

COUNTRY REPORT COSTA RICA 2008

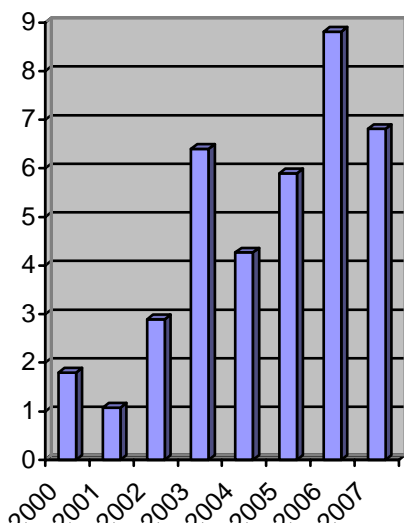
Costa Rica is located in the Central American isthmus, bordering both the Caribbean Sea and the North Pacific Ocean, between Nicaragua and Panama. The country's total area is 55,400 sq Km (roughly 21,390 sq miles) and its topography is mostly mountainous with alternating lowlands throughout its coastlines.

Costa Rica has a population of 4,509,000 with an alphabetization index of 95%, a life expectancy of nearly 79 years and a per capita GDP of US\$5,695.

Economic Development

Economic Activities: Notwithstanding an economic slowdown in the last year, Costa Rica has enjoyed steep economic growth for the three previous years.

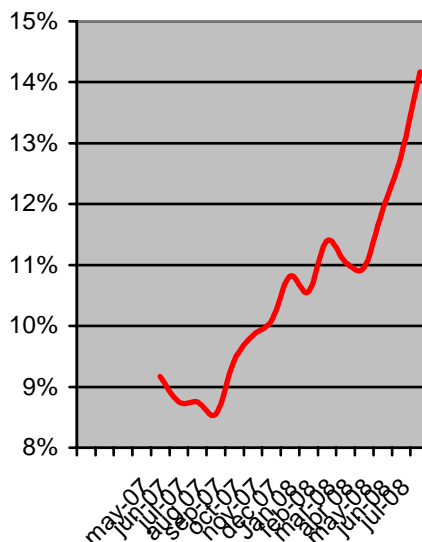
COSTA RICA: Economic growth (%)



In 2007, the country grew at 6.80%, exceeding the average growth rate for the previous years, but two points less from the 8.80% rate in 2006.

The country's Monthly Index of Economic Activity (IMAE, Spanish acronym), at 4.20% in May 2008, evidences the impact the global economic slowdown has had in the last year.

COSTA RICA: Interannual Inflation

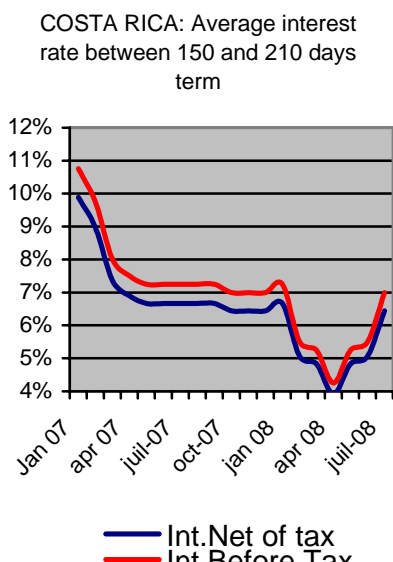


Economic Growth Expectancy: The GDP is expected to grow between 3.30% and 4.1% by the end of 2008.

Prices: Like most other countries, in 2008, Costa Rica has faced inflationary pressures from the rising prices of oil and food. The inter-annual inflation rate reached 14.17% in July 2008.

Unemployment: In 2007, unemployment went down to 4.60% from 6.00% in 2006 and 6.60% in 2005. The growth of the "Business" sector has surpassed 7.00% in the previous two years, which, in part, contributes to reduce unemployment.

Interest Rates: In July 2008, Costa Rica started to adjust raising interest rates after two years of negative real interest rates, which implies a more restrictive economic policy than in previous years.



Expected Interest Rates: In spite of current negative real interest rates, a gradual adjustment of nominal rates is expected so that positive real interest rates may be reached in the second half of 2009.

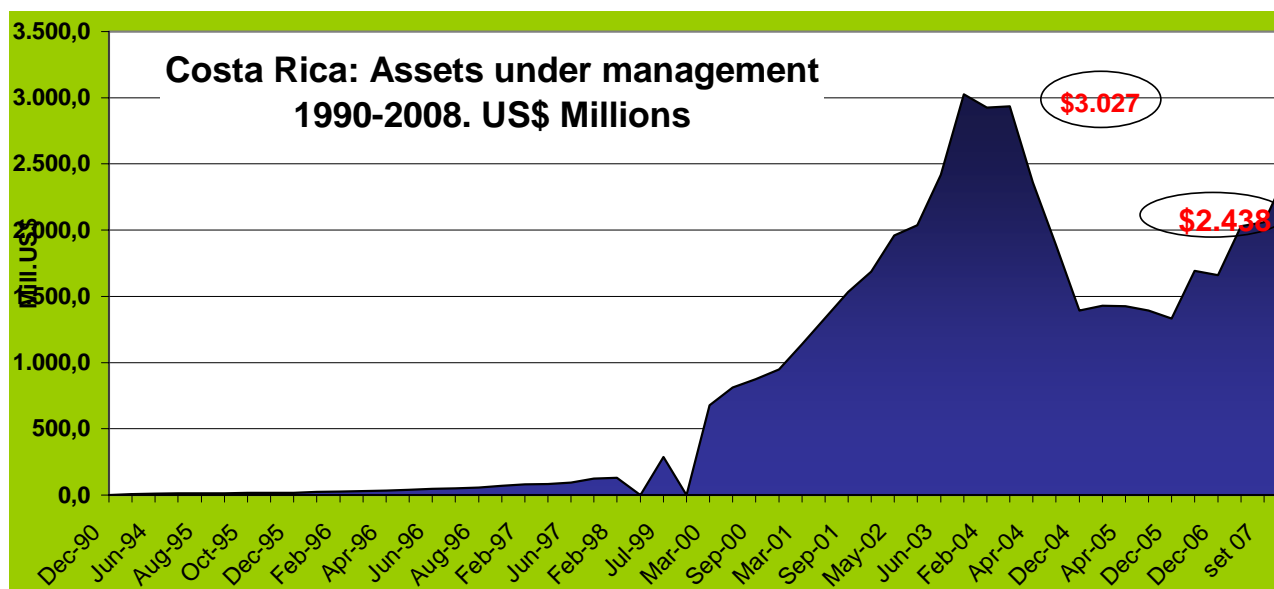
Exchange Rates: Two years ago, Costa Rica implemented an exchange rate band regime. Currently, the upper bound is at ₡556.21 (Costa Rican colones) per US\$ and the lower bound is at ₡500.00 per US\$, which implies an 11.24% difference.

Costa Rica: Economic projections 2008-2009			
	Real	Estimated	
	2007	2008	2009
Change			
GDP real	7,30%	3,30%	4,00%
GDP nominal	17,70%	17,10%	17,00%
Inflation			
Consumer price index	10,80%	14,20%	8%-10%
Balance of payment (% of GDP)			
Current Account	-6,00%	-8,00%	-6,80%
Commercial Account	-13,80%	-17,20%	-16,20%
Monetary data (change %)			
Total liquidity	18,80%	11,50%	17,60%
Private sector credit	41,80%	19,60%	17,70%

Investment Funds in Costa Rica

Background

Investment funds were first introduced in Costa Rica through the 1990 Stock Exchange Regulatory Law. However, they did not really become mainstream until this law was amended in 1998. At first, some independent or non-bank fund operators offered mostly Money Market short-term funds. Later, fixed-income and growth funds were also set forth.



After the 1998 law, the investment fund market became attractive to many banking groups, who multiplied distribution channels, introduced new financial products and developed new non-financial products, such as real-estate funds (1999)¹, mortgage funds², international portfolio funds and, more recently, funds of funds (mega funds) and real-estate development funds³.

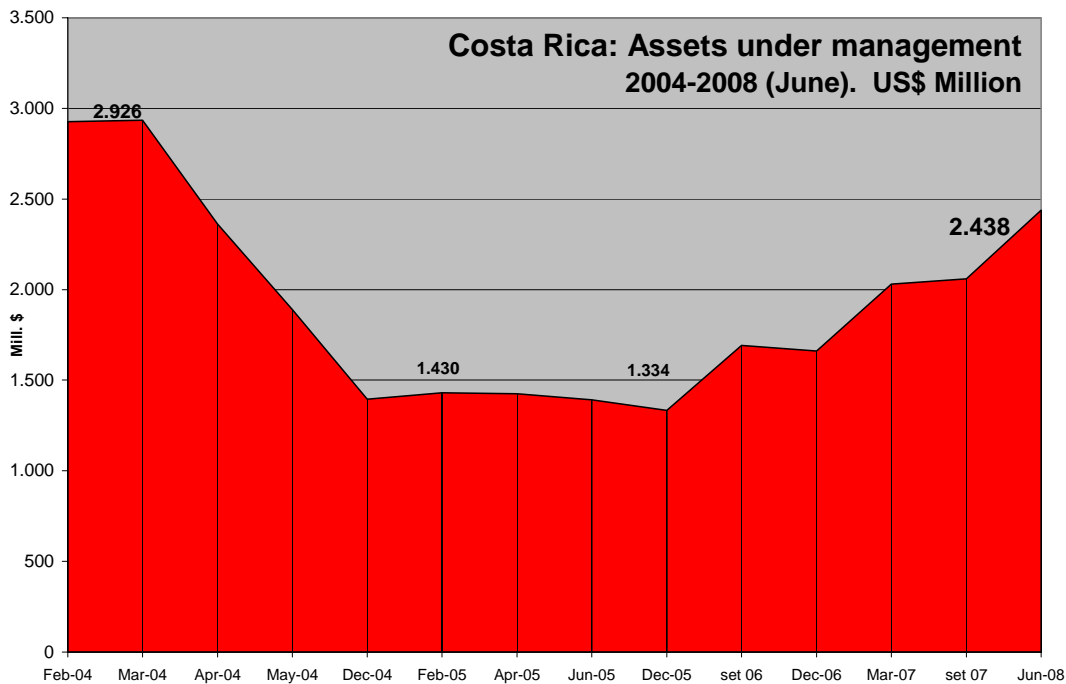
In short, we can identify three general periods:

- 1. 1990-1998:** Non-bank fund operators offering financial short-term and high liquidity hedge funds. Low volume of assets under management.
- 2. 1998-2004:** Banks and Brokerage Firms start operating funds, which expands the representation of the financial sector in the market. In this period, the industry experiments steep growth (more than US\$3,000 million) focusing on long-term products (fixed-income and growth funds) and some innovations, such as mutual, real-estate and mortgage funds.

¹ Real Estate Income Funds, invest directly in acquisition of building, which produce monthly rentals for the fund. They use to distribute the net income among investors. Shares of the fund can be traded in secondary market of the stock exchange.

² Mortgage Income Funds, invest in secondary market bank mortgages. They use to distribute the net income among investors. Shares of the fund can be traded in secondary market of the stock exchange.

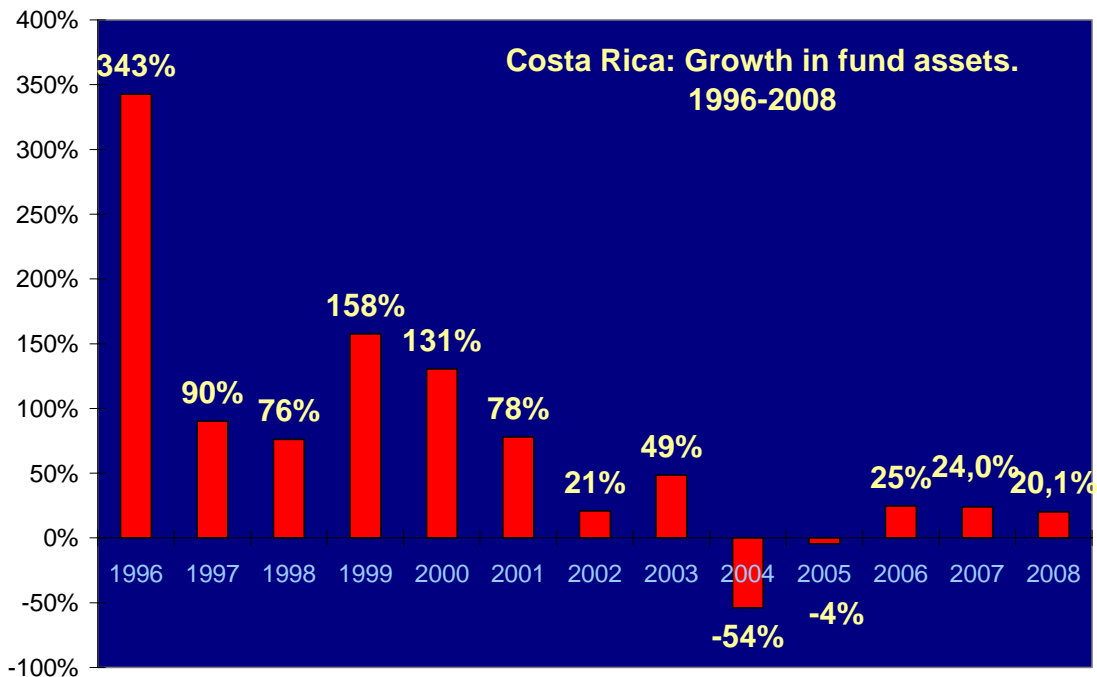
³ Real Estate Development Funds, invest in real estate construction projects. Once the building, or any other kind of real estate is constructed, it is sold or rented. Capital gain from sale, or net income from rent, is distributed among investors. Shares of the fund can be traded in secondary market of the stock exchange.



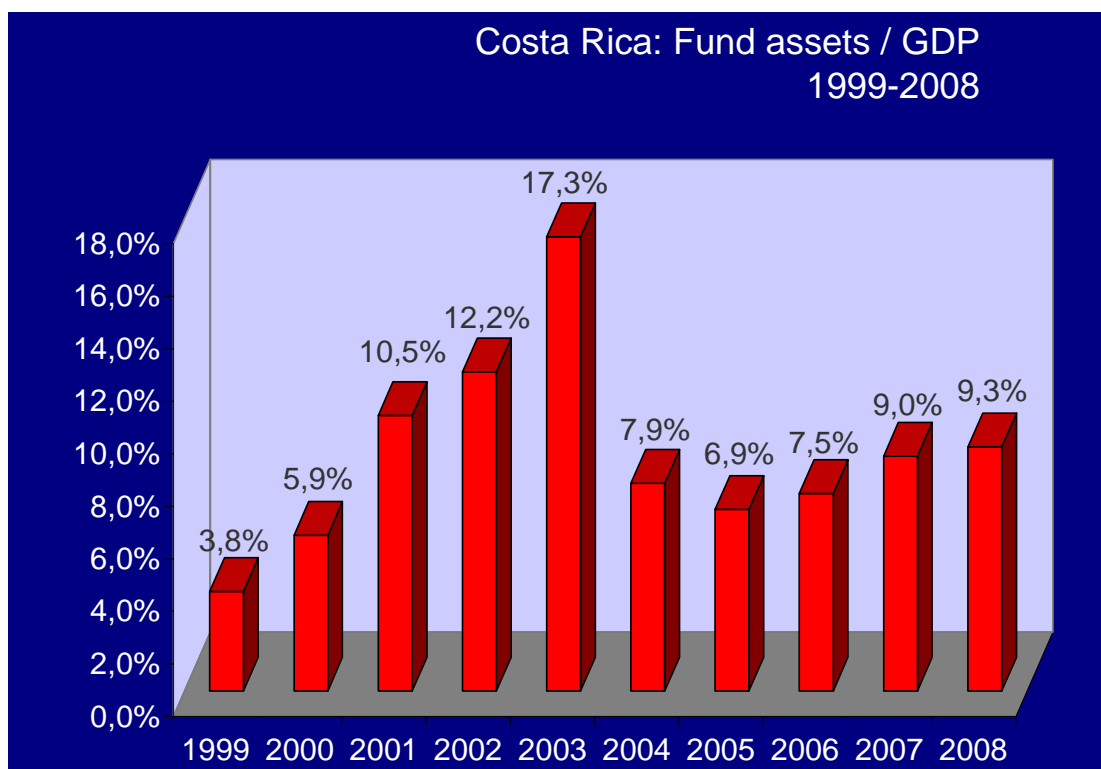
3. 2004-2008: In the first part of this period (2004-2005), the number of assets under management was significantly reduced, but the industry recovered shortly afterwards. At its most critical, there were only US\$1,334 millions in assets under management, when, in June 2008, the current assets under management amount to US\$2,438 millions. In the last year (2007-2008), the market has been boosted by greater portfolio diversification and increases in real-estate, real-estate development and foreign investment funds of funds (mega hedge funds).

Recent developments for the Investment Fund industry

In the 2007-2008 period, assets under management have increased 20.1% to amount to US\$ 2,438 millions. 65% of this amount (US\$1,592 millions) refers to funds in US Dollars, 34% (US\$817.4 millions) to funds in Costa Rican Colones (local currency) and 1% (US\$29.7 millions) to Euros. It is worth noting that Costa Rica issues securities and allows investments in any legal currency and not just in US Dollars, Colones or Euros.



For the aforementioned amount, the ratio between assets under management through investment funds and the GDP is 9.3%. This index has increased in the last three periods, but it still fails to match 2004 levels, when it reached 17.3%.



Regarding the total product offer, there are 124 investment funds distributed among 16 operators and 39,002 investors. Most of the existing funds, both in volume and in assets under management, are open-end: 90 funds and US\$1,467 millions, representing 61.8% of total number of industry assets. There are also 34 closed-end funds, which manage US\$972 millions or 38.2% of all industry assets.

Open-End Funds

Open-End funds are mostly Money Market funds; 44 funds with assets for US\$1,238 millions, representing 51.9% of the investment fund market. In addition, this category groups 22,854 industry customers (51.9% of all investors). Recently, some of these funds have started to accept investments in Euros, which currently manage assets for US\$27.5 millions.

Costa Rica: Investment company industry profile, as of June 30th 2008. Figures in US\$ million.								
Equivalent US\$ million								
Fund category	Assets	%	Funds quantity	Clients	%	CR Colones	US Dollars	Euros
Open end funds	1.467	61,8%	90	30.234	77,5%	769,4	671,5	27,5
GROWTH	83	3,6%	24	3.668	9,4%	35,7	47,8	0,0
INCOME	137	5,9%	20	3.599	9,2%	93,2	44,0	0,0
FUND OF FUNDS	8	0,3%	2	113	0,3%	0,0	8,0	0,0
MONEY MARKET	1.238	51,9%	44	22.854	58,6%	640,4	571,7	27,5
Closed end funds	972	38,2%	34	8.788	22,5%	48,1	920,3	2,2
GROWTH	36	1,6%	3	683	1,8%	0,0	32,3	2,2
SECURITIZATION	3	0,1%	1	64	0,2%	0,0	3,3	0,0
REAL ESTATE DEVELOP.	26	0,7%	2	111	0,3%	0,0	26,1	0,0
INCOME	130	5,4%	8	1.818	4,7%	35,5	94,6	0,0
REAL ESTATE INCOME	776	30,4%	19	6.110	15,7%	12,6	763,1	0,0
FUND OF FUNDS	1	0,0%	1	2	0,0%	0,0	0,9	0,0
						0,0	0,0	0,0
Total	2.439	100,0%	124	39.022	100,0%	817,4	1.591,8	29,6

Closed-End Funds

The most important of all closed-end funds are Real Estate Income funds, which manage assets for US\$776 millions (30.4% of total funds) in 19 funds. Only one of these funds is in Costa Rican Colones and the rest are in US Dollars. These funds are owned by a total number of 6,100 investors, who basically invest in income-generating real estate.

Industry Profitability

The observed average returns by fund type, in their corresponding investment currency, are detailed below. All returns are nominal, without any inflationary adjustment.

Costa Rica: Average return of Investment Funds For the year terminated on June 30, 2008	
	%
Funds in CR Colones	
Open end	
Growth	5,43
Income	5,05
Money Market	3,59
Close end	
Income	4,73
Real Estate income	7,54
Funds in US Dollars	
Open end	
Growth	3,98
Income	3,56
Fund of funds	-13,90
Money Market	3,23
Close end	
Growth	3,87
Securitization fund	6,77
Real Estate development	-6,73
Income	3,40
Real Estate Income	9,36
Fund of funds	-22,37
Funds in Euros	
Open end	
Money Market	2,94
Close end	
Growth	0,88

Investment Fund Market Analysis

The current rising interest rates, both at a domestic and international level, have contributed to polarize collective savings in two ends. On one side, a defensive liquidity strategy from investors and portfolio managers. On the other, liquidity positions have been abandoned for options allowing greater returns without greater relative volatility.

In Costa Rica, where the fixed income markets have traditionally dominated, the market has diversified towards investments on foreign securities and the real-estate sector. In the latter case, some operators have fostered the creation of real-estate funds which already evidence an effective high-return and low-volatility track record for the previous 9 years. In fact, the effective return average for real-estate funds in US Dollars is 9% for the previous 7 years. However, since this is a closed-end fund with a slow growth level due to the nature of its purchases (real-estate), it has not been able to fully develop its savings potential yet. Still, the demand for these instruments currently exceeds the market offer.

In other words, there is room for new efficient products outside the real-estate sector. Even when small efforts have been made towards foreign investments, these portfolios are yet to reach optimal global diversification levels; they are still not significant enough in terms of currencies and variable returns.

Regarding regulatory compliance, the regulations from the Securities Regulator Authority demand detailed information before, during and after the fund selling process. Besides mandatory contracts and prospectuses, funds must submit customer profiles and anti money-laundering information. In addition, financial and general ledger information must be submitted on a daily, monthly, quarterly and yearly basis for mass media publication. Likewise, all funds are subject to risk assessment in order to provide better guidance to investors.

Recently, the same Authority amended the regulations in order to impose a minimum term of 3 months for every investor in any open end fund different than Money Market Fund. If such an investor redeems its shares in that time period, it must be charged with a minimum of 5% p.a.. The article has raised a great opposition from operators, since it has been pointed as an improper intervention of the Regulator in designing the main characteristics of these funds.

In other hand, market supervision is highly technological as evidenced by constant electronic communication between fund operators and the Regulatory Authority.

Both fund sales representatives and financial portfolio managers are required to become licensed or certified to perform said activities. The local association, the Costa Rican Chamber of Investment Fund Operators, has been licensing applicants and certifying risk analysts since 2006. In September 2008, a new certification for Real-Estate Portfolio Managers will also be issued.

To promote Principal at Risk and Corporate Development Funds, the Chamber collected a significant number of experiences to develop a formal regulatory proposal for consideration in the following amendment to the Investment Fund Regulations, currently under debate as of August 2008.

Perspectives

As aforementioned, some fund operators have recently begun to accept investments in Euros and to operate Real-Estate Development funds. Foreign investments are becoming so popular among fund managers and investors that some Foreign Investment Funds of Funds (Mega Funds) have already been set, which aims at global diversification. No less important are efforts to set forth high-investment funds in multiple currencies and structured notes.