2001 Country Reports on Economic Policy and Trade Practices
Released by the Bureau of Economic and Business Affairs
U.S. Department of State, February 2002

PANAMA

Key Economic Indicators

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

	1999	2000	2001 1/
Income, Production and Employment:			
Nominal GDP	9,556	10,049	10,245
Real GDP (1982 prices)	7,158	7,341	7,429
Real GDP Growth (pct) 2/	3.2	2.7	1.2
Real GDP by Sector (1982 prices):			
Agriculture	461	507	495
Manufacturing	1,340	1,343	1,280
Services 3/	5,356	5,571	5,654
Real Per Capita GDP (US$)	2,529	2,571	2,547
Labor Force (000s)	1,050	1,095	1,110
Unemployment Rate (pct)	11.6	13.3	N/A
Money and Prices (annual percentage growth):			
Money Supply (M2) Growth (pct) 3/	8.5	10.0	0.4
Consumer Price Inflation	1.5	1.8	0.1
Exchange Rate (Balboa/US$ annual average) 4/	1	1	1
Balance of Payments and Trade:			
Total Exports FOB 5/	822	860	906
Exports to United States	364	378	398
Total Imports CIF 5/	3,516	3,379	3,132
Imports from United States	1,742	1,764	1,409
Trade Balance 5/	-2,724	-2,519	-2,226
Balance with United States	-1,378	-1,386	-1,011
Colon Free Zone 6/			
Exports	5,160	5,377	5,430
Imports	4,230	4,657	4,843
CFZ Balance	930	720	597
External Public Debt 7/	5,411	5,332	6,278
Fiscal Deficit (-)/GDP (pct) 8/	1.6	1.3	2.5
Current Account Deficit (-)/GDP (pct)	14.4	9.1	5.9
Debt Service Ratio (pct)	8.7	10.9	8.3
Gold and Foreign Exchange Reserves 9/	823	723	1,149

Assistance from United States 10/	17.0	19.1	24.1
Assistance from All Other Sources	N/A	N/A	N/A

1/ Figures for 2001 are estimated unless otherwise indicated.
2/ Figure is based on IMF 8/2001 International Financial Statistics. M2 = Deposit Money + Quasi Money.
3/ Services total includes government spending, which accounts for roughly 14 percent of Panama's GDP.
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, 2001.
8/ Figures indicate deficit of the non-financial public sector as percent of GDP.
9/ Figure is based on IMF 8/2001 International Financial Statistics. Panama reports no gold holdings.
10/ U.S. government agencies' projections (agencies included are USAID, the Department of Agriculture's APHIS Program, and the Department of State's Narcotic Affairs Programs).

1. General Policy Framework

Panama's economy is based on a well-developed services sector that accounts for about 75 percent of GDP. Services include the Panama Canal, container port activities, shipping, ship registry, banking, insurance, wholesaling and distribution out of the Colon Free Zone, and government activities (which represents about 14 percent of GDP). The industrial sector, which accounts for 18 percent of GDP, is made up of manufacturing, mining, utilities, and construction. Agriculture, forestry and fisheries account for the remaining seven percent of GDP.

The economy grew 2.7 percent in real terms in 2000, down from 3.2 percent in 1999. The government of Panama originally estimated 2001 growth would reach 4.0 percent, but has since lowered its forecast to 1.0-1.5 percent. Some independent economists forecast even slower growth. Regardless, real per capita income has been stagnant since 1999. Economic growth has been hindered by low commodity prices for certain agricultural products, the slower than expected rebound of the Colon Free Zone, the continued effects of the departure of the U.S military, and the overall economic weakness of the region. Another debilitating factor has been the Government of Panama's incoherent economic agenda. Since its inauguration in 1999, the Moscoso Administration has also failed to address adequately matters of concern to business, such as Panama's high debt, fiscal imbalance, and costly labor law. These conditions, a protectionist retreat in some areas of trade, the loss of momentum in privatization, along with several unresolved Government of Panama investment disputes and concerns with major foreign investors, have created a feeling of uncertainty about Panama's business prospects and have slowed new investment. Slower growth and rising unemployment are likely on Panama's short- and medium-term horizon.

The main culprit for the slow rebound of the Colon Free Zone is the continued political instability and accompanying economic downturn in its principal customer countries Venezuela, Colombia, and Ecuador. Consumer spending, especially in sectors dependent on disposable income, slowed considerably 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 has reported a serious downturn in 2001, coming off two years of solid growth. Still, the industry remains heavily engaged in the Panamanian economy due to relatively easy bank credit and sustained demand for residential property by migrants from 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. It remains a large, yet passive investor in recently privatized telecommunications, ports, and energy sectors. To its credit, the current Panamanian government lowered Panama's budget deficit from 4.4 percent in 1998 to 1.3 percent in 2000. The Government of Panama's expected 2.5 percent budget deficit for 2001 falls short of its IMF commitments to have a balanced budget, as the slowing economy has raised health and other government costs and depressed revenues and tax collections. The Moscoso administration has slowed the trade liberalization of the previous government, as foreign competition has hit the agricultural sector especially hard. In its second month in office, the government dramatically raised tariffs on some agricultural goods to the top limits of Panama's binding ceilings negotiated for its WTO accession, with some levies reaching over 300 percent. Privatization of the few remaining government enterprises has been stalled, despite their persistent inefficiencies in government hands.

The government has expanded its efforts to encourage growth in the telecommunications and tourism sectors. Several tax and tariff exemptions and long leaseholds have been given to startups in these industries. The government has also moved to enhance its promotion of both these sectors to external markets and investors. It recently approved a new $10 million tourism promotion campaign and has pledged to remove some taxes on outgoing long distance calls in order to attract "call centers" to Panama.

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 80 percent of GDP. The new government postponed tax and spending reform in the face of a slowing economy in 2001, but has hinted it will propose new tax legislation in late 2001.

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

The Moscoso administration came to power in 1999 on a platform that supported higher social spending to alleviate poverty and higher tariffs to ease pressure on a suffering and politically important agriculture sector hurt by the previous Government of Panama 's sudden and dramatic trade opening. During her campaign President Moscoso questioned the government's privatization campaign and pledged to keep IDAAN, Panama's government water utility, public. Her administration's initial economic objective was to find interest rate savings on sovereign debt in order to free money for social spending. The Government of Panama also raised tariffs steeply on some agricultural goods to provide relief to some farmers. The government failed to rally public support for proposals to reduce debt and redeploy funds from privatizations and sales of former U.S. military properties. It also put the brakes, at least temporarily, on its effort to reform Panama's tax system, per its IMF commitments, due to pressure from business, labor, and the political opposition, who argued that tax reform should wait until the economy improves. Other commitments to the IMF, such as the closing of two state banks, overhauling social security, administrative reform of IDAAN, and achieving a balanced budget remain unfulfilled.

Foreign investment, much of it American, flowed into Panama at a steady pace under the former Perez-Balladares Administration. American energy, transportation, telecommunications and port/cargo companies invested significant amounts in newly deregulated and/or privatized sectors and companies. Relations between some of these investors and the current government suffered early on from various causes. The Government of Panama has lately begun to address these problems more constructively. Nevertheless, FDI has dropped considerably. Various incentives for investment exist in Panamanian law, but they are neutralized in many cases by Panama’s outdated and restrictive labor code and the small size of the domestic market.

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, albeit a recent agreement in the banana industry may provide a breakthrough in work rule modernization in that industry. Panama’s constitution requires that the minimum wage be reviewed every two years. In 2000, the Panamanian government raised the wage 12 percent or to just over $250/month and pledged future wage raises that would amount to 40 percent by the end of Moscoso’s term.

Panama is not a party to any free trade agreement. In May 2001, Panama and the Central American Common Market (CACM) agreed on a common text and format for a Free Trade Agreement. The Panamanian government is currently negotiating the list of products and services that will be covered with each participating country. The government hopes to have agreements with both Nicaragua and El Salvador by the end of 2001, with agreements with the other members of the CACM coming within 2002. After completing an agreement with the CACM, the government hopes to restart its stalled negotiations for a trade agreement with Mexico.

Panama is an active participant in FTAA negotiations, and serves as the temporary site of the FTAA Secretariat until February 2002. Panama has expressed a strong interest in becoming the permanent site of the FTAA.

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. There are no restrictions on the repatriation of profits.

4. Debt Management Policies

Panama's public external debt totaled $6.28 billion dollars at mid-2001, while domestic debt totaled just under $2.1 billion. Although Panama's sovereign debt rating remains just below investment grade, several Panamanian banks enjoy investment grade status. The Moscoso government initially stated its reluctance to take on more foreign debt, but ended up borrowing an additional $750 million in early 2001. Debt service (principal and interest) exceeded $1.7 billion (17 percent of GDP) in 2000 and will climb to 23 percent when $500 million of principal is due in February 2002. Panama's total debt has grown as a result of continuing fiscal deficits, a slowing economy, dysfunctional tax collection, and a heavy government payroll. Many expect the current Panamanian government to try once again to tap Panama's $1.3 billion Fiduciary Fund, money accrued from privatizations and the sale of former U.S. military properties, to pay down some of its debt. The government sought legislative approval for a similar measure in early 2000, but obtained only modest changes to the law governing the use of the funds. Panama's $1.35 billion Fiduciary Fund remains, for now, subject to strict investment and capital preservation guidelines. Despite the country's relatively heavy debt burden, the sovereign debt rating agencies have maintained their ratings on Panama at just below investment grade.

5. Significant Barriers to U.S. Exports

Panama's accession to the WTO transformed for the better a tariff regime that just a few years ago was one of the most protectionist in the region. However, the Moscoso government's primary trade initiative was an abrupt increase in tariffs on various agricultural imports. Through its Ministry of Agricultural Development, Panama has too frequently 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 Moscoso Administration has refused to include the Panama Canal Authority as part of it offer for accession to the WTO Government Procurement Agreement (GPA). Despite repeated efforts to engage the Government of Panama on the issue, it continues to stall the accession process.

The Panamanian judicial system presents another potential obstacle to investors and traders. There is a large backlog of criminal and civil cases that can take 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. Panama has begun to implement a system for automated, electronic submission of documents, as per its FTAA "business facilitation" obligations. Importers of agricultural goods continue to face sudden and arbitrary changes in procedures and practices.

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.

6. 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 processing, or duty free for export production, except for the several so called sensitive agricultural products, such as rice, dairy products, pork products, and tomato products. This was negotiated and approved under Panama's accession to the WTO. Extraordinary quotas have been authorized for rice and pork products when stocks have gone down in order to prevent scarcity of food products.

Because of its WTO obligations, Panama has revised its export subsidy policies. The Tax Credit Certificate (CAT), which was given to firms producing nontraditional exports when the exports' national content and value-added met minimum established levels, is scheduled to be phased out in 2002. But during the WTO Doha meetings in November 2001, the Government of Panama asked for and received an extension from the WTO regarding the use of CATs. As of December 2001, a final date for a CAT phase-out has yet to be announced. The government has become more strict in defining national value-added, attempting to reduce the amount claimed by exporters and to eliminate recently publicized cases of corruption it the system.

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.

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.

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 Panama. 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.

7. Protection of U.S. Intellectual Property

Panama is a member of the World Intellectual Property Organization (WIPO), the Geneva Phonograms Convention, the Brussels Satellite Convention, the Universal Copyright Convention, the Berne 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 addition, Panama was one of the first countries to ratify the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty.

Protection of intellectual property rights (IPR) in Panama has improved significantly over the past several years. The government passed an Anti-Monopoly Law in 1996 mandating the creation of commercial courts to hear anti-trust, patent, trademark, and copyright cases exclusively. Two district courts and one superior tribunal began to operate in 1997 and have been adjudicating intellectual property disputes. IPR policy and practice in Panama is the responsibility of an Inter-institutional Committee. This committee consists of representatives of six government agencies and operates under the leadership of the Vice-Minister of Foreign Trade. It coordinates enforcement actions and develops strategies to improve compliance with the law.

Copyrights

The National Assembly in 1994 passed a comprehensive copyright bill (Law 15), 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. Although the lead prosecutor for IPR cases in the Attorney General's Office has taken a vigorous enforcement stance, the Copyright Office remains small and ineffective.

The Copyright Office has been slow to draft and move forward further improvements to the Copyright Law to implement the new WIPO treaties (the WIPO Copyright Treaty and the WIPO Performances and Phonographs Treaty). Nevertheless, their proposal also would establish new offenses, such as for internet-based copyright violations, raise the penalties for infractions, and enhance border measures. This proposed draft legislation is moving forward with technical assistance from SIECA (the Central American Economic Integration System).

Patents

A new Industrial Property Law (Law 35) went into force in 1996 and provides 20 years of 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 Industrial Property Law provides specific protection for trade secrets.

Trademarks

Law 35 also provides trademark protection, simplifying the process of registering trademarks and making them renewable for ten-year periods. The law's most important feature is the granting of ex-officio authority to government agencies to conduct investigations and to seize materials suspected of being counterfeited. Decrees 123 of November 1996 and 79 of August 1997 specify the procedures to be followed by Customs and CFZ officials in conducting investigations and confiscating merchandise. In 1997, the Customs Directorate created a special office for IPR enforcement, followed by a similar office created by the CFZ in 1998. The Trademark Registration Office has undertaken significant modernization with a searchable computerized database of registered trademarks that is open to the public.

8. 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 or 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, financial resources, and competing priorities in the face of local tolerance, particularly among indigenous peoples.

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 and families 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 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. Although training and workplace enforcement of safety regulations and the use of safety equipment has been lax, Panama has recently inaugurated new programs in cooperation with the U.S. Department of Labor to raise public awareness of worker safety issues and improve local safety standards. Complaints of health and safety problems continue in the construction, banana, cement, and milling industries, among others.

f. Rights in Sectors with U.S. Investment: Worker rights in sectors with U.S. investment generally mirror those in other sectors. Banana workers continue to complain of health hazards largely due to alleged exposure to pesticides.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad on an Historical Cost Basis **--** 2000

(Millions of U.S. Dollars)

Category	Amount	
Petroleum		273
Total Manufacturing		152
Food & Kindred Products	40	
Chemicals & Allied Products	(D)	
Primary & Fabricated Metals	30	
Industrial Machinery and Equipment	0	
Electric & Electronic Equipment	0	
Transportation Equipment	0	
Other Manufacturing	(D)	
Wholesale Trade		446
Banking		16
Finance/Insurance/Real Estate		34,388
Services		182
Other Industries		-50

TOTAL ALL INDUSTRIES	35,407

(D) Suppressed to avoid disclosing data of individual companies.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.