

FACING THE CRISIS IN EUROPE: REFLECTIONS ON THE CASE OF COSTA RICA

I. CRISIS IN EUROPE AND ITS EFFECT

The world economy continued its recovery in 2012, albeit at a slower pace in comparison to the two previous years. Nevertheless, developed nations made little headway in resolving fiscal imbalances and reducing high debt levels, made more acute by the measures adopted to face the world economic and financial crisis of 2008-2009, which affected economic performance. In the Eurozone, in particular, economic activity contracted once again toward late 2012. Emerging economies, for their part, which had shown a far better performance in the post-crisis period, also slowed their growth, partly due to a weak demand for imports from developed economies, which grew only 1.7% (BCCR, 2013).

With regard to the international financial markets, in 2012 their performance was marked by developments in Europe. Events, such as the capitalization of the Bankia bank in Spain and the difficulties in Greece to set up a coalition government, temporarily upset the calm reached after the efforts and initiatives proposed to improve economic and financial conditions.

In a context of meagre world economic recovery, with difficulties such as high unemployment, fiscal imbalance, and bank bailouts at global level, and in spite of Costa Rica's significant commercial and financial integration with economies that in 2012 slowed or contracted, as well as the fact that throughout the year there was uncertainty about how the economies of the country's main trading partners would evolve, domestic output grew 5.1% during this period, a rate higher than the year before. Service exports continued to grow at relatively high rates, albeit less than in 2011. Most relevant were services related to business and call centres, goods transport, and tourism. In line with a higher level of economic activity, job creation in the country increased in 2012.

TABLE 1: Latin America and Costa Rica: GDP trend and forecasts, 2009-2013
(annual GDP percentage variations)

Institutions	2009	2010	2011	2012	2013
Latin America and the Caribbean	-1.5	6.1	4.6		
- International Monetary Fund (IMF)				3.0	3.4
- Economic Commission for Latin America and the Caribbean (ECLAC)				3.0	3.5
Costa Rica	-1.0	4.7	4.2		
- International Monetary Fund (IMF)				5.0	4.2
- Economic Commission for Latin America and the Caribbean (ECLAC)				5.1	3.5

Source: IMF (2013) *World Economic Outlook. Hopes, realities, risks* (Washington, D.C., IMF)
ECLAC (2013) *Balance económico actualizado de América Latina y el Caribe 2012* (Santiago, ECLAC), April

In terms of employment, the open unemployment rate in 2012 was 7.8%, notwithstanding 44,399 jobs were created year-on-year from 2009 to 2012, whereas the labour force increased 43,494. This means that unemployment decreased from 8.4% in 2009 of the labour force in 2009 to 7.8% in 2012 according to ENAHO. In addition, 72% of the working population is directly insured, 2 points more than in 2010, nevertheless, visible underemployment remains close to 13%.

II. DIFFERENCES BETWEEN THE CURRENT SITUATION AND IN 2008¹

Contrary to what happened in 2009, when GDP contracted by 1.0%, the performance of the Costa Rican economy achieved growth rates between 4.2 and 5% in 2010-2012. Nevertheless, facing the absence of high domestic demand, the outlook could become worse should the crisis in Europe deepen, if growth comes to a halt in the USA, or if growth slows further in Costa Rica's emerging trade partner countries. Likewise, notwithstanding the announced policies to foster employment, which will be discussed later, and the growth of the economy, employment did not grow as much as expected.

2012 was marked by the expansion of export sales, highlighting the activities of enterprises subject to special regimes. Regular regime enterprises (definite), for their part, maintained relatively stable growth during the year, with the greatest sales in manufactured goods and, to a lesser extent, farming products. On the other hand, growth in domestic demand was mostly marked by rises in private consumer spending, in line with the behaviour of real available domestic income and the expansion of credit in the financial system for consumer goods. Most significant was the rise in consumption of imported goods (BCCR, 2013).

Although many macroeconomic indicators and of the labour market have shown a slight improvement, there are still concerns with regard to the domestic economic situation. Since mid-2009, the Costa Rican economy has shown significant progress in reducing inflation, as it went from having one of the highest inflation rates in Latin America in 2005 (13.8%) to be, in 2011, one of the countries with inflation below the average for the region (4.9%). Nevertheless, current conditions in 2012 posed risks and restrictions for the continuation of this process.

The greatest risk has been controlling the fiscal deficit, since its funding could have consequences not only for inflation and real activity, but also in terms of interest

rates. This outlook could become worse should the risk materialise of a slowdown of the world economy (recession in the Eurozone) and financial difficulties at global level.

Likewise, in the first quarter 2013, available foreign currency increased in Costa Rica, leading the BCCR to follow an active intervention policy to defend the lower threshold of the currency band (BCCR, 2013). This greater availability of currency was, among other causes, encouraged by short-term capital inflows, in turn attracted by high domestic interest rates (in comparison to rates outside the country) and scarce or non-existent expectations for exchange rate variations.

It is important to mention that during the past crisis, the fiscal situation and capital inflows were in a more stable situation than today, which allowed the Government to implement several public works construction projects to offset the effects of the many jobs destroyed by the crisis. Hence, should the crisis worsen, it is less likely this instrument could be applied in the present context.

In January 2009, the Government of Costa Rica announced the "Escudo Plan" to face the financial crisis by means of a series of measures intended to "offer social protection and economic stimulus for the sectors most affected by the crisis". A series of policies were announced, which included extending the coverage of the *Avancemos* programme (conditional cash transfers for secondary education); reducing the interest rate for the housing sector; reducing the price of public transport; increasing pensions under the non-contributory regime of the Social Security fund of Costa Rica (CCSS); and favourable measures in the housing sectors for low-income families.

The main assistance policy consisted in extending the *Avancemos* programme. Although this programme had not been created with the financial crisis in mind, extensions to the plan were adopted to face its effects and reduce the pressure of young people joining the labour market, in exchange for a more favourable inclusion in future. Extending the programme during the crisis was progressive, benefitting 56,125 students in 2008 and 165,749 in late 2009. The *Avancemos* programme still continues today.

In order to provide technical inter-institutional and multi-disciplinary support for local governments, and facilitate the execution of funds coming from the Solidarity Fund provided by the Government, Municipal Support Brigades were formed with the assistance of the Municipal development institute, IFAM. IFAM instructed Municipalities on how to select projects to be funded with these resources. A fixed amount of US\$ 197 thousand (100 million colones) was assigned to each of the eight District Municipality Councils (OML Costa Rica, 2011).

Greater impulse was also given to the construction of public works as a means for creating jobs. Facing the

1 On the basis of ILO-OLACD, 2013, *Impactos de la crisis mundial en el mercado laboral de Centroamérica y República Dominicana* (2009)

crisis in this sector, public works were announced to compensate, to a certain extent, the decline in the private sector. Added to this, measures were taken to increase external debt and construct public works, for a total sum of US\$ 1.439 billion. Nevertheless, these measures were applied only partially. In the current situation, it is unlikely these measures could be again implemented should there be a worsening of the impact of the international crisis.

Work by the Development Banking steering council (SBD) began in October 2008, under the purview of the Ministry of Economy, Industry, and Trade (MEIC) and the Ministry of Agriculture (MAG), to strengthen the system, giving priority to measures to support micro, small, and medium enterprise through credit and business development services. So far, US\$ 531.4 million have been invested.

Same as with housing credits, interest rates were reduced for credit to micro, small, and medium enterprises: 2% through national banks and cooperatives. Two State banks established mechanisms to refinance the debt of enterprises in arrears due to the impact of the crisis.

Likewise, the aim to renew enterprise assets was fulfilled using an Accelerated Depreciation of Assets. This measure was determined by Executive Decree, published in the *La Gaceta* official gazette in March 2009. The measure was applied by the Ministry of Finance, only from March 2009 to January 2011.

III. POSSIBLE AREAS FOR INTERVENTION

At a time of uncertainty in the international and domestic contexts, it is useful to review the labour market policy instruments that Costa Rica put into effect during the last crisis. The possibility of the crisis recurring could represent an opportunity to highlight the productive responses proposed during the last recessive episode to create decent work and employment.

In May 2012 the country agreed with the ILO on the main pillars of the national programme for decent work, which states tripartite consensus in relation to the areas for intervention. The present fiscal space in the country, as well as the unclear international economic climate, mean policy options for Costa Rica are more limited than in 2008. This notwithstanding, some options are available, such as resolving the mismatch between labour supply and demand, including areas outside the Greater Metropolitan Area to extend growth to more areas of the country. This is considering the country has already consolidated schemes in education, health, and social security, and should now look for a new social pact to reach an even higher level of development.

a) *New development poles*

Costa Rica's development strategy has focused on attracting Foreign Direct Investment (FDI), mainly in the

area of electronic components, medical equipment, and others related to technology, sectors that have shown great dynamism. This strategy has led to benefits for a group of the population, but has not trickled-down to the rest. Hence, strategies to attract investment should focus on looking for additional benefits aside from increasing payrolls. This could occur, for example, through partnerships, as was the case with robotics and electronics.

b) *Professional training and education*

Developing policies for prospection and direction of labour market demand are necessary tools to increase the match between curricular-supply and expected labour-demand. To accompany this process it is necessary to strengthen the role played by technical education in general (at technical training institutes as well as technical secondary education) to resolve bottlenecks in the growth of some sectors that have so far shown resilience to the crisis, such as the medical industry and back-office services. In this sense, the labour market continues with asymmetries between the profile of persons joining the labour market and the type of jobs created. This appears clearly when university graduation figures (many graduates in social sciences) are compared to labour-demand figures as published by CINDE (an NGO working in the area of development initiatives and attracting investment) with engineering at the top of the list.

c) *Youth employment*

The young population has been especially hit by the crisis, being the first to be laid off and also slow to recover employment. Policies for supporting young people to quickly find a job, as promised by the EMPLEATE strategy (training in high-demand careers, with financial support for studies), is a benchmark for future action. This type of policy should be consolidated, as well as others that combine education and work, such as dual training.

d) *Promoting microenterprises*

Likewise, there is space to support microenterprises by improving access to credit, since they represent only 8.6% of credit portfolios, but 47% of total employment and 30% of GDP. Another area for intervention in terms of MSME's is technical support and the simplification of procedures, both nationally and locally. The role of accompanying, access to funds (not only credit) and support for marketing. Procedures have been simplified centrally for construction permits, for example, but could be extended to health permits as well as other procedures for MSME's (one-stop-window, one-form). Arrangements could also be made for MSME's to be benefitted by public sector procurement and supplies.

e) *Decentralization and local development*

One particular challenge facing the current crisis is developing economic activities beyond the central region.

Although the latter concentrates approximately 3/5 of the population, this is not the case in terms of the poor population or workers in precarious employment, which leads to the need for more local development initiatives.

In this sense, it is necessary to devise plans to foster productive chains, developing facilities to benefit growers, for example through centres for collection and storage, or marketing services. This would be the case for secondary cities as well as rural areas.

Agreements should be sought to guide and coordinate these actions based on a shared vision for the long-term. For this purpose it is important to promote dialogue. In Costa Rica there are three national councils that have played a relevant role in the labour market: Superior

Council for Labour, National Council for Wages, and the National Council for Occupational Health. It is, nevertheless, necessary to extend the space for dialogue, for example on how to improve the relationship between education, enterprise, and workers with regard to training and research and development. Regionally it is also necessary to strengthen the space for dialogue, with the ability to reach agreements and monitor their implementation.

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