IMF Country Report No. 22/93

COSTA RICA

March 2022

FIRST AND SECOND REVIEWS UNDER THE EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY, REQUEST FOR EXTENSION OF THE ARRANGEMENT, AND REPHASING OF PURCHASES—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR COSTA RICA

In the context of the First and Second Reviews Under the Extended Arrangement Under the Extended Fund Facility, Request for Extension of the Arrangement, and Rephasing of Purchases, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on March 25, 2022, following discussions that ended on March 3, 2022, with the officials of Costa Rica on economic developments and policies underpinning the IMF Extended Fund Facility arrangement. Based on information available at the time of these discussions, the staff report was completed on March 10, 2022.
- A **Statement by the Executive Director** for Costa Rica.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

PRESS RELEASE

PR22/91

IMF Executive Board Completes the First and Second Reviews Under Costa Rica's Extended Arrangement under the Extended Fund Facility; and Approves Extension of the Arrangement and Rephasing of Access

FOR IMMEDIATE RELEASE

- The IMF Executive Board concluded today the combined first and second reviews under the Extended Fund Facility (EFF) for Costa Rica, allowing for an immediate disbursement equivalent to about US$ 284 million.
- The Costa Rican authorities have made important progress under their economic reform program supported by the IMF over the last year. Sustained reform efforts remain critical to strengthen the economy resilience to shocks and to foster inclusive and sustained growth and job creation.
- The extension of the EFF arrangement will provide additional time for the incoming administration to design and implement reforms under the IMF-supported program.

Washington, DC – March 25, 2022: The Executive Board of the International Monetary Fund (IMF) completed today the First and Second Reviews of Costa Rica's economic reform program supported by the IMF's extended arrangement under the Extended Fund Facility (EFF). Completion of these reviews makes available SDR 206.23 million (about US$ 284 million), bringing total disbursements under the arrangement to SDR 412.57 million (about US$ 569 million). The Executive Board also approved an extension of the arrangement by five months, until July 31, 2024, and a rephasing of access.

Costa Rica's three-year extended arrangement was approved on March 1, 2021, in the amount of SDR 1.23749 billion (US$1.778 billion or 335 percent of quota in the IMF at the time of approval of the arrangement. See Press Release No. 21/53).

Following the Executive Board's discussion on Costa Rica, Mr. Kenji Okamura, Deputy Managing Director and Acting Chair of the Board, issued the following statement:

"The Costa Rican authorities have made important progress under the IMF-supported program, including a strong fiscal overperformance in 2021 and major advances in strengthening the efficiency and fairness of the public administration.

"While the proactive response to the COVID-19 shock and sustained export performance have supported a robust recovery, the economic outlook remains subject to important global risks posed by the pandemic as well as higher commodity prices and tighter global financial conditions. It is therefore important to build on recent progress to ensure debt sustainability, maintain monetary and financial stability, and promote inclusive, green, and sustainable growth.

"Sustained fiscal consolidation under the fiscal rule remains a priority, while continuing to allocate adequate resources to protect the most vulnerable. Further efforts are needed to enhance revenue mobilization and public financial management.

"The Central Bank of Costa Rica (BCCR) provided key support in buffering the COVID-19 shock. Given the stronger inflation outlook, the ongoing withdrawal of monetary accommodation is warranted, in line with the BCCR's data-dependent and forward-looking approach, supported by continued exchange rate flexibility. Ongoing steps to further enhance the BCCR's law will underscore its operational autonomy and governance. The central bank's roadmap to integrate climate change considerations into its core activities is commendable.

"The financial system has shown resilience throughout the pandemic due to supportive monetary policy and a proactive approach to monitoring risks and updating contingency plans. Ongoing efforts to monitor credit risks, enhance the crisis management framework and incentivize de-dollarization remain critical.

"The authorities should press ahead with their ambitious reform agenda to promote an inclusive and green economy, creating high-quality jobs, for which greater formalization and digitalization, financial inclusion, women's economic empowerment, and the transition to a lower carbon economic model will be instrumental. The extension of the current EFF arrangement will provide additional time for the incoming administration to design and implement reforms under the IMF-supported program."

Costa Rica: Selected Economic and Financial Indicators

	2019	2020	2021	2022	2023	2024	2025	2026	2027
			Projections						
Output and Prices			(Annual percentage change)						
Real GDP	2.4	-4.1	7.5	3.6	3.3	3.2	3.2	3.2	3.2
GDP deflator	2.6	0.2	2.0	3.3	3.4	3.1	3.0	3.0	3.0
Consumer prices (period average)	2.1	0.7	1.7	4.8	3.7	3.2	3.1	3.0	3.0
Savings and Investment			(In percent of GDP)						
Gross domestic saving	14.8	14.7	15.6	16.0	16.3	16.3	16.4	16.4	16.5
Gross domestic investment	16.1	15.8	18.9	19.1	19.2	19.2	19.1	19.0	19.0
External Sector									
Current account balance	-1.3	-1.1	-3.2	-3.1	-2.9	-2.8	-2.8	-2.6	-2.6
Trade balance	-6.0	-2.9	-4.9	-6.6	-7.4	-7.4	-7.3	-7.3	-7.3
Financial account balance	-2.0	-1.9	-3.2	-3.1	-2.9	-2.8	-2.7	-2.6	-2.5
Foreign direct investment, net	-4.2	-2.6	-5.5	-5.1	-5.0	-4.9	-4.8	-4.8	-4.7
Gross international reserves (millions of U.S. dollars)	8,937	7,232	6,921	8,611	9,081	9,951	9,957	10,478	11,278
External debt	47.6	50.6	52.2	58.0	58.3	59.0	58.0	57.0	56.1
Public Finances 1/									
Central government primary balance	-2.6	-3.8	-0.3	0.7	1.3	1.8	2.0	2.1	2.3
Central government overall balance	-6.7	-8.4	-5.2	-4.5	-3.6	-3.0	-2.5	-2.3	-2.0
Central government debt	56.4	67.2	68.5	68.6	68.3	67.5	66.3	65.0	63.4
Money and Credit									
Credit to the private sector (percent change)	-2.3	3.4	2.8	3.8	6.0	6.0	6.0	6.2	6.2
Monetary base 2/	7.1	8.3	7.9	8.0	8.2	8.3	8.4	8.3	8.4
Broad money	44.8	55.0	54.0	53.0	53.1	53.2	53.2	53.1	53.1
Memorandum Items									
Nominal GDP (billions of colones) 3/	37,832	36,356	39,832	42,592	45,464	48,342	51,352	54,541	57,927
GDP per capita (US$)	12,691	12,118	12,381	12,663	13,267	13,787	14,364	14,971	15,602
Unemployment rate	12.4	20.0	13.7	13.0	12.0	10.5	9.5	9.0	8.8

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

1/ For comparison purpose, starting from 2019, central government figures include public entities that are consolidated under the central government from 2021 onwards as required by Law 9524.

2/ We use a narrower definition of monetary base that includes only currency issued and required reserves.

3/ National account data reflect the revision of the benchmark year to 2017 for the chained volume measures, published in January 2021.

INTERNATIONAL MONETARY FUND

COSTA RICA

March 10, 2022

FIRST AND SECOND REVIEWS UNDER THE EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY, REQUEST FOR EXTENSION OF THE ARRANGEMENT, AND REPHASING OF PURCHASES

EXECUTIVE SUMMARY

Context. On March 1, 2021, the IMF Executive Board approved a 36-month arrangement under the Extended Fund Facility (EFF) with access of SDR 1.23749 billion (335 percent of quota, equivalent to US$1.778 billion) to support the country's response to the pandemic and its reform efforts toward strong, inclusive, and sustainable growth. The authorities' proactive response to the COVID-19 crisis, combined with sustained export performance, have supported a robust recovery. The outlook remains subject to downside risks, amid tighter global financial conditions, higher commodity prices, and the threat of new COVID variants.

Program performance. The EFF arrangement was ratified by the Legislative Assembly on July 19, 2021, as required by the Constitution. The authorities are making important progress with their economic reform program. All end-July and end-December quantitative performance criteria (PC) were met by comfortable margins. The end-August 2021 structural benchmark (SB) on the central bank law was met as were the end-December SBs on the centralization and digitalization of the social assistance cash programs and on the new Tax Compliance Improvement Plan. The SB on the Public Employment Bill was not met by end-May 2021 as envisaged; the bill was eventually approved by the Legislative Assembly in early March 2022. The end-December SB to publish the 2020 financial statements of three state-owned under International Financial Reporting Standards (IFRS) was not met due to reporting issues at two companies.

Focus of the Review. The review focused on the authorities' efforts to advance their fiscal consolidation plans, while strengthening fiscal institutions; the Central Bank of Costa Rica (BCCR)'s move towards a neutral stance, given the stronger inflation outlook; the supervisory efforts to strengthen financial oversight; the steps to mitigate the disproportionate impact of the pandemic on the most vulnerable and plans to capitalize on the economic and job opportunities from the transition to a lower carbon economy. To accommodate legislative delays in program implementation and provide additional time for the incoming administration to design and implement reforms under the EFF-supported program, the authorities requested an extension of the current arrangement and rephasing of access, together with the completion of the reviews.

Approved By
Nigel Chalk (WHD) and Martin Cerisola (SPR)

The team consisted of Manuela Goretti (head), Charlotte Lundgren, Alberto Behar, Nan Geng, Pedro Juarros, and Huidan Lin (all WHD), Miguel Pecho (FAD), Piyabha Kongsamut (MCM), Russell Green (SPR), Julia Bersch and Ivania Garcia Cascante (Resident Representative Office), with assistance from Heidi Canelas, Rozi Lamprakaki, and Cristhian Vera Avellan (all WHD), and Orlando Carvajal (Resident Representative Office). Discussions were held remotely from Washington, DC during September 22-October 6, 2021 and February 22-March 3, 2022. The team held virtual meetings with Costa Rica's President Alvarado, BCCR's President Cubero, Minister of Finance Villegas, Minister of Planning Garrido, and other senior government and financial sector officials, members of the Legislative Assembly, academics, private sector, civil society, and union representatives as well as other development partners. Pablo Moreno and Valerie Lankester (both OED) joined some of the meetings. Nigel Chalk (WHD) joined the concluding meetings.

CONTENTS

TABLES

ANNEXES

APPENDICES

CONTEXT

1. Costa Rica's proactive response to the pandemic, combined with sustained export performance, have supported a robust recovery. The authorities have been striking a careful balance between containing the virus and reopening the economy. Economic activity rebounded faster than expected, supported by sustained export growth and a robust domestic recovery. The Legislative Assembly ratified the EFF arrangement in July 2021,[1] confirming broad political support for the program. The end-December 2021 program targets were comfortably met, amid strong revenue overperformance and improving market conditions, and, despite some delays, the authorities made significant progress on their ambitious structural agenda.

2. Sustained policy efforts will be critical to secure macroeconomic stability and foster growth and job creation. The authorities are on track to meet the medium-term fiscal targets under the program, supported by strong revenue yields and spending discipline under the fiscal rule. The Public Employment Bill (PEB) will strengthen the efficiency and equity of government spending and amendments to the central bank law will enhance its autonomy and governance. Additional steps will be needed to further strengthen Costa Rica's tax system and social safety net.

3. Both presidential candidates have expressed their support for the objectives of the Fund-supported economic program. Rodrigo Chaves from the Social Democratic Progress Party and Jose Maria Figueres from the National Liberation Party will face a second-round presidential election on April 3, 2022. The new government is expected to take office on May 8, 2022, with a less fragmented Legislative Assembly than in the past, based on the February 6 election results.

RECENT DEVELOPMENTS

4. The country's well-established universal healthcare system and targeted containment measures have helped manage four COVID-19 waves. As of end-February 2022, 74 percent of the population were fully vaccinated, and 26 percent had received a booster dose. The authorities' goal is to fully vaccinate the eligible population, including children, and apply booster vaccines to vulnerable groups by end-2022.

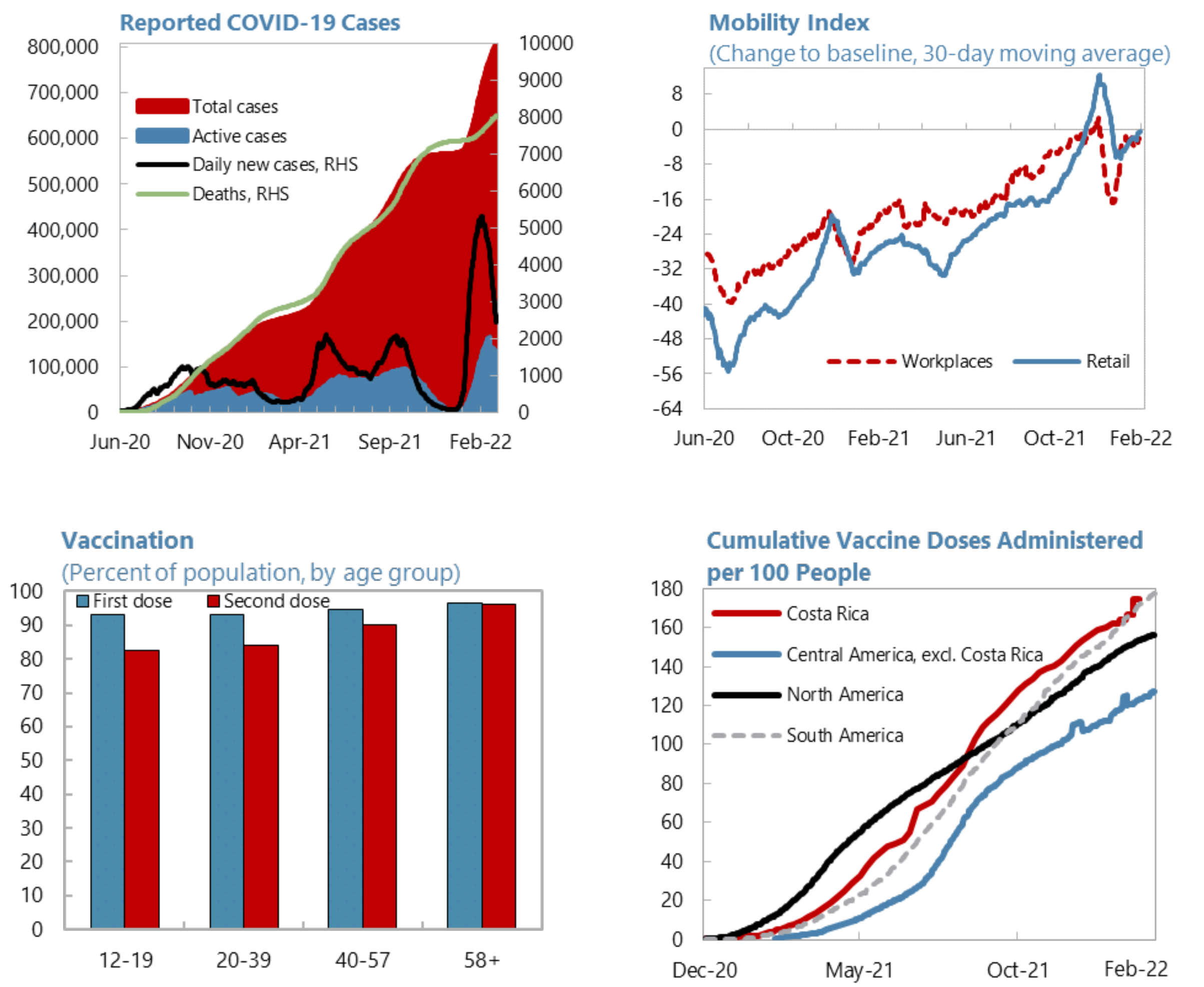
5. The Costa Rican economy is recovering faster than expected.

- *Real GDP* expanded by 12.1 percent (y-o-y) in Q3, with high frequency indicators continuing to point to strong growth in manufacturing, albeit with an uneven recovery in services (Figure 1).
- *Unemployment* came down significantly from a peak of 24 percent to 13.7 percent as of end-2021. Job creation in the informal and lower-skilled sectors is, however, lagging.

[1] As required by the Constitution for any financing that is deemed to be external borrowing by the government under domestic law.

- *Headline inflation* reached 4.9 percent (y-o-y) in February, driven by higher commodity prices. Core inflation rose to 3.8 percent (y-o-y).
- The *current account deficit* is expected to remain at around 3 percent of GDP in 2022. A strong export performance is being offset by weak tourism receipts and higher oil prices (Figure 2).
- *Financial conditions* have loosened due to a decline in sovereign spreads. FDI inflows have picked up, with new green-field investments. Portfolio outflows remain sizable (largely due to domestic pension funds diversifying into offshore assets).
- *International reserves* were US$6.8 billion at end-January or about 95 percent of the IMF's Assessing Reserve Adequacy (ARA) metric, amid increasing pressures from higher commodity prices and sustained portfolio outflows. The exchange rate depreciated by 4.6 percent against the U.S. dollar in 2021 (and 4.5 percent in real effective terms).

Costa Rica: COVID-19 Developments



Sources: Ministry of Health; Google Community Mobility Report; and IMF staff estimates.
Note: Active cases = total confirmed - total recovered - total deaths. Vaccination data as of February 28, 2022.

OUTLOOK AND RISKS

6. **The economic outlook has steadily improved during the course of 2021.** GDP growth is expected to have rebounded to 7.5 percent in 2021 (compared to 2.6 percent forecast at the time of the EFF request) and is projected at 3.6 percent in 2022. This reflects strong goods exports throughout the pandemic and a faster-than-expected recovery in tourism and domestic demand. After increasing to 4.8 percent in 2022, inflation is expected to return within the BCCR's tolerance band within a one- to two-year horizon. The current account deficit should adjust to around 2½ percent of GDP over the medium term.

7. **Risks remain to the downside, amid rising external pressures.** The successful vaccination campaign has led to a visibly smaller domestic impact of the COVID-19 shock. Nevertheless, a new pandemic wave triggered by more aggressive variants could depress external demand and derail the domestic recovery. This would negatively impact the fiscal position—with lower revenues and higher COVID-related spending—and increase vulnerabilities. Higher oil prices or a tightening of global financial conditions—amid concerns about geopolitical risks from the conflict between Russia and Ukraine (Annex I)—would hit confidence and weigh on growth. On the upside, a quick resolution of the pandemic and/or faster reform momentum would help boost investment and job creation.

PROGRAM PERFORMANCE AND POLICY DISCUSSIONS

A. Strengthening Fiscal Institutions

Background

8. **There was a sizable fiscal overperformance in 2021, supported by strong revenue yields and restrained spending.** The end-December fiscal targets were comfortably met (MEFP Table 1). The primary deficit was 0.3 percent of projected GDP (compared to 1.7 percent of GDP at the time of the EFF request). The strong overperformance was underpinned by robust revenues from a stronger economic recovery, some one-off factors,[2] better-than-expected yields from the 2018 tax reform,[3] and improving revenue administration. Spending, including COVID-related emergency spending of 0.3 percent of GDP, was well below that anticipated in the 2021 budget. Nonetheless, current spending breached the ceiling implied by the fiscal rule by about 0.3 percent of GDP.[4] This was a result of higher social, education, and other pandemic-related outlays (that were not included

[2] One-off revenues worth an estimated 0.7 percent of GDP include: (i) collections from public entities; (ii) partial recovery from the 2020Q2 tax moratorium; and (iii) higher income tax payments in March 2021 due to the 15-month fiscal year (the 2018 tax reform shifted the fiscal year from October-September to a calendar year basis).

[3] Yields from the implementation of the 2018 tax reform are estimated at 1.4 percent of GDP by 2021, higher by about 0.15 percent of GDP than previously anticipated, mainly on account of VAT reforms.

[4] Spending ceilings bases are automatically reduced by any extraordinary spending under the rule or breaches.

in the COVID-19 emergency decree), interest payments, and settlement of outstanding debt with the social security fund. The end-December debt target was also comfortably met.

Costa Rica: Central Government Operations, 2020-22										
	2020		2021				2022			
	Actual		EFF Request		Actual		EFF Request		Proj.	
	Billions of colones	Percent of GDP	Billions of colones	Percent of GDP	Billions of colones	Percent of GDP	Billions of colones	Percent of GDP	Billions of colones	Percent of GDP
Revenue	5,077	14.0	5,486	14.7	6,326	15.9	5,970	15.3	6,391	15.0
Expenditure	8,147	22.4	8,121	21.7	8,379	21.0	8,268	21.2	8,326	19.5
Non-interest	6,446	17.7	6,125	16.4	6,438	16.2	6,187	15.8	6,104	14.3
Interest	1,701	4.7	1,996	5.3	1,941	4.9	2,162	5.5	2,221	5.2
Primary balance	-1,368	-3.8	-640	-1.7	-112	-0.3	-136	-0.3	287	0.7
Overall balance	-3,069	-8.4	-2,635	-7.0	-2,052	-5.2	-2,298	-5.9	-1,934	-4.5
Memorandum item										
Central government debt 1/	24,420	67.5	27,100	72.5	26,794	67.3	29,744	76.3	28,919	67.9

Sources: Costa Rican authorities and IMF staff estimates.
1/ Outturn evaluated at program exchange rates.

Policy Discussion

9. The 2023 primary balance target of 1 percent of GDP is expected to be met. There has been insufficient consensus to date to approve revenue measures in the Legislative Assembly but, even without these measures, the program targets appear comfortably within reach. The 2022 budget targets a primary balance of 0.7 percent of GDP (see Table 2). Revenues are expected to remain solid, even after adjusting for one-offs and cyclical factors, supported by the accruing yields of the 2018 tax reform. Spending execution will be constrained by the fiscal rule, while making space for social programs and capital spending. If needed, the program would allow for up to 0.3 percent of GDP in 2022 in additional health and related spending in response to the pandemic.

Costa Rica: Authorities' Fiscal Package, 2021-23 (Cumulative change from 2020 in percent of GDP)						
	EFF Request			Proj.		
	2021	2022	2023	2021	2022	2023
Revenue measures:	**0.4**	**0.8**	**1.4**	**0.2**	**0.3**	**0.4**
2018 tax reform yields	0.1	0.1	0.3	0.2	0.3	0.4
New permanent measures	0.4	0.7	1.1	0.0	0.0	0.0
Expenditure measures:	**-1.3**	**-1.8**	**-2.3**	**-1.5**	**-2.9**	**-3.4**
Wage bill	-0.6	-0.8	-1.0	-0.6	-0.9	-1.3
Purchases of G&S	-0.1	-0.2	-0.3	-0.1	-0.2	-0.3
Current transfers	0.0	-0.5	-0.8	-0.3	-1.4	-1.7
o.w. Social assistance	0.1	0.1	0.1	0.0	0.0	0.1
Capital spending	-0.5	-0.3	-0.1	-0.5	-0.4	-0.2
Total structural measures	**1.7**	**2.5**	**3.7**	**1.7**	**3.2**	**3.8**
+ One-off measures	0.6	0.7	0.6	0.9	0.4	0.4
+ Cyclical impact/tax admin gains	0.1	0.4	0.6	0.8	0.9	0.9
Primary balance	**2.3**	**3.6**	**4.9**	**3.5**	**4.4**	**5.1**
Primary balance (Percent of GDP)	**-1.7**	**-0.3**	**1.0**	**-0.3**	**0.7**	**1.3**

Source: IMF staff estimates.

10. The Public Employment Bill, approved by the National Assembly in early March 2022, will help strengthen the equity and efficiency of government spending. This structural benchmark was not met by end-May 2021 due to legislative delays, including extensive consultations and constitutional reviews. The bill improves the fairness of public compensation, reduces the high public-private wage premium, and lessens the gender gap (Annex II). With IDB support, implementation plans for the introduction of a single pay spine and related regulations are expected to be finalized within 12 months from the bill's approval (proposed end-March 2023 SB).

11. The authorities are strengthening the social safety net. Supported by IMF TA, the National Treasury centralized and digitalized the payment system for cash transfer social-assistance programs (an end-December 2021 SB). The main institutions that administer social assistance programs have already started to channel transfers through the new IT platform (SUPRES). They also continue adopting SINIRUBE's targeting tools for benefit allocation, with World Bank support. These initiatives, once fully implemented, will significantly improve targeting, freeing resources for an expansion in the coverage and generosity of social transfer programs to eligible beneficiaries.

12. Reforms to improve the institutional framework for fiscal policy are proceeding, with support from IMF TA.[5]

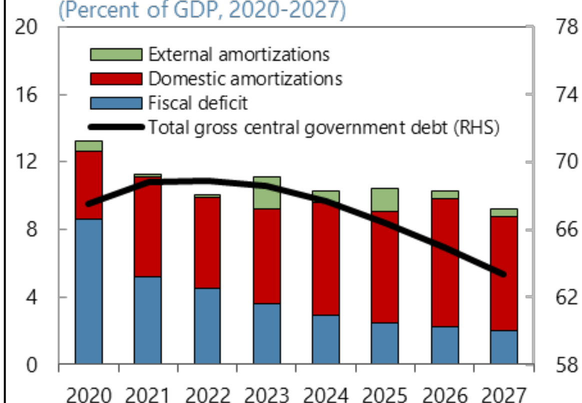
- **Revenue administration.** The authorities are stepping up their anti-tax evasion efforts focusing on the enforcement of recently approved tax reforms. Implementation of the new risk-based Tax Compliance Improvement Plan (end-December SB) is expected to reduce VAT and CIT compliance gaps. A new Customs Law, expected to be approved by end-March 2022, will help facilitate trade, deter fraud, and sustain revenue collection.

- **Public financial management.** The first Medium-Term Fiscal Framework (MTFF) for the CG was published in April 2021 (and updated in September 2021) with clearly defined deficit and debt objectives as well as an assessment of fiscal risks. Work is ongoing to expand the MTFF to the nonfinancial public sector (end-April 2022 SB). Efforts are also underway to operationalize the Fiscal Council and implement a plan to phase in gender budgeting (Box 1).

- **Public investment management.** Drawing on the recent Public Investment Management Assessment (PIMA), the authorities have identified priority actions to improve projects appraisal, selection and implementation as well as medium-term capital budget allocation. This will also support the development of a roadmap to strengthen climate-resilience infrastructure, in line with the recommendations of the PIMA climate module (¶30).

13. The debt outlook has improved but remains vulnerable to shocks. CG debt is expected to peak at 68½ percent of GDP in 2022, more than 7 percent of GDP lower than that at the time of the EFF request. The improvement in the debt trajectory reflects a combination of higher nominal GDP and fiscal savings. The debt path remains vulnerable to growth, exchange rate, interest rate, and contingent liability shocks (Annex III). To strengthen public debt management, the authorities created an Assets and Liabilities committee to oversee policy coordination, have published their Medium-Term Debt Management Strategy (MTDS), and are preparing a

Costa Rica: Gross Fiscal Financing Needs and Debt
(Percent of GDP, 2020-2027)



Sources: Ministry of Finance and IMF staff estimates.

[5] See Annex IV for the Country Strategy Note on Capacity Development Integration.

semi-annual plan for debt issuance. Efforts are underway to bring all government debt-related functions under a unified debt management office. The MTDS is being updated (end-April 2022 SB) to address risks associated with SOE debt and underpin the Annual Borrowing Plan.

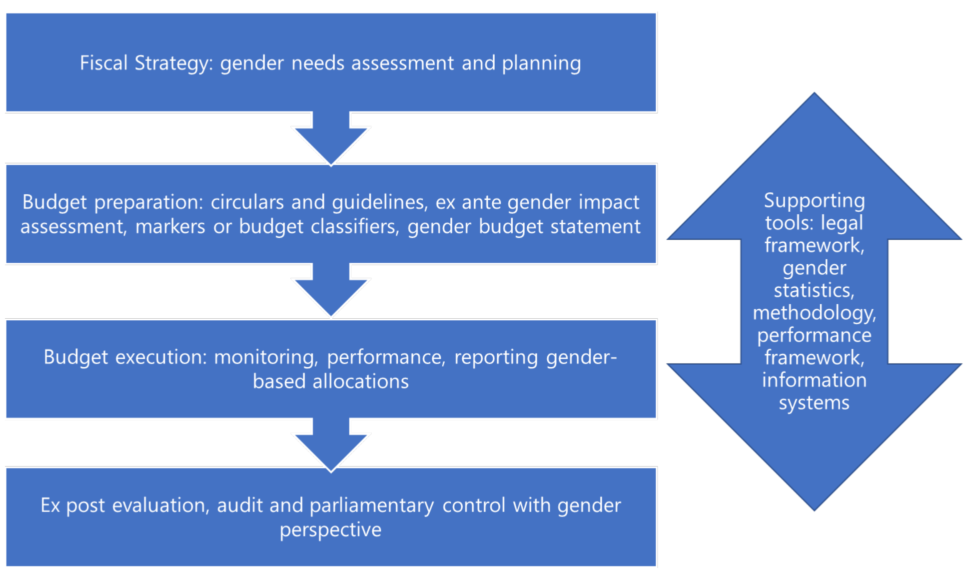
Box 1. Gender Budgeting for Costa Rica[1]

Gender budgeting (GB) uses fiscal policy and PFM to promote gender equality. GB introduces a gender lens throughout the budget process and helps governments understand the impact of expenditure and revenue policies on gender and operationalize policies that promote gender equality at all the stages of the budget cycle—preparation, execution, and control. GB introduces tools to translate gender-equality policies into budget allocations, hence it is key to holding governments accountable for their gender-related commitments.

International experiences suggest that the most successful GB efforts encompass both policy and PFM. Austria, Canada, Mexico, among others, show good practices in GB as they try to link policy objectives with gender budgeting tools, including gender impact assessments and budget markers or classifiers. These tools help to highlight the intended and unintended impact of new policies on gender and mark accordingly the relevant budget allocations. They can also help to develop a gender budget statement, which documents how the budget contributes to the gender-related policy objectives and it's implemented through appropriations to the relevant entities.

With support from IMF TA, the authorities have developed a plan to introduce GB. In Costa Rica, GB is expected to support the implementation of the Gender Parity Initiative aimed at increasing women's participation in the labor force and leadership as well as reducing the gender wage gap. With support from IMF TA, the authorities have identified an action plan to identify gender spending, establish adequate coordination mechanisms between the Ministry of Finance, Women's Ministry, sectoral entities, and decentralized and autonomous entities, and introduce new GB instruments such as budget markers, budget circulars, and gender budget statements.

A Roadmap for Gender Budgeting



[1] Prepared by Virginia Alonso and Laura Gores (both IMF).

14. The authorities continue to improve fiscal transparency and accountability. Most of the major non-financial SOEs are fully compliant with IFRS. However, the relevant end-December SB was not met due to partial IFRS compliance in their 2020 financial statements by two companies: *AyA* has committed to fully comply with IFRS standards in their 2021 financial statements and *CNP* will need to put in place a new accounting system for a smaller company in order to be compliant. Supported by the IDB, the Planning Ministry has rolled out a transparency portal, *Rendir Cuentas*, to provide information on COVID-related emergency assistance. The new public procurement law will enter into force by November 2022 and introduce a transparency and accountability framework for managing public purchases. The implementing regulation, published in early March, will ensure collection and publication of beneficial ownership information for awarded contracts.

15. Efforts to improve the efficiency of energy companies and further reduce electricity prices are underway. The national electricity company is restructuring its debt and pursuing a cost reduction plan. A recently approved bill will also simplify private participation in power generation from renewable sources.

16. Despite solid revenue outturns, there is scope to improve Costa Rica's tax system to make it more efficient and progressive. Staff plans to engage with the new administration at the time of the next review on a tax reform package to foster competitiveness and inclusive growth after the pandemic, with support from IMF TA. For example, more progressive personal income taxes, broader VAT bases, and fairer taxation of multinationals could make space for a more neutral taxation of corporate income.

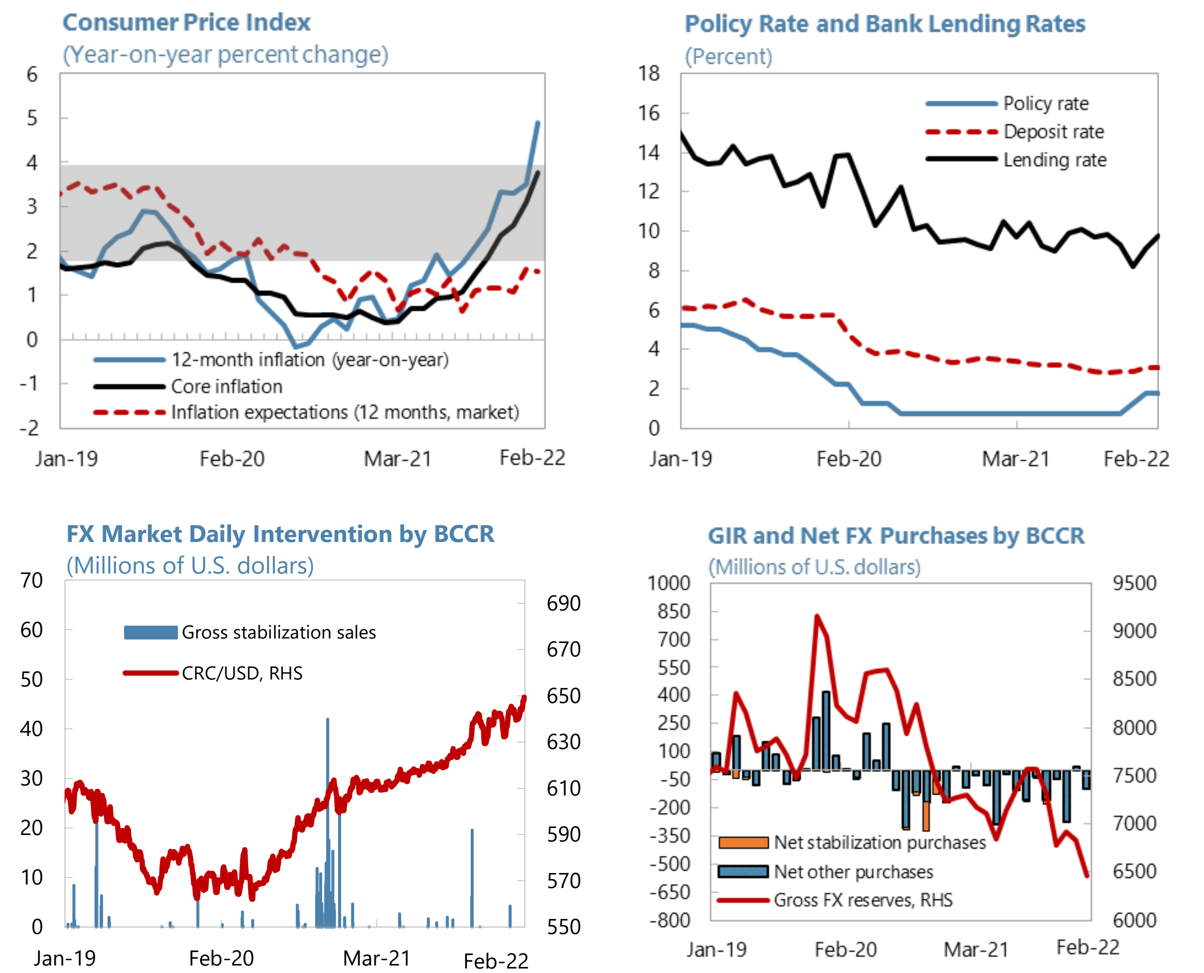
B. Safeguarding Monetary and Financial Stability

Background

17. Given a pickup in inflation, the BCCR has started a gradual withdrawal of monetary support. The inner band of the Monetary Policy Consultation Clause (MPCC) under the program—set at the time of the EFF request under a very different outlook for global price pressures—was breached in December (3.0 percent compared to 2.8 percent) and Fund staff held a consultation with the BCCR Board. The BCCR raised policy rates in December and January from 0.75 to 1.75 percent. Also, the medium-term repo facility (to provide additional liquidity support for on-lending to businesses and families hit hard by the pandemic) ended in mid-2021.

18. The end-December PC on net international reserves (NIR) was met by a comfortable margin, despite external pressures. Increasing imports, amid rising commodity prices, still-weak tourism receipts, and sizable portfolio investment outflows from local pension funds diversifying abroad were partially offset by a rebound in FDI and improving market conditions. The SDR allocation helped support international reserves. Net FX sales (of US$1.3 billion during 2021) were used to meet lumpy FX demand from the nonfinancial public sector (NFPS), as sustained BoP pressures constrained the BCCR's ability to offset them with FX purchases.

Costa Rica: Inflation, Interest Rate, and FX Market Developments



Sources: BCCR and IMF staff estimates.

19. The supervisors are unwinding COVID-related regulatory measures. Banks restructured roughly half of their loan portfolio to provide temporary relief to borrowers affected by the pandemic. Measures related to loan restructuring and asset classification were unwound in 2021, while the ability to use already-accumulated countercyclical provisions was extended through December 2022. A Guarantee Fund, aiming to support job retention in businesses hit hard by the pandemic (MEFP¶30), was approved by the Legislative Assembly and is expected to be soon implemented.

20. Preparedness efforts are ongoing to strengthen the resilience of the financial system to downside risks. Banks' regulatory capital adequacy ratio was 13.1 percent as of end-December 2021 (above the 10-percent regulatory minimum), with loan loss provisions of 4.3 percent of total loans. System-wide NPLs remain low at 2.3 percent. However, credit quality is expected to worsen over the coming months as a result of the expiration of COVID-related regulatory measures ("high risk" loans are reported at 14 percent of the total as of November, of which around 5 percent expected to be non-viable). In this context, the authorities have required banks to regularly assess borrowers' capacity to repay, estimate and provision for expected losses, while running stress tests and updating crisis preparedness plans.

Policy Discussion

21. **The BCCR's move towards a more neutral stance is warranted given the rise in inflation and in inflationary risks.** In the current uncertain external environment, the BCCR's data-dependent and forward-looking approach to monetary policy, in line with its inflation targeting framework, is even more critical. In response to the stronger inflation outlook, the BCCR should continue to raise the policy rate, and increase the tightening pace were inflationary pressures to persist. The program center targets have been updated to align them with the BCCR's inflation target (of 3 percent) to support the BCCR's communication efforts and help anchor inflation expectations. The central bank should continue its efforts to be clear and transparent about its outlook for inflation, risks around the outlook, and the implications for monetary policy.

22. **FX intervention by the BCCR remains limited to periods of market volatility.** The BCCR is required by law to meet all FX demand by non-financial public sector entities, but other FX sales are confined to addressing disorderly market conditions. To offset any FX sales to public sector entities—amid rising external pressures from higher commodity prices and tighter global financial conditions—and maintain adequate reserves, the BCCR should continue to opportunistically purchase FX in the market. Ongoing efforts to deepen the FX market, with IMF TA, include introducing FX swaps as a tool for BCCR participation in the FX market, resetting the net open FX position limits in line with international best practices, and promoting a legal reform to allow for more NFPS FX transactions to take place with private intermediaries.

23. **The BCCR is making good progress on the recommendations from the 2020 Safeguards Assessment.** Amendments to the BCCR Law were finalized and submitted to the MoF on August 31, 2021, meeting the relevant structural benchmark, to (i) clarify that the BCCR's main objective is to maintain low and stable inflation, (ii) provide for a clear allocation of functions among its decision-making bodies, (iii) strengthen its institutional, functional, personal, and financial autonomy, and (iv) enhance its transparency and accountability practices. The amendments are now expected to be submitted to the Legislative Assembly by end-December 2022 (proposed SB).

24. **The authorities' proactive monitoring of credit risks remains critical as temporary forbearance is unwound.** Supervisors should continue to closely follow loan performance as regulatory requirements are returned to pre-pandemic settings. Banks should be encouraged to draw on their countercyclical provisions, as needed, and ensure that capital buffers remain solid. The authorities appear on track with their plans for a phased adoption of Basel III. A roadmap to further enhance the legal framework for deposit insurance and bank resolution was adopted in June, with legal amendments expected to be submitted to the Assembly by end-March 2023. Efforts should continue to further disincentivize dollarization, including by revising the definition of unhedged borrowers and additional capital requirements (MEFP ¶32). Ongoing fiscal consolidation and debt management efforts are also expected to reduce banks' holdings of government securities.

Costa Rica: Proposed Amendments to the BCCR Law

Mandate	- Prioritize the BCCR's main objective of maintaining low and stable inflation and separate objectives from its function - Include the functions of lender of last resort in the event of a lack of liquidity and of compiling and producing statistics
Decision-making	- Clearly allocate policy formulation and oversight to the Board comprising a majority of non-executive members - Allocate the general executive management function to the Governor and strengthen collegiality under the current Presidential model - Include an Audit Committee comprising non-executive members from the Board of Directors
Institutional autonomy	- Explicitly prohibit: (i) government representatives from being members of the Board in any capacity; (ii) the BCCR and its decision-making bodies from seeking or taking instructions from a third party; and (iii) third parties, including the government, from influencing the BCCR's decision-making bodies
Functional autonomy	- Eliminate provisions that require prior authorization from external entities to carry out the BCCR's duties
Personal autonomy	- Include a double-veto procedure for the appointment and dismissal of the Governor - Broaden incompatibility requirements with respect to the decision-making bodies of the central bank - Strengthen the eligibility criteria for the Governor and Board members
Financial autonomy	- Include a dynamic profit distribution provision and explicitly prohibit distribution of unrealized gains - Explicitly prohibit the BCCR from conducting quasi-fiscal and developmental activities and other activities pertaining to the State - Establish a general framework authorizing the BCCR to perform operations to fulfill its functions
Transparency and accountability	- Provide for the legal basis of a modern internal audit function - Establish that the BCCR's financial statements must be audited annually by an external audit firm - Include provisions on the external auditor's appointment mechanism, selection criteria, terms, and rotation policy

Source: BCCR.

25. The authorities' financial inclusion plans involve facilitating access to their comprehensive payment system and increasing financial education. The authorities have simplified requirements for opening a bank account and launched a nationwide electronic payment system for public transportation. They are promoting digital financial services and financial innovation, while ensuring new technologies meet financial integrity, consumer protection, and financial stability requirements. A new bankruptcy law, which entered into force on December 1, 2021, should help with the restructuring of distressed firms.

26. The BCCR has developed a roadmap to integrate climate change considerations into the design of monetary and financial policies. The BCCR has started to identify data requirements and build a repository with climate-related information as a pre-requisite to develop its analytical capacity in this area and foster the proper pricing of climate-related risks. The central bank is working with the supervisory authorities, within their respective mandates, to obtain firm-level disclosures of climate-related risks with a view to eventually design regulatory and supervisory approaches to manage these risks (Box 2).

Box 2. Greening the Financial Sector in Costa Rica

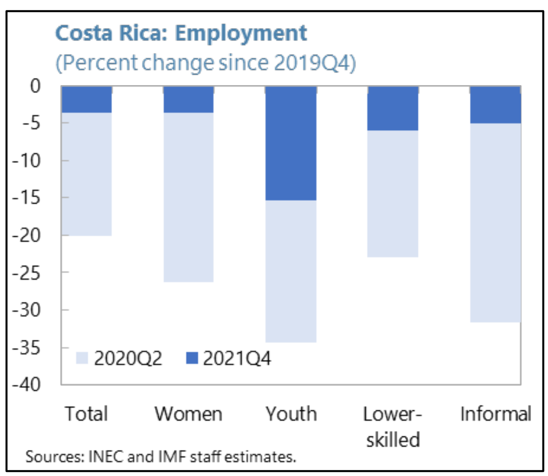
Climate change poses challenges to financial stability given their link to business disruption, property damage, and asset value impairment, as well as through a disorderly transition to a low-carbon economy. To address the impacts and risks related to climate change on its main objectives, the BCCR established the Group for Strategic Analysis of Climate Change (GAECC), comprising representatives of different departments of the BCCR, CONASSIF, and the superintendencies. With GAECC support, the BCCR has developed a roadmap for 2021-2024 with four key action areas:

- ***Establishing reliable and comparable data.*** Few financial entities in Costa Rica are incorporating mitigators (such as forward-looking provisions) to address well-recognized climate risks. This partly reflects a lack of reliable data and metrics to map climate vulnerabilities into financial risks. The BCCR is taking stock of the required data to adequately analyze the impact of climate change and aims to identify suitable indicators that can serve as a reference to monitor climate-related risks (that would be placed in a comprehensive information repository by end-2023).
- ***Strengthening modeling and analytical capacity for scenario analysis.*** The BCCR has developed an integrated economic and environmental model to conduct impact analysis of climate policies. The BCCR aims at being fully operational in the analysis of different climate scenarios combined with various mitigation and adaptation policies by end-2024.
- ***Promoting climate-change risk management in the financial system.*** The BCCR is assessing the interlinkages between climate-related and macro-financial variables as well as the risks to the financial system from climate change. The BCCR plans to incorporate the recommendations of the Network of Central Banks and Supervisors for Greening the Financial System in its "top-down" stress-testing methodologies by end-2022.
- ***Greening international reserves.*** The BCCR hopes to lead the search of an investment portfolio for its international reserves that is environmentally friendly and increases exposures to issuers with the best environmental performance. The BCCR aims to publish indicators of the "greenness" of its reserve holdings by end-2022.

C. Promoting an Equitable, Low Carbon Economy

Background

27. Women and the youth, especially in the lower-skilled and informal sectors, were the most adversely impacted by the pandemic. Job losses peaked at 25 percent for women and 35 percent for the young. Women also shouldered the burden of caring for children and other family members (leading to a significant drop in their labor force participation). Alongside the ongoing recovery and vaccination campaign, female employment has improved but employment of the young remains 15 percent below pre-pandemic levels. The number of



homes without internet access grew during the pandemic (from 13.7 percent in July 2019 to 18.7 percent in July 2021) and over one-third of students did not have internet access, creating significant inequalities in learning.

Policy Discussion

28. **Lessening incentives for informality and expanding digitalization will help promote inclusive growth.** The authorities have lowered the number of minimum wages and plan to continue simplifying the minimum wage structure over time. To incentivize formalization, a plan is under development to adjust the minimum contribution base for part-time workers to ease their burden (proposed end-June 2022 SB). Steps are being taken to increase the quality of education by enhancing teachers' digital training and securing equipment, especially for low-income families. Efforts are being made to strengthen integration between universities and firms and provide vocational programs in digital technologies and higher-skilled health care.

Costa Rica: Reform Strategy to Promote Inclusive Growth

Digitalization

- Strengthen digital infrastructure
- Develop National Telecommunications Plan, focusing on expanding access to the vulnerable

Education

- Develop digital learning and enhance teachers' digital capacity
- Enhance vocational training programs to meet evolving demand for specific skills

Financial Inclusion

- Broaden access to payment system
- Promote digital banking and financial innovation
- Introduce reporting of non-regulated credit providers to public credit registry

Formalization

- Reduce social security payments for part-time workers
- Reduce administrative burden for firms
- Streamline minimum wage structure

Gender

- Develop Gender Budgeting
- Implement National Care Plan and expand childcare services
- Introduce and expand paternity and maternity leave

Social Safety Net

- Strengthen coverage and targeting of social assistance programs
- Digitalize and centralize cash payment system

Sources: Costa Rican authorities and IMF staff.

29. **To reduce the burden of family care, a National Care Plan was launched in March 2021 to overcome gaps in coverage and quality and provide innovative services.** The authorities aim

to provide home care support to caregivers to allow them to enter (or remain in) formal employment. Monetary transfers are being considered for caregivers living in extreme poverty and the authorities are expanding childcare services for low-income households. The PEB extends maternity leave by two months (in specific cases), introduces a one-month paternity leave, and provides paid leave to care for a family member (through reduced working hours for up to one year). The authorities' gender budgeting plan is expected to support female labor force participation.

30. The authorities are pressing ahead with their efforts to adapt to climate change.[6] The authorities have developed a National Adaptation Plan and have created climate risk maps for 23 cantons (with coverage of all 82 cantons by end-March 2023). A roadmap to enhance infrastructure resilience to climate change (an end-September 2022 SB) is under development, with support from the WB. Updated methodological guidelines for the preparation and appraisal of public investment projects were recently issued to incorporate information on the exposure and resilience of public works to extreme weather events. The authorities are implementing the recommendations of the recent PIMA climate module to strengthen institutional readiness to address climate-related risks (through infrastructure planning and investment and development of relevant institutions).

31. The National Decarbonization Plan continues to guide the authorities' ambitious goal of fully decarbonizing the economy by 2050. To reduce emissions from transportation, the authorities have established a concessionary tariff for electricity supply to electric-bus charging centers and are developing a revenue-neutral feebate scheme to promote low-emission vehicles. The authorities' goals for a "blue" (coastal) and "green" (regenerative agriculture and forestry) economy are aimed at ensuring conservation and expanding ecotourism. In this context, Costa Rica—who was also recently awarded the Earthshot prize for its conservation efforts—is receiving around US$110 million from the Green Climate Fund and Forest Carbon Partnership Facility to support continued reforestation and ecosystem conservation.

PROGRAM MODALITIES

32. Program conditionality has been updated as follows:

- **Quantitative targets.** New PCs and ITs have been proposed (MEFP, Table 1). Given the still-high uncertainty surrounding the pandemic, the adjustors to the primary balance and debt targets for additional COVID-related emergency spending have been extended to 2022. New MPCC targets, including for the existing end-March 2022 target, have been proposed, centered on the BCCR's 3 percent inflation target.

[6] See Annex IX on "Costa Rica's Climate Change Response" in the 2021 Article IV Consultation and EFF Request Staff Report.

- **Structural benchmarks.** New SBs have been proposed to implement the approved PEB, submit to the Legislative Assembly amendments to the BCCR law, and adjust social security contributions for part-time workers (Table 10).

33. The authorities have requested a 5-month extension of the EFF arrangement and a rephasing of access. To accommodate legislative delays in program implementation and to provide additional time for the incoming administration to design and implement reforms under the EFF-supported program, the authorities are requesting an extension of the current arrangement until July 31, 2024, and a rephasing of access (shifting SDR 103.115 million from each of the first- and second-review purchases to a new sixth review, see Table 8 and 9). The proposed rephasing is consistent with the duration of the extended arrangement as ratified by the Costa Rica Legislative Assembly in July 2021.

Costa Rica: Program Financing

(In millions of U.S. dollars)

	2022	2023	2024
Financing need	2,288	1,938	1,224
Reserve accumulation	1,690	470	870
Underlying BOP need 1/	598	1,468	354
Official multilateral financing	2,288	1,938	1,224
IMF	582	589	297
Other multilateral creditors	1,705	1,349	928
World Bank	426	369	335
Inter-American Development Bank (IDB)	613	350	353
CAF Development Bank for Latin America	50	500	0
Central American Bank for Economic Integration (CABEI)	617	130	239
Unidentified financing	0	0	0
Memorandum items:			
Capital market access	1,000	1,000	1,000
Gross international reserves	8,611	9,081	9,951
In percent of the ARA metric	106	107	111

Source: IMF staff estimates.

1/ Net of private sector and bilateral financing.

34. Capacity to repay remains adequate and the program is fully financed. Access under the EFF is helping Costa Rica meet its sizable balance-of-payments needs and will continue to be used for direct budget support. The program remains fully financed (with firm financing commitments over the next 12 months and good prospects thereafter). The Fund's exposure is relatively low, with outstanding Fund credit peaking at 2.7 percent of GDP or 6.5 percent of exports (of goods and services) in 2023 (Table 7).

35. The program remains subject to downside risks, including from a worsening of the pandemic or higher external pressures, amid rising geo-political tensions (Annex I). The program, however, has the flexibility to accommodate such negative shocks. The authorities stand ready to take additional measures as needed to achieve their program goals. A return to international bond markets is planned but additional financing could be mobilized domestically and from regional partners in the event that downside risks were to materialize.

STAFF APPRAISAL

36. The authorities' proactive response to the pandemic, including a vigorous vaccination campaign, and sustained export performance have supported a robust recovery in Costa Rica. Nonetheless, the threat of new COVID variants as well as higher commodity prices and tighter global financial conditions, including from rising geo-political tensions, pose important downside risks to Costa Rica's economic outlook.

37. **The authorities have made important progress under the EFF-supported program.** The end-December 2021 targets under the program were comfortably met. Despite some legislative delays due to extensive consultations and constitutionality reviews, the authorities were able to strengthen social safety nets and improve the efficiency of the public administration.

38. **Sustained fiscal consolidation through revenue mobilization and prudent spending under the fiscal rule remains a priority.** The authorities delivered a strong fiscal overperformance in 2021. The fiscal position has been bolstered by revenue mobilization efforts from the 2018 tax reform, improved tax administration, and prudent spending under the fiscal rule even as more resources have been allocated to support the vulnerable and respond to the pandemic. Nevertheless, further efforts are needed to improve the tax system to make it more equitable, supporting a balanced reduction of the fiscal deficit and ensuring a more sustainable path for public debt over the medium term.

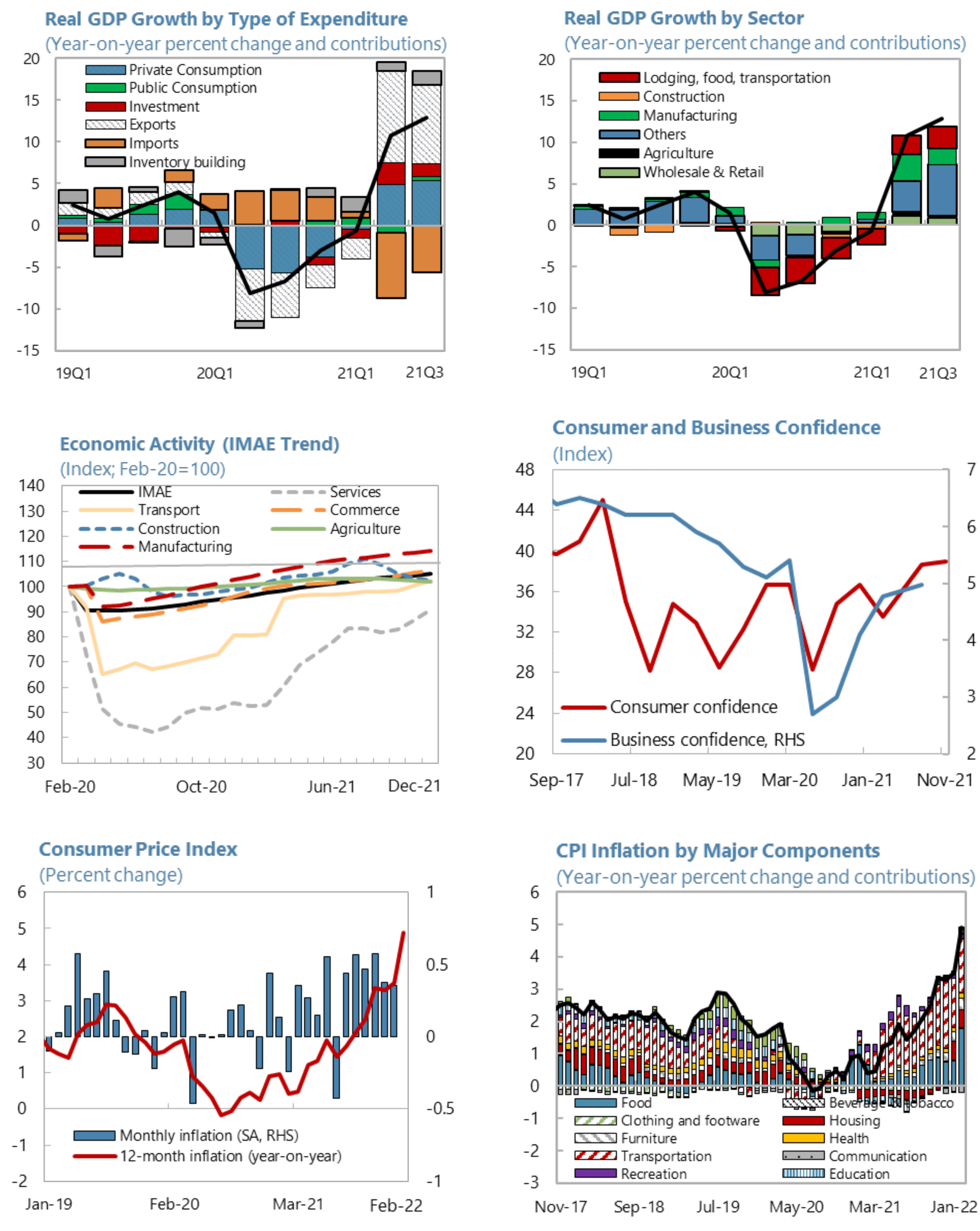
39. **The BCCR's ongoing withdrawal of monetary accommodation is warranted given the rise in inflation and in inflationary risks.** In the current uncertain external environment, the BCCR's data-dependent and forward-looking approach to monetary policy, focused on ensuring low and stable inflation as its primary objective, is even more critical. In response to the stronger inflation outlook, the BCCR should continue to raise the policy rate, and increase the tightening pace were inflationary pressures to persist. Continued clear and transparent communication and exchange rate flexibility will support these efforts. Ongoing steps to enhance the central bank law will underscore the BCCR's operational autonomy and governance.

40. **The financial system has shown resilience throughout the pandemic due to supportive monetary policy and a proactive approach to monitoring risks, running stress tests, and updating contingency plans**. Basel III requirements are being phased in a systematic way, giving banks adequate time to adjust to the new regime. Ongoing efforts to enhance the crisis management framework and incentivize de-dollarization remain critical and will further benefit the financial system.

41. **The authorities should press ahead with their ambitious agenda to promote an equitable, low-carbon economy.** The pandemic has brought Costa Rica's inequality challenges to the forefront. Ongoing efforts to support the most vulnerable, incentivize formal employment, pursue women's economic empowerment, increase digitalization, and transition to a lower carbon economic model will be instrumental to achieving inclusive and green economy that creates high quality jobs for all Costa Ricans.

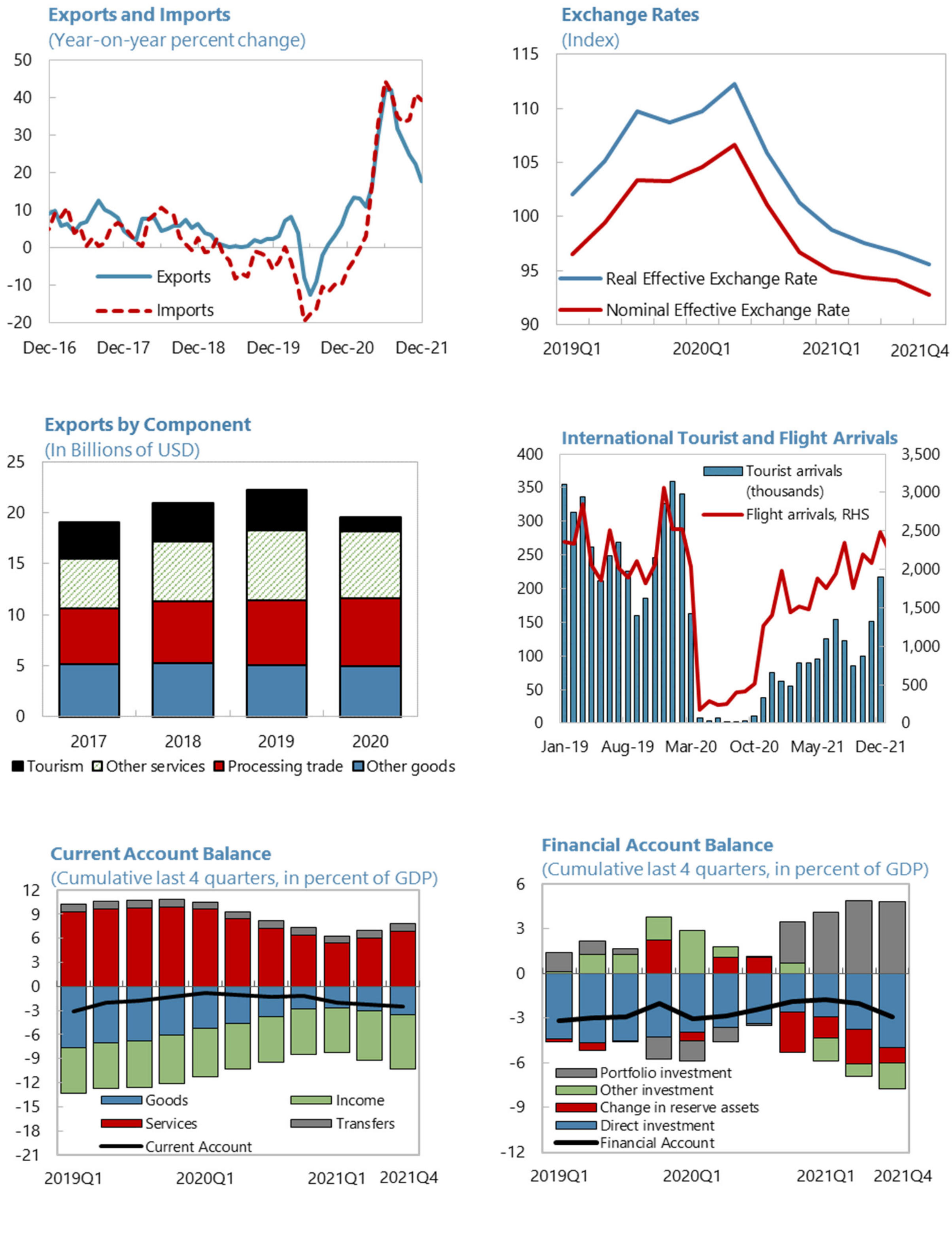
42. **Staff supports the completion of the first and second reviews, the extension of the arrangement, and rephasing of access.** There has been important progress to date and the authorities have demonstrated their commitment to strong policies and reforms.

Figure 1. Costa Rica: Real Sector Developments



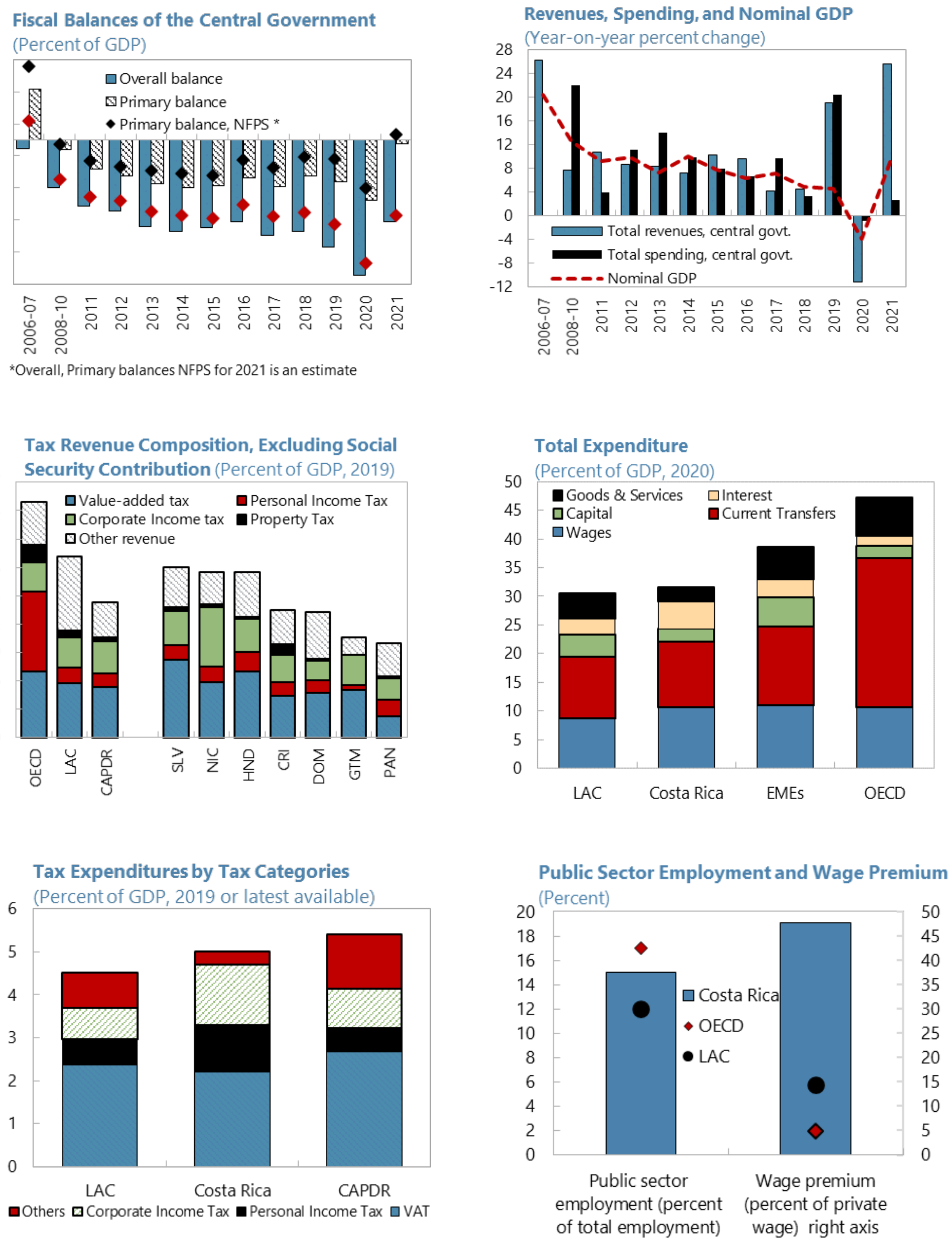
Sources: National authorities and IMF staff estimates.

Figure 2. Costa Rica: External Sector Developments



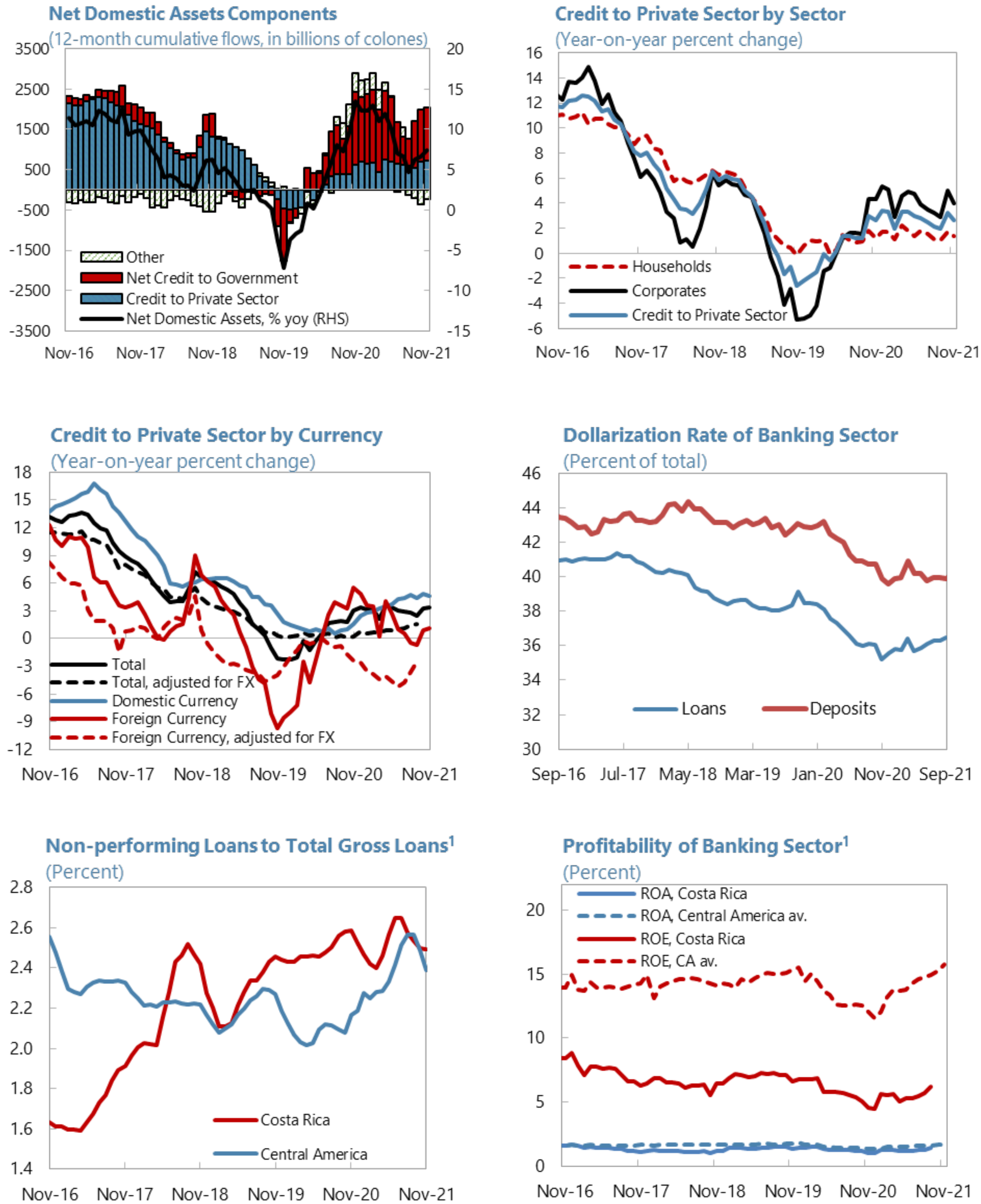
Sources: National authorities and IMF staff estimates.

Figure 3. Costa Rica: Fiscal Sector Developments



Sources: National authorities; World Bank April 2019 Costa Rica Public Finance Review; and IMF staff estimates.

Figure 4. Costa Rica: Monetary and Financial Sector Developments



Sources: National authorities and IMF staff estimates.

[1] Central America (CA average) includes El Salvador, Guatemala, and Honduras.

Table 1. Costa Rica: Selected Economic and Financial Indicators

					Projections								
	2017	2018	2019	2020	2021 EFF request	2021	2022 EFF request	2022	2023	2024	2025	2026	2027
National Income					(Annual percentage change)								
Real GDP	4.2	2.6	2.4	-4.1	2.6	7.5	3.3	3.6	3.3	3.2	3.2	3.2	3.2
Domestic demand	3.5	1.9	0.2	-3.6	2.4	6.7	2.8	2.4	2.7	3.0	3.0	3.0	3.1
Consumption	4.8	1.7	2.5	-3.8	1.4	4.7	1.6	2.8	2.5	2.7	2.6	2.8	2.8
Private	5.6	1.9	1.7	-5.0	2.0	5.7	2.3	3.6	3.2	3.2	3.2	3.2	3.2
Public	2.0	0.6	5.9	0.6	-0.8	1.1	-0.9	-0.7	-0.4	0.5	0.4	1.3	1.4
Gross fixed capital formation	0.1	1.6	-8.2	-1.7	3.8	7.8	4.5	4.3	5.4	5.2	5.1	5.0	5.0
Exports of goods and nonfactor services	7.0	4.9	4.3	-10.9	8.4	17.6	7.8	9.2	7.6	6.2	5.9	5.4	5.2
Imports of goods and nonfactor services	5.0	2.9	-2.3	-10.2	8.2	16.1	6.4	6.2	6.3	6.1	5.7	5.3	5.4
					(Contributions to real GDP growth)								
Domestic demand	3.5	1.9	0.2	-3.5	2.4	6.5	2.7	2.3	2.5	2.8	2.8	2.8	2.9
Consumption	3.9	1.4	2.0	-3.1	1.2	3.8	1.3	2.2	1.9	2.1	2.0	2.2	2.2
Gross domestic investment	-0.4	0.6	-1.8	-0.4	1.3	2.7	1.4	0.1	0.6	0.7	0.8	0.6	0.8
of which: Inventory changes	-0.4	0.3	-0.3	-0.1	0.6	1.4	0.6	-0.6	-0.3	-0.2	-0.1	-0.2	-0.2
Net exports	0.6	0.7	2.2	-0.6	0.2	0.9	0.6	1.2	0.7	0.3	0.4	0.3	0.2
Prices					(Annual percentage change)								
GDP deflator	2.9	2.2	2.6	0.2	1.4	2.0	1.0	3.3	3.4	3.1	3.0	3.0	3.0
Consumer prices (period average)	1.6	2.2	2.1	0.7	1.2	1.7	1.1	4.8	3.7	3.2	3.1	3.0	3.0
Consumer prices (end of period)	2.6	2.0	1.5	0.9	1.2	3.3	0.9	4.4	3.4	3.2	3.1	3.0	3.0
Savings and Investment					(In percent of GDP)								
Savings	18.1	18.4	16.1	15.8	16.5	18.9	17.5	19.1	19.2	19.2	19.1	19.0	19.0
Domestic savings	14.4	15.4	14.8	14.7	13.3	15.6	14.5	16.0	16.3	16.3	16.4	16.4	16.5
Private sector	16.4	17.9	17.5	20.5	17.2	18.6	16.9	18.1	17.2	16.7	16.3	16.2	16.0
Public sector	-2.0	-2.5	-2.7	-5.8	-3.9	-3.0	-2.4	-2.1	-0.9	-0.4	0.1	0.2	0.5
External savings	3.6	3.0	1.3	1.1	3.2	3.2	3.0	3.1	2.9	2.8	2.8	2.6	2.6
Gross domestic investment	18.1	18.4	16.1	15.8	16.5	18.9	17.5	19.1	19.2	19.2	19.1	19.0	19.0
Private sector	15.3	16.2	13.2	13.7	14.4	17.1	15.1	17.0	17.0	16.9	16.8	16.7	16.6
Public sector	2.8	2.1	2.9	2.1	2.1	1.8	2.4	2.1	2.3	2.2	2.3	2.3	2.4
External Sector													
Current account balance	-3.6	-3.0	-1.3	-1.1	-3.2	-3.2	-3.0	-3.1	-2.9	-2.8	-2.8	-2.6	-2.6
Trade balance	-7.2	-7.4	-6.0	-2.9	-4.8	-4.9	-6.0	-6.6	-7.4	-7.4	-7.3	-7.3	-7.3
Services	7.9	8.9	9.8	6.4	6.6	7.2	7.9	8.9	9.9	10.0	10.2	10.3	10.5
Capital account balance	0.1	0.0	0.0	0.0	0.1	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Financial account balance	-4.0	-3.5	-2.0	-1.9	-3.2	-3.2	-2.9	-3.1	-2.9	-2.8	-2.7	-2.6	-2.5
Foreign direct investment, net	-4.4	-3.9	-4.2	-2.6	-3.2	-5.5	-3.7	-5.1	-5.0	-4.9	-4.8	-4.8	-4.7
Gross international reserves (millions of U.S. dollars)	7,150	7,501	8,937	7,232	8,004	6,921	8,956	8,611	9,081	9,951	9,957	10,478	11,278
-as percent of ARA metric	119.6	118.3	131.4	104.5	111.7	95.2	114.3	105.5	107.5	110.8	107.7	109.2	116.4
-in months of next year's imports	4.2	4.4	6.0	3.9	4.6	3.3	4.7	3.7	3.7	3.9	3.7	3.7	4.0
External debt	44.5	46.4	47.6	50.6	59.1	52.2	61.5	58.0	58.3	59.0	58.0	57.0	56.1
Real effective exchange rate, avg. (percent change)	-4.6	-2.6	0.6	0.8	...	-8.4	...	...	...	...	...	...	...
Public Finances 1/													
Central government primary balance	-2.9	-2.2	-2.6	-3.8	-1.7	-0.3	-0.3	0.7	1.3	1.8	2.0	2.1	2.3
Central government overall balance	-6.0	-5.7	-6.7	-8.4	-7.0	-5.2	-5.9	-4.5	-3.6	-3.0	-2.5	-2.3	-2.0
Central government debt	47.1	51.8	56.4	67.2	72.5	68.5	75.0	68.6	68.3	67.5	66.3	65.0	63.4
Money and Credit													
Credit to the private sector (percent change)	8.5	6.3	-2.3	3.4	6.1	2.8	6.4	3.8	6.0	6.0	6.0	6.2	6.2
Monetary base 2/	8.0	7.8	7.1	8.3	8.6	7.9	8.8	8.0	8.2	8.3	8.4	8.3	8.4
Broad money	46.5	45.3	44.8	55.0	52.5	54.0	51.7	53.0	53.1	53.2	53.2	53.1	53.1
Memorandum Items													
Nominal GDP (billions of colones) 3/	34,344	36,015	37,832	36,356	37,388	39,832	39,004	42,592	45,464	48,342	51,352	54,541	57,927
Output gap (as percent of potential GDP)	1.1	1.1	0.2	-3.4	-3.0	-0.2	-1.4	-0.1	0.1	0.1	0.1	0.0	0.0
GDP per capita (US$)	12,185	12,429	12,691	12,118	11,803	12,381	12,315	12,663	13,267	13,787	14,364	14,971	15,602
Unemployment rate	9.3	12.0	12.4	20.0	16.0	13.7	14.0	13.0	12.0	10.5	9.5	9.0	8.8

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

1/ As of January 2021, the CG definition has been expanded to include 51 public entities as per Law 9524. Data are adjusted back to 2019 for comparability.

2/ Includes currency issued and required reserves.

3/ National account data reflect the revision of the benchmark year to 2017 for the chained volume measures, published in January 2021.

Table 2. Costa Rica: Central Government Balance[1/]

							Projections						
	2017	2018	2019	2020	2021 EFF request	2021	2022 EFF request	2022	2023	2024	2025	2026	2027
						(In billions of colones)							
Revenue	**4,560**	**4,767**	**5,676**	**5,077**	**5,486**	**6,326**	**5,970**	**6,391**	**6,877**	**7,316**	**7,750**	**8,210**	**8,723**
Tax revenue	4,390	4,567	4,940	4,385	4,741	5,566	5,284	5,710	6,168	6,567	6,959	7,376	7,843
Nontax revenue[2/]	170	199	735	693	745	760	685	681	709	749	791	834	880
Expenditure	**6,611**	**6,830**	**8,223**	**8,147**	**8,121**	**8,379**	**8,268**	**8,326**	**8,510**	**8,752**	**9,027**	**9,461**	**9,863**
Current noninterest	4,907	5,096	5,803	5,781	5,562	5,839	5,422	5,349	5,377	5,526	5,685	5,937	6,151
Wages	2,290	2,395	2,613	2,612	2,589	2,624	2,610	2,664	2,695	2,736	2,759	2,833	2,909
Goods and services	217	224	327	337	351	342	324	303	307	322	344	366	391
Transfers	2,400	2,477	2,863	2,832	2,622	2,874	2,488	2,381	2,375	2,467	2,582	2,737	2,851
Interest[3/]	1,054	1,254	1,553	1,701	1,996	1,941	2,162	2,221	2,242	2,284	2,302	2,406	2,482
Capital	650	480	867	665	564	599	684	756	892	943	1,040	1,117	1,230
Primary balance	**-997**	**-810**	**-994**	**-1,368**	**-640**	**-112**	**-136**	**287**	**609**	**848**	**1,025**	**1,156**	**1,342**
Overall Balance	**-2,051**	**-2,064**	**-2,547**	**-3,069**	**-2,635**	**-2,052**	**-2,298**	**-1,934**	**-1,633**	**-1,436**	**-1,277**	**-1,250**	**-1,140**
Total Financing	2,068	1,999	2,494	3,388	2,635	2,178	2,298	1,934	1,633	1,436	1,277	1,250	1,140
External (net)	62	150	1,119	724	1,713	713	1,755	2,256	1,252	1,196	328	747	855
Domestic (net)	2,006	1,849	1,376	2,665	922	1,465	543	-322	381	240	949	504	284
Unidentified financing	0	0	0	0	0	0	0	0	0	0	0	0	0
Central government debt	**16,163**	**18,670**	**21,347**	**24,420**	**27,100**	**27,272**	**29,241**	**29,215**	**31,068**	**32,648**	**34,058**	**35,448**	**36,735**
External	3,468	3,836	4,765	5,898	7,546	6,779	9,198	9,040	10,445	11,746	12,175	13,029	14,001
Domestic	12,695	14,834	16,582	18,522	19,554	20,493	20,043	20,174	20,623	20,902	21,883	22,419	22,734
Other debt (multilateral financing)	0	0	0	0	0	0	0	0	0	0	0	0	0
						(In percent of GDP)							
Revenue	**13.3**	**13.2**	**15.0**	**14.0**	**14.7**	**15.9**	**15.3**	**15.0**	**15.1**	**15.1**	**15.1**	**15.1**	**15.1**
Tax revenue	12.8	12.7	13.1	12.1	12.7	14.0	13.5	13.4	13.6	13.6	13.6	13.5	13.5
Nontax revenue[2/]	0.5	0.6	1.9	1.9	2.0	1.9	1.8	1.6	1.6	1.5	1.5	1.5	1.5
Expenditure	**19.2**	**19.0**	**21.7**	**22.4**	**21.7**	**21.0**	**21.2**	**19.5**	**18.7**	**18.1**	**17.6**	**17.3**	**17.0**
Current noninterest	14.3	14.2	15.3	15.9	14.9	14.7	13.9	12.6	11.8	11.4	11.1	10.9	10.6
Wages	6.7	6.6	6.9	7.2	6.9	6.6	6.7	6.3	5.9	5.7	5.4	5.2	5.0
Goods and services	0.6	0.6	0.9	0.9	0.9	0.9	0.8	0.7	0.7	0.7	0.7	0.7	0.7
Transfers	7.0	6.9	7.6	7.8	7.0	7.2	6.4	5.6	5.2	5.1	5.0	5.0	4.9
Interest[3/]	3.1	3.5	4.1	4.7	5.3	4.9	5.5	5.2	4.9	4.7	4.5	4.4	4.3
Capital	1.9	1.3	2.3	1.8	1.5	1.5	1.8	1.8	2.0	2.0	2.0	2.0	2.1
Primary balance	**-2.9**	**-2.2**	**-2.6**	**-3.8**	**-1.7**	**-0.3**	**-0.3**	**0.7**	**1.3**	**1.8**	**2.0**	**2.1**	**2.3**
Overall Balance	**-6.0**	**-5.7**	**-6.7**	**-8.4**	**-7.0**	**-5.2**	**-5.9**	**-4.5**	**-3.6**	**-3.0**	**-2.5**	**-2.3**	**-2.0**
Total Financing	**6.0**	**5.5**	**6.6**	**9.3**	**7.0**	**5.5**	**5.9**	**4.5**	**3.6**	**3.0**	**2.5**	**2.3**	**2.0**
External (net)	0.2	0.4	3.0	2.0	4.6	1.8	4.5	5.3	2.8	2.5	0.6	1.4	1.5
Domestic (net)	5.8	5.1	3.6	7.3	2.5	3.7	1.4	-0.8	0.8	0.5	1.8	0.9	0.5
Unidentified financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Central government debt	**47.1**	**51.8**	**56.4**	**67.2**	**72.5**	**68.5**	**75.0**	**68.6**	**68.3**	**67.5**	**66.3**	**65.0**	**63.4**
External	10.1	10.7	12.6	16.2	20.2	17.0	23.6	21.2	23.0	24.3	23.7	23.9	24.2
Domestic	37.0	41.2	43.8	50.9	52.3	51.4	51.4	47.4	45.4	43.2	42.6	41.1	39.2
Other debt (unidentified financing)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:													
Non-interest expenditure growth (percent)													
in nominal terms	8.2	0.4	19.6	-3.4	-6.3	-0.1	-0.3	-5.2	2.7	3.2	4.0	4.9	4.6
in real terms	6.4	-1.8	17.2	-4.1	-7.4	-1.8	-1.4	-9.5	-1.0	0.0	0.8	1.8	1.6
Nominal GDP (billions of colones)	34,344	36,015	37,832	36,356	37,388	39,832	39,004	42,592	45,464	48,342	51,352	54,541	57,927

Sources: Ministry of Finance and IMF staff estimates.

1/ As of January 2021, the CG definition has been expanded to include 51 public entities as per Law 9524. Data are adjusted back to 2019 for comparability.

2/ Before 2019, transfers to the Social development and Family Transfers Fund (FODESAF) are recorded in net terms.

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

Table 3. Costa Rica: Balance of Payments

	2017	2018	2019	2020	2021 EFF request	Est. 2021	2022 EFF request	Projections 2022	2023	2024	2025	2026	2027
						(In millions of U.S. dollars)							
Current Account	**-2,189**	**-1,867**	**-824**	**-707**	**-1,976**	**-2,079**	**-1,915**	**-2,055**	**-2,048**	**-2,093**	**-2,140**	**-2,161**	**-2,205**
Goods and services balance	393	919	2,424	2,224	1,083	1,475	1,269	1,515	1,739	1,961	2,247	2,461	2,736
Trade balance	-4,367	-4,620	-3,868	-1,779	-2,932	-3,125	-3,847	-4,371	-5,198	-5,424	-5,657	-5,990	-6,276
Export of goods (f.o.b.)	10,811	11,730	11,831	11,991	12,253	14,795	12,896	16,076	17,060	17,961	18,928	19,881	20,910
Import of goods (f.o.b.)	15,178	16,350	15,700	13,770	15,185	17,921	16,743	20,447	22,259	23,384	24,585	25,870	27,186
Services balance	4,760	5,539	6,292	4,003	4,015	4,600	5,116	5,886	6,938	7,385	7,903	8,451	9,012
Of which: Travel balance	2,612	2,931	2,953	1,085	1,202	997	2,245	2,021	3,015	3,211	3,336	3,462	3,607
Exports of services	8,598	9,751	10,906	8,005	7,570	9,072	9,179	10,786	12,467	13,191	13,966	14,810	15,667
Imports of services	3,837	4,212	4,614	4,002	3,555	4,472	4,063	4,901	5,529	5,806	6,063	6,359	6,655
Primary Income	-3,161	-3,344	-3,830	-3,499	-3,566	-4,130	-3,703	-4,202	-4,449	-4,750	-5,116	-5,385	-5,739
Secondary Income	579	558	582	568	507	576	519	633	662	696	729	763	798
Capital Account	**41**	**28**	**32**	**17**	**37**	**19**	**40**	**21**	**23**	**25**	**28**	**30**	**33**
Financial Account	**-2,445**	**-2,203**	**-1,268**	**-1,199**	**-1,940**	**-2,061**	**-1,875**	**-2,035**	**-2,025**	**-2,068**	**-2,112**	**-2,130**	**-2,171**
Public sector	-222	-790	-1,002	401	-2,348	-274	-2,011	-2,282	-913	-1,286	-362	-769	-1,037
Private sector	-1,805	-1,802	-1,658	154	-364	-1,469	-816	-1,442	-1,582	-1,652	-1,756	-1,882	-1,935
Foreign direct investment, net	-2,652	-2,434	-2,695	-1,644	-1,982	-3,524	-2,388	-3,413	-3,521	-3,608	-3,756	-3,923	-4,074
Other private sector flows	847	631	1,037	1,799	1,618	2,055	1,572	1,971	1,939	1,956	2,000	2,041	2,140
Change in International Reserves (increase +)	-419	390	1,393	-1,754	773	-317	952	1,690	470	870	6	521	800
Errors and Omissions	**-297**	**-364**	**-475**	**-508**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
						(In percent of GDP)							
Current Account	**-3.6**	**-3.0**	**-1.3**	**-1.1**	**-3.2**	**-3.2**	**-3.0**	**-3.1**	**-2.9**	**-2.8**	**-2.8**	**-2.6**	**-2.6**
Goods and services balance	0.6	1.5	3.8	3.6	1.8	2.3	2.0	2.3	2.5	2.7	2.9	3.0	3.2
Trade balance	-7.2	-7.4	-6.0	-2.9	-4.8	-4.9	-6.0	-6.6	-7.4	-7.4	-7.3	-7.3	-7.3
Export of goods (f.o.b.)	17.9	18.8	18.4	19.3	20.0	23.1	20.0	24.2	24.3	24.4	24.4	24.3	24.3
Import of goods (f.o.b.)	25.1	26.2	24.4	22.2	24.8	27.9	26.0	30.8	31.7	31.7	31.7	31.7	31.6
Services balance	7.9	8.9	9.8	6.4	6.6	7.2	7.9	8.9	9.9	10.0	10.2	10.3	10.5
Of which: Travel balance	4.3	4.7	4.6	1.7	2.0	1.6	3.5	3.0	4.3	4.4	4.3	4.2	4.2
Exports of services	14.2	15.6	16.9	12.9	12.4	14.1	14.2	16.3	17.8	17.9	18.0	18.1	18.2
Imports of services	6.3	6.7	7.2	6.4	5.8	7.0	6.3	7.4	7.9	7.9	7.8	7.8	7.7
Primary Income	-5.2	-5.4	-5.9	-5.6	-5.8	-6.4	-5.7	-6.3	-6.3	-6.4	-6.6	-6.6	-6.7
Secondary Income	1.0	0.9	0.9	0.9	0.8	0.9	0.8	1.0	0.9	0.9	0.9	0.9	0.9
Capital Account	**0.1**	**0.0**	**0.0**	**0.0**	**0.1**	**0.0**	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Financial Account	**-4.0**	**-3.5**	**-2.0**	**-1.9**	**-3.2**	**-3.2**	**-2.9**	**-3.1**	**-2.9**	**-2.8**	**-2.7**	**-2.6**	**-2.5**
Public sector	-0.4	-1.3	-1.6	0.6	-3.8	-0.4	-3.1	-3.4	-1.3	-1.7	-0.5	-0.9	-1.2
Private sector	-3.0	-2.9	-2.6	0.2	-0.6	-2.3	-1.3	-2.2	-2.3	-2.2	-2.3	-2.3	-2.2
Foreign direct investment, net	-4.4	-3.9	-4.2	-2.6	-3.2	-5.5	-3.7	-5.1	-5.0	-4.9	-4.8	-4.8	-4.7
Other private sector flows	1.4	1.0	1.6	2.9	2.6	3.2	2.4	3.0	2.8	2.7	2.6	2.5	2.5
Change in International Reserves (increase +)	-0.7	0.6	2.2	-2.8	1.3	-0.5	1.5	2.5	0.7	1.2	0.0	0.6	0.9
Errors and Omissions	**-0.5**	**-0.6**	**-0.7**	**-0.8**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum Items:													
Non-oil current account (percent of GDP)	-1.4	-0.4	1.2	0.2	-1.2	-0.8	-1.1	-0.1	-0.2	-0.3	-0.3	-0.3	-0.3
Terms of trade (annual percentage change)	-5.8	-3.8	-1.1	4.7	-2.2	-3.7	1.3	-1.0	1.3	1.2	1.0	0.9	0.8
Gross international reserves (millions of U.S. dollars)	7,150	7,501	8,937	7,232	8,004	6,921	8,956	8,611	9,081	9,951	9,957	10,478	11,278
Net international reserves, program definition (millions of U.S. dollars) 1/	4,573	4,709	6,099	3,712	3,768	2,884	4,208	3,830	3,622	4,291	4,275	4,648	5,390
External debt (percent of GDP) 2/	44.5	46.4	47.6	50.6	59.1	52.2	61.5	58.0	58.3	59.0	58.0	57.0	56.1

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

1/ The program definition of NIR excludes FX deposits of residents other than the central government.

2/ Includes public and private sector debt.

Table 4. Costa Rica: Gross External Financing Needs and Sources

					Est.	Projections						
	2018	2019	2020	2021	2021	2022	2022	2023	2024	2025	2026	2027
				EFF request		EFF request						
	(In millions of U.S. dollars)											
Gross external financing needs	**-9,172**	**-8,310**	**-10,963**	**-10,245**	**-10,891**	**-10,869**	**-11,910**	**-11,775**	**-10,270**	**-10,662**	**-10,325**	**-10,167**
Current account balance	-1,867	-824	-707	-1,976	-2,079	-1,915	-2,055	-2,048	-2,093	-2,140	-2,161	-2,205
Amortization	-4,037	-4,789	-5,168	-5,149	-5,366	-5,893	-5,094	-6,085	-4,787	-5,261	-5,124	-5,061
Public sector, of which	-285	-740	-1,125	-487	-377	-911	-356	-1,452	-278	-615	-384	-287
Central government	-96	-93	-340	-130	-97	-138	-120	-426	-35	-317	-295	-196
Central bank	-2	-377	-627	0	0	0	0	0	0	0	0	0
Private sector	-3,752	-4,048	-4,043	-4,661	-4,988	-4,982	-4,738	-4,633	-4,509	-4,646	-4,740	-4,775
of which: short-term	-2,299	-3,048	-2,999	-2,987	-3,842	-3,193	-3,650	-3,467	-3,294	-3,398	-3,473	-3,503
Other net capital inflows 1/	-3,267	-2,697	-5,087	-3,121	-3,446	-3,061	-4,761	-3,642	-3,389	-3,261	-3,041	-2,901
Gross external financing sources	**8,832**	**7,807**	**9,575**	**7,567**	**9,737**	**9,124**	**9,623**	**9,904**	**9,311**	**9,914**	**9,534**	**9,217**
Capital transfers	28	32	17	37	19	40	21	23	25	28	30	33
Direct investment, net	2,434	2,695	1,644	1,982	3,524	2,388	3,413	3,521	3,608	3,756	3,923	4,074
Borrowing	6,759	6,473	6,159	6,321	5,877	7,648	7,879	6,830	6,548	6,136	6,101	5,909
Public sector, of which	1,771	2,274	547	531	433	1,570	2,086	1,579	1,441	1,058	1,189	1,159
Central government	13	1,539	215	255	91	1,294	1,344	1,287	1,099	566	622	518
of which: Eurobonds	0	1,467	0	0	0	1,000	1,000	1,000	1,000	500	500	500
Central bank	1,000	0	0	0	0	0	0	0	0	0	0	0
Private sector	4,988	4,198	5,612	5,789	5,444	6,078	5,793	5,251	5,107	5,078	4,912	4,750
Change in International reserves (increase -)	-390	-1,393	1,754	-773	317	-952	-1,690	-470	-870	-6	-521	-800
Use of IMF credit	**0**	**0**	**522**	**581**	**294**	**581**	**582**	**523**	**31**	**-201**	**-75**	**-177**
Purchases	0	0	522	581	294	581	582	589	297	0	0	0
RFI	0	0	522	0	0	0	0	0	0	0	0	0
EFF	0	0	0	581	294	581	582	589	297	0	0	0
Repurchases	0	0	0	0	0	0	0	-66	-266	-201	-75	-177
Other gross multilateral financing	**332**	**495**	**858**	**2,098**	**861**	**1,165**	**1,705**	**1,349**	**928**	**949**	**867**	**1,126**
World Bank	...	...	105	584	313	305	426	369	...	...	...	...
Inter-American Development Bank (IDB)	...	...	282	597	404	457	613	350	...	...	...	...
CAF	...	...	448	550	0	0	50	500	...	...	...	...
Central American Bank for Economic Integration (CABEI)	...	...	23	367	144	403	617	130	...	...	...	...
Unidentified financing	0	0	0	0	0	0	0	0	0	0	0	0
Memorandum items:												
Gross multilateral support	332	495	1,380	2,679	1,154	1,746	2,288	1,938	1,224	949	867	1,126
In percent of GDP	0.5	0.8	2.2	4.4	1.8	2.7	3.5	2.8	1.7	1.2	1.1	1.3
Of which, committed	...	...	1,380	2,679	1,154	1,746	2,288	1,938	1,224	949	867	1,126
Of which, disbursed	...	...	1,380	0	1,154	0	0	0	0	0	0	0
IMF share of total gross multilateral financing (percent)												
Purchases and disbursements, flow basis	...	...	38	22	25	33	25	30	...	...	...	...
Purchases and disbursements, cumulative basis	...	...	38	27	27	29	28	29	...	...	...	...
Current account balance (percent of GDP)	-3.0	-1.3	-1.1	-3.2	-3.2	-3.0	-3.1	-2.9	-2.8	-2.8	-2.6	-2.6
Gross international reserves	7,501	8,937	7,232	8,004	6,921	8,956	8,611	9,081	9,951	9,957	10,478	11,278
In percent of the ARA metric	118	131	104	112	95	114	106	107	111	108	109	116
In percent of ST debt (remaining maturity)	157	173	135	135	132	124	137	175	178	187	195	310
In percent of gross external financing requirement	113	149	119	101	95	98	103	126	129	133	139	511
In months of next year's imports of G&S	4.4	6.0	3.9	4.6	3.3	4.7	3.7	3.7	3.9	3.7	3.7	4.0

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

1/ Also reflects the 2021 SDR allocation and changes in banks', corporates', and households' gross foreign assets.

Table 5. Costa Rica: Monetary Survey

	2017	2018	2019	2020	2021 EFF request	Est. 2021	Projections 2022 EFF request	2022	2023	2024
	(In billions of colones, unless otherwise indicated)									
Central Bank										
Net foreign assets	4,280	4,180	5,035	4,474	5,399	4,007	5,968	5,084	5,492	6,137
Of which : Gross international reserves										
(In millions of U.S. dollars)	7,150	7,501	8,937	7,232	8,004	6,921	8,956	8,611	9,081	9,951
Net domestic assets	-1,530	-1,368	-2,367	-1,441	-2,177	-852	-2,538	-1,680	-1,772	-2,123
Net domestic credit	-1,603	-1,735	-2,166	-1,894	-1,177	-1,592	-1,230	-1,901	-2,049	-2,166
Monetary stabilization instruments (-)	-2,034	-1,934	-1,859	-1,564	-1,645	-1,364	-1,748	-1,364	-1,364	-1,364
Other items (net)	-137	95	-710	-226	-1,434	-112	-1,465	-631	-575	-810
Capital account (-)	2,244	2,206	2,367	2,243	2,079	2,216	1,904	2,216	2,216	2,216
Monetary base 1/	2,749	2,813	2,667	3,033	3,222	3,155	3,429	3,404	3,720	4,014
Currency	1,197	1,238	1,305	1,498	1,648	1,529	1,813	1,621	1,718	1,821
Required reserves	1,553	1,575	1,362	1,535	1,574	1,626	1,617	1,783	2,002	2,193
Other Depository Institutions										
Net foreign assets	-2,607	-2,430	-1,681	-720	-1,309	-199	-1,560	-213	-227	-242
Net domestic assets	23,829	24,747	24,885	27,100	28,010	28,608	29,476	30,591	32,595	34,596
Net domestic credit	27,073	28,369	28,483	30,630	31,424	32,731	33,076	33,850	36,073	38,150
Credit to nonfinancial public sector (net)	2,385	2,330	2,674	3,900	4,385	5,563	4,397	5,255	5,609	5,823
Credit to nonfinancial private sector	20,112	21,381	20,896	21,601	22,758	22,204	24,215	23,053	24,443	25,906
In national currency	12,233	13,017	13,249	13,583	14,624	14,118	15,847	14,875	16,178	17,552
In foreign currency	7,879	8,364	7,647	8,019	8,134	8,086	8,368	8,178	8,265	8,354
Credit to financial corporations (net)	4,576	4,658	4,913	5,129	4,280	4,964	4,465	5,541	6,020	6,421
Other items (net)	1,065	985	1,352	1,602	1,907	1,414	1,950	2,662	2,841	3,166
Capital account	-4,309	-4,607	-4,950	-5,131	-5,320	-5,537	-5,550	-5,920	-6,319	-6,720
Liabilities to nonfinancial private sector	21,223	22,317	23,204	26,380	26,702	28,409	27,916	30,378	32,368	34,355
In national currency	13,621	14,012	15,059	16,593	16,983	17,433	17,768	18,641	19,898	21,158
In foreign currency	7,602	8,306	8,146	9,787	9,719	10,977	10,148	11,737	12,470	13,197
Of which: Deposits (including CDs)	21,046	22,101	23,025	26,201	26,581	28,086	27,834	30,141	32,663	35,287
Consolidated Financial System										
Net foreign assets	1,673	1,750	3,354	3,753	4,090	3,808	4,408	4,871	5,264	5,895
Net domestic assets	21,246	22,374	21,080	23,953	25,833	25,443	26,938	26,329	27,910	29,276
Net domestic credit	22,382	23,694	23,021	25,465	30,247	27,461	31,847	28,002	29,746	31,422
Other items (net)	928	1,081	643	1,376	473	1,302	485	2,031	2,267	2,357
Capital account	-2,064	-2,401	-2,583	-2,888	-3,241	-3,320	-3,646	-3,704	-4,103	-4,503
Broad money	15,958	16,298	16,957	19,990	19,617	21,490	20,175	22,584	24,125	25,700
Memorandum Items	(Annual percentage change)									
Monetary base 1/	10.8	2.3	-5.2	13.7	6.2	4.0	6.4	7.9	9.3	7.9
Broad money	1.5	2.1	4.0	17.9	-2.2	7.5	2.8	5.1	6.8	6.5
Credit to the private sector	8.5	6.3	-2.3	3.4	6.1	2.8	6.4	3.8	6.0	6.0
In national currency	11.8	6.4	1.8	2.5	7.8	3.9	8.4	5.4	8.8	8.5
In foreign currency	3.6	6.2	-8.6	4.9	3.1	0.8	2.9	1.1	1.1	1.1
Credit to the private sector (adjusted by exchange rate changes)	7.6	3.8	0.1	0.8	6.6	1.6	7.0	4.0	5.9	6.1
	(In percent of GDP)									
Monetary base 1/	8.0	7.8	7.1	8.3	8.6	7.9	8.8	8.0	8.2	8.3
Broad money	46.5	45.3	44.8	55.0	52.5	54.0	51.7	53.0	53.1	53.2
Of which: Deposits denominated in foreign currency	14.6	15.0	14.2	18.5	17.1	19.4	16.6	18.8	18.5	18.3
Credit to the private sector	58.6	59.4	55.2	59.4	60.9	55.7	62.1	54.1	53.8	53.6
Of which: In foreign currency	22.9	23.2	20.2	22.1	21.8	20.3	21.5	19.2	18.2	17.3
Central bank balance	-0.2	0.1	-0.4	0.3	0.4	0.1	0.4	0.0	0.0	0.0

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

1/ Includes currency issued and required reserves.

Table 6. Costa Rica: Financial Soundness Indicators

	2016 Dec	2017 Dec	2018 Dec	2019 Dec	2020 Dec	2021 Dec
	(In percent)					
Capitalization						
Risk-adjusted capital ratio	16.4	16.8	16.7	17.5	16.8	16.5
Capital-to-assets ratio	14.1	13.9	14.2	15.2	14.4	14.4
Asset quality						
Nonperforming loans to total loans	1.5	2.0	2.1	2.4	2.5	2.3
Non-income generating assets to total assets	15.7	16.2	16.3	15.8	18.3	17.1
Foreclosed assets to total assets	0.8	0.8	1.0	1.1	1.1	1.0
Loan loss provisions to total loans	2.2	2.8	3.3	3.5	4.2	4.3
Credit in foreign currency to total credit	41.0	39.2	39.1	36.6	37.1	36.5
Management						
Administrative expenses to total assets	3.3	3.1	3.1	3.2	3.0	2.9
Noninterest expenses to gross income	67.6	73.7	77.6	83.1	82.0	79.1
Total expenses to total revenues	91.3	94.8	95.6	96.7	97.2	94.6
Profitability						
Return on assets (ROA)	1.2	0.9	0.9	1.0	0.6	0.9
Return on equity (ROE)	8.8	6.5	6.8	6.8	4.6	6.5
Interest margin to gross income	32.4	25.3	21.3	16.4	18.9	26.9
Liquidity						
Liquid assets to total short-term liabilities	95.9	102.7	98.6	96.8	93.9	89.9
Liquid assets to total assets	28.2	29.1	28.0	29.8	33.0	35.7
Loans to deposits[1/]	115.8	112.3	113.1	105.6	99.0	95.6
Liquid assets to deposits	45.0	45.5	43.7	44.6	50.0	52.4
Sensitivity to market risk						
Net open FX position to capital	21.4	22.7	21.1	23.5	25.1	25.6
Other						
Financial margin[2/]	6.9	6.6	7.1	7.1	6.7	7.0

Source: Superintendency of Banks (SUGEF).
1/ Loans (including contingent credits) divided by deposits held by the public.
2/ Difference between implicit loan and deposit rates.

Table 7. Costa Rica: Indicators of Fund Credit

	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Fund obligations based on existing credit (millions of SDRs)													
Principal	0.0	46.2	184.7	138.5	34.4	34.4	34.4	34.4	34.4	34.4	0.0	0.0	0.0
Charges and interest 1/	5.3	7.2	6.0	3.8	2.5	2.0	1.6	1.2	0.8	0.4	0.2	0.2	0.2
Fund obligations based on existing and prospective credit (millions of SDRs)													
Principal	0.0	46.2	184.7	138.5	51.6	120.3	189.1	206.3	206.3	206.3	154.7	85.9	17.2
Charges and interest 1/	10.3	24.7	33.6	29.2	27.3	27.6	21.6	13.2	7.4	4.9	2.6	1.0	0.2
Total obligations based on existing and prospective credit													
Millions of SDRs	10.3	70.9	218.3	167.7	78.9	147.9	210.6	219.4	213.6	211.1	157.3	86.9	17.4
Percent of exports of goods and services	0.1	0.3	1.0	0.7	0.3	0.6	0.8	0.8	0.7	0.7	0.5	0.2	0.0
Percent of gross international reserves	0.2	1.1	3.1	2.4	1.1	1.9	2.6	2.6	2.4	2.2	1.5	0.8	0.2
Percent of GDP	0.0	0.1	0.4	0.3	0.1	0.2	0.3	0.3	0.3	0.3	0.2	0.1	0.0
Percent of quota	2.8	19.2	59.1	45.4	21.4	40.0	57.0	59.4	57.8	57.2	42.6	23.5	4.7
Outstanding IMF credit based on existing and prospective drawings													
Millions of SDRs	988.2	1,354.5	1,376.0	1,237.5	1,185.9	1,065.6	876.5	670.3	464.0	257.8	103.1	17.2	0.0
Percent of exports of goods and services	5.1	6.5	6.2	5.4	4.9	4.2	3.3	2.4	1.5	0.8	0.3	0.0	0.0
Percent of gross international reserves	16.0	21.2	19.5	17.7	16.3	13.9	10.8	7.8	5.1	2.7	1.0	0.2	0.0
Percent of GDP	2.1	2.7	2.6	2.3	2.1	1.8	1.4	1.0	0.7	0.3	0.1	0.0	0.0
Percent of quota	267.5	366.7	372.5	335.0	321.0	288.5	237.3	181.5	125.6	69.8	27.9	4.7	0.0
Net use of IMF credit (millions of SDRs)	412.5	366.3	21.5	-138.5	-51.6	-120.3	-189.1	-206.3	-206.2	-206.3	-154.7	-85.9	-17.2
Disbursements	412.5	412.5	206.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	0.0	46.2	184.7	138.5	51.6	120.3	189.1	206.3	206.3	206.3	154.7	85.9	17.2
Memorandum items:													
Exports of goods and services (millions of U.S. dollars)	26,862.6	29,527.2	31,151.5	32,894.5	34,690.3	36,844.6	39,132.7	41,562.9	44,144.0	46,885.4	49,797.0	52,889.4	56,173.9
Gross international reserves (millions of U.S. dollars)	8,611.2	9,081.2	9,951.2	9,957.2	10,478.2	11,128.9	11,820.0	12,554.1	13,333.7	14,161.7	15,041.2	15,975.2	16,967.3
Quota (millions of SDRs)	369.4	369.4	369.4	369.4	369.4	369.4	369.4	369.4	369.4	369.4	369.4	369.4	369.4

Source: IMF staff estimates and projections.

1/ Based on the GRA rate of charge of 1.217 percent as of February 24, 2022.

Table 8. Costa Rica: Current Access and Phasing Under the Extended Fund Facility

Availability Date	Millions of SDR	Percent of Quota	Conditions
March 1, 2021	206.34	55.86	Board approval of the Extended Arrangement under the Extended Fund Facility
October 15, 2021	206.23	55.83	First review and continuous and end-July 2021 performance criteria
March 15, 2022	206.23	55.83	Second review and continuous and end-December 2021 performance criteria
October 15, 2022	206.23	55.83	Third review and continuous and end-June 2022 performance criteria
March 15, 2023	206.23	55.83	Fourth review and continuous and end-December 2022 performance criteria
October 15, 2023	206.23	55.83	Fifth review and continuous and end-June 2023 performance criteria
Total	1237.49	335	
Memorandum item:			
Quota	369.40		

Source: IMF staff calculations.

Table 9. Costa Rica: Proposed Access and Phasing Under the Extended Fund Facility

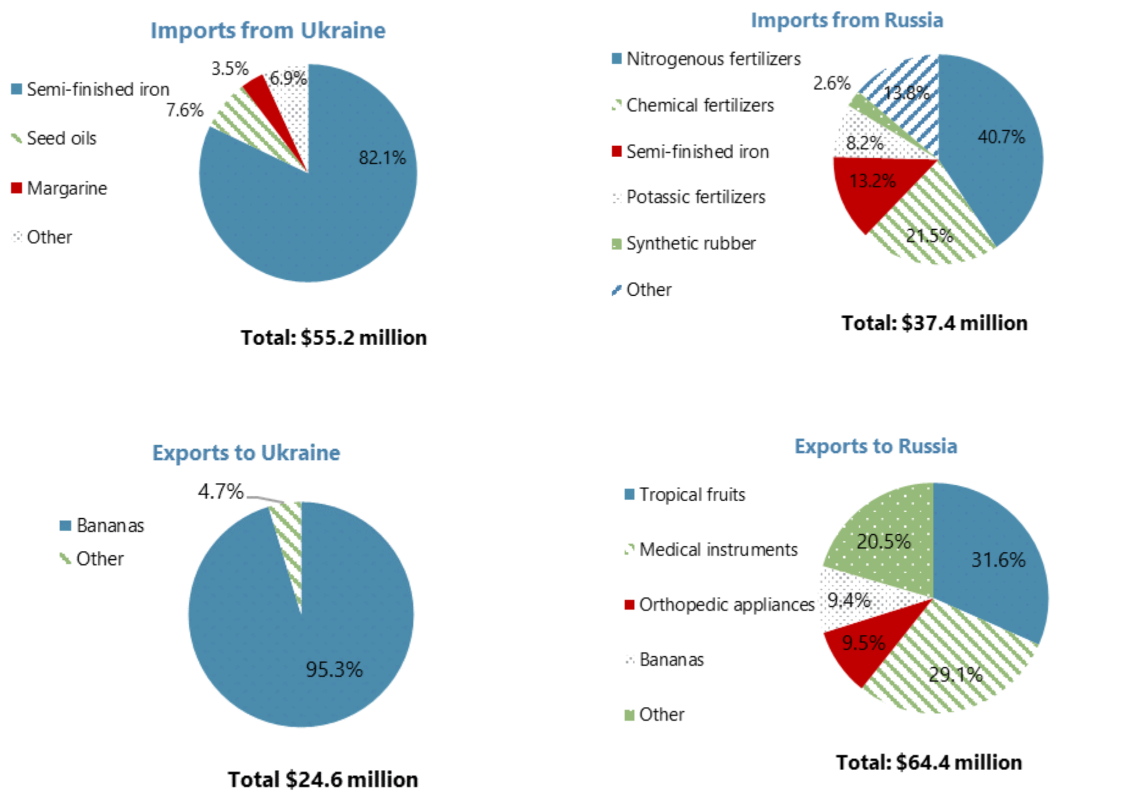
Availability Date	Millions of SDR	Percent of Quota	Conditions
March 1, 2021	206.34	55.86	Board approval of the Extended Arrangement under the Extended Fund Facility
October 15, 2021	103.115	27.91	First review and continuous and end-July 2021 performance criteria
March 15, 2022	103.115	27.91	Second review and continuous and end-December 2021 performance criteria
October 15, 2022	206.23	55.83	Third review and continuous and end-June 2022 performance criteria
March 15, 2023	206.23	55.83	Fourth review and continuous and end-December 2022 performance criteria
October 15, 2023	206.23	55.83	Fifth review and continuous and end-June 2023 performance criteria
March 15, 2024	206.23	55.83	Sixth review and continuous and end-December 2023 performance criteria
Total	1237.49	335	
Memorandum item:			
Quota	369.40		

Source: IMF staff calculations.

Annex I. Implications of the Russia-Ukraine Conflict for Costa Rica

1. **Direct trade linkages.** Russia and Ukraine account for about 0.2 percent of tourist arrivals and imports from Russia and Ukraine are less than 0.5 percent of the total. However, imports of semi-finished iron are sourced from Russia and Ukraine and around one-quarter of fertilizer imports are sourced from Russia and Belarus.

Costa Rica: Trade Linkages with Russia and Ukraine



Sources: COMTRADE and IMF staff estimates

2. **Commodity prices.** Model-based and empirical estimates suggest a 10-percent increase in fuel prices[1] would raise inflation in Costa Rica by 0.5-1 percent, reduce the current account by around ¼ percent of GDP, add 0.1 percent of GDP to the primary deficit, and lower growth by around 0.1-0.3 percent. Such a negative terms of trade shock is also likely to put downward pressure on the currency. Higher international food and metal prices would add to these effects.

[1] For comparison purposes, energy prices increased by nearly 50 percent between October 2010 and March 2012. A shock of comparable size and duration would depress GDP growth in Costa Rica by 0.5-1.5 percentage points, with likely second-round effects from a slowdown in trading partners.

3. **Global financial conditions**. Increased global risk aversion and a faster pace of tightening by advanced economy central banks could tighten financial conditions, raising the costs of planned placements of sovereign debt in international markets in 2022 (although Costa Rica does have scope to substitute to domestic markets and tap contingency lines from regional partners).

4. **Banks' balance sheets**. Direct bank exposures to Russia and Ukraine are negligible so the principal impact on bank balance sheets and credit quality would be via lower growth and tighter financial conditions. However, stress tests suggest banks can withstand a significant shock to growth, interest rates, and the exchange rate.

5. **Contingency planning.** The program would have space to accommodate a negative global shock within the current structure. The authorities would likely need to:

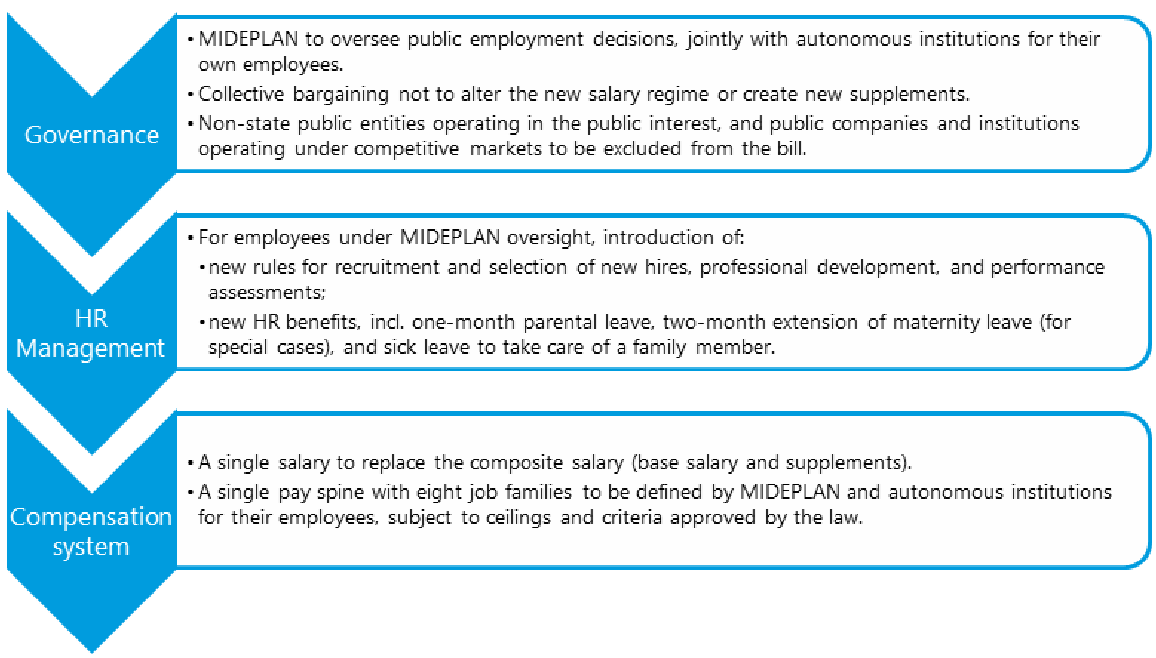
- Accelerate the pace of monetary policy normalization to counter second round inflationary effects of the external shock and anchor inflation expectations.
- Rely on the exchange rate as a shock absorber while using limited FX sales to counter disruptive market conditions.
- Reprioritize public spending to increase social assistance programs and mitigate the effects of rising commodity prices on the poor.
- Mobilize additional financing from regional partners and domestic debt markets.
- Potentially allow for the drawdown of countercyclical buffers in the banking system.

Annex II. Public Employment Reform in Costa Rica[1]

1. **Over the past decade, high public wage growth—which has widened the public-private wage premium, has been at the root of Costa Rica's fiscal vulnerabilities.**[2] The compensation system is complex and fragmented, making it difficult to control, adjust, target, and manage. Salary includes a base pay plus numerous additional bonuses and supplements that can account for half of the total remuneration (and are tied to seniority rather than performance). Wages, as a result, are not competitive at entry levels and there are large discrepancies in compensation for employees performing similar tasks.

2. **The Legislative Assembly has approved a new Public Employment Bill which improves the sustainability, fairness, and productivity of public employment.** The main goals are to introduce a better integrated HR management system, a single pay spine, transparent and performance-based non-monetary incentives, and additional employment benefits, including parental leave. The new pay structure will apply directly to new hires, with a mandatory transition for existing workers with salaries below their corresponding job reference wage. Due to the large wage premium in the public sector, the salaries of the many existing workers that fall above the spine will be frozen until they are reached by the single pay scheme.

Costa Rica: Key Elements of the Public Employment Bill

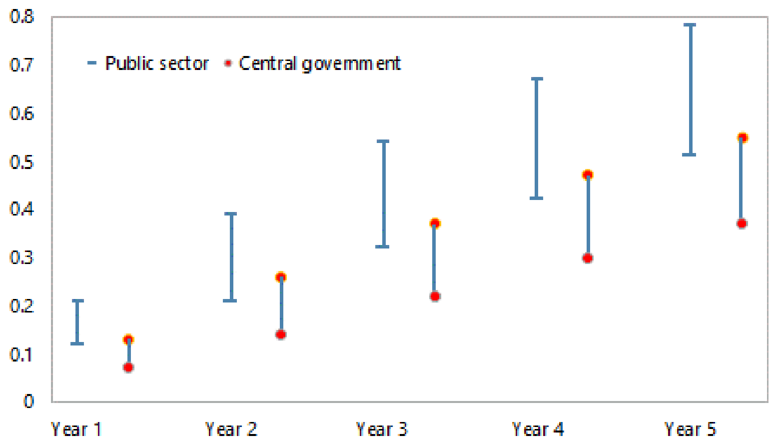


[1] Prepared by Nan Geng and Miguel Pecho (IMF) and Martin Ardanaz, Andrew Wolfe, and Mariano Lafuente (IDB).

[2] See "The inequality and Informality Challenge" in the 2021 Article IV Consultation and EFF Request Staff Report.

3. Depending on the new reference salaries, expected savings from the bill are 0.5 to 0.8 percent of GDP over a five-year horizon for the entire public sector (0.4 to 0.6 percent of GDP for the central government), according to IDB estimates. The Ministry of National Planning and Economic Policy (MIDEPLAN) has started working on the implementation plans for the introduction of the single pay spine and related reforms under the law, which are due to be implemented within 12 months of the Bill's approval date, by March 2023. These include job evaluation exercises to map all professions, grades, and posts into the unified pay spine and private market surveys used to decide the appropriate salary level for each job family.

Potential Fiscal Savings from the Public Employment Bill
(Percent of GDP)



Source: IDB.

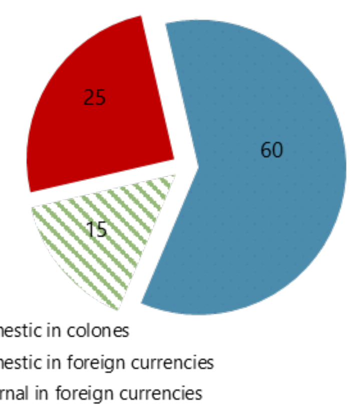
Annex III. Debt Sustainability Analysis

Under the baseline scenario, Costa Rica's debt is assessed to remain sustainable, as the economic recovery and fiscal consolidation plans under the program help strengthen debt dynamics. Public debt is projected to start declining over the medium term after peaking at about 69 percent of GDP in 2022 and stabilizing in 2023. Risks to the debt path are moderate, including from weaker growth, materialization of contingent liabilities, and interest rate and currency shocks.

A. Background and Key Assumptions

1. **Costa Rica's public debt increased significantly over the last decade, with a recent spike due to the COVID-19 shock.** Since the global financial crisis, public debt increased by about 40 percent of GDP amid an expansion in fiscal spending, relatively weak growth dynamics, and increasing interest costs. After rising by 4½ percentage points in 2019, the public debt ratio increased further from 56½ percent of GDP at end-2019 to 68½ percent of GDP at end-2021, reflecting COVID-related pressures as well as a growing interest bill. Domestic debt (mostly bonds issued in colones or U.S. dollars) accounts for about 51½ percent of GDP or about three quarters of total public debt. External public debt consists of multilateral and bilateral loans (about 8 percent of GDP or 10 percent of total) as well as Eurobonds (9 percent of GDP or 13 percent of total). Foreign-currency denominated debt accounts for about 40 percent of the total. In line with the new requirements under the Debt Limits Policy, information on the debt holder profile is presented in Table AII.7. As of end-2021, Costa Rica's debt-to-GDP ratio stands higher than most peers and the emerging market (EM) average.

Costa Rica: Composition of Total Debt by Currency
(Percent of total debt, December 2021)



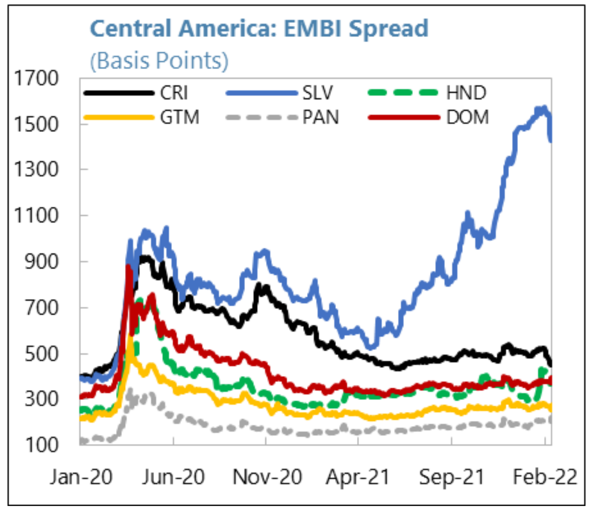
2. **The public debt sustainability analysis (DSA) focuses on the central government (CG), due to data availability constraints for the broader public sector.** The CG definition has been expanded, with support from IMF TA, to include 51 public entities that, starting in 2021, are required to be consolidated under central government (CG) by Law 9524 (accounting for about 0.4 percent of GDP in debt as of end-2020). The CG accounts have been consolidated retroactively back to 2019, to ensure data comparability. The rest of the public sector, not included under the DSA, has been broadly in balance in recent years as the cash surplus of the social security system and other decentralized government entities broadly offsets the small central bank deficit—resulting from its past liquidity management operations—while public enterprises are broadly in balance. However, different reporting standards and weak data reporting of state-owned enterprises do not allow for consistent data availability, constraining staff's ability to monitor the entire public sector.

3. The baseline scenario of the DSA reflects the medium-term macroeconomic projections and policies under the proposed extended arrangement under the EFF. Under the baseline, real GDP growth is estimated at 3.6 percent in 2022, after a 7.5 percent rebound in 2021. Over the medium term, growth is expected to stabilize around its potential of 3 percent. End-2021 inflation stood at 3.3 percent. After reaching 4.8 percent in 2022, inflation is forecast to gradually decline towards 3 percent over a one- to two-year horizon—in line with the BCCR's inflation target. The primary balance is projected to continue to strengthen from a 0.3 percent of GDP deficit in 2021 to a surplus of around 2¼ percent of GDP in 2027. The baseline is underpinned by the spending ceilings and corrective mechanisms under the fiscal rule. The baseline revenue assumptions remain conservative, even after adjusting for one-offs. The phased implementation of the 2018 tax reform is expected to deliver higher yields over time than reflected under the current baseline. Moreover, the baseline does not include yields from any planned measures by the authorities, pending their formal approval, or from the implementation of the Public Employment Bill or the new Tax Compliance Improvement Plan. Interest payments are expected to remain sizable due to the still high public debt, with projections based on actual interest payments for existing debt and prevailing interest rates in the primary market for newly issued debt, adjusted in line with developments in domestic and global financial conditions.

B. Public Debt Sustainability

4. The authorities' sustained fiscal consolidation will help strengthen debt dynamics over the medium term. Under the baseline scenario, central government debt is projected to reach about 68½ percent of GDP in 2022, just below the 70-percent benchmark for emerging markets. Debt is expected to decline to 63½ percent of GDP by 2027. The debt adjustment will be supported by additional gains from structural measures of 3½ percent of GDP over 2022-27, including sustained implementation of the fiscal rule—that ties down the growth of spending—over the medium term. Gross financing needs will peak at 11¼ percent of GDP in 2023 before declining to below 10 percent of GDP in 2027. The baseline assumes access to external financing in the form of official financing and US$4.5 billion in Eurobond issuances over 2022-27. However, additional contingency financing could be mobilized from domestic banks and from regional partners, were downside risks to materialize.

5. Risks to debt sustainability are moderate, as signaled by the heat map and stress scenario analysis. The heat map indicates a moderate risk to debt sustainability. Baseline debt does not exceed the 70 percent of GDP benchmark for EMs in 2022 through 2027, but the benchmark is exceeded for some shocks. A contingent liability shock in the context of a deterioration of asset quality could push the peak debt-to-GDP ratio to 80 percent, while GDP growth or real exchange rate shocks would also drive debt above the 70 percent of GDP benchmark. If the primary balance were to fall short of the forecast for 2023 and 2024, for example if the contribution of one-off factors to revenue in 2021 was underestimated or if unanticipated COVID-related emergency spending leads to spending that is higher than forecast, the debt-to-GDP ratio would remain marginally below 70 percent but delay its downward path. Gross financing needs would remain below the benchmark of 15 percent of GDP in all standardized macro-fiscal stress tests except for the historical and contingent liability shock scenarios. When all these shocks are combined, the debt to GDP ratio would reach 85 percent in 2023 and gross financing needs would increase to around 13-14 percent of GDP. In terms of the realism of the baseline assumptions, the envisaged maximum three-year improvement in the structurally adjusted primary balance by 3.8 percent of GDP over 2020–23 is higher than in 83 percent of international experiences. This highlights the ambition of the fiscal consolidation plan embodied in the fiscal rule and revenue reform, also given elevated risks to the growth outlook. The debt profile analysis indicates a moderate degree of vulnerabilities related to market perception, external financing requirement, debt held by non-residents, and debt denominated in foreign currency. Specifically, since the time of the EFF request, spreads have fallen comfortably below the 600 basis points upper early warning benchmark. Foreign-currency denominated debt as share of total debt reached about 40 percent as of end-2021 and is projected to continue to rise until 2024 owing to financial assistance from the Fund and other IFIs to respond to the COVID-19 shock and support the recovery. The foreign currency share will nevertheless remain below the high-risk of debt distress benchmark of 60 percent.



C. External Debt Sustainability

6. **The ratio of total external debt (public and private) to GDP is projected to peak in 2024 and then decline over the medium term.** External debt is projected to increase by 5.8 percent in 2022 to 58.0 percent of GDP, due to the widening current account deficit as weak tourism receipts, higher oil prices, and increased demands for intermediate inputs offset the strong performance of goods exports. It is projected to peak in 2024 at around 59 percent of GDP and then decrease to around 56 percent by 2027 as GDP growth and the trade balance normalize.

7. **The main risk to external debt sustainability is a sharp depreciation of the exchange rate.** Currency risks, notably vis-à-vis the U.S. dollar, are high. The stress test analysis suggests that a 30 percent real depreciation in 2022 could lead to a sizable increase in the external debt-to-GDP ratio to about 88 percent by 2024. Nevertheless, the stress tests show that other common risk factors—from interest rates, growth, and the current account primary balance—pose relatively low risk. Robustness was further evidenced by the fact that the debt-to-GDP ratio fell substantially in 2021—and the forecast is similarly lower—relative to forecasts at the time of the EFF request, despite a nearly five percent depreciation. Further FDI is projected to more than cover the current account for the foreseeable future. Nevertheless, further tightening in global liquidity conditions as well as country-specific shifts in investor confidence, for example related to a weakening of the fiscal and debt trajectory, could raise rollover risks and interest costs.

Figure AIII.1. Costa Rica: Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(In percent of GDP unless otherwise indicated)

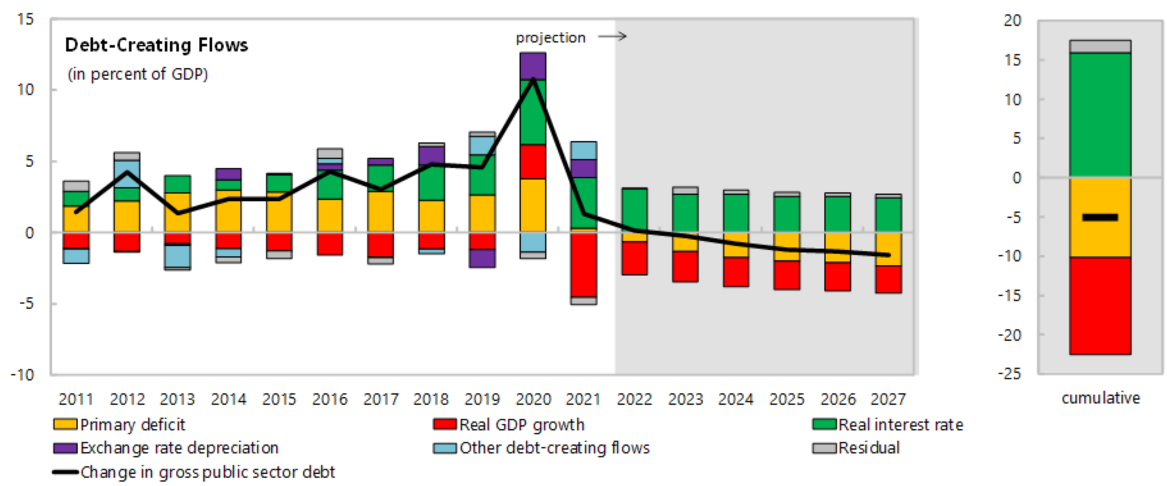
Debt, Economic and Market Indicators 1/

	Actual		Prel.		Projections					
	2011-2019 2/	2020	2021		2022	2023	2024	2025	2026	2027
Nominal gross public debt	41.7	67.2	68.5		68.6	68.3	67.5	66.3	65.0	63.4
Public gross financing needs	11.4	13.0	11.2		10.1	11.3	10.2	10.6	10.3	9.1
Real GDP growth (in percent)	3.6	-4.1	7.5		3.6	3.3	3.2	3.2	3.2	3.2
Inflation (GDP deflator, in percent)	3.7	0.2	2.0		3.3	3.4	3.1	3.0	3.0	3.0
Nominal GDP growth (in percent)	7.5	-3.9	9.6		6.9	6.7	6.3	6.2	6.2	6.2
Effective interest rate (in percent) 4/	8.1	8.0	7.9		8.1	7.7	7.4	7.1	7.1	7.0

As of February 17, 2022		
Sovereign Spreads		
EMBIG (bp) 3/		452
5Y CDS (bp)		274
Ratings	Foreign	Local
Moody's	B2	B2
S&Ps	B	B
Fitch	B	B

Contribution to Changes in Public Debt

	Actual			Projections							
	2011-2019	2020	2021	2022	2023	2024	2025	2026	2027	cumulative	debt-stabilizing
Change in gross public sector debt	3.1	10.7	1.3	0.1	-0.3	-0.8	-1.2	-1.3	-1.6	-5.1	primary
Identified debt-creating flows	3.1	11.2	1.8	0.1	-0.7	-1.1	-1.5	-1.6	-1.8	-6.6	balance 9/
Primary deficit	2.5	3.8	0.3	-0.7	-1.3	-1.8	-2.0	-2.1	-2.3	-10.2	0.5
Primary (noninterest) revenue and grants	13.4	14.0	15.9	15.0	15.1	15.1	15.1	15.1	15.1	90.5	
Primary (noninterest) expenditure	16.0	17.7	16.2	14.3	13.8	13.4	13.1	12.9	12.7	80.3	
Automatic debt dynamics 5/	0.5	8.8	0.3	0.8	0.6	0.7	0.5	0.5	0.5	3.6	
Interest rate/growth differential 6/	0.3	7.0	-1.0	0.8	0.6	0.7	0.5	0.5	0.5	3.6	
Of which: real interest rate	1.6	4.6	3.6	3.1	2.7	2.7	2.5	2.5	2.4	15.9	
Of which: real GDP growth	-1.3	2.4	-4.6	-2.3	-2.1	-2.0	-2.0	-2.0	-1.9	-12.3	
Exchange rate depreciation 7/	0.2	1.9	1.2	...	...	...	...	...	...	...	
Other identified debt-creating flows	0.0	-1.4	1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Use of Deposits (negative)	0.0	-1.4	1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes 8/	0.1	-0.5	-0.5	0.0	0.5	0.3	0.3	0.3	0.3	1.6	



Source: IMF staff calculations.

1/ Public sector is defined as central government, which includes deconcentrated public agencies as of 2019.

2/ Based on available data.

3/ EMBIG.

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

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

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

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

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

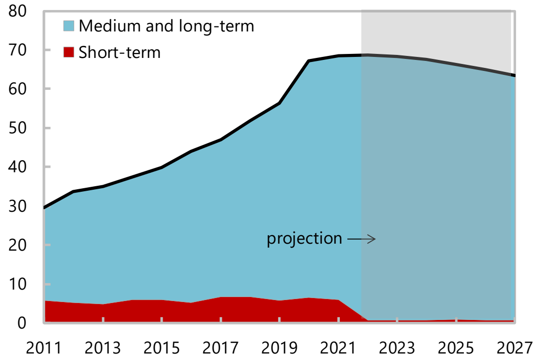
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure AIII.2. Costa Rica: Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

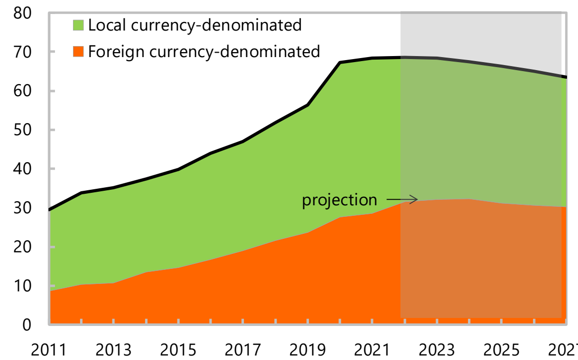
By Maturity

(in percent of GDP)



By Currency

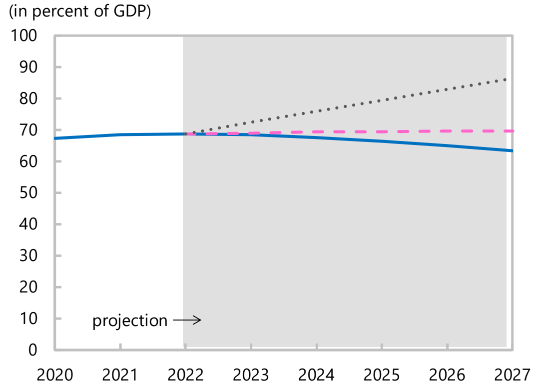
(in percent of GDP)



Alternative Scenarios

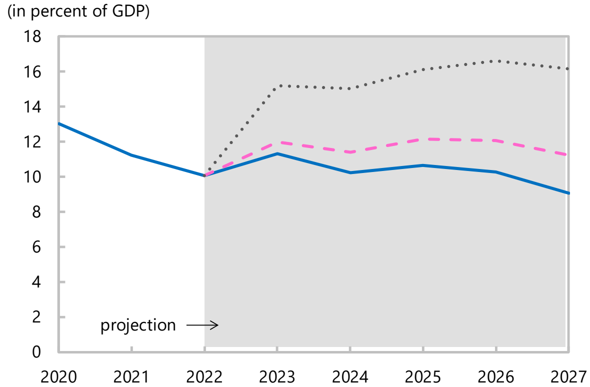
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

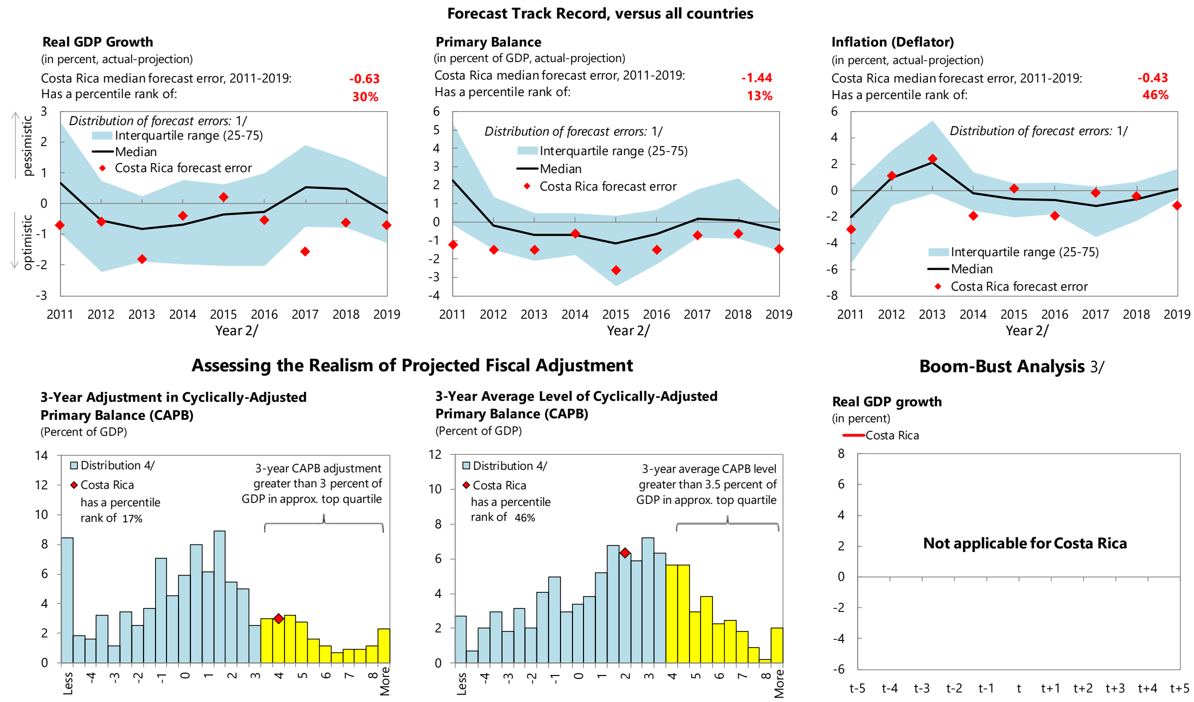
(in percent)

Baseline Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	3.6	3.3	3.2	3.2	3.2	3.2
Inflation	3.3	3.4	3.1	3.0	3.0	3.0
Primary Balance	0.7	1.3	1.8	2.0	2.1	2.3
Effective interest rate	8.1	7.7	7.4	7.1	7.1	7.0
Constant Primary Balance Scenario						
Real GDP growth	3.6	3.3	3.2	3.2	3.2	3.2
Inflation	3.3	3.4	3.1	3.0	3.0	3.0
Primary Balance	0.7	0.7	0.7	0.7	0.7	0.7
Effective interest rate	8.1	7.7	7.3	7.0	7.0	6.9

Historical Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	3.6	3.1	3.1	3.1	3.1	3.1
Inflation	3.3	3.4	3.1	3.0	3.0	3.0
Primary Balance	0.7	-2.5	-2.5	-2.5	-2.5	-2.5
Effective interest rate	8.1	7.7	7.4	7.1	7.2	7.1

Source: IMF staff calculations.

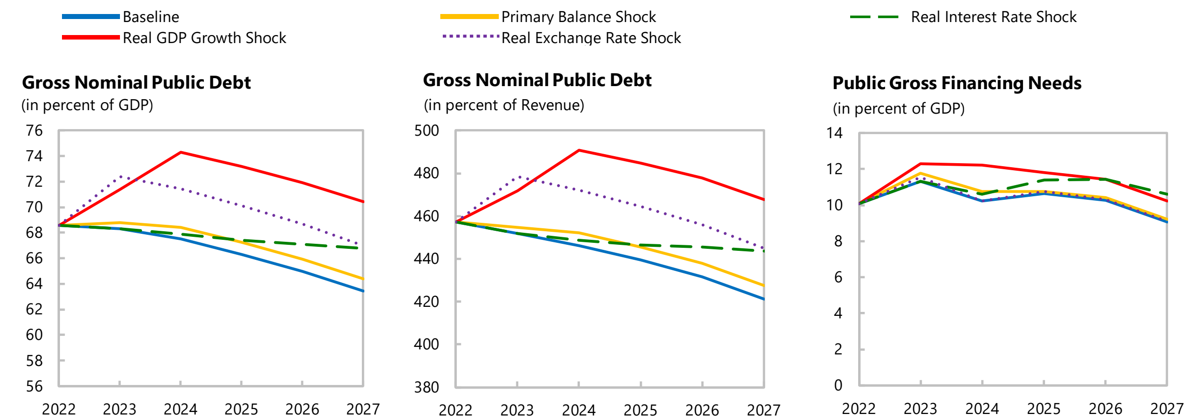
Figure AIII.3. Costa Rica: Public DSA - Realism of Baseline Assumptions



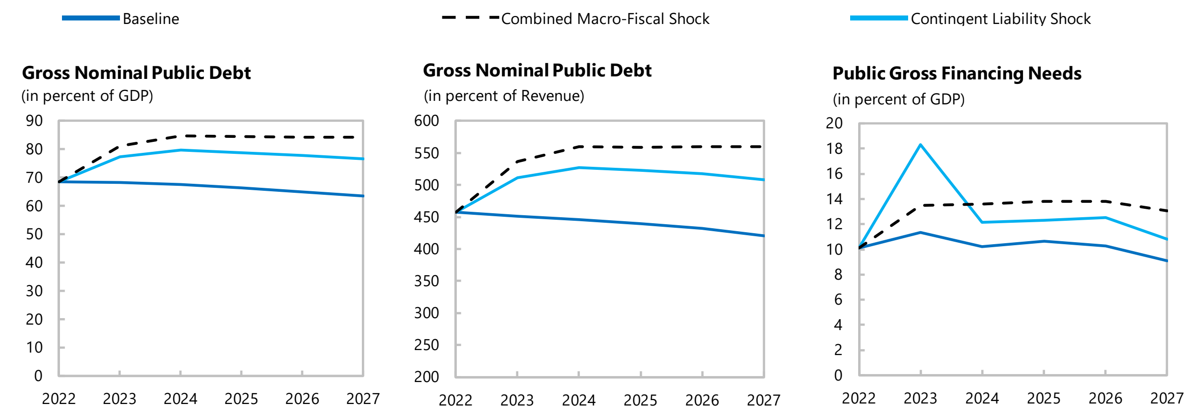
Source : IMF Staff calculations.
1/ Plotted distribution includes all countries, percentile rank refers to all countries.
2/ Projections made in the spring WEO vintage of the preceding year.
3/ Not applicable for Costa Rica, as it meets neither the positive output gap criterion nor the private credit growth criterion.
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure AIII.4. Costa Rica: Public DSA - Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

	2022	2023	2024	2025	2026	2027
Primary Balance Shock						
Real GDP growth	3.6	3.3	3.2	3.2	3.2	3.2
Inflation	3.3	3.4	3.1	3.0	3.0	3.0
Primary balance	0.7	0.9	1.3	2.0	2.1	2.3
Effective interest rate	8.1	7.7	7.4	7.1	7.1	7.0
Real Interest Rate Shock						
Real GDP growth	3.6	3.3	3.2	3.2	3.2	3.2
Inflation	3.3	3.4	3.1	3.0	3.0	3.0
Primary balance	0.7	1.3	1.8	2.0	2.1	2.3
Effective interest rate	8.1	7.7	7.9	8.1	8.7	9.0
Combined Shock						
Real GDP growth	3.6	0.3	0.2	3.2	3.2	3.2
Inflation	3.3	2.6	2.3	3.0	3.0	3.0
Primary balance	0.7	0.8	0.8	2.0	2.1	2.3
Effective interest rate	8.1	8.3	7.6	7.8	8.3	8.7

	2022	2023	2024	2025	2026	2027
Real GDP Growth Shock						
Real GDP growth	3.6	0.3	0.2	3.2	3.2	3.2
Inflation	3.3	2.6	2.3	3.0	3.0	3.0
Primary balance	0.7	0.8	0.8	2.0	2.1	2.3
Effective interest rate	8.1	7.7	7.4	7.1	7.1	7.0
Real Exchange Rate Shock						
Real GDP growth	3.6	3.3	3.2	3.2	3.2	3.2
Inflation	3.3	10.9	3.1	3.0	3.0	3.0
Primary balance	0.7	1.3	1.8	2.0	2.1	2.3
Effective interest rate	8.1	8.3	7.0	6.7	6.8	6.7
Contingent Liability Shock						
Real GDP growth	3.6	0.3	0.2	3.2	3.2	3.2
Inflation	3.3	2.6	2.3	3.0	3.0	3.0
Primary balance	0.7	-4.8	1.8	2.0	2.1	2.3
Effective interest rate	8.1	8.2	7.6	7.3	7.3	7.2

Source: IMF staff calculations.

Figure AIII.5. Costa Rica: Public DSA - Risk Assessment

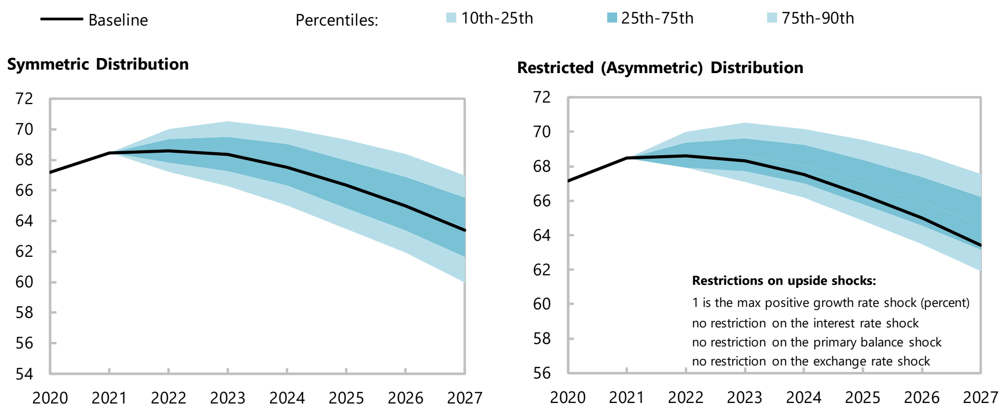
Costa Rica Public DSA Risk Assessment

Heat Map

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

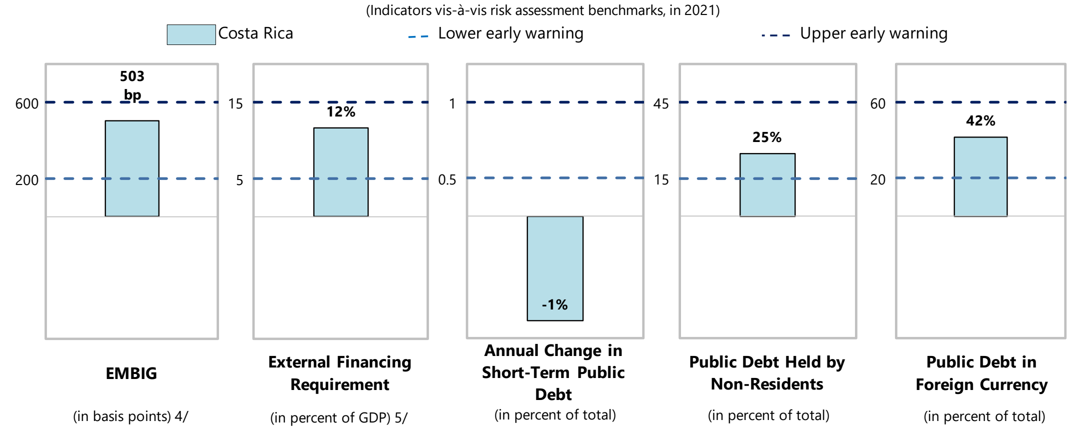
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2021)



Source: IMF staff calculations.

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

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

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

Lower and upper risk-assessment benchmarks are:

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

4/ EMBIG, an average over the last 3 months, 19-Nov-21 through 17-Feb-22.

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

Table AIII.1. Costa Rica: External Debt Sustainability Framework, 2017-27

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2017	2018	2019	2020	2021	10-Year Historical Average	10-Year Standard Deviation	2022	2023	2024	2025	2026	2027	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	44.5	46.4	47.6	50.6	52.2			**58.0**	**58.3**	**59.0**	**58.0**	**57.0**	**56.1**	**-5.6**
Change in external debt	1.0	1.9	1.2	3.0	1.6			5.8	0.3	0.7	-1.0	-0.9	-0.9	
Identified external debt-creating flows (4+8+9)	-2.1	-2.4	-4.4	0.1	-3.9			-3.9	-3.9	-3.8	-3.9	-3.9	-3.9	
Current account deficit, excluding interest payments	2.3	1.4	-0.3	-0.3	1.9			1.7	1.3	1.1	0.8	0.7	0.6	
Deficit in balance of goods and services	-0.6	-1.5	-3.8	-3.6	-2.3			-2.3	-2.5	-2.7	-2.9	-3.0	-3.2	
Exports	32.1	34.4	35.3	32.2	37.2			40.5	42.1	42.3	42.4	42.5	42.5	
Imports	31.4	32.9	31.5	28.6	34.9			38.2	39.6	39.6	39.5	39.4	39.3	
Net non-debt creating capital inflows (negative)	-4.5	-4.0	-4.3	-2.7	-5.5			-5.2	-5.0	-4.9	-4.9	-4.8	-4.8	
Automatic debt dynamics 1/	0.2	0.2	0.1	3.2	-0.3			-0.4	-0.2	0.0	0.1	0.2	0.3	
Contribution from nominal interest rate	1.4	1.6	1.6	1.5	1.3			1.4	1.6	1.8	1.9	1.9	2.0	
Contribution from real GDP growth	-1.8	-1.1	-1.1	2.0	-3.7			-1.8	-1.8	-1.8	-1.8	-1.7	-1.7	
Contribution from price and exchange rate changes 2/	0.6	-0.2	-0.3	-0.3	2.1			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	3.1	4.3	5.6	2.9	5.5			9.6	4.2	4.6	2.8	3.0	3.0	
External debt-to-exports ratio (in percent)	138.7	134.9	134.8	157.3	140.3			143.0	138.5	139.6	136.7	134.4	132.0	
Gross external financing need (in billions of US dollars) 4/	6.3	5.9	5.6	5.9	7.4			7.3	8.3	7.3	7.7	7.5	7.6	
in percent of GDP	10.4	9.5	8.7	9.5	11.6			11.0	11.9	9.9	10.0	9.2	8.8	
Scenario with key variables at their historical averages 5/								**58.0**	**60.8**	**63.5**	**64.7**	**66.0**	**67.3**	**-5.0**
Key Macroeconomic Assumptions Underlying Baseline														
Real GDP growth (in percent)	4.2	2.6	2.4	-4.1	7.5	3.1	2.9	3.6	3.3	3.2	3.2	3.2	3.2	
GDP deflator in US dollars (change in percent)	-1.3	0.5	0.8	0.6	-3.9	1.1	3.1	-0.2	2.5	1.8	2.1	2.1	2.1	
Nominal external interest rate (in percent)	3.2	3.6	3.5	3.0	2.6	3.1	0.3	2.9	3.0	3.2	3.4	3.5	3.7	
Growth of exports (US dollar terms, in percent)	4.1	10.7	5.9	-12.1	19.4	5.7	7.8	12.6	9.9	5.5	5.6	5.5	5.4	
Growth of imports (US dollar terms, in percent)	5.9	8.1	-1.2	-12.5	26.0	4.3	9.7	13.2	9.6	5.0	5.0	5.2	5.0	
Current account balance, excluding interest payments	-2.3	-1.4	0.3	0.3	-1.9	-2.0	1.7	-1.7	-1.3	-1.1	-0.8	-0.7	-0.6	
Net non-debt creating capital inflows	4.5	4.0	4.3	2.7	5.5	4.3	0.8	5.2	5.0	4.9	4.9	4.8	4.8	

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

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

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

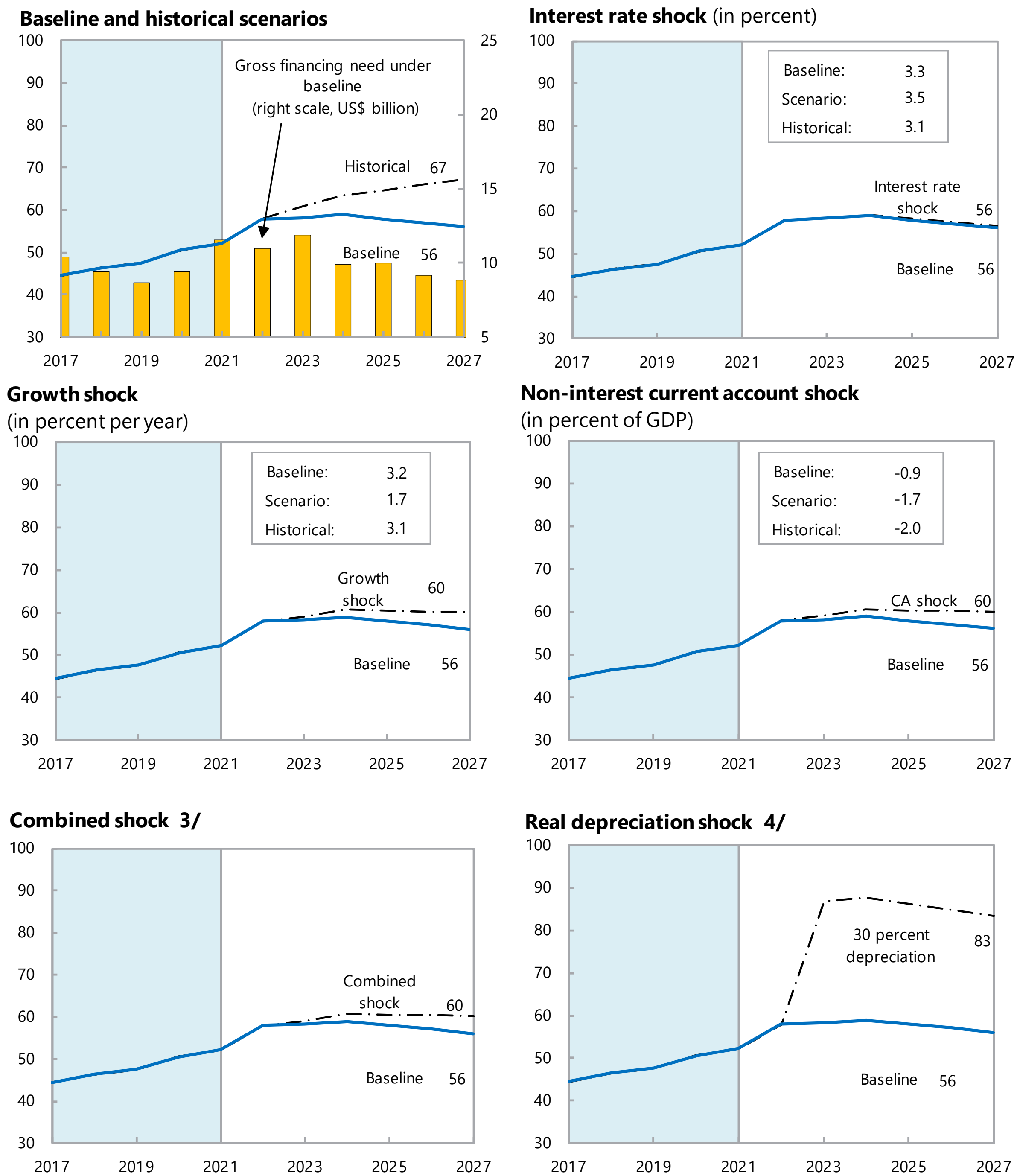
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

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

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

Figure AIII.6. Costa Rica: External Debt Sustainability: Bound Tests[1/2/]

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2023.

Table AIII.2. Costa Rica: Decomposition of Public Debt and Debt Service by Creditor, 2021-23[1]

	Debt Stock (end of period) 2021			Debt Service 2021	2022	2023	2021
	(In millions of US$)	*(Percent of total debt)*	*(Percent of GDP)*	*(In millions of US$)*			*(Percent of GDP)*
Total	**42,436.1**	**100.0**	**66.5**	6,790.6	7,051.0	7,989.2	10.6
External	**10,548.1**	**24.9**	**16.5**	541.0	706.8	1,922.2	0.8
Multilateral creditors[2]	4,590.4	10.8	7.2	195.5	346.4	477.1	0.3
IMF	805.8	1.9	1.3				
World Bank	1,291.6	3.0	2.0				
ADB/AfDB/IADB	1,555.0	3.7	2.4				
Other Multilaterals, o/w:	938.1	2.2	1.5				
CAF	526.8	1.2	0.8				
Central American Bank for Economic Integration (CABEI)	411.3	1.0	0.6				
Bilateral Creditors	457.7	1.1	0.7	16.5	31.3	27.9	0.0
Paris Club, o/w:	220.4	0.5	0.3	10.9	16.3	11.5	0.0
French Development Agency (AFD)	144.9	0.3	0.2				
Japan International Cooperation Agency (JICA)	66.9	0.2	0.1				
Non-Paris Club, o/w:	237.3	0.6	0.4	5.6	15.1	18.1	0.0
Exim Bank of China	237.3	0.6	0.4				
Bonds	5,500.0	13.0	8.6	329.1	329.1	1,417.2	0.5
Commercial creditors	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other international creditors	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	**31,888.0**	**75.1**	**49.9**	6,249.6	6,344.2	6,067.0	9.8
Held by residents, total	31,246.7	73.6	48.9	n/a	n/a	n/a	n/a
Held by non-residents, total	641.3	1.5	1.0	n/a	n/a	n/a	n/a
T-Bills	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Bonds	31,585.4	74.4	49.5	6,234.0	6,324.3	6,058.0	9.8
Loans	302.5	0.7	0.5	15.7	19.9	9.0	0.0
Memo items:							
Collateralized debt[4]	0.0	0.0	0.0				
Contingent liabilities	5,664.3	13.3	8.9				
o/w: Public guarantees	867.4	2.0	1.4				
o/w: Other explicit contingent liabilities[5]	4,796.9	11.3	7.5				

1/As reported by Country authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same as the DSA.

2/ "Multilateral creditors" are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears).

3/ Debt service figures reflect budgetary execution, which is not forecast beyond the current year at the creditor level.

4/ Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral.

5/ Includes other-one off guarantees not included in publicly guaranteed debt (e.g. credit lines) and other explicit contingent liabilities not elsewhere classified (e.g. potential legal claims, payments resulting from PPP arrangements).

Annex IV. Capacity Development Integration: Country Strategy Note[1]

Costa Rica's capacity development (CD) efforts are aligned with the reform objectives under the Fund-supported program, building on the progress to date. CD priorities include improving fiscal institutions, strengthening the central bank's autonomy and governance and the supervisory and crisis management, and advancing structural reforms to foster green and inclusive growth. The authorities' engagement and ownership on these issues remain strong. Given their heavy use of CD from the Fund and other partners, close integration between CD activities and program priorities as well as coordination with other technical assistance providers remain critical.

Context

1. **Despite the authorities' timely response, the COVID-19 pandemic took a heavy toll on Costa Rica, exacerbating pre-existing fiscal and social challenges.** Following the disbursement under the Rapid Financing Instrument in 2020, the Executive Board on March 1 approved the country's request for a three-year arrangement under the Extended Fund Facility (EFF) to further support the authorities' response and gradual economic recovery, while anchoring their policy and reform efforts. The program's reform priorities have benefited from the authorities' broad-based political and social dialogue with key stakeholders and are anchored by three key pillars: (i) implementing equitable fiscal reforms to ensure debt sustainability, while protecting the poor and most vulnerable; (ii) maintaining monetary and financial stability, while continuing to strengthen the central bank's autonomy and governance and addressing structural financial vulnerabilities; and (iii) advancing structural reforms to support inclusion, while boosting labor productivity, under the government's strong commitment to fighting climate change. With a new government set to take office in May 2022, CD will continue to play a key role in the Fund's engagement with the authorities to advance the implementation of priority reforms.

Engagement Strategy

- **Fund's CD Engagement with Costa Rica**. Historically, the Costa Rican authorities have received extensive CD, with generally good traction and implementation record. Some of the CD implemented over the years has offered textbook cases of how CD can improve the quality of policy making, for example, with the punctual update of the base year of the national accounts (NA), which helps measure the informal sector, or the publication of tax expenditure reports as part of the budget process. Table AIII.1 and AIII.2 summarize the key CD priority areas and

[1]This country strategy note and the attached table matrices illustrate the integration of capacity development and program objectives, guided by key recommendations in the IMF Board Paper *2018 Review of the Fund's Capacity Development Strategy*. The acronyms in the note refer to the following IMF and other CD providers: Central America-Panama-Dominican Republic Regional Technical Assistance Center (CAPTAC-DR); Fiscal Affairs Department (FAD), Finance Department (FIN), Institute for Capacity Development (ICD); Legal Department (LEG), Monetary and Capital Markets Department (MCM); Statistics Department (STA); Inter-American Development Bank (IDB); Organization of Economic Cooperation and Development (OECD); World Bank (WB); and United Nations (UN).

engagement since January 2019. Looking ahead, Costa Rica is expected to remain a heavy user of CD, consistently with the program agenda.

- **Integration of CD in Fund's surveillance and lending.** CD delivery in Costa Rica has traditionally been closely integrated with the surveillance priorities identified in previous Article IV Consultations and been following recommendations of the 2018 Financial Sector Stability Review. This coordination effort is being stepped up under the EFF-supported program, with the country team and CD providers working closely together, including through mission participation, to ensure CD is consistently integrated in the authorities' reform priorities and effectively supports program implementation. Appropriate sequencing of CD across reform streams is coordinated by the country team, in consultation with the authorities and CD providers, including CAPTAC-DR, as appropriate. The Fund's resident representative office also plays a key role in these efforts.

- **Collaboration with other partners** remains strong, especially in the areas of debt management and targeting accuracy of social safety net where efforts with the WB are being closely coordinated. To support the authorities' goal of improving public spending efficiency and transparency as well as fostering an inclusive and green recovery, staff continues to engage with multilateral and bilateral donors—including the WB on climate change adaptation and business climate; the IDB on public employment reform, climate change mitigation, FinTech, and development of road infrastructure through public-private partnership; the OECD on improving reporting standards of state-owned enterprises; and the UN on gender and education. Staff is engaging with other CD partners on a regular basis through joint meetings and/or missions and regularly debriefs donors to ensure consistency of policy advice and synergies in supporting the program's objectives.

CD Priorities

2. The main CD objectives for Costa Rica focus on consolidating the achievements to date and making further progress on macro-critical reform areas under the authorities' Fund-supported program. These include implementing fiscal reforms to support inclusive and green growth while ensuring debt sustainability and further strengthening the autonomy and governance of the Central Bank of Costa Rica (BCCR) as well as the supervisory and crisis management framework to maintain monetary and financial stability. Fund's CD is expected to support these main reform areas as follows:

3. Implement fiscal reforms to support inclusive and green growth while ensuring debt sustainability. To tackle the large fiscal imbalances built up over the past decades, the authorities approved a comprehensive fiscal reform in 2018, which included a mix of tax reforms and spending measures as well as the introduction of a new fiscal rule with spending ceilings to ensure debt sustainability. The authorities also plan to take steps to strengthen price incentives to support their National Decarbonization Plan through revenue instruments, based on the options for environmental tax reforms identified by past CD by FAD. Building on these efforts, the Fund-supported program aims at improving fiscal institutions, including through more efficient revenue administration and public financial management, strengthening the social safety net, as well as high-quality data reporting and analytical and forecasting capacity going forward.

- *Revenue administration: FAD/CAPTAC-DR.* To promote further tax reform gains, this workstream supports the authorities' revenue mobilization efforts through Tax and Custom Compliance Improvement Plans (SB) and the implementation of the Hacienda Digital project and new dual income tax.

- *Public financial management: FAD/CAPTAC-DR.* CD in this workstream supports the planned development of a comprehensive Medium-Term Fiscal Framework covering the entire non-financial public sector (SB) as well as improvement of the Treasury's cash management. To foster inclusive growth, CD efforts also focus on an action plan on gender budgeting as well as the recent centralization and digitalization of the payment system for all cash transfer social assistance programs (SB), supporting parallel work by the WB to strengthen targeting accuracy of social safety net. The recent PIMA will improve public investment efficiency and resilience to climate change) in support of the authorities' ambitious climate change infrastructure agenda (SB).

- *Debt management: MCM, in coordination with the WB.* CD efforts aim at deepening the domestic debt market and enhancing debt management in line with international best practices, including by updating the Medium-Term Debt Strategy (SB).

- *Government financial statistics (GFS) and macro-fiscal capacity building: STA/CAPTAC-DR/ICD.* Building on progress to date, CD by STA/CAPTAC-DR in the GFS area continue to support efforts to improve the quality and timeliness of fiscal reporting, expand coverage beyond the central government, and transition from GFSM 1986 to GFSM 2014. CD by ICD will also help enhancing the analytical and forecasting capacity of the MoF with the development of a comprehensive macro-fiscal framework and delivery of customized training.

4. Further strengthen the autonomy and governance of the BCCR and the supervisory and crisis management framework. The authorities have advanced the implementation of the 2018 FSSR recommendations, including by approving new laws on consolidated supervision and banking resolution, strengthening the macroprudential framework and monitoring of systemic risk, and implementing the national financial education strategy. Progress is underway in several critical areas to maintain monetary and financial stability and address remaining structural financial vulnerabilities.

- *Central bank operations: LEG/MCM/CAPTAC-DR.* This workstream by LEG supports the authorities' efforts to further strengthen the BCCR's operational autonomy and governance, as recommended by the 2020 Safeguards Assessment (SA), with draft amendments to the BCCR Law prepared in August 2021 (SB) for submission to the Legislative Assembly (SB). CD by

MCM/*CAPTAC-DR* is also supporting the deepening the FX market to facilitate effective risk management and increased intermediation in local currency.

- *Financial Crisis Management*: *LEG/MCM*. CD by LEG/MCM will support the authorities' efforts to improve alignment of the legal framework on bank resolution and deposit insurance with international practices based on the already conducted gap analysis that will guide further reforms, including with regard to adequate institutional arrangements for the deposit insurance fund and the resolution authority, safeguards for resolution, and clear resolution triggers.

- *Financial Supervision and Regulation: CAPTAC-DR/MCM*. Ongoing CD by CAPTAC-DR/MCM is also helping strengthen supervision and regulation, including by enhancing consolidated supervision and gradual adoption of Basel III. In addition, CD by CAPTAC-DR/MCM will engage in dialogue with Costa Rican authorities on climate change issues and will support the authorities' efforts to enhance FinTech regulation and cybersecurity.

Table AIV.1. Costa Rica: Capacity Development Integration Matrix Under the EFF-Supported Program

Specific Area	Objectives	TA/Training engagement	Achieved Outcomes	Future CD and Program Outcomes
Implementing Fiscal Reforms to Support Inclusive and Green Growth While Ensuring Debt Sustainability				
Ensuring debt sustainability by improving tax collections, fiscal institutions, and analytical capacity, while strengthening social protection				
Tax Policy	Improve tax policy under principles of efficiency, fairness, and sufficiency.	• FAD: options for environmental taxation; tax expenditures analysis and measurement.	• Publication of tax expenditure reports as part of the budget process.	• Assess available revenue options to strengthen price incentives to support climate change. • Achieve full compliance with BEPS.
Revenue Administration	Mobilize revenue by strengthening core tax administration functions and improving tax compliance.	• FAD: Tax Administration and Diagnostic Assessment Tool (TADAT), Revenue Administration Gap Assessment, risk and tax liability management and Compliance Improvement Plans (CIPS). • CAPTAC-DR: risk-based post-clearance audits.	• TADAT assessment completed. • New Custom Portal aligned with WTO TF Agreement. • Submission of a bill containing a new Custom Law. • Develop and implement Tax CIPs.	• Update estimates of VAT and CIT compliance gaps. • Implement Hacienda Digital project.
Public Financial Management	Strengthen treasury and fiscal risk management, strengthen the medium-term fiscal framework (MTFF), introduce gender budgeting (GB), and improve public spending efficiency	• FAD: efficiency improvement of the payment system for social programs and PIMA, and development of a MTFF and GB. • CAPTAC-DR: improve Treasury and fiscal risk management and coverage and	• First MTFF report for the central government (CG) published. • Methodology for fiscal risk reporting formulated. • General assessment of the Treasury Single Account (TSA) operation and coverage completed.	• Create and staff a macro-fiscal unit. • Publish a MTFF for Non-Financial Public Sector (NFPS). • Expand coverage of the TSA. • Implement PIMA recommendations. • Develop GB.

Table AIV.1. Costa Rica: Capacity Development Integration Matrix Under the EFF-Supported Program (continued)

		quality of fiscal and financial reporting.	• Centralize and digitalize payment system for cash transfer social assistance programs.	
Financial Integrity	Further promote transparency and accountability of public procurement processes.	• LEG: strengthen legal framework to enable collection and publication of beneficial ownership information.	• New public procurement law approved.	• Draft and enact implementing regulations to enable collection and publication of beneficial ownership information for awarded contracts.
Debt Management	Enhance public debt management by undertaking institutional reforms, updating the medium-term debt management strategy (MTDS), and developing the domestic debt market.	• MCM: Assist with institutional reforms of debt management function and deepening of domestic debt markets. • MCM/WB: Update MTDS.	• Publication of guidelines for public institutions debt management. • Debt Committee established on public debt management.	• Structure operational responsibilities of the Public Credit Directorate and the National Treasury. • Deepen domestic debt market and improve price formation and auction mechanism. • Update MTDS to also include government's contingent liabilities.
Macro-Fiscal Capacity Building	Improve macro-fiscal projections and develop a comprehensive macro-fiscal framework	• ICD: Assist with the development of a macro-fiscal projection model.		• Develop comprehensive macro-fiscal framework to support policy decisions and MTFF.
Government Financial Statistics (GFS)	Improve timeliness, quality, and comprehensiveness of public sector fiscal, financial and debt accounting.	• CAPTAC-DR: Compile and reconcile high frequency CG GFS and PSDS and expand coverage.	• Higher frequency of GFS and PSDS complied and disseminated. • 51 public institutions.	• Fully adopt 2014 GFSM accrual accounting standards for NFPS data.

Table AIV.1. Costa Rica: Capacity Development Integration Matrix Under the EFF-Supported Program (continued)

		• STA: Support towards 2014 GFSM adoption.	consolidated under CG	•
Maintaining Monetary and Financial Stability				
Strengthening exchange rate flexibility, the central bank's autonomy and governance, and supervisory and crisis management framework, while addressing structural financial vulnerabilities				
Specific Area	**Objectives**	**TA/Training engagement**	**Achieved Outcomes**	**Future CD and Program Outcomes**
Central Bank Operations	Strengthen BCCR's operational autonomy and governance as well as its functions as a risk monitor, a lender of last resort (LOLR), and an inflation targeter.	• CAPTAC-DR: Design a LOLR facility. • MCM/CAPTAC-DR: Deepen FX market and develop derivatives markets. • LEG/FIN: Update SA, and clarify BCCR's legal mandate, and strengthen its decision-making structure, autonomy, and transparency and accountability mechanisms.	• Regulation on emergency liquidity assistance facility approved by the BCCR Board in July 2018. • Legal reforms to further strengthen the BCCR's operational autonomy and governance drafted and submitted to the MoF.	• Deepen FX market, increase daily variation in net open FX position limits, introduce BCCR FX swaps, develop interbank markets to increase liquidity, and promote legal reform to allow greater NFPS' FX activity with FX intermediaries. • Amend the BCCR law to align its mandate, autonomy, decision-making structures, and transparency and accountability mechanisms with international best practices.
Financial Supervision and Regulations	Strengthen the resilience of the financial sector through enhancing consolidated supervision of financial groups, mitigating risks associated with high financial dollarization, as	• MCM: FSSR follow-up. • CAPTAC-DR: Revamp credit risk management framework, improve liquidity risk monitoring; strengthen supervisor's stress testing capacities,	• Greater exchange rate flexibility, and prudential policies implemented to discourage dollarization. • Liquidity risk monitoring improved with the introduction of liquidity coverage	• Further discourage financial dollarization by: (i) revising the definition of "unhedged borrowers"; (ii) assessing the change from provisions to additional capital requirements on foreign currency loans

Table AIV.1. Costa Rica: Capacity Development Integration Matrix Under the EFF-Supported Program (continued)

	well as advancing risk-based prudential supervisory framework.	and develop regulatory framework for consolidated supervision. • MCM/CAPTAC-DR: regional training and country dialogue on integrating climate change consideration into financial policies; enhancing FinTech and cybersecurity regulation.	ratio (LCR) and the expected introduction of a net stable funding ratio (NSFR). • Credit-risk regulation revamped. • Strengthened supervisory stress test models/tools of credit, market, liquidity and contagion risks.	to unhedged borrowers and issuing the corresponding regulation; and (iii) publishing data on unhedged FX borrowing. • Introduce regulations for consolidated supervision of financial groups. • Integrate climate change into financial policies. • Enhance FinTech and cybersecurity regulation.
Macroprudential Policy Framework and Systemic Risk Analysis	Strengthen the resilience of the financial sector through enhancing macroprudential (MAP) frameworks and systemic risk monitoring.	• MCM: FSSR follow-up. • Develop a NSFR.	• Financial Stability Committee established to coordinate MAP policy. • A NSFR to take effect from 2023. • Crisis management protocols in place.	• Strengthen macro-financial stress testing tools, including on climate risks.
Financial Crisis Management	Enhance financial safety net and crisis preparedness framework.	• MCM/LEG: Strengthen banking resolution and deposit insurance legal framework.	• A roadmap developed to close the gaps identified in the legal framework. • Legal amendments drafted for submission to CONASSIF.	• Submit the revised law on bank resolution and Deposit Guarantee Fund for Legislative Assembly's approval.
Real Sector Statistics	Strengthen compilation and dissemination of macroeconomic and financial statistics for	• CAPTAC-DR: compile a quarterly supply and use table (SUT) and improve monthly economic activity	• GDP rebased to 2017. • Rebased GDP published by industry and expenditure	• Develop financial accounts, balance sheets, revaluation and other volume changes in asset accounts, and

Table AIV.1. Costa Rica: Capacity Development Integration Matrix Under the EFF-Supported Program (concluded)

	decision making according to internationally accepted statistical standards.	indicator (IMAE), annual accounts, and non-financial asset balance sheets.	approach, in line with the 2008 SNA. • Main 2008 SNA recommendations implemented.	quarterly SUT for all sectors to meet national data and ISWGNA minimum requirements.

Table AIV.2. Costa Rica: IMF Capacity Development Missions, 2019-to date[1]

TA/Training Mission	Provider	Mission Date
Implementing Equity-Enhancing Fiscal Reforms to Ensure Debt Sustainability		
Revenue Administration		
Strengthening taxpayers' registry	CAPTAC-DR	February 2019
Strengthening risk management	CAPTAC-DR	May, November 2019, February 2020
Customs: improvement of risk analysis	CAPTAC-DR	March 2019
Improvement of clearance process	CAPTAC-DR	March 2019
Risk management for improving tax and customs compliance & improving registration process	CAPTAC-DR	June 2019
Process management	CAPTAC-DR	June, October, November 2019
Integral cargo control plan	CAPTAC-DR	June 2019
TADAT Assessment	FAD	June 2019
Improving management of declarations	CAPTAC-DR	August 2019, January 2020
Improving tax filing compliance	CAPTAC-DR	January 2020
Strengthening Strategic Planning	CAPTAC-DR	June 2020
Strengthening the identification, assessment, and quantification of compliance risks	CAPTAC-DR	July, October 2020
Improving tax services for tax compliance plan	CAPTAC-DR	September 2020
Improving import and export process	CAPTAC-DR	October 2020, February 2021
Workshop: Tax compliance risk management	CAPTAC-DR	December 2020
Enhancing cargo control program	CAPTAC-DR	March 2021
Strengthening auditing of large taxpayers	CAPTAC-DR	February, April 2021
New Customs Law	CAPTAC-DR	April 2021
Definition of new functionalities and technology transfer for the new Customs Web Portal	CAPTAC-DR	April 2021
Development of Tax CIP	FAD	April 2021
Improvement in tax compliance risk management	CAPTAC-DR	May, July 2021
Strengthening of tax audit	CAPTAC-DR	October 2021
Implementation of Tax CIP	CAPTAC-DR/FAD	August, October 2021
Post clearance audit Mission	CAPTAC-DR	October 2021
[1] Missions completed by February 15, 2022.		

Table AIV.2. Costa Rica: IMF Capacity Development Missions, 2019-to date (continued)		
Public Financial Management		
Fiscal risk-specific risks	CAPTAC-DR	April, November 2019, November 2020, June 2021
Treasury management and fiscal risks	CAPTAC-DR	April 2019, January, March, April 2021
Treasury management – coordination between Treasury and Credito Publico	FAD	June 2019
Hackathons on the payment system of social programs	FAD	June, July, November 2019, February 2021
Accounting - IPSAS & consolidation	CAPTAC-DR/FAD	July, November 2020, August 2021
Treasury Single Account	FAD	August-September 2021
Medium-term fiscal framework (MTFF)	FAD	July 2020, March 2021
Centralization and digitalization of cash transfer social assistance programs	FAD	August 2021
Management for the improvement of assets and liabilities	CAPTAC-DR	November-December 2021
Public investment management assessment (PIMA)	FAD	November-December 2021
Gender budgeting	FAD	January-February 2022
Comprehensive, credible and policy-based budget preparation – MTFF & MTFF for NFPS	CAPTAC-DR	December 2021
Financial Integrity		
COVID financial integrity measures	LEG	March-December 2021
Debt Management		
Updating medium-term debt management strategy (MTDS), and institutional reform and deepening debt markets	MCM	November 2021
Macro-Fiscal Capacity Building		
Macro-fiscal projecti on model	ICD	September 2021
Government Finance Statistics		
Assessment of CG high frequency data	CAPTAC-DR	June 2019
Compilation of high frequency CG GFS and PSDS, including data from ODs	CAPTAC-DR	September 2020
Reconciliation of high frequency CG GFS and PSDS, including data from ODs	CAPTAC-DR	October 2020
Adoption of GFSM 2014 for CG GFS and PSDS	CAPTAC-DR	June 2021
Improving compilation and coverage of GFS and PSDS – Including customized training for PSDS	CAPTAC-DR	September, October 2021
Maintaining Monetary and Financial Stability		
Central Bank Operations		
Safeguards assessment update	FIN/LEG	July 2020
Developing FX market framework	MCM	February 2021
Assisting the BCCR to prepare amendments to the Central Bank Law	LEG	March, July 2021

Table AIV.2. Costa Rica: IMF Capacity Development Missions, 2019-to date (concluded)		
Monetary operations scoping mission	CAPTAC-DR	August 2021
Derivatives Market Development: Introduction of Currency Swap	CAPTAC-DR	November 2021
Financial Supervision and Regulation		
Regional TA: CCSBSO Accounting standardization process	CAPTAC-DR	October 2019, August 2020
Credit risk regulation: strengthening management and provisioning regulations, including COVID-19 effects	CAPTAC-DR	January, April, May 2019, July-August 2020
FSSR follow-up: insurance and pensions (WAH)	MCM	February 2019
Regional TA: Cross-border consolidated supervision procedures related to Corporate Governance	CAPTAC-DR	March 2019
Supervisory liquidity stress test	CAPTAC-DR	December 2019, September-December 2020
FSSR follow-up: insurance supervision	MCM	October 2020
Regional TA: IFRS convergence and COVID-19	CAPTAC-DR	October 2020
Developing regulations for consolidated supervision of financial groups	CAPTAC-DR	February-March 2021
Regional TA: IFRS 15 and banking commissions	CAPTAC-DR	May 2021
Financial Crisis Management		
Roadmap for strengthening legal framework for banking resolution and restructuring	MCM	April 2021
Strengthen legal framework for deposit insurance and bank resolution	LEG/MCM	February 2022
Real Sector Statistics		
Preparation of quarterly SUT and sectoral accounts for rebasing national accounts to 2017	CAPTAC-DR	July 2019, August 2020
National accounts: define statistical samples for the monthly survey of non-financial services	CAPTAC-DR	October 2019
Annual sectoral accounts: compile non-financial balance sheets for the total economy and the non-financial corporations	CAPTAC-DR	December 2019
Implementation of 2008 SNA	CAPTAC-DR	March 2020
National accounts statistics: Source data for the volume of services index	CAPTAC-DR	January 2021
National Accounts Statistics: balance sheet	CAPTAC-DR	February, October-November 2021
Webinar on Business Information and Macroeconomic Management	CAPTAC-DR	February 2021
Quarterly accounts and seasonal adjustment	CAPTAC-DR	July 2021
Price statistics	CAPTAC-DR	January 2022
National accounts statistics: Source data for the use of the digital fiscal invoice	CAPTAC-DR	December 2021

Appendix I. Letter of Intent

San José, March 9, 2022

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Ms. Georgieva:

This Letter of Intent (LOI), and the attached memoranda, present our updated policy commitments at the First and Second Review of the Extended Arrangement under the Extended Fund Facility (EFF) from the IMF. Amid the ongoing challenges posed by the COVID-19 pandemic, our economic program, supported by the extended arrangement, is playing a critical role in securing macroeconomic stability, supporting a vigorous economic recovery, and promoting a stronger, greener, and more inclusive growth over the medium run.

For the first and second reviews, we have met all the end-July and end-December 2021 quantitative performance criteria by comfortable margins. On the back of prudent spending under the fiscal rule and strong revenue overperformance, fiscal outcomes have been much better than anticipated, resulting in improved confidence and more favorable market conditions. The inner target band under the program's Monetary Policy Consultation Clause, set under a very different outlook for global price pressures, was breached in December, triggering a consultation with IMF staff. We continue to comply with the continuous performance criteria. We are also advancing our ambitious structural reform agenda. We met the structural benchmark on the BCCR's law, with the draft amendments submitted to the Ministry of Finance to further enhance the BCCR's operational autonomy and governance. We also met the end-December structural benchmarks on the centralization and digitalization of the social assistance cash programs and on the new Tax Compliance Improvement Plan. While the structural benchmark on the Public Employment Bill was not met by end-May 2021 as originally envisaged, the Legislative Assembly approved this landmark reform to strengthen the equity and efficiency of the public compensation system in early March. The end-December benchmark to publish the 2020 financial statements of three state-owned enterprises according to IFRS standards was not met and we are taking actions to resolve remaining reporting issues.

Our ongoing fiscal consolidation efforts have delivered a strong fiscal overperformance in 2021 and we are on track to achieve a primary surplus of 1 percent of GDP by end-2023 and a debt-to-GDP ratio of 50 percent of GDP by end-2035, in line with our program objectives. Given the still heightened risks to the outlook and the social impact of the pandemic, we remain committed to making progress on our proposed fiscal package in the Legislative Assembly, with progressive revenue measures and stronger social cash-transfer programs, to ensure a balanced composition of our fiscal consolidation efforts.

The attached Memorandum of Economic and Financial Policies (MEFP) and Technical Memorandum of Understanding (TMU) update the versions dated February 10, 2021 and set out the economic policies that we intend to implement to achieve the objectives of our Fund-supported program. The government and the BCCR will continue to provide the Fund with the data and information necessary to monitor performance under the program, including those specified in the TMU. We believe that the policies set forth in the attached MEFP, together with the previously issued MEFP and LOI, are adequate to meet the objectives of our economic program, but we stand ready to take additional measures as appropriate. We will maintain close communication and consult in advance with the Fund on the adoption of new measures or revisions of the policies contained in the MEFP and in this letter, in accordance with the Fund's policies on such consultations.

In view of the strong quantitative performance, the macroeconomic policies implemented to achieve the main program objectives and the progress on the structural reforms under the program, we request completion of the First and Second Reviews of the Extended Arrangement under the EFF. We request the purchase of SDR 206.23 million upon completion of these reviews. We also request a five-month extension of the current arrangement until July 31, 2024, the addition of one review and a rephasing of access, shifting SDR 103.115 million from both the first- and second-review purchases to a new sixth review, with a March 15, 2024 availability date. The proposed extension and rephasing will provide additional time to the incoming administration to design and implement reforms under the EFF-supported program, anchoring macroeconomic stability and supporting investor confidence, and is consistent with the duration of the extended arrangement as approved by the Costa Rican Legislative Assembly in July 2021. In keeping with our policy of transparency, we authorize the publication of this letter and its attachments as well as the associated staff report.

We are grateful to the IMF for the ongoing support to Costa Rica during the pandemic, including through the new SDR allocation which helped bolster the BCCR's reserves. IMF support has been absolutely critical in strengthening market confidence and anchoring our fiscal consolidation efforts. We look forward to continuing our close cooperation under the EFF.

Sincerely yours,

/s/	/s/
Rodrigo Cubero President, Central Bank of Costa Rica Governor of the IMF	Elian Villegas Minister of Finance

Attachments (2)
Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

1. The government of Costa Rica remains fully committed to the economic reform program supported by the extended arrangement under the EFF. The arrangement was approved by the IMF Executive Board on March 1, 2021 and ratified by the country's Legislative Assembly on July 19, 2021. This memorandum outlines in detail the progress we have made toward meeting the objectives of our Fund-supported program and our policy plans to advance these objectives. Tables 1 and 2 summarize performance to date and how we plan to update the quantitative targets going forward, as well as progress made with structural benchmarks.

2. Our economic reform program aims at securing macroeconomic stability, while fostering an inclusive, green, and sustainable recovery from the pandemic. Our policy and reform efforts remain anchored around three main pillars: (i) gradually implementing equitable fiscal reforms to ensure debt sustainability, while protecting the most vulnerable; (ii) maintaining monetary and financial stability, while continuing to strengthen the central bank's autonomy and governance and addressing structural financial vulnerabilities; and (iii) advancing structural reforms to facilitate inclusion, while boosting labor productivity and fighting climate change. These broad-based efforts will help support a more inclusive, green, and sustainable growth in Costa Rica over the medium term.

I. MACROECONOMIC DEVELOPMENTS AND OUTLOOK

3. The Costa Rican economy is showing a strong recovery, despite external headwinds. Prior to the COVID-19 shock, macroeconomic conditions were broadly stable, although the fiscal situation was fragile, with a high fiscal deficit and rising public debt, which had contributed to slowing growth since 2016. The pandemic hit the Costa Rican economy hard in 2020, severely impacting the already weak fiscal accounts and generating sizable balance-of-payments needs. Strong export performance, supported by higher growth in trading partners and rapid adjustment of exporters to the new conditions, allowed for a smoother-than-expected contraction in 2020. Despite global supply chain bottlenecks, a severe deterioration in the terms of trade and ongoing fiscal consolidation efforts, economic activity has recovered very vigorously in 2021, on the back of a robust rebound in domestic demand, helped by the availability of vaccines, and continued export dynamism. Real GDP growth is estimated at around 7.5 percent in 2021 and projected at 3.6 percent in 2022. The outlook remains subject to downside risks, amid the threat of new and more aggressive COVID variants, tighter global financial conditions, and higher commodity prices. Over the medium term, economic growth is expected to moderate back to its potential of around 3 percent. Inflation accelerated in the last quarter of 2021, reaching 4.9 percent y/y in February 2022, mainly driven by the increase in commodity prices, but is expected to adjust back within the BCCR's tolerance band of 2-4 percent over a one- to two-year horizon. The slow recovery in tourism receipts, an important source of income in the balance of payments, combined with a higher import bill, will continue to weigh on the current account deficit in the short term, notwithstanding strong goods export performance.

II. PROGRAM PERFORMANCE

4. **We have made important progress with program commitments.** The end-July and end-December Quantitative Performance Criteria (QPC) on the central government (CG) primary balance were met with large margins, reflecting strong revenue performance and our prudent approach to spending. As a result, we also comfortably met the end-July and end-December Indicative Targets (IT) on the ceiling on debt stock of CG, although the end-September IT was missed by a small margin due to higher-than-expected pre-financing. The end-July and end-December net international reserves QPCs were also met after adjusting for lower-than-programmed domestic FX debt issuance and multilateral disbursements, supported by the SDR allocation last August. The inner target band under the program's Monetary Policy Consultation Clause, set in early 2021 under a very different outlook for international inflation, was breached in December as a result of strong external price pressures, triggering a consultation with IMF staff. We continue to observe the continuous PCs on non-accumulation of new external arrears, non-imposition/intensification of restrictions on the making of payments and transfers for current international transactions, non-imposition/modification of multiple currency practices (MCPs), non-introduction/intensification of import restrictions for BOP reasons, and no conclusion of bilateral payments agreements that are inconsistent with Article VIII obligations. We have also made important progress with our reform agenda. The structural benchmark on the draft amendments to the BCCR's law was met, with the amendments submitted to the Ministry of Finance (MoF) on August 31, 2021. The end-December 2021 structural benchmarks on the new Tax Compliance Improvement Plan and on digitalizing the payment system for cash transfer social assistance programs were also met. The structural benchmark on the Public Employment Bill was not met by end-May 2021 as envisaged, due to unexpected legislative delays on account of pandemic-related suspensions and two thorough constitutional reviews, but the bill was finally approved by the Legislative Assembly on March 7, 2022. The end-December benchmark to publish the 2020 financial statements of three state-owned enterprises according to IFRS standards was not met, as the authorities have needed more time to resolve reporting issues at two companies.

III. FISCAL POLICY

Fiscal Stance

5. **The main priorities of fiscal policy are advancing our efforts to secure debt sustainability, while meeting critical social and health needs and supporting the recovery.** Costa Rica's fiscal balance deteriorated sharply over the past decade, due to a permanent increase in current spending following the global financial crisis. Recognizing the pressing fiscal and financing challenges facing our country, the Government promoted a comprehensive fiscal reform bill to rein in spending and strengthen revenue. This reform, approved by the Legislative Assembly in December 2018, put public debt on a declining trajectory over the medium term, mostly by forcing a significant decline in spending as a share of GDP. The economic contraction caused by the pandemic, however, has made an additional fiscal adjustment necessary to keep debt at manageable levels. Building on a strong revenue overperformance in 2021, we are committed to pressing ahead with the required fiscal consolidation, while continuing to protect the vulnerable and

supporting a sustainable economic recovery. Our efforts to date have contributed to an improved fiscal outlook and we are on track to achieve a primary balance of 1 percent of GDP by end-2023 and reach a debt-to-GDP ratio of 50 percent by 2035. Nevertheless, given the still high level of public debt and risks to the outlook, we plan to implement additional progressive income and expenditure measures during the program period to deliver a faster decline in debt, secure macroeconomic stability and support investor confidence, while fostering inclusive and sustainable growth, in line with the program objectives.

6. **The 2018 reform represented a major milestone towards debt sustainability through strict and comprehensive spending limits and a more efficient and fair taxation system.** The 2018 fiscal reform included tight restraints on public sector remunerations taking effect in 2019 and a fiscal rule tying down spending growth starting in 2020. The reform also enabled reallocation of: earmarked revenues and legally mandated spending (except those mandated by the Constitution) if debt exceeds 50 percent of GDP. In addition, from July 2019, the reform introduced a full-fledged VAT to replace the General Sales Tax. The new VAT taxes services fully while allowing for a proper crediting system. Income taxation was also strengthened mainly through: (i) globalization and harmonization of capital income and gains tax at a 15 percent rate since October 2019; (ii) phasing-in of new rules for corporate income taxation (CIT), including anti-tax haven rules, anti-BEPS measures, thin-cap rules, and loss carry-forward among others as of January 2020; and (iii) further progressivity in personal income taxation (PIT) with additional brackets of 20 and 25 percent for employment income, since October 2019.

7. **In 2020, our fiscal stance was a balancing act between addressing the health, social, and economic effects of the crisis and maintaining fiscal sustainability.** The COVID-19 shock hit the country as the initial phase of implementation of the 2018 fiscal reform just started to bear fruits (with our cumulative deficits in February 2020 more than halved from the previous year). To meet critical needs prompted by the health crisis and respond to the worsening macroeconomic outlook, we swiftly adopted targeted measures, with four supplementary budgets. COVID-related spending in 2020 amounted to about 0.8 percent of GDP at the central government (CG) level and 1.3 percent of GDP at the general government level, of which the majority was devoted to the *Bono Proteger* cash transfer program to protect the most affected and the rest to transfers to the Social Security Fund and health-related spending. To mitigate the impact on business and employment, we also approved a three-month moratorium on tax payments, temporary reductions in the minimum tax base for health and pension contributions and in the ownership tax on transport vehicles, as well as a deferral of the roll-out of the VAT on construction and tourism services. To mitigate the widening of the deficit, as tax revenues fell by 11 percent in 2020, we reduced non-critical spending and adopted offsetting revenue measures. Despite these efforts, the primary deficit for the CG, including newly consolidated public entities, reached 3.8 percent of GDP and the headline deficit reached 8.4 percent of GDP in 2020.

8. **We made important progress towards the program fiscal targets in 2021, supported by expenditure restraint and a strong revenue performance.** The cumulative primary deficit as of end-December was CRC112 billion, about 0.3 percent of GDP, compared to the program target

deficit of CRC640 billion (or about 1.7 percent of GDP) before application of the relevant adjustor. The fiscal overperformance in 2021 largely reflected strong revenue collection, in part a result of a better economic outturn, higher yields from the 2018 tax reform, and improved tax administration but also due to stronger-than-expected one-off revenues from: (i) collections from public entities; (ii) partial recovery from the 2020Q2 tax moratorium; and (iii) higher income tax payments in March 2021 due to the 15-month fiscal year (as the 2018 tax reform shifted the fiscal year from October-September to a calendar year basis); which more than offset the revenue losses from the temporary reduction of the vehicle property tax. These windfalls helped fund additional spending on infrastructure projects than originally planned in the budget, implementation of new COVID protocols for schools, and vaccine doses. On the latter, the Legislative Assembly approved in January, September, and December 2021 resource allocations for the one-off purchase and distribution of COVID-19 vaccines for a total of 0.25 percent of GDP. Moreover, targeted compensatory measures were approved in February to preserve social assistance spending as a share of GDP in 2021. The additional resources were channeled through some of the social assistance programs with the best targeting. We also met unanticipated social, education and other pandemic-related outlays that were not included in the COVID-19 emergency decree, higher interest payments, and settlement of outstanding debt with the CCSS (*Caja Costarricense de Seguro Social*). While this was achieved well within the 2021 budget envelope, we could not prevent a breach of the current spending ceiling under our fiscal rule by about 0.3 percent of GDP. Interest spending was lower than our initial program projections, thanks to improved market conditions and our ongoing debt management efforts. This helped to achieve a much lower overall fiscal deficit. The end-July and the end-December debt ITs were also comfortably met, although we missed the end-September IT by a small margin due to higher-than-expected pre-financing.

9. **We remain committed to further advancing our fiscal consolidation efforts in 2022.** In particular, we will target a primary surplus of CRC287 billion by end-December 2022 (or about 0.7 percent of GDP). To deliver the needed structural adjustment, net of one-offs, we are committed to implementing the following revenue and expenditure measures, consistent with the 2022 budget approved in November 2021 and the fiscal rule:

- ***Tax measures***. The implementation of the 2018 tax reform will continue to generate incremental yields over those already achieved of about 0.04 percent of GDP in 2022, through the scheduled rate increases of VAT on construction-related and tourism services and the phasing-in of new sub capitalization rules for corporate income tax. To further strengthen revenue and deliver a more balanced, inclusive fiscal adjustment, we also remain committed to advancing the progressive and growth-friendly tax bills currently under discussion in the Legislative Assembly. These include (i) removing the income tax exemption for the 14th month salaries for public sector employees; (ii) bringing forward the harmonization of capital gains and income tax at 15 percent; (iii) increasing withholding tax rates on most transfers to non-residents by 5 percentage points (family and personal remittances are exempted); (iv) amending existing legislation to allow for distribution of dividends by SOEs to the CG; (v) further globalizing personal income tax, including by reducing the tax-exempted threshold for wage income from CRC 10 million to CRC 8.4 million; and (vi) replacing the current solidarity property tax with a new luxury immovable property tax. These measures will be complemented by compensatory social transfers to the poorest deciles of the population (see the next bullet).

- ***Spending measures***. To gradually advance debt reduction while meeting critical spending needs, total spending is expected to grow by around 2 percent in 2022 (after excluding emergency spending), in line with the fiscal rule requirements. Any 2021 spending excluded for fiscal rule calculations triggers a downward revision in the 2021 spending base for the calculation of the spending ceilings for 2022. As per another provision of the fiscal rule, the slippage in the fiscal rule current spending ceiling in 2021 has been automatically adjusted downward in the calculation of the total spending ceilings for 2022 (to ensure a return to the spending limits under the rule) and we continue to closely monitor spending execution and adjust appropriations to line ministries monthly. The reduction in primary expenditure as a share of GDP is estimated at 2 percentage points in 2022, net of additional allocations to social programs, and is based on (i) continued wage constraints imposed by the 2018 fiscal reform (freeze in base salaries, annuities, and new hiring; and elimination of all vacancies); (ii) annual nominal reduction of temporary wage components (such as overtime) by 8.5 percent; (iii) freeze in pensions of public sector retirees and current transfers to the public sector excluding CCSS transfers; (iv) cut in non-pension private transfers, non-CCSS public transfers, and transfers with external resources; and (v) annual nominal reduction in spending on goods and services by 11 percent. Following the temporary cuts in 2021 due to delays and reprioritization of capital projects in 2021, capital spending is projected to gradually increase. All these spending measures will continue to be applied over 2022-25. Given that the debt to GDP ratio exceeded 60 percent in 2020 and 2021, in line with the fiscal rule and the PEB, the freeze in basic wage and accrual of annuities will be extended beyond 2025. Although our budget proposal to secure additional funds for social assistance spending in 2021 did not receive support in the Legislative Assembly, we are resolved to secure adequate resources for social protection, especially for the poorest and most vulnerable (MEFP ¶14). We remain committed to staying current on all our payment obligations and not accumulating any spending arrears. Approval by the Legislative Assembly of external loans by our multilateral partners, together with continued improvement in market conditions and ongoing debt management efforts will also help reduce interest expenditure, supporting a lower headline deficit and further debt reduction.

10. Given the still high degree of uncertainty related to the COVID-19 crisis and economic recovery, our program builds in flexibility to deal with unforeseen shocks. Ongoing improvements in tax and customs administration are expected to continue supporting revenue yields in 2022. Approval of the pending tax bills in the Legislative Assembly would also secure our public finances on a firmer footing. Nevertheless, were revenues to underperform, we will propose to the Legislative Assembly temporary tax measures and we will reprioritize non-critical spending as needed to ensure that the primary target goal remains within reach. However, in the event of additional COVID needs, due to a more protracted pandemic, the program targets also allow for an adjustor to accommodate increased COVID-19 emergency spending, for up to 0.3 percent of GDP in 2022, that might emerge from increased transfers to support health services, stronger targeted support to households and businesses heavily affected by the pandemic, or further enhanced social assistance programs to support the most vulnerable groups. On the upside, should the economic recovery continue to take hold faster than expected, we are committed to saving any revenue over-performance in 2022 and outer years to accelerate our debt reduction plans.

11. We will further advance our fiscal consolidation efforts in 2023 and over the medium term to secure debt sustainability, while making space for critical infrastructure and social needs. Additional structural measures over the medium term would consolidate the gains we have made so far. These adjustments will be underpinned by new revenue measures, including those currently under discussion by the Legislative Assembly (MEFP ¶9), to secure a more progressive tax structure to support competitiveness and inclusive growth after the pandemic, as well as the continued yields of the already approved expenditure measures that will remain in place over the medium term (MEFP ¶9), in line with the fiscal rule. In addition, the implementation of our ambitious reform of public-sector employment (MEFP ¶14) will further support our commitment to keeping nominal spending growth low. We will do these while we continue to modernize and strengthen our social safety net. Expected efficiency gains and greater revenue mobilization from the modernization of the tax and custom administration (MEFP ¶13) and PFM reforms (MEFP ¶15) provide important upsides to our ability to tackle our current debt and financing challenges faster than expected under the program, thereby supporting macroeconomic stability and growth.

Structural Fiscal and Debt Management Reforms

12. We plan to take further steps to strengthen price incentives to support our climate change response through revenue instruments. Costa Rica has pledged to reduce greenhouse gas emissions to a net absolute maximum of 9.11 million tons of carbon dioxide equivalent (CO_2e) for 2030, a maximum net emissions budget in the period 2021 to 2030 of 106.3 million tons of carbon dioxide equivalent (CO_2e). It has also pledged to achieve zero net emissions by 2050 (MEFP ¶42). As part of our efforts to strengthen price incentives, we are developing a revenue-neutral feebate scheme to promote low-emission vehicles comprising a sliding scale of fees to vehicles with above average emission rates and a sliding scale of rebates to vehicles with below average emission rates, and re-structuring annual taxes on used vehicles to include a revenue-neutral feebate component related to local air emission rates for accelerating retirement of older, more polluting vehicles (excluding farm vehicles), in conjunction with the current tax on vehicle value. We finalized and published our assessment of available options in early March 2022. This will be followed by a public consultation. These measures will be phased in to minimize the impact on the lowest quintiles of the population. Other efforts to strengthen price incentives include updating and expanding the current Payment for Environmental Services (PES) scheme to support payment for ecosystem services beyond carbon sequestration (including transfers for reforestation efforts to inhabitants of remote areas), to support more types of carbon sequestration (including blue carbon and organic carbon in soils) in the context of the Costa Rican Offset Mechanism (MCCR), which replaces the existing "Mercado Doméstico de Carbono." The PES expansion will be financed by the Green Climate Fund of US$54 million awarded to Costa Rica by UNDP in May 2021 in recognition of the capture of CO_2 made possible by the country's reforestation.

13. We are strengthening revenue administration to support our fiscal consolidation plans. Since 2018, we have taken steps to strengthen tax collection by enforcing electronic invoicing, deploying new audit programs, and improving our framework for tax information exchange with other jurisdictions. Building on the 2019 Tax Administration Diagnostic Assessment Tool (TADAT) assessment, we are committed to adopting a compliance risk management approach, revamping taxpayer services, and improving the collection of tax arrears. On the customs side, with the expected approval of the new Customs Law by end-March 2022, with IMF TA support, we expect to continue promoting trade facilitation to help increase productivity growth in trade-related sectors and improve revenue collection through more effective risk-based enforcement. To reduce VAT and CIT compliance gap levels, we are refocusing our anti-tax evasion efforts towards enforcement of recently approved tax reforms. The Tax Commissioner approved a new Tax Compliance Improvement Plan in December 2021 (**structural benchmark**), supported by IMF TA, with compliance strategies underpinned by more robust large-scale automated-information cross-matching to detect inaccurate reporting and revamped audit programs focused on VAT on services and erosion of CIT bases through cross-border transactions (BEPS). Progress in the implementation of different compliance risk mitigation strategies will be monitored on a quarterly basis from April 2022 using quantitative and qualitative indicators. We will further enhance our information-driven enforcement capabilities by end-December 2022 through a tax and customs coordinated risk management approach and an effective use of corporation shareholders and beneficial owners' registers, automatic exchange of information on financial accounts (CRS) and Country-by-Country (CbC) reports. We also plan to formulate a complete impact evaluation assessment framework to identify compliance improvement gains by end-2023. Additional revenue administration efficiencies are expected from the MOF's digital transformation plan "*Hacienda Digital para el Bicentenario*", supported by the WB, which will upgrade tax and customs procedures and information systems.

14. We are committed to rationalizing and improving the efficiency and quality of government spending. Beyond what was already mandated by the December 2018 reform, there is significant scope to further rationalize the public wage bill, bringing it back on a sustainable path after its excessive expansion over the last 15 years. We are also committed to enhance the targeting accuracy and delivery of our social protection programs, leveraging on digitalization. As approved under the 2018 fiscal reform, we are effectively reallocating spending away from legally mandated uses (with the exemption of those mandated by the Constitution) when the debt-to-GDP ratio is above 50 percent of GDP.

- ***Public employment reform.*** Although we did not meet the end-May 2021 **structural benchmark,** the Legislative Assembly approved the Public Employment Bill on March 7, 2022, following pandemic-related legislative delays as well as several consultations and two Constitutional reviews. The Bill seeks to modernize and streamline the public administration, bringing the public wage bill on a sustainable path, in line with OECD recommendations. It applies to all public sector institutions except for non-state public entities that operate in the public interest and state-owned companies and institutions that operate under competitive markets. The reform will enhance fairness and productivity by replacing the current salary system, which indiscriminately rewards seniority and civil-service exclusivity, generating perverse incentives for public servants. The new regime adopts a single pay spine with eight job families, consolidating within the single salary other wage supplements such as annuities, bonuses, incentives, and others. Oversight over the design of the single wage spine will be shared between MIDEPLAN and autonomous institutions for their employees (Judiciary and Legislative Branches, Supreme Electoral Tribunal, public universities, municipalities, and CCSS), following the criteria and ceilings approved by the Bill. The Bill will enter into force 12 months after approval, but preparations for the introduction of the single pay spine and related reforms have already started. The Bill, including the introduction of a single pay spine, will be implemented by end-March 2023 (**proposed structural benchmark**). Due to the large wage premium in the public sector, the salaries of the many existing workers that fall above the spine will be frozen until they are reached by the single pay scheme. This, along with the gradual transition to the single wage spine for existing workers whose salaries fall below the reference wage for their occupation (Transitory Disposition XI), will imply that savings can be immediately rendered from the effectiveness of the reform. Depending on new reference salaries, IDB estimates that savings from the reform will range between 0.5 and 0.8 percent of GDP during the first five years for the entire public sector. The Public Employment Bill foresees that new hiring under the new rules will start no later than twelve months after its entry into force. The Bill also introduces rules for recruitment and selection, professional development, and performance assessment, including of top-ranked officials; and new employee benefits including one-month parental leave, two-month extension of maternity leave (for special cases), and sick leave to take care of a family member.

- ***Social assistance***. Costa Rica devotes important resources in its budget (1.8 percent of GDP in 2021) to fighting poverty and reducing inequality. There are opportunities to build on recent improvements and further enhance the effectiveness of some of its social assistance programs through improved coverage and targeting. The delivery system is highly fragmented with different entities engaging in social assistance activities, with scope for improvement in payment processes, institutional arrangements, and transparency of these programs. Following the results of the 2019 hackathon, co-organized with the IMF, we centralized and digitalized the payment system for all cash transfer social assistance programs at the MOF's National Treasury in December 2021 (**structural benchmark**). Specifically, we signed agreements with responsible institutions, issued appropriate regulations, and incorporated the payment software solution into the Digital Treasury system, in coordination with IMAS (Joint Institute for Social Welfare), the CCSS (Costa Rican Social Security Fund), PRONAE (National Employment Program), CONAPDIS (National Council for Persons with Disabilities), PANI (Children's National Welfare Agency), the Ministry of Labor and Social Security, and the BCCR. We are already using the new system with pilot programs for *Avancemos (*including *Crecemos)* and *Programa Nacional de Empleo*. The new system is expected to be fully operational, including for *Régimen No Contributivo de Pensiones,* by end-April 2022. We estimate that this measure will reduce the payment processing time needed to reach the final beneficiaries from 3-5 days to just 24 hours, while improving service delivery to beneficiaries, fiscal operations efficiency, and financial inclusion of the low-income population, especially women, through the adoption of digital payment tools. To continue enhancing the targeting accuracy of our social assistance programs, with the support of the WB, we continue strengthening the role of SINIRUBE (*Sistema Nacional de Información y Registro Único de Beneficiarios del Estado*) as the main instrument to target social protection benefits and services, which will also contribute to a more harmonized framework for inter-institutional coordination. Major social assistance programs have already adopted SINIRUBE. IMAS is supporting institutions that deliver the remaining programs (which represent about 30 percent of social assistance expenditure) to overcome their capacity constraints in using the information from SINIRUBE to better target beneficiaries. In addition to boosting inclusiveness, these two measures will improve spending efficiency, freeing resources for an expansion in the coverage and generosity of social transfer programs to eligible beneficiaries and supporting other fiscal consolidation efforts. In this context, building on the recently approved IMAS Directive 0122-2022, we plan to increase the capabilities of SINIRUBE to respond to higher demands and ensure effective compliance with Directive 060-MTSS-MDHIS, including by assessing whether existing beneficiaries remain eligible or not, based on the information updating process, the established period of validity of benefits and regulated exceptional cases, and the socioeconomic classification of SINIRUBE.

15. We are taking further actions to improve public financial management (PFM) to ensure proper implementation of our fiscal rule.

- **Medium-Term Fiscal Framework**. With support from IMF TA, the MoF published in April 2021 a first Medium-Term Fiscal Framework (MTFF) covering the CG, which provides macro-fiscal forecasts for 2021-2025, improving the credibility of the budget process and presenting a coherent fiscal strategy in line with the fiscal rule. It also contains an analysis of fiscal risks linked to government debt, lawsuits against the state, pension regimes, natural disasters, municipal governments, non-financial public enterprises, financial institutions, and public-private partnerships. This MTFF was updated in September 2021, as part of the submission of the 2022 budget, including a first analysis of macroeconomic shocks and further analysis of debt management. We are working in close coordination with local governments, decentralized institutions apart from the CCSS, and public enterprises in the preparation of the MTFF covering the entire Non-Financial Public Sector to be published by end-April 2022 (**structural benchmark**), one year ahead of the deadline established by the Fiscal Responsibility Law, and working on enhancing NFPS's fiscal projection models, with IMF's TA. That MTFF will also include an analysis and reporting of fiscal risks with contingent liabilities, debt guarantees, and explicit fiscal contingency reserve schemes, and integrate into the fiscal strategy a medium-term public investment plan/framework.

- **Public Investment Management Assessment**. To improve the planning, allocation, and implementation of public investment among the numerous entities currently responsible for infrastructure development, the MoF and MIDEPLAN undertook a Public Investment Management Assessment (PIMA), including a new Climate Module, in November-December 2021, carried out by the IMF jointly with the WB and IDB. Based on the assessment, we have defined a roadmap aimed at strengthening public investment efficiency while making fiscal space for our climate change-related and other critical infrastructure needs, including through improved methodologies for Public Private Partnership projects' evaluation (MEFP ¶40). As part of the roadmap, we will improve project appraisal, selection and implementation as well as medium-term capital budget allocation. In this regard, our planned next steps are to (i) define selection criteria, including climate objectives and a ranking methodology by end-May 2022; (ii) issue guidelines for PPP project appraisal by end-August 2022; (iii) modify the general decree for the public investment system to clarify the appraisal process by end-December 2022; and (iv) build a centralized system to monitor major projects during their implementation phase for the non-financial public sector, as envisaged by bill 22.470 currently under discussion in the Legislative Assembly, by end-April 2023. These efforts will be complemented by specific actions to promote climate-resilient infrastructure (MEFP ¶43).

- **Other key PFM institutional reforms.** In line with IMF TA recommendations, the MoF is also gradually setting up a macro-fiscal unit under which the preparation of the MTFF is centralized. The MOF and the Comptroller's Office will continue working together along the entire budget cycle to ensure compliance with the fiscal rule. We are also taking actions to introduce gender budgeting to better operationalize the gender equality policy agenda. With IMF support, we will complete an initial pilot exercise to identify gender budget spending by end-December 2022 and approve the appropriate legal framework and governance arrangements for gender budgeting by end-December 2023, in coordination with the Comptroller Office for entities outside the CG budget. In addition, we will define a new set of gender budget markers for Hacienda Digital. We have recently resumed our efforts to reduce budget fragmentation, with the consolidation under the CG budget from 2021 of all public entities, as required by Law 9524 of April 2018. Further enhancements on budget consolidation will be analyzed as part of the public sector reform. In addition, with IMF TA support, we will continue improving management of public sector liquidity by extending the Treasury Single Account to decentralized and autonomous entities. Specifically, we will support the reduction of cash held by decentralized and autonomous entities in commercial bank accounts, subject to an analysis of the impact on the liquidity of the financial system, coordinated by SUGEF, BCCR and MoF. We are also working on fully operationalizing the Fiscal Council, with the goal of the Council publishing its first public assessment of the government's fiscal strategy in 2022. We will support the Fiscal Council in developing proper communication tools as well as a memorandum of collaboration with the MoF to clarify the separation of functions and information sharing. Additional expenditure administration efficiencies are expected from the MOF's digital transformation plan "Hacienda Digital para el Bicentenario", supported by the WB, which will modernize and integrate our PFM information systems to better align expenditure policies across core PFM entities, planning, and spending units.

16. We are modernizing our public procurement processes. In accordance with the Social Dialogue's agreements, we are enforcing the use by all procuring entities of the electronic platform Sistema Integrado de Compras Públicas (SICOP). The reform aims at generating potential fiscal savings through better prices, lower transaction costs and improved capacity and expertise. The Public Procurement Law (No. 9986) approved in May 2021 introduced a sound regulatory and institutional framework for managing and implementing umbrella contracts for goods and services, eliminating past exceptions to public bidding processes and increasing competition for government contracts. To promote further transparency and accountability, the MoF has started developing new implementing regulations with specific provisions on the collection and publication of beneficial ownership information, with the regulations to be published by November 2022. The regulation will require all competing bidders to submit accurate and current beneficial ownership information through affidavits as part of the bidding process, which will be made publicly available through a renovated e-procurement portal for all awarded bidders. As an interim measure, with the support of IMF TA, we have issued an amendment to the existing procurement regulation to enable the collection and publication of beneficial ownership information for awarded public procurement contracts. The amendment was published in the Official Gazette in early-March 2022. We launched the new Public Procurement Observatory, which offers open data on public procurement since 2010 contained in the SICOP and SIAC (*Sistema Integrado de la Actividad Contractual*) systems.

17. We continue to foster transparency and adhere to best practices in the procurement and contract awards of any COVID-related spending. The Comptroller's Office developed a Fiscal Transparency Portal for COVID-19, with published information on public purchases and audit results on the use of emergency assistance, while the Ministry of Labor and Social Security created a transparency portal on the Bono Proteger program, which includes the list of beneficiaries, statistics, and reports. Moreover, with IDB support, MIDEPLAN launched a revamped Transparency Portal (*Rendir Cuentas*) with the intention of disseminating CG's COVID-19-related public purchases, subsidies and donations, including data from SICOP, IMAS, MTSS, MINSA, CNE, CCSS and SINIRUBE. On public purchases, the data published in the Portal include information on awarded vendors, including their legal ownership (if tenders required it). The Comptroller's Office continues carrying out specific audits on emergency cash transfers to ensure related funds are used properly and publish them in its Portal.

18. We are committed to improving governance and increasing transparency in SOEs. Although SOEs play a dominant role in many key sectors of the economy, such as electricity, telecoms, transportation, banking and insurance services and petroleum products, some of them present data reporting weaknesses, constraining full assessments of their balance sheets and potentially hiding risks to public finances and taxpayers. To foster greater transparency in line with international standards, we are committed to accelerating full adoption of International Financial Reporting Standards (IFRS) by SOEs. As regards the publication of the 2020 financial statements for three SOEs according to IFRS (end-December 2021 **structural benchmark)**, ICE (*Instituto Costarricense de Electricidad*) was fully compliant, AyA (*Instituto Costarricense de Acueductos y Alcantarillados*) was nearly compliant, and CNP (*Consejo Nacional de Producción*) was partially compliant. Almost all of the remaining SOEs already published their 2020 financial statements in line with IFRS standards. Going forward, AyA is expected to become fully IFRS compliant with the publication of the 2021 financial statements, while CNP will need to implement a new accounting system to fully comply with IFRS. We published the 2020 aggregate report on SOEs performance in February 2021, expanding its coverage to include updates on the implementation of state ownership policy, dividends policy, overall financial performance and values, total employment, cost and funding of public policy objectives, and other SOE-related issues. The 2021 aggregate report was published in February 2022. With support from the OECD and WB, we are committed to bringing SOEs' public procurement within the SICOP by end-December 2022, limiting the use of exceptions for direct public procurement, and gradually eliminating regulations that grant them the right to withhold confidential information.

19. There is significant scope to improve the efficiency of energy companies and support aggregate productivity through lower electricity prices. While Costa Rica's energy companies do not receive CG transfers, they impose a high cost of energy for consumers and the productive sector. During the last year, the Costa Rican Institute of Electricity has been implementing an efficiency strategy to reduce electricity prices in the context of its strategic plan for 2019-23 (Strategy 4.0). This strategy includes actions such as reducing operational costs, restructuring debt, and implementing the IFRS. These efforts were reflected in cumulative tariff reductions in 2021 of 15.98 percent, 12.73 percent, and 13.44 percent in generation, distribution, and transmission, respectively, compared to December 2020. The Government is committed to advancing this efficiency strategy through further debt restructuring and cost reduction in order to achieve lower and more competitive tariffs. For further reduction in energy prices, ICE will continue the execution of its Financial Sustainability Roadmap to reduce fixed costs and renegotiate debt conditions. In particular, ICE will not renew or will renegotiate at affordable terms the private generator contracts as they expire, as a stop of future liabilities. To complement this effort, a bill (No. 22.561) on authorizing private energy generators to sell their surplus energy (after supplying local demand) to the regional market has been submitted to the Legislative Assembly. Autoridad Reguladora de Servicios Públicos (ARESEP) will expand its efforts through 2022 to reduce electricity prices charged by other generators beyond ICE, through applying new tariff methodologies to other distribution and transmission companies, vis-à-vis with the adoption of new benchmark tariffs for generation, distribution, and transmission, with IDB support. ARESEP will continue monitoring distribution companies' financial costs to ensure their investment projects' financing terms fit with the underlying assets' useful lifespan. Efforts are also ongoing to increase competition in the energy sector, with a law (No. 10086) to simplify the administrative procedures for private participation in power generation from renewable sources approved in October 2021.

20. We have launched a comprehensive reform of debt management. To contain the risk of rising debt levels, the President of Costa Rica and the Minister of Finance approved in 2019 a Debt Policy for the Public Sector (Executive Decree 41935-H), which establishes solid guidelines for public institutions to put debt on a sustainable path in the long term. The rising levels of public debt and financing risks amid the COVID-19 crisis have highlighted the urgent need to diversify sources of fiscal financing and better manage the outstanding debt stock. Going forward, our reform agenda will center on three pillars: institutional reforms, medium-term strategy, and domestic market development. Specifically:

- ***Institutional debt management reforms.*** We recently established an Assets and Liabilities Committee, comprising the Treasury, the Public Credit Department (DCP), and members of the soon-to-be-established Macroeconomic Analysis Unit of the MoF as well as the BCCR, to provide strategic guidance and oversee inter-agency coordination of policy decisions related to government debt. By end-December 2022, we will submit an amendment to Law 8131 to the Legislative Assembly to bring all debt-related functions of the government within a unified debt management office, by structuring the operational responsibilities of the DCP and the National Treasury along the front, middle, and back-office functions in line with best international practice, and further improve transparency and reporting of public debt. Finally, as the individual approval of external loans creates additional burden on debt management, we will liaise with the Legislative Assembly to seek a general authorization for external borrowing consistent with the approved annual budgetary and borrowing limits and debt management strategy (see below). As in the case of Laws 7970 and 9070 of 1999 and 2012, respectively, the general authorization will provide the government with greater flexibility for international issuances or official loans.

- ***Medium-term debt management strategy (MTDS).*** We have formalized the publication of the MTDS through Directive Order and have started to update our MTDS for 2023-26, with support from the IMF. We will publish it by end-April 2022 (**structural benchmark**), For the first time, the report will also cover government's contingent liabilities, especially guarantees provided to state-owned companies. Furthermore, we will publish and adhere to Annual Borrowing Plans and Quarterly Issuance calendars in line with the MTDS. Meanwhile, we will strengthen the accounting and budget execution processes of public debt payments at the MOF to improve debt data monitoring and budget control.

- ***Domestic market development.*** We are taking steps to improve the functioning of the primary market and markets operating under the principle of market concentration (Article 23 of Law of the Securities Market) by focusing our issuance on standard fixed-rate bullet bonds of select maturities. Open bond windows and bilateral bond sales are being gradually phased out. We will reform the auction mechanism for Treasury to become a price-taker in bond auctions to improve the price discovery process and form a technical pricing committee to develop guidelines for pricing methodologies. We will further encourage non-resident participation in our debt market by easing regulatory barriers and harmonizing the tax regime for non-resident investors, subject to macroprudential considerations, and are in consultations with Euroclear to allow clearing and settlement of our debt securities on that platform. We will continue to make active use of liability management operations to reduce the rollover risks associated with debt maturing in the next 12-24 months and to smooth the impact of maturing benchmark bonds, in line with our MTDS. Finally, by end-September 2022, with support from the BCCR and IDB, we will roll out a pilot market-making/primary dealer program with a small group of participants with well-defined rights and responsibilities.

21. We are advancing our efforts to improve data quality and transparency in fiscal reporting. We are committed to improving the timeliness, quality, and comprehensiveness of the fiscal, financial and debt accounting for the public sector, with support from IMF's TA. On the quality of the fiscal data, we resumed efforts to fully adopt 2014 GFSM accrual accounting standards for fiscal and debt information, initially achieving this at the CG level. By end-December 2021, we published monthly CG historical series and corresponding metadata. Interest data continue to be cash-based, but we plan to start publishing data on accrued interests by end-March 2022. We will progressively extend this effort to the rest of the public sector, envisaging full adoption of international standards for the fiscal and debt data of the general government by end-December 2022 and of the entire non-financial public sector by end-December 2023. In this context, with IMF TA support, we have started to work in the consolidation of assets and liabilities of local governments, social security and SOEs, and in the reporting of fiscal risks (in the context of the MTFF), to include contingent liabilities, guarantees, concession contracts, and the indebtedness of municipal governments and SOEs. These improvements include the comprehensive collection and reconciliation of financing (below-the-line) data, the harmonization of both methodology and data coverage among national accounts, government finance and public sector debt statistics, as well as coordinated improvements on public sector accounting to guarantee stock-flow consistency, allow balance sheet enhanced analysis and provide improved data for decision making. We will update the program coverage and definitions in line with progress in these areas in subsequent reviews and reflect them in the attached TMU.

IV. MONETARY AND EXCHANGE RATE POLICY

22. **Monetary policy continues to be underpinned by our firm commitment to low inflation within an inflation targeting framework.** Maintaining low and stable inflation, under a flexible exchange rate, is critical to secure domestic and external stability, consistent with the BCCR's mandate. The strong credibility afforded by this regime has allowed not just to keep headline and core inflation moderate, despite strong pressures from import prices, but also to maintain inflation expectations well anchored. In that context, the BCCR has been able to run a strongly countercyclical policy stance during the pandemic, reducing the policy rate to a record low of 0.75 percent in June 2020. Given the more persistent external inflationary pressures, a narrowing output gap and upside risks to the inflation forecast, the BCCR raised rates in December and January 2022 to 1.75 percent to begin unwinding the expansionary monetary policy stance. The inner Monetary Policy Consultation Clause (MPCC) band under the program, set in early 2021 under a very different outlook for global price pressures, was breached in December. As a result, the BCCR Board held a consultation with IMF staff in February 2022.

23. **The Central Bank has taken several measures to support liquidity and facilitate credit conditions in response to the COVID-19 shock.** To support its counter-cyclical stance, the BCCR conducted liquidity and open market operations so as to maintain ample aggregate liquidity. In addition, the BCCR introduced in September 2020 a special, temporary repo facility to provide liquidity support to financial intermediaries for on-lending to debtors affected by the pandemic at favorable conditions. By June 2021, CRC826 billion (2 percent of GDP) had been disbursed. Overall, the favorable credit conditions created by BCCR´s countercyclical monetary policy stance and supportive policies provided immediate cashflow relief to indebted households and firms and helped support credit to the private sector in 2021. While in April 2020 a legal amendment enabled the BCCR to purchase capped amounts of sovereign securities in the secondary market to support market liquidity in episodes of systemic stress, such instrument was only marginally tapped in 2020, with the BCCR unwinding the resulting position by end-July 2021.

24. Monetary policy will remain data dependent and forward looking to meet the inflation target of 3 percent, with a tolerance band of ±1 percentage point, over the medium term. The BCCR will continue to monitor inflation developments closely and communicate clearly and transparently on the drivers of inflation, inflation outlook, and prospects for monetary policy. While inflation remains moderate compared to regional and global developments to date, risks are tilted to the upside. In response to the stronger inflation outlook, the BCCR will continue to raise the policy rate and increase the tightening pace as warranted to keep inflation within the BCCR's tolerance band over a one- to two-year horizon. Progress in meeting the inflation target under the program will continue to be monitored through a Monetary Policy Consultation Clause (MPCC) around quarterly targets (Table 1), as described in the attached TMU.

25. We are committed to maintaining adequate international reserve buffers, while allowing the exchange rate to adjust in line with economic fundamentals and market conditions. Costa Rica operates under a flexible exchange rate regime, intervening only to moderate excessive market volatility. Our foreign-exchange reserve assets, bolstered by financial support from the IMF's RFI, the ongoing EFF arrangement, the August-2021 SDR allocation, and credit lines from other IFIs, have played a critical role to buffer the impact of the pandemic on our balance of payments. The end-July and end-December NIR targets were met by a margin of US$240 million and US$392 million, respectively, net of the relevant adjustors. We will aim at maintaining adequate levels of reserves, in line with the IMF's Assessing Reserve Adequacy (ARA) metric and the net international reserves floor set under the program (Table 1). The Internal Audit Office of the BCCR will regularly review the NIR and underlying data, in line with the definition in the TMU, and, as needed, reconcile them with the audited financial statements as of the end of the fiscal year.

26. To support these efforts, we plan to develop the FX derivative market to enhance effective management of FX risks, with help from IMF TA. In order to deepen the market and help FX intermediaries manage large orders, we plan to revise the net open FX position requirements in line with international best practices. We will promote a legal reform to allow a greater proportion of non-bank public sector entities' (NBPSE) FX activity to be conducted with FX intermediaries. As an intermediate step, we will encourage NBPSE to internalize the market impact of their FX needs by setting indicative daily limits for purchase or sale of FX through the BCCR for each entity, along with fees for exceeding the limits. We will restrict the MONEX to FX intermediaries by end-September 2022. Additionally, we will introduce FX swaps as a tool for BCCR participation in the FX market, by end-September 2023. The envisaged reforms will be conducted in a manner consistent with our Article VIII commitments and the IMF's Institutional View on Liberalization and Management Capital Flows. All these actions to deepen the FX market and allow for greater flexibility of the exchange rate should complement other measures being taken to reduce financial dollarization (MEFP ¶32), which in turn should reduce financial vulnerabilities and strengthen monetary policy transmission.

27. We stand ready to further strengthen the BCCR's independence, transparency, and accountability in the implementation of the flexible inflation targeting regime. The amendments to the BCCR Law in 2019—to tighten the dismissal rules for the BCCR Governor, delink the Governor's term from the political cycle, and remove the Minister of Finance's voting rights in the BCCR Board—have improved the personal autonomy provisions in the law. To further strengthen the BCCR's operational autonomy and governance, and in line with the recommendations of the IMF's 2020 Safeguards Assessment, we submitted to the MoF draft amendments to the BCCR law at end-August 2021, meeting the relevant **structural benchmark**. The final amendments, once approved by the MoF and the President of the Republic, will be submitted to the Legislative Assembly by end-December 2022 (**proposed structural benchmark**). The Executive Branch will take the necessary steps in order to fill the current vacancy in the BCCR Board. In addition, we will develop a long-term roadmap to continue to strengthen the BCCR´s equity position.

V. FINANCIAL SECTOR POLICIES

28. We have made significant progress in financial sector reforms. Over the last years, we have approved and implemented several important financial sector reforms, building on the IMF's 2018 Financial Sector Stability Review (FSSR) and OECD recommendations. Also, as a result of sound prudential policies, the banking system entered the COVID-19 crisis with strong capital and liquidity buffers, as evidenced by the stress test results published in our 2019 Financial Stability Report. Nevertheless, high levels of unhedged FX borrowing and indebtedness in the household and corporate sectors are sources of important vulnerabilities in the financial system.

29. In response to the COVID-19 crisis, we temporarily opened the regulatory space for credit relief provision by financial intermediaries to households and businesses. In March 2020, CONASSIF approved transitional measures to provide space for financial entities to restructure loans, such as by allowing a temporary moratorium on loan servicing for affected borrowers without affecting their credit history and reducing the minimum accumulation of counter-cyclical provisions for financial entities to zero. This led to comprehensive loan restructuring by banks, particularly to the most affected sectors. The BCCR also introduced the special facility to support credit to the private sector (MEFP ¶23).

30. In view of the robust economic recovery, we cautiously unwound many of the temporary measures, while strengthening monitoring and preparedness efforts. Pre-pandemic settings have been restored on the regulatory treatment of restructured loans as of January 1, 2022. At the same time, the use of already accumulated countercyclical provisions and the softer regulatory capital thresholds that define banks' "irregularity" was extended until December 2022. In parallel, we strengthened reporting and monitoring efforts, as laid out in the attached TMU. The Legislative Assembly approved in December 2021, with a delay compared to the original schedule, a 15-year government-funded program for US$270 million to provide guarantees to smaller-sized businesses affected by the pandemic. The program will be administered in line with regulatory best practices, and, to avoid moral hazard, participating banks will remain liable for 25 percent of loan principal, with borrower eligibility limited to loans that were performing prior to the pandemic.

31. We will continue to strengthen our macroprudential policy framework and stress testing capabilities. To coordinate macroprudential policy across agencies, we established in 2016 the Financial Stability Committee (FSC), comprising the President of the BCCR, the President of the National Council for Supervision of the Financial System (CONASSIF) and the Minister of Finance. In May 2019, the FSC strengthened its framework by creating the Monitoring and Coordination Group (MCG), comprising senior representatives of the BCCR, CONASSIF, the Superintendencies, and the MoF, along with supporting technical groups. In January 2020, we changed the presidency of the FSC from a six-month rotation to a permanent basis and appointed the BCCR President as the FSC President. With the unwinding of the extraordinary COVID-19 measures, the technical group supporting the MCG has been meeting frequently to follow up on key systemic developments and financial risks and seeking to detect and anticipate sources of stress. We have strengthened communications with the public, including by publishing our annual Financial Stability Report for the first time in July 2020. Over the years, we have made significant progress in systemic risk assessment by strengthening our credit, market and liquidity risks' stress test models and contagion risk tools. Bottom-up and top-down stress test results have been included in our Financial Stability Report. Going forward, we will continue updating our stress test results and publish them in the Financial Stability Report.

32. **We plan to take further actions to reduce the risks from financial dollarization, as the economic recovery takes hold.** Since 2018, the BCCR has allowed for greater exchange rate flexibility, helping agents internalize exchange rate risks (MEFP ¶25-26), and in 2019 introduced differentiated reserve requirements by currency (with a higher rate for FX liabilities), with the aim to discourage financial intermediation in foreign currency. To complement these efforts, the FSC is closely monitoring the risks from dollarization, and SUGEF and CONASSIF have taken further measures to discourage dollarization, including (i) establishing a higher general provision requirement for loans to non-FX generators, (ii) calculating liquidity coverage requirements by currency, (iii) requiring additional capital requirements for foreign currency mortgages to unhedged borrowers, based on LTV thresholds; and (iv) requiring banks to assess the sensitivity of debtors' payment capacity to exchange rate changes. The latter measure was, however, suspended as one of the regulatory COVID response measures and will be gradually reintroduced in the course of 2022. In line with IMF TA recommendations, SUGEF and CONASSIF plan to (i) review the definition of an unhedged borrower by end-June 2022, with effect from January 2023; and (ii) complete an assessment of the change from provisions to additional capital requirements on foreign currency loans to unhedged borrowers and issue the corresponding regulation by end-December 2023 to take effect from January 1, 2025. Both measures will apply to marginal loans from the corresponding effective date and will take into consideration the Basel III recommendation for risk weight multipliers for unhedged exposures. To increase transparency, we will also begin to regularly publish data on unhedged FX borrowing.

33. **We are advancing efforts to strengthen the prudential regulatory and supervisory regime.** The reforms to the laws on consolidated banking supervision and on securities market regulation passed in 2019 (Law no. 9768) marked important milestones towards effective supervision by strengthening the powers of supervisors, including sanctioning ones, in line with international best practices. SUGEF will introduce by October 2022 regulations to implement the revamped legislation on supervising financial groups. This includes issuing guidelines to strengthen

regulatory provisions and information sharing, and to update the solvency and capital requirements for financial groups. To facilitate effective cross-border supervision, we will also consider expanding SUGEF's scope of supervision to include financial companies that may be linked by common foreign ownership. We are taking further steps to advance our risk-based supervision framework, including by adopting Basel III standards in a phased manner: (i) SUGEF is enhancing its liquidity risk management through recent improvements in the monitoring of the liquidity coverage ratio, and the net stable funding ratio is expected to come into effect from January 1, 2023; (ii) SUGEF is also revamping its credit risk management framework by introducing forward-looking assessment of losses and provisioning requirements, with new regulation and guidelines for provisioning finalized in November 2021, to come into effect from January 1, 2024; (iii) we have revised banks' capital definition, established conservation and systemic importance capital buffers, and the definition of systemically important institutions, in line with Basel III, with the regulation issued in August 2021, to come into effect from January 1, 2025. These effective dates will allow for a sufficient adjustment period in the context of the pandemic and the combined effect of the new regulations on the financial system. During the adjustment period, the financial entities will be required to assess operational and financial impacts and send these results to SUGEF on a quarterly basis starting in the last quarter of 2022.

34. We will continue to strengthen our financial safety net by implementing our banking resolution and deposit guarantee framework in line with best practices. We have advanced our crisis preparedness framework considerably, with the approval by the Legislative Assembly in February 2020 of the law on banking resolution and the creation of a deposit guarantee fund (DGF) (law no. 9816). Implementing regulations have been in effect since May 2021, and quarterly payments into the DGF started in October 2021. We have adopted a roadmap, with support from IMF TA, to further strengthen the legal framework on bank resolution and deposit insurance, including adequate institutional arrangements for the DGF and the resolution authority, safeguards for resolution, and clear resolution triggers. In this context, we plan to prepare and submit amendments to Law 9816 to CONASSIF by end-July 2022, and to the Legislative Assembly by end-March 2023, to allow time for consultations with the industry and other stakeholders. The draft will include the legal power to regulate and supervise resolution and recovery plans. The financial safety net and the crisis preparedness framework have also been strengthened by the continuous monitoring of macro-financial risks by the MCG (MEFP ¶31), assisted by the recent implementation of an early warnings system (which was updated with the pandemic); the implementation by the FSC of an updated contingency plan for episodes of financial stress, with the inclusion of a communications protocol; and the BCCR´s recent enhancement of its Lender of Last Resort mechanism.

35. We are pressing ahead with our efforts to promote financial inclusion and banking competition. During the pandemic, a sharp increase in the use of electronic transactions and the allocation of *Bono Proteger* (MEFP ¶7) have led to a significant increase in bancarization and financial inclusion. However, structural issues, such as limited banking competition and partial coverage of the credit registry, push up lending rates and hinder financial inclusion. In line with the IMF's FSSR recommendations, we have developed a national strategy for financial education, coordinated by the Ministry of Economy, Industry and Commerce (MEIC), and made good progress in its implementation. We formed a strategic alliance with 20 financial institutions, which have provided financial training to around 350 thousand people and achieved 14 million views of financial education material on social media. To broaden access to our payment system and promote digital banking, we have simplified requirements for opening a bank account and launched an electronic payment system for public transport nationwide. CONASSIF and the four superintendencies, in coordination with the BCCR and the Ministry of the Economy, are also working on draft legislation for financial consumer protection. With support from IMF TA, we will ensure that our regulation strikes a good balance between fostering innovation and protecting financial stability. In addition, with support from the IDB, CONASSIF, BCCR and the superintendencies are working on the design and implementation by end-June 2022 of a Financial Innovation Center to support and provide guidance to fintech startups. The Center will support our plans to strengthen and develop new regulation on fintech, including sandboxes and crypto assets. We are committed to improving the design and scope of the public credit registry, *Centro de Información Crediticia* (CIC). With support from the Alliance for Financial Inclusion, we will prepare draft legislation by end-December 2022 to build a modern credit registry, with information from supervised financial entities and non-supervised credit providers. We are committed to strengthening the governance and efficiency of the SBD as well as developing alternative instruments to strengthen synergies between private banks and SMEs, including through the guarantee fund (MEFP ¶30). This should facilitate access to credit by SMEs and under-served sectors. The BCCR and MEIC have also recently launched a database that compares credit products across the financial system, to enhance information for financial consumers and foster bank competition.

36. We remain fully committed to combating money laundering and countering terrorism. Costa Rica continues to strengthen its technical compliance with the FATF standards on AML/CFT to help the fight against money laundering and terrorist financing. CONASSIF has approved regulations to make our sanctioning framework more effective, proportionate and dissuasive, incorporate new regulated subjects, and adopt a new regulatory and legal framework related to beneficial ownership, including in revised SUGEF Regulation 12-21 of September 2020. CONASSIF has also updated regulations (effective from January 1, 2022) to strengthen the due diligence measures that financial entities must carry out for politically exposed persons, the financing of political parties, and the receipt of cash especially in foreign currency. In January 2021 CONASSIF approved SUGEF regulation 35-21 that established the *Centro de Información Conozca a su Cliente* (CICAC) as a centralized repository of customer information that will promote transparency, efficiency, and cost reduction concerning know-your-client (KYC) monitoring and supervision. This regulation became effective in January 2022. The CICAC is now accessible to financial entities supervised by the four superintendencies attached to CONASSIF and the gradual filling of the database will start in July 2022. In accordance with Law 9416 and Decree no. 41040-H, to strengthen information and transparency on beneficiary ownership, we created a centralized registry and started collecting shareholder and beneficial ownership information in 2019 for all legal entities except trusts, third-party resource managers and non-profit organizations. As of October 2021, trusts have been included, and we intend to include the rest of the entities by end-December 2023. With respect to designated non-financial businesses and professions, close to 5,000 legal entities and individuals are registered in SUGEF. The regulation allows SUGEF to "suspend" the registration of legal entities and individuals that do not comply with regulatory requirements, which prevents regulated financial intermediaries to provide services to them. More than 1,500 registered legal entities and individuals have been suspended (all by automated means) and 694 remained suspended as of end-December 2021. CONASSIF and the Financial Intelligence Unit will continue to dedicate resources to AML/CFT supervision and collaboration between competent authorities and carry out inspections with the required frequency.

37. We are pressing ahead our efforts to green the financial sector, in support of Costa Rica's ambitious climate change agenda. In 2019, the BCCR joined the Network of Central Banks and Supervisors for Greening the Financial System (NGFS). We also established within the BCCR the Group for Strategic Analysis of Climate Change (GAECC), comprising representatives of different departments of the BCCR, and now also CONASSIF and the superintendencies, to address the impacts and risks related to climate change on the central bank's main objectives. With support from GAECC, we have developed a roadmap to integrate climate change considerations (MEFP ¶42-43) into the design of monetary and financial policies. The roadmap is centered around four blocks: establishing reliable and comparable data, strengthening modeling and analytical capacity for scenario analysis, promoting climate change risk management in the financial system, and greening international reserves.

- ***Data.*** The BCCR is taking stock of the required data to adequately analyze the impact of climate change and, with support of the WB, aims to identify suitable indicators that can serve as a reference to measure and monitor climate-related risks (that would be placed in a comprehensive information repository by end-December 2023).

- ***Modeling.*** With support from the IDB, the BCCR has developed an integrated economic and environmental model to conduct impact analysis of climate policies. The BCCR aims at being fully operational in the analysis of different climate scenarios combined with various mitigation and adaptation policies by end-December 2024.

- ***Climate change risk management***. The BCCR is assessing the interlinkages between climate-related and macro-financial variables as well as the risks to the financial system from climate change. The BCCR plans to incorporate the recommendations of the Network of Central Banks and Supervisors for Greening the Financial System in its "top-down" stress-testing methodologies by end-December 2022.

- ***Greening international reserves.*** The BCCR hopes to lead the search of an investment portfolio for its international reserves that is environmentally friendly and increases exposures to issuers with the best environmental performance. The BCCR aims to publish indicators of the "greenness" of its reserve holdings by end-December 2022.

GAECC, CONASSIF, and the superintendencies have been coordinating efforts on climate change issues, including aligning CONASSIF´s agenda with the National Strategic Plan 2050. The BCCR plans, in coordination with the supervisory authorities and within their respective mandates, to obtain firm-level disclosures of climate-related risks to inform the design of regulatory and supervisory approaches to manage these risks.

VI. STRUCTURAL REFORMS TO BOOST PRODUCTIVITY AND PROMOTE GREEN AND INCLUSIVE GROWTH

38. We are resolved to further advancing our growth-enhancing reform agenda, supporting a resilient recovery from the COVID-19 crisis. In May 2021, Costa Rica officially became an OECD member, following a successful accession process, which saw the introduction of 14 landmark legal reforms and many administrative reforms. Going forward, we remain fully committed to further advancing our reform agenda. Specifically, our strategy hinges on three key objectives: (i) protecting the most vulnerable from the impact of the crisis and supporting inclusion, including by promoting greater female labor force participation; (ii) boosting productivity growth, including by eliminating barriers to business formalization, investment, and job creation; and (iii) promoting a green recovery, anchored by our National Decarbonization Plan and the goal of becoming a zero net emission economy by 2050.

39. We have implemented a comprehensive package of measures to protect the most vulnerable from the COVID-19 shock and support the reopening of our economy. In response to the pandemic, we have promoted and enforced compliance with health protocols, and expanded hospital capacity. In December 2020, we launched a large-scale vaccination campaign, to control the pandemic and support the reopening of the economy. As of February 28, 2022, 74.1 percent of the population was fully vaccinated, and 25.7 percent had already received a booster dose. We aim to fully vaccinate all eligible population and apply booster vaccines to vulnerable groups by end-2022. In 2020, we also introduced temporary tax relief as well as targeted subsidies to households affected by the pandemic through the *Bono Proteger* (MEFP ¶7). Building on earlier efforts to increase labor market flexibility, we enacted a new legislation to protect employment through temporarily reduced working hours, made social security contributions proportional to the time worked and deferred their payments until the end of the year, and lowered minimum social security contributions for a period of six months (MEFP ¶7). In addition, in December 2021, the Legislative Assembly approved a temporary US$270 million credit guarantee fund to support businesses affected by the pandemic (MEFP ¶30). We have also launched measures to support small-and medium-sized agricultural businesses and exporters via the *Alivio* program. Costa Rica has been successful in attracting near-shoring-oriented FDI during the pandemic. We will continue to explore these and other opportunities to further catalyze the economic recovery, including by creating incentives for employment in the tourism sector.

40. We are taking steps to foster productivity growth to attract investment and create jobs. Our efforts focus on reducing skill mismatches and promoting innovation, closing infrastructure gaps, cutting red tape, and attracting FDI:

- ***Education.*** We have taken measures to improve the quality of the education system to address skill mismatches and increase human capital. We completed a review of the evaluation system for teachers in November 2021. This will inform the development of a new performance-based evaluation model, which we plan to start implementing in February 2023. Updated curricula (with basic and specialty subjects) are expected to be implemented for 175 schools by end-June 2023, with 80 schools already approved for implementation. We have resumed the regular student performance tests for 2021, including in digital and scientific fields, which had been suspended due to the pandemic. In February 2021, we introduced a Bilingualism Education Policy, with an Action Plan to ensure all students, include those in rural areas, are proficient in a second language by 2040. To help address the impact of the pandemic on educational outcomes, we are establishing training plans and we will be offering training courses nationwide to improve teaching performance in the use of digital technologies, in collaboration with universities and other entities. Going forward, we will continue to reduce the digital gap by providing the necessary infrastructure, improving teachers' digital capacity (including through mandatory training), and ensuring teachers and students, especially from low-income families, have access to the necessary equipment, among other measures. In addition, we are developing a work plan, aimed mainly at vulnerable groups (such as migrants), to enhance the equity of our education system and attract more investment in education, in collaboration with the UN. We will also continue to ensure sufficient resources for equity programs within the Ministry of Public Education. To address the demand for specific technical skills, we passed a dual vocational training law in 2019 and improved the access, quality, and innovation capability of the public higher education system, in collaboration with the WB. We are revising our existing vocational curricula in the context of Industry 4.0, to be implemented by end-December 2023, with support from the IDB. The INA (Instituto Nacional de Aprendizaje)'s Organic Law has been amended to provide this vocational institution with greater autonomy and agility for administration and hiring, with employability as its key objective, in line with ILO recommendations. We will also continue linking public universities' funding to labor market needs and enhance their connections to the business world through integration in the National Science and Technology Information System to promote innovation and allow firms to benefit from access to state-of-the art knowledge and skills, in line with recommendations from the IDB and the OECD.

- ***Investment climate.*** To attract investment, we are making efforts to identify spending priorities and promote PPPs, with support from CABEI and IDB, to reduce existing physical and digital infrastructure gaps, consistent with our fiscal consolidation plans under the program. With IDB support, we recently launched the Program of Road Infrastructure and Promotion of PPP and will provide critical training on PPP development across central and local governments during 2022-2024. Another critical step in promoting investment is our ongoing effort to reduce electricity tariffs (MEFP ¶19). To help reduce firms´ transaction costs, through the Digital Transformation Strategy 2018-2020, we have strengthened our digital infrastructure, including with the establishment of a digital government portal and improving cybersecurity. As a result, Costa Rica ranked #76 in the Global Cybersecurity Index 2020, advancing 39 positions from 2019. To further reduce the digital divide in the country, especially increasing access for the most vulnerable, we are developing—with support of the IDB—a new National Telecommunications Plan 2022-2027 by end-April 2022. To reduce red tape, we have designed a national strategy to promote administrative reforms and strengthen regulatory reform efforts of the central government. We have also launched Costa Rica Fluye—a project aimed at Smart

Deregulation in 25 public institutions—and implemented a single-window system (VUI) where businesses can apply for licenses and permits. In line with OECD recommendations, we reformed in November 2021 the Law for the Protection of Citizens from Excess Requirements and Administrative Procedures to reduce the administrative burden for businesses, including by promoting the use of sworn declarations. To further cut red tape, we are working with 23 additional local governments to simplify procedures to start a business, integrate environmental permits, and centralize procedures at the national level to provide for a single point of contact, in line with OECD recommendations, by end-June 2022. In addition, the new bankruptcy law (Ley 9957), which entered into force on December 1, 2021, simplifies the bankruptcy process to reduce the duration and cost of liquidation proceedings and promote restructuring of affected firms—a key toolkit to support the post-COVID recovery. To foster FDI attraction, already one of Costa Rica´s strengths, we will promote innovation clusters to remove information barriers and facilitate the integration of domestic firms in global value chains.

- ***Formalization.*** To incentivize formalization, in 2019 the CCSS modified the social security contributions model to temporarily lower employer and employee social security contributions for new microenterprises during their first four years of operation. In 2017, the CCSS launched a sectoral pilot program with a reduced minimum contribution base for domestic workers. To ensure the burden of social security payments is lower for vulnerable workers, in 2020 the CCSS expanded these programs with the creation of a specific mechanism to provide coverage for coffee harvest workers, including migrants. This novel model changed the tripartite contribution mechanism involving the worker, employer and state to a two-party modality where contributions are covered by the state and ICAFE, Costa Rica´s coffee institute, eliminating the burden for workers. To encourage formal part-time or flexible employment, the CCSS is currently formulating a plan to adjust the minimum contribution base for part-time workers, which will be approved by the CCSS Board of Directors by end-June 2022 (**proposed structural benchmark**) and implemented by end-July 2022. In addition, to help workers move to the formal sector jobs and reduce unemployment, we have established a nationwide single-window shop (*ane.cr*) that facilitates the contact between job seekers and companies and connects people to training opportunities and will include other complementary services, such as childcare. To reduce the administrative burden for firms, over the last four years we reduced the number of minimum wages from 26 to 16 and plan to further reduce it to 11 by end-December 2022, in line with OECD recommendations. We will further support these efforts by implementing our national strategy for transitioning to the formal economy, with technical assistance from the ILO.

41. As part of our efforts to promote inclusive growth, we continue to focus on increasing female labor force participation. Costa Rica's long-standing provision of universal healthcare, pensions, and general education has supported greater inclusiveness and equality of opportunities. We aim at further promoting inclusive growth by strengthening female labor force participation, which is considerably lower than for men, despite women's better education outcomes. In this context, we launched in September 2020 the Gender Parity Initiative (IPG), with support from the IDB, WEF, and AFD, to reduce women's care burden—the top obstacle to female labor force participation—and promote their participation in the labor market and leadership positions. Under the IPG, we plan to implement, over a minimum period of three years, an action plan with measures ranging from regulatory changes to awareness-raising initiatives that involve public and private sectors. We are also exploring options for gender budgeting to support the implementation of IPG and other initiatives to reduce the gender economic gap (MEFP ¶15).

- ***Childcare.*** The 2018 fiscal reform expanded the definition of public education to include early education centers, with a view to helping reallocate funds to increase the supply of public childcare services. In 2021, we increased childcare services to cover 15,000 additional children (relative to 2017), with a focus on children up to 5 years old, improving access for low-income households and implementing a co-payment scheme for middle-class families. We are aiming to further expand childcare services to cover an additional 8,000 children (relative to 2021) to enable an increase in childcare coverage to 8 per 100 children aged 0 to 12 years (which represents 23 percent of children aged 0 – 12 living in poverty). Stronger childcare facilities can in turn support educational outcomes and labor productivity (MEFP ¶40). The Public Employment Bill has also introduced for public sector workers one month of paternity leave, a two-month extension of maternity leave (in specific cases), and paid leave to take care of a family member.

- ***Long-term care.*** We launched in early 2021 a National Care Policy 2021-2031 to establish a long-term care system and reduce women's family care requirements (Decree 42878-MP-MDHIS). The plan will be progressively implemented along five pillars: governance, data intelligence, strengthening of care supply and benefits, generation of conditions for closing gender gaps in labor markets, and quality assurance. In addition to strengthening the coverage of day centers and long-term residences, the system will also establish home care and assistance services for dependent people. The Mixed Institute of Social Help (IMAS), the National Institute of Women (INAMU) and the Ministry of Labor and Social Security (MTSS) are working, with support from UN Women, on a mechanism to prioritize provision of care services in households where there is potential for women to enter (or remain in) formal employment, and to ensure money transfers to caregivers living in extreme poverty where the prospect for paid employment is low. We plan to complete the protocols for eligibility by end-March 2022 and we might refine them after a planned pilot with support from UN Women. We intend to fully implement the new Policy for all eligible women by end-December 2022. We will also launch by end-March 2022 three pilots of care services to test its feasibility and cost/efficiency, financed by the IDB. In parallel, in an effort to unify access to services and extend coverage, we will implement a single dependency scale and a co-payment scheme based on family income by end-December 2022.

- ***Education and entrepreneurship.*** The ongoing efforts to strengthen our education system and vocational training (MEFP ¶40) as well as to deepen financial inclusion (MEFP ¶35) will be critical to support women's economic empowerment. We will continue to foster the participation of women in STEM fields, in collaboration with the IDB, and implement our national action plan for gender equality in scientific and technological fields, which will strengthen female labor force participation and productivity growth.

42. We are strongly committed to promoting environmentally sustainable medium-term growth, implementing our ambitious National Decarbonization Plan. Recognizing the need for prompt and bold action to mitigate climate change, in 2019, we launched a National Decarbonization Plan, which aims at transitioning to a zero net emissions economy by 2050, in line with the Paris Agreement. With almost 100 percent of the electricity matrix currently sourced from renewables, we start off from a strong position.

- ***National Strategic Plan and governance.*** In March 2021, we released the Territorial Economic Strategy for an Inclusive and Decarbonized Economy 2020-2050, with support from the IDB. The Strategy aims to make a gradual transition to an inclusive and decarbonized economy by 2050, with 12 development poles, six corridors—that will facilitate the interaction between these poles—and 12,750 km^2 of territorial management areas. The strategy involves policy measures on economic growth, social inclusion, human capital, gender, infrastructure and connectivity, and natural capital. After a broad-based consultation with public sector stakeholders and with support from the IDB and GIZ, we plan to launch by end-April 2022 the National Strategic Plan 2050, which will serve as the country's main long-term planning instrument to implement the Strategy. MINAE's National Directorate of Climate Change oversees our Carbon Neutrality Country Program (PPCN 2.0), which supports the country's mitigation efforts by providing a mechanism for the voluntary adequate management of greenhouse gas emissions for public and private organizations. To further support the governance of the ecosystems, we will establish a Secretariat for the Energy and Ecological Transition, to mainstream decarbonization and adaptation measures across line ministries, by end-June 2022. The Secretariat will also implement, coordinate, and operate the National Climate Change Metrics System (SINAMECC) to facilitate compliance with the Plan's reporting requirements and access to information to measure the progress in meeting the revised nationally determined contributions (NDCs). Moreover, we will set up the National Ambition Cycle aimed at establishing a data-driven, highly inclusive process to update NDCs and long-term climate action plans including the National Decarbonization Plan. The National Ambition Cycle decree will be ready by end-March 2022 and will establish the Strategic Climate Change Planning System (SiPECC)—initially intended to comprise MINAE, MIDEPLAN, BCCR and UCR—to ensure the sustainability of the modelling and analysis capabilities that have been developed over the last six years. Our recent modeling work, with support from the UN, has confirmed the job creation potential of our National Decarbonization Plan, which will also support the recovery efforts from the pandemic. Moreover, we are developing models to conduct impact assessment of the overall climate change strategy, with a focus on jobs and growth as well as gender and inequality, with a first study completed in November 2021. Additional analytical work will study the technical profiles for new green and blue jobs by end-November 2022 and identify transition pathways for different industries to move towards decarbonization by end-March 2023. We are also establishing a just-transition governance structure to ensure that the transition to a zero net emission economy does not cause adverse consequences for the labor market, with support from the ILO. In addition, with a view to promoting the greening of the financial sector, the BCCR joined the Network for Greening the Financial System in 2019 and completed in June 2021 a roadmap to integrate climate change considerations into the design of monetary and financial policy (MEFP ¶37).

- ***Electrification of transport sector.*** To reach our goal, we will continue to encourage fleet electrification processes in the transport sector—the largest contributor to greenhouse gas emissions. Specifically, we have set up a promotional electric tariff for the supply of electricity associated with charging centers for electric buses and incorporated it into the current tariff schedules of electricity distribution companies. With support from the IDB, we have installed 40 charging centers nationwide, with other 21 centers expected by end-December 2022 and included unit (fleet) electrification considerations in the operators' concession contracts. For the latter, bill 22.923 extending the periods of line concessions for public buses—subject to a commitment to convert at least 40 percent of the fleet to electric units during the contractual term—from 7 to up to 15 years, was submitted to the Legislative Assembly in early March 2022. In parallel, we have started to sign agreements with the bus companies. By end-May 2022, we expect to have signed 12 agreements to cover all the bus routes for the Greater Metropolitan Area. Moreover, we are developing price incentives to support this transformation to a zero net emission economy (MEFP ¶12).

- ***Agriculture, forestry, and marine ecosystems.*** The agriculture and forestry sector play a major role in carbon sequestration and are therefore key to reaching our zero net emission target. With support from the WB, we will further support farmers in adopting low-carbon technologies and practices by providing technical assistance, promoting agricultural research on low-carbon solutions, and further developing financing instruments. We are also developing nationally appropriate mitigation actions for rice, sugarcane and bananas, with support from the IDB and AFD. In recognition of our emissions reduction during 2014-15, we received the first disbursement (US$23.9 million out of a total of US$54 million) from the Green Climate Fund in January 2022 to support our continued efforts in reforestation and ecosystem conservation (through the National Fire Management Program, the enhancement to the Indigenous Payment for Environmental services, and the Payment for Environmental Services). We will also receive, during 2022-25, US$60 million from the Forest Carbon Partnership Facility through the Emission Reductions Purchase Agreement (ERPA), for the projected CO_2 reduction during 2018-2024. In addition, with support from the WB, we will implement the Benefit Sharing Plan associated with the ERPA, which includes allocation of grants to reduce deforestation and forest degradation, which will foster the green economy and improve communities' resilience and livelihoods. Additional initiatives aim at reducing emissions in the construction and industrial manufacturing sectors as well as improving wastewater management. We are also committed to supporting the "blue" economy through sustainable and innovative approaches to the use of coastal areas while ensuring their conservation. We aim at protecting 30 percent of our marine territory under conservation schemes by end-December 2022. To this end, in December 2021, we signed the decree 43368-MINAE to expand the protection of Coco Island National Park and Montes Submarinos Marine Area to consolidate the protection of important marine ecosystems as well as endangered species and high commercial value ones and promote sustainable tourism and other economic activities while preserving the health and resilience of the ocean. This is part of a broader regional conservation and management strategy in the Eastern Tropical Pacific which aims to establish a transboundary biosphere reserve to consolidate swim-ways or underwater biological corridors that will connect Cocos Island (Costa Rica), Galapagos (Ecuador), Malpelo (Colombia) and Coiba (Panama) by end-December 2024.

- ***Environmental trade.*** We are making progress in negotiating an Agreement on Climate Change, Trade and Sustainability (ACCTS) with five other countries (Fiji, Iceland, New Zealand, Norway, Switzerland) to ensure that our trade policy supports the goals set forth by the National Decarbonization Plan. We and other ACCTS members have agreed to work towards eliminating tariffs on environmental goods trade, barriers to environmental services trade, and environment-damaging subsidies and commitments, as well as promoting good practices for the development of voluntary eco-labeling systems.

43. In parallel, we are pushing ahead with our adaptation efforts, given the considerable vulnerability of our people and economy to climate change. To establish adaptation goals for 2018-2030 and bring together efforts from different sectors of the economy, we launched the National Policy on Adaptation (PNA) to climate change in 2018.

- ***National Adaptation Plan.*** A National Adaptation Plan is expected to be completed by end-March 2022. We have already developed climate risk maps for extreme hydrometeorological events for 23 cantons of the country and expect to cover all remaining cantons by end-March 2023. In addition, with support from the WB, we are strengthening our National System for Disaster Risk Management—which has been in force since 2006—in line with the Institutional Strategic Plan 2018-2022 of the National Commission for Risk Prevention and Emergency Care, with a particular focus on financial management in public investment (see below). To support the most vulnerable productive sectors, we also introduced a new insurance scheme in 2019, which allows agricultural producers to insure their harvest against climate change risks and offers lower premia for producers implementing adaptation measures. In 2020, we started AGROINNOVA 4.0, a national program which promotes the application of technology to increase productivity and sustainability in the agricultural sector.

- ***Infrastructure resilience.*** Going forward, we will continue to support adaptation initiatives by climate-proofing our infrastructure, which is crucial to mitigating the fiscal impact of climate-related natural disasters and protecting coast lines. Specifically, with WB support, we have built climate change considerations into public financial management, by updating the methodological guidelines for the preparation and appraisal of public investment projects to incorporate principles to handle exposure and resilience of public works to extreme weather events. We are addressing the recommendations of the climate module of the PIMA (MEFP ¶15), with support from IMF TA, to strengthen our institutional readiness to address climate-rated risks through infrastructure planning and investment and support the development of relevant institutions. As part of the key recommendations, we will (i) develop a standardized methodology for climate change analysis in project appraisal and incorporate it in the existing MIDEPLAN guidelines annex on natural disaster risks by end-November 2022; (ii) include climate policy objectives among the transparent set of selection criteria in revisions of the technical rules by end-May 2022; and (iii) include climate related risks in a standardized methodology for the non-financial public sector for estimating capital maintenance needs, as envisaged by bill 22.470

currently under discussion in the Legislative Assembly, by end-April 2023. These efforts will support the ongoing development of a roadmap, with support from the WB, to enhance infrastructure resilience by end-September 2022 (**structural benchmark**) with a view to guiding the technical planning and implementation, including through an assessment of the medium-term investment needs and associated costs, beyond what is already in the pipeline, as well as available private and public sector financing options to support them. With support from IDB, we are developing criteria to align and prioritize projects that support the National Decarbonization Plan in the National Public Investment System by end-March 2022, through the mandatory use of standardized sustainability criteria from our earlier cost-benefit analyses. In addition, to systemically track and monitor climate-related budgetary expenditures, we are developing a new classification of climate change and disaster risk expenditure, with support from IDB and AFD, which is expected to be approved by end-April 2022. In collaboration with the IDB, we also aim at increasing the resilience of transport infrastructure (MEFP ¶40).

VII. RISKS AND CONTINGENCIES

44. The direction of the pandemic, international commodity prices, and global financial conditions pose the greatest economic and financial risks to our program. The successful vaccination campaign has dampened the domestic impact of the COVID-19 shock. Nevertheless, a resurgence of infections could depress activity domestically or abroad, derailing the recovery. This could lead to weaker-than-expected revenue performance and higher COVID-related spending, impacting our fiscal consolidation strategy. A prolonged downturn could expose macro-financial vulnerabilities amid private sector distress. A tightening of global financial conditions, for example due to concerns about geopolitical risks or monetary tightening in advanced economies would hit confidence and weigh on economic growth. Higher-than-projected commodity prices, particularly oil, would imply a deterioration in the terms of trade and could further affect growth. These downside risks could challenge and renew concerns about debt sustainability. Should any of these risks materialize, the government of Costa Rica stands ready to adjust promptly its policies, in close consultation with IMF staff. On the upside, were domestic or external developments to support a stronger economic performance, we stand ready to accelerate the adjustment and reform process, strengthening the resilience of our economy to future shocks.

VIII. PROGRAM MONITORING

45. Progress in the implementation of our policies, which are supported by the IMF, is monitored through semi-annual reviews, performance criteria (PCs), indicative targets (ITs), and structural benchmarks (SBs). These are detailed in Tables 1 and 2, with definitions and data requirements provided in the attached TMU. Purchases under the EFF will be used for direct budget support during the program period. The BCCR and the MoF have updated their Memorandum of Understanding on the responsibilities for servicing financial obligations to the IMF.

Table 1. Costa Rica: Quantitative Performance Criteria (PC) and Indicative Targets (IT)[1/]

(Cumulative from the beginning of the year, in billions of colones, unless otherwise noted)

	2021												2022				2023
	End-Jul (PC)				End-Sep (IT)				End-Dec (PC)				End-Mar	End-Jun	End-Sep	End-Dec	End-Mar
	Prog.	Adj. Prog.	Act.	Met / not met	Prog.	Adj. Prog.	Act.	Met / not met	Prog.	Adj. Prog.	Act.	Met / not met	IT	PC	IT	PC	IT
I. Quantitative Performance Criteria																	
Floor on cash primary balance of the central government (-= borrowing)	-390		100	met	-480		99	met	-640	-700	-112	met	-34	144	215	287	152
Floor on net international reserves of the Central Bank (stock, in millions of U.S. dollars)	3,660	3,351	3,591	met	4,336	3,212	3,636	met	3,768	2,492	2,884	met	4,123	3,007	2,791	3,830	2,314
II. Continuous Performance Criteria[2/]																	
Ceilling on accumulation of new external arrears (in millions of U.S. dollars)	0		0	met	0		0	met	0		0	met	0	0	0	0	0
III. Monetary Policy Consultation Clause (MPCC)[3/]																	
Year-on-year inflation in the consumer price index[4/]																	
Upper outer band limit (3 percent above center point)	4.4		...		4.4		...		4.3		...		6.0	6.0	6.0	6.0	6.0
Upper inner band limit (1.5 percent above center point)	2.9		...	within	2.9		...	within	2.8		...	inner	4.5	4.5	4.5	4.5	4.5
End-of-period inflation center point (percent)	1.4		1.6	inner	1.4		1.8	inner	1.3		3.0	band	3.0	3.0	3.0	3.0	3.0
Lower inner band limit (1.5 percent below center point)	-0.1		...	band	-0.1		...	band	-0.2		...	breach	1.5	1.5	1.5	1.5	1.5
Lower outer band limit (3 percent below center point)	-1.6		...		-1.6		...		-1.7		...		0.0	0.0	0.0	0.0	0.0
IV. Quantitative Indicative Targets																	
Ceiling on debt stock of the central government	26,625		26,250	met	26,833		26,958	not met	27,100	27,160	26,794	met	28,747	28,791	28,855	28,919	29,718
V. Memorandum Items																	
External program financing (in millions of U.S. dollars)[5/]	250		300		1,100		300		1,930		580		0	932	1,439	1,601	0
External project financing (in millions of U.S. dollars)	57		118		73		125		97		190		49	121	264	313	61
External commercial borrowing (in millions of U.S. dollars)	0		0		0		0		0		0		1,000	0	0	1,000	0
Domestic FX-denominated debt issuance (in millions of U.S. dollars)	888		562		888		644		888		842		0	634	884	1,098	0
Proceeds from commercialization of public assets to non-residents (in millions of U.S. dollars)	0		0		0		0		0		0		0	0	0	0	0
Amortization of official external debt by the central government (in millions of U.S. dollars)	55		59		74		94		103		221		20	84	157	191	64
Amortization of external commercial loans (in millions of U.S. dollars)	0		0		0		0		0		0		0	0	0	0	1,000
Interest payments of official external debt by the central government (in millions of U.S. dollars)	273		249		416		394		537		456		190	248	423	567	180
Domestic FX-denominated debt service (in millions of U.S. dollars)	684		799		793		928		1,797		1,643		480	782	1,269	1,394	123

1/ Definitions as specified in the Technical Memorandum of Understanding (TMU).

2/ The Standard Continuous Performance Criteria will also apply: (i) Not to impose new or modify existing restrictions on the making of payments and transfers for current international transactions; (ii) Not to introduce new or intensify existing multiple currency practices; (iii) Not to conclude bilateral payments agreement that are inconsistent with the IMF's Articles of Agreement (Article III); and (iv) Not to impose new or intensify existing import restrictions for balance of payments reasons.

3/ The Monetary policy consultation clause bands consist of two types of thresholds. The inner band triggers a staff consultation and the outer band triggers a Board consultation as detailed in the TMU.

4/ See the TMU for how to measure year-on-year inflation.

5/ Excluding IMF financing.

Table 2. Costa Rica: Structural Benchmarks

Structural Benchmarks	Target Date	Status	Comment
Efficiency of government spending			
Legislative Assembly to approve Public Employment Bill.	End-May 2021	**Not Met**	Approved on March 7, 2022.
Implementation of Public Employment Bill, including introduction of a single pay spine.	End-March 2023		Proposed new SB
Revenue mobilization			
The Tax Commissioner to approve a new Tax Compliance Improvement Plan, in line with IMF staff recommendations.	End-December 2021	**Met**	
Fiscal governance and transparency			
Publication of financial statement under IFRS standards for fiscal year 2020 for three SOEs (ICE, AyA, CNP).	End-December 2021	**Not met**	ICE fully compliant with IFRS. Partial compliance by AyA and CNP.
Cabinet to approve and publish a Medium-Term Fiscal Framework for the entire Non-Financial Public Sector for 2023-2026.	End-April 2022		Ongoing
Cabinet to approve and publish a Medium-Term Debt Strategy (MTDS) for 2023-2026.	End-April 2022		Ongoing
Social safety nets			
MOF's National Treasury to centralize and digitalize the payment system for all the cash transfer social assistance programs, in coordination with social assistance units.	End-December 2021	**Met**	
Monetary and financial sector reforms			
The BCCR to submit to the Ministry of Finance draft amendments to the BCCR Law, prepared in consultation with IMF staff, to strengthen the central bank's operational autonomy and governance framework.	End-August 2021	**Met**	

Table 2. Costa Rica: Structural Benchmarks (concluded)			
The government to submit amendments to the BCCR Law to the Legislative Assembly, prepared in consultation with IMF staff, to strengthen the central bank's operational autonomy and governance framework.	End-December 2022		Proposed new SB
Macro-structural reforms			
CCSS to formulate and approve a plan to adjust the minimum contribution base for part-time workers.	End-June 2022		Proposed new SB
Authorities to develop a roadmap to enhance infrastructure resilience to climate change, including cost assessment and financing options.	End-September 2022		Ongoing

Attachment II. Technical Memorandum of Understanding

1. This Technical Memorandum of Understanding (TMU) sets out a framework for monitoring the performance of Costa Rica under the program supported by the Extended Arrangement under the Extended Fund Facility (EFF). It specifies the performance criteria and indicative targets (including adjustors) under which Costa Rica's performance will be assessed through semiannual reviews. Monitoring procedures and reporting requirements are also specified.

2. The quantitative performance criteria and indicative targets specified in Table 1 attached to the Memorandum of Economic and Financial Policies (MEFP) are listed as follows.

a) a quantitative performance criterion on central government primary balance (floor);

b) a quantitative performance criterion on net official international reserves (floor);

c) a continuous quantitative performance criterion on new external payment arrears by the nonfinancial public sector and the BCCR (ceiling);

d) a monetary policy consultation clause;

e) an indicative target on debt stock of the central government (ceiling);

3. In addition to the performance criteria listed in Table 1, the arrangement will include the performance criteria standard to all Fund arrangements, namely:

a) no imposition or intensification of restrictions on the making of payments and transfers for current international transactions;

b) no imposition or intensification of import restrictions for balance of payments reasons;

c) no introduction or modification of multiple currency practices;

d) no conclusion of bilateral payments agreements that are inconsistent with Article VIII of the IMF Articles of Agreement.

- These four performance criteria will be monitored continuously.

4. For program monitoring purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at "program exchange rates" as defined in Table 1 below, except for items related to fiscal operations which will be measured at current exchange rates. Going forward, the program rates are those that prevailed on January 31, 2022. Monetary gold will be valued at US$ 1,797.17 per troy ounce, which was the price prevailing on January 31, 2022.

Table 1. Costa Rica: Program Exchange Rates (January 31, 2022)	
Colones to the U.S. dollar	642.73
U.S. dollar to the SDR	1.3917
U.S. dollar to the Yen	0.008687
U.S. dollar to the Euro	1.1235
U.S. dollar to the Canadian dollar	0.7869
U.S. dollar to the Chinese RMB	0.1572
U.S. dollar to the British Pound	1.3447
Gold price per troy ounce (U.S. Dollar)	1,797.17

5. Throughout this TMU, the central government figures comprise all branches of the government (executive, legislative, and judiciary), including the Comptroller's Office and the Ombudsman's Office; the Supreme Electoral Court; the budget lines "Servicio de la Deuda Pública", "Regímenes de Pensiones con cargo al Presupuesto de la República" and "Obras Específicas"; and the public entities that is required to be consolidated under central government (CG) from 2021 by Law 9524 (see below). The Central Bank of Costa Rica (BCCR), the state-owned enterprises and other public sector agencies are excluded from the definition of central government. Debt is defined in accordance with paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), adopted December 5, 2014.

Specifically, the following entities are required to be consolidated under CG by Law 9524:

1. Agencia de Protección de Datos de los Habitantes (PRODHAB), 2. Casa de Cultura de Puntarenas, 3. Centro Costarricense de Producción Cinematográfica, 4. Centro Cultural e Histórico José Figueres Ferrer, 5. Centro Nacional de la Música, 6. Comisión Nacional para la Gestión de la Biodiversidad (CONAGEBIO), 7. Comisión Nacional de Prevención de Riesgos y Atención de Emergencias (CNE), 8. Comisión Nacional de Vacunación y Epidemiología, 9. Comisión de Ordenamiento y Manejo de la Cuenca Alta del Río Reventazón (CONCURE), 10. Consejo Nacional de Clubes 4-S, 11. Consejo Nacional de Concesiones (CNC), 12. Consejo Nacional de la Persona Adulta Mayor (CONAPAM), 13. Consejo Nacional de la Política Pública de la Persona Joven (CPJ), 14. Consejo Nacional de Vialidad (CONAVI), 15. Consejo de Salud Ocupacional (CSO), 16. Consejo de Seguridad Vial (COSEVI), 17. Consejo Nacional de Investigación en Salud (CONIS), 18. Consejo Nacional de Personas con Discapacidad (CONAPDIS), 19. Consejo Superior de Educación (CSE), 20. Consejo Técnico de Asistencia Médico Social (CTAMS), 21. Consejo Técnico de Aviación Civil (CTAC), 22. Consejo de Transporte Público (CTP), 23. Dirección Nacional de Centros de Educación y Nutrición y de Centros Infantiles de Atención Integral (Dirección de CEN-CINAI), 24. Dirección Nacional de Notariado, 25. Fondo de Desarrollo Social y Asignaciones Familiares (FODESAF), 26. Fondo Nacional de Becas (FONABE), 27. Fondo Nacional de Financiamiento Forestal (FONAFIFO), 28. Instituto sobre

Alcoholismo y Farmacodependencia (IAFA), 29. Instituto Costarricense sobre Drogas (ICD), 30. Instituto Costarricense de Investigación y Enseñanza en Nutrición y Salud (INCIENSA), 31. Instituto Nacional de Innovación y Transferencia en Tecnología Agropecuaria (INTA), 32. Instituto de Desarrollo Profesional Uladislao Gámez Solano, 33. Junta Administrativa del Archivo Nacional (JAAN), 34. Junta Administrativa de la Dirección General de Migración y Extranjería, 35. Junta Administrativa de la Imprenta Nacional (JAIN), 36. Junta Administrativa del Registro Nacional, 37. Laboratorio Costarricense de Metrología (LACOMET), 38. Museo de Arte Costarricense, 39. Museo de Arte y Diseño Contemporáneo (MADC), 40. Museo Histórico Cultural Juan Santamaría, 41. Museo Nacional de Costa Rica (MNCR), 42. Museo Dr. Rafael Ángel Calderón Guardia, 43. Oficina de Cooperación Internacional de la Salud (OCIS), 44. Patronato de Construcciones, Instalaciones y Adquisiciones de Bienes, 45. Servicio Fitosanitario del Estado, 46. Servicio Nacional de Salud Animal (SENASA), 47. Sistema Nacional de Áreas de Conservación (SINAC), 48. Sistema Nacional de Educación Musical (SINEM), 49. Teatro Nacional (TNCR), 50. Teatro Popular Melico Salazar (TPMS), and 51. Tribunal Registral Administrativo (TRA).

Data from Unidad Ejecutora del Proyecto (UEP) was included in the historical series presented in the program document in 2019. From 2020 onwards, data related to Unidad Ejecutora del Proyecto (UEP) is already included in the budgetary central government.

I. PERFORMANCE CRITERIA

A. Performance Criterion on Central Government Primary Balance

6. The overall balance of the Central Government is defined as the difference between budgetary revenue and total expenditure. Cash primary balance is defined as overall balance excluding net interest payment. Revenue data are registered on a cash basis, whilst expenses are accruals except in the case of interest, which are recorded when disbursements are made. Capital expenditure reflects the accrued amounts recorded under investment projects, not fully reconciled with the concept of the transactions categorized as net acquisition of nonfinancial assets. This system is internationally known as modified cash. The proceeds from privatization or commercialization of public assets to residents or non-residents will not be recorded as part of central government revenues. The consolidation of the data from entities contained in paragraph 5 and the other entities of central government as well as the consolidation of data within the entities included above consider funds granted as both current and capital transfers. Consolidation process is done entity by entity and never aggregated. Whenever consolidation adjustments are necessary to maintain primary and overall balance unalterable, following international best practices, these residuals affect capital transfers (income and/or expense). Financing (below the line) data are not currently used for the calculation of primary or overall balance. Any variable or definition that is omitted but is relevant for primary balance is defined in accordance with the Fund's statistical manuals and shall be aligned with the framework of a modified cash approach. Figures until 2018 do not comprise the entities included in paragraph 5. For the purpose of program monitoring, the cash primary balance of the central government will be monitored from above the line data as described on the previous paragraph.

7. The performance criterion on the central government cash primary balance will have one adjustor for 2021 and 2022. The floor on central government cash primary balance will be adjusted downward by the full amount of any increase in COVID-19 emergency spending compared to budgeted amounts such as transfers to the health system, transfers for targeted support to families, workers, and firms heavily affected by the pandemic, or social assistance programs to the most vulnerable groups. Such additional expenditure should be clearly identified and reflected in an appropriate document (e.g., supplementary budget, government resolution, a circular of the ministry of finance). The adjustor is capped at CRC 112 billion for 2021 and CRC 128 billion for 2022 (about 0.3 percent of GDP).

B. Performance Criterion on Net Official International Reserves

8. For the purpose of program monitoring, net official international reserves (NIR) will be measured as the U.S. dollar value of the difference between (a) and (b) below, and will be called the "Program NIR":

a) Gross international reserves of the BCCR. They include monetary gold; foreign exchange balances (foreign currency cash, deposits with foreign correspondents, and holding of foreign securities); the reserve position at the IMF and SDR holdings. Excluded from gross foreign reserve assets are participation in international financial institutions; holdings of nonconvertible currencies; holdings of precious metals other than monetary gold; claims on residents (e.g., statutory reserves on foreign currency deposits of commercial banks and central bank foreign currency deposits with resident commercial banks); pledged, non-liquid, collateralized or otherwise encumbered foreign assets; and claims in foreign exchange arising from derivative transactions (such as futures, forwards, swaps and options).

b) Gross reserve-related liabilities of the BCCR. They include: all short-term liabilities to nonresidents denominated in convertible foreign currencies with an original maturity of one year or less; all short-term liabilities to residents denominated in convertible foreign currencies; the stock of IMF credit outstanding; the nominal value of all short-term derivative positions (including swaps, options, forwards, and futures), implying a sale of foreign currency or other reserve assets. Excluded from these liabilities are foreign exchange liabilities to the general government or related to deposit guarantees.

- At end-2020, the Program NIR, evaluated at market exchange rates, stood at US$3,712 million. Targets for the Program NIR are set for cumulative flows from the end of the previous year. To calculate the cumulative flows, the Program NIR at the test dates and the end of the previous year are evaluated at the program exchange rates and gold price specified in paragraph 4.
- The following adjustment will apply:

9. If (i) the amount of foreign program financing by the central government and the BCCR net of IMF purchases and all debt service; (ii) the amount of external commercial borrowing (including international sovereign bonds and syndicated loans) by the central government net of debt service;

(iii) the amount of project loans and grants disbursed to the central government net of debt service; (iv) the amount of foreign exchange-denominated domestic debt issued by the central government net of debt service; and (v) proceeds from commercialization of public assets to non-residents;—as set out in Table 1 of the MEFP—are higher/lower in U.S. dollar terms than assumed under the program, the floor on the program NIR will be adjusted upward/downward by the cumulative differences on the test date. The proceeds from commercialization of public assets are defined as cash receipts from the sale or lease of publicly held assets. Such assets will include, but not be limited to, publicly held land, public holdings of infrastructure or commercial real estate, and public or quasi-public enterprises. These adjustors will apply to the NIR floor for end-July 2021 and thereafter.

10. If the sum of amortization of official external debt and interest payments on official external debt by the central government or the BCCR in U.S. dollar terms—as set out in Table 1 of the MEFP—is higher/lower than assumed under the program, the floor on the program NIR will be adjusted downward/upward by the cumulative differences on the test date. Official external debt refers to external debt owed to multilateral and official bilateral creditors, as defined in the *2013 External Debt Statistics: Guide for Compilers and Users*. These adjustors will apply to the NIR floor for end-July 2021 and thereafter.

II. CONTINUOUS PERFORMANCE CRITERIA

A. Performance Criterion on New External Payment Arrears by the Nonfinancial Public Sector and the BCCR

11. A continuous performance criterion applies to the non-accumulation of new external payments arrears on external debt contracted or guaranteed by the nonfinancial public sector and the BCCR. The nonfinancial public sector is defined following the 1986 Government Finance Statistics Manual and the 2008 System of National Accounts. It includes (but is not limited to) the central government as defined in paragraph 4 and nonfinancial public enterprises, i.e., boards, enterprises and agencies in which the government holds a controlling stake. External payments arrears consist of debt-service obligations (principal and interest) to nonresidents falling due after the date of Board approval of the arrangement that have not been paid at the time they are due, as specified in the contractual agreements, subject to any applicable grace period. However, overdue debt and debt service obligations that are in dispute by the authorities with respect to their amount and/or validity will not be considered as external payments arrears for the purposes of program monitoring. This PC also excludes arrears on external financial obligations of the government subject to rescheduling. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

III. MONETARY POLICY CONSULTATION CLAUSE

12. The inflation target bands are specified in Table 1 attached to the MEFP. For this purpose, the year-on-year inflation, as measured by the headline Consumers Price Index (CPI) published by the National Institute of Statistics and Census (INEC), for each test date is measured as follows:

$$\{CPI^*(t) - CPI^*(t-12)\} / CPI^*(t-12)$$

where

t = the month within which the test date is included

CPI(t) = CPI index (all items) for month t

CPI(t-k) = CPI index (all items) as of k months before t

$CPI^*(t) = \{ CPI(t-2) + CPI(t-1) + CPI(t) \} / 3$

$CPI^*(t-12) = \{ CPI(t-14) + CPI(t-13) + CPI(t-12) \} / 3$

If the observed year-on-year inflation falls outside the outer band limits of +/- 3 percentage points around the targets as specified in Table 1 attached to the MEFP for the relevant semi-annual test dates, the authorities will complete a consultation with the IMF Executive Board, which would focus on (i) the stance of monetary policy and whether the Fund-supported program remains on track; (ii) the reasons for deviations from the specified band, taking into account compensating factors; and (iii) on proposed remedial actions, as deemed necessary. When the consultation with the IMF Executive Board is triggered, access to Fund resources would be interrupted until the consultation takes place and the relevant program review is completed. If the observed year-on-year inflation falls outside the inner band limits of +/- 1.5 percentage points around the targets for the relevant semi-annual test dates, the authorities will conduct a consultation with IMF staff on the reasons for the deviation and the proposed policy response.

IV. INDICATIVE TARGETS

A. Indicative Target on Debt Stock of the Central Government

13. The term "debt", as defined in the Guidelines on Public Debt Conditionality in IMF Arrangements, Decision No. 15688-(14/107), will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debt can take a number of forms, the primary ones being loans, debt securities, bonds, commercial loans, buyers' credits and off-budget project loans.

14. All foreign currency denominated debt will be converted into colones using the program exchange rates set out in Table 1. All domestic debt denominated in inflation indexed units (TUDES) will be converted into colones using the program rate set out in Table 1.

15. The performance criterion on debt stock of the central government will have one adjustor for 2021 and 2022. The ceiling on debt stock of the central government will be adjusted upward by the full amount of any increase in COVID-19 emergency spending compared to budgeted amounts such as transfers to the health system, transfers for targeted support to families, workers, and firms heavily affected by the pandemic, or social assistance programs to the most vulnerable groups. Such additional expenditure should be clearly identified and reflected in an appropriate document (e.g., supplementary budget, government resolution, a circular of the ministry of finance). For 2021, the adjustor is capped at CRC 112 billion. For 2022, the adjustor is capped at CRC 128 billion.

V. DATA REPORTING REQUIREMENTS

16. Costa Rica shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Costa Rica in achieving the objectives and policies set forth in the Memorandum of Economic and Financial Policies and Letters of Intent. All the program monitoring data will be provided by the Ministry of Finance, IMAS, FODESAF, BCCR, and SUGEF. For the purpose of monitoring the fiscal performance under the program, data will be provided in the format as shown in Tables 2, 3, and 4. For the purpose of monitoring the external sector performance under the program, data will be provided in the format shown in Tables 5 and 6. For the purpose of monitoring the performance against the indicative target on treasury guarantees, data will be provided in the format shown in Table 7. For the purpose of monitoring financial sector performance under the program, data will be provided as described in paragraph 20.

17. Data relating to the fiscal targets (Tables 2, 3, and 4) will be furnished within the following timelines:

- Data on the cash primary balance of central government will be provided on a monthly basis, no later than three weeks after the end of the month to which the cash balance is calculated.
- Data relating total stock of debt of the central government will be provided on a monthly basis, no later than three weeks after the end of the month, with breakdowns listed in Table 4.

18. Data relating to the external targets (Table 5) and monetary consultation band will be furnished within no more than three weeks after the end of each month, except for data on official reserve assets (Table 6), which will be furnished within one week after the end of each week.

19. Data regarding the level of social safety net spending (program spending only, not including wage and salaries and administrative costs of relevant agencies; see Table 7) will be provided on a quarterly basis, no later than four weeks after the end of the quarter.

20. Data relating to the financial sector will be reported as follows:

- Financial soundness indicators of banks and cooperatives, bank by bank, group (public and private), and system level. Data will be reported monthly, no later than four weeks after the end of each month.
- Anonymized bank by bank asset quality indicators, including by risk buckets (e.g., low, medium, high/viable, high/nonviable), and disaggregated, by type of credit, economic sector, and currency. Data will be reported on a monthly basis, no later than four weeks after the end of each month. Such data on individual banks will be treated as strictly confidential and will not be published except in aggregate form.

Table 2. Costa Rica: Central Government Operations[1/]

(In billions of colones)

Total Revenue
Current Revenue
Income Tax
Tax on Income and Profits
Income and to natural and legal per:
Income and to Individuals
Revenue and Profit Corporations
Dividends and interest s / Securities
Remittances Abroad
Banks and non-domiciled Financ
Property Tax
Owned vehicles
Supportive Housing Imp
Import Tax
Tariff:
1% Customs Value:
Export Tax
Exported Banana Case
Der.de Exp.ad / valorem
Sales Tax
Internal
Customs
Consumption Tax
Internal
Customs
Undistributed Customs
Indirect Tax
Single tax fuels
Tax soft drinks
Tax soap
Alcohol tax
Transfer used vehicles
Transfer property
Fiscal Stamp
Exit fees Homeland
Consular Rights
Tax Law on Migration and Aliens
Tax on Tobacco
Other tax revenue
Social Security Contributions
Non Tax
Current transfers
Capital Income
Recovery of Loans
Capital Transfers
Donation
Admin.Finan Act. (Cash only)

Table 2. Costa Rica: Central Government Operations (concluded)[1/]
(In billions of colones)

Total Expenditure
No Interest Expense Total
Current expenses
Salaries
Wages and salaries
Social Security Contributions
Social Security Contributions CCSS
Social Security Contributions Worker Protection Act
Social Security Contributions Others
Purchase of Goods and Services
Interest Expenditure
Internal Interest Expenditure
Interest Expenditure External
Transfers
Transfers Private Sector
Pensions (including CCSS)
Transfers Others
Transfers Public Sector
Transfers External Sector
Transfers Ctes with external resources
Capital Expenditure
Investment
Capital Transfers
Capital Transfers Private Sector
Capital Transfers Public Sector
Capital Transfers External Sector
Capital with external resource transfers
Capitalization banks

Primary Balance

Overall Balance
Residual

Total Financing
Net Domestic Financing
Net Foreign Financing
Privatization

1/ As agreed for the purpose of monitoring the program.

Table 3. Costa Rica: Central Government Financing[1/]
(In billions of colones)

Financing
Net Domestic Financing
Net BCCR Financing
BCCR Renegotiated debt
Deposits BCCR
Deposits BCCR Initial Balance
Deposits BCCR Final Balance
BCCR Net loans
Banking System Financing
Banking System Financing Loans
Banking System Financing Amortization
Banking System Financing Deposits
Banking System Financing Var. Securities
Banking System Financing Var. Securities Initial Balance
Banking System Financing Var. Securities Final Balance
Banking System Financing Cash and Banks
Banking System Financing Cash and Banks Initial Balance
Banking System Financing Cash and Banks Final Balance
Banking System Financing Net Loans
Central Government Financing
Central Government Financing Amortization of government
Central Government Financing Change in Government Securities
Central Government Financing Change in Government Securities Initial Balance
Central Government Financing Change in Government Securities Final Balance
Other domestic financing
Other domestic financing Credit providers
Other domestic financing Disbursements
Other domestic financing Amoritizations
Other domestic financing Var. Dep in other entities
Other domestic financing Var. Dep in other entities Initial Balance
Other domestic financing Var. Dep in other entities Final Balance
Other domestic financing Other financ. internal
Other domestic financing Exchange Losses
Other domestic financing Net loans
Net Foreign Financing
Net Foreign Financing Disbursements
Net Foreign Financing Amortization
Net Foreign Financing Var. Dep abroad
Net Foreign Financing Var. Dep abroad Initial Balance
Net Foreign Financing Var. Dep abroad Final Balance

1/ As agreed for the purpose of monitoring the program.

Table 4. Costa Rica: Central Government Debt[1/]
(In billions of colones)

Debt stock
Domestic
- Bonds
Tasa basica
Zero coupon colones
Zero coupon dolares
Fixed coupon colones
Fixed coupon dolares
Floating coupon colones
Floating coupon dolares
Inflation-linked bond (TUDES)
- Other liabilities
External
- Bilateral
- Bonds
- Multilateral
Unidentified financing
Domesticdebt stock by maturities
o.w.: OD domestic debt by maturities
External debt stock by maturities
o.w.: OD external debt by maturities
Total borrowing requirement
Financial deficit of CG
CG debt amortization
Domestic
o.w.: OD domestic debt amortization
External
o.w.: OD external debt amortization
- Bilateral
- Bonds
- Multilateral
Source of funds
Domestic placement or disbursement
External placement or disbursement
- Bilateral
- Bonds
- Multilateral
Use of government deposits

1/ As agreed for the purpose of monitoring the program.

Table 5. Costa Rica: Foreign Exchange Cashflows of the Central Bank and the Government[1/]

(In millions of U.S. dollars)

1. Total Inflows
Official sector disbursement
Program loans
IMF
World Bank
IDB
CABEI
ADF
CAF
Project loans and grants, of which
World Bank
IDB
CABEI
bilateral: KFW/JICA/China Eximbank
Commercial loans
Syndicated loans
Sovereign bond, incl Eurobonds
Domestic FX debt issuance
Other inflows
BCCR Interest receipts and other net items
Change in balances in public accounts
o/w proceeds from public asset sale
2. Total outflows
External debt service
Amortization (excl. to IMF), of which:
Official loans, of which:
World Bank
IDB
CABEI
CAF
Bilaterals: AFD/KFW/JICA/Eximbank
Commercial loans
Syndicated loans
Sovereign bonds
Interest payment (incl. to IMF)
Domestic FX debt service
Residents
Non-residents
Net capital transfers and miscellaneous
3. Net FX intervention, of which
Net intervention for volatility management
Programmed reserve accumulation
Net FX purchases for rest of public sector
4. Other net flows
Net Central Government<-->BCCR transactions[1/]
Change in short-term liabilities with non-residents
Change in liabilities w/ residents
Net International Reserves (at market exchange rates)[2/]
Net International Reserves (at program exchange rates)[2/]
Gross International Reserves (at market exchange rates)

1/ As agreed for the purpose of monitoring the program.

2/ As defined in ¶18.

Table 6. Costa Rica: Gross Official Reserve Position[1/]

(In millions of U.S. dollars)

Date	Central Bank				Government	Gross Official Reserves	Liabilities				Net International Reserves
	Reserves managed by BCCR		Reserve Position at IMF & SDR holdings	Total	Foreign Reserve Asset Balances		Short-termLiabilities with Residents	Short-term Liabilities with Non-Residents	Drawings from the IMF	Total	
	Foreign Assets (FA) (Without DA)	Domestic Assets (DA)		(1)+(2)		(3) + (4)				(6)+(7)+(8)	(5) - (9)
	1		2	3	4	5	6	7	8	9	10

1/ As agreed for the purpose of monitoring the program.

Table 7. Costa Rica: Priority Social Spending[1/]

(In billions of Colons)

	FODESAF	Central Govt transfers	Other sources of financing	Total public sector spending	Number of beneficiaries
1. Non-contributory pensions and healthcare					
1.1. Non contributory pensiones regime (RNC)					
2. Targeted social assistance programs					
2.1. Conditional cash transfer *Crecemos* [2/]					
2.2. Conditional cash transfer *Avancemos*		-			
2.3. Poverty reduction and income support					
2.3.1. Basic needs (Atención a Familias)					
2.3.2. Family allowance (Asignación Familiar)					
2.3.3. Emergencies					
2.3.4. Fishing subsidies (Veda)					
2.4. Childcare					
2.4.1. Childcare transfer					
2.4.2. Childcare transfer CIDAI					
2.4.3. Childcare services (API intramuros)					
2.5. School programs					
2.5.1. School lunch program					
2.5.2. School transportation					
2.5.3 Social scholarship program [3/]					
2.6. Housing subsidies					
2.6.1. Housing improvement					
2.6.2. Housing grants					
2.7. Food security and nutrition programs					
2.7.1. Prestación alimentaria					
2.8. Active labor market programs					
2.8.1. Employment National Program (PRONAE)					
2.8.2. Small enterprises' support program (PRONAMYPE)					
2.8.3. Productive ideas					
2.8.4. Training aid					
2.8.5. Training voucher program [4/]					
2.9. Other targeted programs					
2.9.1. Subsidies for elderly persons					
2.9.2. Subsidies for persons with disabilities					
2.9.3. Subsidies for violence female victims					
2.9.3. Subsidies for teenage mothers					
3. Capital transfers to social assistance programs					
3.1. Community infrastructure and socio-productive projects					
TOTAL					

1/ As agreed for the purpose of monitoring the program.
2/ Crecemos program will be merged under Avancemos program starting in 2022.
3/ Since 2020, the program reports only tertiary education scholarship information, with primary education scholarships information (that used to be reported under this program) consolidated under Crecemos.
4/ Starting in 2022, this program will provide support to students enrolled in private institutions' training programs when the National Institute of Apprenticeship (INA) cannot provide the service directly.

Statement by Mr. Moreno and Ms. Lankester Campos on Costa Rica
March 25, 2022

Our authorities want to express their gratitude to management and staff for their close engagement in order to conclude successfully the first and second reviews under the Extended Fund Facility (EFF) arrangement. They also extend their especial appreciation to Ms. Manuela Goretti, the Mission Chief and her team, for their excellent work, commitment and productive discussions with the authorities, civil society, and presidential candidates.

Amid the ongoing global challenges, and those posed by the COVID-19 pandemic, the economic program laid out by the Costa Rican authorities, and supported by the EFF, has been critical to safeguard macroeconomic stability, ensure a strong economic recovery, and promote a greener, more inclusive growth over the medium term. The EFF has also been instrumental in catalyzing additional financial support from other multilateral institutions and international capital markets. IMF support through this program and the new SDR allocation bolstered the countries' international reserve position, strengthened market confidence, and anchored the fiscal consolidation efforts.

The EFF Program

The program's three key objectives are: (i) gradually implementing equitable fiscal reforms to ensure debt sustainability while protecting the most vulnerable; (ii) maintaining monetary and financial stability while continuing to strengthen central bank autonomy and governance and addressing structural financial vulnerabilities; and (iii) on the structural front, advancing on key reforms to promote inclusive, green, and sustainable growth.

For the first and second reviews, the Costa Rican authorities have met all the end-July and end-December 2021 quantitative performance criteria by comfortable margins. Fiscal outcomes have been much better than anticipated, given prudent spending and the strong revenue overperformance. These results have improved confidence and they have delivered more favorable market conditions. Indeed, after the approval of the Public Employment Bill, a structural benchmark under the program, Fitch and Standard & Poor's revised up their outlook on Costa Rican sovereign debt.[1]

We would like to emphasize the authorities' ownership and strong commitment to the EFF, and the appreciation to the Fund's support on capacity development. As outlined in the staff report's Informational Annex, Costa Rica has actively engaged in the use of Fund technical assistance,

[1] On March 11th, Fitch ratings affirmed Costa Rica's long term foreign currency and local currency issuer default ratings at 'B' and revised the rating outlook to stable from negative. A week after, on March 17th, Standard & Poor's also improved their outlook on Costa Rica's debt from negative to stable. Moody´s had already upgraded the outlook to stable on December 10th, 2021.

including on fiscal and national accounts statistics, financial regulation and supervision, customs efficiency, revenue mobilization, central bank governance, and exchange market operations.

In view of the strong quantitative performance, the macroeconomic policies implemented to achieve the main program objectives and the progress on the structural reforms, and considering the legislative delays in program implementation, we believe it is in the best interest of the Fund and Costa Rica to provide additional time for the incoming administration to adjust the reform agenda under the EFF supported program.

Background information and recent developments

Costa Rica boasts one of Latin America's oldest and strongest democracies: it is one of only two countries in the Latin American region (along with Uruguay), and one of only 21 countries in the world, whose democracies are considered "full", tied with Austria, according to the Economist Intelligence Unit's Democracy Index. Also, it ranks as one of the highest in the region in UNDP´s Human Development Index, classified within the *very high* range.

Costa Rica, a small open economy, also rides high in the regional rankings on health care, education, and public safety. Three decades ago, it started a profound transformation from an agriculture-based economy to a knowledge-intensive, service-oriented one, benefitting from larger flows of foreign direct investment. Since then, its economy has diversified with new industries, such as medical devices, ecotourism, and renewable power. On the latter, the National Electricity Control Center (CENCE) projects that the five renewable sources available to the Costa Rican matrix – water, geothermal, wind, biomass, and sun – would make up for 98% of national generation in 2022.

In May 2021, Costa Rica formally became the 38th OECD Member, after an accession process that began in April 2015. During these years, the authorities have adopted wide-ranging structural reforms aligned with international best practices and OECD standards, aimed at boosting the economy's growth potential, reducing inequality, and improving the living conditions of the population, with a strong commitment to decarbonization and building resilience to climate change. Specifically, Costa Rica has taken decisive steps forward in areas such as competition, statistics, anti-corruption, corporate governance, financial markets, and tax transparency.

Nonetheless, public spending has outpaced revenues over the last two decades. A long-standing fiscal deficit, temporarily interrupted in 2006 and 2007 by fiscal buoyancy, was made worse when, in response to the Global Financial Crisis of 2008, an expansionary fiscal policy was adopted as a counter-cyclical measure. Since then, Costa Rica's fiscal situation deteriorated sharply. Its government debt ratio, measured as a percentage of GDP, grew at one of the fastest rates in the region.

Costa Rica has a strong and high-quality primary health care public system. By December 2020, the authorities launched a large-scale vaccination campaign to control the pandemic and support the reopening of the economy. Fourteen months later, 74.1 percent of the population was fully vaccinated, and 25.7 percent had already received a booster dose. They aim to fully vaccinate all eligible population and apply booster vaccines to vulnerable groups by end-2022.

Costa Rica's robust health system and sanitary measures were instrumental to reduce covid-related fatalities. As "excess deaths" estimates show, Costa Rica has had one of the lowest death tolls from Covid per one million inhabitants.

However, the economic fallout from the pandemic was enormous, and entailed that, after a profound fiscal reform in December 2018, an additional fiscal adjustment was necessary to keep debt at manageable levels over the medium term. At the outset of the crisis, the country requested Fund support through the RFI, which helped ease the economic consequences. Right after, the authorities requested an EFF program for budget support purposes to help anchor macroeconomic policies over the medium term.

Economic Outlook

Against an international context, characterized by a rebound in growth in 2021 but a severe negative terms of trade shock from the sharp increase in commodity prices, the Costa Rican economy has been recovering and continues to recover faster than expected, showing resilience and the impact of sound policies taken in the past. For 2021, GDP grew 7.6 percent (after a 4.1 percent contraction in 2020), and the Central Bank (BCCR) projects growth of around 4 percent in 2022 and 2023. In January 2022, the monthly index of economic activity expanded 9.0 percent, y-o-y. The labor market has also been recovering, but more slowly than activity, with the unemployment rate coming down from a peak of 24.4 percent to 13.1 percent in January 2022, but still slightly above pre-pandemic levels.

While subject to the unprecedented degree of uncertainty arising from the pandemic, inflationary pressures and geopolitical tensions, the outlook is anchored on: (i) continued strong external demand; and (ii) vigorous domestic private demand, supported by credit conditions and stronger consumer and business confidence, as vaccination continues, and despite still deteriorating terms of trade.

The conflict between Russia and Ukraine is not expected to have a large direct impact on Costa Rica's economy as the two countries account for small shares of exports, imports, and tourism. However, the indirect effects may be significant, channeled via higher commodity prices and lower global growth.

Inflation accelerated during the last quarter of 2021, propelled by external pressures (particularly higher commodity prices), and ended the year at 3.3 percent. The BCCR projects headline inflation to reach 5.9 percent and return to within the tolerance band of 3 percent plus-minus one percent in 2023, with core inflation remaining within the tolerance band in the two years.

Fiscal policy

To restore sustainability, the authorities approved a comprehensive fiscal reform in December 2018, which included broadening the base for the value-added tax, higher rates of income tax, and a fiscal rule to limit expenditure growth.

Just as the benefits from the 2018 fiscal reform were materializing, the Costa Rican economy was hit hard by the pandemic, with the deepest economic contraction since 1982 and a heavy toll on the important tourist industry. In response, in 2020 the authorities increased health-related spending and introduced a transfer program (*Bono Proteger*) to support the most vulnerable households, while containing non-priority primary spending, to limit the fiscal impact. Also, they adopted a mix of monetary and prudential policies to lower interest rates, improve credit conditions, and ensure adequate functioning of financial markets.

In 2021, the fiscal balance turned out to be much better than expected. The primary deficit was 0.3 percent of GDP (3.4 percent in 2020), below the EFF target of 1.7 percent, and the overall deficit was 5 percent (8 percent in 2020). These results are explained, firstly, by a strong revenue overperformance, which benefitted from the robust economic recovery, higher than expected yields from the 2018 fiscal reform and one-offs[2]. Secondly, the strong fiscal outcomes were driven by a decline in primary expenditure as a share of GDP. These results allowed the government to face a lower cost of financing in the local market and a lower country risk premia.

Fiscal performance continues to be strong. In February 2022, primary expenditure was at its lowest in eleven years, at 2.5 percent of GDP, while total revenue was 2.6 percent of GDP, the highest in the last seventeen years, delivering a primary surplus of 0.1 percent of GDP.

Going forward, the authorities have reaffirmed their commitment to the required fiscal consolidation, while continuing to protect the vulnerable and supporting a sustainable economic recovery, in order to achieve a primary balance of 1 percent of GDP by end-2023 and reach a debt-to-GDP ratio of 50 percent by 2035. In particular, they target a primary surplus of 0.7 percent of GDP by end-December 2022. To achieve it, they are committed to implementing further revenue and expenditure measures, consistent with the 2022 budget approved in November 2021.

Monetary policy

The BCCR's monetary policy approach is data-dependent and forward-looking, within an inflation targeting framework. Its well-communicated counter-cyclical stance, with the policy rate reduced to its lowest ever of 0.75 percent, played a key role in mitigating the harsh impact of the pandemic,

[2] One-off revenues: (i) collections from public entities; (ii) partial recovery from the 2020Q2 tax moratorium; and (iii) higher income tax payments in March 2021 due to the 15-month fiscal year (as the 2018 tax reform shifted the fiscal year from October-September to a calendar year basis).

without risking expectations. As a result, inflation remained contained by international standards in 2021, despite unrelenting external price pressures.

However, to keep expectations in check amidst external inflationary forces, the BCCR started normalizing its rate in December 2021, with three consecutive rate increases, of 50 basis points each in December and January and 75 b.p. in March 2022.

Continuing its forward guidance, the central bank has announced that it will continue to raise its policy rate in 2022 toward a neutral stance, with liquidity management supporting policy normalization. The Central Bank has reiterated its commitment to the inflation target, and explained its outlook for inflation, risks around the outlook, and the implications for monetary policy. They are vigilant about the tightening of global financial conditions and the risks posed by sustained global price pressures, worsened by the war in Ukraine.

The FX market has reflected pressures arising from higher commodity prices, transport costs, and the cost of imports in general, as well as from internal factors such as a higher demand from the non-financial public sector (NFPS) to meet FX-denominated debt maturing and from portfolio diversification efforts into foreign assets by pension funds. By the end of 2021, the exchange rate had depreciated 4.4 percent, with the BCCR's participation in the FX market limited to limiting abrupt exchange rate movements without changing its trend and to meeting the FX needs of the NFPS.

Structural reforms

Costa Rica has laid out a comprehensive roadmap for structural reforms to align public governance and policies with international best practices, and foster transparency, efficiency, and growth while reducing inequality and protecting the most vulnerable. The authorities are committed to continue advancing on this structural reform agenda, including on climate change, which started years ago within the accession process to OECD.

The latest structural reform is the public employment law approved on March 7th, 2022. It constitutes a key element of the fiscal program on the expenditure side as it creates a single pay scale across the public sector, eliminating salary components such as bonuses and annuities. It improves the fairness of public compensation and reduces the high public-private wage premium. Given its ambitious scope to modernize and streamline the public administration while containing the wage bill, all in line with OECD recommendations, it faced strong opposition from public sector unions and some members of Congress. Consequently, it took longer than expected to resolve collective action disagreements, legal consultations, and two reviews by the Constitutional Court, which delayed the accomplishment of the structural benchmark. This reform was approved by a qualified majority in Congress in early March and will enter into force in March 2023, but preparations for the introduction of the single pay spine and related reforms have already started.

The government estimates savings of 0.7 percent of GDP per year in reduced wages during the first years of implementation. This reduction will facilitate compliance with the fiscal rule as wages count for almost one third of central government spending.

The structural fiscal program also envisages gains from reforms to public procurement, modernization of the tax and customs administration, and public financial management reforms. There is an ongoing work to expand the Medium-Term Fiscal Framework, MTFF, to the nonfinancial public sector by end April 2022. Efforts are also underway to operationalize the Fiscal Council and implement a plan to phase in gender budgeting. In these areas, Costa Rica has actively engaged in the use of Fund technical assistance. Capacity building has been instrumental, and it is critical for the success of the policy agenda under the program.

Finally, it contemplates protection of capital expenditure and well targeted social spending to address critical infrastructure needs and to support the most vulnerable.

The BCCR completed draft amendments to its Organic Law in August 2021. These are expected to be submitted to the Legislative Assembly by end-December 2022. The goal is to clarify the Central Bank´s objectives, to provide for a clear allocation of functions among its decision-making bodies, to strengthen its institutional, functional, personal, and financial autonomy, and to enhance its transparency and accountability.

The authorities have reiterated their commitment to climate change reforms, with measures to reduce greenhouse gas emissions, for instance by promoting the electrification of public transport, and to strengthen Costa Rica's adaptation capacity, for example by assessing the medium-term investment needs for enhancing resilience of the country's physical infrastructure. Costa Rica has pledged to reduce greenhouse gas emissions to a net absolute maximum of 9.11 million tons of carbon dioxide equivalent (CO_2e) by 2030, a maximum net emissions budget in the period 2021 to 2030 of 106.3 million tons of carbon dioxide equivalent (CO_2e), and to achieve zero net emissions by 2050 under the National Decarbonization Plan.

Also, to address the impacts and risks related to climate change on its main objectives, the BCCR established the Group for Strategic Analysis of Climate Change (GAECC) and has developed a roadmap for 2021-2024 with four key action areas: establishing reliable and comparable data, strengthening modeling and analytical capacity for scenario analysis, promoting climate-change risk management in the financial system, and greening international reserves.

Political Assurances

Presidential elections took place on February 6th, 2022. Former president José María Figueres won with 27.3 percent of the vote, followed by Rodrigo Chaves with 16.7 percent. Hence, Figueres and Chaves will contest a second round on April 3rd. Both candidates strongly agree on the need of continuing the fiscal consolidation, the importance of the EFF program and their commitment[3] with the objectives of the program.

[3] On March 1st, 2022, the presidential candidate José María Figueres made a press release where he states: "Our priority is economic reactivation and employment; to achieve this, it is essential to have a climate of confidence, while maintaining monetary and financial stability. Therefore, we reiterate our commitment to the essential objectives of the agreement with the International Monetary Fund (IMF), which include ensuring debt sustainability, with a primary surplus of at least 1% of GDP by 2023 for the Central Government". Press release (Eng, Esp).

On February 28th, 2022, the presidential candidate Rodrigo Chaves on an interview with the newspaper, El Mundo, said about the interaction with the Mission Chief, Manuela Goretti: with this dialogue, I want to establish mechanisms to help debt sustainability, reach a primary balance of at least 1 percent of GDP by 2023, maintain monetary and financial stability and promote a strong inclusive growth that considers the climate agenda. Article by El Mundo.