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PANAMA

Key Economic Indicators

(Millions of U.S. dollars unless otherwise indicated)

	1998	1999	2000 1/
Income, Production and Employment:			
Nominal GDP	9,143	9,608	10,049
Real GDP (1982 prices)	6,933	7,158	7,344
Real GDP Growth (pct) 2/	3.9	3.2	2.6
Real GDP by Sector (1982 prices):			
Agriculture	449	461	508
Manufacturing	1,304	1,340	1,344
Services	4,206	4,347	4,470
Government	974	1,009	1,022
Real Per Capita GDP (US$)	2,509	2,577	2,648
Labor Force (000s)	1,083	1,089	1,095
Unemployment Rate (pct)	13.4	11.6	N/A
Money and Prices (annual percentage growth):			
Money Supply (M2) Growth (pct) 3/	13.0	8.5	2.8
Consumer Price Inflation	0.6	1.5	1.8
Exchange Rate (Balboa/US$ annual average) 4/	1	1	1
Balance of Payments and Trade:			
Total Exports FOB 5/	784	821	779
Exports to U.S.	312	364	268
Total Imports CIF 5/	3,398	3,440	3,442
Imports from U.S.	1,753	1,742	1,764
Trade Balance 5/	-2,614	-2,619	-2,663
Balance with U.S.	-1,441	-1,378	-1,502
Colon Free Zone 6/			
Exports	6,001	5,160	5,377
Imports	5,318	4,230	4,657
CFZ Balance	683	930	720
External Public Debt 7/	5,179	5,411	5,332
Fiscal Deficit (-)/GDP (pct) 8/	-4.4	-1.6	-1.5
Current Account Deficit (-)/GDP (pct)	13.2	13.9	13.4
Debt Service Ratio (pct)	7.6	11.5	N/A

Gold and Foreign Exchange Reserves 9/	1,370	1,516	1,616
Aid from USAID	4.8	5.3	4.4

1/ Figures for 2000 are estimated unless otherwise indicated.
2/ Embassy Estimate
3/ Figure is based on IMF 10/2000 International Financial Statistics. M2 = Deposit Money + Quasi Money.
4/ The balboa/dollar exchange rate is fixed at 1:1. The legal tender is the U.S. dollar, so there is no parallel exchange rate.
5/ Trade statistics do not include the Colon Free Zone.
6/ The Colon Free Zone (CFZ) is the largest free trading area in the hemisphere.
7/ External debt balance on June 30, 2000.
8/ Figures indicate deficit of the non-financial public sector as percent of GDP.
9/ Figure is based on IMF 10/2000 International Financial Statistics. Panama reports no gold holdings.

1. General Policy Framework

Panama’s economy is based on a well-developed services sector that accounts for just over 60 percent of GDP. Services include the Panama Canal, container port activities, shipping, flagship registry, banking, insurance, as well as wholesaling and distribution out of the Colon Free Zone. The industrial sector, which accounts for 19 percent of GDP, is made up of manufacturing, mining, utilities, and construction. Agriculture, forestry and fisheries account for 7 percent of GDP. Government accounts for the remaining 14 percent of GDP.

The economy grew 3.2 percent in real terms in 1999, down from 3.8 percent in 1998. The Government of Panama estimates growth in 2000 of slightly below three percent, but independent economists forecast even slower growth. Economic growth has been hindered by the continued slump of the Colon Free Zone, the departure of the U.S military, and the general economic uncertainty that followed the change in governments. Another impediment has been the inexperience of the new administration. The Moscoso Administration lacks a clear economic agenda and has as yet neglected to address matters of concern to business, such as Panama's debt, fiscal imbalance, and costly labor law. This has created a feeling of uncertainty about Panama's business prospects and has slowed new investment. A rare, recent instance where the Panamanian government acted to bolster Panama's business reputation was its passage of laws to address international criticism that Panama is soft on money laundering. Nevertheless, slower growth and unemployment are on Panama's short- and medium-term horizon.

The main culprit for the decline of the Colon Free Zone is the continued political instability and accompanying economic downturn in its principal customer countries Venezuela, Colombia, Peru, and Ecuador. Weather problems, shrimp viruses, European banana policy, inefficiency, and labor disputes continue to hurt Panamanian agricultural exports harshly. Consumer spending slowed during the first half of the year. The combination of relatively high costs for utilities and low productivity of labor continues to make unit production costs higher than average for the region. The construction industry, although not nearly as vigorous as a year ago, maintains solid growth, fueled mainly by easy bank credit and the availability of capital fleeing South America.

Overall, the state has reduced its direct involvement in the Panamanian economy in recent years. Despite this favorable trend, the Panamanian government has retained market-distorting indirect taxation as well as investments in recently privatized telecommunications, ports, and energy sectors. To their credit, the previous and current Panamanian government have lowered Panama’s budget deficit from 4.4 percent to 1.6 percent and 1.5 percent respectively. The incoming administration of Mireya Moscoso (September 1999) slowed the trade liberalization and privatization trends of the previous government, especially as the new competition began. In its second month in office, it dramatically raised tariffs on some agricultural goods. For a brief period after Panama joined the World Trade Organization (WTO), it had the lowest tariffs in Latin America. The Moscoso hike took agricultural tariffs to the top limits of Panama’s WTO accession binding, with some levies reaching 300 percent. Privatization of the few remaining inefficient government enterprises has been stalled, contrary to pledges to the International Monetary Fund.

The use of the U.S. dollar as Panama's currency means fiscal policy is the government's only macroeconomic policy instrument. Therefore, government spending and investment are strictly bound by tax and nontax revenues, as well as by the government's ability to borrow. The latter may be reaching its upper limits, as Panama's overall debt is now nearly 60 percent of GDP. The new government has postponed tax and spending reform in the face of a slowing economy. The newly published budget points to the need for increased social spending, but does not address how the government intends to obtain such new funds.

The government recently has initiated several programs to boost tourism. Proposals in the new budget also point for increased government spending in the tourist sector. The government also supported the development of new facilities in two Colon ports for visits by cruise ships for the first time since 1965. That said, tourism promotion infrastructure and ancillary service support have not kept pace with ambitious public sector projections for the sector.

2. Exchange Rate Policy

Panama's official currency, the balboa, is pegged to the dollar at a 1:1 ratio. The balboa circulates in coins only. All paper currency in circulation is U.S. currency. The fixed parity means the competitiveness of U.S. products in Panama depends on transportation costs as well as tariff and nontariff barriers to entry. U.S. exporters have no risk of foreign exchange losses on sales in Panama.

3. Structural Policies

In her election campaign, President Moscoso promised to repeal the drastic reduction of agricultural tariffs by her predecessor, and to improve the lot of Panama's poor, especially the rural poor. The Panamanian government has not undertaken any further initiatives toward trade liberalization nor reduction of structural economic distortions. Privatization of the state-run water and sewage company (IDAAN) is off the table, and a similar plan for the international airport is on hold. A bid tender for the local convention center was just held and the government plans on releasing the winner's name in early October. Progress to attract investment in the reverted areas was slowed due to the government transition, and continues to suffer due to internal differences over plans for major new projects. Panama remains close to completing a free trade agreement with Mexico, but talks are bogged down over differences in the financial services and agricultural sectors, even despite a high-level visit by President Moscoso to Mexico City.

Foreign investment, much of it American, flowed into Panama at a steady pace under the former Perez-Balladares Administration. American energy, telecommunications and port/cargo companies invested significant amounts in newly deregulated and/or privatized sectors and companies. However, the current government has done little for the new investors of the previous administration, and FDI has now reached its lowest level in over a decade. Moreover, various Panamanian government entities have adopted confrontational postures in dealing with many of these new investors, thus discouraging new forays. An unhelpful Panamanian government attitude and festering disputes have discouraged potential investors from setting up in Panama.

The restrictive Panamanian Labor Code was revised in 1995, though strong opposition allowed only marginal reform. Unions continue to oppose reform initiatives, on occasion violently. Notwithstanding several health and housing programs, government and World Bank estimates claim nearly 40 percent of Panamanians live in poverty. Considering the relatively high per capita income level of over $3,600 (current dollars), Panama's historically skewed income distribution does not appear to be abating. Panama's constitution requires that the minimum wage be reviewed every two years. In 2000 the Panamanian government raised the wage 12 percent or just over $250/month to the applause of the business community and the ire of workers. The unrest ended when Moscoso pledged future wage raises would amount to 40 percent by the end of her term.

Panama maintains no restrictions on capital flows or capital repatriation by foreign investors, nor does it reserve large sectors of the economy for its nationals.

4. Debt Management Policies

Panama's public external debt totaled $5.33 billion dollars at mid-2000. Although Panama's sovereign debt remains just below investment grade, several Panamanian banks enjoy investment grade status. Panama's outstanding domestic debt was $2.27 billion at mid-year. The newly installed government has stated publicly its reluctance to take on more foreign debt, but accrued $400 million in its first year and plans on taking another $500 million in the 2001 budget. That said, overall public debt should fall slightly by the end of the year, as principal amortization will exceed new borrowings by $30 million. Debt service (principal and interest) will exceed $1.7 billion (20 percent of GDP) this year. The current Panamanian government intended to pay down some of its debt, with proceeds from the sale of the Panamanian government's stock in the private telephone monopoly run by Cable and Wireless (UK) and its Fiduciary Fund, a government holding accumulated from various recent privatizations, but failed to garner the support from its then majority in the National Assembly. As a result, Panama's $1.35 billion Fiduciary Fund remains, for now, subject to strict investment and capital preservation guidelines.

5. Aid

Development assistance from the United States in 1999 totaled $5.3 million. In addition, the United States Department of Agriculture's Animal and Plant Health Inspection Service (APHIS) operates a screw worm eradication program in Panama. APHIS plans to build a sterile screw worm fly plant in Panama at a cost of roughly $80 million, for entry into service in 2003.

Development aid from other sources came primarily from the Inter American Development Bank (IDB), which currently possesses a $953 million portfolio for Panama ($911 million to be disbursed within the next four years), and a standby agreement (not disbursed) from the International Monetary Fund (IMF). The World Bank funds various development and infrastructure projects in Panama. The U.S. State Department's Narcotic Affairs Division gave over $500,000 in FY2000 to combat illegal activities in Panama. The Republic of China and the government of Japan both have given significant amounts of aid in both 1999 and 2000.

6. Significant Barriers to U.S. Exports

Panama's accession to the WTO transformed for the better a tariff regime that just a few years earlier was one of the highest in the region. However, the new Moscoso government's primary trade initiative was an abrupt increase in tariffs on various agricultural imports. Through its Ministry of Agricultural Development, Panama has also adopted a *de facto*, arbitrary import licensing regime for goods that are subject to sanitary and phyto-sanitary permits under Panamanian law. The plant inspection and certification process required of foreign meat and poultry processing plants is time consuming, lacks transparency, and constitutes an additional barrier.

The Panamanian judicial system presents another potential obstacle to investors and traders. There is a large backlog of criminal and civil cases, which can take several years to be resolved. Many investors have concerns over the potential for corruption in the judicial process.

As a WTO member, Panama has ensured that its customs valuation system now conforms to international standards. Overall, the processing of customs documents for manufactured or mineral imports is reasonably quick, efficient, and reliable. However, some importers have complained of product misclassification and, in isolated cases, demands for excessive duties. Importers of agricultural goods continue to face sudden and arbitrary changes in procedures and practices. Panama is an active participant in negotiations for the FTAA and will serve as host for the new round of negotiations that are to begin in March 2001.

In the financial services sector, restrictions on foreign ownership are minimal except in the case of non-bank finance companies. U.S. banks, insurance companies and brokerages are welcome and in some cases are leaders in the local market.

7. Export Subsidies Policies

Panamanian law allows any company to import raw materials or semi-processed goods at a duty of three percent for domestic consumption or production, or duty free for export production. In addition, companies not already receiving benefits under the Special Incentives Law of 1986 are allowed a tax deduction of up to 10 percent of their profits from export operations through 2002. The Tourism Law of 1994 (Law 8) allows deduction from taxable income of 50 percent of any amount invested by Panamanian citizens in tourism development.

Because of its WTO obligations, Panama has revised its export subsidy policies. The Tax Credit Certificate (CAT), which used to be given to firms producing nontraditional exports when the exports' national content and value-added met minimum established levels, will be gradually phased out. The policy allows exporters to receive CATs equal to 15 percent of the exports' national value-added until the year 2002, down from 20 percent prior to 1998. After 2002, the program will be eliminated. The certificates are transferable and may be used to pay tax obligations to the government, or they can be sold in secondary markets at a discount. The government has become stricter in defining national value-added, attempting to reduce the amount claimed by exporters.

A number of industries that produce exclusively for export, such as shrimp farming and tourism, are exempted from paying certain types of taxes and import duties. The Government of Panama uses this policy to attract foreign investment. Companies that profit from these exemptions are not eligible to receive CATs for their exports.

Law 25 of 1996 provides for the development of "export processing zones" (EPZ's) as part of an effort to broaden the Panamanian manufacturing sector while promoting investment in former U.S. military bases that were transferred to Panamanian control. Companies operating in these zones may import inputs duty-free if products assembled in the zones are to be exported. The government also provides other tax incentives to EPZ companies. Most EPZ's remain in the early stages of development, with only a few tenants. They are growing sporadically depending on location.

8. *Protection of U.S. Intellectual Property*

Intellectual Property Rights: Panama is a member of the World Intellectual Property Organization (WIPO), the Geneva Phonograms Convention, the Brussels Satellite Convention, the Universal Copyright Convention, the Bern Convention for the Protection of Literary and Artistic Works, the Paris Convention for the Protection of Industrial Property, and the International Convention for the Protection of Plant Varieties. In November 1998 it was one of the first countries to ratify the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty.

Protection of intellectual property rights in Panama has improved significantly over the past several years, but serious concerns remain about widespread use of pirated software in government offices, inadequate border measures to combat transshipment of counterfeited goods through Panama, and enforcement in the Colon Free Zone (CFZ). In 1998 an Intellectual Property Department was created in the CFZ. This is viewed as a positive step demonstrating Panama's will to improve enforcement, and the new Department has enjoyed some success, but an expanded effort will be required to address this problem more completely.

In August 1994 the Legislative Assembly passed Law 15 (the Copyright Law) to help modernize copyright protection. This comprehensive copyright bill was based on a World Intellectual Property Organization model. The law modernizes copyright protection in Panama, provides for payment of royalties, facilitates the prosecution of copyright violators, protects computer software, and makes copyright infringement a felony.

A new Industrial Property Law (Law 35) went into force in November 1996. It provides 20 years of patent protection in place of the former period of 5 to 15 years for foreigners and 5 to

20 years for Panamanians. The law grants patent protection from the date of filing. Pharmaceutical patents are granted for only 15 years, but can be renewed for an additional ten years, if the patent owner licenses a national company (minimum of 30 percent Panamanian ownership) to exploit the patent. The law also provides for protection of trademarks, simplifying the process of registering trademarks and making them renewable for ten-year periods. The Industrial Property Law provides specific protection for trade secrets.

The government also passed an Anti-Monopoly Law in early 1996 mandating the creation of four commercial courts to hear anti-trust, patent, trademark, and copyright cases exclusively. Two courts and one superior tribunal began to operate in mid-1997, but establishment of the other courts has been delayed. Some U.S. intellectual property owners have experienced significant delays when they have sought infringement remedies in the Panamanian judicial system.

Over the past several years, Panamanian authorities have conducted numerous raids against large video piracy operations, and several cases are pending in the courts. In a series of raids in late 1998, authorities seized more than five million pirated compact discs being transshipped through Tocumen International Airport, believed to be the largest seizure ever in Latin America.

Although the Attorney General's Office has taken a vigorous enforcement stance, the Copyright Office has been ineffective, and Panama's judicial system has not provided speedy and effective remedies for private civil litigants under the law. Panama is in the process of modernizing its copyright registration and patent and trademark registration capabilities. The government is also drafting amendments to its copyright law that would fully implement the new WIPO treaties. An initiative which would consolidate copyright, patent, and trademark functions into a single autonomous entity and another initiative to create a specialized Prosecutor's Office for IPR have been delayed due to resource constraints and government transition.

9. Worker Rights

a. *The Right of Association:* Private sector workers have the right to form and join unions of their choice, subject to registration by the government. The government does not control nor financially support unions, but most unions are closely affiliated with political parties. There are over 250 active unions, grouped under 6 confederations and 48 federations, representing approximately 10 percent of the employed labor force. Civil service workers are permitted to form public employee associations and federations, though not unions. Union organizations at every level may and do affiliate with international bodies.

b. *The Right to Organize and Bargain Collectively*: The Labor Code provides most workers with the right to organize and bargain collectively. The law protects union workers from anti-union discrimination and requires employers to reinstate workers fired for union activities. The Labor Code also establishes a conciliation board in the Ministry of Labor to resolve complaints and it provides a procedure for arbitration. The Civil Service Law allows most public employees to organize and bargain collectively and grants them a limited right to strike.

c. *Prohibition of Forced or Compulsory Labor*: The Labor Code prohibits forced or compulsory labor, and neither practice has been reported.

d. *Minimum Age for Employment of Children:* The Labor Code prohibits the employment of children under 14 years of age as well as those under 15 if the child has not completed primary school. Children under age 16 cannot work overtime; those under 18 cannot work at night. Children between the ages of 12 and 15 may perform light farm work that does not interfere with their education. The Ministry of Labor enforces these provisions in response to complaints and may order the termination of unauthorized employment. However, it has not enforced child labor provisions in rural areas due to insufficient staff.

e. Acceptable Conditions at Work: The Labor Code establishes a standard workweek of 48 hours and provides for at least one 24-hour rest period weekly. It also establishes minimum wage rates, though in the relatively high cost urban areas, the minimum wage is not sufficient to support a worker and family above the poverty level. The Ministry of Labor does not adequately enforce the minimum wage law due to insufficient personnel and financial resources. Panamanian businesses routinely evade Social Security payroll contributions. The government is responsible for occupational health and safety standards. On paper the government has the responsibility for conducting periodic inspections of particularly hazardous work sites, but in practice its ability to perform adequate safety inspections is hindered by poor funding and the lack of trained personnel. The labor code permits workers to remove themselves from situations that present an immediate health or safety hazard without jeopardizing their jobs, however this practice almost never occurs. Health and safety standards generally emphasize safety rather than long-term health hazards, but training and workplace enforcement of safety regulations or on the use of safety equipment is lax. Complaints of health and safety problems continue in the construction, banana, cement, and milling industries.

f. Rights in Sectors with U.S. Investment: Worker rights in sectors with U.S. investment generally mirror those in other sectors. As mentioned above, the banana industry, which has significant U.S. investment, continues to produce complaints of health hazards largely due to workers' exposure to pesticides.

Extent of U.S. Investment in Selected Industries in Panama—U.S. Direct Investment Position Abroad on an Historical Cost Basis—1999

(Millions of U.S. dollars)

Category		Amount
Petroleum		648
Total Manufacturing		157
Food & Kindred Products	36	
Chemicals & Allied Products	31	

Primary & Fabricated Metals	17	
Industrial Machinery and Equipment	0	
Electric & Electronic Equipment	0	
Transportation Equipment	0	
Other Manufacturing	72	
Wholesale Trade		442
Banking		131
Finance/Insurance/Real Estate		31,805
Services		285
Other Industries		-38
TOTAL ALL INDUSTRIES		33,429

Source: U.S. Department of Commerce, Bureau of Economic Analysis.