in the social lives of most Panamanians. An individual without kin to turn to for protection and aid was in a precarious position. Loyalty to one's kin was an ingrained value, and family ties were considered one's surest defense against a hostile and uncertain world. This loyalty often outweighed that given to a spouse; indeed, a man frequently gave priority to his responsibility to his parents or siblings over that extended to his wife.

Co-resident parents, children, and others living with them constituted the basic unit of kinship. Family members relied upon each other for assistance in major undertakings throughout life. Extended kin were important as well. Grandparents, uncles, aunts, and cousins faithfully gathered to mark birthdays and holidays together. Married children visited their parents frequently—even daily. In some small remote villages and in some classes (such as the elite), generations of intermarriage created a high measure of interrelatedness, and almost everyone could trace a kinship link with everyone else. Co-residence, nonetheless, remained the basis for the most enduring ties an individual formed.

A significant portion of all marriage unions were consensual rather than contractual. A formal marriage ceremony often represented the culmination of a life together for many mestizo and Antillean couples. It served as a mark of economic success. Grown children sometimes promoted their parents' formal marriage. Alternatively, a priest might encourage it for an elderly sick person, as a prerequisite for receiving the rite of the anointing of the sick.

The stability of consensual marriages varied considerably. In rural areas where campesinos' livelihood was reasonably secure and population relatively stable, social controls bolstered informal unions. Mestizos themselves made no distinction between the obligations and duties of couples in a consensual or a legal marriage. Children suffered little social stigma if their parents were not legally married. If the union was unstable and there were children, the paternal grandparents sometimes took in both mother and children. Or, a woman might return to her mother's or her parents' household, leaving behind her children so that she could work. Nevertheless, there were a significant number of female-headed families, particularly in cities and among the poorest segment of the population.

Formally constituted legal marriage was the rule among the more prosperous campesinos, cattle ranchers, the urban middle class, and the elite. Marriage played a significant role for the elite in defining and maintaining the family's status. A concern for genealogy, imputed racial purity, and wealth were major considerations. Repeated intermarriage made the older elite families into a broadly interrelated web of kin. As one upper-class wife noted, ". . . no member of my family marries anyone whose greatgrandparents were unknown to us."

Men were expected to be sexually active outside of marriage. Keeping a mistress was acceptable in virtually every class. Among the wealthier classes, a man's relationship with his mistress could take on a quasi-formal, permanent quality. An elite male could entertain his mistress on all but the most formal social occasions, and he could expect to receive friends at the apartment he had provided for her. Furthermore, he would recognize and support the children she bore him.

The ideal focus for a woman, by contrast, was home, family, and children. Children were a woman's main goal and consolation in life. The tie between mother and child was virtually sacrosanct, and filial love and respect deeply held duties. Whatever her husband's extramarital activities, a woman's fidelity had to be above reproach. An elite or middle-class woman derived considerable solace from her status as a man's legal wife. Nevertheless, middle-class and more educated women often found their traditional role and the division of labor irksome and were particularly offended by the diversion of family funds into their husbands' pursuit of pleasure.

Campesinos, too, divided social life into its properly male and female spheres: "The man is in the fields, the woman is in the home." As a corollary, men were "of the street" and able to visit at will. Women who circulated too freely were likened to prostitutes; men who performed female tasks were thought to be dominated by their wives.

Childrearing practices reinforced the traditional male and female roles and values to a greater or lesser degree among all classes. Boys were permitted considerably more latitude and freedom than girls. Girls were typically tightly supervised, their companions screened, and their activities monitored.

Because children were deeply desired, their birth was celebrated, and a baptism was a major family event. The selection of godparents (*padrinos*) was an important step that could have a pronounced influence on the child's welfare and future. It resulted in a quasi-kinship relationship that carried with it moral, ceremonial, and religious significance, and broadened family ties of trust, loyalty, and support.

Parents tried to choose for their children godparents whom they respected, and trusted, and who were as high on the social scale as possible. A certain degree of formality and ceremony was expected of godparents in social interaction, but the bonds primarily involved protective responsibility and a willingness to render assistance in adversity.

Campesinos followed two distinct patterns in choosing godparents. The parents might choose a person of wealth, power, or prestige, thereby gaining an influential protector. Such a contact could give a parent the confidence to launch a child into an alien outside world, in which he or she might have little personal status or experience. By contrast, among some campesinos there was strong informal pressure in the opposite direction. They believed it was inappropriate to ask someone of higher economic status to act as a godparent, so they sought out instead a relative or friend, especially one who lived in the same area. The choice here tended to reinforce existing social ties and loyalties.

Rural Society

The opening of the trans-isthmian railroad in the mid-nineteenth century and the Panama Canal early in the twentieth century reinforced the distinctions basic to Panamanian society: the dichotomies between rural and urban inhabitants; small-scale, mixed agriculturalists and larger cattle ranchers; the landless and landowners; and mestizos and whites. By the late 1980s, urban-based control over rural lands was considerable. The metropolitan elite not only had substantial rural landholdings, but monopolized pivotal political posts as well. Wealthy city dwellers also controlled food-processing and transportation facilities. For the bulk of the mestizo peasants, though, limited population and ample reserves of land made elite control of resources less onerous than it might have been, as did the fact that urban elites tended to view their holdings less as agricultural enterprises than as estates in the countryside.

Traditional slash-and-burn agriculture was the basis of rural livelihood for most human settlement on the isthmus (see Agriculture, ch. 3). All able-bodied household members were expected to contribute to the family's support. The peasant family was a single production and consumption unit. There was a marked division of labor by sex, and most of the work associated with crops and planting was done by men. Mestizos recognized the significant contribution children made to the agricultural output of a household. Boys and girls gradually assumed responsibilities for assisting with the duties deemed appropriate to their gender. As children, especially boys, grew older, they received part of the income from the sale of crops or part of a field that was "in their name."

Agricultural production was geared to the household's consumption. A family typically kept some livestock and planted a variety of foodstuffs, of which maize was the principal crop. Peasants gained temporary access to land by entering an agreement to clear and maintain cattle pastures for absentee landowners. A family would agree to clear a stand of forest (ideally secondary growth) and plant it in crops for one to two years. At the end of the cycle, they would often seed the plot with grasses before moving on to a new site. Peasants also owed landowners a minimal number of days in labor each year. They faced further demands on their labor to build and maintain communal buildings, such as churches and schools, and to assist with certain public works required by the government.

Since the 1950s, however, traditional slash-and-burn farming and the system of social relations it supports have been in the throes of change. Increasing population pressure, the rapid expansion of cattle ranching, and production of a variety of other cash crops in the interior provinces have put pressure on the land base necessary to maintain slash-and-burn agriculture while preserving the tropical forest. Improved transportation has been accompanied by a rapid expansion in cattle ranching in regions hitherto inaccessible. The process as a whole has meant an increasing consolidation of landholdings and displacement of traditional small-scale farmers engaged in mixed crop and livestock production. The number of farms classified as family owned and operated has declined, in favor of larger units worked by agricultural laborers. This pattern has been accompanied by an increase in and intensification of land disputes.

The consolidation process has been particularly intense in the lowlands of the Pacific coast and in Colón Province southwest of the city of Colón. In these regions, the expansion of the road network and the increasing number of all-weather roads have given potential cattle ranchers access to the large urban beef markets in Colón and Panama City. Cattle ranches grew five-fold in size in the hinterlands of Colón Province in the 1960s. Similar forces had a comparable impact on the Pacific coast, where cattle ranching increased by more than 400 percent from the 1950s through the 1970s, and land values tripled.

The increased demands on the land base affected peasant farmers on many levels. Growing population pressure and the felling of most untouched stands of tropical forest meant a decrease of hunting and, therefore, of animal protein in the family diet. Peccary, deer, and iguana, once relatively common supplements to the mestizo diet, were less available. The same process limited the forest products available for home construction and firewood. Ironically, the expansion in cattle ranching limited the ability of small-scale farmers to keep larger livestock. The purchase price of cattle rose;

Mountainous countryside in Chiriquí Province
Courtesy Organization of American States

and, because increased planting meant that animals could not forage as freely as before, they had to be penned or fenced. Finally, where drought-resistant pasture grasses were seeded, the forest itself regenerated much more slowly—limiting still further the land's ability to support an expanding population of both cattle ranchers and small farmers.

The decline in the land available for slash-and-burn agriculture and the increase in cash cropping also drew peasants more deeply into commercialized agriculture in the 1980s. At the same time that small farmers faced declining harvests and increased pressure on the family's subsistence base, they were forced to compete in markets for cash crops where the price was largely determined by larger-scale producers. Most of their production of cash crops was sporadic and in response to unpredictable situations. Difficulties in marketing placed small producers at a further disadvantage.

Sugarcane provides an instructive example. Farmers often planted sugarcane as a second-year crop in the fields they had cleared. The crop was pressed on the draft-animal presses some families owned and used for home consumption. As transportation improved, more small farmers gained access to large-scale, commercial sugarcane mills and had the option of growing sugarcane on contract for the mills. Although this opportunity offered the cultivator a possible source of more reliable income, small farmers were disadvantaged in a number of ways. Planting cane precludes using a plot for foodstuffs during the second year of cultivation. In addition, it requires hired labor, and small-scale producers were hard pressed to offer wages competitive with those that larger farmers or the mills themselves could pay. Finally, small farmers were unable to control the timing of their harvesting, which is essential for gaining optimal yields, because producers had to cut and transport their harvest whenever they were able to contract laborers and truckers for hauling the crop to the mill.

By the late 1980s, peasant families had become vastly more dependent on the money economy. In many regions, consumer goods replaced the traditional craft items produced at home, and hired labor was used in preference to labor exchange among households. Neighbors previously linked through myriad ties of exchange and interdependence were now bound by their common link with external markets. The amount of cash purchases families had to make rose dramatically: corrugated roofing replaced thatch, metal cookware replaced gourds and wooden utensils, nails served instead of vines as fasteners, and, in rare instances, gas stoves were used instead of wood-burning ranges.

Peasant families had a variety of subsidiary sources of income at their disposal. Men and women alike had opportunities to earn a little cash income. Women husked and cleaned rice for neighbors who could afford to pay, sewed, made hats, cooked, and washed clothes, while men made furniture. Those fortunate enough to own draft animals or trucks hauled goods for other farmers. Depending on location, season, and a variety of other factors, there was occasional demand for casual laborers. Such options represented a "safety net" that farmers took advantage of when crops failed or harvests were short. Nevertheless, nonfarming sources of income did not represent a viable alternative to agriculture for most families.

The general increase in cash in circulation affected various segments of the rural population differently. Younger or more highly educated and trained workers were able to compete for better-paying jobs and thus outearn their parents. Despite this, the impact on family life was cushioned because parents never counted on controlling their grown children. In one sense, families were better off because well-employed children were better able to assist their elderly parents. Where the increased cash purchases included milled rice, women were spared the arduous task of husking and milling rice themselves. Educational opportunities benefited all able to take advantage of them. Women gained in particular from the increase in employment opportunities for primary-school teachers.

In addition to peasant farmers and ranchers, Panama had the core of a rural educated middle class by the mid-twentieth century. Frequently educated at the teachers' college in Santiago, in the province of Veraguas, these educated sons and daughters of more prosperous agriculturalists and small merchants were of marginal influence in comparison with the urban elite. Long excluded from any effective role in the nation's politics, they proved a bulwark of support for the Torrijos regime (see The Government of Torrijos and the National Guard, ch. 1).

Land reform legislation drafted under the influence of the Alliance for Progress in the early 1960s recognized the peasants' right to land (see The National Guard in Ascendance, ch. 1). Nevertheless, the law's consequences in the countryside were often unforeseen. The plots allocated under the law were usually too small to support slash-and-burn agriculture; they did not allow sufficient land for fallowing. And, for a substantial portion of peasant families, the cash outlay required to purchase land was prohibitive. Although the relatively poor were unable to assume such debts, the more prosperous were. Some of the more successful emigrants to the city managed to acquire land through land reform and rented it to farmers under terms equivalent to those previously available through larger absentee owners.

In the late 1960s and early 1970s, the government attempted to model its land reform efforts on a collective farming system borrowed from Chile (see Land Tenure and Agrarian Reform, ch. 3). The government acquired tax-delinquent properties and set up a variety of collectively operated agro-enterprises. The collectives enjoyed mixed success, however. They tended to be heavily mechanized and dependent on outside infusions of technical assistance and capital, while they generated only minimal employment. The most dramatic successes were achieved in regions like Veraguas Province where small farmers competed with cattle ranchers for land. Collectives were less successful in areas where smallholdings predominated.

Where small farmers held title to their lands—an infrequent pattern in traditional rural Panama—they often sold their lands to the larger, more heavily capitalized cattle ranches. The numbers of landless, or nearly landless, cultivators in search of plots to "borrow" for a season's planting rose. Substantial numbers of these displaced small farmers chose migration as an alternative.

Mestizo migrants from regions where cattle ranching was expanding entered the lowlands of the Atlantic coast and the Darién Peninsula in increasing numbers. Migrants arrived and cleared forest land (generally away from the rivers favored by the region's earlier black, Indian, Hispanic Indian, and Hispanic black settlers). The process then repeated itself: the new settlers remained for a few years until improved roads brought more cattle ranchers; the *colonos* (internal migrants) who originally cleared the forest then sold their lands and moved yet deeper into the tropical forest.

Migration

Migration has played an increasingly significant role in the lives of Panamanians and has followed a distinct pattern throughout the twentieth century. Population movement has been into those districts and provinces enjoying a period of economic prosperity, typically associated with the canal. As the economic boom peters out, the migrant population moves back to the primarily agricultural districts, to be reabsorbed into subsistence farming or small-scale businesses and services in the country's predominantly rural interior. The pattern has been repeated several times with the ebb and flow of economic activity. In the late 1980s, it remained to be seen what adaptations migrants would make given the shrinking rural land base.

The 1911 census provides a baseline for population movements throughout the century. At that time, the provinces of Chiriquí and Panamá accounted for nearly 40 percent of the total population. Chiriquí's growth was the result of migrants from Colombia in the nineteenth century; Panamá's came as a result of the canal construction begun just after the turn of the century. The central provinces—Veraguas, Coclé, Los Santos, and Herrera (in order of population)—accounted for slightly more than 40 percent of the total. The entire region had been populated along the coasts since the colonial era and had grown in response to increased demand for foodstuffs in Panama City and Colón in the second half of the nineteenth century. The decade following the census saw dramatic population growth in response to the United States presence and the building of the Panama Canal. The need to feed the massive numbers of Antillean black laborers who came to work on the construction project generated a boom in agriculture.

Subsequent censuses revealed a specific pattern of rural-rural and rural-urban migration. Some rural districts of a province lost population, while others even relatively close grew rapidly. The pattern reversed itself during periods of economic stagnation. Then, migrants retreated into subsistence agriculture in regions that had enjoyed limited participation in the previous boom. Between 1910 and 1920, for example, the Chepigana District in Darién was in the midst of a boom and enjoyed a significant influx of population, while the neighboring Pinogana District lost population. Their roles were reversed in the following decade.

The 1920s represented such a period of stagnation. The regions of highest growth in the previous decade grew much more slowly—if they grew at all. Colón and Bocas del Toro were the most heavily affected. Panamá Province continued to grow at rates slightly in excess of the national average; nonetheless, a large number of foreign workers left, as did a significant portion of the small business owners who had provisioned them and who were ruined by the decline in clientele.

Rural regions absorbed these surplus laborers and served as centers of population growth throughout the 1920s. Some such as Veraguas and Darién grew in excess of 5 percent annually during the intercensal period. District capitals in predominantly rural provinces tended to enjoy significant growth as well, probably as a result of their administrative functions, and the rise of banana plantations in Chiriquí attracted workers from throughout Central America.

The pattern reversed again in the late 1930s and mid-1940s. The immediate pre-World War II period as well as the war itself were times of significant economic expansion for the country as a whole. The province of Panamá headed the country in population growth, and the entire western portion of the province was a region of economic expansion. Colón, by contrast, lost in importance. Its annual rate of increase, 1.44 percent, was barely half the national average. The decline in Colón's fortunes reflected the centralization of economic and administrative activity in Panama City. Furthermore, Colón's importance as a port on the Atlantic diminished with the construction of the Trans-isthmian Highway (also known as the Boyd-Roosevelt Highway).

The economic expansion accompanying World War II eliminated problems associated with the increase in large-scale agroenterprises in the interior. Although substantial numbers of small farmers were displaced, they were readily absorbed by the demand for labor in cities and the countryside. Even in the period of economic contraction following the war, cities in predominantly rural provinces enjoyed significant growth. The war fueled the development of small-scale industrial and processing activities throughout the country. The dimensions of this growth were such that large numbers of rural youngsters—sons and daughters of small farmers—remained in the provinces in which they were born rather than migrating to Panama City or the Canal Zone.

World War II also saw Panama's last major influx of foreign workers. Most of these workers left with the economic slowdown at the war's end. As in previous periods of economic contraction, increasing numbers of displaced migrants took refuge in subsistence farming. The late 1940s was a time of growth for the rural regions of the country.

Overall, population grew at an annual rate of 2.9 percent in the 1950s; Panama was in the midst of a demographic transition as birth rates remained high while death rates dropped. The press of the population on the land base reached critical proportions. Peasants, displaced by the spread of large-scale agro-enterprises in the country, found it more and more difficult to find unoccupied land to put into production. At the same time, rural-urban migrants found it increasingly difficult simply to return home and resume farming during periods of economic contraction.

The pressure on the land base was acute enough to precipitate significant conflict over holdings in the 1950s and 1960s. In the province of Panamá, peasants invaded and seized the land around Gatun Lake as well as some regions of the districts of La Chorrera, Capira, and Chaime. Although many of these squatters were successful in maintaining their claim on the holdings, most peasants in other parts of the country were not so fortunate. The expansion of large cattle ranches in much of Los Santos and Veraguas continued the migratory process begun earlier, and peasants were pushed farther and farther along the agricultural frontier.

Substantial numbers of these displaced peasants migrated to less settled regions in Chiriquí, Los Santos, and Veraguas. Likewise, banana plantations in Chiriquí and Bocas del Toro drew significant numbers of migrants. The principal destination for much of the rural populace, however, was Greater Panama City.

Nearly two-thirds of all migrants had as their destination the heavily urban province of Panamá—a proportion that has remained roughly constant since the 1950s. In terms of absolute numbers, Los Santos and Veraguas were the major contributors to the migration stream: together they accounted for one-third of all migrants. The relatively depressed districts around Colón contributed large numbers of migrants, as did a number of districts in Chiriquí and Bocas del Toro. Based on rates of out-migration rather than absolute numbers, Los Santos, Darién, and Coclé were the main places of origin.

Within the province of Panamá, the greater metropolitan area of Panama City attracted most migrants. The districts surrounding the city averaged a growth rate of more than 10 percent per year in the 1960s and 1970s. Panama City played a significant role in the migration patterns of virtually every other province in the country. Over 90 percent of the migrants from Darién went there,

Squatter dwellings in San Miguelito
Courtesy Agency for International Development

as did roughly 80 percent of those from Coclé, Colón, Los Santos, and Veraguas. In the relatively prosperous mid-1960s to mid-1970s, most migrants managed to find employment. Many joined the ranks of peddlers and other small-scale self-employed individuals.

The manufacturing sector expanded significantly during the 1960s, resulting in a doubling of the industrial labor force. The service sector—traditionally the country's most dynamic—was fueled by the expansion of manufacturing as well as Panama's pivotal position as a transit zone. The service sector absorbed more than half the increase in the economically active population and grew at a rate of more than 6 percent annually. For the city-bound migrant, that meant jobs in public and domestic service and construction. Nevertheless, some observers expected the rate of migration to the metropolitan region to decline with economic reverses in the 1980s and the increase in opportunities in other regions, such as the Cerro Colorado copper project in Chiriquí.

Overall, the migration stream in the 1970s was composed of three components: rural-urban migrants (accounting for more than half of all migrants), urban-urban migrants (roughly one-quarter of all migrants), and urban-rural migrants (nearly 20 percent of those questioned about their place of residence 5 years earlier had been living in a city). The exact proportion and significance of urban-rural migration were difficult to judge. Approximately half the migrants were former residents of the smaller cities of the interior and presumably had left their farms for seasonal work in a nearby city or to attend school. Nearly one-third of these return migrants had lived in Panama City and its environs. Many were specialized workers; others were peasants unable to find permanent employment in the city; still others were children sent home to be cared for by kin.

Those people who migrated were, as a whole, young. In the 1970s nearly 75 percent of them were under 35 years of age; among rural-urban migrants, the percentage rose to more than 80 percent. School-age migrants represented a significant group in the migration stream. Although many simply accompanied their parents on moves, a significant minority were sent by their rural families for education in nearby cities. Men formed the majority among rural-urban migrants to Colón; women, however, accounted for a slight majority of all rural-urban migrants. This tendency was most marked in migration of women to cities in the interior but was also found among migrants to Panama City. In general, observers attributed the high rate of female migration to the metropolitan region to the opportunities for employment available for young women there. Unemployment was lower among urban females than among their rural counterparts, whereas the reverse was true for males.

Urban Society

Since the 1950s, Panama has been in the midst of massive urban expansion. In 1960 slightly more than one-third of the total population was classified as urban; by the early 1980s, the figure had risen to 55 percent. Between 1970 and 1980, overall population increased by 2.5 percent per year, urban population by 2.8 percent, and the metropolitan population surrounding Panama City by 3.7 percent. Regional cities shared in the general urban expansion: the number of people in Santiago grew at 4.1 percent annually; David, 3.7 percent; and Chitré, 3.3 percent. Economically depressed Colón lagged with an annual increase of less than 0.5 percent. Economic activity and population density in Panama were concentrated along two main axes: the Pan-American Highway (also known as the the Inter-American Highway) on the Pacific corridor from La Chorrera to Tocumen and the Trans-isthmian Highway from Panama City to Colón (see fig. 8).

Far and away the most significant focus of urban development was the path following the former Canal Zone that stretches from Colón on the Atlantic coast to Panama City on the Pacific. In the mid-1980s, the region accounted for more than half the total population of the country and over two-thirds of all those classified as inhabitants of cities. It also included most nonagricultural economic activity: 76 percent of manufacturing, 85 percent of construction, 95 percent of transportation, and 84 percent of communications. Growth was not spread evenly throughout the region, and since the 1950s, Panama City and its environs had eclipsed Colón. Colón remained the only significant urban center on Panama's Atlantic coast, but by the early 1980s, substantial numbers of that city's business and professional community had emigrated in response to Panama City's expanding economy.

In terms of sheer numbers, most of the urban expansion was concentrated in slum tenements and, since the 1950s, in squatter settlements around the major cities. As was the case in most urban trends, Panama City led the way. In 1958 there were 11 identifiable slums or squatter settlements housing 18,000 people associated with the city; by the mid-1970s, there were some 34 slum communities, and their population had mushroomed more than five-fold. Surveys indicated that 80 percent of slum and squatter settlement inhabitants were migrants to the city.

Many of the tenements took the form of two-story frame houses built as pre-World War I temporary housing for the canal labor force. They continued to be occupied, although in the early 1980s they were in an advanced state of decay. When one part of a building collapsed, slum dwellers continued to live in those sections of the building that remained standing. The structures were frequently condemned, which merely added to their attractiveness for impoverished city dwellers because the rent therefore dropped to nothing. Squatter settlements offered their own inducements. If squatters were able to maintain their claims to land, the settlements tended to improve and gained amenities over time. Because they were essentially rent-free, they gave their inhabitants considerable advantages over costly and over-crowded, if more centrally located, tenements. A substantial portion of the squatters settled on government land, and there were numerous programs to permit them to purchase their housing sites. The Torrijos regime allocated funds for low-income housing projects, and there were efforts to upgrade the amenities available to the urban poor. By the 1980s, about 96 percent of the urban population had access to potable water and nearly 70 percent had electricity. Despite indications of some slowing in the rate of rural-urban migration in the 1980s, migrants represented a major strain on public services and the economy's ability to generate employment.

Although rural society was relatively homogeneous and simple in the social distinctions it made, urban Panama was not. It was ethnically and socially diverse and highly stratified. City dwellers took note of ethnic or racial heritage, family background, income (and source of income), religion, culture, education, and political influences as key characteristics in classifying individuals.

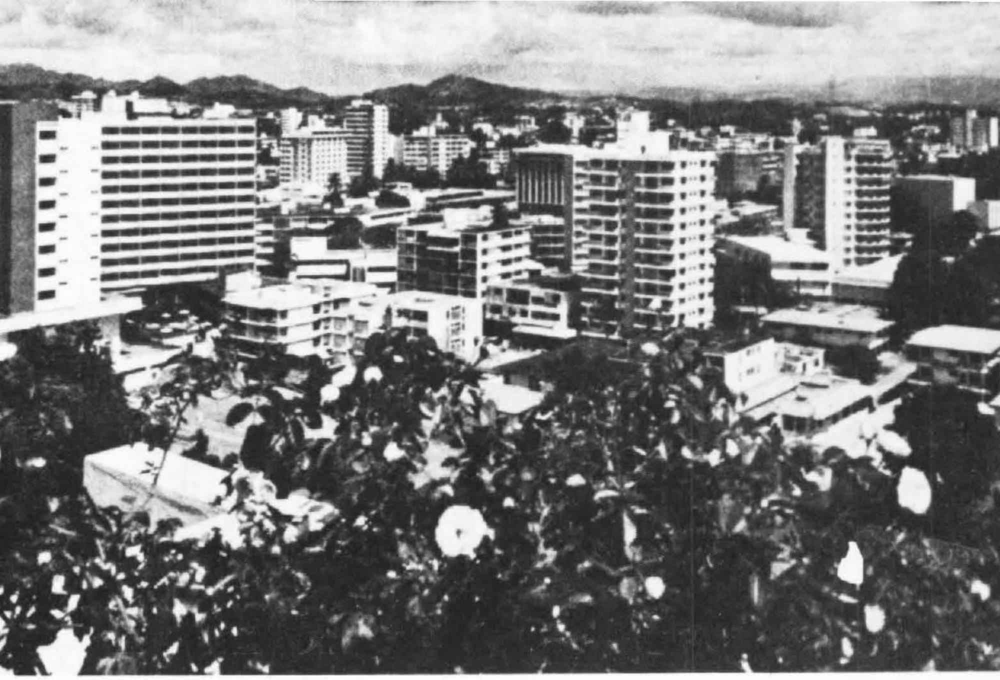
But, in the late 1980s, the boundaries among the elite, the middle class, and the lower class were neither especially well defined nor impervious. The ambitious and lucky city dweller could aspire to better significantly his or her social and economic status. Neither were the distinctions between rural and urban inhabitants absolute. City and countryside were linked in numerous ways; given the frequency with which migrants moved, this year's urban worker was last year's and (not uncommonly) next year's peasant. There was considerable social mobility, principally from the lower to the middle class and generally on an individual rather than a group basis. Wealth, occupation, education, and family affiliation were the main factors affecting such mobility.

The Elite

Urban society in the late 1980s included virtually all members of the elite. Centered mainly in the capital, this class was composed of old families of Spanish descent and a few newer families of immigrants. All elite families were wealthy, but the assets of the immigrant families were more tightly linked with commerce and Panama's twentieth-century development as a transit zone. Older families were inclined to think of themselves an aristocracy based on birth and breeding. Newer families, lacking such illustrious antecedents, had less prestige and social status. Until the advent of Torrijos, whose power base was the National Guard, an oligarchy of older elite families virtually controlled the country's politics under the auspices of the Liberal Party (see Organizing the New Republic; the Oligarchy under Fire, ch. 1).

The upper class was a small, close-knit group that had developed strong ties of association and kinship over the years. Prominent family names recurred frequently in the news of the nation: Arias, Arosemena, Alemán, Chiari, Goytía, and de la Guardia. People without a claim to such a family background could gain acceptance, at least for their children, by marriage into an elite family.

Since colonial times, education had been recognized as a mark of status; hence, almost all men of elite status received a university education. Most attended private schools either at home or abroad, and many studied a profession, with law and medicine the most favored. The practice of a profession was viewed not as a means of livelihood, but as a status symbol and an adjunct to a political career. The elite maintained a dual cultural allegiance, because



Panama City skyline
Courtesy Embassy of Panama

families usually sent their sons to Western Europe or the United States to complete their education. Increasing numbers of women also attended college, but most families did not see such education as essential.

Politics was the quintessential career for a young man of elite background. The old, aristocratic families had long provided the republic's presidents, its cabinet ministers, and many members of the legislatures. Young women were increasingly finding employment in public administration and commerce in the 1980s.

Older elite families were closely interrelated and were careful to avoid racially mixed unions. Antillean blacks enjoyed little success in attaining elite status, although a wealthy, Spanish-speaking, Roman Catholic black could gain acceptance. There was an increasing degree of admixture with mestizo and more recent immigrant elements. Many such families entered the elite and intermarried with members of the older families. In a sense, commercial success had in large measure become a substitute for an illustrious family background. "Money whitens everyone" was a popular saying describing the phenomenon.

The Middle Class

The middle class was predominantly mestizo, but it included such diverse elements as the children and grandchildren of Antillean blacks, the descendants of Chinese laborers on the railroad, Jews, more recent immigrants from Europe and the Middle East, and a few former elite families fallen on hard times. Like the elite, the middle class was largely urban, although many small cities and towns of the interior had their own middle-class families. The middle class encompassed small businessmen, professionals, managerial and technical personnel, and government administrators. Its membership was defined by those who, by economic assets or social status, were not identifiably elite but who were still markedly better off than the lower class. As a whole, the middle class benefited from the economic prosperity of the 1960s and early 1970s, as well as the general expansion in educational opportunities in the late twentieth century.

Members of the middle class who had held such status for any length of time were rarely content to remain fixed on the social scale. Emulating elite norms and attitudes, they exerted great effort to continue their climb up the social ladder. They were aware of the importance of education and occupation in determining status and the compensatory role these variables could play in the absence of family wealth or social background. Middle-class parents made great sacrifices to send their children to the best schools possible. Young men were encouraged to acquire a profession, and young women were steered toward office jobs in government or business. In contrast with the elite, the middle class viewed teaching as an appropriate occupation for a young woman.

Nationalist sentiment served to unify the diverse elements of the middle class in the decades following World War II. University students, who were predominantly middle class in family background, typified both the intense nationalism and the political activism of the middle class. Political observers noted a sharp class cleavage in the political consciousness of the Spanish-speaking natives and the more recent, unassimilated immigrant families. Middle-class immigrants tended to be preoccupied with commercial pursuits and largely conservative or passive in their politics.

The Lower Class

The lower class constituted the bulk of the country's urban population. As a group, it was stratified by employment and race. In terms of livelihood it was made up of unskilled or semiskilled workers, including artisans, vendors, manual laborers, and servants. The basic cleavages were between those who were wage earners and the self-employed, and those employed in the former Canal Zone, who constituted a "labor elite" earning twice the average of the metropolitan region as a whole.

Self-employment offered a precarious existence to most who pursued it, but served as an alternative for those unable to find other work when the economy contracted in the late 1970s and 1980s. Unemployment ran in excess of 10 percent in the late 1970s and early 1980s, and much of it was concentrated in the metropolitan region, which accounted for approximately four-fifths of the country's jobless. In poorer neighborhoods, the rate ran closer to 25 percent, and among low-income families, roughly 40 percent were unemployed (see Human Resources and Income, ch. 3).

Because the majority of rural-urban migrants to the metropolitan region were women, women outnumbered men in many larger urban areas. Many came in search of work as domestics. Young, single mothers constituted a significant proportion of the urban population; in Colón, for example, they represented one-third of all families. Women suffered higher unemployment rates than did men, and their earnings, when they were employed, averaged less than half those of males.

Ethnically, the lower class had three principal components: mestizo migrants from the countryside, children and grandchildren of Antillean blacks, and Hispanicized blacks—descendants of former slaves. The split between Antillean blacks and the rest of the populace was particularly marked. Although there was some social mixing and intermarriage, religious and cultural differences isolated the Antilleans. They were gradually becoming more Hispanicized, but the first generation usually remained oriented toward its Caribbean origins, and the second and third generations were under North American influence through exposure to United States citizens in the former Canal Zone where most were employed. Although some Antillean blacks were middle class, most remained in the lower class.

Increasing numbers of urban lower-class parents were sending their children to school. A secondary-school diploma, in particular, served as a permit to compete for white-collar jobs and elevation to middle-class status. This kind of mobility was on the rise throughout the 1960s and 1970s. Mestizos were better able to take advantage of these opportunities than most, but Antilleans who were educated and conformed to Hispanic cultural norms enjoyed considerable mobility as well. The National Guard, and later the FDP, have been an avenue of advancement for both Hispanic and Antillean blacks. A substantial portion of the enlisted personnel have come from the ranks of the black urban poor and, increasingly, the rural mestizo population. Enlisted personnel could hope to advance to the officer corps. Under the Torrijos regime, many troop commanders were promoted from the ranks.

Religion

The Constitution prescribes that there shall be no prejudice with respect to religious freedom, and the practice of all forms of worship is authorized. However, the Constitution recognizes that the Roman Catholic faith is the country's predominant religion and contains a provision that it be taught in the public schools. Such instruction or other religious activity is not, however, compulsory.

The Constitution does not specifically provide for the separation of church and state, but it implies the independent functioning of each. Members of the clergy may not hold civil or military public office, except such posts as may be concerned with social welfare or public instruction. The Constitution stipulates that senior officials of the church hierarchy in Panama must be native-born citizens.

The majority of Panamanians in the late 1980s were at least nominal Roman Catholics. The Antillean black community, however, was largely Protestant. Indians followed their own indigenous belief systems, although both Protestant and Catholic missionaries were active among the various tribes. Roman Catholicism permeated the social environment culturally as well as religiously. The devout regarded church attendance and the observance of religious duties as regular features of everyday life, and even the most casual or nominal Roman Catholics adjusted the orientation of their daily lives to the prevailing norms of the religious calendar. Although some sacraments were observed more scrupulously than others, baptism was almost universal, and the last rites of the church were administered to many who during their lives had been indifferent to the precepts of the faith or its religious rituals.

In the mid-1980s, when nearly 90 percent of the population was Roman Catholic, there were fewer than 300 priests in the country. Virtually every town had its Roman Catholic church, but many did not have a priest in residence. Many rural inhabitants in the more remote areas received only an occasional visit from a busy priest who traveled among a number of isolated villages.

Religious attitudes, customs, and beliefs differed somewhat between urban and rural areas, although many members of the urban working class, often recent migrants from rural regions, presumably retained their folk beliefs. According to one anthropologist, the belief system of the campesinos centered on God, the Devil, the saints, and the Virgin. Christ was viewed as more or less the chief saint, but as peripheral to the lives of men. The Virgin Mary served as an inspiration and model to women, but there was no comparable model for men.

The Golden Altar in the Church of San José, Panama City

Although the campesinos believed that each individual "is born with a destiny set by God," they also believed that the destiny could be altered if the individual succumbed to the constant blandishments and enticements of the Devil. The rural dwellers possessed a clear sense of reward and punishment that centered on All Souls' Day. On that day all who died during the previous year are summoned to judgment before God and the Devil. The life record of each person is recited by Saint Peter, and the good and bad deeds are weighed out on a Roman balance scale, thus determining the person's afterlife.

Throughout the society, birth and death were marked by religious rites observed by all but a very few. One of the first social functions in which newly born members of the family participated was the sacrament of baptism, which symbolized their entry into society and brought them into the church community. In the cities, church facilities were readily available, but in rural areas families often had to travel some distance to the nearest parish center for the ceremony. The trip was considered of great importance and was willingly undertaken. In fact, baptism was generally considered the most significant religious rite.

If the family lived near a church that had a priest in regular attendance, children received an early exposure to the formal teachings of the church and were usually taken to mass regularly by their mothers. As they grew older, they took an increasing part in church liturgy and by the age of ten were usually full participants in such activities as catechism classes, communion, and confession. As they approached manhood, boys tended to drift away from the church and from conscientious observation of church ritual. Few young men attended services regularly, and even fewer took an active part in the religious life of the community, although they continued to consider themselves Roman Catholics.

Girls, on the other hand, were encouraged to continue their religious devotions and observe the moral tenets of their faith. Women were more involved in the church than men, and the community and clerics accepted this as a basic axiom. There was social pressure on women to become involved in church affairs, and most women, particularly in urban areas, responded. As a rule, they attended mass regularly and took an active part in church and church-sponsored activities. Religious gatherings and observances were among the principal forms of diversion for women outside the home, and to a great extent these activities were social as much as devotional.

Education

Public education began in Panama soon after independence from Colombia in 1903. The first efforts were guided by an extremely paternalistic view of the goals of education, as evidenced in comments made in a 1913 meeting of the First Panamanian Educational Assembly, "The cultural heritage given to the child should be determined by the social position he will or should occupy. For this reason education should be different in accordance with the social class to which the student should be related." This elitist focus changed rapidly under United States influence.

By the 1920s, Panamanian education subscribed to a progressive educational system, explicitly designed to assist the able and ambitious individual in search of upward social mobility. Successive national governments gave a high priority to the development of a system of (at least) universal primary education; in the late 1930s, as much as one-fourth of the national budget went to education. Between 1920 and 1934, primary-school enrollment doubled. Adult illiteracy, more than 70 percent in 1923, dropped to roughly half the adult population in scarcely more than a decade.

By the early 1950s, adult illiteracy had dropped to 28 percent, but the rate of gain had also declined and further improvements were slow in coming. The 1950s saw essentially no improvement; adult illiteracy was 27 percent in 1960. There were notable gains in the 1960s, however, and the rate of adult illiteracy dropped 8 percentage points by 1970. According to 1980 estimates, only 13 percent of Panamanians over 10 years of age were illiterate (see table 5, Appendix A). Men and women were approximately equally represented among the literate. The most notable disparity was between urban and rural Panama; 94 percent of city-dwelling adults were literate, but fewer than two-thirds of those in the countryside were—a figure that also represented continued high illiteracy rates among the country's Indian population (see Indians, this ch.).

From the 1950s through the early 1980s, educational enrollments expanded faster than the rate of population growth as a whole and, for most of that period, faster than the school-aged population. The steepest increases came in secondary and higher educational enrollments, which increased ten and more than thirty times, respectively (see table 6, Appendix A). By the mid-1980s, primary-school enrollment rates were roughly 113 percent of the primary-school-aged population. Male and female enrollments were relatively equal overall, although there were significant regional variations.

Enrollments at upper levels of schooling had increased strikingly both in relative and absolute terms since 1960. Between 1960 and the mid-1980s, secondary-school enrollments expanded some four-and-a-half times and higher education, nearly twelve-fold. In 1965 fewer than one-third of children of secondary school age were in school and only 7 percent of people aged 20 to 24 years. In the mid-1980s, almost two-thirds of secondary-school-aged children were enrolled, and about 20 percent of individuals aged 20 to 24 years were in institutions of higher education.

School attendance was compulsory for children from ages six through fifteen years, or until the completion of primary school. A six-year primary cycle was followed by two types of secondary-school programs: an academic-oriented program and a vocational-type program. The academic program, which represented nearly three-quarters of all secondary-school enrollment, involved two three-year cycles. The lower cycle was of a general or exploratory nature, with a standard curriculum that included Spanish, social studies, religion, art, and music. The upper cycle consisted of two academic courses of study: in arts and sciences, leading to entrance to the university, or a less rigorous course of study, representing the end of a student's formal education (fewer than 4 percent of students pursued this course of studies in the mid-1980s).

In addition to the academic program, there was a vocational-type secondary-school program that offered professional or technical courses aimed specifically at giving students the technical skills needed for employment following graduation. In the mid-1980s, roughly one-quarter of all secondary students pursued this type of course. Like the more academic-oriented secondary-school program, the vocational-type program was divided into two cycles. Students could choose their studies from a variety of specializations, including agriculture, art, commerce, and industrial trades.

Admission to the university normally required the *bachillerato* (graduation certificate or baccalaureate), awarded on completion of the upper cycle of the academic course of studies, although the University of Panama had some latitude in determining admissions standards. The *bachillerato* was generally considered an essential component of middle-class status. Public secondary schools that offered the baccalaureate degree also offered the lower cycle. They were generally located in provincial capital cities. The oldest, largest, and most highly regarded of these was the National Institute in Panama City. The University of Panama grew out of it, and the school had produced so many public figures that it was known as the Nest of Eagles (Nido de Aguilas). It tended to draw its student body from upwardly mobile rather than long-established elements of the elite. Its students were well known for their political activism.

School in Antón, Coclé Province
Courtesy Agency for International Development

Higher education on the isthmus dates from the founding of a Jesuit university in 1749; that institution closed with the order's expulsion from the New World in 1767. Another college, the Colegio del Istmo, was started early in the nineteenth century, but the school did not prosper, and Panamanians who wished to pursue a higher education were required to go abroad or to Colombia until 1935, when the University of Panama was founded. In the mid-1980s, most postsecondary schooling took place within the university. Other institutions, such as the School of Nursing and the Superior Center for Bilingual Secretaries, accounted for less than 3 percent of enrollment at this educational level.

Nearly three-quarters of all university students attended the University of Panama in the 1980s. The university had, as well, a number of regional centers and extensions representing a small portion of the school's enrollment and faculty. The University of Santa María la Antigua, a private Roman Catholic institution established in 1965, enrolled another 5,000 to 6,000 students in the 1980s. A third university, the Technical University, was founded in 1981. It accounted for approximately 7,000 students. A substantial portion of the well-to-do continued to study abroad.

Most education was publicly funded and organized. In addition to the University of Santa María la Antigua, there were some private primary and secondary schools. Typically located in cities and considered very prestigious, they accounted for 5 to 7 percent of primary-school enrollment and approximately 25 percent of secondary-school students in the mid-1980s.

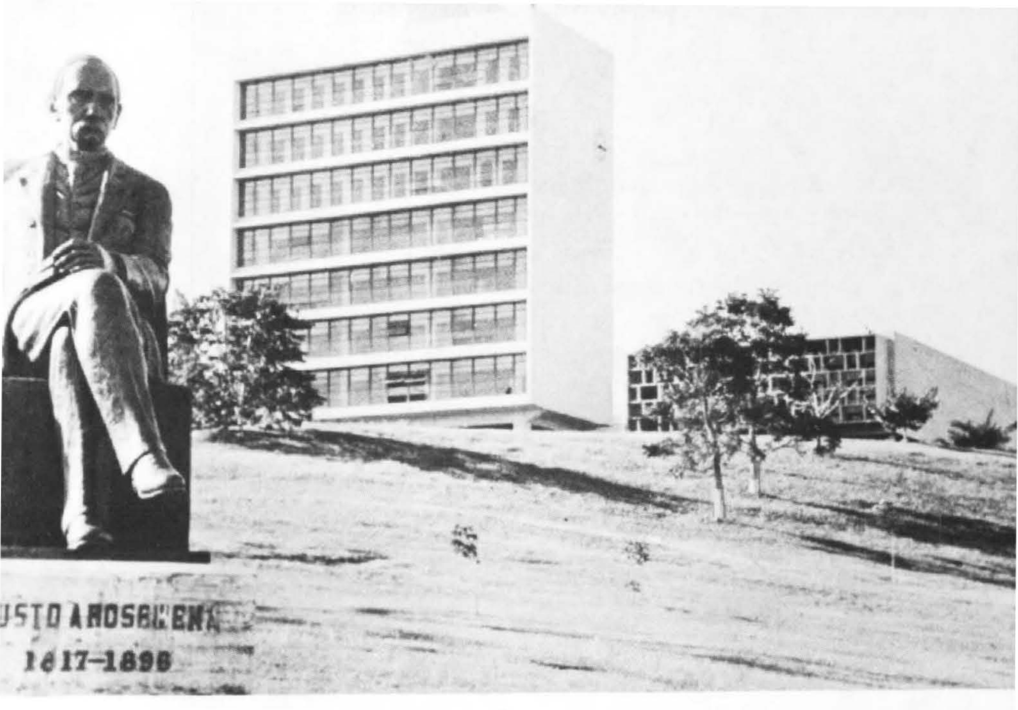
Education continued to claim a large share of government budgets. It represented 15 to 20 percent of the national government's expenditures in the early to mid-1980s (see table 7, Appendix A). Most funding went to primary schooling, although both secondary and higher education received proportionately higher funding per student. Primary schools received roughly one-third of government education spending, secondary and higher education approximately 20 percent each (see table 8, Appendix A). Budgets from 1979 through 1983 allocated on average B220 per primary school student, B274 per secondary school student, and B922 per university student (for value of the balboa—see Glossary).

The growth in enrollment was accompanied by a concomitant (if not always adequate) expansion in school facilities and increase in teaching staff. Teacher education was a high priority in the 1970s and 1980s, a reflection of the generally poor training teachers had received in the past. Schools increased at every level during the early 1980s; secondary schools made the most notable gains, more than doubling (see table 9, Appendix A). Pupil-teacher ratios for all levels were in the range of nineteen to twenty-six pupils per teacher in the mid-1980s.

Health and Welfare

The Ministry of Health bore primary responsibility for public health programs in the late 1980s. At the district and regional levels, medical directors were responsible for maintaining health-care services at health-care centers and hospitals and monitoring outreach programs for the communities surrounding these facilities. The Social Security Institute also maintained a medical fund for its members and ran a number of health-care facilities, which members could use for free and others for a nominal fee. In practice there was a history of conflict between Social Security Institute and Ministry of Health personnel at the district and regional levels. Since 1973 the Social Security Institute and the Ministry of Health had attempted—with limited success—to coordinate what were in essence two public health-care systems, in an effort to eliminate redundancy.

Despite the bureaucratic conflicts, a number of health indicators showed significant improvement. Life expectancy at birth in 1985 was seventy-one years—an increase of nearly ten years since 1965 (see table 10, Appendix A). Infant mortality rates in 1984 were less than one-third their 1960 levels, and the childhood death



University of Panama
Courtesy Organization of American States

rate stood at less than 20 percent of the 1960 level. The number of physicians per capita had nearly tripled.

The Department of Environmental Health was charged with administering rural health programs and maintaining a safe water supply for communities of fewer than 500 inhabitants—roughly one-third of the total population. The National Water and Sewage Institute and the Ministry of Public Works shared responsibility for urban water supplies.

By 1980 approximately 85 percent of the population had access to potable water and 89 percent to sanitation facilities. In rural Panama in the early 1980s, roughly 70 percent of the population had potable water and approximately 80 percent had sanitation facilities. The quality of water and sewage disposal varied considerably, however. Water transmission was less than reliable on the fringes of urban centers. In rural areas, much depended on the community's dedication to maintaining sanitation facilities and an operating water system. Many water treatment facilities were poorly maintained and overloaded, because of the intense urban growth the country had experienced since the end of World War II. In rural Panama, latrines and septic tanks tended to be over-used and under-maintained. The system as a whole stood in need of substantial renovation and repair in the late 1980s.

Public health, especially for rural Panamanians, was a high priority. Under the slogan "Health for All by the Year 2000," in the early 1970s the government embarked on an ambitious program to improve the delivery of health services and sanitation in rural areas. The program aimed at changing the emphasis from curative, hospital-based medical care to community-based preventive medicine. The 1970s and early 1980s saw substantial improvements in a wide variety of areas. Village health committees attempted to communicate the perceived needs of the villagers to health-care officials. The program enjoyed its most notable successes in the early 1970s with the construction of water delivery systems and latrines in a number of previously unserved rural areas. Village health committees also organized community health-education courses, immunization campaigns, and medical team visits to isolated villages. They were assisted by associations or federations of these village health committees at the district or regional level. These federations were able to lend money to villages for the construction of sanitation facilities, assist them in contacting Ministry of Health personnel for specific projects, and help with the financing for medical visits to villages.

Village health committees were most successful in regions where land and income were relatively equitably distributed. The regional medical director was pivotal; where he or she assigned a high priority to preventive health care, the village communities continued to receive adequate support. However, many committees were inoperative by the mid-1980s. In general, rural health-care funding had been adversely affected by government cutbacks. Facilities tended to be heavily used and poorly maintained.

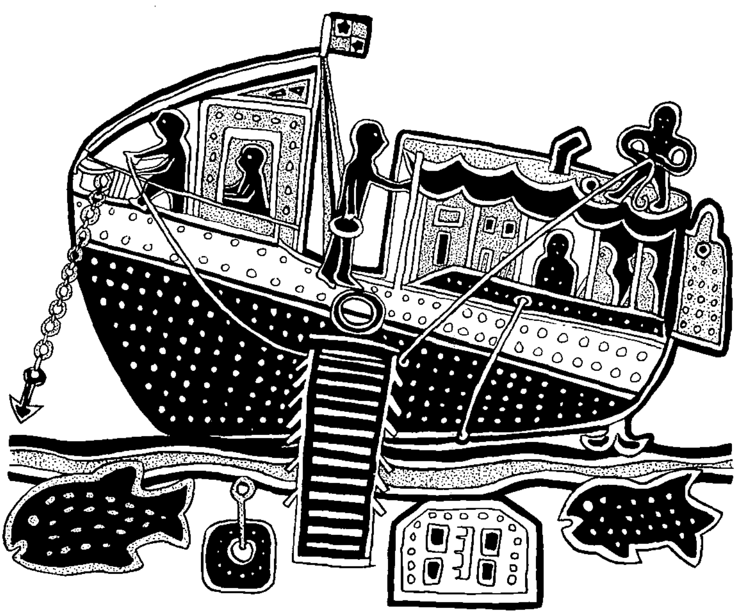
In the early 1980s, there continued to be marked disparities in health care between urban and rural regions. Medical facilities, including nearly all laboratory and special-care facilities, were concentrated in the capital city. In 1983 roughly 87 percent of the hospital beds were in publicly owned and operated institutions, mostly located in Panama City; one-quarter of all hospitals were in the capital (see table 11, Appendix A). Medical facilities and personnel were concentrated beyond what might reasonably be expected, even given the capital city's share of total population. Panama City had roughly 2.5 times the national average of hospital beds and doctors per capita and nearly 3 times the number of nurses per capita (see table 12, Appendix A). The effect of this distribution was seen in continued regional disparities in health indicators. Rural Panama registered disproportionately high infant and maternal mortality rates. Rural babies were roughly 20 percent more likely to die than their urban counterparts; childbearing was 5 times more likely to be fatal in rural Panama than in cities (see table 13, Appendix A). In the early 1980s, the infant mortality rate of Panamá Province was one-third that of Bocas del Toro and one-fourth that of Darién.

Panama's social security system covered most permanent employees. Its principal disbursements were for retirement and health care. Permanent employees paid taxes to the Social Security Institute; the self-employed contributed on the basis of income as reported on income tax returns. Agricultural workers were generally exempted. Changes in 1975 lowered the age at which workers could retire and altered the basis on which benefits were calculated. The general effect of the changes was to encourage the retirement of those best paid and best covered. It did little to benefit the most disadvantaged workers.

* * *

There are a number of useful works on Panamanian society. John and Mavis Biesanz's *The People of Panama,* although dated, remains the most complete treatment of Panamanian society in its entirety. Stephen Gudeman's *The Demise of a Rural Economy* looks at the changing situation of small farmers and describes mestizo life in the countryside. There is extensive literature on Panama's principal Indian tribes. Of particular use to the general reader are *Ngawbe* by Philip D. Young (on the Guaymí), as well as his article co-authored with John R. Bort, "Politicization of the Guaymí," and *The Kuna Gathering* (about the Cuna) by James Howe. Statistical information on a wide variety of topics is available from the Panamanian government's *Panamá en Cifras.* (For further information and complete citations, see Bibliography.)

Chapter 3. The Economy



Cuna Indian mola *design of a San Blas inter-island boat at dock*

SEVERAL DISTINCTIVE FEATURES characterized Panama's economy in the late 1980s; the most striking was its internationally oriented services sector, which in 1985 accounted for over 73 percent of the gross domestic product (GDP—see Glossary), the highest such percentage in the world. That distinctiveness was best symbolized by the Panama Canal, which has dominated the country's economy in the twentieth century. The scope of the services sector has expanded and broadened through increased government services and initiatives such as the Colón Free Zone (CFZ—see Glossary), a trans-isthmian oil pipeline, and the International Financial Center.

Another distinguishing feature was Panama's paper currency, the United States dollar. The local currency, the balboa, was tied to the United States dollar but was available only in coins. Panama's money supply was determined by the United States Federal Reserve System; therefore, the country could neither print money nor devalue the currency. Because its monetary instruments are limited, Panama has avoided the cycle of exchange-rate devaluations and the accelerating inflation that have typified most Latin American economies. The balboa has remained on par with the United States dollar, and Panama has enjoyed the lowest average annual rate of inflation in Latin America—7.1 percent in the 1970s, and only 3.7 percent between 1980 and 1985.

The third economic distinction is that the Panamanians have one of the highest levels of per capita income in the developing world. Construction of the Panama Canal across the isthmus in the early 1900s and expanding world commerce have combined to foster rapid economic growth in the country throughout the twentieth century. By 1985 per capita gross national product (GNP—see Glossary) reached US$2,100, twice the average in Central American countries, greater than all South American countries except for Venezuela (US$3,080) and Argentina (US$2,130), and on a level with Mexico (US$2,080). Panamanians, however, have not shared equally in the rising living standards, because the distribution of income has been highly skewed.

The military leaders who seized control of the government in 1968 under the leadership of General Omar Torrijos Herrera instituted economic policies that aimed at greater equity as well as integration of various facets of the country's fragmented economy. By the time of Torrijos's death in July 1981, they had achieved some remarkable results, but at the expense of a low rate of private investment, increased urban unemployment, continued rural poverty, and growing external public debt. A document entitled *Towards a More Human Economy* was published in 1985 by Panama's Archbishop Marcos Gregorio McGrath, revealing a society in which 38 percent of the families lived in poverty and in which 22 percent of the population failed to earn at least US$200 a month—the minimum amount considered necessary to purchase a basic basket of goods. The document went on to criticize many measures taken by the Torrijos government in the 1970s. At the same time, however, the publication recognized that remarkable progress had been made in other areas, such as a decline in infant mortality rates, a rise in the literacy rate, and social security coverage for 60 percent of the population as compared with only 12 percent in 1960. Indeed, the economic policies instituted by the Torrijos regime (1968–81) were pivotal in Panama's history, but the results were mixed.

Growth and Structure of the Economy

Since the early 1500s, Panamanians have relied on the country's comparative advantage—its geography. Exploitation of this advantage began soon after the Spanish arrived, when the conquistadors used Panama to transship gold and silver from Peru to Spain (see The Conquest, ch. 1). Ports on each coast and a trail between them handled much of Spain's colonial trade from which the inhabitants of the port cities prospered. This was the beginning of the country's historical dependence on world commerce for prosperity and imports. Agriculture received little attention until the twentieth century, and by the 1980s had—for much of the population—barely developed beyond indigenous Indian techniques. Industry developed slowly because the flow of goods from Europe and later from North America created a disincentive for local production.

Panama has been affected by the cyclical nature of international trade. The economy stagnated in the 1700s as colonial exchange via the isthmus declined. In the mid-1800s, Panama's economy boomed as a result of increased cargo and passengers associated with the California gold rush. A railroad across the isthmus, completed in 1855, prolonged economic growth for about fifteen years until completion of the first transcontinental railroad in the United States caused trans-isthmian traffic to decline. France's efforts to construct a canal across the isthmus in the 1880s and efforts by the United States in the early 1900s stimulated the Panamanian economy.

The United States completed the canal in 1914, and canal traffic expanded by an average of 15 percent a year between 1915 and 1930. The stimulus was strongly felt in Panama City and Colón, the terminal cities of the canal. The world depression of the 1930s reduced international trade and canal traffic, however, causing extensive unemployment in the terminal cities and generating a flow of workers to subsistence farming. During World War II, canal traffic did not increase, but the economy boomed as the convoy system and the presence of United States forces, sent to defend the canal, increased foreign spending in the canal cities. The end of the war was followed by an economic depression and another exodus of unemployed people into agriculture. The government initiated a modest public works program, instituted price supports for major crops, and increased protection for selected agricultural and industrial products.

The postwar depression gave way to rapid economic expansion between 1950 and 1970, when GDP increased by an average of 6.4 percent a year, one of the highest sustained growth rates in the world. All sectors contributed to the growth. Agricultural output rose, boosted by greater fishing activities (especially shrimp), the development of high-value fruit and vegetable production, and the rapid growth of banana exports after disease-resistant trees were planted. Commerce evolved into a relatively sophisticated wholesale and retail system. Banking, tourism, and the export of services to the Canal Zone grew rapidly. Most importantly, an increase in world trade provided a major stimulus to use of the canal and to the economy.

In the 1970s and 1980s, Panama's growth fluctuated with the vagaries of the world economy. After 1973 economic expansion slowed considerably as the result of a number of international and domestic factors (see Recent Economic Performance, this ch.). Real GDP growth averaged 3.5 percent a year between 1973 and 1979. In the early 1980s, the economy rebounded with GDP growth rates of 15.4 percent in 1980, 4.2 percent in 1981, and 5.6 percent in 1982. The acute recession in Latin America after 1982, however, wreaked havoc on Panama's economy. GDP growth in 1983 was a mere 0.4 percent; in 1984 it was negative 0.4 percent. In 1985 Panama experienced economic recovery with 4.1-percent GDP growth; the corresponding figure for 1986 was estimated to be 2.8 percent.

Changing Structure of the Economy

The structure of Panama's economy in the twentieth century has been characterized by the dichotomy of a large internationally

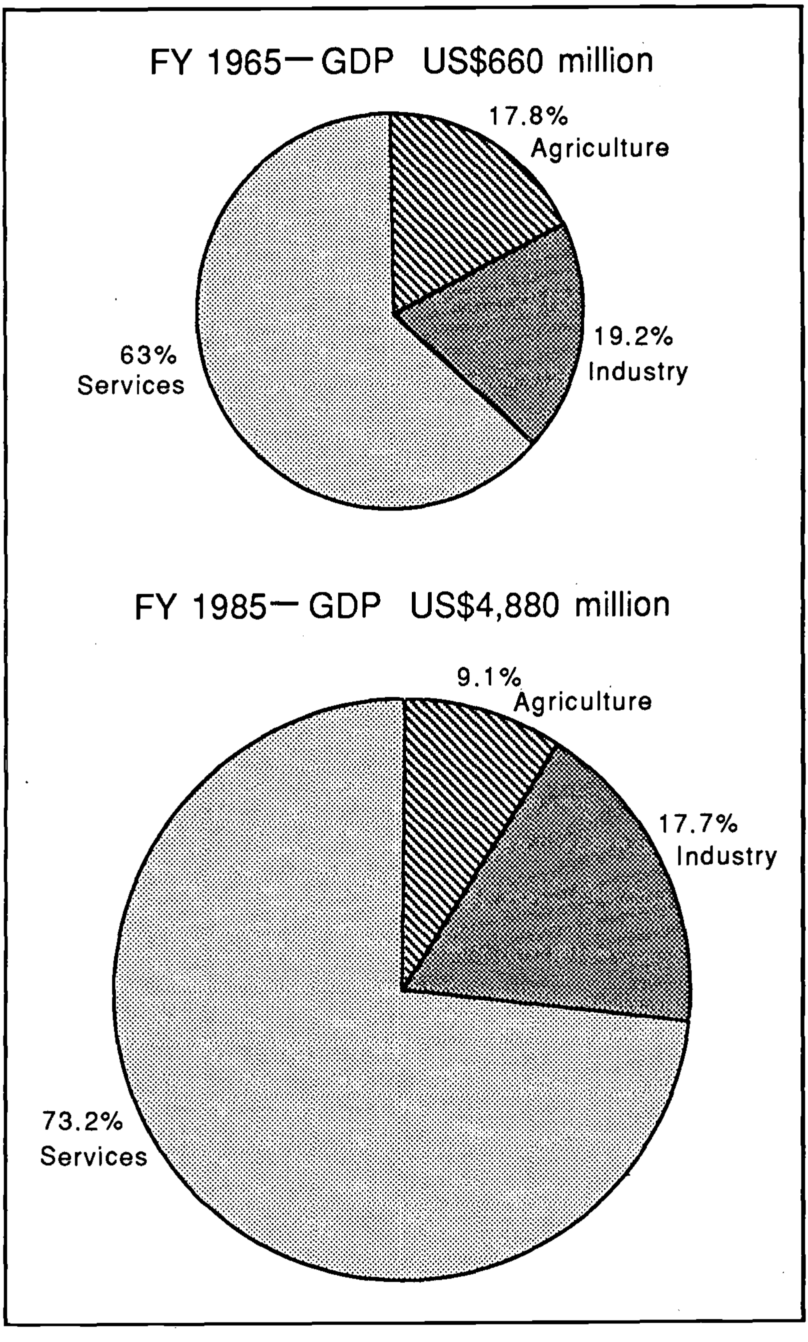


Figure 7. Gross Domestic Product by Sector, 1965 and 1985

oriented services sector and a small inward-looking goods sector. The major change in that structure has been the rapid growth of the services sector. In 1950 services accounted for about 57 percent of GDP; that share rose to 63 percent in 1965 and to over 73 percent in 1985 (see fig. 7). Given Panama's geographic location, modern infrastructure, and an educated population trained in commercial and financial activity, services will likely remain the leading sector of the economy.

In contrast, the goods sector has declined in relative terms. Although efforts have been made to stimulate agriculture and industry—and both registered substantial growth—their share of GDP has fallen as that of the services sector has risen. In the late 1980s, one of the greatest challenges facing Panamanian policymakers was that of using the services sector as a springboard for growth, primarily in industry but also in agriculture.

During the Torrijos administration, the economy was stimulated in several areas. The principal stimulus to the services sector was banking, particularly offshore banking (see Glossary). Transportation also increased rapidly, along with expansion of the road network. Substantial investments were made in the communications system in an effort to meet international standards expected by the extensive network of foreign businesses. Storage and warehousing grew rapidly in response to the economy's own needs and particularly to the foreign business conducted in the CFZ.

Industrialization progressed rapidly after 1950, with industrial production rising from 10 percent of GDP in 1950 to 19 percent in 1965. This expansion was based primarily on import substitution. Industry continued to grow at an average annual rate of 5.9 percent from 1965 through 1980, but registered negative 2.2-percent average annual growth between 1980 and 1985.

As a result of the lack of growth as well as the rapid rise of the services sector, industrial production had dropped slightly as a percentage of GDP in 1985—to just under 18 percent. Manufacturing accounted for about half of the industrial sector, followed by construction, energy, and mining. Given the small size of the domestic market, observers believed that future industrial growth would rely primarily on foreign markets. Success, therefore, would depend to a large extent on Panama's ability to make its industry internationally oriented and competitive.

Although the agricultural sector continued to expand and to employ the largest number of workers, its share of GDP declined substantially, from 29 percent in 1950 to 18 percent in 1965 and about 9 percent in 1985. This sector grew at a respectable average annual rate of 2.4 percent between 1965 and 1980, and 2.7 percent between 1980 and 1985, but it could not keep pace with the rapid growth rate of the services sector. Bananas, shrimp, and sugar continued to lead the list of export items. The expansion of the agricultural sector hinged on exports and product diversification.

Recent Economic Performance

The Torrijos era (1968–81) stands as a dividing point in Panama's economic history. Under Torrijos, the state took a more active role in the economy and initiated ambitious social projects. The public sector expanded to an unprecedented degree, as did the fiscal deficit and the external debt. In the 1980s, Panama was forced to address some of the excesses of the 1970s and to adjust its policies, often under the aegis of the International Monetary Fund (IMF—see Glossary) and the World Bank (see Glossary).

In the 1960s, Panama experienced buoyant growth in virtually all areas of the economy as a result of the boom in canal-related activities and the growth in private investment. GDP expanded at an average of 8 percent per year. Employment grew at 3.5 percent per year, well above the population growth of about 3 percent a year. Most of the new jobs were generated by the private sector.

In the 1970s, Panama's average annual growth rate of GDP fell to 3.4 percent. Many factors contributed to the decline. In the international arena, reduced canal use (especially after the Vietnam war), rising oil prices, international inflation, and recession in the major industrial countries had a negative impact on Panama's economy. Domestically, investment fell in response to government policies of agrarian reform, expropriation of private power companies, creation of state industries, protection of labor, controls on housing, subsidies, and high support prices. In addition, the prolonged negotiations between the United States and Panama over the canal adversely affected investor confidence. The government sought to regain private investment by investing in large infrastructure projects and by expanding or acquiring productive enterprises. Two-thirds of the new jobs created in the 1970s were in the public sector. The public-sector deficit expanded, and the government was forced to borrow money from abroad. By 1980 the external debt had reached 80 percent of GDP.

In 1982 Panama, like most of Latin America, felt the impact of the world recession. Once again, the government sought to remedy the declining private-sector investment through increased public expenditures. In the same year, the public-sector deficit reached 11 percent of GDP. In 1983 and 1984, the government imposed a severe austerity program, which had the imprimatur of the IMF. Public investment was reduced by 20 percent in 1983 and by a further 8 percent in 1984. The public deficit was also cut, to about 6 percent of GDP in both years. In addition, the government undertook structural adjustment measures in the areas of industry and agriculture and instituted changes to streamline the public sector. The simultaneous recession and reduction in public expenditures caused GDP to fall in 1984, the first decline in more than twenty years. In the following years, however, Panama, avoiding the economic slump that plagued most Latin American countries, experienced moderate growth.

Role of Government

The government has played a limited role in economic matters throughout most of Panama's history, restricting its activities to infrastructural development and creating a climate conducive to private investment. The government's role expanded dramatically after 1968, when the National Guard, now called the Panama Defense Forces (Fuerzas de Defensa de Panamá—FDP), took control of the government under Torrijos's leadership. Members of the National Guard tended to be provincial, racially mixed, and lower- or middle-class in background and thus provided an outlook different from that of the urban-oriented elite that had dominated Panamanian politics in the twentieth century (see The Government of Torrijos and the National Guard, ch. 1).

The National Guard implemented policies that attempted to reduce the most glaring discrepancies between the urban and rural economies. In 1968 economic activity was heavily concentrated in the two provinces of Panamá and Colón, which accounted for over two-thirds of GDP and an even larger share of the country's manufacturing, construction, trade, transport, and communications (see fig. 1). Residents of the metropolitan areas had access to relatively well-developed education, health, and other services. Their consumption pattern was closer to that of affluent developed countries; they owned most of the country's cars, refrigerators, telephones, and television sets. Their tastes and aspirations were patterned on those of United States citizens in the Canal Zone and the many international visitors. In contrast, rural residents had access to far fewer services, and their living conditions were substantially below those of urbanites (see Rural Society, ch. 2). The majority of the population in the countryside had incomes of less than one-third of those in Panama City and Colón, and many had little more than one-tenth. The economic policies of the military leaders aimed at continued high growth of the urban economy, from which resources could be channeled to the poorer elements of the society to bring about greater economic and social integration.

High growth of service industries in the terminal cities was considered essential because of several constraints: canal-related activities were not expected to provide much of a growth stimulus; import substitution opportunities in manufacturing had been largely exhausted; and expansion of banana exports appeared limited by international conditions. Panama became a regional financial center after 1970, when the government created the International Financial Center. Tourism was bolstered by construction of additional airports, a convention center, new hotels, and resorts. The CFZ was upgraded, and transportation and warehousing facilities were also improved.

Under Torrijos the government became more active in the goods sectors. In agriculture, land reform was accelerated, and cooperative farming was promoted. In industry, state-owned companies expanded, most notably in sugar refining, cement production, and electric power. Torrijos intervened more forcefully in other areas of the economy, such as in the setting of wages and prices; a 1972 labor code increased job security and promoted union organization.

These measures created a more equitable society, but often at the expense of efficiency and overall growth. Government expenditure rose sharply, and the public sector became bloated with a proliferation of new government agencies. In the services sector, construction declined in the mid-1970s, in part because of the disincentive created by rent controls. In agriculture, considerable improvements in social conditions were not accompanied by increased incomes. Moreover, greater government participation and prolonged canal negotiations created difficulties and uncertainties for private investors, and private investment declined precipitously.

After 1975 the government became more pragmatic and modified its programs to stimulate economic activity. Incentives to investors were increased. The 1972 labor code was modified in 1976 to meet some of the objections by employers. A freeze on collective bargaining agreements was established that in effect prohibited wage increases. Government-set prices were raised to encourage production.

Under a structural adjustment program in 1983 and 1984, Panama reduced the scope of the public sector in the economy. In March 1986, and as preconditions for two structural adjustment loans from the World Bank, the government passed several major laws that revised its labor code, removed protective tariffs, changed the price structure for agricultural goods, and encouraged foreign investment. In August 1986 the government launched a privatization program and proposed the sale of state assets worth US$13 million.

Monetary Policy

Panama's monetary system is unique. United States dollar notes serve as the paper currency and are legal tender in Panama. The local currency is the balboa, which, since its creation in 1904, has remained tied to and equal to the United States dollar. Panama issues only coins corresponding in size and metallic content to United States coins. No foreign exchange restrictions existed in Panama in the mid-1980s.

With no need for a bank to issue and protect the paper currency, Panama did not have a central bank. The National Bank of Panama (Banco Nacional de Panamá—BNP), a state-owned commercial bank, was responsible for nonmonetary aspects of central banking. The BNP was assisted by the National Banking Commission, which was created along with the country's International Financial Center, and was charged with licensing and supervising banks. In 1985 the level of M1 (currency and demand deposits) was US$410 million, while M2 (M1 plus time deposits) was US$1.95 billion.

In a sense, Panama could not have a monetary policy, because it lacked the instruments to implement such a policy, such as money creation and exchange-rate manipulation. In effect, Panama's money supply was determined by the balance of payments, by movements in interest rates, and by the United States, which controlled the number of dollars available for the country's international transactions.

Panama's monetary system has benefited the country in numerous ways. The country has enjoyed almost automatic monetary and price stability. International transactions have been facilitated by the use of the United States dollar. No short-term transfer problems are associated with the balance of payments. The foreign exchange constraint felt by most developing countries has been obviated by the dollars circulating in the economy and the ability to borrow.

In the late 1980s, the financial system consisted largely of banking. Panamanian businesses relied relatively little on public stock or bond issues. No formal stock exchange existed; supervised, independent brokers handled the limited trading in regulated financial certificates, stocks, and bonds. In addition, some insurance companies, savings and loan associations, and unregulated consumer-finance companies were formed. The country's social security fund invested in government bonds and various development projects.

Fiscal Policy

Panama's financial stability and international credit standing were determined not by monetary policy, but principally by fiscal policy and balance of payments. Fiscal policy was thus more important for Panama than for most other countries, and as a result, public-sector deficits were especially problematic for the government.

From 1971 through 1975, the annual average for the consolidated public-sector deficit was 6.5 percent of GDP. That figure nearly doubled to 12.9 percent between 1976 and 1980, at the height of government spending on infrastructure and ambitious social programs. In the 1980s, the figure has declined, from 10.8 percent in 1982 to 5.8 percent in 1984 (see table 14, Appendix A). The 1982 figure represented an aberration, brought about by the political uncertainty and lack of fiscal restraint following Torrijos's death. Most impressively, the deficit was reduced to 2.5 percent of GDP in 1985, a figure even lower than the 3.5 percent targeted by the IMF. The reduction was brought about by increased revenues, reduced expenditures, and streamlined administration.

Budget Process

Panama developed an efficient and centralized budgetary system in the mid-1960s. By law, the budget had to balance, so increasing recourse was made to handle some expenditures outside the budget. One such device was the creation of autonomous government agencies. These agencies increased in numbers and importance in the 1960s and 1970s. Their areas of operation included banking, the national electrical system, welfare, tourism, and gambling. Their budgets were excluded from that of the central government, although various transfers were made.

The collection of direct taxes (on income, businesses, and corporations) was relatively efficient in Panama. Direct taxes totalled 7 percent of GDP in 1983. Although this figure is high compared with those of other countries in the region, direct taxes have brought stability to Panama's budget system and avoided the fluctuations that occurred in neighboring countries, which were more dependent on import and sales taxes. In the late 1980s, only a fraction of Panama's revenue was derived from taxes levied on foreign trade.

Revenues

In the first half of the twentieth century, Panama's tax base was narrow, and taxes were regressive. Up to 40 percent of the urban work force was employed in the Canal Zone (including most of

Ship transits Miraflores Locks, Panama Canal
Courtesy Agency for International Development

those with higher wages) where, because of treaty arrangements, their incomes could not be taxed by Panama. The rural population was largely untaxed because of farming's subsistence nature and the high costs of collecting rural taxes. Before the 1940s, over half of the taxes were from imports, mainly consumption goods for urbanites.

A 1955 treaty revision substantially expanded government revenue sources. The treaty permitted taxation of Panamanians working in the Canal Zone; it increased wage scales for those workers. A major tax reform, undertaken in 1964, made individual and corporate income taxes more progressive and improved the procedures for tax collection. By 1968 the tax structure compared favorably with that of other developing countries. Nearly half the tax revenues came from taxes on income and wealth; import duties and excise taxes on nonessential commodities provided an additional 15 percent of tax revenues.

The structure of government current revenue changed in 1979 because of the implementation of the Panama Canal treaties. Total revenue increased from US$477 million in 1979 to US$986 million in 1985. Direct taxation grew as a share of revenue, from 45.2 percent in 1979 to 52.6 percent in 1985. Tax receipts (direct and indirect taxation), as a share of revenue, dropped from 84.9 percent in 1979 to 69.8 percent in 1985. The drop was brought about primarily by the rise in the annual income received from operating the canal, which accounted for about 40 percent of non-tax revenue in 1985. Other sources of non-tax revenue included royalties and taxes from the trans-isthmian oil pipeline and levies on gambling.

Expenditures

In the 1950s and most of the 1960s, the expansion of revenue sources and the growing economy permitted an increase in government expenditures. Spending remained concentrated on the canal, and only a small share went to agriculture, industry, or commerce. Government investments were not large, but revenues financed only a part of them, thereby requiring a substantial increase in the public debt to fund the remainder. Expanding private investment was achieved through a high rate of private savings in spite of a considerable increase in per capita private consumption in the terminal cities.

In the 1970s, government current expenditures expanded dramatically. Most of that increase was a result of the rise in interest payments on the public debt, from 2 percent to 6 percent of GDP. In 1979 expenditures totalled US$554 million, most of which covered administrative costs (52.4 percent) and interest payments (23.6 percent). By 1985 expenditures had risen substantially to US$1.4 billion, but the actual structure of government expenditures changed very little; administrative costs accounted for 56 percent of the budget, followed by interest payments at 32.3 percent.

Between 1972 and 1983, the share of total expenditures fell in the categories of education (from 20.7 percent to 11.0 percent), health (15.1 percent to 13.1 percent), and economic services (24.2 percent to 13.5 percent). The share of expenditures allocated for housing, amenities, social security, and welfare rose during the same period from 10.8 percent to 12.2 percent. The biggest increase, however, was in the "other" category, which rose from 29.1 percent to 50.2 percent, mostly because of a larger debt service share (including interest payments and amortization).

Human Resources and Income

A 1985 World Bank study concluded that in spite of a relatively well-educated work force, unemployment was Panama's "gravest economic and social problem." The unemployment rate climbed steadily, from 8.1 percent in 1978 to 11.8 percent in 1985. The study predicted that the unemployment situation would further deteriorate unless the government took forceful measures to change structural rigidities in the labor code and market. Legislation approved in March 1986 addressed some of the rigidities in the 1972 labor code. Those changes may have been responsible, at least in part, for the lowering of the unemployment rate in 1986 to 10 percent.

Employment

As a result of declining birth rates and stabilizing mortality rates, Panama's overall population growth rate fell from an annual average of 2.6 percent between 1965 and 1980 to 2.2 percent between 1980 and 1985 (see table 2, Appendix A). The working-age population (15 years and over) increased from 1,011,700 in 1978 to 1,256,800 in 1985, at a rate of approximately 4 percent a year. From 1970 through 1984, the rate of job creation was less than half the growth rate of GDP. Analysts have estimated that the economy would have to grow indefinitely by 7.5 percent a year to absorb new entrants into the labor market—a level almost impossible to sustain and far above Panama's average annual growth rates in the past.

Panama's experience suggested that a government's ability to improve the employment situation through direct intervention in the labor market is severely limited. In the 1960s, an average of 13,000 new jobs were created each year. During the recession in the 1970s, unemployment rose dramatically. In late 1977, the government sought to reverse the deteriorating employment situation with an emergency jobs program. As a result, 28,000 new jobs were created within a year—20,000 of which were in the public sector. The employment program drained government resources, however, and in 1980 it was terminated. Only 11,000 jobs were created annually between 1979 and 1982.

In 1985 the sectoral distribution of the labor force reflected shifts that had taken place since the 1960s (see table 15, Appendix A). The services sector, led by financial services, continued to grow and accounted for 57.4 percent of the total labor force in 1985. Agriculture (including forestry and fishing) consistently experienced a relative decline, but still furnished 26.5 percent of the jobs. Industry's share of the labor force grew slightly between 1965 and 1980, but dropped to 16.1 percent in 1985.

The public-sector share of total employment rose slightly from 11 percent in 1963 to 13.1 percent in 1970. With the expansion of the public sector in the 1970s under Torrijos and the Emergency Employment Program in 1977, that share peaked at 25.1 percent in 1979. In 1982 the public sector still accounted for 25 percent of total employment.

Wage Policy and Labor Code

Panama's salaries were high by regional standards in the mid-1980s. In a 1982 study comparing salaries in manufacturing, Costa Rica's average monthly salary was only 41 percent that of Panama's; Guatemala's, 71 percent; and Honduras's, 84 percent. In 1985 the average monthly salary in Panama was US$450, but that figure was influenced by salaries in the canal area, which averaged US$1,300 per month. In 1985 the minimum wage in the metropolitan area was US$0.82 per hour; that wage was adjusted for location and type of industry.

In the 1970s, the government became heavily involved in labor matters and intervened actively to increase wages. Although a labor code had existed for many years, only the minimum wage provisions were consistently enforced. In 1971 two decrees were issued; the first imposed an education tax and the second required employers to pay workers an extra month's wage each year.

In early 1972 a broad labor code, patterned after that of Mexico, substantially changed labor-management relations. Workers' security, benefits, and bargaining power were increased considerably. Collective bargaining and unionization were encouraged and resulted in rapid growth of union membership (see Business, Professional, and Labor Organizations, ch. 4).

Although the 1972 labor code contributed to political stability in the 1970s, it substantially raised costs for employers, especially those in labor-intensive activities. The code also created disincentives to further hiring and private investment. Employers were prohibited from reducing a worker's salary. Therefore, piecework and assembly-type industries could not reward workers on the basis of productivity. As a partial result of these rigidities, Panama's labor costs were among the highest in the Caribbean Basin. According to a 1984 World Bank report, the annual cost of running a textile plant with 500 workers was US$588,300 in Haiti; US$789,800 in Costa Rica; US$919,700 in the Dominican Republic; US$1,048,500 in Colombia; US$1,057,600 in Mexico; and US$1,156,700 in Panama. Only Jamaica's costs were higher (US$1,828,300).

The labor code caused the effective cost of wages to rise, fueling inflation and discouraging private investment. The government, unable to devalue the currency, was forced to address the root of the problem—high labor costs. Law 95, which became effective in 1977, modified provisions of the labor code that related to job security and benefits. Previously, employers could only dismiss workers during their first two years on the job; that term was extended to five years. New provisions inhibited union actions, such as strikes, and imposed a two-year moratorium on collective bargaining agreements, which froze wages.

As a condition for the disbursement of a structural adjustment loan, the World Bank in 1985 recommended making the code more flexible. Panama's then-President Nicolás Ardito Barletta Vallarino (October 1984–September 1985) fully backed the World Bank recommendations. Opposition from unions and from within his own party, the Democratic Revolutionary Party (Partido Revolucionario Democrático—PRD), forced Ardito Barletta to withdraw the proposed changes and contributed to his resignation. His successor, Eric Arturo Delvalle Henríquez, was more successful. In March 1986, the Legislative Assembly approved major reforms in the labor code, in spite of widespread protests and a ten-day work stoppage by the unions. The changes included production-based wages, uniform rates of overtime pay, piecework provisions, removal of protective measures in industry, and flexible agricultural pricing. On the whole, the labor code modifications were aimed at making Panama's industry and agriculture more competitive internationally and expanding employment opportunities. Nonetheless, the economy was deemed likely to continue to experience high unemployment, especially in the metropolitan area, where unemployment rates tended to be much higher than the national average.

Income Distribution

One of Torrijos's major goals was to address the problem of unequal income distribution, which during the 1960s was one of the most skewed in the world. In 1970 the richest quintile (20 percent) of the households received 61.8 percent of the income; in stark contrast, the poorest quintile received only 2 percent of the income. Results of a study conducted in 1983 by the Panamanian government suggested that the Torrijos policies did, in fact, make income distribution more equitable. The income share of the richest quintile fell to nearly 50 percent, while all other income groups increased their share: the fourth quintile (second-to-richest) from 20 percent to 23 percent; the third quintile from 11 percent to 15 percent; the second quintile from 5 percent to 9 percent; and the first (poorest) quintile to 3 percent. Nevertheless, despite the program's success, the 1983 study confirmed a continuing pattern of a relatively prosperous metropolitan area and poor rural provinces.

Panama Canal

The Panama Canal continued to play a central role in world trade and Panama's economy in the mid-1980s. Some 5 percent of the world's trade in goods passed through the canal, contributing 9 percent of Panamanian GDP in 1983. This canal's location at one of the crossroads of international trade has spawned a plethora of other service-oriented activities, such as storage, ship repair, break bulk (the unloading of a portion or all of a ship's cargo), transshipment, bunkering, and distribution and services to ship travelers. The dynamism of the canal also was instrumental in the development of the CFZ, the trans-isthmian pipeline, and offshore financing. Evidence suggests, however, that the canal's relative importance to world trade is likely to continue to experience a small relative decline in the future, which has led Panama, together with the United States and Japan, to study alternatives for improving or replacing the canal.

Role of the Canal from 1903 to 1977

In 1903 the United States secured the right, by treaty, to build a canal across Panama (see The 1903 Treaty and Qualified Independence, ch. 1). The United States rejected plans to build a sea-level canal similar to that attempted by the French and opted instead for a system based on locks. Construction began in 1907 and was facilitated by medical work that largely eradicated yellow fever and reduced the incidence of malaria (see Building the Canal, ch. 1).

Construction of the canal involved damming the Río Chagres to create the huge Gatun Lake in the middle of the isthmus. Channels were dug from each coast, and locks were built to raise and lower ships between sea level and Gatun Lake. Three sets of locks were constructed: Gatun Locks on the Atlantic side and the Pedro Miguel and Miraflores Locks on the Pacific side. The lock chambers were 303 meters long by 33 meters wide, which limited vessel size to approximately 287 meters in length and 32 meters in width. Distance through the canal is eighty-two kilometers, and in 1987 transit took about fifteen hours, nearly half of which was spent in waiting. The canal began commercial operations in 1914.

The United States operated the canal and set tolls from the beginning of operation. Tolls covered operation costs but were kept low to encourage canal use. Direct benefits to Panama were minimal, consisting of annual annuity payments that increased infrequently, usually in response to Panamanian demands. In the 1975 to 1977 period, the annuity payments reached US$2.3 million a year. Indirect benefits to Panama's economy were substantial, however, and included the jobs of its citizens working in the Canal Zone, value of goods and services sold to the Canal Zone and to passing ships, and expenditures by visitors.

Economic Implications of the 1977 Treaties

The 1977 treaties and the related documents, which became effective October 1, 1979, signaled important changes for the Panamanian economy. The most obvious benefit was in receipts from operation of the canal. Under the terms of the treaties, the government of Panama receives from the Panama Canal Commission: a fixed annuity of US$10 million; an annual payment of US$10 million for public services such as police and fire protection, garbage collection, and street maintenance, which Panama provides in the canal operating areas and housing areas covered by the treaties; a variable payment of US$0.30 per Panama Canal net ton (see Glossary) for each vessel transiting the canal (in 1986 this amounted to US$57.6 million); and an additional annuity, not to exceed US$10 million, to be paid only when canal operations produce a profit. In 1986, for example, US$1.1 million was paid; in 1984, on the other hand, canal operations registered a US$4.1-million loss, and no payment was made.

The United States controls the tolls because of its majority (five members) on the nine-member Panama Canal Commission, which will operate the canal until December 31, 1999 (see The 1977 Treaties and Associated Agreements, ch. 1). In order to encourage use of the canal, tolls have remained relatively low, although high enough to cover costs. (Under the United States law that implemented the canal treaties, the canal must be operated on a self-sustaining basis.) Maximum use of the canal is in Panama's interest, because its annuity depends on transit tonnage. Tolls were raised by nearly 30 percent in October 1979 and by an additional 9.8 percent in March 1983.

Under treaty provisions, the canal administrator is an American and his deputy is a Panamanian. In 1989, a Panamanian will become administrator and the deputy an American. In order to prepare Panama to assume operation of the canal in the year 2000, the Panama Canal Commission has encouraged the hiring and training of Panamanians for all types of canal-related work. The commission's work force was approximately 82 percent Panamanian in 1987.

According to the treaty provisions, Panama also received substantial assets in the former Canal Zone, including three large ports (Colón, Cristóbal, and Balboa), the railroad across the isthmus, two airfields, 147,700 hectares of land (including housing, utility systems, and streets), a dry dock, large maintenance and repair shops, and service facilities formerly operated by the Panama Canal Company (see fig. 3). Ownership and operation of the canal ports of Balboa and Cristóbal were transferred to Panama in October 1979, but a portion of these port facilities will continue to be used by the Panama Canal Commission for canal operations until the year 2000. Panama also received housing that belonged to the former Panama Canal Company but will continue to supply housing to the Panama Canal Commission and the United States Department of Defense in decreasing amounts until 2000. Some assets and functions of the government of the former Canal Zone, such as schools and hospitals, are maintained by the United States Department of Defense. The Panama Canal Commission continues to operate utilities in the zone areas that it received under the treaty.

The 1977 treaties had important provisions concerning employment and wages. Panamanians would gradually replace United States citizens in the operation of the canal. Perhaps most important was the provision that former Canal Zone employees who became employees in Panama under the treaties were guaranteed wages and conditions similar to those that their position in the zone had commanded. In 1979 a zone employee received about twice the wages of someone employed in a similar position elsewhere in the economy. The canal areas will therefore continue to exert a pull on other domestic wages, making the country less competitive internationally.

Current Use and Future of the Canal

In both the short and the long term, the impact of the 1977 treaties on the economy will depend to a large extent on canal traffic. Since 1979, when the treaties went into effect, the amount of canal traffic has stagnated. In 1979 the canal was transited by 13,056 ships; by 1984 that number had fallen to 11,230—the lowest number in 2 decades. Cargo tonnage also dropped during the same period, from about 154 million to about 140 million tons. Despite the decline in the number of ships and cargo tonnage, toll revenues expanded over the period from US$208 million to US$298 million because of the toll increase in March 1983.

The decline in canal traffic was in large measure a result of the opening of the trans-isthmian oil pipeline, which carries Alaskan North Slope oil. In 1983 the pipeline diverted 30 million tons of oil from the canal. In terms of Panama's economy, the diversion of oil from the canal to the pipeline did not cause alarm as it was little more than a transfer of services.

Some observers expressed concern that the canal had seen its best days and that it would decline in importance over the long run. Latin American trade, much of which passes through the canal, has stagnated because of prolonged regional recession and balance

Thatcher Bridge over Panama Canal
Courtesy Pan American Union

of payments constraints resulting from the regional debt crisis. Many supertankers and bulk cargo carriers are too big for the canal. Even some smaller vessels sought to avoid the delays associated with transiting the canal. Increased tolls also lowered the demand for canal usage. Many coal and banana producers shunned the canal and shipped to Europe from the Caribbean Basin and to the Pacific Basin from the west coast of Latin America. In addition, the canal faced competition from Mexican and United States land bridges (roads or railroads linking Atlantic and Pacific ports). Standardized cargo containers have made land bridges an increasingly attractive option, even though the distances involved are much greater (the United States land bridge is over 5,600 kilometers long) than across the canal. The concern over the future of the canal was partially allayed by the increase in total canal traffic between 1984 and 1986. In 1986 11,925 ships transited the canal, carrying 139 million long tons of cargo and generating US$321 million in tolls and revenues. In 1987 canal tolls and revenues totaled US$330 million. The increase in 1986 was due in large measure to increased automobile trade.

In 1982 Panama joined the United States and Japan, the two principal users of the canal, in an agreement to establish a tripartite commission aimed at studying improvements in or alternatives to the canal. The US$20-million study was expected to be ready in 1991. One modest proposal, at a cost of US$200 million, was that of widening the canal at the Gaillard Cut, its narrowest channel. The Gaillard Cut measured approximately 100 meters when the canal opened in 1914, and in the 1960s it was broadened to about 165 meters. The proposal called for doubling the width of the Gaillard Cut. A more extensive plan, at a cost of US$500 million, proposed widening the entire canal by 16 meters to allow for uninterrupted 2-way traffic along the waterway. The canal's existing capacity was forty-two vessels a day; the less expensive proposal would accommodate fifty ships. The most ambitious plan, however, was that for a second, sea-level canal, which could handle even the largest supertankers without the use of locks. This plan's estimated cost was US$20 billion, considered prohibitive in the light of foreseeable toll revenues. Alternatives to a second canal included an improved railroad system, an express highway for container traffic, and additional pipelines.

Services

Panama's services sector dwarfed agriculture and industry, and its share of GDP was growing in the late 1980s. In 1965 services accounted for about 63 percent of GDP; by 1985 that share had risen to about 73 percent. In the latter year, transportation contributed 25.3 percent of GDP, followed by financial services (14 percent), government services (13.2 percent), wholesale and retail trade (12.3 percent), and other services (8.1 percent).

Transportation and Communications

Transportation was the single most important contributor to Panama's service-oriented economy. The Panama Canal has given great impetus to other transportation services, and many of those, such as the oil pipeline and the CFZ, have achieved a dynamism of their own. In the area of communications, Panama was served by 213,400 telephones in 1984, in addition to 142 radio stations, 6 television channels, and 6 daily newspapers.

The transportation sector has been further broadened by a network of roads, ocean ports, and airports (see fig. 8). The major roads were the Pan-American Highway and the Trans-isthmian Highway (also known as the Boyd-Roosevelt Highway) between Panama City and Colón. In 1984 Panama had 9,535 kilometers of roads, of which 32 percent were asphalted. Panama had only three railroads: two in the west originating in David and Almirante and extending to the Costa Rican border, and one linking Panama City and Colón. The General Omar Torrijos Herrera International

Airport (commonly known as Tocumen International Airport), located near Panama City, served international airlines.

Panama had fourteen ports, the most important of which were Balboa on the Pacific side and Cristóbal on the Atlantic, located at the entrances to the canal. Together, the two ports served 70 percent of the international ships arriving in Panama in 1983. The two ports, however, have declined in regional importance since the 1970s, in part because of technological change and competition. In their prime, Balboa and Cristóbal were transshipment centers of break-bulk traffic. In the 1970s, containerization became widespread; large ships could break the bulk cargo into containers at any port offering container facilities, at which point the cargo could be stored or transshipped through the canal on a smaller vessel. Miami and Kingston developed sophisticated container facilities and contributed to the precipitous decline (from 145,000 tons in 1969 to 38,707 tons in 1980) in transshipment traffic through Balboa and Cristóbal. In order to compete more effectively, US$18 million was spent on Cristóbal in the early 1980s, making it the first container port in Panama. Later plans call for upgrading eight other ports as well.

Oil Pipeline

The trans-isthmian oil pipeline served as a transshipment point for Alaskan North Slope oil en route to the east coast of the United States. The pipeline, completed in October 1982, was 81 kilometers long and had a capacity to move 850,000 barrels of oil a day. The pipeline joined two terminals owned by Petroterminales de Panamá, a joint venture between the Panamanian government and a United States company, Northville Industries.

In 1982 the pipeline generated US$69 million, a figure that rose to US$138.8 million in 1986. The pipeline accounted for 7.4 percent of Panama's GDP in 1985, when value added peaked at US$158.7 million; in 1986 its share of GDP fell to 6 percent. In fact, the pipeline's net contribution to GDP has been small. Despite the increase in activity since 1982, the pipeline has never reached capacity; its daily throughput in mid-1987 was 575,000 barrels. Moreover, if the pipeline had not been built, the transportation of oil across the isthmus could still be accommodated by the canal. The pipeline did, however, free up the canal and was expected to make a greater net contribution to GDP.

Panama's oil pipeline faced competition from the All American Pipeline, which extended from Santa Barbara, California, to McCarney, Texas, where it connected with other pipelines that led to the east coast of the United States and to the Gulf of Mexico.

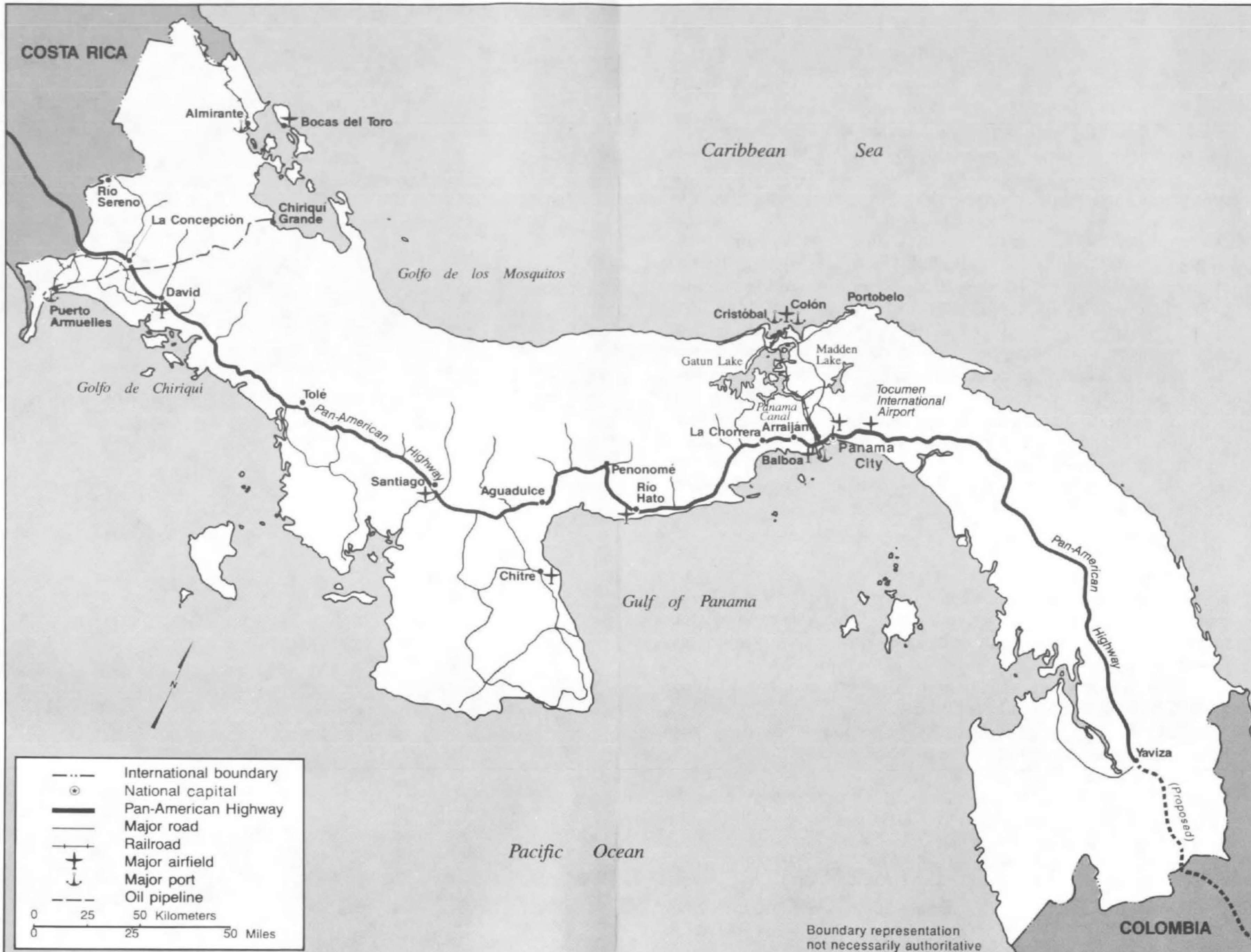


Figure 8. Transportation System, mid-1980s

Nearly completed in 1987, the new pipeline, owned by Celeron Oil Company, was the longest in the United States. Whether the American pipeline would be able to compete effectively with Panama remained uncertain; overland pipeline transport was generally more expensive than sea transport in large tankers.

Colón Free Zone

The CFZ has grown rapidly to become the second largest free zone in the world, after Hong Kong. The CFZ, in existence since 1953, was a base for 460 companies in the late 1980s. Goods from foreign countries were landed and stored or repackaged there and shipped onward without being subject to Panama's customs duties. Among the CFZ services offered were commercial intermediation, break bulk, warehousing, assembly, and transshipment. In addition to its excellent location, foreign firms were attracted to the CFZ because of good transport, communications, and banking services. A state-owned corporation operated the free zone, providing the necessary infrastructure and services.

The CFZ has contributed greatly to Panama's economy. In 1983 the CFZ provided direct employment for 6,000 workers. CFZ earnings in export services were second only to the canal. In 1985 CFZ imports and re-exports totalled US$3.3 billion, down from a peak of US$4.3 billion in 1981; value added in the CFZ made a net contribution of 2.8 percent to GDP. The declining figures reflected the Latin American recession and the concomitant fall in regional trade. The CFZ linked producers in industrialized countries, which in 1984 supplied 60 percent of CFZ imports, primarily with Latin American countries, and accounted for 59 percent of CFZ exports. Since 1983 Japan's exports to the CFZ have surpassed those of the United States; in that year, Japan exported 21 percent of the goods entering the CFZ, followed by the United States (15.5 percent), Taiwan (10 percent), and Hong Kong (9.3 percent).

Observers believed that dependence on the Latin American markets might limit the growth potential of the CFZ. Other constraints to growth included competition from Miami and the tendency of Latin American countries to circumvent the CFZ through bilateral transactions. The greatest potential for CFZ growth lay in expanding manufactured exports, especially to the United States, under the terms of the Caribbean Basin Initiative (CBI). Until the mid-1980s, the value added for manufacturing in the CFZ was rather small; transport, storage, and warehousing contributed the largest share. CFZ activities declined between 1982 and 1984, but stabilized in 1985 and expanded by 15 percent in 1986.

Finance

Panama was considered the most important international banking center in Latin America in the late 1980s. In 1970 only 28 banks operated in Panama's international banking center; by 1987 there were 120, with assets of nearly US$39 billion. The growth in Panama's Eurocurrency (see Glossary), or offshore banking, has contributed to the country's relative prosperity and accentuated the importance of the services sector in the economy. As an example of offshore banking, the Central Bank of India established an office in Panama in the late 1970s to finance its trade with Brazil.

The idea of opening Panama up to international banking was the brainchild of Ardito Barletta, who, as Torrijos's minister of planning in 1969, sought to diversify Panama's economy away from the canal and the CFZ. His timing could not have been better; Panama benefited greatly from the recycling of petrodollars after the 1973 and 1979 oil price hikes. Panama also became a center for flight capital from Latin America and tax evasion dollars from the United States and other countries.

Panama's success in attracting offshore banking has been attributed to the political stability of the Torrijos years, the dollar-based economy, the country's tradition as a trade and business center, and a policy of low taxes on deposits and income. Most importantly, however, Panama's success has been a result of its stringent secrecy laws. In 1970 banking laws were liberalized, secrecy was guaranteed, currency controls were abolished, and few restrictions were imposed on bank transactions. Panama's banking commission had the sole right to conduct general inspections of bank records, and banks were not allowed to disclose information concerning their customers. Ardito Barletta once claimed that Panama's secrecy laws were stricter than those of Switzerland.

Observers disagreed on the benefits derived from offshore banking. Banks were required to maintain offices in Panama, where they generated employment for 10,000 Panamanians, slightly more than the number of jobs associated with the canal. Approximately US$200 million has been injected into the domestic economy each year through loans. Some critics have charged, however, that the offshore banking has "denationalized" Panama's economy. According to this line of thought, offshore banking limits a nation's political and economic autonomy because the government must maintain a favorable investment climate. International capital is highly fungible and is subject to flight in the event of major political or economic disturbances, as occurred in the latter part of 1987.

Panama City street
Courtesy Organization of American States

Total deposits in the offshore banks peaked at US$47 billion at the end of 1982 and then fell, primarily as a reflection of Latin America's financial crisis. In 1984 numerous United States banks reduced their Panamanian assets, such as Citibank (by 70 percent) and Bank of America (50 percent). Some banks (Chase Manhattan and Citibank) also reduced their operations within Panama, while others (Security Pacific and Libra Bank International, a London-based consortium) actually left Panama. This drain, however, was partially offset by the increased exposure of other United States banks, such as First National Bank of Chicago, and by the influx of Japanese banks, many of which have made Panama their Latin American banking headquarters. Also, "narcodollars" (income derived from the sale of illegal drugs) reportedly were transferred to Panama from Caribbean havens that were placed under closer scrutiny.

In 1985 the largest banks in Panama's International Financial Center were First National Bank of Chicago (assets worth US$3.6 billion); Banco de la Nación Argentina (US$2.8 billion); American Express Bank (US$2.4 billion); BNP (US$1.4 billion); Deutsche Sudamerikanische Bank (US$1.3 billion); Crédit Lyonnais, Sanwa Bank, Bank of Tokyo, and Sumimoto Bank (US$1.2 billion); and Banco do Brasil (US$1.1 billion).

The foreign share of total deposits in the International Financial Center declined from 94 percent in 1979 to 85 percent in 1985. The assets of 14 Panamanian banks remained virtually constant, at US$5.5 billion from 1982 through 1984; their relative share of total deposits increased from 10 percent in 1982 to 15 percent in 1985 as a result of the reduction of foreign deposits. Founded in 1904, the BNP was the country's most important bank. It served as the government's depository and fiscal agent in addition to being the largest commercial bank with forty-seven branches throughout the country and an agency in New York. The other major state-owned financial institutions were a savings bank (established 1934), a mortgage bank (1973), an agricultural development bank (1973), and a development finance company (1975). The latter two institutions were founded to provide longer-term credit for agricultural and industrial development than was generally available from the commercial banks.

Panama's offshore banking confronted severe challenges in the late 1980s. Firstly, it faced charges that it had become the center for laundering drug money. Given the secretive nature of Panama's banking legislation, substantiating such charges was difficult. According to the United States Department of the Treasury, an estimated US$600 million in drug-related money is laundered through Panama's offshore banking system annually. Since 1985 the United States has pressured Panama to sign the Mutual Legal Assistance Treaty (MLAT), which lifts banking confidentiality. A similar treaty has been signed by the Cayman Islands, the Netherlands Antilles, the Turks and Caicos Islands, Switzerland, Turkey, and Italy. Although Panama has resisted any changes in its banking secrecy regulations, fearing negative repercussions on its International Financial Center, it did make major concessions in a law passed on December 26, 1986. The new law had three basic provisions: penalties for drug trafficking were made more severe; extradition procedures were established; and money-laundering was made a crime. The measures fell short of those established in the MLAT, but they were expected to deflect United States criticism, at least in the short term (see Other Aspects of Panamanian-United States Relations, ch. 4; Involvement in Political and Economic Affairs, ch. 5).

A second major challenge to offshore banking in Panama was that of political instability. The political turmoil of mid-1987 damaged Panama's reputation as a safe haven. International banks were a major target for attacks by progovernment groups seeking to blame foreign elements for the political disturbances. In June the government further shattered investor confidence when it suspended interest payments on its debt to foreign governments, a de facto default. One international bank lowered Panama's rating on the political risk scale, and First National Bank of Chicago closed its Panama branch. Perhaps one-tenth of the estimated US$40 million in deposits left the country as capital flight, creating a liquidity crisis for the country.

Tourism

Panama offered a wide range of tourist attractions and gambling facilities. In 1983 the National Tourism Council was founded to coordinate national tourism in conjunction with the Panamanian Tourism Institute. The number of tourists peaked in 1980 at 377,600 and declined to 302,400 in 1984. Despite the reduction, the expenditures by visitors (in addition to tourists, this category includes travel that is related to business and education) remained virtually unchanged, at about US$130 million per year from 1979 to 1983. During the same period, travelers in transit (including those only changing planes and those who remained in Panama up to 48 hours) injected an additional US$38 million per year into the economy.

Agriculture

For centuries agriculture was the dominant economic activity for most of Panama's population. After construction of the canal, agriculture declined; its share of GDP fell from 29 percent in 1950 to just over 9 percent in 1985. Agriculture has always employed a disproportionate share of the population because of its labor-intensive nature. Nevertheless, the percentage of the labor force in agriculture has also dropped, from 46 percent in 1965 to 26 percent in 1984.

In 1985 crops accounted for 63.3 percent of value added in agriculture, followed by livestock (29.5 percent), fishing (4.3 percent), and forestry (2.9 percent). Despite its relative decline, agriculture was the main supplier of commodities for export, accounting for over 54 percent of total export earnings in 1985. The agricultural sector satisfied most of the domestic demand. The principal food imports were wheat and wheat products, because climatic conditions precluded wheat cultivation. In 1985 the value of food imports was US$108.7 million (8.8 percent of total imports), only half that of food exports.

Between 1969 and 1977, the government undertook agrarian reform and attempted to redistribute land. The expanded role of the state in agriculture improved social conditions in rural areas, but long-term economic effects of the agrarian reform were modest. In the early and mid-1980s, the government sought to reverse the decline of agriculture by diversifying agricultural production, lowering protection barriers, and reducing the state's role in agriculture. In March 1986, the government instituted major changes in the agricultural incentives law and removed price controls, trade restrictions, farm subsidies, and other supports.

Land Use

Panama's land area totals approximately 7.7 million hectares, of which forests account for 4.1 million hectares, followed by pasture land (1.2 million hectares) and permanently cultivated fields (582,000 hectares). About 2 percent of the land was used for roads and urban areas. Nearly all of the cultivated and pasture land was originally forested. A large amount of virgin land has been opened up for cultivation by the Pan-American Highway.

Panama's climate and geology impose major constraints on the development of agriculture. Heavy rainfall throughout the year prevents cultivation of most crops on the Atlantic side of the continental divide (see Regions of Settlement, ch. 2). The Pacific side has a dry season (December to April) and accounts for most of the cultivated land (see fig. 9). The mountainous terrain also restricts cropping. In addition, the country does not have high-quality soils. Most of the areas classified as cultivable are so considered on the assumption that farmers will practice conservation measures, but many do not. The topsoil is thin in most areas, and erosion is a serious problem. Most of the nearly level areas conducive to cultivation are in the provinces of Los Santos, Coclé, Veraguas, and Chiriquí.

A further constraint on production is the practice of slash-and-burn cultivation, in which trees, brush, and weeds are cut and then burned on the patch of ground selected for cultivation. Indians utilized the slash-and-burn method for centuries, and the Spanish made few changes in techniques. In the 1980s, most farmers practiced a slash-and-burn type of shifting cultivation. The thin and poor-quality topsoil yielded an initially good harvest, followed by a smaller harvest the second year. Typically, the land was cultivated for only two years, and then the farmer repeated the process on another plot, allowing the first plot to rest ten years before refarming.

Much of the farming was of a subsistence nature and accomplished with a minimum of equipment. Plowing was generally not practiced on subsistence farms; the seeds were placed in holes made by a stick. Tree cutting, land clearing, weeding, and harvesting were accomplished with a few kinds of knives, principally the machete and the axe, which comprised the major farm implements.

Land Tenure and Agrarian Reform

Before the 1950s, land was readily available to anyone who was willing to clear and plant a plot. The cutting and clearing of forests greatly accelerated as the population increased. By the 1960s, subsistence farmers sometimes reduced the rest period of cleared plots from ten years of fallow to as few as five years because of the unavailability of farm land. The reduced fallow period diminished soil fertility and harvests. Consequently, cropped acreage peaked during the 1960s. The hard life and low income of farmers accelerated the exodus of workers from the countryside to the cities (see Rural Society and Migration, ch. 2).

The long period when new land was easily obtainable contributed to a casual attitude toward land titles. In 1980 only 32.9 percent of the 151,283 farms had such titles. The decline in available agricultural land has made land titling more necessary. Moreover, insecure tenure has been a particularly severe constraint to improved techniques and to commercial crop production. The cost of titling a piece of land, however, has been too high for most subsistence farmers.

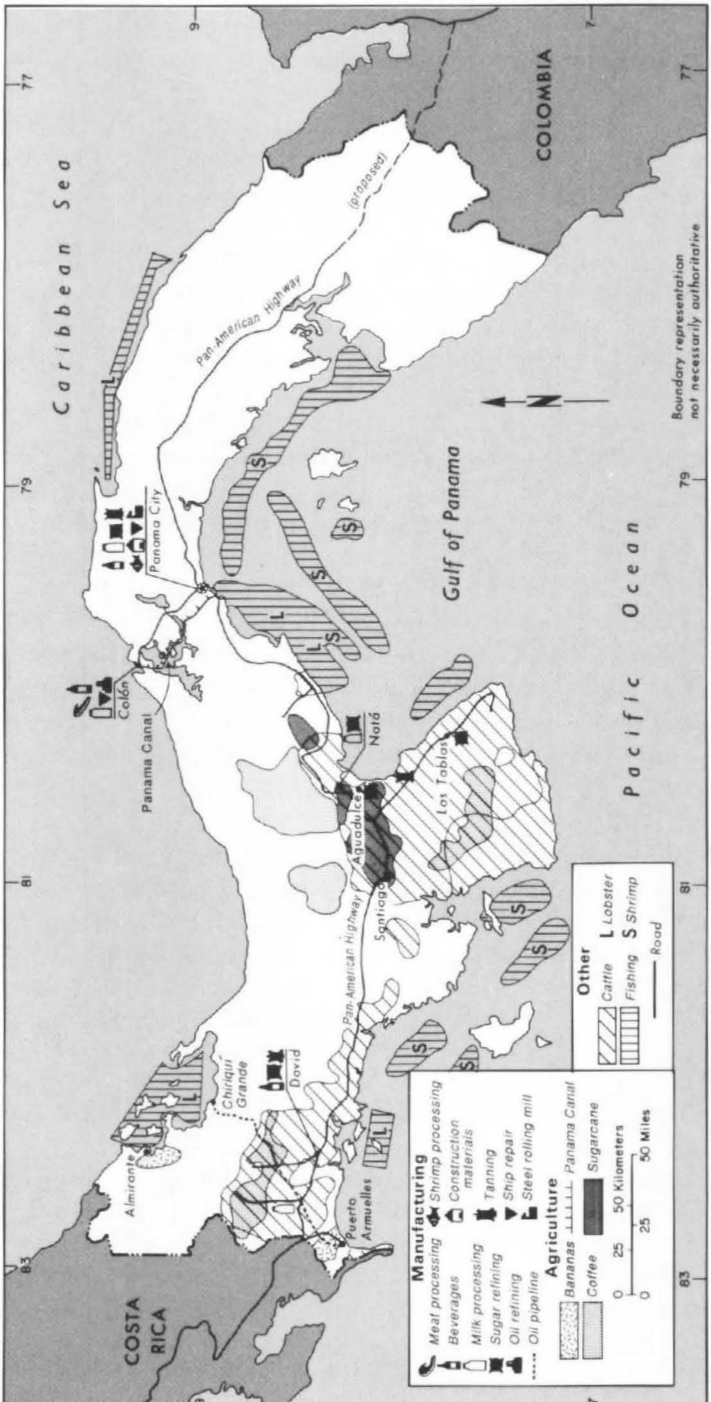


Figure 9. Location of Major Economic Activity

Between 1969 and 1977, the government attempted to redistribute land. In the late 1980s, however, the distribution of land and farm incomes remained very unequal. In 1980 58.9 percent of farms had an annual income below US$200. The issue of unequal land distribution, however, has not been as explosive in Panama as in many other Latin American countries. This was because of the service-oriented nature of the economy and because about half of the population lived in or near Panama City. Also, about 95 percent of all farm land was owner-operated, and virtually all rural families owned or occupied a plot.

In an effort to redistribute land, the government acquired 500,000 hectares of land and expropriated an additional 20 percent of the land. About three-quarters of the land acquired was in the provinces of Veraguas and Panamá. By 1978 over 18,000 families (about 12 percent of rural families in the 1970 census) had access to either individual plots or collectively held land as a result of the redistribution. The land acquisition created uncertainty, however, and adversely affected private investment in agriculture, slowing production in the 1970s.

As part of its agrarian reform, the government placed heavy emphasis on organizing farmers into collectives for agricultural development. Several organizational forms were available, the two most important being *asentamientos* (settlements) and *juntas agrarias de producción* (agrarian production associations). The distinctions between the two were minor and became even more blurred with time. Both encouraged pooling of land and cooperative activity. In some instances, land was worked collectively. Other organizational forms included marketing cooperatives, state farms, and specialized producers' cooperatives for milk, chickens, or pigs. Growth of these agricultural organizations slowed by the mid-1970s, and some disbanded, as emphasis shifted to consolidation.

The cost of agrarian reform was high. The government channeled large amounts of economic aid to organized farmers. Rural credit was greatly increased; farm machinery was made available; improved seeds and other inputs were supplied; and technical assistance was provided. Cooperative farm yields increased, but these higher yields were not impressive, considering the level of investment. Despite the high costs of the government programs, incomes of cooperative farmers remained low. After the mid-1970s, the government changed its policy toward cooperatives and stressed efficiency and productivity instead of equity.

Although the economic results of agrarian reform were disappointing, the social conditions of most farmers improved. The number of rural residents with access to safe water increased by

50 percent between 1970 and 1978. Improved sewerage facilities, community health programs, and rural clinics reduced mortality rates considerably. Major expansion of educational facilities, including education programs for rural residents, helped rural Panamanians become better educated and more mobile.

Crops

The crops category is the largest within agriculture, but its share has fallen slightly, from 66.1 percent in 1980 to 63.3 percent in 1985. During that period, crop production was erratic, and annual growth averaged a mere 1.7 percent. The major crops and foreign exchange earners were bananas and sugar. In the 1980s, however, crop production became increasingly diversified. The production of corn, coffee, beans, and tobacco has increased, as has that of such nontraditional products as melons and flowers. Fruits (especially citrus), cacao (the bean from which cocoa is derived), plantains, vegetables, and potatoes were produced on a minor scale; nevertheless, they were important cash crops for small farms.

Bananas were the leading export item, and in 1985 accounted for 23 percent (US$78 million) of total exports. In that year, the Chiriquí Land Company, a subsidiary of United Brands (formerly United Fruit Company), produced 70 percent of all bananas, followed by private Panamanian producers (25 percent) and the state-owned Corporación Bananera del Atlántico (5 percent). The volume of bananas produced in Panama peaked in 1978 and slowly declined in the 1980s. Observers doubted that United Brands would expand its production in Panama because bananas could be produced more cheaply in Costa Rica and Ecuador.

The history of banana production in Panama virtually coincides with that of United Brands, which has been in Panama since 1899. The company built railroads, port facilities, and storage areas for the processing and export of bananas. In the 1930s, a disease seriously curtailed banana production. In the 1950s, disease-resistant plants were developed, and production increased rapidly. In the early 1970s, a "banana war" erupted when banana-producing countries disagreed among themselves and with United Brands about an export tax on bananas. Panama threatened to take over United Brands' plantations. An agreement was reached in 1976 to tax banana exports. In that year, the tax provided the government with US$10 million, nearly 4 percent of all revenues. In addition, United Brands sold all 43,000 hectares of land that it owned in Panama to the government; payment was in tax credits. The government leased back to United Brands over 15,000 hectares for banana production and export operations. Part of the

Harvesting bananas
Courtesy Organization of American States

excess land went to the government's newly established banana companies.

Sugar has traditionally been Panama's second largest crop in terms of production and export value. Panama consumed about half its sugar output and exported most of the rest to the United States. The production of sugar in Panama increased during the 1970s, peaked in 1982 at 260,000 tons, and fell to 165,000 tons in 1986. The dramatic decline after 1982 was because of low world prices and the rapid reduction in the United States quota from 81,200 tons in 1983 to 26,390 tons in 1987. Annual sugar exports earned an average US$40 million from 1975 through 1981 but fell steadily from US$41.3 million in 1983 to US$33 million in 1984, US$27.3 million in 1985, and US$22 million in 1986.

The state has been heavily involved in Panama's sugar production. Under the 1983-84 structural adjustment program, however, the state has privatized, closed, and tried to sell numerous sugar mills. Nonetheless, of the six major sugar mills in Panama, four were still under state control in 1987. The largest was the Corporación Azucarera La Victoria, which in 1985 accounted for 64 percent of total sugar production. Several small mills operated throughout the country, but their output was for domestic consumption only.

The production of coffee has steadily expanded, from 7,000 tons in 1981 to 11,000 tons in 1985. Coffee was Panama's third-largest crop export earner. In 1985 it earned US$15.6 million, which was 4.6 percent of total export earnings.

Rice and corn production also increased in the early 1980s. Panama imported rice in the 1970s but by the mid-1980s experienced a surplus, as a result of the expansion of production in the early 1980s, from 178,000 tons in 1982 to 200,000 tons in 1985. Panama produced 75,000 tons of corn in 1985, but in the same year it imported about 40 percent of the corn it consumed, some of which was used for poultry feed. The government granted incentives to increase corn production.

Livestock

Panama was virtually self-sufficient in livestock production, which included cattle, pigs, chickens, eggs, and milk. Beef was by far the most important product, and output was growing slowly in the 1980s. Between 1981 and 1985, the number of cattle slaughtered rose from 239,000 to 295,000; during the same period, the total stock of cattle increased only slightly, from 1.43 million head to 1.44 million head. Milk production remained steady between 1981 and 1985, averaging 89,140,400 liters a year.

Cattle raising for both meat and milk was common on land on the Pacific watershed and was concentrated in the provinces of Chiriquí, Los Santos, and Veraguas. Most ranches produced both meat and milk, although some specialized in dairy farming. The majority of ranches had fewer than 100 hectares. Cattle were almost entirely grass fed. The grasslands were not particularly productive, lacking added nutrients and other improvements; on average, more than one hectare is required for each head of cattle. Low government credits, competition from regional cattle producers (especially Colombia), and United States market restrictions have hindered the growth of Panama's cattle production.

From 1982 to 1985, poultry production grew rapidly, from 4.5 million chickens to 6.1 million. During the same period, annual egg production also increased, from 28,859 dozen to 31,205 dozen. Pork production has remained steady; the number of pigs in 1985 totalled 210,000.

Fishing and Forestry

Fishing was more important to Panama's economy than forestry, supplying the domestic market and providing substantial export earnings. The waters of the two oceans afforded a variety of fish and crustaceans. Shrimp provided 84 percent of the total value of fishing, and their share of total export earnings increased from 16 percent in 1983 (US$51.4 million) to 18 percent in 1985 (US$60 million). Fish production increased from 117 million kilograms in 1981 to 127 million kilograms in 1985. The most important fish products were anchovies and herring, which were processed into fish meal and oil. Lobster accounted for a minuscule share of fishing products.

Large portions of the country's forests are commercially exploited. Forestry production remained virtually constant in the early 1980s, when the annual forestry output averaged 2,047 cubic meters. The government has implemented a program of reforestation, but the pace of depletion has exceeded that of replanting. Deforestation was most pronounced along the canal, posing a long-term threat to the canal's water level.

Industry

Industrial development has been uneven in Panama. Between 1965 and 1980, industry grew at an average annual rate of 5.9 percent; between 1980 and 1985, that rate was negative 2.2 percent. In 1985 industry accounted for nearly 18 percent of GDP. Within the industrial sector, manufacturing (based primarily on the processing of agricultural products) and mining contributed 9.1 percent to GDP, followed by construction (4.7 percent) and energy (3.4 percent).

Several factors contributed to the rapid expansion of industry between 1950 and 1970. A 1950 law granted liberal incentives and protection from imports to investors, including those in manufacturing. An agreement in 1955 phased out a number of manufacturing activities in the Canal Zone and opened a market for such Panamanian products as bakery goods, soft drinks, meats, and bottled milk. Foreign investment went into relatively large plants for oil refining, food processing, and utilities. The government invested in the infrastructure, especially in roads and the power supply. A building boom increased the demand for construction materials and furniture, further stimulating manufacturing. Management gained experience during the period, and labor productivity increased.

The stagnation in industrial growth during the 1970s resulted from external and internal causes that reduced private investment. Externally, the rise of oil prices, recession in the industrialized countries, and uncertainty relating to the future status of the canal clouded the investment climate. Domestically, a recession reduced construction activity and lowered the demand for manufactured goods. The government built cement and sugar mills to compete with privately owned mills; it also implemented an agrarian reform program, instituted a liberal labor code, and enforced rent control laws. These measures created apprehension on the part of investors, and although the government granted tax holidays, export incentives, and protection from imports, private investment declined. A key goal of the structural adjustment program of the mid-1980s was to increase private investment in industry and to make Panama's industry competitive internationally.

Manufacturing

In 1984 the value added in manufacturing totaled US$344 million, distributed approximately as follows: food and agriculture, 42 percent; textiles and clothing, 11 percent; chemicals, 8 percent; machinery and transport equipment, 1 percent; and other manufacturing, 37 percent. Manufacturing was almost completely oriented toward the domestic market; manufactured goods accounted for a mere 2.5 percent of the value of exports of goods and nonfactor services. Production was concentrated in Panama City (over 60 percent of establishments), with smaller industrial centers at David (10 percent) and Colón (5 percent).

Industrial development has faced the serious constraints of the small size of the domestic market, lack of economies of scale, high labor and unit costs, and government policies of high protection

Field-workers harvest pineapples
Courtesy Inter-American Development Bank

against imports. The greatest growth in manufacturing occurred in response to import-substitution industrialization in the 1960s and 1970s. By the 1980s, however, the "easy phase" of import-substitution industrialization was over; a second phase, that of industrial deepening, was more difficult to carry out in such a small economy. The economy's obvious limitations in manufacturing have been partially offset by an educated labor force, highly developed internal and external transport and communication links, extensive financial facilities, the country's centralized location, and relatively few restrictions on foreign investment. The Panama Canal treaties provided additional space for expanding the CFZ, an ideal location for light industry and assembly plants.

During the 1970s, the public sector took the lead in manufacturing by building a cement plant, sugar mills, and iron and steel works. The structural adjustment program of the mid-1980s sought to reduce the state's role in the economy and to make the private sector the engine of manufacturing growth. The industrial incentives legislation of March 1986 encouraged manufacturers to be export-oriented by removing tax exemptions for those firms that produced for the domestic market. The legislation also provided for maintaining tax exemptions on imported inputs, income, sales, and capital assets for those firms that produced exports. The legislation also lowered import barriers over a period of five years in an effort to increase the productivity and competitiveness of local manufacturing. In addition, new companies were given tariff reductions of up to 60 percent for the first 7 years and 40 percent thereafter.

Since the early 1970s, industrial expansion and job creation have lagged behind the growth of the labor force. In the 1960s, an average of 2,400 jobs was created each year in manufacturing. The rigidities of the industrial incentives law in 1970 and the labor code in 1972 contributed to a decline in manufacturing employment; an average of only 530 new jobs was created each year in manufacturing during the 1970s. The changes introduced in the labor code in March 1986 sought to reverse the antiemployment bias in manufacturing. The slight reduction in the overall unemployment rate in 1986 may be partially attributed to the labor code revisions.

Despite government measures to stimulate manufacturing, Panama's becoming a major industrial center seemed unlikely. Under the CBI, some potential arose for the development of twin-plant operations, especially in association with firms in Puerto Rico, where labor costs were higher than in Panama. In general, however, Panama was unable to compete effectively with Mexico, given the latter country's low labor costs and proximity to the United States market. Also, the possibility existed that industries from East Asia, especially clothing manufacturers, might increasingly relocate to Panama, in an attempt to circumvent United States quotas. This possibility was limited by uncertainty over the United States response. The United States Department of Commerce had called for the reduction of United States imports from Panama, precisely in those products manufactured by Asian investors.

Mining

Despite the variety of mineral deposits and the potential of copper production, the contribution of mining to GDP was negligible, accounting for only US$2.5 million in 1985, down from a 1982 peak of US$4.1 million (both figures at 1970 market prices). The production was restricted to the extraction of limestone, clays, and sea salt. A state company, Cemento Bayano, produced limestone and clay and operated a cement plant with an annual capacity of 330,000 tons.

In the 1970s, several copper deposits were discovered. The largest was Cerro Colorado, in Chiriquí, which if developed would be one of the largest copper mines in the world. Commercial development of the Cerro Colorado project was in the hands of the state-owned Corporación de Desarrollo Minero Cerro Colorado, which had a 51-percent stake in the operation, and of Río Tinto-Zinc,