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¿Es posible construir la social-democracia en la era global? Reflexiones a partir del caso de Costa Rica.

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¿Es posible construir la social-democracia en la era global?
Reflexiones a partir del caso de Costa Rica[1]

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Resumen en español

El enfoque sobre variedades de capitalismo reconoce de forma implícita o explícita las características positivas del modelo social-demócrata del Norte de Europa—incluyendo la combinación de crecimiento económico y equidad. En la periferia, sin embargo, ha habido muy pocos países capaces de desarrollar un modelo social-demócrata exitoso. Costa Rica ha sido una de las excepciones ya que después de la Segunda Guerra Mundial fue capaz de mantener a la vez políticas sociales universales, un modelo dinámico de crecimiento y una distribución de la renta relativamente equitativa. ¿Hasta qué punto ha mantenido el país ese tipo de modelo durante las últimas dos décadas? ¿Es posible mantener alto crecimiento y equidad en la época global? Esta ponencia escrita en idioma inglés trata de contestar a estas preguntas a través de un análisis detallado de las interrelaciones entre producción y distribución y una evaluación de los resultados del modelo. Mi principal argumento es que la consolidación de una estructura económica cada vez más heterogénea ha erosionado las bases del modelo socialdemócrata, reduciendo las posibilidades de una distribución más equitativa y dificultando la creación de consensos entre distintos actores sociales. La ponencia concluye con una serie de reflexiones sobre la evolución del modelo de capitalismo latinoamericano y sobre la posibilidad de reconducir este a una senda más progresista en la época de globalización post-crisis.

NOTA: documento en inglés en elaboración. Por favor, no citar sin permiso del autor.

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1. Introduction

Costa Rica's development trajectory has commonly been used as a model in Latin America. Considered one of the most progressive and democratic countries in the region, it has traditionally been characterized as a successful case of economic growth with equity. Sandbrook et al (2007, 9), for example, include it within a sample of four "social-democratic pioneers", which have achieved "exemplary socioeconomic development." Most of the literature emphasizes its unique characteristics and also use it to question the existence of a common Latin American variety of capitalism (Sanchez-Ancochea, 2009).

More recently, Costa Rica has been used as an example of the positive effects that globalization can have on the process of development. UNCTAD (2002) considers Costa Rica as one of the successful examples of creation of new comparative advantages through the selective promotion of foreign direct investment (FDI). A background paper for UNDP's *2001 Human Development Report* argued that "over the last decade Costa Rica has experienced a tremendous leap forward in the development of a technology and knowledge-driven economy" (Rodriguez Clare, 2001, 1), insisting on the importance of Intel in the process of technological upgrading.

While recognizing Costa Rica´s unique achievements in the last six decades, this paper aims to offer a more nuance view of the country´s *recent* trajectory. During the period 1950-80, the golden age of Costa Rica´s social-democracy, the economy grew rapidly, the fruits of development were relatively well distributed and the welfare state expanded at an impressive speed. Yet in the 1980s, Costa Rica undertook a slow modification of its economic model. Trade liberalization, financial deregulation, a slow-down in the growth of the public sector and extensive promotion of FDI and exports resulted in a more diversified and dynamic insertion in the global economy. At the same time, however, the new model has created significant tensions and problems: inequality and economic duality have increased significantly and social tensions around the nature of the economic model have intensified. It has thus become impossible to combine the best of both periods and sustain a process of equitable economic growth supported by a broad social coalition—a lesson that should inform broader discussions about the nature of Latin America´s variety of capitalism and its likely change in the long run.

The paper is divided in five sections. Section 2 discusses Costa Rica´s long term performance and identifies the main characteristics of the pre- and post-1980 economic models. Section 3 describes the evolution of the social-democratic model and explains its main successes and few shortcomings. Section 4 shows the devastating effect that the debt crisis of the early 1980s had in Costa Rica and the initial steps that the Costa Rican government took towards a more neoliberal model. Section 5 presents a discussion of the central features of the neoliberal model and reviews its contradictory record. The paper concludes with some reflections on Latin America´s variety of capitalism in light of the Costa Rican contradictory evolution.

1. Costa Rica's long term evolution: two different stages

Costa Rica´s success in promoting human development since the 1950s is particularly clear when one compares it to the rest of Latin America. Table 1 presents the evolution of human development index (HDI) in Costa Rica and the rest of Latin America for the period 1975-2005. Costa Rica has been among the four countries with higher HDI in the region during the whole period, outperforming larger countries like Brazil, Mexico and Colombia. As discussed with more detail in other chapters, Costa Rica has been particularly successful in increasing life expectancy and educational attainments rapidly in the last five decades—both trends that reflect the general equitable nature of the Costa Rican model.

Table 1. Latin America. Ranking and trends in the human development index (HDI), 1975-2005

HDI Rank 1975	HDI Rank 2005	Country	1975	1980	1990	1995	2000	2005	Total growth 75-05
24	38	Argentina	0.79	0.80	0.81	0.84	0.86	0.87	10.00
37	40	Chile	0.71	0.74	0.79	0.82	0.85	0.87	22.46
28	46	Uruguay	0.76	0.78	0.81	0.82	0.84	0.85	11.81
30	48	Costa Rica	0.75	0.77	0.79	0.81	0.83	0.85	13.40
38	52	Mexico	0.69	0.74	0.77	0.79	0.81	0.83	19.45
35	62	Panama	0.72	0.74	0.75	0.78	0.80	0.81	13.09
46	70	Brazil	0.65	0.69	0.72	0.75	0.79	0.80	23.27
34	74	Venezuela	0.72	0.74	0.76	0.77	0.78	0.79	9.54
43	75	Colombia	0.66	0.69	0.73	0.75	0.77	0.79	19.31
49	79	DR	0.63	0.66	0.70	0.72	0.76	0.78	24.04
47	87	Peru	0.65	0.68	0.71	0.74	0.76	0.77	19.47
48	89	Ecuador	0.64	0.68	0.71	0.73	..	0.77	21.38
41	95	Paraguay	0.67	0.70	0.72	0.74	0.75	0.76	13.19
54	103	El Salvador	0.60	0.59	0.65	0.69	0.72	0.74	23.53
56	110	Nicaragua	0.58	0.59	0.61	0.64	0.67	0.71	21.78
61	115	Honduras	0.53	0.58	0.63	0.65	0.67	0.70	32.58
64	117	Bolivia	0.52	0.55	0.61	0.64	0.68	0.70	33.91
65	118	Guatemala	0.51	0.55	0.59	0.63	0.67	0.69	34.05
27	21	Hong Kong	0.76	0.80	0.87	0.89	0.92	0.94	22.80
33	25	Singapore	0.73	0.76	0.83	0.87	..	0.92	26.47
36	26	Korea	0.71	0.75	0.83	0.86	0.89	0.92	29.17

Source: own elaboration with data from UNDP (2006)

Advances in the HDI have been accompanied by a rapid expansion of the economy. Real gross domestic product (GDP) in local currency increased at an average rate of 5% between 1950 and 2007 and it was below 2.5% only in the 1980s (table 2). This helped the country to improve its income per capita levels faster than both the Latin America and the world average. Its GDP per capita in real US dollars of 2000 (which was 4,973 in 2007) increased from 87% of the Latin American average in 1950 to a

110% in 2006. The country also converged towards the world average in that same period, although at a much lower speed (figure 1).

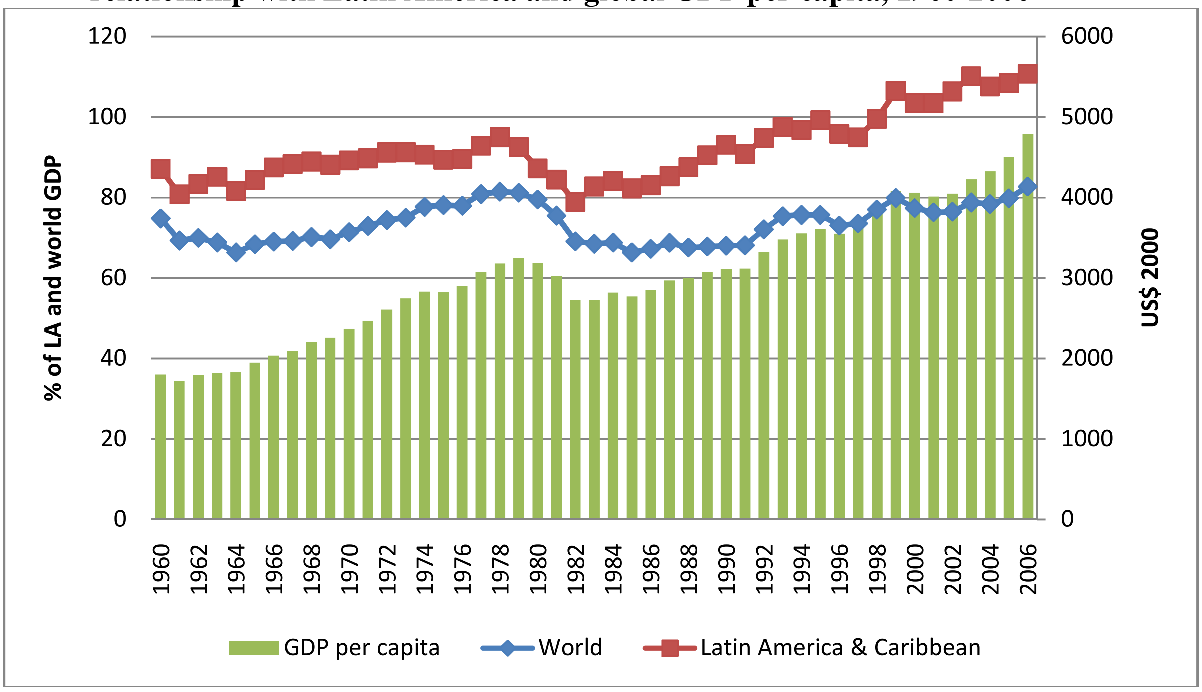
Table 2. Costa Rica. Gross domestic product in real colones of 1966, annual average rate of growth, 1951-2007

	Annual average	Variance
1951-1960	5.75	5.14
1961-1970	6.05	3.06
1971-1980	5.64	2.58
1981-1990	2.41	5.07
1991-2000	5.20	2.99
2001-2007	4.78	2.70
1951-1980	5.82	3.63
1950-2007	5.03	3.71

Source: own calculations from Costa Rica en cifras and Central Bank's webpage

NOTE: I have used based numbers to link the series with 1966 prices and the more recent series with 1991 prices

Figure 1. Costa Rica in comparative perspective. GDP per capita (US$ of 2000) and relationship with Latin America and global GDP per capita, 1960-2006



Source: own elaboration with data from the World Bank (2008)

Behind these positive long term trend, however, hides a more complex and, in many ways, worrisome reality. While the period 1950-1978 was one of rapid social and institutional advances that resulted in the consolidation of a social-democratic model, the last three decades have been more problematic. The external shocks of the late 1970s affected Costa Rica even more than other Latin American countries, with the ratio of GDPs per capita going from 94% in 1978 to 84% in 1982. Successive governments responded to the crisis by promoting a new economic model that aimed to reduce the involvement of the state in the economy and aggressively promote non-traditional exports.

It may thus be useful to distinguish two different models in Costa Rica's trajectory in the last sixty years: the first one we will call here the "Golden Age"—echoing a similar terminology used for developed countries (Glyn et al, 1992), while the second one can be defined as one of neoliberal adaptation. Table 3 summarises the differences between these two economic models that will be discussed with detail in the rest of the paper.

Table 3. Costa Rica's two models of development and its characteristics, 1950-2008

Key dimensions	Golden Age 1950-1980	Neoliberal Globalization 1980-2008
Key sectors	Agriculture and manufactures for the the domestic market	Export processing zones, new Services
Key social coalition	Encompassing social coalition with medium and large capitalists, cooperatives and, increasingly, trade unions in the public sector	Unstable coalition dominated by large domestic firms linked to transnational corporations (TNCs)s
Role of the state	Large, concentrated in increasing social services and actively promoting structural change	Small reduction. It remains active in social spending and concentrates on promoting the export sector through tax incentives
External insertion	Traditional (based on coffee, banana and other primary goods)	Development of manufacturing exports in the export processing zones and growth of service exports
Economic growth	High with convergence	High with slower convergence
Poverty	Significant reduction of poverty, Particularly in the 1970s	Poverty increases in the 1980s and is followed by some hysteresis
Income distribution	Relatively equal with an extended	Increasingly unequal with a more

	middle class	heterogeneous middle class than in the past

Source: own elaboration

2. The Golden Age of Costa Rican social-democracy

During the three decades between 1950 and 1980, Costa Rica moved towards the creation of a social-democratic model of development. The public sector played a central role in promoting new economic sectors and, more importantly, supporting a sustained expansion of health and education. The nationalization of the banking system and the creation of a civil service after the Civil War of 1949 were particularly important in strengthening the state and diversifying the access to finance. At the same time, the political dominance of the social-democratic National Liberation Party (‘Partido de Liberacion Nacional’, PLN) supported the rapid expansion of the public sector, particularly in its social dimensions, and the active promotion of new economic sectors.

The result of the model was rapid growth, which benefited workers through higher wages, and sustained improvement of human development indicators. Yet the economic model was unable to significantly transformed Costa Rica’s comparative advantages in primary goods and showed its economic limitations during the 1970s.

The origins: liberal attempts to open up the system in the 1940s

During the 1940s, the Conservative government of Rafael Angel Calderón Guardia introduced important social reforms influenced by the social doctrine of the Catholic Church. In 1940 the University of Costa Rica (UCR) was created with the aim of developing both undergraduate education and research. The UCR would later become a central networking institution, where the political, intellectual and bureaucratic elite of the post-Civil War era spent their formation years and interrelated with each other. In 1941 the Calderon Administration founded a social security system, the “Caja Costarricense del Seguro Social”. The system was financed by forced monthly contributions from the state, employers and workers and provided health and maternity care, old age pensions and death benefits (Rottenberg, 1993).

Calderon’s reforms generated significant polarization in the Costa Rican economy. The Communist Party (‘Partido Vanguardia Popular’), which was by then a reformist party, provided Calderon with much needed support. The alliance between the government and the Communists resulted in the incorporation in 1942 of a chapter on social guarantees in the Constitution, which established workers’ rights such as a minimum wage, an eight-hour working day and the right to strike. Social reform was further enhanced in 1943 when a new Labor Code was approved.

The alliance between the government and the communist, which extended to the administration of Teodoro Picado (1944-1948), was different segments of the elite and the middle classes. The traditional agro-exporting elite and a large segment of the importers wanted to maintain the traditional status quo; A new group of social democrat intellectuals and professionals, who believed in the modernization of Costa Rica through industrialization, also opposed Calderón and Picado. This group was inherently anticommunist and was dissatisfied with the increasing influence that the communists had in the government.

A critical juncture: the Civil War and the creation of a new institutional structure
Disagreement over the result of the 1948 presidential election was the final element that triggered a short Civil War, which brought face to face an alliance of Caldenronistas and Communists and the social-democratic-oligarchy one. The Civil War finished in less than two months with an agreement between all participating forces and with the Social-democratic Party led by Jose Figueres as the clear winner. While the Communist Party was banned, Figueres was appointed to preside a provisional government aimed at stabilizing the country. The Provisional Government (the "Junta Fundadora de la Segunda Republica"), which held power between May 1948 and November 1949, used this opportunity to implement some measures that partly determined the subsequent social-democratic path of the Costa Rican development model:

1. The nationalization of the banking system, which was implemented to democratize the access to credit and promote new sectors and new firms, limited the economic power of the financial class (which had close ties with the coffee sector) and increased the influence of the state on the allocation patterns.
   The importance of this measure, which was enthusiastically supported by trade unions and university professors and students, cannot be underestimated. Although credit allocation did not change as dramatically as it could have been expected (see below), the nationalization gave access to resources for investment to new segments of the Costa Rican population. It also took a profitable source of accumulation away from traditional capital.
2. A 10% tax on capital assets and a negotiated 15% tax on profits to the United Fruit Company, which dominated banana production and exports in Costa Rica at that time (Rovira, 2000).
3. A new wage policy oriented towards wage expansion. Figueres was personally committed to maintaining significant increases of real wages in order to improve workers' living standards and deepen the domestic market. In June of 1948 he established an increase in nominal wages for workers in the coffee and sugar sectors (10%) and for many public servants. He also created the National Wage Council where representatives of trade unions, employer associations and the state, which has set minimum wages in all sectors of the economy ever since.
4. The nationalization of the Institute for the Defense of Coffee and the creation of the ICE. The Institute for the Defense of Coffee was renamed "Oficina del Café" (Coffee Office) and received the task of setting the price that the "beneficios" had to pay small coffee growers. The ICE was created to assure electricity production and soon became a key element in the new development model of the country.
5. The elimination of the army on December 1, 1948, which free significant public resourced to social priorities like health and education.

All of these elements, together with the approval of a new Constitution, constituted building blocks for the consolidation of the new economic model in Costa Rica. The new model was characterized by three elements, (1) An increasingly diversified economic structure in which industrial promotion within the Central American Common Market played a central role; (2) Active efforts were developed to create business opportunities to more Costa Ricans and to reduce the observed tendencies towards concentration of capital; and (3) Expansion of the role and size of the state leading towards the consolidation of the urban middle class, which gained significant political influence during this period and demanded higher public spending in health, education and other social services. I will review each of them in the rest of this section.

Import substitution and the Central American Common Market

As in most other countries in Latin America, import substitution industrialization slowly became the dominant policy model in the post-war era. Nevertheless, during the 1950s, when the old rural oligarchy was still strong, the public sector did not concentrate its attention in the industrial sector. In fact, successive administrations rejected several proposals of the Chamber of Industries (in 1953 and 1955) to pass legislation in favor of fiscal incentives for domestic industries.

Instead the state focused on the diversification of the agricultural sector and, particularly, on the modernization of coffee production. In 1957 more than one third of total credit still went to the agricultural sector and basic grains such as beans, rice or corn were promoted through the Consejo Nacional de Producción (National Production Board) (Brenes, 1990). Coffee received 50% of total credit to the primary sector, and benefited from public support for the use of fertilizers, the introduction of better coffee plants (as mentioned in section 2) and the development of new techniques (Rovira, 2000).

Policy concentration in agriculture resulted in significant diversification. According to data collected by Bulmer-Thomas (1987) real value added in the primary sector oriented to the domestic market (measured in 1970 prices) more than doubled between 1950 and 1960 while export agriculture grew by 10%.[2] In 1960 the country was producing significant amounts of basic grains, sugar, milk and cattle, in addition to coffee and banana. Nevertheless, the weight of the primary sector in the overall economy decreased substantially during the 50s, which can be partly explained by significant improvements in productivity. Coffee yields measured in kilos per hectare, for example, experienced a dramatic expansion from 373 in 1950 to 801 at the beginning of the 1970s (cited in Bulmer-Thomas, 1987).

The approval of the Industrial Protection Law ('Ley de Protección Industrial') in 1959 shifted the focus of economic policy towards the promotion of the industrial sector. The Law (number 2426) established incentives such as a tax that increased by 300% the tariffs levied on those imports that competed with domestic production; an 99% exemption on import duties of machinery, motors, raw materials and intermediate inputs required to produce manufacturing goods in Costa Rica; and tax exemption on local taxes (for a period defined by the municipality), taxes on capital and profits (100% exemption during the first half of the period agreed between the government and the company, 50% during the second half), export taxes and taxes on those profits that were reinvested.

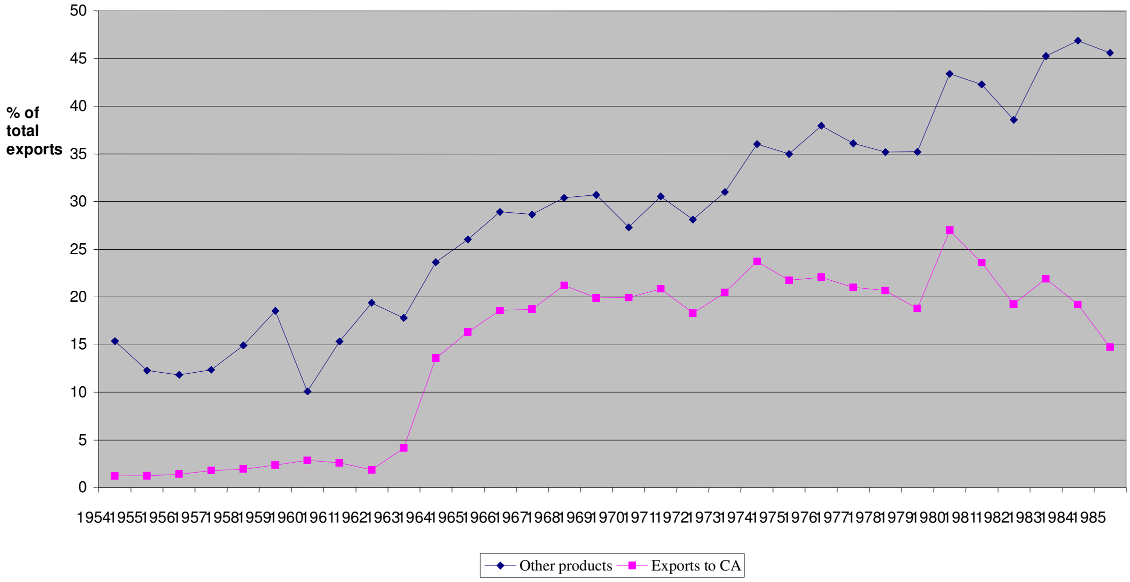
[2] It is important to acknowledge that figures of GDP by sector in Bulmer-Thomas (1987) and in my tables (taken from Costa Rica en cifras, 1950-1998) have some differences in absolute terms: compare table 4 below with tables 12.2 and 12.3 in Bulmer-Thomas' book. Nevertheless, there are not differences in the direction of change between both data sets.

The new incentives went hand in hand with the incorporation of Costa Rica into the Central American Common market in 1963, which opened the door for the emergence of a new manufacturing class and the expansion of foreign investment. Transnational corporations (TNCs) played a very active role in the regional-based process of industrialization; from 1962 to 1969 around 19% of the resources devoted to fixed and working capital came from FDI, including profit reinvestment (Bulmer-Thomas, 1987).

In Costa Rica average FDI per year as a percentage of GDP was four times higher in the period 1960-1979 than in the 1950s. Investment inflows were increasingly concentrated on the industrial sector; from 1970 to 1979, for example, 54.3% of all capital inflows went to that sector. Many large manufacturing TNCs such as Merck Sharp, Dohme and Pfizer (pharmaceuticals), S.C Johnson's (other chemical products), Firestone (tires), Polymer (plastic) and GTE Sylvania (electric appliances) arrived during the 1960s and, to a lesser extent, the 1970s (Ulate, 1993).

The Central American Common Market became a central piece of the industrialization effort of the region. In the case of Costa Rica, the share of exports other than coffee, banana, sugar and cattle began to increase at exactly the same time than exports of Central America did (see figure 2). From 1962 to 1974 the behavior of other exports (which refers mainly to manufactures) followed exactly the same evolution than that of the exports going to Central America. This close association, however, weakened in the second half of the 70s and broke completely during the 1980s. The expansion of the regional market and the Industrial Promotion Law of 1959 contributed to high industrial growth in the 1960s. Industrial production in real terms more than doubled between 1960 and 1970 and contributed to around one fourth of total economic expansion.

Figure 2. Exports to Central America and non-primary exports, percentage of total exports, 1954-1985



Source: CR en cifras, 1950-1998

The creation of new business opportunities through state intervention
One of the most impressive achievements of the Costa Rican model when compared to neighbouring countries was its success in creating a relatively democratic economic structure. There is little doubt that industrialization and state-promoted economic growth led to the appearance of relatively large investors with interests in several sectors. It was the case, for example, of the family Jiménez Borbón, which participated in the most important Costa Rican newspaper (La Nación), one of the leading industrial firms (Florida Ice and Farm, which had a monopolistic position in the beer market) as well as sugar and cattle production. Yet large capitalists were not as large and powerful as in the Dominican Republic, El Salvador and Guatemala and smaller private actors were successful as well.

The nationalized banking system made an invaluable contribution to this process of economic democratization. While domestic credit remained more concentrated than expected, access to subsidized credit was a major factor in opening the door to new capitalists (Rovira, 1993). In the late 70s, for example, 40% of the owners of industrial firms had a father that had not been a firm owner himself (Garnier and Hidalgo, 1991).

The democratization of the economic structure was further facilitated by other policy interventions, such as the promotion of cooperatives. The Constitution of 1949 entrusted the government with the task of promoting cooperatives "with the aim of facilitating better standards of living for workers" (article 64). Between 1959 and 1963 the number of cooperatives rose from 42 to 218 and by 1985 the number had raised to 464, which accounted for 11% of total GDP and 15% of total exports (Reding, 1986). In the 1970s the government created the National Institute for Cooperative Development, which was in charge of providing technical assistance and access to credit to cooperatives

(Reding, 1986). Cooperatives have been particularly important in the coffee and dairy sectors. In 1962 the Federation of Cooperatives of Coffee ('Federacion de las Cooperativas del Café') was created and received immediate support from the public banking system. The Federation had 33 affiliates in 1985, which sold 40% of their harvest directly to the world markets (Brenes, 1990). Meanwhile the Cooperativa Dos Pinos, which produces milk and other daily products since 1947, has continuously grown in the last five decades and has become one of the most important firms in the country (Melendez, 1998).

The growing role of the state in economic activity and social provision
The growth of the public sector since the 1950s was significant. Public spending from the central government as a share of GDP went from 8.8% in 1950 to 13.1% in 1960, 14.9% in 1970 and 21.7% in 1980.[3] The expansion of autonomous institutions was even more spectacular. Between 1948 and 1977 119 new institutions were created so that by 1980 there were 185 different public institutions in the country (Rottenberg, 1993). That number included institutions as important as the Costa Rican Social Security Board (founded in 1943), the Costa Rican Institute of Electricity (ICE, created in 1949) and the National Learning Institute (1965).

This dramatic extension of the state resulted in the creation of a large number of stable employments that were regulated by the Civil Service Law or similar arrangements. Public employment grew at an annual average rate of 7.3% (more than twice that of total employment) and went from 6.2% of total employment in 1950 to 18.5% thirty years later (Castro, 1995). It became one of the main engines of growth of the middle class since public jobs were comparatively well paid and received social recognition. During the 1970s average wages in the autonomous institutions (the best paid jobs within the public sector) were twice as large as average wages in the private sector.

The growth of public employment was driven by a rapid expansion of public spending in health and education. Social spending influenced Costa Rica's distributional structure in two different ways. Per capital spending in real terms multiplied by three in the health sector and by eight in education between 1940 and 1980 (Trejos, 1991). As a result many jobs for doctors, teachers, nurses and related personnel were created: between 1950 and 1990, for example, the number of physicians per 1000 people went from 3.1 to 7.8, which given population growth, illustrates the magnitude of the job growth in the health service.

Social spending had a direct impact on equity and, especially, on overall human development. Costa Rica's education and health indicators are only comparable with those of countries in the Center. Costa Rican social progress during this period was larger than that of most other peripheral countries, as table 4 illustrates. In 1987 only two countries in the periphery (out of 96 analyzed) had lower infant mortality, only four had lower illiteracy rate and none had a better life expectancy than Costa Rica. In all three areas Costa Rica's comparative position improved between 1960 and 1987.

[3] Data comes from CR en cifras, 1950-1998.

Table 4. Comparisons with 94 other developing countries in terms of human development, 1960-1987

	Infant mortality[1]		Life expectancy		Adult iliteracy	
	1960	1987	1960	1987	1960	1987
Number of countries with better indicators than CR	13	2	5	0	3	4
Low Income Countries	0	0	0	0	0	0
in Latin America	0	0	0	0	0	0
Medium Income Countries	3	0	1	0	0	1
in Latin America	1	0	1	0	0	1
Medium-High Income Countries	10	2	4	0	3	3
in Latin America	6	1	3	0	3	3

(1) It refers to children younger than five years.
(2) This is the group where Costa Rica is included.

Source: Trejos (1991) with data from UNICEF and the World Bank

The limitations of the model in the 1970s

During the period 1950-1980 Costa Rica was unique in its combination of high economic growth, democratic institutions and rapid advances in human development (Rovira, 1992). Yet the economic model also had significant limitations, which were partly linked to the way in which the industrialization project was implemented.

Dependence on FDI and, especially, over-dependence on US aid to maintain the Central American Common Market's institutional structure soon became a problem for the integration effort.[4] It added to other major structural flaws of the process. First, Central American countries did not create adequate mechanisms to assure an even distribution of the benefits of the process of integration. Honduras and Nicaragua benefited little from industrial development and suffered a growing imbalance with the other members of the Common Market. Second, the traditional insertion of the region in the global economy was never questioned. In 1970 banana and coffee still constituted 75.6% of total extra-regional exports in Costa Rica and constraint the country's ability to generate foreign exchange.

During the 1970s, successive governments tried to overcome some of the limitations of the economic model by deepening the role of the public sector. In 1972, the second Figueres administration (1970-1974) created the Costa Rican Development Corporation (CODESA) to encourage private and, especially, public investment in new sectors of the economy. At the same time, and as discussed with more detail in other chapters of this research, the government created new social programs, including the

[4] US official aid, partly through the Alliance for Progress, was incorporated into the budget of most regional institutions. In some of them the contribution of the member countries was close to zero reducing their level of commitment (Bulmer Thomas, 1987).

Social Assistance Institute ('Institute Mixto de Ayuda Social', IMAS) and the Family Allowance Fund ('Fondo de Asignaciones Familiares', FODESAF). Both of these programs funded with direct taxes on labour and the indirect sales tax were targeted programs for the poor that complemented the rapid expansion of universal spending (Martínez Franzoni, 2009).

While some of these were very successful, CODESA never reached the magnitude that its founders had ambitioned and never had time to develop and grow. By the 1978 the deteriorating economic conditions and the opposition of a significant part of the business elite were already questioned the long term survival of the public corporation and its numerous firms (Rovira, 1993).

3. Confronting the crisis and initiating reforms

Costa Rican became one of the first victims of the external shocks that affected Latin America during the late 1980s. The second oil price hike in 1978, together with the deterioration in coffee prices and other primary resources in 1980 and the recession in developed countries created severe economic problems. In Central America, the situation was even more worrisome as a result of the crisis of the Central American Common Market, which has supported domestic industrialization for nearly two decades. Civil wars in El Salvador, Guatemala and Nicaragua converted regional exports in an adventure with risky returns.

In less than two years (from August 1980 to May 1982), the colon suffered a sharp devaluation of more than 600% and short term foreign debt grew rapidly (Villasuso, 2008). Between 1981 and 1982 real GDP decreased more than 10% between 1981 and 1982 and did not recuperate its level of 1980 until 1985. Workers were particularly hit by the crisis but recuperated slightly during the second half of the decade. Minimum real wages decreased by more than 15% between 1980 and 1983 and by 1989 they still at its level of 1980.

Structural adjustment thus became not an imposition but a necessity for domestic capital. According to a former high official of the Chamber of Industries, the crisis of the Central American Common market "placed many businesses against the wall. The collapse of the Central American market left the country with the need to search for other markets... and some firms were able to make this shift".[5] A general consensus among the business community on the importance of exporting to non-regional markets emerged. Not even the industrial sector was totally opposed in Costa Rica to gradual liberalization of the current account as long as it was accompanied by export incentives and subsidies.[6] Industrialists saw export subsidies as a compensation for the inefficiencies that the state

[5] Interview in San Jose, Costa Rica, August 2002.

[6] In an interview with a well known Costa Rican economist and public manager (San Jose, Costa Rica, August 2002), he explained that opposition to liberalization was probably smaller than to other type of measures. Also, in 1989 Samuel Yankelewitz, then leader of the Costa Rican industrialists, argued that "nobody can negate that the Chamber of Industries has been a strong supporter of the Structural Adjustment Program since its beginning five years ago… Especially after the collapse of the Central American Common Market" (newspaper article from April 23, 1989 collected in Yankelewtiz, 1990).

created including expensive and low quality public services, lack of infrastructure, high margins of intermediation and a slow customs system.[7]

Costa Rica's success was vital for all the Washington-based institutions if leftist movements were to be stopped in Nicaragua and the rest of the Isthmus. This partly explains why in the period 1984-1990 Costa Rica successfully negotiated two SALs with the World Bank, signed a letter of intent with the IMF and built a strong relation with USAID. US aid flows to Costa Rica from 1983 to 1989 amounted to 4.1% of GDP (Lizano, 1999, annex 5).

The World Bank, IMF and USAID built strong relations with the more neoliberal segments of the Costa Rican government to push for a broad neoliberal agenda.[8] Three measures within the new policy package had a particularly direct influence on the progressive abandonment of the social-democratic model: the process of trade liberalization and export promotion, the deregulation of the financial liberalization and the freeze in public employment.[9] The crisis also forced the Costa Rican government to reduce its commitment to social spending in health and education and to drastically decrease public investment.

Responding to the crisis: fiscal stabilization and employment freezes

The early stabilizing effort had a particularly dramatic effect on public social spending. Between 1980 and 1982 public social spending fell from 20.7% to 15.2% as a proportion of GDP –decreasing also as a proportion of public spending (see table 5).[10] At the end of the 1980s Costa Rica had yet to recover the levels of social spending of the 1970s; real social spending per capita in 1990 was still 10% lower than in 1980.

[7] Interview with officers from the Chamber of Industries, San Jose (Costa Rica), August 2002. According to a well know business leader (interview, San Jose, Costa Rica, August 2002), the Chamber of Industries accepted liberalization but demanded that financial assistance with the process of restructuring as well as the reduction in the costs caused by the state.

[8] Robinson (2003, chapter 2) argues that in Costa Rica like in the rest of Central America a new generation of politicians emerged during the 1980s that were in favor of a more liberal development path. This is clear when the outcome of several "battles" within the Costa Rican government are analyzed. Eduardo Lizano, one of the most prestigious and intelligent proponents of neoliberalism, was in the middle of most of these debates and always prevailed. Several institutions within the public sector including the Central Bank were also active in the promotion of business organizations that defended the need for a more open economic environment.

[9] A third measure that was important during this period was the privatization of the CODESA, which was agreed by the two major political parties and financed with funds from USAID. While trade unions were partly affected by the reforms, CODESA's privatization did not meet as much opposition as other market-friendly measures. This is so because the firms in the conglomerate were relatively new, had never had the support of the private sector and most had high losses.

[10] The reduction is even larger if we take the data from MIDEPLAN as presented in Quesada et al (1999, 165). According to MIDEPLAN's numbers public social expenditure went down from 23.3% to 14.3%. See Sauma and Trejos (1999) for the methodological difference between the two indicators.

Table 5. CR. Social public expenditure, 1980-1990

	1980			1985			1990		
	% of social Expenditure	% of GDP	Real per capita[1]	% of social expenditure	% of GDP	Real per capita[1]	% of social expenditure	% of GDP	Real per capita[1]
Education	29.90	6.19	30926.766	25.20	4.36	20213.676	25.30	4.76	23306.107
Health	42.40	8.78	43856.016	39.00	6.75	31283.07	42.00	7.90	38689.98
Social Security	22.30	4.62	23065.782	29.60	5.12	23743.048	24.60	4.62	22661.274
Housing	3.60	0.75	3723.624	4.40	0.76	3529.372	6.80	1.28	6264.092
Other social services	1.80	0.37	1861.812	2.00	0.35	1604.26	1.30	0.24	1197.547
Total	100	20.7	103434		17.3	80213		18.8	92119

Source: Sauma and Trejos (1999)

(1) Real per capita at prices of 1996

NOTE: It is important to point out that estimations on social spending or even on its tendencies over time are not completely consistent among authors.
For example, according to MIDEPLAN's webpage social spending in education and health as a proportion of GDP in 1990 was 3.9% and 5% respectively. At the same time, World Bank (1997) describes a much sharper reduction in per capita social spending in the 1980s than Sauma and Trejos. According to table 1 in World Bank (1997) social expenditure in education in colones of 1993 went from 24,071.7 in 1980 to 16,958.1 in 1985 and 14,917.7 in 1990. The corresponding numbers for health are 30,230.3, 23,277.1 and 22,638.5

While the crisis of the 1980s brought the historical growth of social spending to a halt, the inertia from the previous period prevented a sharper reduction in social spending. As a result, public investment was forced to carry a large share of the adjustment burden. According to the database *Costa Rica en cifras, 1950-1998*, private investment fell from 2.6% of GDP in 1984 to 0.78% in 1990 (see table 6). The reduction was also large in terms of the participation of investment in total public spending; its share in 1990 was one third of that in 1984.

Table 6. Costa Rica. Public investment, percentage of GDP and of total public spending, 1980-1995

	% GDP	% total spending
1980	2.62	12.03
1981	2.10	12.12
1982	1.48	8.86
1983	2.20	10.28
1984	2.61	12.19
1985	1.60	8.41
1986	1.16	5.04
1987	0.94	4.87
1988	0.75	3.85
1989	0.92	4.64
1990	0.78	3.67
1991	0.84	4.23
1992	0.81	3.91
1993	1.12	4.73
1994	1.09	4.44
1995	0.88	3.69

Source: CR en cifras, 1950-1998

The effort to reduce the public deficit and stabilize the economy was further enhanced with the approval of the Financial Equilibrium Law ('Ley de Equilibrio Financiero') in 1984. The Law contained a broad set of measures to adjust and reform the economy including fiscal reform, reorganization of the export incentives, reorganization of some state institutions and the freeze of public employment. This latest goal was also included in the letter of intent that Costa Rica signed with the IMF in 1984 and in the first SAP (Ulate, 2000). Public employment remained stable at around 155,000 employees and its contribution to total employment decreased by more than 3 percentage points between 1985 (19.1%) and 1991 (15.9%). The freeze in public employment eroded significantly the bargaining position of trade unions and affected more generally the influence of labor in policy design.[11]

Trade liberalization and the promotion of exports

From 1985 to 1990 a slow but steady program of tariff reductions was implemented in several stages (Lizano, 1999). First, all non-tariff measures were converted into ad valorem tariffs and the maximum tariff for final goods was established at 80%. Second, the maximum

[11] The impact of the freezing of public employment on the strength of the trade unions was highlighted by a high official of one of the main trade union confederations in Costa Rica, San Jose (Costa Rica), August 2002.

tariff went down first to 40% and then to 20%. At the same time, the minimum tariff rate was slowly reduced until it reached 5%. According to Herrera (1992) the result of this measure was a reduction in the average tariff rate from 27% in 1986 to 19.7% in 1900 and a reduction in the standard deviation from 24.45 to 16.5% at the end of the period (cited in Lizano, 1999, 77).

To compensate for the tariff reduction, the Costa Rican government reorganized and deepened its program of export promotion, which become the center piece of the growth strategy from 1985 to 1995. Each interested firm signed with the public sector an export contract that established all the applicable incentives, including a tax break called "certificado de abono tributario" (CAT). The government also used some of the funds from the SALs to implement a program of industrial restructuring, benefiting some important firms like Durman Esquivel; yet, the plan was never as ambitious as some sectors within and outside the government wanted.[12]

As in many other Latin American countries, trade liberalization was preceded by a sharp devaluation. The mounting of the trade deficits in the second half of the 1970s led to an increasing gap between the official exchange rate and that of the black market. In December of 1980, after several attempts to avoid devaluation, the government was forced to take steps –the floating of the exchange rate first, the adoption of system of mini-devaluations later- to reduce the value of the currency.[13]

The Costa Rican government also used more explicit instruments to promote export expansion. The most important instrument was the export contracts ('contrato de exportacion') created in 1984. Export contracts, which were signed by the state and each individual firm, incorporated all the incentives that a firm received for exporting to third markets. While most of these incentives had existed since the early 1970s, the contract grouped them together, thus increasing the transparency of the system. The export contract incorporated the following measures (Arriagada, 1992):

1. Expansion of the tax exemption certificates ('certificados de abono tributario', CATs), which reduced the amount of taxes that exports with at least 35% of domestic value added had to pay;
2. Duty free imports of raw materials, inputs and capital goods used by exporters in the production process;
3. A 100 per cent tax exemption for the profits generated in export activities.[14]

The CATs were the most important component of this export promotion package. They consisted on a payment of 15 to 25% of the FOB value of exports that could be used to reduce the tax payments of the company. The CATs, which could be used for 42 months since the time that the foreign currency from exports was received, could also be sold to other companies. As such, a CAT resulted in an immediate increase of more than 15% in the profit margin of any export.

Since its creation and until the final disappearance of the incentive in 1999, the total amount of CATs granted experienced a dramatic expansion. Between 1985 and 1996 they

[12] Interview with a former minister and well known economist, San Jose (Costa Rica), September 2002.

[13] The system of mini-devaluations continued during the rest of the decade, but could not prevent a systematic appreciation of the colon in real terms. A real exchange rate index constructed with CPI and exchange rate data collected from the Central Bank shows the real exchange increasing from 79.9 in 1980 to 245.7 in 1981 and then decreasing steadily until it reached 100.0 in the base year 1991.

[14] Export contracts included other minor measures such as the simplification of other procedures to export (which was achieved for all exports through the creation of the one-window) and some measures that were never implemented such as special port rates and subsidized interest rates.

increased from 973.5 millions colones to 24,551 millions; this represents an expansion of more than 300% in real terms.[15] This increasing financial subsidy constituted one of the key determinants of the export expansion in Costa Rica. According to a survey that Corrales and Monge (1990) carried out among 16 agriculture firms and 38 industrial firms, 87% of the firms considered the CATs as very important for their decision to export. On the other hand, only 18% of the firms rated overall trade liberalization as very important for their export decision.

During the 1980s Costa Rica also created or expanded other export regimes, primarily aimed to expand manufacture exports for the US market. In 1981 the government approved Law 6695 for the Processing Zones for Export and Industrial Parks ('Ley de Zonas Procesadoras de Exportación y Parques Industriales'). The Law created a public corporation to build and promote new export zones, which have to be located in underdeveloped regions. Law 6695 established the following incentives for firms located in the FTZs (Arriagada, 1992): partial exemption of local taxes during five years (the exemption would go down from 80% the first year to 15% the last); preferential loans to national firms that generated at least 35% of value added domestically, and reductions in the rents on the buildings for the first two years. The FTZ regime came to complement the regime of temporal admission (RTA, 'régimen de admisión temporal'), originally created in 1972. The RTA, which was granted only to firms that exported all their production to non-regional markets, allowed for duty-free import of all goods that were to be re-exported back in the following year after being stored, repaired or assembled in Costa Rica (Arriagada, 1992). The regime, which was created to promote simple assembly operations in all regions of the country, also established duty-free import of the capital goods used by exporting firms.

Thanks to these incentives and to an peaceful environment (particularly when compared to neighbouring Central American countries), Costa Rica was one of the first countries in the Caribbean Basin to attract foreign investment in apparel, thus rapidly increasing its market share in the US from less than 1 percent of total US apparel imports in the late 1980s to 1.8 percent in 1993.

In parallel with the creation of new incentives, the Costa Rican government created new institutions to manage the process of liberalization and the promotion of exports. The Ministry of Foreign Trade (MINEX in its Spanish Acronym) and the National Investment Board were both created as part of the President Office to coordinate trade policy and promote foreign investment. In 1983 the Costa Rican Investment Promotion Agency ('Coalición Costarricense de Iniciativas de Desarrollo', CINDE) was created with financial assistance from USAID. CINDE was part of the US government efforts to promote a new economic model in Central America through the promotion of new foreign investment and the expansion of manufacturing exports (Ulate, 2000; Villasuso, 2008).

Financial deregulation and the opening of the banking sector

In the financial front the informal coalition between the Central Bank and USAID pushed for the deregulation of the financial sector and the development of new private intermediaries.[16] USAID funds were used to support several financial institutions in trouble (CODISA), in process of expansion (Banex) or recently created ('Corporación Financiera de Inversiones) (Lizano, 1999, 70). The Central Bank also created an emergency fund with contributions from the private banks to be used in periods of crisis. Even more important were the

[15] The data comes originally from PROCOMER and appeared in COMEX (1997).

[16] The reforms of the financial system in the 1980s and 1990s culminated a long struggle between the defenders of the nationalized banking system and its opponents. Prior episodes within that struggle had been the failed attempt to eliminate the monopoly on the creation of deposits of the public banks (during the Trejos administration) and the creation of non-banking financial firms ('financieras') in 1972. See Jiménez (1993).

measures that increased the ability of private banks to obtain private funds for its activities. In 1984 the Central Bank was allowed to undertake rediscount operations with private banks using resources from foreign institutions (Jiménez, 1993). Between 1987 and 1989 private banks were also allowed to issue certificates ('títulos') at increasingly shorter term; in 1987 private banks could only get resources after 180 days; by 1989 the Central Bank was offering credit overnight (Espinoza, 2002).

The political economic impact of the break in the public monopoly of the financial sector cannot be underestimated. In a short period, private banks dramatically increased their participation in the economy; according to Gonzalez Vera and Mesalles (1993) the participation of private banks in total credit increased from 4.6% in 1983 to 15.3% in 1986 and 29.1% in 1990. This expansion of private banks reduced the dependency of the business classes from state financing, promoted the creation of new ties between the financial and the productive sector and led to the consolidation of a few export-oriented business conglomerates.

USAID, by giving loans for new export projects to the new banks to manage, played a key role in the process.[17] The loans promoted the creation of new banks by large domestic capitalists, usually allied under sectoral arrangements. Banco del Comercio and Banex constitute excellent examples.[18] The Banco del Comercio was founded in 1978 by the owner of Purdy Motors and other members of the Costa Rican Chamber of Commerce. During the 1980s Banco del Comercio concentrated its support in service and trade activities (nearly two thirds of total lending was concentrated in the tertiary sector in 1987) and grew thanks to foreign resources from USAID and other institutions.[19] Banex was funded in 1981 by the Chamber of Industry and the coffee growers. Some of its key investors included the owners of leading Costa Rica firms such as Florida Ice and Farm and Atlas Eléctrica (Sojo, 1995). Nearly 80% of Banex's credit profile during the 1980s was concentrated in the agro-industrial and industrial sector, including projects for the development of non-traditional exports. The Bank received financial assistance from USAID and the World Bank's International Finance Corporation.[20]

Summary and conclusion

The long-term implications of the crisis were significant. While the short-term distributional effects were not as bad as in other Latin American countries, the model of accumulation and distribution of the 1960s and 70s did not survive. The state ceased to be an engine for employment creation and the bargaining power of trade unions was gradually eroded. At the same time, the private sector witnessed a dramatic process of internal transformation. Large investors joined to create new private banks and used the newly available export incentives to diversify their activities and gain increasing political influence. The abandonment of the old development model made the old leading coalitions between trade unions in the public sector, a heterogeneous domestic capital and the state no longer viable.

[17] Interview with a former Minister of Planning and Costa Rican academic, San Jose (Costa Rica), September 2002. See also Villasuso (1990) and Sojo (1995).

[18] Other private banks were also created at the beginning of the 1980s by investors with primary interests in other sectors of the economy. The family Aizemann, large importer of cars and other consumption goods, created the Banco Mercantil. The Banco de San José had foreign investors as its main owners but had also participation from expanding domestic firms such as Durman Esquivel and Lachner and Saenz. See Sojo (1995) and *Actualidad Economica* (several issues).

[19] Information from *Actualidad Economica*, 3 (9), March-April 1989 and Actualidad Económica 10 (8), 1995.

[20] Information from *Actualidad Economica*, 3 (10), April 1989 and 5 (10), 1991.

5. The Neoliberal model: achievements and limitations

During the last two decades, Costa Rica has deepened its commitment to a new model centered on the promotion of non-traditional exports and the deregulation of the domestic economy. Public policy has been concentrated on the weakening of the state's direct involvement in the economy, the development of the private financial system and the growth of exports. Governments from different political persuasions have pushed for a further deregulation of domestic markets and a more intense protection of TNCs. The entry into force of the Central American Free Trade Agreement (CAFTA) with the United States at the beginning of 2009 will be the last step in this process of intense reform.[21]

Better external conditions and the success of large firms as well as FTZs and tourism have resulted in relatively high economic growth. Yet job insecurity, increasing income inequality and structural heterogeneity have accelerated social polarization and questioned the social-democratic character of Costa Rican society.

The changing role of the state and its bureaucracy

The reduction of the role of the state that have began during the 1980s as a response to the crisis became a structural feature of the Costa Rican new model in the period 1990-2008. This was particularly evident in two fronts: the weakening of the bureaucracy and the reduction of its direct involvement in production.

The effort to reduce the size of the public sector and increase its flexibility was particularly intense during the Calderon administration (1990-94), which used a new Structural Adjustment Loan (SAL3) to push for reforms (Aguilar, 1995, Villasuso, 1999). In 1991 the government reached an agreement with the IMF to reduce public employment by nearly 20% (25,000 employees) and changed the program of forced labor "mobility" to a program of voluntary mobility. Despite some protests from within and outside the government, he programs of voluntary mobility continued for the whole period of 1991 to 1994 with funding from USAID (Villasuso, 1999). The program entitled public workers who renounced from their posts to generous benefits, including a one-time payment equivalent to three months worth of salaries (with a maximum of 200,000 colones).[22]

Voluntary mobility ('movilidad voluntaria') had a negative effect on the quality of the civil service and, as a result, in the autonomy and long-term performance of the public service because the most successful and qualified workers used the program to change jobs As a former director of the Civil Service explained, "[the program of voluntary mobility] allowed a lot of good workers to leave because they could find a job somewhere else. The bad workers remained". [23]

A second significant change in the Costa Rican public administration was the expansion of the number of "puestos de confianza" –i.e. people that are directly appointed by the Ministers or director of each institution and that leave with her/him- also expanded (Estado de la Nacion, 2001, chapter 1). The tendency to the creation of these new posts outside the bureaucracy began in the 1980s with financial assistance from the United Nations and other international institutions.[24] The Minister of Foreign Trade and all his team of advisors, for example, were initially paid with funds from USAID. In the 1990s these group of professional technocrats become even more important, especially after a modification of

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[21] See the study promoted by CEPAL and edited in Ulate in 2000 (especially chapters 1 and 2) for an excellent discussion of the economic reforms in Costa Rica during the 1980s and 90s.
[22] Interview with a former director of the Civil Service, San Jose (Costa Rica), October 2002.
[23] Quote in Spanish from the interview done in the summer of 2002: "Yo creo que permitió que mucha gente buena se fuera porque podía conseguir empleo en otro sitio. La gente mala no se fue, se mantuvo"
[24] Interview with a Costa Rican economist and former Ministry (San Jose, Costa Rica, September 2002).

the Law of the Civil Service in 1998 that expanded the number of public positions that could be occupied by non-civil servants to all general directors and sub-general directors in each institution.[25]

While privatization and domestic market liberalization in Costa Rica has taken place at a slower pace than in other countries of the region (like Argentina or El Salvador), it has nonetheless contributed to reduce the participation of the state in the economy and expand the spaces for capital accumulation. During the first part of the 1990s, the government pushed for the deregulation of the financial system as reflected in a summary table in the annex. In 1992 subsidies on interest rates were eliminated and the current account was liberalized, giving banks access to new financial resources. In 1995, and after a long struggle between different interest groups, private banks were allowed to offer checking and saving accounts. The privatization of the public industrial conglomerate CODESA, which had been created in the 1970s, was completed with the sale of the last two firms.

The efforts to reduce public monopolies intensified since 1995 with particular attention to the deregulation of the telecommunication sector. The first step in this direction was the arrival of Millicom International to provide cellular services in Costa Rica, which was cut short when the Constitutional Court ruled its operations illegal. In 2000 the Rodriguez Administration (1998-2002) introduced a proposal to reform the ICE, open the telecommunication sector to private producers, and expand the private involvement in the generation and production of electricity (Estado de la Nacion, 2001; Solis, 2002). The law was approved by the National Assembly, but met with massive protests in the streets and was finally declared unconstitutional. Yet this proved to be just a postponement of the process of liberalization until 2008, when the approval of the Central American Free Trade Agreement with the United States (DR-CAFTA) gave the government the perfect excuse to introduce competition in telecommunications and insurance and weaken the public companies in both sectors.

Export promotion through foreign investment

The expansion of FDI and non-traditional manufacturing exports has become the second permanent component of Costa Rica's recent model.[26] While in the 1980s exports had been promoted through export subsidies that primarily benefited producers of non-traditional primary goods, the FTZs have become a more important policy instrument in the last two decades.

In the early 1990s, the Costa Rican government came to realize that it could no longer expand exports of apparel and other low wage assembly products. Costa Rica decided then to actively promote foreign investment in other sectors—an effort that accelerated during the administration of José María Figueres Olsen (1994-1998). His government aimed to develop "an aggressive policy of investment attraction" in sectors that made "a sophisticated and well paid use of productive resources and not extensive and poorly rewarded use of cheap labor" (MIDEPLAN, 1998, 51).

The attraction of Intel in 1997 constituted a major success in this strategy. Intel's decision, which was partly driven by the government's commitment and the continuous work of CINDE, resulted in a rapid expansion of new exports and helped to later attract other influential TNCs such as Abbot, Procter and Gamble and Microsoft. Costa Rica slowly became a regional leader not only in electronics but also in medical devices, medicines, back-office services and other high tech goods and services. In the particular case of electronics, the country is slowly developing a successful cluster with 47 different foreign firms in the

[25] Interview with a former director of the Civil Service (San Jose, Costa Rica, October 2002).
[26] The discussion in this sub-section relies heavily on Ernst and Sanchez-Ancochea (2008)

free trade zones that specialize in telecommunications, semiconductors and assembly of electronic products. They generate 12,000 direct jobs and account for approximately 30% of the total exports of goods.

The expansion of non-traditional exports has also been supported by an ambitious agenda of preferential trade agreements. In the last few years, Costa Rica has signed agreements with Mexico, CARICOM, the Dominican Republic, Chile, Panama, Canada and the United States (DR-CAFTA). The signing of CAFTA in 2004 was probably the most important because it involved Costa Rica's largest trading partner and because it included a radical agenda of institutional reform. New regulations in areas like intellectual property rights and the liberalization of telecommunications were particularly polemical and resulted in sharp social divisions and political tensions. Its approval in referendum by less than 30,000 votes constituted a major victory to the proponents of the neoliberal model and moves Costa Rica further away from its social-democratic past.

The new role of the financial sector as a source of accumulation

The move from a state-owned financial sector, where the allocation of credit was determined by political objectives, to a more deregulated system with closer links between private banks and large corporations has been consolidated since the early 1990s. Although the largest banks remain in public hands, private banks have grown more rapidly as reflected in table 7. At the end of 2007, public banks had only 1.57 times more assets than private banks, down from 5.10 in 1989 and 2.77 in 1996.

Table 7. Total assets of public and public banks, millions of colones, 1986-2007

	Private	Public	Banco Nacional	Public / Private	BN / Total (%)
1986	17,900	104,483	48,266	5.84	39.44
1989	39,115	199,461	95,613	5.10	40.08
1993	130,993	441,216	207,314	3.37	36.23
1997	315,328	873,064	387,978	2.77	32.65
1999	502,687	1,242,336	566,528	2.47	32.47
2003	1,314,112	2,141,493	911,686	1.63	26.38
2007	4,086,551	6,435,179	2,634,086	1.57	25.03

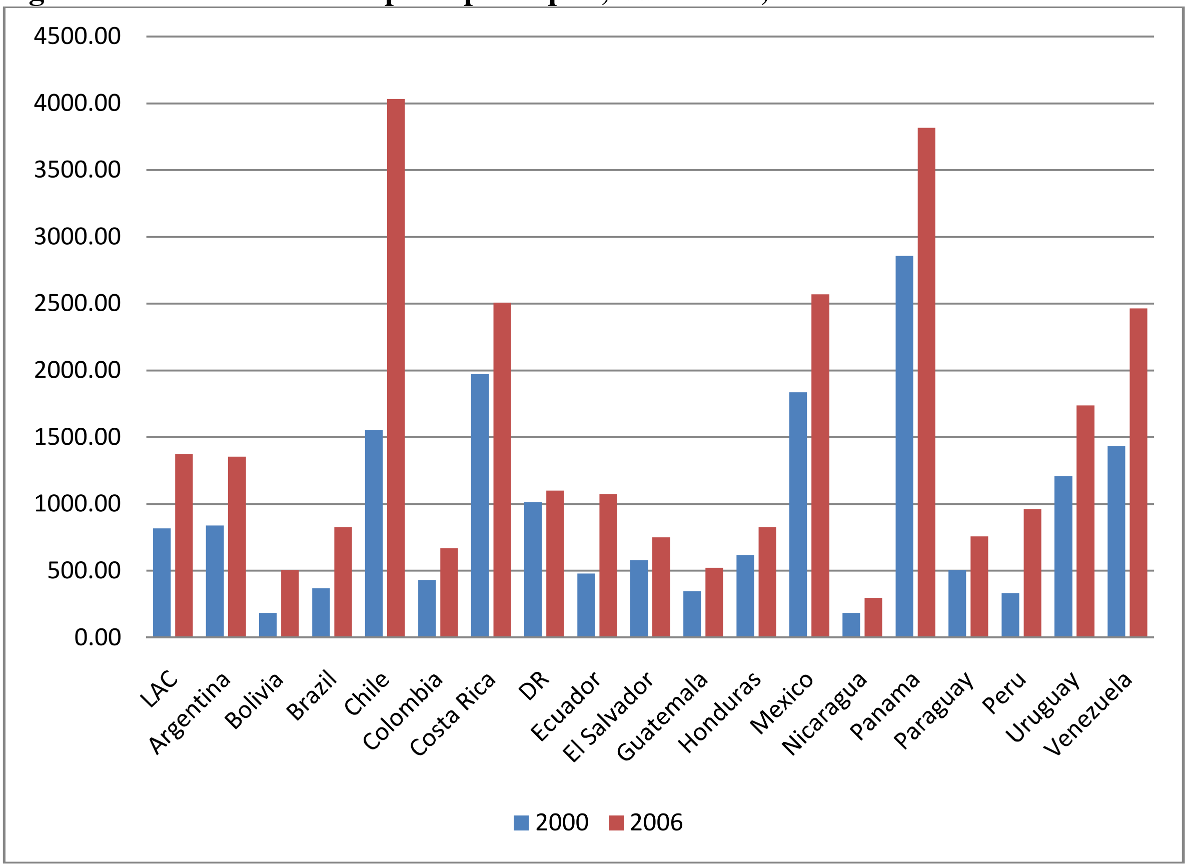
NOTES: the data for 2003 is from May.
Source: own elaboration with data from Actualidad Economica (various years)

In the private banking sector, Costa Rica has experienced a simultaneous process of concentration and transnationalization. Between 1997 and 2007, the share of the three largest private banks in total assets of the private sector increased from 30.7% to 60%. This process took place through a succession of large operations of mergers and acquisitions, where large foreign banks were more active than ever before. In the last ten years the Scotia Bank has bought Banco Mercantil and Interfim, thus becoming the second largest private bank and the fifth overall. In 1999 Banex (the third largest Costa Rican bank until them) was purchased by Panama's Grupo Banistmo, which in turn was sold to HSBC in 2006. The Salvadoran giant Grupo Cuscatlan, which entered into the Costa Rican market in 1999, was bought in 2007 by Citigroup, who also acquired Grupo Uno (Leon, 2008; Sanchez-Ancochea, 2005).

The contradictory results of the new model
At one level, Costa Rica's new economic model achieved very positive results, helping to upgrade and diversify the economic structure. Nowhere is this more dramatic that when one considers the changes in the export structure, which moved first from traditional to non-traditional primary goods and later to high tech manufactures. In 1982 coffee and banana accounted for 56% of total exports, which were dominated by traditional primary exports and a few manufactures going to the Central American Market. In 1995 the share of the two main commodities had gone down to just 40%, and new exports to third markets like tropical fruit, flowers and jewellery assembly had appeared for the first time in the list.

Between 1996 and 2007, exports grew at an annual average rate of 8.6% --surpassing US$9.3 billions in the latter year. As a result of this sustained expansion, Costa Rica has become one of the best export performers in Latin America: in 2006 (figure 4), it was ranked fifth in terms of exports per capita after Chile, Panama, Mexico and Venezuela (all of which benefited from high commodity prices or a large re-export level). Costa Rica's exports also enjoy a higher technological content than the Latin American average (excluding Mexico): as table 8 indicates, in 2005, high technology exports accounted for 29% of all exports of goods from Costa Rica as compared to only 4% in the whole region (excluding Mexico).

Figure 4. Latin America. Exports per capita, US dollars, 2000 and 2006



Source: own calculations with data from World Bank (2008)

Table 8. Costa Rica and Latin America (without Mexico). Export structure by technological content, percentage of total exports, 1987-2005

	1987	1990	1995	2000	2005

	CR	LA	CR	LA	CR	LA	CR	LA	CR	LA
Primary goods	***68.4***	***46.3***	***57.6***	***49.8***	***58.3***	***40.2***	25.9	***41.1***	23	***47.4***
Manuf. based on natural resources	*8.7*	*27.0*	*11.4*	*24.5*	*15.7*	*28.6*	13.7	*27.6*	14	22.9
Manuf. low technology	*12.1*	*10.6*	*12.8*	*10.3*	*10.9*	*9.0*	16.8	*8.6*	14.4	7.5
Manuf. medium technology	*5.2*	*12.7*	*6.1*	*12.2*	*7.0*	*13.8*	16.6	*14.0*	18.7	15.8
Manuf. high technology	*3.2*	*2.2*	*3.2*	*2.0*	*2.9*	*5.7*	26.6	*6.0*	29	4.1
Other transactions	***2.4***	***1.2***	***9.0***	***1.3***	***5.3***	***2.7***	0.5	***2.7***	0.8	***2.3***

Source: own elaboration with data from ECLAC

Export expansion went hand in hand with the growth of FDI, which became a primary source of capital accumulation. FDI increased from an average of US$323,5m per year between 1992 and 1997 to an average of US$575m between 1998 and 2005. In 2004, foreign inflows were US$617m, equivalent to 3.3% of GDP and 15.3% of gross capital formation. The stock of foreign investment that same year was US$4,815m.

While in the late 1980s some Costa Ricans firms benefited from export subsidies to become exporters, in more recent times FDI has been the driver of the export success. Most large exporters are foreign firms located in the FTZs and the few Costa Rican firms in the ranking specialized in primary goods. Of the 25 largest exporters in 2001, just 10 firms produced outside the FTZs and only three (one of them public) were Costa Ricans (Sánchez-Ancochea, 2004).

The rapid expansion of both exports and FDI has some welcoming effects, including relatively high rates of economic growth and a more diversified source of foreign exchange. Costa Rica was one of only four Latin American countries to grow at more than 4.5% (in dollars of 2000) in 1990s and early 2000s (table 9) . Costa Rica's annual average rate of GDP and GDP per capita between 1990 and 2004 was 4.8% and 2.6%, well above the Latin American averages of 2.7% and 1.3%.

Table 9. Annual average rate of growth of GDP and GDP per capita, 2000 US dollars, 1990-2004

	GDP	GDP per capita	Abs. value 2004
Argentina	3.30	2.06	7,511
Bolivia	3.44	1.26	1,036
Brazil	2.55	1.18	3,675
Chile	5.65	4.18	5,448
Colombia	2.61	0.73	2,069
Costa Rica	4.76	2.63	4,534
DR	4.94	3.25	2,450
Ecuador	2.55	0.71	1,435
El Salvador	3.81	1.87	2,124
Guatemala	3.61	0.93	1,676
Haiti	-1.26	-3.24	437
Honduras	3.30	0.51	952
Mexico	2.92	1.31	5,968

Nicaragua	3.14	0.37	778
Panama	4.56	2.83	4,373
Paraguay	1.81	-0.57	1,413
Peru	3.81	2.02	2,207
Uruguay	2.05	1.39	5,826
Venezuela, RB	1.63	-0.38	4,575
LA average	2.90	1.31	3,921

Source: own calculations with data from World Bank (2008)

Although economic growth was relatively high, the problem was its relatively unequal distribution not only among individuals but also among economic sectors.[27] The process of financialization and export promotion has resulted in the creation of two different Costa Ricas, one based on non-traditional exports and some modern services and the other based on more traditional activities that have problems to secure productivity growth and compete with the growing level of imports. According to Garnier and Blanco (forthcoming, 183): "on the one hand, new activities—mainly linked to exports, tourism and certain services—emerged that are characterized by high productivity, a more skilled labour force and that, as a result, pay higher and growing wages… On the other, the growth of other type of jobs, which are characterized by low productivity, low skills and low income is worrying,"[28]

Table 10 offers some indication of this trend, although at a very aggregate level. The traded good sectors show a relatively high level of productivity growth between 1987 but a poor performance in terms of employment. This is particularly clear in the agricultural sector, where a yearly 4.3% expansion of productivity was just the result of no employment creation. On the other hand, the service sector has become and "employment buffer" for those workers that could not find employment in more productive sectors.

Table 10. Value added, employment and labor productivity in Costa Rica, annual average of growth, 1987-2007

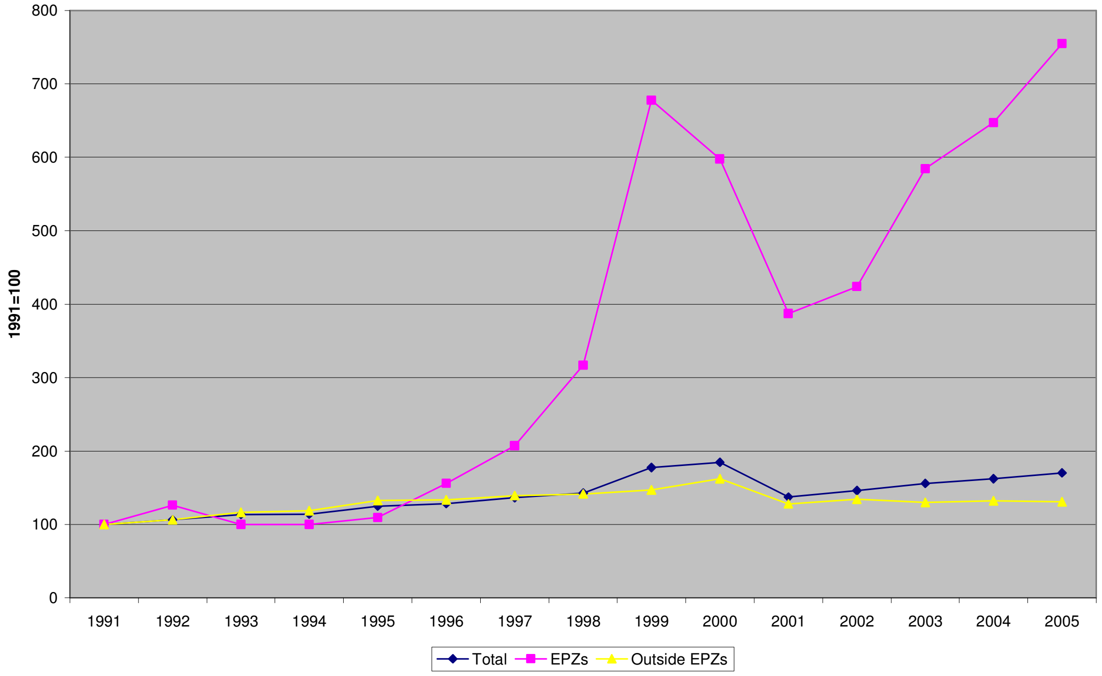
	Production	Employment	Labor productivity
Gross value added / Total employment	5.0	**3.7**	**1.3**
Agriculture, silviculture and fishing	4.2	-0.1	4.3
Manufacture and mining	5.6	2.3	3.3
Electricity and water	5.1	3.1	1.9
Construction	5.3	5.3	0.1
Transport, storage and communication	8.9	6.1	2.6
Other services	4.0	5.4	-1.3

Source: own calculations with data from the Central Bank

A similar trend can be found within the manufacturing sector, at least regarding the asymmetric evolution of productivity. Productivity in the export processing zones (EPZs)—where most high tech activities are concentrated—was 7.5 times higher in 2005 than in 1991, while it remained almost stagnant in the rest of the manufacturing sector (figure 5).

[27] The following two paragraphs rely heavily on Sanchez-Ancochea (2009).
[28] Own translation.

Figure 5. Productivity in total manufacturing, export processing zones (EPZs) and all other manufacturing activities. Based numbers from data in real colones, 1991-2005



Source: own calculations based on data from PROCOMER, MIDEPLAN and Central Bank of Costa Rica
NOTE: data on employment comes from two different sources and is calculated differently so that results should be interpreted with care.

In the case of the manufacturing sector, the problem has been that high tech manufactures—as well as large segments of the tourist and financial sectors—are de-linked from the rest of the economy and create few positive effects on productivity and wages at the macro-level (Ernst and Sanchez-Ancochea, 2008; Paus, 2005). TNCs, while receiving high tax incentives to operate in the country, have little interest in creating new supplying arrangements with domestic firms and thus create an aggregate positive impact. Meanwhile, small and medium Costa Rican companies are generally incapable of providing the type of inputs that TNCs demand (Paus, 2005) because they lack financial and technological support to accumulate knowledge-based assets.

This pattern of dual development has been one of the factors contributing to the expansion of inequality (Martínez Franzoni and Castro, 2009), which has also accelerated social polarization in Costa Rica. Debates about the liberalization of telecommunication and insurance and about the fate of the Central American Free Trade Agreement with the US (DR-CAFTA) have dominated the policy agenda, which is no longer concentrating on securing a social-democratic model based on high social spending and a more opportunities for the whole population.

6. Varieties of capitalism and the Costa Rican experience

A recent influential and path-breaking analysis of Latin America´s variety of capitalism has emphasized both its stable nature and its unequal and hierarchical character (Schneider, 2009; Soskice and Schneider, 2009). By emphasizing the importance of transnational corporation and large family groups and the lack of incentives for innovation and accumulation of human capital, this type of work tends to minimize the impact of globalization on Latin America.

The experience of Costa Rica discussed in this paper, however, raises some doubts about this presumption. The implicit model developed in this paper recognizes the importance of domestic and transnational firms, but also emphasizes the role of the state and trade unions when discussion any model of capitalism in Latin America. As soon as you add these other authors, it is clear that the notion of stability in economic models must be questioned. In fact, Costa Rica represents as much a case of break-down with the past in the last two decades than of continuity in some institutions.

The Costa Rican case has an additional lesson that may be important when thinking about the future of Latin America. Despite a recent reduction on income inequality in recent times in some parts of Latin America (Cornia, 2009), globalization may create new tensions and difficulties to sustain a model that is both vibrant and equitable. Liberalization creates new winners and erodes some of the capacities of the state to build social consensus around high social spending and a large government. In that sense, Latin American countries may have a perpetual difficulty to promote equity, even if their model experience more constant change than sometimes considered.

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