



# en breve



November 2003 No. 35

A regular series of notes highlighting recent lessons emerging from the operational and analytical program of the World Bank's Latin America and Caribbean Region

## COSTA RICA SOCIAL SPENDING AND THE POOR

*Helena Ribe and Roxana Víquez<sup>1</sup>*

Costa Rica has made substantial progress in reducing poverty and improving social sector indicators over the past decade. Headcount poverty declined from 27 percent in 1990 to 21 percent in 2000, and there is near universal access to healthcare and primary education. Life expectancy has risen, while infant mortality rates have fallen. However, there are also worrying signs that progress in these areas is stalling, and that future improvements may be harder to achieve. The pace of reduction in income poverty slowed during the second half of the nineties, and between 1990 and 2000, Costa Rica fell from 28th to 48th in the Index of Human Development. In education, there has been an increase in the gross enrollment rate to 61.2% of the population, although there was also an increase in repetition rates. Across the board, education levels are worse for those in the lower income quintiles. In health, performance continues to improve in terms of life expectancy, infant mortality and health systems performance, but there is increasing dissatisfaction with the system, as waiting lists grow, and patients requiring more sophisticated treatment for chronic diseases are turned away. In Social Protection, Costa Rica has a well-established social assistance network to protect vulnerable groups, but it does not adequately reach the very poor.

Costa Rica is not likely to be able to rely on favorable economic conditions to reverse these trends. Macroeconomic projections do not show signs of the consistent growth that characterized the past ten years, and which allowed the government to continue increasing investment in the social sectors. Relative to GDP, Costa Rica already spends more on social services overall than other countries in Latin America, and considerably more than the average for other countries at similar stages of development outside the region. More-

over, fiscal pressures will not only limit the government's ability to increase social spending, but could also act as a drag on real growth prospects for the economy as a whole (see Table 1). This underscores a key finding of the report: that social sector challenges can not be resolved only through the allocation of more resources, but that they will require reforms which improve management and efficiency in the use of available resources. New instruments and approaches will be required that

**Table 1 - Costa Rica - Key Economic Indicators , 1990-2000**

Indicators	1990	1996	1997	1998	1999	2000
GNP growth (%)	3.5	0.9	5.6	8.4	8.2	2.2
Inflation (% , CPI final period)	27.2	13.9	11.2	12.4	10.1	11
Unemployment (%)	4.6	6.2	5.7	5.6	6	6
Public Sector Balance (% of GDP)	-2	-4.1	-2.6	-2	-3.6	-3.7
Current Account Deficit (% of GDP)	-7.4	-3.8	-4.9	-5.3	-3.1	-3.1
Foreign Direct Investment (% de GDP)	---	0.04	0.03	0.04	0.04	0.03
Domestic Public Debt (% of GDP)	18.3	24.5	23.1	21.8	25.1	23.2

focus on obtaining value for money in the social programs.

There are three key questions which frame the analysis of these factors in the new World Bank report, "Poverty and Social Spending in Costa Rica". First, **who are the poor and vulnerable groups in Costa Rica?** The report addresses this by providing an in-depth, multi-dimensional analysis of poverty. Over 65 percent of the poor in Costa Rica reside in rural areas, although only 49% of the total population live there. Poverty incidence is highest in families where the head of household is working in agriculture, or self-employment, micro enterprise or domestic service, or is under- or unemployed. Poor families are younger, have higher dependency rates and most have no or only one income earner. Poor families are larger than non-poor families (4.7 family members vs. 3.7 for non-poor) and have a higher number of people below 12 years of age (1.7 vs. 0.9). Women head an estimated 48 percent of families in extreme poverty compared to 33 percent in near-poor families. One of

<sup>1</sup> Full report prepared by Tarsicio Castañeda, James Cercone, Luisa Fernández, Fabio Durán, Rodrigo Briceño, Stephan Brunner, Juan

the most striking facts regarding extremely poor families is the very high unemployment rate for all family members. The extreme poor and poor, when occupied, work primarily in temporary activities, while the near-poor work primarily in permanent activities. Furthermore, 16 percent of the income-poor families in Costa Rica have no income earner in the family. Education levels are much lower for the population in the lowest income quartile group. Health conditions also vary considerably between the non-poor and the poor, and despite a universal health system, roughly 30 percent of poor have trouble accessing programs (the Caja Costarricense de Seguro Social (CCSS)) for the uninsured.

	Education (%)	Health (%)	Pensions and Social Assistance (%)	Housing (%)	Total (%)
Argentina	3.5	1.8	8	0.8	14.1
Bolivia	7.4	2.2	4.5	0.2	14.3
Brazil	3	1.7	11	0.6	16.2
Chile	3.2	2.5	7.1	1.2	14
Colombia	5.4	2	4.9	0.7	13
Costa Rica	5.1	6.8	6.3	0.1	18.2
Dominican Republic	2	1.7	0.7	2.1	6.5
Indonesia	1.3	0.4	1.1	3	5.7
Korea	3.7	0.2	2.2	0.5	6.5
Malaysia	5	1.4	1.5	1.4	9.3
Mexico	3.8	0.5	3	0.5	7.8
Panama	4.6	5.6	5.7	1.2	17.1
Philippines	3.4	0.5	0.5	0.3	4.7
Turkey	3.5	0.7	1.4	0.4	5.1
Uruguay	2.1	1.9	19.4	0.5	23.9
Latin America <sup>1</sup>	4	2.7	7.1	0.8	14.5
East Asia	1	3.4	0.6	1.3	6.6

Note: Percentage of GDP.  
1. These figures only include countries in the table.  
Source: World Bank, 2000b, based on the IMF Government Finance Statistics Yearbook (1998)

Two groups appear particularly vulnerable. About 84,000 children aged between 0 and 5 (95% of the poor group) are not attending CEN-CINAI or Hogares Comunitarios centers. Similarly, those over 65 years of age living in extreme poverty can also be considered highly vulnerable because of their ill health and low incomes. About 46 percent of extremely poor people older than 65 years of age reported permanent or temporary physical or mental limitation with about 14,000 elderly of them (about 50 percent) not being covered by contributory or assistance pensions.

The second key question is: **what has been the impact of social spending on programs that aim to improve the welfare for the poor?** The report addresses this by examining the effectiveness of government policies and spending in the social sectors on the poor. During the 1990's, Costa Rica made impressive progress in making social spending a priority and increasing the allocations to priority programs. As a result, the main indicators improved significantly. Coverage of primary and secondary education improved substantially and illiteracy dropped to only 5 percent of the population over 12 years of age. Life expectancy at birth is above 76 years, the infant mortality rate dropped from 15 to 13 for every thousand live births (10.3 in 2001) and access to drinking water is practically 100 percent.

**Despite these accomplishments, the analysis indicates that the national averages hide discrepancies between the income levels and that Costa Rica's performance in key areas lags considerably behind comparator countries in the Region** (see Table 2). In some areas, notably health care, Costa Rica's striking performance is comparable

to that in some OECD countries. However, in other areas, such as secondary education, progress has been uneven. In primary education, despite high levels of absolute coverage, there have been increases in repetition and drop-out rates. Although access to services for poor groups has improved considerably, a lack of effective targeting mechanisms reduces the cost-effectiveness of social programs. For example, the share of social assistance programs resources received by the poorest 25 percent of the population just approximates their share in the population, implying little or no re-distributive impact of spending. More spending alone will not solve these problems.

Finally, given these problem areas, and the limited capacity to increase public expenditures on social services, we ask: **how can government spending be used more effectively to reach the poor and to contribute to reducing headcount poverty?** While the objective of the report was not to prescribe solutions, it provides both sector-specific and general policy options that the government can consider. A common theme in the sector specific recommendations is the need for greater flexibility in the implementation of existing programs, coupled with more efficient coordination and administration to improve targeting and respond to the needs of the poor. For example, one of the key channels for the provision of social assistance (FODESAF) is obliged to allocate funds to low priority spending under outdated legislation. More generally, the report advocates the creation of a policy-making mechanism—charged with setting social policy, evaluating the costs, benefits and impact of social programs, exploiting synergies, and reducing programs overlaps. The government should consider possibili-

ties for improving coordination of social policies, define priorities and regularly evaluate the impact and targeting of social programs.

## The Road Ahead: Policy Suggestions

### Education

Some of the actions recommended for primary education include the following: (i) strengthening the teaching and learning of reading, writing and math skills in first through sixth grades; (ii) making more effective use of learning assessment findings; (iii) improving in-service teacher training; and (iv) strengthening community and parental participation in school-related matters.

To ensure efficient use of available resources, the following structural changes should be sought: (i) update the curricula; (ii) improve teacher training; (iii) increase the supply of secondary education through several options that include traditional schools *tele-secundarias*, distance learning, open-access education, virtual schools and vocational training; (iv) promote collaboration with the private sector to improve the relevance of secondary education; and (v) help parents and students, especially in rural areas, to finance part of the opportunity costs of studying through scholarships, conditional cash transfers, and other supplemental financing schemes.

During the past five years, less progress has been made among the poor than in higher-income groups. For this reason, and in addition to the coverage and quality improvement efforts described above, the Ministry of Education should aim to improve the targeting and equity of school food programs, transportation and scholarships.

The cost implications of the actions recommended for primary and secondary education are relatively modest when compared to the resources currently allocated to education. Overall, it is estimated that the efforts suggested will increase costs in the order of 6 to 7 percent of current expenditures. This cost increase could be financed through internal efficiency improvements, for instance by reducing grade repetition rates and poorly targeted programs that provide resources to less needy populations. General estimates suggest that the costs involved in primary grade repetition amount to approximately US\$21.2 million/year, about 10% of the budget for primary education; the costs involved in secondary repetition rates are of about US\$14.8 million/year.

### Health

Costa Rica needs to continue with the reform process launched in the mid 90's in order to cut inefficiencies and im-

prove services. This includes, (i) consolidating the Ministry of Health's role as steward and policy maker and strengthening health education and public health programs; (ii) consolidating the Basic Teams for Integrated Health Care (EBAIS) model and improving access in order to reach the 12 percent of the population that are still not covered; (iii) improving administrative and budgeting procedures in the CCSS, and promote a culture of performance agreements with hospitals and other health care providers, in order to increase coverage of primary health care and improve overall system efficiency; (iv) promoting changes in the system in order to improve the financial and management autonomy of the health care providers, under the 1999 Deconcentration Act; (v) reducing current disparities in expenditures levels by region; (vi) introduce changes in the drug procurement systems to cut down storage and purchase costs; (vii) strengthening the CCSS's collection system and promoting changes in financial information systems; and finally (viii) establish alternative service arrangements through public-private partnerships that complement the public services supplied by the CCSS, to gradually introduce managed competition in the health care market.



The **cost implications** of the continued reform process have been estimated at about US\$70 million over five years, but these costs are about half the savings that can be obtained from the reforms over the same period. The Costa Rica Health Sector Strengthening and Modernization Project will produce substantial savings for the sector, primarily through reductions in hospitalization costs resulting from ambulatory surgery (\$12 million per year), pharmaceutical management, and reduced overhead from increasing decentralization (\$12 million per year). Improvements in pharmaceutical supply chain management alone could save over \$30

million per year by reducing unnecessary inventory costs. Even under conservative assumptions regarding the effectiveness and speed of change, direct benefits would exceed \$24 million per year.

### Social Protection

**Pensions.** The country still faces major challenges going forward: (i) to reduce replacement rates and future costs of the public scheme and introduce incentives that increase contributions in the early years of the earnings cycle, in order to get them to an affordable level and to guarantee their financial sustainability; (ii) to expand coverage, improve the membership management and the control of contributions; (iii) to increase coverage and improve targeting of non-contributory pensions, and (iv) to strengthen the reforms that will guarantee the long-term sustainability of pension schemes for civil servants. If reforms are not undertaken, as the population ages sharply over the next 30

years—due to falling fertility rates and rising life expectancy—the increasing financial imbalance could lead to pension fund insolvency.

In social assistance, the spending priorities require urgent reform. Priority measures involve the following three areas: (i) changing legislation (the FODESAF law) to permit government to vary spending priorities in accordance with needs, and to allow the allocation of more resources to vulnerable groups, and be able to respond to crises; (ii) improving the coordination among programs to prevent duplications; (iii) improving the targeting, coverage and design of social assistance programs such as CEN-CINAI; and (iv) completing the coverage for poorer groups through non-contributory pension schemes.

The cost implications of expanding pre-school education programs for poor children and non-contributory pensions for the poor elderly are also relatively low and may be covered within the existing social assistance budget. As estimated, expanding pre-school coverage to all children through care programs offered by centers and parents-community would amount to approximately US\$26 million per year. The current annual budget for the CEN-CINAI program is around US\$19 million and an additional US\$11 million would be required to cover all poor children. These are general estimates based on the assumption that non-poor children will not benefit from public programs. Costs could be cut even further if the CEN-CINAI programs are modified to reduce food and health care subsidies provided by the CCSS. If the programs were to reach the 7,000 poor elderly that are still not covered, total annual costs would amount to US\$3.1 million, which could be paid with the resources currently used to benefit non-poor pensioners.

### ***Improving Institutional Coordination***

The impact of social spending in Costa Rica could be improved, particularly its impact on the poor, with the creation of a policy-making mechanism charged with setting social policy, exploiting synergies, and reducing program overlaps. The government should consider possibilities for improving coordination of social policies by exploring the creation of a Council for Social Policy Coordination under the direction of the President, with a technical secretariat to define priorities and regularly evaluate the impact and targeting of social programs. Such an entity would define programs and their goals, beneficiary populations, and the institutional arrangements to carry out key strategies. Efforts in this direction have been undertaken in recent administrations, but they have been hampered by institutional rigidities and laws which have undermined coordination efforts and the reform or elimination of ineffective programs or institutions. In this regard, allowing FODESAF greater flexibility to channel resources to vulnerable groups and to respond to changing conditions, particularly during crisis, will greatly contribute to improving the effectiveness of social spending.

## **Strengthening, monitoring and evaluation systems**

The lack of an effective monitoring and evaluation systems system for the social sectors is an impediment to ensuring value for money in social spending. This is most evident in programs such as the CEN-CINAI where—had a good evaluation program existed—resources could have been saved by finding the most cost effective alternative for child care. Different modalities of child care, some including only parental education, others—including center-based stimulation and early child education—could have been evaluated to determine their impacts and relative costs. Monitoring and evaluation is key to evaluate progress, evaluate impact of programs and make more efficient decisions on programs to improve social indicators of the poor. The practice of establishing base-lines and measuring the impact of specific programs should be implemented routinely in order to draw lessons from experience—which can be used to modify programs and improve their impact. In addition, instruments such as Living Standards and Measurement Surveys and improved household surveys provide valuable information on key target groups and on the outcomes of the main social programs, complementing the annual household surveys currently carried out by the Statistical Institute. At the same time, evaluation should include ex-ante and ex-post evaluation of social sector programs using cost-effectiveness and cost-benefit analysis to assess programs.

The collective impact of the actions presented in the report would contribute to progressive improvements in the impact of social spending and to ensuring that poverty reduction is not tied exclusively to rapid economic growth. Clearly, improvements should focus on how to improve the impact of existing resources and ensuring that additional resources that may be allocated to the social sectors are disproportionately targeted to the poor.

## **About the Author**

Helena Ribe is a Sector Leader within the Human Development Department of the Latin America and Caribbean Region, based in Washington D.C. Roxane Viquez is the ex-President of IMAS in Costa Rica.

## **Want to Know More?**

The report “Social Spending in Costa Rica” starts with a profile of the poor. Poor families tend to be younger, larger and have higher dependency rates than non-poor families, with most having no, or only one, income earner. On average, they are disproportionately rural and headed by women. The poor benefit less from educational opportunities, and may have trouble accessing healthcare. The report provides both sector-specific and general policy options to improve the impact of social spending and to ensure that poverty reduction is not tied exclusively to rapid economic growth. Clearly, improvements should focus on how to improve the impact of existing resources and ensure that any additional resources that may be allocated to the social sectors are effectively targeted at the poor. Download the report from <http://www.worldbank.org/CR>