COSTA RICA

Costa Rica's economy is being undermined by balance-of-payments difficulties. Measures to halt the deterioration include braking economic growth but not dousing inflation or labor unrest.

At the heart of the problem is the trade deficit. It has been expanding at a breakneck pace, but the government steadfastly refuses to impose strict import controls. Another element aggravating the shaky balance-of-payments position is debt service obligations, which amounted to about $240 million last year.

The administration is making a determined effort to slow inflation and is thus persisting in its tight credit policies. The result, though, is a badly hobbled industrial sector.

All the signs point to a devaluation as a partial solution to the country's balance-of-payments woes. However, the political consequences of devaluation will make life harder for President Rodrigo Carazo. He is already in the thick of political fighting, Congress has been blocking his bills, and unions are angry with his occasional antilabor stance. Industry is upset with the administration's monetary policies.

Carazo's troubles will not cause him to step down, however, and the traditional political stability that Costa Rica enjoys will continue. The country will be preoccupied next year with preparations for the 1982 presidential elections.

Gross domestic product will rise 4% at best this year, marking no significant advance over last year's modest 3.5% expansion. The government's austerity measures and slack private-sector investment are the prime reasons for moderate growth. The mild growth pattern should persist into 1981. Currently GDP equals close to $4 billion.

- **Modest GDP growth**
- **Stable political climate**
- **Widening trade deficit**
- **Continued high inflation**

Agriculture is suffering because of poor weather conditions and labor disruptions. Production last year rose 6.2%, but this year's rise is not expected to go beyond 5%. The sector should pick up in the 1981 crop year, barring more weather setbacks. The 1980 coffee crop, estimated at 1.48 million bags, will be just a fraction over the 1.4 million bags harvested in 1979 (when a labor shortage caused losses) and still well under the 1.7 million bags picked in 1978. The 1981 output, however, is forecast at a more favorable 1.66 million bags.

Banana production has been hampered by strikes and by black sigatoka disease. Output was estimated at 1.1 million MT, but this year's production will not exceed one million MT.

Also on the downside this year is beef production, which has fallen about 15% compared with 1979. Exports of heifers accelerated last year, thus depleting the cattle available for slaughter this year. The government is granting a $12.5 million credit to promote cattle breeding.

Sugar production is down 5% this year from 1979's 194,000 MT, and because of the shortfall—and a non-bumper crop last year—sugar mills are working at only 65% capacity. However, favorable international prices for sugar will help compensate for the reduction in volume. Next year, the government intends to promote additional planting of sugarcane, in preparation for a gasohol plant.

The government will continue its low-cost credit program to stimulate production of nontraditional products, such as African palm oil.

Industrial production will rise about 4–4.5% this year after an increase of 5.3% in 1979. The slowdown is occurring because of tight credit conditions, higher operating costs (e.g. fuel and interest rates) and a reduced market for industrial exports, which primarily go to the Central American Common Market (CACM).

Industries that fared particularly well last year were coffee processing, lumber, paper and chemicals, all posting higher production levels.

Tourism may be in for a growth push. Mexico plans to help Costa Rica develop its tourist sector, and a joint committee has been formed to study the matter. So far, Costa Rica's small but lively industry seems unaffected by the political turbulence in Guatemala and El Salvador.

Investment. The government is relying on private-sector investments to spur the economy, inasmuch as it has pledged to reduce its own spending as part of the austerity program. However, new private investment projects announced so far this year amount to no more than $4 million in total. They are primarily concentrated in small industries, such as wooden-toy manufacture, furniture and packaging.

Despite promises to cut spending, the government does have a variety of projects lined up, particularly in energy-related fields and agribusiness ventures.

Officials have contracted with a Japanese firm to do a feasibility study for a free zone to be established in the ports of Moin on the Atlantic and Caldera on the Pacific. The plan, which would encompass a 4–6 year period starting in 1981, envisions space for more than 30 exporting industries. Priority sectors would be electronics, textiles and metalworking—all labor-intensive.

In the energy field, the Carazo administration will pursue the development of hydroelectric resources with the construction of the $150 million Corobici Dam that is to produce 174 Mw of electricity. Another plant, nearly completed, is the Arenal hydroelectric project, capable of generating 157 Mw.

Additionally, the government has obtained financing for a rural electrification project from the Inter-American Development Bank, (IDB). The loan is for $26 million. Over 20,000 residents will benefit from the program once it is completed. Other loans have been contracted for road construction and waterworks.

The government's plan to buy the fertilizer plant Fertica from the Mexican government is creating a political uproar. The price tag is $22 million but could go higher. The plant, highly dependent on imported raw materials and a money loser all along (since its output cannot compete with imports), is causing political problems for President Carazo.

Prices. No strides will be made against inflation this year. The COL is expected to climb to at least 16% compared with 15.2% in 1979. The upward push is coming from higher import costs, plus rises in food and beverage prices.

Efforts to reduce inflation are centered on tight monetary and fiscal policies, as well as on a limited tariff reduction program aimed at inducing competition at home. The government is also striving to cut deficit spending by state agencies and to limit foreign borrowings.

Next year, the government's anti-inflation efforts are likely to be undone by an expected devaluation, which could send a charge through the COL raising it to the 18–20% level.

Labor unrest has plagued the Carazo administration. Numerous strikes have been staged by public and private-sector workers. One of the longest was in the banana-growing sector. The banana workers won an 18–22% wage increase, but the average raise for industrial workers this year has been only 10.9%. Unions will undoubtedly press for higher wages, and more strike activity may be forthcoming—especially if the colon is devalued, since this would cut even deeper into real wages.

Money and credit. A tight lid will be kept on credit expansion this year and probably next. In 1980, credit to the private sector is expected to grow only 15%, compared with 20% in 1979, while that available to the public sector is anticipated to expand by 19%, half of last year's 38.7% rise.

To attract foreign exchange to the banking system, the Central Bank has authorized an interest-rate hike on foreign-currency time deposits. One-year deposits now pay 12% (previously the rate was 11%) and six-month deposits, 11.5% (vs 10.5%).

Foreign trade. Another huge trade deficit of about $625 million is expected this year, following 1979's $560 million shortfall. Exports rose in 1979 to $890 million, while imports surged to $1.45 billion. This year, exports are expected to reach $975 million and imports, about $1.6 billion.

Part of the country's trade troubles lie in the sluggish performance of its traditional commodity exports—coffee, bananas and sugar. But far more devastating is unbridled import growth. Costa Rica's main imports are petroleum, capital goods, wheat and intermediate consumer items. Its principal suppliers are the US and CACM.

On the export side of the ledger, some traditional products performed well last year. Coffee produced $325 million in export income, principally because of favorable prices, but also as a result of a volume increase, since part of the 1980 crop was included in the 1979 shipments. This year, coffee receipts will be at least 15% less because of a falloff in the world price of the commodity.

Sugar exports, on the other hand, will fare better, reflecting higher international prices. Revenues from sugar totaled $17.5 million last year. Bananas produced $155 million in 1979, but income is expected to shrink in 1980 because of production shortfalls.

Trade with CACM in the first four months of the year was in the black, with exports of $77.9 million and imports of $72.8 million. The favorable balance was due mainly to a rise in exports to Nicaragua, which bought $35 million worth of Costa Rican items.

No improvement will be seen in the trade deficit next year, unless the government restricts imports severely.

Foreign exchange reserves. Costa Rica faces an exchange shortage because of its trade deficit and the debt-servicing commitments on its $1.6 billion foreign debt. As of May 1980, reserves were just $86.7 million, down from the $134.8 million registered a year earlier. The government recently obtained $125 million in foreign loans from four commercial banks to bolster reserves.

The administration is anxious to stave off a devaluation. However, such a move seems inevitable. It could occur either at year-end or sometime in 1981; the magnitude of the depreciation will probably be around 20%, bringing the rate up to C10.28:$1 from the current C8.57:$1.

Measures to avoid a devaluation, imposed by the government with the advice of the IMF, have not been successful. Earlier this year, the IMF granted a stand-by agreement of approximately $94 million. However, the government has only been able to draw some of that because of its failure to keep state agencies' spending in line, sufficiently trim the central government's fiscal deficit and hold down foreign borrowing. A refinancing of the debt is also a certainty in the coming 12 months.