

REPORT

PANAMA EMPLOYMENT STUDY

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**THIS STUDY DOES NOT ATTEMPT
TO REPRESENT THE VIEWS OF THE
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT
OR THE GOVERNMENT OF PANAMA**

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Executive Summary

This report analyzes labor market performance during the decade of the 1980s and evaluates the future prospects for employment in the absence of structural reforms. It also reviews provisions of the Labor Code that inhibit employment and suggests modifications. The difficulties we encountered with the available data led us to include comments on the available labor statistics. Finally, we offer suggestions for action by USAID that could help resolve some of the problems identified in the course of the study.

Employment conditions in Panama appear to have deteriorated during the decade of the 1980s. Recorded rates of unemployment rose from an 8 - 10 percent range at the beginning of the decade to over 16 percent after the onset of the economic crisis of 1988. While there is little doubt that unemployment has increased over time, the erratic nature of the labor force data and the definition of unemployment used leave open to question the precise volume of unemployment. During the decade real wages of formal sector employees appear to have stagnated as did productivity of the labor force as a whole. While some workers gained increases in real wages, others suffered offsetting losses. The crisis years saw productivity plunge by about 18 percent while real wages of modern sector employees remained virtually unchanged.

The prospects for the 1990s do not appear encouraging. In the absence of structural changes we have estimated that the rates of growth of the gross domestic product and employment will not

suffice to reduce unemployment much below its present level. More discouraging is that the sharp drop in productivity suffered during the crisis years 1988 - 1989 will not be recouped. This implies that it will be difficult to sustain current levels of real wages let alone increase them. This could foretell a decade of considerable social and economic unrest as various economic groups try to improve their real income positions. Given the limited growth in GDP that is forecast, any gains realized by any one group must necessarily come at the expense of others. In the current economic setting, upward revisions of the legal minimum wage would appear to have unfavorable consequences for employment.

Provisions of the Labor Code that tend to inhibit employment creation were reviewed. Provisions dealing with severance pay, shift payments, piece work were among those discussed. Suggestions for modification were advanced. There is also recognition that provisions dealing with collective bargaining merit reconsideration with a view to reducing the degree of government intervention in industrial relations.

After a discussion of observed shortcomings in the labor force data, the report offers suggestions of possible ways in which USAID might assist the Panamanian government improve the quality, timeliness, and interpretation of labor force data.

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Introduction

This study has been designed to provide an analysis of employment conditions in the Panamanian labor market and to recommend measures that could be expected to contribute to a reduction in unemployment via an accelerated rate of employment creation. It is a fitting time to undertake such a study because of the coincidence in time of two pressing concerns. First, the country is in the early stages of a recovery from the traumatic events of 1987-89 that left the economy in a severely depressed state, and unemployment is reported to have reached unprecedented high levels. Thus a short-term objective is to accelerate the recovery of employment and a parallel reduction in open unemployment. This requires a prior appreciation of the actual conditions in the labor market at the present time.

The second consideration involves a longer-term perspective that takes into account the impact on employment that structural adjustments that are under review may have, and, conversely, the implications that the existing institutional arrangements may have for the successful implementation of the adjustment. There is substantial agreement that the Labor Code poses serious obstacles to the efficient functioning of the labor market and that it

requires substantial amendment if it is to prove consistent with the economic goals defined by the current government.

This report attempts to respond to both of these concerns. The first section offers an analysis of the existing labor market information and comments on the adequacy of the techniques employed to measure unemployment. The second part addresses the longer-term issues of employment creation and the possible obstacles posed by the institutional arrangements governing employment relationships.

I. The Measurement of Employment and Unemployment

The principal source of information about labor market conditions is the Direccion de Estadistica y Censo, a dependency of the Contraloria General de la Republica. The Direccion conducts a household survey in August of each year and publishes the results in Situacion Social, Estadisticas del Trabajo. Unfortunately, this cannot be relied upon to provide a timely reading of the labor market, for there are long delays between the completion of the survey and its processing and publication. For example, the 1989 survey has yet to appear; however, we were fortunate to be given access to the tabulations that are now ready to go to press. During 1990, the household survey was not conducted since resources were devoted to the enumeration and processing of the population census that was undertaken during the month of May. That inquiry contains a limited amount of information pertaining to employment on which we will comment below. To date, results have been published for only the District of Panama and for San

Miguelito. Thus, the last reading of labor market conditions that is available to us is already more than a year old.

If one were to take the labor force statistics provided by the Direccion at face value, one would conclude that the decade of the 1980s witnessed a gradual deterioration in employment conditions that was accentuated at the end of the decade by the political and economic crisis that engulfed the country. A summary of the relevant statistics as reported appears in Table 1. Over the decade 1979-89, the population of labor force age (15 years and above) and the labor force grew at approximately the same rate, between 3.1 and 3.2 percent, while employment expanded more slowly at 2.3 percent per annum. The discrepancy in the two rates obviously must be reflected in a rising rate of unemployment.

A more detailed examination of the data reveals patterns that, in most cases, are consistent with those found in other Latin American countries or in less developed countries generally. There has been a decline in labor force participation rates among the oldest age groups of male workers that has been offset by increases in those of individuals aged 15 to 24 as well as among older women under 60 years of age. The increases and decreases have pretty much cancelled each other out, thus yielding a fairly stable overall participation rate. The rise in female participation rates is likely to be attributable to the increasing levels of education among women as well as declining fertility rates, changes that increase the availability of women for employment and improve their earnings potential. It is also likely to be associated with the

TABLE 1. Labor Force, Employment and Unemployment, 1979-89

| Year (August) | Population Age 15 and over | Labor Force | Participation Rate (%) | Employment | Unemployment | Unemployment Rate (%) |
|---|-------------------------------|-------------|---------------------------|------------|--------------|--------------------------|
| 1979 | 1,039,653 | 598,904 | 57.6 | 546,315 | 52,589 | 8.8 |
| 1982 | 1,140,757 | 612,566 | 53.7 | 561,064 | 51,502 | 8.4 |
| 1983 | 1,179,791 | 661,564 | 56.1 | 597,345 | 64,219 | 9.7 |
| 1984 | 1,217,841 | 682,732 | 56.1 | 613,937 | 68,795 | 10.1 |
| 1985 | 1,256,762 | 715,224 | 56.9 | 626,973 | 88,251 | 12.3 |
| 1986 | 1,294,886 | 719,574 | 55.6 | 643,827 | 75,747 | 10.5 |
| 1987 | 1,334,048 | 769,439 | 57.7 | 678,314 | 91,125 | 11.8 |
| 1988 | 1,373,790 | 782,172 | 56.9 | 654,405 | 127,767 | 16.3 |
| 1989 | 1,414,180 | 820,042 | 58.0 | 686,334 | 133,708 | 16.3 |
| Annual Rate of Growth 1979-89 (%) | 3.1 | 3.2 | | 2.3 | 9.8 | |

Source: Contraloría General de Panama, Dirección de Estadística y Censo

increasing concentration of population in urban areas where employment opportunities for women are more numerous. This is reflected in a much higher participation rate for women in the metropolitan area at 41.9 percent as opposed to 27.6 percent in the rest of the country.

According to the tabulations of the Direccion, the unemployment rate reveals a gradual upward trend during the early and middle years of the decade of the 1980s, moving from the 8 to 10 percent range in the former to a 10 to 12 percent range in the latter. With the onset of the crisis, the unemployment rate rises sharply to 16.3 percent during the last two years of the decade. Unemployment rates in predominantly urban areas, as represented by the Metropolitan Region, exceed those in the Rest of the Country, largely rural; in Panama in 1989, the two areas reported rates of 20.4 and 10.7 percent respectively, little changed from 1988. Female unemployment rates surpass those of males by a significant margin of 21.6 to 13.7 percent, a relationship similar to that in other countries. Over time, the unemployment rate of women relative to that of men has been declining; whereas female rates during the 1960s and 1970s tended to be at least double those of men, during the 1980s the difference has narrowed to one of about 50 percent.

As in other countries, unemployment is clearly a declining function of age. The young are much more heavily represented among the unemployed than are older groups. For example, in 1989, individuals ages 15 and 24 represented only 26 percent of the labor force but fully one-half of the unemployed. As one moves into

the mature population, the incidence of unemployment declines sharply. For example, through most of the 1980s, unemployment rates among the young 15 to 24 years of age were typically on the order of eight times those reported by adults in their 40s and 50s, a ratio that is markedly greater than that found in most countries. Only during the last two years of the decade did the ratio of youth to mature worker unemployment rates decline to between 4 and 5, a consequence of increases in unemployment among the mature population. See Table 2.

The higher rates that are found among the young can generally be explained by reference to factors such as the following. As new entrants to the labor force, they are engaged in a process of "shopping" for a job to which they would be willing to commit. Because this search involves a process of trial and error, the young more frequently move among jobs than do adults, and therefore are more likely to be caught in a state of unemployment at any moment in time. This behavior is evidenced in the much higher rate of voluntary quits among the young. According to the 1988 household survey of the Direccion, fully 30 percent of unemployed teen-age workers in the metropolitan area became unemployed as a result of voluntary quits. This contrasts with only 7.2 percent of the unemployed aged 40-49.

Furthermore, because such individuals are more likely to be still living at home, they may enjoy the luxury of family support during their search for a "desirable" job. In other countries it is common to find unemployment rates higher among young people with

Table 2. Unemployment Rates by Age and Sex, 1982-1989

| Age & Sex | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 |
|-----------|------|------|------|------|------|------|------|------|
| TOTAL | 8.4 | 9.7 | 10.1 | 12.3 | 10.5 | 11.8 | 16.3 | 16.3 |
| 15 - 19 | 22.4 | 23.3 | 25.1 | 27.5 | 25.8 | 28.0 | 30.9 | 33.5 |
| 20 - 24 | 19.0 | 20.5 | 21.6 | 20.7 | 22.9 | 23.3 | 31.2 | 30.3 |
| 25 - 29 | 10.0 | 10.7 | 11.7 | 15.3 | 11.9 | 15.3 | 20.7 | 20.0 |
| 30 - 39 | 4.1 | 5.7 | 6.0 | 7.6 | 5.8 | 6.9 | 11.2 | 11.5 |
| 40 - 49 | 2.2 | 3.9 | 2.6 | 3.8 | 3.7 | 3.5 | 7.1 | 7.6 |
| 50 - 59 | 2.3 | 3.4 | 2.5 | 3.0 | 2.2 | 3.6 | 6.6 | 5.9 |
| 60 - 69 | 2.4 | 2.5 | 3.3 | 2.4 | 2.7 | 3.3 | 5.4 | 3.3 |
| 70 & Over | 1.7 | 3.0 | 0.2 | 2.3 | 1.8 | 3.4 | 3.3 | 3.5 |
| WOMEN | 13.3 | 14.5 | 14.2 | 18.5 | 14.5 | 16.7 | 21.4 | 21.6 |
| 15 - 19 | 29.0 | 31.4 | 32.4 | 38.0 | 33.0 | 35.2 | 43.1 | 43.6 |
| 20 - 24 | 27.4 | 27.2 | 28.4 | 38.8 | 31.3 | 32.8 | 41.2 | 42.2 |
| 25 - 29 | 13.0 | 15.1 | 15.3 | 21.8 | 14.8 | 21.7 | 48.6 | 28.0 |
| 30 - 39 | 7.4 | 8.9 | 9.2 | 11.0 | 8.2 | 10.4 | 13.3 | 13.4 |
| 40 - 49 | 3.1 | 6.7 | 3.1 | 5.3 | 4.0 | 4.5 | 7.0 | 8.3 |
| 50 - 59 | 5.4 | 4.0 | 1.1 | 5.1 | 1.3 | 3.5 | 4.4 | 4.1 |
| 60 - 69 | 2.7 | 0.8 | 5.6 | 1.3 | 2.9 | 3.9 | 6.6 | 0.4 |
| 70 & Over | - | 3.2 | - | 4.2 | 2.0 | 3.1 | - | 5.4 |
| MEN | 6.3 | 7.7 | 8.2 | 9.5 | 8.7 | 9.4 | 14.0 | 13.7 |
| 15 - 19 | 19.0 | 19.9 | 21.9 | 23.2 | 22.7 | 24.8 | 25.9 | 29.0 |
| 20 - 24 | 14.5 | 17.0 | 18.2 | 20.2 | 18.4 | 18.2 | 26.1 | 23.9 |
| 25 - 29 | 8.2 | 8.2 | 9.6 | 11.7 | 10.2 | 11.7 | 16.8 | 15.7 |
| 30 - 39 | 2.5 | 4.1 | 4.2 | 5.6 | 4.4 | 4.7 | 10.0 | 10.3 |
| 40 - 49 | 1.9 | 2.8 | 2.3 | 3.1 | 3.5 | 3.1 | 7.2 | 7.2 |
| 50 - 59 | 1.5 | 3.3 | 2.9 | 2.4 | 2.4 | 3.6 | 7.3 | 6.4 |
| 60 - 69 | 2.3 | 2.7 | 2.8 | 2.6 | 2.6 | 3.2 | 5.2 | 3.9 |
| 70 & Over | 1.9 | 3.0 | 0.3 | 2.0 | 1.3 | 3.4 | 3.6 | 3.2 |

higher levels of education. For them, unemployment may represent an investment in their search for a "good" job. To the extent that higher educational levels are also associated with higher family incomes, such youths can better "afford" the luxury of unemployment. But even youths less bountifully endowed with education or family resources may still be able to count on family support during a job search.

Finally, from the vantage point of employers offering preferred employments, they may be hesitant to employ workers with little or no job experience or skills. Thus, it is not unusual to find young entrants to the labor market moving from one short-term and relatively low-wage employment to another until they acquire enough experience to appear attractive to employers offering jobs on more attractive terms.

One of the conditions that may be more indicative of the state of the labor market than the level of unemployment is the duration of unemployment. A short duration of unemployment is likely to characterize a labor market in which employment opportunities abound so that the time expended in job search is short. As employment conditions deteriorate, the number of job opportunities shrink, open unemployment increases, and the duration of unemployment also increases. In Panama, employment opportunities are generally believed to have shrunk, and measured unemployment has certainly increased. Yet, until the severe crisis beginning in 1988, there was no apparent tendency for the duration of unemployment to increase. As can be seen in Table 3, for example

among men in the metropolitan area, the proportion of the unemployed reporting a duration of under six months fluctuates widely but evinces no trend. In 1988, however, one can detect a decline in the proportion of the shortest-term unemployed from 53.1 percent in 1987 to only 36.1 percent in 1988. The proportion with a duration of unemployment between 6 and 12 months, on the other hand, doubled from 12.8 to 24.8 percent. In 1989, a further lengthening of the duration of unemployment is discernable; more than half the unemployed now report a duration in excess of a year.

A similar pattern is discernable among women in the metropolitan area and among both sexes in the rest of the country. Note, however, that the duration of unemployment has been consistently shorter for men in the rest of the country while that for women exceeds that for those in the metropolitan area. These contrasts probably are explainable, in the case of men, by the heavier incidence of agriculture and the greater availability of casual employment associated with that sector. In the case of women, the longer duration is probably a function of a greater scarcity of job opportunities in rural areas than exists in the larger urban areas.

Thus far, we have recorded the course of unemployment as defined by the Direccion. It is useful to recall that there is another source of information regarding the labor force and its employment status, the population census. While the 1990 census results are not yet available for the whole country, those for the Districts of Panama and San Miguelito are. These therefore do offer

Table 3. Percentage Distribution of Unemployed Workers by Duration of Unemployment Region, and Sex 1982 - 1989 (1)

| Region & Year METROPOLITAN REGION | Duration and Sex | | | | | | | | | |
|---|-------------------------|------|-----------|------|----------|------|--------------------|------|---------|-----|
| | Less than Six Months | | 6-12 Mos. | | 1-2 Yrs. | | 3 or More Years | | N.A.(2) | |
| | M | W | M | W | M | W | M | W | M | W |
| 1982 | 54.2 | 30.5 | 15.4 | 12.2 | 20.3 | 35.0 | 9.5 | 20.8 | 0.7 | 1.4 |
| 1983 | 46.7 | 33.0 | 20.4 | 17.1 | 24.2 | 28.7 | 8.1 | 17.5 | 0.4 | 3.6 |
| 1984 | 40.3 | 32.7 | 24.3 | 16.3 | 23.9 | 28.3 | 10.7 | 21.9 | 0.9 | 0.7 |
| 1985 | 49.4 | 28.2 | 13.2 | 17.2 | 25.0 | 34.4 | 11.7 | 18.5 | 0.7 | 1.7 |
| 1986 | 47.7 | 33.8 | 14.7 | 12.1 | 24.6 | 33.6 | 11.6 | 18.8 | 1.3 | 1.7 |
| 1987 | 53.1 | 38.4 | 12.8 | 13.0 | 21.1 | 25.6 | 13.1 | 21.6 | - | 1.3 |
| 1988 | 36.1 | 31.6 | 24.8 | 19.8 | 26.9 | 30.3 | 11.8 | 16.7 | 0.4 | 1.6 |
| 1989 | 34.6 | 23.3 | 11.1 | 12.5 | 34.2 | 36.4 | 20.1 | 26.5 | - | 1.3 |
| REST OF COUNTRY | | | | | | | | | | |
| | M | W | M | W | M | W | M | W | M | W |
| 1982 | 59.3 | 43.2 | 25.9 | 18.8 | 13.2 | 25.4 | 3.0 | 11.8 | 0.4 | 0.8 |
| 1983 | 62.2 | 42.7 | 18.3 | 14.8 | 15.6 | 23.6 | 3.9 | 14.2 | - | 4.8 |
| 1984 | 53.3 | 38.1 | 19.5 | 23.8 | 19.7 | 24.9 | 6.9 | 11.5 | 0.7 | 1.6 |
| 1985 | 64.5 | 33.6 | 13.1 | 19.3 | 16.5 | 28.5 | 4.5 | 17.6 | 1.3 | 1.0 |
| 1986 | 61.8 | 39.9 | 14.5 | 15.1 | 14.5 | 30.0 | 8.8 | 12.3 | 0.4 | 2.8 |
| 1987 | 61.7 | 39.4 | 13.7 | 13.9 | 15.6 | 32.6 | 8.7 | 12.1 | 0.3 | 2.1 |
| 1988 | 41.6 | 30.0 | 24.0 | 19.5 | 24.3 | 31.9 | 9.6 | 17.6 | 0.5 | 1.1 |
| 1989 | 45.2 | 35.7 | 17.0 | 15.9 | 25.1 | 30.9 | 12.7 | 17.1 | - | 0.5 |

Source: Contraloria General de la Republica, Direccion de Estadisticas y Censo.

Notes: 1. The unemployed recorded here include only those who became unemployed by virtue of separation from a prior employment. New labor force entrants are excluded.

2. N.A. - no answer

a basis of comparison with 1980. This comparison reveals that in 1980, these two districts together reported an unemployment rate of 10.7 percent, as compared to the national rate of 8.4 percent. The 1990 census reports an unemployment rate for these same two districts of 13.9 percent.¹ This stands in sharp contrast to the rate of 20.4 for the metropolitan area recorded in August 1989 by the household survey. One would not expect the rate in these two districts to depart so widely from that for the metropolitan area nor is it reasonable to believe that the true rate of unemployment could have fallen so sharply over an interval of only nine months. No attempt will be made to resolve or explain these differences at this point. I will return to an evaluation of the statistics later in this report.

There are other developments regarding the 1980s that are worthy of comment. The 1980s saw little in the way of structural change of the economy. The distribution of the labor force over the various sectors shows little variation between 1982 and 1989 according to the Direccion's household survey. The one exception is the construction sector that virtually collapsed during the economic crisis of 1988-89. Another notable feature of the 1980s is the absence of any growth in the productivity of the labor force. The gross domestic product divided by the employed labor force yields an annual output per worker of 3,125 balboas (of 1970) in 1980, 3,123 and 3,131 balboas in 1984 and 1987, respectively. The sharp decline in economic activity in 1988 and 1989 without a commensurate decline in total employment is reflected in a sharp

fall in output per employed worker to 2,568 balboas in 1989, a drop of 18 percent.²

An economy in which productivity is stagnant can hardly be in a position to improve the real wages of workers unless it is at the expense of some other economic group's share of total output. So, it should come as no surprise if real wages were to prove equally stagnant. Unfortunately, Panama does not publish earnings data for the entire labor force based on its household survey. Rather, it limits its publication to the median earnings only of wage earners. Detailed distributions of earnings of public sector workers are provided, including both the central government and autonomous agencies. Also published is a separate accounting of earnings in the banana producing regions. More complete coverage is provided by the population census; cash earnings for all classes of employed workers appear.

Since 1986, the Direccion has not published earnings data for private sector employees on a national basis. Such data are available for the 1980-86 interval. Over that span of time, real monthly wages remained virtually constant at 336.78 and 334.14 balboas in the end years, both values in balboas of 1980.³ For the latter part of the decade, earnings for all salaried employees are available for the metropolitan area alone. In contrast to the average monthly earnings given above, the series for the metropolitan area presents median weekly earnings. Between 1984 and 1986, real median earnings rose by 4.6 percent, only to fall back to the 1984 level by 1989. (See Table 4)

Table 4. Earnings, Various Year 1980 – 1989

4.A Average Real Average Monthly Earnings by Sector
(Balboas of 1980)

| Year | Private Business Firms | Banana Zones | Central Government | Public Autonomous Agencies | Municipalities | Canal Zone |
|--------------------|------------------------|--------------|--------------------|----------------------------|----------------|--------------|
| 1980 | 336.78 | 335.10 | 317.25 | 349.03 | 215.63 | 1,036.22 |
| 1981 | 332.02 | 336.58 | 305.05 | 347.81 | 204.90 | 985.21 |
| 1982 | 336.15 | 303.87 | 294.96 | 362.98 | 198.77 | 1,136.46 |
| 1983 | 331.92 | 309.89 | 320.63 | 385.04 | 206.27 | 1,123.05 |
| 1984 | – | 312.73 | 331.66 | 382.44 | 212.46 | 1,141.06 |
| 1985 | – | 318.63 | 338.35 | 414.95 | 212.79 | 1,179.60 |
| 1986 | 334.10 | 330.72 | 338.05 | 417.30 | 215.82 | 1,264.37 |
| 1987 | – | 331.70 | 344.55 | 446.89 | 228.50 | – |
| 1988 | – | 335.72 | 346.04 | 445.20 | 225.78 | 1,268.00 (E) |
| 1989 | – | 285.27 | 344.03 | 444.02(P) | 226.39(P) | 1,333.54 (E) |
| Percentage 1980–89 | | –14.9 | 8.4 | 27.2 | 5.0 | 12.9 |

4.B Median Real Weekly Earnings of Employees, Metropolitan Region, 1984 – 89 (Balboas of 1984)

| Year | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 |
|----------|------|-------|-------|-------|-------|-------|
| Earnings | 69.7 | 69.90 | 73.07 | 71.57 | 71.48 | 69.96 |

Source: Direccion de Estadisticas y Censo, Situation Social, Estadisticas del Trabajo, various issues.

It is difficult to know how representative the median earnings recorded in this table are of average earnings. In 1986, it was possible to compare average and median earnings for a given population, that of private sector employees. That comparison yielded a large difference, fully 25 percent, between the two, an average monthly earnings of 336.78 balboas against a median of only 268.84. The difference between the two measures of wages is smaller in the central government at 13.4 percent but wider in the autonomous public sector at 32.8 percent. The published data seem to reflect wage structures in which the bulk of employees are concentrated within a rather narrow range of salaries and in which professionals and managerial personnel enjoy large differential earnings over the former. As long as the distribution of employees through the wage structure remains relatively stable, the rate of change in earnings should be similar regardless of whether one resorts to the mean or the median.

Given the diverse wage series at our disposal it is possible to infer at least the direction in the change in real earnings in the private firm sector. Since the series of weekly earnings of all salaried personnel in the metropolitan area yields a virtual constancy in real earnings at the same time that the published data for the public sector reveal substantial increases, it follows that earnings in the private sector must have fallen significantly relative to the public sector. Our estimate of the decline in the real earnings of private sector employees in the metropolitan area is on the order of 5.6 percent between 1984 and 1989. Actually,

this does not represent a full measure of the gain of public sector employees since employment in the public sector expanded at a slightly more rapid rate than in the private sector over the same interval.

The partial earnings data that are available from the census of 1990 provide another reference point for assessing the evolution of earnings over the whole decade but for only two districts, those of Panama and San Miguelito. Table 5 summarizes the earnings data by economic sector. It must be emphasized that the grouping of various productive activities is not the same for the two years. We have tried to assemble the 1990 data to correspond to those of 1980. However, we are aware that the correspondence is not perfect so there is a margin of error that cannot be specified. The data for the trade and service sectors are those that are likely to contain the largest errors.

The median real earnings over the decade for all sectors reveals only a slight increase of 1.8 percent. However, there are wide differences in the size of the change as among sectors. Large relative gains appear to have been made by workers in agriculture, public utilities and transportation and communications. Manufacturing and services, which includes the central government, report virtually constant real earnings. The largest loss of earnings were suffered in construction, still suffering from a very sharp decline at the time of the census, the financial sector, and the tiny mining sector. The trade sector reports a decline, but part of that may be due to the addition of activities to this

Table 5. Employment and Median Monthly Earnings by Sector, Province
Province of Panama 1980 and Districts of Panama and San Miguelito 1990

| Sector (3) | 1980 | | 1990 | | % Change in Earn- ings |
|------------------------------------|---------------------|---|---------------------|---|------------------------------|
| | Employ- ment (2) | Median Monthly Earnings (1980 B/.) | Employ- ment (2) | Median Monthly Earnings (1980 B/.) | |
| Agriculture & Fishing. | 21,048 | 91.7 | 6,766 | 121.8 | 32.8 |
| Mining | 191 | 272.9 | 176 | 236.0 | -13.5 |
| Manufacturing | 30,910 | 206.2 | 33,073 | 203.9 | - 1.1 |
| Public Utilities | 4,707 | 325.4 | 3,866 | 425.0 | 30.6 |
| Construction | 17,686 | 207.1 | 11,663 | 171.8 | -17.0 |
| Trade, Hotels & Restaurants | 43,225 | 210.3 | 67,635 | 197.9 | 5.9 |
| Finance & Real Estate | 16,024 | 363.6 | 22,023 | 326.2 | -10.3 |
| Transportation & Communications | 15,815 | 275.2 | 22,816 | 350.4 | 27.3 |
| Services | 81,519 | 227.1 | 99,182 | 229.3 | 1.0 |
| Not elsewhere classified | 4,497 | 205.5 | 8,144 | 170.4 | -17.1 |
| TOTAL | 235,622 | 227.6 | 275,344 | 231.7 | 1.8 |

Source: Direccion de Estadística y Censo, Censos Nacionales de 1980, Vol. IV Características Económicas, Table 17; Censo Nacionales de Población y Vivienda, May 13, 1990, Table 9.

- Notes: 1. Median Earnings of those reporting income only.
2. Employment includes all workers.
3. The sectoral classifications are not strictly comparable for the two years for the trade and service sectors. Certain repair services moved from services to the trade sector.

sector that may be relatively low-wage. Similarly, it is impossible to evaluate the sharp drop in the unclassified category since its composition may have undergone substantial changes.

These wage data do not suggest a decade of as serious or as general a deterioration in employment conditions as do the measures of open unemployment. Indeed, the wage data suggest a decidedly mixed picture with gains for some groups of workers and losses for others. The relative stability of earnings in the face of such a sharp drop in national income is probably attributable, at least in part, to the downward wage rigidity that is provided for by the labor code. Thus, the response to an economic crisis such as that of 1988-89 is more likely to be reflected in employment adjustments rather than in wages.

Another way of assessing changes in the quality of employment is by observing changes in distribution of the labor force by employment status. From the household surveys, one can observe the impact of the crisis on the components of the work force. (See Table 6) Following a slow growth in the early years of the decade, wage employment is reported to have declined in 1988 by 12 percent, largely the result of an almost 17 percent decline in private sector employment. Remarkably, wage employment is held to have recovered half the 1988 loss in 1989 even as the crisis deepened, a rather unlikely occurrence. Two other components that are considered to represent inferior employment conditions increased in number, self-employed and unpaid family workers. The former recorded a 30,000 person increase between 1987 and 1989, while the

Table 6. Employed Work Force Aged 15 Years & Over by Employment Status, 1984-89

| Employment Status | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 |
|-----------------------|---------|---------|---------|---------|---------|---------|
| Total | 613,937 | 626,973 | 643,827 | 678,314 | 654,405 | 686,334 |
| Salaried Employment | 414,730 | 411,671 | 431,558 | 447,165 | 393,476 | 422,561 |
| Government | 149,701 | 147,039 | 153,404 | 153,101 | 145,063 | 149,132 |
| Private Sector | 250,579 | 249,668 | 263,908 | 276,784 | 229,995 | 252,394 |
| Canal Zone | 14,450 | 14,964 | 14,246 | 17,280 | 18,418 | 21,035 |
| Self-employed | 157,026 | 174,774 | 168,630 | 175,572 | 197,142 | 206,793 |
| Employers | 14,761 | 10,053 | 12,931 | 13,856 | 16,468 | 13,498 |
| Unpaid Family-Workers | 27,420 | 30,475 | 30,708 | 41,721 | 47,319 | 43,482 |

Source: Direccion Estadisticas y Censo, Situacion Social, Estadisticas del Trabajo

latter, at its height in 1988, numbered almost 17,000 over 1986 levels. Then we observe an unexpected decline in unpaid family workers in 1989.

As before, we do have recourse to census data for comparisons of the distribution of the labor force by status as between 1980 and 1990. The censuses also have an added advantage of providing earnings data for the various labor force groups. Again, however, we are limited to the fragmentary data represented by the districts of Panama and San Miguelito for 1990 and for the province of Panama for 1980. The data are recorded in Table 7. To the self-employed and the unpaid family workers we have added another category of what might be considered an inferior employment status, temporary workers. This comparison suggests an improvement rather than a deterioration over the decade. The proportion of employed workers engaged as temporary workers shows a small decline as a proportion of total employment. Furthermore, median earnings for this class of worker rose relative to those of permanent workers. The self-employed increased from 13.5 to 18.6 percent of total employment, while unpaid family labor proved insignificant in both years. However, median earnings of the self-employed rose in real terms by over 20 percent in the inter-censal period and gained significantly on the median earnings of permanent employees.

Of course, observation of only the end points, 1980 and 1990, tells us nothing about the possible course of earnings in the intervening years; thus, it is entirely possible that the 1990 observation does represent a decline from a higher level in the

Table 7. Employed Labor Force by Selected Categories of Employment Status and Earnings 1980 and 1990: Province of Panama

| | Employment Status | | | | Total Employment |
|---|-------------------|---------------|----------------------|---------------------|------------------|
| | Temporary Worker | Self-Employed | Unpaid Family Worker | Permanent Employees | |
| 1980 - Province of Panama | | | | | |
| Number | 37,665 | 33,713 | 3,626 | 169,286 | 248,302 |
| % of Total | 15.2 | 13.5 | 1.5 | 68.2 | |
| Median Monthly Earnings (balboas) | 143.6 | 112.80 | - | 267.2 | 227.6 |
| % of Permanent Employees' Earnings | 53.7 | 42.2 | | | |
| 1990 District of Panama & San Miguelito | | | | | |
| Number | 45,665 | 51,942 | 1,653 | 175,273 | 249,811 |
| % of Total | 16.3 | 18.6 | 0.6 | | |
| Median Monthly Earnings (balboas) | 164.25 | 164.34 | - | - | 278.53 |
| % of Permanent Employees' Earnings | 48.1 | 48.2 | | | |

Source: Dirección de Estadísticas y Censo, Censos Nacionales de 1980, Vol. IV, Características Económicas, Table 18; Censos Nacionales de Población y Vivienda, Resultados Finales Básicos para los Distritos de Panama y San Miguelito, Table 10.

intervening years, although the household survey data would seem to indicate that the decade did not see much variation in earnings on average.

What is the upshot of all these comparisons? It is probably easier to say what they do not show rather than what they do show. They do not seem to indicate a wholesale and deep deterioration in working conditions. True, the unemployment level has increased, though the precise margin of increase is open to question given the large difference between the household survey and census results. Nor do the earnings data that we have assembled from both sources point to a drastic decline even for those categories of labor whose wages are likely to be market determined. Indeed, how earnings levels could be maintained in the face of such a sharp drop as is purported to have occurred in the gross domestic product poses a mystery that suggests substantial qualitative problems with the data. However, a caveat must be entered at this point. Recall that the census data that we reviewed are limited to only a part of the metropolitan area and do not shed any light as to what may have occurred in the rest of the country. If there is reason to believe that the economy of the rest of the country marches to a radically different drum than does the metropolitan area, it may be inadvisable to project changes observable in the latter to the whole country.

Having said that, however, it is appropriate at this point to offer some observations about the data with which we have had to work. It seems to us that it is very difficult to draw firm

conclusions from the available data regarding the course of output and employment over the past three years. As given, these data do not fit together in a way that yields a consistent story. The lack of correspondence between the two series leads us to suggest that the one or both of these statistical series may be flawed.

Throughout the 1980s, the employment series reveal year-to-year fluctuations in their components, as for example in labor force participation rates, that are not credible. The fact that three-fourths of the households surveyed in any one year are identical to those surveyed the previous year would lead one to expect a higher degree of stability in most of the population and labor force components than the Panamanian series evince. A critical year for evaluating the impact of the crisis of 1988 is that of 1987. In Table 6 we presented total employment broken down by employment status. According to the data, employment in 1987 increased sharply, by 6.8 percent over 1986 in spite of a modest increase in GDP of only 2.3 percent. (The labor force is reported to have increased by 6.9 percent.) In order to fully appreciate the lack of correspondence between employment and output changes, we offer in Table 8, employment levels by industrial sector from 1985 to 1989.

Manufacturing employment in 1987 is shown to have increased by over 8,000, or 13 percent, in the face of an increase in output of only 3.7 percent.⁴ The trade sector is reported to have undergone an increase in employment of almost 14,000, or 15 percent while its contribution to GDP decreased by 4.7 percent. The service sector

witnesses an increase of 6 percent in employment while output barely increased by less than one percent. If the data for GDP are believed to be reliable for 1986 and 1987, then it becomes difficult to avoid the conclusion that the increases in labor force and employment reported for 1987 are substantially overstated. Not only do they not fit with the output data for that year, but the rates of change in labor force aggregates over the preceding years would not lead one to expect such drastic changes in 1987.

If 1987 data are biased in an upward direction, their comparison with the reported employment levels for 1988 will yield an exaggerated notion of the declines in employment that occurred in the latter. If instead of increasing by 13 percent, as reported by the Direccion, employment had increased in line with the average increase of the decade, 1987 would have reported employment of approximately 658.6 thousand. Compared to this level, the decline in total employment for 1988 would have measured less than one percent! Or compared to 1986, the employment level of 1988 is greater while the GDP is less by some 14 percent. Further, this occurred with no recorded declines in earnings according to the household survey.

Now consider the employment data by economic sector for 1989 presented in Table 8. These show an increase in employment in all sectors save construction in the face of a further decline in GDP. If the drop in output had been as severe as measured, would not one have expected employers to be retrenching in employment? Employment in manufacturing is up over 9 percent in the face of only a 5.3

Table 8. Employed Labor, 15 Years and Older by Sector of Employment,
1985 – 1989

| Sector | Employment | | | | |
|---|------------|---------|---------|---------|---------|
| | 1985 | 1986 | 1987 | 1988 | 1989 |
| Total | 626,973 | 643,827 | 678,314 | 654,405 | 686,334 |
| Agriculture & Fishing | 184,759 | 184,522 | 180,257 | 198,986 | 203,219 |
| Non-Agriculture | 442,214 | 459,305 | 498,057 | 455,419 | 483,115 |
| Mining | 443 | 420 | 490 | 311 | 278 |
| Manufacturing | 66,614 | 64,173 | 72,490 | 61,895 | 67,551 |
| Electricity, Gas, Water | 9,073 | 8,687 | 8,511 | 8,710 | 9,395 |
| Construction | 33,289 | 34,597 | 35,371 | 21,937 | 21,617 |
| Trade, Restaurants & Hotels | 87,149 | 93,480 | 107,256 | 97,218 | 99,068 |
| Transportation, Whare- housing & Communi- cations | 37,368 | 37,558 | 38,247 | 36,827 | 38,591 |
| Finance, Real Estate & Business Services | 24,360 | 26,926 | 27,808 | 23,176 | 25,324 |
| Services, Public & Personal | 168,954 | 179,218 | 190,527 | 186,247 | 199,698 |
| Canal Area | 14,964 | 14,246 | 17,357 | 19,098 | 21,593 |

percent increase in output. If the drop in 1988 output had left firms with redundant labor, would the recovery in output have necessitated new hiring? In the context of a decline in overall output, would one have expected to see a recovery of output of the commerce sector by 3.6 percent as well as an increase of almost 2 percent in employment, particularly in view of the growing liquidity shortage? Nor can these employment increases be dismissed as simply the product of a bulging informal sector, for Table 6 recorded a 9 percent increase in private wage employment in 1989 over 1988.

Another datum that seems inconsistent with a large output drop is the small decline in electricity produced in 1988 from levels of the previous year, only 4.2 percent.⁵ By way of comparison, in 1984, GDP declined by 0.4 percent while electricity production declined by 1 percent, for an elasticity of electricity output to GDP of 6.25. If we apply the same elasticity to the 1988 decline in electricity production, we would have predicted a decline in GDP of only 0.7 percent! While we would not suggest that that was the true measure of the decline in GDP, it departs so far from the measured decline that the latter would seem open to question.

On the other hand, close observers of the Panamanian economy point to the virtual paralysis of some sectors of the economy for a one-to-two month period during 1988 when the liquidity shortage became acute. To the extent that the loss of output of that period was not offset by subsequent increases in output, the recorded decline in GDP would be credible.

What we are suggesting is that we consider it unlikely that both the employment and output data can be representative of reality. Either one or both are misleading. Certainly the employment data are not consistent with an output decline as sharp as that recorded in the national accounts. Is it possible that GDP is understated for 1988 and 1989? Those two years witnessed an increasing liquidity crisis that led firms and individuals to resort to all sorts of barter arrangements in order to maintain production. Is it possible that the usual techniques for measuring output failed to capture non-cash transactions? Since GDP probably understates the contribution to aggregate output of the informal sector because of difficulties of measurement, is it possible that the drop in the measureable formal sector output was not matched in the informal sector? Finally, is it possible that the increasing political uncertainty of these years might have affected the effectiveness of the agencies charged with the collection and processing of information?

Obviously, we are in no position to resolve the contradictions posed by the data we have reviewed. However, we believe that there are grounds for doubting that the crisis produced as deep a drop in output and as great an increase in unemployment as the official data report. It may very well be that the unemployment rate reported by the census for the two districts of the state of Panama, 13.9 percent, is closer to the truth than the 20 percent figure being cited for the metropolitan region for 1990. Since unemployment in the metropolitan region always registers well above

that for the rest of the country, it would follow that the national rate of unemployment lies below that value.^o We may also mention at this point that the way in which unemployment is defined is likely to lead to an overstatement of the actual rate; however, discussion of this issue is deferred to a later section.

II. Employment Prospects for the Future

While the data for the 1980s may not paint as bleak a picture as is generally represented, neither do they offer much room for comfort. In the face of inaction on a broad front of developmental issues, the prospects for improvement in employment and the living standards of the work force would appear to be very poor. The economic recovery that is now under way is not likely to carry with it a significant expansion of employment in preferred sectors. The productive sectors have ample excess capacity of capital and labor with which to expand output. Recall that productivity levels are likely to have declined during the crisis, though probably not in the measure suggested by official data, implying that output levels can increase substantially without increasing employment at least until previous levels of productivity are restored.

In fact, however, it is likely that in many areas the adjustments made in response to the crisis will permit an expansion of output beyond previous levels without significant increases in employment. In the industrial sector, for example, many firms responded to the crisis by seeking ways to improve their efficiency. Private sector representatives pointed to selective

reductions in work forces and an emphasis on increasing the efficiency of existing factors of production. Given the painful lessons learned during the crisis and the current legal constraints on adjustment in work force size, firms have been characterized as very cautious in hiring unless they perceive prospects of sustained growth in output.

The decade of the 1980s has not set a very attractive table for the future. From a high level at the beginning of the decade, gross investment levels declined. From a peak in 1981, it fell by 35 percent in real terms, reaching a low in 1984. Thereafter it recovered partially through 1987, but still remained some 22 percent below the 1981 level. The 1988-90 period appears to have produced no net increase in the capital stock but rather a decline. Thus, the economy's ability to create new employment will be severely limited once current installed levels of capacity are reached.

The 1980's witnessed a much more favorable evolution of employment, up to 1988, than might normally be expected. Employment and output increased at the same rate, yielding a constancy in productivity levels. As we noted earlier, the failure of productivity to increase implied no room for increases in real wages, and, indeed, the decade saw a relative constancy in the average real wage level. Any gains that were made by particular groups, largely those well organized, were offset by losses among others. On the bright side, the failure of wage levels to rise generally probably facilitated the expansion that we have witnessed

in employment and limited the rise in unemployment.

The beginning of the 1990s leaves the economy facing serious challenges. The last few years witnessed a sharp drop in public investment, and it has yet to recover. Infrastructure maintenance and expansion have been deferred as a result of which capacity limits are being reached in electricity and water. The retirement of the United States from the military bases in the canal area will cost the Panamanian economy an estimated 400 million dollars a year. And as a consequence, the local labor market will be faced with the prospect of absorbing several thousand workers accustomed to wage levels more than twice those in the local market. The labor force continues to grow albeit at a slower rate than in the past. Given the constraints on government resources, it will be in no position to absorb more workers in public employment. Indeed, already faced with labor redundancy, government may be forced to retrench employment in order to release resources for more urgent purposes.

Nor do the developmental prospects of Panama look very bright in the absence of substantial reforms. One has only to look around the Caribbean basin to observe the increasing encroachment of other countries in the provision of services that have traditionally been provided by Panama. The current level of uncertainty regarding the economic program of the government and the perception of inaction are said, by the business community, to be retarding a renewal of the investment necessary to the future growth of the economy.

There is no doubt but that reforms are difficult to introduce

since they involve uncertainties regarding the impact they will have on particular economic groups of the society as well as on the growth of the economy as a whole. On the other hand, if reforms are not introduced, what can one expect in the way of future growth of output and employment? Would a projection of past performance into the future suggest an evolution of employment and living standards consistent with the society's expectations? This is the question to which we now turn.

We have attempted to prepare some projections of future employment growth on the basis of a set of "naive" assumptions regarding some of the parameters that govern such growth. Table 9 develops the basic ingredients of the projections. First, we observe the levels of net capital investment in each year of the 1980s and observe their effect on output and employment. The decade up through 1987 is divided into two distinct sub-periods, 1980-83 and 1984-87. During the first of these, capital inflows permitted the achievement of a high rate of investment, though the returns in terms of output were modest. Every increase in GDP of one balboa required net investment of 4.95 in the first sub-period and 4.18 balboas in the second. Among economists, this relationship is referred to as the incremental capital-output ratio or ICOR. For each additional employment created, 51,644 balboas were required in the first period and only 20,750 balboas in the second, thus defining an incremental capital-employment ratio, or ICER. It may be noted in passing that these values compare poorly with those of less developed economies generally.⁷

Table 9. Net Fixed Capital Investment & Changes in Gross Domestic Product
& Employment, 1980 - 1987

| Year | Net Fixed Capital Formation | | Change In GDP | | Incremental Capital Output Ratio | Incremental Employment Ratio |
|------|-----------------------------|----------|----------------------------|----------|----------------------------------|------------------------------|
| | Balboas of 1980 (millions) | % of GDP | Balboas of 1980 (millions) | % of GDP | | |
| 1980 | 614.4 | 17.3 | 164 | | | |
| 1981 | 749.0 | 20.6 | 149 | | | |
| 1982 | 770.0 | 20.2 | 197 | | | |
| 1983 | 502.0 | 13.3 | 22 | | | |
| 1984 | 382.4 | 8.9 | -17 | | | |
| 1985 | 380.4 | 7.6 | 186 | | | |
| 1986 | 454.1 | 8.5 | 137 | | | |
| 1987 | 463.2 | 9.5 | 96 | | | |
| 1988 | 7.9 | | | | | |
| 1989 | N.A. | N.A. | | | | |

| (Balboas of 1980) | | | | | | |
|-------------------|-----------------------------|----------|---------------------|----------------------------|----------------------------------|------------------------------|
| | Total Net Capital Formation | % OF GDP | Total Change In GDP | Total Change In Employment | Incremental Capital Output Ratio | Incremental Employment Ratio |
| 1980-83 | 2,635.4 | 17.8 | 532 | 51,030 | 4.95 | 51,644 |
| 1983-87 | 1,680.1 | 8.6 | 402 | 80,969 | 4.18 | 20,750 |
| 1980-87 | 4,315.5 | 13.2 | 934 | 131,999 | 4.62 | 32,693 |

| (Balboas of 1990) | | | | | | |
|-------------------|-----------------------------|----------|---------------------|----------------------------|----------------------------------|------------------------------|
| | Total Net Capital Formation | % OF GDP | Total Change In GDP | Total Change In Employment | Incremental Capital Output Ratio | Incremental Employment Ratio |
| 1980-83 | 3,373.5 | 17.8 | 681 | 51,030 | 4.95 | 66,108 |
| 1983-87 | 2,150.5 | 8.6 | 515 | 80,969 | 4.18 | 26,560 |
| 1980-87 | 5,523.8 | 13.2 | 1,196 | 131,999 | 4.62 | 41,847 |

Source: GDP and Investment: World Bank, Panama: Policy Issues and Agenda for Action

The large ICOR and ICER of the early 1980s appear to be associated with large public investments in a new airport, convention facilities, and hydroelectric installations. Unfortunately, the returns expected from the first two of these have not been realized. In retrospect, the low returns to capital in terms of both output and employment suggest that the investment resources could have been put to better uses. On the other hand, at least some of the employment and output growth of 1984-87 years may be attributable to the "overinvestment" that occurred earlier, in which case the average values for the entire 1980-87 period, reported in Table 9, may be the most representative.

For purposes of this exercise, we have chosen a value for net fixed capital investment that is closer to that of the second than to the first interval, or 10 percent. This lower value reflects our belief that Panama will not be the beneficiary of the large capital flows from abroad that characterized the early 1980s. While official lending may be resumed, if satisfactory disposition of outstanding issues can be achieved, such flows will be offset, in part, by the debt service obligations that Panama is likely to assume. Indeed, the assumption that all the forthcoming investment will result in an immediate income response is optimistic in view of the amounts that will have to be devoted to simply restore capital stocks to past levels and condition. For the incremental capital-employment ratio we select the one more favorable to employment creation, that of the second interval rather than the average for the whole period.

In Table 10, we present the predicted outcomes. We start with GDPs in 1991 and 1992 growing at an annual rate of 6 percent, increases that will carry the economy back to a level of output approximating that of the pre-crisis year of 1987. This growth is not viewed as a function of investment but rather one of simply exploiting an existing productive capacity. Net investment undertaken in 1992 equal to 10 percent of GDP then is reflected in an increase of GDP in 1993 of 2.4 percent. The constancy in the investment ratio determines a parallel constancy in the rate of growth for the remainder of the decade, given the assumed constant ICOR. The ICER of the second sub-period has been adjusted for price changes and stands at 26,500 balboas of 1990. As can be seen, the growth of employment is not sufficiently rapid to reduce the unemployment rate by very much. By the year 2000, it will still hover close to 14 percent.

More disturbing is the failure of productivity to recover to pre-crisis levels. It will be recalled that we found output per employed person to have remained virtually constant during the 1980s and then to have plunged in the two crisis years, 1988-89. The exercise we have undertaken here suggests little improvement, only 4 percent over 1990, by the year 2000. However, that would still leave productivity almost 16 percent below that of the pre-crisis level of 1987. The last readings on wages that we have, have yet to reflect fully the decline already suffered in productivity so it is reasonable to expect declines in real wages to become more marked. Should this scenario be played out in even approximate

Table 10. Estimates of Gross Domestic Product, Employment and Unemployment,
1990 – 2000

Assumptions:

1. Growth rate of population 15 years and over 2.45 percent
2. Labor force participation rate: 1990–95 .58; 1995–2000 .59
3. Net fixed investment as percent of GDP 10.0
4. Incremental capital – output ratio 4.18
5. Incremental capital – employment ratio 26,500 Balboas.

All monetary values are in Balboas of 1990

| Year | G D P | | Net Capital Formation | Employ- ment | Labor Force | Unemployment | |
|------|---------------------|-------------------|--------------------------|-----------------|----------------|--------------|---------|
| | Millions Balboas | Percent Change | | | | Number | Percent |
| 1990 | 4,885.0 | | | 738,294 | 878,922 | 140,628 | 16 |
| 1991 | 5,178.1 | 6.0 | | 756,382 | 900,455 | 144,073 | 16 |
| 1992 | 5,488.8 | 6.0 | 549 | 784,138 | 922,516 | 138,378 | 15 |
| 1993 | 5,620.1 | 2.4 | 560 | 804,855 | 945,118 | 140,263 | 14.8 |
| 1994 | 5,754.1 | 2.4 | 575 | 825,987 | 968,273 | 142,286 | 14.7 |
| 1995 | 5,892.2 | 2.4 | 589 | 847,685 | 991,996 | 144,311 | 14.5 |
| 1996 | 6,033.6 | 2.4 | 603 | 869,911 | 1,016,300 | 146,389 | 14.4 |
| 1997 | 6,178.4 | 2.4 | 618 | 892,666 | 1,041,999 | 148,533 | 14.3 |
| 1998 | 6,326.7 | 2.4 | 633 | 915,987 | 1,066,708 | 150,721 | 14.1 |
| 1999 | 6,478.5 | 2.4 | 648 | 939,874 | 1,092,843 | 152,969 | 14.0 |
| 2000 | 6,634.0 | 2.4 | 663 | 964,327 | 1,119,618 | 155,291 | 13.9 |

form, one can foresee a troublesome decade of frustrated expectations and socio-economic conflict as economic groups battle over a pie that grows no faster than the labor force.

We would be hard pressed to defend the above exercise as a definitive statement of coming events. It does not take into consideration all of the variables, favorable as well as unfavorable, that determine economic welfare. However, in order to compensate for the favorable impact of any omitted variables we purposely drew from the past, values for parameters of the exercise that would yield the most optimistic outcome. Thus, should new investment be allocated as inefficiently as in the past even these estimates on output and employment creation will prove to have been overestimated. Furthermore, the exercise does not factor in the possible negative effects on employment and unemployment levels of the retirement of U.S. military bases from the Canal area.

There is one important policy implication that can be drawn from the analysis thus far that has an immediate relevance. We take note of press reports that the Ministry of Labor is undertaking a reassessment of the legal minimum wage with an eye to its increase. In view of the fact that productivity levels have fallen sharply since the last adjustment of the minimum and that prospects for restoring these to past levels are not bright, a strong case can be made against any increase at this time. As we have pointed out, in the presence of stagnation in output per head, any move that improves the position of any one group must involve the deterioration of the position of others. And those "others" are

more likely to include the poorest elements of the society, not the richest.

Nor is it valid to argue that, because earnings in some sectors are already above the minimum wage, an increase would have only a limited unfavorable impact. (Indeed, if this were the case, one might legitimately ask why an increase in the minimum would be desirable or necessary.) If the argument in favor of an increase is based on the observation of average earnings levels, it should be recalled that an average is composed of values both above and below the average and, thus, provides no information regarding the impact of a change in the minimum wage. One need only consult the earnings distributions available from census and household survey data to observe a significant proportion of workers whose earnings would appear to be below the legal minimum. Furthermore, what this argument also overlooks is the ratcheting effect such an increase would have. In many sectors, such as manufacturing, the minimum wage serves as an entry wage. If that is increased, the relation of that wage to the wages of existing employees changes. Earnings of new and low-skill workers will gain relative to the earnings of the skilled and experienced. This, in turn, generates pressures for wage increases for the rest of the workers in order to restore previous occupational wage differentials. Thus, not only would an increase at this time have an adverse effect on income distribution but it also would encourage a greater substitution of capital for labor, inhibit the growth of labor-intensive activities, and contribute to a deterioration in employment conditions for a large

proportion of the labor force.

III. The Regulation of the Terms of Employment

One of the issues that is invariably raised by the business sectors whenever the subject of economic reform is broached is that of government regulation of conditions, particularly as prescribed by the Labor Code and the associated enforcement procedures. The present code dates back to 1972 and a newly empowered military government anxious to curry political support. The result was a code that defines conditions and terms of employment in great detail and provides for minimum terms of employment that must rank among the most liberal in the world as viewed from the perspective of workers fortunate enough to be employed in jobs where the law can be enforced. As a result of the law's "largesse" it is charged that Panamanian labor is very expensive and renders Panamanian products non-competitive with goods produced abroad in the absence of generous tariff protection.

Before addressing the question of whether or not Panamanian labor is really "dear" and, therefore, renders Panamanian goods non-competitive, let us review some of the provisions of the law that are at issue. Panama has in place a minimum wage regime that provides for different minima across regions and occupational groups. While the law provides for a periodic determination of the minimum not to exceed two years, the current minimum was established in 1982 and has not been reviewed since. For the Metropolitan Region, a minimum of 78 cents per hour was set, or

approximately 162 balboas per month for a full-time covered employee working a standard 48-hour week. This represents the highest of the several regional rates in force. Payroll taxes for social security, workers' education, and compensation for injury increase payroll costs by 15.42 percent. In addition, all workers are entitled to 30 days paid vacation and 18 days of sick leave, days that, in practice, are taken as additional vacation, according to one source.⁸ Finally, each worker is entitled to a 13th month's pay as an annual bonus. These taxes and benefits raise the cost of each hour actually worked by 42 percent over the net wage. Thus, for a worker employed at the legal minimum wage of 78 cents, the hourly cost of labor is B/.1.11.

However, we must counsel some caution in interpreting the cost of these various fringe benefits. What is significant about these is not merely their existence but rather their economic incidence, that is, the ultimate resting place of their cost. In other contexts, it appears that part of their cost is shifted back on to workers themselves. That is, these costs are offset by providing for a lower wage rate than would otherwise have been paid. To the extent that that occurs, one cannot dismiss the entire monetary cost of these fringes as having a negative effect on employment. Of course, in the case of those workers employed at the legal minimum wage, this burden cannot be shifted back unless the real minimum wage is allowed to drift downward. This study cannot pretend to undertake an examination of the incidence issue, but that should not be interpreted to mean that we consider it irrelevant.

Nor can one conclude from the higher price of labor services in Panama relative to that in other Central American and Caribbean nations that the cost of production in Panama must therefore necessarily be higher than those in the same other countries. Whether Panamanian wage levels render Panamanian goods and services uncompetitive will depend on how productive local labor is, and productivity is a function of several determinants including the quality of labor and of management. One could reasonably expect that the higher level of educational attainment of the Panamanian labor force would yield advantages for certain Panamanian goods and services over those available from countries with more poorly endowed labor. Such an advantage might hold, for example, in the production of goods and services of high quality or technological content that require a high order of worker skills. Finally, a consideration of the competitiveness of Panamanian goods needs to look beyond merely the price of labor to the prices of other inputs to the production process that may suffer distortions traceable to excess protection or local monopoly.

Perhaps the feature of the law that generates the most heat is that governing stability in employment. By this, we refer to strictures on the employer's freedom to dismiss a worker. Once an employee has served for three months but less than two years, he/she cannot be discharged without just cause without the payment of a severance allowance. After two years, an employee cannot be discharged without cause even if the employer is willing to pay the specified severance allowance. An employee that feels unjustly

discharged for cause can appeal through an administrative and judicial process that is very lengthy, often stretching over three years. Employers hold that, until recently, the appeals process reflected a bias in favor of workers and that discharge was virtually impossible.

An amendment to the law now provides that if an employer loses an appeal of a "justified" discharge, he/she has the choice of re-employing the individual or paying a 50 percent premium over the established severance allowance in addition to any pay lost during the appeals process. Given the length and cost of the appeals process, many employers prefer to "buy off" workers they wish to discharge with payments in excess of the legally prescribed severance allowance. Employers in some sectors employing low-skill workers, such as retailing, prefer to simply discharge workers before they fulfill three months service, replacing them with other workers and/or rehiring the same worker after an interval of a few weeks. However, the use of such "temporary contracts" must avoid the appearance of serving as a subterfuge to avoid granting a worker the status of a permanent worker, for the employer could, on appeal, be forced to grant him/her that status.

A concession to employers was extended by Law 27, Art.4 of 1990 that extended the probationary period from three to six months with one renewal for a total length of one year during which the employer was free to discharge a worker without obligation. However, it was adopted only as a temporary measure and expires at the end of 1991.

While the provisions of the law governing tenure are defended by organized labor as one its great conquests, it is clear that it does not achieve its original purpose of guaranteeing workers permanent employment. While those sectors that are organized and require labor embodying skills or experience may afford such stability, it is at the expense of other low-skilled workers who are rendered unstable by virtue of a high turnover policy on the part of employers. Nor does it guarantee the payment of the required severance allowance as many workers learned during the recent crisis when many small businessmen are said to have walked away from bankrupt businesses leaving behind all their unfunded liabilities.

Certainly, the present law is extreme in its requirements, for it provides for no flexibility to adjust employment to varying needs. Producers find it preferable to forego orders for goods that would require the hiring of additional workers rather than risk being "stuck" with more workers than needed once the temporary peak in production has passed. Again the gains of some workers are purchased at the expense of others, usually less fortunate workers who might have enjoyed at least temporary employment.

One of the consequences of the absence of flexibility is that it tends to convert labor into a fixed rather than a variable cost. A rational response of employers might be expected to be to limit the number of workers hired by substituting capital, e.g., machines, for labor. To the extent that this is the response, a trade-off is again made in favor of those lucky enough to hold jobs

Table 11. Severance Allowances

| Length of Service | Incremental Allowance - Weeks Pay | Cumulative Weeks Pay |
|----------------------|-----------------------------------|----------------------|
| 0 - 3 months | 1 | 1 |
| 3 - 6 months | 1 | 2 |
| 6 - 9 months | 1 | 3 |
| 9 - 12 months | 1 | 4 |
| 1 year and 2 months | 1 | 5 |
| 1 year and 4 months | 1 | 6 |
| 1 year and 6 months | 1 | 7 |
| 1 year and 8 months | 1 | 8 |
| 1 year and 10 months | 1 | 9 |
| 2 years | 1 | 10 |
| 3 years | 3 | 13 |
| 4 years | 3 | 16 |
| 5 years | 3 | 19 |
| 6 years | 3 | 22 |
| 7 years | 3 | 25 |
| 8 years | 3 | 28 |
| 9 years | 3 | 31 |
| 10 years | 3 | 34 |
| 11 years | 1 | 35 |
| each additional year | 1 | |

Note: For workers employed in an enterprise for less than two years, notice of one month is required to discharge. In the absence of notice, the employee is entitled to one month's pay upon discharge, in addition to the severance allowance as described above.

Source: Ministry of Planning and Economic Policy

at the expense of those who would like them. Essentially, what must always be kept in mind when there is a debate regarding "labor's" interests and rights, is that not all labor is equal, and that, in some cases, gains for one class of worker come at the expense of others. (This is equally true, of course, when the debate is over other group interests.)

If the purpose of the stability law is to simply protect workers against the risks of unemployment, then, ideally, it would be preferable to replace the severance allowance provisions with an unemployment insurance scheme financed by a payroll tax. Unfortunately, in the current Panamanian context, this does not pose a realistic alternative. The logical administrator of such a program would be the social security agency. However, in view of its current difficulties, no one has any confidence it could administer any new programs assigned it.

Therefore, it is necessary to think in much more modest terms. The current provisions would seem to be perverse in that they reward increments in services at the beginning of a worker's employment with a firm at a much higher rate than increments in the services of long-term employees. Currently, an employee begins to accumulate claims towards a severance allowance upon completion of only three months' employment, and the allowance increases rapidly with the length of service. (See Table 11.) After three months of service, the worker is entitled to one week's pay as a severance allowance. Each subsequent three month period, up to a year, entitles him/her to an additional week's pay. Thus, after one year

of service, the applicable severance allowance is four weeks' pay.

During the second year of employment, the incremental rate rises to one week's pay for every two additional months of service so that at the end of two years of service the severance allowance amounts to 10 weeks of wages. In contrast, after ten years of service, each additional year merits an increase in the severance allowance of only one week's pay. Thus, an employer would have every incentive to terminate a worker as soon as possible after hiring if he/she does not immediately achieve a high level of performance. One might have thought it desirable to give a worker a more prolonged period in which to demonstrate his/her worth.

I would suggest that it would be worthwhile to consider lengthening the period during which the employer has full discretion to lay-off or discharge workers to two years seniority without incurring an obligation to pay a severance allowance. While this might not change the behavior of employers currently practicing a high turnover policy, it would, at least, provide greater continuity to workers than they now enjoy. In industries characterized by large seasonal or other fluctuations in demand, there would be a greater disposition to hire more temporary labor.

An important improvement would involve speeding up the administration of the appeals process. The current delays of up to three years create an intolerable burden on both parties to a dispute. Other possible changes might include a cap on the size of payments. Or, treating the accumulation of reserves against severance claims as a cost for tax purposes would be a welcome

improvement.

The stability provisions of the code pose the greatest difficulty for new firms that are likely to experience considerable variability in their labor requirements until they become firmly established. Mature firms, however, can adapt if they have competent managements well versed in techniques of manpower management. Most discharges of workers that are reversed are likely to suffer from inadequate documentation of workers' inadequacies. Good supervision can establish the grounds for discharge of an inefficient worker by making clear the performance expected of workers and recording each lapse from that standard. As one manager informed us, his firm has never lost a discharge appeal because the ground is adequately prepared. To be sure, traditional managers may not be skilled in modern management techniques, but these can be learned or hired.

Another area where reform should be possible is in the definition of work shifts and the accompanying overtime provisions. These presumably were intended to discourage overtime in favor of hiring additional workers. But in view of the implied costs of hiring more labor, these provisions serve merely to increase costs for producers, particularly those who operate around the clock. Ideally, the definition of shifts should be left to the parties in the employment relationship so that work schedules can be adapted to the requirements of each production unit.

The current law also places limitations on employers with respect to the assignment of tasks. Unless a worker consents,

he/she cannot be required to accept even a temporary reassignment of tasks. This limitation in the flexibility in the allocation of labor again seems misguided. This is another issue that would seem better left to the parties in the employment relationship.

The code permits the employment of workers on piece work, in principle. However, it also provides for the regulation of such methods of payment unless they are a product of a collective bargaining agreement. For a non-union shop, this means securing the approval of the Labor Ministry of the scheme as well as any amendments. This effectively rules out any attempt to adopt such a system of payment. It would also appear to rule out the establishment of industries in Panama, like the garment industry and some assembly operations, that are organized on the basis of incentive systems of payment. Particularly in garments, where the product or style is constantly changing, administration of a piece rate system would become a veritable nightmare. As long as the employer is obliged to pay at least the legal minimum wage regardless of a worker's output, why is further regulation of each scheme required?

An employer is also forbidden from ever reducing a worker's wage. This holds even in the case where the firm's survival is at stake. Even if most workers in such a firm were to be agreeable to a reduction, all it would take is a subsequent appeal by a single worker to force the employer to restore all the foregone wages. Again, this provision makes no allowances for variations in the fortunes of employers. In some cases, this could mean that the law

prefers no employment to employment at a wage below some historical level. In the absence of ample alternative sources of employment, one must question the desirability of such rigidity. During the recent crisis, workers and employers did negotiate reductions in pay as well as sharing of work on an informal basis in order to ensure employers' solvency. Lest employers subsequently be charged with violation of the law, the government has seen fit to legislate the retroactive legality of those arrangements.

It is likely that most, if not all, of the above suggestions would be welcomed by employers, and, from the point of view of the broader society as well, would seem to be desirable. However, one can be assured that they will be vigorously opposed by the organized labor movement unless some of its grievances are also acted upon. Procedures for seeking certification of a new union are unduly harsh and provide ample scope for harassment. The requirement that a union must have at least 51 members makes it very difficult for workers in small establishments to organize unless they can form a coalition with workers in other firms. In a small country dominated by small establishments this requirement seems unreasonable to us. The recognition process could be accelerated and simplified by substituting an election process for the current administrative one. A majority vote among the workers in an employment unit should suffice to establish the legitimacy of the union's claim to representation. Such a process might also have a healthy effect of promoting a more democratic and participatory unionism.

The suspension by Law 13 (1990) of contract renegotiation for up to two years, ostensibly as a response to the economic crisis, has aroused strong opposition of the labor movement. In place of negotiations, the terms of the current agreements are extended. Thus, if the current agreement provided for wage increases, the increases are to be repeated over the extended life of the agreement. If the government hoped to restrain wage increases by this measure, it is a poor vehicle for that purpose. Workers whose current contract provided for no increase are denied the opportunity to bargain over the wage terms while other workers may be beneficiaries of increases that they could not have received had they had to negotiate a new contract. This measure thus does not permit the tailoring of the terms of employment to fit the economic situation of the affected firms.

The absolvment of employer responsibility to bargain collectively for three years in new establishments (Law 13 1990) and for four years in export processing firms (Law 16 1990) has also become a bone of contention. One can only speculate regarding the intended purpose of this law; presumably a non-union environment is considered favorable for the attraction of new investment. But one wonders whether the postponement of the "threat" of unionism for four years is likely to be a decisive factor in encouraging new investment. The workers' freedom to organize has certainly not deterred the growth of the maquila industry on Mexico's northern border. The government seems to assume that unions cannot learn "responsible" behavior and would

rather drive firms out of business than agree to terms that would permit their mutual survival. If this is the case, how will "responsible" unions ever develop? In any case, given the existing culture of collective bargaining, the government has always had sufficient muscle to influence the outcomes to labor disputes in which it took an interest. So was the prohibition really necessary?

Finally, there is the issue of the conditions under which compulsory arbitration can be invoked in a labor dispute. Until recently, arbitration could be invoked at the request of a union alone or if the government deemed a strike to be a threat to public welfare. Law 13 has recently added a third condition. The Labor Minister may order arbitration whenever he deems a strike to threaten the financial health of a firm. In my judgment, only the second basis for intervention is justified. To accord the union the right unilaterally to invoke a process that will be binding on the employer is no more justified than the unilateral intervention of the Minister on behalf of a firm. Except in the threat to public safety, binding arbitration should be employed only when it enjoys the consent of both parties to a conflict. After all, how will unions and employers ever learn to become "responsible" unless they are allowed to make mistakes?

It is difficult for us to assess the chances for meaningful reform of the labor code. Employer and union representatives profess a willingness to discuss reforms, but what each would want and what each would be willing to cede is difficult to foretell. Our discussions with both parties yielded only vague comments on a

possible meeting ground. However, we come away with the impression that neither side is considering a reform that would reduce the degree of government intervention significantly even though both complain about the "unfairness" of specific cases of intervention. Each side seems to willing to take its chances that it will be able to enlist the government on its own behalf or to convince it to broker an outcome favorable to itself. The kinds of changes that are contemplated do not appear to pose a serious challenge to established ways of doing things. We certainly sensed no enthusiasm for a radical reform that would decentralize decisionmaking on employment matters to the parties directly involved. The corrolary to the dependence on government intervention is, of course, that outcomes will very much depend on who is in power at a moment in time and the political agenda of that government. The parties then must be prepared to gamble that they have more to gain with that uncertainty than from opting for a process that places a greater responsibility for resolving issues on the parties themselves.

Nor would one be likely to find much enthusiasm for radical reform among government leaders. Past regimes have been manipulative using the power the law grants them to dispense favors for political gain. To expect political leaders voluntarily to relinquish any of the carrots and sticks at their disposal would be to expect them to act in uncharacteristic fashion. Big, intrusive government is hardly likely to retreat from power unless forced to do so by the body politic. Thus, we do not foresee much meaningful reform of the labor code until and unless economic realities change

and make the necessity of change so obvious to all that it can no longer be avoided. That class of realities is likely to become persuasive only in the wake of substantial structural changes in the economy. As long as Panama opts for its traditional protected and regulated economy, persuasive reasons for change are likely to be absent.

IV. Notes on Labor Statistics

This section is devoted to a discussion of aspects of Panama's labor statistics. We begin with a discussion of the measures of unemployment and underemployment and then will discuss some of the problems the statistical series present. Finally we will consider forms of assistance that A.I.D. might consider in order to improve the quality of the data themselves as well as their interpretation.

The underutilization of labor has emerged as one of the more pressing concerns of almost all developing countries. Whereas a couple of decades ago underutilization was represented by a single value, open unemployment, the intervening years have seen the development of additional measures that purport to provide a more complete accounting of the degree of underutilization. Thus, to the open unemployed are added those classified as underemployed and as "discouraged workers." It is important that those who follow labor market developments be fully aware of what these categories of workers represent as well as their implications for employment policy making. In particular, one should be aware of how sensitive these values are to differences in the manner in which they are

defined.

Consider, for example, the various components of the unemployed population as they appear in the results of the 1989 household survey and the 1990 census.

| Category | Percent of the Labor Force | |
|--|----------------------------|--------|
| | Survey | Census |
| Actively sought work the week preceding the survey | 9.4 | 3.4 |
| Had sought during past three months | 1.5 | - |
| Had applied and awaiting response | 1.5 | 3.1 |
| Did not look - believed no jobs were available | 3.8 | 5.1 |
| Total | 16.3 | 11.6 |

Let us leave aside for now the possible explanations for all the differences between the two values and simply consider each building block. If the unemployment rate was defined solely by reference to those who actively sought employment during the reference period, the week prior to the survey, the rates would be 9.4 percent and 3.4 percent. These would then be comparable to the concept employed in the United States that currently yields an unemployment rate of 7 percent.

By simply lengthening the reference period to three months, the household survey adds another 1.5 percent to the unemployment rate. The census questionnaire did not offer this as an alternative response. A third category includes those who, at some time in the past, applied for work and are now awaiting a response from prospective employers. This category accounts for approximately one-fourth of the census unemployed but less than a tenth of the

survey unemployed. Finally, we have the so-called "discouraged workers," those who took no action to seek employment out of a conviction that no jobs existed. These accounted for almost half the census unemployed and almost a quarter of the survey unemployed.

These totals can be interpreted as providing a generous estimate of unemployment, taking the respondent's reply as a true indication of his/her actual status. However, it is likely that these represent an overstatement of the number of individuals seriously interested in employment. For example, consider the so-called discouraged workers. These are identified by posing the following question to individuals of labor force age who reported that they had not sought work during either of the reference periods: "Why did you not seek work?" It is not uncommon for people who have no intention of working to reply that they believed no jobs were available. PREALC (Regional Program on Employment for Latin America and the Caribbean, an ILO agency) conducted a series of detailed labor force studies in Latin American urban areas during the 1970s and followed up such responses with a series of questions designed to determine the degree of seriousness of the respondents. The studies led to the conclusion that the majority of those responding in this manner were really not candidates for employment, for when they were asked whether they were available and willing to accept employment if it were proffered, they pointed to current activities and obligations that prevented them from accepting. Thus, in the absence of further probing, responses

citing a belief that job opportunities were lacking cannot be relied upon to yield a true measure of hidden unemployment.⁹

PREALC's conclusion at that time was that this category of individual could not be relied upon to represent truly unemployed individuals.

In order to clarify the status of those so replying it would be useful to follow the response with additional questions that would clarify the respondent's actual availability for employment. In the case of Panama, there is reason to question the seriousness of many of those who gave this response. For example, special tabulations prepared for us by the Direccion de Estadistica provide insights into the relationship of these individuals to the labor market. 31,339 individuals gave this response, whom we divide into two groups according to whether or not they reported any previous work experience. 53.3 percent reported previous experience, 46.7 percent reported none. Refer to the Table below.

The responses to questions about previous job search and employment status yield reservations about the seriousness of their status as labor force members. Over half had not actively sought employment during the preceding three months. Indeed, almost half had never sought employment while an additional 16.5 had not done so in over a year. Furthermore, almost 58 percent said they had no intention of seeking employment during the next six months. Surely, it would strain credulity to consider such individuals as truly unemployed. Furthermore, among those with previous work experience, 17 percent had not worked in over three years and another 10

percent had not done so for two years. Again, the longer one has been divorced from employment, the less likely is he/she to be seriously considering seeking a job again. Clearly, more refinements could be made to try to distinguish between candidates for retirement from the the labor force and the truly unemployed, but we will not attempt to do so here. Suffice it to say that serious consideration should be given to eliminating this response as indicative of unemployment unless it is followed up with additional questions designed to determine the true status of the respondent.

| Response | Total | | With Ex- | Without Ex- |
|---|---------|-------|---------------|---------------|
| | No. | % | perience % | perience % |
| | 31,339 | 100.0 | 100.0 | 100.0 |
| Did not seek work last three months | 10,336 | 54.5 | 45.6 | 65.4 |
| Does not plan to seek work during next six months | 18,0770 | 57.7 | 59.8 | 55.2 |
| When last sought job: | | | | |
| Never have sought | 14,968 | 47.8 | 43.2 | 53.0 |
| Over one year ago | 5,168 | 16.5 | 18.5 | 14.2 |
| Time since last job: | | | | |
| More than three years | 1,806 | | 10.8 | |
| 2 - 3 years | 1,894 | | 11.3 | |
| 1 - 2 years | 295 | | 1.8 | |

Another group whose responses should be probed further includes those who stated that they have sought employment and are now awaiting a response. It would be desirable to determine how long ago the last search was made. The further into the past the search was made, the less likely is the person to be one in serious search of employment.

The concept of underemployment is one that is poorly understood by the general public. In the public mind it is often equated with unemployment so that elevated levels of underemployment give rise to very distorted views of their significance. And the conversion of underemployment data into open unemployment equivalents is a practice that can give rise to very misguided policy decisions. For Panama, a recent study reported that the rate of unemployment and underemployment was 34 percent in 1988; in terms of unemployment equivalents, this yielded a rate of 22.9 percent.¹⁰

There is no single methodology employed for the measurement of underemployment. Applied to the same country for the same moment in time, the different methodologies yield different measures of underemployment. This reflects the arbitrariness of the parameters employed to derive the number so affected. The methodology that was applied in the study of the Panamanian labor market cited above separated the underemployed into two categories, visible and invisible. The visible are those who worked less than a full work week and were desirous of additional hours of work; these accounted for 7.5 percent of the labor force.

A larger number, 10.2 percent of the labor force, was defined as invisibly unemployed. By this it was meant that they worked full time but earned less than the legal minimum wage. Why this group should be considered underutilized has never been obvious to me. These individuals are fully employed in a time sense. The fact that they earn less than the legal minimum wage tells us nothing about

the capacity of these to fill jobs at higher wages if they existed. The measure of underemployment implicitly assumes they are. Furthermore, the conversion of underemployment into open unemployment equivalents implies that this provides a reliable measure of the number of people actually available to fill new job should they become available, an assumption that can lead to disastrous macroeconomic policymaking, as Mexico discovered following its embarkation on an expansion policy designed to mop up a 25 percent open unemployment equivalent at the end of the 1970s.¹¹

What then is the prescription for a reduction in underemployment? We would suggest that it would involve more than just an increase in the rate of growth in GNP or the creation of new jobs, though both are indispensable to the improvement of overall employment conditions over time. But growth cannot be expected to bear the whole burden of eliminating underemployment not only because the cost would be prohibitive but also because the causes of low earnings may not be so addressed. A reduction in the incidence of low earnings requires, first of all, a fuller understanding of their correlates, that is, the conditions associated with low earnings. These are usually indicative of very low productivity that, in turn, may be associated with low endowments of human capital, poor health, old or very young age, insufficient cooperating inputs of production, e.g., credit, tools, etc., rudimentary technical skills, limited access to markets, and so on. A careful definition of the correlates of low earnings can

then assist in the formation of programs that address this issue directly, usually at a far lower cost than that of creating new employments at high levels of productivity. Over time, of course, an improved quality of human resources and enhanced mobility, would permit a gradual shift of the labor force from low- to high-productivity employments as long as an adequate rate of growth is maintained.

The use of the mechanistic formula usually employed in the measurement of underemployment raises an interesting question. How will a country ever know when underemployment has been eliminated? As long as income is distributed unequally in a society, some proportion of wage earners will always fall below some arbitrary boundary line. Even the richest countries are afflicted by substantial levels of underemployment if the conventional formulas are applied to them. Indeed, in Panama, if minimum wages are raised as a way to reduce underemployment, this will have the immediate paradoxical effect of increasing the rate of underemployment since more individuals will now be earning less than the new minimum wage! This, in spite of the fact that the real economic welfare of most of the underemployed will not have changed one whit.

Underemployment is frequently associated with the concept of poverty. Again, care needs to be exercised in the interpretation of the concept. Underemployment is a phenomenon associated with the earning status of an individual. Poverty, on the other hand, is a function of total household income and the number of individuals in the household. Because one individual has low earnings does not

necessarily imply that he/she is poor. New entrants to the labor market may earn low wages because of lack of skills and experience yet form part of a household with an adequate level of income. On the other hand, low earnings on the part of head of family, particularly if the head is a female, may reveal a closer association with poverty. In rural areas, where productivity levels are lower on average than in urban employments, one may also find a closer association between the low earnings of family heads with poverty. However, in the case of this latter group, the household survey falls short in one respect for purposes of defining the poverty status of households. The survey captures only cash income and ignores income in kind. To the extent that rural families produce goods for their own consumption, the survey data will consign a larger proportion to poverty than is merited.

In short, we do not consider the concept of underemployment as it usually measured and employed to be useful. (It is only fair to point out that this view is not likely to be shared widely in Latin America.) As a measure of the number of individuals lacking productive employment it is totally misleading. As a measure of the number of jobs that must be created in order to eliminate underutilization it greatly exaggerates that number. Nor does the concept in and of itself provide any guide to appropriate labor market policies. However, lest we be misunderstood, we do not object to measures of the earnings realized by producers. Indeed, this is information vital to the charting of the economic welfare of all the components of the labor force. We would prefer that low

earnings be presented as just that, rather than as an indicator of underutilization of labor resources.

V. Possible Roles for U.S.A.I.D.

Earlier in this report we recounted the problems that the available data presented for purposes of analyzing the course of the Panamanian economy. In the case of the results of the household employment series, we found erratic movements in its components that raise questions about its accuracy. We have been assured by the persons responsible for that survey that its methodology has been examined by technical experts and found to be acceptable. If that is the case, then one must suspect that the irregularities originate in the collection of the household data at the source. This would suggest the need for more careful training and supervision of the interviewing staff. Apparently, the training does not include actual interviewing of households but is based on a long, detailed manual, the absorption of which must pose a challenge. More seriously, the Direccion does not have the resources to undertake the re-interviewing of a sample of households approached by each interviewer. This failure opens the door to carelessness on the part of interviewers. At the very least, it means that consistent errors by an interviewer will not be discovered and corrected. We were also informed that the interviewing is done by temporary employees and that the annual rate of turnover among these is approximately 25 percent. This heightens the need for reviewing the training procedures to assure

uniformity in the way interviewers conduct their data collection.

An equally serious problem arises in the processing of the data once it has been collected. We noted, in particular, the long delays between the collection and the publication of information. The delay is attributable entirely to the absence of sufficient computer capacity to process the household survey. The computer available to the survey is one shared by the rest of the Contraloria, and competition for access is intense. Unfortunately, the household survey does not enjoy a high priority in this competitive environment. Thus, there is little prospect of improving the timing of the dissemination of survey results as long as the problem of insufficient computer capacity is not addressed. Particularly if the survey data are to be subjected to careful analysis, more computer capacity is indispensable, as attested to by our experience. For purposes of our inquiry we requested special tabulations from the Direccion. The staff there were most cooperative and willing to meet our requests. However, the limited access to an overloaded computer involved long delays, and it was impossible to fulfill our requests except in small part.

We have also weighed the desirability of a second survey. In most developing economies, seasonal variations in economic activity and employment can be important. In Panama, for example, the household survey is conducted in August, a month of reduced activity in the agricultural sector. A second survey in a month of greater activity, e.g., March, would provide an additional observation that would enhance our evaluation of employment

conditions and provide greater insights into the modus operandi of the labor market.

The question of cost, of course, looms as an obstacle. This has led to the consideration of the option of limiting the second survey to only the metropolitan area. While this would be a second-best course of action, the real variations in labor market activity, in relation to the August survey, are more likely to be observed in the rest of the country. This would argue for a national survey. We have no measure of the marginal cost of extending the survey beyond the boundaries of the metropolitan area. If it is not "great," in relation to the likely capability of the Panamanian government to assume the full cost of that extension at some future date, then we would argue for a second national survey.

However, unless the other problems to which we have referred are addressed, little will be gained by adding a second survey. The financing of a second survey by A.I.D. should include funds, or be contingent on the provision of such funds by the Panamanian government, for an orderly re-interviewing of a sample of households and a more thorough training of interviewers. Otherwise the quality and usefulness of the data will not be enhanced. Nor should a second survey be undertaken unless additional computer capacity can be provided. Such a provision should be made contingent on the processing of the survey results within a reasonable length of time, e.g., three months. Otherwise their usefulness deteriorates the longer the interval between collection

and dissemination.

Finally, the greater availability and improved quality of data will have a significant pay-off only to the extent that there is a developed capability to analyze them. We would suggest that considerable room for improvement exists in the analysis of labor market phenomena. Generally speaking, in Latin America, the study of labor markets by economists has been sadly neglected, largely because it is not a field that holds rewards for economists. Much of labor market analysis is delegated to social scientists who are not economists and do not emphasize the economic significance of labor market activity. Therefore, we would suggest the desirability of providing some training to individuals in government in order to extend their understanding of the economics of the labor market and, hopefully, improve the quality of analysis.

Ideally, it would be desirable to train some individuals in labor economics through the Ph.D. level. Regardless of whether or not that is feasible, in terms of A.I.D. resources available for training purposes, it would be desirable to set up a crash course in labor economics for government employees here in Panama. We would envision a course of perhaps a month's duration requiring daily attendance for half a day. In this way, a significant body of individuals with improved analytical skills could be formed. The engagement of a labor economist with an intimate familiarity with Latin American labor markets should be contemplated. Obviously, the greatest pay-off for Panama would be realized if all of these initiatives could be pursued as a package.

1. Contraloria General de la Republica, Direccion de Estadisticay Censo, Censos Nacionaler de 1980, Volumen IV, Caracteristicas Economicas, Table 1; Censos Nacionales de Poblacion y Vivienda, 13 de Mayo de 1990, Resultados Finales Basicos, Distrito de Panama; ibid., Distrito de San Miguelito, Table 3.

2. The data used in this calculation are as follows: GDP of 1,745.8, 1917.6, 2123.8, and 1762.4 for 1980, 1984, 1987, and 1989 respectively, all in balboas of 1970. Employment for the same years numbered 558,648, 613,937, 678,314, and 686,334 respectively. All data originate with the Controlaria General de la Republica.

3. Direccion de Estadisticas y Censo, Situacion Social, Estadisticas del Trabajo Ano 1988, Table 441-41.

4. All references to GDP are taken from a World Bank paper, Panama: Policy Issues, Agenda for Action, August 17, 1990, Table 2.5. The data are attributed to the Contraloria General de la Republica.

5. Direccion de Estadisticas y Censo, Indicadores Economicos y Sociales de Panama 1980-89, p.24.

6. It should be noted that it is not uncommon for household surveys to record higher rates of unemployment than do population censuses. This is attributed to the greater skill of the regular household surveyors in extracting accurate employment information. On the other hand, it is also worthy of note that the 1980 population census reported a national level of unemployment that did not vary at all from the 1979 and 1982 levels of the household surveys. (No household surveys were conducted in 1980 and 1981.)

7. The reader interested in a discussion of the efficiency of past investment in Panama is referred to a study by Pedro Pou, Empleo, Inversion y Crecimiento Economico en Panama Durante la Decada de los Setenta (Ministerio de Planificacion y Politica Economica, 1985).

8. The World Bank, op. cit., p. 24.

9. Kritz, Ernesto and Joseph Ramos, "The Measurement of Urban Underemployment: A Report on Three Experimental Surveys," International Labour Review 113:1 (1976), pp. 124-125.

10: Ministerio de Trabajo y Bienestar Social, El Mercado de Trabajo Panameno: Un Analisis Retrospectivo y Prospectivo, Documento presentado a la VII Conferencia Regional del Empleo en America Latina y el Caribe, Santiago de Chile, Diciembre 1990, Table 21.

11. Gregory, Peter, The Myth of Market Failure: Employment and the Labor Market in Mexico (Baltimore: The Johns Hopkins University Press, 1986).

LIST OF INTERVIEWS

- Maria Teresa de De León, Directora de Estadística y Censo,
Contraloría General de la República
- Ovidio Angulo, Sub-Jefe, Población y Vivienda, Contraloría General
de la República
- Pedro Pablo Carrasquilla, Jefe, Encuestas de Hogares, Contraloría
General de la República
- Carol Horning, Acting Chief, Office of Public Administration, USAID
- Kermit Moh, Chief, Private Sector Development, USAID
- Luisa de Soto, Directora de la Unidad Coordinadora del Plan
Económico, Ministerio de Planificación y Política Económica
- Isabel Atencio, Código Laboral, Unidad Coordinadora, Ministerio de
Planificación y Política Económica
- Federico Humbert, Presidente, Banco General
- Hernán Arboleda, Cuentas Nacionales, Unidad Coordinadora,
Ministerio de Planificación y Política Económica
- Rosa Elena de De la Cruz, Jefe del Departamento de Planificación
Social, Ministerio de Planificación y Política Económica
- Daniel Comazón, Funcionario en Asuntos de Empleo del Departamento
de Planificación Social, Ministerio de Planificación y
Política Económica
- Graciano Cruz, Gremialista de Exportadores de Productos Agropecua-
rios No Tradicionales
- Nicolás Ardito Barletta, Director, Centro Internacional de
Crecimiento Económico
- Juan Luis Moreno, Asesor, Unidad Coordinadora del Plan Económico
Ministerio de Planificación y Política Económica
- Juan Pascual, Industrialist
- Bill Riley, American Chamber of Commerce
- Ricardo Alemán, President, Cámara de Comercio, Industria y
Agricultura de Panamá

Carlos Jayes, President, Hotel Owners Association

Walter Durling, Labor Expert, Legal Consultants and Counsellors,
Inc.

Markela de Nuñez, Jefe, Centro de Información, Dirección de
Sistematización, Contraloría General de la República

Arturo Hoyos, Supreme Court Justice

Jose Galán Ponce, Vice-President, Economist, Investigación y
Desarrollo, S.A. (INDESA)

Harold Baum, Labor Attache, U.S. Embassy

Dario Selles, President, Sindicato de Industriales de Panamá

Dean Butcher, AIFLD

Julie Perkins, AIFLD

Adriano Pinzón, Secretary General, Confederación de Trabajadores de
la República de Panamá