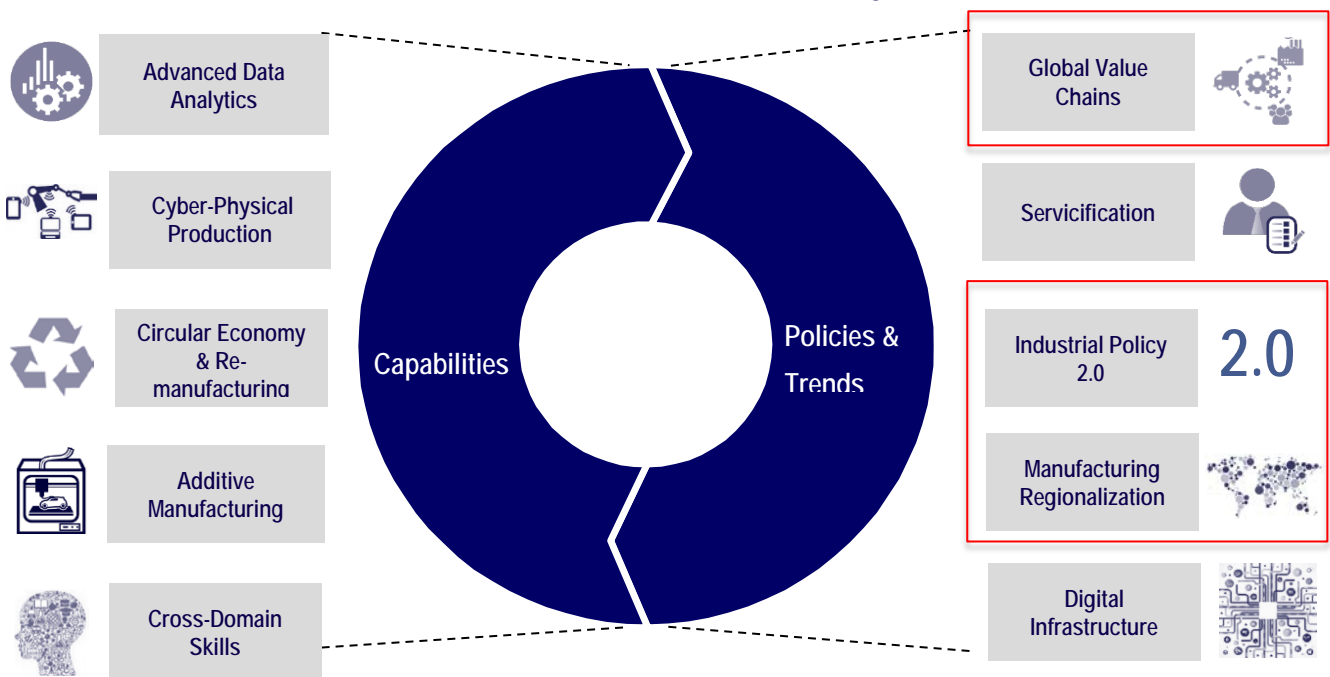


Case 11

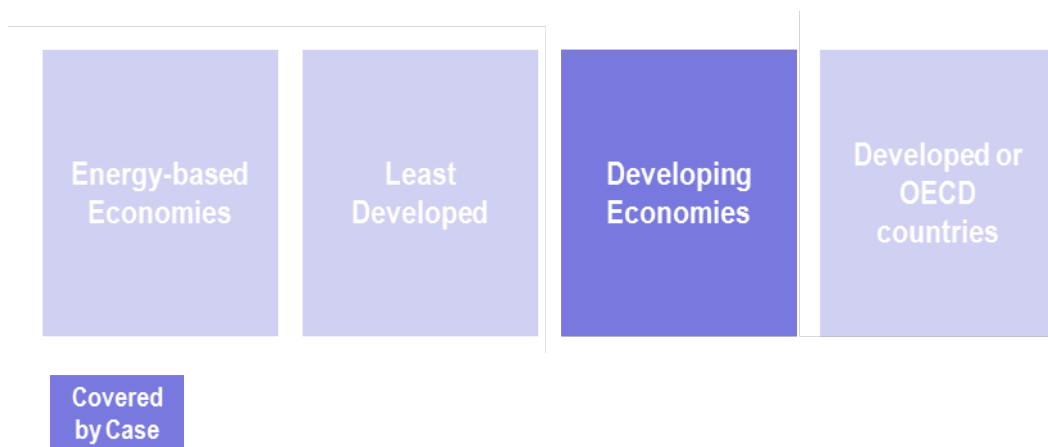
Costa Rica

Medical Devices

Drivers of the Future of Manufacturing



Source: World Economic Forum Global Agenda Council on the Future of Manufacturing, Whiteshield Partners framing



1. Challenge Confronted

In the late 1990s, CINDE, Costa Rica's investment promotion agency, felt that its **FDI-attraction strategy was too focused** on the global electronics industry which was itself very volatile. The challenge was to identify and attract an industry that could significantly contribute to Costa Rica's economic growth.

2. Solution Used

Costa Rica deliberately targets the global medical devices industry using an **export oriented FDI-driven strategy** to attract foreign investors and multinationals who are interested in locating their manufacturing or service entities in Costa Rica. In support of this strategy:

- CINDE offers **"handholding" services** and provides daily advice to foreign companies as they navigate Costa Rica's administrative procedures during site selection. Additionally, CINDE acts as a key **facilitator between private and public sectors** leveraging its strong and well-established working relationship with multinationals, government ministries, public and quasi-public entities, industry groups, and universities.
- **CINDE's role goes well beyond investor attraction; support to multinationals and foreign investors continues even after they have settled in Costa Rica.** As a **"first port of call"** for foreign companies experiencing almost any issue, CINDE troubleshoots problems that can range from expat workers' visa delays or helping multinationals retrieve inputs held up at customs to acting as a facilitator between rival companies when disputes arise. These services are **indefinite and free of charge**.
- PROCOMER also **manages a supplier marketplace** through which it tries to **match the procurement needs of multinationals with local suppliers** who might be able to meet that need. PROCOMER uses this platform to help local firms identify areas for development (investment, certification, process upgrading etc.) which could make them more attractive to lead firms.
- The Free Trade Zone (FTZ) regime allows **FTZ-located companies' exemption from income tax for up to 12 years** in the San José Greater Metropolitan Area with the option to be renewed subsequently, and unlimited exemption from import duties, excise duties and remittances repatriation tax.

3. Lessons Learned



1. As the industry enters a new phase of development and Costa Rica seeks to **amplify positive spillovers** into its local economy (outside of the free trade zones), PROCOMER may need to play a more prominent role; **providing the same level of support and range of services to local suppliers** that CINDE offers foreign companies as part of its investment attraction and aftercare functions.

Costa Rica Medical Devices

Dates: 1990s

Keywords: clusters, exports, FDI, investment promotion strategy, medical devices, value chains

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Key facts:

- In order to attract FDIs to build local manufacturing capabilities, Costa Rica deliberately targets the global medical devices industry using an export-oriented FDI-driven strategy.
- CINDE, Costa Rica's investment promotion agency, offers "handholding" services, attracts investors and troubleshoots problems for foreign companies free of charge.
- Investment Promotion policies coupled with FTZs can be very successful generating employment, infrastructure investment and fostering knowledge transfer through on-the-job training.
- Costa Rica's export-oriented FDI-driven strategy has resulted in an influx of investment, steady growth in exports reaching \$1.7 billion in 2014 and the creation of approximately 19,000 jobs by 2014.
- However, impact and spillovers may be limited if not paired with targeted policies to "localize" the industry.



2. After 15 years of concerted effort, Costa Rica has a thriving advanced manufacturing hub that could work towards **evolving into a Costa Rica-centric medical device (Porterian) cluster** through stronger and more strategic Costa Rican medical faculties, R&D centres in technical universities and CCSS (Costa Rican Public Healthcare System).



3. In the meantime, while CINDE might continue to target higher-value added activities (in R&D and software/firmware, for instance) to try and “nudge” Costa Rican industry towards more attractive segments of the global value chain (thus creating additional jobs and generating knowledge transfer through on-the-job training), these **activities may remain relatively isolated from the rest of the economy if the structure of public support remains the same.**



4. **Investment promotion policies coupled with FTZs can be very successful, generating employment, infrastructure investment and fostering knowledge transfer through on-the-job training.** However, impact and spillovers may be limited if not paired with targeted policies to “localize” the industry, anchor higher-value-added activities and create competitive advantages beyond operational effectiveness. In so doing, industry development agencies can also **increase the associated switching costs multinationals would face in relocating outsourced activities** to a different country or region.

Description of the Work Performed

In the mid-1990s Costa Rica decided to **deliberately and directly target the medical devices industry for development in Costa Rica.** Costa Rica was **already well-positioned to attract multinationals** due to its attractive tax incentives, which included (at that time) full exemption from income tax, full exemption from import tariffs (on intermediate capital goods, raw materials and inputs), full exemption from local taxes (sales, VAT, municipal and royalties) and free management of foreign exchange offered to companies within the FTZs. In light of this and Costa Rica’s **low-wage profile, stable economy, educated and trainable workforce and proximity to the United States,** Costa Rica had potential as a manufacturing hub for medical devices that could well serve the US market.

Throughout this period of development, **CINDE has been a significant driving force,** continuing in its mission to attract medical devices multinationals, to bring jobs to the region and to increase the sophistication of Costa Rica’s product and process offering. Though officially a private, not-for-profit organization, CINDE was declared “of public interest” in 1984 and has been the recipient of some government funding in recent years.

Acting as Costa Rica’s official investment promotion agency, CINDE proactively reaches out and provides support to foreign investors and multinationals who are interested in locating their manufacturing or service entities to Costa Rica. It offers **“handholding” services** and provides **daily advice** to foreign companies as they navigate Costa Rica’s administrative procedures during site selection. This includes providing information and advice pertaining to **human resource pay-scales, land/building acquisition and rental, corporate service providers** (from legal services and accounting to caterers and furniture providers), **local supplier base, Costa Rica’s tax regime, labour regulations, introduction and familiarization with Costa Rica’s FTZs** and much more.

However, **CINDE’s role goes well beyond investor attraction; support to multinationals and foreign investors continues even after they have settled in Costa Rica.** As a first port of call for foreign companies experiencing almost any issue, CINDE troubleshoots problems that can range from expat workers’ visa delays or helping multinationals retrieve inputs held up at customs to acting as a facilitator between rival companies when disputes arise. These services

are indefinite and free of charge. CINDE sees itself as a key facilitator between private and public sectors that is able to leverage its strong and well-established working relationship with multinationals, government ministries, public and quasi-public entities, industry groups and universities to facilitate key initiatives that benefit the industry (CINDE, 2015). Such activity is the responsibility of CINDE's **Aftercare division** which has four key areas of activity: **education** (including certification, curricula development and training trainers); **language training** (in recognition that a key part of Costa Rica's offering is the wide availability of English and Portuguese speakers); **"procedures"** (which focus on Costa Rica's legal framework, regulations and guidelines and simplifying procedures); and lastly, the agency works towards **widening the scope of foreign investment beyond San José's Greater Metropolitan Area (GMA)**.

Significant though CINDE's investor attraction efforts have been, **the tax regime in Costa Rica's Free Trade Zones (FTZs) has played a large part in Costa Rica's industrial growth**, including the medical devices sector. Firms located in Costa Rica's FTZs may be exempt from income tax for up to eight years and have an unlimited exemption from import duties, excise duties and remittances repatriation tax. An additional eight-year renewal may also be granted if considerable additional investment is made (for instance, works in progress, non-depreciable real estate, machinery or software). Although early versions of the FTZ regime required companies to export, there is no minimum export threshold, though requirements related to strategic sectors, minimum employment numbers differ depending on whether the FTZ is within or outside Costa Rica's GMA, and on the size of the project/investment.

Key Outcomes

- Costa Rica's export-oriented FDI-driven strategy has resulted in an **influx of investment**, steady growth in **exports reaching \$1.7 billion in 2014** and the **creation of approximately 19,000 jobs** by 2014.
- Process and product upgrading has become more sophisticated but multinationals are still principally **outsourcing lower value-added activities to Costa Rica** (e.g. components manufacturing) rather than other activities with potentially higher margins (e.g. research and development).
- **Spillovers** to the rest of the economy beyond direct employment and salaries have been **slow to develop**; lead firms typically spend on average **23% of their overall procurement budget in Costa Rica** (not including utilities and overheads) and the bulk of that outsourcing is limited to packaging, non-technical services (catering, logistics, facility maintenance), or low-tech components (carton & plastic packaging, moulds, injection moulding).

Drivers & Enablers



Investment
Promotion
Policies



Free
Trade
Zones



- Employment
- Infrastructure investment
- Knowledge transfer

Barriers

- The challenges to increasing the value and sophistication of local spend can be stylized as a **"catch-22"** situation in which **multinationals are reluctant to make commitments to local suppliers until those suppliers have made necessary investments** (capital equipment/certification etc.), and small companies often cannot make necessary investments until multinationals have made commitments.
- Costa Rica's challenge will now be to **maintain its competitiveness as other low-cost global manufacturing hubs become more politically stable** and manufacturing competency increases.