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Costa Rica's Free Trade Victory

CAFTA's main effect will be to change Costa Rica's business environment, which needs urgent improvements.

BY JERRY HAAR

Costa Rican supporters of free trade dodged a bullet on October 7th as slightly more than half of the voters in a national referendum responded “yes” on whether to join DR-CAFTA trade agreement. The results of the Costa Rican vote were surprising, as opinion polls had predicted an easy defeat for the anti-pact coalition.

Critics of the pact comprised the usual suspects in the anti-trade coalition: labor unions, leftists, nationalists, populists, NGOs, subsidized farmers and protected small businesses. The principal objections of DR-CAFTA opponents are the requirements that Costa Rica open its telecom, services and agricultural sectors to greater competition.

TELECOM AND AGRICULTURE

While DR-CAFTA would require competition in telecom and services, it would not privatize ICE, the government telecom carrier, but simply open the sector to competition. The inefficient, high cost, low quality state monopoly adversely affects consumers and businesses. In El Salvador, a nation with half the income of Costa Rica, nearly twice as many citizens own a mobile phone; and competition is fierce. As for agriculture, a University of California at Davis study found that the welfare of the rural poor will actually improve under DR-CAFTA. The accord grants duty-free access to all agricultural exports from Costa Rica, protecting that nation’s rice farmers (who produce only half of domestic needs) with a 20-year phase out of tariffs, and excludes from tariffs altogether onions and potatoes—the principal crops of Costa Rica’s poorest farmers.

One of the biggest winners for Costa Rica will be textiles and apparel—industries subjected to ferocious international competition from China and other Asian nations. Nearly all textile and apparel goods that meet the agreement’s rules of origin will be duty-free and quota-free immediately, promoting new opportunities for U.S. and regional fiber, yarn, fabric, and apparel manufacturing.

In addition to spurring job growth—an impact experienced by all other countries that have implemented DR-CAFTA—the accord will, to quote a White House press statement, “expand Costa Rica's access to the U.S. market, safeguard that access under international law, attract U.S. and other investment and link Costa Rica to some of the most dynamic economies of our hemisphere."

IMPROVING BUSINESS ENVIRONMENT

Ironically, the most critical element to the success of any free trade agreement has been absent from Costa Rica’s internal debate over DRCAFTA—namely, business environment. Without fair, efficient, transparent, and market-enabling conditions that facilitate the creation, operation, and expansion of business, no country can reap the full benefits of trade liberalization.

It is here where Costa Rica faces the most urgent challenge and unilateral opportunity to institute sweeping reforms.

While Costa Rica prides itself on its eco-tourism, retirement haven for foreigners, coffee and bananas, and Intel plant, the truth is that the country lacks a competitive business environment. The World Bank's authoritative, Doing Business 2008 report ranks Costa Rica 115 out of 178 countries. The country has the worst business environment of any DR-CAFTA nation except Honduras which it edged out only slightly; and worldwide ranks behind Bangladesh, Yemen, and Ethiopia.

In the global rankings of investor protection, Costa Rica comes in at 158, tax burden 162, starting a business 130, and closing a business 104--worse than Sub-Saharan Africa. On other measures, too, Costa does not fare well. For example, Costa Rica's public infrastructure has suffered from a lack of maintenance and new investment and is worse in a number of key transit points than that of some of its poorer regional neighbors. This situation impedes efficiency in logistics and supply chain management not only for the export and import of international trade but for intra-country commerce as well.

NOT AS TRADE-FRIENDLY

Additionally, Costa Rica is not as “trade-friendly,” as commonly believed. U.S. exporters complain of lost earnings and unforeseen costs from delayed entry of products into the country due to burdensome importlicensing requirements and arcane and lengthy testing and registration rules governing foods, chemicals, agricultural and pharmaceutical goods. Other impediments include inadequate intellectual property protection and unfair practices in the bidding and awarding of government contracts. Investors are locked out of Costa Rica's insurance, telecommunications, electricity distribution, petroleum distribution, potable water, sewage, and railroad transportation industries--all state monopolies. All of these practices are incompatible with free trade, in general, and DR-CAFTA specifically.

For Costa Rica to compete in the 21st century it must shun the archaic vestiges of the mid-20th century nanny-state, reform its public institutions to unleash private enterprise, and join its regional neighbors in fully embracing DR-CAFTA and the opportunities that globalization presents to improve the lives of ordinary citizens.

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