DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

COSTA RICA

LIQUIDITY PROGRAM FOR GROWTH SUSTAINABILITY IN COSTA RICA

(CR-L1033)

LOAN PROPOSAL

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1. Annual work plan
Not applicable (see paragraph 3.5)

2. Monitoring and evaluation provisions
http://idbdocs.iadb.org/wsdocs/getDocument.aspx?Docnum=1780770

3. Safeguards policy filter
http://idbdocs.iadb.org/wsdocs/getDocument.aspx?Docnum=1780625

4. ESMR
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5. Procurement plan
Not applicable (see paragraph 3.5)

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1. Sector aspects 1
[Macroeconomic]
http://idbdocs.iadb.org/wsdocs/getDocument.aspx?Docnum=1780222

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Abbreviations

BCCR	Central Bank of Costa Rica
DGAP	Liabilities and Asset Management Division (of the BCCR)
ESMR	Environmental and social management report
IFI	Intermediary financial institution
LIBOR	London interbank offered rate
LPGS	Liquidity Program for Growth Sustainability
MPC	Multisector credit program
SUGEF	Superintendency of Financial Institutions

PROJECT SUMMARY

COSTA RICA
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(CR-L1033)

Financial Terms and Conditions			
Borrower: Central Bank of Costa Rica (BCCR)		Amortization period:	5 years
		Grace period:	3 years
Executing agency: BCCR		Disbursement period:	12 months*
Source	**Amount US$ million**	Interest rate:	Six-month LIBOR plus 400 basis points annualized
IDB (Ordinary Capital)	500	Initial committment fee:	1%
Local	0	Credit fee:	0.75%
Cofinancing			
Total	500	Currency:	U.S. dollars

Project at a glance

Project objective:
The *objective* of the proposed program is to increase the liquidity of the Costa Rican financial system, thereby providing financing to strengthen competitiveness of export manufacturers. The *purpose* is to channel credit in foreign exchange to the manufacturing sector through intermediary financial institutions (IFIs) in order to mitigate the consequences of the global financial crisis (paragraph 1.22)

Special contractual conditions:

As conditions precedent to the first disbursement, the executing agency must demonstrate to the Bank that the program Credit Regulations and the special BCCR standards previously agreed with the Bank to govern lines of credit to IFIs are in effect (paragraph 3.6).

Exceptions and extensions to Bank policies:
The Central Bank's Internal Audit Department will audit the program (paragraph 3.10). To complement the Central Bank's asset and liability management strategy, the option of charging LIBOR on outstanding balances has been added in accordance with document FN-507-4 (paragraph 2.1).

Special considerations.
The program will have the following special execution conditions: (i) the terms and conditions of the financing (paragraph 2.3); (ii) eligibility of businesses and eligible subloans (paragraph 2.4); (iii) environmental management mechanism (paragraph 2.9); (iv) a Revolving Fund of up 10% of the program financing (paragraph 3.7); (v) presentation of quarterly reports by the BCCR (paragraph 3.9); (iv) inspections of IFIs to verify compliance with contractual conditions and the possibility of engaging technical consulting services as necessary (paragraph 3.9).

Project consistent with country strategy: Yes [X] No [ ]

Project qualifies as: SEQ [ ] PTI [ ] Sector [ ] Geographic [ ] Headcount [ ]

Procurement: N/A

Verified by ESR on: 25 November 2008

* This period may be automatically extended for a further 12 months if during the first 12 months 70% of the financing has been disbursed, or otherwise by agreement between the parties.

I. DESCRIPTION AND OUTCOMES MONITORING

A. Frame of reference, problem areas, and rationale

1.1 In response to the current global financial crisis, the Bank has launched a Liquidity Program for Growth Sustainability (LPGS) to support efforts by Latin American and Caribbean governments to mitigate the effects of the crisis on macroeconomic stability, growth, and employment. The purpose of the program is to restore the flow of credit to the real economy, temporarily offsetting shortfalls in financing resulting from the crisis. By restoring credit for working capital in dollars, including funds to back foreign trade transactions, the program is expected to: (i) support domestic production; (ii) protect employment levels in the region; and (iii) preserve macroeconomic and social stability.

1.2 The proposed program would provide US$500 million in financing to the Central Bank of Costa Rica (BCCR) to enable it to provide credit lines in dollars for working capital and trade financing to exporters and other enterprises within the export chain. The BCCR will channel the funding through regulated first-tier financial institutions currently facing restrictions on liquidity and access to external and interbank sources of funding. The program will also address the financing needs of domestic enterprises heavily dependent on direct financing from foreign suppliers that have recently been cut off from such sources of financing because of the current global financial environment and must now seek financing on the local market. The program is supported by the International Monetary Fund (IMF), as reflected in its recent letter. Meetings have been held with the IMF for the purpose of coordinating and preparing the program.

1. Recent macroeconomic performance and prospects

1.3 Costa Rica has put in a satisfactory macroeconomic performance in recent years. The economy has posted strong growth, public sector accounts have improved substantially, and the country has strengthened its external payments and international reserves position. Costa Rica's strong economic growth is due to a confluence of external and internal factors. On the external front are strong demand for exports, including tourist services, and substantial foreign direct investment, particularly in the tourist, real estate, and agricultural sectors.[1] Internally, relatively high levels of consumer and investor confidence combined with low interest rates due to inflows of capital have resulted in expanded domestic credit. This has led in turn to accelerated consumption and private investment, strong activity in the construction sector, and robust growth in manufacturing, particularly in high-technology industries. The interaction of these factors produced economic growth of 5.9% in 2005, 8.8% in 2006, and 6.8% in 2007. The expansion in output combined with increased social transfers resulted in a steady reduction in unemployment (from 6.5% in 2005 to 4.6% in 2007), poverty (from 21.2% in 2005 to 16.7% in 2007), and extreme poverty from (5.6% in 2005 to 3.3% in 2007).

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[1] The external sector (X+M) represents over 100% of the gross domestic product (GDP). In addition, there is a considerable degree of dollarization in the financial system (see infra).

1.4 The economy is expected to grow by 3.6% in 2008, well below the gains posted in 2006 and 2007. The favorable investment climate that prevailed last year has given way to increasingly tight liquidity conditions, while persistent inflationary pressure, rising interest rates, a marked slow down in external and domestic credit growth, and the recent depreciation of the colon have begun to affect consumer confidence, and thus consumer spending. Although exports grew during the first half of the year despite the slowdown in the U.S. economy since late 2007, a decline that began early in the second half started accelerating in September in response to the current global financial crisis. In addition to its effects on demand and prices, the crisis appears to be affecting many domestic businesses by restricting access to supplier credits, and commercial banks, particularly private banks, by restricting their access to facilities from correspondent banks.

1.5 Exports and capital inflows are expected to decline further in 2009 as a result of the continued deleveraging of the United States economy and its adverse impacts on the global economy. Assuming that these declines do not exert significant pressure on the foreign exchange market leading to restrictions on internal and external liquidity (which would among other things bring about a sharp contraction in domestic credit), the economy could grow by an estimated 2.4%.

1.6 In this context, the program is intended to temporarily mitigate some of the effects of decreased financing flows so as to preserve economic growth insofar is possible in an international environment that has yet to show signs of recovery. Link Sector aspects 1

2. Financial system

1.7 ***Background.*** The favorable macroeconomic conditions described earlier have had a positive impact on financial sector performance. In recent years, the banking system has enjoyed healthy profitability, moderate risk levels, and sound levels of capitalization. However, these indicators have weakened recently due to the significant growth of credit.

1.8 The positive developments in the banking system have been accompanied by improvements in regulation, prudential standards, and supervision. In addition, the recent entry of international banks into the country is helping to modernize the domestic financial system through increased competition and the transfer of more robust management practices and tools.

1.9 The relatively favorable state of the banking system is one factor that is helping to contain the adverse effects of the global financial crisis. However, the authorities are aware that the financial sector is vulnerable to the crisis, and are therefore already taking steps to mitigate its adverse effects on the sector and, by extension, on the real economy.

1.10 However: (i) the level of dollarization in the banking system, approximately 50% of both loans and deposits, creates indirect credit risks associated with unexpected exchange rate movements (dollar-denominated debt held by borrowers that do not

generate dollars); and (ii) the private banks' share of the system's dollar deposits (37%) makes the banking system highly dependent on external financing.

1.11 ***Recent developments.*** The level of lending and deposits in the financial system has clearly slowed in recent months. While nominal credit growth was 30% in 2006 and 54% in 2007, the trend has been down in 2008, particularly in the second half. While credit growth was 33% in the first half, figures since July point to a clear downtrend. A similar trend is apparent in deposits. While nominal annual growth was 25% in 2006 and 2007, annualized growth in the first half of 2008 was 15%, declining to 11% in the period since July. Also, deposits tend to be dollars, to the detriment of the colon.

1.12 One factor explaining the foregoing is that high levels of growth in recent years have not been accompanied by equivalent increases in capital, particularly for public banks. As a result, levels of capitalization in the banking system have tended towards the minimum requirements set by prudential regulations, limiting the prospects for a credit expansion.

1.13 The global financial crisis has forced the banking system to further restrict its lending activities due to:

a. the slowing activity of international bank subsidiaries, which account for a significant proportion of Costa Rica's private banks. In view of the problems faced by the parent companies, subsidiaries have received specific instructions not to increase, or in some cases reduce, their credit exposure in the country;

b. the limited availability and increased cost of funding for trade financing and working capital by correspondent banks to local financial institutions. The authorized volume of credit lines with correspondent banks has declined by approximately 15% in 2008. In addition, there are lines that remain formally open but are inactive in practice as a result of correspondent bank business decisions. According to local bank representatives, financing through correspondent bank lines has fallen roughly 20% for large banks and 50% for smaller ones. Similarly, the cost of available financing facilities is up by 40% over the costs before the crisis.[2]

c. a greater preference for liquidity in the banking system given the uncertainty over the magnitude of the crisis and its potential impact on the local economy. In fact, the ratio of liquid assets to total deposits increased from 18% in December 2006 to 23% in October 2008.

1.14 ***The authorities' response.*** The authorities have agreed on steps to restore stability, in particular:

[2] Estimates obtained by the project team indicate (i) external lines totaling approximately US$1.2 billion prior to the crisis; and (ii) an intercompany loan and loan from foreign suppliers (also in dollars) of US$400 million.

a. increasing local currency liquidity facilities, basically through increased flexibility and broadening the scope of the central bank's discount windows;

b. reviewing prudential standards for triggers warning of irregular financial situations envisaged in the regulations governing corrective actions and bank resolutions. Profitability and liquidity ratios, in particular, have been corrected, without compromising sound prudential principles, to prevent the occurrence of artificial distortions linked to inflationary dynamics that could affect bank performance;

c. strengthening the capital of three of the four state banks through a capital injection of US$117 million. This will facilitate increased lending by State banks, particularly to support the productive sectors most affected by the credit squeeze. The proposed capitalization of the public sector banking system will be presented to the Congress shortly for approval;

d. taking out dollar-denominated loans from multilateral entities to compensate for the drying up of external financing and to make credit lines available in the event that flows of private financing to the local economy should further contract.

1.15 ***Prospects***. In theory, the financial system is well positioned to face the negative effects of the crisis. However, the prospects for the sector will ultimately depend on the severity of the crisis and its effects on the real sector. Certain factors can be identified at this point that will likely impact system performance, including:

a. a decline in credit portfolio quality. Bank portfolios are unlikely to maintain their current low risk levels. The combined pressures of slumping economic growth, higher interest rates, and the local currency depreciation against the dollar will likely affect borrower payment capacity and the quality of bank loan portfolios;

b. external financing constraints. Restrictions on access to external financing and the cost of such financing is likely to continue until the crisis reaches an inflection point;

c. a preference for liquidity. In a context of uncertainty, local banks can reasonably be expected to maintain their preference for higher levels of liquidity in order to respond to possible depositor withdrawals.

d. a sluggish credit market. These three factors, combined with constraints on credit growth linked to adjusted capitalization levels, suggest that the current credit slowdown will continue until the underlying causes correct.

1.16 The recapitalization of State banks and the authorities' formal request to prepare and approve this operation will help alleviate two of the constraints discussed above. Eliminating these constraints should have a positive effect on credit growth and hence on the real sector. Link Sector aspects 2

3. Problem to be addressed and rationale

1.17 The recent deterioration in external accounts and the ensuing pressure on the exchange rate is beginning to impact negatively on internal liquidity, pushing lending rates up and reducing the availability of credit. The present crisis underscores one of the challenges facing the authorities: how to maintain an adequate supply of credit to the real economy that is sufficient to generate reasonable and sustained economic activity.

1.18 In November 2008, internal financing in dollars was characterized by: (i) a 2% interbank lending rate; (ii) an average dollar deposit rate of 3.7%; (iii) a mean intermediation spread of approximately 8%; (iv) an average portfolio lending rate of 11.9%; and (v) a relatively illiquid market due to the market structure (the predominance of dollar deposits in State banks). Link Sector aspects 3

1.19 Compounding the problems on the domestic front, the crisis (i) produced significantly higher interest rates on external lines in dollars (currently at 2.5% to 3.75% over LIBOR) and (ii) caused credit lines to be partially blocked or canceled and credit limits lowered. This affected private banks in particular, for which external lines represented 26.9% of borrowing (compared with less than 5% in the State banks) as of September 2008. Link Sector aspects 4

1.20 In view of the foregoing, the Costa Rican authorities decided to seek alternative sources of external financing, such as the proposed program, to enable the real economy to gradually adjust to the new realities of the international environment.

1.21 The program is consistent with the Bank's Strategy with Costa Rica, which supports the government's efforts to consolidate macroeconomic stability and economic growth through continued support to the productive sectors to position them in the world markets.

B. Objectives, description, and components

1.22 ***Objective***. The objective of the proposed program is to increase the liquidity in the Costa Rican financial system, and thereby provide financing to strengthen the competitiveness of export manufacturers. The purpose is to channel credit in foreign exchange to the manufacturing sector through intermediary financial institutions (IFIs) in order to mitigate the consequences of the global financial crisis.

1.23 ***Description***. The program fits in with the Bank's activities to support private sector development. The program will provide public funds to support those areas of private financial intermediation not performed effectively by the market. Specifically, the program seeks to make up the shortfall in correspondent bank dollar facilities that have dried up as a result of the crisis because the banking systems lacks the funds to finance the export activities of Costa Rican businesses. Link Sector aspects 5

1.24 In the current economic climate, given the additionality the program would bring to this objective, the Costa Rican government has requested that program financing:

(i) be drawn on the Bank's public financing window; (ii) be part of the Emergency Facility; and (iii) be implemented with the Central Bank of Costa Rica (BCCR) as the borrower. Link Sector aspects 6

1.25 The present program would not be a trade finance program strictly speaking. Although the purpose of the financing would be the same, the conditions would be different. In a traditional trade finance program with international banks, financing conditions (i.e. rates, terms, etc.) are based on export guarantees. In contrast, the executing agency in the present program is the BCCR, which is not permitted to assume counterparty risk of any kind. Accordingly, the BCCR would need to secure first-demand guarantees from the participating IFIs as collateral for the lending operations, and would therefore not necessarily require a lien on the assets generated with its funding. Also, the BCCR would ensure that the IFIs use the funds received for eligible loans and control and monitor the use of funds disbursed and recovered:

a. loans made with program funds would be guaranteed with first-tier securities or dollar-denominated receivables (*documentos de crédito*) not necessarily related to the financing;

b. the terms of the eligible loans credits will be modeled on those of the Trade Finance Facilitation Program (TFFP) (RG-L1003) in order to adapt them to the needs of the private sector, which is continuously monitored by this Bank unit, to ensure complementarity between the program and the support provided to the sector through the Bank's private window;

c. any IFI that fails to provide information or provides inaccurate or incomplete information in order to obtain resources from the program will be sanctioned as specified in the BCCR Charter and barred from future participation in the program.

1.26 The current structure of market rates suggests that IFIs would use the BCCR lines (rates are now higher) only if the combination of dollar-denominated funding available on the local market and international lines currently available to them are not sufficient to meet their needs. A further deterioration in the global economic environment could impact the situation under two additional scenarios: (i) if the rates charged for correspondent bank facilities tend to exceed the rate charged under the program; and (ii) if foreign banks continue to cut back or close existing facilities. In either case, the program would enable local banks to borrow funds so long as the business projects could support the new lending rate based on the new funding rate and spread.

1.27 ***Components***. – The program will have a single credit component in the amount of US$500 million.

C. Outcomes indicators

1.28 It is important to note that in this operation, as in any loan of this type, the IFIs will select the most viable enterprises and projects. Therefore, if the economy's

structural variables remain constant, the impact of the projects would be determined by the market. The IFIs would select the best enterprises and projects, and if they maintain sufficiently low arrears rates in repaying the loans, the market mechanism itself would: (i) ensure selection of the best enterprises and projects; and (ii) establish the indicator levels. From this perspective, any indicator of "goal" or "purpose" could be considered only an a priori estimate of what the market might achieve, and therefore not used to judge the success or failure of the operation.

1.29 On this basis, the principal indicators in the results matrix are: (i) in terms of outputs, the establishment of second-tier lines (the only factor determined by the project itself); and (ii) depending on the basic assumptions for this type of program (the mutual willingness of borrowers and IFIs to take and make loans) and therefore exogenous to the operation: (a) as an intermediate outcome, requests for credit lines and their allocation to IFIs under the program; and (b) as final outcomes, the volume of disbursements.

1.30 In accordance with the guidelines of the Bank's Office of Evaluation and Oversight for the evaluation of multisector credit programs (MCPs), an ex post report of MPC outcomes (table of final indicators) will be prepared, in addition to the results matrix, to provide additional information and enable the operation's impact to be quantified (Table of Indicators [Goal])

II. FINANCING STRUCTURE AND PRINCIPAL RISKS

A. Financing mechanism

2.1 The financing will be offered on the same conditions as emergency loans from the Bank's Ordinary Capital: (i) the loan contract must be signed within 60 days after the date it is approved and take effect within 180 days after that same date; (ii) the amortization period will be five years and the grace period three years; (ii) the annual interest rate will be six-month dollar LIBOR plus 400 basis points;[3] (iv) the initial commitment fee will be 1% of principal; and (v) the credit fee will be 0.75%, on undisbursed balances and will begin to accrue 60 days after contract signature.

2.2 The borrower and executing agency will be the BCCR, which will execute the program by providing financing to IFIs that lend in turn to the productive sector for eligible projects.

2.3 The terms of the BCCR financing to IFIs and the IFI loans will be governed by the program Credit Regulations and special rules approved by the BCCR for this purpose. The basic terms and conditions of the financing will be: (i) a variable interest rate; (ii) BCCR assumes IFI risk; (iii) the IFIs assume the subborrowers' risk; and (iv) in no case will the BCCR bear losses associated with program

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[3] The rate charged on outstanding balances may be set at the borrower's option, in accordance with the policy set out in document FN-507-4.

intermediation activities. The basic terms of the BCCR financing to the IFIs will be as follows:

a. *Eligibility*. Eligible entities are State-owned banks and private banks subject to supervision by the Superintendency of Financial Institutions (SUGEF) that meet the financial criteria established in the Credit Regulations;

b. *Financing conditions*. The lines will be five-year revolving credit lines in United States dollars. The maximum term of each disbursement will be two years. Each disbursement must be onlent for the maximum term established in the Credit Regulations. The maximum amount of each line will be based on: (i) the IFI's volume of external financing, if available, and its total obligations as specified in the BCCR special rules; and (ii) the ceiling set for the total program financing established in the Credit Regulations. The IFIs must either relend loan recoveries within the period term indicated in the Credit Regulations or repay them.

2.4 The IFIs will, in turn, provide financing to subborrowers on the following terms:

a. *Eligible enterprises*. The enterprises eligible for the program will be: (i) those with business projects geared to the export of goods and services; and (ii) enterprises in the supplier chain related to goods and services exports being financed in United States dollars;[4]

b. *Eligible subloans*. Eligible subloans within this universe of enterprises will be: (i) denominated in dollars; (ii) used to finance exports, imports, or working capital; (iii) granted for a maximum period of two years; and (iv) below the ceiling established in the Credit Regulations.

2.5 The program costs are summarized in the following table:

Program cost by source of financing
(US$ millions)

Investment component	IDB	Local counterpart	Total
Credit	495	0	495
Initial fee	5	0	5
Total	500	0	500

B. Risks

2.6 *Macroeconomic risks*. The program's success will depend on a macroeconomic framework and investment climate favorable to productive investment and thus private-sector demand for credit. In the current international context, authorities are redoubling their efforts to maintain macroeconomic stability. On the fiscal front,

[4] The term United States dollar is understood to mean any hard currency used as a basis for foreign trade operations as defined by the Credit Regulations.

public sector accounts are expected to post a surplus in 2008 for the second consecutive year. Also, the authorities began tightening monetary policy in the second half of the year to bring inflationary pressures under control and contain prices in general.

2.7 *Fiduciary risks*. The program is considered to entail low fiduciary risk. The BCCR is an autonomous public-law entity with legal status and capital of its own. It was created by Law 1130 of 28 January 1950 as an independent body responsible for Costa Rica's monetary, exchange, and credit policy. The BCCR: (i) enjoys administrative autonomy; (ii) applies laws of governance; and (iii) discharges the functions identified in its Charter, the National Banking Act, and other legislation.

2.8 *Financial risks*. The program poses less risk than a regular multicredit program. Its financial viability and risks will be determined by: (i) the interest rate; (ii) the profitability of the BCCR loans to IFIs; (iii) IFI market profitability; and (iv) the first-demand guarantees the BCCR obtains from the IFIs.

2.9 *Environmental risks*. In accordance with the Bank's policies, specifically Directive B.13 of the Environmental and Safeguards Compliance Policy, the program does not require an environmental classification. The nature and impacts of its operations cannot be known in advance, but will be subject to Costa Rican environmental mechanisms and legislation. In light of its status, the BCCR is not required to verify each operation, and enforcement of legislation will be left to the first-tier entities. Nevertheless, the Credit Regulations: (i) provide a list of activities that cannot be financed; (ii) provides a list of those sectors eligible for financing upon presentation by the subborrower of the proper environmental documentation, including licenses and permits; (iii) specify that subborrower operations not included in the first two categories will be eligible for financing provided they comply with national environmental legislation; and (iv) specify that violations of environmental legislation will result in early termination of the loan and loss of eligibility for the business. Contracts between subborrowers and IFIs will include a declaration by the subborrower that is in compliance with applicable environmental legislation. As part of the processes discussed in paragraphs 3.9 to 3.11, the Bank will review subloans to verify they conform to these provisions and request, if necessary, additional information from the IFIs (see ESMR).

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation mechanisms

1. Borrower and executing agency

3.1 The BCCR will be the borrower. Given its technical and operational capacity and authority, it will also be the executing agency, acting through the Liabilities and Asset Management Division (DGAP). The Financial Operations Department will serve as the program coordination unit (PCU).

2. Execution and management

3.2 The BCCR will: (i) allocate funds to eligible IFIs in accordance with the Credit Regulations and the BCCR special rules for IFI financing; (ii) ensure proper custody and management of the securities and/or receivables provided as guarantees; (iii) perform the functions of supervision and control on the basis of contractual clauses whereby loans to IFIs may only be used for eligible activities; (iv) provide the personnel and technological and budget resources for program execution as duly specified; (v) present to the Bank documentation confirming fulfillment of the disbursement conditions; and (vi) carry out other operational activities essential for program execution. Separate accounts will be established for program execution and administration, and may be converted to an ad hoc vehicle, if necessary.

3.3 The program will be executed in accordance with the Credit Regulations and special BCCR rules governing lines of credit to IFIs. The Credit Regulations will: (i) be consistent with the Bank’s and the BCCR’s standards and policies and with financial legislation and practices in Costa Rica; (ii) stipulate that violation of their provisions will result in denial of access to financing; and (iii) require the Bank's no objection in the event of modification. The main provisions of the Credit Regulations and special rules concerning IFI financing will include:

a. *Eligibility.* The institutions eligible for financing under the program are State commercial banks and private banks subject to supervision by the SUGEF that meet the criteria as to financial condition set out in the Credit Regulations.

b. *Currency and amount.* The lines of credit to IFIs will be denominated in dollars and granted on a first-come first-served basis as program funding is made available. As established in the Credit Regulations, the credit line maximum will be determined on the basis of: (i) an IFI's total obligations;[5] (ii) the total volume of external financing, if applicable; and (iii) a maximum percentage of the total program financing. The financing will count toward the maximum total credit the BCCR may extend to the same IFI based on the most recent financial information submitted to the SUGEF (50% of the IFI’s purchasable assets).

c. *Term.* The program will grant revolving lines of credit to IFIs for a maximum period of five years. Starting in year three, when amortization begins, the existing lines of each IFI will be reduced by a corresponding proportion. Under the program, disbursements will be made to IFIs for a maximum period of two years or for such other duration as established in the Credit Regulations.

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5 The Reglamento sobre Operaciones Especiales para Enfrentar Requierimientos de Liquidez [Regulations concerning Special Operations to Address Liquidity Requirements] issued by the BCCR on 3 November 2008 provide that the maximum line for each IFI will be the equivalent in dollars of 30% of its total demand obligations and 10% of its total term obligations on the last day of the month prior to the credit application.

d. *Interest rate and fees.* The interest rate charged on disbursements to IFIs will be equal to the interest rate on the Bank's line of credit plus a spread to be specified by the BCCR. The payment of interest will be synchronized with BCCR payments to the Bank in order to avoid a maturity mismatch. The BCCR will charge each IFI accessing credit under the program: (i) an initial supervision and inspection fee on the total financing line approved for each IFI; and (ii) a commitment fee on the undisbursed balance of the approved line.

e. *Amortization.* The balance of each disbursement must be repaid at maturity. However, IFIs may prepay all or part of their lines of credit. Recoveries of loans not used within the time specified in the Credit Regulations must be returned to the BCCR. The same will apply to amounts disbursed to IFIs but not loaned to businesses.

f. *Guarantees.* Financing provided under lines approved for IFIs must be guaranteed by first-tier securities issued in United States dollars by the Central Bank, the Costa Rican government, or commercial State banks; United States treasury bills (or treasury bills/bonds of other governments); or dollar-denominated receivables with an A1 or A2 rating by SUGEF. In all cases, the maximum financing so guaranteed will be less (by a spread to be established in the Credit Regulations) than the value of the guarantees, as determined by the DGAP at the time of valuation;[6]

g. *Principal obligations of IFIs*: The IFIs' principal obligations include: (i) requesting the line of credit from the BCCR and signing the respective loan contract; (ii) reviewing and evaluating the activities to be financed, as well as the subborrowers' financial solvency, payment capacity, and guarantees; (iii) transferring funds to the subborrowers in accordance with the terms and conditions of the Credit Regulations and the BCCR special rules; (iv) signing a securities custody agreement for the deposit of guarantees by mutual agreement with the BCCR; (v) assuming all credit risks relating to the subloans; (vi) ensuring that subborrowers use the funds for the purposes declared; and (vii) providing the Bank and the BCCR with any information required concerning the credit portfolio established with program funds;

h. *Noncompliance and penalties.* An IFI's participation in the program will be understood to mean it is familiar with and accepts the applicable laws and regulations and powers of interpretation, and agrees to submit to regulation and control by the BCCR and SUGEF in areas within their purview. Eligible participating IFIs will assume full responsibility for proper processing and execution of operations with their clients. Thus: (i) if an IFI fails to comply

6 For this liquidity facility, the amount of financing guaranteed by securities may not exceed 85% of the value of securities maturing in 360 days or less or 75% of the value of securities with longer maturities. For dollar-denominated receivables, the amount of financing cannot exceed 70% of the outstanding balance, less a percentage determined according to the credit category.

with any of the terms, conditions, or obligations in the Credit Regulations; or (ii) if an IFI or subborrower uses resources in violation of the provided in the Credit Regulations or otherwise fails to comply with established terms and conditions; or (iii) if an IFI fails to provide information or provides inaccurate or incomplete information to obtain resources under this line: (a) the IFI concerned will be suspended from the program and all loans received will become immediately due and payable; (b) the BCCR may debit the amount owed from the IFIs' accounts with the BCCR and execute the guarantees; and (c) in addition to the foregoing, the IFI may be subject to the applicable penalties specified in the BCCR Charter.

3.4 With respect to subborrower financing, eligibility rules and restrictions on use of funds are indicated in paragraph 2.4 above and the Credit Regulations.

3. Disbursement and execution mechanisms

3.5 The program will not require a plan of operations (per se) or a procurement plan, since the outputs will be the second-tier lines of credit opened and maintained with the BCCR.

3.6 The execution period will be 12 months as will the disbursement period.[7] As conditions precedent to the first disbursement, the executing agency must present to the Bank for its no objection evidence that the Credit Regulations, and the BCCR's special rules governing IFI lines of credit are in effect.

3.7 Once the program has met those conditions, (i) it will be declared eligible; (ii) expenses incurred since 20 October 2008 will be recognized retroactively to a maximum of 25% of the program amount; and (iii) a revolving fund of up to 10% of the total program amount will be set up.

3.8 Subsequent disbursements will be made through the revolving fund or from reimbursements received. The disbursements/reimbursements will be processed as quickly as the IFIs request them. As a condition precedent to successive disbursements to the revolving fund or reimbursements, as the case may be, the executing agency will provide the Bank with a list of subborrowers and corresponding subloans certified by each IFI's internal audit department. Link: execution

B. Summary of outcomes monitoring provisions

3.9 The program will comply with the general monitoring and evaluation procedures established by the Bank. In particular: (i) the BCCR, at the Bank's request, will present quarterly progress reports for the duration of the program; (ii) disbursements will be reviewed ex post; and (iii) the Bank, in cooperation with the PCU, will schedule inspections of the IFIs to verify compliance with program contractual conditions. To this end, technical consulting services may be hired as

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[7] This period may be automatically extended for a further 12 months if during the first 12 months 70% of the financing has been disbursed, or otherwise by agreement between the parties.

necessary, to assist the BCCR with program audits and to verify the eligibility of the subloans.

3.10 The program-financed audits will be performed: (i) within 120 days after the end of the fiscal period for the duration of the program; and (ii) by the BCCR internal audit department according to the terms of referenced agreed with the Bank.[8]

3.11 The Bank will carry out two external evaluations: the first 18 months after signature of the loan contract, and the final evaluation 48 months after signature of the loan contract. The evaluations will assess the extent to which program objectives have been accomplished and their impact according to the indicators in the Results Matrix and Table of Indicators (Goal).

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[8] On the basis that: (i) the Internal Audit Department works independently from BCCR Administration and reports directly to the board of directors; and (ii) the Auditor General of the Republic verifies that the internal audits of entities and bodies under its institutional jurisdiction perform fully the functions specified in its governing regulations

RESULTS MATRIX
COSTA RICA: LIQUIDITY PROGRAM FOR GROWTH SUSTAINABILITY IN COSTA RICA (CR-L1033)

Objective of the operation	Increase liquidity in the Costa Rican financial system, thereby providing financing to strengthen export sector competitiveness.
Purpose of the operation	Channel credit in foreign exchange to the productive sector through intermediary financial institutions (IFIs) in order to mitigate the consequences of the global financial crisis.

INDICATORS[1]						**DESCRIPTION**
	Base-line	**Year 1**	**Year 2**	**Year 3**	**Target**	
COMPONENT I: BCCR opens lines of credit for IFIs.						
Output						
IFIs have the opportunity to access financing facilities with IDB funding.	0	Up to 100%	Up to 100%	Up to 100%	Up to 100%	This percentage represents the BCCR's theoretical capacity to lend program funds (if there is market demand for the funds).
PURPOSE: The productive sector obtains funds provided to mitigate the effects of the global financial crisis.						
Intermediate outcome						
	Base-line	**Year 1**	**Year 2**	**Year 3**	**Target**	
IFIs apply to the BCCR for financing to access program funds (according to market conditions).	0	Up to 100%	Up to 100%	Up to 100%	Up to 100%	The BCCR allocates lines of credit to IFIS based on the criteria and limits established in the program Credit Regulations.
Final outcome						
IFIs with access to BCCR financing obtain program funds.	0	Up to 100%	Up to 100%	Up to 100%	Up to 100%	Level of program financing absorbed by existing demand. This percentage represents cumulative lending as a proportion of total IDB financing. This financing will be immediately used for eligible financing to the productive sector of the export chain.

[1] In this operation, as in any multisector credit program, the IFIs will select the most viable enterprises and projects, and therefore the projects' impacts will be determined by market conditions. Accordingly, the proposed indicators are only an estimate of what the market could achieve.

In order to provide additional information to quantify the operation's impact, an ex post evaluation will be conducted based on the following indicators:

Table of Indicators (Goal)

INDICATORS	**Year 1**	**Year 2**	**Year 3**	**Description**
Level of Program Activity				This indicator will reflect: (i) the number of subloans made by the IFIs; (ii) the total amount of subloans made by the IFIs; and (iii) the number of program beneficiary enterprises.
Evolution of subloan portfolio of IFIs participating in program compared to trends in equivalent financial system portfolio.				The program is intended to alleviate the shortage of short-term financing facilities. This indicator is intended to show whether the program is strengthening the IFI's capacity to provide short-term financing to the productive sector in light of current market conditions, considering that the portfolio of credit for working capital and trade financing may be affected by various factors exogenous to the program. This variable will be calculated as the percentage change in the proportion of eligible loans in the total portfolio of participating IFIs to the change in the relative weight of this portfolio for the banking system as a whole.[2]
Proportion of system represented by IFIs participating in the program.				This indicator shows the ratio of total assets of participating IFIs to total assets in the national banking system.

[2] The Superintendency of Financial Institutions (SUGEF) receives the balance sheets of supervised financial institutions and publishes them monthly. This indicator was calculated using those sources. If details for all types of eligible credits are not available, the indicator will be approximated using the account "Activo Productivo por Actividad de Servicios: Garantías otorgadas y Cartas de Crédito" [Productive Assets by Service Activity: Guarantees Provided and Letters of Credit], and is posted on the SUGEF website.