

7 Democratic patient finance

The Banco Popular and community-based water operators in Costa Rica

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Costa Rica boasts one of the highest rates of access to improved drinking water in Latin America, having achieved nearly universal service coverage. Nonetheless, service gaps and challenges remain. Sanitation coverage rates remain low, and Costa Rica is at risk of multiple climate change-related hazards, including floods and landslides, cyclones, storm surge and sea level rise. Meeting these challenges will require significant investments in water and sanitation infrastructure.

In this chapter, we analyze the role of Costa Rica's Popular and Community Development Bank (Banco Popular y de Desarrollo Comunal, or BPDC) in financing public water supply and sanitation (WSS) systems. We focus on the bank's relationship with community-based water operators, known as water supply and sewerage system management associations (Asociaciones administradoras de los Sistemas de Acueductos y Alcantarillados, or ASADAs). ASADAs provide water services in rural and semi-urban areas of Costa Rica. Since 2006, the BPDC has built important relationships with the ASADAs and the Costa Rican Institute of Water and Sewerage (Instituto Costarricense de Acueductos y Alcantarillados, or AyA), which is also responsible for providing water and sanitation services in Costa Rica's urban areas and acts as the national regulator of the WSS sector. This chapter focuses on BPDC's relationship with the ASADAs, however, since it has a direct financing relationship with them.

The BPDC's programmes to finance the ASADAs exemplifies its role in providing patient finance to populations that do not otherwise have access to credit. The BPDC is considered to be the most democratic public bank in the world (Marois 2021). It was founded in the 1960s as a bank that is owned and controlled by workers. Since the late 1980s, an elected Workers' Assembly has exerted social control over the bank, setting its mandate and holding it to account. Under the influence of the Workers' Assembly, the BPDC has strengthened and expanded its role in the solidarity economy by democratizing credit, including establishing a new fund financed by the

banks' corporate profits that is dedicated in part to the ASADAs. Through this and other loan programmes, the BPDC serves communities that other banks fail to serve.

We examine four Costa Rican ASADAs that have current or recently expired loans with the BPDC to understand the variety of BPDC's financial offerings and their impact. These ASADAs also represent the four different loan programmes within the BPDC conglomerate's portfolio, offering additional insights. But while the ASADAs we feature in this chapter reflect some of the geographic diversity in Costa Rica, they are not meant to be representative of the country's ASADAs in general. The ASADAs we selected are amongst the best-performing ASADAs in Costa Rica, having achieved high rankings in AyA's benchmarking system used to evaluate performance.

This paper is the first study of the BPDC to provide a critical analysis of its financing of public water in Costa Rica. The research reveals how the BPDC works concretely in fulfilling its social mission in the WSS sector and uncovers the kinds of challenges that lie ahead in building an integrated water system in the context of uneven development and climate change. We argue that there is significant room for the BPDC to expand its patient financing role via public–public collaborations akin to what it has developed with the ASADAs. For Costa Rica to meet the UN sustainable development goals (SDGs) for water and sanitation—as well as related climate change goals—we recommend strengthening public–public collaborations by expanding BPDC's existing loan programmes, finding ways to streamline the loan approval process and creating new lines of credit for water operators, such as a syndicated loan programme amongst public banks dedicated to water and sanitation.

This study is based on an extensive review of the BPDC's annual reports, legal regulations and academic studies of Costa Rica's WSS sector and the BPDC. We conducted semi-structured interviews with the presidents and/or administrators of the ASADAs and reviewed ASADA statutes and other forms of ASADA documentation. In addition, we conducted interviews with former and current managers from the BPDC, project managers from the AyA, academics and experts from the United Nations Development Programme (UNDP) and non-governmental organizations (see Appendix A for a list of interviewees).

The first section of this chapter provides an overview of public services in Costa Rica, focusing on the banking and WSS sectors. The second section describes BPDC's financing mechanisms for ASADAs and its contribution to public WSS. It also identifies promising lessons and ongoing challenges. The third section discusses the potential and limits of debt financing for improving equity in WSS services and highlights the potential of public–public collaborations to finance WSS infrastructure. The chapter concludes with a summary of our main findings.

Public services in Costa Rica: banking and water supply and sanitation

Costa Rica is well-known for its stable and well-functioning democracy, robust civil society and relatively high levels of social equality, in addition to being a world leader in environmental conservation (Sandbrook et al. 2007; Pagiola 2008). In 1948, a popular uprising led to the installation of a social democratic government that disbanded the standing army, subsequently allowing for greater fiscal resources to be channelled into public goods, such as health and education (Booth 1998). Public investment in water and sanitation infrastructure in the post-World War II period was part of this trend. To this day, public banks play a key role in the Costa Rican economy. Yet like in other nations in Latin America, the turn to neoliberalism since the 1980s debt crisis has eroded redistributive aspects of the welfare state. Public investment in water and sanitation has stagnated. Despite the constant threat, Costa Ricans have remained deeply resistant to pro-market advocates' pushes to privatize public goods in order to preserve society's pro-public gains.

The Costa Rican banking sector

In 1948, the Costa Rican government nationalized the financial system as a marker of its national developmental ambitions and to advance the democratization of credit (Honey 1994, 78; Marois 2005). The National Banking System remained under public ownership and control until the debt crisis of the 1980s. In 1984, the government allowed private banks to start granting credits. In 1995, further liberalization measures increased private and foreign participation in the banks that, in turn, increased competition between the public, private and cooperative banks (Monge-González 2009, 8).

Today, the financial system in Costa Rica is dominated by banks and other financial intermediaries, as opposed to more market-based sources of direct financing (for example, via the stock market). Public, private and cooperative banking institutions combined account for over 91 per cent of overall financial system assets (OECD 2020, 8–9). Therein, public banks constitute about 35 per cent, private banks 33 per cent and cooperatives about 11 per cent of total financial assets as of March 2020. The remaining 12 per cent is made up of various public and private banks and non-banking financial institutions. Within the banking sector specifically, public banks are dominant (see Table 7.1). The largest banks in Costa Rica are the Banco Nacional de Costa Rica and the Banco de Costa Rica, which are 100 per cent state-owned. When combined with the BPDC, these three banks control 58 per cent of total banking sector assets. Eleven private banks hold the other 42 per cent of banking assets.

Our focus institution, the BPDC, is defined as a non-state public bank (explained below), and it is the fourth-largest bank in Costa Rica with just over 13 per cent of total banking assets. While the two other state-owned banks enjoy explicit state backing by law, the BPDC does not (OECD 2020,

Table 7.1 Public banks in Costa Rica

<i>Name (Year established)</i>	<i>Type of bank</i>	<i>Form of public bank</i>	<i>% of assets in banking sector</i>
Banco Nacional de Costa Rica (1914) ^a	Universal Commercial	State-owned	26.3
Banco de Costa Rica (1877) ^b	Universal Commercial	State-owned	18.4
Banco Popular y de Desarrollo Comunal (1969)	Universal Commercial	Non-state public law bank	13.4
Banco Hipotecario de la Vivienda (1986)	2nd Tier	Non-state public law bank	N/A

Sources: OECD (2020, 15); Fitch Connect (2023).

Notes:

^a First created in 1914 as the Banco Internacional de Costa Rica then renamed as the Banco Nacional de Costa Rica in 1936.

^b First created in 1877 as the Banco de la Unión then changed its name to Banco de Costa Rica in 1890.

16). That said, senior BPDC staff have communicated that they generally believe the BPDC to have an implicit state backing against default (Marois 2021, 209). As a bank governed under special public law, however, the Banco Popular is not required to hold capital reserves in the Central Bank of Costa Rica, reducing its cost of lending.

Over the last 15 years, Costa Rica has developed an innovative development financial institution, the Development Banking System of Costa Rica (Sistema de Banca para el Desarrollo, or SBD). The aim of the SBD is to support financial inclusion, productive development, innovation and technology, and micro-, small- and medium-size enterprises (MSMEs). Created by public law in 2008 (Law N° 8634), the SBD is constituted by the participation of all the public and state-owned financial and development institutions in Costa Rica. Private banks may participate in the SBD if they opt not to fulfil certain financial inclusion stipulations (like being active in specified regions) that would exempt the private bank from contributing resources to the SBD. To be clear, the SBD is not a bank per se. The SBD is a means of systemic coordination of development finance and does so by drawing in deposits from existing financial institutions and redirecting these financial resources into priority development programmes and geographical areas as authorized by its governing council (OECD 2020, 15, 19). Each bank that participates in the SBD administers their portion of these special funds. As of June 2023, the SBD has served over 73,000 clients (98 per cent of these are MSMEs) with loans totalling just over US\$4 billion. Loans average around US\$6000 each at a 5.98 per cent interest rate.¹

The Banco Popular y de Desarrollo Comunal

The BPDC is a unique public bank because it is worker-owned and classified as a *non-state* public bank (BPDC 2022, 12). It is not a cooperative, but rather a uniquely constituted public institution. The BPDC was founded in 1969 in public law (N° 4351, *Ley Orgánica del Banco Popular y de Desarrollo Comunal*) as a bank by and for the working class. A 2002 reform, the Law of the Democratization of Decision-Making Processes of the Popular and Community Development Bank (*Ley de Democratización de las Instancias del Decisión del Banco Popular y de Desarrollo Comunal*, or “Democratization Law”) reinforced its public character, solidified the role of the Workers’ Assembly in providing overall direction and accountability, and concretized the BPDC as what is considered to be the most democratic bank in the world (Marois 2021, 211–2).

The original 1969 BPDC Law states that the BPDC is 100 per cent owned by the working class of Costa Rica (BPDC 2012, 7), which in this case refers to formal workers whose deposits capitalize the bank. The BPDC emerged out of Costa Rica’s particular history. In the post-World War II era, workers and peasants struggled to make the country more egalitarian and democratic (Edelman 1999). Cooperatives, public services and workers’ rights emerged as high priorities. Nonetheless, accessible and appropriate financial services remained elusive to many. By the 1960s, workers and social sectors demanded a bank by and for workers (Cortés 2014, 60). Collective efforts culminated in the government transforming the pre-existing Monte Nacional de Piedad financial institution into an authentic workers’ bank, the BPDC. Notably, this initiative was championed by a woman from the opposition party, Cecilia González Salazar, who managed to gain near consensus on the bill with only one vote against (Marois 2021, 207; Mora Alfaro 2002).

Since its modest beginning as a single office, the BPDC has evolved into a full-service, nationwide universal commercial public banking conglomerate that provides both commercial and development banking products and services. The BPDC accepts personal deposits and offers a full range of personal, household and business financial services. These include savings and current accounts, personal and business credit, credit and debit cards and savings certificates. BPDC also offers financial services in pensions; stock market, brokerage and securities services; insurance; investment funds; interbank payments; and salary and tax payments. BPDC holds assets exceeding US\$6.6 billion and generates returns on average assets in line with private commercial banks at around one per cent (see Table 7.2) (the private Banco BAC San José averages around 1.3 per cent) (Marois 2021; Fitch Connect 2023).

The BPDC conglomerate is divided into five different institutional entities that serve different financial functions and mandates. These include the following:

Table 7.2 Banco Popular y de Desarrollo Comunal overview, 2023

	2022	2021	2020	2019	2018
Total assets (US\$ billions)	6.62	6.30	7.02	6.24	5.89
Return on average assets (ROAA) (%)	1.10	1.05	0.33	0.94	0.61
Return on average equity (ROAE) (%)	5.23	5.64	1.84	4.89	3.20
Net income (US\$ millions)	74.61	70.03	21.85	58.09	35.20
Number of employees (2020)	3872				
Credit rating (2023)	BB-				
Year of incorporation	1969				
Current Mission	To give economic protection and well-being to workers.				
Type of Public Bank	Universal Commercial (with development functions)				
Highest Governing Body	290-member Workers' Assembly				
Board of Governors	7-member National Board of Directors (3 from government and 4 from Workers' Assembly)				
Ownership	100% Working class of Costa Rica				

Sources: Marois (2021); Fitch Connect (2023); Banco Popular website (2023).

- 1 BPDC (Banco Popular y de Desarrollo Comunal), the main banking entity, which includes a Business and Corporate arm as well as Social Development Bank arm;
- 2 Popular Securities and Stock Market (Popular Valores Puesto de Bolsa);
- 3 Pension Plan Operator (Operadora de Planes y Pensiones);
- 4 Popular Investment Fund Company (Popular Sociedad de Fondos de Inversión);
- 5 Popular Insurance Agency Society (Popular Sociedad Agencia de Seguros).

In this chapter, we focus on the two arms of the BPDC that serve ASADAs: the Business and Corporate Bank and the Social Development Bank.

The BPDC has a unique manner of capitalization based on personal deposits that also makes workers co-owners of the BPDC. By law, the BPDC manages mandatory pension fund contributions equivalent to 1.5 per cent of the total payroll of public and private sector workers (0.5 per cent comes from the employers and 1.0 per cent from the employees). These employee contributions are used to capitalize the bank. For the first 18 months, these funds are channelled into a Labour Fund that is used to grant housing credits and for loans to MSMEs. After the 18-month period, the BPDC deposits 1.25 per cent, with interest, to the pension operator of the worker's choice (including within the BPDC Pensions division, if they like), while 0.25 per cent is retained by the BPDC as a form of permanent capitalization (OECD 2020, 15; Marois 2021, 208).

The BPDC's mandate as a workers' bank is reinforced by its democratic governance structure. In 1986, the Workers' Assembly became the highest governing body of the BPDC. The Assembly is made of up 290 representatives elected from ten identified social and economic sectors in Costa Rica: artisanal, communal, cooperative, self-managed, independent, teachers, professional, confederated syndicates, non-confederated and solidarity syndicates. The Assembly provides overall strategic direction and a forum of accountability. The Assembly also elects four of the seven members to the National Board of Directors—the bank's highest administrative body. The Costa Rican government appoints the other three members to the National Board of Directors. By law, all major BPDC decision-making bodies, from the Assembly down to regional bodies, must be at least 50 per cent women. The BPDC was the first public institution in Central America to achieve gender equality within its decision-making fora (BPDC 2017, 13).

In most areas of its lending (but not in the WSS sector), the BPDC competes directly with private, public and cooperative banks. The BPDC provides about 12 per cent of total loans in Costa Rica and holds about 9 per cent of deposits (OECD 2020, 9–10). In providing these loans, the BPDC seeks to generate returns, but not only returns at the expense of all else. Following nationwide consultations, the BPDC has adopted a triple bottom-line approach that takes responsibility for advancing economic, environmental and social objectives (BPDC 2023).

The BPDC is not focused on “skimming the cream,” that is, the banking practice of targeting the wealthiest clients in choice urban settings. BPDC clients are broad-based and include workers, peasants, MSMEs, as well as local governing authorities inclusive of communal, cooperative and municipal development associations in rural areas. Working in these communities, the BPDC has over 15 years' experience offering a series of financial products to the rural ASADAs, including normal loans and a series of special funds that are part of the BPDC's commitments to the SDB and its efforts to democratize finance.

Costa Rican water supply and sanitation sector

The water and sanitation sector in Costa Rica is almost universally public. Water has been considered the domain of the state since the Water Law of 1942 (N° 276, *Ley de Aguas*). Financing of the WSS sector has also been almost universally public, financed by taxes (public investment by governments) and transfers from multilateral development banks and other donors. Until 2020, domestic regulations prohibited water operators from borrowing money from any financial institution other than public banks.

The Costa Rican Institute of Water and Sewerage (Instituto Costarricense de Acueductos y Alcantarillados, or AyA) provides water to 50.7 per cent of the population mostly in and around the capital and most populated city, San José, while other local governments (municipalities) provide water services

to 18.8 per cent of the population (UN Water 2022, 5). There are estimated to be about 1500 ASADAs that serve about 25.5 per cent of the population, mostly in rural and semi-urban areas (UN Water 2022, 5).

ASADAs are legal entities that have signed an agreement with the AyA to provide water services and as such they are subject to AyA's regulations. In addition to these formal community water operators, it has been estimated that there are an additional 1400 small, rural water committees that serve about 5 per cent of rural communities (Mora-Alvarado & Portuguese-Barquero 2020, 1; UN Water 2022, 5). These informal water committees do not have a delegation agreement with AyA and are therefore not subject to credit; they are known as rural aqueduct management committees (the *Comités Administradores de Acueductos Rurales*) (Mora-Alvarado & Portuguese-Barquero 2020, 1; UN Water 2022, 5).

Costa Rica has the highest coverage rate for potable water in Central America. As of 2019, 98 per cent of households have access to an improved water supply (UNICEF 2020). Nonetheless, there are service gaps. First, access to water does not necessarily mean that it is safe. According to AyA in 2020, only 89 per cent of the population served received potable drinking-water quality, which means that 11 per cent of Costa Rica's population consume water of non-potable quality, thereby increasing the risk of developing waterborne diseases (Barrantes et al. 2022). About 1.8 per cent of the population (92,000 people of a population of 5.1 million) only receive piped water in the yard, and about 0.4 per cent of the population (21,000 people) have no service and are supplied directly from artesian wells and springs (Mora-Alvarado & Portuguese-Barquero 2020, 1; UN Water 2022, 5). Most of those who lack access to improved household water supply live in semi-urban areas of informal settlements and in rural areas, particularly in agricultural zones with high rates of poverty (interviews 6, 7). Second, Costa Rica is also failing at sanitation compared to its peers. Coverage rates remain very low, with only 10.49 per cent of total wastewater being treated as of 2017, compared to Honduras which treated 13.44 per cent (Fernández et al. 2021, 23). Untreated sewage and wastewater lead to ground and surface water contamination, degrading water quality, increasing the costs of providing clean drinking water and creating negative health effects.

Costa Rican Institute of Water and Sewerage (AyA)

Founded in 1961, AyA serves the purposes of overseeing, designing, constructing and managing drinking water infrastructure in urban and rural communities nationwide. From the 1960s to the late 1980s, there was a boom in construction of infrastructure to provide drinking water thanks to public investment. During these decades, over 60 per cent of the sector investments came from government resources, half of which were financed by multilateral and international loans (Lockwood 2004). As elsewhere in Latin America, this development of WSS infrastructure unfolded unevenly

as investments were channelled to urban areas. By 1980, water access in urban areas reached 88 per cent, but remained at only 63 per cent in rural communities (Dobbin & Sarathy 2015, 390; Morice & Robles 2011).

Since the late 1980s, the expansion of AyA's system has slowed (Alpízar 2016; Ortega Ponce 2006). For example, while AyA managed to build an important aqueduct that brought more water to San José and surrounding areas in 1987, they were forced to postpone the extension of the sanitary sewerage system. In the 1980s, the AyA also suffered a serious institutional crisis, revolving around mismanagement, that led to severe water shortages (Alpízar 2016, 47). This led to an intervention between 1986 and 1988 in which the national government installed a new board of directors to carry out an evaluation of AyA policies and administrative functioning, as well as to make recommendations on how to avoid future water shortages. During these years, numerous disputes erupted between members of the intervening board and the dismissed board of directors. Various directors resigned (Alpízar 2016, 47). These kinds of scandals related to accusations of corruption and mismanagement continue to this day (Mesen 2023).

In terms of corporate governance, the AyA is an autonomous agency, but the national government appoints the members of the board of directors. As UNDP advisor Gerardo Quiroz explains (interview 17), some AyA boards have been more favourable towards providing financial and technical support to the ASADAs than others. Some boards have embraced a "solidaristic mission" to finance projects in other areas of the country while others have understood the organization's mandate more narrowly to focus on serving users within AyA's own concession area (the capital city San José), in addition to its role as a regulator. Without a clear national directive on cross-subsidization, it will be difficult to develop a more equitable and predictable national financing strategy in order to build an integrated water system.

Water supply and sewerage system management associations (ASADAs)

Since 1976, water committees have built piped water systems that were operated under the umbrella of the respective development associations of each community. In 2005, these committees were transformed into ASADAs through delegation agreements. ASADAs are under the technical supervision of the AyA both in terms of water quality (the National Water Laboratory of the AyA) and sanitary sewerage (Alpízar 2016, 48). However, current regulations do not establish any obligations to provide sewerage services, which has created a regulatory vacuum. Yet ASADAs are obliged to protect water sources and watersheds, even though enforcement is clearly lacking (Alpízar 2016, 44). As of 2022, only 1 per cent of ASADAs provide sanitation services (Araya 2022). In most rural areas, waste management is done by free disposal, either by means of septic tanks or in open channels.

Costa Rica's ASADAs are democratic, community-based organizations that are run by volunteer boards. By law, every ASADA must hold an annual assembly open to all their members, which are known as "subscribers." Any subscriber may also run for election for a position on the board if they are in good standing. However, given that the subscriber must also hold a land title in the service area, ASADA boards tend to be male dominated. Despite legal changes in 1990 that allow for joint titling of property and shared administrative rights for married couples, equality in property ownership has not been achieved. It has been estimated that only about 15 per cent of ASADA presidents identify as female (interview 4). Many of our respondents also expressed concern about declining rates of citizen participation, especially by youth (interviews 2, 3, 4, 6, 7). Some ASADAs are exploring ways to allow for subscribers to delegate their authority to encourage more women and young people to participate.

The ASADAs have been rightly celebrated for vastly improving the rates of water coverage in the country (Romano et al. 2021). However, Dobbin and Sarathy point out that the focus on high coverage rates obscures "a more complex and nuanced story of co-management and its relative success" (2015, 389). ASADAs also face environmental and climate-related challenges. The demand for water is increasing due to irrigation, tourism and increasing rates of household consumption. As state-led investment has slowed in the past few decades, conflicts have erupted around water allocation, policy and scarcity, particularly within the drier provinces. While Costa Rica is a water-abundant, tropical country, climate change is creating new pressures and has uneven effects. Hydrologists have identified the Pacific slope in Central America as one of the areas in the world most prone to hydro-climatic emergencies, such as intense precipitations leading to floods and landslides, as well as drought (Stan et al. 2022). In some of the northern regions, scientists predict that significant water shortages will create semi-arid conditions, having a severe negative economic impact on the livelihoods of local communities (UNDP 2021).

ASADAs face structural challenges as well. Providing access to quality water services in semi-urban and rural areas entails higher average costs than compared with urban areas where economies of scale are possible. Particularly, in communities with dispersed populations, existing water supply infrastructure is often outdated and overloaded. This generates inefficiencies in water service delivery, which complicates the collection of fees from end users. For many ASADAs, instability in fee collection leads to financial uncertainty. This in turn creates a vicious cycle that impedes the ASADA's ability to plan for and implement targeted improvements and new investments—not to mention erecting barriers to accessing needed financing. While a few ASADAs have managed to secure donations from embassies, foundations and non-governmental organizations (NGOs), the main sources of revenue are tariffs and debt financing from public banks such as the BPDC (interviews 2, 3, 5, 6, 7, 15).

Patient, democratic financing for public water: the BPDC, the AyA and the ASADAs

The BPDC and Costa Rica's system of ASADAs are part of a wider solidarity economy that seeks to advance the interests of workers and enhance the well-being of the people (Li Bonilla & Villegas Barahona 2013). The mandate of the BPDC is to "to serve the social and sustainable welfare of Costa Rican inhabitants." One of the ways that they do this is by democratizing credit, for example, through the offering of soft concessional loans to communities that are otherwise "unbankable." The unregulated funds that have been established as a response to the demands of the Workers' Assembly also offer more flexibility. Ana Lucía Solano Garro, Executive Advisor in Promotion and Development at the Social Development Bank arm of the BPDC (interview 12), puts it succinctly:

We serve populations that no other bank serves. This is the advantage we have. In order to fulfil our social mission, we must bank the vulnerable populations. We use different terms to assess the credit risk between the regulated and the unregulated funds. The analysis of credit risk is tailored to what assets they have and their particularities.

The formal relationship between the BPDC, the AyA and the ASADAs began in 2006. The president of Costa Rica at the time, Óscar Arias Sánchez (2006–10), had secured a loan with the Central American Bank for Economic Integration (CABEI), a regional public multilateral bank (Deras et al. 2021), to support the expansion of WSS infrastructure. Arias Sánchez, along with executives from the AyA, approached various public banks looking for partners to contribute additional financial resources. As Roger Conejo, Director of the Business and Corporate Bank—who is credited by his peers at the BPDC for having initiated their programmes for ASADAs—describes it, "The executives of the AyA knocked on the doors of the local banks. We were the only ones who answered" (interview 11).

As of 2023, the BPDC conglomerate offers four different types of financial products to ASADAs: two by the Business and Corporate Bank and two by the Social Development Bank. The products are differentiated according to the ASADAs' capacity to pay. As mentioned, while there are around 1500 ASADAs in Costa Rica, the BPDC has but a handful of active engagements. As of February 2023, the BPDC had 45 active credits and guarantees with 39 different ASADAs across the country. (All data about the number of loans provided below were provided by the BPDC in 2023 and compiled by the authors.)

The Business and Corporate Bank of the BPDC

The Business and Corporate Bank arm of the BPDC conglomerate provides regular access to business loans from the BPDC's own funds to Costa Rica's

ASADAs. These loans represent the largest portfolio with respect to BPDC loans in the water sector in terms of amount of money. ASADAs that access credit from this part of BPDC operations tend to serve larger populations, be more financially developed and have higher administrative capacity than their peers. Since these loans are part of the “normal” business operations of the bank, there is no set limit on the size of the loans. Nor are there special concessional interest rates or repayment schedules. For example, the Río Blanco ASADA took out a loan from the Business and Corporate Bank and used it to buy property in the community where two of its wells are located in order to protect groundwater resources.

The Business and Corporate Bank also provides BPDC contributions to the national SBD. The BPDC does so via FOFIDE (Fondo de Financiamiento para el Desarrollo, or Development Finance Fund). FOFIDE is designed to contribute to MSMEs. In particular, FOFIDE has specific target clients: women entrepreneurs (Mujeres, BP Empresarias); financial inclusion through microfinance (Población con baja inclusión financiera, Microfinanzas); and water (Agua, ASADAS). FOFIDE identifies ASADAs that are focused on the protection of the water supply for their regions as target clients. FOFIDE provides financing for the development of a fixed-term investment plan. ASADAs may borrow up to US\$188,000 with a term of up to 240 months with interest at the basic passive rate set by the Central Bank of Costa Rica (otherwise known as the prime rate), which varies over the term of the loan. In June 2023, the basic passive rate was 6.33 per cent. For example, the Corralillo Nicoya ASADA obtained a loan from FOFIDE to purchase equipment, build an office and warehouse, and purchase the land where the buildings are located.

As of June 2023, there were 33 active loans to ASADAs with the Business and Corporate bank in these two portfolios: 11 with the bank’s funds, 21 with FOFIDE and one being a mix of the two.

The Social Development Bank of the BPDC

The Social Development Bank arm of BPDC offers financing to sectors of the social economy that are unable to access regular BPDC loans. Therein, the Social Development Bank has a special fund for the development of MSMEs (Fondo Especial para el Desarrollo de las micro, pequeñas y medianas empresas or FODEMIPYME). FODEMIPYME was created in 2002 by Law 8262, the “Law for the Strengthening of Small and Medium-Sized Enterprises.” The BPDC dedicates 5 per cent of its corporate profits to this fund. In addition to loans, FODEMIPYME provides grants and guarantees. Grants tend to be for technical training and other capacity-building activities, but not for financing infrastructure. As we explain in more detail below, to access this fund, the ASADA must have a certificate from the Ministry of Labour and Social Security that demonstrates that it is a social economy organization. The ASADA also needs to show capacity to pay (for example, income from

tariffs) but it does not have to have any other form of collateral. ASADAs can borrow up to US\$50,000 with a term of up to 120 months with interest at the basic passive rate plus a risk margin. As of February 2023, there are ten active funds for ASADAs under this programme. For example, the Sarapiquí ASADA received a loan from this fund to finance the construction of a warehouse and purchase the land where the building is located.

The special development fund (Fondos Especiales de Desarrollo, or FEDE) of the Social Development Bank is the most solidaristic of the BPDC loan programmes. The FEDE was created in 2011 thanks to a demand from the Workers' Assembly. This programme is financed by part of the 15 per cent of BPDC's corporate profits. FEDE supports ASADAs, as well as projects for social housing and community organizations in various sectors. FEDE is aimed at smaller ASADAs with lower capacity to pay. Importantly, as Solano Garro notes above, these funds are not "regulated," meaning that the amounts do not appear in the BPDC's balance sheet. ASADAs can borrow up to US\$275,000 from this fund. Loans have very flexible terms, and the interest rate is a basic passive rate with a ceiling (limit) that is guaranteed at the time the loan is granted. As of February 2023, there were two active credits to ASADAs under this programme. For example, the San José de la Montaña ASADA received a loan from this fund to build a new, modern office building for their administrative personnel.

Why the low level of take-up of BPDC loans?

When we inquired in interviews as to the reasons for why so few ASADAs had loans from the BPDC, respondents emphasized that it was not related to lack of demand for finance amongst ASADAs, nor the BPDC's lack of supply of sufficient, appropriate and affordable credits. Rather, they identified the problem as resting with the bureaucracy (interviews 1–7, 15–17). In the process of negotiating and seeking approval for a loan, ASADAs and the BPDC personnel face many barriers created by the regulatory system established by the national government and the AyA.

It is important to stress that the ASADAs in a position to secure bank loans to improve their services—such as the ASADAs featured in this chapter—are the exception rather than the rule. A report commissioned by the AyA nearly two decades ago estimated that out of the 1700 ASADAs at the time, only about 12 per cent were in a financial position to obtain credit (Lockwood 2004). Around 40 per cent were estimated to have savings of more than US\$2000. Nearly half, however, were facing financial problems of one kind or another (Lockwood 2004, 35). While the AyA has made efforts over the past two decades to help ASADAs build administrative and technical capacity, the lack of savings and access to appropriate financing remains a problem. For example, in a 2021 survey of 38 ASADAs in the water-stressed north of the country, "lack of financing" was identified as the most important challenge affecting their sustainability (55 per cent of respondents) (UNDP 2021, 74).

Table 7.3 ASADAs interviewed for this study

ASADA, location (canton)	Rio Blanco, Limón (Central)	Sarapiquí, Heredia (Sarapiquí)	Corralillo Nicoya, Guanacaste (Nicoya)	San José de la Montaña, Heredia (Barva)
Type of loan	Normal loan (Business and Corporate Bank)	FODEMIPYME (Social Development Bank)	FOFIDE (Business and Corporate Bank)	FEDE (Social Development Bank)
Regulated or unregulated	Regulated	Regulated	Regulated	Unregulated
Loan amount	Not available	CRC 55 million (approx. US\$101,000)	CRC 40 million (approx. US\$73,500)	CRC 165 million (approx. US\$303,000)
Term of payment	15 years	12 years	20 years	10 years
Reason for loan	Land with two wells and a house; protect the watershed	Land and infrastructure, warehouse	Land and equipment, office and warehouse	New office for administrative personnel
Qualification in AyA's Blue Flag Programme ^a	A	A	B	A
Number of subscribers	2300	4000	540	1759
Population benefitting from loan	8000	18,000	1890	7000

Source: Authors, based on interviews and analysis of documents.

Note: ^aAyA's Blue Flag programme is a benchmarking system that aims to promote environmental responsibility and quality water services.

This was followed closely by challenges related to “lack of technical capacity” and “institutional support” (45 per cent for both).

However, it is not the case that ASADAs are uniquely cash strapped compared to other water operators. Indeed, most water operators—even those in large cities in North America and Europe—are not able to generate the income needed for capital investments based on tariffs alone (McDonald et al. 2021; Alaerts 2019; Libey et al. 2020; Reis 2022; Heidler et al. 2023). As such, water operators throughout the world, both public and private, depend on investment and concessional loans from governments to finance both their operations and maintenance as well as capital investments needed for the expansion of infrastructure, which involves large, upfront sunk costs.

Public banks—even those with a strong social and development mandate like the BPDC—also face challenges when lending in the WSS sector because these banks must still exist and persist within a wider competitive and often financialized market (Marois 2021, 72–3). Public banks must be financially sustainable or risk collapse. Their status as banks limits their ability to offer loans to operators that have weak capacity to pay. As one former BPDC executive explained in an interview, many ASADAs do not possess resources that can be considered collateral (referring to an asset that could be seized or sold off should a loan become non-performing). In the case of the WSS sector, the infrastructure needed to make water drinkable and transportable (such as wells, pumps and pipes) is not easily dug up, uninstalled and sold off for cash. In short, the only collateral some ASADAs might have are cash savings, real estate, equipment and vehicles (interviews 1, 16). A further complication that interviewees stressed is that water services are essential services, and water is a natural resource that is under the public domain (interviews 1, 16). The human right to water is now enshrined in Costa Rica’s constitution. As such, the ASADA’s most precious asset—water—cannot be seized in the cases of non-payment of a loan.

Nevertheless, in the case of the FODEMIPYME, BPDC managers have found creative ways to redefine what can be considered a guarantee for a loan to work around this constraint. Under this fund, the BPDC has been able to lend to an ASADA with no fungible assets by asking them to move their users’ payment accounts to the BPDC. In this way, the cash flow generated by users paying their water bills serves as the guarantee. This form of financial conditionality may be seen as developing a form of public bank–public water collaboration designed to overcome some of the structural barriers that are characteristic of contemporary financial markets. At the same time, it helps to sustain, and even foster, future public banking capacity.

In this regard, BPDC personnel recounted the legal and institutional challenges barriers that they have confronted in trying to find ways to finance ASADAs (interviews 9–14). For example, when the FODEMIPYME programme first started, ASADAs were classified as small businesses to be able to access these loans. However, the new minister at the time objected to the classification, noting that ASADAs are not for-profit businesses but rather essential service providers. By working together, public servants from BPDC and AyA found a solution that acknowledges that while ASADAs are MSMEs, they are also companies that provide an essential public service on a not-for-profit basis. An ASADA applying for the fund must now seek certification as a “social enterprise” from the Ministry of Labour and Social Development in order to qualify. However, this requirement erects yet another hurdle (or unintended consequence) in what is already a time-consuming and highly bureaucratic process.

Many of the interviewees complained about problems created by AyA’s high degree of centralization. Under the terms of the delegation agreements, an ASADA must begin its request at one of the regional offices but get

approval from the AyA board of directors at the San José central office to qualify for a loan. Sometimes, loan requests are approved at the regional office only to be rejected by the central office. A retired manager of the BPDC social funds describes it as being a very frustrating process:

Other colleagues from the bank would say...“I do not want to work with the ASADAs.” It is a lot of work, and it is slow. [The project] passes by the whole cavalry of the AyA. First the regional office, [...] then the legal department, which would always send the file back. [...] In the meantime, the original documents expire. We at the BPDC cannot approve the loan until we have the go-ahead from the Board of Directors of the AyA. So, the process to approve a loan takes at least a year, or a year and a half.

(Interview 16)

As a former project manager with the BPDC, Geovanny Mora, put it succinctly, working with the ASADAs and the AyA requires “Franciscan patience”—perhaps adding new connotations to the economic term “patient finance.” Elected officials from ASADAs expressed similar frustration (interviews 2–3, 5–7, 15). In one extreme case, an ASADA reported that nearly five years had elapsed from the time of application until the first disbursement of the loan.

The AyA lacks institutional capacity to be able to process loans in a more expedient manner. In addition to providing water services to almost half of the population, AyA also serves as the sector’s regulator. Fulfilling each aspect of AyA’s mandate requires recurrent and steady resources. Both the UN Special Rapporteur on Water (de Albuquerque 2009, n.p.) and the UNDP (2021, 56) have observed that AyA staff are severely overworked, and that the agency does not have adequate personnel or operating budget to perform its various functions. As they argue, more investment is necessary for AyA to be able to fulfil its mandate. For example, the processing of BPDC/ASADA loan applications requires adequate levels of specialized staff who feel valued and empowered to do their jobs.

There is little doubt that AyA faces considerable resource constraints, both human and financial. Its main source of income is tariffs from water and sanitation services, which are set by the national regulatory agency, the Public Services Regulatory Authority (Autoridad Reguladora de los Servicios Públicos). AyA’s customers pay some of the highest water tariffs in Latin America and the Caribbean (Fernández et al. 2021, 44), but its budget for financing capital expenses in addition to operation and maintenance costs even in its own service area remains limited, leaving little space to support new WSS projects in rural areas or to increase the number of staff in its regional offices. Currently, AyA receives no fiscal transfers from the national government (interview 8; Fernández et al. 2021). The AyA also obtains sovereign-backed loans from multilateral and foreign national public banks (such as the Inter-American Development Bank, the CABEI and the German KfW) but is responsible for the corresponding debt service costs and capital

repayment (Fernández et al. 2021, 34). This puts further pressure on the AyA budget. Policy change is required to enable AyA to be better at supporting public–public collaborations.

Notwithstanding the challenges, in their current form, the BPDC’s loan programmes for the ASADAs are considered successful, at least from the BPDC’s perspective. In addition to the fact that the loans support the delivery of vital services in communities, as Geovanny Mora, former chief area supervisor of special funds for the Social Development Bank put it, the ASADAs “are good customers” (interview 1). The ASADAs with loans from the BPDC have all paid on time. Impressively, ASADAs kept up their payments during the COVID-19 pandemic, even though the government imposed a moratorium on water cut-offs from March to October 2020. Mora explained that in the special funds (including FEDE), the BPDC made two decisions in the first weeks of the pandemic to ease financial stress. First, the bank lowered the base interest rate from 6.5 to 4 per cent in each of the three loan portfolios (ASADAs, housing and social organizations in various sectors). Second, in the housing portfolio, the BPDC implemented a moratorium on payments of the principal. Since these tend to be the largest loans in their portfolio, in some cases, a customer’s payment would drop by about 75 per cent. As Mora explained, “it meant that customers could pay their other bills, such as water and electricity.” In total, during the intense pandemic years of 2020–21, the default in payment of the special development funds (FEDE) went up from 5 to 6 per cent, a very slight increase despite the severity of the COVID-19 crisis.

In sum, the BPDC is playing an important supporting role in financing the expansion of quality water services in Costa Rica by providing a combination of “hard” and “soft” loans to water providers, but these programmes could be expanded.

Strengthening public–public collaborations

If Costa Rica is to meet its SDG targets for water, particularly for sanitation and climate change, what is needed is not just more financing but more supportive, appropriate and patient financing. This means fostering and expanding innovative public bank–public water collaborations—such as that developed between the BPDC and the ASADAs—and expanding the loan programmes offered by public banks such as the BPDC to include the AyA.

Expanding the BPDC programmes to be able to serve smaller and more vulnerable ASADAs will require a renewed commitment to the social development mandate of the bank and strategic policy decisions about how to offset higher levels of risk within the BPDC. Making this strategy viable requires dialogue with and support from the national government. The costs and losses associated with concessional water lending need to be covered by dedicated government financial transfer or through democratically determined concessions made from within the BPDC.

At the strategic–institutional level of the BPDC, the board and senior management could task the BPDC with playing a larger role in the WSS sector (backed, or pushed, by the Workers’ Assembly). This could be done by setting quotas and creating incentives to bank personnel to offer more loans to ASADAs. Currently, the BPDC plays a somewhat passive role by waiting for ASADAs to come to the bank to solicit services. Efforts to advertise the existing programmes could be strengthened by having BPDC personnel with experience negotiating these loans attending association meetings of the community-based water operators and ASADAs.

Another way to create incentives is to improve the way that the BPDC measures the impact of its activities. For example, the impact of the FEDE funds is currently not measured in any discernible way except financial return. In Argentina, FONPLATA has made results related to job creation and employment equity a key criterion for the allocation and monitoring of the loan (see Tobías & Case-Ruchala, this volume). Efforts to benchmark the BPDC’s performance could also make better use of social indicators. The co-creation of transparent metrics that matter to both the funder and the affected community increases the effectiveness and efficiency of finance for development projects, not to mention allowing spacing for democratic oversight and consent (see Ray et al. 2020; Marois 2022; Marois et al. 2023).

Finding a path forward also entails finding the right balance between the need for regulatory oversight and operational speed. In the current regulatory framework, if any ASADA fails to pay back their loan, the AyA has the authority to put in place measures to rectify the situation, including dismissing the volunteer board of directors and seizing accounts to ensure that creditors are paid. The AyA is therefore absorbing the perceived risk of BPDC’s investments by acting as a guarantor. So, while bureaucratic delays involved in the loan approval process require patience from bank personnel trying to meet yearly targets, these steps also provide a guarantee that once the project is approved ASADAs are very unlikely to default. Nonetheless, the AyA could streamline its procedures and delegate some of the decision making for the smaller loans to the regional offices. To make this possible, the AyA would need to increase the number of qualified personnel in the regional offices who are empowered to make these judgments and boost capacity in the central office as well, in order to prevent delays.

Here, there is another possibility of deepening the collaboration between the two public entities. As we have documented in this chapter, the BPDC has found imaginative ways to support and strengthen the participation of local communities in improving water and sanitation management by offering a variety of different kinds of loans under conditions tailored to meet the ASADAs’ needs. The BPDC has developed valuable expertise in the process. One of the former BPDC executives put it as follows: “I can tell almost immediately by looking at an ASADA’s accounts what their capacity is to pay”

(interview 1). The AyA, BPDC and ASADAs could create a collaborative funding panel composed of representatives from each institution to decide on financing requests. Such an initiative would have the knock-on benefit of democratizing credit and promoting financial knowledge building outside of the banks and water-provisioning knowledge within the banks.

Finally, finding a path forward will also require a new financing strategy designed to address existing service gaps. One option involves creating a line of institutional credit for the AyA. The BPDC has financed the public electricity company, the Costa Rican Electricity Institute (Instituto Costarricense de Electricidad) in this way, but it has no active credits with the AyA. The AyA could then expand its own services and play a more direct and rapid role in allocating credit to ASADAs, particularly to address service gaps in sanitation and drinking water provision in rural and remote communities. In moving forward, the BPDC can deepen relationships built with the AyA and other key stakeholders to drive more innovative and responsive policy-based programmes. The public sector can and should lead in the area, reclaiming and bolstering pro-public capacity.

One public bank such as BPDC should not be expected to resolve the water finance challenge alone, of course. New forms of non-competitive collaboration are needed. We concur with researchers who have called for increased financing from the international community for community-based management in Costa Rica, as well as in Nicaragua and Honduras (Romano et al. 2021, 815). However, in a place like Costa Rica, which has a robust public banking sector, these funding streams can come from *national* as well as international sources. Domestic public banks have a vital role to play in financing WSS infrastructure in communities and local regions. That is, banks like the BPDC can fill in part of the gap with patient domestic finance. Domestic banks reduce the cost of capital, notably foreign currency capital, which has the added advantage of lessening the currency risk (McDonald et al. 2021; Reis 2022). In addition, domestic public banks also fill the knowledge gap given their locations within communities and knowledge of the local economy (Buhr et al. 2018).

To these ends, one of the most innovative ideas gaining traction in international policymaking and climate finance circles is the creation of a syndicated public–public loan programme involving multilateral, foreign development and national development banks (Marois et al. 2023). The recently formed Water Finance Coalition of the French Development Agency (AFD) and the Finance in Common Summit is a nascent attempt to foster this kind of collaboration for SDG 6, Water for All. In Costa Rica’s case, the AyA and the BPDC could take the initiative in cooperation with the other national public banks, such as the Banco Nacional and the Banco de Costa Rica, along with financing from multilateral development banks, such as CABEL, and from foreign public banks like the KfW and French Development Agency. Such a public–public syndicated loan programme would help distribute the

risk amongst several actors in the financial ecosystem, reduce the costs of capital, and do so while maintaining a clear public purpose of supporting public WSS services.

It would be possible, for example, to create a public syndicated loan programme in Costa Rica dedicated to the WSS sector, especially for upgrading systems to improve water quality, expanding sanitation services and helping communities adapt to climate change. Improving water quality requires improving sanitation by reducing contaminants entering surface and ground water. Historically, sanitation is the most expensive part of the service. Even once the networked infrastructure is built, providers face the “last mile” problem as households are reluctant to connect without proper incentives (Hall & Lobina 2008; Reis 2022). Meeting Costa Rica’s goals for sanitation will require much higher levels of public investment. A multilateral public–public programme could also blend in grant and development assistance funds to support such infrastructure in ways that are climate resilient and equitable.

Conclusion

Although not without challenges, the relationships between the BPDC and the ASADAs are an example of a successful public–public collaboration. The BPDC has carved out an important niche within a broader financial ecosystem. The BPDC could play an even greater role in financing the water sector, and it is interested in doing so. However, the BPDC cannot replace the government in investing in infrastructure given its limited resources and the fact that it is a bank responsible for its own institutional sustainability. It must finance projects that are financially viable. Where BPDC does not have sufficient or appropriate resources itself, the national government, foreign aid agencies and multilateral institutions can partner to enhance the BPDC’s capacity to deliver patient and appropriate financing at the local level, along with other public banks.

The BPDC is therefore an important actor in the story of financing public water and sanitation systems, but it plays a crucial *supporting* role. It is not a silver bullet in and of itself. The problems of uneven service coverage and quality, expanding sanitation services to mitigate the pollution problems and meeting the needs to adapt to climate change cannot be solved by public banks alone. National public water providers, like AyA, must innovate and find ways to reduce internal barriers to the delivery of effective and equitable WSS services. The national government must sufficiently resource and support *pro-public* public entities, and in doing so reclaim their public purpose. Multilateral and international actors need to rethink the disproportionate focus on leveraging and blending private finance and instead provide the resources needed to support existing public institutions, which is where the possibility for innovation lies.

Note

1 Website of the SBD: <https://app.powerbi.com/view?r=eyJrIjoiZTNmM2QyMTAtMTVjMS00M2U2LTk2ZDAtMjAzMjE5NGIwNzk0IiwidCI6IjQxOTEwZmU0LTc0Y2MtNDA3NC1iMjFjLTI4YmJmNzg3MjI4MCIslmMiOjR9>. Accessed June 26, 2023.

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Appendix A: Interviews conducted

<i>Interview</i>	<i>Name</i>	<i>Role</i>	<i>Date</i>
1	Geovanny Mora Charpentier	Retired, former Chief Area Supervisor of Special Funds, worked at BPDC for 15 years	February 17, 2023
2	Guiselle Urbina	President of ASADA Rio Blanco	February 20, 2023
3	Julissa Jiménez	Administrator at ASADA Rio Blanco	February 20, 2023
4	María Fernanda Vargas Gonzalez	Advisor at Fundación Avina	February 21, 2023
5	Rodolfo Gamboa	Administrator at ASADA José de la Montaña	February 21, 2023
6	Rubén Salas	President at ASADA Sarapiquí	February 22, 2023
7	Zaray Molina Herrera	Administrator at ASADA Sarapiquí	February 22, 2023
8	Rosa María Gómez Arce	General Director Sustainability Service at AyA	February 24, 2023
9	Omar Sánchez Lizano	Director of the Social and Development Bank at BPDC	February 27, 2023
10	Eddie Garro Elizondo	Chief of the Special Funds, Social and Development Bank at BPDC	February 27, 2023
11	Roger Conejo Cubero	Director of Business and Corporate Bank at BPDC	February 27, 2023
12	Ana Lucía Solano Garro	Executive Advisor in Promotion and Development of the Social and Development Bank at BPDC	February 27, 2023
13	Alejandro Grossi Vega	Director of FODEMIPYME at BPDC	February 27, 2023
14	Juan Francisco Rodríguez Fernández	Businesses Deputy Manager at BPDC	February 27, 2023
15	Mario Alberto Paniagua Rodríguez	President of ASADA Nicoya	February 27, 2023