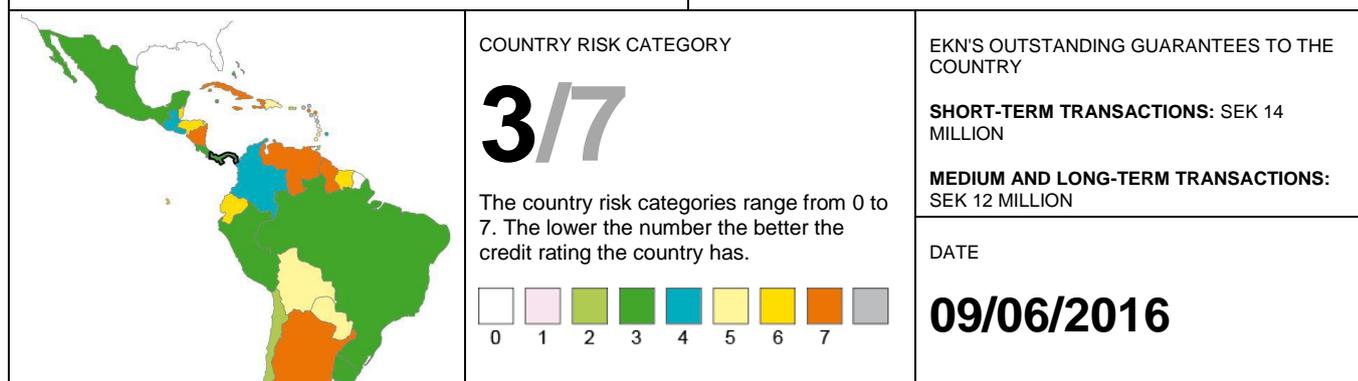


# Panama



## Panama and its canal continue to grow

Panama has seen strong growth and a high degree of macroeconomic stability over the past years. In spite of the country's high level of economic transparency, the lack of its own monetary policy and its high dependence on external financing, the country's economy has proven resistance to the negative shocks which have impacted other countries in the region. The country has had the highest growth in the region, driven by extensive investments. The Panama Canal and the stability resulting from the dollarisation of the economy are two solid foundations that have played a role in making the country attractive as a regional, financial and logistical hub. As the public infrastructure projects wind down in the coming years, the country's high growth rate is expected to decrease slightly and be increasingly driven by revenue from the canal, which will open in 2016 after the extension, and by export revenue from industries such as mining. The country's ability to comply with applicable budget regulations has proven weak, but otherwise the country's economic policies are stable and investor-friendly. The regulatory environment is weak in certain respects and corruption is a substantial problem which the sitting president has attempted to address. Overall, Panama's outlook is considered positive thanks to political stability, and a strong and diversified economy.

### THE COUNTRY'S STRENGTHS AND WEAKNESSES

#### Strengths

- Among the best business environments in the region
- Stable growth which has been the highest in Latin America over the past ten years
- High inflows of foreign direct investment have raised the country's productivity level

#### Weaknesses

- Inability to pursue its own monetary policies due to dollarisation
- Weak spending controls from the government
- Low average level of education holding back long-term growth in productivity

### **Stable country risk categorisation**

EKN has categorised Panama in country risk category 3 since the country was upgraded in 2007. The country risk categorisation is made in collaboration with the other OECD countries. The dollarisation of the Panamanian economy puts Panama in a group of countries where companies can be assessed a higher credit rating than the country and thus have a lower premium. EKN has no special restrictions for buyer categories or credit periods. Instead, each transaction is assessed on its own merits.

### **WHAT MIGHT CAUSE A CHANGE IN THE COUNTRY POLICY?**

#### **The policy may be made less restrictive in the event of**

- Better control over public finances providing greater fiscal flexibility
- Improved compliance with regulations and institutional environment
- Structural reforms that permanently increase productivity, such as a higher level of education

#### **The policy may be made more restrictive in the event of**

- Failure to implement financial transparency reforms posing a risk of decreasing the willingness to invest and access to the international capital markets
- Continuing budget deficits exceeding the levels stipulated by the framework

### **EKN'S EXPOSURE AND EXPERIENCE**

#### **Transport sector dominant**

EKN's outstanding exposure currently totals approximately SEK 100 million, with the lion's share consisting of offers. Until recently, EKN's guarantee exposure was larger because a loan amounting to SEK 1.1 billion in the transport sector was paid off in advance. EKN's experience of guaranteeing transactions with Panama is limited but positive, and willingness to pay can be considered high.

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## Background

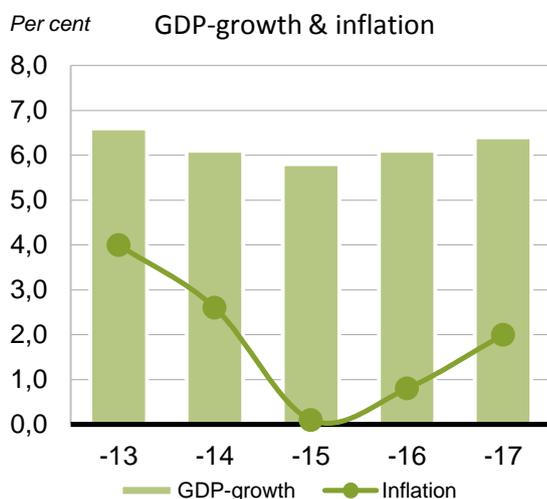
Panama has been characterised by political stability since the early 1990s. Power has shifted between different political parties in an orderly fashion, and all of these parties have prioritised creating solid conditions for investment and entrepreneurship in the country. Panama has been fully dollarised for over 100 years since the Panama Canal was completed under the supervision of the US. The geopolitical position of the canal and the dollarised economy serve as the cornerstones of the country's success as a logistical and financial hub in the region. Over the past ten years, the country has experienced an impressive period of growth with an average annual increase in GDP of 8 per cent, which is the highest in Latin America. This led to GDP per capita in 2015 of USD 13,000, which is up 80 per cent from 2009. This strong growth has been driven by investments in the expansion of the canal, which is expected to be re-opened in the first half of 2016 and the completion of the Cobre copper mine in the Colón Province.

The ambitious public investment programme combined with higher recurring expenses led to higher public deficits than initially budgeted. This in turn led to recurring adjustments to the budget target by the government, a pattern which weakens confidence in the fiscal framework. In spite of the deficits, the gross debt of the public sector, measured as a percentage of GDP, has continuously decreased due to the strong growth. The debt was lower than 40 per cent of GDP at the end of 2015.

## Most recent trends

The sitting president, Juan Carlos Valera from the Panameñista Party, was elected in the summer of 2014 and has now completed one third of his five-year term of office. He took office with an agenda to reduce social discrepancies and raise transparency, efficiency and accountability in public administration. The rate of reform has been held back so far because President Valera's government is a minority government (the Panameñista Party holds 16 of 71 seats in the legislative assembly). However, the major document leak (the Panama Papers) from law firm Mossack Fonseca in spring 2016 will most likely speed up the harmonisation of the country's legislation with international standards concerning the exchange of information between countries. President Varela, who is under heavy international pressure to speed up this process, has said that the country will have harmonised legislation to ensure

greater transparency by 2018. It is possible that the financial sector in Panama will be negatively impacted in the short term by a decrease in interest from certain investors due to the country's promises to harmonise its legislation with international standards concerning the exchange of information. However, the country will continue to be preferred, primarily due to the dollarised economy and its position as a regional financial hub, and this is expected to remain the case in the future for the most part.



Inflationen returns to normal levels

Source: WEO

Panama's economy is largely based on services, as opposed to other parts of the

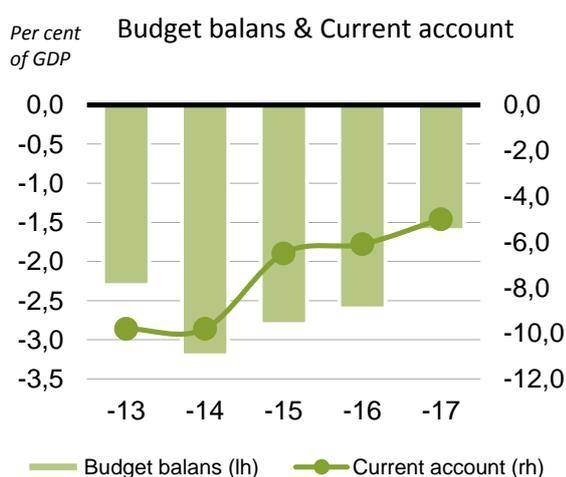
region, which are more heavily based on commodity exports to a varying extent. The services sector ranges from businesses with a direct link to the canal, such as transport, logistics management and the Colón free zone, to financial services and tourism. The country has relatively recently acquired the status of a popular tourist destination. There is potential for further growth in tourism and investments will most likely be made in the coming years.

Growth in the US and the lower oil prices will continue to be beneficial for Panama, while the strengthening of the US dollar has a direct negative impact on Panama's goods exports to countries other than the US. However, dollarisation has served Panama well over time by eliminating the currency risk for investors. Along with low transfer risks, this has served as the foundation for the excellent access to the international capital markets enjoyed by the country. However, the lack of its own monetary policy instruments makes fiscal policies more important for managing any macroeconomic fluctuations. This amplifies the importance of the government meeting the fiscal framework in the future in order to retain the confidence of investors.

### Long-term trends

The growth rate is expected to fall slightly from the high levels of the past ten years and come in at around six per cent over the coming years, driven in part by investments in the mining sector and public infrastructure projects. This includes the expansion of the Panama City Metro, a growing tourism sector and economic diversification.

Continuing strong GDP growth combined with lower spending on public investments and higher revenues via the reopened canal will contribute to a stable and possibly somewhat lower gross debt (as a percentage of GDP) for the public sector in the coming years. It is likely that the budget deficits will decrease slightly in the coming years. However, the consolidation of the public finances will be tested, such as in the context of President Varela's



Current account deficit decreases as infrastructure investments recedes  
Source: WEO

recurring promises to step up resources for various social welfare programmes. These includes grants to reduce the number of primary school students without a leaving certificate and pensions for individuals outside of the insurance system.

Panama will continue to have a trade deficit in the future and it will contribute to the current account deficit. However, import growth is expected to be slowed down by a lower rate of investment. This results in a deficit corresponding to seven per cent of GDP, down from an average of ten per cent of GDP between 2011 and 2015. As before, the current account deficit is expected to be largely financed

by foreign direct investment, which contributes to increasing the long-term growth potential of the local economy. Although the lion's share of foreign direct investments goes to the financial sector and trade, other sectors such as mining, transport and the power industry have become increasingly important foreign investment targets.

The government is expected to continue seeking to strengthen economic ties with major trade partners in the future. The country has several bilateral free trade agreements and signed a new one in 2014 with Mexico, a step in the Panamanian government's strategy to become a member of the Pacific Alliance (an integration agreement on free movement of goods and people between Chile, Colombia, Peru and Mexico).

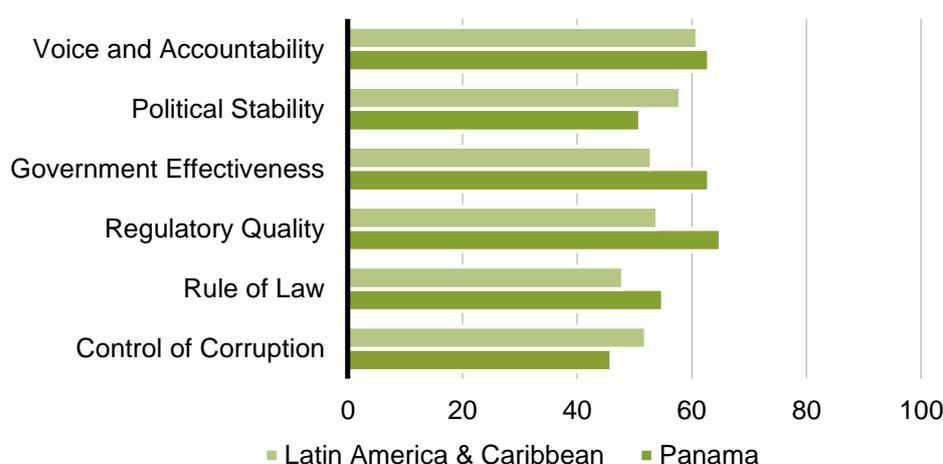
The Panamanian government will have to make major efforts in the coming years to improve the country's reputation in the international community as a result of the leak of the Panama Papers and the financial sector may decline in importance for the country in the long term. The resources which would be freed up as a result of this would likely be allocated to expanding sectors such as commodities and tourism. The country's next presidential elections will be held in 2019, and Valera will not be able to run because a sitting president is not eligible for re-election in Panama. However, it is highly likely that the investor-friendly policies will be continued.

**BUSINESS CLIMATE IN PANAMA RANKED SEVENTH BEST IN THE REGION**

**The region's commercial hub**

**BUSINESS ENVIRONMENT**

*Ranking from 0 (worst) to 100 (best)*



Note: rank between 0 (worst) och 100 (best)  
 Source: Worldwide Governance Indicators 2015

The business climate in Panama is good overall and has benefited from the prevailing political consensus on policies to promote investment. In the World Bank's Doing Business Index (annual survey of regulatory differences between countries), Panama comes in 69th place out of 189 countries, while the average ranking for the region as a whole is 104. Panama excels particularly with regard to the low barriers to starting a business in the country, access to credit and opportunities for cross-border trade. The country has a positive view of free trade and has bilateral agreements with several countries, including the US. However, there are deficiencies in other areas that are having a negative impact on the business environment. Corruption in particular is considered a greater obstacle in Panama than for the rest of the region. 5