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The Agency for International Development
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Central American Capital Markets
Panama: Macro-Financial Background

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Introduction

Panama is currently recovering at a reasonable pace from a political and economic crisis that had been developing for several years but only became strongly disruptive in 1988 and lasted until mid 1990. This crisis revealed clearly the major extent of internal and external political conflicts.

The internal political crisis allowed a growing participation by the armed forces in the administration of the Panamanian Government. Political freedom was restricted and election results were not acknowledged, with the apparent intention of perpetuating the power of a military elite. The external political crisis arose after a confrontation with the United States Government that resulted in economic sanctions that aggravated the overall crisis. Public outlays were used for political purposes, and widespread corruption in the administration of the country produced civil unrest affecting civil liberties and private property.

Panama's problems cannot, however, be attributed exclusively to this recent crisis. The fundamental problems have their origins in several decades of a misguided approach to economic development. Some of the main results of this misguided approach, which are presently inhibiting growth, are:

- the lack of a well organized securities market able to mobilize savings and channel them to productive investments or to allow the trading of a significant volume of securities;
- the lack of participation in capital markets by large public utility companies providing energy, transportation and communications -- such companies are usually leading providers of instruments traded on securities markets -- because these enterprises are state owned and operate at low levels of efficiency; and
- government intervention throughout the economy due to an ideological persuasion that the private sector can produce neither an efficient allocation of resources nor a reasonable distribution of income.

In spite of the lack of a securities market, the existence of distortions in labor markets with rigidities created in particular by restrictive labor legislation issued at the beginning of the 1970s, and restrictions on international trade, the Panamanian economy nonetheless managed to achieve some growth. In fact, prior to 1982 the economy had attained rapid growth based in its unique geographical location -- situated on a narrow isthmus between North and South America. The Panama Canal worked well as a leading sector, allowing the development of commercial and financial sectors that serviced the rest of Latin America.

The international debt crisis that started in 1982 reduced Panama's financial role and, as in many other countries in the region, its external debt burden increased and its economic growth slowed. From 1984 to 1987 there was some recovery, but the major problems continued to be present, and few measures were taken to improve resource allocation in any fundamental way.

The 1988 crisis evolved with fiscal disarray, which in turn led to a suspension of debt payments and the freezing of deposits in the banking system. After the United States' invasion in December 1989, a new government took office that reduced the power of the military and introduced some fiscal discipline. Beginning in 1990, payments on debts owed to international financial institutions were again made, and talks have begun or rescheduling the debts owed to commercial banks and bilateral lenders. Substantial economic assistance has come from the United States which, jointly with multilateral organizations, is studying proposals for clearing Panama's arrears so that lending activities can be resumed.

In addition to the recent crisis, Panama has always been a special case among Latin American countries because Panama does not have its own currency. The Balboa is pegged one to one to the United States dollar, and Panama's constitution forbids the issuance of fiat money as legal tender. This has various important implications for the potential development of its capital market.

- First, there is no possibility of currency substitution between local and foreign currencies. Accordingly, the holding of any kind of domestic financial instrument is not exposed to exchange rate risk. Moreover, full integration of its capital market, including free capital mobility, also avoids changes in the value of domestic financial assets resulting from changes in domestic interest rates. Changes in domestic interest rates are fully determined by international rates except for the country risk premium, so that -- apart from country risk -- the asset value of Panamanian financial instruments fluctuates according to international interest rates.

- Second, since the Panamanian Government cannot print money, it cannot collect seigniorage or inflation tax revenues to finance its fiscal deficit. The public sector deficit has to be financed either by raising taxes or by issuing public debt, either domestic -- such as government bonds, loans from the Banco Nacional de Panama (BNP) or arrearages (floating debt) to government suppliers -- or foreign with international donors or commercial banks. Wealth holdings in domestic financial instruments cannot be taxed through the inflation tax, as happens so often in most other Latin American countries. This is an important advantage for capital market development. Nonetheless, Panamanian financial instruments are heavily taxed through the income tax, as discussed more fully in later sections of this report.

- Third, Panama lacks monetary autonomy in the sense that its money supply is entirely determined by the demand for money, thereby implying that prices of Panamanian financial instruments are driven by United States' monetary policy together with Panamanians' demand for money balances. Accordingly, restraint in the growth of the United States' money supply will imply a reduction in the prices of Panamanian financial assets -- just as if Panama were another state. On the other hand, a once and for all increase in the demand for money balances by Panamanians reflected by a capital inflow -- as recently happened -- will bring down interest rates (i.e., push up the prices of Panamanian financial assets). As financial instruments in Panama are still poorly developed, the way that this capital inflow took place was through an increase in deposits in the banking system, stimulated in large part by reduced perceptions of country risk. These capital inflows were also the result of more conservative bank lending policies, thereby forcing Panamanians to bring back their own funds to finance a higher level of transactions.

Nonetheless, the Panamanian case is not fully consistent with capital market development, as freedom of capital flows is not sufficient for total mobility of goods and factors. The inconsistency between capital market integration and high trade barriers, the latter more fully discussed in other parts of this report, undermines the growth potential of the productive sectors -- and these productive sectors should be the leading providers of instruments to be traded in Panamanian securities markets.

As a small open economy, Panama should grow not only on the basis of its service sector (e.g., commercial and banking services associated with the Panama Canal) but also by developing its tradeable export sector. Prices, as signals for allocating resources in an economy, are the same as international prices, except for the tariff regime. However, the prices of non-tradeables are increased by high tariff protection, so that inflation can deviate from the rate in the United States and the real exchange rate can be affected. Accordingly, the production of tradeables is discouraged by high import tariffs, while exports cannot be stimulated through a higher real exchange rate because the lack of monetary autonomy does not permit devaluation.

Panamanian price indices suggest that inflation in Panama has been lower than inflation in the United States since the mid 1980s. Taken at face value, this suggests that Panama has achieved a real effective devaluation which should have had a favorable effect on Panama's international competitiveness and on its trade balance. However, theory suggests that significant deviations between inflation in Panama and in the United States would occur only if there have been changes in trade regimes -- which would call into question possible effects on international competitiveness. Alternatively, there could be inaccuracies in the measurement of inflation in Panama (e.g., due to inappropriate weights in price indices as often occurs in developing countries). In any case, differences in inflation rates have not been great enough to imply meaningfully higher real interest rates in Panama.

Notwithstanding its fully open capital account and its well developed banking system, saving performance and investment have deteriorated sharply in Panama during the 1980s. Table 1 shows the evolution of the investment-saving process over the past ten years. The main issue that emerges from these figures is the persistently declining rate of investment in Panama since 1982, probably originating at least in part with the Mexican crisis. Although the Panamanian economy began to recover during the 1984-87 period, this was followed by the political crisis and the major confrontation with the United States already discussed. During 1988-89, investment declined even further, reaching a minimum of 2.6 percent of GDP in 1989. Table 1 provides the figures on gross domestic investment, gross national saving and foreign saving for Panama during the 1980s.

The impact of rising debt service -- negative net factor income associated with high public-sector external indebtedness -- together with deteriorating terms of trade (see Table 2) undermined national saving capacity and the availability of resources for investment. The 1988-89 crisis sharply reduced revenues from United States owned corporations and from the Panama Canal. In spite of reductions in public expenditures, public sector savings became negative, and there was a systematic reduction in the availability of resources for public investment. As the Panamanian Government does not have the ability to levy an inflation tax, and foreign credit was simultaneously restrained, the increased public sector deficit had to be financed by:

(1) the accumulation of foreign and domestic debt service arrears;

(2) increased borrowing from the BNP; and

(3) payments arrears to domestic suppliers, a mechanism through which the public sector forced the private sector to save to compensate for public dissaving.

Private sector saving thus grew at the expense of a sharp decline in both consumption and investment. Table 1 shows clearly that the private sector has been permanently in surplus, reflecting persistent deflationary conditions and the lack of investment opportunities in Panama, as well as public sector dissaving.

Table 1
The Saving - Investment Process
(percent of GDP)

	Gross Domestic Investment			Gross National Savings			Foreign
	Private	Public	Total	Private	Public	Total	Savings
1980	20.3	7.4	27.7	14.6	3.7	18.3	9.4
1981	21.6	8.5	30.1	15.8	4.2	20.0	10.1
1982	18.2	9.5	27.7	15.9	1.2	17.1	10.6
1983	13.1	8.3	21.4	12.8	2.9	15.7	5.7
1984	9.8	6.9	16.7	11.2	2.5	13.7	3.0
1985	10.6	4.8	15.4	9.3	3.2	12.5	2.9
1986	12.6	4.1	16.7	14.0	3.5	17.5	-0.8
1987	13.8	3.6	17.5	14.2	3.0	17.2	0.3
1988	4.6	2.3	6.9	21.3	-9.2	12.1	-5.2
1989	0.9	1.7	2.6	12.9	-10.3	2.6	0.0
*1990	14.8	1.5	16.3	8.9	-1.8	7.1	9.2
**1991	13.5	2.5	18.0	-0.2	10.3	10.1	5.9

*Estimated values for 1990
**Projected values for 1991

Source: Elaborated on the basis of World Bank Report Statistical Tables (1990).

Table 2
Some Determinants of National Saving
(percent of GDP)

	National Saving	GDP Growth	Net Factor Income	Terms of Trade
1980	18.3		-4.5	81.2
1981	20.0	4.2	-7.1	79.7
1982	17.1	5.5	-8.2	74.9
1983	15.7	0.4	-7.4	77.2
1984	13.7	-0.4	-6.3	80.9
1985	12.5	4.7	-7.6	84.4
1986	17.5	3.4	-6.4	87.2
1987	17.2	2.3	-6.0	80.7
1988	12.1	-15.6	-8.7	77.0
1989	2.6	-0.9	-9.6	

Source: Elaborated on the basis of World Bank Report Statistical Tables (1990).

After the new Panamanian Government took office in December 1989, the situation changed substantially. Confidence in the country was largely restored, which led to a huge capital inflow and a significant recovery in economic activity (GDP grew by almost 4 percent in 1990). In addition, as noted elsewhere in this report, payments to international donors related to arrears have been made since April 1990, and a foreign debt rescheduling was reached with the Paris Club under a conditional agreement with the IMF. A new budget was passed that maintains a deficit of 2 percent of GDP but nonetheless includes substantial amounts of rehabilitation investments. Although the Panamanian Government still faces serious financial constraints -- both domestic and foreign -- the foreign position of the BNP has improved significantly as a result of capital inflows.

Financial deepening -- measured by the ratio of domestic deposits to GDP -- has evolved in a way similar to savings, declining from a peak of 82.6 percent in 1981 with the Mexican crisis and recovering somewhat by the end of 1986. However, deposit mobilization was dramatically affected by the subsequent political crisis, together with the revealing of information about "laundered dollars" in Panama's banking system, which caused a sharp contraction in both domestic and foreign deposits. Deposits fell below their 1980 level (see Table 7 below), and financial deepening reached a minimum of 62 percent at the end of 1989.

Deposits in the banking system have recovered rapidly, and deposits from Panamanians have already regained their level before the crisis. Interest rate differentials compared to international levels, the return of confidence, and the recapitalizations that banks achieved with their own efforts were instrumental for this result. Non-resident deposits have also begun to recover, but even with higher interest rates in real as well as nominal terms it has not been possible to regain the levels before the crisis. According to the opinions of Panamanian bankers, confidence will not be fully restored until a Treaty of Mutual Legal Assistance is signed between the Governments of Panama and United States, as happened with other financial centers such as Switzerland and the Cayman Islands. In any case, drug-related dollars are not expected to reflow to Panama, so that it will take a long time for the banking system to regain its previous level of non-resident deposits.

Although certain good results have been achieved since the new Panamanian Government took office, there is nonetheless a widespread perception of inactivity and lack of ability by the Government to address key structural problems such as reducing the size and inefficiency of the public sector, changing the tariff system to reduce protection and eliminate distortions, and removing wage and price restraints. In addition, delays during 1991 in implementing policy reforms have increased concerns about the fiscal deficit, the prospects for clearing external arrears and whether new external capital inflows will be forthcoming. Most importantly, however, from the long-term perspective, as long as the system of incentives is not changed to promote growth, it will be difficult for the saving-investment process to recover, and this is a major constraint limiting capital market development.

The Fiscal Deficit and Its Financing

During the 1980s, the Central American economies decreased their public expenditures, with the exception of Nicaragua and Panama until 1987. In most of these countries the slowdown in public outlays was due to external restrictions against increased foreign indebtedness, but in Panama indebtedness continued to be the main source that allowed a high level of government spending to be maintained. During 1988 and 1989, however, the precarious financial situation of the country meant that drastic reductions in government expenditures had to be undertaken. This, however, was not an easy task, and in many cases government expenditures were financed by accumulating debts to local suppliers and by not paying public agencies for services provided.

At the beginning of 1990, the Panamanian Government imposed temporary expenditure ceilings to gain time to prepare a budget, which was approved by the National Assembly in April. These ceilings, together with higher government revenues -- mostly due to the lifting of economic sanctions -- resulted in a significant improvement in public finances. This improvement in turn permitted a decline in net credit from the BNP to the nonfinancial public sector.

A significant part of the improvement in the fiscal situation was due to the resumption of payments from the Panama Canal Commission, which allowed 1990 government outlays to be funded without a large increase in tax revenues. Since part of the 1990 payments from the Canal Commission were for arrearages, and hence are an extraordinary source of revenue that will not be available in future years, there is need for a significant increase in tax revenues, especially since an increase in government indebtedness is not possible (and would not be advisable even if it were possible).

Current outlays of the Panamanian Government declined in 1990, mostly as a consequence of a reduction in the wage bill and other current outlays that more than compensated for the increase in purchases of goods and nonpersonal services. The government reduced excess personnel, particularly in the military, and extended the suspension of the thirteenth-month salary bonus. In addition, the government cut the maximum level of public sector salaries and limited the remuneration of newly-hired employees to 90 percent of what had been paid to employees already holding such jobs.

The Government of Panama has, in addition, developed an IMF-monitored program with the intention of beginning to normalize its relationships with international financial institutions and other external creditors. This program includes a reduction of the nonfinancial public sector deficit from 11 percent of GDP in 1988-

89 to 7 percent in 1990 and to about 5 percent in 1991. As indicated above, this fiscal adjustment is to be achieved through continuing improvements in public sector revenues and sustained restraint in current expenditures. Public sector revenues are estimated to have increased from an average of 24 percent of GDP in 1988-89 to about 27 percent in 1990 and are projected to be 28.5 percent in 1991. Current expenditures are estimated to have declined from an average of about 34 percent in 1988-89 to 31.5 in 1990 and are projected to be 30 percent in 1991. (See Table 3.)

The fiscal adjustment producing these results includes:

- o the strengthening of central government cash revenues and restraint in current and capital outlays;
- o the resumption of payments of taxes, dividends, and other items that were suspended with the economic sanctions of 1988-89; and
- o an increase in the operating surplus of public enterprises from an average of 2.75 percent of GDP in 1988-89 to a projected 4.5 percent of GDP in 1991, mainly through tightening collection procedures and reducing the unregistered expenditures and uncollected bills of public utilities.

Financing of the deficit for 1990 was covered by the use of unblocked funds, a portion of the United States aid package, a rescheduling of interest obligations in the context of the Paris Club, and the accumulation of external interest arrears to commercial banks and other non-guaranteed debt to private creditors. In 1991, financing of the deficit will require further rescheduling of interest with the Paris Club and commercial banks, along with gross disbursements from multilateral institutions. It is expected that the government will reduce its debt to the BNP, as well as other domestic debt, in 1991.

The new government's approach to economic development is based on the view that Panama's future economic growth will be generated largely by the private sector. Therefore, the government has established a Privatization Commission, including private sector organizations and labor unions, to identify activities to be transferred to the private sector. However, the progress of this commission and the overall privatization process has been very slow until recently. Nonetheless, there seems to be a trend in public opinion in favor of privatization after the marked failure of several decades of public sector dominance of various economic activities. Privatization is currently being considered for several public enterprises in agriculture, insurance, transportation, tourism and trading.

To finance its investment program, the Panamanian Government has traditionally turned to international and bilateral lending agencies and the Eurocredit market. Public utilities and large companies have not issued securities because many of them are government owned or closely held and also because of the lack of a domestic securities market. The absence of such a market, together with the openness of the financial system, has left the Panamanian Government with few instruments for domestic financing of the government.

An important source of government finance in many countries is to increase reserve requirements on the banking system. In countries with fiat money this is usually done in the following way. First, the central bank issues money to finance the government, and then, to inhibit the acceleration of inflation, the central bank increases reserve requirements to sterilize the monetary expansion. Another way of doing the same thing is first to introduce an increase in reserve requirements and then to allow special government debt instruments to be counted as part of required reserves.

In Panama, reserve requirements cannot be used to sterilize increases in credit to the government because the openness of the financial system would jeopardize the existence of Panamanian banks. Reserve requirements higher than international standards would make it impossible for Panamanian banks to compete because higher reserve requirements imply higher spreads.

Comparing the inflationary performance of Panama with countries having a wide array of instruments to carry out monetary policy leads to the conclusion that there is no clear advantages from having a large number of instruments that may induce the government to borrow heavily in domestic financial markets. In many countries, government debt is a major source of inflation as the government eventually has to rely on monetary emission to pay the interest on such debt. This does not mean that a securities market is unimportant, but rather that the main impetus for the development of a securities market should be the creation of private securities rather than government debt.

Table 3
Government Finances

Panama: Operations of the non financial public sector (In millions of Balboas)	1988	1989	Budgeted 1990	Projected 1990	Projected 1,991
REVENUE AND GRANTS OF CONSOLIDATED PUBLIC SECTOR	1,072.8	1,088.0	1,297.1	1,302.4	1,514.1
General Government	940.2	928.7	1,122.0	1,132.3	1,253.0
Central Government	569.3	529.8	728.6	738.9	831.0
Social Security Agency	335.9	362.9	346.5	346.5	371.0
Decentralized Agencies	35.0	36.0	46.9	46.9	51.0
Operating Balance of Public Enterprises	104.2	138.6	154.1	149.1	234.1
Balance of nonconsolidated Public Sector	28.4	20.7	4.2	4.2	10.0
Grants	0.0	0.0	16.8	16.8	17.0
EXPENDITURES OF CONSOLIDATED PUBLIC SECTOR	1,550.0	1,582.0	1,703.8	1,639.8	1,775.2
CURRENT EXPENDITURES OF GENERAL GOVERNMENT	1,490.6	1,551.2	1,552.1	1,534.3	1,584.8
Central Government	983.5	1,015.1	984.1	966.3	988.8
Social Security Agency	425.5	461.5	481.3	481.3	506.0
Decentralized Agencies	81.7	74.6	86.7	86.7	90.0
CAPITAL EXPENDITURE	59.4	30.8	151.7	105.5	190.4
PUBLIC SECTOR SAVINGS (1)	(417.8)	(463.2)	(255.0)	(231.9)	(70.7)
OVERALL CASH SURPLUS OR DEFICIT (-)	(477.2)	(494.0)	(406.7)	(337.4)	(261.1)
ACCRUED REVENUES BLOCKED ABROAD	164.8	185.2	0.0	0.0	0.0
OVERALL ACCRUED SURPLUS OR DEFICIT (-)	(312.4)	(308.8)	(406.7)	(337.4)	(261.1)
FINANCING	312.4	308.8		337.4	261.1
External (net)	49.2	15.4		25.4	373.2
External Interest Arrears	354.0	402.6			
Domestic Arrears	107.9	34.0		(51.0)	(30.0)
National Bank	(0.5)	42.0		0.0	(29.7)
Blocked Funds Abroad	(164.8)	(185.2)		350.0	0.0
Other	(33.4)	0.0		13.0	(52.4)

Panama: Operations of the non financial public sector (Percent of GDP))	1988	1989	Budgeted 1990	Projected 1990	Projected 1991
Public Sector Revenues and Grants	23.7	24.1	26.7	26.8	28.7
General Government Revenue	28.0	20.6	23.1	23.3	23.8
Operating Balance of Public Enterprises	2.3	3.1	3.2	3.1	4.4
Public Sector Expenditure	34.3	35.1	35.1	33.8	33.7
Current Expenditure of the General Government	33.0	34.4	32.0	31.6	30.0
Capital Expenditure	1.3	0.7	3.1	2.2	3.6
Public Sector Savings	(9.2)	(10.3)	(5.3)	(4.8)	(1.3)
Overall Deficit (-) Cash Basis	(10.6)	(11.0)	(8.4)	(7.0)	(5.0)

Source: Statistical Appendix.

The Foreign Exchange and Trade Regimes and the Balance of Payments

As already mentioned, Panama's Constitution forbids the issuance of fiat money as legal tender. The Balboa is the national currency that circulates only in the form of coins, while the United States dollar circulates as paper money and is used as the unit of account for both domestic and external payments. There is no exchange rate policy other than maintaining the convertibility of coins in agreement with the Constitution. Trade with the rest of the world is mostly carried out in United States dollars, but under a system where import protection and export promotion prevail in almost every sector of the economy.

Protection for domestic agriculture and manufacturing is high on the average, as is the dispersion of tariffs. According to World Bank estimates, the unweighted average tariff in Panama is about 33 percent, with maximum tariff rates reaching 270.5 percent for agriculture and 257.5 percent for manufacturing. Tariff rates can be even higher in some case as specific tariffs may be substituted rather arbitrarily for ad valorem tariffs. In addition, tariffs on consumer goods are higher than those on intermediate goods, and these in turn are higher than tariffs on capital goods. Production-weighted nominal protection of manufacturing is well above unweighted protection and, together with tariff exemptions on inputs, establishes high rates of effective protection for import substitution industries. In fact, the production-weighted average tariff is 67 percent, while the import-weighted tariff is only 25 percent. In addition, agricultural products such as rice, corn, onions, milk, butter and vegetable oils are subject to quota systems that further restrict trade.

Non-traditional exports, as well as fruits and vegetables, fall under special promotion laws that fully exempt inputs from import tariffs. These products are also exempted from corporate income taxes, production taxes, sales taxes, and taxes on assets. In addition, Tax Credit Certificates, equal to 20 percent of the value of export production, are given to firms with domestic content of at least 20 percent of manufacturing costs and domestic value added of at least 20 percent of the value of production. These Tax Credit Certificates are nominative, transferable, and can be used to pay any tax. However, they do not yield interest and are payable in 9 months (50 percent) and in 18 months (50 percent). In spite of several decades of such policies of export promotion -- attempting to compensate for policies of import substitution -- the non-traditional sector remains small, accounting for only about 9 percent of total exports of goods and services.

The characteristics of Panama's crisis (i.e., cut off from external funds) resulted in Panama running a current account surplus during 1988-1989 as a reflection of its fiscal situation. However, preliminary estimates indicate a current account deficit of 3.75

percent of GDP for 1990, and under the IMF shadow program (see Table 4) a current account deficit of 3 percent of GDP is projected for 1991. The deficits for 1990 and 1991 are largely due to increased imports associated with a recovery of public and private investment and are being financed by capital inflows.

Table 4
Balance of Payments

PANAMA: BALANCE OF PAYMENTS (In Millions of U.S. Dollars)	1986	1987	1988	1989	Projections 1990	Projections 1991
CURRENT ACCOUNT	40.2	(16.4)	291.9	35.1	(183.8)	(160.1)
Balance of Goods and Services	(54.9)	(80.9)	206.8	(34.4)	(255.4)	(234.5)
Trade Balance	(767.7)	(798.3)	(429.7)	(603.3)	(812.9)	(903.9)
Exports, FOB	359.4	367.3	304.7	316.5	330.0	382.9
Imports, FOB	(1,127.1)	(1,165.6)	(734.4)	(919.8)	(1,142.9)	(1,286.8)
Freight and Insurance	11.3	15.3	48.2	(11.4)	(23.2)	(34.4)
Transportation	372.6	383.0	392.4	379.6	390.6	444.3
Travel	121.8	98.1	79.8	76.1	89.4	111.7
Investment Income	(330.5)	(320.1)	(406.2)	(442.6)	(496.8)	(500.8)
Of which: public debt interest	(324.1)	(309.3)	(366.0)	(407.3)	(430.1)	(427.3)
Other Services	537.6	541.1	522.3	567.2	597.5	648.6
Colon Free Zone	228.6	248.1	231.6	263.7	285.2	308.5
Rest of the World	309.0	293.0	290.7	303.5	312.3	340.1
Unrequited Transfers	95.1	64.5	85.1	69.5	71.6	74.4
CAPITAL ACCOUNT	(260.2)	(925.5)	(1,575.7)	(802.2)	518.2	(70.3)
Official Capital	(287.6)	(462.5)	(734.2)	(613.6)	533.4	(124.4)
Nonfinancial	(282.5)	(418.9)	(723.1)	(593.5)	433.9	(120.4)
Drawings	195.6	89.5	57.3	2.5	413.0	155.0
Repayment	(481.1)	(508.4)	(615.6)	(460.9)	(279.1)	(275.4)
Blocked Funds.	0.0	0.0	(164.8)	(135.2)	300.0	0.0
Official Bank, other long-term foreign liabilities	(5.1)	(43.6)	(11.1)	(20.1)	99.5	(4.0)
Private Capital.	27.4	(463.0)	(841.5)	(188.7)	(15.2)	54.1
OVERALL BALANCE	(220.0)	(941.8)	(1,283.8)	(767.1)	334.4	(230.4)
Financing	220.0	941.8	1,283.8	767.1	(334.4)	230.4
Banking System Net Foreign Assets (increase -).	(146.9)	391.3	190.8	(179.7)	(438.8)	(250.0)
Rescheduling.	366.9	407.8	(385.6)	0.0	142.9	230.4
Arrears	0.0	142.7	1,478.6	946.8	(38.5)	250.0

Sources: IMF and Office of the Comptroller General.

Preliminary estimates indicate an increase in imports of 20 percent in 1990 and 10 percent in 1991 as part of the first stages of trade reform. Exports, which grew moderately in 1990, are expected to grow rapidly in 1991 when the benefits from the reopening of the United States market to Panama's sugar and other agricultural exports will largely be felt.

The capital account, after large net outflows in 1988-89, changed to a surplus in 1990 as a consequence of the release of blocked funds in the United States, the disbursement of the United States aid package, and other official disbursements linked to the expected elimination of arrears to multilateral institutions. Under the IMF shadow program (see Table 4) the capital account in 1991 is projected to revert to a small net outflow, as scheduled repayments of public debt will more than offset official bilateral flows, disbursements from multilateral institutions, and private capital inflows.

Panama's authorities are in the process of normalizing relations with external creditors, starting with payments to multilateral institutions to settle arrears. In 1990, external debt service obligations (principal and interest) amounted to US$ 788 million. For 1991, debt service is US$ 755 million, or about 14 percent of GDP (see Table 5), but is expected to be lower in later years.

Table 5
External Arrears

PANAMA: EXTERNAL DEBT ARREARS AS OF END 1989 AND DEBT SERVICE 1990-91 (In millions of U.S. Dollars)	Stock of Arrears end-1989	1990 Principal	1990 Interest	1990 Total	1991 Principal	1991 Interest	1991 Total
TOTAL	2,706.8	357.9	430.1	788.0	328.1	427.3	755.4
Multilateral Institutions.	547.2	172.9	108.2	281.1	142.9	74.1	217.0
IMF	217.7	78.7	35.0	113.7	52.8	9.9	62.7
World Bank	177.5	50.9	36.5	87.4	51.1	24.1	75.2
IDB	147.6	41.3	34.6	75.9	37.0	27.4	64.4
IFAD	4.4	2.0	1.4	3.4	2.0	1.1	3.1
New Disbursements	0.0	0.0	0.7	0.7	0.0	11.6	11.6
Bilateral	281.2	30.4	44.5	74.9	39.2	52.6	91.8
Of which: on new disbursements	0.0	0.0	3.8	3.8	0.0	9.9	9.9
Commercial Banks	1,848.5	143.0	269.4	412.4	134.6	292.2	426.8
Suppliers' Credits	29.9	11.6	8.0	19.6	11.4	8.4	19.8
Memorandum Items (In percent)							
Debt Service/GDP				16.2			14.3
Debt Service ratio				43.7			38.3

Source: IMF.

Normalization of relations with other official and private creditors is expected to continue during 1991 under Paris Club type agreements and through contacts with the advisory committee of private commercial banks. As a consequence of severe payments constraints, no significant payments to commercial banks were made in 1990, but some modest payments are expected in 1991. For the future, under a formal program with the IMF, Panama's Government can be expected to seek enhancements, including set-asides, for conducting commercial bank debt and debt service reduction operations.

Inflation, Interest Rate Policies, and Domestic Credit Policies

By Latin American standards, Panama is one of the most stable countries due to its particular currency system, based on free circulation of the United States dollar. During the period 1975-90 the average annual inflation rate was 3.2 percent in terms of the consumer price index and 6.4 percent in terms of the wholesale price index (see Appendix). Most of the variation in the price level is related to changes in international prices and, secondarily, to changes in commercial policy that result in variations in the prices of both traded and non-traded goods from international prices.

The openness of the Panamanian financial system has ensured liberal interest rate policies to allow Panamanian banks to compete in deposit and credit markets. However, some restrictions exist: (1) interest on demand deposits is prohibited; and (2) savings deposits below US$3,000 have interest rate ceilings of 4.5 percent for commercial banks and 5.5 percent for saving banks. Interest rates on time deposits and loans are uncontrolled, and deposit rates (shown in Table 6) are closely related to LIBOR. Credit is largely allocated according to market signals instead of a regulatory framework. Panamanian Governments have, however, attempted to direct credit to priority sectors with special programs for housing and agriculture at subsidized interest rates (about half the market lending rate) with the subsidy being financed by a levy of 1 percentage point on domestic consumer and commercial loans.

Table 6
Term Structure of Interest Rates

	Term Structure of Interest Rates		
	Dec. 1989	June 1990	Sep. 1990
Three-Month Time Dep.			
Domestic Banks	8.5	8.9	9.2
Foreign Banks	7.1	7.5	7.4
Six-Month Time Dep.			
Domestic Banks	8.6	9.1	9.6
Foreign Banks	6.4	7.8	7.6
Twelve-Month Time Dep.			
Domestic Banks	10.5	10.2	10.2
Foreign Banks	6.8	8.6	8.0

One great advantage of Panama's currency system, as already mentioned, is that it provides an effective constraint on the government's ability to finance the non-financial public sector deficit through money creation. Chronic inflation in most developing countries is fundamentally a monetary phenomenon resulting from central bank financing of government deficits. The existence of fiat money allows the central bank to print what is necessary to provide "advances" to the treasury, and this transitory financing almost inevitably becomes permanent, thereby producing a sustained increase in the monetary base leading to inflation. In Panama, the BNP finances the government, but the source of this financing is deposits in United States dollars at the bank rather than a printing press. Of course, continuing excessive fiscal deficits financed in this way through a state-owned commercial bank would ultimately jeopardize the solvency of the bank and require its recapitalization or funding with long term external debt.

Savings mobilization in Panama is carried out primarily through a well developed banking system that arose in large part from new legislation enacted in 1970 to modify the regulatory environment and allow for the development of offshore banking. From about twenty banks prior to this change, Panama was converted by the 1980s to a major international banking center with more than a hundred banks. There are currently two important state banks (the BNP and the Caja de Ahorro), 63 banks with general licenses (headquartered in Panama and conducting banking transactions both inside and outside the country), and 18 banks organized under foreign law but with licenses for operations in Panama.

After the recent crisis there were doubts whether Panama's banking system could recuperate. Nonetheless, the restrictions that had been imposed on deposits, affecting the withdrawal of time deposits in particular, were successfully lifted in 1990. As Table 7 shows, from March 1990 to November 1990 there was a significant increase in both internal and external deposits, attesting to the basic health of the system once restrictions were removed.

The impressive growth of the banking system and its ability to recuperate from a credibility crisis does not mean that Panama has the best financial system for mobilizing savings and channeling them to productive investments. The well developed national banking system, that is, banks engaged in both national and international transactions, provides financial services to domestic borrowers, but much of the development of offshore banking has not been complementary to the development of the domestic financial system in general or the securities market in particular.

Table 7
Banking System Assets and Liabilities

YEAR	ASSETS & LIABILITIES	LIQUID ASSETS		CREDIT PORTFOLIO		INVESTMENTS IN SECURITIES	DEPOSITS		CAPITAL & RESERVES
		INTERNAL	EXTERNAL	INTERNAL	EXTERNAL		INTERNAL	EXTERNAL	
1970	853.6	74.8	65.8	419.8	245.4	10.5	341.2	410.9	34.2
1971	1,185.2	84.8	104.4	562.9	375.4	11.9	426.9	602.2	65.2
1972	1,918.9	135.6	332.9	765.9	608.5	15.4	601.8	1,108.4	76.0
1973	3,590.8	123.0	931.1	1,026.0	1,313.8	71.6	656.9	2,603.4	129.8
1974	7,687.2	246.7	2,255.6	1,352.3	3,405.8	124.0	795.9	6,022.5	260.0
1975	10,296.0	411.6	2,692.4	1,525.3	5,304.2	106.5	849.6	8,532.9	317.9
1976	12,703.0	444.0	4,145.7	1,628.3	6,050.8	140.9	994.8	10,350.4	303.8
1977	16,583.7	491.6	5,371.2	1,765.5	8,192.6	244.2	1,199.4	14,012.8	415.7
1978	22,166.0	516.0	7,304.5	1,843.3	11,661.6	206.1	1,533.0	19,155.2	486.5
1979	36,245.6	1,178.2	14,077.2	2,133.2	16,799.6	931.3	1,802.4	31,197.3	632.4
1980	38,439.6	1,163.9	11,280.1	2,530.8	20,425.7	1,625.9	2,406.0	31,493.2	923.1
1981	46,359.9	1,514.9	10,325.7	3,146.0	27,433.2	1,708.3	3,201.5	36,481.6	1,132.4
1982	49,002.6	1,587.0	10,814.3	3,350.9	29,288.2	1,731.6	3,526.8	36,805.0	1,542.6
1983	42,785.6	1,270.0	11,620.2	3,553.4	22,847.3	1,526.8	3,364.8	30,830.9	1,591.0
1984	37,987.6	1,173.3	9,320.3	3,763.5	19,990.2	1,424.6	3,371.0	26,398.2	1,662.3
1985	38,989.8	1,343.4	10,183.1	3,923.4	19,828.6	1,587.3	3,710.6	28,316.0	1,689.5
1986	40,350.1	1,603.1	11,232.9	4,188.5	18,688.8	2,603.9	4,274.9	28,948.3	1,817.1
1988	14,885.0	371.0	2,782.0	3,906.0	5,942.0	590.0	2,834.0	8,154.0	944.0
1989	15,395.0	440.0	2,284.0	3,853.0	6,110.0	1,047.0	2,820.0	8,707.0	981.0
Mar. '90	16,216.0	363.0	3,115.0	3,859.0	6,088.0	1,025.0	3,572.0	8,807.0	814.0
Nov. '90	18,304.0	887.0	3,449.0	4,035.0	6,730.0	1,217.0	4,270.0	10,502.0	911.0

Sources: Comision Bancaria Nacional.

One of the main conclusions that can be drawn from a thorough analysis of Panama's banking system, and especially its growth and efficiency during most of the recent past, is that a well functioning securities market may not be crucial for supplying most financial services. The Panamanian Government and private sector enterprises already have, in general, good access to credit from the banking system at reasonable cost. In the following discussion this point will be developed through a brief examination of off-shore and on-shore lending, the allocation of credit among domestic economic sectors, intermediation costs and subsidized interest rates.

Off-Shore and on-shore lending. As can be seen in Table 8, off-shore lending has been well below the level of external deposits, so that Panamanian banks have substantial external liquid assets (see also Table 7 above). In addition, it is reported that foreign banks tend to lend more abroad and Panamanian banks to lend more domestically. An important question is how much of domestic lending has been financed with external funds. This question is especially important because of the bad experience with such behavior in the countries of the Southern Cone.

Table 8 shows that this has not been a major problem in Panama except during the crisis that began in 1987 and ended by late 1989 when the banking system relied heavily on foreign deposits for domestic lending. After the new Panamanian Government took office, the gap between domestic credit and domestic deposits closed quickly. Although the situation is not problematic at this time, it is important to emphasize the potential danger. An off-shore financial center should not mix foreign and domestic funds because the volatility of deposits during a crisis can put serious pressure on the banking system -- as happened in the recent crisis and could be repeated in the future.

The gap between domestic deposits and domestic lending was closed quickly for two main reasons. First, there was a huge inflow of Panamanian deposits after the change in government, which has been the primary factor contributing to the increase in bank resources. Second, the demand for credit is, for the moment, almost flat because of lack of opportunities for investment in Panama. In addition, banks have followed more conservative lending policies. As a result, liquidity indicators (in Table A1 of the statistical annex) show that the banking system has recently become extremely liquid, especially at state banks and mortgages banks but also at Panamanian private banks.

Table 8
Sources of Finance for Credit Portfolios
(millions of U$S)

	Credit Portfolio		Deposits		Gap
	Domestic(1)	External	Domestic(2)	External	(1)-(2)
1980	2,530	20,425	2,406	31,493	-124
1981	3,146	27,433	3,201	36,481	55
1982	3,351	29,288	3,527	36,805	176
1983	3,533	22,847	3,365	30,831	-168
1984	3,763	19,990	3,371	26,398	-392
1985	3,923	19,828	3,711	28,316	-212
1986	4,189	18,689	4,275	28,948	86
1987	4,363	13,513	3,750	20,601	-613
1988	3,906	5,942	2,834	8,154	-1072
1989	3,853	6,110	2,820	8,707	-1033
Mar.90	3,859	6,088	3,572	8,807	- 287
Nov.90	4,035	6,730	4,270	10,502	235

Source: Comisión Bancaria

<u>Sector Lending</u>. Lending activity in Panama has begun to recover somewhat from the low point reached during the crisis. However, the huge inflow of capital in the form of deposits in the banking system is not yet being lent for private sector economic

activities. Table A1 in the statistical annex reveals a significant increase in the level of liquidity in the banking system as a result of a weak demand for credit together with more conservative lending policies.

Since the public sector is large compared to private sector, the allocation of credit by the Panamanian banking system has been concentrated in the public sector. Table A2 in the statistical annex shows in detail the way the banking system has allocated credit to different sectors of the economy. Although it must be kept in mind that the fungibility of credit makes it difficult to know the actual use of credit, several interesting conclusions can nonetheless be reached.

Government owned banks do not appear to crowd out private banks in allocating credit to the private sector, except possibly in the case of housing. According to Table A2 in the statistical annex, private banks account for the majority of the credit market (58.3 percent in 1990 and 54.6 percent in 1989). However, as the Banco Nacional Agropecuario and the Banco Hipotecario do not take deposits, they are not included in the figures for the Panamanian banking system, so that the share of the state owned banks in the credit market may be significantly understated.

There appears to be a degree of segmentation among banking institutions in allocating credit to different economic sectors. While credit to the public sector is allocated mainly through stated owned banks, credit to the private sector is more likely to come from private foreign banks, and to a lesser extent from private Panamanian commercial banks and mortgage banks.

Reflecting the productive structure of Panama, private sector credit is mainly allocated to trade and housing construction activities -- the latter partly subsidized -- and to a lesser extent to industry, other types of construction and consumption. Housing is an important way of saving in Panama. Although rent controls exist, they can be avoided, thus yielding favorable returns compared to other productive activities, and this has been reinforced by the recent decline in interest rates. Credit to the agricultural sector is insignificant, largely reflecting risk aversion in view of the uncertain and variable returns as well as a lack of guaranties.

Foreign banks concentrate mostly in financing trade, which represented 52.2 percent and 56.3 percent of their total lending during 1989 and 1990 respectively. Panamanian banks concentrate more in housing, which represented 53 percent and 47 percent of their total lending during 1989 and 1990 respectively.

During the recent crisis not only was the number of banks reduced but also the number of agencies. In the case of banks with a general license -- the majority in Panama -- eleven closed while four new banks entered in the system. The number of agencies was reduced from 185 at the end of 1986 to 155 at the end of 1990. In the case of banks with an international license, four closed and one opened. As a result of this reduction, especially in the number of agencies, it has become more difficult for credit to be allocated to agricultural activities.

There are several important implications of the credit allocation patterns described above.

- First, the specialization of state owned banks in public sector lending is dangerous because it represents a large concentration of credit which could lead to severe problems if the Panamanian Government cannot pay its loans on time. The BNP does not make provisions for credit to the public sector, but such credit nonetheless implies a high degree of risk. After the crisis, when the United States Government reopened the accounts of the country, the BNP was able to increase its stock of international reserves substantially. However, that was a once and for all event which helped during 1990 but will not occur again in the future. To the extent that the fiscal deficit is not reduced, the sustained demand for credit by the public sector could threaten the future survival of the BNP.

- Second, the concentration of Panamanian commercial banks and mortgage banks in loans for housing construction has led to a dangerous mismatching in the term structure of funds. Table A3 and A4 in the statistical annex show the maturity structures for both kinds of banks, and loans of more than six months duration represent 68 percent of total loans of Panamanian commercial banks and 95 percent of total loans of mortgage banks. On the other hand, their funds come from deposits that are mostly concentrated in shorter maturities. Deposits of less than six months represent 72.3 percent of total deposits of Panamanian commercial banks and 62.4 percent of total deposits of mortgage banks. Such term mismatching indicates a potentially risky situation that could put strong pressures on these institutions especially if, as happened in the recent past, there is a run on bank deposits.

- Third, bank risk aversion against lending to the agricultural sector leaves an important portion of productive economic activity without reasonable access to credit, thus driving demand for credit to the Agricultural Development Bank (BDA). However, the BDA is characterized by high arrears, with a substantial proportion of its portfolio either in default or rolled over, which seriously limits its lending capacity. As a result, agricultural activities receive little financial support from the banking system.

<u>Costs of Intermediation</u>. The Panamanian banking system operates in

general very efficiently, especially in the case of foreign banks. Although there is little information directly available on spreads, they must be very low and similar to other international financial centers in order to be competitive.

- o First, reserve requirements, which act as an implicit tax on bank deposits and therefore translate into spreads, are low and similar to those in the United States, thereby allowing Panamanian banks to compete in the region by attracting deposits from various Latin American countries to lend abroad.

- o Second, the full integration of the capital account forces interest rates on deposits -- to which spreads are directly related -- to be at least as high as international rates.

- o Third, the Panamanian banking system adjusted significantly during the crisis by dealing with problem loans and by cutting costs through reducing the number of employees and agencies, thereby allowing lower spreads for future operations. Although Panamanian banks began to reopen some agencies in 1991, foreign banks have continued to operate with lower costs.

Table 9 presents information on interest rates on deposits and loans for the Panamanian banking system, and from this certain interesting points emerge.

- o First, interest rates on deposits have begun to decline in real as well as in nominal terms, probably as a result of increasing liquidity in the system and reconfirmation of the belief that Panama is fully committed to total capital mobility. Nonetheless, continuing high rates could inhibit the development of securities markets, especially because of the premium necessary to compensate for generally higher risks in securities markets.

- o Second, interest rates on loans, with the exception of commerce and housing, are somewhat lower at the BNP than at private banks. However, since the BNP lends heavily for housing at higher interest rates, lower rates for other activities are not likely to present a problem for profitability. In addition, the BNP benefits from public sector deposits at zero marginal cost. (Dangers for the BNP from loan concentration to the public sector have already been discussed above.)

- o Third, spreads at the private banks have not changed significantly as the majority of loans are allocated to commerce for which interest rates have been declining along with deposits rates. Nonetheless, given Panama's low inflation, lending rates continue to be high in real terms which may contribute to the low private sector demand for credit -- although uncertainty about policies to encourage the private sector, as well as questions of future stability, may be the primary reasons for this low demand.

Table 9
Interest Rates in the Panamanian Banking System

	Dec. 89	Jun 90	Sept. 90	Dec. 90	Average
Deposits of 6 months maturity					
Private banks	8.8	8.6	8.2	7.9	8.4
Panamanian	8.6	9.1	9.6	9.5	9.4
Foreign	6.4	7.8	7.6	7.2	7.25
B.N.P	n.a	n.a	n.a	n.a	8.8
Loans by Private Banks					
Agriculture	13.0	13.0	13.0	13.0	13.0
Housing	13.0	13.0	13.0	13.25	13.1
Commerce	13.2	12.9	13.0	12.7	12.9
Consumption	12.6	13.0	14.5	14.4	13.6
Loans by the B.N.P					
Agriculture					9.0
Industry					11.0
Commerce					13.5
Consumption					12.0
Housing					13.5
Fishing					9.5

Source: Comisión Bancaria y Banco Nacional de Panama

- o Fourth, differences in interest rates on deposits between Panamanian banks and foreign banks of around two percentage points -- probably reflecting different perceptions of risk for the two kinds of institutions -- result in spread differentials in favor of foreign banks. Further reductions in spreads will depend mostly on how the Panamanian banks adjust to the shrinkage in the volume of resources in the banking system. Foreign banks have already made stronger efforts to adjust their infrastructure and operating costs during the crisis than Panamanian banks, thus giving the foreign banks a competitive advantage. Moreover, before the unfreezing of deposits in July 1990, many banks, especially the Panamanian ones, increased interest rates to try to keep their deposits. However, increases in interest rates on deposits could not be translated to increases in lending rates because of the danger of increasing the volume of non-performing loans. As a result, both the profits and spreads of Panamanian banks were reduced. However, to compensate for the increase in interest rates on deposits, some Panamanian banks began to allocate credit to consumption at higher rates as shown in Table 9.

<u>Subsidized Interest Rates</u>. Interest rates are subsidized for priority activities. Cross subsidies in favor of agriculture and housing and against consumption result from the reference rates set by the Comisión Bancaria. In the case of agriculture, the Comisión Bancaria sets a 13 percent reference rate, in addition to which producers receive a 4 percentage point subsidy. In a similar way, interest rates for housing loans below US$ 50,000 are subsidized with 4 percentage points, while those below US$ 20,000 receive 5 percentage points, thus yielding interest rates of 9.25 percent and 8.25 percent respectively for the two classes of recipients (based on a reference rate for housing of 13.25 percent). These subsidies are financed through the Fondo de Compensación de Intereses (FECI) by a surcharge of 1 percentage point on consumption loans.

Subsidized credits do not have as important implications for the Panamanian financial system as they do for the financial systems in most other Latin American countries, because the subsidies are not given through rediscounts and hence do not discourage saving mobilization and create pressures for additional monetary emission. In addition, according to Table A2 in the statistical annex, subsidized credit for agriculture is insignificant, and subsidized credit for housing -- approximately 50 percent of total housing credit -- is not very important either.

Main Financial Instruments and the Organization of the Securities Market

There are few savings instruments at the disposal of the public in Panama. The usual ways that people hold their wealth in Panama are:

(1) dollar deposits in the banking system;

(2) housing property; and

(3) to a lesser extent, bonds and shares of private corporations and government bonds.

The Panamanian securities market is incipient and characterized by a small regulated market concentrated mainly in government paper and a few private sector instruments. As in many other Latin American countries, a parallel informal market exists for private documents, the magnitude of which is difficult to know. The informal market exists primarily because the fiscal treatment of capital gains on savings instruments has discouraged the use of the regulated market. More recently, and especially during the crisis when banks were closed by the Panamanian Government, liquidity needs for transactions contributed greatly to the development of the informal market and to the creation of the Bolsa de Valores of Panama.

According to many observers, the efficiency of the banking system has contributed to the small and underdeveloped nature of the securities market, as creditworthy private corporations have good access to credit on attractive terms making it unnecessary to resort to the securities market for funds. Bank credit is the cheapest source of financing, and even long term loans -- although officially nonexistent except for housing -- can be obtained indirectly through the continuing rollover of short term loans. The fact that the Bolsa de Valores was created and developed during the banking closure, and that it came to a standstill after the banking system reinitiate its operations in 1990, are additional indications confirming this conjecture.

The securities market is organized around official agents (corredores), but there are also informal agents. The recently created Bolsa de Valores is supervised by the Comisión Nacional de Valores (CNV) which is a part of the Ministerio de Comercio e Industria. The CNV had already been created in 1970 to prevent frauds involving mutual funds. The CNV supervises private corporations that offer bonds or shares in the official market -- these must be registered at the CNV and provide information openly -- and the CNV is also the only entity authorized to give licenses to official agents.

The profits tax on capital gains can be avoided for firms that have only a few owners of shares by voluntarily registering at the CNV with the Registro Voluntario. In the case of firms offering shares or bonds publicly, however, it is a requirement to be registered with the Registro Oferta Pública. As of early 1991, there were 125 firms registered, 71 of them with the Registro Oferta Pública.

Table 10 summarizes the main financial instruments officially available in Panama and the amount in circulation for each. The total value in circulation reveals the small size of the securities market compared to the amount of deposits in the banking system. It is also interesting to note the wide range of implicit interest rates on government papers and how these rates do not put upward pressure on the level of interest rate in Panama.

Table 10
Circulation of Financial Instruments
(thousand US$)

	Circulation 12/31/90	Nominal Int.Rate	Quotation Range
Government Paper	119,387		
Government Bonds	70,672	4 - 6%	68 - 70%
Treasury Bills	15,595	3%	No quote
Pagarés MOP	2,110	11%	No quote
Pagarés C.Seg.Social	10,000	0%	92 - 95%
CATs	10,184	0%	72 - 98.5%
CPC	265	0%	98.4%
Fiscal Credits	10,559	0%	99.3%
Private Corporate Bonds	91,659		
CEDIs	29,959		
Private Banks		5.5 - 9.25%	92 - 96%
Banco Nacional de Panama		2.0 - 4.5%	87%
Bonds	61,700	9.0 - 13.0%	89 - 100%
Private Corporate Shares	400,000		
Total	611,046		

Source: Bolsa de Valores de Panama

- Government papers account for 20 percent of the total value in circulation and include a wide range of different categories of financial instruments.

- Long term government bonds have maturities between five and ten years and different nominal interest rates. The quotations for all of these are similar and reflect a low demand as a result of the default on debt service payments by the Panamanian Government. For example, bonds that matured in 1988 were not honored and interest payments were also postponed. Implicit interest rates are thus quite high on government bonds -- around 50 percent per year -- as these bonds are mainly demanded to be used as collateral.

- Treasury Bills are held by banks as they can be used to fulfill reserve requirements so they are not quoted on the Bolsa. The Panamanian Government is servicing the interest payments.

- MOP promissory notes with four years maturity have recently been issued, but they were not accepted in the market because of the general default of the Panamanian Government in debt service payments. Only two million out of ten were placed.

- Social Security promissory notes with fourteen months maturity and zero interest rates have implicit rates ranging from 5.3 percent for three months to 8.7 percent for twelve months.

- Certificados de Abono Tributario (CAT) serve as payment instruments, and their implicit interest rates range from 1.5 percent for one month maturity to 39 percent for twenty months maturity.

- Certificados de Poder Cancelatorio (CPC) correspond to tax reimbursements, and their implicit interest rate is 1.6 percent for a one month maturity.

- Creditos Fiscales correspond to interest subsidy reimbursements, and their implicit interest rate is 1.5 percent for a one month maturity.

- Among private debt instruments, CEDIs and corporate bonds are the most common.

  - CEDIs correspond to certificates of deposits frozen in the banking system that were issued during the crisis. Quotations vary according to nominal interest rates and maturities, and the implied rates range between 10 and 20 percent for private banks. There are no significant differences in implicit rates among private banks or between private banks and the BNP.

  - Corporate bonds have implicit rates of return of around

12 percent. Corporate bonds are accepted in general but the degree depends on the company's prestige and the transparency in the subscription mechanism.

- In terms of total amounts in circulation, shares are the most important instruments. However, equities are mainly held by small numbers of families or groups, and only about one third are traded in the market -- and even of these, a large portion is held by a small number of persons. Most shares have very low quotations relative to book value, and few corporations are willing to disclose information to fulfill the requirements imposed by the CNV. Of the small number of firms that are registered at the CNV, approximately thirty are traded on the Bolsa.

Taxation of Financial Markets and Securities Market Instruments

One surprising fact regarding Panama is the sharp contrast between a well developed banking system and an incipient securities market. One explanation may be that the ownership of private enterprises is predominantly in the hands of closed family groups or association of individuals who are not interested in having more broadly based ownership. This may in part be the consequence of two main factors: (1) the presumption that family and friendship are necessary for faithfulness; and (2) that procedures for tax evasion and black market operations require small groups of individuals.

Another explanation, perhaps equally important, is that Panama's tax system discriminates against the development of a securities market. As already noted, Panama's tax system needs an overall reform to improve its impact on resource allocation and equity. Taxes are in particular discriminatory against a securities market and in favor of interest from bank deposits and government bonds that are tax free. Among the most important non-neutral aspects of the tax system are:

- a value-added tax of 5 percent that excludes services instead of being a generalized tax;

- a personal income tax with a 10 percent withholding tax on dividends and a range 2.5 percent to 56 percent on other types of income;

- a corporate income tax that ranges from 20 percent to 50 percent;

- favoritism for corporations in the Colon Free Zone which pay corporate income taxes at rates ranging from only 2.5 percent to 8.5 percent;

- favoritism for non-traditional exporters who are exempt from all taxes on their exports, including the corporate income tax, and receive negotiable tax certificates equal to 20 percent of value added in export production that can be used to pay tax liabilities arising from non-export activities;

- imports tariffs that range from 0 percent to 90 percent (and even higher in cases where specific tariffs can be applied), although only a limited number of items pay the highest rate;

- a tariff rate of 27.5 percent for capital equipment, but with most producers receiving exemptions that reduce the effective tariff to 3 percent; and

- provisions for accelerated depreciation and write-offs for the reinvestment of profits.

A number of aspects of the tax system are biased against bonds and especially against equities (and in favor of deposits in the banking system) and thereby undermine the development of a securities market.

- o Interest on bank deposits and government bonds are exempt from taxes.
- o Short term bonds (less than three years maturity) are taxed at 5 percent on interest payments, with the remaining 95 percent not accrued to taxable income.
- o Dividends are taxed at 10 percent with the remaining 90 percent not accrued to taxable income, and 40 percent of undistributed profits are taxed at 10 percent.
- o Capital gains accrue to taxable income.

According to Table 11, tax collections on dividends were high during the 1985-87 period but became negligible by 1990, so that there would not be a significant reduction in fiscal revenues if the dividend tax were eliminated. In fact, the CNV is proposing legislation to exempt dividends on ordinary shares (or preferred shares convertible to ordinary shares) with rights of voice and vote from income tax. The alternative of taxing interest income from bank deposits would not be advisable because of implications for the international competitiveness of Panamanian banks.

Table 11
Tax Collections on Dividends
(thousand of US$)

	Dividends	Undistributed Profits	Total Fiscal Revenues	Percent of total
1983	7,377	5,748	661,700	1.98
1984	6,559	4,718	634,733	1.78
1985	12,295	5,075	688,729	2.52
1986	11,464	5,229	753,431	2.22
1987	20,848	5,478	789,742	3.33
1988	4,787	4,341	443,002	2.06
1989	5,000	2,352	410,008	1.79
1990	7,892	3,345	623,791	0.54

Source: Ministerio de Hacienda y Tesoro

Nonetheless, it does not appear that asymmetric tax treatment is the main factor limiting the development of securities markets -- rather disclosure of information and openess to outsiders are the main restrictions to future securities market development.

Concluding Comments and Major Recommendations

Panama is recovering well from a political and economic crisis that began in 1988 and lasted until mid 1990. However, Panama's problems cannot be attributed exclusively to this recent crisis. There are more fundamental problems that have their origins in several decades of a misguided approach to economic development.

The Panama Canal has long functioned as a leading sector, allowing the development of trade and financial sectors servicing the rest of Latin America. However, the international debt crisis that started in 1982 reduced Panama's financial role; and, as in many other countries in the region, its external debt burden increased and its economic growth slowed. Between 1984 and 1987 there was some recovery from the debt crisis, but fundamental measures were not taken to improve resource allocation.

The 1988 crisis evolved with fiscal disarray, which in turn led to the suspension of debt payments and the freezing of deposits in the banking system. After the United States invaded in December 1989, a new government took office that reduced the power of the military and introduced greater fiscal discipline. Beginning in 1990, payments on debts owed to the international financial institutions have been made, and talks have begun on rescheduling debts owed to commercial banks and bilateral lenders.

Among the factors presently inhibiting growth are:

- o the lack of a well organized securities market able to mobilize savings and channel them to productive investments or to assimilate the trading of a significant volume of securities;

- o large public utilities providing energy, transportation and communications -- which usually account for a major proportion of activity in securities markets -- do not participate in the Panamanian securities markets because they are state owned and operate at low levels of efficiency; and

- o government intervention throughout the economy due to an ideological persuasion that the private sector can provide neither an efficient allocation of resources nor a reasonable distribution of income.

Nonetheless, some fundamental changes in public opinion are taking place, and the prospects for the development of a securities market in Panama may be improving. Although Panama currently lacks an active securities market, the banking sector has developed steadily with efficiency and sophistication. Moreover, Panama is second to none in Latin America in its integration into world financial markets. The secret to this success has been very simple: Panama is favored with a strategic geographical location for trade and finance and has been able to maintain a stable currency system based on the United States dollar.

Panama's private sector is well aware of the poorly developed securities market that is currently trading insignificant volumes of equity and debt issues just two day a week. There is, moreover, some interest in the Bolsa as it is owned by a broad consortium of banks and other investors and includes eight brokerage houses. In particular, the Panamanian Chamber of Commerce has a project with the Chicago Mercantile Exchange based on the assumption that Panama has the potential to become a more important financial and investment center for Latin America. These two institutions are currently in the process of providing assistance to develop a regulatory infrastructure, knowing that the success of any financial center depends on investors' confidence in the security of their capital. This in turn requires a regulatory environment that provides efficient enforcement mechanisms to insure the security of investments. The basic idea is that an optimal structure involves a self-regulatory entity that provides primary enforcement, supplemented by a government structure that functions when primary enforcement proves inadequate.

A major attraction of the Bolsa project is that it is oriented toward international markets where Panama has been shown to possess significant comparative advantage. Its geographical location and the robustness of its financial sector, which emerged from the recent crisis with its domestic and international integrity largely intact despite the freezing of deposits, are important advantages. The Bolsa also has the attraction of being thought of as a private entity for trading securities of all kinds, both domestic and international. This contrasts sharply with projects in many other countries that are thought of primarily as ways of developing a market for domestic government debt.

Prospects for developing a securities market in Panama may also be enhanced by success in implementing the Government's privatization program and by an increase in the demand for long term funds as a result of the banking system's more conservative lending policies. In addition, the Government is considering the payment of arrears to domestic suppliers (the floating debt) of about US$ 160 million by issuing promissory notes of different maturities. Furthermore, Panama's foreign debt could be reduced through a voluntary debt equity swap mechanism, for which a securities market would be essential. There may also be prospects for increased demand for instruments that might be traded on a Panamanian securities market. For example, insurance companies can hold their technical reserves either in government or private bonds. The Social Security System, although in poor financial condition after the recent crisis (partly because the government stopped paying its obligations), might become healthy and thus be an important provider of long term funds to the securities market, as happens in many other countries.

The potential for developing a securities market will nonetheless also depend on several macrofinancial and institutional issues.

- First, there are few good opportunities for investment in physical capital in Panama. Demand for long term funds, either debt or equity, would first require the demand for investment to recover. Until the macroeconomic environment and the system of incentives for growth are changed through structural reforms that stimulate production of tradeables and reduce the size of the public sector, it seems unlikely that the securities market could become more developed.

- Second, the efficiency of the banking system reduces the need to resort to the securities market for funds. Moreover, as insider lending is allowed in Panama, large firms and economic groups have an easy and cheap way to finance their investments by creating their own banks -- or lending to themselves indirectly through crossing financial support among different Panamanian bank groups. Future regulations that limit insider lending to related groups may be an indirect way to contribute to the development of the securities market.

- Third, the small number of firms that have fulfilled the CNV's conditions for public offerings of bonds and shares, together with the large number of state-owned enterprises, also impede the development of the securities market.

- Fourth, the failure to make payments on bonds and to service foreign debt is a severe limitation for any future government bond market. Uncertainties about future payments make government bonds undesirable, as reflected in the low quotations discussed above. It is surprising that the Panamanian Government seems to give such a low priority to this issue. It is well known that, during 1990, the foreign exchange position was restored so that debt service payments could be reinitiated to reinforce domestic financial markets in general and the market for government paper in particular.

- Fifth, the unwillingness of important economic and family groups to open their companies to outside investors and to disclose information to the general public is perhaps the most severe restriction to developing a securities market. As an example of how closed Panamanian corporations are, it can be noted that the CNV authorized the issuance of US$ 61.5 millions in equities during 1990, but only US$ 2.4 was transacted on the Bolsa. This means that the remaining authorized capital was transacted among groups and families that register their firms voluntarily at the CNV to avoid taxes.

Statistical Appendix

Table A1

Central Government Operations

Panama: Central Government Operations (In millions of Balboas)	1988	1989	Budget 1990	Estimate 1990	Project 1991
CURRENT REVENUES	601.1	566.0	839.7	877.3	961.4
Tax Revenues	467.2	435.0	497.7	533.1	604.0
Income Tax	194.6	146.5	182.1	187.3	216.0
Other Direct Taxes	36.6	27.7	30.6	34.1	36.0
Taxes on Foreign Trade	54.4	64.4	78.4	98.1	116.0
Taxes on Domestic Transactions	181.5	196.4	206.6	213.6	236.0
Nontax Revenue	133.9	131.0	325.2	327.4	340.4
Panama Canal	18.6	2.2	69.8	66.0	68.0
Oil Pipeline Royalties and Taxes	2.1	0.0	19.0	7.8	7.8
Transfers form the Rest of Public Sector	39.8	48.0	153.3	161.6	158.4
Other	73.4	50.8	83.1	92.0	106.2
Grants-in-Aid	0.0	0.0	16.8	16.8	17.0
TOTAL EXPENDITURE	1,130.9	1,191.5	1,272.9	1,215.8	1,228.8
Current Expenditures	1,095.7	1,151.5	1,215.0	1,185.3	1,178.8
Wages and Salaries	451.3	447.3	433.1	425.0	430.0
Goods and Services	104.7	82.7	131.4	111.4	121.0
Pensions and Transfers	187.8	205.4	274.6	273.0	246.0
of which: Social Security Agency	77.9	90.1	173.5	171.3	140.0
Decentralized Agencies	70.5	45.4	54.9	47.7	50.0
Public Enterprises	9.6	0.9	2.5	0.0	0.0
Other	29.8	69.0	43.7	54.0	56.0
Interest	329.2	411.4	375.9	375.9	381.8
Internal	43.5	84.6	37.0	37.0	35.0
External	285.7	326.8	338.9	338.9	346.8
Other Current Expenditure	22.7	4.7	0.0	0.0	0.0
Capital Expenditure	35.2	40.0	57.9	30.5	50.0
Fixed Capital Formation	35.2	31.1	39.1	20.0	0.0
Transfer to rest of the consolidated Public Sector:	0.0	8.9	18.8	10.5	0.0
To Decentralized Agencies	0.0	0.0	0.0	0.0	0.0
To Public Enterprises	0.0	0.0	0.0	0.0	0.0
Current Account Surplus or Deficit (-)	(494.6)	(585.5)	(375.3)	(308.0)	(234.0)
Overall Surplus of Deficit (-)	(529.8)	(625.5)	(433.2)	(338.5)	(267.4)
	Annual percentage Change				
Current Revenue	(44.0)	(5.8)	48.4	4.5	9.6
Tax Revenue	(41.5)	(6.9)	14.4	7.1	13.3
Nontax Revenue	(51.3)	(2.2)	148.2	0.7	4.0
Total Expenditure	(3.6)	5.4	6.8	(4.5)	1.1
Current Expenditure	1.6	5.1	5.5	(2.4)	(0.6)
Capital Expenditure	(63.0)	13.6	44.8	(47.3)	63.9
	As percent of GNP				
Current Revenue	13.3	12.6	17.0	17.7	17.9
Tax Revenue	10.3	9.6	10.3	11.0	11.5
Nontax Revenue	3.0	2.9	6.7	6.7	6.5
Total Expenditure	25.0	26.4	26.2	25.1	23.3
Current Expenditure	24.2	25.5	25.0	24.4	22.4
Capital Expenditure	0.8	0.9	1.2	0.6	0.9
Current Account surplus or deficit (-)	(10.9)	(13.0)	(7.7)	(6.3)	(4.4)
Overall surplus or deficit (-)	(11.7)	(13.9)	(8.9)	(7.0)	(5.1)

Source: IMF, Office of the Comptroller General, and Ministry of Planning.

Table A2
Central Government Revenue

Panama: Central Government Revenue	1988	1989	Est. 1990	Proj. 1991
TOTAL REVENUE				
Tax Revenue	467.2	435.0	533.1	604.0
Direct Taxes	231.2	174.2	221.4	252.0
Income Tax	194.6	146.5	187.3	216.0
Other	36.6	27.7	34.1	36.0
Taxes on Foreign trade	54.4	64.4	98.1	116.0
Export Taxes	0.1	0.1	13.0	14.0
Import Taxes	53.1	63.3	83.0	99.5
Consular Dues	1.3	1.0	2.1	2.5
Taxes on Domestic Transactions	181.5	196.4	213.6	236.0
Tobacco and beverages	26.1	28.0	33.7	35.0
Value added tax	49.2	54.3	60.0	69.0
Petroleum products	75.1	79.2	77.0	85.0
Ship registration fees	4.9	4.2	9.3	10.3
Stamp taxes	16.0	20.7	19.1	21.1
Other	10.2	10.0	14.5	15.6
Nontax Revenue	133.9	131.0	327.4	340.4
Receipts from Panama Canal	18.6	2.2	66.0	68.0
Oil Pipeline royalties	2.1	0.0	7.8	7.8
Services	8.2	4.7	15.8	16.4
Gambling Earnings	21.8	26.3	37.6	39.1
Transfers from rest of public sector	39.8	48.0	161.6	158.4
Of which: consolidate public sector	17.5	20.7	121.6	113.4
Nonconsolidated public sector	22.3	27.3	40.0	45.0
Other	43.4	49.8	38.6	50.7

Source: IMF, Office of the Comptroller General, and Ministry of Planning.

Table A3
Decentralized Agencies

Panama: Summary of Decentrelized Agencies	1988	1989	Est. 1990	Proj. 1991
Operating Revenue	35.0	36.0	46.9	51.0
Operating Expenditure	86.4	74.6	86.7	90.0
Interest Obligations	18.9	8.4	13.7	13.7
Other Current expenditure	67.5	66.2	73.1	76.3
Operating Surplus or Deficit (-)	(51.4)	(38.6)	(39.9)	(39.0)
Current Transfers (net)	47.4	45.4	4,038.0	43.1
Transfers from Central Government	47.7	45.4	47.7	50.0
Transfers to Central Government	(0.3)	0.0	(6.9)	(6.9)
Current account surplus or deficit (-)	(4.0)	6.8	0.9	4.1
Capital Transfers form Central Government	0.4	0.0	2.5	0.0
Capital Expenditure	(5.9)	(7.4)	8.2	4.2
Fixed Investment	1.6	0.0	21.6	
Net Lending	(7.5)	(7.4)	(13.4)	
Overall surplus to deficit (-)	2.3	14.2	(4.8)	(0.1)

Source: IMF, Office of the Comptroller General, and Ministry of Planning.

Table A4
Operations of Public Enterprises

Panama: Summary Operations of Public Enterprises

	1988	1989	Est. 1990	Proj. 1991
Operating Revenue	515.6	493.5	520.0	585.0
Operating Expenditure	40.3	354.9	370.8	350.9
Interest Obligations	92.2	95.0	93.7	83.9
Other Current expenditure	310.3	259.9	277.2	267.0
Operating Surplus or Deficit (-)	113.1	138.6	149.1	234.1
Transfers Net of Taxes	(57.4)	(35.3)	(92.5)	(106.5)
Current transfers from Central Gov.	0.0	0.9	0.0	0.0
Transfers to Central Government	(57.4)	(36.2)	(92.5)	(106.5)
Current account surplus or deficit (-)	55.7	103.3	56.6	127.6
Capital revenue	0.0	0.0	2.0	0.0
Capital Expenditure	49.0	12.8	54.4	115.6
Overall surplus to deficit (-)	6.7	90.5	4.2	12.0

Source: IMF, Office of the Comptroller General, and Ministry of Planning.

Table A5
Operations of the Social Security Agency

Panama: Operations of the Social Security Agency

	1988	1989	Est. 1990	Proj. 1991
Current Revenue	335.9	362.9	346.5	371.0
Contributions	261.5	273.0	251.7	271.0
Professional Risk Premium	16.6	17.0	16.7	18.0
Thirteenth-month contribution	0.0	0.0	0.0	0.0
Contrib. to public employees' comp. Pension	17.0	34.0	34.6	35.0
Income from investments	22.5	20.4	17.7	19.0
Other	18.2	18.5	25.7	28.0
Current Expenditure	425.5	461.5	481.4	506.0
Administration	16.5	18.0	19.4	0.0
Payments of benefit and other	409.0	443.5	462.0	0.0
Current operating surplus or deficit (-)	(89.6)	(98.6)	(134.9)	(135.0)
Current transfers (net)	77.9	90.1	149.1	140.0
From Central Government	77.9	90.1	171.3	140.0
Current account surplus or deficit (-)	(11.7)	(8.5)	14.3	5.0
Capital Expenditures	2.9	0.7	13.0	5.0
Fixed Investment	1.8	0.4	1.3	0.0
Financial Investment	0.0	0.0	0.0	0.0
Housing program and others	1.0	0.3	0.0	0.0
Overall surplus or deficit (-)	(14.5)	(9.2)	13.0	0.0

Source: IMF, Office of the Comptroller General, and Ministry of Planning.

Table A6
Operations of the Banking System

Panama: Summary Operations of the Banking System	Dic. 1988	Dic. 1989	Prel. May 1990	1990	Proj. Dec. 1991
Net foreign assets	(706.7)	(577.7)	46.2	(139.0)	111.0
of which: National Bank	(383.9)	(324.2)	(204.8)	(113.0)	(105.0)
Net Domestic Assets	3,519.5	3,290.9	2,899.1	3,285.3	3,556.4
Public Sector (net)	728.4	664.7	321.3	505.1	488.0
Private Sector	2,751.6	2,567.7	2,501.7	2,721.8	3,010.0
Other assets (net)	39.5	5,834.0	76.1	58.4	58.4
Long-term foreign liabilities	(216.9)	(234.1)	(234.1)	(342.1)	(392.1)
SDR allocation	(35.4)	(34.6)	(34.5)	(34.3)	(34.3)
Liabilities to domestic private sector	2,560.3	2,444.4	2,676.7	2,770.0	3,241.0
Monetary liabilities	1,889.3	1,808.4	2,054.7	2,128.9	2,494.0
Demand Deposits	299.3	300.9	349.7	367.5	415.2
time and savings deposits	1,590.1	1,507.5	1,705.0	1,761.4	2,078.9
Time deposits	1,155.2	1,126.3	1,286.6	0.0	0.0
Savings deposits	434.9	381.1	418.4	0.0	0.0
Private capital and surplus	671.0	636.0	622.0	641.1	746.9
	In percent of GDP				
Net domestic Assets	77.9	73.0	59.8	67.7	67.4
Public sector (net)	16.1	14.7	6.6	10.4	9.2
Private sector	60.9	57.0	51.6	56.1	57.1
Liabilities to private sector	56.7	54.2	55.2	57.1	61.5
Monetary liabilities	41.8	40.1	42.3	43.9	47.3
Private capital and surplus	14.9	14.1	12.8	13.2	14.2
	(12-month percentage change in relation to liabilities to the private sector at the beginning of the period)				
Net domestic Assets	(21.0)	(8.9)	0.0	(0.2)	9.8
Public sector (net)	(0.9)	(2.5)	0.0	(6.5)	(0.6)
Private sector	(16.4)	(7.2)	0.0	6.3	10.4
Liabilities to private sector	(28.3)	(4.5)	0.0	13.3	17.0

Table A7
Operations of the National Bank

Panama: Operations of the National Bank	Dic. 1988	Dic. 1989	May 31 1990	Proj. Dic 31 1990	Proj. Dic. 31 1991
NET LIQUID ASSETS	(4.1)	16.4	376.4	78.0	81.7
Liquid Assets	123.9	137.8	489.5	184.0	0.0
Of which: Bank deposits	80.6	67.1	431.1	130.4	0.0
Short term liabilities	128.0	121.3	113.1	111.1	0.0
NET DOMESTIC ASSETS	586.4	524.3	228.6	586.2	587.4
Net credit to the public sector	345.4	338.5	15.6	388.8	359.1
Assets	868.0	1,032.7	1,085.0	1,085.0	0.0
Liabilities	(522.6)	(694.2)	(1,069.4)	(696.2)	0.0
Credit to the private sector	300.5	286.7	263.5	263.5	294.4
Other assets (net)	(59.5)	(82.7)	(50.5)	(66.1)	(66.1)
LIABILITIES TO THE PRIVATE SECTOR	166.9	160.9	180.5	190.0	220.0
Demand deposits	25.7	33.7	38.2	40.2	0.0
Savings deposits	30.1	28.1	29.1	29.1	0.0
Time deposits	111.1	99.0	113.2	120.7	0.0
LONG-TERM FOREIGN LIABILITIES	216.7	224.0	224.0	224.0	224.0
LIABILITIES TO LOCAL BANKS	116.7	92.0	118.5	130.1	143.1
CREDIT FROM U.S.AID FOR ECONOMIC REACT.	0.0	0.0	0.0	38.0	0.0
Drawings	0.0	0.0	0.0	108.0	108.0
Certificates of deposit in other banks	0.0	0.0	0.0	(70.0)	(108.0)
COUNTER-ENTRY OF FUND ACCOUNTS	82.0	82.0	82.0	82.0	82.0

Table A8
Financing of Public Sector Operations

PANAMA: Financing of Public Sector Operations (In millions of US Dollars)	1990	1991
REVENUES	1,302	1,514
EXPENDITURES	1,640	1,775
BALANCE	(338)	(261)
FINANCING	338	261
1. Principal Obligations Falling due	(380)	(361)
External	(358)	(328)
Of which: Multilateral institutions	(173)	(143)
Paris Club	(21)	(19)
Commercial Banks and Bonds	(143)	(135)
Other	(21)	(32)
Domestic	(22)	(33)
2. Refinanceable Obligations. 1/	507	540
Interest	322	354
Principal	185	186
3. Cash Payments	(74)	(139)
Domestic Arrears	(51)	(30)
Paris Club	(23)	(29)
National Bank of Panama	0	(30)
Other	0	(50)
4. Use of Blocked Funds	220	0
5. U.S. Budgetary Assistance	30	84
6. Multilateral Institution Loans	27	210
7. Bridge Loan Repayment	(27)	(123)
8. Project Related Disbursements	0	50
9. Nontraditional Funds. 2/	35	0

1/ Includes assumed Paris Club and other bilateral debt reschedulings and accumulation of arrears to commercial banks and other private creditors.

2/ Refers to nonrecurrent transfer to the Central Government from public agencies outside the consolidated nonfinancial public sector.

Sources: Panamanian authorities; and Fund Staff estimates.

Table A9
Consumer Price Index

Consumer Price Index 1975 - 1990 (1975 = 100)	Panama City (Low and Middle Income)				
	Total	Food	Housing	Clothing	Miscellaneous
			(In Percent)		
Weights	100.0	39.4	23.0	9.3	28.3
			(Period Average)		
1975	100.0	100.0	100.0	100.0	100.0
1980	139.2	137.6	135.4	130.5	145.6
1981	149.4	150.2	141.9	137.5	156.7
1982	155.7	159.1	148.8	144.4	160.0
1983	159.0	162.8	153.1	146.2	162.7
1984	161.5	165.2	155.9	148.2	165.1
1985	163.2	165.7	159.1	149.7	166.8
1986	163.1	166.4	159.3	151.4	165.4
1987	164.7	170.6	160.8	152.4	164.7
1988	165.3	171.0	162.3	152.3	165.0
1989	165.1	168.7	162.9	153.1	166.1
			(End of Period)		
1975	101.4	100.0	103.7	102.9	104.8
1980	145.1	144.9	139.1	134.7	152.1
1981	152.1	154.3	144.4	140.8	158.1
1982	157.7	161.8	151.4	145.3	161.0
1983	160.8	163.9	155.8	146.9	164.6
1984 March	161.0	163.8	156.1	148.1	164.9
June	161.2	165.3	154.3	148.1	165.1
September	162.4	166.8	157.0	148.4	165.3
December	162.3	166.1	157.1	149.0	165.5
1985 March	163.1	165.9	158.9	149.5	166.6
June	163.6	166.2	159.3	150.2	167.1
September	163.5	165.7	160.0	149.3	167.4
December	162.9	164.7	159.5	159.3	166.9
1986 March	163.6	165.0	159.7	151.5	167.9
June	162.3	165.9	158.6	151.5	164.1
September	163.6	168.9	159.3	151.5	164.4
December	163.6	168.4	159.3	152.5	164.5
1987 March	164.1	168.7	160.8	152.6	164.6
June	165.1	171.7	160.8	152.4	164.7
September	165.1	171.5	161.4	152.3	164.6
December	165.0	170.9	161.3	152.2	165.0
1988 March. a/					
June	164.4	168.9	162.3	152.5	164.4
September	165.5	171.5	162.4	152.2	165.1
December	165.5	171.4	162.4	152.0	165.2
1989 March	164.9	168.9	162.6	153.3	165.5
May	165.1	169.1	162.7	153.2	165.9
June	165.1	168.4	162.7	153.2	166.4
July	165.5	169.4	163.0	153.2	166.6
August	165.0	167.9	163.0	153.3	166.6
September	165.2	168.3	163.1	153.2	166.6
December	165.1	167.9	163.3	153.3	166.6
1990 March	165.5	168.8	163.4	153.1	166.8
May	165.5	168.6	163.5	153.5	167.1
June	165.7	168.8	163.5	153.9	167.3
July	166.0	169.9	163.7	154.5	166.5
August	166.6	170.5	163.7	156.8	167.1
September	166.6	170.1	163.8	156.8	167.5
December					

a/ No data gathered during this month.
Source: Office of the Comptroller General.