

CANDRIAM 

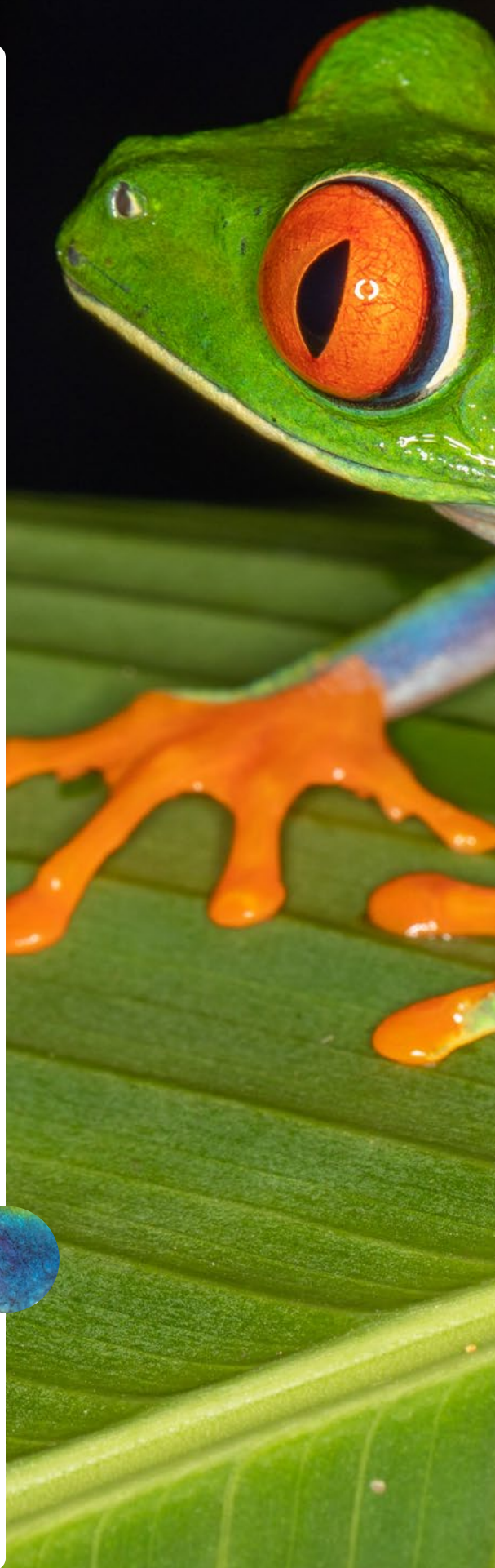
Costa Rica

Active Engagement



MAY 2024

Marketing communication



Costa Rica is a democratic country of five million people which includes ecotourism among its main economic drivers. It has historically been more politically and economically stable than most Latin American nations. Candriam’s proprietary Sovereign Sustainability Model ranks Costa Rica in the top third of all nations.

Yet clouds have appeared in the sky. In February of 2023, Costa Rica was added to the EU List of Non-cooperative Jurisdictions for Tax Purposes.¹ For investors, this should suggest at least a review of governance assumptions of the sovereign issuer. Direct dialogue with the issuer, so frequent with corporate equity issuers, is a relatively rare path for investors in sovereigns to take.



¹. European Council, 14 February 2023, press release. [added to EU list of non-cooperative jurisdictions for tax purposes \(europa.eu\)](https://europa.eu/european-council/story/2023/02/14/eu-list-non-cooperative-jurisdictions-tax-purposes) Accessed 22 April, 2024.

The topic.

Costa Rica was included in the EU List of Non-cooperative Jurisdictions for Tax Purposes² in February, 2023³, for failing to abolish or amend the harmful aspects of its foreign source income exemption regime. Put another way, some taxpayers found Costa Rica attractive for its 'exceptional tax privacy'.

The addition to the EU List has material financial and non-financial consequences for a sovereign issuer. How can a responsible investor – especially one based in Europe – hold securities of an issuer on an EU 'watch list'?

Our first priority is to protect the interests of our clients. A rapid sale would depress the value of our clients' assets. Bonds are not as liquid as equities, especially those in emerging markets. Conversely, this negative development increased the risk, which could also depress the value of the holdings. The lack of cooperation with other nations can negatively affect the nation's financial situation, can delay foreign direct investment into the country, and have other effects which can damage the economy of the country on the list. Some existing investors, both in sovereign bonds and direct investors, may back out.

This insufficient cooperation with international bodies contrasts with the aspirations of Costa Rica to be a sustainability leader amongst developing economies. For example, the widely-used Freedom House Index awards Costa Rica a score of 91, or 'Free', similar to the score of 89 for France. Only a minority the Emerging Market debt issuers are classified as 'Free' by Freedom House.⁴

Unsurprisingly, therefore, Costa Rica ranks ninth-best of 123 nations in greenhouse gas intensity, according to Candriam's proprietary emissions model. Comparing to developing economies, Costa Rica ranks sixth in sustainability.⁵

Candriam's Sustainable Risk Committee (including our CIO, the head of our Risk Department, and representatives from our ESG departments) insisted on a clear assessment of the new situation on which to base their decision for, or against, a downgrade and/or divestiture due to increased risk.

The Committee gave our Emerging Market Debt Team and our Engagement Team six months to determine how material this development actually might be, what it meant for governance of the country of Costa Rica, and what steps its government might take, and the likely time frame for government action, so that the Sustainable Risk Committee could make a better-informed decision. Our engagement program was launched in May, 2023.

2. The EU list of non-cooperative jurisdictions for Council, Consilium, Europa.eu) and 12 as of February, 2024 (European Council, Consilium, EY Ernst and Young).

3. European Council, [Timeline](#), accessed 20 November, 2023.

4. Freedom House, [Countries and Territories | Freedom House](#), accessed 20 November, 2023.

5. [Sustainability in the age of the grey swan | Candriam](#) These model figures have been updated since the publication of the report.

Results.

In October 2023, the **EU removed Costa Rica from its list of non-cooperative jurisdictions** for tax purposes, and is now considered as a *'country which cooperates with the EU and has pending commitments'*.

The engagement was successful, and closed in October, six months after launch.

Our sovereign sustainability investment categories are not purely numerical. For the proprietary model, the inclusion of Costa Rica on the EU List of non-cooperative jurisdictions warranted a penalty to the score. Yet, the information gained through our engagement offered the ESG Analysis Team (and the sovereign analyst) enough confidence in a resolution that the ESG opinion was re-confirmed, and Costa Rica remains eligible for sustainable portfolios.

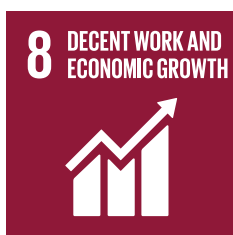
Next steps?

This engagement with Costa Rica is a rare example of direct dialogue with a sovereign issuer.

Direct ownership of corporations by shareholders obviously makes equities the largest universe for investor engagement. Engaging with issuers in other asset classes may be less common, and perhaps more complex, but with sustainable investments now available in essentially all asset classes, these are the new frontier.

To benefit from collective leverage, sovereign engagements tend to be collaborative. Often, 'engaging' with a sovereign consists of an investor statement or letter(s). With this engagement with Costa Rica, we spoke directly with stakeholders (eg, government ministers, the IMF) for a specific and well-defined objective to gain insight into a situation.

At Candriam, our goal is to partner with issuers in their sustainable journey. We are carrying out a direct engagement with another Central American sovereign on a similar issue. This time, we expect a more difficult path. But we broadening our sovereign engagement effort.





**Costa Rica is a rare example
of direct dialogue with
a Sovereign issuer.**



€145 B

AUM at end
Dec. 2023*



+600

Experienced and
committed professionals



+ 25 years

Leading the way in
sustainable investing

This marketing communication is provided for information purposes only, it does not constitute an offer to buy or sell financial instruments, nor does it represent an investment recommendation or confirm any kind of transaction, except where expressly agreed. Although Candriam selects carefully the data and sources within this document, errors or omissions cannot be excluded a priori. Candriam cannot be held liable for any direct or indirect losses as a result of the use of this document. The intellectual property rights of Candriam must be respected at all times, contents of this document may not be reproduced without prior written approval.

Candriam consistently recommends investors to consult via our website www.candriam.com the key information document, prospectus, and all other relevant information prior to investing in one of our funds, including the net asset value ("NAV") of the funds. This information is available either in English or in local languages for each country where the fund's marketing is approved.

*As of 31/12/2022, Candriam changed the Assets Under Management (AUM) calculation methodology, and AUM now includes certain assets, such as non-discretionary AUM, external fund selection, overlay services, including ESG screening services, [advisory consulting] services, white labelling services, and model portfolio delivery services that do not qualify as Regulatory Assets Under Management, as defined in the SEC's Form ADV. AUM is reported in USD. AUM not denominated in USD is converted at the spot rate as of 31/12/2023.



CANDRIAM. INVESTING FOR TOMORROW.
WWW.CANDRIAM.COM

CANDRIAM