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PANAMA

**IDB GROUP COUNTRY STRATEGY WITH PANAMA
2021-2024**

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ABBREVIATIONS

AECID	Agencia Española de Cooperación Internacional y Desarrollo [Spanish Agency for International Development Cooperation]
AIG	Autoridad Nacional para la Innovación Gubernamental [National Authority for Government Innovation]
ANA	Autoridad Nacional de Aduanas [National Customs Authority]
CAIPI	Centro de Atención Integral a la Primera Infancia [Comprehensive Early Childhood Care Center]
CGR	Contraloría General de la República [Office of the Comptroller General of the Republic]
CIAT	Centro Interamericano de Administraciones Tributarias [Inter-American Center of Tax Administrations]
COVID-19	Coronavirus disease caused by the SARS-CoV-2 virus, first detected in 2019
CRF	Corporate Results Framework
CSS	Caja del Seguro Social [Social Security Fund]
DGI	Dirección General de Impuestos [Internal Revenue Office]
ECLAC	Economic Commission for Latin America and the Caribbean
FATF	Financial Action Task Force
GDP	Gross domestic product
IDAAN	Instituto de Acueductos y Alcantarillados Nacionales [National Water and Sewer Systems Institute]
ICF	International Classification of Functioning, Disability, and Health
IMF	International Monetary Fund
INAC	Instituto Nacional de Cultura [National Cultural Institute]
INEC	Instituto Nacional de Estadística y Censo [National Statistics and Census Institute]
IPSAS	International Public Sector Accounting Standards
ITBMS	Impuesto a las Transferencias de Bienes Corporales Muebles y la Prestación de Servicios [Goods and services tax]
MAPS	Methodology for Assessing Procurement Systems
MINSA	Ministry of Health
MSMEs	Micro, small, and medium-sized enterprises
NCB	National competitive bidding
PEG	Plan estratégico de Gobierno [Government Strategic Plan]
SAI	Supreme Audit Institution
SAI-PMF	SAI Performance Measurement Framework
SINAC	Sistema Nacional de Áreas de Conservación [National System of Conservation Areas]
SMEs	Small and medium-sized enterprises
UNICEF	United Nations Children's Fund

EXECUTIVE SUMMARY

Context	<p>The sharp slowdown in Panama's economy following completion of the canal expansion in 2016, in conjunction with a slower than expected rate of poverty reduction during the period of strong economic expansion, revealed the need to diversify the country's productive structure and develop new sources of growth, based on criteria of inclusion and resilience. In response to this challenge, over the past five years Panama has taken steps to promote the growth of sectors such as tourism, to boost the competitiveness of the logistics cluster, and to improve the delivery of basic services, particularly in indigenous comarcas. The effects of the COVID-19 pandemic have heightened the importance of Panama making progress in these areas, as it was one of the hardest hit countries in the region, in both health and economic terms. In this context, in the years ahead the country should balance actions to address the most immediate impacts of the crisis with initiatives to promote inclusion and a sustainable recovery in productive activity, while adapting the economy to the changes brought by COVID-19.</p>
The IDB Group in Panama	<p>The Bank's Country Strategy with Panama for the 2015-2019 period focused on three areas: (i) improving the delivery of basic services to population segments living in poverty; (ii) strengthening the education profile of the population; and (iii) enhancing the logistics services, efficiency, and connectivity of the productive infrastructure. The IDB Group approved resources of US\$3.975 billion, including US\$3.396 billion in 25 sovereign guaranteed operations (US\$1.346 billion in investment loans, US\$1.65 billion in policy-based loans, and US\$400 million in emergency support). Additionally, 74 technical cooperation operations and 1 grant for US\$28.7 million were approved. IDB Invest approved operations totaling US\$545 million, and IDB Lab approved US\$6 million.</p>
Priority areas	<p>Given the country's challenges and the impact of COVID-19, the objective of the country strategy for the period 2021-2024 is to support the authorities' efforts to jumpstart economic recovery, to help Panama consolidate its position as a high-income country over the medium term in an inclusive and sustainable way. Three areas were identified during the dialogue process in which the IDB Group can contribute to this objective in the coming years: (i) modernizing public management; (ii) improving the delivery of basic services; and (iii) reigniting and diversifying productive activity. The IDB Group's support will be tailored to the country's needs arising from the health crisis and its social and economic impact, as well as with the process of rekindling growth. Information technology will be considered in each strategic area and the crosscutting issues of gender, diversity, environmental sustainability and climate change adaptation, and institutional strengthening will be addressed.</p>
Projected lending scenario	<p>The Bank projects annual sovereign guaranteed approvals averaging US\$465 million, for a total of US\$1.861 billion over the period 2021-2024. At the end of the strategy, the debt with the IDB could account for 45.6% of Panama's multilateral debt and 9.2% of its total public debt.</p>
Implementation considerations	<p>To contribute to the strategy's objective, the Bank will work with the authorities to speed up portfolio execution and pursue synergies within the IDB Group and with the international donor community. Consolidation of the ISTMO integrated financial information system and the general treasury account will continue, increasing the use of country systems over the long term.</p>

Risks

The main risks stem from the fiscal, financial, and social challenges the country faces in the wake of the COVID-19 crisis and its continued presence on the Financial Action Task Force (FATF) “grey list”. These issues may affect investment, the availability of financing for both the public and private sectors, as well as social cohesion. Lastly, environmental risks exist, mainly in relation to water resources, which are essential for the Panama Canal’s operations and for the energy sector. These risks are exacerbated by climate change. The proposed strategy envisages actions to help mitigate these risks.

I. COUNTRY CONTEXT

- 1.1 For over a decade (2004-2015) Panama posted one of the world's fastest growth rates, averaging 7.6% per year. This enabled Panama to have Latin America's highest per capita income and be classified as a high-income country.¹ The canal expansion between 2007 and 2016, together with other major public works, catalyzed the Panamanian economy's growth, although the biggest contribution came from private investment, mainly in construction and the real estate sector.²
- 1.2 However, following completion of the canal expansion works in 2016, the economy began to show clear signs of slowing. This highlighted the need to diversify the productive structure and develop new avenues for promoting inclusive, resilient growth in the face of climate change and natural disasters. Moreover, although Panama's economic success enabled it to cut poverty from 36.5% to 20.7% between 2007 and 2017, the rate of decrease was slower than in other countries with more moderate growth. In this period, poverty in Panama dropped by 0.15 points for each point of gross domestic product (GDP) growth, compared with a regional average of 0.22 points. The urban-rural divide narrowed, but the rural poverty rate (41%) remained almost twice the national average and was higher still among the indigenous population (82%), at four times the national average.
- 1.3 In response, the country drew up an agenda to promote the diversification of production and strengthen the contribution of growth to poverty reduction, focused particularly on rural areas. In this vein, over the past four years Panama has prioritized: actions to raise the level of sophistication of the logistics sector, tourism development by capitalizing on the country's cultural heritage and natural capital, mining, and certain niches in the agricultural sector. This was accompanied by a strategy to address extreme poverty more effectively through better targeted social safety nets and investment programs to improve the delivery of basic services to poor populations.
- 1.4 As a result, Panama has strengthened its position as a global business center and continued to witness significant growth in the tourism sector, with tourism exports coming to 6.8% of GDP in 2019, exceeding those of the canal (4.8%).³ The poverty rate has dropped by five points since 2014, to stand at 20.7%, which is below the region's average of 29%,⁴ and the urban-rural divide narrowed from 36 to 30 points. According to Panama's multidimensional poverty index, the percentage of households with energy shortages decreased from 15.2% to 6.3% of the total

¹ According to the World Bank classification.

² Construction's share of gross domestic product (GDP) has more than doubled since 2007, today accounting for approximately 18%, one of the world's highest percentages. The year 2007 is taken as a reference because there was a change in the national accounts methodology that year, and sector comparisons with current figures have only been possible since then.

³ In logistics, net tonnage passing through the canal rose from an average of 326 million tons between 2011 and 2014 to 387 million tons between 2015 and 2018, and the number of visitors entering via Tocumen International Airport rose from 5.8 million to 7.9 million over the same period (National Statistics and Census Institute, INEC). Progress was also made on the sector's institutional structure, such as the consolidation of the Logistics Cabinet, tasked with interagency coordination, and the development of the National Logistics Strategy 2017-2030, which establishes the long-term roadmap for generating more value added in the sector following the expansion of the Panama Canal.

⁴ Poverty data are from the Ministry of Economy and Finance, 2017.

between 2014 and 2017, while the share of households lacking improved sanitation fell from 20.5% to 9.1%.

- 1.5 Maintaining this trend and locking in these gains face the huge challenges of the global coronavirus (COVID-19) pandemic, however. The country recorded its first case on 9 March 2020 and since then has been implementing some of the region's strictest containment measures in an effort to avoid overwhelming the health system. As of 31 December, 248,217 confirmed cases and 4,022 deaths had been recorded, the highest rates in Central America. Panama also had the highest number of cases per 100,000 population (5,883) in the region.⁵
- 1.6 The government's response to the pandemic has focused on increasing health sector spending, promoting measures to prevent, detect, and treat the disease, supporting the people affected, and shoring up banking system liquidity. Despite these efforts, Panama's GDP plummeted by 17.9% in 2020. This pattern of economic activity widened the tax gap and the nonfinancial public sector deficit came to 10.1% of GDP, much higher than the precrisis projection of 2.8%, with an increase in the debt-to-GDP ratio of 23 percentage points. Central government current revenues contracted by 22.3% and Social Security Fund (CSS) revenues by 17.7%.
- 1.7 On the social front, the potential consequences of COVID-19 are shrinking household incomes and rising unemployment, poverty, and inequality, as the impacts will fall disproportionately on the most vulnerable groups and women. Poverty increased an estimated 2.9 points in 2020 (Economic Commission for Latin America and the Caribbean, ECLAC), although the impact is very likely to be greater, while unemployment rose from 7.1% in 2019 to 18.5% in 2020, and informality rose from 44.9% to 52.8%. This crisis is more regressive than its predecessors, and it may have severe repercussions for social welfare and stability, as it will accentuate the economic slowdown the country has been experiencing in recent years and presents additional obstacles for the agenda to diversify production to reignite growth, as it particularly affects tourism and air transport.
- 1.8 The prolonged pandemic is intensifying the short-term challenges associated with managing the health crisis, the population's increased vulnerability, job losses, and possible permanent business closures. These compound the more structural challenges the country faces in regaining economic dynamism and making growth more inclusive. These are mainly associated with institutional quality, limited economic diversification, and sharp inequalities in access to basic and productive services, including education, which particularly affect rural areas and indigenous comarcas.⁶ In this regard, in the coming years, Panama faces the double challenge of balancing measures to overcome the most immediate socioeconomic impacts of

⁵ The fact that it is one of the countries in the region hardest hit by the pandemic is partly due to its position as a logistics hub. Panama is also one of the countries performing the most testing, and it publishes COVID-19 statistics daily, providing a more accurate picture of how the virus is spreading.

⁶ The inequality between regions in El Salvador or Uruguay, for example, is a quarter of that in Panama, while in much larger countries such as Mexico and Brazil, regional inequalities are 65% and 40%, respectively, of Panama's (Astudillo, J.; Fernández, M., and Garcimartín, C., 2019: La desigualdad de Panamá: Su carácter territorial y el papel de las inversiones públicas. IDB, Technical Note IDB-TN-1703).

the crisis with initiatives to support the recovery with measures to adapt the economy to the changes brought by COVID-19 in a more inclusive way than was achieved during the period of stronger economic growth. Moreover, this is all against the backdrop of Panama's location in one of the regions most vulnerable to natural disasters and the effects of climate change, such that these risks will need to be managed appropriately to ensure economic and social progress is sustainable.

II. THE IDB GROUP IN PANAMA

A. Strategy implementation

- 2.1 The objective of the Country Strategy with Panama 2015-2019 was to contribute to Panama's medium- and long-term inclusive development by focusing the IDB Group's action on three areas: (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. Diversity, climate change, and environmental sustainability were addressed as crosscutting issues. The strategy supported the priorities of the Government Strategic Plan (PEG 2015-2019) and helped finance the five-year investment plan, which was geared to boosting competitiveness and fostering social inclusion in the framework of a sustainable and inclusive development model.
- 2.2 Strategy implementation was held back by institutional factors deriving from weak management capacity in certain areas, complex ex ante monitoring processes, and budgetary constraints. Nonetheless, the combination of different financial and technical support mechanisms and the Bank's close monitoring made it possible to obtain results, particularly as regards the delivery of basic services and social protection, the cultural relevance of the interventions, and consolidation of the national logistics system. Flexibility and the capacity for dialogue with diverse actors enabled the IDB Group to position itself as Panama's leading multilateral partner.
- 2.3 As a result of the COVID-19 crisis, in 2020 the IDB Group put in place a series of corporate, operational, and governance measures to bolster the timeliness and relevance of its support to the countries of the region.⁷ In Panama's case, at the authorities' request, the Bank approved an extension of the strategy's validity period until 30 June 2021⁸ and adjusted the program and active portfolio to support the authorities' response to the health crisis, help mitigate the social impacts and the effects on the productive fabric, and address financing requirements in

⁷ Proposal for the IDB Group's Governance Response to the COVID-19 Pandemic Outbreak (document GN-2996). Proposal for the IDB Group's Response to the COVID-19 Pandemic Outbreak (document GN-2995).

⁸ Document GN-3018.

coordination with the International Monetary Fund (IMF).⁹ IDB Invest provided liquidity to financial institutions by approving new lines and expanding existing foreign trade facilitation programs, while IDB Lab supported the scaling up of materials for COVID-19 detection.¹⁰

- 2.4 During the country strategy period,¹¹ the Bank approved 25 sovereign guaranteed loan operations for a total of US\$3.396 billion, including US\$1.346 billion in investment loans, US\$1.65 billion in policy-based loans (PBLs), and US\$400 million in a special development loan. Sovereign guaranteed loan disbursements in the country strategy period totaled US\$2.998 billion,¹² with a net cash flow for the country of US\$1.193 billion. Additionally, 74 nonreimbursable technical cooperation operations were approved, for US\$25.9 million, mainly in the gender and diversity, social protection and health, environment and rural development, climate change, education, and science, technology and innovation sectors, and an investment grant of US\$2.8 million was approved under the Regional Initiative to Eliminate Malaria.
- 2.5 IDB Invest approved nonsovereign guaranteed operations with 16 clients for US\$545 million,¹³ mainly targeting: (i) improved access to financial services for small and medium-sized enterprises (SMEs) and women entrepreneurs; (ii) an expanded range of cleaner energy sources; (iii) development of sustainable tourism and telecommunications sectors; and (iv) foreign trade finance facilitation through syndicated loans and issuance of credit guarantees. Meanwhile, IDB Lab approved nine technical cooperation operations and a loan under the Social Entrepreneurship Program for a total of US\$6.04 million, to spur the application of robotic technologies to solve social and environmental problems, the orange economy, the generation of digital entrepreneurship, COVID-19 solutions, and female entrepreneurship. In particular, the initiative to strengthen banks' capacity

⁹ Programmed resources were redirected to the Global Credit Program for Safeguarding the Productive Fabric and Employment (operation PN-L1164 for US\$150 million), one of the project prototypes to respond to the COVID-19 pandemic. Additionally, in the context of a joint effort with the IMF, special development lending of US\$400 million was approved under operation PN-L1163, together with the Support Program for Reforms in the Water, Sanitation, and Energy Sectors II (operation PN-L1159 for US\$200 million), to support the country's financing requirements. As regards the active portfolio, the reformulation of up to US\$123 million of the loan for operation PN-L1121 was authorized for a COVID-19 prototype operation to support vulnerable population groups, and US\$16 million was redirected for conditional cash transfers. Additionally, the active portfolio was used to meet ad hoc needs such as: purchasing personal protective equipment for healthcare workers and equipping intensive care units, digitalization of processes linked to management of COVID-19, printing books, and providing educational resources for teachers. Specific analyses were also conducted to ensure Panama was able to access the resources of the Bank's Migration Facility.

¹⁰ The measures to support Panama include the approval of a US\$20 million line for Davivienda Panamá, and the expansion of the Towerbank and Banco Aliado lines to US\$25 million and US\$40 million, respectively. To support the SME segment, it pledged a loan of US\$40 million to Banistmo and mobilized a B loan to Global Bank for US\$30 million. Under the technical cooperation prototype modality, IDB Lab approved the "Viral Transportation Medium to Address COVID-19" project (operation PN-T1263) for US\$150,000.

¹¹ Number of operations and amounts since country strategy approval, as of 31 December 2020.

¹² Includes the legacy portfolio when the country strategy for 2015-2019 was approved, which included 13 loans totaling US\$783 million and an undrawn balance of US\$438 million.

¹³ These figures do not include regional operations.

to supply credit to women-led SMEs stands out, having led to the structuring of the first IDB Invest social bond with a gender focus for a value of US\$50 million.

B. Main results of the 2015-2019 country strategy

2.6 The IDB Group achieved results¹⁴ under each of the priority objectives and also made solid progress on the strategy's dialogue areas. With the objective of **improving the delivery of basic services to population segments living in poverty**, the strategy proposed a two-pronged approach: targeting the social safety net, and improving the supply of basic health, water and sanitation, and electrification services. In the area of **social protection**, the Bank provided financial and technical support, making concrete progress in the targeting, management, and transparency of conditional cash transfer programs and, in the context of the COVID-19 crisis, it financed transfers to over 40,000 households living in extreme poverty. Specifically, a uniform criterion was applied to classify poverty, 40% of beneficiaries of the *Red de Oportunidades* [Opportunities Network] and of the "120 a los 65" program for older adults were recertified, and the legal and operational framework for the National Registry of Beneficiaries was developed. This system will make it possible to eliminate potential duplications in the delivery of government benefits and manage them transparently and efficiently.¹⁵

2.7 In the **health** area, the IDB helped reduce maternal and infant mortality in the indigenous comarcas of Ngöbe Buglé, Guna Yala, and Emberá Wounaan by expanding access to health care services in the country's most isolated areas. The Estrategia de Extensión de Cobertura de Atención Primaria [Strategy to Expand Primary Care Coverage] was given financial and technical support, providing care to over 520,000 people, representing coverage of 42% (Ngöbe Buglé) and 75% (Darién) of the total population of the prioritized provinces.¹⁶ With the Salud Mesoamérica Initiative (ISM) the rules and coverage for care in childbirth and measles vaccination coverage were improved. The Bank also supported improvements in the **coverage and quality of comprehensive early childhood care** by strengthening institutional and community offerings. In the case of institutional care, progress was made on the design of a quality management system for Comprehensive Early Childhood Care Centers (CAIPs), and 11 CAIPs across the country were refurbished and expanded, a curriculum was implemented for 0-3-year-olds, as was a payment per capita and by results model increasing government investment in these centers.¹⁷ A focus on cultural relevance was

¹⁴ Includes the results of the active portfolio and the operations approved during the strategy period.

¹⁵ This refers to the Programs for Transparency and Equity in Spending on Social Protection I, II, and III (PN-L1103, PN-L1118 and PN-L1152), and the Social Inclusion and Development Program (PN-L1105), which were accompanied by three technical cooperation operations.

¹⁶ Interventions in the health sector include the Health Equity Improvement and Services Strengthening Program (operation PN-L1068) and the Integrated Health Service Networks Strengthening Program (operation PN-L1115).

¹⁷ Social Inclusion and Development Program (operation PN-L1105). In the case of community care, progress was made on a home visits model for children ages 0-3 and their families living in remote areas to offer childhood development guidance and stimulation as part of the technical cooperation operation to offer Integrated Early Childhood and Education Services (operation PN-T1133). This model is being scaled up.

maintained in the delivery of social services and the design of infrastructure works in indigenous comarcas in the health and social protection sectors.¹⁸

- 2.8 In order to improve the delivery of **drinking water and sanitation services**, a strategy was proposed that combined investments to address access gaps with institutional enhancements to increase efficiency. This involved projects to enable drinking water coverage to be expanded in urban areas, benefiting approximately 313,852 inhabitants. Sewerage and wastewater treatment systems were refurbished, directly benefiting 64,552 inhabitants of the cities of Aguadulce and Pedasí.¹⁹ Public health and environmental conditions were improved in the Panama City metropolitan area, which is home to 27.8% of the population living in poverty, sewerage system coverage was extended, 105 kilometers of rivers, streams, and coastline were remediated, and wastewater treatment was provided for 820,000 inhabitants.²⁰ In rural and indigenous areas, comprehensive rural water and sanitation works were undertaken, benefiting 43,000 inhabitants.²¹ On the institutional front, progress was made on interagency coordination in the water and sanitation sector and its strategic planning, with the creation of the National Water Council (CONAGUA) and preparation of the “Agua para Todos” [Water for All] National Water Security Plan 2015-2050.²² However, the weak institutional capacity of the technical counterparties and the lack of timely decisions on key projects to make the sector more efficient²³ affected the expected outcomes.
- 2.9 The interventions under this strategic objective addressed crosscutting themes relating to gender and diversity, cultural relevance, climate change, and environmental sustainability. The IDB Group supported the development of policies and instruments to promote women’s physical, economic, and decision-making autonomy²⁴ and consolidated the issuance of the first social bond with a gender

¹⁸ The Bank worked on the co-design of the specifications for the construction of basic health care infrastructure, school facilities, Comprehensive Early Childhood Care Centers (CAIPs), and rural roads, and on establishing a permanent dialogue with the authorities in the comarcas.

¹⁹ National Water and Sewer Systems Institute (IDAAN) Water and Sanitation Investment Program - Phase I (operation PN-L1042) and the Water and Sanitation Multiphase Investment Program - Phase II (operation PN-L1093).

²⁰ Panama City and Bay Sanitation Project Supplemental Financing (operation PN-L1053) and the Panama City and Bay Sanitation Program II (operation PN-L1109).

²¹ Rural and Indigenous Water and Sanitation Program in Panama (operation PN-G1003).

²² During the country strategy period, a programmatic series of two operations (operations PN-L1145 and PN-L1159) was approved for a total of US\$500 million with the objective of contributing to the sustainability of the energy sector, as well as increasing coverage and improving management of water supply and sanitation services, through policies to strengthen and supplement the regulatory and institutional framework of the energy and water and sanitation sectors.

²³ Program to Improve the Operational Management of the National Water and Sewer Systems Institute in the Panama City Metropolitan Area (operation PN-L1148 for US\$250 million) was approved in 2017 and reached partial eligibility in May 2020 to support the sector during the COVID-19 emergency. Its objective is to improve the quality of drinking water services for the population of the Panama City metropolitan area by helping to enhance IDAAN’s management capacity and optimize the drinking water production and distribution system.

²⁴ Program to Support Gender Equality Policies (operation PN-L1156). Key outcomes include the approval of the regulation on pregnant minors, the creation of an interagency care committee, the approval of standards for the family planning program and sexual violence protocols, and the creation of a National Gender Parity Council under the Gender Parity Initiative.

focus²⁵ in Latin America, fostering women's economic empowerment and entrepreneurship. Cultural relevance was prioritized in the delivery of social and productive services in indigenous comarcas and the co-design of infrastructure works in the health and social protection sectors.²⁶ The climate change and environmental sustainability dimensions were considered in designing interventions in the water and sanitation sector.²⁷

- 2.10 To support the strategic objective of **strengthening the educational profile of the population**, the strategy aimed to enhance the quality and equity of the education system, in both urban and rural areas, and to strengthen human and institutional capacities to stimulate the innovation, science, and technology systems. As regards the **educational system**, the Bank focused on the expansion and improvement of school facilities in rural and indigenous areas, benefiting over 18,000 students in remote areas.²⁸ Initiatives were supported nationwide to improve education quality. Specifically, the first large-scale student evaluation system was put in place, incorporating national writing, math, and science tests for third and sixth grade students, and teaching skills in Spanish and math in public primary schools were strengthened.²⁹ With respect to **innovation**, public calls for proposals were financed to implement 96 research and innovation projects, with the goal of promoting productivity and social inclusion.³⁰ Specifically, mission-oriented research³¹ was promoted in response to the challenges defined by the government and to increase the number of researchers devoted to research and development activities.
- 2.11 Under the strategic objective of **enhancing the logistics services, efficiency, and connectivity of the productive infrastructure**, the strategy sought to address the institutional and infrastructure gaps that affect the productivity of the canal's logistics cluster and its ability to spur growth in the country's productive sectors and regions outside the capital. Based on this approach, Panama's legal and regulatory framework for **logistics** was strengthened, easing the performance constraints on value added logistics services and regional trade. The National Logistics Strategy was designed, with a 2030 horizon, along with the Transportation and Logistics Plan for the Interoceanic Zone, and the Logistics Cabinet—the high-level agency for interagency and private sector coordination on

²⁵ Banistmo Gender Bond (transaction 12174-02) for US\$50 million.

²⁶ The Bank worked on the co-design of the specifications for the construction of basic health care infrastructure, school facilities, and CAIPs, and on establishing a permanent dialogue with the authorities in the comarcas.

²⁷ For example, the Panama City and Bay Sanitation Program II (operation PN-L1109) envisages works and institutional strengthening geared to increasing wastewater treatment capacity.

²⁸ Educational Facilities and Learning Quality (operation PN-L1064) and Innovation in School Infrastructure (operation PN-L1072).

²⁹ The outcomes derive from the Program to Improve Efficiency and Quality in the Education Sector (operation PN-L1143) with the support of a series of technical cooperation and intra-regional technical cooperation (CT/INTRA) operations to support the sector.

³⁰ Innovation Program for Social Inclusion and Productivity (operation PN-L1117).

³¹ Mission-oriented research is funded by public agencies, based on sectors' needs and challenges. Missions are defined and prioritized by the government to guide the resources devoted to innovation.

logistics matters—was strengthened.³² The “Panamá Digital” portal now enables 150 government formalities to be done online. At the local level, 67 municipios have put priority formalities online, as well as helping update the National Cybersecurity Strategy, and so contribute to the country’s competitiveness and social inclusion.³³

- 2.12 In **transportation**, the condition of the national highway system was improved, with the refurbishment of 211 kilometers of highway and more frequent maintenance on 600 kilometers of priority national routes and corridors. The sustainability of highway maintenance operations was promoted with the implementation of a service standards mechanism covering 7% of the national network and a refurbishment and maintenance contracts system for 9% of the rural road network.³⁴ The design of new refurbishment and road improvement works³⁵ included ethnoengineering³⁶ components to ensure cultural relevance and climate change resilience. In **energy**, the implementation of the Energy Transition Agenda was fostered to enhance energy security through diversification of the energy matrix, increasing energy efficiency and regional integration, and to support the preparation of the Rural Electrification Master Plan, with a view to ensuring universal access to power by 2030. In line with the Plan, 6,463 households, 30 schools, and 7 health centers across the country were electrified via grid connections and standalone systems.³⁷
- 2.13 Progress was made in the **dialogue areas**, particularly in the **labor market** area, with headway made on a public-private platform called Marca Tu Rumbo³⁸ to promote labor market access among young people. This fostered participation by 30,800 young people and 84 companies in training and employment services. To support productive development through human capital, the first call for proposals for funds awarded by competition was launched, receiving 90 proposals, of which 68 met the eligibility criteria.³⁹ In the **macrofinancial and fiscal stability area**, the preparation of the Tax Administration Diagnostic Assessment Tool (TADAT) was supported. This tool will measure the efficiency and productivity of the Panamanian

³² Programmatic series comprising three operations approved in 2015, 2016, and 2018 with the objective of helping improve Panama’s logistics performance by easing regulatory and institutional constraints (operations PN-L1110, PN-L1119, and PN-L1151).

³³ Panama Online Program (operation PN-L1114). Additionally, in regional integration, the contract was awarded for the construction of the border control facility at Paso Canoas (Customs Logistics Integration Program, operation PN-L1107), and approval from the Guna Yala and Kuna Wargandi comarcas was obtained to conduct an environmental impact assessment on the Panama-Colombia electrical integration program.

³⁴ Puebla Panama Plan Multiphase Road Infrastructure Program to Enhance Competitiveness-II (operation PN-L1047).

³⁵ Support for the Development of Territorial Connectivity in Panama’s Central and Western Regions (operation PN-L1147).

³⁶ IDB. Guías de Etnoingeniería. Washington, D.C., 2005. These guides describe participatory methodologies to ensure the cultural relevance of the design and maintenance of small infrastructure works built in local communities.

³⁷ Sustainable Rural Electrification Program II (operation PN-L1095). The operation was accompanied by a permanent dialogue with the comarca authorities on the extension of the first electricity distribution line in the Guna Yala comarca.

³⁸ IDB Lab support: New Employment Opportunities for Youth – NEO-Panama (operation PN-M1027).

³⁹ Program to Support Productive Development through Human Capital in Panama (operation PN-L1153).

tax administration against an Organisation for Economic Co-operation and Development (OECD) benchmark. Additionally, an analysis was conducted to identify the main taxpayers (accounting for 67% of total tax revenue) and a roadmap set out to modernize electronic invoicing. In relation to **decentralization**, the decentralization efforts of the National Secretariat for Decentralization were supported with technical cooperation resources.

- 2.14 During this period, in response to the authorities' commitment to the digital agenda, the creative industries, and the revitalization of urban cultural heritage, the IDB Group made inroads into additional sectors to those agreed in the strategy. The Bank supported the adoption of the Panama Digital Hub Strategy to promote the information and communication technologies industry, and the creation of the Ministry of Culture with an institutional mandate that includes development of the creative and cultural economy, copyright, and the cinematographic and audiovisual industry. Additionally, through the Patrimonio Vivo [Living Heritage] program, the strategic plan for the comprehensive renewal of the historic center of Panama City was developed. Meanwhile, IDB Invest and IDB Lab improved access to finance and promoted value chains. Specifically, 484 individual foreign-trade transactions were supported, directly benefiting 57 Panamanian companies, 38 of which were SMEs. Access to finance for investment projects was also improved for 106 micro, small, and medium-sized enterprises (MSMEs). Projects to promote value chains based on natural capital, nutrition, coffee, female entrepreneurship, and financial and nonfinancial services benefitted 457 families in indigenous communities and supported over 3,500 female-led entrepreneurship initiatives.

C. Portfolio in execution and lessons learned

- 2.15 **Portfolio.** As of 31 December 2020, the IDB portfolio comprised 24 sovereign guaranteed operations for an approved total of US\$2.052 billion and an undisbursed balance of US\$1.287 billion. Of this balance, 44% was in the water and sanitation sector,⁴⁰ 15.5% in urban development, 8% in health and social protection, 3% in energy, 6% in transportation, 6% in education, 5.8% in integration, 3% in gender and diversity, 3% in fiscal and municipal management, and 5% in other sectors. The portfolio also includes 51 nonreimbursable operations, for a total of US\$51 million, including technical cooperation operations for US\$18.9 million and investment grants for US\$32 million. IDB Invest has a portfolio⁴¹ of 10 operations with an approved total of US\$509 million, mainly in the infrastructure sector, supporting the Panama Canal expansion, and access to finance for segments with credit constraints, such as women-led companies and SMEs, and foreign-trade facilitation. The IDB Lab portfolio comprises seven technical cooperation operations for US\$4.1 million and a Social Entrepreneurship Program loan for US\$1 million, targeting innovation, 21st century skills for at-risk youth, the orange economy, gender equality, COVID-19 solutions, climate change, and the circular economy.

⁴⁰ Of this balance, US\$123 million from the Sanitation Program for the Districts of Arraijan and La Chorrera (operation PN-L1121) was reformulated in December 2020 in response to the COVID-19 crisis to help support minimum consumption levels for persons living in poverty, extreme poverty, and situations of vulnerability.

⁴¹ Figures as of November 2020.

- 2.16 **Lessons learned.**⁴² At the **strategic** level, the prioritized areas of work were relevant for the country's development and remain so today. The most important lessons arising during the period, which will be factored into the new strategy, include the following: (i) weaknesses in public management limit the effectiveness of investment programs, such that prioritization of these topics in the Bank's actions with the country could help improve the effectiveness of public investment projects in general, and of the Bank's interventions, in particular; (ii) evaluating the political feasibility of institutional change in the sectors prioritized in the strategy is key to determining the sequence and structure of the Bank's program and the scope of the expected outcomes during the period;⁴³ (iii) in order to support and sustain the reforms fostered by the policy programs, they must be complemented with sector and technical cooperation operations to help the expected outcomes from the reforms to materialize in a timely way; (iv) the approach to crosscutting themes like diversity and cultural relevance required extensive and comprehensive support from the analysis of the technical challenges, dialogue with indigenous comarcas to identify needs and solutions, and coordination of a flexible multisectoral response by the Bank—this process took time and required technical and financial resources that should be anticipated in future interventions;⁴⁴ and (v) making headway on the climate change agenda requires dialogue with the authorities to identify policies and investments contributing to the country's commitments under its Nationally Determined Contribution (NDC).
- 2.17 At the **operational** level the following considerations stand out: (i) given Panama's good access to external financing, the Bank's value at the operational level lies in its technical contribution and capacity to support executing agencies on project implementation—a factor to which particular attention should be paid when designing new operations; (ii) addressing the needs of the most vulnerable population groups effectively requires an investment in substantive dialogue with beneficiaries to achieve relevant solutions,⁴⁵ and technical cooperation resources that support operation preparation and execution; (iii) early definition of land titling mitigates the risks of delay to execution of infrastructure works;⁴⁶ (iv) to improve execution, there need to be realistic estimates of the time the CGR requires for ex ante review of individual contracting processes and associated payments, while

⁴² The sources for this section include project completion reports submitted during the strategy period, semiannual portfolio meetings, and the Office of Evaluation and Oversight Country Program Evaluation.

⁴³ Program to Improve the Operational Management of the National Water and Sewer Systems Institute in the Panama City Metropolitan Area (operation PN-L1148), approved in 2017, suffered delays to its eligibility process due to the high relevance of the process of enhancement of IDAAN at the political level.

⁴⁴ The actions proposed under the Panama Action Plan with OVE 2020-2024 for inclusion in this lesson learned include: (i) fostering sector and geographic coordination of the Bank's interventions in rural and indigenous areas from the design and planning stage; and (ii) continuing to promote exchanges of experience to present alternatives enabling the government to adapt innovative models of service delivery in isolated areas.

⁴⁵ The OVE Plan of Action with Panama for 2020-2024 includes preparing the documentation on the strategy for working with Panama's indigenous peoples and documenting lessons learned from the Bank's interventions in these communities.

⁴⁶ For example, the Customs Logistics Integration Program (operation PN-L1107), Support for the Conservation and Management of Cultural and Natural Heritage (operation PN-L1146), and the Social Inclusion and Development Program (operation PN-L1105).

at the same time promoting the modernization of public management; (v) against the backdrop of budgetary constraints, it is key to monitor that execution units use the resources allocated to their project in the general state budget, and that these budget allocations are consistent with the planned activities; and (vi) to maximize IDB Invest's development impact through partnerships with financial institutions, clients should be selected that are interested in growing specific portfolios so as to leverage resources, aim for replicability, and disseminate lessons learned.

III. PRIORITY AREAS

- 3.1 The objective of the country strategy for the period 2021-2024 is to support the authorities' efforts to jumpstart a post-COVID-19 economic recovery that helps Panama consolidate its position as a high-income country over the medium term in an inclusive and sustainable way. Three areas have been identified in which the IDB Group can contribute to this objective in the years ahead: (i) modernizing public management; (ii) improving the delivery of basic services; and (iii) reigniting and diversifying productive activity. Due to the critical value the crisis has revealed information technology (IT) to have in productive and social resilience, the inclusion of IT will be considered in each of the strategic areas. Additionally, the issues of gender, diversity, environmental sustainability, and climate change will continue to be addressed in a crosscutting way. In view of the uncertainty caused by COVID-19, in the proposed approach each of the IDB Group's three areas will tailor its response to the country's immediate needs arising from the health crisis and its social and economic impact, and the process of reviving growth, while addressing the dimensions of equity and resilience to natural disasters and climate change.
- 3.2 The priority areas are the outcome of a dialogue with the authorities based on the priorities of the government program,⁴⁷ the Country Development Challenges document,⁴⁸ lessons learned from the previous strategy, the Bank's positioning, and the recommendations of the Office of Evaluation and Oversight (OVE) on the 2015-2019 country program (see Annex V), and are aligned with the objectives of the second Update to the Institutional Strategy 2020-2023.⁴⁹

A. Modernizing public management

- 3.3 Panama has moved up 21 positions on the global per capita GDP ranking (in purchasing power parity terms) over the past 15 years, attesting to its economic success. By contrast, the country's position in terms of institutional quality

⁴⁷ The priority areas of the Government Strategic Plan (2020-2024) are: (i) good governance; (ii) law and order and the rule of law; (iii) a competitive economy that creates jobs; (iv) combating poverty and inequality; and (v) education, science, technology, and culture. Its [Nationally Determined Contribution](#) commitments are also considered.

⁴⁸ See the [Country Development Challenges document](#).

⁴⁹ In particular, the prioritized areas seek to strengthen the capacity of the State, provide inclusive and sustainable infrastructure services, develop human capital, integrate the productive sector in global value chains, and improve the institutional context for the promotion of business development. It also aligns with IDB Invest and IDB Lab priority areas as it highlights institutional improvements for the smooth operation of the private sector, financial inclusion, innovative entrepreneurship, and climate-smart agriculture. IDB Invest Business Plan 2020-2023 (document CII/GA-77-8) and IDB Lab Business Plan 2019-2021 (document MIF/GN-235-3).

indicators remains unchanged.⁵⁰ In the specific case of public management, according to the World Bank's Government Effectiveness Index, which measures the quality of public services, the civil service, and policy formulation and implementation, Panama went from sixth to ninth position among the countries of the region between 2015 and 2018. This relative institutional weakness represents a major challenge both in managing the current crisis and in spurring an inclusive and sustainable economic recovery in a fiscal panorama that has shown signs of deterioration in recent years—a trend that COVID-19 has accentuated. The public deficit has been expanding, rising from 1.8% of GDP in 2016 to 3.1% in 2019, to stand at 10.1% in 2020. As a consequence, in the last three years the limits set in the fiscal rule have had to be raised to avoid a possible breach. In the medium term it will be necessary to return to the path of fiscal consolidation. This will require increased revenues in order to expand social spending and finance the public pension system deficit. Spending and spending management will need to become more efficient, and public administration made more effective in general, in terms of access to the population, transparency, and speed of formalities.⁵¹ In this regard, there are three dimensions of public management where it is essential to overcome these institutional weaknesses: tax administration, spending prioritization and management, taking into account the objectives of equity and sustainability, and digital government.

- 3.4 Between 2014 and 2019, Panama's tax revenues fell from 10.1% of GDP to 8.7%, the lowest rate of tax collection in Latin America and the Caribbean.⁵² These low and decreasing tax receipts are partly a result of the design of the various taxes, some of which have narrow bases and low rates.⁵³ This is compounded by limited analysis of the effectiveness and impacts of tax measures (exemptions, special systems, etc.). The low tax take also derives from inefficiencies in the tax administration, where there are high levels of noncompliance, ranging from 34% in the case of personal income tax to 45% for consumption taxes and 73% in the case of corporate taxes.⁵⁴ Moreover, although informality in Panama is below the Latin American average (51.4% and 60.4%, respectively, according to the latest data from ECLAC), this does not correspond to its income level if compared with Chile (29.3%) or Uruguay (29.2%), which is another factor in the low tax take.
- 3.5 Despite its low revenue collection capacity, the tax system is an obstacle to business development in Panama. According to the World Bank's Doing Business indicators, Panama ranked 176th out of 191 countries analyzed under the category of "tax payments." The reasons for the low efficiency of the tax administration include an out-of-date register of taxpayers, a low-tech approach, inadequate staff training, and a somewhat ineffective functional organization with little coordination

⁵⁰ Based on an average of the World Bank governance indicators.

⁵¹ Panama was 64th on the World Economic Forum Global Competitiveness Ranking in 2018 but fell to 66th in 2019. Much of the loss of competitiveness was due to backsliding in the "Institutions" component.

⁵² Central government tax revenues.

⁵³ The rate for the goods and services tax (ITBMS), for example, is the lowest in the region. Nevertheless, the tax expenditure is among the highest. Peláez, 2018: "Panorama de los Gastos Tributarios en América Latina". Inter-American Center of Tax Administrations (CIAT) Working Paper 6/2017.

⁵⁴ Internal Revenue Office (DGI) (2017): Boletín Estadístico Tributario 2017.

- among the three key agencies concerned: the Internal Revenue Office (DGI), the National Customs Authority (ANA), and the Social Security Fund (CSS).
- 3.6 On the public spending side, Panama is second from last on the regional ranking of public spending management.⁵⁵ Weaknesses exist in planning and monitoring processes, leading to delays in execution and a loss of efficiency and transparency in the use of resources, in addition to which there are problems of sustainability of the public pensions system.⁵⁶ The ex ante control system applied by the CGR causes excessive delays, which limits spending effectiveness, and there are inefficiencies in generating relevant and timely information with which to evaluate the impact of policies in areas of interest for the country, such as equity, inclusion of vulnerable groups (including migrants), environmental sustainability, climate change, or diversity. Meanwhile, spending management is limited by fragmented processes in the public sector, which are basically manual, and in some cases redundant.
- 3.7 The government has been fostering the digital transformation of public administration to improve service delivery, information availability, and transparency. The country has climbed 15 places on the latest United Nations e-government ranking. Nonetheless, it is still 84th worldwide, well below countries with similar income levels, such as Uruguay (26th) or Chile (34th). The authority responsible for digitalization, the National Authority for Government Innovation (AIG), has been strengthened in recent years, but does not have the operational or budgetary capacity necessary to catalyze the digitalization process to produce tangible improvements in the delivery of general services to citizens and the private sector. Specifically, there is little coordination between this agenda and the sector agencies responsible for providing services such as health care, education, and social protection, and the potential to simplify and automate formalities to improve the quality of general services to citizens and the climate for attracting and promoting investments has not been harnessed. Moreover, expanding the digitalization agenda to encompass fiscal management, operational management of public agencies, and an ever broader range of services to the population will require additional efforts in cybersecurity.
- 3.8 On this pillar, through its existing portfolio and new operations, the IDB Group will support public management modernization efforts on both the revenue and spending sides, prioritizing increased effectiveness of the tax administration and oversight agencies, digital transformation of public administration in a way that builds trust, and strengthening the analytic and planning capacity of the sector ministries with which the Bank works, with emphasis on areas such as health, social protection, and education.

B. Improving the delivery of basic services

- 3.9 Panama remains one of the most unequal countries in Latin America and the world. This is apparent in the marked regional gaps in access to basic services,

⁵⁵ Izquierdo, A., C. Pessino, and G. Vuletin. 2018. "Better Spending for Better Lives: How Latin America and the Caribbean Can Do More with Less." IDB. Washington, D.C. Refers to public investment.

⁵⁶ It is estimated that the system's contributions and reserves will be insufficient to meet existing commitments in the years ahead, so more resources from the treasury will start to be needed to pay pensions. IMF, Article IV Consultation Staff Report, April 2020.

which are all the more conspicuous in rural areas, including the indigenous comarcas. In health, for example, maternal mortality is 3.3 times higher in rural areas than in urban ones, and the infant mortality rate (among children under 1) stands at 18.4 deaths per 1,000 live births in rural areas compared with 11.7 in urban areas.⁵⁷ Water and sanitation services, which are crucial to preventing and avoiding the spread of disease, remain a challenge. Water and sanitation coverage in urban areas is 98.8%, compared with 84% in rural areas, and less than 60% in the indigenous comarcas. Continuity of operation of the water supply service remains low and 76% of households using this service have 24-hour access to drinking water during the rainy season and 70% during the dry season. In the case of sanitation services, the national coverage rate for basic service is 83.3%, which is below the regional average (86.1%) and much lower than the rate in countries like Costa Rica (97.8%), Uruguay (96.5%), or Colombia (89.6%). At the international level, Panama is in 82nd place out of 140 countries for the reliability of its water supply.⁵⁸ Climate vulnerability and weaknesses in water resource management jeopardize supply for both human consumption and productive use.⁵⁹ The COVID-19 health crisis has made the need to address these challenges more pressing.

- 3.10 Shortcomings are also apparent in the educational system, hindering social mobility and the productivity of the economy. The average level of learning and skills students develop is low, and there are significant differences in access depending on income level.⁶⁰ Region-wide educational tests (SERCE, TERCE)⁶¹ find that half (48.9%) of third grade primary students do not understand what they read, compared with 39.5% across the Latin American and Caribbean region. Just 54.7% of young Panamanians complete secondary schooling, compared with 79.4% in Chile, and many young people drop out of the system after repeated academic failure and are at risk of dropping out due to being over grade-age. There is a serious risk of this situation worsening with the COVID-19 crisis, as the educational system has not successfully used distance learning to ensure continuity of teaching for many of its students. It is important to underscore that these challenges are more acute in the comarcas, creating the need for a differentiated response aligned with bilingual intercultural education.⁶²
- 3.11 Weaknesses in the educational sector are also an obstacle to graduates making a successful transition to the labor market and contributing to productivity gains. According to the 2018 ManpowerGroup Talent Shortage Survey, 35% of

⁵⁷ Ministry of Health Vital Statistics. Panama City. 2016.

⁵⁸ Global Competitiveness Report 2019. World Economic Forum.

⁵⁹ Climate change scenarios project a reduction in the availability of water of up to 77% by 2100 (ECLAC, 2015, Climate Change in Central America: Potential Impacts and Public Policy Options).

⁶⁰ According to the multiple indicator cluster survey (MICS), 67% of the infant population in the fifth highest income quintile received early childhood education, compared with 27% in the poorest quintile.

⁶¹ Second and Third Comparative and Explanatory Regional Studies (SERCE and TERCE, respectively), UNESCO Regional Bureau for Education in Latin America and the Caribbean (OREALC).

⁶² The impact evaluation of the Jadenkä program, which aimed to close the learning gap for Panama's indigenous children by means of bilingual preschool mathematics programs in Ngäbere and Spanish, and incorporating features of Ngäbere culture, showed positive impacts on several student dimensions, such as math and ethnomathematics skills (IPA. Impact evaluation study on the Ari Taen Jadenkä pilot project: "*Jadenkä: Matemática divertida para la educación inicial*", 2018 and 2019 cohorts).

employers have difficulty hiring workers with the required skills, while according to the Global Competitiveness Ranking 2017-2018, an inadequate workforce is the third biggest constraint on doing business in the country.

- 3.12 In social protection, although Panama has an array of cash transfer programs for poverty reduction, their impact is relatively modest,⁶³ partly as a result of weaknesses in certification, low coverage, and, in some cases, high leakage. Social programs targeting the country's poor cover more than 70% of households living in poverty, but some of them reach just 19% of their target population. Meanwhile, around 80% of beneficiaries of some of these programs are not living in overall poverty and 56% of beneficiaries of the main program (*Red de Oportunidades* [Opportunities Network]), targeting extreme poverty, do not belong to this category.* This highlights the importance of improving the management of existing programs.
- 3.13 Although no significant gender difference is observed in the poverty rate (21.8% for women and 20.8% for men), gaps exist in other respects that affect women's opportunities and welfare. The malnutrition rate stands at 11.4% for preteen and adolescent girls compared with 9.5% for preteen and adolescent boys, and the teenage fertility rate is 84 per 1,000 women ages 15 to 19 compared with an average of 69 across Latin America and the Caribbean. Pre-crisis, the female unemployment rate was three points higher than the male unemployment rate, and the female employment rate was 24 points lower. Moreover, the proportion of women in better-paid sectors remains low.⁶⁴ This has been exacerbated during the COVID-19 crisis, with the impact in terms of jobs and income falling disproportionately on women.
- 3.14 The slower rate of social progress relative to economic progress observed in Panama highlights the need to continue strengthening public investment in the delivery of basic infrastructure and quality social services and to take a subnational approach to reduce these gaps⁶⁵ in a way that takes into account crosscutting themes such as gender and diversity, resilience, and climate change adaptation. The urgent need to foster equitable, sustainable, and quality access has come to the fore in the COVID-19 crisis, as it has highlighted the vulnerabilities arising out of shortcomings in service access and quality, as well as weaknesses in the information systems used to support decision-making.

⁶³ As a whole, in 2019 these programs reduced overall poverty by 2.6 points and extreme poverty by 3.1 points. Guerra Rodríguez, J. (2020): *Pobreza e indigencia por ingreso según Encuesta de Hogares de agosto de 2019*, Ministry of Economy and Finance.

⁶⁴ For example, transportation and storage, and construction, mines and quarries, in which wages are higher than the mean, are among the three activities with the smallest share of women (13%, 6%, and 4%, respectively).

⁶⁵ In general, the higher a province's per capita income, the larger the public investment received. On average, over the period 2013-2017, Panama province, the country's highest-income province, received investment per capita that was 28% above average. By contrast, the comarca of Ngäbe Buglé, with just 26% of the national average per capita income, received 70% less investment per inhabitant. Astudillo, J.; Fernández, M., and Garcimartín, C. (2019). *La desigualdad de Panamá: Su carácter territorial y el papel de las inversiones públicas*. IDB, Technical Note IDB-TN-1703. Additionally, social spending has remained fairly stable at 8.8% of GDP over the past 10 years, almost three points lower than the Latin American and Caribbean region average and half that of Chile and Uruguay (ECLAC).

3.15 With the aim of reducing inequality and poverty, and enabling human capital to contribute to the country's competitiveness, the IDB Group will continue to pursue the previous strategy's objective regarding the delivery of basic services to people living in poverty, and, in addition to the management improvements envisaged in the previous priority area, it will support the following areas: (i) expanding service access and quality, especially in the case of health care, water and sanitation, and social protection, paying particular attention to rural areas and indigenous comarcas; and (ii) initiatives to enhance the quality and relevance of the educational system at the national level and its linkages with the needs of the productive sector, prioritizing the development of new economy skills and gender and diversity considerations. The Bank will continue supporting implementation of the Gender Parity Initiative to provide women with access to opportunities under equal conditions to men and it will incorporate criteria of resilience, climate change adaptation, and greenhouse gas emissions in the development of infrastructure to support the delivery of these services.

C. Reigniting and diversifying productive activity

3.16 Although Panama offers a favorable environment for business initiatives, it has made little progress on diversifying production into higher value-added sectors relative to other countries of the region. The economic slowdown underway prior to the COVID-19 crisis already made it clear that it needed to foster activities other than construction and real estate services with the capacity to jumpstart the economy sustainably and inclusively. This lack of economic diversification has resulted in a high concentration of productive activity in the province of Panama and to a lesser extent in Colón, with considerable gaps in other regions of the country.

3.17 The country has productive activities with the potential to drive growth sustainably, create jobs, and achieve a better balance between regions. First, the logistics complex could serve as a platform for attracting investments to help the country raise its technological sophistication and integration in global value chains and enable it to position itself as a regional leader in e-commerce logistics. Furthermore, the tourism sector, which pre-pandemic had become one of the most dynamic activities in the Panamanian economy, offers opportunities for diversification through better utilization of the country's cultural and natural heritage. Lastly, in the agricultural sector, which employs approximately 14% of the labor force and on which many families in rural areas⁶⁶ depend for subsistence, there are opportunities for productivity gains and to make growth more inclusive and environmentally sustainable.

3.18 In addition to the imperative of diversifying production, there is also a need to ensure that the short-term effects of COVID-19 do not turn into lasting difficulties that erode certain sectors' capacity to recover and grow. In the specific case of tourism, the sector has been hard hit by the pandemic, with a significant risk that companies involved either directly in tourism or in the associated supply chains may disappear. Both objectives—diversifying production and avoiding a severe

⁶⁶ According to data from the National Statistics and Census Institute (INEC), it is the main source of income for 40% of the population in rural areas (68.7% in the indigenous comarca of Ngöbe Buglé, and 67.3% in the comarca of Emberá).

loss of the current productive fabric—require Panama to accompany the above-mentioned public management initiatives and delivery of basic services with actions in three key areas: competitiveness of the financial system, digitalization, and development of infrastructure and productive services geared toward environmental sustainability, resilience, and spreading economic opportunities more evenly across the country.

- 3.19 Although the financial system is one of the country's great assets, its international competitiveness and its capacity to address companies' needs, particularly those of MSMEs, has weakened. Indeed, financial services exports declined from 2.3% of GDP in 2015 to 1.7% in 2019, and although significant improvements in the depth, access, and efficiency of its institutions and financial markets were observed up until 2009,⁶⁷ they have since stagnated. This trend is a cause for concern because the financial sector is one of the activities contributing to the creation of formal jobs in Panama.
- 3.20 While the global financial industry has been evolving to adapt to markets and users, the Panamanian system has limited product diversification, with a strong concentration in a limited number of productive segments and geographic areas. In terms of credit segments, construction, home loans, personal consumption, and trade account for almost 90% of credit to the private sector, leaving little room for other activities.⁶⁸ In terms of client types, there is a strong bias toward large corporates.⁶⁹ Lastly, the portfolio has a strong geographic concentration in Panama City and the surrounding area (83% of the total). In sector terms, businesses in the tourism or agricultural sectors do not find it easy to obtain bank financing, and MSMEs located outside the capital find it harder still. Furthermore, the concentration of the banking business in one geographic area and a limited number of sectors has produced a conservative system with a limited range of products and lacking the capacity to adapt rapidly and offer innovative solutions to other sectors of the economy. All in all, this represents a bottleneck for an economic revival based on diversifying production, digital transformation, and environmental sustainability.
- 3.21 Despite having one of the highest rates of loan penetration in the region (87.7%), the country has weaknesses in terms of financial inclusion.⁷⁰ For example, the level of access to bank accounts in the provinces is 20% lower than in urban areas; access to credit by the poorest segment is 89% lower than among the population as a whole; and the percentages of women with access to accounts and bank credit are 17% and 21%, respectively, which are lower than the rates among men.⁷¹ Indigenous peoples also face barriers in access to finance owing to the lack of instruments suited to their collective non-distrainable land rights and the capacity of financial institutions to identify and analyze their portfolio on the basis of diversity criteria.

⁶⁷ IMF Financial Development Index.

⁶⁸ Data from the Superintendency of Banks.

⁶⁹ According to analysis by the World Bank Group's International Finance Corporation in 2017, the financing gap for the MSME sector in Panama was 78%, in other words, only 22% of these companies' credit demand was being met, a much smaller percentage than the regional average of 33%.

⁷⁰ World Development Indicators, World Bank 2018.

⁷¹ Global Findex Database, World Bank 2017.

- 3.22 In addition to the constraints on access to finance, there are challenges to reigniting and diversifying the economy associated with connectivity, a factor that plays a central role in fostering digital transformation and the resilience of companies both during the pandemic and thereafter. The level of digitalization of production is low, with just 26.7% of companies selling online and 28.6% having digitalized their supply chain.⁷² One of the reasons is that international broadband Internet suffers from quality issues, and there are weaknesses in companies' connections to broadband, particularly among MSMEs.⁷³ There is a significant digital divide in rural areas, with telecommunications infrastructure and fixed broadband coverage mainly concentrated in Panama City. The capacity to support growing demand may run into bottlenecks even in areas that currently have better service, making more investment in the sector necessary. A somewhat out-of-date governance and regulatory framework, limited institutional capacity among the sector's governing agencies, and a relative shortage of digital talent lead to low levels of competitiveness, service quality problems, interoperability challenges, and cybersecurity risks, all of which are holding back the development and use of products in various areas such as financial services and digital payments, and the expansion of broadband and/or fifth generation (5G) coverage in rural areas and the comarcas.
- 3.23 A third complementary area to Panama's efforts to rekindle growth and diversify the economy is the development of climate-resilient and low-emissions infrastructure that interconnects the country and facilitates market access for rural producers. Although Panama ranks 38th out of 160 economies on the World Bank Logistics Performance Index, the quality logistics infrastructure is concentrated in the central hub in the interoceanic zone, while the rest of the country lags behind.⁷⁴ The energy sector has been strengthened in recent years and has reduced its dependence on fossil fuels. However, electricity service coverage is unevenly distributed across the country, with 81% of rural homes having electricity compared with 99.6% of urban homes. Infrastructure challenges largely derive from low levels of investment outside the central region of the country, together with institutional weaknesses and a lack of planning, prioritization, and preparation of projects, which hinders private-sector involvement.
- 3.24 In addition to constraints on finance, digital connectivity, and infrastructure, there are specific obstacles to diversification and sustainable productive development of the country's bypassed regions by building on their specialization in agriculture or their potential for tourism. In the agricultural sector, the policy framework relies on price protection mechanisms rather than services such as agricultural health, resilient and environmentally sustainable productive innovations, and access to

⁷² Andean Development Corporation (CAF) (2017): "Hacia la transformación digital de América Latina y el Caribe: El Observatorio CAF del Ecosistema Digital". Caracas.

⁷³ Firm Innovation and Productivity in Latin America and the Caribbean: The Engine of Economic Development. IDB (2016).

⁷⁴ Nationally, 23.5% of roads are paved whereas in the indigenous comarcas that figure drops to 4.4%. The figure is over 30% in just four of the twelve provinces. In all, 82% of secondary and tertiary roads are in fair or poor condition, leaving some settlements relatively isolated with limited access to basic services and markets. INEC.

markets to boost productivity and reduce their environmental impact.⁷⁵ In the case of tourism, weaknesses in governance and regional planning, compounded by a lack of adequate statistics, is jeopardizing the sustainable development of the sector in the post-pandemic period. Additionally, weak institutional capacity and limited sources of finance prevent adequate management of the country's cultural and natural heritage, jeopardizing its contribution to the population's quality of life and its sustainable utilization.⁷⁶ For example, available data indicate that just 3% of international visitors to Panama visited a protected area, which is low when compared with 36% in Costa Rica.⁷⁷ The main causes identified include the lack of tourism promotion, infrastructure, and ecotourism services.

- 3.25 To contribute to the country's economic recovery and diversification based on criteria of inclusion and environmental sustainability, the IDB Group will provide technical and financial support to enable: (i) expansion of access to credit among underserved segments (women, rural areas, MSMEs), modernization of the financial sector, and development of products to support the productive fabric, in particular in the agricultural sector and tourism and their value chains, and greater financial inclusion overall; (ii) improving levels of digital connectivity to facilitate Panama's digital transformation, emphasizing institutional considerations, development of digital talent, and adaptation of infrastructure to support productivity and inclusion; (iii) developing resilient, quality, low-emissions infrastructure services that help tap the productive potential of the country's bypassed regions, bearing in mind the needs of communities and their local heritage, utilization of potential regional interconnection, and also continuing with the support for diversifying the energy matrix and for the competitiveness of the logistics sector, taking an approach permitting private sector participation; and (iv) strengthening tourism- and agriculture-specific services to boost their competitiveness, paying particular attention to the management, promotion, and sustainable utilization of cultural and natural heritage, environmental sustainability, climate change adaptation, access to markets, and public-private coordination.
- 3.26 **Dialogue areas.** A technical dialogue will be maintained concerning the extractive industries, migration, evaluation of public policies, financial transparency, social security, and citizen security and justice. In view of the importance mining has acquired in Panama, the IDB Group will provide technical support to the authorities geared toward strengthening the sector's institutional framework. In migration, the emphasis will be on identifying best practices and opportunities for integration of Panama's immigrant population. As regards public policy evaluation, experiences will be shared on the analysis of the incidence of fiscal policy on poverty and equity, in particular, given the repercussions of the COVID-19 crisis for the labor market. In the area of financial transparency, the Bank will continue to support the authorities on the adoption of measures enabling Panama to be taken off the Financial Action Task Force (FATF) "grey list" of jurisdictions with deficiencies in

⁷⁵ Agriculture alone is responsible for 95% of the country's deforestation and causes severe soil degradation. In conjunction with climate change, this activity is one of the main drivers of the country's growing water insecurity.

⁷⁶ Of the 18 public museums administered by INAC, six are currently closed, including the Reina Torres de Araúz Anthropological Museum (MARTA). The sector's weakness has also affected major heritage sites, such as the Portobelo and San Lorenzo fortifications.

⁷⁷ Statistics from Costa Rica's National System of Conservation Areas (SINAC). 2014.

their measures to combat money laundering and the financing of terrorism. Given the deteriorating financial situation of the Social Security Fund, the IDB Group will also work with the authorities on options to strengthen the pensions system. Lastly, as regards citizen security and justice, the dialogue will be geared toward strengthening and modernizing the capacities of the institutions responsible for detecting, preventing, and resolving crimes, including the utilization of digital tools and technological innovations.

- 3.27 **Crosscutting themes.** Within the agreed priority areas and the proposed dialogue areas, the potential contribution in relation to resilience, climate change adaptation and environmental sustainability, gender and diversity, and institutional strengthening will be considered. In the area of climate change and resilience, support will be sought for actions at the national and regional level to strengthen the disaster risk management governance framework and compliance with the climate targets set in the Nationally Determined Contribution, through low-emissions designs that bolster the resilience of infrastructure to climatic phenomena and foster good management of water resources, and by supporting the protection and restoration of natural capital (such as mangroves and forests). Additionally, gender aspects, diversity, and cultural relevance will be considered in interventions to help bridge gaps in rural areas and indigenous comarcas. In addition to the crosscutting aspects of public management mentioned in the first strategic area, the IDB Group will continue to pursue institutional strengthening in the various sectors with which it is engaged. The IDB Group has the potential to support private sector involvement in each of these areas, particularly in the development of financial products enabling greater financial inclusion and climate change adaptation and mitigation in the productive sector, development of the tourism industry and agroindustrial sector based on criteria of environmental sustainability, and the use of public-private partnerships, particularly for the development of digital infrastructure.

IV. PROJECTED FINANCIAL SCENARIO

- 4.1 The indicative sovereign lending scenario assumes average annual approvals of US\$465 million, totaling US\$1.861 billion over the period 2021-2024. This amount is subject to the allocation of the Bank's Ordinary Capital resources. Under these assumptions, at the end of the period the IDB's share of Panama's multilateral debt is projected to remain at 45.6%, while its share of the country's total public debt would fall slightly to 9.2%.

V. IMPLEMENTATION CONSIDERATIONS

- 5.1 **Portfolio execution.** The IDB Group's program should be addressed comprehensively, considering the instruments available, including the active portfolio. It will therefore be necessary to review operations' relevance in light of the challenges and opportunities of the post-COVID-19 context. The Bank will work in coordination with the Ministry of Economy and Finance and the sector authorities to prioritize interventions and speed up execution, seeking adequate budgetary allocations within the current fiscal constraints and continuing the ongoing dialogue with the CGR to shorten the time it takes to countersign

contracts. New projects will explore execution mechanisms that respond to executing agencies' specific capacity-building needs.

- 5.2 **Donor coordination.** Through the Country Office in Panama, the Bank will coordinate with bilateral and multilateral donors operating in the country to identify synergies and provide a coordinated response to each target sector's challenges. Specifically, the Bank will coordinate with other agencies operating in the following sectors: (i) water and sanitation, with the Development Bank of Latin America (CAF), the European Investment Bank (EIB), the World Bank, the Spanish Agency for International Development Cooperation (AECID), and the Japan International Cooperation Agency (JICA); (ii) energy, with the Fund for Development Promotion (FONPRODE); (iii) gender and diversity, with the World Bank, UN Women, the United Nations Development Programme (UNDP), the International Labour Organization (ILO), (iv) health, with the Pan American Health Organization (PAHO), the United Nations Population Fund (UNFPA), and the United Nations Children's Fund (UNICEF); (v) environment and climate change, with the Global Environment Facility (GEF); (vi) Cultural heritage, with AECID; (vii) education and early childhood, with the Organization of Ibero-American States (OEI) and UNICEF; (viii) social protection, with the World Bank, and (ix) fiscal matters, with the International Monetary Fund (IMF) to ensure complementarity of activities.
- 5.3 **Use of country systems.** The country information system, "Panamá Compra," is used to manage and supervise procurement. The small purchases and framework agreements systems are also being used. During this strategy period, the Bank will continue to work with the Government of Panama on consolidating the integrated financial information system ISTMO and the general treasury account (CUT), increasing the use of country systems in the long term. In addition, the Bank will support the CGR on improving its 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 Public Procurement Bureau in setting up an economic analysis and studies office and will provide technical assistance on specific aspects of system improvement, such as the electronic platform, framework agreements, regulatory modernization, and training, boosting the efficiency and transparency of public procurement.
- 5.4 **Environmental governance.** Panama has a solid legislative framework for basic social and environmental rights that is conducive to environmental management. The IDB will aim to support the country in strengthening its environmental and social systems in order to: (i) enhance interagency coordination, consistency, and the effectiveness of economic policies with climate change objectives; and (ii) enhance the compilation, documentation, data management, and environmental and social documents, as well as access to information in accordance with the recently ratified Escazú Agreement.

Table 1. Country systems

Use of country systems	Baseline 2020 ⁷⁸	Projected 2025	Planned actions under the country strategy
Budget	100%	100%	Dialogue
Treasury	100%	100%	Increased use of the general treasury account in operations
Accounting and reporting	21%	100%	Implementation of International Public Sector Accounting Standards (IPSAS) Technical support and increased use of ISTMO
Internal audit	5%	5%	Dialogue
External control	5%	5%	Comprehensive modernization of the CGR, improvement of processes and increased adoption of international audit and accounting standards.
Information system	100%	100%	Continuous dissemination
Shopping	100%	100%	Use of method
Individual consulting	0%	100%	Methodology for Assessing Procurement Systems (MAPS) study / analysis of national competitive bidding and individual consulting / support in implementing reverse auctions/strengthening of framework agreements.
Partial national competitive bidding	5%	100%	
Advanced national competitive bidding	5%	5%	

VI. RISKS

- 6.1 **Fiscal and financial risks.** The powerful fiscal impact of the COVID-19 crisis has pushed up the debt-to-GDP ratio significantly. Although the IMF projects that this ratio will fall rapidly over the next few years, its estimates are based on a sharp rise in tax revenues and strong economic growth (5% over the medium term). If these conditions are not met, the debt could rise to above pre-pandemic levels, with a potential adverse impact on Panama’s country risk rating and borrowing conditions. These risks are compounded by the situation of the Social Security Fund (CSS). Pre-crisis, it was calculated that the defined benefit pensions subsystem would go into deficit in 2027, but in the wake of the pandemic this will probably happen sooner, putting pressure on the public finances. There is also the risk that the country is unable to get itself taken off the FATF “grey list” in the near term. Although, unlike previous occasions, it did not lose correspondent bank relationships and there was no significant outflow of foreign deposits when it was put on the list in June 2019, this could change. In the financial sector, if the crisis drags on, the rising number of nonperforming and past-due loans could weigh on banks’ balance sheets, particularly in the case of smaller and less profitable banks. This series of risks could constrain the government’s capacity to make headway on initiatives requiring a sustained commitment of resources, such as digital transformation and delivery of basic services and infrastructure, as well as the financial system’s ability to close the credit gap for MSMEs. To mitigate these risks, the IDB Group will work with the government on financial and nonfinancial products to support: (i) fiscal sustainability, while also analyzing changes over time

⁷⁸ Reported use of internal systems for audits, external control, shopping, individual consultancy, partial national competitive bidding, and advanced national competitive bidding corresponds to their use in policy-based loans, which by their nature require the use of country systems.

- in the main indicators through the macroeconomic safeguard mechanisms currently in effect and in coordination with other donors; (ii) financial transparency; (iii) a technical dialogue on the situation of the CSS; (iv) modernization of the financial system; and (v) improvements in the efficiency of social protection programs. Additionally, progress on the COVID-19 vaccination program will be monitored, working with the authorities to identify actions where the IDB Group can support this process.
- 6.2 **Increased social vulnerability.** The crisis has highlighted the vulnerability of large segments of the population. In the absence of a rapid recovery and targeted policies to mitigate the socioeconomic impacts, this may result in widespread social unrest or conflicts between social groups. This could put pressure on public policies and delay policies with longer-term impacts, such as improving educational quality or adaptation to climate change. To mitigate this risk, the strategy puts a strong emphasis on delivering basic social services to the most vulnerable groups, which are diverse in Panama, and on increasing the effectiveness of social protection programs, accompanied by actions, particularly relating to financing, aiming to rekindle the activity of SMEs, which are the main source of jobs in the country. Leveraging tools to measure trends on social media, the Bank will also monitor possible patterns that might alert to sources of social unrest.
- 6.3 **Implementation risks.** The existing portfolio faces execution challenges that have been exacerbated by the health crisis. This calls for greater responsiveness from executing agencies to buffer the impact on projects' expected outcomes. The Bank will therefore coordinate with the Ministry of Economy and Finance to step up activities such as training, consulting services, and technical support by Bank staff to strengthen these agencies. It will also provide technical and financial support to strengthen the role of the CGR in the public investment project implementation process and explore opportunities to work with external agencies to speed up execution and generate lessons that can inform decision-making on future projects.
- 6.4 **Natural disaster risks and the effects of climate change.** Water resources are essential for the operation of the Panama Canal and for the country's electricity matrix, which is highly dependent on hydroelectric power. These two factors accentuate the economy's vulnerability to extreme climate events. Furthermore, Panama faces risks associated with deforestation, which affects key ecosystem services, such as water cycle regulation, protection against natural disasters, and soil conservation. Panama is also highly exposed to seismic risk, particularly in the west of the country. The IDB Group will seek to mitigate these risks by supporting the authorities in managing water resources, providing technical support on strengthening the governance framework for risk management, and incorporating crosscutting measures to build resilience and address natural disasters and the impacts of climate change.

ANNEX I: RESULTS MATRIX AND COUNTRY SYSTEM MATRIX

1. Results matrix

Government priorities	Priority area	Strategic objective	Expected results	Indicators	Baseline, source and year
Good governance. Rule of law, law and order	Modernizing public management	Enhance the effectiveness of the tax administration	Increased effectiveness of enforcement	Amount collected as a result of enforcement/amount selected for enforcement ¹	12.8% (Internal Revenue Office (DGI), 2019)
			Improved tax payment service	Number of hours businesses need to comply with their tax obligations	408 hours (World Bank, 2020)
		Promote the digital transformation of public administration	Increased proportion of formalities for citizens and businesses digitalized	Percentage of government formalities digitalized (%) ²	10% (AIG, 2020)
Combat poverty and inequality. Education, science, technology, and culture.	Improving the delivery of basic services	Expand access to, and quality of, social protection, health, and water and sanitation services for vulnerable population groups	Improve access to essential health services for indigenous populations	Coverage of births attended by professional personnel in the Ngöbe Buglé comarca	57.5% (CGR/Ministry of Health (MINSA), 2018)
			Increased coverage of immunization against COVID-19	Coverage of immunization against COVID-19 among population over 18	0% (MINSA, 2020)
			Increased urban wastewater treatment coverage	Households with connection to sanitary sewerage service and treatment in urban areas	407,886 (IDB, ³ 2020)
			Increased access to drinking water	Households with access to drinking water 24-hours a day year-round	84.17% (IDB, ⁴ 2017)
			Improved efficiency and targeting of social protection programs	Proportion of persons with disabilities certified under ICF ⁵ parameter nationally	2.5% (National Certification Registry, 2019)
		Number of conditional cash transfer program beneficiaries registered in the integrated beneficiary system		366,491 (Ministry of Social Development (MIDES), 2020)	
		Improve quality and relevance in the educational system	Increased school attendance in early childhood	Net preschool education attendance rate	53.2% (Multipurpose Survey, 2017)
			Increased quality of learning in primary education	Percentage of students 15 years of age attaining at least level 2 in reading comprehension	36% (Programme for International Student Assessment (PISA), 2018)
			Reduced school dropout rate	Percentage of students who complete secondary education	54.7% (Ministry of Education (MEDUCA), 2018)

Competitive economy that creates jobs	Reigniting and diversifying productive activity	Expand access to credit for underserved sectors	Improved access to credit for MSMEs	MSME financing gap (% of estimated credit demand)	78% (MSME Finance Gap-SME Finance Forum, International Finance Corporation, and World Bank, 2017)
			Increased financial inclusion of women	Percentage of women over 15 with loans from a financial institution (% of total)	7.3% (Global Findex-World Bank, 2017)
		Improve levels of connectivity and digital adoption	Increased digital connectivity in bypassed regions	Average percentage of households with fixed and mobile Internet connections in the provinces (excluding Panama and Colón)	Fixed: 16.6% Mobile: 48.4% (Multipurpose Survey, 2018)
		Develop quality infrastructure services based on inclusion and environmental sustainability criteria	Improved road connectivity in rural and indigenous areas	Percentage of road network paved in the provinces and indigenous comarcas (excluding the province of Panama, % of total road network)	20.58% (National Statistics and Census Institute (INEC), 2018)
			Shorter freight transportation dispatch times at the northern border	Average time to cross border ⁶	8 hours (National Customs Authority (ANA) and IDB, 2018)
			Increased access to electricity service	Households with access to electricity service (%)	93% (National Energy Secretariat, 2019)
			Increased share of nonconventional renewable energy sources in the energy matrix	Percentage of gross energy generation from nonconventional renewable energy sources	8.9% (Energy Secretariat, 2019)
			Increased female participation in infrastructure sectors	Percentage female participation in transportation, storage, and construction activities.	Transportation and storage: 13% Construction: 6% (INEC, 2019)
			Develop services for sustainable and inclusive growth of tourism and agriculture	Activities linked to the tourism industry rekindled	Growth in gross value-added of hotels and restaurants
		Increased number of beneficiaries of sustainable use of cultural and natural heritage		Daily visits to public museums in Panama	213 (National Cultural Institute (INAC), 2017)
				Registered visitors in protected areas	277,000 (Ministry of the Environment (MiAmbiente), 2019)
		Increased productivity, resilience, and sustainability of Panamanian agricultural producers		Percentage of producers who adopt more productive and sustainable practices and technologies	0.9% (Ministry of Agricultural Development (MIDA), 2014)
		Reduced greenhouse gas emissions		Greenhouse gas emissions (GgCO ₂ eq: Giga-gram of CO ₂ equivalent)	15,876.97Gg CO ₂ eq (MiAmbiente, 2013)

1. Annual indicator produced by the Internal Revenue Office (DGI) (annual management report by the Enforcement Department)
2. Refers to total formalities.
3. Inter-American Development Bank. Support Program for Reforms in the Water, Sanitation, and Energy Sectors II <https://www.iadb.org/projects/document/EZSHARE-1356705249-105?project=PN-L1159>.
4. Sector technical note on water supply and sanitation in Panama. Water and Sanitation Division (INE/WSA).
5. International Classification of Functioning, Disability, and Health (World Health Organization)
6. Calculated using the World Customs Organization methodology based on three classic modalities (imports, exports, and transit). Measured during a normal (non-peak) month.

2. Country systems matrix

Strategic objective	Expected outcomes	Indicator	Unit of measurement	Baseline	Baseline year	Main objective	Time distribution	CRF alignment
Increased use of country systems	Maintain use of the accounting and reports subsystem	Active portfolio using the accounting and reports subsystem	Percentage of active portfolio	100%	2020	100%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality
	Increased use of the general treasury account	Active portfolio using the general treasury account	Percentage of active portfolio	21%	2020	100%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality
	Increased use of the individual consulting subsystem	Active portfolio using individual consulting subsystem	Percentage of active portfolio	0%	2018	100%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality

Strategic objective	Expected outcomes	Indicator	Unit of measurement	Baseline	Baseline year	Main objective	Time distribution	CRF alignment
	Increased use of the partial national competitive bidding (NCB) subsystem	Active portfolio using the partial NCB subsystem	Percentage of active portfolio	5%	2018	100%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality
	Increased use of the advanced NCB subsystem	Active portfolio using the advanced NCB subsystem	Percentage of active portfolio	5%	2018	100%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality
Strengthening of country systems	CGR evaluated using the SAI-PMF methodology	SAI-PMF final evaluation report	SAI-PMF report	0	2020	1	2021	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality
	Implementation of action plan for adoption of IPSAS	Progress on implementation of the action plan	% progress on plan implementation	22%	2020	75%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality
	Implementation of action plan resulting from the MAPS evaluation (*)	Progress on implementation of the action plan	% progress on plan implementation	0%	2018	50%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality

Strategic objective	Expected outcomes	Indicator	Unit of measurement	Baseline	Baseline year	Main objective	Time distribution	CRF alignment
	Executing agencies trained in the use of International Federation of Consulting Engineers (FIDIC) contracts	FIDIC training workshops held	# workshops held	1	2018	4	At the end of the country strategy	<ul style="list-style-type: none"> - Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality

* Increased use of the accounting and reporting subsystem in IDB projects will depend on the progress of the pilot project with the Ministry of Works.

ANNEX II: MAIN ECONOMIC AND SOCIAL INDICATORS

	2014	2015	2016	2017	2018	2019	2020
Social indicators							
Population (millions)	3.9	3.9	4.0	4.0	4.1	4.2	4.3
Overall poverty rate (% of population)	25.6	23.0	22.1	20.7	-	-	-
Extreme poverty rate (% of population)	10.8	10.2	9.9	9.8	-	-	-
Gini coefficient	0.49	0.49	-	-	-	-	-
Unemployment rate (% of labor force)	4.8	5.1	5.5	6.1	6.0	7.1	18.5
Nominal GDP (billion)	49.9	54.1	58.0	62.3	65.1	66.8	52.9
Nominal GDP per capita (US\$)	12,757	13,607	14,356	15,198	15,660	15,834	12,373
Real sector ($\Delta\%$)							
Real GDP	5.1	5.7	5.0	5.3	3.7	3.0	-17.9
Real GDP per capita	3.4	3.8	3.4	4.0	2.2	1.5	-19.1
Nominal GDP	9.5	8.4	7.1	7.5	4.6	2.6	-20.7
Nominal GDP per capita	7.7	6.5	5.6	5.8	3.1	1.1	-21.8
Inflation rate (Consumer Price Index)	2.6	0.2	0.7	0.9	0.8	-0.4	-1.5
Public finances (% of GDP)							
Total nonfinancial public sector (NFPS) revenue	20.5	19.8	20.1	20.0	19.6	18.4	18.4
Total NFPS expenditure	23.6	22.0	21.9	21.8	22.4	21.5	28.5
Current expenses	15.9	15.3	15.2	15.4	15.8	16.2	21.4
Capital expenditure	7.7	6.7	6.7	6.5	6.6	5.3	7.1
Primary NFPS balance	-1.4	-0.5	-0.1	-0.1	-1.1	-1.3	-7.4
Total NFPS balance	-3.1	-2.2	-1.8	-1.9	-2.9	-3.1	-10.1
Gross public debt	36.5	37.4	37.3	37.5	39.4	46.4	69.8
External accounts (% GDP)							
Current account	-13.4	-9.0	-8.0	-5.9	-8.2	-5.2	-
Foreign direct investment	10.0	9.5	9.6	6.7	8.1	7.2	-

Source: Ministry of Economy and Finance, National Statistics and Census Institute, Superintendency of Banks. Note: NFPS = nonfinancial public sector.

ANNEX III: ESTIMATED FINANCIAL SCENARIO FOR SOVEREIGN DEBT 2021-2024

	2015-2019 Strategy*						2021- 2024 Strategy				
	2016	2017	2018	2019	2020**	Total 2015-2020	2021	2022	2023	2024	Total 2021-2024
Approvals 1/	602.0	757.0	682.0	525.0	830.0	3,396.0	521.0	440.0	450.0	450.0	1,861.0
Total disbursements	513.2	389.2	478.2	394.9	730.8	2,506.3	605.0	430.0	400.0	400.0	1,835.0
Repayments	157.5	207.5	182.8	179.1	186.7	913.6	248.6	266.6	318.2	350.8	1,184.2
Net lending flow	355.7	181.7	295.4	215.8	544.1	1,592.7	356.4	163.4	81.8	49.2	650.8
Subscriptions	1.7	0.0	0.0	0.0	0.0	1.7	0.0	0.0	0.0	0.0	0.0
Interest and fee payments	80.4	80.7	93.8	115.7	102.0	472.6	86.9	74.6	70.0	63.6	295.1
Net cash flow	273.6	101.0	201.6	100.1	442.1	1,118.4	269.5	88.8	11.8	-14.4	355.7
IDB debt balance	2,493.1	2,674.8	2,970.2	3,186.0	3,730.1		4,086.5	4,249.9	4,331.7	4,380.9	
IDB debt / Total debt (%)	11.5	11.4	11.6	10.3	10.1		9.9	9.6	9.5	9.2	
IDB debt / External public debt (%)	14.8	14.5	14.4	13.2	12.5		12.5	12.2	12.0	11.7	
Debt with IDB / with multilaterals (%)	54.6	52.4	52.7	52.6	45.6		45.6	45.6	45.6	45.6	
IDB debt/GDP	4.3	4.3	4.6	4.8	6.2		6.5	6.4	6.1	5.7	

1/ Biannual amounts defined in the Ordinary Capital resource allocation exercises.

* The country strategy transition was due in 2020. However, the government requested an extension and the existing strategy will remain in effect until 30 June 2021.

** The response to COVID-19 is reflected, and approvals through to December 2020 are included.

ANNEX IV: DEVELOPMENT EFFECTIVENESS MATRIX (SUMMARY)

COUNTRY STRATEGY UPDATE: DEVELOPMENT EFFECTIVENESS MATRIX

In August 2008, the Board of Directors approved the Development Effectiveness Framework (GN-2489) to increase the evaluability of all Bank development products. The Development Effectiveness Matrix for Country Strategies (DEM-CS) is a checklist of the elements that are necessary to evaluate a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation."

COUNTRY STRATEGY: Panama

STRATEGIC ALIGNMENT

Refers to the degree to which the design and objectives of the CS are consistent with the country development challenges and with the government's development plans and priorities.

EFFECTIVENESS

This measures whether the country strategy is likely to achieve its intended objectives, through an examination of four dimensions: (i) the quality of the diagnostics on which Bank action is based in each area of work; (ii) the quality of the results matrix for the strategy; and (iii) the use and build up of country systems.

Effectiveness dimensions	
I. Country Diagnosis - Country Development Challenges (CDC)*	Yes/No
- The CDC is comprehensive / holistic / complete	Yes
- The CDC clearly identifies the main development challenges	Yes
- The CDC presents magnitudes of the main development challenges that are based on empirical evidence	Yes
II. Priority Areas Diagnostics	%
- That clearly identify and dimension, based on empirical evidence, the priority area's specific constraints and challenges	100%
- That clearly identify and dimension, based on empirical evidence, the main factors or causes contributing to the specific constraints and challenges	100%
- That provide corresponding policy recommendations	100%
III. Results matrix**	%
- The strategic objectives are clearly defined	100%
- The expected outcomes are clearly defined	100%
- The strategic objectives and expected results that are directly related to the main constraints identified in the Diagnosis	100%
- The indicators are outcome indicators and are SMART	100%
- The indicators have baselines	100%
IV. Vertical logic	Yes/No
- The CS has vertical logic	Yes

ANNEX V: OVE COUNTRY PROGRAM EVALUATION RECOMMENDATIONS

Management's response to the Country Program Evaluation Recommendations: Panama 2015-2019

OVE recommendation	Management's response
<p>Recommendation 1: Find mechanisms to continue and strengthen the comprehensive approach to rural and indigenous areas. In particular,</p> <ul style="list-style-type: none"> i. Foster better sector and geographic coordination of interventions from the design and planning stage. ii. Recognize in the Bank's programming that the nature of these operations requires greater adaptation to the local context and entails higher costs and longer time frames for preparation, execution, and supervision. iii. To sustainably accommodate these costs, look for ways to promote and offer the country a program that balances the higher costs of these operations with lower-cost operations. iv. To make interventions more cost-effective, the viability and relevance of adapting innovative models implemented in other countries for service delivery in isolated areas (e.g., distance education in Brazil) could be explored in the Panamanian context. 	<p>Agree</p> <p>Management agrees with OVE on the importance and relevance of continuing work in rural and indigenous areas, where the Bank can add value with its interventions to improve social inclusion and opportunities for the poor. In particular:</p> <ul style="list-style-type: none"> i. The Bank will continue to foster sector and geographic coordination of interventions from the design stage during the next strategy period. Recently approved operations have already incorporated this recommendation. For example, the Universal Access Energy Program (operation PN-L1155), approved in 2019, focused from the design stage on the delivery of electricity to health centers and Bank-financed schools in rural and indigenous areas. ii. During annual programming exercises with the authorities, the Bank will identify interventions for which additional resources and longer time frames to support design and execution are warranted due to their complexity. iii. The priorities agreed upon between the Bank and the government under the new country strategy and the annual programming exercises will be used to determine which loan modality or intervention type is best to address the country's development objectives and will be supported by the Bank. The Bank will continue to offer an array of loan modalities, based on the annual allocation of resources for the country. iv. Management will continue exploring innovative models for service delivery in isolated areas. For example, the Indigenous Entrepreneurship and Financial Inclusion Program (operation PN-L1157) was based on groundbreaking models from Chile, Peru, and Colombia, while CT/INTRA intraregional technical cooperation operation PN-T1218 explored the viability and relevance of adapting to the Panamanian context innovative models of service delivery in isolated areas implemented in Guatemala. Several operations focusing on rural and indigenous areas will be executed during the next strategy cycle. Lessons learned from these operations will be taken into account as new operations are programmed, which could lower the cost of these interventions.

OVE recommendation	Management's response
<p>Recommendation 2: Systematically document the lessons learned from this experience for use in the Bank's work with indigenous communities in other countries.</p>	<p>Agree</p> <p>Management agrees with OVE on the importance of documenting the lessons learned from the Bank's work with Panama's indigenous communities. This work has produced a valuable, innovative way of partnering with these communities that considers their unique organizational and cultural features as well as the execution challenges that arise from limited access to these parts of the country.</p> <p>The Bank will document the strategy it has used with indigenous peoples in Panama since 2015 and publish a technical note on territorial development with identity, which has been the approach implemented. In addition, it will use existing operational tools, specifically project completion reports, to document strategic and operational lessons learned from interventions.</p>
<p>Recommendation 3: In developing a new strategy, redouble efforts to find a general solution to crosscutting challenges and, particularly, promote dialogue and offer necessary technical and financial support to strengthen the CGR's role. The Bank has considerable experience in supporting the strengthening and modernization of supreme audit institutions in the region, which may be offered to the Government of Panama as part of the next strategy (Appendix IV of the Annex, Box 4.1).</p>	<p>Agree</p> <p>The IDB Group agrees that it should push ahead with its efforts to find a general solution to crosscutting challenges for loan execution. It will continue to promote dialogue and offer the necessary technical and financial support to strengthen management of the nonfinancial public sector and its oversight and audit institutions. The results achieved will depend on interest at, and economic policy constraints faced by, the various public-sector institutions with this agenda.</p>
<p>Recommendation 4: Approach sustainability more systematically from the design stage of operations (e.g., infrastructure maintenance and availability of human resources), and, given that the institutional capacity of local counterparts plays an important role, heighten the emphasis on institution-strengthening and management activities, components, or operations. Accordingly, Recommendation 3 of the previous evaluation remains relevant.</p>	<p>Agree</p> <p>The analyses conducted as part of preparation of the new strategy have identified institutional quality as a key factor for development in Panama. Therefore, in its dialogue with the government, the Bank will promote support for improving public management through operations or specific components, and/or technical assistance.</p> <p>At the operational level, the Bank will continue to include, from the design stage, actions that ensure a commitment to (i) maintaining the public infrastructure financed and (ii) strengthening the institutional capacity of the execution units, based on the analyses conducted as part of operation preparation. However, in view of the fact that the Government of Panama has centralized hiring of execution unit staff using its own resources, it will be difficult to ensure the availability/continuity of human resources mentioned by this recommendation.</p>

OVE recommendation	Management's response
<p>Recommendation 5: Maintain and expand value-added service offerings for the private sector in Panama. In particular, (i) leverage the appetite for technical assistance in the financial sector in certain areas to explore products with components aligned to the country's development priorities; and (ii) look for opportunities to add value in sectors with high development potential for the country, leveraging the IDB Group's reputation.</p>	<p>Agree</p> <ul style="list-style-type: none">i. IDB Invest has resources and ample experience providing technical assistance on topics related to gender, climate change, and small and medium-sized enterprises in Latin America and the Caribbean, which will enable it to explore products with components aligned to the country's development priorities.ii. In terms of looking for opportunities to add value in sectors with high development potential for the country, IDB Invest will explore options to replicate and adapt to the Panamanian market solutions developed by IDB Invest and proven to work in other markets. One of the pillars of the new country strategy, now in preparation, is the strengthening of dynamic sectors of the Panamanian economy to enhance competitiveness and increase the economic complexity of the goods and services produced in the country. IDB Invest has the capacity to support the country in these sectors, which include infrastructure, agroindustry, manufacturing, and services (including sustainable tourism).