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UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D. C. 20523

PANAMA

PROJECT PAPER

FINANCIAL STABILIZATION & ECONOMIC RECOVERY II

PAAD

AID/LAC/P-243

Loan Number:525-K-602
Project Number:525-0282

UNCLASSIFIED

CLASSIFICATION:

AID 1120-1

PAAD

AGENCY FOR INTERNATIONAL DEVELOPMENT

PROGRAM ASSISTANCE APPROVAL DOCUMENT

1. PAAD NO. 525-0282 525-K-602

2. COUNTRY: Panama

3. CATEGORY: Cash Transfer

4. DATE: ~~August 1985~~

5. OYB CHANGE NO.

5. TO: AA/LAC, Malcolm Butler

6. OYB INCREASE

7. FROM: LAC/DR, Dwight Johnson

TO BE TAKEN FROM: Economic Support Funds

8. APPROVAL REQUESTED FOR COMMITMENT OF: $ 20,000,000

10. APPROPRIATION - 72-1151037 LESA85-35525-KG31 (537-65-525-00-50-51)

11. TYPE FUNDING: ☐ LOAN ☒ GRANT

12. LOCAL CURRENCY ARRANGEMENT: ☐ INFORMAL ☐ FORMAL ☒ NONE

13. ESTIMATED DELIVERY PERIOD: August 1985

14. TRANSACTION ELIGIBILITY DATE

15. COMMODITIES FINANCED

16. PERMITTED SOURCE

U.S. only:

Limited F.W.:

Free World:

Cash: 20,000,000

17. ESTIMATED SOURCE

U.S.:

Industrialized Countries:

Local:

Other:

18. SUMMARY DESCRIPTION

The purpose of the assistance is to provide urgently needed budgetary support to the Government of Panama to enable (1) compliance with the 1985 IMF standby arrangement, (2) facilitate GOP access to the recently(June 1985) negotiated syndicated commercial bank loan (180 banks holding GOP debt) to cover amortization requirement for 1985 and 1986, (3) maintain financial stability at a critical political juncture and (4) assist the GOP in instituting policy reforms needed to resume economic growth through the private sector.

19. CLEARANCES

		DATE
LAC/CEN: GAdams	CA	8/28/85
LAC/DP: WWheeler		8/28/85
LAC/DR: CPeasley		8/27/85
GC/LAC: PJohnson	KM	
~~M/FM~~ PAFAD: ~~Christensen~~		8/28/85

20. ACTION

☒ APPROVED ☐ DISAPPROVED

Aug 28

AUTHORIZED SIGNATURE DATE

Assistant Administrator

Agency for International Developme

TITLE

CLASSIFICATION:

PROGRAM ASSISTANCE APPROVAL DOCUMENT

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ACRONYMS

AID	Agency for International Development
BHN	National Mortgage Bank
BNP	National Bank of Panama
ESF	Economic Support Fund
GDP	Gross Domestic Product
GOP	Government of Panama
IMF	International Monetary Fund
IBRD	International Bank for Reconstruction an Development
IRHE	Institute of Hydraulic and Electrical Resources
MIPPE	Ministry of Planning and Economic Policy
PAAD	Program Assistance Approval Document
PRD	Democratic Revolutionary Party
SAL	Structural Adjustment Loan
USAID/P	United States AID Mission to Panama
UNADE	National Democratic Union

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I. Summary and Recommendation

A. Economic Background and Outlook

During the decade of the 1960's, Panama's real GDP grew at the annual average rate of 8%, one of the highest rates of sustained economic growth in the world. Nevertheless, it was widely held that the fruits of this extraordinary performance were inequitably distributed. The government, which took power with the military coup late in 1968, sought to introduce major social reforms and improve the economic and social infrastructure. The strategy followed was one of massive and growing state activism, characterized particularly by chronic deficit spending, direct and continually growing participation in the economy via state enterprises and public employment, and detailed, discretionary and extensive market interventions in many areas and regulations designed to control economic interrelationships and to redistribute income and wealth.

During the decade of the 70's the government "controlled" the unemployment rate through a number of artifices (e.g. reduction in minimum age for retirement from 65 to 55, direct public sector employment which accounted for 80% of the increase in total employment) which have run their course. Panama's demographics now indicate that the labor force will increase by 25 to 30 thousand each year in the immediate and medium term. Unemployment is an immediate and growing problem for the Panamanian economy.

By the end of the first five years (1973) of the military government (well before there was worldwide concern about debt crises) Panama was the world's fourteenth leading debtor nation (measured as the ratio of foreign debt to GDP). The first year after signing the Panama Canal Treaty, the Government of Panama (GOP) increased its foreign debt by over $550 million (a net increase in public sector foreign debt of 44%) finishing 1978 as the world's fourth leading debtor and essentially guaranteeing the current debt crisis.

Over the last six years, Panama's GDP per capita has grown at an annual average rate of 2.1%. However, <u>all</u> of that growth came from the "autonomous"sector (new value added due to the Panama Canal Treaty and the transisthmian oil pipeline). Real per capita growth in the rest of the economy was zero, with growth in the public sector (still fueled by deficit spending) offsetting the decline in the private sector. Total public sector debt increased from 30% of GDP in 1970 to 106% in 1983. During at least the next five years, Panama will experience net capital outflows estimated at $230 million per year. Panama faces a difficult fiscal situation in the short and medium term.

The GOP met the terms of the mid-1983, 18 month Stand-by Arrangement thanks to the FY 1984 ESF grant. Having met the IMF's cumulative targets through the end of 1984, allowed the GOP to begin negotiating a $700 million 1985-86 refinancing package with commercial creditors. On July 15, 1985 the GOP received formal IMF approval for a new Stand-by Arrangement. The most crucial and immediate fiscal problem is the GOP's ability to comply with the budgetary conditions set in the new IMF Stand-by arrangement. Failure to meet quarterly targets sufficient for the IMF to halt disbursements will also immediately unravel access to the commercial creditor (180 banks holding GOP debt) refinancing package. Finally, the GOP is seeking a SAL II from the World Bank. This complicates the intricately interwoven set of conditions in the IMF and the commercial credit refinacing agreements, as it is an additional precondition to GOP access to the commercial refinancing facility.

Even if Panama were to weather its short-term financial crisis, it faces a difficult medium-term outlook. In a situation characterized by economic stagnation and mounting unemployment, Panama will confront a serious problem of international adjustment. In a country where absolute parity is maintained with the U.S. dollar, this latter adjustment will have to come fully from a readjustment in the real exchange rate, i.e., a lowering of the price of non-tradeables in relation to tradeables. Unless Panama were to adjust real wages downward and/or receive increased levels of concessionary resources, it is highly probable that there will be a reduction in GDP and a sharp increase in unemployment.

B. Program Summary

The proposed program provides for a cash transfer in August of 1985 of a $27,000,000 ESF grant to the Government of Panama. The program will assist the GOP maintain financial stability by providing budgetary support at a critical political juncture. Without the $27 million grant assistance requested under this PAAD, combined with additional painful budget cuts, the GOP will be hard pressed to meet the IMF performance standards, thus jeopardizing at an early stage, not only the new Stand-by Arrangement but also access to the syndicated loan with commercial banks. As the U.S. is currently the only additional source of financing available, it is imperative that the U.S. Government provide the resources requested thereby enabling Panama to weather the impending economic crisis with a minimum of social and political unrest, maintaining essential public services and programs vital for develpment and for the thrust of our country development strategy. No more effective contribution to Panama's continuing economic and political stability can be made than the timely provision of the requested grant assistance.

In consideration for providing the proposed grant assistance, the GOP will finance with their own funds priority construction activities selected from the 1985 investment budget, largely basic infrastructure projects in transport, health and education sectors (i.e. essential public services and programs vital for development). While the projects will be executed by the GOP, construction activities will actually be carried out by private sector construction firms thereby creating private sector employment and providing stimulus to a labor intensive sector in the economy. Finally, we have conditioned our assistance on actions which will reduce the role of government in the economy. Our assistance will contribute to the government's success in carrying out its programs of financial stability, economic reform spreading the benefits of growth and strengthening democratic institutions. The number and complexity of financial and political challenges facing the new government are enormous, and the implications involved in the success or failure of this government are wide-ranging and of immediate consequence for U.S. interests in Panama and Central America.

C. Grantee

The grantee will be the Government of Panama, represented by the Ministry of Finance (Ministerio de Hacienda y Tesoro). The ESF grant funds will be deposited in the Banco Nacional de Panama and will be utilized by the GOP for budget support requirements.

D. Conditions and Covenants

Conditions and Covenants are discussed in detail in Section VI and VIII of the PAAD.

E. Recommendation

The U.S. Mission recommends authorization of an Economic Support Fund grant to the Government of Panama in the amount of $27,000,000. The grant is to be obligated and disbursed in the form of a cash transfer for urgent budget support requirements. Obligation and disbursement will occur in August 1985 ($20 million) and September 1985 ($7 million).

II. Background

A. General Background

1. U.S. Interests and Policy Objectives

As the site of a key interoceanic canal and of associated U.S. military bases, Panama is of great strategic importance to the United States. The U.S./Panamanian partnership in operating the canal as established in the 1977 Panama Canal Treaties has worked well. This positive relationship will continue to be important as we turn complete control of the canal over to Panama, a process which by virtue of the Treaties is to be completed on December 31, 1999. U.S. economic interests in Panama apart from the canal are also strong: U.S. private investment in the country is the third largest in all Latin America (greater than in all the neighboring Central American countries combined). Further, a pipeline across Panama now transports Alaskan oil destined for the United States East Coast. Politically, the U.S. has a strong interest in the development of Panama's nascent democratic institutions.

Geographic proximity to the Central American crisis area, Panama's stagnant economy, and the fragility of Panama's new democratic political institutions raise concerns with respect to Panama's continued institutions raise concerns with respect to Panama's continued political stability and economic well-being. Over time these factors could damage Panama's relative tranquility and threaten U.S. interests.

Our primary policy objectives in Panama, therefore, include assisting the government in (1) fostering a democratic political system; (2) attaining economic stabilization; and (3) implementing a series of policy reforms to achieve the structural adjustment needed for a resumption of sustained economic growth.

2. Political Update

In 1984, after 16 years of military rule, Panama held its first direct Presidential elections. The new President, Dr. Nicolas Ardito Barletta, took office on October 11, 1984, for a five-year term. Representing the governing Democratic Revolutinary Party (PRD), supported also by a group of smaller parties, and backed by the military, Dr. Barletta was declared the winner by a tiny plurality over his octogenarian, charismatic opponent, Dr. Arnulfo Arias. The opposition -- which had waged a bitter struggle against the PRD, its military backers, and what the opposition characterized as official corruption -- charged that Barletta had been fraudulently elected.

Resultant problems of political legitimacy, Panama's difficult economic situation, and the inherent problems of political transition after sixteen years of military rule have combined to make President Barletta's initial months in office difficult ones. A University of Chicago-trained economist with experience as Panama's Minister of Planning and a vice President of the World Bank, Barletta has focused his energies on Panama's economy. President Barletta is fully aware of the need for major economic policy reforms if the Panamanian economy is to grow over the long term.

President Barletta's reform efforts, however, have generated serious political problems for the government. The Barletta Administration confronted a particularly strong surge of popular protest in November and December of 1984, after the President proposed a series of fiscal austerity measures. Since then discontent has been more diffuse but still has inhibited the President's economic program.

At mid-year the government was endeavoring, through a formalized "national dialogue", to build support for economic reform. Whatever the outcome of this process, it appears clear that the Barletta Administration will continue to face serious political obstacles as it shapes its governmental program.

3. Social Update

Panama achieved impressive improvements during the 1970's in the provision of schools, health and family planning services, potable water, electricity and communications for its low income population. This achievement required heavy public investment and is reflected in a comparison of social progress indicators for the years 1970 and 1980 (See Annex II, Table 1). Other investments (e.g., construction of a convention center, airport, sugar mills, Cerro Colorado, etc.) through massive foreign borrowing, were not well chosen. The GOP is now obliged to shift its attention away from debt financed economic development and severely limit public expenditures in order to remain solvent. Without economic growth, the social development which has been achieved cannot be preserved, sustained or expanded.

Notwithstanding the change of emphasis from social to economic problems, the Government cannot ignore Panamanians' expectations. At a minimum, the existing level of services must be sustained, consolidated and expanded to the extent necessary to keep pace with population growth, or the risks of social unrest will increase. As there are significant inefficiencies in the operations of many government agencies, it should be possible to introduce cost-saving measures. The main purpose of several of USAID's Development Assistance projects is to improve the efficiency of public sector institutions.

There still remain some areas of severe poverty and malnutrition in the countryside as well as in the urban areas. A major problem in rural areas, especially in the central provinces, is the presence of isolated communities which offer little opportunity for off-farm employment. Urban areas suffer from growing unemployment and continued migration from the countryside. The plight of the urban poor is most evident in the congested, decaying tenements of the inner city and sprawling squatter settlements on the fringes of the metropolitan area. The situation is particularly acute in Colon where the unemployment and crime rates have reached crisis proportions.

B. Economic Background

1. Macroeconomic Trends and Current Fiscal/Debt Crisis

During the decade of the 1960's, Panama's real GDP grew at the annual average rate of 8%, one of the highest rates of sustained economic growth in the world. Nevertheless, it was widely held that the fruits of this extraordinary performance were inequitably distributed and that the social and economic infrastructure outside the metropolitan corridor had remained at a low level of development. The government which took power with the military coup late in 1968 sought to introduce major social reforms and improve the economic and social infrastructure, while attempting simultaneously to sustain the rapid GDP growth experienced during the 1960's. To this end, from its very inception the government has followed a strategy of massive and growing state activism, characterized particularly by chronic deficit spending, direct and continually growing participation in the economy via state enterprises and public employment, and detailed, discretionary and extensive market interventions and regulations designed to control economic interrelationships and to redistribute income and wealth.

A second, dominant feature of the evolution of Panama and its economy from 1970 to date centers, as it always has, on the Panama Canal. The one overriding political issue during the seventies was the process of negotiating the Panama Canal Treaties, finally signed in 1977. It is frequently asserted that many of the now questionable economic policies implemented prior to signing the Treaty constituted governmental concessions thought necessary to achieve and maintain broad political support for the government's negotiating strategy. It is further asserted that the act of signing the Treaty ended a period of uncertainty related to the negotiations, thus helping to restore confidence and increase private investment. Finally, and concretely, starting in 1980 and due to the combination of Treaty provisions and national accounting conventions, the contribution of the Canal to Panama's GDP increased by over $100 million (in 1970 prices) per year, an annual increase of over 6.5% of real 1979 GDP.

A third outstanding and recent feature of the Panamanian economy was the construction of the transisthmian oil pipeline designed to reduce the costs of transporting Alaskan oil to the east coast of the U.S. This was one of two major investment projects which propelled Panama's construction sector between 1980 and 1982. Perhaps more strikingly, when the pipeline entered into full operation in 1983, its <u>increased</u> contribution to aggregate value added meant the difference between real GDP growth of 0.4% (the official, published figure) and a true recession of approximately 5%, (the amount by which the rest of the economy fell in 1983). While the rest of the economy grew by 0.3% in 1984, value added from the pipeline fell and thus total GDP fell by 0.4% in 1984.[1/]

1/ In this context, it is important to note a serious statistical discrepancy. In the GOP's national accounting procedures, pipeline value added is deflated by a composite index of oil shipping rates, an index whose value is well below that of the GDP deflator and whose validity for calculating the pipeline's real value added is widely questioned. Further, data provided to (or anyway used by) the IMF and the international financial community includes pipeline value added deflated by the GDP deflator; the result is that real value added from this source is more than third lower than in official Panamanian publications, and, with this modification, GDP in 1983 <u>fell</u> by 1.5% and by another 0.4% in 1984.

This basic statistical discrepancy is of course disconcerting, and such discrepancies are by no means limited to just the national accounts. It is therefore remarkable that the IMF, in its Panama Staff Report of June 17, 1985, states: "Panama's economic statistics are generally adequate and timely. Statistical information is adequate and up-to-date for national accounts, prices, wages, monetary accounts, public sector finances and the balance of payments". One of the most important goals of USAID/Panama's Development Policy Studies program is to develop the basis for consistent, coherent and credible statistics, especially those referring to public-sector finances.

The results of the GOP, activist strategy, complete with the benefits of the new Panama Canal Treaty and the pipeline, have been mixed. On the clearly positive side are the social progress indicators referred to above (See Annex II, Table 1). Likewise, measured, open unemployment has been held in check; in 1970 the unemployment rate was 10%, in 1980 it had fallen to 8.4% and preliminary estimates for 1984 put it at only 9.4%, in spite of the current recession. Aggregate economic growth, although notably lower than in the sixties, has averaged 4.9% per year from the end of 1968 through the end of 1984. Finally, a U.N. financed project on critical poverty, nearing completion, indicates that the distribution of income may have improved slightly since 1970.

However, these latter economic indicators, on an average and aggregated basis, are misleadingly optimistic. For example, although the officially reported unemployment rate has not increased, these figures are widely questioned, and private-sector spokesmen (not exclusively from the political opposition) insist that the true unemployment rate is between 15 and 20%. On the other hand, even the official figures hide the true magnitude of Panama's emerging and growing employment problem. In fact, the unemployment rate has been "controlled" by means of three explicit policy measures: (1) A massive program to increase school attendance and retention, especially at the secondary and university levels. As a result, the labor force participation rate for Panamanians between 10 and 24 years of age fell by 10 points from 1970 to 1980. (2) A reduction in the minimum age for retirement, from 65 to 55, with which the labor force participation rate of those 55 and older also dropped by 10 points in the decade. (3) During the decade of the 1970's, the increase in <u>direct</u>, public-sector employment (7.5% per year) accounted for approximately 80% of the increase in total employment in the economy. The rate of increase in public-sector employment has slowed somewhat in the first four years of the present decade (5.6% per year), but in a generally stagnant economy, the government still represents the most likely source of new jobs.[2/] All three of these artifices have contributed directly to Panama's current fiscal and foreign-debt problems, and all three have run their

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2/ Recent employment data present another important statistical discrepancy, or at least serious doubts. According to the census for 1980 and the Household Survey for 1984, total employment has increased by 124 thousand, 50% more in 4 years than the <u>total</u> increase during the previous 10 years. Of these 124,000 new jobs, 28,000 were in the public sector. Thus, private-sector employment would have increased by 96,000, 5.8% per year, in spite of the facts that: (a) an <u>over</u>estimate of the growth of private-sector GDP is -0.4% per year in this period; and (b) there were no policy measures taken in these four years to decrease the cost of labor relative to other inputs. Thus, employment data so far in the 1980's are highly suspect, the IMF notwithstanding.

course. It would be virtually impossible to increase schooling again or to lower further the retirement age. And the currently required fiscal restraint implies that public-sector employment can no longer continue growing. Meantime, Panama's demographics indicate that the labor force will increase by 25 to 30 thousand persons each year in the immediate and medium-term future. Thus, in spite of official unemployment figures, employment is an immediate and growing problem for the Panamanian economy.

Second, although the growth of GDP over the past 16 years would appear to be satisfactory, at least relative to other countries, the aggregated, annual average figures hide the composition of GDP growth and thus the sources of the current and pending crises. A logical, although inexact, disaggreagation would distinguish three broad components (see Table 3):

(i) The "autonomous" component, i.e. autonomous to the Panamanian economy itself, consisting of the Panama Canal and the transisthmian pipeline;

(ii) The "official" component, consisting of government services, the state's utility monopolies (electricity, water and telecommunications) and import duties;

(iii) The "private" component, GDP less components (i) and (ii). Since this residual component still includes a number of important state enterprises (sugar, cement, airline, and so forth) and other decentralized agencies, it represents a significant overestimate of true private-sector activity.

During the first five years of the military government, GDP continued to grow at the relatively rapid annual rate of 7.3%. As value added by the "autonomous" sector was virtually constant, growth originated (in approximately equal rates) in the "official" and "private" sectors. It is worthwhile noting, however, that the strategy of state activism and the consequent increase in deficit spending had already, by the end of 1973 and well before there was any worldwide concern as to debt crises, converted Panama into the world's fourteenth leading debtor.3/

In the following four years, to the end of 1977, GDP grew at only 1.7% per year; the "autonomous" sector declined at the average rate of 1.2% in these years while "private" sector value added grew at 1.4% per year. The "official" component continued to grow at the annual rate of 4.2%, and at the end of 1977, Panama had become one of the world's five leading debtors. 1978, the first year after signing the Panama Canal Treaty, was a very good year, as real GDP increased by 9.8% and all three components participated in that growth, the autonomous component in 4.1%, the private component in 11.2% and the official component in 6.0%. However, 1978 was also a watershed year for

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3/ Measured as the ratio of foreign debt to GNP. World Bank Debt Tables, 1983-84.

the public finances. In spite of the fact that during 1978 the GOP found it necessary to refinance almost a quarter of its foreign debt outstanding, the GOP increased its foreign debt during that same year by over $550 million, a net increase in public-sector foreign debt of 44%, the GOP's largest one-year debt increase in its history. Thus, having finished 1978 as the world's fourth leading debtor, Panama's current debt crisis was essentially guaranteed.

Over the last six years, Panama's GDP per capita has grown at the annual average rate of 2.1%. However, all of that growth has come from the autonomous component, the new value added due to the Panama Canal Treaty and the pipeline. (Both account for less than 3% of total employment.) Real per capita growth in the rest of the economy was zero, with growth in the official sector--still fed by deficit spending--offsetting the decline in per capita output of the "private" component of the economy. Apparently, the confidence allegedly re-acquired after signing the new Treaty was very short lived.

Therefore, once it is recognized that, on the one hand, unemployment has been controlled through fiscal spending and policy artifices that cannot be repeated and that, on the other hand, GDP growth has been fueled by autonomous injections, which probably will not repeat themselves in medium term, and by the government's deficit spending and foreign indebtedness, which must now be halted, it becomes clear that Panama now finds itself facing a serious and immediate economic crisis. Moreover, given the public sector's now limited capacity for further net borrowing and its projected interest-payment obligations, during at least the next five years Panama will experience net capital outflows estimated at $230 million per year. Part of the economy's corresponding adjustment mechanism will inevitably include a reduction in real wages, an increase in unemployment, or both. One result might well be a worsening of the country's distribution of income. Finally, unless something is done to reactivate the private sector-(the growth of the "private" component of GDP from 1973 to 1984 has not kept pace with the increase in population)-Panama may soon face the danger of losing some of the progress made in basic, social indicators. Maintaining these indicators will require a permanent flow of internally generated resources as it will no longer be possible to rely exclusively on foreign indebtedness for this purpose.

It is often asserted that Panama's current economic difficulties reflect the worldwide recession that emerged late in 1981. However, although it is obvious that the world's economic plight has had detrimental effects on Panama, it simply is not true that the current crisis has had an external origin. From 1978 through 1984, Panama's external terms of trade deteriorated by almost 17% which, in 1970 prices, cost the economy a total of $470 million over these six years. Likewise, the increase in international interest rates, relative to the average rate paid in the years 1975-1977, meant that in these six years "excess" interest payments amounted to $178 million. However, over just the four-year period 1980-1984, the external sector has transferred to Panama, via the pipeline and the provisions of the new Canal Treaty, increased value added which, in 1970 prices, sums to $731 million. Hence, these four external factors together have given Panama a boost totalling $83 million, $13.8 million, approximately 1% of real GDP, per year. Thus, although the world recession has not helped Panama, there is no sense in which the country's internal recession can be attributed to external factors. Rather, the root causes are home-grown and their solution will require internal measures to bring about fundamental structural changes in the economy.

The necessity to change strategies became apparent in 1982 when, in the midst of the emerging regional debt crises and the world recession, attention was called to the government's own precarious debt situation. Although the GOP had incurred in deficits for 27 consecutive years, in 1982, due to a variety of reasons (particularly cost overruns in La Fortuna hydroelectric project and an ambitious (and later scandalous) program of housing construction financed by the social security system), the deficit jumped to the unprecedented level of 11% of GDP, almost twice the amount stipulated under the GOP's stand-by arrangement with the IMF.[4] Efforts were undertaken to re-gain control of fiscal spending, efforts which included, in mid 1983, a new 18-month stand-by agreement with the IMF, a SAL (structural adjustment loan) with the World Bank, and a two year refinancing arrangement with Panama's commercial creditors. The IMF stand-by arrangement, in the amount of SDR 150 million, covered the period ending December 31, 1984 and stipulated, in essence, that Panama would not borrow on a net basis from

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4/ The definition, measurement and reporting of the public sector deficit represents perhaps the single most important area of statistical discrepancies, and the availability of reliable timely data on government [illegible]es is widely recognized (at least in Panama) as a serious obstacle to be overcome. The IMF defines the public-sector deficit as the sum of net foreign borrowing by the consolidated public sector and its net borrowings from the Banco Nacional de Panamá (BNP), which in a strict, accounting sense must be correct. However, the equivalent and more direct, intuitive definition, central government spending less total tax and non-tax revenues--which should automatically include net transfers to/from decentralized agencies and state enterprises--was, in 1982, 15.6% of GDP, as compared to the IMF's definition of 11%. Two other indicators of the deficit in 1982 are the change in public-sector external debt (12% of GDP) and the change in total--internal <u>and</u> external--public-sector debt (14% of GDP). All of these measures do in fact emphasize the same phenomenon--in 1982 the fiscal deficit jumped to a dangerously unsustainable level. But the precise amount of the deficit, i.e. the amount that should be confirmable through cross-checks, is currently an unknown. In terms of this statistical discrepancy, 1982 was not a unique year; differences of the kind mentioned here exist on a year by-year basis. Since for Panama's international financial negotiations the parameter that matters is that accepted and used by the IMF, this document will refer to the IMF figures. As mentioned earlier, improving the public-sector accounts is a high priority goal in USAID/Panama's Development Policy Studies project.

commercial sources, that it would not borrow on a net basis from the Banco Nacional de Panamá (BNP) over the levels of December 31, 1982, and that it would not increase its short term commercial debt. The overall deficit of the consolidated public sector was to be limited to $270 million in 1983 and to $250 million in 1984, and these deficits were to be financed fully from non-commercial sources. Maximum net borrowing for the 18-month period was thus limited to US$520 million.

During 1983, the strict control on government expenditures was truly remarkable. Non-interest expenditures fell by $257 million, and interest payments fell by $45 million. The total reduction in central government spending was in an amount equivalent to just over 7% of GDP, and for the year the public sector deficit was $23 million less than the amount allowed under the IMF stand-by arrangement.

Although the GOP financial parameters were held within the quarterly targets set by the IMF throughout the first half of 1984, the combination of increased world interest rates, additional expenditures inherent in the electoral process in the first semester, and lower-than projected tax revenues due to the deepening internal recession, put into doubt the GOP's ability to comply with the cumulative targets by the end of the year. In fact, the deficit target was reached thanks to the 1984 ESF grant of $30 million.

The first priority of President Ardito Barletta's new government (inaugurated in October 1984) continued to be the financial-budgetary crisis facing his government. By November, a package of new revenue measures had been proposed and approved by the legislature. However, as the package included relatively important and extremely unpopular tax measures, the general public rejected it and, in mid-December, the package was repealed. This of course was a setback not only for final approval of the 1985 fiscal budget--finally enacted in March--but also for negotiations with the IMF of a new financial arrangement for 1985 and beyond. In fact, upon repealing the first revenue package, it was necessary to convince foreign commercial banks not to reduce their lines of credit to the BNP below levels outstanding on December 14, 1984.

In mid-June, the GOP published its letter of intent with the IMF for a new stand-by arrangement supported by a total of SDR 90 million for the period from the second quarter of 1985 through the first quarter of 1986. The central features of this program are again fiscal austerity and maintenance of the liquidity position of the BNP. The fiscal deficit is to be further limited, from 6% of GDP achieved in 1984 to 3.5% in 1985 and 2.6% in 1986 (all deficit figures corresponding to the IMF definition). The program received formal IMF approval on July 15, 1985. In addition, agreement for 1985 and 1986 was reached with Panama's commercial creditors for $60 million in new loans, refinancing of amortizations due in 1985 and 1986 ($603 million), working capital for several decentralized agencies ($56.4 million), basically an extension of the "freeze" on lines of credit ($133 million) to the BNP through March 31, 1987, and a petroleum import facility, also for the BNP, in the amount of $28 million.

2. Production by Sector

<u>Services</u> account for three fourths of GDP and provide employment to one half of the labor force. A significant proportion of services are related to international transactions and are based on the exploitation of the geographic position as well as of Panama's liberal banking legislation. The most important items are the tolls collected for passage through the canal, fees for the use of the transisthmian oil pipeline, services offered by the Colón Free Zone, and international banking. <u>Agriculture</u> accounts for about 10% of GDP and employs more than one fourth of the labor force. The main products are livestock, bananas, rice, sugarcane, and coffee. <u>Manufacturing</u> accounts for about 10% of GDP and employs about the same percentage of labor force. Production for the domestic market is highly protected and based on food processing, light industry and construction materials. Exports consist of petroleum derivatives and some light consumer goods such as garments. <u>Construction</u> accounts for about 7% of GDP and employs 6% of the labor force. Especially in the early 1970's, value added in the sector was based on high income housing and buildings for office space for the international banking center. Recent civil works projects, such as the transisthmian pipeline and the La Fortuna hydroelectric dam, have contributed to a marked increase in value added by the construction sector. Now that those large projects have been completed, the sector is depressed.

3. Prices

Panama is a small, open economy and does not attempt to affect monetary aggregates. As a consequence, domestic price trends follow closely international prices. In 1984, the consumer price index increased at an average rate of 1.6%, compared with 2.1% in 1983, 4.2% in 1982 and 7.3% in 1981. Panama has had a system of price controls designed to maintain the purchasing power of low-income consumers, but as part of the strategy to deregulate the economy, price controls on most goods are being eliminated.

4. Public Sector Finances

Aside from the global trends and problems detailed in subsection 1. above, certain characteristics of central government finances are worth emphasizing. First, in terms of total spending, the past three decades can be divided into three distinct periods. From 1956 through 1968, central government, non-interest expenditures averaged 16.3% of GDP; in the following decade, 1969 through 1978, spending jumped to 21.6% of GDP, clearly reflecting the development strategy based on state activism; and from 1979 through 1982, i.e. before fiscal austerity had to be imposed, non-interest spending jumped again to 25.6% of GDP, portending the debt crisis that emerged to public view at the end of 1982.

Central government revenues, obviously, did not keep pace. In the same three periods, respectively, total revenues averaged 13.5%, 15.2% and 19.8% of GDP. Given especially the central role of the Panama Canal, as well as the provision of other services, it is important to note that non-tax revenues have traditionally been a significant and stable source of government finance. Over the entire period from 1956 through 1979, non-tax revenues averaged 27.7% of tax revenues. With the new Canal Treaty and the operation of the transisthmian pipeline, non-tax revenues have averaged more than 36% of tax revenues from 1980 through 1984. Unfortunately, this major increase in non-tax revenue has not been sufficient to permit the GOP to pay even the interest on its foreign debt without recurring to tax and austerity measures.

5. The Financial Sector

The Panamanian financial system is highly integrated with international financial markets. The U.S. dollar is the medium of exchange and as there are no capital controls there is almost perfect capital mobility. Up to now, domestic credit activities have not been constrained by the availability of domestic resources but have been demand-determined as the banking system has been able to tap the international market virtually at will to supplement domestic resources. This situation may change if the fiscal position of the GOP were to deteriorate further, and international banks decide to reduce their exposure to the private as well as to the public sector.

Panama does not have a central bank. The Banco Nacional de Panamá (BNP) has a number of the attributes of a central bank including: a) it is the fiscal agent for the public sector; b) it holds the required minimum reserve of the commercial banks; c) it handles paper currency via transfers to and from the U.S. and d) it runs the clearinghouse. The National Banking Commission, an autonomous agency with a board of directors headed by the Minister of Planning, carries out a supervisory role and is responsible for licensing and inspecting banks.

Given the almost perfect capital mobility and the openness of the economy, there is little scope for an active monetary policy. Although the banking legislation provides for several policy instruments that might be applied in the attempt to manipulate monetary aggregates in the short run, these have wisely not been used. There are interest-rate ceilings on time deposits of less than $14,000, and some other, minor regulations, but domestic interest rates are otherwise determined by international interest rates.

6. The Balance of Payments[5/]

Given Panama's monetary system, the size of the current account deficit of the balance of payments is fully determined by the availability of foreign financing. In Panama, the trade balance is highly negative but is partly compensated by the balance of non-factor services.

From 1980 through 1982, the current account deficit of the balance of payments averaged 9.1% of GDP. A deterioration in the merchandise trade account was compounded by a sharp increase in interest payments abroad, resulting from both the increase in international interest rates and the growth of public sector external debt. Net non-factor service receipts grew

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5/ Data on the balance of payments of Panama are inherently inaccurate because of the inability to identify transactions between residents and non-residents, particularly in the case of capital transactions.

throughout the period, largely as a result of the transshipment of Alaskan oil through the Canal. In 1983, the current account deficit fell sharply to 3.7% of GDP. Both the slowdown in domestic growth and, particularly, the sharp reduction in the fiscal deficit produced a sharp fall in import levels which more than offset a drop in Panama's exports. The improvement in the trade deficit coincided with a decline in world interest rates, an increase in tolls charged for canal traffic, and the opening of the petroleum pipeline. In 1984, the current account deficit rose again to 6.4% of GDP, reflecting the increase in world interest rates and the economic recession in Panama.

The composition of net identifiable capital inflows has varied in recent years, and has depended to a large extent on fiscal policy. Net official capital inflows fell from nearly 9% of GDP in 1979 to 4% in 1981, while private-sector borrowing abroad rose from 6% of GDP in 1979 to 8% in 1981, reflecting the construction of the oil pipeline in 1981. The completion of the oil pipeline in 1982 led to a sharp reduction in private capital inflows although that reduction was more than compensated by the increase in foreign borrowing by the public sector. Total capital inflows fell from over 13% of GDP in 1982 to 5.5% in 1983 and to 3.1% in 1984.

III. MAJOR DEVELOPMENT PROBLEMS

A. Economic Policy

Panama's economic policies differ markedly between sectors. While the [illegible] sector (especially banking and the Colón Free Zone) developed with a minimum of government regulation and control, there has been significant intervention in other sectors. Agricultural policy in the past decade emphasized self-sufficiency in basic food commodities through price support policies and quantitative import controls which increased the cost of living, added to the public-sector deficit, misallocated resources, and helped to stymie growth in the sector. Although price policy was intended to be used to some extent as a mechanism to transfer income from urban to rural areas, the major redistribution achieved went in favor of large and efficient producers, especially rice farmers. Additionally, there was increased government intervention manifested through the establishment of government owned enterprises, such as sugar mills, large-scale marketing activities, and the creation and support of agrarian reform communal farms (asentamientos). Employment in the public agriculture sector and in the government as a whole mushroomed. The Ministry of Agricultural Development (MIDA) emphasized the provision of social services and gave relatively less emphasis to promoting agricultural production, particularly by private farmers. Furthermore, policies in the sector have been inconsistent and often unpredictable due to frequent changes at senior levels in the numerous sector agencies which often seem to operate as autonomous fiefdoms. The net result is that in 1984 value added per capita in Panama's agricultural sector is more than 10% lower than it was in 1970.

In the industrial sector, the policy of import substitution which began in the early 1960's was continued. Protection of domestic industries was accomplished basically through a system of import quotas, and the domestic prices of items subject to quotas were regulated through price controls administered by the Office of Price Regulation. Studies indicate that, although the average rate of effective protection has changed very little from 1969 to 1983, the dispersion of protection has increased by a factor of 10, as the authorities have chosen to apply the discretion allowed them by law in order to discriminate heavily among firms seeking protection. As a result, the industrial sector is more inefficient, from the viewpoint of the economy, but those sectors that have achieved high protective barriers have even greater vested interests in maintaining the system, as the transfers that they thereby receive are significantly lucrative.

On the other hand, in 1972, the Torrijos Government enacted a labor code which significantly increased labor costs, contributed greatly to the inefficiency observed in the entire economy (perhaps particularly in the industrial sector) and restricted the flexibility of entrepreneurs in areas such as productivity payments and apprentice training. This is of course viewed by Panamanian and foreign investors as a major disincentive for investment and employment in Panama, and is one of the basic reasons for the employment problem documented above in Section II.B.1.

The Government attempted to reduce <u>housing</u> costs by establishing rent controls and by providing loans at subsidized interest rates. As a consequence, the supply of low cost rental housing and of private mortgage financing has been severely restricted. Additionally, protection of the construction materials industry and a very strict construction standards code have raised housing costs significantly.

The pursuit of the set of policies briefly outlined above resulted in a misallocation of resources and constrained growth in all sectors with the exception of the service and government sectors. In this regard, one of the first studies completed in our Development Policy Studies program calculates that if the general efficiency of the Panamanian economy had maintained its level of the 1960's, even with no technological progress in the decade of the 1970's, the amount of new investment and new employment <u>should</u> have given Panama a GDP between 20% and 29% larger than it was in 1980. The need to stimulate the economy to compensate for the (largely government induced) private sector slack, the expensive nature of many Government programs, and the losses sustained by most government enterprises resulted in levels of government spending which greatly exceeded revenue and which required the excessive levels of foreign and internal indebtedness documented earlier. <u>Total</u> public-sector debt increased from 32% of GDP in 1970 to 106% in 1983. Since efforts to begin to control and correct this debt situation will now severely constrain foreign borrowing by the public sector, future economic growth in Panama will have to depend on the reactivation of the private sector, which can be achieved only through the implementation of a more appropriate and coherent set of policies. This redirection of economic policy will not be universally welcomed as there is significant opposition from interest groups, including leading members of the coalition which won in the national elections, which benefit from present policies. Tighter control of fiscal spending is the only fundamental change in economic policy introduced and implemented to date under the new government.

B. Rapid Urbanization

Panama faces the continuing problem of rural-to-urban migration and transformation. In 1970 the country was half urban, with 44% of the population living in the metropolitan area (Panama, Colón and suburbs). By 1980 the figures were 57% urban and 49% in the metropolitan area, and by the year 2000 the metropolitan area alone is projected to hold more than 60% of the population. This rapid transformation from a rural to an urban society has had a direct and visible impact on the Canal area, increasing the unemployment rate and straining urban infrastructure. Fully 73% of the country's unemployed are concentrated in the metropolitan region; in certain areas adjacent to Panama City, such as San Miguelito, unemployment is close to 20%, and it is estimated to exceeed 25% in the City of Colón. The concentration of unemployment in a few urban areas contributes significantly to the explosiveness of the unemployment issue, which is viewed by many as the most important problem facing Panama today. Moreover, although extensive public investment has maintained water, sewerage, education, health and other public services at adequate levels, urban development has not kept pace with demand. The problems associated with this rapid growth call for the provision of shelter, services and facilities for the burgeoning population. In normal circumstances, the task would be formidable; coupled with the GOP's fiscal/debt reality, the coming problems are easily seen to be monumental.

IV. ECONOMIC PROSPECTS

A. Short Run Economic Prospects

Economic prospects for 1985 are not bright and the immediate future (through 1986) is still very uncertain. The World Bank is dissatisfied with Panamanian policies, and is not prepared to undertake a SAL II without further GOP economic policy commitments. Even though the GOP has just concluded the successful negotiation of an acceptable, two-year financial package with the IMF and the international banking community, the most pressing and crucial, immediate problem is Panama's ability to comply with the budgetary conditions set in the IMF stand-by program. Quite simply, GOP budget projections, particularly revenues, were based on assumptions as to the growth of GDP, inflation and the yields of new taxes. Apparently the government has so far been able to hold the line on expenditures--in fact, it has reportedly been holding back from budgeted levels--but tax revenues are already lagging behind projections, as was publicly announced by the Minister of Finance. According to this speech, shortfalls are particularly acute in revenues from the income tax and from the value added tax. One response may be to reduce even further the government's investment budget.

The causes of reduced revenues are two: the economy's continued stagnation and (apparently) an increase in tax evasion. However, from the standpoint of the new financial package, the reason for failure to reach any of the deficit/debt targets is unimportant. Rather, given the intricate, tightly interwoven set of conditions in both agreements, any failure to meet quarterly targets sufficient for the IMF to halt disbursements will also immediately unravel the rest of the new, global financial package. In this connection it is crucial to understand that, as a part of these agreements, the GOP has explicitly included, as a projected source of funds, USAID (ESF) in the amount of $60 million in calendar year 1985.

The situation is summarized in the accompanying table, taken from the GOP document, Republic of Panama: External Financing Program, 1985-1986 (June 1985), which was distributed to Panama's commercial creditors. The target for the maximum public-sector deficit (derived from projections as to total revenues and total expenditures), plus principal payments due to creditors during each year, gives the GOP's gross financing needs, $559.7 million and $717.4 million for 1985 and 1986, respectively. For 1985 $143.7 million (26% of total financing needs) will be provided in the form of project assistance that has already been approved and programmed, mostly through multilateral and bilateral agencies. In addition, financing of $356 million from the IMF, commercial banks, suppliers and the Paris Club (the latter representing only $8 million for 1985, which should receive final approval in September) has been negotiated and secured, subject to compliance with the IMF quarterly targets. Thus, for 1985, the financing that has been secured comes to $499.7 million, $60 million short of total needs for this calendar year.

The size of the deficit, the net increase in foreign borrowing and net borrowing from the BNP agreed upon with the IMF, and the volume of financing sought from Panama's commercial-bank creditors, were determined on the basis of the assumption that US economic assistance funds would amount to these same $60 million. Thus, assuming that all of the projections as to revenues, expenditures and other sources of financing turn out to be correct, any shortfall below this figure in the ESF grant for the year will automatically push the GOP beyond the IMF targets, forcing a further cut in fiscal expenditures or an IMF decision as to Panama's non-compliance with the stand-by arrangement.

SOURCES AND USES OF FUNDS

(US$ Millions)

	1985	1986
Financial Requirements		
- Deficit of the non-financial sector[a]	160.0	109.1
- Total debt amortizations[b]	399.7	608.3
T O T A L	559.7	717.4
Sources of Financing[b]		
- Project assistance from multi-lateral and bilateral agencies	143.7	165.5
- Other sources of financing	141.0	139.7
U.S. AID (Economic Support Fund) ***	60.0***	*** 15.0***
IMF[c]	35.0	44.0
World Bank	-	60.0
Floating Rate Notes	20.0	-
Supplier Credits	26.0	12.0
Securities	-	8.7
- Refinancing of official credit (Paris Club)[d]	8.0	16.4
- Refinancing of commercial bank amortizations[e]	225.0	377.8
- New money from commercial banks[e]	42.0	18.0
T O T A L	559.7	717.4

a. Statistical Appendix, Table 12.
b. Statistical Appendix, Table 13.
c. July 15 stand-by arrangement.
d. To be finalized in September 1985.
e. June/July 1985 negotiations now approved.

Source: Republic of Panama: External Financing Program 1985 - 1986.

When this fact is coupled with the potential shortfall of tax revenues mentioned above, the precarious nature of the financial crisis already facing the Ardito Barletta administration for the rest of 1985 becomes dramatically clear.

The amount of ESF requested for FY 1985, $27 million, is 45% of the amount presumed by the GOP in its negotiations with the international financial community. Although the immediate gap of $33 million will in fact force some combination of increasingly painful spending cuts and IMF "flexibility" with respect to pre-set targets, the necessary adjustments will be much more feasible than would those required if the gap were $60 million. The $27 million ESF grant will undoubtedly alleviate the immediate budgetary difficulties facing the GOP.

The revenue measures taken so far include:

(1) Widening of the income-tax base by including firms operating in the former Canal Zone;
(2) A 10% surcharge on business income-tax liabilities for 1985/86;
(3) Elimination of import tax exemptions for the public sector, <u>without</u> compensating budget increases;
(4) Continuation of conversion of quotas to tariffs, and changing the value basis for tariff calculations from FOB to CIF effective August 1, 1985;
(5) Creation or increases of a series of fees and indirect taxes.

Taken together, these measures were projected to increase revenues by 7.5% over 1984 levels, but projections in general may have been optimistic.

Expenditure policy, on the other hand, has attempted to emphasize austerity and control. Besides curtailing overall spending on goods and services and sharply reducing (perhaps by $100 million or more) capital expenditures, the GOP enacted a one-year wage freeze on December 31, 1984. That freeze has already proven difficult to maintain, and pressures, up to and including work stoppages and strikes, for wage increases will undoubtedly mount through the rest of the year. Since public sector employees constituted one of the major sources of support for the new government, such pressures will be even more difficult to resist. Moreover, in the letter of intent to the IMF, it is stated that $7.5 million will be saved via measures affecting the wage bill (the accompanying IMF staff report specifically states that public-sector employment will be reduced by 5,000 during the second half of 1985). Achieving these intentions will prove to be a severe test for the current administration.

A potentially important measure for control of spending now requires that public enterprises and agencies report revenues and expenditures to the Comptroller within 15 days after the close of each quarter. In cases where revenues exceed budgeted projections, the excess must be deposited in the BNP and no expenditure increases can be made without prior amendments to the budget by the Legislature. In cases where revenues fall short of projections, expenditures must be accordingly adjusted. However, even with these new rules, and even with the completion of La Fortuna hydroelectric project, the state electricity company IRHE has reportedly (but not publicly) found itself in the embarassing predicament of having already spent its alloted annual budget for gasoline at mid-year.

The above examples illustrate the kinds of difficulties that the government has encountered within the public sector itself in implementing requisite fiscal measures. And of course tax-revenue measures affecting the private sector, aside from their inherent contradiction with the underlying strategy of promoting private-sector activity, have been even more difficult to introduce. The only measure that was instituted without problems was a new system for "preferential" interest rates for low-cost housing mortgages. Although the lower rates to be paid by house buyers are ostensibly designed to facilitate taking advantage of normal income-tax deductions for mortgage interest, the parameters built into the new law convert the measure into a housing subsidy, replacing (at least in some measure) the explicit subsidy that had been repealed earlier.

Other more fundamental and far-reaching measures simply have not yet been taken. A proposal for reforming the labor code has been prepared by the government, but just the knowledge of the existence of the proposal--it has not yet been formally submitted to the Legislature--led to demonstrations and a partially successful, 48-hour strike by organized labor. Moreover, proposed changes in the industrial-incentives law, changes which would eventually lower protection, have led industrial groups to ally themselves with organized labor against changes in either the labor code or the existing industrial-incentives law. As a result of all of these interactions, the GOP has, again with difficulty, organized a "national dialogue" in order to lay out a consensus plan for the country's economic development.

All of these examples of the problems so-far encountered on the road to establishing economic adjustment policies are symptoms of the more fundamental problem that continues to affect the current government and the entire economy. President Ardito Barletta entered office with a minimal margin of victory in the elections in May 1984, and hence a broad-based mandate for his program of government did not exist. Worse still, since important segments of his supporters would be adversely affected by some of the economic-policy changes necessary to re-order the economy, the government has in fact begun to lose political support. The result has been to generate a general atmosphere of uncertainty which has had a detrimental effect on potential private-sector initiatives. Until the government manages to forge a consensus sufficient to inaugurate a clear economic strategy, the uncertainty will continue and there will be little prospect for reactivating the Panamanian economy. In the meantime, the GOP's financial timetable keeps moving toward the inevitable IMF quarterly target dates.

B. The Prospects for 1986 and Beyond

Even if the problems of achieving a political consensus are quickly overcome, economic prospects for even the medium-term future are not overly optimistic, especially in view of the slow growth forecasted for Panama's main trading partners, the growing threat of protectionism in the developed countries, and the contractionary effects of the fiscal austerity dictated by

Panama's public-sector financial predicament. Thus, the private sector must re-emerge as the primary vehicle for future economic growth, and this will require a progressive and coherent set of economic policies. The process of economic reform began with the De la Espriella administration, especially with the sharp controls on fiscal spending in 1983 and some initiatives undertaken with the first World Bank SAL.

However, due to the political dynamics among the groups that fix policy and those affected by them, most of the measures have turned out to be less than what initial appearances would indicate. For example, the central feature of the first SAL was the substitution of quotas by tariffs, ostensibly to increase fiscal revenue, increase economic efficiency and, eventually, to increase trade. Although the majority of the quotas have in fact been eliminated, in many cases--perhaps the majority, studies are in progress--the tariffs that replaced them appear to have increased nominal protection, perhaps by as much as 70%, on average. Moreover, preliminary estimates indicate that total tariff revenues on these goods have actually fallen by 5%. One particularly telling case was that of potatoes, where quantitative import controls (via IMA) and price controls were eliminated, but the (specific) import tariff was increased tenfold, and in 1983 imports fell to zero while the price to consumers increased by 60%. In 1984, imports reappeared but no tariff revenue was generated due to the exemptions enjoyed by the importer. (Studies are in progress to ascertain results in markets for other vegetables where government intervention was also eliminated).

The official support price for rice was lowered from 14 to 13 cents per pound for the 1984-85 harvest, but acreage limitations were established to minimize surpluses and a nominal agreement was reached whereby millers would continue to pay 14 cents, although in fact producers are reported on average to have received less. Meanwhile, prices to consumers have not been changed. The support price for 1985-86 harvest has already been announced at the same 13 cents per pound.

As mentioned earlier, the GOP has prepared a preliminary proposal for modifying the labor code. Among other measures, the proposal would make productivity premiums feasible, permit apprenticeship contracts, piece work and work in the home, all of which would represent important improvements even if they turned out to be available only for new firms. However, the proposal also contains unfavorable aspects, the most important probably being the extention of job security provisions--widely considered to be one of the most negative aspects of the existing labor code--to several sectors which had previously been exempted. Even though the administration took pains not to alter so-called labor "conquests", organized labor has so far taken the extreme position of rejecting any change whatsoever in the labor code, and their recent strike was the key factor which precipitated the initiation of the "national dialogue" on economic policy.

As part of its longer-run strategy for reactivating the private sector, the GOP will be negotiating a second SAL with the World Bank. Central policy issues proposed will concentrate on modifications of the present structure of industrial and agricultural incentives. The most significant part of the program proposed to the World Bank is the modification of the structure of protection. Over a very gradual period of adjustment, 6 to 10 years, the economy would arrive at the following tariff structure:

(a) 10% (minimum) for imported inputs and machinery;
(b) 20% for goods not presently produced in Panama;
(c) 30% for goods currently enjoying nominal protection of 80% and less;
(d) 50% for goods currently enjoying nominal protection greater than 80%.

Although such a system could, if in fact implemented, represent a clear improvement over the existing structure of protection, the final result would be neither uniform nor low (at least not for final goods currently receiving protection). Nevertheless, in spite of the generous adjustment period, the industrial sector adamantly opposes any such modification, and discussions of the industrial law therefore carry crucially important political implications for the Ardito Barletta administration.

V. RATIONALE FOR U.S. ASSISTANCE

Panama is completely different from other countries because of its monetary system. It has no central bank and although the Balboa is the national unit of account, only a small volume of Balboa coins circulates and no Balboa bills are issued. The effective medium of exchange is the US dollar and, as a consequence, Panama does not present the same type of foreign exchange risk as other countries in the region. Macroeconomic equilibrium is a fiscal phenomenon and the direct indicator of macroeconomic stability is the public-sector deficit. Therefore, any contribution to financial stabilization must be targeted to the fiscal deficit.

The rationale for immediate U.S. assistance is to maintain financial stability by providing budgetary support to the GOP at a critical political juncture. Without the $27 million assistance requested under this PAAD, combined with additional painful budget cuts, the GOP will be hard-pressed to meet the IMF performance standards, thus jeopardizing at an early stage not only the new stand-by arrangement but also access to the new syndicated loan with commercial banks. One obvious result would be to force the GOP to restructure its debt in a less orderly manner. Given the openness of the Panamanian economy and almost perfect capital mobility, the orderly financing of the public sector deficit is necessary if capital flight and a liquidity crisis of the banking sector are to be avoided. Obviously, massive capital flight would result in a financial crash that would threaten the social and political stability of the country.

This latter point is central to U.S. interests. Panama has in the past been characterized by financial (if not fiscal) and political (if not democratic) stability. It is an ironic and unfortunate fact that the first elected government in 16 years has had to step into a situation in which the danger of losing the country's financial stability is very real and imminent and in which failure on this count could well halt the very recent progress toward the installation of fully democratic institutions. Avoiding financial collapse will continue to require severe fiscal restraint; reactivating the economy will require policies entailing major structural changes. And both sets of policies must be carried out by a government which has not yet been able to form a clear majority mandate.

Although measures leading toward increased liberalization of the economy, favored and encouraged by the World Bank, the IMF and USAID, will provide increased benefits in the future, the process of policy reform will result in short-run costs concentrated in certain segments of society (e.g., for entrepreneurs and workers in protected industries, and farmers who are presently receiving prices for their output above world market prices). Significant opposition to policy reform already has begun and is likely to intensify in the coming months. The U.S. government must show support and confidence in the budding democracy. The current government needs still more time to be able to forge the political support necessary to be able to carry out a consistent and coherent economic program.

Our ESF assistance would help to stimulate the economy and thus mitigate some of the short-run costs associated with the process of policy reform. The difficulties of the transition process are compounded by Panama's critical financial situation, which by itself effectively restricts the time available to the GOP for taking at least some of the requisite measures. Without a central bank or currency of its own, Panama cannot resort to a devaluation or to monetary expansion. Furthermore, commercial borrowing alternatives have already been defined and thus clearly restricted. As the US is at this juncture the only source of grant financing available, we believe that it is imperative for the US Government to provide the resources requested thereby helping Panama to weather the impending economic crisis with a minimum of social and political unrest, maintaining essential public services and programs vital for development and for the thrust of our country strategy.

VI. POLICY AGENDA

A. Current Strategy Policy Agenda

The development strategy initiated by the Torrijos Government in 1968 emphasized the provision of social services, while economic growth and employment creation were stimulated through a sharp expansion of government spending financed by external borrowing. With the advent of the De La Espriella government, the GOP began to shift the focus of its economic policy. The GOP is now emphasizing the necessity of employment creation through a reactivation of the private sector, particularly for the production of export commodities and to greater reliance on market mechanisms. However, achieving the political concensus to forge a clear and consistent economic strategy remains the main obstacle to continue the establishment of the fundamental policy reforms proposed in our FY 1984 ESF program.

Significant additional leverage towards meeting three 6/ essential policy changes included as covenants in our FY 84 ESF program has been added as they are now explicitly linked to the refinancing package and the proposed World Bank SAL II. This fragile refinancing structure could collapse if the Barletta administration does not move decisively to reform the labor code, the agricultural incentives law and the industrial incentive law well before the end of FY 85 since those policy changes are part of the SAL II and the SAL II is a precondition to access the $600 million refinancing facility.

The fourth convenant in the FY 84 ESF program, the establishment of a system to consolidate accounts of the public sector by the end of FY 85, is currently under preparation by our Development Policy Studies Project. The fifth covenant, to provide USAID/Panama with copies of all reports to the IMF as they are issued, regarding compliance with the stabilization program, has not been complied with. Finally, the sixth covenant, modification of cumbersome GOP contracting procedures, was satisfied on March 28, 1984, through Presidential Decree No. 18 authorizing Ministers to sign contracts which are fully or partially funded by international or bilateral development agencies.

We stated in the FY 84 PAAD that the FY 85 ESF program would include a) a covenant that would require introducing legislation eliminating rent control on newly constructed housing at all rental levels and b) a condition precedent eliminating Law 28 (Law 28 establishes a 0.5% tax on commercial and industrial loans and uses the proceeds to subsidize low income housing). In large measure, as a result of our policy dialogue, the GOP has recently a) passed Law 38 excluding all new construction from the system of rent control and b) passed law 36 eliminating the 0.5% tax proceeds to subsidize low income housing.

Additionally, the most inefficient sugar mill (Felipillo) was closed and some assets, notably a luxury hotel, were sold. COFINA (the state finance company) has ceased lending operations and the BNP will from now on serve as trustee for collecting COFINA's oustanding loans. The sale of several other assets has been proposed and studied, (e.g. Aeroperlas and the Contadora Hotel), but final decisions and procedures have yet to be established.

6/ (a) To present to the Legislature during 1985 a bill to reform the industrial incentive law through a system of low, uniform tariff protection.

(b) To present to the Legislature during 1985 an agricultural incentive law which emphasizes increasing exports, rather than encouraging self-sufficiency.

(c) To present to the Legislature during 1985 a proposal to modify those provisions of the current labor code which regulate payments for piecerate work.

B. FY 85 ESF Policy Agenda

USAID has been the major provider of housing resources and has been successful in attaining various policy changes such as the elimination of Law 28 of 1984 which taxed bank loans for commerce and industry and used the proceeds to subsidize interest rates, and the promulgation of Law 39 of 1984 which separated management responsibilities of MIVI and BHN, established a BHN Board of Directors (including major private sector participation) and eliminated some important restrictions on the S and L system. However, the net impact of some policy changes (e.g. the new system for preferential interest rates and Law 36) is ambiguous.

One of the conditions of the ESF program is the preparation and publication of a national housing policy. The covenants and conditions precedent on our FY 86 housing program will include GOP actions to adopt a national housing policy; to reduce the norms and standards of housing construction and thereby its cost; to strengthen the Savings and Loan system through administrative reforms; and to strengthen the housing finance system through measures to increase the flow of private resources for shelter development (e.g., secondary mortgage market operations).

The GOP has created a series of incentives to promote construction of housing. There is, however, no national housing policy which addresses the sector as a whole. We have, therefore, included as a covenant to this year's ESF assistance the preparation and publication by the GOP of a national housing policy which sets forth the strategy and objectives for meeting low-cost housing needs over the next five years, and which defines the roles of the public and private sectors in meeting those needs.

A bloated public sector is a major factor in government waste and inefficiency. We have conditioned our FY 1985 ESF assistance on the presentation to the Legislature of a civil service law which includes detailed plans for professionalizing GOP public administration and limiting public employment by detailing specific tasks, job descriptions, and qualifications for employment as an initial step in a program for improving the structure and efficiency of government agencies. Reduction in government spending and increase in its efficiency would contribute to financial stability by reducing the deficit of the public sector. To this end, we have also conditioned the proposed ESF assistance on turning over the operation and management to the private sector of the three grain storage silos financed by USAID/Panama under the Grains and Perishables Marketing Project (525-0178).

Finally, while divestiture is a sensitive political issue, we believe it is an absolute necessity because of the present and medium term fiscal situation. Accordingly, we have conditioned the proposed assistance on the preparation by a professionally qualified commission of a report to be submitted to the Legislature evaluating the financial and operational history and prospects of all state-owned enterprises. The report will evaluate the potential for improving the profitability of successful enterprises and the likelihood of saving money-losing enterprises. The report will recommend those enterprises which should be closed. In addition, the report will assess the utility and feasibility of divestiture in each case and evaluate the amounts the Government of Panama might realize through the sale of its ownership or of the assets of the businesses. This activity will be financed under USAID's Development Policy Studies Project. We also plan to use resources from the Policy Studies Project to advise the GOP on ways to streamline the current cumbersome divestiture procedures.

VII. THE PROPOSED PROGRAM

The USAID/Panama development strategy (see the recently submitted Action Plan for a more detailed discussion) consists of economic policy reforms designed to reactivate the economy by stimulating the private sector, promoting exports and efficient import substitution, and embarking on an austerity program to control public sector spending. The development strategy includes four major objectives; financial stabilization, economic growth, increased equity, and strengthening democratic institutions. The proposed ESF program significantly addresses three of these objectives.

As a result of the inordinate accumulation of government debt, the public sector will remain under severe financial constraints and cannot be expanded as in the past to stimulate the economy. A fiscal austerity and financial stabilization program which began in 1982 and which was reinforced with the mid 1983, 18 month IMF Stand-by Agreement will continue to be implemented according to the targets set under the July 15, 1985 new IMF Stand-by Arrangement. The proposed program grant will assist the GOP in meeting the September and December 1985 IMF quarterly targets. Unless the GOP meets the IMF targets, access to the refinancing facility will be in jeopardy creating an atmosphere of financial uncertainty which will make progress towards the other major strategy objectives significantly more difficult.

A. Financial Stabilization

USAID provided an essential component to Panama's 1984 financial stabilization program by supplying a $30 million cash transfer for budget support to the GOP thereby enabling the government to meet the terms of the mid 1983 IMF stand-by arrangement. Furthermore, compliance with the 18 month stand-by management subsequently allowed the GOP to negotiate in June of this year a syndicated commercial bank loan to refinance 1985-86 amortization payments of $603 million, obtain $60 million in new loans and $56.4 million for working capital.

The GOP's austerity program initiated in 1983 has produced a significant decline in the overall deficit of the public sector from 11% of GDP in 1982 to 6% during 1984. The recently concluded stand-by arrangement with the IMF has imposed further constraints on public spending by limiting the overall deficit of the public sector during 1985 to 3.5% of GDP.

By providing budgetary support to the GOP, U.S. assistance will furnish urgently required financing without which the GOP will have little maneuverability to be able to meet the IMF's performance standards thereby jeopardizing the new stand-by arrangement and access to the new syndicated loan for maturities of Panamanian public sector obligation due between January 1, 1985 and December 31, 1986.

B. Economic Growth

The economy of Panama has stagnated for the past two and a half years and will continue to do so this year. Our projects and policy dialogue are designed to remove restrictions to growth and assist in the reactivation of the economy.

Both USAID and the GOP continue to view construction sector investment and employment as a way to mitigate the impact of fiscal austerity while policy reforms to reactivate private sector growth are put into place.

To this end, the FY 86 Private Sector Shelter Development Project (HG-013) and HG-012 will improve employment prospects in the construction sector providing jobs for 6,000 persons in the short term. To generate additional employment through increased private investment USAID is: (1) supporting comprehensive economic policy analysis and development in conjunction with structural adjustment assistance from the World Bank; (2) working with the GOP and private entitites to expand availability of credit and technical assistance for small business; and (3) strengthening promotion and investor services capabilities of the National Investment Council and developing mechanisms to facilitate export production and marketing.

In consideration for providing the proposed grant assistance, the GOP will finance with their own funds priority construction activities in the 1985 investment budget which generate significant private sector employment. Annex III provides a sectoral breakdown of activities the GOP will maintain in the investment budget and provide funding for.

The criteria utilized by USAID and the GOP to select a set of priority activities included the following key considerations: (1) implementation of the proposed activities would not increase the number of employees in the public sector, (2) the activities would be implemented rapidly, i.e. the projects would be selected from those activities already approved by the legislature, (3) the activities would contribute to political stability and economic development, i.e., the projects would be of high visibility and development impact which provide employment creation, and can be implemented within a relatively short period of time, and (4) construction activities would be carried out by private sector firms. Construction by force account would be utilized only on an exceptional basis.

C. Increased Equity

A final key consideration to securing GOP funding for priority public investments towards the development and maintenance of basic infrastructure, the benefits of which would be equitably shared, were the recommendations from the NBCCA report. The report advises, inter alia, that a major investment thrust should be in labor intensive infrastructure for such areas as rural roads, bridges, municipal water, school construction and repair, strengthening major universities and improvement in the health care delivery system.

VIII. CONDITIONS AND COVENANTS

The Condition Precedent to disbursement and the covenants shown below have been discussed with appropriate representatives of the GOP, who have agreed to their inclusion in the grant agreement.

The first covenant deals with the preparation of a national housing policy for meeting low-cost housing needs, while the following three deal with reducing the role of the public sector and rationalizing public sector employment.

A. Condition Precedent to Disbursement

1. A statement of the name(s) of the person(s) holding or acting in the name of the grantee, and any additional representatives, together with a specimen signature of each authorized person specified in such statement.

B. Covenants

The Government of Panama will covenant to accomplish the following four specific actions within one year from the date of signing the project grant agreement.

1. To prepare and publish a national housing policy which sets forth the strategy and objectives for meeting low-cost housing needs over the next five years and which emphasizes the role of the private sector, especially in the areas of finance and construction, in meeting these needs. Specifically, the study will analyze the possibility of reducing the norms and standards of housing construction in order to reduce unit costs, it will propose measures to strengthen the Private Savings and Loan systems through administrative reforms, and it will design measures to increase the flow of private resources for shelter development (e.g. secondary mortgage markets).

2. To turn over the operation and management to the private sector of the three grain storage silos financed by USAID/Panama under the Grains and Perishables Marketing Project (525-0178).

3. To have a professionally qualified commission prepare a report which will be submitted by the Executive to the Legislature which:

(a) evaluates the financial and operational history and prospects of all state-owned enterprises;

(b) establishes the value of successful enterprises to demonstrate how much the government will profit from their sale, recommends how to improve the profitability of unsuccessful ones in order to enhance their market value, and recommends which enterprises should be closed;

(c) for those enterprises for which privatization is not feasible, recommends ways and means of improving the their operational efficiency.

4. As an initial step in a program for improvement of the structure and efficiency of government agencies, to present to the Legislature a civil service law which includes detailed plans for professionalizing GOP public administration and limiting public employment by detailing specific tasks, job descriptions and qualifications for employment.

Finanlly, in addition to the above covenants, the grant agreement will include all covenants from the supplemental FY 84 ESF grant agreement which have not yet been fulfilled.

A N N E X   I

5C(1) - COUNTRY CHECKLIST

Listed below are statutory criteria applicable generally to FAA funds, and criteria applicable to individual fund sources: Development Assistance and Economic Support Fund.

A. GENERAL CRITERIA FOR COUNTRY ELIGIBILITY

1. FAA Sec. 481; FY 1985 Continuing Resolution Sec. 528. Has it been determined or certified to the Congress by the President that the government of the recipient country has failed to take adequate measures or steps to prevent narcotic and psychotropic drugs or other controlled substances (as listed in the schedules in section 202 of the Comprehensive Drug Abuse and Prevention Control Act of 1971) which are cultivated, produced or processed illicitly, in whole or in part, in such country or trasported through such country, from being sold illegally within the jurisdiction of such country to United States Government personnel or their dependents or from entering the United States unlawfully?

   No.

2. FAA Sec. 620 (c). If assistance is to a government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) the debt is not denied or contested by such government?

   No.

3. FAA Sec. 620(e)(1). If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities?

   No.

4. FAA Sec. 620(a), 620(f), 620(D); FY 1985 Continuing Resolution. Sec. 512 and 513. Is recipient country a Communist country? Will assistance be provided to Angola, Cambodia, Cuba, Laos, Syria, Vietnam, Libya, or South Yemen? Will assistance be provided to Afghanistan or Mozambique without a waiver?

   No.

5. FAA Sec. 620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction by mob action of U.S. property?

   No.

6. FAA Sec. 620(l). Has the country failed to enter into an agreement with OPIC?

   No.

7. FAA Sec. 620(o); Fishermen's Protective Act of 1967, as amended, Sec. 5. (a) Has the country seized, or imposed any penalty or sanction against, any U.S. fishing activities in international waters?

   No.

   (b) If so, has any deduction required by the Fishermen's Protective Act been made?

8. FAA Sec. 620(q); FY 1985 Continuing Resolution Sec. 518. (a) Has the government of the recipient country been in default for more than six months on interest or principal of any AID loan to the country? (b) Has the country been in default for more than one year on interest or principal on any U.S. loan under a program for which the appropriation bill (or continuing resolution) appropriates funds?

No.

9. FAA Sec. 620(s). If contemplated assistance is development loan or from Economic Support Fund, has the Administrator taken into account the amount of foreign exchange or other resources which the country has spent on military equipment? (Reference may be made to the annual "Taking into Consideration" memo: "Yes, taken into account by the Administrator at time of approval of Agency OYB." This approval by the Administrator of the Operatinal Year Budget can be the basis for an affirmative answer during the fiscal year unless significant changes in circusmtances occur.)

Yes. The Administration has taken it into account at the time of approval of the Agency's OYB.

10. FAA Sec. 620(t). Has the country severed diplomatic relations with the United States? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption?

No.

11. FAA Sec. 620(u). What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearages taken into account by the AID Administrator in determining the current AID Operational Year Budget? (Reference may be made to the Taking into Consideraton memo.)

Panama is not in arrears in payment of its U.N. obligations.

12. FAA Sec. 620A; FY 1985 Continuing Resolution Sec. 521. Has the country aided or abetted, by granting sanctuary from prosecution to, any individual or group which has committed an act of international terrorism? Has the country aided or abetted, by granting sanctuary from prosecution to, any individual or group which has committed a war crime?

No.

13. FAA Sec. 666. Does the country object, on the basis of race, religion, national origin or sex, to the presence of any officer or employee of the U.S. who is present in such country to carry out economic development programs under the FAA?

No.

14. FAA Sec. 669, 670. Has the country, after August 3, 1977, delivered or received nuclear enrichment or reprocessing equipment, materials, or technology, without specified arrangements or safeguards? Has it transferred a nuclear explosive device to a non-nuclear weapon state, or if such a state, either received or detonated a nuclear explosive device? (FAA Sec. 620E permits a special waiver of Sec. 669 for Pakistan.)

No.

15. ISDCA of 1981 Sec. 720. Was the country represented at the Meeting of Ministers of Foreign Affairs and Heads of Delegations of the Non-Aligned Countries to the 36th General Session of the General Assembly of the U.N. of Sept. 25 and 28, 1981, and failed to dissasociate itself from the communique issued? If so, has the President taken it into account? (Reference may be made to the Taking into Consideration memo.)

Yes. It was taken into account at the of approval of the Agency's 1985 OYB.

16. FY 1985 Continuing Resolution. If assistance is from the population functional account, does the country (or organization) include as part of its population planning programs involuntary abortion?

N/A

17. FY 1985 Continuing Resolution Sec. 530. Has the recipient country been determined by the President to have engaged in a consistent pattern of opposition to the foreign policy of the United States?

No.

B. FUNDING SOURCE CRITERIA FOR COUNTRY ELIGIBILITY

1. Development Assistance Country Criteria

a. FAA Sec. 116. Has the Department of State determined that this government has engaged in a consistent pattern of gross violations of internationally recognized human rights? If so, can it be demonstrated that contemplated assistance will directly benefit the needy?

N/A

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2. Economic Support Fund Country Criteria

a. FAA Sec. 502B. Has it been determined that the country has engaged in a consistent pattern of gross violations of internationally recognized human rights? If so, has the country made such significant improvemenmts in its human rights record that furnishing such assistance is in the national interest?

No.

5C(2) PROJECT CHECKLIST

Listed below are statutory criteria applicable to projects. This section is divided into two parts. Part A. includes criteria applicable to all projects. Part B. applies to projects funded from specific sources only: B.1. applies to all projects funded with Development Assistance Funds, B.2. applies to all projects funded with Development Assistance loans, and B.3. applies to projects funded from ESF.

CROSS REFERENCES: IS COUNTRY CHECKLIST UP TO DATE? HAS STANDARD ITEM CHECKLIST BEEN REVIEWED FOR THIS PROJECT?

A. <u>GENERAL CRITERIA FOR PROJECT</u>

1. <u>FY 1985 Continuing Resolution Sec. 525; FAA Sec. 634A; Sec. 653(b).</u>

(a) Describe how authorizing and appropriations committees of Senate and House have been or will be notified concerning the project; (b) is assistance within (Operational Year Budget) country or international organization allocation reported to Congress (or not more than $1 million over that amount)?

(a) This assistance was included in the FY Congressional Presentation at the level of $20 million. A Congressional Notification however, will be sent to Congress for the additional $7 million.

(b) This assistance is within the OYB.

2. <u>FAA Sec. 611(a)(1).</u> Prior to obligation in excess of $100,000, will there be (a) engineering, financial or other plans necessary to carry out the assistance and (b) a reasonably firm estimate of the cost to the U.S. of the assistance?

(a) Yes.

(b) Yes.

3. FAA Sec. 611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?

No further legislative action will be required by the assistance agreement.

4. FAA Sec. 611(b); FY 1985 Continuing Resolution Sec. 501. If for water or water-related land resource construction, has project met the standards and criteria as set forth in the Principles and Standards for Planning Water and Related Land Resources, dated October 25, 1973, or the Water Resources Planning Act (42 U.S.C. 1962, et seq.)? (See AID Handbook 3 for new guidelines.)

This is not a water or water-related land resource construction project.

5. FAA Sec. 611(e). If project is capital assistance (e.g., construction), and all U.S. assistance for it will exceed \$1 million, has Mission Director certified and Regional Assistant Administrator taken into consideration the country's capability effectively to maintain and utilize the project?

N/A. The assistance to be provided is a cash transfer for budgetary support.

6. FAA Sec. 209. Is project susceptible to execution as part of regional or multilateral project? If so, why is project not so executed? Information and conclusion whether assistace will encourage regional development programs.

No. This program assistance compliments the assistance efforts of multilateral agencies and providing a cash transfer has been deemed to be the most appropriate to achieve the desired economic and political program objectives.

7. FAA Sec. 601(a). Information and conclusions whether project will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; and (c) encourage development and use of cooperatives, and credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture and commerce; and (f) strengthen free labor unions.

The cash transfer program assistance will (a) have a positive influence on trade, (b) stimulate the private sector through the required competitive award of contracts for construction activities to private sector firms; (d) contribute to the spread of the benefits of growth and (e) increase public sector and technical efficiency. No major impact on labor unions (f) or cooperatives (c) is contemplated.

8. FAA Sec. 601(b. Information and conclusions on how project will encourage U.S. private trade and investment abroad and encourage U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).

The program assistance will provide the necessary resources for the Government of Panama to maintain the financial and political stability necessary for continued investor confidence in the country and its public and private institutions.

9. FAA Sec. 612(b), 636(h); FY 1985 Continuing Resolution Sec. 507. Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies owned by the U.S. are utilized in lieu of dollars.

No.

10. FAA Sec. 612(d). Does the U.S. own excess foreign currency of the country and, if so, what arrangements have been made for its release?

There is no local currency in Panama. U.S. Dollars are used exclusively

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11. FAA Sec. 601(e). Will the project utilize competitive selection procedures for the awarding of contracts, except where applicable procurement rules allow otherwise?

All contracts awarded pursuant to this program assistance will be competed.

12. FY 1985 Continuing Resolution Sec. 522. If assistance is for the production of any commodity for export, is the commodity likely to be in surplus on world markets at the time the resulting productive capacity becomes operative, and is such assistance likely to cause substantial injury to U.S. producers of the same, similar or competing commodity?

No.

13. FAA 118(c) and (d). Does the project comply with the environmental procedures set forth in AID Regulation 16. Does the project or program take into consideration the problem of the destruction of tropical forests?

Yes. Nonproject assistance is being provided here.

14. FAA 121(d). If a Sahel project, has a determination been made that the host government has an adequate system for accounting for and controlling receipt and expenditure of project funds (dollars or local currency generated therefrom)?

This is not a Sahel project.

15. FY 1985 Continuing Resolution Sec. 536. Is disbursement of the assistance conditioned solely on the basis of the policies of any multilaleral institution?

No.

B. <u>FUNDING CRITERIA FOR PROJECT</u>

1. <u>Development Assistance Project Criteria</u>

a. <u>FAA Sec. 102(b), 111, 113, 281(a).</u> Extent to which activity will (a) effectively involve the poor in development, by extending access to economy at local level, increasing labor-intensive production and the use of appropriate technology, spreading investment out from cities to small towns and rural areas, and insuring wide participation of the poor in the benefits of development on a sustained basis, using the appropriate U.S. institutions; (b) help develop cooperatives, especially by technical assistance, to assist rural and urban poor to help themselves toward better life, and otherwise incourage democratic private and local governmental institutions; (c) support the self-help efforts of developing countries; (d) promote the participation of women in the national economies of developing countries and the improvement of women's status; and (e) utilize and encourage regional cooperation by developing counntries? — N/A

b. <u>FAA Sec. 103, 103A, 104, 105, 106.</u> Does the project fit the criteria for the type of funds (functional account) being used? — N/A

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c. FAA Sec. 107. Is emphasis on use of appropriate technology (relatively smaller, cost-saving, labor-using technologies that are generally most appropriate for the small farms, small businesses, and small incomes of the poor)?

N/A

d. FAA Sec. 110(a). Will the recipient country provide at least 25% of the costs of the program, project, or activity with respect to which the assistance is to be furnished (or is the latter cost-sharing requirement being waived for a "relatively least developed" country)?

N/A

e. FAA Sec. 110(b). Will grant capital assistance be disbursed for project over more than 3 years? If so, has justification satisfactory to Congress been made, and efforts for other financing, or is the recipient country "relatively least developed"? (M.O. 1232.1 defined a capital project as "the construction, expansion, equipping or alteration of a physical facility or facilities financed by AID dollar assistance of not less than $100,000, including related advisory, managerial and training services, and not undertaken as part of a project of a predominantly technical assistance character."

N/A

f. FAA Sec. 122(b). Does the activity give reasonable promise of contributing to the development of economic resources, or to the increase of productive capacities and self-sustaining economic growth?

N/A

g. FAA Sec. 281(b). Describe extent to which program recognizes the particular, needs, desires, and capacities of the people of the country, utilizes the country's intellectual resources to encourage institutional development; and supports civil education and training in skills required for effective participation in governmental processes essential to self-government.

N/A

2. Development Assistance Project Criteria (Loans Only)

a. FAA Sec. 122(b). Information and conclusion on capacity of the country to repay the loan, at a reasonable rate of interest.

N/A

b. FAA Sec. 620(d). If assistance is for any productive enterprise which will compete with U.S. enterprises, is there an agreement by the recipient country to prevent export to the U.S. of more than 20% of the enterprise's annual production during the life of the loan?

N/A

3. Economic Support Fund Project Criteria

a. FAA Sec. 531(a). Will this assistance promote economic or political stability? To the extent possible, does it reflect the policy directions of FAA Section 102?

Yes. The purpose of the assistance is to provide urgently needed budgetary support to the Government of Panama and this contribution is essential to the continued financial and political stability of Panama.

b. <u>FAA Sec. 531(c).</u> Will assistance under this chapter be used for military, or paramilitary activities?	No.
c. <u>FAA Sec. 534.</u> Will ESF funds be used to finance the construction of or the operation or maintenance of, or the supplying of fuel for, a nuclear facility? If so, has the President certified that such use of funds is indispensable to nonproliferation objectives?	No.
d. <u>FAA Sec. 609.</u> If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made?	No commodities will be granted under this program.

ANNEX II

Table I

Summary of Social Indicators

	Panama		Middle Income Latin American Country
	1970	1980	1980
GNP/Capita	760	1910	2090
Life expectancy at birth	66	71	65
Infant mortality rate (per 000)	49	21	63
Access to safe water (% of population)	69	85	65
Access to excreta disposal (% of population)	78	89	55
Population per physician	1580	980	1776
Population per nurse	550	420	1012
Population per hospital bed	330	250	477
Primary school enrollment (%)	106	113	105
Secondary school enrollment (%)	39	65	40
Adult literacy rate (%)	78	85	80

Table 2
GROSS DOMESTIC PRODUCT AT MARKET PRICES BY SECTOR, 1970 PRICES, 1970-83
(Millions of 1970 Balboas)

Sector	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Agriculture, Forestry & Fishing	149.1	160.7	155.4	157.1	147.9	158.6	167.1	175.5	189.1	181.0	173.7	188.1	185.2	194.4	192.0
Mining & Quarrying	1.9	2.2	2.4	2.9	2.7	2.5	2.2	2.1	2.2	2.4	3.1	3.8	4.1	4.4	4.4
Manufacturing	127.3	135.4	141.6	150.5	152.5	147.0	150.7	152.5	154.9	172.0	182.1	176.1	179.9	176.1	176.0
Electricity, Gas & Water	21.8	23.8	24.9	31.7	33.1	38.3	42.6	44.0	46.7	52.4	53.5	56.2	59.2	65.7	65.5
Construction	60.2	85.0	87.0	99.6	87.9	96.9	99.6	73.8	102.5	102.4	124.3	128.3	154.7	106.6	96.7
Commerce, Hotels & Restaurants	161.0	176.3	185.2	193.3	202.6	191.0	197.9	202.3	219.6	240.9	256.4	252.9	251.0	235.2	233.2
Transport, Warehousing & Communications	61.2	69.7	80.5	90.7	118.2	116.0	109.7	121.6	145.1	155.4	207.6	216.5	251.1	320.6	281.6
Financial Establishments, Insurance and Real Estate	122.1	136.3	150.1	165.7	170.7	178.8	184.2	193.8	199.7	222.9	227.2	243.5	252.6	262.9	269.5
Social and Community Services	68.2	76.2	88.5	92.3	97.3	102.0	109.9	100.9	118.3	127.8	142.6	150.1	163.3	165.1	173.2
Services to Panama Canal Area b/	75.0	75.5	74.4	75.1	77.8	74.7	70.0	71.4	74.3	76.4	0.0	0.0	0.0	0.0	0.0
Panama Canal Com. Commission a/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	175.5	188.4	204.7	175.7	174.6
Less: Imputed Commission at Banking Sector	10.8	11.4	20.6	24.1	30.5	30.1	33.0	43.6	33.3	56.4	47.2	54.2	68.2	64.9	67.1
INDUSTRY SUBTOTAL	845.2	929.7	969.4	1,034.8	1,060.2	1,075.7	1,096.1	1,103.3	1,219.1	1,277.2	1,498.8	1,549.7	1,637.6	1,631.8	1,599.6
Government Services	117.8	127.5	130.7	141.5	157.2	169.9	172.1	181.7	187.6	196.3	201.2	222.9	232.1	242.3	249.8
Domestic Services	21.3	21.6	21.0	20.6	18.5	19.2	17.2	16.3	17.6	16.3	17.7	18.5	19.3	19.5	20.0
plus: Import Duties	36.9	40.6	41.6	36.6	27.0	20.9	21.7	20.1	26.5	26.3	28.1	27.7	29.6	32.7	33.2
GROSS DOMESTIC PRODUCT AT MARKET PRICES	1,021.2	1,119.4	1,170.7	1,233.5	1,263.7	1,285.7	1,307.1	1,321.4	1,450.8	1,516.3	1,745.8	1,818.8	1,918.6	1,926.3	1,902.6

a/ In 1980 the Panama Canal Treaties became effective which incorporated Canal activities into the GDP accounts.
b/ Preliminary
Source: Comptroller General

Table 3

GDP by Major Components*

(Milliones of 1970 Balboas)

	G D P	%	% per capita**	"AUTONOMOUS"	%	% per capita**	"OFFICIAL"	%	% per capita**	"PRIVATE"	%	% per capita**
1970	1,021.2	-	-	75.0	-	-	186.4	-	-	759.8	-	-
1973***	1,233.5	6.5	3.7	75.1	0.0	-2.8	222.6	6.1	3.3	935.8	7.2	4.4
1977****	1,321.4	1.7	-0.9	71.4	-1.2	-3.8	262.3	4.2	1.6	987.7	1.4	-1.2
1978	1,450.8	9.8	7.4	74.3	4.1	1.7	278.1	6.0	3.6	1,098.4	11.2	8.8
1979	1,516.3	4.5	2.2	76.4	2.8	0.5	294.3	5.8	3.5	1,145.6	4.3	2.0
1980	1,745.8	15.1	10.9	204.8	168.1	163.9	303.0	3.0	-1.2	1,238.0	8.1	3.9
1981	1,818.8	4.2	2.0	220.1	7.5	5.3	328.3	8.3	6.1	1,270.4	2.6	0.4
1982	1,919.6	5.5	3.3	273.7	24.4	22.2	343.8	4.7	2.5	1,302.1	2.5	0.3
1983	1,926.3	0.4	-1.8	342.0	25.0	22.8	364.3	6.0	3.8	1,220.0	-6.3	-8.5
1984	1,902.6	-1.2	-3.4	311.2	-9.0	-11.2	373.5	2.5	0.3	1,217.9	-0.2	-2.4
Average 1984/78:		4.6	2.1	-	27.0	23.8	-	5.0	2.4	-	1.7	-0.8

*Autonomous = Canal zone and oil pipeline; Official = Government services, Public utilities (electricity, gas, water and communications) and import duties; Private = the rest of GDP.

**Population figures from MIPPE (in thousands) are: 1970: 1,487.2; 1973: 1,616.7; 1977: 1,791.5; 1978: 1,835.1; 1979: 1,878.1; 1980: 1,956.5; 1981: 1,999.6; 1982: 2,043.7; 1983: 2,088.6; y 1984: 2,134.2.

***Percentage changes are annual averages, end 1970 to end 1973.

****Percentage changes are annual averages, end 1973 to end 1977.

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TABLE NO. 4

PANAMA: REAL SECTOR OVERVIEW

	1980	1981	1982	1983	1984[2]
GDP (at current mkt prices in US$ millions)	3,558.8[1]	3,878.0	4,278.9	4,379.4	4,429.2
Growth rates (%)					
Nominal GDP	14.3[1]	9.0	10.3	2.3	1.1
Real GDP*	6.7[1]	4.2	4.7	-1.5	-0.4
GDP deflator	7.1	4.6	5.4	3.9	1.5
Wholesale price index	15.4	10.0	0.3	2.4	1.0
Consumer price index	13.0	7.3	4.2	2.1	1.6
Nominal wages	8.8	4.2	6.2	2.8	7.0

1 Changes for 1980 exclude the effect of the incorporation of the Canal Zone to Panama in 1980.

2 Estimated

* Pipeline deflated by GDP deflator

Source: Office of the Comptroller General.

TABLE NO. 5

PANAMA: SECTORAL ORIGIN OF GDP

(in millions of balboas at 1970 prices)

	1980	1981	1982	1983	1984
GROSS DOMESTIC PRODUCT	1,735.1	1,808.2	1,892.5	1,864.1	1,857.0
PRIMARY ACTIVITIES	176.8	191.9	189.3	198.8	196.4
Agriculture	173.7	188.1	185.2	194.4	192.0
Mining	3.1	3.8	4.1	4.4	4.4
SECONDARY ACTIVITIES	306.4	304.4	334.6	282.7	272.7
Manufacturing	182.1	176.1	179.9	176.1	176.0
Construction	124.3	128.3	154.7	106.6	96.7
SERVICES	1,271.0	1,338.4	1,407.2	1,414.8	1,421.8
Public utilities	53.5	56.2	59.2	65.7	65.5
Commerce, restaurants and hotels	256.4	252.9	251.0	235.2	233.2
Transport and communication	113.8	121.8	154.5	197.7	185.0
of which: oil pipeline*	[18.6]	[21.1]	[42.9]	[104.1]	[87.2]
Colon Free Zone	83.1	84.1	70.5	50.7	51.0
Panama Canal Commission	175.5	188.4	204.7	175.7	174.6
Financial intermediation	96.3	106.4	110.6	117.1	120.1
Housing rent	130.9	137.1	142.0	145.8	149.4
Public administration	201.2	222.9	232.1	242.3	249.8
Other services	160.3	168.6	182.6	184.6	193.2
less imputed banking services and import taxes	(19.1)	(26.5)	(38.6)	(32.2)	(33.9)

Source: Office of the Comptroller General

* Pipeline deflated by GDP deflator

TABLE NO. 6

PANAMA: BALANCE OF PAYMENTS

	1982	1983	1984	1985	1986
Trade Balance, f.o.b.	-1007.3	-924.8	-889.2	-858.1	-846.4
Exports (nonpetroleum)	322.1	306.9	278.7	290.5	322.1
Petroleum Trade	-242.0	-263.4	-195.5	-168.4	-156.4
Imports (nonpetroleum)	-1087.4	-968.3	-972.4	-980.2	-1012.1
Services Balances	582.5	710.6	582.0	589.4	607.3
Freight and Insurance	-53.3	115.7	68.7	77.4	27.3
Transportation	397.0	350.0	343.9	354.5	363.5
Travel	93.2	97.3	118.7	128.0	137.7
Investment Income	-361.9	-312.5	-398.3	-458.5	-442.9
(Of Which:					
Interest on Public Debt)	(-350.3)	(-288.6)	(-316.6)	(-391.1)	(-370.0)
Govt, not incl. elsewhere	-15.0	-18.0	-7.7	-7.9	-8.0
Other Services	522.5	478.1	456.7	495.9	529.7
Colon Free Zone	219.6	142.4	148.0	164.8	174.9
Other	302.9	335.7	308.7	331.1	354.8
Unrequited Transfers	36.0	41.0	48.2	48.2	48.2
Current Account	-388.8	-173.2	-259.0	-220.5	-190.9
Capital Account	760.5	90.7	124.0	145.3	123.1
Official Capital	526.1	253.3	207.4	178.7	114.0
Nonfinancial	435.8	152.5	99.2	202.4	181.5
Official Banks	90.3	100.8	108.2	-23.7	-67.5
Use of IMF Resources	-9.5	116.8	97.7	10.0	12.1
Other Liabilities	38.1	-16.0	10.5	-33.7	-79.6
Oth. Off. Bank Transactions	38.1	-142.6	-12.5	0.0	0.0
Private Capital	196.3	-20.0	-70.9	-33.4	9.1
Direct Investment	138.6	49.2	35.8	6.1	10.2
Direct Private Borrowing	125.2	-158.0	-136.2	-69.0	-30.6
Private Banks (net)	-67.5	88.8	29.5	29.5	29.5
Net Errors & Omissions	-370.0	83.9	136.7	75.2	67.8
Valuation Adjustment	-1.7	-1.4	1.7	0.0	0.0

Source: Office of the Comptroller General

TABLE NO. 7

PANAMA: COMPOSITION OF MERCHANDISE EXPORTS

(In millions of U.S. dollars)

	1980	1981	1982	Prel. 1983	Est. 1984
Merchandise exports, f.o.b.	526.1	496.1	488.7	427.5	419.2
Petroleum	233.3	209.1	166.6	120.6	133.0
Nonpetroleum exports, f.o.b.	271.6	261.0	240.1	267.7	250.9
Bananas					
Value	61.6	69.2	66.0	75.0	74.6
Volume (millions of boxes)	27.6	30.2	31.1	36.2	36.1
Unit value	2.232	2.291	2.122	2.072	2.066
Sugar					
Value	65.8	52.6	23.7	41.3	33.3
Volume (thousands of metric tons)	130.3	97.1	107.0	120.0	82.1
Unit value	0.505	0.542	0.221	0.344	0.406
Shrimp					
Value	47.7	42.7	52.9	51.4	49.4
Volume (thousands of metric tons)	6.2	6.4	6.8	6.1	5.9
Unit value	7.048	6.672	7.779	8.426	8.372
Coffee					
Value	10.2	13.5	12.1	15.2	12.0
Volume (thousands of metric tons)	3.1	5.1	4.3	5.6	4.3
Unit value	3.290	2.647	2.814	2.714	2.791
Fish meal					
Value	10.1	4.3	1.6	5.5	2.7
Volume (thousands of metric tons)	28.1	11.7	4.4	14.8	6.9
Unit value	0.359	0.367	0.364	0.372	0.391
Clothing					
Value	10.4	14.0	17.3	7.6	9.3
Volume (thousands of metric tons)	334.3	411.3	546.5	281.2	335.0
Unit value	0.031	0.034	0.032	0.027	0.028
Other exports	69.8	64.7	66.5	71.7	69.6
Balance of payments adjustments	14.1	16.8	16.3	20.2	13.3
Re-exports	7.1	9.2	65.7	19.0	22.0

Source: Office of the Comptroller General.

TABLE NO. 8

PANAMA: COMPOSITION OF MERCHANDISE IMPORTS

(In millions of U.S. dollars)

	1980	1981	1982	Prel. 1983	Est. 1984
Merchandise imports, f.o.b.	1,342.0	1,469.9	1,496.0	1,352.3	1,341.6
Nonpetroluem imports, f.o.b.	874.1	976.5	1,007.4	891.7	928.9
Food	97.0	93.4	101.5	107.1	104.4
Beverages and tobacco	7.5	8.7	8.8	7.9	8.1
Raw materials	8.3	9.2	8.3	7.1	7.4
Animal and vegetable oils	18.5	13.3	13.8	15.0	15.1
Chemicals	131.1	140.5	141.5	148.1	160.1
Manufacturers	243.0	263.9	254.7	205.4	225.3
Machinery and transportation equipment	258.7	319.8	355.6	280.8	264.4
Miscellaneous manufactures	116.6	120.9	121.6	118.2	125.4
Other	2.4	6.8	1.6	1.7	18.7
Petroleum imports, f.o.b.	424.4	426.1	408.6	384.0	350.2
Imports of fuels and lubricants (net)	191.1	217.0	242.0	263.4	217.2
Re-exports of fuels and lubricants	233.3	209.1	166.6	120.6	133.0
Imports of the Panama Canal Commission, f.o.b.	24.5	46.0	53.5	51.9	35.8
Balance of payment adjustments	19.0	21.3	26.5	24.7	26.7

Source: Office of the Comptroller General.

Table No. 10

1983/84 IMF Stand-by Program Targets and Results

(In Millions of U.S. Dollars)

	Program Objectives	Actual Results	Favorable Margin
Non-Financial Public Sector Deficit	520.0	513.7	6.3
Internal Financing Credit from BNP	0.0	16.9	-16.9
Net Increase in Public Sector External Debt	520.0	507.0	13.0
Net Increase in Commercial Debt	0.0	-21.7	21.7

TABLE NO. 11

1985 IMF STAND-BY PERFORMANCE CRITERIA [1]

(in millions of U.S. dollars)

	Mar 31[2]	Jun 30	Sep 30	Dec 31
rget 1. Fiscal Deficit	14.8	68.0	108.0	160.0
rget 2. Internal Financing[3] (Net Credit of BNP to the Public Sector)	45.9	70.0	30.0	0.0
Target 3. Net External Financing	-31.1	-2.0	78.0	160.0
Target 4. Total External Commercial Financing	-19.9	5.0	30.0	32.0
Target 5. Short-Term Commercial Financial				40.2

[1] Specific targets for 1986 will be defined later during the program.

[2] Actual

[3] Any shortfalls/excesses on the net external financing target may be compensated by a similar increase/decrease in the level of net credit extended by BNP to the nonfinancial public sector.

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TABLE NO. 12

PANAMA: CONSOLIDATED PUBLIC SECTOR NON-FINANCIAL OPERATIONS

(in Millions of U.S. dollars)

	1981	1982	1983	1984	1985 Forecast	1986 Forecast
Public Sector Revenues	1,169.0	1,264.5	1,387.0	1,424.6	1,531.8	1,548.2
General Government	1,106.0	1,223.3	1,316.6	1,260.5	1,392.2	
Central Government	775.2	837.5	862.6	858.6	975.8	
CSS	266.7	318.7	333.1	312.4	328.5	
Agencies	64.1	67.1	120.9	89.5	87.9	
Operations Balance Public Entities	62.4	41.2	70.4	134.1	139.6	
Donations	0.6	0.0	0.0	30.0	0.0	0.0
Public Sector Expenses	1,383.7	1,726.5	1,651.7	1,699.0	1,690.8	1,657.
General Govt. Current. Expenditures	1,013.6	1,208.1	1,244.5	1,333.6	1,383.9	1,367.
Central Government	685.2	828.8	814.1	898.0	907.7	
CSS	235.7	266.5	314.7	334.4	356.0	
Agencies	92.7	112.8	115.7	101.2	111.2	
Public Sector Savings	155.4	56.4	142.5	91.0	147.9	180.
Capital Expenditures	370.1	518.4	407.2	365.4	312.9	290.
Surplus or Deficit (-) Consol. Public Sector	-214.7	-462.0	-264.7	-274.4	-165.0	-109.
Non-Consolidated Public Sector Balance	6.6	-2.0	17.4	8.0	5.0	0.
Surplus or Deficit (-) Public Sector	-208.1	-464.0	-247.3	-266.4	-160.0	-109.
FINANCING						
External	76.8	432.8	250.0	91.4	160.0	109.
Bco Nacional de Panama	131.3	31.2	0.0	175.0	0.0	0.
as % of GDP						
Revenues	30.1	29.6	31.7	32.2	33.9	33.
Current Expenses	26.1	28.2	28.4	30.1	30.7	29.
Capital Expenses	9.5	12.1	9.3	8.2	6.9	6.
Public Sector Savings	4.0	1.3	3.3	2.1	3.3	3.
Public Sector Deficit	-5.4	-10.8	-5.6	-6.0	-3.5	-2

TABLE NO. 13

PANAMA: SOURCES AND USES OF FUNDS
(in Millions of U. S. dollars)

SES	1985	1986
Public Sector Revenues	1,531.8	1,548.2
Public Sector Current Exp.	1,383.9	1,367.3
Public Sector Savings	147.9	180.9
Capital Expenditures	312.9	290.0
Consolidated Public Sector Balance	-165.0	-109.1
Non-Consolidated Public Sector Balance	5.0	0.0
PUBLIC SECTOR DEFICIT	-160.0	-109.1
AMORTIZATIONS	399.7	608.3
World Bank	24.0	30.7
U.S. AID	2.7	2.7
Inter-Amer. Dev. Bank	14.4	25.0
Others	1.9	0.6
Suppliers	17.0	13.4
Commercial Banks	225.0	377.8
Securities	50.3	29.9
FIVEN	16.5	56.7
PEMEX	19.6	19.6
IMF	28.3	38.9
Impregilio	0.0	13.0
GROSS FINANCING NEEDS	559.7	717.4
SOURCES		
DISBURSEMENTS	284.7	296.5
World Bank (Projects)	40.0	50.0
World Bank (SAL)	0.0	60.0
U.S. AID (Projects)	30.9	42.0
U.S. AID (ESF)	60.0	15.0
Inter-Amer. Dev. Bank	60.9	70.0
IMF	35.0	44.0
Floating Rate Notes	20.0	0.0
Suppliers	13.0	12.0
FIVEN	5.7	0.0
Impregilio	13.0	0.0
Others	6.2	3.5
Domestic Bonds (net)	0.0	0.0
Short-term (net)	0.0	0.0
NET FINANCING NEEDS	275.0	420.9
Paris Club	8.0	16.4
Securities Replacement		8.7
Commercial Bank Refinancing	225.0	377.8
"FRESH" COMMERCIAL CREDIT	42.0	18.0

TABLE NO. 14

PANAMA: OUTSTANDING EXTERNAL DEBT

(in millions of U.S. dollars)

	1979	1980	1981	1982	1983	1984	1985	19
STOCKS OUTSTANDING AT END OF PERIOD								
TOTAL	2275.4	2502.7	2698.0	3197.6	3492.8	3677.2	3859.2	3976.
TOTAL (Net of Domestic Bonds)	2167.9	2400.7	2602.5	3105.6	3405.3	3596.6	3778.6	3895.
IBRD	117.8	132.7	162.6	185.8	257.8	288.2	364.3	443.
IDB	151.3	196.3	197.8	256.4	320.8	395.0	441.5	486.
IMF	41.4	23.0	93.6	83.9	192.7	271.0	281.0	293.
US AID	154.5	161.0	165.1	184.2	196.0	207.7	295.9	350.
FIVEN	37.3	43.3	86.5	121.1	144.5	156.2	145.4	88.
PEMEX	0.0	0.0	18.2	55.9	70.9	73.0	53.4	33.
OTHER BILATERAL	83.1	81.3	90.6	103.0	100.0	100.1	104.3	107.
of which: Venezuela	(63.6)	(61.4)	(71.8)	(584.2)	(82.7)	(85.3)	(87.4)	(89.
COMMERCIAL BANKS	1155.8	1305.2	1369.2	1723.7	1795.3	1803.2	1843.2	1874.
EXTERNAL SECURITIES	360.4	351.1	344.6	298.8	262.9	245.4	195.1	165.
SUPPLIER'S CREDITS	39.9	35.6	29.2	28.8	23.3	16.6	14.3	12.
SHORT-TERM	26.4	71.2	45.1	64.0	41.1	40.2	40.2	40.
DOMESTIC BONDS	107.5	102.0	95.5	92.0	87.5	80.6	80.6	80.
OF WHICH:								
MULTI AND BILATERAL	585.4	637.6	814.4	990.3	1282.7	1491.2	1685.8	1803.
COMMERCIAL	1582.5	1763.1	1788.1	2115.3	2122.6	2105.4	2092.8	2092
(In Percent of GDP)								
TOTAL	81.3	70.3	69.6	74.7	79.8	82.9	84.9	84
MULTI AND BILATERAL	20.9	17.9	21.0	23.1	29.3	33.6	37.1	38
COMMERCIAL	56.5	49.5	46.1	49.4	48.5	47.5	46.1	44
NET OF DOMESTIC BONDS	77.4	67.5	67.1	72.6	77.8	81.1	83.2	83

TABLE NO. 15

PANAMA: EXTERNAL DEBT MATURITY PROFILE

(in millions of U. S. dollars)

	External Debt O/S at Year-End	Contracted Amortizations					
	1984	1985	1986	1987	1988	1989	1990
:al	3596.7	399.7	595.3	674.0	594.1	467.4	284.9
:t'l Organization	1491.2	107.4	174.2	198.0	157.7	162.3	190.1
World Bank	288.2	24.0	30.7	37.5	40.5	40.8	44.5
AID	207.7	2.7	2.7	2.7	5.0	5.0	5.0
IDB	395.0	14.4	25.0	29.2	30.9	31.8	33.3
IMF	271.0	28.3	38.9	71.8	70.6	78.2	106.8
Other Bilateral and Multilateral	100.1	1.9	0.6	0.4	0.4	1.3	0.5
FIVEN	156.2	16.5	56.7	41.9	6.3	4.0	0.0
PEMEX	73.0	19.6	19.6	14.5	4.0	1.2	0.0
Suppliers	16.6	17.0	13.4	13.0	13.0	12.0	2.7
External Securities	245.5	50.3	29.9	30.0	28.1	17.0	17.1
Commercial Banks	1803.2	225.0	377.8	433.0	395.3	276.1	75.0
Short-Term	40.2						

TABLE No. 16

PANAMA: MEDIUM-TERM OUTLOOK

	1985	1986	1987	1988	1989	1990
Fiscal Deficit	160.0	109.1	100.0	104.6	112.3	105.8
Amortizations	399.7	608.3	674.2	599.1	501.5	331.1
Commercial Banks	225.0	377.8	433.2	400.3	310.2	121.2
Contracted Amounts	225.0	377.8	433.2	395.3	276.1	75.0
1985/86 Refinancing					24.1	36.2
1985/86 Term Credit				5.0	10.0	10.0
Securities	50.3	29.9	30.0	28.1	17.0	17.1
Intl. Organizations	124.4	200.6	211.0	170.7	174.3	192.8
World Bank	24.0	30.7	37.5	40.5	40.8	44.5
U.S. AID	2.7	2.7	2.7	5.0	5.0	5.0
IDB	14.4	25.0	29.2	30.9	31.8	33.3
Other Bi/Multilateral	30.2	39.5	72.2	71.0	79.5	107.3
FIVEN	16.5	56.7	41.9	6.3	4.0	0.0
PEMEX	19.6	19.6	14.5	4.0	1.2	0.0
Suppliers	17.0	26.4	13.0	13.0	12.0	2.7
Total Financing Needs	559.7	717.4	774.2	703.7	613.8	436.9
Intl Agencies	284.7	296.5	372.8	316.2	340.6	386.8
Project Lending	169.7	177.5	190.0	196.2	210.6	226.8
Budgetary Support	80.0	15.0	40.0	45.0	50.0	55.0
IMF	35.0	44.0	82.8	75.0	80.0	105.0
SAL	0.0	60.0	60.0	0.0	0.0	0.0
Net Financing Gap	275.0	420.9	401.4	387.6	273.2	50.1
Paris Club	8.0	16.4				
Securities	0.0	8.7				
Refin. of Comml Banks	225.0	377.8	433.2	395.3	276.1	75.0
New Term Credit	42.0	18.0				
Surplus	0.0	.0	31.8	7.7	2.9	24.9
Real GDP Growth	0.4	0.8	1.6	2.0	2.4	2.7

TABLE NO. 17

PANAMA: CONSOLIDATED BANKING SYSTEM

(In Millions of Balboas)

	1980	1981	1982	1983	1984
Net Foreign Reserves	4836.4	5379.5	6462.7	6994.4	6347.0
Asset	5761.0	6667.9	8098.4	8933.8	8108.7
Liabilities	924.6	1288.4	1635.7	1939.4	1761.7
Overseas Operations (Net)	-5393.5	-6003.6	-6683.9	-7183.3	-6606.3
Credit to Non-Residents	13327.1	18125.1	19093.9	15921.3	14338.5
Deposits from Non-Residents	18607.3	23891.6	25291.5	22635.1	20376.6
Other Foreign Liability	113.3	237.1	487.3	469.5	568.2
Net Domestic Assets	2699.3	3187.1	3354.3	3418.5	3641.6
Public Sector Net	265.6	389.9	518.0	669.3	874.9
Private Sector	2210.7	2619.2	2687.7	2697.2	2740.7
Unclassified Assets (Net)	223.0	178.0	148.6	52.0	26.0
Long Term Foreign Liabilities	63.9	136.0	215.2	259.4	275.4
SDR Allocation	27.7	30.7	29.0	27.6	25.9
Liabil. To Domestic Private Sector	1453.3	1713.9	1936.2	1954.6	2101.3
Demand Deposits	328.8	353.7	375.4	366.2	383.9
Time Deposits	885.0	1100.0	1269.9	1275.4	1378.6
Savings Deposits	235.6	254.4	282.4	295.7	320
Other Deposits	2.9	5.8	8.5	17.3	18.8
Private Capital and Surplus	597.3	682.4	952.7	988.0	979.7

ANNEX III

62

LISTA DE OBRAS DEL PROGRAMA DE INVERSIONES A MANTENERSE EN EL PRESUPUESTO FINANCIADAS CON FONDOS DEL GOBIERNO DE PANAMA

SECTOR	RENGLON	SUB SEC	SECTOR
EDUCACION			7,533,100
	1. Ministerio de Educación	6,463,100	
	2. Universidad Tecnologica	500,000	
	3. Universidad de Panamá	570,000	
SALUD			6,219,700
	1. Ministerio de Salud	4,130,700	
	2. Direccion Metropolitana de aseo	2,089,000	
TRANSPORTE			10,986,300
	1. Ministerio de Obras Públicas	8,236,800	
	2. Ferrocarril de Panamá	749,500	
	3. Construcción Carretera de Acceso al Nuevo Relleno Sanitario (Ejecutor MOP)	2,000,000	
MULTISECTORIAL			2,727,300
	1. Construcción de Obras de PROINCO (Ejecutor MIPPE)	2,227,300	
	2. Ejecución del Proyecto Acuicola de Areas Marguinadas	200,000	
	3. Obras Múltiples en el Distrito Especial de San Miguelito (Ejecutor MIPPE)	300,000	
	TOTAL		27,466,400

LISTA DE OBRAS DEL PROGRAMA DE INVERSIONES A MANTENERSE EN EL PRESUPUESTO FINANCIADAS CON FONDOS DEL GOBIERNO DE PANAMA

SECTOR	RENGLON	SUB-TOTAL	TOTAL
EDUCACION			7,533,100
	MINISTERIO DE EDUCACION	6,463,100	
	1. Financiamiento para la construcción de 107 aulas de clases en escuelas rurales del interior del pais.	711,500	
	2. Financiamiento para la construcción de ampliaciones de varias escuelas del pais.	295,000	
	3. Financiamiento para la reparación de escuelas a nivel de todo el pais.	3,686,600	
	4. Financiamiento para la compra de Equipo Educacional (Laboratorios) para varias escuelas del pais.	295,000	
	5. Financiamiento para la Construcción de Mobiliario escolar para las escuelas del pais.	450,000	
	6. Financiamiento para la construcción de un anexo en la Escuela Nautica	300,000	
	7. Financiamiento para Terminación de la Biblioteca Nacional.	625,000	
	8. Financiamiento para construcción del centro Cultural en la ciudad de Santiago	100,000	
	UNIVERSIDAD TECNOLOGICA	500,000	
	9. Financiamiento para la Construcción de un edificio (pabellon) adicional para la Universidad Tecnologica en Tocumen.	500,000	
	UNIVERSIDAD NACIONAL DE PANAMA	570,000	
	10. Financiamiento para la ampliación del edificio de Administraccin Publica en la Universidad de Panamá	370,000	
	11. Financiamiento para la conctrucción del Centro Regional Universitario en la Ciudad de Colón.	200,000	

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SECTOR	RENGLON	SUB-TOTAL	TOTAL
SALUD			
	MINISTERIO DE SALUD	4,130,700	6,219,700
	1. Financiamiento para la Construcción de Acueductos rurales en diferentes partes del pais.	520,200	
	2. Financiamiento para la remodelacion y adicion de Equipamiento al Hospital Santò Tomas/Panamá.	1,030,000	
	3. Financiamiento para la remodelacion y adicion de Equipamiento al Hospital Amador Guerrero/Colón.	1,500,000	
	4. Financiamiento para la remodelacion de quince (15) Hospitales en varias partes del pais.	980,500	
	5. Financiamiento para la Compra de seis (6) Ambulancias para uso en diferentes Hospitales y centros del pais.	100,000	
	DIRECCION METROPOLITANA DE ASEO	2,089,000	
	6. Financiamiento para el saneamiento Ambiental del antiguo Crematorio de Panama Viejo.	1,000,000	
	7. Financiamiento para la compra de Equipo de recolección de basura.	1,089,000	

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SECTOR	RENGLON	SUB-TOTAL	TOTAL
TRANSPORTE			10,986,300
	MINISTERIO DE OBRAS PUBLICAS	10,236,800	
	1. Financiamiento para la reconstrucción de caminos de acceso en areas de produción, mejoras a calles de Centros Urbanos en ciudades secundarias del País.	3,231,800	
	2. Financiamiento para la pavimentación, rehabilitación y mejoras de calles en la ciudad de Panamá y ciudades del interior del pais.	1,375,000	
	3. Rehabilitación del Equipo de mantenimiento del Ministerio de Obras Públicas en todo el país.	1,100,000	
	4. Financiamiento para la construcción de Drenajes Pluviales en la Ciudad de Panamá	930,000	
	5. Financiamiento para la rehabilitación de la carretera Cañitas-Panamá Bayano Santa Fé-Canglón Darién	900,000	
	6. Financiamiento para la rehabilitación del Camino desde la Carretera Pan-Americana hasta Nvo.Guararé Chapala Panamá	50,000	
	7. Financiamiento para la rehabilitación del Camino desde Volcán hasta Río Sereno en Chiriquí.	300,000	
	8. Financiamiento para la rehabilitación del Camino desde Las Tablas hasta Pedasí en Los Santos.	350,000	
	9. Financiamiento para la construcción de la Carretera de Acceso al Nuevo Relleno Sanitario.	2,000,000	
	FERROCARRIL DE PANAMA	749,500	
	1. Financiamiento para la rehabilitación de varias secciones de la vía férrea, rehabilitación de locomotoras, adquisición de equipo y señalización	749,500	

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