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FEATURED Q&A

Will Costa Rica's Soaring Currency Sour the Economy?

The Costa Rican colón has soared in value against the dollar over the past several years. // File Photo: Central Bank of Costa Rica.

Q Costa Rica's currency is at its strongest level against the U.S. dollar in a decade, with the colón falling to around 500 per dollar. Economists have expressed concerns about the colón's strength and its potential effects on exports and tourism. What are the main reasons behind the strength of Costa Rica's currency? How is the rising value of the currency affecting the nation's economy? What actions should Costa Rica's government and central bank take amid the currency's appreciation?

A Ottón Solís, professor at IE University in Spain and founding member of the Citizen's Action Party (PAC): "Former President Carlos Alvarado's administration promoted and implemented an effective package of public employment reforms, a fiscal rule setting tough upper limits on the growth of public expenditures and a debt consolidation program. The international financial community, starting with the IMF, recognized the high quality of these policies and supported them with new lending facilities. This, plus continuous success in the attraction of tourists and foreign investment, created the structural conditions for bringing to a halt the depreciation of the local currency. However, the central bank had different ideas. Given the openness of the Costa Rican economy, a shortcut to reducing inflation would be an appreciation of the exchange rate. The central bank proceeded accordingly, approving a sharp rise in the monetary policy rate (MPR), from less than 1 percent to above 9 percent. As expected, this generated a strong appreciation in the value of the colón (more than 30 percent). The outcome has been an overkill: inflation has become negative, its value is three

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TODAY'S NEWS

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Peru's Boluarte Replaces Six Cabinet Members

Peruvian President Dina Boluarte, who is facing an investigation into illicit enrichment and calls for her ouster, on Monday replaced six cabinet members, including the interior minister.

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ECONOMIC

World Bank Approves Loan of $750 Million for Colombia

The World Bank on Monday announced that it had approved a $750 million loan to help Colombia bolster its renewable energy sector.

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BUSINESS

Mexico's Pemex Reportedly Plans to Cut Oil Exports

Mexican state-run oil company Pemex, led by CEO Octavio Romero Oropeza, is reportedly planning to cut oil exports in order to retain more fuel ahead of the June 2 presidential election.

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Romero Oropeza // File Photo: Mexican Government.

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POLITICAL NEWS

Peru's Boluarte Replaces Ministers Amid Rolex Probe

Peruvian President Dina Boluarte on Monday replaced six of her cabinet members who abruptly resigned in a shuffle that came amid authorities targeting of Boluarte for wearing luxury Rolex watches, Reuters reported. Among the cabinet changes, Victor Torres stepped down as interior minister, a key security post that oversees the national police. "I'm leaving with my hands clean," Torres told reporters, saying that he was stepping down for "family and health issues." Torres was replaced by Walter Ortiz, who previously led the ministry's organized crime unit, Reuters reported. After Torres announced his resignation, the education and women's ministers also resigned. All three expressed support for Boluarte. Last weekend, authorities raided Boluarte's home and the presidential palace in search of evidence amid allegations of illicit enrichment against Boluarte, who was seen in public wearing luxury Rolex watches. One watch she was seen wearing is worth as much as $14,000 in Peru, where the president currently earns a monthly salary of $4,200, the Associated Press reported. Boluarte has denied wrongdoing. Late on Monday, the president announced three other cabinet changes, saying the production, trade and agriculture ministers were also resigning, Reuters reported. The cabinet shake-up came after lawmakers lodged a request in the wake of the raids to remove Boluarte from office for "permanent moral incapacity," the AP reported. The declaration has been used several times in efforts to dismiss other Peruvian presidents in recent years. Lawmakers from various parties, including the Perú Libre party to which Boluarte previously belonged, submitted the request for her ouster. Removing Boluarte from office would require 87 votes in the 130-seat unicameral Congress. So far, five parties that collectively have 54 seats in Congress have voiced support for the president following the raids.

ECONOMIC NEWS

Mexico's Remittances Total $4.51 Billion in February

Mexico received $4.51 billion in remittances in February, which marked an annual increase of 3.8 percent in the money transfers, El Financiero reported Monday, citing data from Mexico's central bank. The growth in remittances in February was the largest in four months, but analysts said the of the transfers could slow. "The moderation of the activity profile in the United States and the high remittance base should lead to a moderation in flows to Mexico in the coming quarters," said Alberto Ramos, the managing director and head of Latin America economic research at Goldman Sachs, the newspaper reported. For 2023, Mexico's remittances totaled $63.3 billion, a 7.6 increase as compared to 2022, Mexico News Daily reported, citing the central bank.

BUSINESS NEWS

Mexico's Pemex Reportedly Plans to Cut Crude Exports

Mexican state-run oil firm Pemex is planning to cut crude oil exports to the global market in order to retain more domestic gasoline and diesel ahead of the June 2 general elections, sources with knowledge of the matter told Bloomberg News in an article published Monday. Pemex has canceled contracts for supplying refineries in Europe, Asia and the United States with its Maya crude oil, according to the sources, Bloomberg News reported. The plans come at a time when oil prices have reached a six-month high and, given that OPEC and other allied oil-producing nations are already lowering their own oil exportation levels, Pemex's decision could result in driving oil prices even higher. Oil exported from Venezu-

NEWS BRIEFS

World Bank OKs $750 Mn Loan for Colombia's Renewable Energy Sector

The World Bank on Monday announced it approved a $750 million loan for Colombia, to help the Andean country boost its renewable energy sector, cut carbon emissions and improve climate change resiliency, Reuters reported. The loan will help finance improvements to electric urban transport and multimodal transport as well as development of green hydrogen, solar plants and offshore wind energy. This loan comes after a $1 billion loan from the World Bank to Colombia in December 2022, which also focused on climate change.

Venezuela's PDVSA Announces New Drilling With Chevron Venture

Venezuelan state-run oil firm PDVSA announced Monday that its joint venture with U.S.-based oil giant Chevron, a project called Petroindependencia, has begun a new drilling campaign, Reuters reported. The United States relaxed sanctions on Venezuela's oil industry last year, allowing PDVSA six months of new partnerships. The United States could reimpose sanctions this month following the Venezuelan government's moves against opponents.

Crédit Agricole Unit Taps Coeurderoy as Senior Country Officer for Brazil

Crédit Agricole Corporate and Investment Bank on Monday named Giliane Coeurderoy as its senior country officer for Brazil. Coeurderoy will be based in São Paulo and will join the bank's Americas Management Committee, the France-based organization said in a statement. Coeurderoy joined Crédit Agricole Corporate and Investment Bank in 2010 and most recently served as deputy chief executive officer of Crédit Agricole Italia.

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ela is also likely to decline due to the possible snapback of U.S. sanctions on Venezuela's oil industry amid President Nicolás Maduro's moves against the opposition after he agreed to hold free and fair elections, an agreement that led the United States to loosen sanctions last October. JPMorgan Chase predicted last week that oil prices this year could rise to as much as $100 a barrel, Bloomberg News reported. Pemex's decision, according to the sources, is an attempt to prove the success of Mexican President Andrés Manuel López Obrador's promise to boost the nation's refining sector and reduce the need to import fuel, Bloomberg News reported. The six refineries in operation in Mexico were producing at their highest levels in more than six months during February. That trend is likely to rise, as Pemex begins operation of the new Olmeca refinery, which can process 340,000 barrels of crude oil a day, Bloomberg News reported. [Editor's note: See related **Q&A** in the Jan. 26 issue of the Dialogue's weekly Energy Advisor.]

Grupo Coppel Unveils $726 Million Investment Plan

Mexican lender and retailer Grupo Coppel said Monday in a statement that it plans to invest more than 12 billion pesos ($726 million) to reduce its environmental footprint and also remodel and open new stores, Reuters reported. The company, which is owned by the Coppel family, plans to open 100 new stores in Mexico, where it already has 1,782 locations, the company said. It added that the investments will also create 8,000 new jobs. Grupo Coppel also said that it will invest an additional 6 billion pesos over the next three years in order to enhance its digital services. The company said that by the end of this year, more than 700 of its stores will have solar panels, offsetting carbon emissions by some 33,000 metric tons, Reuters reported. Grupo Coppel owns a bank and department stores and currently employs more than 120,000 people. In 2018, it indefinitely postponed an initial public offering expected to be worth more than $1 billion.

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percentage points below the inferior value of the target band. This has kept real interest rates very high despite recent reductions in the MPR. Therefore, exporters, producers of goods for the local market that compete with imports and the tourist sector are enduring the double negative impact of high real interest rates and a strong appreciation of the real exchange rate. A prompt and strong reduction of the MPR to no more than 3 percent is the call for the central bank. The government, for its part, should proceed to prepay its more expensive foreign debt so as to get some dollars out of the economy."

Pablo Duncan, senior director of CLC Communications and Public Affairs: "The recent strength of the Costa Rican colón against the U.S. dollar can be attributed to fundamental factors. First, the country has maintained a solid track record of economic growth driven by its focus on exports of services and manufactured goods. This growth model has been supported by stable and robust foreign direct investment flows, a high level of human capital and strong institutions. The country also achieved significant fiscal consolidation in recent years, improving its financial position and maintaining a low sovereign risk premium. However, the appreciation is seriously affecting the competitiveness of local businesses in international markets. The transition to an inflation-targeting system with exchange rate flexibility is a step forward, but it faces challenges, especially concerning the de facto dollarization of the Costa Rican economy. This monetary duality complicates monetary policy decisions. The high dependence on the dollar and the return gaps between currencies present complex dilemmas, such as the need to balance the stability of the local currency with the need to maintain the competitiveness of exports. To address these challenges, the central bank could consider taking measures to effectively manage the colón's appreciation. This could include intervening in the foreign exchange market to moderate the currency's strength, fiscal and monetary policies that support the competitiveness of exports and the tourism sector, and close monitoring of inflation rates and adjustments to monetary policy. These actions could help address the country's long-term structural and social challenges while maintaining a stable and favorable macroeconomic environment for sustainable growth."

Francisco Chacón, former Costa Rican congressman for the opposition National Liberation Party (PLN) and former minister of communications: "The mismanagement of the exchange rate is perhaps the strongest criticism of the Chaves government in economic matters. Protests initially came from the export and tourism sectors, due to the effect it has had on their competitiveness, by increasing costs and reducing profits. Later, multiple voices from sectors competing locally with cheap imports have joined in. The government is accused of interfering with the independence of the central bank and of manipulating the exchange rate to keep it artificially low, benefiting from the impact it has on the public debt and the thresholds required by the 'fiscal rule.' Those actions would allow an increase in public spending in the last months of the government's term. For its part, the central bank argues that its policy is neutral and that the effects are due to the amount of dollars that are entering the country—mainly due to excessive foreign public debt, but also due to investment flows, tourism, exports and illegal activities. The signals that the government has sent so far are discouraging, to say the least, following some very unfortunate statements by Vice President Brunner. Although the room for maneuvering is limited, the use of the resources coming from the approved indebtedness should be rationalized, and interest rates should be reduced more aggressively. Not only is this

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possible, given that inflation is under control, but it would provide much-needed relief for the productive sector. Certainly, a much clearer message from the government and the central bank is indispensable to guide the expectations of economic agents."

Lucas Perelló, assistant professor of political science at Marist College: "President Rodrigo Chaves, a former World Bank employee who briefly served as Costa Rica's finance minister, claims that the strong Costa Rican colón is a 'symptom of the success of the Costa Rican economy.' There is some truth to that statement. The colón's appreciation reflects an influx of dollars into the Central American country. Three factors have contributed to this outcome: 1.) Record-breaking levels of foreign direct investment, led predominantly by U.S. capital; 2.) An expansion of Costa Rican exports, which grew 15.3 percent in 2023; and 3.) The continued development of the tourism industry. Until now, the currency's appreciation has run parallel to economic growth. According to the IMF, real GDP growth averaged 4.4 percent in the last two years, and the inflation rate dropped to pre-pandemic levels. But the good times are not meant to last. Although the central bank's dollar reserves have reached their highest point in seven years, and government gross debt is declining, economic growth will drop to 3.2 percent this year. Furthermore, there are signs that the cheaper dollar is starting to hurt the tourism and export sectors—two engines of economic growth for Costa Rica—which have called upon the central bank to take action. The central bank, led by Róger Madrigal, already cut the policy interest rate by 50 basis points in March, to 5.25 percent. We should expect additional cuts throughout 2024 as inflation remains low and the economy continues cooling down."

> **"The colón's appreciation reflects an influx of dollars into the Central American country."**
>
> **— Lucas Perelló**

Carlos Denton, president of the board at CID/Gallup in Costa Rica: "Costa Rica's currency, the colón, has appreciated approximately 7 percent against the dollar since early 2022. The result has been that imports are cheaper than they were then and exporters, who like most of the world trade in U.S. dollars, are getting less for their products and services. Negative inflation has been present for more than a year. The question that many are posing is 'how can a country with a sovereign debt of more than 62 percent of its GDP have such a strong currency? The country has an especially large and expensive public sector. Costa Rica has faced an insurmountable deficit since 2012 and went on a borrowing spree. Much of the money borrowed went to current expenses rather that to investment and what flowed in (Costa Rica has an excellent reputation as a democratic haven and a tourist paradise) was converted to colóns on the open market. There were many more dollars than there were takers, and the result was that the national currency appreciated. The central bank has done little to slow the process. In June, roughly $400 million of the foreign debt comes due, and the government intends to pay down (not roll over) a substantial portion of this. Buying cheap dollars has helped greatly in the process of accumulating what is needed."

The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta.

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