
PANAMANIAN STOCK MARKET

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PANAMANIAN STOCK MARKET

Purpose:

1. To review the appropriateness of establishing a local stock market.
2. To review the appropriateness of establishing an international stock market.

Conclusions:

1. Very little, if any, enthusiasm exists for establishing a local stock market. Certainly the government opposes.
 - a. Economies of scale are such that an efficient market would be hard to sustain.
 - b. Because equity is closely held, only corporate debt and public debt would be available for trading plus, possibly, short term money market type instruments.
 - c. The current mechanism of private placements seems to adequately serve the issues which would be considered as safe investment by the investing public.
 - d. Other than banks, the only other institutional investors are insurance companies. Their holdings are, by preference, cash or cash equivalents.
2. A study made by the Interamerican Institute of Capital lent some support to the idea of the creation of an international stock market. A careful reading of the report provides little substantive support to the supposition that such a market would be a success.
3. The only real justification for an international stock market would be in support of the international banks resident in Panama in their asset management and trust activities. The size of this market is unknown (the Banking Commission has no statistics) however, interview information indicates that no international banks manage client asset portfolios in Panama.

Recommendation:

1. Defer any studies or activities which would lead to the creation of a stock market in Panama until Capital Markets are more sophisticated. An international market would only be credible if piggy backed on an operating local market that was efficient and honest as well as well supervised by an independent authority

Constraints:

1. Since Panama is a free dollar based economy, investment funds will flow to the area of greatest safety for the greatest return. It is unlikely that any major international corporation would choose Panama as a location to float an issue. Other issues would be speculative in nature and as such would create an unstable market.
2. Without a clear advantage there is no reason to chose Panama as a trading venue.

Discussion:

1. Local Stock Market - It was the unanimous opinion of

those interviewed that not only was it too early to consider the establishment of a local stock market but that one was unnecessary. The reasons given were as follows:

a. Most Panamanian companies are family held or held by tight groups. It is unlikely that the owners would be willing to dilute their equity.

b. Term financing is currently raised by private placement of debt issues (bonds). It is felt that the current system of brokers and banks handling the private placements is adequate.

c. Tax laws discriminate against equity since interest is subject to a 5% withholding tax and dividends are subject to 10% withholding. Furthermore, traders are exempt from capital gains while investors are subject to capital gains. Therefore, there are no financial incentives to invest in equity. Any market would exist for traders and institutional investors.

d. Company management is viewed by many to be weak and undisciplined. The assumption is that the return to the investor would be poor.

e. Equity investments is considered suspect by the general public due to past scandals.

f. The capital base in Panama is felt to be too small to support a stock market.

g. The only institutional investors of any weight in the market are the banks and then only as investors for their own portfolios. However, recent changes in the trust laws may encourage local banks to enter the asset management business. Since there are no private pension plans of any note this market is not available for investing in corporate issues. Insurance companies may invest in corporate debt and equity but the rules surrounding these investments serve as disincentives. Some insurance companies do have small portfolios of corporate issues but it is limited. The favored investment of insurance companies is deposits with banks which have only minimal tax liabilities (Investments in bank CD's are tax free)

h. We have been given to understand that the World Bank as suggested that the government of Panama again issue bonds. Should this come to pass it is unlikely that any other investment would be able to compete since these issues would be priced at world market rates, denominated in dollars, be tax free and guaranteed by the full faith and credit of the Panamanian government.

2. An International Stock Market -

a. Most international stock markets that developed during the 60's and 70's were piggy backed on existing local exchanges that had established reputation for honesty and efficiency with good oversight by independent regulatory bodies. In fact there technically is no such thing as an international exchange what does exist is foreign issues traded and occasionally floated on local exchanges either in local currency or in the home currency of the issuing corporation or, on occasion, in a third currency. Absent a

tested infrastructure it is hard to see how trading in international issues would develop in Panama.

b. The two principal markets for an international exchange would be:

1. Asset management departments of foreign banks resident in Panama.

2. Flight capital - ie. capital seeking political asylum, tax avoidance or inaccessibility by home country law enforcement authorities.

Foreign banks do not currently have asset management operations in Panama. It is unlikely that they could be developed in a large scale since most banks prefer to handle these activities in their home offices (excepting, of course strictly local currency activities for local customers).

Given the other well established havens for flight capital it is unlikely that this alone is a good enough reason to supports an stock market in Panama.

SHOULD IT BE DECIDED TO PROCEED WITH A STOCK MARKET STUDY A SUGGESTED TERMS OF REFERENCE IS ATTACHED.

PANAMA STOCK MARKET STUDY - TERMS OF REFERENCE

Description of services:

1. Determine the feasibility of creating and developing an international financial instruments exchange (the exchange) in Panama.

Evaluation and Award:

The selection of the advisor will be based on the following criteria:

- a. Advisors' experience in the International Capital Markets with special reference to Latin American financial markets.
- b. Expertise of the advisor's personnel to accomplish the financial aspects of the work statement. An estimate of approximate man hour requirements should be included in the proposal.
- c. Technical soundness of advisor's plan for accomplishing the requirements of the work statement. Offerors will include sufficient descriptive material on their methodology, sources of information to be consulted, schedule for completion of the project, and extent of proposed visits to Panama and other locations.
- d. Total cost

Work statement

1. Prepare a feasibility study that examines the following points:
 - a. Identify and quantify target markets for the exchange
 - b. Identify competing markets
 - c. Identify the reasons why Panama is a better alternative/environment than competing markets (tax - secrecy communications, etc.)
 - d. Determine whether a Panamanian stock exchange could be the venue for the trading of Latin American foreign debt
 - e. Assess possible participation of companies from Latin America in the exchange (both as issuers and traders) and identify any legal limitations which may exist (ie issuing dollar denominated instruments).
 - f. Evaluate negative factors affecting the creation and management of an exchange (poor supervisory infrastructure, unstable legal climate, possible government interference, etc)
2. Prepare a final report that incorporates all requested points and any additional considerations of the advisor.