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**AGENCY FOR
INTERNATIONAL
DEVELOPMENT**



PANAMA

**COUNTRY DEVELOPMENT
STRATEGY STATEMENT**

FY 82

january 1980

UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY
WASHINGTON, D.C. 20523

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POLICY!

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EMBASSY OF THE
UNITED STATES OF AMERICA
Panama, R. P.

January 24, 1980

The Honorable
Douglas J. Bennet, Jr.
Administrator
Agency for International Development
Washington, D. C.

Dear Doug:

I have reviewed carefully the USAID/Panama Country Development Strategy Statement, paying close attention to the strategy it proposes in the light of overall U.S. bilateral objectives in Panama.

Our Government's overriding concern is to foster in Panama a democratic political structure and a healthy socio-economic environment. Internal stability and prosperity will serve to strengthen US/Panamanian cooperation in assuring the achievement of mutual interests in the region, including the efficient and secure functioning of the Canal.

The FY 1982 CDSS for Panama has been prepared at a time when unprecedented attention is being focused on this country and on the Central American subregion. The main purpose of this document is to analyze the country's development environment on the basis of AID's development assistance criteria and to propose appropriate responses. At the same time, the political realities which surround Panama cannot be ignored. At this critical juncture, the prevailing conditions of turmoil throughout Central America plus the new spirit of partnership which has evolved between our two countries as a result of the Panama Canal Treaties make it mandatory that we consider the broader ramifications of bilateral assistance. The interdependence which binds the two countries requires a significant program of development assistance which will alleviate the root problems which have led to deep-seated poverty in Panama and to tragic disruptions elsewhere in the region.

I have had the opportunity to observe at first hand the development needs of Panama and the AID programs which address those needs. This CDSS, in my opinion, reflects the best thinking that could be brought to bear on the subject of Panama's development and I concur fully in the strategy it presents. It contains a timely recognition of the problems in the urban areas of this country. It is precisely the poverty, unemployment and underemployment in these areas that represent the greatest potential for political disruption and social unrest.

I am confident that the proposed program of assistance represents a low-cost investment, the impact of which will go far in meeting both Panamanian needs and U.S. interests. I urge your support for the development assistance effort which this CDSS contemplates.

With best regards.

Sincerely,

A handwritten signature in black ink, appearing to read "Ambler H. Moss, Jr.", written in a cursive style.

Ambler H. Moss, Jr.
Ambassador



UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT
U. S. AID MISSION TO PANAMA

SECTION 5
SERIALS
APO Miami 34002

January 25, 1980

Mr. Edward W. Coy
Acting Assistant Administrator
Bureau for Latin America and
the Caribbean
Agency for International Development
Washington, D.C. 20523

Dear Ed:

I am today submitting the USAID/Panama FY 1982 CDSS. I think you will find the strategy presented therein to be both appropriate to the development needs of Panama and consistent with the broader interests of the LAC Bureau regarding the Central American subregion.

There are a few points that I wish to underscore. First, it is important that we view the Panamanian situation and AID's assistance in the context of turmoil in the region. Second, while the proposed program levels are somewhat higher than would be the case if the Indicative Planning Allocation were accepted, you will note that they are not much higher than the levels approved by AID/W as a result of the FY 1981 CDSS review. The most important point, however, with respect to funding levels is that we are proposing a program that can make a significant contribution to solving the problems of Panama's economic malaise and extend direct benefits to the poor. Levels much below those proposed would open the question of whether we would be having any useful impact on the real problems facing Panama today.

Finally, I would comment on the proposed staffing levels. As you know, I am fully supportive of the "more with less" philosophy. So much so that I am proposing to reduce USDH staff during the period covered by the CDSS, even while increasing the size of the program. But this can only be accomplished if we can retain a reasonable level of FNDH staff. I have initiated a move toward greatly increasing the responsibilities of our local professionals so that they may fill the vacuum created with the reduction of USDHs. Well trained, experienced Panamanians are

Mr. Edward W. Coy

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available in most professional disciplines, and we can and should draw upon this resource; the bottom line, though, is having a ceiling which permits us to do so. We need to turn to our local staff for needed competence and continuity which will permit effective implementation of our development strategy.

I trust you will keep these issues in mind as the CDSS review process takes its course. I am counting on your continued support for our proposed assistance effort in Panama.

Best wishes.

Sincerely,



Aldelmo Ruiz
Director

P A N A M A

COUNTRY DEVELOPMENT STRATEGY STATEMENT

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COUNTRY DATA - PANAMA

<u>Area</u>	<u>Population (1978)</u>	<u>Density (1979)</u>
77,082 km ² (roughly equivalent to South Carolina)	1.8 million Natural growth rate 2.4% 58% urban/ 42% rural	24 per km ² 104 per km ² of agri- cultural land

Demographic Indicators (1977)

Crude birth rate (per 1000)	31
Crude death rate (per 1000)	6
Life expectancy	70

Labor Force (1978)

Working age (15-65) population	55%
Economically Active Population	30%
% of Employed in Agriculture	29%
Age Dependency Ratio	0.8
Economic Dependency Ratio	1.7

Economic Indicators (1978)

(Currency: U. S. Dollar)

GDP (mil. curr. \$)	2306
Real An. GDP Growth (1973-8)	1.8%
Real An. GDP Growth per capita (1973-8)	-1.0%
An. Inflation Rate (1973-8)	7.5%
Imports (\$ Mil.)	- 854
Exports	295
(Bananas)	(72)
(Shrimp)	(30)
(Sugar)	(20)
Services (Net)	349
Current Balance	-210

Social Indicators

Adult Literacy (1975)	78%
% of age group (1974) in	
a. Primary Sch. (5-14)	76%
b. Secondary (15-19)	72%
c. Post Secondary(20-24)	17%
% of population with access to safe water (1975)	79%
Daily supply of calories per capita (1974)	2421
Population per physician (1976)	1270

% GDP by Sector (1978)

Services	47.3%
Manufacturing and utilities	17.4%
Agriculture	16.0%
Canal Area (Panamanian wages)	6.5%
Other	12.8%
	<u>100.0%</u>

Government Finances (1978)

Current Revenues (\$ Mil.)	386
Current Expend.	386
Investment Outlays	402
Public Debt-Total	2371
% GDP	103%
Debt Service - Total	398
as % of exports	62%
Debt Service-Cent.Govt. only	190
as % of Cent.Govt.revenue	49%

PANAMA

COUNTRY DEVELOPMENT STRATEGY STATEMENT

1982 - 1986

Introduction

Panama's development has followed a pattern dictated by its geography and the presence of the Canal. Some indicators of this development, such as average per capita income, would appear to describe a prosperous middle income country -- and clearly the Panama Canal and the industries and services which have evolved around it have helped to create conditions which, over the years, have benefitted some Panamanians handsomely, with some positive trickle down effects at the lower levels of the economy. Nevertheless, gaps between the urban and rural population and between the modern and informal sectors have persisted and are accentuated in an environment where urban slum tenements fester under the shadows of modern high-rise buildings housing prosperous international banking and commercial firms.

Stated in different terms, the accident of geography which brought about the presence of the Canal has been a two-edged sword, which along with obvious benefits, has also brought on an excessive dependence on foreign markets and an open, dollar-based economy highly susceptible to world inflation and other international economic and political vagaries which lie outside the country's control. It has created a country dominated, until recent years, by a Metropolitan Area which ignored the isolated and economically depressed rural sector while catering to the specialized needs of the foreign-dominated business community. The unskilled and

undereducated Panamanian poor were left only marginally better off than the poor in El Salvador, Honduras or Nicaragua. Even with recent gains, productivity in the rural areas is as low or even lower than in the other countries of the subregion. In the Metropolitan Corridor, the poor are faced with severe unemployment in an environment where the cost of living is comparable to that found in large U.S. cities.

Despite the Government of Panama's commitment to equity, the economic benefits of development continue to bypass most of the poor. The combination of economic recession, which after five years is only now showing signs of slow and uncertain recovery, and inflation continues to swell the ranks of the poor. Panama today faces a condition where the economic plight of the poor is worse than it was five years ago and where many at the margin of poverty are rapidly falling behind due to decline in real income and employment opportunities.

Attempts by the GOP to counter growth arrest and concomitant massive unemployment, while continuing to pursue the social programs of the "revolution", led, in the late 1970s, to heavy foreign borrowing which has resulted in massive public sector deficits. The result has been a public debt burden which is among the highest in all of the developing world. Unfortunately, even this infusion of capital has not been sufficient to make a real dent in the unemployment level (currently estimated at 22%) or to reverse significantly other negative economic trends.

A policy of heavy government spending which has produced only limited results cannot continue. The GOP has demonstrated that it recognizes the need for new economic strategies. The recently unveiled 1980 GOP budget is further evidence that austerity in public spending combined with in-

centives for new employment generating private investments have become the keystone to the GOP's economic recovery program.

The assistance strategy which emerges out of our analysis is designed to complement the GOP economic recovery program and help lay the groundwork for the kind of development for which Panama is ideally suited and which will help carry Panama into the Twenty-first Century as a small but prosperous country within the family of democratic nations.

This Mission firmly believes that AID and the IFIs must intensify their collaborative efforts with the Panamanians in their struggle to redress the imbalances in their society and to achieve the country's development potential. AID's concessional assistance becomes particularly important at this juncture when the GOP can ill afford additional commercial borrowing to achieve its goals.

The proposed AID development assistance strategy is tailored to address the intermediate and long-term solutions to Panama's economic problems. It is designed to assist in the implementation of required policy reforms and institutional changes. It calls for an employment and productivity-oriented program focused on meeting the needs of the rural poor, while attacking the emerging agenda of urban poverty, environmental degradation and energy resource waste.

We propose an ambitious program, but one that can be achieved with the right combination of factors, primary among which is the Panamanians' own initiative. Our role will be that of a catalyst and collaborator. Our strategy addresses the critical needs of the poor and of the nation. We are confident that the investment proposed will yield tangible dividends as it helps to bring the benefits of development to all Panamanians.

PART I. ANALYSIS

A. Overview

1. Economic Situation

Panama's principal resources and basis for its economic growth are its strategic location and the Canal. Other resources are fisheries, tropical forests, and copper deposits, which could be exploited but only with massive, high-risk investment. Good crop lands are scarce outside the limited commercial banana, sugar and rice areas. An open, dollar-based economy has developed, dominated by a services-oriented metropolitan sector near the Canal entrances, linked to international trade and finance. Services now account for roughly half of Panama's Gross Domestic Product (GDP), with manufacturing one sixth and agriculture one sixth.

Despite a relatively high overall per capita GDP (\$1,264 in 1978), there are wide differences in productivity between Panama's rural and urban sectors, and between the modern and traditional subsectors of each. At the same time, annual output per worker (\$4,612 overall) ranged from \$2,738 in agriculture and \$2,797 in the non-commercial urban service sectors to \$12,000 and higher in the utilities and finance sectors. These two sectors together constitute 57% of the employed workforce, but turn out only 34% of GDP. Moreover, the urban service sector contains the bulk of the nation's unemployed, which means that average annual output per capita in this sector is actually much lower than even in the agricultural sector.

Panama experienced a surge of economic growth during the 1960s and early 1970s (real GDP growth averaged over 7% annually) derived from rising Canal traffic and income, commercial agriculture expansion,

development of some light manufacturing, and a construction boom. This played out and, along with the massive rise in crude oil prices and related decline in world trade, triggered a recession beginning in 1974, which has persisted to the present. This economic stagnation revealed Panama's narrow economic base--limitations imposed by substantial dependency on Canal traffic and other economic flows from the former Canal Zone, a dearth of natural resources, small domestic market, high wage cost structure, GOP labor and price policies and continuing inability of the bulk of the agricultural sector to achieve improved output and income. GDP growth averaged 1.8% annually between 1973 and 1978, a per capita decline of minus 1.0% annually.

The problem has centered on private investment, which fell to a 1978 level that, in real terms, was only two thirds of the peak reached in 1973. This resulted from widespread low returns caused by the factors enumerated above, plus political and economic policy uncertainties and the unpredictable course of Treaty developments. In particular, the GOP's labor and price policies have seriously affected the private sector's willingness to make substantial investments. Massive expansion of public sector investment was not sufficient to prevent a drop in overall investment and employemnt.

To counteract the recession and concomitant drop in private investment and employment, the GOP sharply boosted public sector investment in 1976 by means of heavy foreign borrowing, 90% of which was expensive commercial credit. Under this strategy, public debt rose from \$800 million in 1974 to \$1,200 million in 1976 to \$2,400 million in 1978. Total public debt as a percentage of GDP grew from 44% in 1974 to 103%

in 1978. Servicing costs of the total public debt held directly by the central government rose from 24% in 1974 to 49% of central revenues in 1978, representing one of the world's heaviest debt-servicing burdens.

Mission projections indicate that the GOP will need to hold public investment to current dollar levels over the next few years (declining in real terms) just to keep central government debt service from rising above roughly 50% of current revenues. Also, there is no basis for expecting major gains in Panamanian export earnings over the next few years. Thus, GOP financial constraints will probably limit the total public sector's overall borrowing levels as well as further contain, in particular, the pace at which IFI financing can be utilized, hence its annual investment level.

Although there has been some recovery from Panama's recent economic slump, long-term private investment continues to be negatively affected by constraints on business as described above. Moreover, public sector investment is likely to decline significantly in real terms from its high level of the past 3-4 years. Fiscal projections show that, over the next five years, the increase in the government's interest payment on the public debt, plus the annual operating costs related to Panama's new responsibilities under the Treaties will exceed the estimated \$75 million in new annual revenue from the Canal by well over \$100 million. This means that the government must keep increases in ordinary government outlays significantly below the growth of ordinary revenues, under the present tax structure, in order to prevent a current account deficit. It virtually eliminates hope for public savings through the central government without a severe cutback in ministerial outlays and services to the public.

2. Population and Labor Force

The annual natural population growth rate has fallen from over 3% during the late sixties to an estimated 2.42% for 1978. As a result, the Panamanian census bureau revised population projections for the end of the century downward from a range of 3.0 to 3.6 million to 2.6 to 3.3 million, with most evidence pointing to an outcome of 3.0 million. However, as this decline essentially involves the dependent under-15-year-old group, its impact signifies primarily that certain types of social service demands will not be as pressing during the next two decades; it does not imply an improvement, per se, in individual economic welfare.

Analysis of the population structure shows the working age group, generally defined as those between the ages of 15 and 64, to be the critical growth area. Due to the declining birth rate, this segment of the population is growing significantly faster than the dependent subgroup (under 15 and over 64). The working age group or labor pool was 53% of the national population in 1970 and is likely to increase to a 63-67% range in the year 2000, and, in absolute terms, will double between 1975 and 2000.

The other key aspect of Panama's population growth is its spatial distribution: the society is becoming urbanized at all levels, with its main concentration taking place in the Panama City-Colon Metropolitan Corridor. Not only are urban areas projected to grow 2-3 times as fast as rural areas between 1970-2000, but the metropolitan area will continue its primacy by having approximately 61% of the national population at the end of the century.

TABLE 1
URBAN POPULATION TRENDS
PANAMA: 1940-2000

YEAR	PANAMA-COLON METRO AREA (000s)	% OF NAT'L POP.	OTHER URBAN AREAS (000s)	% OF NAT'L POP.	TOTAL URBAN POP. (000s)	% OF NAT'L POP.
1940	197	32%	37	6%	234	38%
1960	406	38%	99	9%	505	47%
1970	615	42%	157	11%	772	53%
1978	847	46%	208	11%	1055	58%
1985	1096	51%	248	12%	1344	63%
2000 ^{1/}	1823	61%	332	11%	2155	72%

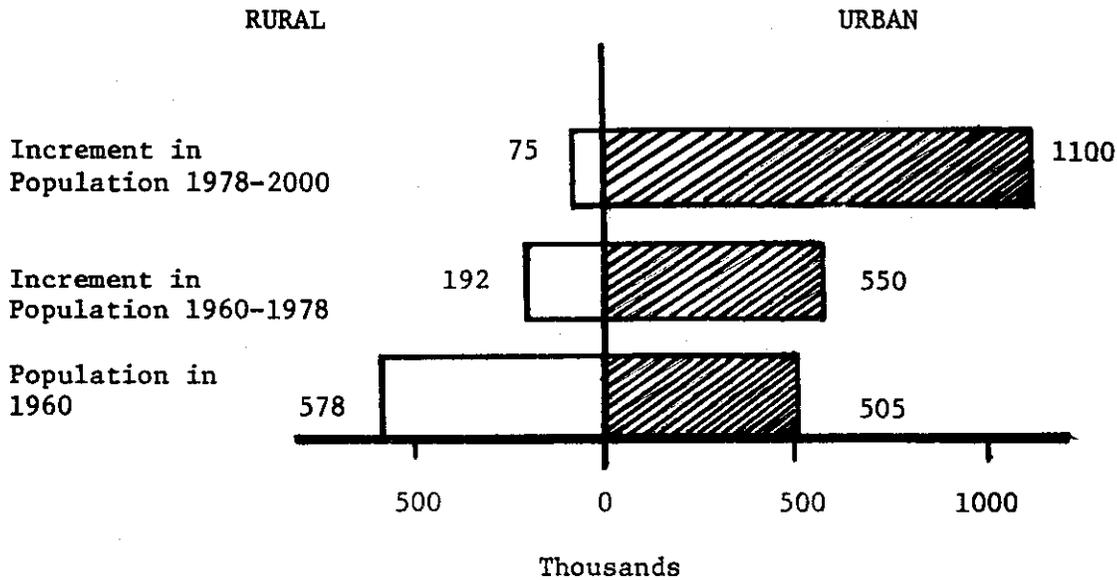
^{1/} Assumes a population of 3 million in the year 2000.

Source: 1970 Census enumerations, Census projections and Mission estimates. Urban was defined in 1970 as a locality of at least 1500 inhabitants wholly or partially served by public sewer/water, electricity, paved streets, a secondary school, and commercial, social and recreational services. The Metropolitan Area includes the districts of Panama, Arraijan, La Chorrera and Colon.

Using a definition of urban which considers agglomerations of urban functions rather than mere population size (see Table 1), Panama in the year 2000 will be over 70% urbanized, with a rural population increasing only from 770,000 in 1978 to 845,00 in 2000. Spurred by lack of on-farm employment opportunities and drawn by expected employment elsewhere, rural migrants will continue their entry into the urban or off-farm labor market. Whether migrants remain close to their homes or move to the larger secondary cities or even to the metropolitan area is not so important as the shift away from agriculture into a monetary,

interdependent urban economy. Underemployment and unemployment become serious economic and political issues for people cut off from the in-kind benefits of subsistence agriculture.

PANAMA: RURAL/URBAN POPULATION ESTIMATES/PROJECTIONS, 1960-2000



The interaction of the growth of the labor pool and urbanization is cause for serious concern not apparent in traditional statistics. For example, the age dependency ratio (ADR) and the economic dependency ratio (EDR) have long been used as supporting indicators to measure economic well-being in many developing countries. However, in the case of Panama, neither the ADR or EDR is sensitive to the economy's worsening inability in the 1980s to absorb the working age population into productive employment (see Annex A). A better measure uses participation and employment coefficients which compare the labor pool to total employment. In this

way, the effects of declining population growth and the moderating influence of participation rates on unemployment are neutralized. The new workforce ratio shows that the employment absorptive capacity of the economy improved through 1974; since then, it has steadily worsened and is estimated to reach a point in 1990 where only 42% of the working age population will have jobs. Put more bluntly, if current economic trends continue, we can expect the unemployment rate to increase from 17.5% in 1978 to 25.1% in 1985 and reach 29.5% in 1990. While underemployment will continue to be a problem in both the urban and rural sectors, a conservative estimate would place urban unemployment at 90% of the national total.

Solving the unemployment problem will not be easy, even under the most beneficial economic conditions. Table 2 presents projected unemployment rates for 1985 and 1990 using different economic growth assumptions. Implicit in each case, except the first, are successful employment/economic stimulation interventions on the part of the private and public sectors.

The rate of job creation indicated in the table may be compared with the actual creation of an estimated 5,000 jobs in 1979 (GOP estimate). It should also be noted that GDP growth was 1.8% for the period 1974-1978.

TABLE 2

EMPLOYMENT CREATION AND EMPLOYMENT

PANAMA: 1979-1990

	GDP GROWTH RATE	EMPLOYMENT/ OUTPUT <u>1/</u> COEFFICIENT	ANNUAL JOBS CREATED 1979-1985 (000s)	UNEMPLOYMENT RATE 1985	ANNUAL JOBS CREATED 1979-1990 <u>1/</u> (000s)	UNEMPLOYMENT RATE 1990
1	4%	0.40	8.3	25.1%	8.7	29.5%
2	4%	0.60	12.8	21.5%	13.6	23.1%
3	6%	0.50	16.3	18.6%	17.6	18.0%
4	6%	0.60	19.8	15.8%	21.8	12.6%
5	8%	0.50	22.3	13.8%	24.7	8.8%
6	8%	0.60	27.3	9.7%	30.9	0.8%

1/ The coefficient is rate of growth of employment over rate of growth of GDP.

Source: Factores Que Afectan La Demanda Por Mano de Obra en Panama by Guillermo O. Chapman Jr., prepared for the Ministry of Planning and USAID/Panama, Panama City, December 1979. In All of the cases above a 60% labor participation rate is assumed.

3. Agriculture

Panama's agricultural economy is characterized by two extreme systems of production and marketing. On the one hand is the commercial crop sector utilizing modern agricultural practices and fully linked to national and, in some instances, international markets. On the other hand is the traditional subsistence sector employing antiquated technologies and linked to local markets. Most of the rural poor are engaged in subsistence agriculture, have limited access to production resources, have no legal title to the land they work, receive no institutional

credit, and utilize very rudimentary production methods with shifting slash-and-burn agricultural practices. This pattern of economic dualism is typical in many Latin American countries, but in Panama it is particularly striking.

Taken as a whole, the agricultural sector expanded in the 1960s at about 5% per annum in real terms, with most of this growth being generated by export crops. Production of bananas increased significantly and the international market became strong, while crops for domestic consumption grew at only half the overall rate, causing shortages in the national market and forcing imports of basic foodstuffs. Since the end of the 1960s, however, the growth rate of both export and local crop production has declined because of a combination of bad weather and political and economic uncertainties.

The growth in domestic crop production has also been affected because the research and extension service of the Ministry of Agricultural Development (MIDA) has not reached most private producers. Since the early 1970s, MIDA's credit, technical assistance and other services have been channelled mainly to government-organized farming communities. A recent World Bank report identifies another element affecting the growth in domestic production: the growing scarcity of readily accessible land, particularly on the Pacific slope, which has supported much of Panama's agricultural expansion. Not only is new land becoming increasingly scarce, but previously cropped land is declining in fertility from heavy use and neglect of soil conservation. Land in crops actually declined in the period 1960-1979, while pasture land increased.

Actually, Panama has little good, flat land relatively suitable

for mechanized agriculture or intensive cattle raising. 1/ This situation partially accounts for the historical pattern of settlement and land use, the generally low productivity of land and, in the case of traditional cropping systems, of labor, and the large number of migratory subsistence farmers who have compounded soil problems by destroying the forests and causing devastating erosion.

Beginning in the early 1970s, the GOP initiated a price support and credit expansion policy in an attempt to stimulate overall agricultural production, with the particular goal of attaining self-sufficiency in the basic staples of rice, corn and beans. Although there was initial response to these incentives, the past three years have seen virtually stable support prices, with production again stagnating. The agricultural sector today is burdened with many domestic agricultural products priced above world market levels, and the country is faced with the prospect of an ever-increasing need to import basic staples. The country still imports some 30% of its bean consumption, 20-25% of its corn consumption and 30% of its milk consumption. Projections indicate that by 1985 Panama may need to import about 27% of its corn and 39% of its beans annually. Other crops show a similar trend.

The current low yields and high production costs experienced in Panama indicate that the quantity of agricultural products imported can at least be reduced, if not eliminated, by increasing the sector's

1/ Most of the terrain is mountainous and the majority (80%) of the soils are unsuitable for cultivation (e. g., types VI, VII and VIII).

efficiency. Compared to other Central American countries, Panama has extremely low yields for beans, corn, rice and sugar cane, and there is every reason to believe that the same disparity exists for other crops as well. Comparative data indicate that Panama's average yields for corn are 40% lower than the average yields for all of Central America. The corresponding figures for beans, rice and sugar are 40%, 19% and 19%, respectively. Poorer climate and soil conditions notwithstanding, there is room for considerable improvement. Increased crop yields could not only increase the output of lands currently under production, but should also lead to increased hectareage in production due to increased profitability per hectare. The tight budgetary situation facing the government for the next several years makes it unlikely that the GOP can maintain the subsidies. Moreover, there has been unsatisfactory production response to these subsidies. Thus, a program to increase yields and reduce the costs of production through better varieties and more appropriate techniques appears to be the most promising solution for reducing dependence on imported agricultural products and for providing a more efficient allocation of the country's resources.

B. Analytical Description of the Poor

1. Summary

Of Panama's 1.8 million persons, approximately 715,000 (or 39%) are poor, of which 384,000 (or 21%) are extremely poor, i.e., earning less money than is required to provide for basic human needs. While members of these two groups are found throughout the country, most live in the central and western provinces of Chiriqui and Veraguas and in the Panama City/Colon Metropolitan Area.

Most rural poor are illiterate, live in houses that lack electricity, potable water and sanitary facilities, are isolated, and receive few health services. Also, many of their children suffer from malnutrition and diseases, which contribute to an infant mortality rate that is higher than the national average.

The urban poor receive some of the basic services denied their rural brethren, but share the same problem of inadequate housing. In addition, the urban poor live in extremely crowded conditions, with only communal water sources and unsanitary waste disposal facilities. Another problem is that many of these people are unskilled, which partly explains why so many are unemployed or underemployed. In a highly monetized, high-cost economy, the urban poor are particularly subject to the negative aspects of economic fluctuation and inflation. The plight of the urban poor is steadily worsening because, inter alia, many unskilled people 1/ are migrating to the cities, adding to the rolls of the unemployed, the badly housed, the desperate. As this segment of the urban population grows, the degree and complexity of their problems also grow.

2. Selected Socio-Economic Indicators

Poverty Line Analysis

Two levels of income are calculated for the country adjusted for location, based on what it would roughly cost a family of 5 persons to purchase a basket of minimal goods and services. The first level, descriptive of 39% of the population, is the income barely adequate to provide for a family's basic needs. This income has been calculated

1/ The 1970 census shows 40% of the migrants 15 years and older had either no education whatever or an incomplete primary education.

at \$517 per capita annually for Panama City and Colon, \$402 for the other urban centers and \$304 for the rural areas.

At the second level of income, descriptive of more than 20% of Panama's population, people live in extreme poverty, or in seriously deteriorating conditions. This extreme poverty line has been calculated at \$270 for the cities of Panama and Colon, \$210 for other urban areas, and \$160 for the rural areas. The FY 1981 CDSS may be consulted for the methodology of this poverty line analysis.

Application of the "poverty" and "extreme poverty" lines to the estimated population distribution for 1978 yields the following data on population living in poverty:

	Pop. Below Extreme (000s)	% of Natl. Pop.	Pop. Below Poverty (000s)	% of Natl. Pop.	Pop. Above Poverty (000s)	% of Natl. Pop.	Total Pop. (000s)	% of Natl. Pop.
Total	384	21	714	39	1,111	61	1,826	100
Rural	245	13	434	24	333	18	767	42
Urban	139	8	280	15	778	43	1,059	58

Location of the Poor

In order to move from the more general description of poverty provided by the income distribution and poverty line data to more location-specific and qualitative information, the Mission has analyzed social indicators and access to services at the district level.^{1/} For the rural areas, three key indicators--infant mortality, birth rate and illiteracy--were examined for each district in the country. These indicators were then

^{1/} The country is divided into 9 provinces and 65 districts. In addition, there is one special district set aside for the Cuna Indian tribe.

compared to national averages.

Fourteen districts have the "least" level of satisfaction of basic needs, i.e., they are below national averages on all three key indicators. All are in the Central and Western regions and located in those provinces with the largest populations below the poverty line. Sixteen additional districts fall below the national averages on two of the three indicators and thus have serious deficiencies in the satisfaction of basic needs. Most of these districts also lie in the Central and Western regions. The major concentrations of poverty are in Veraguas province and neighboring districts in eastern Chiriqui, Cocle and Colon, Herrera and Los Santos.

The majority of these districts have a number of factors in common, including poor soils, mountainous terrain, highly dispersed population and a lack of access roads. The widespread poverty in these districts is further confirmed by a review of other indicators as well, such as housing conditions, water, sanitation and access to health services.

The dearth of on-farm employment opportunities forces many rural dwellers to seek off-farm employment in small towns and secondary cities and in the Metropolitan Corridor which are unable to absorb these excess rural workers. The situation has been exacerbated by haphazard and uncontrolled development throughout the urban hierarchy. The Metropolitan Area, for example, is characterized by a low density, sprawl-type pattern which has permitted development in ecologically sensitive areas on the periphery. This dispersed urban structure, which has caused excessive infrastructure costs, places substantial pressures on government institutions to provide and coordinate the educational, health, recreation, transportation and related services demanded.

The relative economic well-being of the Metropolitan Corridor 1/ makes it the preeminent target for employment-seeking rural migrants who historically have congregated at the urban fringe. The largest migrant settlement is San Miguelito, which has about 150,000 first-generation migrants. The urban poor are not necessarily recent migrants from rural areas. Second- and third-generation urban poor live in slums such as Chorrillo and Caledonia in Panama City, which have the same crowded and unsanitary living conditions and excessive rates of unemployment and underemployment as do the more recent migrant settlements.

Of special note in discussing the spatial aspects of poverty is the internal momentum of the urbanization process. Although rural-urban migration will continue to be an important component of urban growth, the natural increase within urban areas will account for almost two-thirds of future urban population growth. This fact presents both opportunities and problems for the GOP. While the provision of services for the poor and the measurement of program impacts will be much easier and more economical, the need for coordination and planning with the private sector and among government agencies will place severe demands on the government's ability to avoid many of the foreseeable negative aspects of urban growth.

Unemployment and Underemployment

The economically active population (EAP) numbered 543,000 in 1978 (30% of the population), of which 30% were women. Providing jobs for a steadily expanding population was no great problem for Panama during the high growth years of the 1960s and early 1970s. However, since 1974, the

1/ Although median monthly family income in Panama City and Colon in 1976 was \$457 and \$434, respectively, well over 60% of the families in the poor barrios earn less than \$200 monthly, i.e., \$480 per capita annually.

number of jobs has actually declined and unemployment has soared. The problem has become particularly severe in the Panama City/Colon Metropolitan Area where underemployment, a chronic problem in agriculture, has now also become significant.

Table 3 presents official government statistics for the metropolitan region, with a final column making adjustments for low participation rates and the GOP's emergency employment plan.^{1/}

TABLE 3
LABOR FORCE TRENDS FOR THE METROPOLITAN REGION
1974 - 1978

	1974	1975	1976	1977	1978	1978 (Adjusted)
Population 15 years and over	455,800	478,630	501,060	534,260	552,000	552,000
Economically						
Active Population	280,300	284,100	279,760	289,680	314,020	331,200
Participation Rate	61.5%	59.4%	55.8%	54.2%	56.9%	60.0%
Non-economically						
Active Population	175,500	194,530	221,300	244,580	237,980	220,800
Percentage of Pop.	38.5%	40.6%	44.2%	45.8%	43.1%	40.0%
Employed	260,400	259,030	254,920	256,000	281,240	258,240
Unemployed	19,900	25,070	24,840	33,680	32,780	72,960
Unemployment Rate	7.1%	8.8%	8.9%	11.6%	10.4%	22.0%

Source: 1974-1978, Controller General, Bureau of Statistics and Census.
1978 Adjusted - Mission estimates.

Recent increases in educational participation do not account for the significant decline in the EAP. The only explanation, it seems, is

^{1/} The plan was initiated in 1977 to serve as a stopgap measure to deal with the unemployment problem. Public service jobs, at monthly salaries of \$100, were given to 24,000 individuals.

that large numbers of people became discouraged from seeking jobs. Because officially calculated participation rates for the early seventies were all above 60%, adjusting the 1978 participation rate to 60% in the table is likely to be conservative. Although the table shows unemployment increasing from 1974-77, the decline from 1977-78 is less than one thousand despite the GOP emergency employment plan, which mostly affects the Metropolitan Area. For the table, this "temporary" program is factored out of the number of employed, with the result that "real" unemployment, instead of declining to 10.4%, increases to 22%.

With average yearly growth estimates of 30,000 between 1975-80 and 34,000 between 1980-85 for the working-age group at the national level, Panama finds itself in a worsening deficit situation as regards job creation, with the necessity of creating 15,000-20,000 new jobs yearly over the next five years merely to stay even. Most of these jobs will need to be created in the Metropolitan Area where both relative and absolute unemployment are highest--official data set metropolitan unemployment at 75% of the national total.

It is estimated that current underemployment in the metropolitan labor force is in the range of 20-30%. A high proportion is concentrated in the service sector which, as indicated below, is the only major sector where the number of jobs has increased appreciably over the last eight years.

EMPLOYMENT IN THE METROPOLITAN AREA BY SECTOR

	<u>1970</u>		<u>1978</u>		<u>Average Annual</u>
	<u>Number</u>	<u>%</u>	<u>Number</u>	<u>%</u>	<u>Growth Rate</u>
Services	128,000	58.0	186,150	66.2	4.8
Manufacturing	31,200	14.0	32,670	11.6	0.6
Canal Area	22,400	10.1	18,300	6.5	-2.5
Construction	14,900	6.7	16,420	5.8	1.2
Other	24,600	11.2	27,700	9.9	1.5
	<u>221,900</u>	<u>100.0</u>	<u>281,240</u>	<u>100.0</u>	<u>3.0</u>

This concentration of employment in services has important ramifications for the poor because wages in this sector are low and not subject to much increase.^{1/} Areas of the service sector, such as manual labor and domestic services, also have the major concentration of unskilled workers. In 1975, 70% of those employed in these areas had a sixth-grade education or less.

Unemployment and underemployment are particularly high among women and among the young. In 1977, 14% of the female labor force was unemployed and approximately 44% was underemployed, with the comparable figures for men being 10% and 18%, respectively. Opportunities for off-farm employment for rural women are minimal, causing many to migrate to the cities. Female employment in urban Panama is concentrated overwhelmingly in the service sector, and wages paid to women are both lower than those for males and increase at a much slower rate. Unemployment rates among individuals ages 15 to 19 and 20 to 24 (1975 figures including both men and women) were 20.9% and 14.7%, respectively. While the data necessary to calculate underemployment among those aged 25 and younger are unavailable, it may be assumed that there is a high incidence of underemployment in this group as well.

Both women and the young in the Metropolitan Area are relatively low participants in the labor force, and their participation seems to fluctuate strongly as the job market alternately expands and contracts. Given the opportunity, however, both groups would join the labor force in far greater numbers. Experience with the GOP's emergency employment plan provides a case in point with regard to women: 42% of the 16,700 women hired under the plan were not actively seeking employment at the time.

^{1/} Between 1974 and 1976, average weekly wages in the non-government services declined by 1%. Wages in commerce and industry, on the other hand, increased 5% and 16%, respectively.

Housing

A recent Ministry of Housing report illustrated accumulated need, units constructed and new unit demand for the nation and the Panama City-Colon Metropolitan Area for 1977.

TABLE 4

NATIONAL HOUSING NEEDS FOR 1977

	<u>Accumulated Need to 1976</u>	<u>Avg. # of Units Constructed, 1970-76</u>	<u>Need for 1977</u>
Panama	223,173	8,016	185,794 ^{1/}
Metropolitan Area	116,588	7,126	79,513
Remainder of Republic	106,585	890	106,281

Source: Informe Estimación de las Necesidades, MIVI, 1976.

The figures should be tempered by (1) the tendency to overstate need, particularly in rural areas, by applying inappropriate, overly rigid housing code standards (use of local materials, per se, does not imply a substandard dwelling), and (2) the neglect of those units constructed by the informal sector which is responsible for almost all rural housing and many of the dwellings of the urban-poor target group. What must be noted, albeit in indicative terms, is the severe gap between shelter supply and demand, a gap even more serious for the urban poor than is apparent above, as most new metropolitan area housing is destined for people above the median income level.

Rural housing can be characterized by its use of self-help labor, non-manufactured materials and lack of basic amenities such as electricity, potable water and sanitary facilities. The rural poor tend to own their own dwellings and live in low density environs. The dispersed nature of the rural housing problem is such that its solution lends itself to less

^{1/} This figure includes housing that must be replaced as well as the units that must be built to accommodate newly established families.

capital-intensive and formalized approaches through appropriate technology and use of indigenous materials.

While the rural poor often lack access to basic services received by some of their urban brethren, there is an extreme difference between rural and urban tenure patterns. The 1970 Census points out that 87% of rural units were owner-occupied and 13% were rented and leased. By contrast, in urban areas, 39% of the units were owner-occupied, 53% were rented and 8% were leased. If urban wage earners above the median are disaggregated, the rental/lease figures would be significantly higher. Increased urban wage differentials have not been able to make up for comparatively high-rent costs and the loss of in-kind agricultural benefits for urban migrants.

Moreover, the gravity of the urban housing issue is made more glaring by lack of response of the private-housing sector. The Ministry of Planning estimates that 93% of the sector's output is directed to families in the high- and upper-middle-income strata, which represent only 16% of the total demand for housing. Moreover, until recently, public sector interventions in housing have reached only the middle class. Private sector activity in cities has been sporadic and public sector involvement has yet to have any measurable effect.

C. Identification of the Causes of Poverty

The lack of economic growth is, at present, the major contributor to growing poverty in Panama. The symptoms of this problem have been particularly noticeable over the last five years, during which Panama has suffered a severe and continuing economic recession, with a decline in per capita GDP and a stagnant job market. Following is a description of specific causes of poverty, many of which have contributed to the lack of growth and will tend to limit that growth in the future.

1. Decline in Private Investment

Over the past five years, private investment in Panama has declined steadily to a 1978 level that, in real terms, was only two thirds of the peak reached in 1973. Also, the expansion of public sector investment has been insufficient to prevent a drop in overall investment. Private investor interest waned as promising commercial and industrial investment prospects played out. This has resulted in a stagnation of the economy and a steadily shrinking job market.

Government policies have discouraged investors. The Labor Code was made highly pro-labor and more expensive to employers in 1971, further raising Panama's already high-cost labor structure. The government took over ownership and operation of all public utilities in recent years and made a few incursions into the private sector (e.g., sugar, cement), causing private investor apprehension over possible future public sector takeover in their areas of investment interest. Government price controls on a wide array of basic items, at both the wholesale and retail levels, have seriously eroded business profits by holding down prices despite rising costs. High domestic costs have also inhibited exports on which many types of productive activity depend because of Panama's small domestic market. Finally, the GOP has been unable to dispel the private investor's lack of confidence in government policy toward private business and the fear that the "rules of the game" remain subject to sudden, arbitrary change.

Panama's new government, however, has made resumption of economic growth a priority concern, recognizing the role of private sector investment in generating that growth. In an attempt to attract private investment, the GOP is considering revising current economic and labor policies and reducing the role of semi-autonomous government enterprises in the economy. Also,

the government's industrial development financing institution, COFINA, is steadily expanding its efforts to offer financial support to a widening range of profitable, new private investment opportunities in Panama.

In addition, the Canal transition offers new opportunities for private investment and, if handled smoothly and efficiently, can contribute to restoring private sector confidence.

2. Imports Dependence and Limited Exports

In keeping its tradition of serving as a funnel for world commerce, Panama has allowed goods to move in and out of the country freely, keeping import quotas for many articles at a minimum. While this obviously has benefited consumers and permitted the commercial sector (until recently) to thrive, it has served as a deterrent to the development of import-substitution enterprises, and has limited opportunities for creating additional jobs.

Panama's dependence on certain exports has also had a negative impact on its balance of payments in recent years. Panama's only resource to date for redressing trade imbalances has been attempts to increase exports of traditional, largely primary products such as bananas, shrimp, and sugar. However, the drastic drop in the world price of sugar has largely negated this effort. Panama is currently making a concerted effort to expand its exports of non-traditional (both primary and secondary) products, identify markets for them and attract needed private investment. This undertaking represents a difficult challenge, because Panama's increasingly high wage structure makes it less competitive in world markets.

3. Limited Natural Resource Base

Future prospects for productive use of the natural resource base are limited. Outside of the copper deposits in Tole, there are no other known mineral deposits with marketable potential. Poor soils and steeply

sloping terrain make this area suitable primarily for natural forest and tree crops, with some areas suitable for cattle grazing. Increasing amounts of land, however, are being converted to inappropriate uses. Forests are being cut and burned by subsistence farmers to make way for small agricultural plots. Once the soils on these lands are exhausted, the farmers move on to other areas, often leaving the land open to further misuse by cattle ranchers, generally leading to severe erosion problems.

4. Low Agricultural Productivity

There are several reasons for the low productivity of the land cultivated by Panamanian small farmers. A major reason is the use of antiquated agricultural technology, such as improper cultivating techniques, the failure to use fertilizers and proper varieties of seeds.

The annual volume of production in 1971 from a five-hectare or smaller farm yields an average income of approximately \$800 per farm (or a \$160 per capita income), in 1978 prices. The value of actual outside farm sales, however, is far below that amount. Out of a total 43,500 small farms (under five hectares) in 1970/1971, 25,000 made no sales, and 18,000 had sales of less than \$500. More recent data from a 1977 district census of 1,700 farms show 80% of the farms with no sales or sales of less than \$500.

Annual survey data obtained subsequent to the census of 1970 reveal that the area planted and the yields of rice and corn on small farms (under ten hectares) have increased. These yields, however, still remain 40 to 50% below those on large farms and the increases have been insufficient to satisfy domestic consumption needs. As mentioned earlier, Panama will have to import ever-increasing quantities of basic grains and other foodstuffs unless farm productivity improves substantially.

5. Inadequate Development of Human Resources

Low education and skill levels among the rural and urban poor are not only major causes of their condition, but also constraints to its alleviation, because these people are unprepared for employment in sectors that require a minimum of certain basic skills. Not having these skills holds down productivity by limiting opportunities for the rural poor to utilize better technologies and expand into new activities, while locking the urban poor into a limited array of employment opportunities, all in areas where wages and opportunities for advancement are low. Moreover, their deficient nutritional status is exacerbating the problem by affecting the physical and intellectual effectiveness of the poor. Since the majority of them must work in highly labor-intensive occupations, their low nutritional status impairs their physical capacity to respond adequately either on the job or in the school.

6. Isolation

The rural areas have widely dispersed populations living in many small communities isolated from the rest of the country, primarily as a result of an inadequate all-weather road system connecting them to their regional and administrative centers. Surveys reveal that small farmers consider expensive and unreliable transportation service to be the major obstacle to their entry into the money economy, thus restricting their income potential. With small farms comprising 40% of all farm families in the country, the potential income and production lost to these families and the economy is considerable. The experience of having produce rot at the roadside because of lack of timely transportation and the high cost of the transport that is provided have led to the curtailment of production of many potentially remunerative crops.

Other consequences of isolation for the rural poor are inaccessibility to agricultural extension services, production credit, grain storage/processing centers, improved seed and plant material, fertilizers, and vital social services, with all the obvious negative impacts on agricultural productivity and general well-being.

D. Host Country Plans, Commitment and Progress

Development Plan

Despite Panama's recent economic stagnation, the GOP over the past ten years has made a major, successful effort to improve the lot of the poor. The "Revolutionary Government," which has been in power since 1968, set as its general objectives a more complete integration of the country, improved social and economic conditions of the poor through income redistribution, and strengthened bases of economic growth.

To accomplish these objectives, the government substantially increased its involvement in both the social and economic life of the nation. Education and health programs were greatly expanded and extended into the provinces. An agrarian reform program was initiated, major investments in economic infrastructure were made (primarily in transportation, power, and communications) and a new labor code was instituted which was decidedly pro-labor.

The GOP's overall development strategy was formalized in its National Development Plan for 1976-1980. This plan defines development policies with respect to six major objectives and identifies the means to be employed for their achievement. These policies cover (1) increased popular participation and improved distribution of economic benefits; (2) accelerated, diversified, sustained economic growth; (3) greater regional integration; (4) more effective utilization of public finances; (5) strengthened public

sector institutions; (6) more autonomous and independent development. A new five-year development plan is currently being prepared. This is not expected to depart significantly from the above-mentioned policy objectives, but, reportedly, will incorporate a major focus on employment problems.

Performance

With strong commitment backed by significantly increased public investment, the Government has made great strides towards achieving many of its objectives. In general, the GOP's social programs have had considerable success, whereas its production programs have produced mixed results.

With regard to social objectives, progress on the national level as measured by key indicators has been impressive and is especially noteworthy for rural areas. The following table presents data on important health indicators, pointing up some results of the GOP's efforts to reduce rural/urban inequalities.

	1968		1978	
	<u>National</u>	<u>Rural</u>	<u>National</u>	<u>Rural</u>
1. Death rate (per thousand)	7.0	8.1	4.1	4.4
2. Infant mortality (per thousand)	39.6	45.9	24.8	28.0
3. % Population with potable water	66.4	37.7	82.7	63.9
4. % Population with sanitary facilities	74.7	63.2	89.2	80.1

Progress on other indicators for the national level over a similar time frame show illiteracy decreasing from 21.7% to 17.8%, the birth rate declining from 38.9 per thousand to 28.9, and population growth rate decreasing from 3.3% to 2.4% per year.

Commitment to improved access by low-income agricultural producers has been strong, but progress has been slow. The GOP has established a system of price supports and controlled marketing margins and is purchasing several basic commodities from producers to support the market for their crops. The government has supported some 200 asentamientos with over 7,000 families participating in a program which provides land title, credit, technical assistance and other services to organized groups. To date, few asentamientos have achieved financial viability, and the GOP has absorbed their losses. The GOP also has assisted the cooperative movement and other group arrangements.

Human Rights/Political Environment

Panama has had a good record of human rights progress in the last two years. After a decade-long "moratorium" on organized political activity instituted to give the "revolution" an opportunity to consolidate its reforms, as well as to maintain internal cohesion during the protracted Canal Treaties negotiation process, the political system in Panama is currently undergoing a period of liberalization.

The military leaders who assumed power in 1968 set out to bring about fundamental changes in the nation's political, economic and social structure. The GOP responded vigorously and with some success to improve the standard of living of the poor and to incorporate them into the mainstream of Panamanian social and political life.

Panama is governed under a Constitution promulgated in 1972. Under a transitory provision of the Constitution, General Omar Torrijos held broad powers as "maximum leader of the Panamanian revolution" for a six-year period. With the expiration of those powers in 1978, Torrijos retained only his position as Commander-in-Chief; nevertheless, he has continued to exert

great influence in Panamanian governmental affairs, e.g., his designees were elected President and Vice President by the National Assembly in 1978.

Under the Constitution, 505 community representatives are elected by secret, popular vote for six-year terms and constitute the National Assembly. Roughly 70-80% of the electorate participated in the elections held in August 1978. Because representatives are elected from municipal subdivisions (corregimientos), and not on the basis of population, the less populous rural districts are dominant in the Assembly. This system has resulted in greater participation in public life of the less advantaged segments of the population, giving the poor, women and indigenous minorities greater voice in the affairs of state. The representatives are essentially local officials who also serve in representative bodies at the community and provincial levels. The full potential of this representational system, however, remains to be realized. The National Assembly, although popularly elected, had exercised little substantive power until recently when it refused to ratify two bilateral treaties negotiated by the Executive. Under 1978 constitutional reforms, legislative power, except for the power of the purse, was shifted from the Executive to a National Legislative Council composed of National Assembly members. Assembly and Council members are currently pressing for greater substantive power to include review of the national budget. In 1980, a minority of the Council will be selected in direct provincial elections, with the majority appointed by the Assembly. The President and Vice President are to be chosen in direct popular elections beginning in 1984. In the meantime, real power continues to be centered around the small National Guard and the civilian Executive Branch.

Respect for civil and political liberties has increased over the last few years as a result of a series of political reforms, giving legal status to several political parties, some of which have been sharply critical of the government. As to respect for the integrity of the person, reports of degrading

treatment and arbitrary arrest do occur, but such cases are not common. The inviolability of the home is respected. In ordinary criminal cases, Panamanians have the benefit of a fair and public trial. In politically sensitive cases, however, the judiciary appears to have been susceptible to the influence of the Executive Branch. With few exceptions, labor unions are free to organize and operate, and the government frequently solicits their views, as well as the views of a broad range of non-government groups and associations, during the formulation of policy initiatives.

Panama's positive record in meeting the human rights of its citizens and genuine efforts toward giving each individual access to the resources of the nation, limited as they might be, stand in marked contrast to the poor human rights performance of many of the governments in the subregion.

Development Budget

The GOP's consolidated national budget expenditures for 1979 are estimated at \$868 million, comprising about one third of GDP. Central government revenues of an estimated \$475 million (23% over 1978) cover only current expenditures, leaving the investment program to be financed principally by foreign borrowing, as has been the pattern in recent years. Thus, the tax burden in Panama remains comparatively light. About 40% of current expenditures are taken up by interest and transfer payments. Among the ministries, the largest allocation, 18.5% goes to education. The health ministry receives 8.3% and agriculture 2.6%. An estimated 7% goes for defense spending, which, as usual, will come to less than 1% of GDP. The largest allocations in the \$393 million public-sector-investment budget for 1979 are for physical infrastructure: 18% for electricity (hydropower development) and 17% for transportation (roads, ports, airports). Agriculture received 15% and commerce and industry 8%.

Looking ahead, the GOP faces a difficult financial situation over the next few years due to its increasingly heavy debt-service burden, which is likely to limit public sector borrowing, hence its investment program. For this period, the GOP's consolidated budget is projected to expand at less than 9% annually. Since this is significantly below the assumed 13% annual growth projected for GDP (3% real plus 10% inflation), the public sector appears likely to have a negative overall impact on Panama's economic growth over the medium term.

E. Absorptive Capacity

The high level of public investment and external financing has increased the demands placed upon the public institutions. Moreover, the burden on them will increase as Panama assumes its new responsibilities in the former Canal Zone. The government's planning and project development capabilities are quite good, but there are serious weaknesses in implementation. By relative standards, the Panamanian civil servants are already among the better, though still not good enough for the high pressure and quality tasks ahead. The major causes for the shortcomings are inadequate coordination and cooperation among the different public institutions, and the overburdening of the relatively small group of qualified personnel. This cadre of competent professionals is simply too few in number and inadequately backstopped at the middle levels of service.

The assumption by Panama of new responsibilities in the former Canal Zone has exacerbated the problems of the public administration. Many experienced senior and middle-level GOP officials have moved to positions related to this new area of GOP responsibility. This has created, at least temporarily, weaknesses in a number of GOP institutions involved in development planning and administration, particularly in the Ministry of Planning. Until

new personnel gain experience, there will likely be some lessening of the GOP's ability to undertake effectively a number of developmental programs.

The GOP is aware of the challenge and has taken some positive steps to improve the administration of the public institutions. Some of these steps have been the merging of some institutions; the coordinating of government training programs; and the reorganizing of all public institutions into functional sectors. Moreover, the GOP is developing a major program which will combine administrative reform with stepped-up training of middle-level public officials.

The Mission will require rigorous institutional analysis within the context of project development, and it is likely that most future projects will contain a significant component of institutional development.

F. Other Donors

Over the past few years, other donor activity in Panama has been substantial. IFI lending reached a peak in 1977 when the IDB provided \$122 million for hydroelectric power and tourism development and the IBRD provided \$57.7 million for hydroelectric power, livestock development and improvements in the fishing fleet. Assistance from the IDB and IBRD was more limited in 1979, totalling \$62 million for university education, rural telephone systems, tropical tree crops and development banking and \$31 million in 1978 for a pre-investment fund, agricultural credit and highway maintenance. While both banks generally finance capital-intensive projects, increasing attention is being given to social projects, particularly by the IDB. Projects under development continue this mix, including support of rural roads, livestock credit, water and sewerage, urban development, and power distribution.

The UN system provided in 1978 about \$2.9 million in technical assistance, with \$1.3 million through the UNDP and \$1.6 million from the specialized

agencies. This assistance went to a number of sectors, with a concentration in the fields of health, agriculture, transportation and communications, and social and economic planning. New UN projects emphasize agriculture, industrial development, and regional planning. UNDP assistance is programmed to remain over \$1.0 million through 1981.

Bilateral programs of the DAC countries consist primarily of procurement credits and scholarships, with most programs being under \$100,000 per year, accounting for about \$1.6 million in 1977. OAS and IICA activities consist mainly of advisors and scholarships and represent about \$500,000 per year.

Donor activities are effectively coordinated in two ways. The Ministry of Planning and Economic Policy is the major counterpart agency for all donors at the policy level and coordinates all technical-cooperation activities. There are also formal and informal coordinating mechanisms among the donors which are more than satisfactory.

All major donors pursue similar objectives, employing differing but complementary means. The IDB and IBRD tend to concentrate their assistance on infrastructure projects. The UNDP, OAS and other bilateral donors focus on relatively small technical-assistance activities. The AID program fills a gap helping to assure that both the GOP and the other donors do not ignore the interests of the poor in their consideration of overall economic development needs.

IDB AND IBRD LENDING BY SECTOR
PANAMA: 1974-1979
(\$ millions)

<u>Agriculture</u> 1/	<u>Education</u>	<u>Industry</u>	<u>Power</u>	<u>Transport</u>	<u>Other</u> 2/
80.0	26.2	27.0	140.0	64.0	49.7

1/ Includes agriculture, livestock and fisheries.

2/ Includes 3 projects in tourism, rural telephones and water/sewerage.

G. Outlook

Panama's future socio-economic development picture, particularly in the short term, is uncertain. Even assuming a declining level of public borrowing in real terms and lower average rates for interest costs, continued fiscal constraints on the GOP are likely to force some shrinkage in the public sector role in the economy over the next few years, in the absence of major tax increases. When coupled with low productivity, decreased per capita GDP and income since 1973 and a slowly recovering economy, the situation worsens for certain societal groups. Many people previously at the margin of poverty will begin to fall below the poverty line due to the real decline in income and the lack of employment opportunities. The situation is particularly acute as rural-urban migration creates a dependence on cash income for family economic survival without having any of the rural in-kind benefits for support in lean times.

With increased austerity measures more likely on the part of the government, the "burden" of future job creation would appear to fall on the private sector. Unfortunately, the private sector, despite GOP efforts to foster a dialogue, seems reluctant to raise investment to previous levels or to become involved in labor-intensive industries. Moreover, this lack of confidence as regards GOP economic and labor policies is not likely to be turned around soon; meanwhile, the working-age population and the job deficit continue to increase in absolute terms each year.

Thus, increases in the real level of poverty in Panama for those dependent on a monetary economy are based on population, urbanization and economic trends evident since the mid-seventies, with short-term prospects being somewhat worse due to foreseeable increases in energy costs, lack of

substantial public and private investment, and the continued growth of the potential labor pool, especially those without marketable skills. This, in turn, points up the priority need to attack the constraints on private investment in Panama, thereby opening up the additional profitable investment opportunities and creating the new jobs essential to Panama's further economic growth and development. This approach, along with other supply-oriented initiatives aimed at raising worker productivity, especially of the least productive, should reduce unemployment to levels constituting a lesser drag on the economy and on the public sector in providing for the needs of the poor. Of particular note is the importance of preparing AID's long-term programmatic efforts to attack these structural economic problems which have the potential to undermine the long-term political and social viability of the nation.

PART II - STRATEGY

A. Long-range goals and intermediate targets

Panama has the potential to flourish as a hub of international financial, communications and trade services, to increase its level of industrialization for export and import substitution and to become more self-sufficient in food production, with a healthy balance and complementarity of roles among the Metropolitan Corridor, a dozen small cities, and rural areas. The long-range goals are to help return the Panamanian economy to a condition of sustained growth and, on this basis, to share the benefits of such growth among all Panamanians. Stated another way, the aim is to attain and sustain full employment, with the labor force, both urban and rural, gaining its fair share of the proceeds of production.

The intermediate targets are to (1) stimulate investment in job-creating enterprises, (2) increase the marketable skills of the currently unemployed and (3) bring more of the remaining rural poor into the economy. During the CDSS planning period, interventions designed to stimulate private investment and to open new employment opportunities will help ease the burden on the poor and on the economy of the most serious unemployment problems and lay the foundation for the achievement of the long-term goals. Programs to assist the rural poor build upon the momentum achieved over the past decade and hold promise for eliminating most of the extreme poverty. The combination of an institutionally focused agricultural program and geographically focused area and regional development efforts is intended both to facilitate the integration of small farm families into the economy and to secure a permanently healthy economic growth posture in the Panamanian countryside.

Given Panama's size, location and natural and human resources, we see no other way for the country to go than to aim to be a somewhat unique economy in the developing world, continuing to be strong in international financial and trade services while becoming self-sufficient in basic agricultural products, with a significant manufacturing/processing sector competitive in world trade.

B. A.I.D. Assistance Strategy

The central concerns of the AID strategy are employment and productivity. The bulk of our assistance during 1982-86 (and beyond) will be aimed at creating jobs -- in agriculture, industry and commerce; in urban and rural areas -- and at developing the human resources to fill them adequately (whether or not their creation was due to AID assistance). Employment generation will be stimulated by a combination of AID-financed GOP programs in direct support of job-creating private sector enterprises and by indirect assistance in such areas as policy analysis, technology improvement and credit expansion mechanisms.

At the same time, we will continue to pay particular attention to the agriculture sector, with interventions which can increase productivity and reduce sectoral inefficiencies. We will also provide assistance in human resources development which is aimed at upgrading the skills level of Panama's labor force and improving the ability of specific disadvantaged groups, who might otherwise receive little benefit from higher and sustained economic growth, to enter the labor market.

In the housing and urban development sector the Mission will deal with three identified problems, i.e., (1) unemployment and underemployment, (2) the inadequate shelter of many of the poor, and (3) deficient urban

planning.

Resources to be allocated for housing and home improvements will create jobs in labor-intensive construction as well secondary jobs in related activities such as building materials, furniture and furnishings, transportation and professional services. The main product of these resources will be housing, a basic human necessity and key determinant of the life quality for low-income families. These resources will also help strengthen the financial base of principal housing finance institutions and, in doing so, help moderate the drastic fluctuations to which the construction sector is subject.

The integrated development approach to housing will help alleviate urban planning deficiencies in low-income areas. In particular, AID will concentrate its efforts on strengthening the capacity of the GOP to plan, coordinate, design and implement integrated development programs that will serve the broad needs of low-income families by providing necessary infrastructure, community facilities and employment sources in addition to housing. A substantial commitment will be made to ensure that overall physical development will be based upon sound environmental, technical and financial planning. Moreover, the allocation of resources will be consistent with overall GOP policies regarding national development and its geographic distribution.

As discussed earlier, GOP price and labor policies appear to be creating disincentives, or at least reducing the incentives, for entrepreneurs to invest in Panama. In developing our programs, the Mission will carefully analyze the existing investment environment to ensure that projects undertaken will not be hampered by such policy constraints and

that technical assistance will be provided to deal with specific policy issues. We will also enlist the support of the international donors in an attempt to obtain those policy changes deemed necessary not only for the successful implementation of AID-assisted programs, but also for equitable

growth of the economy as well.

While the objectives of the strategy and the areas of concentration of AID assistance remain essentially unchanged from those of the previous CDSS, we find that a clearer understanding of the strategy is achieved by describing it somewhat differently from last year. We believe it useful to describe the proposed AID program in terms of three areas of assistance -- employment generation, asset formation and development support -- all of which are oriented toward benefitting the AID target group and which cut across normal sectoral lines.

C. Areas and Sectors of Assistance

1. Employment Generation

Our concerns about unemployment and underemployment are fundamental to the strategy. The magnitude of the employment problem is such that most of the Mission's proposed activities are designed to contribute to job creation. As described earlier, the lack of economic growth and the slump in private investment constitute the major current cause of poverty.

There is some evidence that growth has resumed, and many of the elements for a greater resurgence of private investment are already in place: government statements encourage it, assumption of Zone resources should facilitate it, there are ample tax and profit repatriation incentives,

cluding the receipt of the Canal revenues and Zone resources, will not, as noted above, suffice to create enough permanent new jobs to match the present excess labor supply, nor to keep up with its growth. What is needed is a program which will simultaneously: resolve policy constraints on private investment; systematically analyze markets for both goods and services that Panama can supply; identify entrepreneurs and match them with appropriate technologies and sources of financing and technical assistance; and ensure in all this that the focus of special concern to AID--the poor--get the training and jobs they need.

While the Mission does not contemplate a direct employment program for the agricultural sector, a successful employment strategy will indirectly create new jobs or make existing ones more remunerative in the sector, as the employed non-farm population expands and the agro-industries increase their demand for domestic agricultural production. The Mission does, however, intend to continue providing assistance to small farmers to allow them to take better advantage of the growing demands upon their production.

A strategy emphasizing employment generation for the poor, as proposed by the Mission, has several important implications for the AID program. First, it requires modification of the traditional distinction between urban and rural areas. In the Panamanian context, "urban" refers not only to the metropolitan area, but also to all the secondary and even tertiary cities found in the traditional rural areas; "rural" refers to those areas engaged in agricultural production. Second, it implies an approach which would attempt to create employment opportunities throughout Panama, wherever relatively labor-intensive opportunities can be created.

This would involve working at differing levels of technology, with higher levels required in areas with more highly specialized economic activities (i.e., the metropolitan region) and relatively simple jobs in rural areas. Third, it implies that we not limit ourselves to consideration of only labor-intensive enterprises, however defined. Relatively capital-intensive enterprises tend to be more attractive to investors, and could lead to significant employment of the target group. Such enterprises can also create a demand for intermediate inputs provided by the more labor-intensive enterprises.

The proposed employment generation strategy involves a shift of emphasis into areas where we know relatively little about how to stimulate private investment which will create large numbers of jobs for the poor. Consequently, our strategy must be two-fold: to better define and seek answers to the problem; in parallel fashion, to proceed with solutions which reflect our increasing knowledge. This process has, in fact, already begun.

a. Enterprise Development

Although the enterprise development program may eventually include projects that stimulate large enterprises, the Mission anticipates that, in the initial stages, the strategy will focus primarily on small businesses and industries within the secondary productive sector and, to a lesser degree, on those within the commerce and service sector. Small-scale enterprises tend to employ more labor than do larger units, both in terms of labor/product value and labor/capital employed; productive sector enterprises tend to create additional jobs in related activities.

AID support for small-scale industries has already begun under the ongoing IIPUP (Type C) and Rural Growth and Service Centers

projects. The former is aimed at providing, on a pilot/research basis, an integrated package of services, i.e., technical assistance, credit, infrastructure and training for small businesses in the poorest sections of the Metropolitan Area. The latter is aimed at strengthening regional/rural development through the improvement of the service delivery and employment-generating capacity of key secondary cities. We propose that this effort be expanded to additional towns (some within the Metropolitan Corridor) through a similar project to be phased in during the CDSS period. This project would insure that the whole process of intermediate city development is studied to make certain that its objectives are fully met, particularly those having to do with small farmer benefits and those relating to employment generation. These regional projects should provide employment opportunities for some of the families who would otherwise migrate to the metropolitan region.

These efforts will be complemented by an innovative project to develop agro-industries through the cooperative movement whose productive capacity the GOP and AID have spent so much time and effort developing. This project might be a good candidate for co-financing with IDB (either directly or through the Latin American Credit Union Federation - COLAC), with the possible added benefit of demonstrating new and potentially replicable financial mechanisms that could greatly increase the flow of resources into investments directly benefiting poor rural families.

The process of upgrading small businesses and industries which are concentrated in the Metropolitan Area will begin under a planned FY-1980 Labor Intensive Enterprises loan. In developing this loan, the Mission will be carrying out several studies which will help to increase our knowledge about the nature of small businesses and their problems and the

options for AID involvement in supporting these establishments. The loan, coupled with a Productive Credit Guarantee Program (PCGP) likely to be signed during FY-80, will address several key needs; technical assistance, access to technology, credit, and perhaps some entrepreneurial development. We propose to build on the experience and knowledge gained by this first effort with a follow-on loan, late in the CDSS period, designed to expand and improve delivery of these services and address other areas identified during implementation of the first loan.

Heavy involvement of many private sector groups who are beginning small-scale assistance programs for their members can be expected.

b. Investment Research and Development

Identifying and securing investments in job-creating industries on a scale sufficient to have meaningful impact on the unemployment problem is neither simple of conception nor execution; nor are the necessary institutions in place. We, therefore, propose to develop, early in the CDSS period, a program of activities to investigate, research, identify and promote new investment opportunities. This program will join the resources of the private sector and the GOP, and will have AID technical and capital (R&D) assistance.

The activities developed would emphasize economic research and have a strong applied technology orientation. The program would include adaptive research and pilot projects for technologies which have the potential to be attractive to investors and generate significant employment opportunities. Once proven, technologies would be disseminated through industrial extension services and a private sector promotion program.

The program would also implicitly require that the role and effect of government policies on private investment be continuously examined and a modest grant project would provide a conceptual framework and consultants on specific policy issues. Its long-term significance, however, would lie in the integral combination of research, extension, promotion, and policy. A key feature in this program would be the development of import-substitution investment opportunities, alternative energy sources, and food products.

c. Housing Guarantee Program

In response to the needs identified in the Part I Analysis, we propose to continue a relatively large Housing Guarantee program focused on the Metropolitan Corridor and secondary cities. The HG Program is, of course, justified on the basis of the needs of the target group for adequate shelter and related infrastructure and services. (The significance of these physical assets in terms of benefits to the poor is discussed in the following section.) The employment impact of the program is, however, not to be overlooked.

The program will finance large numbers of low cost housing solutions. The type of construction involved in such solutions is labor intensive, and the employment generated utilizes a high proportion of unskilled and low-skilled labor, i.e., the target group. The HG program will also create opportunities for small support businesses--e.g., doors, window frames, furniture--many of which may be assisted under the enterprise-development programs described above.

2. Asset Formation

The second area of concentration will be asset formation.

Here we refer to the broad range of social, physical and financial capital necessary for improving the future quality of life of the poor target group. In terms of social capital formation, we will be providing assistance in the fields of human resources development and agricultural technology. The physical capital of the poor will be enhanced by the HG program whose integrated program package of shelter, community facilities and infrastructure will be located near off-farm employment opportunities in primary and secondary urban areas. Financial capital aimed at benefitting the poor will be increased through the enterprise development, investment stimulation and HG activities.

In addition, the Mission will continue monitoring and analyzing other key target group asset deficiencies, especially those seen as key barriers in creating employment or improving productivity. For example, available data suggest that the nutrition situation in Panama is worsening with 4 out of every 7 children under five years of age being malnourished. The Mission believes that, because of the demonstrated correlation between low income, low productivity and malnutrition, nutritional status deserves further investigation. We plan, therefore, to initiate a series of cross-sectoral studies whose findings will identify the extent of malnutrition in the country and contribute to the development of a national nutrition policy. Should these findings confirm the current, incomplete data, our strategy will follow two tracks: 1) a long-term attack on poverty, the main cause of malnutrition, by generating employment and raising income; 2) a complementary series of coordinated interventions aimed at alleviating

the immediate manifestations of malnutrition. Possible program activities might include consumer education, family health, food distribution and environmental sanitation. We also plan a reorientation of the PL 480, Title II program. We will work with voluntary agencies and the Ministry of Health to expand the number of pre-school beneficiaries participating in the MCH feeding program. In addition, in those geographic areas where nutritional status is low, we plan to initiate a series of food-for-work programs. The first effort will integrate the distribution of nutritious foods with labor-intensive road construction being carried out under a current AID loan. CARE will work closely with the Ministry of Public Works and local community organizations such as health committees and housewives clubs to prepare and distribute the commodities to the workers.

We will also monitor over the long term the dynamics of population growth. Panama has had notable success in reducing its population growth rate and birth rate. The Mission's current family planning project will build upon this success by extending the coverage of clinical programs and including additional public and private sector organizations in information and education activities. It is likely that, by the time implementation of our current project is completed in 1984, there will no longer be a need for a bilateral family planning activity. We anticipate that the future needs of Panama's program can be met through such organizations as centrally funded intermediaries (e.g., IPPF, D.A., AVS) and UNFPA.

a. Human Resources Development

We propose to complement the employment-creation activities identified above with a program designed to identify and upgrade small and micro-entrepreneurial talent in Panama. Actual and potential small-scale entrepreneurs will be identified, an assessment will be carried out of their

needs, and a training program will be developed to acquaint them with the technical, legal and financial implications involved in small business and to provide them with the information necessary to link them with appropriate sources of credit and technical assistance already available through public and private sector organizations in Panama. The first step toward identifying and developing this entrepreneurial talent will be taken under one or more experimental projects planned for FY80. Planned for early in the CDSS period is a program for assisting the GOP initiate a system for continuous analysis of the characteristics of Panama's workforce in the face of short- and long-range demand for labor.

One or more follow-on programs will build on the lessons learned from the pilot activities initiated early in the CDSS period. They will also make use of the information obtained through the labor market analysis (i.e., areas in the economy where there are shortages of skilled labor; education and skills levels needed by the urban and rural poor in order to better integrate them into the job market). Pending the results of these analyses, additional programs of assistance focusing on skills upgrading, through the formal and/or non-formal system, and job placement will be launched. Special attention will be placed on training programs emphasizing the development of entrepreneurial and management skills and progressively higher technological training among the target group where appropriate.

b. Agricultural Productivity

The analysis in Part I identified low productivity as the fundamental problem of the agricultural sector, particularly of the small farm sub-sector, with government policies, low level technologies, inadequate

soils and land tenure arrangements as major contributing factors. Despite rapid urbanization, there exists and will continue to exist a significant rural core population, a high proportion of which is composed of small farmers. Given the dimension of rural poverty in Panama and the inability of the country to feed itself, the small farm poor constitute a target group which cannot be overlooked.

In this regard, the Mission will address the lack of technological and informational assets among the poor farmers through relevant agricultural research and dispersion of improved technologies. Given the almost complete lack to date of relevant research and extension capacity, this traditional approach has the greatest potential for significant early improvement in small farm productivity and income. Moreover, the increases in technological/informational capital of poor farmers are likely to have rapid spread effects which engender increased small farmer demand for such assets. Through its current Agricultural Technology Development project, the Mission has already initiated efforts to improve the GOP's applied agricultural research capability and the dissemination of improved technologies to small farmers. We plan to continue efforts in applied research and technology transfer. We also intend to develop activities related to soil conservation, on-farm storage, irrigation and credit.

Some of these and other potential activities are tentative for a number of reasons. For example, further efforts in research, credit and marketing are dependent upon the experience we will have with current Mission projects. Area development projects focused on particularly disadvantaged regions depend greatly on the directions the GOP will take with

its integrated rural development strategy, as well as with our current IRD project, which is being reformulated. The problems of inappropriate government policies and weak sectoral institutions will have to be overcome. Finally, we will need to assure coordination with the other donors (e.g., the IDB and IBRD have programmed considerable funds for the sector, including some projects in the fields of our interest).

c. Housing Guarantee Program

Housing is an important factor in improving the quality of life of AID's target group through its dual role as commodity and asset. As a consumption item, shelter has obvious health and environmental benefits for the poor, yet, in the long run, its role in financial asset formation should not be underestimated. Shelter is a positive investment/savings mechanism, a hedge against inflation, a source of future credit, and collateral for current consumption or expansion of other assets. The poor, however, constrained by legal, financial and information handicaps, have been unable to make use of the external benefits gained through housing investment as have other societal groups.

Through the HG program, we will continue to finance large numbers of low-cost housing solutions in the Metropolitan Corridor and secondary cities. The transfer of these assets to the poor will have positive effects on living conditions, employment, urban development, and the process of creating assets from within. Neither AID nor the GOP can ever supply all the financial resources necessary for long-term physical and social development. The resources must come from within the private sector, and the HG program is one part of a strategy to develop indigenous physical and financial assets. Through the IIPUP Type A program and other HG technical

assistance, support in urban and social planning will be provided in establishing the knowledge base and operational processes through which these indigenous resources can be better used. Of special concern will be improving community participation and evaluation as a means of improving the effectiveness of GOP housing programs. The shelter component will be complemented by efforts to improve infrastructure and community facilities, activities which will affect directly the quality of life of poor urban dwellers as well as permit low-income homeowners to increase their financial assets.

d. Regional Development

A key to Mission strategy is the spatial distribution of assets, particularly as secondary growth centers must be developed to meet the structural shift to an off-farm, employment-oriented economy. Besides increasing employment opportunities, these centers must become complementary engines of development on a regional basis by providing nearby farm areas with necessary goods and services. In this regard, the Mission foresees long-term involvement in regional development activities. Both the current Rural Growth and Service Center project and the HG programs dedicate substantial inputs toward improving the economic and social infrastructure at the secondary city level as part of integrated development packages (including urban planning, industrial and agri-business development, small enterprise promotion and employment creation). The direct and indirect impact on the quality of life and on socio-economic asset formation for the target group should be substantial and have important self-sustained multiplier effects. Follow-on regional development and HG programs will be developed toward the end of the CDSS period, at which time project evaluations will have contributed to refining and orienting the future development, location and appropriate mix of physical, social and financial assets.

3. Development Support

In addition to its concentration on employment creation and asset formation for the target group, the Mission will work in three specific development support areas: development administration, energy and environment. Activities in these areas will have critical long-term effects on the public and private sectors in their efforts to create sustainable sources of economic growth, make the best use of the country's natural and human resources, and avoid the negative consequences of development.

a. Development Administration

The increasing pace of urbanization, the additional administrative demands placed on the GOP under the Panama Canal Treaties, and the continued needs of the urban and rural poor make public management a crucial development support activity. Although Panama already has a competent layer of top leaders and technicians, the Government lacks the depth and specific expertise to carry out effectively its public mandate. Specifically, the public sector lacks trained middle-level managers, is constrained by an archaic administrative/personnel system, and has been unable to develop or effectively utilize the statistical information, studies and surveys required for the planning and implementation of a wide array of development projects.

The Mission has provided the GOP with a great deal of project/program-specific development administration support. Current Mission projects have provided or will provide technical assistance in the areas of municipal administration, urban and regional planning, health and education sector administrative reform, and financial management. While similar efforts will be part of future project support, the administrative shortcomings mentioned previously must be attacked on a public sector-wide basis. In this

regard, the Mission is developing an FY-1980 project to assist the GOP to improve its administrative capability for planning and implementing public sector development projects. Based on a series of studies conducted with the assistance of consultants and the Ministry of Planning, projects will be designed and implemented to: 1) reorganize present management structures; 2) develop and implement new administrative systems and procedures, especially those which are more responsive to the present and future requirements of the poor target group; 3) develop the skills of middle-level managers and planners. In addition, attention will be given to strengthening the GOP's capacity in information gathering, statistical analysis and program evaluation.

b. Environment

USAID/Panama has been in the forefront of assistance efforts to address environmental problems. The FY-1979 \$10 million Watershed Management project was designed to address specific technical and administrative weaknesses within the GOP's Natural Resources Institute and establish management programs in three major watersheds, including that of the Canal. The Mission is currently working with the Ministry of Planning on a Country Environmental Profile (CEP) which will cover the broader long-term issues and implications of environmental management. Results from the CEP will help focus a proposed environmental grant project on the detailed analysis of several environmental problem areas, which, in turn, will be used as the basis of a subsequent major environmental loan later in the CDSS planning period.

Possible areas of concentration with linkages to current and future AID programming are forestation projects in the Darien, soil conservation and reforestation in the central provinces, soil management

and erosion control in the Province of Chiriquí, and water pollution and unsanitary waste disposal in urban areas.

c. Energy

Even though major hydroelectric projects have been brought on line in recent years, Panama still depends on imported oil for 71% of its commercial energy needs. Given rapidly increasing oil costs and the technological difficulties and negative environmental consequences of switching to other non-renewable energy sources, the development of renewable, environmentally appropriate energy sources will be increasingly vital to Panama's sustained socio-economic development. Panama is blessed with abundant non-traditional energy alternatives to imported oil. There are major untapped hydroelectric sites, abundant sunlight, geothermal resources and large unfarmed areas with bio-mass production potential. AID is helping Panama to identify and develop available conversion technologies consistent with Panama's needs and resources. The FY-1979 Alternative Energy Sources grant calls for the creation of an Alternative Energy Master Plan, alternative energy feasibility studies, demonstration projects and a countrywide solar/wind data information system. AID involvement will continue with a FY-1981 loan concentrating mainly on small hydro-electric and bio-mass projects. Follow-on assistance in 1984 will likely focus on a continuation of the development of these resources and branch out into photovoltaic and other conversion technologies expected to be feasible at that time. Special emphasis throughout will be placed on meeting the energy needs of the rural poor as well as choosing technologies consistent with GOP resources and environmental policies.

PART III. ASSISTANCE PLANNING LEVEL

A. Proposed Assistance Planning Level

From the foregoing sections on Panama's economic situation and prospects, on poverty and its causes, and on the proposed USAID strategy, we conclude that a modest funding level can produce significant results. A pattern can be set which will lead to the elimination of extreme poverty in the foreseeable future, and assure that positive action is taken to resolve the problems which would otherwise continue to generate poverty. A five-year Proposed Assistance Planning Level (PAPL) of \$124 million for the CDSS period 1982-86 is the amount necessary to support the program planned to assist this resource-poor country break out of its economic stagnation and establish the bases needed to prevent the worsening of its poverty problems.

The following table presents the PAPL required to carry out the strategy presented in this CDSS. Levels significantly below those proposed would be clearly inadequate to achieve our objectives and would require a radically different strategy, likely one which would not have any serious impact on the social and economic problems of Panama.

The levels proposed would, on the other hand, meet the needs of the strategy and are within the capacity of Panama to absorb without unduly straining human and financial resources. Discussion of the specific types of assistance is presented in Part II. C, Areas and Sectors of Assistance.

PROPOSED ASSISTANCE PLANNING LEVELS

(\$ Millions)

	<u>82</u>	<u>83</u>	<u>84</u>	<u>85</u>	<u>86</u>	<u>Totals</u>
<u>Loans</u>						
<u>FN</u>						
Agricultural Productivity	6	11	5	10	-	32
Regional Development/Agri-business	-	-	11	-	8	19
Environmental Management	7	-	-	-	-	7
Nutrition Improvement	-	-	3	-	-	3
<u>EH</u>						
Workforce Development	5	-	-	-	7	12
Development Administration	-	-	-	8	-	8
<u>SD</u>						
Enterprise Development	-	12	-	4	9	25
Alternative Energy	-	-	6	-	-	6
<u>Grants</u> (all categories)	3	3	2	2	2	12
TOTALS	21	26	27	24	26	124
HG	-	25	-	15	-	
PL 480, Title II	2.1	2.3	2.5	2.8	3.1	

Justification of the PAPL

The Indicative Planning Allocation (IPA) proposed by AID/W for USAID/Panama for 1986 is a mere \$10 million, which is only \$5 million when adjusted for inflation. This compares with a program of \$19 million in FY 1979, \$21 million in FY 1978, and similar levels in previous years. Even more germane, the Approved Assistance Planning Level (AAPL) resulting from AID/W review of our FY 1981 CDSS is \$20 million in each of the years 1982-1985. A reduction of 50% for FY 1986 calls into question the logic and utility of the entire IPA-PAPL-AAPL planning system. With an IPA of \$5 million provided

last year, the Mission took exception and argued for a higher level. AID/W agreed with the Mission's position and approved a level of \$20 million. The IPA for FY 1986 seems to be inconsistent with the approved levels for FY 1981-85.

We believe the AID/W proposed IPA to be unreasonable. Not only does it imply levels during the period FY 1982-1985 which would be lower than the approved planning levels (AAPL), it also overlooks some fundamental factors which should be considered in any calculation of planning levels. In the FY 1981 CDSS, we presented our views on the inadequacy of the IPA calculation. We believe these points are of sufficient importance to repeat them in summary form.

1. The formula employed for calculating the IPA gives too much weight to mean per capita income, a highly unreliable measure of poverty. Income distribution should be factored into the calculation.
2. The IPA factor of commitment should be given more weight, as host country commitment and progress are basic requirements for any development effort oriented to the poor.
3. Modest inputs can produce highly significant results in Panama both in terms of Panamanian development and of discovering valid developmental models.
4. The absorptive capacity of Panama for AID's type of development assistance is high relative to other developing countries. Our strategy, with its elements of development administration and private sector involvement, will both increase absorptive capacity and assure a multiplier effect in the economy.
5. U.S. national interests need to have a high priority in the calculation of the IPA. Panama and the U.S. share a large variety of vital security and economic interests, most notably the Panama Canal, and Panama stands out as a veritable island of stability in a troubled region. The U.S. cannot allow prevailing economic conditions to alter this situation.

B. Staffing Implications

At the close of FY 1979, the Mission's direct-hire ceiling was 27 US (excluding 3 in the Regional Housing Office) and 60 FN. As we move to the initiation of the CDSS planning period (i.e., FY 1982), we assume a reduction in USDH over current ceiling, down to 23, with FNDH remaining essentially unchanged. During the planning period, we see the possibility of reducing gradually to 20 USDH by FY 1986, with a slight reduction in FNDH to perhaps 58. As the program emphasis shifts to those activities with which the Agency has relatively less institutional capability (employment, urban affairs, environment, higher technology enterprise development), we see less need for USDH staff and more need for specialized contract and PASA personnel, as well as increased utilization of PVOs. At the same time, we believe it crucial for the long-term to retain a FNDH staff which can provide the continuity necessary to the successful execution of the strategy. We also justify our FNDH levels on the basis of Panamanian professionals assuming ever-increasing responsibility for many of the functions normally carried out by the USDH staff. The proposed reduction in USDH would not be possible without retaining the FNDH level at a minimum of 58 positions.

USDH STAFFING LEVELS^{1/}

FY 1982 - 1986

	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>
Program Direction and Development	9	9	9	8	8
Agriculture and Rural Development	4	4	4	4	4
Human Resources Development	4	4	3	3	3
Program Support ^{2/}	6	5	5	5	5
TOTALS	23	22	21	20	20

1/ Excludes Regional Housing Office, currently with 3 positions.

2/ Includes engineering staff and one Regional Contracting Officer.