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PANAMA

IDB COUNTRY STRATEGY (2015-2019)

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ABBREVIATIONS

AECID	Agencia Española de Cooperación Internacional para el Desarrollo [Spanish Agency for International Development Cooperation]
CAF	Banco de Desarrollo de América Latina [Development Bank of Latin America]
CGR	Contraloría General de la República [Office of the Comptroller General of the Republic]
DAC	Development Assistance Committee
DCTI	Dirección de Cooperación Técnica Internacional [International Technical Cooperation Office]
DRM	Disaster risk management
EIU	Economist Intelligence Unit
GDP	Gross domestic product
GTA	General Treasury Account
IDAAN	Instituto de Acueductos y Alcantarillados Nacionales [National Water Supply and Sewer System Administration]
IIC	Inter-American Investment Corporation
IMF	International Monetary Fund
INEC	Instituto Nacional de Estadística y Censo [National Statistics and Census Institute]
IPSAS	International Public Sector Accounting Standards
ISSAI	International Standards of Supreme Audit Institutions
ISTMO	Integración y Soluciones Tecnológicas del Modelo de Gestión Operativa [Operating Management Model Integration and Technology Solutions]
LPI	Logistics Performance Index
MAPS	Methodology for Assessing Procurement Systems
MEDUCA	Ministry of Education
MEF	Ministry of Economy and Finance
MIF	Multilateral Investment Fund
MOP	Ministry of Public Works
MSMEs	Micro, small, and medium-sized enterprises
NFPS	Nonfinancial public sector
NSG	Non-sovereign guaranteed
ODA	Official development assistance
OECD	Organisation for Economic Co-operation and Development
OVE	Office of Evaluation and Oversight
PBL	Policy-based loan
PEG	Plan Estratégico de Gobierno [Government Strategic Plan]
PNLog	Plan Nacional de Logística de Cargas [National Freight Logistics Plan]
SCF	Structured and Corporate Financing Department
SG	Sovereign-guaranteed
SIEPAC	Sistema de Interconexión Eléctrica de los Países de América Central [Central American Electric Interconnection System]
SMEs	Small and medium-sized enterprises
TERCE	Tercer Estudio Regional Comparativo y Explicativo [Third Regional Comparative and Explanatory Study]
TFFP	Trade Finance Facilitation Program

UNDP	United Nations Development Programme
WEO	World Economic Outlook
ZLC	Zona Libre de Colón [Colón free trade zone]

EXECUTIVE SUMMARY

Economic and social context:	Between 2010 and 2014, Panama grew at an average annual rate of 8.3%, the highest in Latin America and the Caribbean, driven primarily by expansion of the Panama Canal, increased public investment, and greater private-sector activity in the construction and services sectors. This growth unfolded in a context of macroeconomic stability and fiscal consolidation. From a social standpoint, the economic expansion reduced unemployment and poverty. However, the socioeconomic gaps are still pronounced: in 2014, while the poverty rate in urban areas was 13.8%, it was 49.7% in rural areas and 86.9% in the indigenous <i>comarcas</i> [territorial subdivisions]; in addition, income distribution inequality did not decline between 2009 and 2012. Urban areas, although exhibiting lower poverty rates, account for close to half of the country's population living in poverty and experience shortfalls in terms of coverage and quality of basic services.
The IDB in Panama:	The Bank's country strategy with Panama for the 2010-2014 period focused on six sectors: (i) public finance; (ii) transport; (iii) water and sanitation; (iv) energy; (v) education; and (vi) health. Over the course of the country strategy period, 16 sovereign-guaranteed operations were approved for a total amount of US\$1.754 billion. In addition, the private sector windows approved loan operations for a total of US\$339.5 million.
Priority issues:	The country strategy for 2015–2019 ¹ will focus on: (i) improving the delivery of basic services to the population living in poverty; (ii) strengthening the education profile of the population; and (iii) enhancing the logistics services, efficiency, and connectivity of the productive infrastructure. In pursuing each of these objectives, the strategy will pay particular attention to the population living in poverty and extreme poverty and will incorporate, as applicable, issues of gender, diversity, integration, climate change, and institutional capacity of the local counterparts. For its part, the private sector of the IDB will support the strategy objectives, with an emphasis on investments in transportation and logistics and in energy, while also monitoring areas in the portfolio. This country strategy addresses the structural challenges raised in the Update to the Bank's Institutional Strategy for 2010-2020 of: (i) social exclusion and inequality; (ii) low levels of productivity and innovation; and (iii) lagging economic integration.
Lending framework:	The estimated support for the 2015-2019 period amounts to approximately US\$1.95 billion in sovereign-guaranteed approvals. The financial scenario calls for annual approvals of US\$390 million and annual disbursements on the order of US\$352.8 million.
Main risks:	The main risks affecting implementation of the strategy are: (i) macroeconomic, associated with external shocks and fiscal sustainability; (ii) implementation, related to the execution capacity of the local counterparts; and (iii) risks resulting from the potential occurrence of natural disasters.

¹ This country strategy will be in effect until December 2019.

I. COUNTRY CONTEXT

- 1.1 Panama is the fastest-growing economy in Latin America and the Caribbean, having posted an average annual gross domestic product (GDP) growth rate of 8.3% between 2010 and 2014. This expansion was nourished by an increase in aggregate investment, from 23% of GDP in 2007 to 30% of GDP in 2014. The economic performance and actions in the fiscal, financial, and trade areas enabled the country to further integrate into the global economy and acquire investment grade status,² consolidating its position as a major financial and trade center with easy access to external sources of financing.
- 1.2 The robustness of the Panamanian economy has been fueled by the services and construction sectors. Since 2008, services have accounted for approximately 60% of GDP growth, particularly international banking center, transport, and trade services.³ Construction was responsible for an additional 23.4% of GDP growth, owing to the Panama Canal expansion process. Lastly, the primary sectors contributed 9% of the nation's economic growth.⁴
- 1.3 On the expenditure side, public investment rose from 3.7% of GDP in the 2005-2009 period to an average of 8.2% of GDP in the period from 2010 to 2014.⁵ This increase was associated with the Panamanian government's US\$13.595 billion five-year investment plan for the latter period, which focused on infrastructure works. In addition, the expansion of the Canal generated an increase in foreign direct investment flows, which averaged 10.5% of GDP between 2010 and 2014.
- 1.4 This has been achieved in a context of fiscal stability. Between 2010 and 2014, the nonfinancial public sector (NFPS) deficit averaged 2.5% of GDP, while public debt declined from 43.2% to 38.8% of GDP. The country's fast economic growth and favorable financing terms contributed to fiscal sustainability, playing a key role in reducing the debt load.
- 1.5 This growth led to a reduction in the unemployment rate, from 8.7% in 2006 to 4.1% in 2014, and in the poverty incidence rate, which fell from 38.3% to 25.8% over the same period. However, the effect of growth on poverty reduction was lower than the average for Latin America.⁶ This is due to the country's pronounced social gaps and institutional shortcomings. There are very dynamic sectors in Panama, such as the Canal conglomerate, which enjoy special regulations to facilitate investment and require skilled labor, operating side by side with other sectors, such as agriculture and manufacturing, which employ 20% of the population and continue to be subject to the restrictive and generally rigid provisions of the country's legal and regulatory framework, resulting in low investment and productivity levels. This is coupled with significant gaps in health,

² Panama has maintained its investment grade status since 2010. In 2014, the Emerging Market Bond Index, which measures country risk, was at similar levels to those of Chile and Peru.

³ Of this percentage, transportation and communications together accounted for 21.2% of GDP growth, while financial services and trade accounted for 18% each.

⁴ Public sector activities account for the remaining 7.6%.

⁵ Refers to NFPS investment.

⁶ In Latin America, every percentage point of average annual growth meant a reduction in poverty of almost four percentage points, while the reduction in Panama was of one percentage point. Source: IDB "[Análisis de Desafíos para el Crecimiento](#) [Assessment of Growth Challenges], 2015.

- education, and other basic services, which create barriers that prevent the lower-income population from gaining a foothold in the productive areas undergoing expansion. This has resulted in the lower deciles having a disproportionately low share of income, a distinctive feature of the country with respect to the rest of Latin America.⁷
- 1.6 Poverty levels in rural areas, although reduced, continue to be high. In 2014, the incidence of poverty in rural areas and indigenous *comarcas*⁸ amounted to 49.7% and 86.9%⁹ respectively, compared to an incidence of 13.8% in urban areas. Furthermore, extreme poverty has remained practically unchanged over the past four years, with a slight increase in urban areas in the last year.¹⁰ In addition, Panama has the fourth largest income distribution inequality among Latin American and Caribbean countries, with a Gini coefficient of 0.52 that has remained constant since 2009.
- 1.7 The above-described situation reflects persistent challenges for the public provision of social services and for the consolidation of a social safety net that comprehensively addresses the needs of rural areas and indigenous *comarcas*. It also reflects the difficulties that the major urban centers have been facing in addressing the growing demand for basic services as the population increases. In particular, the rapid population growth in the provinces of Panama and Colón (7.7% between 2010 and 2014) has created problems of overcrowding and aggravated sanitation conditions, revealing limitations in the responsiveness of basic urban services to the needs of periurban areas, where the poor population resides.¹¹
- 1.8 In the productive sphere, the vitality of Canal-driven economic activity, anchored by a productive conglomerate engaged in export logistics and transportation services, has not extended to the tradable production sectors (agriculture and manufacturing),¹² which are characterized by territorially dispersed production, limited diversification, and low productivity levels.
- 1.9 An analysis of the challenges being faced by Panama in sustaining the country's high growth and investment rates, once the Canal expansion works are completed, and in advancing more rapidly toward poverty reduction highlights the need to enhance productivity in the more dynamic, Canal-related sectors, strengthen this

⁷ Székely, M. "Análisis del círculo de la desigualdad de oportunidades" [Analysis of the inequality of opportunity circle], IDB, 2015.

⁸ Panama has about 3.6 million inhabitants, of whom 66% live in urban areas and 34% in rural areas. Roughly 12% of the population considers itself indigenous. The country's territorial division includes five indigenous *comarcas*. These *comarcas* are predominantly rural and are populated by various ethnic groups, notably the Emberá-Wounaan, GunaYala, and Ngäbe -Buglé.

⁹ MEF. Ministry of Economy and Finance (MEF). "Pobreza e Indigencia. Encuesta de Mercado Laboral, marzo 2014" [Poverty and indigence. Labor market survey, March 2014], February 2015.

¹⁰ Between 2011 and 2014, the incidence of extreme poverty went from 11.5% to 11.0%, measured at 3.3% in urban areas and at 26.3% in rural areas. In 2014, urban extreme poverty grew 6% with respect to 2013. MEF. Idem.

¹¹ While the incidence of poverty and extreme poverty is greater in rural areas and indigenous *comarcas* than in urban areas, 47% of the population living in overall poverty in 2014 (272,073 people) resided in urban areas.

¹² In 2014, the agriculture and manufacturing sectors respectively contributed 2.9% and 4.8% to GDP.

conglomerate's links to the rest of the productive sector, and provide an institutional framework that can ensure investment certainty and facilitate growth. This should be accompanied by actions aimed at strengthening human capital formation, improving access to basic services for the population groups living in poverty, and providing social safety net programs that can effectively address the needs of those living in extreme poverty.

- 1.10 To respond to these challenges, the country has prepared a Government Strategic Plan (PEG) for 2015-2019, with a focus on enhancing competitiveness and promoting social inclusion in the framework of a sustainable and inclusive development model.”¹³

II. THE IDB IN PANAMA

- 2.1 **The Bank's country strategy with Panama for 2010-2014** contributed to the country's development in six priority areas: (i) public finance, (ii) transport; (iii) water and sanitation; (iv) energy; (v) education; and (vi) health. During this period, 16 sovereign-guaranteed (SG) operations were approved for a total amount of US\$1.754 billion, including a US\$350 million guarantee and a contingent loan for natural disaster emergencies for US\$100 million. Disbursements totaled US\$1.351 billion and cumulative net flows for the period were positive for the country, amounting to US\$578.6 million.¹⁴
- 2.2 **The Bank's program** focused primarily on two areas: supporting reforms to strengthen fiscal and financial sustainability and reducing vulnerability to climate change and natural disasters; and improving basic services and transportation and energy infrastructure in areas of greater poverty. To this end, US\$1.2 billion was approved in the area of public finance; a total of US\$244 million in water and sanitation, health, and education; US\$90 million in transportation and energy; and US\$220 million in the areas of climate change and natural disasters. Approved technical-cooperation operations totaled US\$16.05 million and focused on the following sectors: environment and natural resources; water and sanitation; transportation, health, and social protection; and education. In addition, investment grants amounted to US\$40.4 million, focusing on citizen security; water and sanitation; and health and social protection.
- 2.3 **With respect to non-sovereign guaranteed (NSG) operations**, 26 loan operations were approved for a total of US\$339.5 million, primarily to support improvements in access to credit for small and medium-sized enterprise (SME),

¹³ Government of Panama. “Plan Estratégico de Gobierno 2015-2019” [Government Strategic Plan 2015-2019], 2015.

¹⁴ As of 31 December 2014, Panama's outstanding debt with the IDB totaled US\$1.908 billion, accounting for 55.9% of multilateral external debt. The CAF is in second place with approximately 22.1%, followed by the World Bank with 19.0%.

mortgage loans for low- and middle-income populations, foreign trade finance, and strengthening of the local capital market and of the financial system in general.¹⁵

- 2.4 **Outcomes achieved.** The Bank's work under the country strategy¹⁶ made it possible to support the country in the design and implementation of **institutional reforms** in the areas of *public finance* and *climate change and natural disasters*.¹⁷ In the first of these areas, the country's resilience to macroeconomic and financial shocks was strengthened by adopting public asset and liability management instruments and by reinforcing sovereign assets through an increase in funding for the Fondo de Ahorros de Panamá [Panamanian Savings Fund]. In the second area, the vulnerability of public investment to natural disasters was reduced by including risk analysis in public investment projects and creating an expenditure item in the Ministry of Economy and Finance (MEF) to allocate funds to public entities for disaster risk management purposes. In terms of **human capital**, coverage of basic social services, primarily *health and education*,¹⁸ was expanded in rural areas and indigenous *comarcas* that are difficult to reach, where the population with the highest extreme poverty levels resides. Specifically, in the area of health care, the sector's responsiveness was improved by implementing a pay-for-performance and capitation financing system for health providers at 75 basic health care units of the fixed and itinerant network. In education, the accessibility and quality of the educational offerings in the indigenous *comarcas* of Ngäbe-Buglé and Emberá-Wounaan were improved, through construction of 41 basic primary schools. Moreover, an innovative school infrastructure model was promoted, through the creation of facilities that foster collaborative learning, scientific experimentation, and technological and linguistic skills, while encouraging holistic student development.
- 2.5 In **infrastructure**, the condition of the country's major *roads*¹⁹ was improved along with the linkage between the country's provinces other than the province of

¹⁵ The total consists of: (i) Structured and Corporate Financing Department (SCF): 12 commercial bank financing operations for US\$169 million and 3 lines of credit under the Trade Finance Facilitation Program (TFFP) for US\$24 million; (ii) Inter-American Investment Corporation (IIC): 8 loan operations for US\$143.5 million; and (iii) Multilateral Investment Fund (MIF): 3 loans for US\$3 million. The latter window additionally approved 10 nonreimbursable technical-cooperation operations for a total of US\$7.4 million in the entrepreneurship development, natural resources, microcredit, and youth employment sectors.

¹⁶ Includes outcomes achieved during the 2010-2014 strategy period from the portfolio in execution as well as from approvals recorded during the period.

¹⁷ Refers to the following operations: Program to Strengthen Fiscal Management (PN-L1066); Fiscal Policy and Tax Equity Consolidation Program (PN-L1067); Program to Reduce Vulnerability to Natural Disasters and Climate Change I (PN-L1070); Program to Reduce Vulnerability to Natural Disasters and Climate Change II (PN-L1074); Strengthening Macrofinancial and Fiscal Management (PN-L1086); Contingent Loan for Natural Disaster Emergencies (PN-X1007); Strengthening Macrofinancial and Fiscal Management II (PN-L1089); and Fiscal and Financial Stability and Transparency Improvement Program (PN-L1100).

¹⁸ Under the following operations: Educational Facilities and Learning Quality (PN-L1064); Health Equity Improvement and Services Strengthening Program (PN-L1068); and Innovation in School Infrastructure (PN-L1072).

¹⁹ Through the Puebla Panama Plan Multiphase Road Infrastructure Program to Enhance Competitiveness – Phase II (PN-L1047), the Penonomé-Agua Dulce highway, which is part of the Pacific Corridor, was rehabilitated and maintained. In addition, performance-based road maintenance contracts were implemented for the rehabilitation and maintenance of 340 kilometers of rural roads in the provinces of Los Santos, Herrera, Chiriquí, Coclé, and Veraguas.

Panama and the province of Colón [hereinafter referred to as “other provinces”] and the national production centers. The accessibility and quality of *water and sanitation*²⁰ services in the other provinces were enhanced, and support was provided for the sector’s reform process by preparing a national strategy for 2014-2018 and creating an interagency committee in the Ministry of the Presidency to lead the reform. The private sector windows finished disbursing the loan approved in 2008 to complete the *Panama Canal expansion*²¹ works, which will make it possible to increase the number and size of vessels sailing through the Canal as well as to develop the capacity needed to address growing port demand by providing competitive levels of service. In *energy*, electricity coverage in rural and indigenous areas was expanded,²² access to financing was increased for power generation from renewable sources and for energy savings through lines of credit from the private sector windows, and an IIC loan was provided to build the 8.6-MW San Lorenzo hydropower plant. In addition, progress was made on integrating the country into the Central American Regional Electricity Market and basic engineering, predesign, and environmental studies were performed for the Colombia-Panama electric interconnection project.²³

- 2.6 **Current portfolio.** As of 31 December 2014, the SG portfolio consisted of 20 operations for a total of US\$556.2 million, with an undisbursed balance of US\$323.8 million, primarily concentrated in the water and sanitation (43%), education (20%), transport (16%), and health and social protection (8%) sectors. The portfolio also included investment grants totaling US\$29.2 million in the areas of citizen security and water and sanitation. In terms of performance, the Panama highway is relatively new, with an average age of 3.1 years and a disbursement rate of 25% in 2014, similar to the Bank’s average of 26%.²⁴ This level of execution was achieved thanks to a proactive road management effort that made it possible to reduce the proportion of loans with extensions from 19% in 2010 to 13% in 2014.
- 2.7 For its part, the NSG portfolio totaled US\$601 million, of which 83% is from SCF, 16.8% from the IIC, and 0.2% from the MIF. This outstanding portfolio is distributed as follows: transportation (66.5%); financial services (25.5%); and energy (7.8%). In addition to the loans, the NSG portfolio includes capital investments of US\$4 million and technical cooperation operations for US\$1 million. The current SG and NSG portfolio will support the strategic objectives and/or dialogue areas identified for the 2015-2019 period.

²⁰ IDAAN Water and Sanitation Multiphase Investment Program - Phase I (PN-L1042).

²¹ In 2008, the IDB approved a loan to the Panama Canal Authority for US\$400 million to support the expansion of the Panama Canal, the largest infrastructure project ever undertaken in Latin America, with a total cost of US\$5.25 billion. According to the Panama Canal Authority, works under this project were 95% completed as of 31 October 2015.

²² In the context of the Sustainable Rural Electrification Program in Panama (PN-0150), electricity coverage in rural areas—including the indigenous *comarcas*—increased by 10%, through the extension of distribution networks and the installation of isolated energy systems (solar panels).

²³ In addition, the private sector participated in other areas of opportunity arising in the financial, low-income housing, foreign trade, and SME credit access areas.

²⁴ Rate of disbursements measured as investment loan disbursements in 2014 as a percentage of the balance eligible for disbursement at the start of the year.

- 2.8 **The main lessons learned** during the 2010-2014 period are: (i) the execution of operations in rural areas and indigenous *comarcas* requires close multisector coordination in order to achieve the planned outcomes and maximize Bank support in those population groups; (ii) the execution arrangements should be adapted to conform to the existing institutional capacities and consider the challenges of each program; (iii) coordination between the MEF, the execution units, and the Bank should be strengthened in order to ensure proper allocation of financing and local counterpart resources throughout the program implementation period; (iv) civil works contracts in rural and indigenous areas require special supervisory arrangements tailored to the characteristics of those areas; (v) alternative execution modalities should be employed, including the use of fiduciary entities or funds managers, to streamline the contracting and disbursement processes; and (vi) in the context of support for policy reforms, changes in the environment can affect the implementation and sequence of the Bank's programmatic interventions, so it is important for the Bank to evaluate alternatives for maintaining the dialogue and monitoring advances in the sector, using all the instruments at its disposal, whether financial or nonfinancial.
- 2.9 **The Country Program Evaluation: Panama (2010-2014)**, prepared by the Office of Evaluation and Oversight (OVE), identified the following recommendations: (i) consider key crosscutting issues such as duality, poverty, productivity, and inequity as part of the country strategy design; (ii) increase Bank support on poverty issues through a greater focus on beneficiaries living in poverty; (iii) continue to support the reinforcement of country systems and project management, and promote the strengthening of municipal and regional institutions, with a view to delivering basic services more efficiently and effectively; (iv) strengthen the design, monitoring, and completion of policy-based loans in order to ensure the continuity of Bank support in priority areas and the achievement of lasting policy reforms; and (v) strengthen risk analysis during project design. The implementation of these recommendations by Management is summarized in Annex VI.

III. PRIORITY ISSUES

- 3.1 The strategy for the 2015-2019 period seeks to contribute to Panama's medium- and long-term inclusive development by focusing Bank actions on three priority objectives:²⁵ (i) improve the delivery of basic services to population segments living in poverty; (ii) strengthen the educational profile of the population; and (iii) enhance the logistics services, efficiency, and connectivity of productive infrastructure.
- 3.2 These objectives were selected on the basis of: (i) the dialogue with the authorities; (ii) an analysis of constraints on growth and social inclusion;²⁶ (iii) the Bank's outstanding portfolio in the priority areas and the lessons learned from the Bank's work in Panama; and (iv) the potential for achieving synergies among

²⁵ These objectives are not conceived of as being independent from one another; accordingly, the investments to be made during this strategy period will seek to take advantage of synergies and pursue close multisector coordination.

²⁶ [Análisis de Desafíos para el Crecimiento](#) [Assessment of growth challenges] and [Análisis del Círculo de la Desigualdad de Oportunidades](#) [Analysis of the inequality of opportunity circle], IDB 2015.

- sector-specific interventions and attaining outcomes during the government's terms of office. In addition, this selection process benefitted from a dialogue with civil society and other development financing organizations.
- 3.3 The actions called for in this strategy are consistent with the priority action areas of the Plan Estratégico de Gobierno [Government Strategic Plan] (PEG) for 2015-2019: improvement in living conditions; reinforcement of human capabilities; and diversification and productivity of the economic base. The targeting within these areas will take into account the critical factors highlighted in the analyses carried out by the Bank. The priority areas and actions also contribute to specific objectives identified in the Update to the Bank's Institutional Strategy for 2010-2020.
- 3.4 The IDB will support these objectives through new operations, technical assistance, and SG and NSG projects in execution, which provide a basis for moving forward during the strategy period and capitalize on the Bank's experience in the country. In addition to the opportunities identified in this strategy's objectives, the NSG operations will utilize public-private or exclusively private mechanisms to identify financing opportunities for micro, small, and medium-sized enterprises (MSMEs), with a particular focus on SMEs with export potential or with the potential for insertion into international value chains, and financing for the housing sector, among other sectors consistent with the Update to the Bank's Institutional Strategy for 2010-2020.
- A. Improve the delivery of basic services to population segments living in poverty**
- 3.5 Rural areas, and particularly indigenous *comarcas*, continue to exhibit the highest poverty and extreme poverty rates in Panama and have inadequate access to basic services. At the same time, urban growth has created pockets of poverty in periurban areas, with tenuous access to basic services, particularly water and sanitation. In this context, improving the quality of life of these population segments requires having in place a targeted social safety net that can comprehensively serve the poor, particularly people living in extreme poverty, while at the same time addressing shortcomings in the supply of health, education, water and sanitation, and electrification services.
- 3.6 In the area of **social protection**, there are currently three conditional cash transfer programs with nationwide coverage aimed at addressing the needs of the population living in poverty.²⁷ However, these programs suffer from targeting problems in the poorest segments, gaps in coverage, limited verification of corresponsibility, and overlapping programs, all of which affects the efficiency of social expenditure. Panama does not have a master registry of beneficiaries to target the allocation of social programs at the national level, nor does it have protocols adapted to the country's cultural diversity. These shortcomings affect the relevance, quality, and coverage of these services, particularly in the indigenous

²⁷ (i) Red de Oportunidades [Network of Opportunities] for population segments living in extreme poverty, including the *Bono Familiar Alimentario* [family food voucher]; (ii) "120 a los 65" [120 at 65], for senior adults; and (iii) "Ángel Guardián" [Guardian Angel], for severely disabled people living in extreme poverty. In addition, the country has a "*Beca Universal*" [Universal Scholarship] program aimed at promoting school attendance by primary, pre-secondary, and secondary school students.

comarcas. In addition, the absence of periodic reviews (recertification) of the beneficiary rolls gives rise to leakages and undercoverage. Furthermore, there is a lack of coordination with education and health services. From a fiscal standpoint, the potential gains from improved targeting²⁸ of these programs are estimated at US\$68 million per year.²⁹

- 3.7 With regard to the provision of **health** services, the high maternal and infant mortality rates and chronic malnutrition rates reflect gaps in access to services, particularly in the country's rural areas and indigenous *comarcas*. Between 1990 and 2013, the maternal mortality rate rose from 53.4 to 55.6 deaths per 100,000 live births, far above the goal of 13.4 set under the Millennium Development Goals (MDGs). In the indigenous communities, the rate is even higher; for example, in 2012, the *comarca* of Ngäbe-Buglé had 274.3 maternal deaths per 100,000 inhabitants,³⁰ five times more than the national average. A large proportion of maternal deaths (69% of the total) is related to direct obstetric causes and results from pregnancy, delivery, and neonatal complications. The infant mortality rate declined between 1990 and 2013 from 18.9 to 16 deaths per 1,000 live births but is still far from the goal of 6.3 deaths per 1,000 live births by 2015 associated with the MDGs. In addition, the neonatal and postnatal mortality rates have not fallen significantly over the last five years and in some cases have increased.³¹ A considerable number of infant deaths is the result of respiratory or diarrheic infections that are easily treatable through basic health services.
- 3.8 The **chronic malnutrition** rate among children under 5 in indigenous *comarcas* is 56%, three times the national average (19%) and nine times higher than the rate in urban areas (6%);³² the prevalence of anemia among infants 6 to 11 months of age in indigenous *comarcas* is 81%³³ versus 36% nationwide, primarily due to inadequate feeding practices and poor access to water and basic sanitation. In addition, the availability of **early childhood development** services is limited. At the national level, a mere 36% of children under 5 have access to these services, and in indigenous regions the figure is only 6%.³⁴ The gaps in coverage are coupled with weaknesses in the design of methods and contents. The programs and services targeted at early childhood (0-3) do not include standards and procedures that can ensure high quality care; they lack supervisory and oversight systems to verify implementation; the staff responsible for the services have uneven training; and they are usually not culturally adapted to each specific indigenous group.
- 3.9 The above-described circumstances are partly the result of inequalities in terms of timely access to and quality of health care services for those living in poverty. In indigenous *comarcas*, there are still settlements with no access or sporadic access

²⁸ Coverage of eligible beneficiaries not being served and exit of ineligible beneficiaries.

²⁹ Refers to the programs Red de oportunidades, 120 a los 65, and Ángel Guardián. Prepared by the IDB on the basis of data from the multipurpose survey of March 2013.

³⁰ INEC, 2012.

³¹ The neonatal mortality rate rose from 6.8 per 1,000 live births in 2008 to 8.5 in 2013.

³² Mesoamerica Health Initiative 2015.

³³ Idem.

³⁴ INEC. Multipurpose survey, August 2013.

to health care services. The inequity of access is related to the absence of an integrated network of services, inefficient use of resources, a lack of policies adapted to the needs of poor population groups, and a low budget allocation for the provision of health care services, especially in the rural areas and indigenous *comarcas*.

- 3.10 In rural areas, a low level of **water supply** services coverage in rural areas is evident, reaching only 78% of the population compared to 93.5% nationwide, while in indigenous *comarcas* the water coverage rate is 56%.³⁵ With regard to urban areas, the population growth experienced by the Panama City metropolitan area (AMP)³⁶ in recent years has put pressure on the delivery of water services. As a result, there continue to be households supplied by water trucks, rivers, and creeks.³⁷ In addition, **sanitation** services are also characterized by gaps in coverage. Urban and periurban areas have a 56%³⁸ rate of access to sanitation sewerage. In the AMP, the sewerage system has operational deficiencies, creating overflows and pollution in bodies of water. In terms of service quality, 80% of the urban population has a continuous supply of water³⁹ during the dry season, and only 17% of the water samples taken in the water supply systems operated by IDAAN⁴⁰ satisfactorily meet potable water quality standards. In addition, the sector's institutional structure and regulatory framework need to be strengthened to address these challenges.
- 3.11 In view of these challenges, the goals of the PEG 2015-2019 are to improve the living conditions of the population, foster inclusion, and reduce territorial asymmetries through actions aimed at expanding the coverage and improving the quality of basic social services (water and sanitation, housing, health, rural electrification, transportation, and community facilities and services).⁴¹ With regard to water and sanitation, the priorities are to close the inequity gaps in terms of service access and quality, in urban as well as rural areas, and to strengthen the sector's organizational model and financing mechanisms. With regard to health care, the PEG proposes ensuring universal access to health care, with an emphasis on indigenous areas, and improving the quality of care with a view to reducing chronic malnutrition in the population and moving forward with a preventive health care approach. In terms of social protection, the government proposes creating a comprehensive social protection system, implementing a master registry of beneficiaries, and advancing toward implementation of a comprehensive early childhood care policy.

³⁵ INEC. 2010 Census. Volume III: Household characteristics, 2011.

³⁶ According to the Office of the Comptroller General of the Republic (CGR), the AMP is an urban area comprised of Panama City, San Miguelito, West Panama City, East Panama City, and the corregimientos of Ancón, Chilibre, Las Cumbres, Pacora, San Martín, and Tocumen. A total of 1.6 million people reside in this area, accounting for 47% of the country's population (ENV, 2010).

³⁷ Government of Panama. Op. cit. 13.

³⁸ IDAAN Statistical Bulletin 26: 2009-2012.

³⁹ Twenty-four hours a day, seven days a week.

⁴⁰ Water supply systems serving communities of more than 1,500 inhabitants.

⁴¹ The country is beginning implementation of the following initiatives: "Colón Urban Renovation Plan," "Basic Health Plan 100/0," and the start of construction of Panama's Metro Line 2 and preparations for Line 3.

3.12 Along these lines and within the framework of this country strategy, the Bank seeks to help strengthen the country's **social protection** system,⁴² enhancing the transparency, efficiency, and coverage of the conditional cash transfer programs targeting the population segments living in poverty and extreme poverty. The strategy will aim to integrate the supply of health care and education services with the incentives promoted by the Red de Oportunidades [Network of Opportunities] program. In **childhood health and nutrition**, the Bank will continue to expand the supply of services, reinforcing the service portfolio based on the epidemiologic profile of the population, with an emphasis on rural areas and indigenous *comarcas*, by means of new operations and technical cooperation projects. In the area of **early childhood care**, the Bank will seek to expand the supply of services through child care centers, improve the quality of care, and develop a community model of comprehensive early childhood care for rural areas and indigenous *comarcas*. At present, the Bank has an outstanding portfolio in health care of US\$27 million, aimed at improving the effectiveness and efficiency of the country's health and nutrition programs and overcoming the barriers of access to basic preventive and primary care services for poor populations, particularly indigenous populations. In addition, through both the outstanding portfolio⁴³ and new operations, the Bank will support expanded coverage and improved quality of **water and sanitation** services in urban centers, other provinces, and rural areas, while at the same time continuing to support the institutional reform process in the sector.

3.13 These actions are aligned with the challenge of *social exclusion and inequality* set forth in the Update to the Bank's Institutional Strategy for 2010-2020, and with its objectives of eradicating extreme poverty and providing inclusive infrastructure and infrastructure services.

B. Strengthen the educational profile of the population

3.14 Strengthening human capital by delivering quality education throughout the school cycle⁴⁴ is essential to help boost productivity, offer better employment opportunities for broader segments of the population, and support the country's capacity for innovation in various areas. In particular, the country's growth and inclusion objectives would be furthered by improving the quality of the education system as well as by training highly specialized professionals to strengthen innovation capacity in the most dynamic productive sectors and in the delivery of basic social services.

3.15 The country's **education sector** shows quality and equity gaps. Despite having a work force with an average of 9.4 years of schooling, which is similar to the Organisation for Economic Co-operation and Development (OECD) level, there is a lag in the quality indexes. As a result, Panama ranks below international

⁴² In addition to basic health care, social protection, and water and sanitation services, rural electrification is an important factor in improving the quality of life of poor populations. The Bank has an outstanding portfolio of US\$18 million designed to extend the coverage of rural electrification services.

⁴³ The Bank's outstanding portfolio in water and sanitation totals US\$138 million and includes investments in both urban and rural areas.

⁴⁴ The education system is divided into three levels: basic general, secondary, and higher education. The basic general level is mandatory and includes two years of preschool, six years of primary school, and three years of pre-secondary school.

- standards. In the PISA 2009 international test, Panama placed 62nd among the 65 participating countries.⁴⁵ In national tests, students in rural and indigenous areas exhibit a much lower performance level and complete fewer years of education.
- 3.16 There are many reasons for these education results, notably low teacher quality, limited learning conditions, and governance and accountability issues in the sector. With regard to teachers, while the country has made significant strides in terms of certification⁴⁶ and training through programs like “Panamá Bilingüe,”⁴⁷ the training process is concentrated on general and theoretical areas and there is a need to provide more training in specific competencies and attract good candidates to the teaching profession.
- 3.17 With regard to learning conditions, the lack of infrastructure, especially in rural areas and indigenous *comarcas*, and the deteriorated state of existing facilities are the main challenge, affecting both school performance and school access. In terms of coverage, the biggest gaps are apparent at the preschool and secondary school levels. In preschool, net coverage expanded from 36% to 64% between 2000 and 2012,⁴⁸ although it remains below the Latin American and Caribbean average of 84%.⁴⁹ Preschool coverage is low in provinces with a large urban population, such as Colón (80.7%) and Panama City (70.2%), where it lies below the national average of 82.4%.⁵⁰ At the pre-secondary and secondary levels, coverage increased from 59% to 76% over the same period, showing gains but still below the Latin American and Caribbean average of 85% in 2014.⁵¹
- 3.18 Improving school attendance levels, particularly in secondary school, is another challenge for the country. Of the total number of students who reach this level of education, only 25% complete it. School dropout is more acute in the indigenous *comarcas*, rural areas, and the province of Panama.⁵² The high dropout rates are the result of poverty, grade repetition, and over-age enrolment, in addition to a lack of schools and the perception that education will not improve job prospects. In addition, the education system has management problems. There are constraints on data collection (which is needed in order to monitor and evaluate progress in the sector) and on efficiency in administrative services, as well as planning problems.

⁴⁵ PISA is the Programme for International Student Assessment of the OECD. The tests targeted to 15-year-olds focus on mathematics, reading, and science. Within these tests, in the subjects of reading and mathematics, respectively 65% and 80% of Panamanian students failed to achieve level 2 (of a total of 6 levels), which is considered the minimum set of skills required to lead a productive adult life.

⁴⁶ In primary schools, the proportion of certified teachers rose from 75% in 2000 to 91% in 2010. In secondary schools there was also a rise, from 81% in 2000 to 88% in 2010.

⁴⁷ The teacher training program “Panamá Bilingüe” seeks to train education graduates from local universities and the Instituto Pedagógico Bilingüe to master a second language (English).

⁴⁸ Ministry of Education (MEDUCA), 2014.

⁴⁹ Székely, M. “Análisis del círculo de la desigualdad de oportunidades” [Analysis of the inequality of opportunity circle], IDB, 2015.

⁵⁰ MEDUCA. Education statistics 2010, 2011.

⁵¹ MEDUCA. Strategic Plan 2009-2014, National Office of Education Planning, 2014.

⁵² School dropout rates: Comarca Ngäbe-Buglé, 39.6% (19.1% boys and 20.5% girls); Comarca Guna Yala, 40% (15.8% boys and 24.2% girls); Darién, 40.5% (23.6% boys and 16.9% girls), and Panama 27.6% (15.4% boys and 12.2% girls). MEDUCA. Op. cit. 50.

- 3.19 Efforts to address the weaknesses in the education system so as to promote productivity and social inclusion should be accompanied by specialized training of professionals and development of an **innovation,⁵³ science, and technology** system that can lead to innovative delivery of basic social services and to enhanced competitiveness in the major economic sectors. With regard to social services, the percentage of national researchers in this field is low, and the public institutions responsible for these services lack the specialized human capital required to provide innovative solutions that can improve service quality. Despite the capacity for innovation in certain sectors of the economy, particularly logistics and energy, and their contribution to the Panamanian economy, these sectors face competitiveness constraints associated with the limited availability of the specialized human capital needed to drive an innovation agenda and the lack of modernization of their institutional structures and resources planning processes.
- 3.20 In order to address these challenges, the PEG 2015-2019 seeks to: (i) maintain and deepen achievements in school coverage, particularly for groups with difficult access based on geography, ethnic identity, and/or low socioeconomic status; (ii) improve the quality of learning through new technologies, teacher training, and the implementation of an evaluation and supervision system; (iii) organize the education system so the various school cycles complement one another; and (iv) foster a culture of innovation, science, and technology so as to manage the production of knowledge and use it to further the country's economic and social development objectives.
- 3.21 The Bank will support the Panamanian government's objectives in the **education sector** through interventions that improve the quality and expand the coverage of education in urban and rural areas alike. In particular, the Bank's interventions will help to expand school coverage at the preschool level, provide more physical infrastructure in rural and indigenous areas, and strengthen student skills in pre-secondary schools. In the indigenous *comarcas*, the interventions will consider the cultural relevance of both the curriculum and the teaching practices. In addition, the Bank will foster improvements in the information systems so as to plan and monitor sector outcomes. At present, there is an outstanding portfolio of U\$66 million, aimed at expanding school infrastructure by building and rehabilitating basic-cycle schools from preschool to pre-secondary school, updating the curriculum, and providing teacher training, particularly in areas of extreme poverty and indigenous *comarcas*. The private sector's outstanding portfolio includes actions aimed at integrating youth and women into the work force through education and entrepreneurship promotion. The Bank will continue its technical dialogue with the country with regard to the links between education and the labor market. The private sector windows will seek to support social services through public-private partnerships and by financing private entities, particularly higher education institutions. In terms of **innovation**, Bank actions will focus on identifying innovative solutions regarding the three objectives proposed under this country strategy, by strengthening the human and institutional capacities of the relevant agencies in the areas of health, education, and water and sanitation, as

⁵³ Innovation can be the implementation of a new, more efficient way of doing something, a new or substantially improved product or process, a new marketing practice, or a new organizational method applicable to business practices, external relations, or workplace organization.

well as in logistics and productive infrastructure services. The available portfolio of US\$4 million will be used to continue to promote the development of instruments to support business innovation.

- 3.22 These priorities are aligned with the challenges of *social exclusion and inequality* and *low productivity and innovation* set forth in the Update to the Bank's Institutional Strategy for 2010-2020, as well as with its objectives of eradicating extreme poverty, providing inclusive infrastructure and infrastructure services, developing quality human capital, and providing adequate knowledge and innovation ecosystems.

C. Enhance the logistics services, efficiency, and connectivity of the productive infrastructure

- 3.23 In order to keep up its current pace of growth, Panama needs to address the institutional and infrastructure gaps that affect the productivity of the Canal's logistics conglomerate and its ability to coordinate and catalyze the growth of the country's productive sectors and regions in the other provinces.

- 3.24 The geographic location advantages of the Panama Canal have facilitated the expansion of transport and logistics services in recent years. Such services accounted for 24% of GDP in 2014, compared to 18% in 2005.⁵⁴ The medium-term growth prospects offered by the Canal's expansion have led the Government of Panama to develop a National Freight Logistics Plan (PNLog) aimed at transforming the Canal from a cargo transshipment center⁵⁵ to a nexus of value-added logistics services. The PNLog seeks to address the logistics demand associated with the national productive sectors, domestic consumption, and foreign trade and improve local production access to the international markets, integrating the country into regional and global production chains.⁵⁶ The country is strengthening the logistics sector's capacities and infrastructure through the expansion of the Panama Canal, the development of export processing zones, and the expansion of ports and airports,⁵⁷ which need to be supplemented by reinforcing road transportation and energy infrastructure and by making institutional adjustments to ensure a favorable framework for comprehensive and territorial development of the logistics system and coordination among the country's various public and private agencies.

- 3.25 The country's infrastructure stock is primarily located in the vicinity of the Canal, in contrast with the scarcity of infrastructure in the other provinces.⁵⁸ Most (80%) of the **rural road network**, used to transport the local production to the urban centers and providing the rural population access to social services, is in poor or fair

⁵⁴ The transport and logistics sector includes the contributions of the Panama Canal and the ancillary logistics support for transshipment, distribution, and associated commercial activities, which are in large part performed in the Colón free trade zone (ZLC).

⁵⁵ Of the containers that use the Panamanian port system, 93% use the ports only for transshipment purposes.

⁵⁶ The PNLog is divided into three subsystems: (i) hub of value-added logistics services in the Canal conglomerate; (ii) support logistics for the agriculture sector; and (iii) support logistics for regional trade.

⁵⁷ Including the expansion of Tocumen International Airport and the construction of the port of Corozal.

⁵⁸ The country's infrastructure includes a complex of ports, airports, road and railroad networks, and logistics infrastructure consisting of nodes of ancillary services to support port activities and the ZLC.

- condition.⁵⁹ Panama lacks systems for road planning and maintenance and for prioritizing roads for intervention based on production and population criteria. This shortcoming reduces the effectiveness of public expenditure in the sector. In addition, despite the Canal's potential trade advantages, there are inefficiencies at **border crossings**. Specifically, the Paso Canoas border crossing, which is used for transporting 99% of the free trade zone merchandise destined for Central America, lacks proper customs facilities. As a result, the average customs clearance time for freight is 15 hours, compared to a regional average of 3.5 hours.⁶⁰
- 3.26 To add to these challenges, the reliability and security of the country's **energy supply** are not ensured over the medium term,⁶¹ primarily due to power generation and transmission limitations. With regard to generation, the limitations relate to the capacity for hydro and thermal generation, which in 2014 respectively accounted for 58% and 40% of Panama's total electricity generation,⁶² and to delays in the commissioning of energy projects and/or power purchase agreements. In addition, the country has failed to use the Central American Electric Interconnection System (SIEPAC) to capitalize on the potential supply of energy available through the Central American Regional Electricity Market, which would make it possible to reduce generation costs as well as CO₂ emissions. This would be consistent with the vision of the country's generation expansion plan, which calls for diversifying the energy matrix into clean sources, such as wind and solar, and natural gas.⁶³ With regard to transmission, the capacity of the network is limited⁶⁴ due to expansion planning flaws and financial constraints, as well as to efficiency and corporate governance problems at the lead company.
- 3.27 In addition to addressing the infrastructure challenges, Panama needs to implement **regulatory and institutional reforms** to complement investment in order to make orderly and sustainable progress on its PNLog. The institutional challenges include: (i) a lack of long-term vision and national government policy in the area of logistics; (ii) poor systematic coordination between public and private entities; (iii) the absence of comprehensive planning that considers infrastructure, associated services, and the country's territorial integration; (iv) inefficiencies in the foreign trade processes and lack of coordination among agencies; and (v) limited technical human resources.
- 3.28 In the framework of this country strategy, the Bank's actions will support implementation of the 2015-2019 PEG and the PNLog, aimed at improving the

⁵⁹ IDB. "Sector note: Transportation and logistics," 2015.

⁶⁰ United States Agency for International Development, 2014.

⁶¹ For the long term, the country has developed an Expansion Plan 2014-2028 (ETESA 2014), which assumes a 2,320-MW increase in generation, resulting in an installed capacity of 5,153 MW in 2027 to address a maximum estimated demand of 3,250 MW in 2027.

⁶² Adverse climate conditions have limited the country's hydropower generation capacity due to the low storage capacity of the two reservoirs (Bayano and Fortuna), which is 740 GWh, equivalent to less than 20% of semiannual demand. With regard to thermal energy, average energy availability is low (60% of installed thermal capacity) and vulnerable to changes in international oil prices.

⁶³ In November 2015, the government inaugurated the "Penonomé Wind Park" project, which will cover an estimated 6% to 8% of the country's annual energy needs.

⁶⁴ Transmission capacity from Occidente to the Panama City metropolitan area is 600MW, through two existing lines, and installed capacity in Occidente is approximately 1,200 MW (IDB, 2015).

country's **logistics performance** and the connectivity of the most dynamic production centers with the rest of the territory by implementing institutional and regulatory reforms designed to bring about an integrated national policy for the sector as well as by improving, rehabilitating, and maintaining the **rural roads** and highways that link the productive sectors with the domestic and export markets, including strengthening the border crossings. The Bank has an outstanding portfolio in transportation of US\$52 million focused on improving the primary road network and implementing a standard-based routine maintenance system and on rehabilitating the country's rural roads. In line with the priorities set forth in the PNLog, the private sector windows will search for opportunities through mechanisms for public-private or exclusively private participation, including investments in highways, ports, and airports, urban transportation, and value-added logistics services.⁶⁵

- 3.29 In the **energy** sector, the Bank will seek to enhance the reliability of the electricity supply, fostering diversification of the energy matrix, participation in the Central American Regional Electricity Market, and the strengthening of transmission infrastructure. The Bank will explore initiatives to support electric power generation through the private sector, thereby helping to diversify the matrix. In addition, the Bank will continue to support the country's electric power integration with Central America and Colombia. Through its US\$18-million portfolio in execution, the Bank will support an expansion of electrification in rural areas and indigenous *comarcas*, thereby contributing to the strategic objective of improving the delivery of basic services to the population living in poverty.
- 3.30 The Bank's support is aligned with the challenges of *social exclusion and inequality, regional integration, and productivity and innovation* set forth in the Update to the Bank's Institutional Strategy for 2010-2020, as well as with its objectives of providing inclusive infrastructure and infrastructure services, establishing smart institutional frameworks, improving regional infrastructure, inserting firms into value chains, and enabling the alignment of integration policies and instruments.

D. Crosscutting areas of action

- 3.31 The strategy will incorporate crosscutting issues of (i) gender and diversity; (ii) integration; (iii) climate change and environmental sustainability; and (iv) institutional capacity of the local counterparts. Specifically, issues of cultural relevance will be incorporated into the objectives of improving the delivery of basic services to the population living in poverty and of strengthening the education profile of the population. Issues of climate change and environmental sustainability⁶⁶ and integration will be taken into account as part of the objective of deepening the logistics services, efficiency, and connectivity of the productive infrastructure. With regard to weaknesses in the execution capacity of the local counterparts, the Bank will continue to design institutional components that strengthen the execution units and contribute to the sustainability of Bank

⁶⁵ In line with the opening of the Canal expansion, the new port planned for Corozal, and other investments currently under way, such as development of the Panama-Pacific area and modernization of the ZLC.

⁶⁶ Bank instruments will be used along with lessons learned by the Bank on reducing vulnerability in both transportation and hydro energy infrastructure works.

programs, and will provide technical assistance in areas such as the management of government human resources. The mechanisms for implementing these crosscutting issues will be determined, as applicable, during the design of the respective programs.

E. Dialogue areas

- 3.32 The Bank will intensify its dialogue with the country in the areas of labor markets, macrofinancial and fiscal stability, and decentralization. In the first of these areas, special attention will be paid to training and job placement in order to improve and expand their coverage and their impact on the country's productivity and competitiveness. In the second area, the Bank will follow up on progress achieved during the 2010-2014 strategy period in terms of macrofinancial and fiscal regulation and will continue to provide technical assistance on financial transparency. In the third area, the Bank will support the country's initiatives to move forward in implementing the Decentralization Law, approved in October 2015, including actions with the municipal governments and the central government entities responsible for leading the process.

IV. LENDING FRAMEWORK

- 4.1 Panama has investment grade status, and the Government of Panama is expected to continue to have access to the financial markets on favorable terms during the period covered by this strategy.⁶⁷ In addition, the country will continue to develop the domestic public debt market, which allows the government to obtain funding through local issues. Furthermore, the authorities continuously manage refinancing risk and have experience in initiating voluntary debt swaps. Lastly, the country maintains contingent lines of credit for natural disasters provided by the Bank and other entities.
- 4.2 Since the country strategy for 2015-2019 will be implemented in a context of broad State access to financing, the proposed focus of the strategy, coupled with the country's expected financing needs, suggests that the approval and disbursement levels should be close to those of recent years. On a preliminary basis, and subject to the availability of resources from the Bank's Ordinary Capital, annual approvals are projected at approximately US\$390 million, with annual disbursements on the order of US\$352.8 million. Support for the 2015-2019 period is estimated at approximately US\$1.950 billion in SG approvals, while expected disbursement levels are estimated at US\$1.764 billion.

V. STRATEGY IMPLEMENTATION

- 5.1 **Intersector coordination.** With a view to achieving the expected outcomes from social infrastructure investments aimed at improving the delivery of basic services in rural areas, indigenous *comarcas*, and periurban areas, the Bank will promote coordinated actions in the areas of education, health, water and sanitation, electricity, and transport as part of the design and execution of programs. Thus, the Bank will seek solutions to the country's challenges from a multisector perspective adapted to the local contexts.

⁶⁷ As a result of having investment grade status since 2010, Panama has benefitted from low funding rates.

5.2 **Use of country systems.** The Bank uses the country information system, “PanamáCompra,” to manage and supervise its operations. In addition, the shopping (for procurement) and budget subsystems are used on a partial basis.⁶⁸ During this strategy period, the Bank will continue to work with the Government of Panama on implementing and consolidating the integrated financial information system ISTMO and the general treasury account (GTA), increasing the use of country systems in the long term. In addition, the Bank will support the Office of the Comptroller General of the Republic (CGR) in improving its ex ante and ex post control processes and adopting international auditing and accounting standards, with a view to enhancing the transparency and operational efficiency of the country’s financial management and, therefore, of Bank operations. Furthermore, the Bank will support the Procurement Bureau in updating the MAPS diagnostic assessment⁶⁹ and will provide technical assistance on specific system improvement aspects, such as electronic platform, framework agreements, regulatory modernization, and training, boosting the efficiency and transparency of public procurement.

5.3 The following table summarizes the status of country systems in Panama and their expected use during this strategy period:

Table 2. Country system

Use of country systems	Baseline 2015 ⁷⁰	Expected use in 2019	Expected actions during the strategy period
Budget ⁷¹	64%	25%	
Treasury	9%	10%	Implementation of the GTA
Accounting and reporting	9%	10%	Implementation of IPSAS* Project module in ISTMO
Internal audit	5%	0%	Strengthening of internal control systems
External control	5%	0%	Comprehensive modernization of the CGR
Information system	100%	100%	Continuous dissemination
Shopping	5%	50%	Implementation in Bank operations
Individual consulting	5%	0%	MAPS; analysis of NCB and individual consulting; support in implementing reverse auctions; strengthening of framework agreements.
Partial NCB	5%	20%	
Advanced NCB	5%	10%	

*International Public Sector Accounting Standards.

⁶⁸ In January 2015, the Government of Panama began to implement a new integrated financial information system known as Integración y Soluciones Tecnológicas del Modelo de Gestión Operativa [Operating Management Model Integration and Technology Solutions] (ISTMO), thus discontinuing use of the SIAFPA-PRO project module, which allowed partial use of the treasury, accounting, and reporting subsystems. As a result, use of these subsystems has been suspended until the new system becomes fully operational. A new evaluation will have to be conducted in 2016 or 2017 to determine the feasibility of using the ISTMO and the need to adjust or develop the project module.

⁶⁹ Methodology for Assessment of Procurement Systems (MAPS).

⁷⁰ As of 31 December 2014. In addition, reported use of the internal audit, external control, shopping, individual consulting, partial NCB, and advanced NCB systems refers to their use in policy-based loans, which by nature involve the use of country systems.

⁷¹ Use of the budget system will decrease due to an expected increase in the use of funds managers or fiduciary agents so as to have more streamlined project execution procedures in place. Moreover, ISTMO implementation will require a new assessment over the next two years to determine the feasibility of using the system and the need to adjust or develop the project module.

- 5.4 **Donor coordination.** The Bank will continue its dialogue and operational coordination with: (i) the Development Bank of Latin America (CAF), the World Bank, and the Spanish Agency for International Development Cooperation (AECID) on water and sanitation; (ii) the European Union on citizen security; and (iii) the World Bank and the CAF on health, education, and social protection. In line with the work done under the previous strategy, the Bank will continue to identify and leverage donor resources, creating links with donor institutions.⁷²

VI. RISKS

- 6.1 **Macroeconomic risks.** The Panamanian economy faces risks associated with global economic developments, particularly trade and capital flows and hydrocarbon prices. Specifically, weaker economic conditions in China or the United States could reduce trade flows and affect Canal activity and revenue, impacting one of the country's main sources of economic growth and public revenues. At the same time, a rise in international fuel and food prices could lead to higher inflation and a decline in the terms of trade. In addition, on the fiscal side, the contingent liabilities associated with mechanisms used in the past to finance public investment pose a risk to the fulfillment of the goals outlined in the "Social Fiscal Responsibility Law." In this regard, the current government administration has implemented actions aimed at reducing these contingent liabilities and limiting their use. Lastly, while Panama is carrying out a series of reforms and actions designed to enhance financial transparency and remove the country from the Financial Action Task Force gray list, this process could take longer than expected and thus affect the competitiveness of the international banking center and related activities. To mitigate these risks, the Bank will continue to offer technical assistance to support Panamanian government initiatives in this area.
- 6.2 **Portfolio execution risks.** This risk is fed by two critical factors. Firstly, the institutional capacity of some execution units, particularly those that implement infrastructure works in rural communities and indigenous *comarcas*, is limited and affects portfolio execution levels. Secondly, the ex ante control processes implemented by the country through the CGR are complex and create delays in the startup and implementation of investments. To mitigate this risk, the Bank will continue to strengthen the institutional capacities of the local counterparts and will provide technical assistance in supervising infrastructure works located in rural and remote areas. In addition, the Bank will develop initiatives aimed at streamlining the CGR's ex ante control processes, moving from a paper-based to a digital process in the current regulatory context and adopting the International Standards of Supreme Audit Institutions (ISSAI). Lastly, during this strategy period, the Bank will use its fiduciary monitoring and control instruments to monitor progress on the institutional strengthening of the local counterparts in these areas.

⁷² See Annex V.

- 6.3 **Natural disaster risks.** The country is vulnerable to natural disasters and the effects of climate change, particularly floods caused by torrential rains and droughts. This fact could pose a risk to macroeconomic stability and productive infrastructure development, which are areas of action under this strategy. To mitigate these risks, the Bank will continue to implement the annual monitoring measures provided in the Contingent Credit Facility for Natural Disaster Emergencies in effect for the country until 2017, and will address this issue with the authorities as part of the annual programming exercises.

ANNEX I. RESULTS MATRIX

Government priority	Strategic objective	Expected outcomes	Indicators	Baseline
Enhance competitiveness and promote social inclusion in the context of a sustainable and inclusive development model	Improve the delivery of basic services to the population living in poverty	Improvement in the efficiency of social programs	Percentage of Red de Oportunidades [Network of Opportunities] beneficiaries ⁷³ who are not living in extreme poverty (leakage) ⁷⁴	42 (2015), INEC, annual
		Reduction in maternal mortality, infant mortality, and prevalence of chronic malnutrition among children under five	Maternal mortality rate in indigenous <i>comarcas</i> (for every 100,000 live births)	274.3 ⁷⁵ (2012), CGR, annual
			Infant mortality rate in indigenous <i>comarcas</i> (for every 1,000 live births)	31.5 (2012), CGR, annual
			Prevalence of chronic malnutrition among children under five in indigenous <i>comarcas</i> (stunting)	55.9 ⁷⁶ (2012) Mesoamerica Health Initiative every five years
		Increase in water supply coverage in urban areas ⁷⁷	Water supply coverage in urban areas (%)	93 (2013) PEG 2015-2019 annual
		Increase in sewer system coverage in urban areas ⁷⁸	Sewer system coverage in urban areas (%)	56 (2013), IDAAN annual

⁷³ All members of households in which one or more people receive a cash transfer are considered beneficiaries.

⁷⁴ Leakage is defined as the percentage of conditional cash transfer program beneficiaries (counting all household members) who are not living in extreme poverty (for *Red de Oportunidades* [Opportunities Network] and *Ángel Guardián* [Guardian Angel]) or in overall poverty (for *120 a los 65* [120 at 65]). There are no applicable restrictions (demographic or related to the receipt of old-age pensions) for purposes of calculating leakage. The current non-poor beneficiaries are expected to be replaced by new beneficiaries living in moderate or extreme poverty.

⁷⁵ *Comarca* of Ngäbe-Buglé.

⁷⁶ *Comarcas* of Emberá Wounaan and Guna Yala.

⁷⁷ The Bank's operations in the sector will seek to target their activities to populations living in poverty and extreme poverty.

⁷⁸ *Idem*.

Government priority	Strategic objective	Expected outcomes	Indicators	Baseline
Enhance competitiveness and promote social inclusion in the context of a sustainable and inclusive development model	Strengthen the education profile of the population	Improved access to preschool programs	Net preschool enrolment rate (% of children four and five years of age)	65.8 (2013), MEDUCA, annual
		Reduced dropout rate in pre-secondary and secondary school	% of pre-secondary and secondary school dropout	11.3 (2014), MEDUCA, annual
		Improved student learning at the basic education level	Average score on reading and mathematics tests in third grade (TERCE)	Reading: 490 Mathematics: 494 (2013) UNESCO, n.a.
			Average score on reading and mathematics tests in sixth grade (TERCE)	Reading: 483 Mathematics: 461 (2013) UNESCO, n.a.
		Increase in the number of researchers ⁷⁹ working (full- or part-time) on R&D activities	R&D researchers per one million inhabitants	142 (2014) PENCYT 2015-2019, annual
	Deepen the logistics services, efficiency, and connectivity of the productive infrastructure	Increased competitiveness of the national logistics system	Logistics Performance Index in Panama (ranking, #) ⁸⁰	45 (2014), World Bank, every 2 years
		Increase in transport and storage activities in the national economy	Share of transport and storage activities in the national economy (% of GDP)	19.6 (2012), CGR every 5 years
		Improvement, rehabilitation, and maintenance of the rural road network	% of km in the rural road network in optimum operating condition (good condition) ⁸¹ (coverage ratio)	1 (2014), MOP, every 5 years

⁷⁹ Researchers are professionals engaged in the conception or creation of new knowledge, products, processes, methods, and systems as well as in the management of the projects concerned. OECD "Frascati Manual. Proposed Standard Practice for Surveys on Research and Experimental Development," 2002.

⁸⁰ The general Logistics Performance Index (LPI) score reflects the perceptions of a country's logistics based on the efficiency of the customs clearance process, the quality of trade and transport infrastructure, the ease of arranging for shipments at competitive prices, the quality of logistics services, the capacity to monitor and track shipments, and the frequency with which shipments reach their consignee on schedule. The index ranges from 1 to 5, where a higher score represents better performance. The LPI is a perception indicator based on surveys of logistics professionals. World Bank, 2015.

⁸¹ International Roughness Index (IRI) values between 3.5 and 10 m/km are considered optimal (very good or good). The IRI measures longitudinal road irregularities adversely affecting the quality of ride, safety, and vehicle operating costs.

Government priority	Strategic objective	Expected outcomes	Indicators	Baseline
		Increase in customs declarations processed per year in Paso Canoas ⁸²	Customs declarations processed per year in Paso Canoas (number of successfully processed declarations)	29,909 (2014), National Customs Authority annual
		Strengthened transmission infrastructure	Kilometers of transmission lines	1,921 (2014), ETESA, annual

⁸² The Paso Canoas border crossing is the main foreign trade nexus between Panama and Central America. In all, 85% of the region's vehicle flows and 99% of the freight from the Colón free trade zone destined for Central America pass through this crossing. PNLog, 2014.

COUNTRY SYSTEMS MATRIX

Strategic IDB objectives	Expected outcomes (2019)	Indicators*	Baseline (Dec. 2014)	Indicative targets	Frequency
Strengthen and increase the use of country fiduciary systems	Reduction in procurement processing time.	Average time between publication and contract signing.	208 days	190 days by the end of the country strategy period	By the end of the country strategy period
	Increase in the use of procurement modalities and functionalities of the country public procurement system.	Percentage of projects that use shopping in IDB operations	5%	50% of projects use shopping in IDB operations by the end of the country strategy period	Annual
		Percentage of projects that use partial NCB in IDB operations	5%	20% of projects use partial NCB in IDB operations by the end of the country strategy period	
		Percentage of projects that use advanced NCB in IDB operations	5%	10% of projects use advanced NCB in IDB operations by the end of the country strategy period	
	International Public Sector Accounting Standards (IPSAS) partially implemented.	% progress in implementing IPSAS.	5%	50% by the end of the country strategy period	By the end of the country strategy period
	International Standards of Supreme Audit Institutions (ISSAI) partially used	% progress in implementing ISSAI	5%	50% by the end of the country strategy period	By the end of the country strategy period

* Indicators of measurable outcomes for the years covered by the strategy.

ANNEX II. MAIN ECONOMIC AND SOCIAL INDICATORS

	2007	2008	2009	2010	2011	2012	2013	2014
Social indicators								
Population (millions)/1	3.4	3.5	3.6	3.6	3.7	3.7	3.8	3.9
Poverty rate*	27.7	26.4	25.7	29.8	27.6	26.5	26.2	25.8
Extreme poverty rate*	13.5	11.2	12.6	12.2	11.5	11.1	11.1	11.0
Unemployment rate (% workforce)/2	6.37	5.58	6.56	6.52	4.48	4.05	4.10	4.10
Per capita GDP (US\$, ppp)	11,388.5	12,561.8	12,918.8	13,813.9	15,368.5	17,022.7	18,417.5	19,455.4
Real sector indicators								
Nominal GDP (%Δ)		17.8	4.2	11.1	15.5	14.1	12.4	8.4
Real GDP (1996 prices) (%Δ)	12.1	9.1	4.0	5.9	10.8	10.2	8.4	6.2
General inflation (% , period-end)	6.4	6.8	1.9	4.9	6.3	4.6	3.7	1.0
Nominal GDP (US\$ millions)**	19,511.4	24,450.0	25,260.0	26,931.6	34,048.4	36,560.4	36,642.9	47,002.5
Fiscal indicators/3								
Total revenue (% of GDP)	28.2	24.6	24.8	25.5	22.8	24.7	27.2	21.4
Total expenditure (% of GDP)	24.7	24.2	25.8	27.4	24.9	26.2	30.0	25.5
Overall balance (% of GDP)	3.5	0.4	-1.0	-1.9	-2.1	-1.5	-2.8	-4.1
Total public debt (% of GDP)	53.7	42.7	43.4	43.2	37.6	39.0	42.8	38.8
Savings and investment/4								
Total investment (% of GDP)	24.1	27.6	25.6	25.5	27.2	28.6	30.0	29.8
National savings (% of GDP)	16.1	16.7	24.9	14.2	11.3	18.8	17.8	17.8
External sector indicators								
<i>External debt balance</i>								
Total external debt (excluding banking sector)				13,812	15,514	16,397	18,635	19,590
External public debt (US\$ millions)/5				10,669	1,122	11,109	12,703	12,705
<i>Selected indicators (%)</i>								
External debt/Goods and services exports				73.1	62.1	58.2	69.0	74.7
Total external debt/GDP				51.1	49.5	43.2	43.7	42.4
Reserve assets/Total external debt				35.4	23.6	16.0	16.2	21.7
<i>External debt service</i>								
External debt service				1,046.7	930.9	1,690.9	1,667.0	1,806.3
Total amortization				320.1	186.0	956.1	921.0	1,057.3
Interest payments				726.6	744.9	734.8	746.0	749.0
<i>Selected indicators (%)</i>								
Debt service /Goods and services exports				5.5	3.7	6.0	6.2	6.9
Interest/ Goods and services exports				3.8	3.0	2.6	2.8	2.9
Interest/GDP				2.7	2.4	1.9	1.7	1.6
Current account balance (% of GDP)	-8.0	-10.9	-0.7	-11.4	-15.9	-9.8	-12.2	-12.0
Foreign direct investment (% of GDP)/4	9.6	9.9	4.2	8.8	13.2	8.8	11.8	10.0
Real effective exchange rate (Δ%) (EIU)		-2.4	2.9	6.1	0.5	-0.8	5.4	1.1
External public debt (% of GDP)		39.2	34.1	39.2	36.2	32.8	28.4	28.7
Credit								
Credit for the private sector (Δ%)		17.9	19.5	1.3	13.3	15.3	13.8	10.4
Average deposit rate (1 year)a		4.8	3.5	3.5	3.0	2.3	2.8	2.8
Average lending rate (1 year)b		8.3	8.2	8.3	7.5	7.2	7.3	7.6

1/ IMF (WEO April 2015).

2/ IMF (WEO April 2015), 2014 is an estimate.

3/ MEF, nonfinancial public sector figures.

4/ IMF (WEO April 2015) /Includes the broadest version of the public sector.

* Based on the ongoing household survey of March 2014 and published by the Ministry of Economy and Finance (MEF) in February 2015

** Implicit – used by the MEF

ANNEX III. MACROECONOMIC CONTEXT

Panama has had a favorable macroeconomic performance. The main economic indicators describe a growing economy, highly integrated into global trade, that in 2014 achieved per capita income of US\$19,455 (ppp)⁸³ and is consequently ranked among the 10 highest-income countries in Latin America and the Caribbean. Following the slowdown associated with the 2009 global financial crisis which reduced GDP growth to 4.0%, the Panamanian economy recovered, posting an average growth rate of 8.3% over the 2010-2014 period.

The vitality of the Panamanian economy was fueled by services and construction. Since 2008, services have accounted for approximately 60% of GDP growth, particularly international banking center, transport, and trade services.⁸⁴ Construction was responsible for an additional 23.4% of GDP growth, owing to the Panama Canal expansion process. Lastly, the primary sectors contributed 9% of the nation's economic activity.⁸⁵

On the expenditure side, the economic expansion has been accompanied by increased investment. Aggregate investment increased from 23% of GDP in 2007 to close to 30% of GDP in 2014. Worth noting is the rise in public investment during the government's five-year investment plan.⁸⁶ While public investment averaged 3.7% of GDP before 2010,⁸⁷ it subsequently climbed to an average of 8.2% of GDP. A large portion of the demand for investment was not met by the domestic investment supply, resulting in high levels of foreign direct investment, which has averaged 10.5% of GDP between 2010 and 2014.

The multiple investment projects were carried out in a framework of fiscal stability. Between 2010 and 2014, the nonfinancial public sector deficit averaged 2.5% of GDP, while the public debt fell from 43.2% to 38.8% of GDP. Although new fiscal framework modifications authorized a maximum deficit of 4.1% of GDP in 2014, fast economic growth and favorable financing terms have made it possible to manage this change in a context of stability and have played a leading role in reducing the debt burden.

In addition, the rebound in economic growth in recent years was accompanied by an average inflation rate of 3.8% between 2009 and 2014. Inflation peaked at 6.3% in 2011 and then gradually declined to an average of 3.1%. Furthermore, the real exchange rate rose relative to the U.S. dollar since the Panamanian inflation rate was consistently higher than its United States counterpart. This persistent appreciation could ultimately have an effect on the competitiveness of tradable goods. It should be noted, however, that this trend was reversed in mid-2014, with an inflation rate of 2.6% that closed the inflationary gap.

The production boom has led to a downward trend in unemployment. The unemployment rate as measured by INEC stood at 4.8% in 2014, compared to 6.6% in 2009, with a significant increase in the employed population. When compared solely in relation to the work force, the figures are 4.1% and 6.6%, respectively. In 2014, the employed population totaled 1.7 million people, which is equivalent to 95% of the economically active population (EAP) and represents a 16.5% increase with respect to 2010. The employed population is predominantly located in urban areas, which account for close to 70% of the employed population.

⁸³ Per capita GDP at current prices was US\$11,700 in 2014.

⁸⁴ Of this percentage, transportation and communications together accounted for 21.2% of GDP growth, while financial services and trade accounted for 18% each.

⁸⁵ Public sector activities account for the remaining 7.6%.

⁸⁶ This refers to nonfinancial public sector (NFPS) investment. The Government Strategic Plan 2010-2014 included a US\$13.595 billion five-year investment plan.

⁸⁷ In 2005-2009.

Despite the economic performance, there are pronounced socioeconomic gaps. The poverty rate declined from 38.3% of the total population in 2006 to 25.8% in 2014. In addition, in 2014 Panama was ranked 65th in the Human Development Index, the seventh-highest ranking in Latin America and the Caribbean. However, income inequality, as measured by the Gini coefficient, remained constant at 0.52 from 2009 to 2012, reflecting particularly acute economic inequality in the three poorest deciles.

In order to continue on the path of economic growth while reducing poverty and promoting more inclusive development, Panama needs to address a series of challenges.

These challenges include those that perpetuate the country's socioeconomic gaps. In particular, the poor population lives in very tenuous conditions in terms of education, health, and basic services, which makes it difficult to break the cycle of poverty. This situation is coupled with the low connectivity of rural and remote areas, which keeps this population isolated from the country's major production and consumer centers and limits its linkage to the production chains operating in the area of the Canal. In addition, there is a need to reinforce the progress achieved in recent years in terms of competitiveness, by improving transportation and energy services and enhancing the logistics systems, which are critical for addressing the new trade flows arising from the Canal's expansion and facilitating local producer access to the global production chains.

ANNEX IV. INDICATIVE LENDING FRAMEWORK

Financing scenario: The Bank will seek similar approval and disbursement levels to those of recent years. On a preliminary basis, and subject to the availability of resources from the Bank's Ordinary Capital, annual approvals are projected at approximately US\$390 million, with annual disbursements on the order of US\$352.8 million. Support for the 2015-2019 period is estimated at approximately US\$1.950 billion in SG approvals, while expected disbursement levels are estimated at US\$1.764 billion.

Financial scenario for sovereign debt 2015-2019
(millions of U.S. dollars)

	2015	2016	2017	2018	2019	Total 2015-2019	Average 2015-2019
Approvals ^{1/}	550.0	350.0	350.0	350.0	350.0	1,950.0	390.0
Disbursements	390.0	338.1	348.7	337.6	349.5	1,764.0	352.8
Repayments	120.4	160.0	187.5	180.6	168.2	816.7	163.3
Net loan flows	269.6	178.1	161.2	157.0	181.3	947.3	189.5
Subscriptions	1.7	-	-	-	-	-	-
Net capital flows	267.9	178.1	161.2	157.0	181.3	945.6	189.1
Interest and fees	57.4	66.3	60.5	54.4	48.7	287.3	57.5
Net cash flow	210.5	111.8	100.7	102.6	132.6	658.3	131.7
IDB debt	2,173.4	2,376.4	2,561.1	2,736.9	2,905.9		
IDB debt/GDP (%)	4.1	4.1	4.1	4.0	3.9		
IDB debt/Public external debt (%)	13.4	13.3	13.5	13.8	14.0		
IDB debt/Multilateral external debt (%)	54.6	54.3	55.1	56.3	56.8		

^{1/} Amounts subject to availability of Bank financial capital. For 2015, approvals are presented as of December.

ANNEX V. DONOR COORDINATION

Background. International development cooperation in Panama is governed by Law 97 of 21 December 1998. Pursuant to this law, the Ministry of Economy and Finance (MEF), acting through the International Technical Cooperation Office (DCTI), is responsible for managing, directing, coordinating, planning, monitoring, and evaluating the use of nonreimbursable technical-cooperation funds provided by multilateral, bilateral, and regional agencies and nongovernmental organizations by implementing technical development cooperation programs and projects.

Strategic guidelines. The definition of international cooperation guidelines is framed in the National Strategy for International Development Cooperation, prepared by the DCTI and aligned with the Government Strategic Plan (PEG) 2015-2019. The strategic challenges notably include poverty reduction, institutional strengthening, construction of a more inclusive country, access to potable water, health, and education, and better employment conditions and income levels, so as to contribute to social development and political stability.

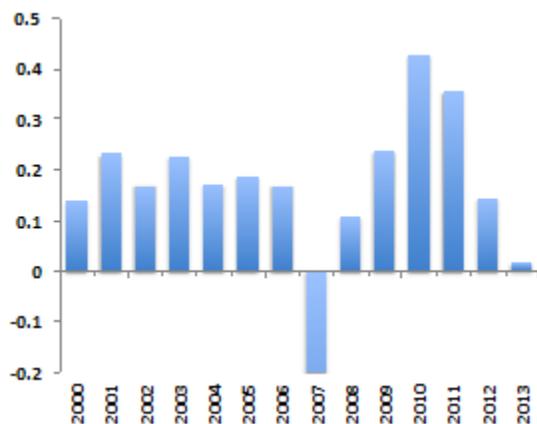
Institutional strengthening. The current international cooperation coordination and management model in Panama could be modified following the National Assembly's enactment of the Ministry of Foreign Relations Act on 12 March 2015. Pursuant to this law, the aforementioned ministry is responsible for fostering international cooperation flows from and to Panama, as well as for coordinating the planning, development, and execution of the respective policies with the relevant public institutions. In this regard, the law also provides for creating an Office of the Deputy Minister of Multilateral Affairs and Cooperation, which will be responsible for coordinating multilateral international relations and foreign policy in the multilateral context. In addition, this office will work with sector ministries and public entities to coordinate, integrate, and increase international cooperation flows to and from the Republic of Panama.

Official development assistance (ODA) flows. Since Panama is a high middle-income country, nonreimbursable technical-cooperation resources are relatively small both in relation to public expenditures and in absolute terms. ODA has responded to the country's list of needs. In particular, between 2009 and 2012, net ODA flows doubled with respect to their levels in the years preceding the financial crisis. Since 2009, Panama has received ODA⁸⁸ averaging close to 0.25% of GDP.⁸⁹ However, this figure is far from the 2.2% of GDP received by the Central American region as a whole. Indeed, Panama is one of the four countries that receive the least ODA in Latin America.

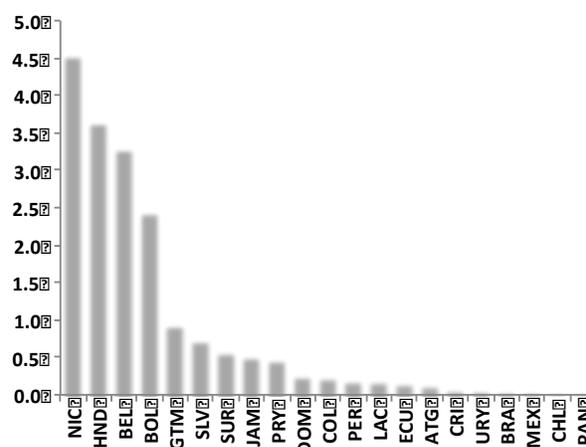
⁸⁸ Net of repayments and refunds. Includes funds from the Development Assistance Committee (DAC) as well as non-DAC funds.

⁸⁹ Base GDP includes net income from abroad as reported in the current account.

**Panama: Net official development assistance
2000-2013 (as % of GDP)***



**Panama: Net official development assistance in 2013
(as % of GDP)***



* Base GDP includes net income from abroad as reported in the current account.

Source: World Development Indicators

Cooperation management

- The DCTI is currently developing a Catalogue of National Capacities, the purpose of which is to foster south-south cooperation and attract new international cooperation for development actors into Panama. This catalogue will serve as an instrument to expand the intraregional cooperation network through collaboration on issues such as training, good practices, or demonstration of successful experiences in the country. The ultimate purpose of this catalogue is to bring about the creation of a Panamanian Foreign Cooperation Agency.
- The MEF is beginning to use the information system for nonreimbursable technical cooperation operations, known as Panamá-Coopera. This project was started in 2014 through the national government-UNDP cost-sharing fund. It is scheduled to continue in 2015 until an integrated information platform has been implemented. The main outcome expected to result from such implementation is a review and update of the DCTI monitoring and accountability system.

Current cooperation balances. As of 31 March 2015, the DCTI reports a total nonreimbursable technical-cooperation contribution of US\$297 million.⁹⁰ The United Nations Development Programme (UNDP) accounts for 56% of the total contribution. The UNDP projects are related to the agency's priority areas of work: (i) poverty reduction and attainment of the Millennium Development Goals; (ii) democratic governance; (iii) crisis prevention and recovery; and (iv) environment and energy.⁹¹ The IDB is in second place with 23% of the total, focusing on water and sanitation and citizen security.

IDB operations with donor funds. At present, the Bank's portfolio includes eight operations in execution using funds from international agencies, namely: (1) investment loan in the energy sector with US\$10 million in cofinancing by the China Co-financing Fund for Latin America and the Caribbean, administered by the Bank; (2) parallel

⁹⁰ This balance, and the one presented in the table, excludes certain nonfinancial forms of cooperation such as training or know-how, as well as assistance which, due to the small amounts involved, is recorded under another public sector function.

⁹¹ In addition, the UNPD incorporates the crosscutting issues of gender equity and development of capacities.

cofinancing projects with the World Bank for a total of US\$90 million in the areas of modernization of the State and water and sanitation; and (3) investment grants in the areas of energy, health, environment, water and sanitation, and citizen security, the latter being the largest grant of resources allocated under the country strategy for 2010-2014, with a total of US\$29.9 million (see Table 1).

During the coming country strategy period, the Bank will continue to work closely and on a coordinated basis with the donors and multilateral agencies that have a presence in Panama with a view to leveraging resources and maximizing the impact of development assistance.

Table 1. Multiyear and multidonor operations approved between 2010 and 2014

Sector	Operation number	Name	IDB approved amount (US\$ million)	Co-lender/donor	Co-lender amount (US\$ million)
PROJECTS WITH COFINANCING RESOURCES					
ENERGY	PN-L1095	Sustainable Rural Electrification Program	10	China Co-financing Fund for Latin America and the Caribbean	10
PROJECTS WITH PARALLEL FINANCING					
STATE REFORM/ MODERNIZATION	PN-L1066	Program to Strengthen Fiscal Management	50	World Bank	50
WATER AND SANITATION	PN-L1042	IDAAN Water and Sanitation Multiphase Investment Program - Phase I	40	World Bank	40
	PN-L1093	Water and Sanitation Multiphase Investment Program - Phase II	14		
INVESTMENT GRANTS					
ENVIRONMENT AND NATURAL DISASTERS	PN-X1003	Mainstreaming Biodiversity Conservation through Low-impact Ecotourism in the SINAP	0	IDB/Global Environment Facility	4
ENERGY	PN-X1005	Strengthening of the Mesoamerican Biofuels Program - Part I	0	Sustainable Energy and Climate Change Initiative Multi-donor Trust Fund	1
CITIZEN SECURITY	PN-X1011	Expansion of the Comprehensive Security Program of Panama	0	European Union	29.9
WATER AND SANITATION	PN-G1003	Rural and Indigenous Water and Sanitation Program in Panama	0	Spanish Cooperation Fund for Water and Sanitation	7.5
HEALTH	PN-G1001	Mesoamerica Health Initiative 2015	0	Mesoamerican Health Fund	2

* Data as of 15 May 2015.

**ANNEX VI. COMMENTS ON THE COUNTRY PROGRAM EVALUATION
PANAMA 2010-2014**

OVE recommendation	Management response
<p>Recommendation 1</p> <p>Work with the client to structure the new country strategy and background analytic work around key cross-cutting issues such as duality, poverty, productivity, and inequity, rather than by narrow sectors.</p>	<p>Agree</p> <p>This recommendation is being implemented. The Bank conducted an analysis of the growth challenges during the preparation of the 2015-2019 country strategy. This is being supplemented by a rigorous review of the social challenges. Both exercises address key cross-cutting issues such as those mentioned in the OVE report (duality, poverty, productivity, and inequity), together with sustainability. The country strategy currently under preparation is being structured around the pillars of the country's national development plan, grouping together challenges that will be dealt with in a multisector way.</p> <p>Actions to implement the recommendation:</p> <ul style="list-style-type: none"> (i) Prepare a study on challenges to growth, inequality of opportunity, and the social sector. (ii) Conduct consultations and reach agreements with the government and the Civil Society Council on the content of the Bank's country strategy. (iii) Approve the Bank's country strategy 2015-2019, based on a multisector approach.
<p>Recommendation 2</p> <p>Given the high levels of inequality in the country and the slow reduction of poverty, seek ways to redouble IDB's efforts to support Government's pro-poor development agenda by focusing budget support more on issues relevant to poverty reduction and by continuing targeting investment lending more toward poor beneficiaries.</p>	<p>Partially agree</p> <p>One of the key features of the dialogue with the authorities during preparation of the new country strategy was the mutual interest in continuing to target interventions on the poorest beneficiaries, incorporating lessons learned that would enable problems affecting this population segment to be addressed in a more holistic way. However, Management believes that the choice of instruments is not the most critical issue for the implementation of this recommendation. A fundamental factor in addressing poverty in Panama is the way in which sector initiatives are implemented. The Bank is committed to redoubling its efforts in this regard to ensure greater synergy between sector interventions that include the poorest population groups among their beneficiaries. This commitment will be reflected in the country strategy that is now being prepared.</p> <p>As regards the choice of instruments, the Bank will include the issue in the strategic dialogue with the country, though this will be fully determined during the programming process, taking into account: (i) their relevance, vis-à-vis the opportunities that arise to advance policy changes in the Strategy's priority areas; (ii) the continuation of existing Bank-financed initiatives; (iii) absorption and execution capacity in sectors that are key to supporting this objective; and (iv) the country's financing needs.</p>

OVE recommendation	Management response
	<p>Actions to implement the recommendation:</p> <ul style="list-style-type: none"> (i) Formulation of the 2015-2019 country strategy, including areas that will contribute to poverty reduction. (ii) Inclusion of poverty criteria as part of the operations programming exercise with the government authorities.
<p>Recommendation 3</p> <p>In the context of the overall strengthening of country systems and project management capacity, continue to support the client with strong institutional components. Support to the client should also include strengthening of municipal and regional development institutions and their capacity to more efficiently and effectively deliver basic services.</p>	<p>Partially agree</p> <p>Management agrees with some aspects of the recommendation, such as:</p> <ul style="list-style-type: none"> • Continue client support with strengthening of country systems and project management capacity. These aspects will be addressed in the 2015-2019 strategy currently under preparation. Specifically, work to strengthen country financial systems is expected to continue, supporting the government's development of a new integrated financial information system, and consolidating the support to the Public Procurement Department. • Project management support for executing agencies is due to be continued through training on project planning and management, aspects of financial management and procurement; cooperation/training with the Office of the Comptroller General on the Bank's procurement processes; and training on planning, which will be carried out as a part of the portfolio review process. • The Bank may also continue to include institutional strengthening components in its interventions, provided these are consistent with the intervention's goals. During the 2010-2014 Strategy, five of the investment loans approved had institutional strengthening components. It should be noted that OVE's recommendation does not specify what constitutes a "strong" institutional component. <p>Nonetheless, as regards the request for the strengthening of municipal and regional institutions, while this matter can be considered in the Bank's strategic dialogue with the country, the decision about future support to municipal development will be determined during the programming process with the government. It should be noted that the Bank is currently using technical cooperation to support Panama City as part of the Emerging and Sustainable Cities Initiative (ESCI).</p> <p>Actions to implement the recommendation:</p> <ul style="list-style-type: none"> (i) Support the government in the strengthening of country systems through a series of actions in financial management, auditing and accounting, and public procurement during the period of the new country strategy. (ii) Provide technical support for the executing agencies to strengthen their project management and planning capacity. (iii) Support execution of institutional strengthening components incorporated into the operations in the portfolio as well as operations to be approved during the period of the new country strategy.

OVE recommendation	Management response
	(iv) Generate studies and other knowledge products aimed at strengthening municipal and regional institutions.
<p>Recommendation 4</p> <p>Strengthen the design, monitoring, and completion of future policy-based programmatic series to avoid interruptions in the Bank's comprehensive support for priority sectors and to ensure the achievement of durable policy reform. When a PBP series is interrupted, it is recommended that the remaining operations be removed from the lending pipeline and a project completion report be prepared for the truncated series.</p>	<p>Disagree</p> <p>Management disagrees with this recommendation for the following reasons:</p> <ul style="list-style-type: none"> • The Bank's approach in the areas in which it has used programmatic instruments, which have been based on rigorous analysis validated by the quality standards prevailing in its policies, has been sound. In that regard, the interruption of the series in Panama cannot be attributed, as might be deduced from the recommendation, to matters of design or monitoring, but to changes in the manner in which the country decides to continue implementation of its reforms in one specific area. • Country ownership is a crucial factor in the sustainability of any structural reform. The Bank may therefore support countries on reform definition through its technical recommendations and incentives –such as policy-based loans– but cannot guarantee that programmatic series are not interrupted. It may sometimes even be desirable to put the reform on hold precisely to ensure its medium- and long-term success. • The nature of the instrument envisages, in the context of institutional reforms/changes and medium-term reform, tailoring the Bank's support to the changing nature of the environment, and promoting an on-going policy dialogue allowing the structural changes to be gradually implemented. • The fact that a series of operations does not fully materialize does not mean that the implemented reforms are not lasting. Not all PBPs' results can only be achieved when the whole series is completed. The reforms may continue without the Bank's support, the Bank having been instrumental in their launch, or require a pause to ensure they are in fact successful. • For clarification, current policies do not envisage a closing date for programmatic series. Series may therefore extend beyond the country strategy's validity period. • Additionally, subsequent phases to a first programmatic loan are not added to the pipeline until the operations are prioritized in the programming exercise. • As regards the recommendation to prepare a completion report, it should be noted that Management recently developed new guides for the preparation of Project Completion Reports (PCRs). These include specific guidelines for programmatic loans, including the specific case in which series are interrupted.

OVE recommendation	Management response
	<p>Actions to implement the recommendation:</p> <ul style="list-style-type: none"> (i) Determine the scope of the policy-based instrument (PBP or PBL) as part of the programming exercise, taking into account the content of the reform, the dialogue with the country, and the programmatic series under way. (ii) Prepare project completion reports for the programmatic series approved during the 2010-2014 period as applicable.
<p>Recommendation 5</p> <p>Strengthen risk analysis during project design and periodically reevaluate and reprioritize the lending program based on dialogue between the Bank and the Government of Panama, with a view to lowering the cost of projects prepared but later removed from the pipeline or canceled. Major deviations in the scope or focus of the country program from that envisioned in the CS should be justified and reported to the Board.</p>	<p>Disagree</p> <p>Management considers the logic of this recommendation and its implications for programming to be incorrect. First, the approach taken by the Bank in Panama has been based on ongoing dialogue with the government, which ensured the delivery of a program that responded to the priorities agreed with the authorities, and minimized deviations by limiting the inclusion of sectors not envisaged in the strategy (see detailed commentary in paragraph 3.8).</p> <p>Second, approved projects underwent rigorous risk analysis under the Bank's quality and evaluability criteria and were satisfactorily validated. This analysis is undertaken in several instances over the project cycle:</p> <ul style="list-style-type: none"> (i) In the identification stage, the project team determines the preliminary risks with the counterpart; these are reflected in the Project Profile and reviewed in the Eligibility Review Meeting (ERM); (ii) During the preparation of the Proposal for Operation Development (POD), there is a workshop on risks using the expert model developed by the Bank with the main stakeholders (executing agency, liaison body, project team, and others) to evaluate the risks of the project. The analysis includes institutional, political, legal, technical, fiduciary and management risks and addresses their corresponding mitigation actions. These are reviewed during the Quality and Risk Review (QRR); (iii) In the launch and execution stage these risks and the mitigating actions are periodically updated and included in progress reports and results based portfolio reviews, as well as in the supervision plan; (iv) In the closing stage the sustainability risks and lessons learned are analyzed. <p>Third, the Bank's support in the dialogue areas allowed headway to be made on concrete initiatives crucial to strengthening the country's sustainability framework, in particular, climate change issues, thus accelerating Panama's necessary institutional change. Fourth, the Bank's investment in basic technical know-how to develop the lending program made it possible to maintain a substantive exchange with the country in priority areas such as hospitals and urban transportation (subway) (paragraph 3.8).</p>

OVE recommendation	Management response
	<p>Lastly, following the monitoring and follow-up mechanisms in force, Management informs the Bank's Board of Executive Directors of the annual operational program, which is indicative of the composition and level of the program proposed for the country. The Bank will continue to emphasize country dialogue as the cornerstone of achieving a strategy that is relevant and the delivery of a program aligned with the priorities identified.</p> <p>Actions to implement the recommendation:</p> <ul style="list-style-type: none">(i) Apply the Project Risk Management Procedures Guide during project design and the execution of projects in the portfolio during the period of this country strategy.(ii) Prepare country programming documents as part of the annual programming exercise.(iii) Hold periodic meetings to review programming with the authorities.

ANNEX VII. DEVELOPMENT EFFECTIVENESS MATRIX

COUNTRY STRATEGY: PANAMA 2015-2019

STRATEGIC ALIGNMENT (measures two dimensions: (i) the degree of consistency between the strategy objectives and the country's development challenges, on one hand, and the government's priorities and plans, on the other; and (ii) the use of a blend of products (financial, knowledge, and technical assistance) to attain the proposed objectives and identify other donor agencies and their areas of action):

Consistency with strategic objectives: The strategy identifies the following priority areas: (i) improve the delivery of basic services to the population living in poverty; (ii) strengthen the educational profile of the population; and (iii) enhance the logistics services, efficiency, and connectivity of the productive infrastructure. The dialogue areas are labor markets, macrofinancial and fiscal stability, and decentralization. The crosscutting issues to be considered are: (i) gender and diversity; (ii) integration; (iii) climate change and environmental sustainability; and (iv) the institutional capacity of the local counterparts. The selected areas address the country's development challenges, are consistent with the priorities set by the national government, and are the result of dialogue between the country and the Bank.

Product blend and participation of other donors: The country strategy specifies the mix of operational products expected to be used to execute the 2015-2019 program. The Bank will continue its dialogue and operational coordination with: (i) the Development Bank of Latin America (CAF), the World Bank, and the Spanish Agency for International Development Cooperation (AECID) on water and sanitation; (ii) the European Union on citizen security; and (iii) the World Bank and the CAF on health, education, and social protection.

EFFECTIVENESS (measured as the extent to which the country strategy is expected to achieve its objectives based on a review of four dimensions: (i) the quality of the diagnostics supporting the Bank's action in each area of work; (ii) the quality of the results matrix accompanying the strategy; (iii) the use and strengthening of country systems; and (iv) the analysis of the lending framework):

Effectiveness dimensions	%
I. Sector diagnostics	
- Identifies the main problems based on empirical evidence	100%
- Identifies the main beneficiaries	100%
- Identifies and assesses factors contributing to the problems identified	100%
- Presents the policy framework and a sequence of events for Bank intervention	100%
- The diagnostics match the objectives presented in the strategy	100%
II. Results Matrix	
- Expected results are clearly defined	100%
- Indicators are outcome-based and SMART	100%
- Indicators have baselines	100%

Seven sector notes were presented as part of the strategy. All (100%) of the notes were validated.

- 100% of the notes clearly identify the sector's main problems based on empirical evidence.
- 100% of the notes identify the potential beneficiaries in each area of intervention.
- 100% of the notes identify or assess factors contributing to the problems identified.
- 100% of the notes present the policy framework and a sequence of Bank actions.
- In 100% of the notes, the issues raised match the Bank's strategic objectives with the country.

Results Matrix: The Results Matrix contains three strategic objectives of Bank intervention and 15 indicators to measure progress toward achieving the proposed objectives.

- The three strategic objectives are clearly defined and include a clear description of the expected outcomes for the set of priority areas involved.
- 100% of the indicators are outcome-based and SMART, and they all have baselines.

Country systems: There are diagnostic assessments of all financial management and procurement subsystems. Most of the country financial management and procurement subsystems will be used. There will be full use of some subsystems and partial use of others. The country subsystems that will not be used are: internal audit, external control, and contracting of individual consultants. All subsystems will be strengthened during the strategy period, with the exception of the budget system.

Lending framework: The strategy contains an analysis of the country's financing requirements and provides a scenario for sovereign-guaranteed lending of US\$1.95 billion in approvals for the 2015-2019 period.

RISKS (measures three dimensions: (i) identification of factors that actually do or might affect attainment of the proposed objectives; (ii) definition of mitigation measures; and (iii) monitoring mechanisms):

The strategy identifies macroeconomic, portfolio execution, and natural disaster risks and also identifies mitigation and monitoring measures for each of these risks.