Country Report
Costa Rica

Sound fundamentals but fiscal fragilities

General Information

GDP	USD49.553bn (World ranking 82, World Bank 2014)
Population	4.94mn (World ranking 118, World Bank 2014)
Form of state	Democratic Republic
Head of government	Luis Guillermo Solis
Next elections	2018, presidential and legislative

Strengths

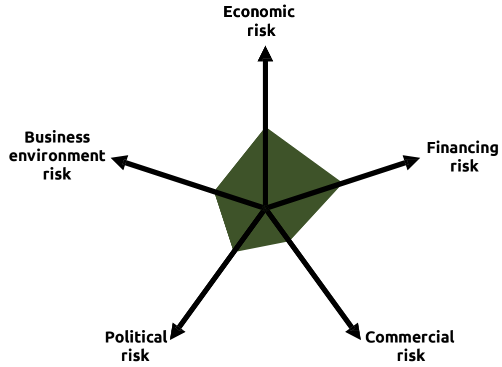
- Stable, enduring democratic framework
- Dynamic tourism sector
- Moderate public and external debt
- Large FDI inflows
- Large foreign reserves, covering more than 5 months of imports

Weaknesses

- High dependency on US (foreign investment in a few large companies, export demand and tourism)
- Large fiscal deficit which requires tax reform to raise the low structural revenue base
- Declining exports

Country Rating

BB1



Source: EulerHermes

Trade Structure

By destination/origin (% of total)

Exports		Rank		Imports
United States	29%	1	48%	United States
China	13%	2	8%	China
Malaysia	10%	3	7%	Mexico
Mexico	8%	4	3%	Japan
United Kingdom	8%	5	3%	Israel

By product (% of total)

Exports		Rank		Imports
Electrical machinery	58%	1	20%	Electrical machinery
Vegetables and fruits	15%	2	12%	Petroleum products
Office machines	5%	3	6%	Road vehicles
Scientific instruments	4%	4	4%	Miscellaneous articles
Miscellaneous articles	2%	5	4%	Telecommunication

Source: ITC, Chelem

Economic Overview

Growth on the path to recovery

Real GDP decelerated to +2.7% in 2015 after +3.5% in 2015. The sharp contraction of exports (-8.6%) caused by Intel's (microchips) withdrawal from the country and negative effects from adverse weather conditions (El Niño) on agriculture output was the main drag on growth. Domestic demand remained indeed dynamic. Private consumption accelerated to +4.6% (from +3.9% in 2014), supported by low oil prices, negative inflation, and buoyant credit growth. Investment also strengthened to +8.2% from 4.5% in 2014

Euler Hermes expects the economy to accelerate to +3.6% in 2016 as (i) the negative effect of Intel's withdrawal vanishes; (ii) monetary policy is expected to remain supportive; and (iii) households' spending and investment should remain dynamic.

Sound macroeconomic fundamentals but public accounts developments should be monitored

The macroeconomic environment is generally sound, with political stability and an overall business-friendly framework. The country remains a place of choice for business, performing above the regional average in terms of ease of doing business, regulatory quality, the rule of law, and control of corruption. The monetary policy is framed for inflation targeting, currently for 3% (+/-1pp). The exchange rate policy was changed in February 2015 from a band system in place since 2006 to a managed float. This shift has had a minor impact on the local currency movement since the Colon had been de facto afloat since mid-2014.

Although still under control, developments in the public accounts are raising some concerns. The government is struggling to reduce the fiscal deficit, which widened to -6% of GDP in 2015 and is expected to remain wider than -5% until 2017. In August 2015, the government proposed a set of tax reforms aiming to raise fiscal revenues by 2 points of GDP through raising the VAT rate (to 14% the first year and 15% the second year) along with a rise in the individual income tax rate (up to 25%) and setting capital taxes. Yet the package was not approved by the Congress which is controlled by the coalition opposition since May 2015. Consequently, the public debt has risen rapidly, reaching 44% of GDP in 2015, almost twice its 2009 levels.

The high dependence of Costa Rica to oil imports (13% of total imports) and to agriculture exports (18% of total exports) makes the small economy vulnerable to the hazards energy and commodities prices. The economy is heavily relying on the economic performance of the US n, absorbing 33% of its exports and providing 61% of total FDI. Besides, the high credit dollarization can be a threat to the banking system. However, external and financing risks are under control especially as Costa Rica enjoys easy access to capital markets. The external debt is relatively low, FX reserves are comfortable (around 6 months of imports). In spite of the persistence of the current account deficit, accounting for 3.8% of GDP in 2015, this latter is narrowing since 2013 (5% of GDP), thus restraining the external vulnerability of the country (80% of the deficit is covered with FDI).

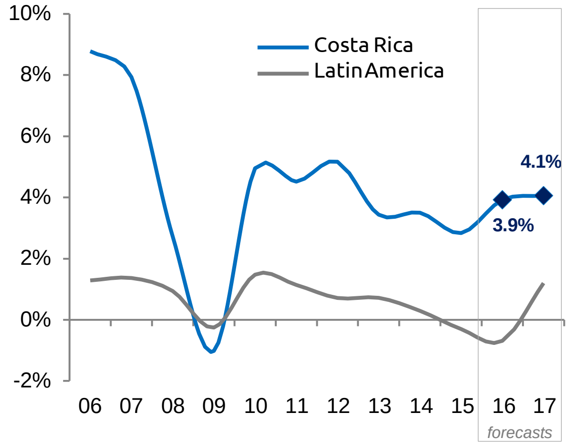
Key economic forecasts

	2014	2015	2016	2017
GDP growth (% change)	3.5	2.8	3.9	4.1
Inflation (%, yearly average)	4.5	0.8	0.5	3.2
Fiscal balance (% of GDP)	-6.0	-5.8	-5.9	-5.5
Public debt (% of GDP)	39.3	42.4	45.3	47.6
Current account (% of GDP)	-4.8	-3.8	-4.0	-4.0
External debt (% of GDP)	41.8	39.6	40.3	41.0

***Includes Local Government; Non-financial Public Corporations; Social Security Funds; State Governments*

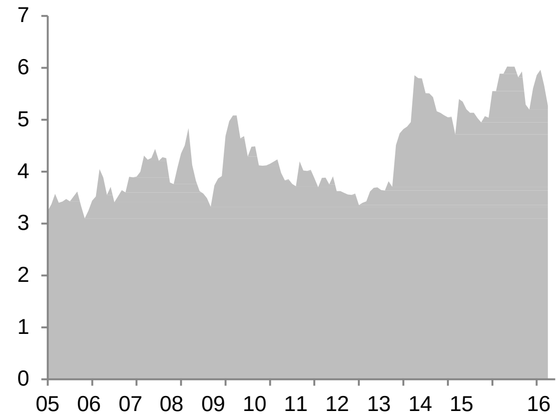
Sources: National sources, IMF-WEO, IHS, Euler Hermes

Real GDP growth (%)



Sources: IHS, Euler Hermes

FX import cover (months)



Sources: National sources, IMF-WEO, IHS, Euler Hermes

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