

Panama

CONNECTING THE DOTS



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This Central American nation has embarked on a bold drive to position itself as a first-class business destination.

Panama has long served as a major crossroads connecting North and South America and the Atlantic and Pacific oceans, and it is taking its business credentials to the next level.

Now in its fifth year, the government of President Ricardo Martinelli has cut taxes, boosted business incentives and improved air, sea and canal capacity to establish the country as a major magnet for foreign and U.S. investment and trade. Panama's economic growth in 2012 topped 10%, with a further 8.5% forecast for 2013, a performance envied throughout the region. Remarkably, unemployment stands at just 4.8%.

Before he turned to politics, Martinelli, a business graduate from the University of Arkansas, was a successful entrepreneur who owned Panama's largest supermarket chain. Elected president with over 60% of the vote in 2009, he intends to make Panama as business friendly as possible. "I am not a politician, and most of the members of my cabinet are businessmen," says Martinelli.

Panama has long used the U.S. dollar as its national currency, allowing international businesses to operate without fear of currency risk or devaluation. In 2011, the government finalized a free trade agreement with the U.S., lowering all import and export duties to 10% or less, and implemented new trade agreements with the EU. The Martinelli government has also slashed taxes on individuals by an amount ranging from 15%-25%, with

the first \$12,000 fully tax exempt, and has cut corporate taxes from 30% to 25%.

The government's plan for \$15 billion invested over the five-year term in strategic sectors such as infrastructure, education, health, and research and development, in addition to a \$5.2 billion Panama Canal expansion project, have been key to the growth agenda.

By the end of this year, the Martinelli government will have spent almost \$3 billion on new roads and bridges and the reorganization of the traffic system in Panama City. It will also have spent \$870 million on education, \$1.25 billion on new hospitals and \$1.8 billion on the country's first subway line.

International companies locating in Panama can take advantage of even greater incentives, including locating in the country's Colón Free Trade Zone, which, according to local officials, is now the world's second-largest free trade area. "If you are in the free zone, you pay no taxes," says Martinelli, "and if you are in the port business, you pay by the movement of containers; you do not pay income tax."

Having spent his term perfecting his vision of Panama, President Martinelli is a man on a mission. "This is one of the few countries in the world that can jump from third-world to first-world status," he says. "We only need the opportunity to do so." ♦

An Ambitious Agenda to Drive Growth

Now over three years into an audacious \$14 billion, five-year government investment plan, the Republic of Panama is already enjoying the fruits of improved infrastructure, a more efficient tax and regulatory environment, and growing revenues from trade and logistics services, tourism and sustainable agriculture.



In less than four years, Panama has built or improved its roads, hospitals, schools, airports, ports, utilities, conference facilities, a free trade zone and a new subway system for Panama City. The Panama Canal, which already carries 5% of the world's shipping, is being expanded to accommodate more and larger ships—improvements which will triple Canal-based annual revenues to over \$4 billion a year by 2022.

Equally important, greater fiscal transparency, a fairer, simpler tax code and low unemployment—coupled with 10% growth—have since 2010 earned Panama investment-grade ratings and upgrades from Fitch, Moody's and Standard & Poor's, helping to attract greater foreign investment. Bringing new people, money and companies to the country is one of the key goals of the current drive for accelerated growth.

"Investment and cooperation are based on trust," stresses Roberto C. Henriquez, minister of the Presidency, a seasoned diplomat and businessman whose ministry oversees all presidential affairs. "No economic agent will jeopardize hard-earned money in a country they cannot trust, so we have tried to create an environment where they feel their investment is safe."

Today, despite the current investment drive, the country's debt to GDP ratio has fallen to under 40%, lower than

that in many South American and even European countries. Inflation is currently running at over 4%—higher than the government would like. However, economists and officials believe that inflation is already moderating, given that commodity prices (a major component of the infrastructure improvements planned to 2014 and beyond) have fallen dramatically this year and are likely to remain stable or decline further if Chinese and Indian demand continues to soften, as many economists predict.

Key to Panama's longer-term future is the social stability that can only be maintained through job creation. Today, the country enjoys an unemployment rate of just 4.8%, one of the lowest in the region. Future development very much aims at reducing economic deprivation wherever possible among the country's 3.6 million citizens.

"This investment plan has created both direct and indirect jobs," says Henriquez. "Some of the investment has been made in areas of high unemployment because we want jobs created for people who have never had a certain source of income, and this is generating new possibilities for consumption and saving." Over the longer term, this approach will hopefully lead to the creation of hundreds of thousands of new jobs, a stronger internal market and more sustainable growth.

"Panama has the opportunity to consolidate itself as the logistics hub of the Americas."

Frank de Lima,
Minister of Economy and Finance

A drive is also well under way to encourage foreign nationals to relocate to and to live, work and invest in Panama. The Martinelli government has enacted unique laws allowing citizens of nearly 40 countries to apply for permanent residency and for work permits immediately upon arrival in Panama. Many are drawn by the country's political stability and its dollar-denominated economy. Eligible countries include the U.S., Canada, nearly all European countries and the more developed economies of East Asia and South America.

"This country now has a very international flavor," says President Martinelli. "We attract people from everywhere, and those who worry about insecurity and do not believe in their government or their currency, come to Panama."

Trade with other nations, however, remains absolutely crucial to Panama's future success—and this involves creating and maintaining a world-class transport and logistics infrastructure. Today, a well-developed business service sector accounts for nearly 80% of the nation's economy. These services

include the Panama Canal, banking and insurance, the Colón Free Trade Zone, container ports and flagship registry.

At the very heart of the Martinelli government's audacious five-year investment plan is its goal to create in Panama a world-class logistics, transport and distribution hub that will draw on trade from all over the globe. Air, rail, port and canal links, combined with conferencing, warehousing and financial centers, will support all aspects of value-added logistics.

"We are trying to emulate what Singapore did with so much success from a logistics perspective," explains Frank de Lima, the minister of Economy and Finance, a Boston University business and finance graduate who also studied at Harvard University. "Panama has the opportunity to consolidate itself as the logistics hub of the Americas."

The government also hopes that Panama's growing presence in manufacturing and mining will generate more jobs. The country already manufactures spare aircraft parts, cements, adhesives and textiles. Its leading exports are bananas, shrimp, sugar, coffee and clothing.

What is coming may be even bigger, for Panama is also home to huge potential copper reserves. A Canadian mining company, First Quantum, is investing in what will likely become a massive copper mine, going operational by 2016. "The investment required for the mine is close to \$6 billion, which is even greater than the money invested in the Panama Canal expansion," says de Lima.

Tourism, too, is on the rise, having doubled since 2010, thanks to growing air transport links and more relaxed visa procedures. With coastlines on both the Caribbean and the Pacific and the second-largest rainforest after the Brazilian interior, Panama has a lot to offer discerning tourists looking for pristine beaches and tranquil mountains.

This small yet diverse country, bridging both two continents and two oceans, has already embarked on a renaissance that will become increasingly clear in the years ahead. ♦

2013: Spotlight on Panama

A chain of international events and celebrations has focused attention on the growing array of interesting business, cultural and tourism activities Panama now offers.

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Tourists visit a waterfall at Chiriqui Viejo river, one of Panama's many natural attractions.

Panama is emerging as a must-see international destination in its own right. Thanks to its abundant natural beauty and ready access to two oceans, as well as an infrastructure that its impressive public investment program has radically improved, the country has attracted many international hotel and resort chains to establish a footprint here.

"In 2012, Panama welcomed 2 million tourists and earned \$3.7 billion in foreign exchange from tourism," says Ernesto Orillac, the vice minister of tourism and a former commercial director of one of Panama's leading tour operators. "We expect around 3 million tourists by 2015 and believe foreign exchange earnings will rise to about \$6 billion."

The country has a lot to offer, with pristine beaches, virgin rainforest, the Coiba National Park and other attractions. It recently opened a unique Museum of Biodiversity, designed and donated to Panama

by U.S. architect Frank Gehry. Hilton, Marriott, Ritz-Carlton, Sheraton, Waldorf Astoria and Westin have all opened hotels or resorts in Panama.

Near Panama City, a \$680 million expansion has transformed Tocumen International Airport into a regional hub connecting over 65 cities in America and Europe, and the airport is expected to be handling 18 million business and tourist passengers annually by 2016.

"We keep investing in our infrastructure, and that really helps if you want to have a long-term vision," explains Juan Carlos Pino, the general manager of Tocumen International Airport.

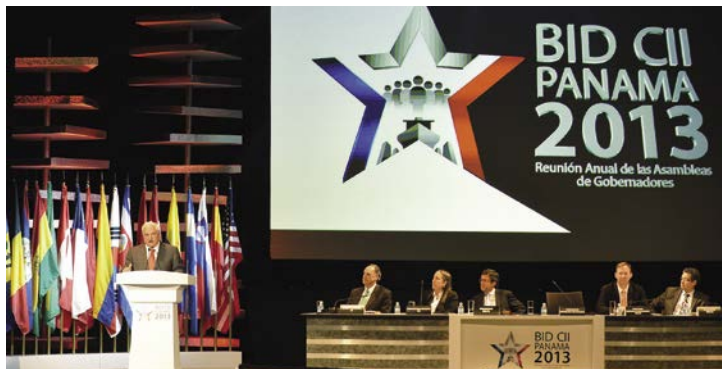
This year Panama is celebrating the 500th anniversary of Spanish explorer Vasco de Balboa's first exploration of the Pacific Ocean. March saw the country host the annual Inter-American Development Bank meeting, while autumn will bring the 22-nation Ibero-American Summit and the 6th International Congress of the Spanish Language to Panama City.

Thanks to the Martinelli government's huge investment in infrastructure, the country now attracts such important meetings. The new Amador national convention center overlooks the scenic Panama Canal and can host events for over 10,000 people.

"This is a great environment," declares Panamanian President Ricardo Martinelli. "This is the place to be, the place to live and the place to invest."

Perfecting Its International Position

Today, Panama has achieved much greater integration with the global economy, and it now benefits from favored trade and tax arrangements with the U.S. and other major economies. This provides the country with a platform to attract greater investment and promote growth.



Panama's President Ricardo Martinelli delivers a speech during the inauguration session of the IDB Annual Governors Meetings in Panama City, held in March 2013.

In the last few years, the Republic of Panama has taken two decisive steps toward achieving its goal of becoming a major regional magnet for international trade and investment. In October 2011, the U.S. Congress approved and President Obama signed the Trade Promotion Agreement with Panama, which dramatically cut import and export levies between the two countries. They have negotiated a further tax information exchange agreement. Panama has signed free trade deals, as well as Tax Information Exchange Agreements and Double Taxation Agreements, with Canada, Chile, China, Singapore, the EU and a host of Latin American nations.

"We have signed treaties with many countries and are opening the country to trade pacts with the U.S. and Europe," says Panamanian President Ricardo Martinelli, the chief architect of Panama's current drive for growth and investment. "We have also gained direct investment for the country and are attracting people to come live here."

Despite the current low-growth outlook for much of the world economy, Panama won a record \$2.8 billion in foreign direct investment in 2012, the best performance measured as a proportion of GDP for any country in Latin America.

The combination of free trade deals, low taxes, 10% GDP growth and the country's strategic geographic position has encouraged over 120 foreign companies to move their regional headquarters to Panama, including Adidas, Hewlett-Packard, Caterpillar, Procter & Gamble and L'Oréal. Improving business

conditions have also boosted the BVPSI, Panama's stock exchange, to new highs.

"We see the exchange exploring opportunities to become a regional market and an offshore center for funds that are today scattered all over the world," explains Roberto Brenes Perez, the general director of the BVPSI. "We are also trying to create a regional debt market with the countries of Central America."

"We have signed treaties with many countries and are opening the country to trade pacts with the U.S. and Europe."

President Ricardo Martinelli

Capitalizing on its strategic position at the Atlantic edge of the Panama Canal, the country's Colón Free Trade Zone is home to over 1,700 companies and generates at least \$6.5 billion in exports and re-exports from all over the world. While Colón has been open for business since 1948, the Panamanian government is investing heavily in a new enterprise zone, the Agency Panama Pacifico (APP), on the opposite Pacific coast, meant specifically to promote local manufacturing and exports.

Established just last year, the APP already employs some 9,000 people. Through this agency, the Panamanian government offers workers training in computer and technology skills and seeks to promote the hiring of as many local people as possible. The main goal is to encourage international companies to establish

value-added production in Panama, rather than simply exporting semi-finished goods.

"We are growing at a rate of about 5,000 employees per year," says Olmedo Alfaro, a former entrepreneur who is now Administrator of the APP. "Here we do not import to re-export, but are developing a manufacturing zone to label goods as 'made in Panama'." Alfaro encourages international firms to come and set up shop and offers them a flexible timeline for hiring a majority of locals to work for them.

Tocumen International Airport serves another key role in Panama's emerging regional logistics and production hub. Already the largest airport in Central America, it is slated to overtake even those of Brazil and Mexico by 2014. Greater airport capacity is an absolute necessity for increasing international business travel. Panama has already built a second runway at Tocumen and is also building a new 915,000-square-foot terminal.

"We are dealing with 7 million passengers already, but I am preparing for 9 million by the end of this year and eventually for 15 million," predicts Juan Carlos Pino, Tocumen's general manager. "We are also handling 100,000 tons of cargo per year."

With three other new airports also recently completed, Panama's transport and logistics capacity is at last beginning to properly serve its unique position as a global crossroads for trade. ♦

A New Era for the World's Greatest Waterway

First opened for business back in 1914, the Panama Canal is currently undergoing a \$5.25 billion expansion project scheduled for completion in 2015. This expansion offers vast potential to position Panama as a world-class international business center.



“Even today, before the work is complete, our Canal already handles over 5% of the world’s entire maritime trade,” declares President Martinelli, whose bold leadership has guided the current expansion. In fact, ships passing through the Panama Canal carry goods to over 160 countries and 1,700 ports worldwide.

That capacity will grow dramatically with completion of the expansion project in 2015, allowing the passage of more and larger ships. The engineering involved is daunting: the construction of two massive new sets of locks on the Pacific and Atlantic sides; the widening and deepening of existing navigation channels in Gatun Lake; the deepening of the Culebra Cut; and four dry excavation projects to create an additional 3.8-mile-long shipping access channel.

Not only will these enhancements contribute almost \$4 billion to Canal revenues within 10 years, they will create further billions in international demand for value-added port facilities, as well as storage and logistics services. “The investment will double the Canal’s maximum sustainable capacity and improve productivity and efficiency,” says Jorge L. Quijano, an engineer by training and the chief executive officer of the Panama Canal Authority, the government entity with exclusive authority over all aspects of its operation and management.

The Martinelli government also wants to enhance Panama’s position as a regional powerhouse providing

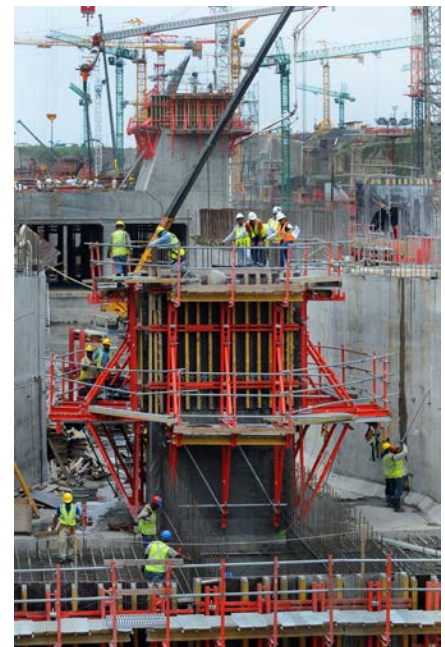
integrated facilities to all those trading with nearby Latin American countries. Half of all European exports into Central America already arrive through the country’s Caribbean coastal ports.

“We want to be the main gate of commerce for the entire region,” says Roberto C. Henriquez, minister of the Presidency, who is closely involved in all issues and projects President Martinelli deems important. “To strengthen our regional position, our country will have to further strengthen its logistical capabilities.”

The Canal expansion will also open new global markets that its original, smaller maritime infrastructure simply could not accommodate. Given the persistently high global oil prices over recent years, liquefied natural gas, compressed and carried by large oceangoing vessels, has become a cost-effective alternative, not least for Asian markets lacking their own petroleum resources.

Strategically positioned between the gas-hungry markets of China, India, Korea and Japan and the newly tapped gas fields off Africa’s west coast, the expanded Panama Canal will certainly become the main conduit for this rapidly growing trade. During 2013 and 2014, 58 new, very large specialized ships carrying nearly 5 million cubic feet of liquefied natural gas apiece are expected to enter fleet service, according to the 2013 LNG Shipping Market Review.

Growing maritime trade in Panama will generate greater demand for all manner



of services for transshipping, warehousing, storage and distribution. The country is preparing to offer an enhanced logistics network that will boost its services conglomerate.

“Panama has evolved from a transport route to a business center for the region, and the Canal expansion improves its competitiveness,” Quijano concludes. “It further reinforces the country’s strategic position.”

The coming months will see the construction of the new locks and the arrival of the huge new lock gates, all leading to a grand celebration next year when an expanded Panama Canal enters its second century of service. ♦

Creating a Knowledge Economy

With Panama's ambitious five-year investment plan already well under way, the government is taking steps to improve educational standards and foster the science and technology skills that are vital to transforming the nation into a regional hub for research and innovation.



The City of Knowledge hosts a variety of businesses as well as scientific and academic organizations.

Incentives and opportunities for education in Panama have grown dramatically in recent years, with school enrollment up a whopping 19% since 2012. According to government officials, every student in the country now receives a free scholarship and a free laptop computer. The government has built new schools and libraries, and trained some 45,000 teachers to teach the students how to use computers.

Panama's government makes a great effort to ensure that access to high-quality education does not end at the city limits of the main urban centers. "We have tried to make this a business for poor parents, especially in indigenous areas, to send their kids to school because they can collect money for doing so," explains President Ricardo Martinelli. "We give them school supplies and we pay for the food eaten at school. So now you have a well-fed child and you don't have to buy books."

Panama is restructuring its higher education system, consolidating 127 existing universities into 100 larger and better-funded ones, as well as adding and improving science, mathematics, technology and business courses. Today over 5,000 Panamanians have been given scholarships to study at overseas universities, many of them in the U.S. Some U.S. universities, including Georgia Tech, have set up dual programs allowing Panamanian students to do

their MBA studies in the U.S. and then return to Panama to complete their thesis, with professors based in Panama to guide them.

These educational improvements have fostered a growing ability to offer foreign companies the skills required to do business in Panama. "Businesspeople find a labor market here with a skilled population ready to compete at the highest levels," says Roberto C. Henriquez, minister of the Presidency.

One major success story arising from public and private investment is the country's *Ciudad del Saber*, or City of Knowledge, located opposite the Panama Canal and just minutes from downtown Panama City. Built on the site of the old Fort Clayton U.S. Army base, the City of Knowledge is a campus of some 200 buildings that host a wide array of businesses and scientific and academic organizations. The idea is to create a knowledge hub of sufficient mass to serve the international companies operating in Panama, and also to attract new investors.

"We have received international support to launch projects from the Inter-American Development Bank, the EU, the World Bank and others," declares Jorge Arosemena, the executive director of the City of Knowledge and a professor of sociology at the University of Panama. "Most of the research that takes place here is clearly geared toward reaching

out to the international market."

The City of Knowledge has already achieved considerable accomplishments. It recently won a grant from the Bill and Melinda Gates Foundation for developing a full-body microwave scanner to cure malaria. Now the main regional center for UN organizations and a growing host of NGOs, the City of Knowledge also coordinated the response to help victims of the 2010 Haiti earthquake disaster.

The Martinelli government has structured its higher-education goals to support the country's growing role as a regional and eventually a global logistics center, thanks to improved infrastructure, growing airport and port capacity, and the expansion of the Panama Canal. Education, to a great extent, should focus on the skills that enterprise requires.

"We support the Panama Canal Authority in identifying its needs and sending students to universities so they are ready to replace those who are going to retire," says Dr. Ruben Berrocal, who heads the National Secretariat for Science, Technology and Education. Clearly, improving skills and strengthening education are vital to Panama's success as a major international business center. ♦

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The sponsors of this report have provided all statistical data.