ASSESSMENT OF THE PRIVATIZATION PROGRAM OF THE GOVERNMENT

PANAMA

REPORT BY

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EXECUTIVE SUMMARY

A project team consisting of Charles Smith (Arthur Young & Company) and Robert Parra (Public Administration Service) visited Panama from March 16 to April 1, 1986 to evaluate the Government of Panama (GOP) Privatizaton Program. The team was able to identify twenty-eight (28) parastatals, and review the current status of the six targeted for divestiture in the first round of the program.

Four major issues and corresponding recommendations emanated from the visit.

First, the GOP Privatization Program, as it has been implemented thus far, evidences certain deficienies. The most important are that centralized control, planning and coordination are lacking; management processes are not defined clearly; short and long term objectives are unformulated both with reference to the overall program and each parastatal to be divested.

The GOP appointed the Executive Director of the Consejo Nacional de Inversiones as the focal point for all privatization activity in December 1985. Unfortunately, the Consejo's staff is thin and already encharged with all of the GOP's investment promotion activity. It is unlikely that they will be able to handle both functions effectively.

> Project Team Recommendation: that a full time director be appointed to head up the program, supported by a staff of financial and technical analysts from within and without the GOP. The Privatization Task Force should have access to its own independent budget. Because the ultimate divestiture of government assets is controlled by the Ministry of Hacienda, the Director and his staff should report directly to the Minister.

The most realistic way to provide funding for the Privatization Program is by earmarking a portion of AID ESF facilities to commence activities on a firm footing. Perhaps $500,000 would be enough to finance the first six months of operations. Thereafter the GOP, itself, could support the on-going program budget by allocating a percentage of the proceeds derived from each successful privatization. Amounts allocated could be varied depending on forecasted needs.

Second, one of the most significant problems associated with the privatization of any parastatal is the severance payments due to dismissed employees. Dismissal and corresponding severance payments may occur in two distinct situations:

(a) liquidation of a given parastatal that has no ongoing commercial viability, including the closure of its operations, concomitant dismissal of its employees and sale of its assets to private buyers; or

(b) sale of the parastatal as an on-going business to private buyers who are unwilling to assume the laboral indemnities accumulated by the parastatal and who require through a complicated legal procedure the liquidation of the company, including the dismissal of its employees and the payment by the GOP of required laboral indemnities prior to execution of the sale.

The dismissal and severance payment problem is quite different depending upon whether the employees of the parastatal are bound by the Administrative Code or the more onerous, Labor Code.

Project Team Recommendation: that a Panamanian labor relations specialist knowledgeable and experienced with regard to the Panamanian Labor Code be available on retainer to the Privatization Task Force. He should also be familiar with the resolution of labor conflicts associated with sale or liquidation of enterprises and the use of techniques to minimize potential laboral strife in the establishment of new enterprises.

Third, it is realistic to assume that the GOP will resist divesting itself of the four utilities as well as the airport and seaport authorities--since they all contribute significantly to the Central Government's revenue base. There is a widespread perception in Panama that utilities derive their substantial cash flow by charging tariffs to the consuming public that are two to three times higher than those prevalent in other countries. Similarly the prevailing tariff structures of the airport and seaport authorities are deemed more expensive than elsewhere. The high tariffs, and resulting revenue streams from these entities, appear to serve the purpose of cross-subsidizing other parastatals which operate at a deficit. Unfortunately, the high tariffs act as a disincentive to private sector activity, as a whole, and are incongruent with current efforts by the GOP to restructure its economy along more realistic, export oriented lines.

Project Team's Recommendations: that the Privatization Task Force address this issue squarely to determine which of the utilities and authorities could be divested successfully without encountering politically intolerable opposition from vested interests. These should be privatized immediately; the others might be retained by the GOP, with rather extensive reliance placed on the contracting of some their discrete activities to the private sector as a means of inducing operating efficiencies and, eventually, lower tariffs.

Fourth, a major barrier to privatization is the mobilization of needed investment capital and credit to underwrite divestures in Panama, or elsewhere for that matter. In many cases, the purchase price for a given parastatal will be moderately high. At the same time, the new owner will have to invest incremental capital to either reactivate assets and/or induce scale economies in others ways. The new owner may be highly desirable in every way--except that he needs additional equity, complementary to his own, to execute the corporate restructuring.

There is no organized stock exchange in Panama. Although equity capital might be raised through private placements made with individual Panamanian investors, this market is too thin to sustain an extensive divestiture program.

__Project Team's Recommendations__: The Center for Privatization should conduct an exhaustive survey, on and offshore, of sources of equity capital that may be available to support AID-assisted Privatization Programs, general terms regarding the availability of such pools, documentation needed to approach them for timely decisions, etc.

ASSESSMENT OF THE PRIVATIZATION PROGRAM
OF THE GOVERNMENT OF PANAMA

INTRODUCTION

A Project team consisting of Charles Smith (Arthur Young and Company) and Robert Parra (Public Administration Services) reviewed the Government of Panama's (GOP) Privatization Program during the period March 16 - April 2. This review was conducted at the invitation of the Consejo Nacional de Inversiones (CNI); the Agency for International Development (USAID); and the Center for Privatization in Washington, D.C.

The precise purpose of the project team's visit was to:

(1) conduct a review of the background and current status of privatization in Panama, including the political, economic and social constraints that might impede its implementation; and
(2) elaborate a long-term technical assistance plan that would assist the GOP in implementing an optimal strategy to privatize targeted parastatals.

During the visit, the project team was able to:

(1) discuss privatization objectives and attitudes with officials of USAID, CNI, various other GOP ministeries and agencies as well as numerous representatives from the Panamanian private sector (a complete list of the scheduled appointments is attached in Annex I of this report);
(2) assimilate background documents and general information applicable to the Privatization Program including;

- "Panama, Structural Change and Growth Prospects", a World Bank country study prepared in February 1985;
- Public Laws No. 3 and No. 46 which modify the Industrial and Labor Codes, respectively
- Public Law No. 2 which decribes briefly the operating budgets of twenty-eight GOP parastatals. (A complete list of the 28 entities is identified in Annex II);

- USAID Country Development Strategy Statement prepared in 1985;
- an inventory and valuation of the fixed assets belonging to Ingenio de Felipillo as well as a profile of Citricos de Chiriqui, prepared by Management Analysis Center (MAC) of Boston, Massachusetts; and

(3) visit and review with senior management the current condition and opportunities for privatization of the six parastatals which are targeted for the first round of the Privatization Program. These are:
- Air Panama;
- two operating subsidiaries of Contadora de Panama: Contadora Resort and Casino S.A. and Aeroperlas, S.A.;
- a citrus fruit harvesting and concentrate processing plant, Citricos de Chiriqui A.N.;
- two sugar milling subsidiaries of Corporación Azucarera la Victoria: Ingenio de Felipillo (closed since 1982) and Ingenio de las Cabras;
- a shrimp hatchery, the implementation of which never passed the design phase despite the approval by a multilateral institution of a $10MM long-term credit earmarked for this purpose.

(See Annex III which describes briefly each of the above enterprises including their current business focus, products and markets served, financial condition, sale prospects, etc.)

The project team attempted, but was unable, to obtain a copy of the scope, timing and content of the GOP's Privatization Program, which is formalized in the International Monetary Fund's 1985 Standby Agreement and the World Bank's 1986 Structural Adjustment Loan (SAL). Had they been available, these Agreements would have permitted the team to evaluate the program within a much more specific framework including the (i) timetable approved by the GOP for the entire program (ii) scope, including an identification of all parastatals targeted for divestiture (rather than just the first six); and (iii) benchmarks specified in the Agreements against which to evaluate progress and/or success of the program.

The report below is organized in two distinct sections:

First, a diagnostic review of the background, current environment, and status of the Privatization Program;

Second, in the context of the diagnostic review, recommendations for a long-term technical assistance plan which might be provided to the GOP, through the involvement of USAID and the Center for Privatization, that would permit the formulation of an optimal privatization strategy for each parastatal and assist in the implementatioon of several parastatal privatizations.

DIAGNOSIC REVIEW

This section reviews the background, current environment, and status of the Privatization Program.

Background

The 1960s saw rapid economic expansion in Panama, with GDP growth averaging 8% per year. Much of the impetus came from Canal-related activities, and the effects of the Remon - Eisenhower treaties which transferred some economic activities from the Canal Zone to Panama. The principal source of investment finance and entrepreneurial talent was the private sector. Private domestic savings averaged about 15% of GDP, while private investment increased at a real 12.5% rate between 1960 and 1970, rising from 12 to 18% of GDP. Total employment grew at 3.5% per year, well in excess of the 2.5% annual increase in population. Nearly all of the expansion in employment opportunities was provided for by the private sector, and occurred in the urban areas; in the agricultural sector, employment expanded at only .7% per year.

Partly because of the poor performance in agriculture during the 1960s, the benefits of this rapid development were concentrated in relatively few hands. Real wages were held down; the nominal minimum salary remained constant between 1960 and 1968. Acute poverty persisted, mostly in the countryside. Statistics in the most recent "World Development Report" indicate that Panama's income distribution in 1970 was one of the most skewed in the Latin American Region.

The development strategy initiated by the Torrijos Government in 1968 aimed at major social reforms while attempting to sustain growth through increasing and diversifing the level of exports. Greater national integration was achieved by increasing and improving the communications and transport linkages among the regions of the country; social improvements were made by supporting human resources development; and by the strengthening of the country's institutional framework. The strategy was executed through expanded and improved social services, particularly in health and education; through the development of infrastructure by constituting public utilities (electricity, telephones, water) into states enterprises; and by an ambitious public investment program.

Although the strategy of combining rapid growth and social reform was initially successful, the economy during the 1970s was affected adversely by external developments - in particular the oil price hikes and the worldwide recession of the mid 1970s. Domestic uncertainty stemmed mainly from the extended Canal Treaty negotiations, although confidence was also undermined by increased regulation of the economy through a highly restrictive Labor Code as well as the introduction of price and rent controls. Consequently, private investment declined markedly both in absolute and relative terms.

During the 1970s, there were some 112,000 new entrants to the Panamanian labor force. Of these, only 20,400 (18%) found jobs in the private sector; another 17,500 (16%) were officially registered as unemployed. The remaining 74,000 (66%) found their way into direct public sector employment. As a result, between 1970 and 1979, public sector employment expanded at an annual rate of 10% and rose from 13% to 25% of total employment.

This major structural shift in the labor market was brought about in three ways: first by the official encouragement of existing public sector entities, as well as the Central Government, itself, to expand employment beyond immediate needs; second by creating new public entities, particularly in the directly productive sectors; and third, by establishing a special emergency employment program in 1978 which provided 20,000 public sector jobs during the two years of its existence.

Five of the six parastatals which the GOP will attempt to privatize in the first round of the program became public enterprises during the 1970s either as de novo, fledging companies (e.g., Ingenio de Felipillo) or as nationalized concerns following the buy-out of private sector interests (e.g., Contadora de Panama, Citricos de Chiriqui, Ingenio de Las Cabras and Air Panama). As a rule the latter nationalizations occurred in firms whose private sector owners had announced an intention to close operations due to lack of profitability. The objective of the GOP was to salvage the employment opportunities offered by these firms.

Despite additional revenue measures, the public sector expansion (and by implication the GOP's employment policy) resulted in a sharp increase in the public sector deficit. Since Panama has a dollar economy and the government does not control its own money supply, the size of the public sector deficit has been determined historically by the availability of foreign financing. Panama was considered very creditworthy by the international banking community during the 1970s. Its access to foreign commercial credit was such that it was able to finance most of the programs initiated by Torrijos. By 1980, the outstanding and disbursed public sector debt equalled approximately 70% of GDP. Nearly three-quarters of that debt was owed to commercial lenders payable over short time frames at record-high interest rates.

Obviously, the expansion of the previous decade could not continue. Thus, for budgetary reasons, the public sector's role as the employer of last resort declined markedly after 1980. Between 1979 and 1982, some 8500 new jobs were created by the public sector, half the annual rate of the previous decade. Partial evidence suggests that some of the public sector entities (e.g., Social Security Agency; the power and water authorities IRHE and IDAAN; as well as the port Authority) have continued to expand employment in recent years, despite an excess of labor. Notwithstanding, progress has been made in other areas. The GOP is 1983 sold a major unprofitable hotel; ended a contractual arrangement of market sharing and cross subsidization involving a state owned cement plant; initiated a major restructuring of the development finance corporation, COFINA; closed Ingenio de Felipillo, the least efficient of the four sugar mills owned by Corporación Azucarera La Victoria; eliminated state subsidies to Citricos de Chiriqui; and began financial and managerial reforms at the national airlines, Air Panma.

According to recent statistics, the officially estimated unemployement is now around 10% nationwide and 14% in the Panama City/Colon Metropolitan Area. It is projected by various sources, that Panama needs to grow by 7.5% from 1985 onwards merely to avoid a further rise in unemployment. With a slower rate of growth say 1-2% per annum, unemployment could reach 100,000 toward the end of this decade.

Current Environment

There seems to be a consensus, among the private and public officials interviewed, that the broad aims of government policy should be to encourage job creation through privately owned, export oriented enterprises and that changes are needed in public policy to accomplish this goal. All, including public sector officials, seem to be in favor of reducing the role of government in the economy. Thus, the Privatization Program seems to have broad support. However, many Panamanian businessmen are apprehensive of other impending changes in public policy which will significantly affect the "rules of the game" for some businesses.

The project team's visit coincided with certain legislative bills, that were being debated and/or subsequently approved in session, which modify the existing Labor, Industrial and Agroindustrial Codes. Although these modifications do not appear to have a significant and direct impact on the Privatization Program, itself, they do appear to exert strong potential influences on the role of the private sector in the future, particularly as a generator of foreign exchange and employment. Both the modifications to the Labor and Industrial Codes are summarized below. (When this report was being drafted the changes in the Agroindustrial Code had not been approved fully by the legislature and, therefore, were unavailable for review).

<u>Labor Code</u> The major modifications to the Code appear in seven areas. It should be noted that the principal beneficiaries are employers (vs. employees) - particularly farms, exporters and small businesses. Changes include:

- an expanded definition of "small businesses" and, for such firms, more flexibility in dismissing employees and other favorable changes which include the obligaton to work overtime and reduced worker entitlements in respect of compensation for overtime;

- a reduction of farm worker's entitlements as they relate to compensation for overtime and holiday work;

- for export-oriented firms, that export all of their production, a reduction in worker entitlements as they relate to compensation for overtime;

- a new definition of "salary" which allows a greater flexibility to fix and adjust salary for piecework, commissions, supplementary bonuses or productivity incentives. (Previously, such payments gave rise to vested rights and downward adjustments or annulments thereof violated worker's rights. As such, they increased the cost of employment benefits);

- elimination of age as a criterion for the payment of one type of severance benefit based on seniority, payable in the event of dismissal or resignation of the employee. Employees with ten or more years of service are now entitled to this "Prima de Antiguedad" (Seniority Premium) at the termination of their employment;

- increase in the probationary period of new employees, from 2 weeks to 90 days; and

- deregulation in the use of labor work in homes.

The Code's other provisions concerning dismissal of employees remain unchanged. Severance payment, on a sharply increasing scale according to years of service, is due to any employee dismissed without a justifiable cause. Workers of small businesses may be dismissed without cause after their probationary period through the payment of one month's salary in lieu of notice plus the corresponding severance pay. Medium and large enterprises must invoke a justifiable cause for dismissal, or reach an amicable agreement with the worker, or face payment of the severance pay with a 50% surcharge plus full salary from the date of termination to the date of the verdict if the court rules the dismissal unjustified. Rulings appealed by the workers or the employee do not accrue additional liabilities while the sentence is reviewed by a superior court.

The severance pay takes into account base wages and overtime. The seniority premium, payable in all cases at termination of employment, takes into account base wages, overtime wages, vacation pay, commission, and other employment-related benefits except profit sharing, donations and payments for the XIII Month. These provisions, virtually unaffected by the approved modifications to the Labor Code are further discussed in the section entitled "Status of the Privatization Program".

Industrial Code Approved modifications to the Industrial Code, also, signficantly favor export oriented industries. Major changes are as follows:

- for export oriented firm (i) continued and indefinite exoneration of corporate income and other taxes as well as (ii) new procedures for handling imported raw materials and other production inputs, which essentially reduce paperwork and, therefore, processing time needed by customs for such goods;

- for firms which process products for the domestic markets, limitations placed on exonerations from corporate taxes, duties on imported capital equipment and/or production inputs;

- for firms located in officially designated "development zones", less beneficial exonerations (than previously) on corporate and property taxes, as well as duties on imported capital equipment and/or production inputs;

- general encouragement of export activity by the GOP's funding of a new program at the Panamanian Institute of Foreign Commerce to identify new exports of products for which Panama has a comparative advantage; attracting appropriate technology proprietors from abroad to process such products through various commercial mechanisms; establishing offices overseas to promote such activities, etc.;

- reduction of protective tariffs over a five year period for those imports which compete with locally produced goods, such that at the end of this period, no tariff will be set at more than 60% of the c.i.f. value of the competing import. Similar provisions exist for new products of all types never before produced in Panama and certain currently produced agroindustrial products except that the maximum protective tariffs at the end of five years are 20% and 90%, respectively.

As indicated previously, the above modifying legislation does not seem to have much direct impact on the Privatization Program, per se. New public policies may have, however, indirect impact--some of which are discussed in the next section.

According to Public Law No. 2, there are at least twenty-eight (28) GOP parastatals whose operating budgets are subject to legislative review. (As a practical matter, the GOP owns more parastatals than those outlined below, the Panama Hilton being a rather prominant omission from the list). Of the twenty-eight (28) government owned enterprises, eight (8) are banks, most of which are engaged in development activities; twenty (20), are corporate enterprises or operate as such.

As a group, the eight financial institutions are expected to mobilize over B/. 420MM in funds during the course of the current year. As anticipated in Public Law No. 2, the bulk of these resources, approximately 85% would be derived from loan recoveries, interest, fees, special taxes and/or incremental deposits. The balance 15% is to come from either (a) external credits sourced largely from multilateral or bilateral entities (B/. 45,429,900 or 13.5% of the total) or (b) internal transfers <u>from</u> the Central Government (B/. 7,513,800 or 1.5%). With regard to the latter item, Public Law No. 2 envisages transfers (during the course of the current year) from the eight financial intermediaries <u>to</u> the Central Government of B/. 3,612,720 or approximately half the amount obligated inversely.

The four largest financial intermediaries are:

Banco de Desarrollo Agropecuario (agriculture)
Banco Hipotecario Nacional (mortgages)
Banco Nacional de Panama (roughly equivalent to a central bank but with commercial operations)
Caja de Ahorros (savings institutions)

It is difficult to determine how efficiently run these organizations are on the basis of the information available. There is no way of knowing, for example, the quality of their portfolios and, in particular, their ability to generate cash on a timely basis from loans outstanding.

Nonetheless, the four financial intermediaries are expected to mobilize B/. 410MM, or 90% of all government controlled financial intermediation activity, including all of the external credit to be drawn from multilateral and bilateral agencies and institutions.

The other twenty (20) corporate parastatals are involved in a variety of activities, including:

(a) legalized gaming e.g.,

- Loterial Nacional de Beneficencia
- Casinos Nacionales
- Hipodromo Presidente Ramon
- Bingos Nacionales

(b) utility services e.g.,

- Dirección Metropolitana de Aseo (solid waste removal)
- IDAAN (water)
- INTEL (communications)
- IRHE (power)

(c) transportation and support e.g.,

- Air Panama
- Ferrocarril de Panama
- Ferrocarril de Chiriqui
- Dirección Aeronautica Civil
- Autoridad Portuaria Nacional

(d) tourism e.g.,

- Contadora de Panama

(e) agroindustry, e.g.,

- Corporación Azucarera La Victoria
- Citricos de Chiriqui
- Empresa Nacional de Maquinaria Agricola
- Empresa Nacional de Semillas
- Instituto de Mercadeo Agropecuario

Public Law No. 2 anticipates that the group of twenty enterprises will generate in excess of B/. 850MM in financial resources from normal operations. The operating costs of this group are forecast to require B/. 460MM, or roughly 54% of total cash available. The balance net operating cash flow (available for debt service, non-recurring charges, capital investment, transfers to Central Government, etc.) is around B/. 390Mm, with five parastatals accounting for B/. 340MM (86%) of the global amount as is shown below:

IHRE	B/. 203,562,731
INTEL	B/. 46,382,000
Loteria Nacional	B/. 46,012,000
IDAAN	B/. 31,981,260
Casinos Nacional	B/. 10,699,000

As can be seen, the gaming and utility enterprises figure heavily in the total net operating cash flow generation of the twenty enterprises. One of these enterprises falls out when one addresses transfers to the Central Government. Anticipated transfers from the group of twenty to the Central Government are on the order of B/. 85,506,100, roughly 10% and 24%, respectively of total cash generation and net operating cash flow as these magnitudes are outlined in Public Law No. 2. Seven parastatals account for B/. 78,325,000 in transfers to the Central Government, or 91% of total transfers as shown below.

Loteria Nacional	B/. 46,632,000
Casinos Nacionales	B/. 10,699,000
IRHE	B/. 8,423,000
Air Panama	B/. 5,045,000
INTEL	B/. 3,600,000
Dirección de Aeronautico	B/. 2,509,000
Hipodromo	B/. 2,417,000

Of the above seven, three are gaming enterprises; two are utilities; one is the airport authority; and one, Air Panama, is among the parastatals which are to be privatized in the first round. (Incidently, Air Panama's favorable forecast may result from their current plans to purchase a new airbus, thereby leading to higher potential revenues, as also from the expectation that fuel prices may remain lower during the current year).

Some preliminary conclusions can be drawn from the above brief survey:

(1)the intrusion of the state into the productive economy, during the 1970's was not as widespread as was the case for several other latin countries e.g., Brazil, Mexico, Venezuela, Honduras to cite a few;

(2) investment in agroindustrial enterprises may have been prompted by the lack of sophistication and/or experience of the domestic private sector in this particular area. A similar motivation may have prompted public investment in the tourist complex, Contadora de Panama. Both proved to be mistaken;

(3) it is realistic to assume that the GOP will resist divesting the four gaming entities; the four utilities; and the airport and seaport authorities -- since they all contribute significantly to the Central Government's revenue base. However, higher operating efficiencies could be achieved by contracting selected activities to private sector entities;

(4) there is a widespread perception in Panama that the utilities derive their substantial cash flow by charging rates that are two to three times higher than those prevalent in other countries. Similarly, the prevailing tariff structure of the airport and seaport authorities are deemed to be higher than elsewhere. It would appear that the utility revenues are used to cross-subsidize the operating deficits of other parastatals. Affordable infrastructure services are a cornerstone of successful development policies. The long-term interests of Panama are better served by lower tariffs for infrastucture services. This could be accomplished by an overall privatization strategy which envisages outright divestiture of some utilities and authorities or, in the case of others, retention of ownership by the GOP, with rather extensive reliance placed on the contracting out of their principal activities as a means of inducing operating efficiencies. Should the GOP decide to divest these entities a public regulatory agency would have to be formed;

(5) every effort should be made to privatize all of the agroindustrial enterprises in a manner which optimizes foreign exchange generation and job creation potential, and in a manner which is consistent with other public sector policies e.g., the new Industrial Code.

Status of the Privatization Program

Various analyses of the current economic situation in Panama comment on activities intended to achieve the privatization of some Panamanian parastatals. As a rule the activities cited have ocurred in order to comply with conditions linked to the World Bank/IMF Structural Adjustment Loan (SAL). In this section the Panamanian Privatization Program is described from the following four perspectives:

- Activities to date
- Current Program
- Problems and Barriers
- Potential Privatization Approaches

Activities to Date

Although no structured Privatization Program is yet in place, several activities leading to the divestiture of parastatals have occurred. It appears that the first such activity occurred in 1983 when COFINA sold an unprofitable, mismanaged hotel to a Japanese investor group. This is a significant achievement and a good foundation from which to launch the Panamanian Privatization Program. This hotel, with sound private sector management, has been converted into a successful, profitable hotel now considered the best in Panama. It is the only hotel now paying taxes to the government.

Another privatization activity that is currently in progress is the offering for sale of two companies belonging to Contadora de Panama S.A.: Contadora Resort and Casino and Aeroperlas. For both divestitures, IPAT undertook to identify and resolve legal barriers as well as to prepare and distribute a sales prospectus. Although the prospectus lacks much of the information that a prospective buyer should know (under the full disclosure concept) the IPAT effort is well organized and will ultimately achieve the divestiture. They have received at least one bid for each parastatal.

On another front, the Ministerio de Desarrollo Agropecuario (MIDA) has contracted the Management Analysis Center (MAC) to advise them on divestiture options for various agribusiness parastatals. Among the results of this effort is the preparation of asset valuation reports for Ingenio de Felipillo and Citricos de Chiriqui. Both reports provide basic information on these parastatals but fall short of discussing privatization options or the problems associated with privatization of these parastatals.

The significant fact associated with these two cases is that they appear to be independent efforts that are not coordinated centrally and do not follow a uniform and systematic approach. Each is responding to a need, perhaps arising from the SAL conditions, but is not administered under a set of approved guidelines that define objectives, priorities and approaches.

Current Program

Based upon the project team's limited review, it appears that the Panamanian Privatization Program lacks a coordinated approach, centralized planning and control of those privatization activities that are occurring. Recognizing the need for such, the President of Panama assigned, in December 1985, these responsibilities to the Director of the Consejo Nacional de Inversiones (CNI), which is the Panamanian goverment organization primarily responsible for developing a foreign investment promotion program. While the attraction of foreign investment and technology will be an important factor in the overall privatization effort, privatization implementation requires a much broader range of activities and skills. It is very important that the Privatization Program have a full-time Director who possesses significant political influence as well as a staff of financial and technical analysts.

Because the ultimate divestiture of government assets is controlled by the Ministry of Hacienda, the Director of Privatization and his staff should report directly to the Minister of Hacienda.

The current status of the Privatization Program can perhaps best be described by certain significant deficiencies. A major motivation for privatization in Panama has been the SAL agreement that not only requires privatization but also specifies a schedule for achieving the privatization of six parastatals. A copy of the SAL agreement was not available at CNI during the two week visit. This document is considered to be vital for the administration of the Panamanian Privatization Program, because it defines the commitment made by the GOP to the World Bank/IMF.

To date no list has been developed identifying all of the Panamanian parastatals. Such a list was requested, along with a brief description of each parastatal, but the information was not available and apparently not easily compiled. The project team was informed that a recent World Bank study of Panamanian parastatals contains much of this information, but the report was not readily available. On the basis of information contained in Public Law No. 2, a list has been compiled of twenty-eight parastatals (see Annex II). However, it is believed this list is incomplete.

Without basic information such as the SAL agreement and the list of parastatals it is very difficult to develop a coordinated operating program defining the activities and priorities of the Government of Panama. Without such coordination, the privatization activities will tend to respond only to the conditions proposed by multilateral agencies such as the World Bank Group. This is because the Government has no alternative program to offer that would achieve similar results but in a priority sequence perhaps more in concert with the needs of Panama.

The privatization activities that are currently in progress are not coordinated by any centralized group nor guided by any standard procedures for privatization. All those officials who are actively involved in the current privatization activities, especially those in IPAT, demonstrate that they have thought out some of the problems related to divestiture of parastatals but none has formulated in advance the full process. Each has resolved problems on an "as you go" basis. Few have thought out the entire process which, among other activities includes:

- identification of all parastatals and the determination of the priority of each vis-a-vis the implementation of privatization;

- determination of an appropriate privatization strategy including:
  - liquidation
  - divestiture, in part or whole
  - retention with contracting of specific activities

- valuation of the parastatals on a going concern and accounting basis including hidden assets and liabilities (i.e. labor indemnities);

- identification of potential problems and barriers including:
  - labor problems
  - market potential
  - appropriateness of technology

- determination of investment requirements;

- identification of sources of financing including the use of licensing and contracting arrangements and the placement of equity with active or passive investors;

- preparation of an offering prospectus and identification of potential purchasers or investors;

- review of proposals, negotiation and finalization of the privatization agreements.

The lack of an overall process formulated in advance and applied uniformly to all parastatals may lead to less than optimum privatization strategies and could result in future difficulties for the Privatization Program. For example, the sale of the Contadora Resort may result in one value if sold as a resort for middle to upper Latin Americans, and quite another value, if sold as an exclusive health maintenance facility for wealthy individuals from around the world. An additional problem is that the officials managing the divestiture of Contadora have prepared a sales prospectus without the benefit of guidelines for its contents. The prospectus that has been prepared falls short of full disclosure in that significant problems are not fully described. One could say "let the buyer beware" but experience has shown that such omissions frequently lead to future legal problems.

As part of the current Privatization Program, an effort is being made to sell Ingenio de Felipillo, a sugar mill that has not been operated for three years, and Ingenio de Las Cabras, a mill that is currently operating with one hundred (plus) year old technology. The privatization effort for these mills is considering alternative technologies such as ethanol. However, the recent decline in oil prices could reduce international demand for ethanol. Domestic demand for ethanol is in doubt wihtout a coordinated national blended gasoline program. The government is also considering the development of an ethanol facility at Ingenio de Alanje. If Felipillo and Las Cabras are divested for ethanol production while the GOP also produces ethanol at Alanje, the domestic market could be over-supplied thereby injuring the viability of all three ingenios. Alternatives that could be considered include cane energy; conversion of cane to fructose; or the sale of the assets for removal from Panama and the subsequent conversion of the land to products other than cane.

All of this points out a flaw in the current approach to Felipillo and Las Cabras. That is, that they are owned by the Corporación Azucarera La Victoria (CALV) which also owns Ingenio de Alanje and Ingenio de La Victoriaa. The privatization analysis should look at CALV as a whole and identify the best strategy for the entire parastatal. That strategy may or may not break up CALV in the way that is now under consideration. Certainly a coordinated approach to CALV would increase the probability of success for the privatization of any of its parts.

The current privatization activity for the other parastatals that have been reviewed demonstrates similar problems resulting from the lack of a uniform approach and centralized control. In the case of Citricos de Chiriqui there is a need for review of alternative products and markets that would reduce its dependence on orange concentrate. Air Panama has extensive hidden assets in its unused route structure as well as at least double the number of employees necessary for efficient operation. (Note that overstaffing is a characteristic of most of the parastatals and could be a severe problem depending upon whether the employees are governed by the Labor Code or the Administration Code.) The shrimp laboratory is not actually a parastatal in that the project has never been implemented. The objectives of the Government of Panama in this case are to privatize the plans for the laboratory so that a private sector firm would implement the project. The planning phase of the project was originally financed by a multilateral insititution.

To summarize the current Privatization Program, there is a lack of planning and centralized coordination and control. No procedures have been developed that define the entire process nor has it been systematically formalized. Consequently, several goverment agencies are actively pursuing privatization activities, each in its own way and each in response to external pressures such as the World Bank SAL agreement.

Problems and Barriers

There are several significant problems and barriers that a successful Privatization Program will have to overcome. The most serious is the lack of a Panamanian Privatization Policy and systematic approach. This has been extensively discussed in the previous section where the current program has been reviewed. Such a policy should clearly define the following issues:

- Panama's goals and objectives;
- priority sequence for evaluation and/or implementation of a privatization strategy for all parastatals;
- uniform process and procedures for the analysis and implementation of all privatization activity;
- centralized coordination and control of all privatization activities.

The first priority of the Privatization Assistance Plan should be to define each of the policy issues and to obtain approval of an official Panamanian Privatization Policy.

One of the most significant problems associated with the privatization of any parastatals is the liquidation of excess personnel. The problem is quite different depending upon whether the empoyees are governed by the Labor Code or the Administrative Code. The applicable codes for the parastatals reviewed are:

- Contadora/Aero Perlas - Labor Code
- Air Panama - Labor Code
- Citricos de Chiriqui - Labor Code
- CALV - Administrative Code
- Shrimp Laboratory - No employees

In the case of employees covered by the Administration Code the problem is not complex. Each employee can be dismissed, without regard to seniority, with payment for their accumulated vacation. In this way, a new owner has the opportunity to restructure the employment relatively easily. For employees covered by the Labor Code, the situation is very difficult. Employees can only be dismissed in order of seniority and the severance payments can be extensive. In most cases, no Panamanian private sector enterprise would be willing to acquire a parastatal unless all employees are dismissed and the severance paid by the government. As an example of its potential magnitude, the project team calculated the severance for an employee who started work in May 1968 and was dismissed in March 1986. The employee would be entitled to forty-nine weeks of severance pay - essentially valued at his average monthly salary plus overtime for the last six months or the last thirty days (whichever is greater) - plus a seniority premium (Prima de Antiguedad) amounting to seventeen additional weeks of salary calculated on the average total earnings of the previous five years. The severance pay could actually increase by as much as 50% if the employee contests the dismissal in court. As a very rough estimate, the total cost of the laboral indemnities for a parastatal like Air Panama could amount to several million Balboas in the event the labor force were dismissed. Typically, this liquidation must be achieved through a bankruptcy/foreclosure process with the new owners establishing a new enterprise that would acquire the assets and rehire some of the employees of the parastatal.

Many of the parastatals that are to be privatized are producing products for which the demand has declined significantly. In some cases (such as Felipillo), they have ceased operations due to lack of demand for their products. For these parastatals, the prospect for a successful privatization effort will be enhanced by a demand analysis of a variety of products and markets that are compatible with the equipment and resources of the parastatals. By identifying alternative products and markerts it might be possible to evaluate the feasibility of using alternative technologies to increase the commercial viability of the parastatals and thereby improve the negotiating position of the Government of Panama in the Privatization effort. Of the parastatals that we reviewed, this type of technology audit would be important in Contadora, the Ingenio de Felipillo, Ingenio de Las Cabras and Citricos de Chiriqui.

One of the barriers to privatization will be the ability of investment capital and credit to finance the divestiture. In most cases the purchase price for the parastatal will be moderately high and the new owner will, at the same time, also have to invest new capital in order to improve the facilities sufficiently to enable the enterprise to be commercially available. For example, for Contadora the purchase price of the enterprise is estimated to be in the range of B/. 6.5 million with a requirement to invest an additional B/. 2 million in improvements. On the other hand, Ingenio de Felipillo could be sold for perhaps B/. 8 million but may require an additional B/. 17 million in new investment to reactivate idle land and establish an ethanol plant. These figures would indicate that the entire Privatization Program will require an extensive amount of capital, perhaps as much as B/. 500 million depending, on how many parastatals are included.

Unfortunately, there is no organized stock exchange in Panama, and it appears that it may be difficult and expensive to create one. Although equity capital could be raised through private placements to individual Panamanian investors, this methodology has not been a source for large issues. For example, from June 1983 to June 1984 only B/. 21.3 million of equity was raised in this manner. In some exceptional cases it may be possible to consider issuing stock in foreign stock exchanges. However this alternative could require the parastatals to meet the requirements of the foreign regulatory agencies (i.e., the Securities and Exchange Commission in the U.S.).

Bank credit may be another option. There are approximately 130 different foreign and domestic banks operating in Panama with a loan portfolio of B/ 4.2 billion (September 1984). These could be the source of long-term bond and debt financing. Various development banks could be good sources of financing under terms similar to venture capital firms. Panamanian banks such as DISA or the new Export Development Bank may be in a position to provide both equity and credit financing. Another source of potential financial could be the International Finance Corporation (IFC), a member of the World Bank Group, which provides both equity capital and credit to private sector firms in developing countries. The Interamerican Investment Corporation is currently being established with a mandate similar to the IFC. Once established this will be a good source of equity and credit financing. In some cases, it may be feasible to covert existing commercial credit owned by the parastatal into equity capital of the new private enterprise. As an option of last resort, the Government of Panama may have to extend credit to the purchasers of the parastatals in order to facilitate the financing of the divestitures. They could be done through a form of long-term bond, or possibly a licensing/royalty agreement that would tie payments to the level of sales of the enterprise.

One of the significant barriers to private sector development in Panama is the high cost of utility services, expecially electric power. To the extent that there is now an economic restructuring of Panama, including the opening of the economy to import competition and encouraging the development of export industries, it is important that the cost of utilities be internationally competitive. Unaffordable utility services are a disincentive to private sector activity, generally. The privatization program could play an important role in helping to bring down these rates. The privatization of the utilities, especially IRHE and IDAAN, could enable private sector management to increase efficiencies and thereby, reduce the rates charged for their services. If not candidates for complete privatization these utilities should be reviewed to identify options for engendering efficiencies by contracting out of discrete activities to the private sector.

Potential Privatization Approaches

Several approaches to privatization have been developed and used in various parts of the world. Perhaps the most famous is the sale of equity shares of British Telecom and British Air through the London stock exchange. Another interesting approach was the sale of revenue sharing bonds for the Bosphorous (toll) Bridge in Turkey (the bonds sold out in one hour). The fact that these and other methods have been successful in other countries does not imply that they are applicable in Panama. In this section we will briefly discuss some of the approaches that may be applicable in this country.

Considering the lack of an organized equity market in Panama, and the fact that in most cases it will be necesary to liquidate the work force of the parastatals, it is likely that many might be sold to joint ventures consisting of a mix of Panamanian or foreign active and passive investors. Another option is the sale of certain parastatals to individuals capable of operating them, and supported by large institutional investors (insurance companies, pension funds, etc.) who will have purchased through private placements large blocks of shares. (We understand, however, that pension funds in Panama have traditionally not been a significant source of investment funds). As a rule the successful placement of equity or debt/equity instruments would require that the new owner of a divested parastatal have in place an established cadre of proven professional managers. This may not be easily achieved if the parastatal must liquidate all employees in order to facilitate its privatization. For those parastatals that are not deemed to be candidates for divestiture, the contracting out privatization approach will be a very attractive option. This will enable certain types of activities currently performed within the parastatals to be provided on a contractual arrangement from the private sector. In this way some private sector efficiencies will be obtainable even within the parastatals not divested.

Another approach that has gained popularity in the United States and Europe is the employee stock ownership plan (ESOP). In the ESOP approach a parastatal would be sold to its employees through a leveraged buy-out. However, in order for this to work well the parastatal must have efficient staffing with a cooperative relationship between employees and management. The ESOP approach puts the employees in an ownership position and gives them a strong voice in the management of the enterprise. Every labor relations specialist in Panama with whom the project team has discussed this approach has categorically stated that the status of labor/management relations is not yet ready to experiment with employee ownership. Consequently, it is not believed that ESOP's are a viable option for privatization in Panama.

In this section of the report, privatization achievements in Panama as well as the status of the current program have been discussed. Problems, barriers and potential approaches that may be successful in Panama were also presented.

Basically, there are some significant problems to overcome in the privatization of Panamanian parastatals especially related to the questions of excess labor and financing of divestitures. There is a great potential for success if Panama develops a well thought out, prioritized privatiation plan that provides a uniform process as well as centralized coordination and control of the implementation of the Privatization Program.

In the next section, the project team presents their recommendations for a Privatization Assistance Plan. The plan includes a description of the required activities as well as a dicussion of the project schedule and staffing requirements.

PRIVATIZATION ASSISTANCE PLAN

CENTER FOR PRIVATIZATION

MAY 1986

PRIVATIZATION ASSISTANCE PLAN

To successfully implement a coordinated Privatization Program in Panama, it is necessary first to organize a Privatization Task Force within the Ministry of Hacienda. The Task Force should have it's own independent operating budget and would consist of a politically appointed Director of Privatization reporting directly to the Minister, and four full-time staff analysts. The Director and his staff would have access to outside privatization specialists, labor advisors and external auditors.

All of the participants in the Task Force should recognize clearly from the onset that the Privatization Program is likely to be a slow and often frustrating process. Because the opportunities, problems and approaches will differ for each parastatal, the members of the Task Force should be both creative and flexible.

The Task Force would provide the central planning and direction needed to facilitate the success of the Privatization Program. It would coordinate the activities of all GOP Ministries and Agencies involved in the Privatization Program. The Task Force would be the principal GOP interface with the outside investment public as well as banks and other financial service entities which would support the Privatization Program through the provision of project finance.

The following are among the important elements of the central planning and direction to be provided by the Task Force:

-- development of a complete list of parastatals, assessing for each the political, economic and social advantages and disadvantages of privatization and recommending to the Minister of Hacienda the priority order and strategy for their privatization;

-- elaboration of very clear GOP objectives for the overall program as well as for the individual parastatals to be privatized;

-- identification of the political ramifications relevant to each entity to be privatized as well as the contending power bases and/or sources of influence, and the development of a specific strategy to deal with opposition groups;

-- development of a variety of options for privatizing the more politically sensitive parastatals;

-- provision of technical assistance, as required, in evaluating the parastatals (on a going concern, accounting and/or alternative use basis);

-- review of all financing mechanisms inside and outside Panama that might be employed to raise debt and equity capital and, for each, preparing a profile that describes the benefits and difficulties of their use;

-- execution of the overall Privatization Programm, including the management of processes required to privatize each parastatal.

From a methological perspective, the Task Force would manage the entire Privatization Program in two clearly defined stages each each consisting of specific activities. The first stage would have the objective of establishing the appropriate privatization approach for Panama and successfully selling some of the initially targeted parastatals. The above mentioned elements of central planning and direction would be the key activities of the first stage. In addition, the successful privatization of some of the initially targeted parastatals would generate considerable momentum for the overall Privatization Program.

The initially target parastatals that have attracted (or could attract) strong buyer interest include Air Panama, Contadora Resort and Casino, Aeroperlas and Citricos de Chiriqui. It is believed that two of these entities -- Contadora Resort and Casino and Aeroperlas -- could be sold within the next two months without creating the Task Force. The sale of the other two, however, would require the creation of the proposed Task Force if the entities are to be sold relatively quickly.

The implementation the first stage as described above, would provide the foundation for a successful second stage. This foundation would consist of a special study addressing the political, economic and social advantages and disadvantages of privatizing all other remaining parastatals, the options available, as well as several other subsidiary issues. Properly done, this analysis could result in a well defined series of action plans which would be the underpinning for the second stage of the Privatization Program. The following are representative examples of conclusions and their corresponding action plans:

Examples of Conclusions	Action Required
-- certain parastatals should be liquidated immediately e.g., Empresa National de Maquinaria Agricola; perhaps Instituto de Mercadeo Agropecuario;	Auction off equipment and other assets.
-- the operating efficiencies of other parastatals are best improved by contracting their overall management and/or certain discrete activities to qualified private sector groups e.g., IRHE, IDAAN, INTEL, the airport and seaport authorities;	Elaborate and execute contracting out plan.
-- some parastatals may be divested by GOP with a minimal analysis of their operations;	Establish general management processes and assemble project team needed to manage each divestiture.
-- other parastatals need considerable rationalization before they are divested e.g., Corporacion Azucarera La Victoria and its four sugar processing subsidiaries;	Organize a special Task Force to deal with rationalization issues precedent to implementation of divestiture strategy.

The second stage of the Privatization Program has the objective of privatizing the remaining parastatals. This stage contains three activities; each corresponding to a different privatization approach: divestiture, contracting, or liquidation. The activities define a series of tasks necessary to achieve the privatization of a parastatal by the specified approach.

During this stage teams of analysts from the Privatization Task Force, including external privatization, labor and audit advisors, would be assigned to each parastatal. Using a modified decision tree approach, the team would implement the required activity (either divestiture, contracting or liquidation) depending upon which approach had, during the first stage been identified as the most appropriate. The teams would perform all tasks required for the privatization including valuations, marketing, investor negotiations and the finalization of agreements. These teams would work through all of the parastatals in accordance with the priority order established during the first stage.

The following is a detailed description of the specific activities and tasks that would be necessary to successfully implement the Panamanian Privatization Program.

DESCRIPTION OF ACTIVITIES

STAGE ONE

ACTIVITY 1 PROJECT INITIATION AND MANAGEMENT

Objective: To establish the project team, organize a Privatization Task Force in the Ministry of Hacienda, formalize the goals and objectives of the Privatization Program and manage all privatization activities.

(The Task Force consists of a politically appointed Director of Privatization reporting directly to the Minister of Hacienda, and four full-time staff analysts. The Director and his staff would have access to outside consultants e.g., labor specialists such as Walter Durling, external auditors such as Arthur Young and Company, and other advisors from the Center for Privatization).

Specific Activities:

- Establish the Privatization Task Force and appoint its Director and staff

- Mobilize the outside consultants including the expatriate privatization advisors, Panamanian labor advisor and external auditors

- Obtain agreement between the members of the Task Force, outside consultants and senior officials of the GOP on the goals and objectives of the Privatization Program

- Finalize the Program workplan and develop a uniform approach for all privatization activities

- Provide centralized direction and control for all privatization activities throughout the full period of the Privatization Program

- Prepare the methodology and benchmarks against which the success of the Privatization Program may be assessed

- Evaluate the program at predetermined intervals and prepare progress reports.

ACTIVITY 2 PRIVATIZATION PLANNING

Objective: To identify all parastatals as well as other business type activities owned and operated by the GOP, determine the appropriate privatization strategy for each and identify the priority order for this privatization.

Specific Activities:

- Identify all Panamanian parastatals as well as other business type activities owned and operated by the GOP. Possible sources for this information include:
  - Law # 2 National Budget of Panama
  - Specific budgets for the following Ministries or Agencies:
    - MICI
    - MIDA
    - IPAT
    - Others to be identified.

- Establish criteria to be used in determining the priority order for the privatization of identified parastatals. Such criteria may include, among others:
  - Commercial viability and potential profitability of the parastatal
  - Demonstrated investor interest
  - Relative ease of privatization

- Potential for successful privatization in terms of económic and social impact.

- Develop a preliminary profile for each parastatal covering basic information on the following:
  - Line of business
  - Financial condition and value
  - Personnel (number of employees and legal status).

- Develop a preliminary estimate as to the appropriate privatization strategy for each parastatal:
  - Divestiture (whole or part)
  - Contracting of specific activities
  - Liquidation.

- Evaluate each parastatal on the basis of the prioritization criteria and develop a list of parastatals in priority order for privatization

- Review all financing mechanisms inside and outside Panama that might be employed to raise debt and equity capital and prepare a profile of each that describes the terms as well as the benefits and difficulties of their use

- Evaluate the economic, financial, and social impact of the Privatization Program

- Develop a plan that specifies the priority disposition of the funds received as a result of the privatization of parastatals. The plan must take into consideration any legal requirements and in addition should provide for payment of the following:
  - Labor indemnities
  - A contribution toward the operating costs of the Privatization Program (this may require a modification of Panamanian Law)
  - Retirement of the official debt associated with the parastatal.

- Develop and conduct a public awareness program to describe the benefits of the privatization effort.

ACTIVITY 3 PRIVATIZATION OF INITIAL PARASTATALS

Objective: To finalize the privatization of the initially targeted parastatals including Contadora de Panama S.A., Air Panama, Citricos de Chiriqui and the Shrimp Laboratory.

Specific Activities:

- For Contadora de Panama S.A., review the proposals already received for the purchase of Contadora Resort and Casino S.A. and for Aero Perlas S.A. and assist IPAT to finalize the negotiations with potential investor groups

- For Air Panama and Citricos de Chiriqui, perform the activities described for processing divestitures (Activity 4)

- For the Shrimp Laboratory, evaluate the status of the project and determine whether any implementation has begun. If, as is now believed, the project is only in the design phase, make contact with various acquaculture firms to determine their interest in acquiring the plans. If there is interest, develop and issue a request for proposal, evaluate the proposals and negotiate the sale. If no interest is identified, liquidate the project.

STAGE TWO

ACTIVITY 4 DIVESTITURE PROCESS

The divestiture process will be followed for each of the parastatals for which divestiture was determined to be the the most appropriate privatization strategy. The following tasks are required for divestiture:

TASK 4-1 ENTERPRISE PROFILE

Objective: To perform a detailed analysis of the parastatal in order to determine the line of business, financial and physical conditions of the enterprise as well as the problems and barriers to privatization. If necessary, an analysis of alternative markets and technologies will also be performed.

Specific Activities:

- Perform a business audit, including:
  - Determine the current line of business
  - Evaluate the historical trend of production and sales as well as the market trends for the products produced
  - Evaluate the efficiency of production and the quality of management.

- Perform a valuation and financial audit:
  - Audit the financial statements and supporting documentation for the last three years

  - Perform a financial (accounting) valuation of the enterprise on a going concern basis, taking into consideration the accounting conventions that apply to private sector firms

  - Perform a valuation of the enterprise on the basis of the actual value of the assets

- Evaluate the revenues and operating costs vis-a-vis those that are characteristic of the applicable industry

- Identify all long and short-term debt including the holders of the debt, the balance owed; the interest rates and maturities

- Estimate the value of hidden liabilities, such as the labor indemnities, collective agreements, contingent liabilities, judicial actions, etc.

- Identify any hidden assets such as trade names, etc.

- Prepare a preliminary estimate of new investments necessary to bring the enterprise to a viable level and quality of operations.

• Perform a market and technology audit **only** for those parastatals whose line of business is deemed to be not commercially viable:
  - Identify and assess potential markets that could be serviced by the enterprise

  - Determine the product mix required to service the market

  - Identify the technology required to produce the product mix as well as the proprietors of the technology

  - Prepare a preliminary estimate of the investments required to develop the technology in the enterprise.

TASK 4-2 ENTERPRISE DIVESTITURE APPROACH

Objective: To define the approach and objectives for the divestiture of the enterprise and to optimize the socio-economic impact on Panama.

Specific Activities:

- Determine the goals and objectives of the Government of Panama in the privatization of the parastatal; for example:
  - Recovery of investment
  - Elimination of government budgetary support
  - Receipt of one large payment or a stream of smaller payments over a period of years
  - Limitation of equity participation to Panamanians or acceptance of foreign investment (partial or total)
  - Assurance of employment levels.

- Determine whether parastatal can be sold as an operating business or whether it must be liquidated and sold as assets which the investor would incorporate into a newly established enterprise.

  The sale as assets (as opposed to an operating business) may be required in order to:
  - Reduce the level of employment
  - Liquidate labor indemnities
  - Minimize the potential for future labor conflict
  - Liquidate debt and unpaid taxes
  - Eliminate contingent liabilities

  (This approach may be required in the majority of the parastatals.)

- Develop the appropriate divestiture approach for the parastatals. Among the options that may be considered are:
  - Sale or merger with a single Panamanian or foreign enterprise
  - Sale of stock to investor groups in overseas markets or through private placements in Panama.

- Identify potential financial options appropriate for the specific parastatal, taking into consideration the applicable privatization strategy as well as the amount required to finance both the initial purchase and any additional investments necessary to achieve a viable operating level. Potential options may include:
  - Capital provided by specific investors
  - Capital raised by sale of common or preferred stock
  - Long or short-term debt or convertible debt (banks, venture capital firms or private investors)
  - Licensing or royalty arrangements
  - Capital asset leasing arrangements
  - Conversion of existing debt to equity.

TASK 4-3 POTENTIAL INVESTORS

Objective: To develop an initial list of potential investors (domestic and foreign) and identify their level of interest and the conditions that would attract them.

Specific Activities:

- Identify potential investors (domestic and foreign) on the basis that their technology, operations and market access would compliment the current or alternative lines of business of the parastatal

- Make initial contact with the investors to establish their interest as well as to identify the factors that would enhance their interest

- Develop a short list of serious investors from whom proposals should be requested.

TASK 4-4 PROSPECTS AND MARKETING

Objective: To provide sufficient data (both verbal and documentary) to enable potential investors to prepare an informed proposal for the acquisition of the specific parastatal.

Specific Activities:

- Prepare a prospectus with complete information on the specific parastatal. The information should include (but is not limited to) the following:

  - Technical information:
    - Description of the company and its assets (equipment, etc.)
    - Description of products, including qualities produced and sold
    - Description of markets served including growth trends
    - Description of employees (number, skill levels, union representation, etc.)
    - Description of current problems and potential solutions
    - Description of alternative technologies or uses of the company assets (if applicable).

  - Financial information:
    - Audited financial statements
    - Cost accounting data related to cost of production (fixed and variable)
    - Accounting valuation of the asset
    - Estimated actual value of the assets
    - Profile of all debt owed by the company
    - Estimated labor indemnities
    - Estimated value of hidden assets and liabilities, including contingencies
    - Estimated new investments that may be required.

- Conditions for the divestiture:
  - •• Government of Panama's objectives in the divestiture
  - •• Limitations to the type of investor, financing mechanism or disposition of the parastatal assets.

- Distribute the prospectus to the potential investors identified during Task 4-3

- Meet with the potential investors to discuss the parastatal and to answer any questions that they may have

- Accompany the potential investors on site visits to the parastatal.

<u>TASK 4-5</u> <u>PROPOSALS</u>

<u>Objective:</u> <u>To establish appropriate criteria for the review of investor proposals and then to apply the criteria in the selection of the investment package most advantageous to Panama.</u>

<u>Specific Activities:</u>

- Prepare a uniform evaluation critera for the parastatal that will enable diverse proposals to be comparatively ranked

- Evaluate the proposals received and recommend acceptance of the best

- Assist the government of Panama to negotiate the final agreement with the selected investor group.

ACTIVITY 5 CONTRACTING PROCESS

The Contracting process will be followed by each parastatal for which, during Activity 2, a determination was made that the appropriate privatization strategy is GOP retention of ownership with the contracting of specific activities to private sector entities. The following tasks are required for contracting:

TASK 5-1 IDENTIFICATION OF CONTRACTING OPPORTUNITIES

Objective: To review the operations of the parastatal in order to identify the extent to which contracting is feasible and to identify those specific activities that could be contracted out.

Specific Activities:

- Review the operations of the enterprise in order to determine whether it is feasible and/or desirable to contract the operation of the entire parastatal to a private sector entity under a contract management arrangement

- If contract management is not feasible, identify specific activities that could be contracted to private sector entities under a contractual services arrangements. Such activities often include:
  - Computer operations
  - Meter reading (for utilities)
  - Maintenance functions
  - Printing services
  - Others to be identified.

TASK 5-2 DEVELOPMENT OF CONTRACTING PLAN

Objective: To identify the potential barriers to contracting and develop a plan for implementing the contracting approach for the activities identified.

Specific Activities:

- Evaluate the impact of contracting on employees currently performing the activities:
  - For dismissal of employees, estimate the value of the labor indemnities that would have to be paid
  - For possible transfer of employees, identify the skills possessed by the employees and the organizational units within the parastatal where they may be applied.

- Develop a plan for contracting with private sector entities for the provision of specific activities including:
  - Definition of the activity to be provided
  - Definition of the contractual terms:
    - •• Specifications of activity
    - •• Frequency of activity
    - •• Performance standards
    - •• Others to be identified.

TASK 5-3 IMPLEMENTATION OF CONTRACTING PLAN

Objective: To identify potential contractors, solicit their proposals for the provision of specific activities and finalize a contractual agreement.

Specific Activities:

- Identify a short list of private sector entities that are qualified to provide the activity to be contracted

- Distribute the request for proposal to them and receive the resultant proposals

- Evaluate the proposals on the basis of responsiveness to the request for proposal, experience and reliability of the bidder and cost of service

- Negotiate the contracting arrangement with the selected firm.

ACTIVITY 6 LIQUIDATION PROCESS

The liquidation process will be followed for each parastatal that, during Activity 2, was identified as having no possible commercial viability. The following tasks are required for the liquidation of parastatals.

TASK 6-1 ENTERPRISE EVALUATION

Objective: To review the parastatal with the objective of identifying and valuing the assets and liabilities as well as determining the barriers that must be overcome prior to liquidation.

Specific Activities:

- Identify all assets and estimate their liquidation value
- Identify all liabilities and develop a profile of all debt, including the holders of the debt, the balance owed and the interest rate. Determine whether any assets have been promised as collateral against the debt.
- Calculate the labor indemnities that must be paid to all employees that are dismissed.

TASK 6-2 LIQUIDATION PLAN

Objective: To develop a set of plans for the effective liquidation of the parastatal.

Specific Activities:

- Prepare a plan for the dismissal of all personnel and the payments of all labor indemnities

- Develop a plan to sell all assets of the parastatal either through:
  - Public auction
  - Public tender
  - Private sale.

- Develop a plan to liquidate all debt and tax liabilities.

TASK 6-3 LIQUIDATION

Objective: To implement the liquidation plans for the parastatals.

Specific Activities:

- Implement the plans developed during Task 6-2.

PROJECT SCHEDULE

For planning purposes the duration of the Privatization Assistance Program is estimated to be two years. As a practical matter, however, the entire program could require much more time depending upon the decision as to how many parastatals will actually be privatized (either by divestiture, contracting or liquidation).

During the first two years of the program activities will occur in two stages. The first stage includes the following activities:

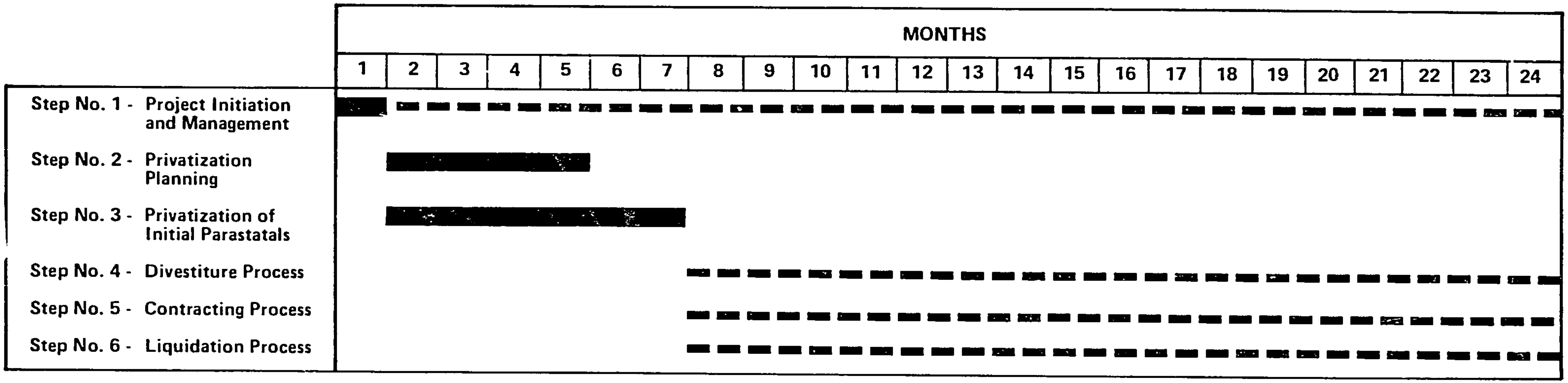
- The project team and GOP Privatizaton Task Force are established
- Privatization procedures are developed
- Parastatals are identified and prioritized and classified as to privatization strategy
- Initially targeted parastatals are privatized.

It is anticipated that these initial activities would take place over a seven to eight month period.

During the second stage divestiture, contracting and liquidation activities will take place at specific parastatals in accordance with the pre-established privatization strategies and prioritites. It is anticipated that the complete divestiture of one parastatal may require approximately five months to perform and that contracting and liquidation will each require somewhat less time. Of course, these estimates will vary depending upon the complexity of each parastatal. Stage two activities would be performed by two privatization teams thereby enabling activities toward the privatization of two parastatals to occur simultaneously.

Attached is a simplified schedule for the first two years of the program.

PANAMA
PRIVATIZATION ASSISTANCE PLAN
PROPOSED SCHEDULE



STAFFING

Government of Panama

The Government of Panama should establish a Privatization Task Force, reporting directly to the Minister of Hacienda, with the responsibility for directing, coordinating and supervising the entire Privatization Program of Panama. This task force would coordinate the efforts of its own staff, assisted by outside consultants/analysts, in the analysis and divestiture of targeted parastatals. The task force would coordinate the colaboration of all Panamanian government ministries in order to assure cooperation in the successful completion of the Privatization Program:

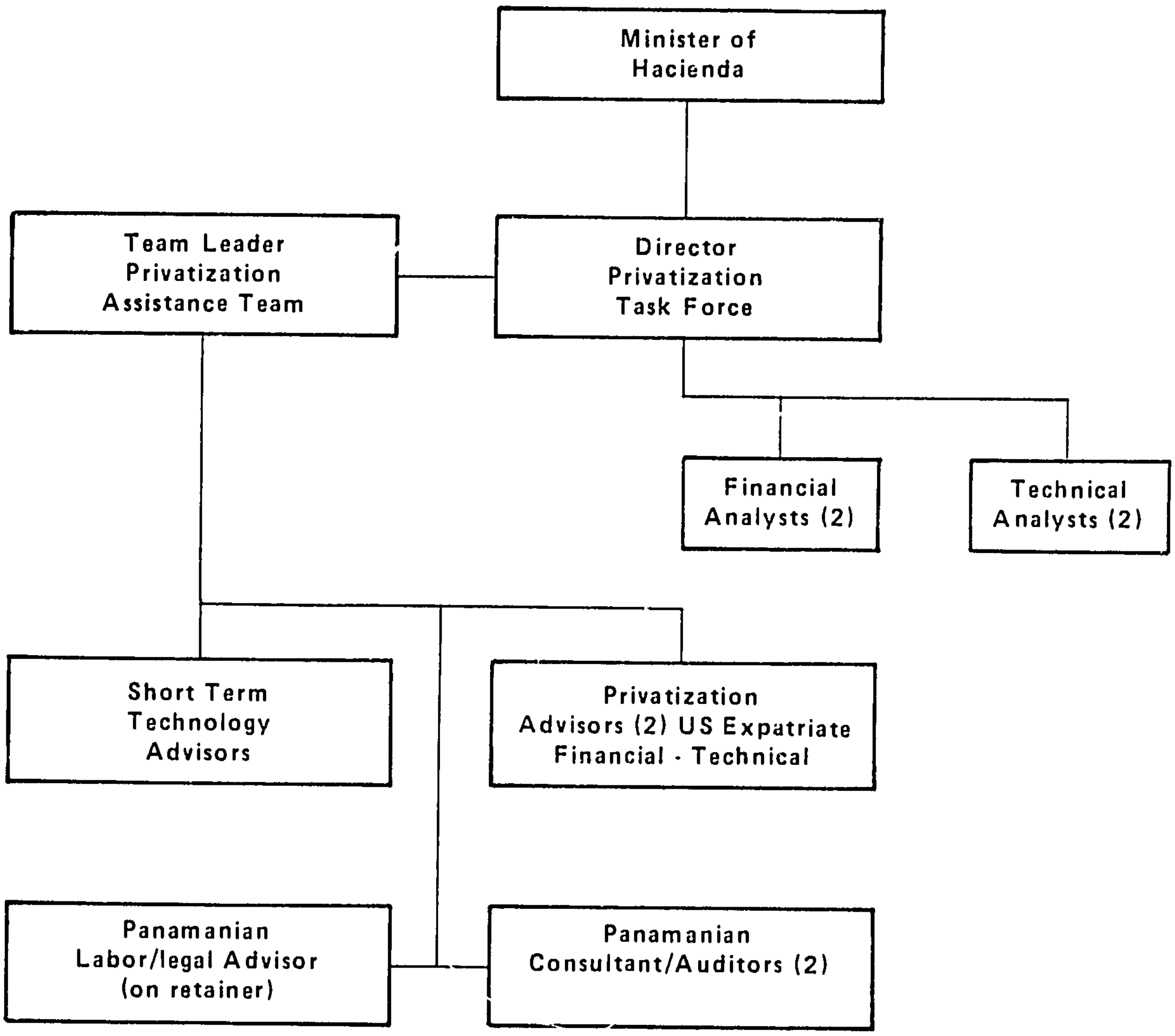
The recommended staffing of the Task Force includes:

- Director - This individual should be a high level political appointee with influence among the cabinet level ministers as well as the Panamanian business community. He should have a solid background in private sector business and finance. Prior experience with divestiture related activities as well as an M.B.A. degree are highly desirable.

- Financial Analysts (2) - These individuals should be mid-level analysts who are experienced in the financial analysis of private sector enterprises as well as government activities or parastatals. A B.B.A. or M.B.A. degree would be highly desirable.

- Technical Analysts (2) - These individuals should be mid-level analysts that have a background in the technical (i.e., production management) aspects of private sector enterprises. Experience in either agri-business, tourism or manufacturing environement is desirable.

ORGANIZATIONAL STRUCTURE
PRIVATIZATION PROGRAM OF PANAMA



- Secretary/Administrative Personnel (3) - These individuals would provide typing and administrative support to the Privatization Task Force as well as the long-term consulting personnel assigned to assist the task force. They should be experienced in the operation of word processing equipment. In addition, experience with personal computers would be desirable.

Privatization Assistance Team

The Privatization Assistance Team would consist of expatriate and Panamanian specialists who would assist the Panamanian Privatization Task Force in the administration and implementation of its Privatization Program. The team would be responsible to provide both expatriate and Panamanian personnel with experience in project management, project finance, privatization, financial analysis/auditing, technology/production techniques and labor/legal analysis. The Team Leader would work with the Director of the Privatization Task Force in managing the overall program while the various analysts would participate on the team assigned to analyze each parastatal, prepare the profile and implement the privatization.

The specific staffing of the team includes:

Expatriate

- Team Leader - This individual is a bilingual expatriate and should be a senior level consultant with extensive experience in mananging technical assistance projects in developing countries. In addition, he should have a good background in contract negotiations, trade, privatization, project finance, financial analysis, technology transfer and both private and public sector management problems.

- Privatization Advisors (2) - These individuals are bilingual, expatriate consultants with extensive experience in privatization, project finance, financial analysis and technology transfer. They should be familiar with the management and finance of both private and public sector enterprises in developing countries. These consultants would play an integral part on each of the parastatal evaluation teams coordinating the efforts of the Government of Panama analysts, the Panamanian consultants/auditors, and the labor/legal advisors.

- Short-term Technology Advisors - These are senior level expatriate consultants with specific specialization in those technologies used in the various parastatals that are subject to the Privatization Program. These short-term consultants would only be brought into the project for evaluations requiring a specialized skill not processed by the long-term project team. Such skills would generally (but not always) be related to the technology assessement of enterprises.

Panamanian

- Panamanian Consultants/Auditors (2) - These are Panamanian financial analysts/auditors from a local accounting and auditing firm. The analysts should be familiar with the Panamanian accounting standards as they apply to private sector enterprises and have experience in the auditing and valuation of the enterprises.

- Panamanian Labor/Legal Advisor - This is a Panamanian labor relations specialist who would be available on retainer to the Privatization Assistance Team. The advisor must have a detailed knowledge of the Panamanian Labor Codes as well as experience in resolution of labor conflicts associated with sale or liquidation of entreprises and the establishment of new enterprises such that future labor conflicts are minimized.

For a two year project the total staffing estimates are as follows:

Government of Panama

Director	24 person months
Financial Analysts	48 person months
Technical Analysts	48 person months
Secretary/Administrative Personnel	72 person months
TOTAL	192 Person months

Privatization Assistance Team

Expatriate

Team Leader	24 person months
Privatization Advisors	48 person months
Short-term Technology Advisors	9 person months
TOTAL	81 person months

Local Panamanian

Short-term Advisors	12 person months
Consultants/Auditors	48 person months
TOTAL	60 person months

ANNEX I

SCHEDULE OF APPOINTMENTS

March 17

Ronald D. Levin
Mission Director
USAID

Frank Skowronski
Chief
Private Sector Development Office
USAID

William M. Campbell
Private Sector Development Office
USAID

Julio Sosa
Executive Director
Consejo Nacional de Inversiones

Menalco J. Solis
Project Manager
Consejo Nacional de Inversiones

Eduardo R. Solas
Regional Director
Consejo Nacional de Inversiones

March 18

Julio Sosa
Executive Dirctor
Consejo Nacional de Inversiones

Alejandro Gaffner
Management Analysis Center
Consejo Nacional de Inversiones

Juan J. De Zan
Management Analysis Center
Boston, Massachusetts

Alberto Garcia de Paredes
Gereral Manager
Instituto Panameño de Turismo

Carmen M. Arias V.
Assistant General Manager
Instituto Panameño de Turismo

Manuel Calderon
Marketing Manager
Instituto Panameño de Turismo

March 19

Doroti de Sing
Vice-Minister
Ministerio de Comercio e Industrias

Manuel José Paredes
General Manager
Air Panama

Lloyd S. Rubin
Geneal Manager
Corporación Transnacional
de Valores e Inversiones

March 20

Ricardo Franco Aguilar
Director General
Corporación Azucarera La Victoria

Mario Acevedo
Technical Director
Corporación Azucarera La Victoria

Mr. González
Ministerio de Desarrollo Agropecuario

Mach 21

Domingo de Obaldia
Executive Director
Asociación de Ejecutivos
de Empresa

March 22

Field Trip to Contadora Island
(Carmen Arias from IPAT)

Met with Gabriel Lewis; Teddy Véliz, Manager of Contadora Resort and Casino, S.A.; and one of the principals interested in the purchase of the hotel and casino property.

March 24

Félix B. Maduro
President
Cámara de Comercio

Marco Fernández
Export Development Bank

Bruce R. Motta
President
Henriquez Zona Libre, S.A.

Jorge Obediente
Partner
Arthur Young & Co.

Raul Arias de la Guardia
General Manager
Banco del Comercio

March 25

Walter Durling
Walter Durling
Consultores y Asociados

Jorge Obediente
Arthur Young & Co.

March 26

Héctor Alexander
Minister
Mnisterio de Hacienda y Tesoro

Rubén Wolcovinsky
Advisor
Ministerio de Hacienda y Tesoro

George Richa, Jr.
General Manager
Fábrica de Velas Devoción

ANNEX II

LIST OF PUBLIC ENTERPRISES

Air Panama International

Port Authority

Bingos Nacionales

Casinos Nacionales

Citricos de Chiriqui A.N.

Contadora Panama S.A.

Corporación Azucarera La Victoria

Dirección Metropolitana de Aseo

Dirección de Aeronautica Civil

Empresa Estatal de Cemento Bayano

Empresa Nacional de Maquinaria Agricola

Empresa Nacional de Semillas

Ferrocarril Nacional de Chiriqui

Ferrocarril de Panama

Hipodromo Presidente Ramon

Instituto de Acueductos y Alcantarillados Nacionales

Instituto de Mercadeo Agropecuario

Instituto Nacional de Telecomunicaciones

Instituto de Recursos Hidraulicos y Electrificación

Loteria Nacional de Beneficencia

Zona Libre de Colon

Banco de Desarrollo Agropecuario

Banco Hipotecario Nacional

Banco Nacional de Panama

Caja de Ahorros

Corporación Financiera Nacional

Corporación para el Desarrollo Integral de Bocas del Toro

Corporación para el Desarrollo Integral del Bayano

ANNEX III

DESCRIPTION OF PARASTATALS

- CONTADORA PANAMA, S.A.

- AIR PANAMA

- CORPORACION AZUCARERA LA VICTORIA

  - Ingenio de Felipillo
  - Ingenio de Las Cabras

- CITRICOS DE CHIRIQUI

- SHRIMP LABORATORY

CONTADORA PANAMA, S.A.

Contadora Panama S.A. owns a complex of properties consisting of (1) real estate sales and development offices on Contadora Island; (2) public utilities services; (3) Aeroperlas S.A. and (4) Contadora Resort and Casino S.A. The latter two properties are up for sale and have interested buyers.

Contadora island is part of the Pearl Island archipelago which lies in Panama bay, on the Pacific side of the Isthmus, 35 nautical miles from Panama City. Approximately 1,000,000 square meters in area, Contadora is serviced from Marcos Gelabert Internatioanl Airport by Aeroperals S.A., one of the properties to be divested.

The island was originally purchased and developed in 1968 by a group of Panamanian investors with the support and participation of the Melia group of Spain. They had two obejctives, the development and operation of a luxury resort on the island and the development and sale of the adjoining land for luxury vacation homes. As the project progressed, it became obvious that the development was undercapitalized. The Panamanian Governmment, recognizing its potential value, purchased it from the original investors and continued to develop it.

By 1970, the Contadora island airport was operational with a 370 meter hard surface runway. Currently the island has 9 kilometers of paved runway, servicing 321 private homes as well as the Contadora Resort and Casino property. The island's public utilities are serviced on a 24 hour basis by four (4) diesel driven power generators with a total capacity of 2800 KW, two lakes containing a total of 28 million gallons of fresh water (during the rainy season) and direct national and international telephone service via Intel's microwave system.

Contadora Resort and Casino, itself, is a 150 room, 9 building hotel complex designed in french colonial style on 126,950 square meters of landscaped beach front property. The eight (8) living area buildings surround the pool and reception/services building on the Playa Larga beach. It also has on the northwest side of the property, 60 cabins with their own restaurant/bar and swimming pool. The buildings and facilities required an original investment of $11,000,000, not counting the cost of the land.

Aeroperlas S.A. owns four (4) Twin Otter aircraft with an air terminal based at Gelabert Internatioanl Airport. Each of these cost approximately $2,500,000 when originally purchased.

Although only two of these aircraft are operational currently, Aeroperlas, aside from Contadora island, services Colon, David, Bocas del Toro, Changuinola and San Miguel. It faces competition from three other domestic airlines on some of these routes. Notwithstanding, Aeroperlas S.A. is nominally profitable. Most of its cash flow, however, is siphoned off to meet some of the operating expenses of the Contadora Resort and Casino property.

Up to three groups are interested in the above hotel property. Two are international resort hotel owners and experienced operators. The third is a consortium of Contadora island residents that is joint venturing the purchase of the hotel with foreign interests linked to the Couples chain in Jamaica. It is anticipated that the GOP will sell off the property to the highest bidder. A formal request for proposals is being prepared and should be ready for distribution within the next 45 days.

AIR PANAMA

Air Panama was purchased by COFINA from Iberia Airlines in the early 1970s for $30,000,000. At the time of its sale, Air Panama owed Citibank N.A. approximately $20,000,000, an obligation which was purchsed from the bank by the Central Government.

Currently, Air Panama flies two (2) fifteen year old, 727/100s on routes to Miami, Bogota, Guayaquil, Caracas, Lima and Mexico City. It also leases a third airplane one day a week to handle Colon Free Zone cargo to and from U.S. commercial markets. Reportedly, management is preparing an international tender which may enable the firm to acquire, via lease, a new Airbus 300, a wide-bodied aircraft with additional cargo as well as seating capacity for 250 people.

As it is presently organized, Air Panama is not a profitable investment for the GOP, for various reasons, including the following:

-- its two 727s are fuel inefficient and may require considerable down time for maintenance;

-- the limited capacity of the aircraft (120-122 people per flight) makes the airline unattractive or unreliable for bookings by U.S. travel agencies and/or charter tour firms;

-- considerable complementary travel services are provided by Air Panama to various agencies of the Government;

-- Air Panama has at least 500 employees, probably almost twice the number needed for its normal operation;

-- its top management is politically appointed with no demonstrated operating experience nor requisite background in this highly specialized industry;

-- continued inability, for budgetary reasons, to acquire aircraft to service attractive new routes, available through reciprocal landing rights, which include Puerto Rico, New York, Los Angeles, Buenos Aires, La Paz and numerous European cities.

Apparently, Air Panama lost money in both fiscal years 1984 and 1985. Nonetheless its current President, Mr. Manuel Paredes (on the job for less than a month) thought that the airline might be profitable during 1986 assuming that prices for fuel do not increase beyond their current levels. He indicated, also, that he was very much in favor of privatizing the airline at the earliest opportunity.

CORPORACION AZUCARERA LA VICTORIA

Corporación Azucarera La Victoria was started in the early 1970's with the objective of making sugar a leading export and expanding employment in poorer rural areas. While the original plans were for one mill (La Victoria), the high world sugar prices of 1974/75, which were projected to continue, led to plans for four more. One was subsequently cancelled, due to falling world prices, and high costs at the original mill at La Victoria.

Capacity by 1983 was at 20,150 tons of cane per day, divided as follows:

Mill Name	Location	Daily Capacity (tons)
La Victoria	Santiago, Veraguas	6,250
Felipillo	Pacora, Panama	5,500
Alanje	Alanje, Chiriqui	7,200
Azuero	Pese, Herrera	1,200
		20,150

The Corporation continued to make heavy losses which by 1983 had exceeded an accumulated B/ .200 million. In March, 1983, the Government closed down Felipillo, the least efficient mill, where total production costs (including depreciation, interest and the mill's share of central office administration costs) for the 1982/83 harvest were 43 cents/lb. compared to an average FOB export price of about 16 cents. Despite its having ceased operations, Felipillo, which has a book value of B/ .35.0 million (excluding land and construction in progress), is still a considerable part of the Corporation's debt burden.

Plant utilization at the La Victoria and Alanje mills has been increased following the closure of Felipillo, resulting in unit cost reductions of around 20%. Since average prices for crude sugar have remained about the same as in 1982/83, La Victoria, the most efficient mill, is near the financial breakeven point.

The Corporation's current losses of aobut $ 3MM each year should be seen in the context of price and marketing policy for the whole industry. In the domestic market, refined sugar is sold ex-mill for 29.3 cents/lb. In the export market, about 67,000 short tons are sold to the US at 16-17 cents fob under a special quota arrangement. Panama currently has 2.9% of the U.S. annual sugar import quota. There is a formal allocation of 87% of the domestic market and 25.5% of the US quota maket to the two private sugar mills which between them produce about 86,000 short tons (almost half the country's total output). Only about 9% of the private mills' output has to be sold at world market prices (4% cents/lb crude in 1984/85), while the corresponding proportion for the Corporation is nearly 25%. Moreover, the Corporation does not sell refined sugar domestically; the price it receives for its crude is 11.5% cents/lb less than the ex-mill price of ther private companies' refined products. Costs at the private mills reportedly total about 16% cents/lb, roughly the same as reported current costs at the original La Victoria mills. (Costs at the two other operating mills owned by Corporación Azucarera La Victoria are roughly 24 cents per/lb of crude sugar processed for Alanje and 37 cents per/lb for Azuero).

The Corporation's mills, moreover, sustain heavy social costs for education, health and similiar facilities. They are also overstaffed. La Victoria, Alanje and Azuero provide, between them, permanent jobs for 13,000 workers and seasonal employement for 8,500 more. In the areas concerned, it would be very difficult to find alternative employment. The Corporation's bloated central office in Panama City costs about B/.2.2 million per year, equivalent to over one cent/lb of crude sugar.

In order to improve the Corporation's financial situation, a number of immediate options are available to the Government, short of wholesale or sale of its assets at deflated prices to the private sector. These include:

- sale of the idle equipment or Felipillo

- closure of the chronically inefficient Azuero mill and transfer of its cane, if economical, to La Victoria

- sale of the Felipillo lands to the private sector with freedom to cultivate what the new owner wishes

- sale of the properties in Cocle, bought by the Corporation in anticipation of the construction of a fifth mill

- closure of the central office in Panama City, or its restructuring in accordance with minimum requirements

- reduction of the permanent labor foce in Alanje and La Victoria to more normal levels for the sugar industry.

Longer term, options involving the carve up and sale of Corporación Azucarera La Victoria should be studied carefully. Current decisions to sell the two most inefficient mills first are probably untenable and should be re-examined in the light of overall government objectives related to the Privatization Program.

CITRICOS DE CHIRIQUI

Citricos de Chiriqui was originally a privately owend 5,000 ha. plantation and concentrate plant. It was taken o r by the Government in 1975 after being abandoned by its original owner, Daniel Ludwig, as a chronic loss maker. In late 1983, the GOP paid about US$6 milion delayed compensation.

Plantation size was reduced to about 2,000 ha. in 1978. Initially, heavy operating losses were incurred. Recently the enterprise has been operating at a small profit (without taking into account the debt to the original owners). Yields are, however, low and costs are high. Only 80% of trees are currently producing and the average yield in 1983 was 1.25 boxes (90 lbs) per tree; a good yield would be 6 boxes. The plant's principal product is orange juice concentrate of which it produces about 14,000 gallons per year operating at about 35% of capacity. This gross underutilization and high raw material costs, due to low yields lead to high production costs. Direct production costs for orange juice concentrate in 1982 were B/ .4.87 per gallon, plus a further B/ .3.30 per gallon for marketing, administrative and other indirect costs. These high costs, which compare with about US$6 per gallon in Florida, can only be sustained over the long term in a protected domestic market. Thanks to temporarily high international prices, the plant is, nevertheless, able to export: some 80,000 gallons were to Costa Rica and the United States in 1983 and 1984.

These are plans for expanding orange production with a view to increase plant utilization. Although Citricos has declared its intention to eventually export most of its increased output, juice and container filling equipment is already being installed with a view to increasing domestic sales. The entity's intentions to sell orange juice directly to consumers in tetrapak containers will involve it in competition for a limited national market with its two principal private customers for orange juice concentrate.

Although Citricos has been operated as state enterprise, it has always been the Government's intention to turn it into a cooperative. Lately, as it became clear that the management problems are too great for workers' cooperative to handle, the Government is considering bringing in foreign capital and management for a mixed enterprise with the workers's cooperative, which is already functioning as a provider of the firm's labor as well as owner and administrator of the social infrastructure and services, such as the cafeteria and gasoline pump.

Management asserts that expressions on interest have been received from 10 firms interested in buying Citricos, including three large food multinationals.

SHRIMP LABORATORY

Information on this, yet to be built, shrimp laboratory is very sparse. Representatives of the Ministerio de Desarrollo Agropecuario (MIDA) were not familiar with the laboratory and were only able to speculate about its current status and the GOPs objectives in privatizing the enterprise.

Plans were initiated in 1982 for the development of a shrimp laboratory to produce shirmp larvae to support the aquaculture industry in Panama. Officials of MIDA thought that the GOP had received a $10 million loan from the Interamerican Development Bank for the planning and design of the laboratory. However, other documents indicated that a loan of $ 8.5 million was made by the World Bank for the laboratory. This shrimp laboratory apparently never got past the design phase and currently has no equipment or staff. It is unclear as to whether the GOP owns the property where the laboratory was to be located.

The objective of the GOP in privatizing the shrimp laboratory is to transfer the plans and designs to a private sector entity that will establish and manage the laboratory.