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**Costa Rica:
Challenges to Stability**

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*NIE 83.4-86
June 1986*

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THE NATIONAL FOREIGN INTELLIGENCE BOARD CONCURS, EXCEPT AS NOTED IN THE TEXT.

The following intelligence organizations participated in the preparation of the Estimate:

The Central Intelligence Agency, the Defense Intelligence Agency, the National Security Agency, and the intelligence organizations of the Departments of State and the Treasury.

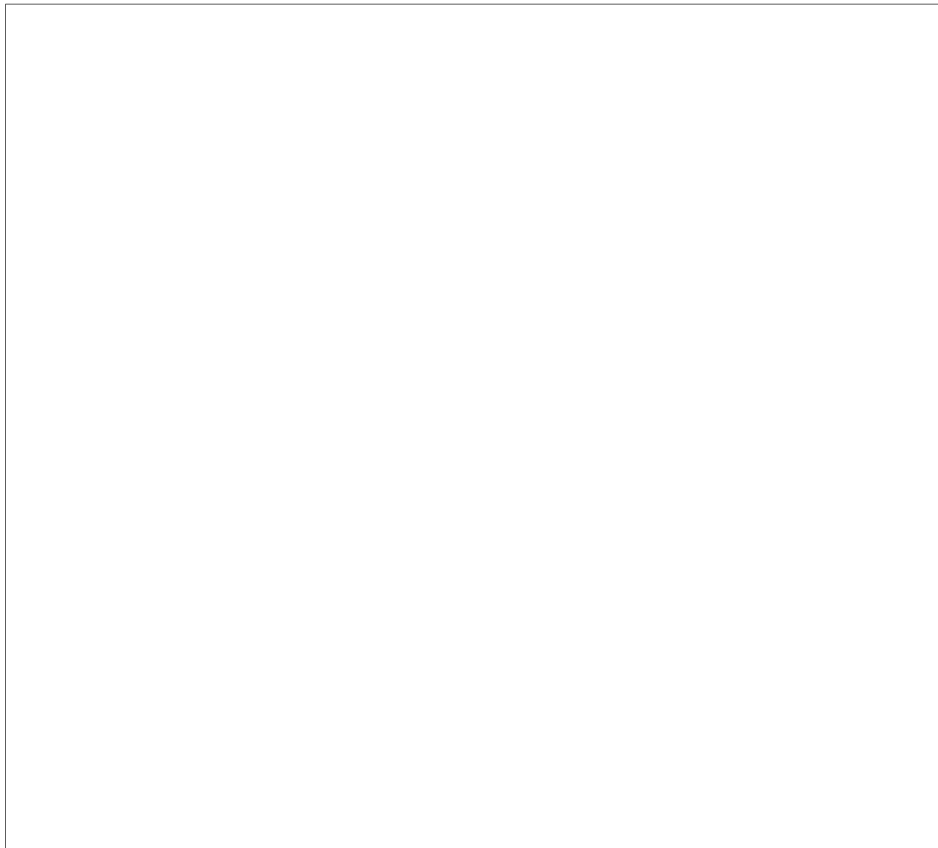
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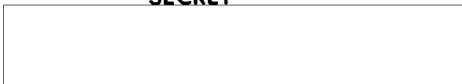
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**COSTA RICA:
CHALLENGES TO STABILITY**

Information available as of 5 June 1986 was used in the preparation of this Estimate, which was approved by the National Foreign Intelligence Board on that date.

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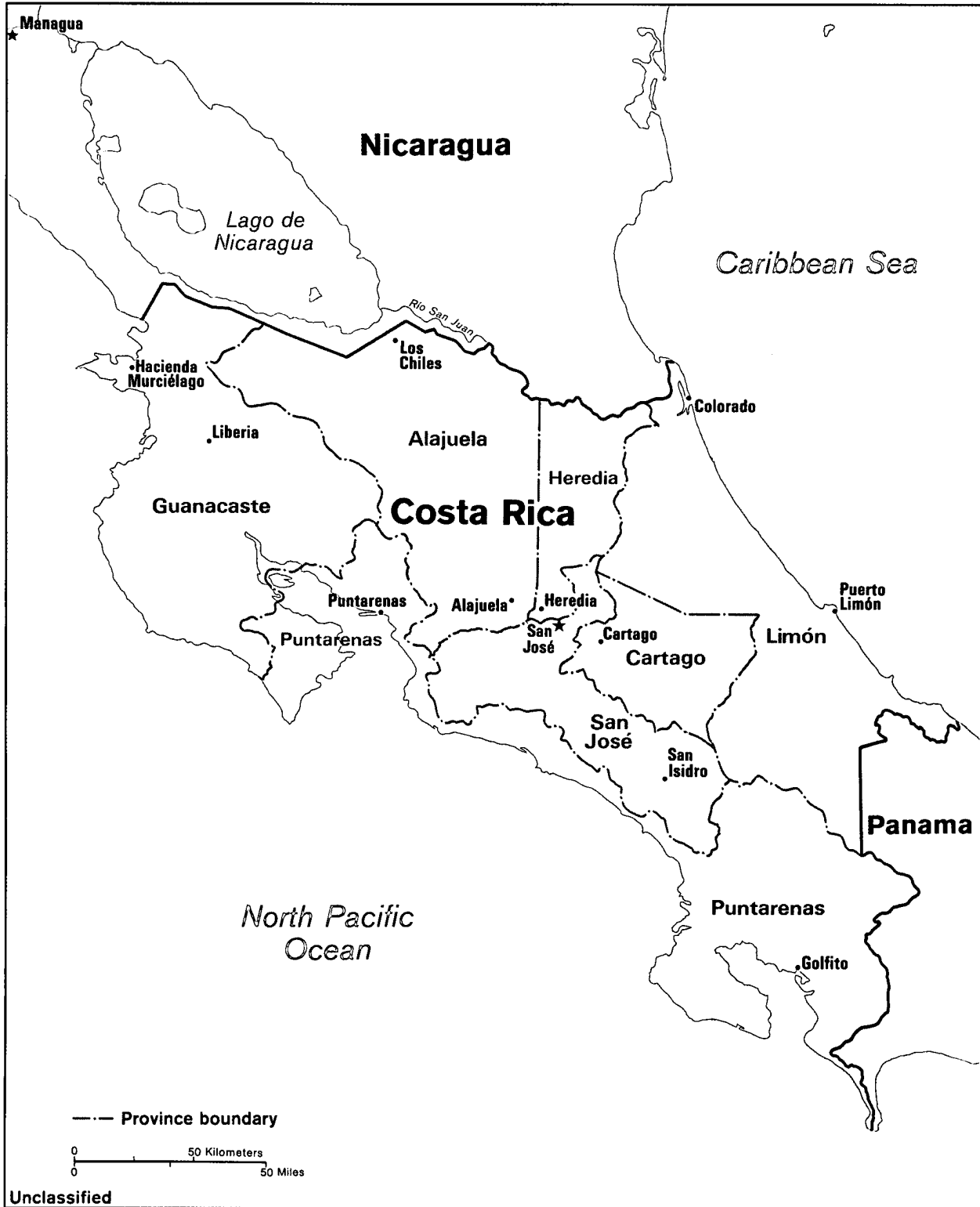
SCOPE NOTE

This Estimate examines the challenges to Costa Rica's political and economic stability that will confront the new and untested administration of President Oscar Arias over the next two to three years. It focuses on economic problems, the activities of extremist groups, relations with Nicaragua's Sandinista regime, and Costa Rica's limited capabilities to deal with these challenges. It also addresses Arias's likely policy toward Nicaragua and the anti-Sandinista insurgents, as well as his willingness to continue close relations and cooperation with the United States.

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KEY JUDGMENTS

Newly installed Costa Rican President Oscar Arias will face a number of challenges over the next several years, including a weak economy and the prospect of rising worker unrest, a more militant extreme left that is receiving clandestine support from Cuba and Nicaragua, and a belligerent and heavily armed Sandinista regime on Costa Rica's northern border:

- The Sandinistas are likely to continue military incursions into Costa Rica in pursuit of Nicaraguan insurgents in an attempt to intimidate San Jose and force it to implement an agreement to permit international monitoring of the border.
- The small groups on the extreme left have been receiving arms and training from the Sandinistas, Cuba, and Libya over the past several years, and the largest faction now has a paramilitary force of several hundred men. They are increasingly capable, should the opportunity arise, of resorting to violence, which would seriously test the widely dispersed, 8,000-man Costa Rican security forces.
- The prospects for economic growth under Arias are constrained by Costa Rica's large foreign debt and the need to undertake austerity measures to maintain access to IMF and World Bank support. Continued slow economic growth and persistent unemployment are likely to stimulate increased labor unrest and popular dissatisfaction.

We believe Costa Rica's strong democratic tradition and responsible approach to government will enable Arias to keep these problems from seriously endangering the country's stability.

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We believe also that Arias, in confronting the key issue of how to deal with Nicaragua, will try to stay on the fine line that allows him to coexist with the Sandinistas but maintain close ties to Washington. At the same time, he will want to protect Costa Rica's image as a democratic, independent, and neutral country. He appears to be less disposed than former President Monge to allowing the insurgents sanctuary in Costa Rica, and he publicly spoke out against US military aid for the anti-Sandinista forces before taking office. He believes that diplomatic pressure on the Sandinista regime is more likely to achieve positive results than is the insurgency, and he is likely to take an active role in efforts by the Central American democracies to persuade Managua to open up its political system.

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We believe Arias, as one means of defusing tensions with Nicaragua, will keep open the option of proceeding with negotiations to reach an agreement enabling an international commission to monitor Costa Rica's northern border. Such an agreement would hinder insurgent operations in the border area as well as resupply from Costa Rica, but the international monitoring team is unlikely to put a serious restraint on rebel activities. And, while Arias is likely to arrest and expel any Nicaraguan insurgent leaders whose presence in Costa Rica becomes too blatant, he is unlikely to close insurgent political offices in San Jose.

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Extremist groups lack enough support to threaten Costa Rica's government seriously over the next few years, and its security forces—with US and other foreign assistance—are gradually improving their organization, training, intelligence, and equipment to cope with the prospect of increased domestic violence. Furthermore, Cuba and Nicaragua do not see Costa Rica as ripe for revolution, nor do most Costa Rican radicals. We believe that Cuba and Nicaragua are encouraging preparations for armed struggle there primarily as a means of creating problems for the United States in the event Washington undertakes direct military action against Nicaragua. Nonetheless, the evolving militancy of the extreme left may result in increased terrorism, especially since Libya reportedly has recently become involved in training and financing one of the more violence-prone factions. Increased terrorism by some leftist groups may also spark a violent reaction by rightist extremists, who are also well armed and financed.

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We believe President Arias is committed to negotiating IMF and World Bank agreements even though these would require tough austerity measures. He believes that he can create enough new jobs to preclude substantial labor unrest, but this will be difficult. Nevertheless, fewer than 20 percent of Costa Rican workers are organized, and their unions lack strong political clout. Thus, organized labor is not likely to be a major factor influencing Arias's decisionmaking on economic policy.

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On balance, President Arias is likely to seek to remain a close ally of the United States, especially because he regards US financial support as crucial to Costa Rica's economic recovery and because he regards Washington as the ultimate guarantor of his country's security. Nevertheless, he is a strong-minded individual, and may pursue diplomatic policy initiatives with Nicaragua, both bilateral and multilateral, that risk undermining US attempts to maintain military pressure on Managua through support to the anti-Sandinista insurgents. He is no friend of the Sandinistas, and his posture toward both Washington and Managua

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will depend heavily on Sandinista behavior toward San Jose, the potential success of the Nicaraguan insurgency,¹ and the performance of the Costa Rican economy over the next several years:

- Arias will have a freer hand to improve relations with Nicaragua if tensions remain low, but he will have to adopt a more confrontational approach if Managua behaves aggressively.
- If Arias perceives the anti-Sandinista insurgency as weakening, he will be more likely to seek an accommodation with Nicaragua.
- If the insurgents get stronger, Arias would be more tolerant of the rebels' presence in Costa Rica.
- A worsening economy would increase Arias's desire to avoid conflict with Nicaragua, whereas a strengthened economy would allow him to take a stronger position against the Sandinistas 

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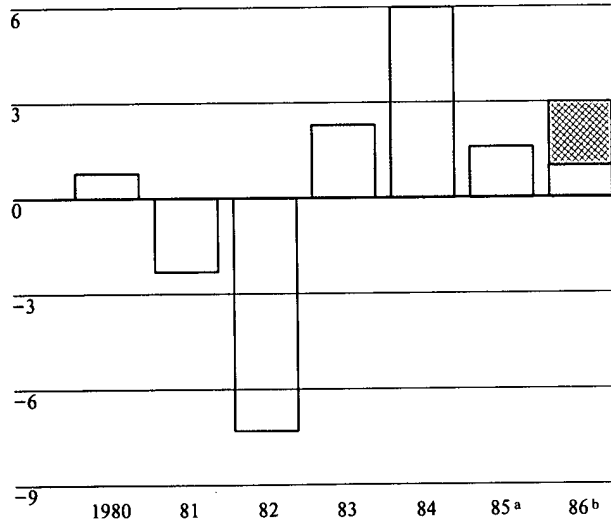
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Costa Rica: Selected Economic Indicators

Note scale changes

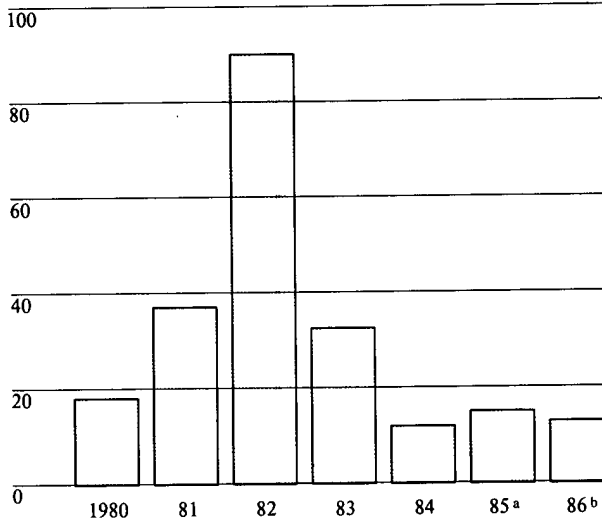
Real GDP Growth

Percent



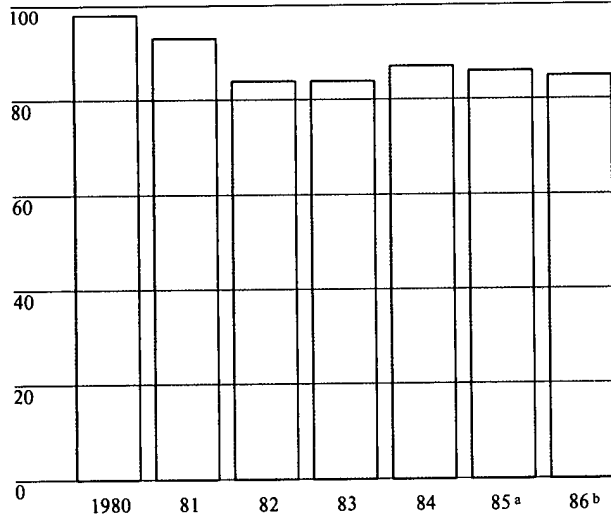
Average Annual Consumer Price Inflation

Percent



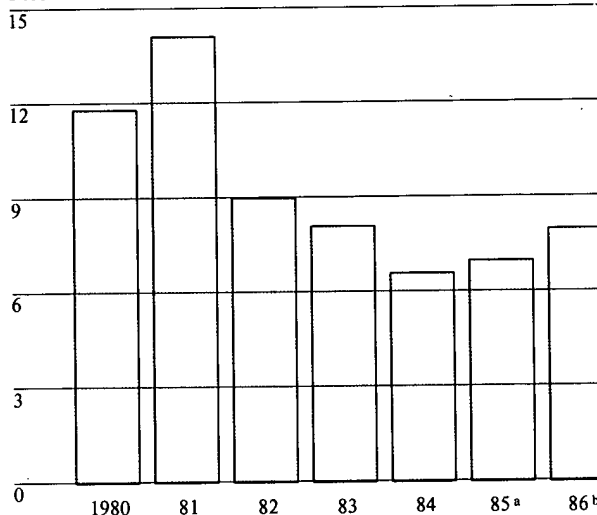
Per Capita GDP

Index: 1979=100



Public Sector Budget Deficit as a Share of GDP^c

Percent



^a Estimated.

^b Projected.

^c Includes Central Bank operating losses.

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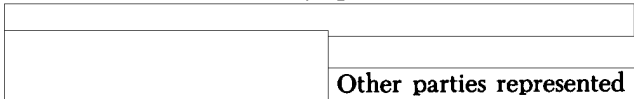


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DISCUSSION

The New Government

1. Newly inaugurated President Oscar Arias will face considerable difficulties in guiding Costa Rica's 38-year-old democratic system. Like popular outgoing President Alberto Monge, Arias comes from the center-left National Liberation Party, Costa Rica's largest political party. Despite his relatively impressive victory at the polls, where he received 52 percent of the vote, Arias will have an uphill battle in pushing his policies—including modest social programs—through the 57-member National Assembly, because his party's 29 seats leave it with only a bare majority. The major opposition coalition, bolstered by a gain of seven seats, now holds 25 and intends to challenge Arias much more than it challenged Monge on a variety of issues. Opposition leaders reportedly believe Arias's apparent intention to chart a foreign policy more independent of the United States will jeopardize US economic aid.



Other parties represented in the National Assembly include the Communists—with two seats—and a small, independent party with one.

2. Arias will confront several key problem areas. Economic matters are an area of significant concern. Although impressive by Central American standards, Costa Rica's average growth rate of 3 percent during the period 1983-85 was generated largely by some \$600 million in US assistance, rather than by internal forces. Heavy external debt, the need to regain access to IMF financial support, and persistent high unemployment are other economic problems with which Arias must cope. Arias also will have to contend with the potential for rising domestic violence by Costa Rican leftists—encouraged and aided by Nicaragua and Cuba—and with countermeasures by rightists.

3. Costa Rica's most volatile political problem is its relationship with its northern neighbor. San Jose wants to avoid any armed confrontation with Nicaragua, as well as spillover effects from the fighting there, and Managua will continue pressing San Jose for a firm agreement on an international commission to monitor

the border and deny anti-Sandinista insurgents the use of Costa Rican territory. Arias's desire to project a neutralist image and demonstrate his independence from the United States will reinforce the search for a modus vivendi with the Sandinistas. In dealing with these issues, however, the President also will be influenced by the need to remain on a correct footing with the United States, Costa Rica's principal trade partner and largest aid donor.

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Domestic Challenges

The Economy

4. The prospects for economic growth over the next two to three years are modest, largely because of Costa Rica's substantial foreign debt, which official figures put at over \$4 billion—one-third larger than GDP—as well as the continued disruption of the Central American Common Market and its inability to diversify exports. (See charts.) Per capita debt stands at \$1,750, among the highest in Latin America. Moreover, already rescheduled debt service obligations will require \$550 million this year. Debt service due during the next two years exceeds \$750 million annually, but San Jose probably will be able to reschedule as much as one-fourth of that. Increased foreign exchange—thanks to lower international interest rates, lower world prices for oil imports, and higher prices for coffee exports—will help Costa Rica catch up on debt arrearages and meet debt servicing obligations, leaving little for expanded imports to fuel economic growth for at least the next two years.²

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5. High on Arias's agenda, therefore, is maintaining the financial support of the IMF, World Bank, and commercial bankers, which have grown impatient with San Jose's missed targets, compromised reforms,

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² The Director, Bureau of Intelligence and Research, Department of State, estimates that economic growth over the next two years is more likely to be in the range of 3 to 4 percent and not as indicated in this Estimate. While some of the foreign exchange windfall from coffee, petroleum, and interest rates will go to pay debt, some will also be used to finance imports of the capital and intermediate goods needed to improve on last year's 1.6-percent growth.

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and debt arrearages. In April the IMF suspended its program, along with standby drawings of \$20 million, because of failure to meet economic performance targets. Meanwhile, the World Bank has delayed disbursement of \$40 million because Costa Rica did not lower tariffs and freeze public sector hiring. On 7 May, the day before Arias took power, San Jose temporarily suspended interest payments until it receives expected funds from the World Bank and the US Government—expected by late June 1986. We believe Arias is committed to negotiating IMF and World Bank agreements even though it will require trimming spending further, reforming commercial laws, and making additional cuts in the public sector. Such an austerity package would allow San Jose to renew debt payments and set the stage for growth in the future, but would hold current growth to modest levels, at best, for at least the next few years. []

6. Access to funding from international institutions is particularly critical because of declining private investment as regional political turmoil continues to dampen business confidence. US investment in Costa Rica, for example, fell from \$303 million in 1980 to \$230 million in 1984, according to the US Department of Commerce. []

[] three major US firms recently terminated their operations and that some of the remaining 100 US-owned companies are considering doing the same. []

7. Even assuming IMF and World Bank funds are restored, some serious problems will remain. Unemployment currently hovers at 10 to 12 percent, and per capita income is only about \$1,250. Living standards probably will remain unchanged—at 15 percent below 1979 levels—and could plummet further unless substantial foreign assistance is received. Nonetheless, inflation, though down from 90 percent in 1982, averaged 15 percent last year but continues to decline. (See table 1.) []

8. Despite these circumstances, Arias has embarked on a domestic program that remains true to his party's ideology, and identifies the state as the major instrument to promote social welfare. During the campaign, he pledged to build 80,000 new housing units, relying on funds from USAID and the Inter-American Development Bank, and to create 25,000 new jobs each year—enough to cover labor force expansion. Arias's campaign promises may have generated excessive public expectations and probably are beyond his reach, given the need for new austerity measures. []

Table 1
Costa Rica by the Numbers ^a

	Costa Rica	Average of Other Core Four Countries ^b
Population growth	2.3%	3.0%
GDP per capita (1979=100)	86	79
Unemployment	10-12%	23%
Inflation	15%	27%
Budget deficit (percent of GDP)	7.0%	7.0%

^a Based on 1985 data.

^b Guatemala, El Salvador, and Honduras.

9. With little prospect for significant economic growth and in the face of increased labor concerns, worker unrest may grow in the next two to three years. Relations between former President Monge (see inset on next page) and organized labor were strained during his term, according to [] press reporting. IMF-imposed austerity measures limited San Jose's ability to meet many worker demands, and the 1984 walkout against United Brands proved the longest and costliest strike in the country's history. Increased labor agitation yielded no significant government concessions, however, and two labor reform initiatives that would have strengthened labor's hand languished in the Legislative Assembly, largely because of opposition by business interests. []

10. Despite increased activism, organized labor's limited membership, disunity, and weak party ties most likely will prevent it from exercising significant influence on national politics over the near term. Fewer than 20 percent of Costa Rican workers are affiliated with unions, and the major democratic and Communist unions are failing to attract a significant number of new members, according to academic studies. In addition, both the democratic and Communist labor movements suffer from internal factionalism and have failed so far to align themselves with the strong political party system. In fact, a major confederation—the Solidarity Movement, which is neither democratic nor Communist—is based on a concept of labor-management harmony that precludes the use of political parties as vehicles for achieving workers' demands. []

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Monge's Economic Legacy

Although President Monge's stabilization efforts were the most successful in Central America, backsliding during the latter part of his administration left Costa Rica with still-daunting economic problems that constrain his successor's policy options.

When Monge took office in 1982, the budget and foreign trade deficits were out of control, inflation was near triple digits, and economic activity was plunging. Monge immediately clamped down on public spending, further devalued the colon, and took steps to promote exports and reduce government's role in the economy. Within six months of taking office, Monge was able to sign a one-year IMF standby agreement and reschedule payments on \$1.1 billion in debt obligations. As a result, inflation declined sharply and the economy began to rebound.

Despite the good start, Monge was unable to maintain policy momentum during the second half of his administration. After his first stabilization program expired, he delayed for over a year in coming to terms with the IMF for a followup program. Monge finally agreed to a second accord in March 1985, only after debt pressures again became unmanageable. Subsequently, commercial bankers rescheduled payments of another \$600 million coming due through 1986 and granted San Jose \$75 million in new loans.

Presidential politicking during 1985 reinforced Monge's reluctance to ask Costa Ricans for further sacrifices and was partly responsible for the haphazard implementation of his second stabilization program. Opposition politicians blocked some required trade initiatives, and the administration failed to make further progress on freezing public-sector hiring, cutting food subsidies, or reducing deficits in public-sector enterprises. In these circumstances, worrisome budget and foreign payments deficits began to reappear. As a result, the rate of economic growth for 1985 fell to an estimated 1.6 percent while per capita growth declined for the first time since 1982.

Although the economic situation today is not as serious as it was during the last change in government, many of the same aspects of economic and financial disarray are present. Neither business confidence nor economic growth has fully recovered to pre-1980 levels, and growth prospects are still dependent on substantial external funding. On the financial front, San Jose continues to test the patience of Costa Rica's creditors because of its chronic delays in payments, and commercial bankers are increasingly unwilling to lend it new money.



Internal Security Threats

11. Reports of growing militancy within Costa Rica's small extreme left, which numbers about 7,000 members (see table 2), may portend renewed violence over the next two to three years, although much will depend on developments in Nicaragua. The left's poor showing in the last several elections has, in our opinion, undercut its traditional strategy of seeking power through peaceful means.

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_____ leaders who advocate preparation for armed struggle have gained increased influence, although leftist violence has thus far been limited:

— The two Communist organizations—the 4,500-member Costa Rican People's Party (PPC) and the more militant 2,500-member Popular Vanguard Party (PVP)—have been building up their paramilitary wings for several years, although much will depend on developments in Nicaragua. Potentially the most dangerous group—should the PPC become more violence prone—is the Mora Canas Brigade, a 300-member force composed largely of PPC militants.

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_____ many Brigade members have received military training in Nicaragua and acquired combat experience by helping the Sandinista Army patrol the southern border and pursue insurgent forces into Costa Rica.

— The New Republic Movement (MNR), with 100 to 200 members, advocates armed insurrection and is probably the most violence-prone group in Costa Rica. The party has clandestine cells that we believe are responsible for a number of terrorist actions. After apprehending some of its members in a bank robbery last year, Costa Rican security officials discovered plans to surveil US personnel.

— The Socialist Party, which claims a membership of 50 to 100, is a pro-Cuban organization that reportedly has headed a campaign—including bomb threats—against a Voice of America station in Costa Rica. Unlike the other three extreme leftist parties, the Socialists lack a paramilitary wing.

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12. Foreign support—particularly from Nicaragua and Cuba—has been critical to the improving paramilitary capabilities of the Costa Rican left. In addition to training, Managua has provided weapons. _____ arms shipments to various radical groups included _____ rifles, _____ rocket-propelled grenade launchers, an _____

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Table 2
Major Leftist Parties ^a

Party	Leadership	Estimated Membership	Comments
Costa Rican People's Party	Manuel Mora	4,500	Holds one congressional seat. Has strong youth wing. Leaders divided over successor to Mora. Pro-Moscow. Has largest paramilitary apparatus, which numbers several hundred and has fought in Nicaragua.
Popular Vanguard Party	Humberto Vargas, Arnaldo Ferreto	2,500	Espouses more militant philosophy than People's Party. Has small paramilitary wing. Controls left's other congressional seat.
New Republic Movement	Sergio Ardon	100-200	Most terrorist-prone group. Has ties to Libya. Seeks destabilization of government and removal of foreign investors.
Socialist Party	Alvaro Montero	50-100	Party leader virulently anti-American and admirer of Fidel Castro. Intellectuals predominate. Has campaigned against Voice of America station in Costa Rica.

^a All of these leftist parties are legal in Costa Rica.

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ammunition between 1981 and 1983. In 1984 and 1985, Costa Rican Communists continued to acquire training and combat experience in Nicaragua:

- Some leftists reportedly have received military training in Cuba as well. In addition, [redacted] Costa Rican Communist leaders frequently journey to Havana to seek advice and other support.

13. Despite its evolving militancy, the extreme left faces serious constraints. It lacks popular support and remains riven by personal rivalries and fractiousness— notwithstanding periodic Nicaraguan, Cuban, and Soviet efforts to encourage unity—that would hamper any attempt to launch an insurrection. [redacted] suggests Nicaragua and Cuba still do not see Costa Rica as ripe for revolution, nor do most Costa Rican

14. Nonetheless, a significant outbreak of violence in Costa Rica would place a strain on a political system with a strong pacifist tradition. [redacted]

[redacted] the limited terrorist activity that emerged during the early 1980s as a spinoff of the insurgent situations in Nicaragua and El Salvador caused considerable public concern. It has targeted primarily foreigners rather than Costa Rican nationals:

- In March 1981, for example, three US Marine guards were injured by a bomb attack on their vehicle. The assailants were members of a small, pro-Cuban, Communist group known as "The Family," apparently linked to the MNR. They subsequently were arrested by the security forces acting on information provided by the public.
- In January 1982, [redacted] an unsuccessful kidnaping attempt by a Salvadoran guerrilla group against a Salvadoran resident of San Jose resulted in the deaths of three would-be kidnapers and the arrests of two others, both Salvadorans who had been trained in Nicaragua.
- In July 1982 a Colombian leftist who bombed a Honduran airline office in San Jose told Costa Rican authorities that three Nicaraguan diplomats had planned the operation. Considering the act part of a Sandinista plan to destabilize the

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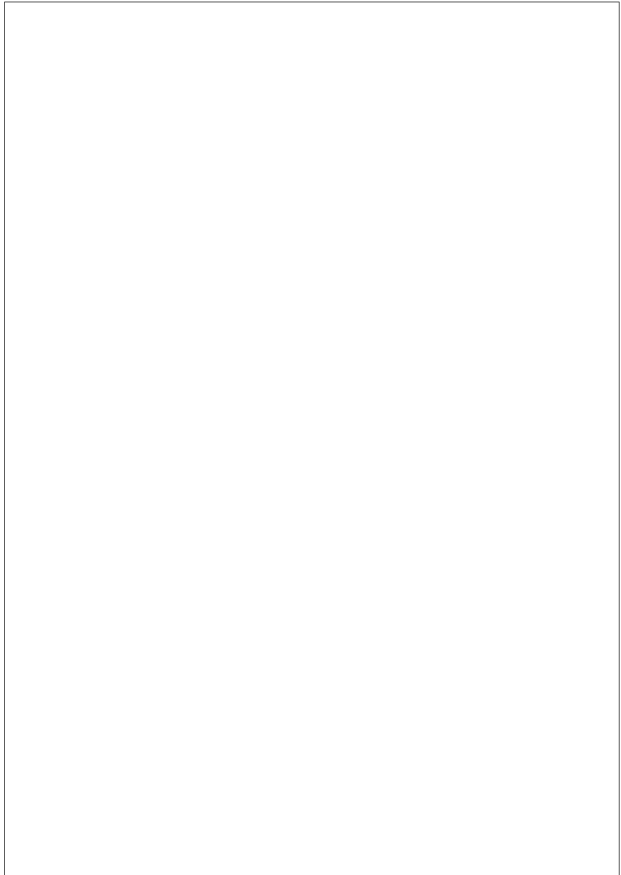


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The Security Forces

Costa Rica has had no standing national defense force since 1948, when the Army was proscribed by the Constitution and officially disbanded. Police and security functions are performed by the Civil Guard, under the Ministry of Public Security, and by the Rural Assistance Guard, under the Ministry of Government and Police. These forces are generally capable of performing routine law enforcement roles but traditionally have not had the equipment, training, or organization needed to perform conventional military functions.

The increasing threat from Nicaragua has created a public consensus to modernize and professionalize these forces with improved intelligence capabilities, better training, and some limited equipment acquisitions to enhance mobility, firepower, and communications. Nevertheless, the country's longstanding neutralist and antimilitary sentiments will continue to preclude the allocation of resources needed for dramatic improvements in force capabilities. Moreover, some 75 percent of positions in the Civil and Rural Assistance Guard forces are subject to political patronage, and turnover attendant to the inauguration of each new administration will continue to affect the competence and effectiveness of most elements adversely.



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Monge government, San Jose expelled the diplomats.

— Assassination attempts against anti-Sandinista leaders Alfonso Robelo and Eden Pastora in 1983 and 1984 were attributed to Managua.

15. Increased leftist activity or new tensions with Nicaragua may spark a violent reaction by the extreme right. The Free Costa Rica Movement, a paramilitary organization with some 1,000 members, who make up a significant part of the security force reserve, has long been active in defending against perceived leftist threats. Following the killing of two members of the Costa Rican Civil Guard by Sandinista troops in a border clash in May 1985, rightists organized a violent demonstration at the Nicaraguan Embassy, and a new group called Fatherland and Freedom claimed credit for bombing an electrical transmission tower providing electrical power to Nicaragua. In addition,

Costa Rican authorities this year identified a new 100-member rightwing paramilitary organization,

which, calling itself the Central American Falange, appears well financed and armed.

16. Costa Rica's security forces—modestly equipped, poorly organized, and spread thin—are unprepared to cope with serious violence, despite recent improvements.



Turnover among officers and enlisted men in both Guards traditionally has been high, because salaries are low and because the political parties view the security forces as a means of patronage.

17. Although Arias intends to follow Monge's policy of upgrading the security forces with US and

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other foreign assistance, improvements over the next two to three years may fall far short of needs. During recent years, the United States replaced the Civil Guard's 1940s-vintage arms with modern rifles and support weapons. In addition, San Jose has formed a rapid-reaction Civil Guard battalion of six US-trained companies numbering about 1,000, as well as a formal reserve force that numbers 3,000 but eventually is to reach 10,000.

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18. The reorganized intelligence service is improving steadily and has scored several successes, including the arrest of Mexican drug king Rafael Caro Quintero last year.

Arias intends to streamline the bureaucracy and put competent officers in midechelon leadership positions to bolster morale. The President also has said repeatedly that he will seek continued US assistance, presumably including counterterrorism training. Given San Jose's economic troubles, however, Arias probably will be unable to offer the higher salaries needed to boost morale and retain competent people.

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Foreign Challenges

Relations With Nicaragua

19. In dealing with Managua, the Costa Rican Government has been influenced by two conflicting strains in public opinion. On the one hand, traditional antipathy toward Nicaragua—the only country ever to invade Costa Rica—has been fanned since 1979 by the Sandinistas' increased Marxist-Leninist tendencies and repeated military incursions into Costa Rica. Public opinion polls consistently show a strong dislike for the Sandinista regime. In a March 1986 poll, 78 percent of the respondents had an unfavorable opinion of Nicaragua, and 91 percent avowed that the Sandinistas represented a threat to Costa Rica. On the other hand, the constitutional proscription of a professional military reflects a general preference for avoiding conflict. In the same March poll, 49 percent expressed approval of the recent normalization of relations with Managua, with only 15 percent opposed. There is also growing popular concern over the influx of Nicaraguan refugees, whose numbers now approach 100,000.

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20. San Jose's attitude toward Nicaragua also has been keyed to other factors, including decreased optimism about anti-Sandinista insurgent prospects, the stalemate in the Contadora peace negotiations, and especially a perceived need to appear more independent of Washington.

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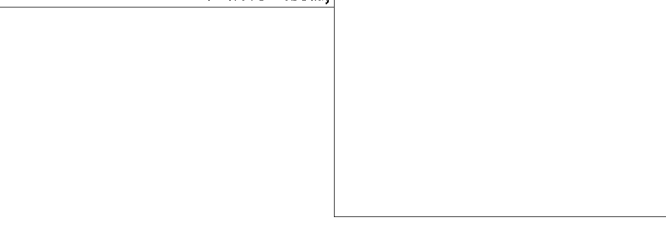
many government officials are convinced that the Sandinista regime is too well entrenched to be ousted by the insurgency, and their tolerance for the insurgents has been strained by reports of rebel involvement in looting, arms and drug smuggling, and possible assassinations. While Costa Rica has supported the Contadora talks, it apparently believes it cannot rely on multilateral solutions to protect its interests.



21. Costa Rica is particularly concerned that its international image as a democratic, unarmed, and neutral country has suffered in South America and Europe from being identified with US efforts against the Sandinistas. San Jose has traditionally relied on its democratic image for international support, and was very disappointed at the failure of other Latin American democracies to condemn Nicaragua following an OAS investigation of the May 1985 border clash in which two members of Costa Rica's Civil Guard were killed by Sandinista troops. Under President Monge, San Jose's foreign policy—especially toward Contadora—was guided by its need to show Managua as the intransigent party in Central America. Arias, like Monge, will try to restore Costa Rica's credibility among Latin American and European social democrats by appearing independent of the United States.



22. Responding to these considerations, Monge tried to reach an accommodation with the Sandinistas, but his need to stand up to periodic Nicaraguan provocations led his policies to trace a zigzag course. In September 1983 he proclaimed Costa Rican neutrality in Central American conflicts and applied the policy explicitly to the civil war in Nicaragua, in part to avoid being seen as a surrogate for the United States. At the same time, he continued to permit the anti-Sandinista rebels to conduct numerous political and military activities out of Costa Rica as long as they did not attract undue attention.



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23. Two subsequent incidents heightened San Jose's suspicions of Nicaragua. In December 1984, Sandinista authorities entered the Costa Rican Embassy in Managua and seized a Nicaraguan youth who had sought asylum there. The regime's refusal to give him up led Monge to recall his Ambassador, to reduce the size of

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Nicaragua's mission in San Jose, and to boycott a scheduled meeting of the Contadora peace talks. Last year's border clash resulting in the deaths of two Civil Guard members inflamed public sentiment even more. Nonetheless, reliable reporting indicates secret talks between the two countries resumed last fall, and these resulted in a normalization of relations in February. In addition, Managua and San Jose again agreed to pursue the formation of an international border commission, although they still disagree on its composition and function.



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In public, however, Arias has been critical of US policy and in April, while on an official visit to South America, again denounced US military aid to the insurgents, despite an earlier US demarche. He is likely to continue to stress that political solutions to the regional conflict deserve priority.

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24. We believe Arias will try to stay on that fine line that allows him to coexist with Managua but maintain close ties to Washington.

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the President considers US support for the anti-Sandinistas counterproductive, because it provides the regime with an excuse for internal repression and intransigence in regional negotiations. Moreover, Arias fears that prolonged violence in Nicaragua will spill over into Costa Rica, increasing the flow of refugees and scaring away foreign investors. Confident the United States would defend Costa Rica in the event of an invasion, Arias feels he has some maneuvering room. The President also believes that a strong economy will protect Costa Rica from Nicaraguan subversion and that a more neutralist foreign policy could win more economic aid, investment, and tourism from West European and Latin American countries.

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Negotiations Posture

27. We believe Arias will keep open the option of proceeding with negotiations for a bilateral agreement to neutralize the border, especially if multilateral talks falter. From his perspective, he probably could justify such an accord on the basis of public opinion polls, a longstanding Costa Rican pacifist tradition, the lack of a military counter to Managua, and the chance to bolster his standing in Europe and Latin America. At the same time, Arias is likely to send messages to Washington that any changes are much less significant than may appear on the surface and do not signal a "fundamental" or "radical" shift in San Jose's policies.

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25. For all these reasons, Arias prefers to stay on correct terms with the Sandinistas while trying to marshal Latin American diplomatic pressure to move them toward democratization. Although Costa Rica's continuing need for US economic aid to help stabilize the economy is likely to prove an incentive for Arias to move cautiously, we believe he doubts the United States will abandon him, and therefore feels he can take a more independent line.

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28. In our judgment, a formal bilateral agreement between Managua and San Jose to neutralize the border is likely to result in some complications for insurgent military operations and resupply activities across the Costa Rican border. Costa Rica has proposed a small, cosmetic international border force, primarily to enhance its international image, while Nicaragua wants a large force to seal the border. Although the two sides have agreed on a framework for future talks, they have not yet settled on the makeup of the border force. Any international border force would face considerable difficulty monitoring the 300-kilometer border. The Costa Ricans are likely to cooperate with an international force and try to prevent members of their security forces from assisting the rebels to avert any embarrassing incident. In our view, Arias is likely to arrest and expel any insurgent leader whose presence becomes too blatant, but he is unlikely to close insurgent political offices located in San Jose.

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Attitude Toward the United States

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29. Like Monge, Arias may find it politically expedient to pursue multilateral and bilateral agreements simultaneously. While he endorses the Contadora process, Arias is skeptical that the process will be success-

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ful. He has embraced an initiative by President Cerezo of Guatemala for the formation of a Central American parliament—including Nicaragua—as a potential alternative negotiations forum, but he sees this principally as another means of putting diplomatic pressure on Managua to open up its political system. [redacted]

Implications for the United States

30. On balance, President Arias is likely to seek to remain a close ally of the United States, especially because he regards US financial support as crucial to Costa Rica's economic recovery and because he regards Washington as the ultimate guarantor of his country's security. Nevertheless, he is a strong-minded individual and may pursue certain diplomatic policy initiatives with Nicaragua, both bilateral and multilateral, that risk undermining US attempts to maintain military pressure on Managua through support to the anti-Sandinista insurgents. His posture toward both Washington and Managua will depend heavily on Sandinista behavior toward San Jose, the potential for success of the Nicaraguan insurgency, and the performance of the Costa Rican economy over the next several years. [redacted]

31. Costa Rica's pursuit of a bilateral agreement with Managua would undermine US interests in several ways:

- It plays into the hands of the Sandinistas, who have tried to divide and neutralize Nicaragua's neighbors by dealing with them individually as an alternative to dealing with them in a multilateral context.
- The creation of a border inspection team would hinder the ability of anti-Sandinista rebels to use Costa Rican territory, as would any further restrictions on their activities introduced as part of an agreement with Managua.

— Finally, Nicaragua would cite an accord with San Jose as a precedent for a similar settlement with Honduras, raising the possibility that the main insurgent group might no longer be able to operate from Honduran bases. [redacted]

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Key Variables

32. In our judgment, the following variables will be critical in determining Costa Rica's political and economic development—including relations with Nicaragua—during the next two to three years:

- **Sandinista Behavior.** Arias will have a free hand to pursue an accommodation with Managua only if tensions remain low. Nicaraguan cross-border operations or other provocative measures would inflame public opinion and narrow the President's freedom of action, as would a large inflow of additional refugees. In addition, cross-border activity probably would further deter foreign investment.
- **Nicaraguan Insurgent Performance.** If Arias perceives the insurgency as weakening, he will be more eager to come to terms with the Sandinistas and more willing to contemplate a total ban on rebel activities. If the insurgents grow stronger, Arias will be more likely to turn a blind eye to their use of Costa Rican territory.
- **Economic Stability.** Failure to enact an economic stabilization program could lead to an unraveling of pending financial agreements with international creditors. A worsening economy also would heighten Arias's dilemma, augmenting his desire both to reach an accommodation with Managua and to continue to receive substantial US aid. Renewed growth, on the other hand, probably would increase his willingness to confront the Sandinista regime. [redacted]

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