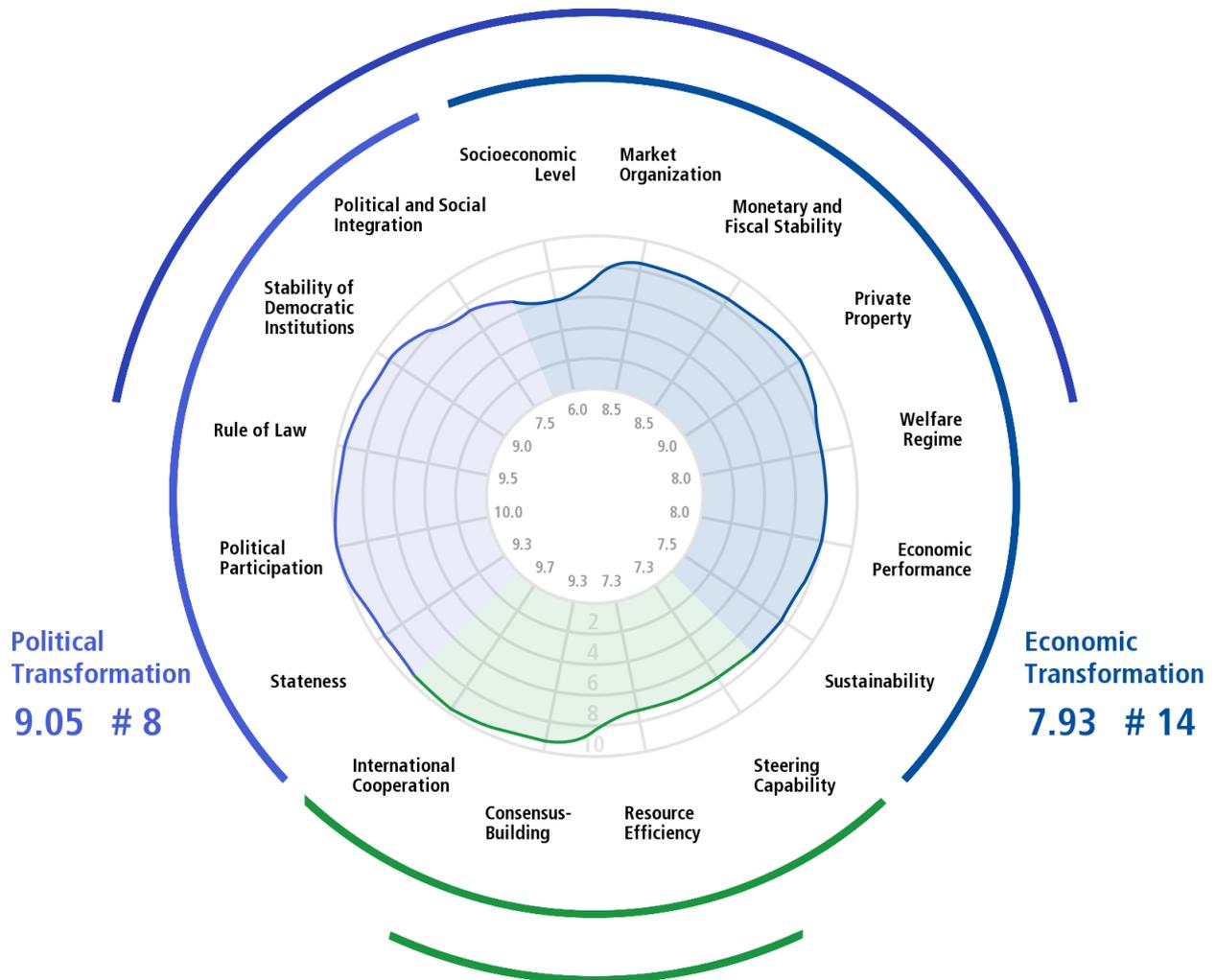


# Costa Rica

## Status Index

**8.49 # 11**

on 1-10 scale out of 137



**Political Transformation**  
**9.05 # 8**

**Economic Transformation**  
**7.93 # 14**

## Governance Index

**6.92 # 9**

on 1-10 scale out of 137

This report is part of the **Bertelsmann Stiftung's Transformation Index (BTI) 2020**. It covers the period from February 1, 2017 to January 31, 2019. The BTI assesses the transformation toward democracy and a market economy as well as the quality of governance in 137 countries. More on the BTI at <https://www.bti-project.org>.

Please cite as follows: Bertelsmann Stiftung, BTI 2020 Country Report – Costa Rica. Gütersloh: Bertelsmann Stiftung, 2020.

This work is licensed under a [Creative Commons Attribution 4.0 International License](https://creativecommons.org/licenses/by/4.0/).

## Contact

Bertelsmann Stiftung  
Carl-Bertelsmann-Strasse 256  
33111 Gütersloh  
Germany

### **Sabine Donner**

Phone +49 5241 81 81501  
[sabine.donner@bertelsmann-stiftung.de](mailto:sabine.donner@bertelsmann-stiftung.de)

### **Hauke Hartmann**

Phone +49 5241 81 81389  
[hauke.hartmann@bertelsmann-stiftung.de](mailto:hauke.hartmann@bertelsmann-stiftung.de)

### **Robert Schwarz**

Phone +49 5241 81 81402  
[robert.schwarz@bertelsmann-stiftung.de](mailto:robert.schwarz@bertelsmann-stiftung.de)

### **Sabine Steinkamp**

Phone +49 5241 81 81507  
[sabine.steinkamp@bertelsmann-stiftung.de](mailto:sabine.steinkamp@bertelsmann-stiftung.de)

**Key Indicators**

Population	M	<b>5.0</b>	HDI	<b>0.794</b>	GDP p.c., PPP \$	<b>17645</b>
Pop. growth <sup>1</sup>	% p.a.	<b>1.0</b>	HDI rank of 189	<b>68</b>	Gini Index	<b>48.3</b>
Life expectancy	years	<b>79.9</b>	UN Education Index	<b>0.716</b>	Poverty <sup>3</sup>	% <b>2.7</b>
Urban population	%	<b>79.3</b>	Gender inequality <sup>2</sup>	<b>0.285</b>	Aid per capita \$	<b>20.0</b>

Sources (as of December 2019): The World Bank, World Development Indicators 2019 | UNDP, Human Development Report 2019. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

## Executive Summary

During the period under review, Costa Rica experienced a slowdown in economic growth and an increase in unemployment and poverty. A large fiscal deficit generated considerable uncertainty, restraining economic actors and dominating the political landscape. However, the authorities were able to preserve macroeconomic stability through monetary and exchange rate policies. A political breakthrough at the end of the period saw the enactment of a fiscal reform package that pulled the country back from the brink of a financial crisis. While insufficient to fully stabilize state finances in the medium and long-term, the reform represents an important first step toward structural transformation. The period also saw the reaffirmation of strength as seen by high levels of human development and active democratic life, and strong commitments to social protection, education and renewable energy. At the same time, structural factors limited the country's ability to progress faster.

The country held a successful, transparent national election in two rounds despite an environment highly polarized around religious and gender issues. Support for democracy strengthened but its volatility may suggest some degree of ambivalence among citizens, which also show low levels of satisfaction with the functioning of democracy. Contributing factors may be the lower levels of economic performance but also higher crime rates and citizen insecurity. Trust in and identification with political elites remained weak and were further damaged by allegations of judicial corruption. Party fragmentation increased in the Legislative Assembly, where the president's party is in the minority and has only the third legislative group by size. This will create challenges for the passage of additional reforms needed to control public expenditures, which are expected to continue outpacing revenues.

Despite high levels of social spending, poverty and extreme poverty levels have remained around 20% and 6% of households, respectively. Inequality levels remained high relative to historical levels. When disaggregated by region and gender these indicators reveal that rural and peripheral areas fare much worse than urban ones, to the disadvantage of ethnic minorities – and women fare worse than men. Women earn less than their male counterparts and suffer from higher

unemployment. While some of the market transformations of previous decades created a dynamic external sector, attracting considerable foreign direct investment (FDI), they also resulted in a two-tier labor market highly favorable to skilled workers, but not the unskilled who represent a majority of the labor force. Education may be falling short as a source of opportunity as dropout rates at the secondary level remain high and achievement scores remain low, despite elevated and increasing levels of spending.

The overall pace of economic and political transformation in the country will continue to be challenged by structural factors that remain unchanged from previous years. The opening of banking, electricity, telecommunications and insurance to competition has contributed to market growth, lower prices and quality improvements in these areas. However, legally sanctioned restrictions and monopolies remain, creating an uneven playing field and limiting gains from additional transformation. An increasingly complex public administration and a large number of veto players in the political system, including an assertive Constitutional Court, a fragmented party system and lax legislative rules of procedure that empower minor parties make change difficult. While a system that fosters consensus may be desirable, at the extreme it can limit adaptation to challenging and changing circumstances. Future transformational capacities will therefore depend on the ability to improve upon some of these features.

## History and Characteristics of Transformation

Costa Rica is the longest continuous presidential democracy in the Western Hemisphere, second only to the U.S. Even among developing nations, the longevity of its democratic regime is second only to India. One of its key transformation moments was the adoption of a new constitution in 1949 after a civil conflict in 1948. This document, and its subsequent reforms, established the bases for the country's political and economic development throughout the second half of the twentieth century. It made the state a key player, entrusting it with the fulfillment of key social, economic, and (later) environmental rights, while maintaining important areas of the economy, like banking, electricity and telecommunications, as state monopolies. It also entrusted the state with the administration of health, education, and housing, and spawned a network of autonomous institutions. The constitution innovated with the abolition of the army and the creation of an Electoral Tribunal. This tribunal has the rank of a fourth branch of government and enjoys complete autonomy from the executive, legislative and judiciary branches.

This constitutional model enabled key accomplishments. It solidified democratic institutions by enabling and assuring widespread participation and robust political party competition. It fostered strong public investments in human and physical capital and the rule of law, which served as backbones to the development of the economy. Finally, it made possible the attainment of high levels of human development, balancing social and economic priorities, reducing poverty and inequality and protecting the country's environmental patrimony.

In the last 60 years, disagreements between the legislative and executive branches have always been settled through institutional channels, consolidating the democratic system. However, the country has endured periods of economic instability. At the end of the 1970s, the state-based model

came under stress through the combined effects of internal inconsistencies and the adverse international conditions sparked by the OPEC shocks and world recession. Rising fiscal and trade imbalances, accompanied by growing debt, climaxed in runaway inflation and massive currency devaluation, leading to a process of structural reform in the early 1980s. Significant liberalization took place during this period mainly within the trading sector, where tariffs and duties were reduced. Privatization was restricted to unprofitable state enterprises while state monopolies in banking, insurance and utilities were left untouched. Only gradually did liberalization advance in these areas, starting with the banking sector in the 1990s. An export-promotion strategy succeeded in attracting foreign direct investment and allowing the country to diversify its production base, first through non-traditional agricultural exports and later through high-tech industries clustered in free trade zones. International insertion also spawned the development of a vibrant tourist industry, much of it premised on the country's ecological riches, which currently brings in over three million visitors – more than half the country's population – annually.

A key transformation occurred in 2007, when the Central American Free Trade Agreement was ratified in the country's first-ever referendum. The agreement encompassed a set of complementary laws that called for the opening of competition in telecommunications and insurance. However, as in banking, no privatization occurred. The state lost its monopolies, but its firms remain and compete against the private sector. While this improved the competitiveness of markets, it is not clear that it provided a completely level playing field.

Another key turning point was the establishment of a fourth, constitutional chamber in the Supreme Court in 1989. The court has jurisdiction over the protection of individual rights, the interpretation of the constitution, and the settling of disputes among the branches of government. Access to the court was made broad and virtually costless, in fact revolutionizing the exercise of constitutionally guaranteed individual rights and their protection. This also facilitated challenges to the constitutionality of laws and statutes, activating a check that had been effectively inoperative since 1949. While highly valuable and important, the court has become an assertive arbiter of political disputes, particularly as executive-legislative relations have become more quarrelsome and gridlocked. The court has also entered the realm of administrative decision-making in its enforcement of individual rights. Because lawmakers can submit bills to the court for prospective opinions about their constitutionality, it has also become an important veto player in the legislative process.

Costa Rica's political and economic performance has shown some signs of stagnation in recent times. Economic inequality has increased, and poverty levels have remained stagnant. The country's basic infrastructure has not been modernized fast enough to support the needs of a more dynamic economy, and not all participants in the labor market have benefited equally from economic modernization. Corruption scandals have tarnished the reputation of traditional parties, contributing to the collapse of the long-standing two-party system and generating widespread disenchantment with politics and politicians. Deficient financial management appears to be undermining the country's welfare system. Thus, transformational change has become increasingly more difficult and Costa Rica's regional lead in basic social and economic indicators has eroded.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

## Transformation Status

### I. Political Transformation

#### 1 | Stateness

The state's monopoly on the use of force remains unchallenged, but it faces considerable threats in the area of citizen security. Inroads by drug-trafficking organizations have made the Central American region dangerously prone to violent crime, with homicide rates averaging four times the global rate. While Costa Rica has not reached the levels of criminal violence of the countries in the Northern Triangle (Honduras, Guatemala and El Salvador), its homicide rates nearly doubled between 2000 and 2015, from 6.1 to 11.5 deaths per 100,000 inhabitants. In 2017, the country reached 12.2 deaths per 100,000, its highest historical level. A significant portion of these deaths are attributable to local drug gangs, which in many cases are surrogates for international cartels, according to national security officials. The state has responded with a series of policies including social violence prevention, stricter gun control, improved coordination of intelligence, and better funding and training for police.

Territorial disputes with Nicaragua continue to be a source of national concern and international attention. Costa Rica has obtained favorable rulings from the International Court of Justice (ICJ) in the Hague reasserting its sovereignty over its maritime boundaries and a disputed stretch of land on the Atlantic coast.

The legitimacy of the nation-state is broadly accepted by the population. There are social and political actors that seek to strengthen their influence through collective action, including through acts of civil disobedience like street blockades, but they do not question the legitimacy of the nation-state. Some public sector unions have on occasion threatened to counter public decisions through "street democracy," and recently claimed the disenchantment of the populace was leading to calls for armed struggle through social media. But what, if anything, beyond popular mobilization this means has remained ambiguous, and unsubstantiated. During the Solís administration there was a significant demobilization of protest attributed to closer links between social sectors and the government. All rights, including human rights,

Question  
Score

Monopoly on the  
use of force

9



1

State identity

10



1

are recognized throughout the country, and are backed by an effective and highly accessible Constitutional Court. All individuals and groups enjoy the right to acquire citizenship without discrimination. Costa Rica has a considerable number of foreign-born among its population, especially Nicaraguans, and is welcoming to refugees and migrants.

Although Article 75 of the constitution establishes Roman Catholicism as the state religion, that same article recognizes freedom of religion. This has generated calls from some sectors for the complete secularization of the state. Catholic archbishops and clergy, together with evangelical political parties are vocal on key political issues, actively opposing in-vitro fertilization, abortion and same-sex marriage. This last issue turned the 2018 presidential election into a referendum on gay rights after the Inter-American Court of Human Rights issued a ruling in January obligating Costa Rica to legalize same-sex marriage. Fabricio Alvarado, an evangelical pastor and religious singer, mobilized conservative opposition to the ruling, promising to remove the country from the regional court's jurisdiction if he won. He won the first round, but not the second, and the Constitutional Court eventually ruled the ban against same-sex marriage unconstitutional and discriminatory, giving the legislature an eighteen-month deadline to change the law.

At an administrative level, the state successfully provides basic services on a national scale, particularly in health, education, potable water, electricity, and telecommunications. In recent years, the state has improved its handling of wastewater. It has also increased tax revenues through improvements in collection and better enforcement, although according to a December 2018 report by the General Comptroller, elusion and evasion remain significant. Executive capacity has been questioned in the area of transportation infrastructure, where projects face continuous delays and cost overruns. A notable example is the development of a 30 km highway to the city of San Carlos, which remains incomplete after thirteen years of construction. The social security system (CCSS) has faced criticism for long health service queues and irregular drug availability. A 2016 actuarial evaluation by the University of Costa Rica also revealed that the reserve fund for the country's retirement and insurance system, administered by the CCSS, may become insufficient in a matter of years in the absence of draconian reforms. These would include raising the retirement age to 70, cutting the replacement rate by one-fifth and increasing the contribution rate from its current 9.5% to 25% by 2055. Other studies have shown salaries in the public sector exceed those in the private sector and are on an unsustainable growth trajectory due to a complex system of perks and benefits.

No interference of religious dogmas



1

Basic administration



1

## 2 | Political Participation

There are no constraints on free and fair elections. The Supreme Electoral Tribunal has evolved into a worldwide prototype of excellence in the organization and management of elections. Electoral registration is automatic and virtually costless with the acquisition of an identity card required for all citizens. Political parties receive state funding based on their vote shares. Electoral participation was expanded with the institution of plebiscites and referenda (2006) as well as the direct election of municipal executives and councils (2002). In 2016, elections for the country's 81 municipal governments were held separately from national elections for the first time with over 30,000 candidates representing 59 political parties. The number of political parties fielding candidates at the national level has also been on the rise with thirteen in the first round of the 2018 presidential election and seven obtaining representation in the legislature.

Democratically elected political representatives have effective power to govern and there is no single group or individual capable of exercising an absolute de facto form of veto power. While there are powerful actors capable of influencing the course of public affairs, notably business groups, public unions, the clergy and the press, among others, none of them can exercise an uncontested veto. No single group can stop the enactment of decrees or legislation without due process and only if the Constitutional Court rules that the legislation or decrees in question are unconstitutional.

Association and assembly rights are unrestricted for individuals and independent political or civic groups and guaranteed by the constitution and labor code. There are multiple groups in multiple sectors organized at the national, regional and local levels, which regularly exert their influence on government and public opinion, including through mobilization and protest. New groups, such as advocates for sexual diversity, indigenous rights, the informal transportation sector and environmentalists have recently emerged onto the social protest scene, experiencing no discrimination from the government. Unionization in the private sector is not extensive, but many workers join solidarity associations that provide low-interest loans, health and recreation services, and savings accounts, and may serve as a channel for labor relations. Whether these organizations serve as a mechanism to hinder unionization, as labor union leaders allege, is a point of contention.

Free and fair elections

10



1

Effective power to govern

10



1

Association / assembly rights

10



1

Freedom of expression is unrestricted for citizens, groups and the press as guaranteed by Articles 26 to 29 of the constitution. A broad array of press outlets, from newspapers to radio, television and the internet inform citizens and provide varied perspectives on the news and current affairs. The country is ranked 10 out of 180 countries in the Reporters Without Borders' 2018 Press Freedom Index, the highest in the Western Hemisphere, including Canada and the United States.

State actors have at times attempted to restrain these rights, but they have been rebuffed through the system of checks and balances. For example, in 2014 the Constitutional Court invalidated orders issued by the General Prosecutor to monitor the communications of journalists at the newspaper "Diario Extra." In 2015, the Solís administration (PAC) proposed a new law that would have established limits to free expression, effectively punishing the use of certain types of language. This widely decried "gag law" was shuttled, and later that year the legislature derogated three articles of a 1954 law that contained similar provisions, but that had long ceased to be enforced. In 2016, the Constitutional Court condemned a state bank for using public funds as a means of coercion and censure aimed at misdirecting public opinion when it withheld advertising contracts from newspaper "La Nación" in retaliation for critical reporting about the bank.

### 3 | Rule of Law

There is a clear separation of powers with mutual checks and balances, structured around the 1949 constitution and its subsequent reforms. The system establishes three branches of government (executive, legislative, and judiciary) adding a fourth, the electoral branch (the Supreme Electoral Tribunal). From a comparative perspective, the Costa Rican executive is relatively weak. Its decree powers are limited and subject to ratification by the Legislative Assembly, hence rarely used for substantive legislative purposes. Control of the legislative agenda is shared with the Legislative Assembly. In recent years, the amount of legislation emerging from the chamber originating from the executive has been decreasing. At the same time, growing party fragmentation and ideological polarization have weakened the decisiveness of the legislature and complicated relations with the executive. This has increased the importance of the judiciary, particularly the Constitutional Court, which is charged with settling jurisdictional disputes between the other branches and interpreting the constitutionality of laws.

An additional component of the separation of powers is the existence of horizontal accountability mechanisms to oversee and regulate the activities of the executive and its administrative entities. These entities, which are decentralized, largely autonomous and functionally specialized, provide services in the health, financial, energy, telecommunications, insurance and water industries. Their budgets account for as much as two-thirds of public spending and are not subject to legislative

Freedom of  
expression

10



1

Separation of  
powers

10



1

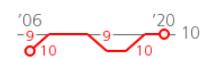
approval. They also enjoy considerable autonomy from the executive in terms of their management. Such levels of decentralization and autonomy require horizontal control mechanisms. Principal among these is the Comptroller General’s Office, which has a broad and strong mandate to supervise the use of public funds, not only based on legality but also efficiency and outcomes. It has recently been critical of high levels of sales tax evasion and the numerous emoluments known as “pluses” that elevate salaries in the public sector.

The judiciary is independent and free from intervention by other institutions. The second article of the Organic Law of the Judicial Branch establishes that its authority is subject only to the constitution, the law, and its own decisions regarding matters within its competence. The independence of the judiciary is also guaranteed by a constitutional provision that grants it 6% of the state’s expected revenues for its operating budget. Norms of independence are entrenched and zealously defended by all sectors, especially the court magistrates themselves. During the process leading to the approval of a fiscal reform law in 2018, the magistrates warned that some of its provisions, which empowered the executive to control expenditures, would violate judicial independence. However, the Constitutional Court eventually pronounced itself in favor of the reform, indicating that general state policies setting limits on expenditures did not necessarily violate the judiciary’s organization and functioning.

The courts are widely trusted and used by citizens and private corporations as an arena to settle disputes. They are not believed to be corrupt in general terms, but cases of corruption do emerge and are prosecuted. One clear example occurred in 2018, when accusations of influence peddling led to the first-ever firing of a Supreme Court magistrate. The judge was charged with improperly interfering with several judicial procedures involving a businessman accused in a fraudulent scheme to import Chinese cement with whom he maintained a close relationship. An inquiry led to the expulsion of the judge from the Supreme Court in February 2018 and the legislature revoked his investiture as magistrate in April of that same year. The Attorney General at the time and three other magistrates were also implicated in the cement case. They were charged with summarily dismissing a criminal case against two legislators who also allegedly attempted to influence the case. They received disciplinary sanctions, in the wake of which, three opted for an early retirement.

Independent  
judiciary

10



1

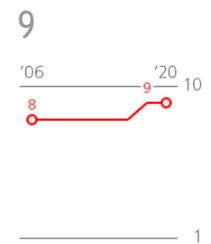
The Costa Rican state has ratified international treaties, approved laws, and supported watchdog organizations against corruption. Its ranking in global corruption studies is generally good. Citizen awareness and activism against office abuse is high, partly because of a vigilant media that has been quick to denounce it. The evidence suggests that allegations of corruption that are exposed will be prosecuted, including those involving former presidents, ministers, judges and mayors. However, even when prosecution occurs it takes a long time and often fails to bring charges against the accused parties. This may account for negative perceptions regarding the prosecution of office abuse. In the 2017 Latinobarómetro poll, 59% of respondents said there had been no progress in the reduction of state corruption over the past two years.

Polling by the University of Costa Rica shows that a view that corruption was the country's main problem diminished steadily during the Solís administration. However, it started rising again in 2017 after a scandal of fraud and influence peddling erupted around an importer of Chinese cement. Dubbed the “Cementazo” – loosely translated, the big cement heist – the case involved a dense network of relationships around a businessman, including a Supreme Court magistrate, an attorney general, several legislators, a mayor, bank administrators and even the president. The question was to what degree such relationships had helped secure multimillion loans from a state bank and shelter the actors from legal scrutiny. As the loans went into default, the main actors were indicted and are now awaiting trial. The case was unprecedented to the degree that it allegedly revealed corrupt dealings among the political class, but especially because it tarnished the judiciary, which had to date escaped the corruption scandals that had plagued the legislative and executive branches. Trust in the judiciary as captured in University of Costa Rica polls fell almost six points at the height of the scandal.

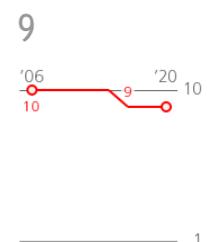
Civil rights and non-discrimination are guaranteed by the constitution and enforced through institutions like the Constitutional Court and the Ombudsman's Office. The Constitutional Court allows individuals to seek recourse (“Amparo”) for the violation of constitutional rights. Access to the court is extremely open and virtually free. Anyone (including non-citizens) can present a writ without needing a lawyer or using specialized language. Only a description of the grievance is required. The court's decisions carry the force of law and cannot be appealed. The Ombudsman's Office (or Defender of the Inhabitants) serves as an advocate of citizen rights and intervenes at the administrative and judicial levels to remediate rights violations, both for individuals and groups. According to the Latin American Public Opinion Project (2016/17), 67% of citizens consider that their basic citizenship rights are protected by the state at or above the median level.

A constitutional amendment was passed in 2015 to define Costa Rica as a multiethnic and pluricultural republic, highlighting the historical relevance of racial and ethnic minorities not formerly acknowledged in the country. Together with laws and regulations safeguarding the rights of indigenous peoples, promoting female electoral

#### Prosecution of office abuse



#### Civil rights



inclusion and preventing violence against women, these institutional structures evidence a formal intention to protect minority rights. However, real outcomes suggest that inequalities persist in the degree of access to these rights. Freedom House (2018) affirms that the LGBTQ community faces persistent discriminatory attitudes and practices from law enforcement officials. There have also been delays in the passage of legislation that would improve LGBTQ rights in the country. For example, while the Constitutional Court ruled the statutes prohibiting same-sex marriage unconstitutional in April 2018 it kept them in place for eighteen months, the period it granted the legislature to issue new, egalitarian regulations. Indigenous people, who make up about 3% of the population, face discrimination. There are no indigenous representatives in the legislature and land disputes involving protected holdings of indigenous communities persist.

#### 4 | Stability of Democratic Institutions

Democratic institutions are the effective means through which political decisions are prepared, made, implemented and reviewed. However, their relative efficiency has been under strain. Fragmentation and ideological polarization have increased in the legislative assembly, where the governing party has not held the majority since 1994. The current government of Carlos Alvarado controls only 18% of the seats in the legislature and has only the third largest legislative group (of seven). Together with factional divisions within political parties, this has increased the difficulty of coordination between the legislative and the executive.

A profusion of veto players within the institutional domain of the state has increased the difficulty of enacting change. At the administrative level, the Comptroller General exercises strict financial and administrative control of the multiple organizations under its purview. While necessary, this greatly reduces the flexibility of the executive. At the citizen level, the Constitutional Court has empowered individuals against administrative action (or inaction) in every aspect of public service covered by the constitution. At the legislative level, procedural rules allow easy filibustering by minority groups, blocking the passage of substantive reforms. Legislators can also submit bills in process to constitutional review. These regime characteristics have diluted the effectiveness of democratic institutions while also reducing accountability, allowing different players to blame each other for stasis.

Costa Rica has a relatively weak executive with practically no decree powers and a limited veto. The enactment of its agenda depends on its ability to negotiate and generate political agreement, if not consensus. The shift from a two-party (1990-2002) to a multiparty system (2002-2018) has made this increasingly difficult. The *Estado de la Nación* finds that bills require nineteen months, on average, to be approved by the legislature, and only about 16% of those passed since 2011 have been of high priority. For the past Congress (2014-2018) the most important bills that

Performance of democratic institutions

8



1

remained pending dealt with fiscal stabilization, including taxation and public spending.

While there have been considerable efforts to increase the level of decentralization of the state by transferring greater competencies and resources to municipal governments, as well as allowing the citizenry to elect local representatives directly, the effectiveness and political reach of these governments still appears limited. The Latin American Opinion Project survey (2016/17) shows that only 7% of respondents attend municipal meetings, and 60% did not vote in the last municipal elections.

All relevant actors accept the legitimacy of democratic institutions. Democratic norms are well internalized and constitute part of the regular discourse among political actors. This includes the respect of due process and the rule of law, the acceptance of rulings handed down by the courts, the peaceful transfer of power, and the respect of civic and political rights as well as the investiture of public officials.

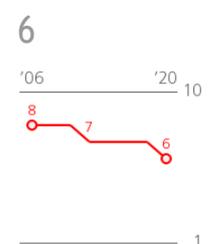
Commitment to democratic institutions



## 5 | Political and Social Integration

While organizationally institutionalized parties exist in Costa Rica, the party system has been relatively fluid since the end of the period of two-party rule in 2001, with a tendency to increase its fragmentation and ideological polarization, and with weak and volatile voter affiliation. This has corresponded with declining levels of electoral participation and a reduction of party loyalty and identification. Party discipline has also diminished, as evidenced by an increase in the number of elected legislators breaking from the party they were elected under. There are seven parties represented in the legislature. Weighted by their seat shares, this amounts to 4.74 effective parties.

Party system

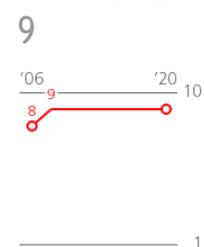


Several studies from Programa Estado de la Nación have highlighted the fragility and volatility of electoral support for the party system since 2006. Party loyalty tends to be short-lived and linked to the personality of party leaders rather than programmatic or ideological characteristics of the organization. According to the Latin American Public Opinion Project survey (2016/17), only about 20% of respondents say they trust political parties or identify with one. In the most recent national election (2018), almost 50% of voters did not vote for the same party they supported in the previous one (2014). Voters also tend to divide their votes, supporting different parties for the presidency and Congress in the same election. In the 2018 election, 30% of those who voted for the two parties that made it to the second round of the presidential vote, Acción Ciudadana (PAC) and Restauración Nacional (RN), voted for the legislative list of a different party.

Ideological polarization has also been on the rise, particularly since 2002. The two largest parties, Liberación Nacional (PLN) and Acción Ciudadana (PAC) have been moving in opposite directions along the left-right spectrum. However, the last presidential election (2018) evidenced a different kind of polarization, based not on socioeconomic factors but on sociocultural ones: same-sex marriage, abortion, sexual education guides and religion divided the electorate into progressive and traditional factions. The two parties at the far ends of the ideological spectrum, the Movimiento Libertario on the right and the Frente Amplio on the left, saw their electoral support fall from double digits in 2014 to barely 1% in 2018. Meanwhile, Fabricio Alvarado, an evangelical candidate for Restauración Nacional (RN), rose rapidly in the polls with support from traditional sectors, eventually winning the first round of the election, although he went on to lose in the second. This marked the first election in the country's modern democratic period in which the PLN was not a main contender, as it garnered only 18.6% of the vote in the first round. That a right-wing populist claimed almost 10% of the first-round votes was also significant.

Costa Rica has a broad range of interest groups, ranging from social movements and community organizations to unions and business and professional associations. There are currently several thousand registered civic associations, 3,704 community development associations, and 594 cooperatives. Unions represent about 14% of the workforce with an additional 16.6% represented by solidarist associations. The peak employer organization (UCCAEP) has 51 affiliates, which are associations in themselves and in turn represent most of the productive sectors of the economy. There have been numerous social movements involving collaboration between a broad spectrum of actors, organized and ad hoc. According to the Programa Estado de la Nación, most mobilizations are staged by organized workers, but they are followed in importance by citizen groups (neighborhood and family associations and others). An annual average of 387 incidents of organized collective action have been reported by the media between 1992 and 2017, but a notable decline was seen during the Solís Rivera presidency, with the final year of the administration (2017) registering the lowest number of episodes on record (176). This is attributable to a close relationship between the administration and union organizations and a significant degree of convergence between their agendas and priorities. The state is generally respectful of collective action, including social protests that sometimes involve illegal road closures, and abstains from repressing or undermining them. At the same time, there are no organized movements that seek to undermine democracy or civil society. Latin American Public Opinion Project surveys (2014, 2016/17) show that the percentage of Costa Ricans that engage in protest marches and demonstrations is roughly 7%.

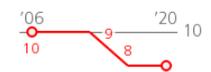
Interest groups



Since 2012, Costa Rica had been showing a downward trend in democratic approval that was consistent with the higher volatility of electoral preferences, lower levels of political participation and high levels of disenchantment with corruption. But recent indicators show an uptick in democratic support. The Latin American Public Opinion Project (LAPOP) measures the levels of diffuse support for democracy through an index of five questions that probe respondents' respect for democratic institutions, norms and rights. This index captures the generalized attachment of citizens to the more intangible objects of the political system and its institutions. In the 2012 LAPOP survey, Costa Rica scored its lowest value since 1978, 55.8 out of 100. Yet, only two years later in 2014, it led the Latin American region with the highest system support index score, 62.7. In a new study conducted in 2015 and reported by the Programa Estado de la Nación, Costa Rica's index score fell by almost four points to a value of 59, its second lowest value ever, marking a loss of nearly 20 points since 1978. But in the 2016/17 LAPOP survey, the system support index for Costa Rica bounced back to 62.2, the fourth highest in the region (including the United States and Canada). Mean levels of system support for democracy are theorized to be stable in the short run, since they capture the inherent value citizens place in democratic institutions, so this level of variability is significant and may suggest some degree of ambivalence about democracy among the citizenry.

Approval of  
democracy

8



1

Variability is more common with specific support for democracy, which is linked to the general performance of the democratic system. This is measured by asking respondents how satisfied they are with the functioning of democracy in their country. The proportion answering that they were very satisfied or satisfied in LAPOP surveys fell from 73.4% to 50.5% between 2014 and 2016/17. That this substantial reduction in levels of satisfaction did not reflect itself in the levels of system support suggests the persistence of a significant reservoir of legitimacy for democracy. This is confirmed by more abstract assessments of democratic support, such as the expressed support for democracy as the best system of government despite its flaws (Churchillian democracy). The number of respondents that agreed with this assessment increased slightly between the 2014 and 2016/17 LAPOP surveys and has hovered around 70%. It should be noted, however, that this level of support is close to the regional average, whereas in previous decades Costa Rica would score at the highest level of the regional rankings.

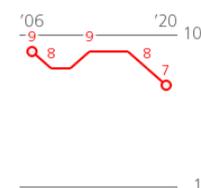
Another dimension of democratic legitimacy is the level of political tolerance among citizens, measured as the respect for the rights of others in ways that are congruent with open democratic competition and dissent. Individuals with high levels of system support and tolerance have attitudes that are conducive to democratic stability. In the 2016/17 LAPOP survey, Costa Rica's index of political tolerance comes in at 54.3, which is above the regional average (52.6) and similar to its 2015 level (55). The proportion of citizens considered to have stable democratic profiles in Costa Rica is 43%, the fourth highest in LAPOP's 2016/17 survey.

In summary, the downward trend in democratic approval that manifested itself between 2012 and 2015 appears to have stopped, but levels have not been restored to the higher levels they had in the past and remain highly variable.

The level of interpersonal trust as measured by opinion surveys is moderate and shows a decreasing trend. In 2010, the Latin American Opinion Project (LAPOP) ranked Costa Rica as having the highest level of interpersonal trust in the Americas, ahead of Canada and the United States. For its 2014 survey, Costa Rica scored right around the mean, and this level decreased further in 2016/17. The percentage of respondents that consider the people in their community to be somewhat or very trustworthy has fallen in every survey since 2010, going from a high of 77% to 69.9% in 2016/17. There is a considerable number of civic associations, unions, solidarist associations, cooperatives and community development associations. The degree to which individuals engage themselves with those organizations does not appear high. Of five types of associations evaluated by LAPOP in 2014 (religious, parents', community improvement, political, and women's), only for religious associations did 50% or more of respondents say they participate at a significant level. For the other four types of associations, upwards of 67% said they never engaged with them.

Social capital

7



## II. Economic Transformation

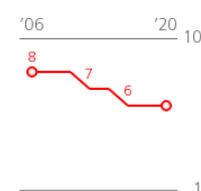
### 6 | Level of Socioeconomic Development

Costa Rica has promoted and maintained social inclusion policies that have resulted in high levels of human development. However, poverty reduction remains stagnant, inequality has increased and the country has not increased its human development score significantly in well over fifteen years (0.794, just below the category of Very High Human Development). The incidence of poverty and extreme poverty have remained above 20% and 6%, respectively, since 1994. Income inequality increased over the last decade, going from a Gini coefficient of 0.495 in 2006 to 0.514 in 2017. It peaked in 2013 at 0.522 and stabilized, with some yearly fluctuations, around an average of 0.518, a level considerably higher than the average during the 1990s (0.472). When adjusted for inequality, Costa Rica's 2017 HDI score falls by 18%, dropping the country ten points in the ranking. The richest 20% of the population accounts for 50.5% of all income, whereas the poorest 20% receives 4%, and the poorest 40% 13.1%. As a result, Costa Rica is no longer considered one of the most equitable countries in Latin America.

Question  
Score

Socioeconomic  
barriers

6



Poverty levels are higher in rural than urban areas (25.1% vs. 19.5% in 2018). Since over 70% of the population lives in urban areas, regional disaggregations reveal a much more negative picture for poverty in peripheral areas. For example, the Brunca

region (south Pacific, bordering Panama) has the highest poverty incidence in the country at 32.2%, almost twice the lowest poverty incidence level, which is found in the Central region, home to most of the population. The Huetar Norte (north-central, bordering Nicaragua) and Huetar Caribe (north Atlantic) have poverty levels above 27%. The Brunca and Huetar Caribe regions represent only about 16% of the national population, but they are home to the majority of the country's indigenous people. Unlike poverty, inequality for the most recent year on record (2017) is lower in rural areas (Gini of 0.489) than in urban areas (0.505). However, the highest inequality in the country is found in the central Pacific region (0.523), which is also the most sparsely populated.

While the HDI of Costa Rican women is 97.4% that of men, this mainly reflects income differentials, because females have higher life expectancy than men (82.4 vs 77.7 years), and higher educational attainment. In the UNDP's 2017 Gender Inequality Index, which measures inequality in achievements against men in reproductive health, empowerment and labor markets, Costa Rica ranks 64th and places in the medium- to high-equality achievement level, better than the Latin American average, but short of the highest category.

Economic indicators		2015	2016	2017	2018
GDP	\$ M	54776.0	57158.0	58174.6	<b>60126.0</b>
GDP growth	%	3.6	4.2	3.4	<b>2.7</b>
Inflation (CPI)	%	0.8	0.0	1.6	<b>2.2</b>
Unemployment	%	9.0	8.6	8.1	<b>8.1</b>
Foreign direct investment	% of GDP	5.4	4.6	4.9	<b>4.6</b>
Export growth	%	2.6	9.4	5.0	<b>4.1</b>
Import growth	%	4.5	8.9	3.2	<b>-0.4</b>
Current account balance	\$ M	-1921.3	-1257.3	-1718.7	<b>-1876.6</b>
Public debt	% of GDP	40.9	44.9	48.6	<b>53.6</b>
External debt	\$ M	23588.8	25562.7	25615.9	<b>27819.0</b>
Total debt service	\$ M	2767.2	2829.5	2958.6	<b>3879.6</b>

Economic indicators		2015	2016	2017	2018
Net lending/borrowing	% of GDP	-	-	-	-
Tax revenue	% of GDP	13.7	13.9	13.8	-
Government consumption	% of GDP	17.5	17.2	17.3	<b>17.0</b>
Public education spending	% of GDP	7.1	7.1	7.4	-
Public health spending	% of GDP	5.8	5.6	-	-
R&D expenditure	% of GDP	0.5	0.5	-	-
Military expenditure	% of GDP	0.0	0.0	0.0	<b>0.0</b>

Sources (as of December 2019): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

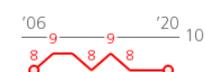
## 7 | Organization of the Market and Competition

Market competition is consistently defined and implemented at the macro and micro levels. Most prices are determined competitively, and currency is easily convertible. The freedom to enter contracts in any currency is legally protected, and there are no restraints on making and withdrawing investments. There are state-guaranteed rules for market competition meant to ensure equal opportunities for all market participants (Law 7474). Article 19 of the constitution grants foreigners the same rights and obligations extended to nationals. Foreign direct investment has been a primary factor for economic development in recent years. However, the OECD reports that foreign acquisitions of land or real estate in the coastal and frontier areas are limited, and there is an explicit preference for local suppliers in public procurement processes. Foreign suppliers can only participate in international tenders on the basis of reciprocity. Restrictions also exist in the energy sector, where petroleum refining and the transmission and distribution of electricity are state monopolies, and power generation by private parties is limited and subject to bids from the public sector. A recent OECD study estimated the cost of pricing fuels administratively instead of through market competition at 1.35% of GDP. Foreign investments are limited to 65% and 49% equity shares in electricity generation and road freight transport companies, respectively, and permits for domestic road freight traffic are only granted to nationals or local companies majority-owned by nationals.

Starting a business in Costa Rica has become much easier in recent years. The World Bank's Doing Business Report 2019 shows it takes 10 procedures, 23 days and costs 9.5% of GNI per capita. The country is ranked 142nd in the starting a business category, performing better than El Salvador (147) and Honduras (154), yet worse

Market  
organization

8



1

than Colombia (100) and Guatemala (89). According to ILO-Data, informal employment increased from 32 % in 2011 to 36 % in 2017 with an upward trend.

Laws to ensure competition are in place, and there is a National Commission for the Promotion of Competition charged with investigating and penalizing monopolistic practices. With the ratification of the Central America Free Trade Agreement and the subsequent passage of its complementary laws, the insurance and telecommunication sectors, state monopolies since 1924 and 1963, respectively, were opened to competition starting in 2008. The electricity sector was also opened partially to allow generation by private entities, but with a cap of 30% of national installed capacity (Law 7200).

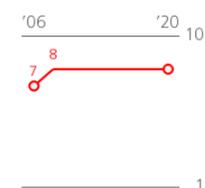
While these actions have decidedly increased market competitiveness, there are still considerable legally sanctioned monopolistic limitations. In the energy sector, electricity transmission, distribution, and export are state monopolies. While regulated by the Autoridad Reguladora de Servicios Públicos, the state energy company, Instituto Costarricense de Electricidad (ICE), has considerable sway over the strategic direction of the sector and the determination of electricity prices. A recent report by the state comptroller found that, for the past 14 years, ICE has overestimated electricity demand, obtaining investment allowances from regulators that have unnecessarily inflated electricity prices. In addition, cost overruns and delays in investment projects have resulted in some of its facilities generating electricity at costs significantly higher than international benchmarks. Private generators also depend on ICE to set contracts out to bid for half the capacity they are entitled to generate. Efforts to further liberalize the sector have not advanced.

The state also retains monopolies in alcohol distillation, the importing, refining and distribution of petroleum and its derivatives, and the operation of railroads, ports and airports. The latter have been offered in concession to private parties with some success, for example the ports of Caldera and Moín, as well as the Juan Santamaría airport. State companies retain important market shares where they previously held monopolies. The state insurance company holds about 74% of the general insurance market, where it retains a monopoly on mandatory workplace insurance, which represents about 30% of the market. Excluding the latter, the state company controls 64% of the market. It is dominant in auto (80%), life (81%) and fire (60%) insurance, but is increasingly challenged by private providers in health care, where it has been pushed to 34% of the market. State banks are also dominant and engage in oligopolistic practices. They enjoy an explicit state deposit guarantee not available to their private competitors, which allows them to control about 70% of the market for demand and savings deposits in local currency. In telecommunications, the state company has lost roughly 48% of its mobile phone market between 2010 and 2017.

Overall, competitive markets have broadened, but anti-monopoly policy remains limited by legal reserves that are unlikely to change in the short-term.

#### Competition policy

8



Costa Rica has continued liberalizing its foreign trade regime, mainly through participation in preferential trade agreements, both bilateral and multilateral, and maintaining a proactive strategy to attract foreign direct investment. The country can be considered widely liberalized with a trade-to-GDP ratio of 67.6% and an average tariff rate applied of 1.8% according to the Heritage Foundation's Index of Economic Freedom 2019. Costa Rica joined the General Agreement on Tariffs and Trade in 1990 and became a founding member of the World Trade Organization in 1994. It has been an active participant in the multilateral trade system, including the trade negotiations of the Doha round. To date, the country has signed free trade agreements with the United States, Dominican Republic and Central America, the Caribbean Community of Nations, Canada, Chile, Mexico, Panama, China, Singapore, and Colombia. It is also a party to an association agreement signed between the European Union and Central America in 2012. Costa Rica initiated accession to the Organization for Economic Cooperation and Development in April 2015. It also has observer status with the Asia-Pacific Economic Cooperation Forum, as well as the Pacific Alliance, and has invested efforts to join the Trans-Pacific Partnership. Two state entities, the Ministry of Foreign Trade and the Promoter of Foreign Trade (PROCOMER), are devoted to pursuing international trade, as is the private export promoting office CINDE.

#### Liberalization of foreign trade



The banking system is solid and governed according to international standards that include prudential supervision and capital adequacy requirements. All intermediaries must be registered with a superintendence (SUGEF) and unregulated players are now rare. At present, there are 49 supervised institutions: fifteen banks of which four are state-owned, eleven private; 24 savings and loans cooperatives; seven non-bank financial institutions, including finance companies and mutual funds; and 3 other specialized savings and loans organizations. State-owned banks are the most sizable of the banks but have been losing ground to private operators. A state bank (Crédito Agrícola de Cartago) closed in 2018 due to low profitability and solvency issues. Its assets were absorbed by another public bank (Banco de Costa Rica).

#### Banking system



There are strict disclosure rules and information on market participants is available to the public. Capital adequacy ratios have stayed around 10% for a decade, but non-performing loans are quite low (below 2%). In a 2017 analytical note, the IMF described the banking sector as sound and in good position to absorb a range of shocks, although it singled out low profitability and high exposure to foreign exchange fluctuations as vulnerabilities. About 40% of credit to the private sector is denominated in foreign currency, and over 70% of this is to unhedged borrowers.

Some 35% of bank liabilities are in foreign currency. Banking spreads in Costa Rica are twice as large as those prevailing in international markets, and this has kept local interest rates high. The average ratio of operating expenses to net revenues for Costa Rican banks is high relative to international benchmarks. The IMF associates this low level of operational efficiency to market distortions like the state guarantee granted

to deposits in state banks, which allows them to engage in oligopolistic practices, capturing up to 70% of the market for local deposits, and making interest rates higher than they would be in a more competitive context. No reforms have been proposed that would correct these inefficiencies.

There is also a development banking system in place aimed at micro-enterprises and small to medium entrepreneurs, established in 2008 and modified in 2014. It aims at providing “development loans” with lower cost and laxer collateral requirements. Its funding comes from various sources, including a 17% levy from demand deposits that private banks must transfer to state banks, and a 5% tax on profits from state-owned banks. A recent analysis reported that this system has had limited impact, with only 4.7% of its potential beneficiaries reached in ten years.

## 8 | Monetary and fiscal stability

The central bank enjoys considerable autonomy and is consistent in pursuing and communicating its plans to achieve a stable monetary policy through prudential management. The bank articulates a monetary program that is amply publicized and regularly adjusted to effectively manage expectations. Recent monetary policy has been directed toward consolidating the low inflation rates maintained since 2009, while exchange rate policy has aimed at maintaining stability in a context of market determined exchange rates through a managed band system. According to the IMF, monetary policy has succeeded in maintaining macroeconomic stability by substantially lowering inflation expectations and keeping them within the 2-4% target introduced in 2016, despite an increase of the inflation rate in 2017 from 0.77% to 2.57%.

The central bank has also been able to accommodate a decrease in net foreign exchange supply, caused by reduced external financing and a switch to dollar deposits by local investors, through a partial, non-critical loss of reserves and more intense depreciation of the currency through 2017 (though still reflecting an appreciation of about 12% compared to 2010). The latter may have contributed to raising foreign competitiveness as evidenced by the persistent strength of foreign direct investment (FDI), which has remained at about 5% of GDP for the last three years, and exports, which grew at an annual rate above 7% in 2016 and 2017. In pursuit of these policies, the central bank raised its basic interest rate from 1.75% to 5% between April of 2017 and February of 2018.

The country’s weak budgetary situation, its reliance on foreign funding and high level of dollar-denominated lending in the domestic financial system make Costa Rica vulnerable to a strengthening dollar and rising international interest rates. As a result, the central bank is expected to continue tightening monetary policy in order to contain inflationary pressures derived from higher currency devaluation.

### Monetary stability

10



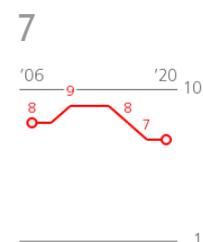
1

Government budget policies have not been conducive to fiscal stability. In 2017, Costa Rica registered its highest fiscal deficit since 1980, 6.2% of GDP, and it will remain close to that level in 2018. Public finances are on an unsustainable path as current revenues are insufficient to cover primary expenditures. This primary deficit has driven central government debt from 28% to 49% of GDP between 2010 and 2017. A continuation of this trend would take the debt to about 70% of GDP by 2021. Its correction would require fresh resources, from increased revenues or reduced expenditures, amounting to 5.1% of GDP: 3.1% to eliminate the primary deficit and 2% to stabilize the growth of public debt. Driving the increase in the deficit is the growth in government spending, which was 9.1% in 2017.

Structural factors, including generous annuities and salary supplements for public employees that rise every year and are written into law, make reductions in spending difficult. Since 2002, three different administrations tried to pass reforms, but they were stymied by opposition from various sectors. A fiscal reform package was finally approved in October 2018, despite a paralyzing strike by public sector unions. The new law converts the sales tax into a value-added tax, broadening its base, and introduces a 15% tax on capital gains. It also creates two new tranches of income tax for higher earners, changes the nature of the tax from territorial to global and increases the tax rate to be paid on earnings by cooperatives. On the expenditure side, the new law establishes a fiscal rule that contains current expenditures when the debt reaches certain thresholds and gives the executive greater discretion to manage dedicated tax revenues and restrain spending growth. It also modifies the salary supplements paid to public employees so that they will not grow automatically and will be subject to performance reviews.

The passage of the reform is a positive development, but it is insufficient to fully stabilize the country's fiscal situation. It is expected to generate 3.5% of GDP in revenue, enough to bring the country back from the brink and eliminate the primary deficit, but not to fully arrest the growth of public debt. Moody's, Standard and Poor's, and Fitch have downgraded Costa Rica's rating citing worsening debt metrics and funding challenges despite fiscal consolidation efforts. However, the new law has increased awareness of the magnitude of the fiscal problem and its fiscal rule has established an institutional safeguard that will restrain permissive spending in the future.

#### Fiscal stability



## 9 | Private Property

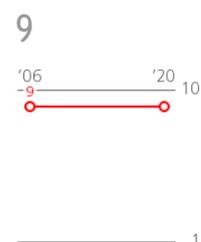
Property rights are secure, and contracts are generally upheld. Rights and regulations associated with property acquisition, benefits, use and sale are well defined and enforced. Public interest exceptions may lead to an override of these rights, but always following due process and with adequate compensation. The government maintains appropriate registries and seeks to protect the individual property rights of its citizens and foreign investors. However, foreigners face specific property limitations in that they can only acquire a state concession property by entering a minority partnership with a Costa Rican citizen unless they have resided in Costa Rica for at least five years. While rights are guaranteed by rule of law, the judicial system can be slow in resolving legal disputes, limiting their effectiveness.

Private companies are viewed as primary engines of economic production and are given appropriate legal safeguards, starting with the constitution. However, there is a long history of state involvement in the economy, which has included the preservation of legal public monopolies in several areas. The ratification of the Central American Free Trade Agreement in 2007 and the implementation of its complementary laws opened most of these areas to competition, but not through privatization. State enterprises continue to compete alongside new private companies in telecommunications, electricity generation, insurance and banking, among others. While the playing field is not entirely level and state enterprises enjoy advantages, the entrance of private competitors has contributed to market expansion, price reductions, and quality improvements. The state has also turned to private enterprises to execute and manage large infrastructure projects as concessionaires. Given the state's budgetary limitations, this is likely to remain an area of continued growth for private investors.

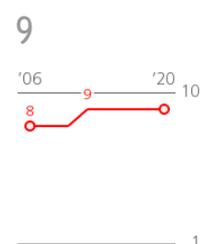
## 10 | Welfare Regime

There has been a broad and sustained effort to develop social safety nets capable of compensating for social risks and preventing poverty. Social investment by the state encompasses universal programs (health and education), contributive programs (pensions), and selective programs targeted to vulnerable segments of the population (conditional cash transfers and non-contributory pensions). Universal programs represent the largest share of public spending, accounting for a combined 24% of GDP in 2017 (6.5% in health, 7.7% in education, 7.1% in social protection, and 2.3% in housing). Health and pensions are managed by the social security organization (CCSS), which is funded mostly through tripartite payroll contributions complemented by government transfers. The coverage of universal services is high, about 74% of the economically active population in health, and 67% in pensions, with most of the remaining population covered as dependents and/or beneficiaries of

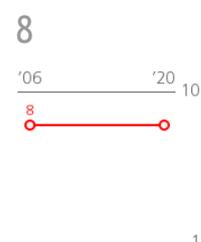
Property rights



Private enterprise



Social safety nets



selective programs. Health indicators for the population are very positive, with high life expectancy, low under-five mortality rates (8.8 per 1,000 live births) and low maternal mortality rates (25 per 100,000 live births). In 2017 total social spending increased by more than 3% in real terms relative to 2016.

Despite this, social investment has been unable to reduce poverty below the 20% level or arrest an increase in income inequality. There is no unemployment insurance, although a modification of labor laws established a severance fund that contributes to the capitalization of an individualized account that workers can tap if they lose their jobs. It is also estimated that about 25% of the most vulnerable among the population are not covered by the programs that are designed to target them. In recent years, the CCSS has faced serious administrative and financial challenges. Its hospitals have struggled to keep pace with demand for specialized treatments as chronic diseases displace infectious ones. An aging population has increased the number of dependents relative to the working population, creating funding problems. Likely reforms will require an increase of payroll contributions, a reduction of pension benefits, an increase in the minimum retirement age, or a combination of all these. In 2017, the CCSS unilaterally raised the payroll contribution of workers by one percentage point.

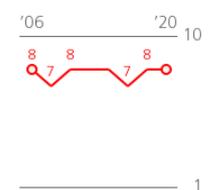
Non-citizens that hold residency status or working permits may access most social protection services, but undocumented migrants are excluded. However, undocumented migrants may receive medical attention in primary health clinics, health centers or emergency rooms. It is estimated that up to 10% of the workforce is of Nicaraguan origin and over one-third of this population is not enrolled with the CCSS. This may be due to the predominance of low-skilled occupations among Nicaraguans, where employers are less likely to fulfill their payroll obligations with the CCSS.

Costa Rican institutions strive to provide equality of opportunity, but with varying levels of success. Access to health is broad with constant quality of service across socioeconomic levels and, increasingly, over geographic areas. However, access to education, the principal source of opportunity, is still far from universal. In addition, dropout rates in Costa Rica remain high despite a conditional cash transfer program (Avancemos) aimed at neutralizing the opportunity costs of schooling for poor families. Notwithstanding, these results are not the product of insufficient investment, as Costa Rica spends more on education than OECD countries do on average (7.1% of GDP).

While women enroll at higher rates than men and have higher educational attainment, they do not enjoy equal opportunities of employment. Their workforce participation rate (43% in 2018) is 30 percentage points lower than men. The driving factor behind this difference is the larger burden of unremunerated household work that women shoulder. Female unemployment in Costa Rica is higher than male unemployment, and because they face greater difficulty securing full-time employment, women tend

Equal opportunity

8



to work fewer hours per week than men. Women also face an earnings gap relative to men that is not explained by differences in educational attainment and has ranged between 12% and 17% (2013-17).

Female representation in politics is significant. Women hold twelve out of the 24 cabinet positions (50%) in the new Alvarado administration. In the 2018 legislative elections, 45.6% of seats went to women, which is also an increase over the two previous elections (2010 and 2014) and higher than the legal mandate requiring 40% of available electoral positions to be open to women. However, only 28% of the Supreme Court magistrates are women.

The country's indigenous populations and Afro-descendants also have more restricted access to opportunities. This is evidenced by lower levels of human development in the Brunca and Huetar Caribe regions where many of them live. These regions also have poverty levels that are fourteen and eleven percentage points higher, respectively, than those of the central region.

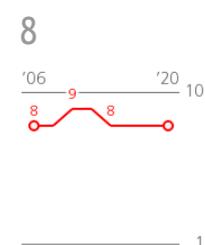
## 11 | Economic Performance

GDP growth in Costa Rica slowed down in 2017 and 2018. According central bank figures, the interannual variation for fourth quarter GDP went from 3.97% in 2016, to 3.02% in 2017, and 2.7% in 2018. According to WDI, GDP per capita growth in 2017 (2.2%) lost almost a full percentage point with regard to 2016 (3.1%). The dependence on export markets also adds volatility to GDP growth, particularly given the continued importance of agricultural exports (bananas and pineapples) and a still limited amount of diversification, with 62% of export revenues coming from twenty products in 2017. GDP per capita (PPP) amounted to \$17,044, the seventh highest in the region.

Unemployment remained above 9% in 2017, as it has over most of the past decade, and it rose to 10% during the third quarter of 2018. One of the largest challenges faced by the country has been the inability to generate dynamic job opportunities in the domestic sector. During 2017, the country experienced a net loss of over 30,000 jobs, the largest in the past twenty years. The emphasis placed on FDI has privileged skill-intensive jobs. While such jobs are well remunerated, they are not numerous. Most of the workforce therefore remains in low-productivity, low-paying sectors. The IMF has observed that the country has an abnormally high level of reliance on the service sector and that there is a lack of backward linkages in its export sector. This limits the extent to which larger portions of the workforce can be incorporated into the more modern sectors and contributes to wage inequalities by keeping skill premiums high.

Inflation increased in 2017 and 2018, though moderately, from 0.77% in 2016 to 2.57%, and 2.03%, respectively. While still within range of the central bank's

Output strength



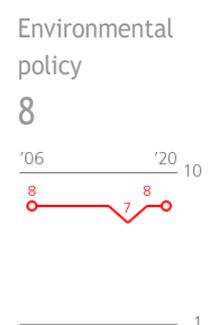
inflation targets, this higher level required a more restrictive monetary stance, which drove interest rates higher, curtailing credit and, in turn, private consumption. This was compounded by a 6% interannual devaluation of the currency by June 2017, which impacted borrowers with dollar-denominated loans. The increase in the price of the dollar resulted from greater demand for the currency driven by higher oil prices, an increase in dollar-denominated investments and a decrease in dollar-denominated loans. Low levels of consumer and business confidence also negatively impacted spending and investment. They resulted from uncertainties raised by a series of internal and external events, including the highly contested presidential election, delay in passing the fiscal reform package, the outlook for rising international interest rates, the rise in the price of oil, the prospect of a trade war between China and the United States (two key trade partners for Costa Rica) and political unrest in Nicaragua.

Despite the more challenging economic environment, the central bank was able to maintain macroeconomic stability. The approval in late 2018 of a fiscal reform package that is expected to rise up to 3.5% of GDP in new revenues over the coming years, and the end of a prolonged strike against it by public unions, which may have cost up to 0.3% in 2018 GDP growth, are positive developments that will contribute to stabilization and ease the upward pressure on interest rates. But the fiscal deficit, which came in at 6.2% of GDP in 2017 and 6% in 2018, according to the latest estimate, will remain high in spite of the reform.

## 12 | Sustainability

Costa Rica has been recognized as a leader in environmental protection and conservation. The right to a healthy and ecologically balanced environment is constitutionally established (Article 50) and subject to enforcement through special environmental courts and the Constitutional Court. More than 25% of its territory is under protected status and the country recovered more than 30% of its forest cover over the last three decades. It has also won plaudits as a leader in renewable energy. However, the country's record is more nuanced with regard to the sustainability of its extractive and economic practices.

While the country generated 99.7% of its electricity from renewable sources in 2017, electricity only accounts for a quarter of the energy resources consumed. Of the remaining energy needs, 73% are filled mostly through hydrocarbons. As a result, greenhouse gas emissions currently outpace the country's absorption capacity, despite its goal to become carbon-neutral by 2021. The transportation sector accounts for 66% of hydrocarbon consumption and 54% of carbon emissions (2015). Costa Rica has the third highest number of automotive vehicles relative to population in Latin America, with 231 units per 1,000 inhabitants, partly due to the absence of a viable system of mass public transportation. The Programa Estado de la Nación



estimates the costs of traffic congestion in the greater metropolitan area at 3.8% of GDP. Monitoring stations in key urban areas show concentration levels of particulate contaminants far exceeding World Health Organization recommendations.

Most residual waters from homes and industries flow into rivers without treatment, impacting the country's Pacific basin with high levels of contamination. There have been noteworthy improvements in the last few years as the percentage of residual waters captured in sewerage for treatment has increased from 4.2% in 2014 to 14.4% in 2017. Yet, even that improved level is still distant from the world average (60%). The use of septic tanks, which creates seepage risks to subterranean water sources, is still the predominant mechanism for water treatment. The reliance on export-based agricultural products that require intensive use of fertilizers and pesticides has had broad environmental impacts. The overexploitation of coastal and marine fisheries has set them in frank decline with some already showing signs of collapse.

According to the Global Footprint Network, Costa Rica exceeds its biologically productive land and water (biocapacity) by approximately 60% and makes up for it through trade, liquidating regional ecological assets or emitting wastes into the global commons. Still, Costa Rica ranked 30 out of 180 countries in the 2018 Environmental Performance Index (EPI), which measures the priority given by countries to environmental health and ecosystem vitality. This is a higher rank than in 2016, although the country's index score actually fell from 80 to 67.8.

Education is a key component of social policy, with preschool and general basic education (until the ninth grade) obligatory, universal, and free, and the public budget for education at all levels constitutionally mandated at a minimum of 8% of GDP (Article 78). Public education is available at all levels, including preschool and tertiary as well as technical and vocational. Adult literacy rates exceed 97% of the population and coverage at the primary level, despite some recent backsliding, is nearly universal. However, only 73% of the eligible population (ages 12-16) is enrolled at the secondary level, and dropout rates are high, ample financial support notwithstanding. While only 53% of those between ages 18 and 24 had completed high school in 2016, 61% of them continued to tertiary education. Over 75% of those starting in state universities proceed from public schools and most receive full financial support. The average number of years of schooling for the population was 8.8 in 2017. In the U.N. Education Index for 2017, Costa Rica ranks 37 out of 133 BTI countries considered and seventh in the region with a score of 0.719.

Recent administrations have increased spending in education, which approached 8% of GDP in 2017, the constitutionally mandated level. However, some indicators suggest this spending may not be entirely effective. Only 39% of the population over eighteen years of age had completed secondary education in 2017, and completion of the last grade of lower secondary general education averaged 67% between 2006 and 2016. International and domestic testing results for high school students are low. 17%

Education policy /  
R&D

7

'06 '20 10

7 6 7

1

of young persons (15-24) in 2018 were neither working nor studying, up from 14% in 2015.

Investment in research and development remains low, at around 0.47% of GDP (2016) – under 25% of the target level in developed economies – and has fallen for the past two years. The country is host to high-tech companies, many of which have invested considerably in research facilities, most notably INTEL Corp. and AD-ASTRA Rocket Company, Microsoft and Baxter Medical. Universities also engage in considerable research activities and account for about 60% of the total amount invested. To what extent this can be increased to produce greater linkages and spillovers for the economy remains unclear, although it is one of the stated goals of the country's Ministry of Science, Technology, and Telecommunications.

## Governance

### I. Level of Difficulty

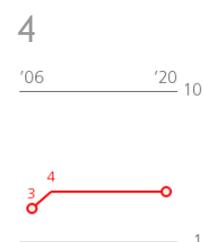
Stagnant poverty rates, rising inequality, fiscal rigidities, a fragmented and shifting party system, and a byzantine network of public institutions and regulations are the main structural constraints on governance capacity. Poverty increased by one percentage point in 2018 to 21.1%, reversing a declining trend over the past two years. The rate has fluctuated around the 20% mark, but has not breached it significantly, much less durably. At the same time, income inequality increased over the last decade and, although it seems to have peaked in 2013 with a Gini of 0.522, it has stabilized around an average Gini of 0.518, whereas in the 1990s the Gini coefficient averaged 0.472. That this has occurred despite rising social spending and sustained social safety-net policies, suggests a high level of difficulty constrains the capacity of political leaders in these areas.

A rigid spending structure beset by constitutional mandates, automatic salary increases, generous pensions, and recalcitrant public unions limit the containment of expenses. Revenues have increased through better tax collection, but one administration after another has been denied tax increases to balance the budget. Achieving such reforms has become increasingly difficult due to fragmentation and polarization of the party system.

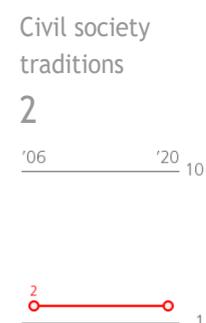
Executives arrive in power without legislative majorities and the system lacks incentives to foster coalitions capable of generating agreement. An intricate overgrown network of state institutions with multiple veto points makes transformation challenging and slow. This trickles down into other critical areas of governance, especially the development and execution of key infrastructure projects necessary to sustain economic growth, which suffer chronic delays and cost overruns or even stoppage, from permitting needs, bureaucratic requirements and legal challenges.

Mechanisms established to ensure horizontal accountability, like the comptroller's and ombudsman's offices, while necessary to avoid corruption and ensure individual rights, can make the government inoperative. Another critical area is public education. High school dropout rates and low-quality instruction, as evidenced in poor testing scores, could limit the opportunities of a significant number of young Costa Ricans, becoming a structural constraint in the future. High unemployment rates and a failure to broaden job opportunities across a wider skillset may have a similar effect.

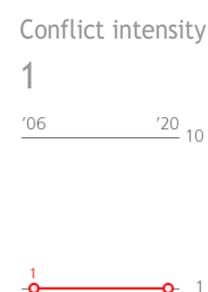
Structural  
constraints



Traditions of civil society are strong. According to Estado de la Nación there are several thousand registered civic associations, 3,704 community development associations and 594 cooperatives. Almost 300 unions represent about 14% of the workforce with an additional 16.6% represented by 1,500 solidarist associations. However, opinion polls suggest that the degree to which individuals engage with those organizations is not great. The level of self-declared interpersonal trust among citizens, an indicator of social capital, is about average when compared to other countries in the Latin American Public Opinion Project (LAPOP) and seems to be in downward trend. There is a considerable level of citizen participation that occurs outside formal organizations. About 25% of all public declarations, meetings and assemblies and public manifestations were undertaken by unaffiliated citizen groups in 2017. Citizens also actively engage through institutions like the Ombudsman's Office where an average of 25,000 requests for mediation were filed over the last three years.



There are no violent incidents based on social, ethnic or religious differences. Some contentious social and economic policy issues have generated conflict, but these have typically been resolved through institutional channels, without greater incident. There are significant levels of popular mobilization to protest policies and exert pressure for political and socioeconomic goals, although they diminished considerably during the Solís Rivera administration (2014-2018). Recent mobilizations include marches for post-material objectives, notably gender equality, animal rights, and environmental rights. The environmental category accounts for about 15% of all collective actions and involves diverse issues including water usage, coastal and marine resources, and industrial agricultural practices. While most protests target the state and often involve street blockages, police violence or repression are rare.

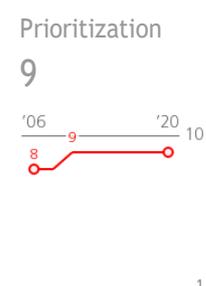


## II. Governance Performance

### 14 | Steering Capability

The executive is required by law to specify its strategic priorities in a national development plan (Plan Nacional de Desarrollo), with detailed goals and objectives for all government institutions, divided by sectors and regions. The Ministry of Economy and Planning (MIDEPLAN) is tasked with the development, execution and coordination of the plan, which articulates the executive's agenda for the four-year duration of the presidential term. There is a national evaluation system that follows the plan through its execution and the comptroller general also evaluates it periodically. The 2015 to 2018 development plan emphasized three main goals: economic growth with quality jobs; reduced poverty inequality; and fighting

Question  
Score



corruption. The government also vowed to streamline the implementation of long delayed infrastructure projects. The 2019 to 2022 development plan reasserts many of the goals of the previous administration, but with a greater emphasis on public investment. Its stated priorities are infrastructure projects to improve mobility and sustainability within urban environments; research and development to improve formal employment through innovation and competitiveness; social security to ensure the sustainability of the CCSS and its social insurance fund, while improving public health; and boosting human security by lowering poverty and guaranteeing personal safety. The plan also reaffirms the importance of macroeconomic stability and vows to control inflation, stabilize fiscal balances and arrest the growth of public debt.

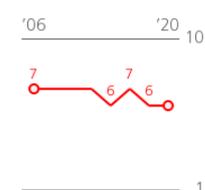
These planning documents are apt diagnostics that identify the country's main strategic challenges. They set specific goals, instrumentalized through variables with predefined, measurable indicators, and assign responsibilities for follow-up and reporting. They also describe coherent policies that, if adopted, have the potential to accomplish significant transformations that are congruent with a solid democratic and market economy. The country has sufficient organizational resources and expertise to conduct evidence-based policy-making and regulatory impact assessments, as well as strategic planning. However, this does not translate de facto into implementation. Political, bureaucratic and financial barriers can derail the best-made plans, as indeed they have.

In its National Development Plan, the Solís administration planned for faster economic growth with more and better employment. While the attained economic growth was positive, results fell short of the mark. Real growth per annum averaged 3.5%, compared to a goal of 5.25%. The expected growth in employment also failed to materialize, with unemployment ending pretty much where it started, above 8%, in June 2018. With regard to poverty and inequality, Costa Rica did not reach the stated goals either. Its effectiveness index actually showed a decreasing trend with the score merely a fourth of the desired objective. These results show that the government, by its own metrics, was not able to implement its strategic priorities.

In more general terms, the government was unable to pass reforms it considered essential – and that social sectors demanded – for managing the fiscal crisis faced by the country. On the revenue side, these reforms included the conversion of the sales tax into a value-added tax and the revamping of income taxes. On the expenditure side, they sought to limit emoluments in the public sector and cap general spending through the introduction of a fiscal responsibility rule. A variant of these reforms was eventually passed during the first year of the Alvarado administration. But the inability to advance on these grounds during the Solís administration generated severe limitations with regard to fiscal management. In its final year, the government underestimated the amount necessary to service the debt in 2018 when it submitted its budget for legislative approval. This unprecedented administrative failure pitched

Implementation

6

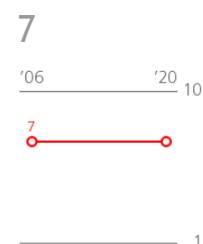


the country between defaulting on the debt or paying it without proper legal authority. The incoming Alvarado administration considered defaulting to be the greater of the two evils and made the payments, but not without considerably damaging the integrity and credibility of the rule of law. With only six months, it is too early to judge the implementation record of the new government. It can be credited with the passage of the fiscal reform law, which required assembling a coalition of different parties and overcoming strong resistance from public sector unions. Whether this coalition can survive the political pressures it will face over the following months will be crucial to attain successive reforms.

In developing policy responses, the government usually relies on best practices, international cooperation, and expert advice. An example of policy learning is the relative shift away from unfunded mandates in the bills approved by the legislature. According to the Programa Estado de la Nación, between 1990 and 2016 Congress passed 879 bills creating or extending individual rights but did not specify sources of revenue to fulfill those mandates in 51% of the cases. This trend reversed in 2015 and 2016. Among new or extended mandates, only 28% did not have a specified source of funding, the lowest level since 1990. Estado de la Nación suggests that the intense discussion generated by the country's fiscal crisis may have resulted in a heightened consciousness about the consequences of enactments that increase public spending, a clear indication of policy learning. Indeed, the fiscal reform law passed in late 2018 (Law 9635) contains provisions that give the government greater discretion in managing mandated transfers under conditions of fiscal stringency. When the government's debt rises above 50% of GDP, the finance ministry can subject transfers to its cash availability, taking into account the actual spending levels and accrued surpluses in the beneficiary institutions. The law also limits the growth rate of public spending to 85%, 75% or 65% of the average growth rate in GDP for the last four years depending on whether the ratio of public debt-to-GDP is 30% to 45%, 45% to 60% or greater than 60%, respectively.

There are sufficient institutional mechanisms in place to allow the government to replace failed policies with innovative ones, including the constant monitoring and evaluation of policies through the comptroller's office and various other supervisory agencies. For example, the comptroller published three pivotal reports in 2018 on sales tax evasion, constitutionally mandated expenses and public sector salary incentives that were vital in shaping the discussion about fiscal constraint. However, the time lag between policy enactments and evaluation is sometimes considerable, blunting the effectiveness of those mechanisms. Over time, the state has developed a highly sophisticated apparatus for generating and tracking statistical information that includes the National Institute for Statistics and the Census (INEC), the central bank, the planning ministry and others. The timely and highly reliable statistics generated by these entities provide the feedback necessary for policy learning and adjustment throughout the various parts of the state. The government also relies on the scientific output and academic expertise provided by labs and research centers at public

Policy learning

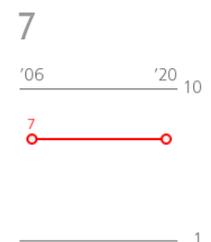


universities. A vital source of analysis for policy learning and innovation is the Programa Estado de la Nación, a research center funded by the public universities (CONARE). However, instances abound where policy failure is compounded by the inability of the state to innovate for quick replacement and adaptation. For example, rail transportation was abandoned hastily in the 1990s, and its infrastructure was left to deteriorate at great cost. It was reintroduced some years ago as an alternative for inter-urban transportation. However, rail crossings were not equipped with necessary rail guards or warning systems. Despite the predictable collisions – and loss of life and property – that have occurred over the years since, the government has only recently started to correct this situation.

## 15 | Resource Efficiency

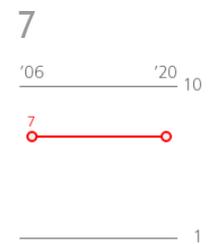
Highly complex administrative structures stand in the way of efficient government use of human and financial resources. The public sector is composed of over 300 entities of diverse juridical and functional nature. The 19 ministries of the executive are subdivided into 80 subunits with different degrees of financial and administrative autonomy. This poses great challenges for coordination, management and control. Politicians and opinion leaders have repeatedly pinpointed the need for state reform, but it has been elusive. While the country has a long-established civil service (1951), it does not encompass all public sector employees and its relative effectiveness varies across areas. In some cases, it guarantees merit-based professionalism while in others it is a source of rigidity and constraint. Given the practical impossibility of firing a civil service employee, many entities have devised ways to hire around it, creating enclaves of variant dynamism within the state. Strong public sector unions have obtained concessions over the years that have raised average levels of compensation in the public sector well above those in the private sector. These benefits include seniority clauses and other statutory recognitions, for example continued education, or exclusivity, as well as special severance packages. They are compounded by defined-benefit pension regimes for different public employees where costs far exceed individual contributions and must be paid out of the state budget. In the recent discussions surrounding the fiscal reform law (9635), the judiciary and public universities invoked their constitutional autonomy to defend these perquisites, although the Constitutional Court eventually ruled such arguments as not pertinent. Altogether, this has had a snowball effect on public spending that has seriously limited its resource efficiency. The World Bank placed Costa Rica around the sixty-second percentile in its 2017 Government Effectiveness Index.

Efficient use of assets



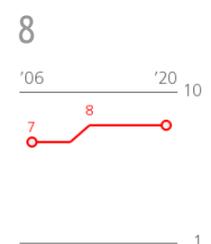
At the level of the executive, the government has the necessary tools to coordinate conflicting objectives into a coherent scheme, but the state apparatus is too unwieldy to allow for policy implementation across all issue areas. Since the Legislative Assembly does not ratify a president's ministers, he commands the loyalty of his cabinet and is at liberty to organize and coordinate it as he deems necessary. Among the mechanisms employed to ensure coordination are regular cabinet meetings (Consejo de Gobierno) where government priorities are set and discussed, the designation of special ministers to coordinate policy across sectors, and the ability to create interministerial councils. But the complexity of the public sector and its fragmentation into multiple organizations and agencies pose difficult coordination challenges that sometimes threaten the coherence of policies. A salient example is the environmental sector. Despite an increase in regulatory statutes, enforcement of environmental laws often lags due to institutional weakness and confusion among multiple organizations with overlapping jurisdictions and redundant functions. Institutional coordination has also been lacking in the areas of foreign policy, territorial planning and rural development. While there are institutional mechanisms, like the Ministry of the Presidency, designed to facilitate coordination with the legislature, loose party discipline and the emergence of competing factions within the main parties, including that of the executive, have made harmonization of objectives challenging. The executive's main tool to advance the discussion of its policy priorities is its prerogative to set the legislative agenda twice yearly during so-called extraordinary sessions. The Programa Estado de la Nación interprets the frequency with which the executive includes, and then removes, a given bill from the agenda within the same extraordinary session as a measure of relative stability. Frequent alterations of the docket indicate an unstable agenda, with bills subject to constant strategic retraction and political negotiations. This instability has increased with the level of party fragmentation in the legislature and reached its apex under the Solís administration.

#### Policy coordination



Costa Rica has laws and regulations against corruption and has ratified international treaties like the Inter-American Convention Against Corruption and the U.N. Convention Against Corruption, which commit the country to combat it. Criminal prosecution of corruption is spearheaded by the Attorney General (Fiscal General) and a special criminal investigative police force (OIJ). A special state office (Procuraduría de la Ética) functions as an anti-corruption watchdog for the public sector, and the Comptroller General exercises strict financial and administrative oversight over all public entities, approving or rejecting contracts and public bids, performing audits, and detecting instances of corruption. Most public entities also have internal auditors who closely monitor their spending. These regulators ensure the transparency of the procurement process, although they also make it cumbersome and slow, one of the factors that has encumbered the public sector's managerial capacity in areas like infrastructure.

#### Anti-corruption policy



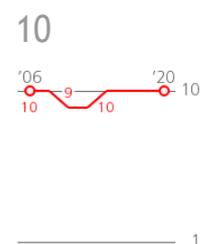
The constitution (Article 30) guarantees public access to all information pertaining to the state and its entities, and most public entities provide the media and citizenry access to their information. However, state entities have invoked state secrecy, an exception allowed by law, to deny public access to sensitive information. State-owned enterprises have also withheld information claiming the need to secrecy in order to remain competitive against the private sector. The final arbiter on the matter is the Constitutional Court. For example, in 1993, it ruled that the salaries of public officials could not be treated secretly and upheld that criterion in several challenges to the ruling. In 2016, it ruled that the state Electricity and Telecommunications Company (ICE) could treat some of its financial information with secrecy, but only where expressly permitted by law, and for a limited and reasonable period.

The criminal code establishes prison sentences of up to 10 years for public officials convicted of receiving bribes. A strict anti-corruption law was passed in 2004 in response to corruption scandals involving high-ranking officials, including three ex-presidents. It established stricter reporting requirements for public officials, including for the disclosure of personal assets and conflicts of interest. These laws, together with a vigilant and assertive media, drive officials to investigate and pursue cases of corruption. However, prosecutions are lengthy and often result in failed convictions or suspended sentences. A 2018 study by the Estado de la Nación also finds that there are substantial differences in the probity required across sectors of the public administration with regard to negligence, power abuses, recusal duties and labor loyalty. There are also differences regarding sanctions and the level of discretion allowed in their application. Such deficiencies can diminish the effectiveness of corruption prevention at the administrative level.

## 16 | Consensus-Building

All major actors agree on the goal of consolidating democracy. The country has a long-standing democratic tradition that is a source of national pride. In recent years, the level of public approval for democracy has fallen due to popular discontent with public corruption, economic performance, and political dysfunction. The Latinobarómetro survey (2017) finds that only 16% of respondents believe the country is governed in the interest of the people. However, studies show individuals highly dissatisfied concurrently with economic performance, institutional performance and representativeness, and therefore most likely to challenge democratic stability, tend to be relatively few (below 4% for 2015). Costa Rican citizens tend to question the country's exceptionalism as a peaceful, green and prosperous republic, but do not necessarily challenge these as desirable ideals. In a more general sense, dissatisfaction has taken shape in a fluid and fragmented party system that is seeking to, but has yet been unable to, reconstitute itself. Diffuse support for the democratic political system is high, though variable. Political tolerance is above the regional average, as is the number of citizens that consistently

Consensus on goals



affirm that democracy is the best system of government despite its problems. On the other hand, recent levels of satisfaction with the functioning of democracy are relatively low. This may be viewed as a healthy questioning of specific policies and administrative failures, rather than a broader questioning of democracy, that could serve as a catalyst for transformation in a mature democratic context.

All major actors agree on the goal of consolidating a market economy, although there is some disagreement regarding the extent of state involvement in economic activity. Public sector unions have traditionally contested market-based competition in certain sectors, and continue to support state monopolies where they exist, as in the energy sector. Together with political parties on the left and some sectors of public universities, they question the motives of multinational capital and the value of global insertion. However, the political consensus has resulted in a general transformation toward an increase in market-based competition, though with state companies remaining as relevant, and sometimes privileged, competitors. All major actors share a consensus that extended social protection should exist as an integral component of the market economy.

There are no anti-democratic veto actors with anti-democratic interests, such as the military or influential economic actors. Some social movements oppose reform through extra-parliamentary and sometimes contentious means, but not with anti-democratic intent.

The political leadership has prevented cleavage-based conflict from escalating by promoting dialog and respect for the country's democratic traditions. Appeals to long-standing practices of consensus-building and incremental change contribute to depolarization. The dominant emergent cleavage is between those who benefit from the socioeconomic order and those who feel excluded, as well as those who do not consider themselves adequately represented by, and are disillusioned with, existing political institutions. Sociocultural cleavages around issues of religion, environment, sexual preference and reproductive health are also increasingly salient. Political parties are no longer the sole channel for interest aggregation and political representation. They have been joined by social movements as citizens mobilize and engage in various forms of political expression to pursue specific causes and protest injustices. While contestation may in certain instances have become more conflictual, it has always remained within institutional boundaries. The state, often the object of protest, has been respectful of democratic rights and has generally refrained from repression.

Anti-democratic actors

10



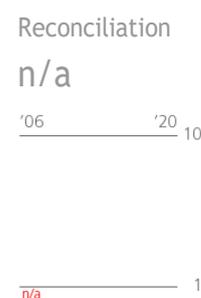
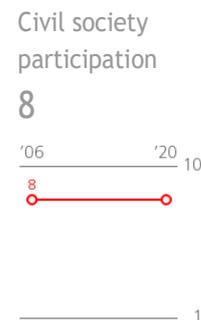
Cleavage / conflict management

9



The political leadership enables civil society participation in many areas and assigns an important role to civic leaders in policy discussions, but also shows a tendency to engage in top-down agenda setting and policy formulation. Different spaces have been created to enable the participation of civil society. When new laws are enacted or existing laws are reformed, organized representatives of sectors affected by the laws will typically be heard by legislative committees. Some government policies, like those governing minimum wages and salary increases, are defined in consultation with the organized representatives of workers and employers. There are also examples of participatory policy-making at the local level, such as the formulation of county plans for local human development, the constitution of citizen audits, and some level of participatory budgeting. Social movements are another form of civil society participation, and they take part in hundreds of marches and protests each year. Yet, low levels of citizen engagement with formal organizations, at least according to opinion polls and regional comparisons, seem to suggest that more could be done to enable civil society participation. For example, civic groups could be engaged in the assessment of the social and environmental impacts of projects in the planning and development of zoning regulations, as well as other activities at the local level. The voice of indigenous communities was for a time largely ignored by the state in its pursuit of large hydroelectric projects that impacted their territories. An intervention from the United Nations Special Rapporteur for Indigenous Rights reminded the state of its obligation under international treaties to engage those communities in a prior consultation process, and a statute regulating and establishing the procedures for such a mechanism was finally published in 2018 after a seven-year delay.

The country has not experienced major historical injustices of the type covered by this question.



## 17 | International Cooperation

The political leadership makes well-focused use of international assistance to implement its long-term development strategy. In its National Development Plan, the government recognizes the importance of international cooperation and highlights the possibility of joining new international forums, such as the OECD and Pacific Alliance, as a potential source of new opportunities in this area. The Solís administration emphasized a South-South cooperation model, centered on exchanges of information, technology, and general knowledge between countries with comparable development levels. Costa Rica has established such cooperative agreements with Mexico, Argentina, Chile, Uruguay, Peru and Colombia. As a middle-income country, Costa Rica has seen a considerable reduction in direct flows of international assistance, with the emphasis shifting away from concessionary aid to international loans. Traditionally, most cooperation has come from multilateral organizations, primarily the Inter-American Development Bank, the Central American Bank for Economic Integration, and the World Bank. More recent flows have seen an increase in bilateral cooperation, mainly from China, but also Japan, Germany, South Korea, the United States, the Netherlands, and Spain. Most of the funding from these sources is destined for four sectors: energy and environment, public works and transportation, economic and financial development, and health and social development.

Costa Rica has traditionally exerted an outsized international influence relative to its physical and economic power. It has represented Latin America as a temporary member of the United Nations Security Council on three occasions. It has also promoted international treaties and conventions in the areas of arms control, disarmament, international cooperation and environmental protection. The government pursues the promotion of human rights, peace and democracy as a matter of foreign policy. Together with trade and sustainable development, these issues dominate the agendas of its diplomatic missions abroad and in international forums. The country is in good standing with international financial institutions, although its debt ratings have been downgraded in recent months by international rating agencies due to its deteriorating fiscal position. The country is also now in compliance with a ruling from the Inter-American Court on Human Rights ordering the restoration of in-vitro fertilization procedures. More recently, the same court ordered Costa Rica to legalize same-sex marriage. The Constitutional Court threw out existing prohibitions as unconstitutional and gave the legislature eighteen months to pass a legalization statute.

Effective use of support

10



1

Credibility

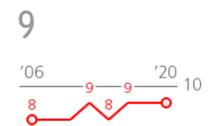
10



1

The political leadership actively and successfully builds and expands cooperative neighborly and international relations, although it has faced some challenges in recent years with its northern neighbor, Nicaragua. The country is part of the Central American Integration System (SICA) and has traditionally been an active participant, although in 2015 President Solís pulled the country out of the political mechanisms of the organization for six months, while remaining in the economic and integration system. This was to protest the unwillingness of partner members to assist with a humanitarian crisis produced when Cuban migrants en route to the United States were stranded on Costa Rican soil after Nicaragua denied them overland passage. The country is also engaged in different initiatives to build and expand cooperation with regional neighbors. It is a member of the Central American Free Trade Agreement and belongs to the Community of Latin American and Caribbean States, in which it served as president pro tempore in 2015, hosting its summit in San José. The country has also subscribed to a Cross-Border Cooperation Agreement with Panamá to facilitate binational cooperation in multiple fields. While there is no similar agreement with Nicaragua, there are a series of bilateral commissions to promote cross-border development and coordination. Regional coordination has also been advanced through the Central American Rural and Territorial Development Strategy, an initiative under SICA that establishes trans-border territories to facilitate rural development and capitalize on joint opportunities. Costa Rica does not participate in the Central American Parliament or the Central American Court. Efforts to strengthen ties with the rest of Central America have been obstructed by the incursion of Nicaraguan troops into Costa Rican territory starting in 2010. This led to disputes before the International Court of Justice in The Hague, which eventually confirmed the violation of Costa Rica's sovereign territory and ordered Nicaragua to pay an indemnification for the environmental damages caused by its dredging activities on Costa Rican soil. More recently, Costa Rica has denounced the increasing levels of authoritarianism exhibited by the Ortega regime and has exerted leadership at the Organization of American States to apply the Democratic Charter to Nicaragua, which could lead to its suspension from the multilateral body. Costa Rica is also part of the Lima Group, which has been working to find a peaceful solution to the current political, economic and humanitarian crises in Venezuela.

## Regional cooperation



1

## Strategic Outlook

For Costa Rica to maintain its significant accomplishments in the economic, social and political realms, and further deepen them in the future, it must tackle the structural limitations that increasingly threaten progress. This will require a set of administrative reforms to enhance the state's execution and implementation capabilities and a set of political reforms to improve representation, strengthen the accountability of legislators and encourage better coordination between the executive and the legislative branches.

The Costa Rican state continues to expand, adding layers of organization, producing a vast institutional structure that is difficult to coordinate and control. Correcting this should not mean gutting the state of key functions, but rather strengthening its capabilities so that it may accomplish them more rationally and expeditiously, including in key areas that are currently weak, like infrastructure, citizen security, secondary education, solid waste disposal and transportation. Effectiveness and efficiency are the main challenges in these areas, not funding. Strengthening the state while balancing fiscal revenues and expenditures is the greatest trial the country faces going forward. An important first step was the 2018 fiscal reform law, which transformed the sales tax into a value-added tax and established fiscal rules to constrain the growth of expenditures. The legislature has also taken steps to restrict lavish pensions in the public sector paid out of the state budget. Additional reforms to arrest the automatic growth of public payrolls will also be necessary.

Political reforms are also necessary to improve the quality and responsiveness of representation. Costa Rican society has become more plural, urban, and educated. This richer social context must find representation in the country's political institutions if trust in the political system is to be restored. While there are many options in terms of institutional design, there are some general objectives that should be targeted. For one, representation should be proportional to the size of the population. In Costa Rica, the number of deputies has not changed since 1961, despite a trebling of the population. For another, representatives should have incentives to build political careers in the legislature, developing a record and demonstrating their accountability to the electorate. This is currently inhibited by a ban on continuous re-election that precludes specialization and hampers learning through experience, negatively impacting the quality of representation and legislation. Finally, institutional mechanisms should foster the strengthening of political parties and facilitate the creation of legislative majorities, something the current political system does not do well.

There could also be gains from fine-tuning parliamentary procedures. Cross-national comparisons show that the Costa Rican legislature is unduly permissive on several dimensions, including the use of the floor and the submission of amendments. Together with the ability to consult the constitutionality of bills, this often leads to unduly obstructionist tactics. Reforms should aim to provide an institutional environment that, while inclusive, also fosters negotiation and consensus, thereby lessening the relevance of obstructive tactics. A more coherent legislature with improved

mechanisms for coordination with the executive would likely foster a rebalancing of power among the branches, lessening the need for judicial adjudication by the Constitutional Court.

The Alvarado administration has tried to overcome its legislative weakness by forming a “national government,” with key cabinet positions assigned to opposition parties. This strategy may foster the convergence of political forces around key reforms. But it may also create strong incentives for opposition parties to stake their own political ground, as it increases their risk of becoming undifferentiated from the governing party and its politically costly reforms. If this prolongs the political quagmire of the last two decades, the country will become more vulnerable to the kind of demagogic leadership that has emerged in other parts of the Americas, Europe and elsewhere, with its concomitant risks to democracy.