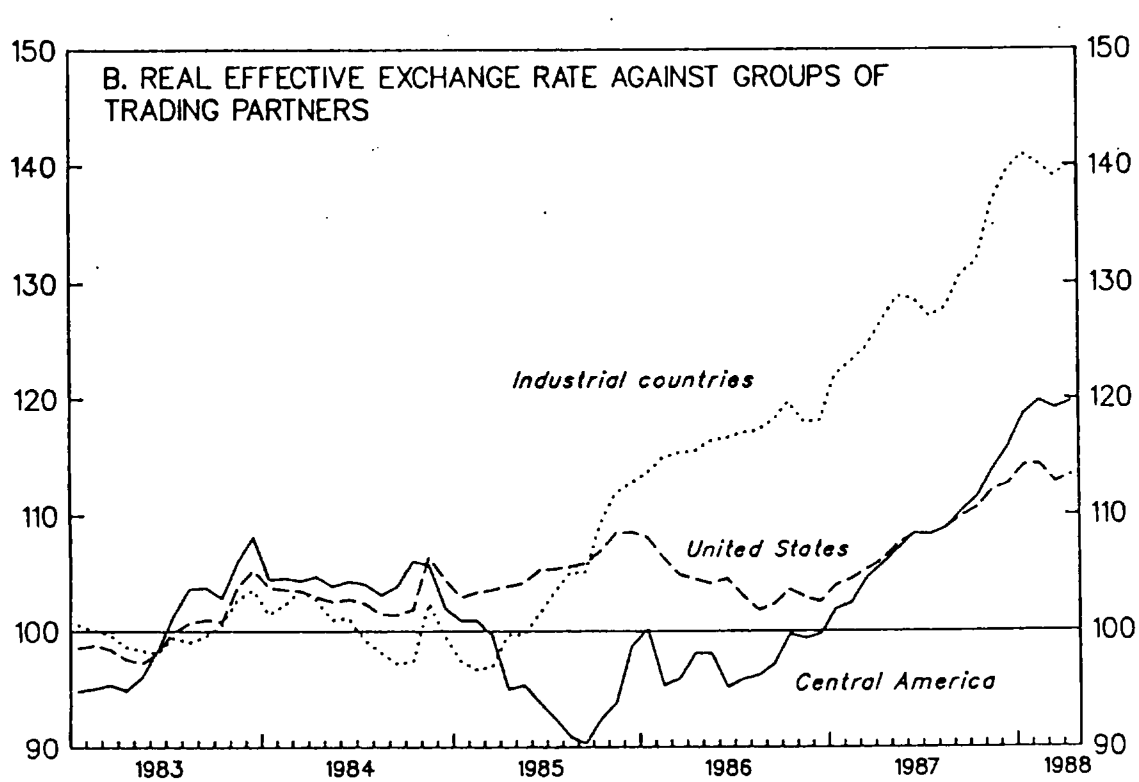
	1985	1986	Prel. 1987	Prog. 1988	Projected 1989	1990	1991	1992
	(In millions of U.S. dollars)							
Current account 1/	-289.7	-152.1	-368.2	-222.5	-226.0	-232.3	-232.9	-238.8
Trade balance	-171.8	-77.4	-271.4	-133.2	-134.1	-139.8	-146.6	-157.9
Exports	939.1	1,085.8	1,113.6	1,176.8	1,266.5	1,359.0	1,458.6	1,564.3
Imports	-1,110.9	-1,163.2	-1,385.0	-1,310.0	-1,400.6	-1,498.8	-1,605.2	-1,722.1
Factor payments	-282.2	-280.7	-286.3	-300.9	-309.9	-319.2	-324.4	-330.8
Of which: public sector interest due	-280.3	-281.7	-284.7	-298.1	-304.9	-309.2	-314.4	-320.8
Other services and transfers	164.3	206.0	189.5	211.6	217.9	226.7	238.0	249.9
Capital account	-73.8	-195.1	-251.9	-170.0	-161.7	-123.6	-81.0	54.7
Public 2/	-172.4	-244.4	-366.0	-325.8	-276.8	-243.6	-201.0	-65.3
Disbursements	185.2	135.2	79.6	123.9	116.0	130.1	143.1	157.4
Amortization due	-357.6	-379.6	-445.6	-449.7	-394.7	-373.7	-344.1	-222.7
Private, and errors and omissions	98.6	49.3	114.1	155.8	115.0	120.0	120.0	120.0
Balance of payments support	200.0	120.6	120.0	205.0	155.0	118.0	135.0	114.0
U.S. AID (ESF)	160.0	80.6	120.0	125.0	85.0	68.0	55.0	44.0
IBRD (SAL)	40.0	40.0	--	80.0	70.0	50.0	80.0	70.0
Overall balance before exceptional financing	-163.5	-226.6	-500.1	-187.5	-232.7	-237.9	-178.9	-70.1
Debt relief	357.8	145.9	42.9	--	--	--	--	--
Rescheduling of current obligations	300.8	133.0	21.8	--	--	--	--	--
Rescheduling of past obligations	57.0	12.9	21.1	--	--	--	--	--
Financing gap	--	--	300.5	509.4	283.6	282.3	218.8	118.1
Expected rescheduling of current obligations 3/	--	--	--	309.4	...	...	...	...
Expected rescheduling of past obligations 3/	--	--	--	300.5	...	...	...	...
Arrears subject to rescheduling	--	--	300.5	-300.5	...	...	...	...
Residual financing gap	--	--	--	200.0 4/	...	...	...	...
Overall balance after exceptional financing (deficit -)	194.3	-80.7	-156.7	321.9	50.9	44.4	39.9	48.0
Net international reserves	-194.3	80.7	156.7	-321.9	-50.9	-44.4	-39.9	-48.0
Net official reserves (increase -)	-99.8	-55.0	76.7	-61.7	-50.9	-44.4	-39.9	-48.0
Net use of Fund resources	30.0	-36.0	-62.2	-15.1	-22.1	-24.4	-17.9	-24.0
Other net official reserves 5/	-129.8	-19.0	138.9	-46.7	-28.8	-20.0	-22.0	-24.0
Change in arrears (reduction -)	-169.5	135.7	80.0	-260.2	--	--	--	--
Outstanding public debt (including exceptional financing)	3,708.8	3,855.6	4,107.6	4,207.1	4,261.9	4,326.1	4,406.0	4,504.8
Debt service (including IMF)	-659.6	-697.3	-792.5	-804.4	-734.8	-708.5	-679.5	-579.5
Amortization	-379.3	-415.6	-507.8	-506.3	-429.9	-399.3	-365.2	-258.7
Of which: IMF	-21.7	-36.0	-62.2	-56.6	-35.2	-25.7	-21.1	-36.0
Interest	-280.3	-281.7	-284.7	-298.1	-304.9	-309.2	-314.4	-320.8
Of which: IMF	-14.5	-17.5	-13.2	-11.1	-10.3	-8.3	-6.6	-5.2
	(As percent of GDP, unless otherwise specified)							
Exports	27.1	29.0	27.8	27.8	28.1	28.3	28.4	28.6
Imports	-32.1	-31.1	-34.6	-30.9	-31.1	-31.2	-31.3	-31.4
Trade balance	-5.0	-2.1	-6.8	-3.1	-3.0	-2.9	-2.9	-2.9
Current account balance 1/	-8.4	-4.1	-9.2	-5.3	-5.0	-4.8	-4.5	-4.4
Capital account 2/	-2.1	-5.2	-6.3	-4.0	-3.6	-2.6	-1.6	1.0
Exceptional financing 6/	16.1	7.1	4.1	19.2	3.4	2.5	2.6	2.1
Overall balance after exceptional financing	5.6	-2.2	-3.9	7.6	1.1	0.9	0.8	0.9
External debt (including use of Fund credit)	107.1	102.9	102.5	99.4	94.5	90.1	85.9	82.2
Debt service ratio (before rescheduling) 7/	-53.8	-49.2	-54.9	-52.5	-44.8	-40.5	-36.3	-29.0
Debt service ratio (after rescheduling) 7/	-29.3	-39.8	-53.4	-32.3	...	...	...	...
Memorandum items								
GDP (in millions of U.S. dollars) 8/	3,462	3,746	4,008	4,233	4,509	4,802	5,129	5,478
Foreign interest rates (in percent)	7.8	7.4	7.2	7.2	7.2	7.2	7.2	7.2

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

1/ Excludes official transfers for balance of payments support (U.S. AID).
2/ Excludes disbursements of IBRD's structural adjustment loans.
3/ In 1988, assumes rescheduling of current and past due obligations on terms similar to those agreed upon in 1985.
4/ Consists of the financing of interest in arrears to banks at the end of 1987 plus the amount not paid in 1988.
5/ Includes revolving credit facilities and valuation adjustment.
6/ Includes balance of payments support and financing gap.
7/ As percent of exports of goods and nonfactor services.
8/ GDP in colones has been converted into U.S. dollars using a constant real exchange rate between the colon and the U.S. dollar at the 1988 level.

CHART 1
COSTA RICA
EFFECTIVE EXCHANGE RATES[1]





Sources: IMF, *International Financial Statistics;* and Fund staff estimates.
[1] 1983=100. Calculated on the basis of Costa Rica's wholesale price index. An increase (decrease) in the index indicates depreciation (appreciation) of the colon.
[2] 1980 trade weights excluding oil and Nicaragua.

4. External financing

The authorities reaffirmed their resolve to normalize relations with creditors and to settle all outstanding arrears in the course of 1988, through either cash payments or rescheduling. Accordingly, the negotiations with commercial banks on a possible rescheduling agreement have continued. The Costa Rican representatives have taken the position that a rescheduling on conventional terms would limit economic growth and that more favorable terms were required. At the same time, representatives of some commercial banks have maintained that a new money package could not be undertaken because of the need to make required reserve allocations. Against this background, discussions on new options for debt refinancing have been taking place, including consultations with the staff of the World Bank and the Fund.

The latest round of negotiations with the representatives of the commercial banks steering committee took place in late May and June. These discussions are to continue in the coming weeks. Given the present uncertainties about the timing of an arrangement, the Costa Rican authorities have indicated that they are prepared to set up an escrow account into which they would deposit the full interest payments falling due (starting July) minus the US$5 million a month that they would continue to pay directly to banks.

With regard to official creditors, the Costa Rican authorities intend to seek a rescheduling within the framework of the Paris Club, and are in the process of sounding out members on the possibility of scheduling a meeting in the coming weeks.

III. Medium-Term Outlook

The medium-term outlook for Costa Rica's economy is based on the same general assumptions included in the projections presented at the time of the first program review. Revisions have been introduced to reflect the effect of valuation changes on the stock of external public debt, a more steeply declining schedule of amortization payments, and a change in the timing of disbursements of the IBRD SAL loan. Also, the ratios of certain variables (that were not otherwise affected) to GDP were modified because of recent revisions of national accounts data.

Because the stock of debt has been raised, the current account deficit is projected to be somewhat higher, declining to 4.4 percent of GDP in 1992 instead of 4 percent as had been estimated earlier, to reflect higher interest payments. On the capital account, scheduled amortization payments have been revised to incorporate updated information. The net effect of these revisions is to reduce the size of the financing gap by increasingly larger amounts over the next five years. Accordingly, the financing gap is now projected to be 2 1/4 percent of GDP in 1992 instead of 5 3/4 percent as shown previously. In line with the revised estimates for amortizations, the potential relief that would be available from conventional debt rescheduling with commercial banks and bilateral creditors has been lowered, thus leaving gaps of some US$30 million to US$40 million a year that would need to be financed by new loan commitments from multilateral and bilateral creditors. No new bank financing is contemplated.

This baseline scenario continues to assume a further improvement in public sector savings over the period to 1992, consistent with a reduction of the fiscal deficit. The scenario also is based on a very modest rise in the ratio of investment to GDP, thus constraining the growth of output over the period to an average of 3 percent a year, implying only a negligible growth on a per capita basis.

IV. Staff Appraisal

Costa Rica has made considerable progress in recovering from the deep recession and serious balance of payments difficulties of the early 1980s. The position of the nonfinancial public sector has been strengthened markedly, steps have been taken to open up the economy and reduce distortions, and improvements have been made in the management of interest rates and the exchange rate. At the same time, as a result of the country's heavy debt burden, the external position remains weak and the prospects for more rapid economic growth in the medium term are likely to be constrained.

The economic program for 1987-88 involved a tightening of financial policy, including adoption of a tax package, and a sizeable depreciation of the colon. However, the balance of payments outcome fell short of that sought in 1987 because of slippages in the implementation of credit policy.

For 1988, the authorities have adopted several measures to attain the objectives of the program, including a further devaluation of the currency and a tightening of credit policy. The results in the first quarter of 1988 were close to the program targets; the deviations on central government expenditures and on credit to the public sector were not large. The authorities also were successful in managing an incipient financial crisis provoked by the bankruptcies of a number of finance companies that threatened confidence in the financial system.

Despite the improved performance so far in 1988, there are a number of factors that will need to be monitored closely--and responded to by policy actions as necessary--since they have a bearing on the success of the adjustment program. Inflation, although reflecting to a large extent adjustments in administered prices, accelerated in the early months of 1988 and nullified in large measure the benefits of the January step devaluation. The modest rate of crawling peg adjustments since January has restored only a small portion of the intended depreciation of the real effective exchange rate. In addition, pressures for wage adjustments have increased, with potentially adverse consequences for the public finances. Credit to the private sector is still expanding above the limits set by the Government, with a consequent increase in imports so far in 1988. Finally, the proposed action to sterilize surpluses in the rest of the nonfinancial public sector has been delayed for several reasons, thus limiting the effectiveness of monetary policy.

The Costa Rican authorities are aware of these problems and they have acted by raising the interest rate on shorter-term stabilization bonds of the Central Bank and they also plan to increase the legal reserve requirements on demand deposits. Together with the implementation of efforts to sterilize the surpluses of RECOPE and CCSS, these measures should contribute to a tightening of credit and to a noninflationary outcome of the wage negotiations in July.

The authorities have reiterated their commitment to re-establish normal relations with Costa Rica's external creditors, and discussions are continuing with commercial bank creditors. The authorities have indicated their intention to continue with a negotiated approach. In the event an agreement with the commercial banks is not reached in the coming weeks, the authorities have expressed their willingness to set up an escrow account into which Costa Rica would pay its full current interest obligations to commercial banks except the portion that would continue to be paid directly. A meeting with bilateral creditors under the auspices of the Paris Club also is being arranged.

Although the deviations from the March performance criteria were not large and were associated with temporary events and circumstances, the authorities do not intend to ask for a waiver. It is their view that the policies presently in force will be adequate to meet the performance criteria for end-June, thus enabling them to purchase subsequently upon completion of the second program review.

In sum, the authorities have presented a program that is expected to strengthen Costa Rica's external position and improve economic performance more generally. The efforts of the authorities need to be complemented by external cooperation if the program is to be implemented successfully, with the achievement of orderly payments arrangements. In light of the measures already adopted and those which are being implemented, the staff is of the view that the authorities' program for 1988 justifies continued support from the Fund.

A proposed decision is not included at this time because negotiations with external creditors over the financing of the program are still in progress. The staff will follow these discussions closely and will keep the Executive Board informed as developments occur. Once a Board meeting is scheduled, the staff will issue a supplement to this paper, together with a proposed decision regarding the completion of the program review.

Fund Relations with Costa Rica
(as of May 31, 1988)

I. Membership Status

(a) Date of Membership: January 8, 1946

(b) Status: Article VIII

(A) Financial Relations

II. General Department

(a) Quota: SDR 84.1 million

		Millions of SDRs	Percent of Quota
(b)	Total Fund holdings of colones:	165.00	196.19
(c)	Fund credit: Total	80.88	96.17
	Of which: Credit tranches	23.29	27.69
	CFF	4.65	5.53
	EAR	44.97	53.47
	Extended facility	6.56	7.80
	Supplementary facility	1.41	1.67
(d)	Reserve tranche position:	--	--

III. Recent Stand-By or Extended Arrangements and Special Facilities

(a) Stand-by and extended arrangements:

Type of Arrangement	Amount (SDR million)	Percent of Quota	Duration	Amount Drawn (SDR million)	Status
SBA	40.00	47.6	10/28/87-3/31/89	--	Active
SBA	54.00	64.2	3/13/85-4/30/86	34.0	Expired
SBA	92.25	150.0	12/82-12/83	92.25	Expired
EFF	276.75	450.0	6/81-5/84	22.5	Canceled Dec. 1982
SBA	60.50	147.6	3/80-2/82	15.4	Canceled June 1981

(b) Special facilities:
Compensatory financing

Date of Approval	Amount Drawn SDR Million	Amount Drawn Percent of Quota
Sept. 1983	18.60	30.2
June 1981	30.10	48.9

IV. SDR Department

	Millions of SDRs	Percent of Allocation
(a) Net cumulative allocation:	23.73	100.00
(b) Holdings:	0.18	0.75
(c) Current designation plan:	--	--

V. Administered Accounts: None.

VI. Financial Obligations Due to the Fund (millions of SDRs)

	Overdue Financial Obligations (May. 31, 1988)	Principal and Interest Due June-Dec. 1988	1989	1990	1991
Repurchases	--	17.9	26.1	19.0	5.2
Charges and interest including SDR (provisional)	--	4.0	4.9	3.1	1.9
Total	--	21.9	31.0	22.1	7.1

(B) Nonfinancial Relations

VII. Exchange Rate Arrangements: The representative exchange rate for the Costa Rican colon is the unified banking rate which was quoted at ₡ 75.75 (selling) per U.S. dollar as of June 20, 1988. All transactions take place at this rate except for remittances to students registered with the Central Bank prior to 1981, to whom foreign exchange is sold at the official rate of ₡ 20.00 per U.S. dollar; this special exchange rate gives rise to a multiple currency practice under Article VIII, Section 3.

VIII. Exchange Restrictions: Costa Rica maintains a restriction on payments and transfers for current international transactions evidenced by external payments arrears and engages in a multiple currency practice for certain remittances for study abroad. On April 4, 1988, the Executive Board approved the retention of the multiple currency practice for certain remittances until the earlier of the completion of the second review of the stand-by arrangement approved that date or June 30, 1988 (EBM/88/56). Costa Rica's exchange restriction, evidenced by arrears on external debt obligations, was not approved by the Fund at that time.

IX. Last Article IV Consultation: Consultation discussions were held in November 1987-February 1988 and completed by the Executive Board on April 4, 1988 (EBM/88/56). Consultations are conducted on a 12-month cycle.

X. Technical Assistance:

(a) CBD: A staff mission reviewed the Central Bank and financial sector legislation in February 1986. From April to November 1986 an Advisor was assigned to the Central Bank in the area of organization and methods. Since April 1986, an Advisor has been assisting the Central Bank in the area of accounting procedures. A panel expert was assigned to the Central Bank in September 1986 as an Advisor on external debt management. In November 1986 a CBD mission visited San José to advise the authorities on procedures and techniques used in the formulation of monetary policy.

(b) FAD: A panel expert was assigned to the Ministry of Finance from August 1980 to December 1983, to provide assistance principally in the area of budgetary procedures.

(c) Bureau of Statistics: Technical assistance missions to improve the reporting of monetary data were fielded in December 1984 and May 1985. In January 1985 a technical assistance mission on balance of payments accounting visited Costa Rica. In May 1986 a STAT economist assisted the authorities in the implementation of procedures to improve the classification and monitoring of the Central Bank's net unclassified assets. A government finance statistics mission visited the country in July 1986. In September 1987 Costa Rica was included in a technical assistance mission on the five countries of the Central American Monetary Council to promote methodological consistency in the preparation and formulation of monetary and financial accounts.

XI. Resident Representative/Advisor: In January 1988 Mr. Ignacio Tampe replaced Mr. Hector Avila as the Fund's resident representative in San José.

Costa Rica: Schedule of Purchases During Period of Stand-By Arrangement

Scheduled Availability Date	Amount	Program Conditions Necessary For Purchases 1/
After April 28, 1988	SDR 10 million	Observance of quantitative performance criteria as of March 31, 1988.
After July 28, 1988	SDR 10 million	Observance of quantitative performance criteria as of June 30, 1988 and completion of the second program review.
After October 30, 1988	SDR 10 million	Observance of quantitative performance criteria as of September 30, 1988 and any other conditions to be decided upon in the second program review.
After January 30, 1989	SDR 10 million	Observance of quantitative performance criteria as of December 31, 1988 and any other conditions to be decided upon in the second program review.

1/ Other than generally applicable conditions under the arrangement and nonquantitative performance criteria, including the performance clauses on the exchange and trade system.

Relations with the World Bank Group

Costa Rica has received to date 31 Bank loans, 1 IDA credit, and financing through IFC of 5 investment projects, totaling US$515 million (see table below). Of this amount, less than US$35 million remains to be disbursed.

Prior to 1981, World Bank lending to Costa Rica was concentrated primarily on developing basic infrastructure. With the growing financial and economic deterioration in Costa Rica that occurred in the early 1980s, the Bank's strategy was redesigned to encourage long-term structural changes needed to restore dynamism to the economy, while also assisting the more directly productive sectors. In this context, the Bank's approach supports three key goals: (a) revamping the incentive framework to promote new sources of growth in the economy, with particular emphasis on developing exports to new markets outside the region; (b) improving public sector efficiency and resource use to increase the availability of resources for productive investments; and (c) strengthening Costa Rica's creditworthiness.

As a first phase of this effort, an Export Development Loan was approved in May 1983, which was fully disbursed by mid-1985. This operation was followed by a Structural Adjustment Loan (SAL) of US$80 million, that was approved in April 1985 and disbursed by mid-1986. The SAL aimed at supporting the Government's structural adjustment program, with the objective of promoting renewed export-led growth, with particular emphasis on expanding nontraditional exports to markets outside Central America. The main areas covered by the first phase of the Government's medium-term program included: (a) trade reform geared to a lowering of effective protection; and (b) fiscal reform directed to a reduction of the size of the public sector and improvement in the efficiency of public sector institutions and programs. In the area of trade policy, Costa Rica took initiatives for the reform of the regional tariff regime of the Central American Common Market. These initiatives included tariff reductions, a shift of specific tariffs to an ad valorem basis, introduction of a modern nomenclature, and reduction of import surcharges. Regarding public sector management, the program aimed at limiting the growth of the public sector, including curtailing certain public sector investments, reducing public sector employment, and initiating actions to improve the cost effectiveness of certain loss-making institutions.

More recently, in October 1986, the Bank approved a US$26 million loan for the Atlantic Agriculture Development Project which aims at expanding agricultural exports. The loan was signed in April 1987 and approved by the Legislative Assembly in February 1988.

The Costa Rican authorities have reached agreement with the World Bank on the principal elements of the next phase of a structural reform program. These include: (i) trade reform policies; (ii) banking reform policies; (iii) management of the public sector and public savings targets; (iv) incentive policies and organizational reforms in the productive sectors to promote exports; and (v) external debt management. The above reform program would be supported by a second World Bank structural adjustment loan which was appraised in September 1987; the overall package is expected to be cofinanced by the Government of Japan. The following tabulation describes Costa Rica's financial relations with the World Bank group.

(In millions of U.S. dollars, as of December 31, 1987)

A. IBRD/IDA/IFC Operations

	Number of Credits	Disbursed to Date	Undisbursed	Total	Repaid
1. IBRD loans	31	481.6	33.3	514.9	163.9
Agriculture	4	29.7	26.0	55.7	16.7
Education	1	6.0	--	6.0	0.7
Export	1	25.2	--	25.2	1.0
Imports	2	6.5	--	6.5	4.6
Industry	3	19.9	--	19.9	9.9
Power	7	126.4	0.5	126.9	62.0
Technical assistance	1	1.5	2.0	3.5	--
Telecommunications	4	57.9	--	57.9	26.5
Transport	6	107.3	--	107.3	34.9
Water supply	1	21.2	4.8	26.0	7.6
SAL	1	80.0	--	80.0	--
2. IDA credit	1	5.5	--	5.5	1.5
Transport	1	5.5	--	5.5	1.5
3. IFC investments	5	6.7	--	6.7	...

B. IBRD Loan Transactions 1/

	1981	1982	1983	1984	1985	1986	1987
Net disbursements	13.7	7.5	5.8	17.0	62.4	31.0	-18.0
Gross Disbursements	22.3	19.7	23.5	36.2	84.1	55.2	13.6
Pincipal Repayments	-8.6	-12.2	-17.7	-19.2	-21.7	-24.2	-31.6

Source: IBRD.

1/ Data are for fiscal years which end on June 30.