PANAMA

1. General trends

The Panamanian economy grew 4.9% in real terms in 2016, recording slower growth than in 2014 (6.1%) and 2015 (5.8%), owing to the performance of financial intermediation, hotels and restaurants, transport, storage and communications, real estate, business services and rentals, all of which grew at positive rates but more slowly than the year before. Slower growth in the Colón Free Trade Zone also hurt output. Partially offsetting this was the solid performance of the construction sector, buoyed mainly by public infrastructure works.

The national unemployment rate rose year-on-year to 5.5% in August 2016 (5.1% the same month year before), while the average inflation rate stood at 0.7% in December 2016 (0.13% in December 2015). The deficit of the non-financial public sector (NFPS) came in at 2.4% of GDP at the end of 2016 (2.3% in 2015), while the adjusted deficit —which frames the limits of fiscal responsibility— represented 1.5% of GDP (2.0% in 2015). Stability of fiscal results was due to a rise in tax collections that was countered by an increase of similar magnitude in total central government spending. At December 2016, the current account deficit stood at 5.6% of GDP, compared with 7.3% in 2015, owing mainly to a decline of 2.7 percentage points of GDP in the goods deficit.

The National Assembly of Panama approved Law No. 47 in October 2016, thus providing the framework for the country's agreement with the United States to improve its international tax compliance and execute the Foreign Account Tax Compliance Act (FATCA). Under this legislation, all Panamanian financial institutions (custodian, deposit-taking, investment or specific insurance institutions) will have to provide financial information (account holder, balance or account value, and interest and dividends paid) automatically and on an annual basis for all United States accounts filing with Internal Revenue Service (IRS) of the United States. Lastly, it is worth noting that the case known as the "Panama Papers" had only a marginal effect on the country's economic and financial performance.

According to ECLAC forecasts, Panama's economy should grow at a rate of 5.6% in 2017, on the back of a sound performance by the construction, transport and communications, and financial intermediation sectors. The rise in income from the new set of locks on the Panama Canal opened in June 2016 will also boost economic activity. The current account deficit will likely remain stable or narrow further. The NFPS adjusted deficit is also expected to narrow, as a result of greater tax collection, containment of current spending and contributions from the Canal. Inflation is expected to remain close to 1%.

2. Economic policy

(a) Fiscal policy

The NFPS deficit stood at US$ 1.350 million at December 2016 (2.4% of GDP), equivalent to an 11% rise in real terms compared with the year before. However, in GDP terms this represented only a 0.1 percentage point increase.

Under Article 3 of Law No. 38 of 2012, which created the Panama Savings Fund (FAP), as from 2015 a new formula for calculating the NFPS adjusted fiscal deficit came into effect for the purposes of ensuring compliance with the Fiscal Responsibility Law. In observance of Executive Decree No. 71 of 2013, which establishes the mechanisms to calculate the adjusted fiscal balance, an accounting adjustment equivalent to 1 percentage point of GDP was performed so that the NFPS adjusted deficit would not exceed 1.5% of GDP in 2016, as stipulated by law.

Central government tax revenues totalled US$ 5.537 billion (10% of GDP), an increase of 8.4% in real terms and of 0.3 percentage points in GDP terms. This was attributable to the considerable rise in direct tax revenues (13.1%) in real terms, together with the moderate rise in indirect receipts (3.5%). Improved collection was the results of new billing operations, the opening of the new payment centre and the establishment of withholding agents, large taxpayers responsible for withholding from buyers 50% of the movable goods and services transfer tax (ITBMS). All of these initiatives form part of the new strategic planning scheme and efforts to strengthen the General Directorate of Revenue.

Income tax receipts increased significantly, by US$ 326.5 million (15.3% in real terms), owing mainly to a rise in the takings from corporate income tax (22.4%), capital gains from securities tax (128.4%) and payroll tax (6.3%).

The rise in indirect tax receipts was a result of increases of US$ 148 million in the ITBMS on sales (18.5%), of US$ 51.8 million in fuel consumption tax (32.8%) and of US$ 29.6 million in selective taxes on gambling (125.3%). This was partially offset by a fall of US$ 38.8 million (6.9%) in indirect receipts from the ITBMS on imports, and a drop of US$ 45.9 million (11.8%) in import tariffs.

Total expenditures of the central government grew 7.7% in real terms, reaching 18.2% of GDP, which represented a rise of 0.4 percentage points of GDP compared with the year before. Current expenditures rose 5.2%, owing mainly to increases in personal services (13.7%), spending on goods and services (19.4%) and interest payments (6.1%). Capital expenditures grew 12.2%, owing to different public infrastructure projects, including Line 2 of the Metro, the urban renovation of Colón, social housing projects, and road expansion and rehabilitation.

The public debt balance stood at US$ 21.602 billion (39.1% of GDP) at the end of 2016, an increase of 0.3 percentage points compared with the year before. External public debt represented 78.2% of the balance. Of total debt, 88.2% was long-term debt (average maturity 8.4 years), 10.6% was medium-term debt (average maturity of 2.6 years) and 1.2% was short-term debt (average maturity of 0.3 years), giving an overall average of 7.7 years. The weighted average cost of the debt portfolio at December 2016 remained stable at 4.8%, similar to the level recorded in the same month the year before.

With the aim of containing government current spending, in April 2017 the Ministry of Economy and Finance announced a recruitment freeze on 50% of NFPS vacancies, with exceptions for the judiciary, the legislature, the Electoral Council, the Office of the Public Prosecutor, public universities, the Social Security Fund and financial intermediaries.

Tax revenues of the central government fell 2.8% in real terms in the first quarter of 2017 compared with the year-before period. This was explained by a drop of 33% in receipts from corporate income tax, which was partially countered by the rise in the other components of direct taxes. In turn, indirect taxes fell 1.9% in real terms owing to declines in receipts from fuel consumption tax (38.3%), the ITBMS on sales (4.6%) and the ITBMS on imports (4.3%).

(b) Credit policy

In keeping with the deceleration of the Panamanian economy, the loan portfolio of the national banking system grew 7.7% in 2016, less than the 11.9% rate in 2015. The main drivers of credit activity were construction (18.0%), industry (17.0%), personal consumption (13.2%) and mortgage lending (12.4%), while the commerce and services sector recorded declines (4.5%), mainly reflecting slower growth in the Colón Free Trade Zone.

Certain indicators of loan portfolio quality deteriorated slightly, but remained sound. The ratio of past-due plus non-performing loans to the total domestic loan portfolio at December 2016 was 2.66% (2.20% in 2015), while the capital adequacy ratio, defined as regulatory capital over risk-weighted assets, stood at 15.1% in 2016, slightly below 2015 levels (15.2%) and well above the legally required minimum (8%).

At December 2016, nominal interest rates on one-year loans for the commercial, consumer and industry segments stood at 7.57%, 8.35% and 7.64%, respectively, reflecting a small annual decline of 4 and 13 basis points in the first two sectors, and an increase of 2 basis points in the third. Nominal interest rates paid on three- and six-month deposits remained practically unchanged, at 1.33% and 2.12%, respectively.

The loan portfolio of the domestic national banking system grew 4.2% in the first quarter of 2017, compared with the year-before period, a slight improvement on growth of 4.0% recorded in the prior-year quarter. The fastest-growing sectors of credit activity were construction (17.0%), personal consumption (12.7%), industry (11.5%), livestock (11.2%) and mortgage lending (10.2%).

(c) Other policies

As a result of efforts in 2015 by the National Assembly of Panama to establish a legal framework to support a more transparent financial system and global cooperation to combat tax evasion, money laundering and the financing of terrorism, in February 2016 the Financial Action Task Force on Money Laundering (FATF) approved Panama's removal from the "grey list", to which it had been added in June 2014. The regional entity of FATF, the Financial Action Task Force of Latin America (GAFILAT) began evaluation of Panama in October 2016, followed by an on-site visit in May 2017.

In April 2017, the National Assembly of Panama approved Law No. 487, under which the National Bank of Panama will be reorganized. The purpose of the bill is to strengthen the Bank's administrative and operational structure by making changes to its board of directors, human resources and other management, administration and operational aspects.

Also ratified in April 2017 was Law No. 484, which provides measures to promote and develop the industrial sector through a new institutional and regulatory framework designed to foster the sector's competitive development. The law provides for the creation of a new national industrial registry, a national competitiveness programme for developing a national industrial policy strategy, and the launch of a one-stop shop for the sector.

Law No. 412, passed in May 2017, provides for the regulation and supervision of fiduciary agents. Its main purpose is to establish rules to ensure the orderly development of fiduciary activities and to harmonize national legislation with international fiduciary standards. Under the law, the

Superintendence of Banks of Panama will have the exclusive power to regulate and supervise licensed fiduciary agents, as well as others legally authorized to engage in the trust business.

3. The main variables

(a) The external sector

The decline of 5.6% of GDP in the current account deficit (7.3% of GDP the previous year) was the result of a drop of 2.7 percentage points of GDP in the goods deficit (15.9% of GDP in 2016), an effect that was partially offset by a decline of 0.6 percentage points in the surplus on the services balance (18.7% of GDP in 2016) and an increase of 0.4 percentage points in the income balance deficit (8.1% of GDP in 2016).

The narrower goods trade deficit resulted from the marked decline in national imports (6% of GDP), excluding the Colón Free Trade Zone, which exceeded the drop in exports (3.3% of GDP). The smaller deficit reflected lower prices for raw materials, the relative stability of fuel prices at below historical levels, slacker demand for imported goods for Panama Canal expansion works —which were completed mid-2016— and the strengthening of the dollar.

The goods trade balance of the Colón Free Trade Zone posted a surplus of US$ 445 million, well above the surplus recorded the year before (US$ 182 million), thanks to the fact that re-exports fell by less (US$ 862 million) than imports did (US$ 1.125 billion). Re-exports continued to trend downwards, owing to the difficulties experienced by Panama's main trading partners, Puerto Rico and the Bolivarian Republic of Venezuela, and to Colombia's protectionist policies.

The surplus on the services balance surplus declined (by 0.6 percentage points of GDP), because the drop in imports (1.4 percentage points of GDP, compared with the year before) exceeded the decline in exports (0.8 percentage points). This performance was driven mostly by the drop (0.7 percentage points of GDP) in the surplus registered on the other business services account.

The widening of the income account deficit (0.4 percentage points of GDP) was explained by an increase of US$ 492 million in payments to foreign investors, mainly payments of dividends and earnings.

Foreign direct investment (FDI) reached US$ 5.209 billion in 2016 (9.4% of GDP), which reflected an increase in inflows equivalent to 0.8 percentage points of GDP over the previous year. Of this total, 66.5% were reinvested earnings, 15% investments in equities and 18.5%, other forms of investment. The bulk of FDI (US$ 2.750 billion) went to non-financial firms.

(b) Economic activity

Panama's growth in 2016 (4.9%), which was below 2015 levels, was driven by different economic activities, the most significant being: electricity, gas and water supply (10.6%), mining and quarrying (8.4%), construction (8.3%), financial intermediation (6.6%) and real estate, business and rental activities (4.7%).

Growth in electricity, gas and water supply services was the result of both cost reductions (33.7%) in electric power generation —owing to lower oil prices— and increased power generation via renewable sources. The larger supply and lower production costs combined to produce a 21% drop in the price of electricity per kilowatt hour (kWh), which stimulated demand and, consequently, production.

Solid performance in construction was attributable to progress in many projects, such as Line 2 of the Metro, the Santiago-David section of the Pan-American Highway, the construction of Terminal 2 of Tocumen International Airport, the urban renovation of Colón, the third bridge over the Panama Canal and the social housing project Techos de la Esperanza. Mining and quarrying activities were boosted by a rise of 29.3% in investments in construction projects in the final quarter of 2016, while financial intermediation continued growing during the year (6.6%), albeit below 2015 levels (10.4%).

The transport, storage and communications sector grew 1.8% in 2016, compared with 4.7% in 2015, as a result of the slowdown in Panama Canal and in ports system activity, owing to the drop in international trade, although this was offset by a rise in the volume of passengers travelling through Tocumen International Airport. Other sectors recording low levels of growth were hotels and restaurants (2.2%) —caused by low occupancy rates (47.7%) resulting from oversupply of rooms— and commerce (3.3%), as re-exports from the Colón Free Trade Zone remained subdued and growth in the sector was almost exclusively limited to domestic trade.

In turn, manufacturing and fishing contracted 2.8% and 8.4%, respectively, the former affected by a drop in livestock slaughtering and natural milk production, and the latter by an overall contraction.

The Panamanian economy grew 6.2% in the first quarter of 2017, compared with growth of 5.0% in the year-earlier period. Greater economic activity was reflected in the results of the commerce sector, owing especially to rises in re-exports from the Colón Free Trade Zone (16.5%) and in local wholesale trade (11.1%). The transport, storage and telecommunications sector was another significant driver of growth, expanding by 10.4% as a result of stronger activity in the Panama Canal, increased movement of containers in the ports system and greater volumes of passenger transportation. Similarly, construction remained buoyant and grew 6.6%.

(c) Prices, wages and employment

The average annual inflation rate, measured by the variation in the consumer price index (CPI), reached 0.7% in 2016, above the level seen in 2015 (0.1%). The main drivers of inflation were restaurants and hotels (5.6%), alcoholic beverages and tobacco (3.1%), and health (2.9%). In turn, four groups of goods and services recorded price declines for the year: transport (2.0%), housing, water, electricity and gas supply (1.0%), footwear and apparel (0.9%), and recreation and culture (0.1%). The CPI was 0.8% up year-on-year in May 2017.

The participation rate increased slightly, from 64.2% in August 2015 to 64.4% in August 2016, with significant disparity by gender (78.6% for men and 51.1% for women). Among the employed, 15.4% work in the primary sector, 18.4% in the secondary sector (manufacturing) and 66.2% in the tertiary sector (services).

The overall unemployment rate reached 5.5% in August 2016, equivalent to a 0.4 percentage point rise year-on-year, while the open unemployment rate increased by 0.6 percentage points, reaching 4.4% in August 2016.

On 22 December 2015, Executive Decree No. 293 was promulgated, raising the minimum wage by 8.5%, a level that came into effect in January 2016 and will prevail for two years. The adjustment is equivalent to a 7.2% increase in real terms, relative to inflation in 2014 and 2015.

Table 1

PANAMA: MAIN ECONOMIC INDICATORS

	2008	2009	2010	2011	2012	2013	2014	2015	2016 a/
	Annual growth rates b/								
Gross domestic product	8.6	1.6	5.8	11.8	9.2	6.6	6.1	5.8	4.9
Per capita gross domestic product	6.7	-0.1	4.0	9.9	7.4	4.9	4.4	4.1	3.2
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	2.6	-12.0	-6.1	0.3	1.0	3.5	8.0	-0.7	-1.9
Mining and quarrying	28.1	7.1	35.3	22.1	25.3	22.6	17.0	7.0	8.4
Manufacturing	4.0	-0.2	4.4	6.0	7.9	1.3	0.9	-1.3	-2.8
Electricity, gas and water	14.7	11.1	3.6	17.6	11.3	9.3	4.7	13.6	10.6
Construction	29.4	4.2	8.5	22.1	28.2	31.1	14.0	6.8	8.3
Wholesale and retail commerce, restaurants and hotels	7.6	3.8	7.0	18.1	10.0	0.4	1.0	4.7	3.1
Transport, storage and communications	7.5	-3.6	4.6	13.6	4.2	1.6	5.5	4.7	1.8
Financial institutions, insurance, real estate and business services	8.0	4.7	5.4	7.0	6.6	7.8	7.6	7.6	5.4
Community, social and personal services	3.8	2.6	2.8	4.8	3.9	2.5	4.0	6.8	7.3
Investment and saving c/	**Percentajes of GDP**								
Gross capital formation	41.6	30.4	37.2	43.5	44.4	45.8	47.0	46.6	…
National saving	30.5	29.8	27.6	29.0	35.6	36.0	33.4	39.3	…
External saving	11.1	0.7	9.6	14.5	8.8	9.8	13.7	7.3	5.7
Balance of payments	**Millions of dollars**								
Current account balance	-2 722	-179	-2 765	-4 993	-3 528	-4 401	-6 730	-3 809	-3 151
Goods balance	-4 546	-2 181	-4 543	-7 217	-6 415	-9 540	-10 823	-9 709	-8 785
Exports, f.o.b.	10 323	12 038	12 675	16 926	18 857	17 057	14 972	12 783	11 705
Imports, f.o.b.	14 869	14 218	17 218	24 143	25 272	26 597	25 795	22 492	20 490
Services trade balance	3 155	3 324	3 490	3 933	4 696	7 783	7 789	10 027	10 169
Income balance	-1 570	-1 449	-1 849	-1 911	-1 897	-2 707	-3 818	-4 020	-4 381
Net current transfers	238	126	138	202	88	63	122	-106	-155
Capital and financial balance d/	3 302	785	3 072	4 765	2 570	4 292	7 127	2 824	4 478
Net foreign direct investment	2 196	1 259	2 363	2 956	3 254	3 612	4 130	3 966	5 041
Other capital movements	1 105	-475	709	1 809	-685	679	2 997	-1 142	-563
Overall balance	579	606	307	-228	-958	-109	397	-984	1 327
Variation in reserve assets e/	-579	-606	-307	228	-36	-402	-1 222	78	-609
Other financing	0	0	0	0	994	511	825	907	-718
Other external-sector indicators									
Real effective exchange rate (index: 2005=100) f/	106.5	103.5	103.0	103.9	94.4	92.2	89.0	85.5	84.6
Terms of trade for goods (index: 2010=100)	97.3	101.9	100.0	97.8	98.2	97.7	99.7	97.0	94.3
Net resource transfer (millions of dollars)	1 732	-664	1 223	2 854	1 667	2 096	4 134	-289	-621
Gross external public debt (millions of dollars)	8 477	10 150	10 439	10 858	10 782	12 231	14 352	15 648	16 902
Employment	**Average annual rates**								
Labour force participation rate g/	63.9	64.1	63.5	61.9	63.4	64.1	64.0	64.2	64.4
Unemployment rate h/	6.5	7.9	7.7	5.4	4.8	4.7	5.4	5.8	6.4
Open unemployment rate i/	5.0	6.3	5.8	3.6	3.6	3.7	4.1	4.5	5.2

Table 1 (concluded)

	2008	2009	2010	2011	2012	2013	2014	2015	2016 a/
Prices	**Annual percentages**								
Variation in consumer prices									
(December-December)	6.8	1.9	4.9	6.3	4.6	3.7	1.0	0.3	1.5
Variation in average real wage	-4.1	2.6	7.2	0.1	3.3	0.3	5.5	3.3	3.9
Nominal deposit rate j/	3.5	3.5	3.0	2.3	2.1	2.1	2.2	2.1	2.1
Nominal lending rate k/	8.2	8.3	7.9	7.3	7.0	7.4	7.6	7.6	7.6
Central government	**Percentajes of GDP**								
Total revenue l/	18.6	16.8	17.3	16.2	16.2	15.4	14.4	13.9	13.9
Tax revenue	9.9	9.9	10.7	10.3	11.1	10.8	10.2	9.7	10.0
Total expenditure	18.3	18.1	19.6	19.4	18.8	19.2	18.4	17.8	18.2
Current expenditure	13.1	12.4	12.8	12.1	11.4	10.7	11.6	11.5	11.5
Interest	2.9	2.6	2.4	2.1	1.9	1.8	1.7	1.8	1.8
Capital expenditure	5.3	5.8	6.8	7.3	7.4	8.5	6.8	6.3	6.7
Primary balance	3.2	1.3	0.1	-1.1	-0.7	-1.9	-2.3	-2.1	-2.5
Overall balance	0.3	-1.3	-2.4	-3.2	-2.6	-3.8	-4.0	-3.9	-4.3
Central government public debt	42.0	40.7	39.6	36.7	35.2	35.0	36.8	38.5	38.8
Domestic	7.5	2.7	3.7	5.1	8.3	7.7	7.9	8.5	8.5
External	34.4	38.0	35.9	31.6	26.9	27.3	29.1	29.9	30.4
Money and credit	**Percentages of GDP, end-of-year stocks**								
Domestic credit	58.2	52.6	56.8	57.9	58.8	47.6	58.1	60.8	68.1
To the public sector	-8.5	-8.2	-6.3	-3.6	-3.5	-5.6	-7.2	-7.0	-6.3
To the private sector	84.5	79.7	84.4	81.9	81.3	67.2	83.0	86.8	91.0
Others	-17.9	-18.9	-21.2	-20.5	-19.0	-14.1	-17.7	-19.0	-16.6
Monetary base	0.9	0.9	0.9	1.7	1.0	0.8	1.0	1.2	1.1
M2	80.7	82.0	83.8	76.4	73.1	57.5	70.5	69.4	69.1

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
a/ Preliminary figures.
b/ Based on figures in local currency at constant 2007 prices.
c/ Based on values calculated in national currency and expressed in current dollars.
d/ Includes errors and omissions.
e/ A minus sign (-) indicates an increase in reserve assets.
f/ Annual average, weighted by the value of goods exports and imports.
g/ Nationwide total.
h/ Urban total. Includes hidden unemployment.
i/ Urban total. Includes an adjustment to the figures for the economically active population for exclusion of hidden unemployment.
j/ Six-month deposits rate.
k/ Interest rate on one-year trade credit.
l/ Includes grants.

Table 2
PANAMA: MAIN QUARTERLY INDICATORS

	2015				2016				2017	
	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2 a/
Gross domestic product (variation from same quarter of preceding year) b/	6.2	6.0	5.7	5.3	5.0	5.3	4.7	4.5	6.2	...
Gross international reserves (millions of dollars)	4 273	4 259	4 195	3 818	4 041	4 774	4 226	4 206	4 107	4 195 c/
Real effective exchange rate (index: 2005=100) d/	86.4	85.8	84.9	84.9	84.1	85.0	85.0	84.3	84.2	85.3 c/
Consumer prices (12-month percentage variation)	0.0	0.0	-0.4	0.3	0.6	0.1	1.2	1.5	1.5	0.8 c/
Nominal interest rates (average annualized percentages)										
Deposit rate e/	2.2	2.2	2.2	2.1	2.1	2.1	2.1	2.2	2.1	...
Lending rate f/	7.7	7.5	7.7	7.6	7.5	7.6	7.6	7.6	7.6	...
Sovereign bond spread, Embi + (basis points to end of period) g/	199	195	249	218	212	213	168	186	153	152 c/
Risk premiia on five-year credit default swap (basis points to end of period)	141	141	186	182	160	161	142	127	120	95
International bond issues (millions of dollars)	1 250	450	-	-	1 000	575	75	550	150	1 200 c/
Domestic credit (variation from same quarter of preceding year)	5.7	5.2	4.9	9.9	15.3	12.8	13.6	13.3	7.7 h/	...
Non-performing loans as a percentage of total credit	0.8	0.8	0.8	0.9	1.0	1.0	1.2	1.2	1.3	...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
a/ Preliminary figures.
b/ Based on figures in local currency at constant 2007 prices.
c/ Figures as of May.
d/ Quarterly average, weighted by the value of goods exports and imports.
e/ Six-month deposits rate.
f/ Interest rate on one-year trade credit.
g/ Measured by J.P.Morgan.
h/ Figures as of January.

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