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FEATURED Q&A

How Serious Have Costa Rica's Fiscal Problems Become?

Costa Rica's finance minister, Rodrigo Chaves, recently said the government will sell state assets in order to lower its debt level. // File Photo: Costa Rican Government.

Q **Costa Rican Finance Minister Rodrigo Chaves announced this month that the government is planning to sell state-owned liquor distillery Fanal and a public bank in a bid to lower expenditures and use savings to pay down debt. The announcement came the same day as Moody's Investors Service downgraded the country's long-term issuer and senior unsecured bond ratings from B1 to B2. Standard & Poor's credit rating for Costa Rica stands at B+ with a negative outlook, the same as Fitch's latest rating. Why are ratings agencies taking a dim view of Costa Rica's finances? Are the government's plans to sell some of its assets financially significant, and what else should it do to manage the country's ballooning deficit? What factors are driving Costa Rica's growth, and what headwinds will the economy face in the period ahead?**

A **Eli Feinzaig, economic consultant and chairman of the Liberal Progressive Party (PLP):** "At 7 percent of GDP, Costa Rica's fiscal deficit exceeded the government's own projections by 0.8 percentage points in 2019, despite a 1.1 percentage-point jump in tax revenues due to the implementation of the December 2018 fiscal reform. The primary deficit jumped to 2.8 percent from 2.2 percent in 2018. Finance Minister Rodrigo Chaves' announcements lacked credibility for the same reason that the deficit ballooned: the government has shown no taste for fiscal discipline. His proposed action plan is lacking in detail. His promise to cut tax evasion in half within two years depends on a highly unlikely timetable of events, and no particulars were provided as to how that goal could be achieved. Although the minister's plan to

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The northeastern state in the past five days recorded 147 homicides, five times more than the same period last year, as a police strike entered its seventh day.

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Demonstrators Block Streets in Haitian Capital

Anti-government protesters blocked streets in Port-au-Prince a day after police demanding better working conditions attacked the army headquarters. Demonstrators want Jovenel Moïse's resignation.

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Moïse // File Photo: Haitian Government.

POLITICAL NEWS

Streets Blocked in Port-au-Prince Amid Deadly Protests

Anti-government protesters blocked key streets in the Haitian capital of Port-au-Prince on Monday, a day after police demanding better working conditions attacked the country's army headquarters, BBC News reported. President Jovenel Moïse's government called the attack "a coup attempt," and the armed forces referred to it as a "war situation." At least two people were killed during the unrest on Sunday. Protesters on Monday burned tires and used scattered bricks to barricade the roads leading to Moïse's home. They are demanding the president's resignation in the latest wave of anti-government protests that have been ongoing for months. "We are under fire by weapons of all kinds, automatic rifles, petrol bombs, tear gas," Gen. Jodel Lesage of the Haitian armed forces told local media, BBC News reported. The government called the protests "an attack on freedom and democracy." Police officers, who have been protesting for weeks, demanding a union and better pay, said they had come under attack first. Moïse last week said he would create a financial fund for relatives of police who have been killed in the line of duty, but the announcement failed to appease disgruntled officers. Following the shootout between police and soldiers on Sunday, authorities announced the cancellation of the country's carnival, due to the risk of a "bloodbath," The Guardian reported.

Homicides Soar in Brazil's Ceará State as Police Strike

Brazil's Ceará state recorded 147 homicides in the past five days, a fivefold increase from the same period last year, as a police strike entered its seventh day, according to security officials in the state, the Associated Press reported Monday. Brazilian Justice Minister Sérgio Moro and two other cabinet officials met Monday with Ceará's governor to discuss security operations. Brazil's federal government has deployed 2,500 soldiers in the state in an effort to maintain order. Military police officers in the state began striking on Feb. 18, demanding higher pay. Brazilian law bars strikes by police officers and other public employees who "provide essential services to society," the AP reported.

BUSINESS NEWS

Santander Buying Payments Platform Elavon México

Spain-based Santander Group on Monday announced that it is acquiring all shares of merchant payments platform Elavon México, a subsidiary of U.S. Bancorp, for 1.6 billion pesos ($86 million). Under the terms of the deal, Santander México will own 49 percent of the operation, and Santander Merchant Platform Solutions, a unit of Santander Group, will own 51 percent. Since 2010, Elavon México has operated Banco Santander's merchant acquiring business in Mexico. "It performed extremely well and built a strong team that will now form part of Banco Santander México," Santander Group said in a statement. The partnership has approximately 140,000 active customers, with a 16 percent market share and 250,000 card payment terminals as of December, Santander said. Also, the company handled 419 million transactions last year, a 23 percent increase from 2018. "We see excellent opportunities to continue developing the business, improve the value proposition for our customers and take advantage of economies of scale as other Santander markets connect to the platform," Héctor Grisi Checa, the executive chairman of Banco Santander México, said in a statement. Elavon CEO Jamie Walker called the deal "a mutually beneficial opportunity that will allow Santander to operate the business holistically and allow Elavon to focus investments in

NEWS BRIEFS

Chile's Piñera Calls for Calm Ahead of Expected March Protests

Chilean President Sebastián Piñera on Monday called for calm ahead of expected protests in March, Reuters reported. The month traditionally brings protests to Chile as people return from holidays and commemorate the victims of Chile's military dictatorship and International Women's Day. At least 31 people have been killed in Chile since anti-government protests began in October.

Former Guatemalan Chief Prosecutor Granted Asylum in U.S.

Thelma Aldana, Guatemala's former chief prosecutor, said Monday that she had been granted asylum in the United States in light of charges in her home country that she claims are retaliation for her anti-corruption campaign, the Associated Press reported. Aldana has been living in the United States for almost a year after a court in Guatemala rejected her candidacy in the 2019 presidential election. Another court had issued a warrant for Aldana over alleged embezzlement, which she has denied.

Mexico's Economy Ministry Says Cyberattack Affects Some Servers

Mexico's economy ministry on Monday said it had detected a cyberattack on some of its servers a day earlier, adding that it considered no sensitive information to have been compromised, Reuters reported. The ministry also said it had strengthened security measures. It was the second high-profile cyberattack on Mexico's government since November, when hackers demanded $5 million in bitcoin from state oil company Pemex, forcing it to shut down computers nationwide. The economy ministry said mostly email and archive servers had been affected.

higher growth opportunities in other markets in the United States, Canada and Europe." The transaction is expected to close within the next few weeks and is subject to regulatory approval, Elavon said, adding that the deal will not affect the company's other operations.

PDVSA Taps Army Official for Supply & Trading Unit Role

Venezuelan state oil company PDVSA has named an army lieutenant colonel as vice president of its supply and trading division in shake-up at the firm that follows an "energy emergency" declaration and U.S. sanctions on a Russian trading brokerage that helped Venezuela to export crude, Reuters reported Monday, citing two people with knowledge of the appointment. Antonio Pérez Suárez, who has no apparent industry experience, will now lead the supply and trading division. Pérez was previously head of "Productive Venezuela," a state-run distributor of locally made products, Reuters reported. He will replace Marcos Rojas, who will maintain his position as international affairs chief at PDVSA, the sources said. Rojas had assumed the supply and trading vice presidency on an interim basis in June. PDVSA last week asked several vice presidents to resign as part of a series of measures that Venezuelan President Nicolás Maduro announced with the aim of revamping the company, including the creation of a commission to rehabilitate the country's crumbling oil industry, Bloomberg News reported. The moves came one day after the United States blacklisted Rosneft Trading, a unit of Russian state oil company Rosneft, which had been serving as intermediary for Venezuelan crude exports since last year, in light of U.S. sanctions against PDVSA. The supply and trading position will likely take an important role given these developments, Reuters reported. PDVSA has not officially announced the change internally or externally, and it was not immediately clear whether the appointment was permanent or a temporary measure until Maduro's commission presents recommendations, the sources told Reuters.

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concession the state-owned liquor distillery and sell a public bank are a welcome policy change, success is not guaranteed in a highly divided congress. Furthermore, with public debt hovering near 60 percent of GDP, the government is expected to raise no more than $200 million from both transactions, barely 0.5 percent of outstanding debt. With the full impact of the tax increase on economic growth to be felt only in 2020, current expenditures growing 50 percent faster than revenues, a weak economy growing well below its full potential and unemployment (12.4 percent) at its highest in four decades, the government's plan to close the budget gap by selling relatively minor assets and tightening tax collection efforts will further erode consumer and producer confidence, which already stand near historic lows. It is precisely the opposite of what is needed at this juncture."

A **María Inés Solís, chief of the Christian Social Union Party (PUSC) faction in Costa Rica's Legislative Assembly:** "In recent days, several items of bad news roiled the Costa Rican economy. We were informed and surprised by news that the fiscal deficit was higher than what political authorities expected, reaching nearly 7 percent of GDP. Subsequently, it was announced that Moody's lowered Costa Rica's rating, from B1 with negative outlook to B2 with a stable outlook. Following those announcements, the government proposed a series of measures, including the sale of Fábrica Nacional de Licores (Fanal) and the International Bank of Costa Rica (BICSA). Although they are necessary actions, they are not enough. We must take measures that can really affect the Costa Rican economy, including a plan for structural reforms. The sale of these two institutions would only contribute 0.03 percent to GDP in the case of Fanal and 0.04 percent in the case of BICSA. It is a pity that the Alvarado administration did not decide to sell two institutions that would significantly provide resources to the state, such as the Bank of Costa Rica (BCR) or the telecommunications sector of the Costa Rican Institute of Electricity (ICE). It is also urgent for Costa Rica to pass other laws that can contribute to reducing the government deficit, such as the constitutional fiscal rule and the public employment law. It is an opportune time to start talking about state reform, one that would allow eliminating existing redundancies of state enterprises, as well as merging or closing down public entities. With the implementation of such measures, we would contribute to a cleansing of state finances."

A **Silvia Hernández, chief of the National Liberation Party (PLN) faction in Costa Rica's Legislative Assembly:** "The Finance Ministry's measures to combat the weight of debt interests and Moody's ratings downgrade have as a common denominator the adjustment process for public finances as well as doubts regarding the sufficiency and terms of that process. The downgrade comes because of doubts as to whether the reform is sufficient, and above all, whether the executive branch will be capable of carrying out the adjustment, especially when it comes to expenditures. The reform's tax component has been resolved, so the question now is whether the fiscal rule will be applied correctly, and whether it will be enough to recover sustainability of the public debt. The problem Costa Rica faces to generate credibility and confidence is not just an economic problem, but also a political one, since the state doesn't feel it is part of the necessary adjustment. This is why external actors increasingly don't get their hopes up. In the current fiscal adjustment process, doubts have arisen because of the adjustment's size and its effects on the debt, but above all, because a political calmness is perceived, as if the problem were already solved. A greater emphasis on trying to make adjustments and trying to achieve concrete results quickly is missing, as well

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as clearer results, beyond programs or plans—results aimed at reducing the primary deficit and at showing that we are handling public finances more ably. New measures seeking to reduce debt, the primary deficit and access to external financing cannot be just to save time and make the adjustment process more digestible. There is a fear that there will be no emphasis on the structural reforms needed, and that we will end up with more debt and closer to a scenario as recent and terrible as that of 2018, which was very traumatic for the country."

A **Gabriel Torres, vice president and senior credit officer at Moody's Investors Service:** "Costa Rica's main credit challenge is its high fiscal deficits, averaging more than 6 percent of GDP since 2015. These large deficits have in turn pushed debt increasingly higher, and we expect it will reach 63 percent of GDP this year. On Feb. 10, Moody's downgraded Costa Rica's sovereign rating to B2 based on these elevated deficits and deteriorating debt metrics. In 2018, the government passed a fiscal consolidation law, but we expect the adverse fiscal trends will likely continue since the reform will be gradually implemented, and the government has found it difficult to maintain fiscal discipline. Last year Costa Rica's fiscal deficit reached 7 percent of GDP. Despite an 8-percent increase in overall revenues last year, the government deficit was considerably wider than the authorities' original target, driven by increased interest costs and higher capital spending. Based on current trends, we expect debt will continue to rise, approaching 70 percent of GDP by 2022. Further fiscal reform will likely be required to bring the deficit down to levels that stabilize the debt. One-off measures, including selling government assets, can reduce the debt, but lowering the deficit will require more permanent measures. Costa Rica remains vulnerable to external shocks, but it has historically shown an ability to adapt and has even managed to create a high-tech export sector, uncommon among other countries in the region. We expect the economy to grow close to 2.5 percent in 2020, below its long-term potential but higher than in 2019."

A **Ottón Solís, Costa Rica representative at the Central American Bank for Economic Integration and former presidential candidate for the ruling Citizen's Action Party (PAC):** "Costa Rica has strong fundamentals for growth and stability. Ratings agencies do not confer weight to literacy levels or access to electricity, communication services and clean water, nor to low crime, political stability, respect for human rights and environmental sustainability, which are the factors driving Costa Rica's growth. Fortunately, private capital does. That is why foreign direct investment continues to grow, central bank foreign reserves stand at record levels, the colón currency is fully stable against the dollar, and inflation averages that of the most advanced economies. Privatizing noncore businesses and using surpluses from successful government enterprises to extinguish debt is a major and significant step toward limiting its growth. The primary deficit is under control. It would have fallen but for some once-and-for-all expenditures that required budgeting in 2019, related to the strong pruning and altogether closing of government entities. Most importantly, that deficit increased also as a result of a very welcome boost (of half of a percentage point of GDP) to infrastructure expenditure. The core of the deficit problem for Costa Rica lays on the interest payments bill. It is urgent to complement actions already undertaken and others just unveiled, with a restructuring of public debt, extending maturity and lowering interest rates. It was expected that after the painful and comprehensive revenue and expenditure reforms of 2018 that Washington multilateral banks would be forthcoming toward reshaping Costa Rican debt. That has not been the case. Therefore, the government is seeking that funding from other sources."

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