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STRATEGIC AGREEMENT BETWEEN PANAMA AND THE IDB GROUP COUNTRY STRATEGY

2025 – 2029

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CONTENTS

LINKS

1. Country Development Challenges - Panama (CDC)
2. Fiduciary technical note
3. Portfolio summary
4. Civil society consultation
5. Monitoring and evaluation capacity assessment
6. Government of Panama Strategic Plan 2025-2029
7. Development effectiveness matrix
8. Strategic positioning analysis

ABBREVIATIONS

AAUD	Autoridad de Aseo Urbano y Domiciliario (Urban and Household Sanitation Authority)
ACP	Autoridad del Canal de Panamá (Panama Canal Authority)
ATP	Autoridad de Turismo de Panamá (Panama Tourism Authority)
CABEI	Central American Bank for Economic Integration
CDC	Country Development Challenges
CAF	Development Bank of Latin America and the Caribbean
CGR	Contraloría General de la República (Office of the Controller General of the Republic)
CSS	Caja de Seguro Social (Social Security Fund)
DDT	Dirección de Desarrollo Territorial (Territorial Development Directorate)
DGCP	Dirección General de Contrataciones Públicas (Public Procurement Office)
DGI	Dirección General de Ingresos (Internal Revenue Office)
DIPRENA	Dirección de Presupuesto de la Nación (National Budget Directorate)
ERCE	Estudio Regional Comparativo y Explicativo (Regional Comparative and Explanatory Study)
ICPR	Independent Country Program Review
ICS	Innovation in Citizen Services Division
ILO	International Labour Organization
IMF	International Monetary Fund
INEC	Instituto Nacional de Estadística y Censo (National Statistics and Census Institute)
IPSAS	International Public Sector Accounting Standards
ISTMO	Integración y Soluciones Tecnológicas del Modelo de Gestión Operativa (Integration and Technological Solutions of the Operational Management Model)
LRSF	Ley de Responsabilidad Social Fiscal (Fiscal Social Responsibility Law)
MAPS	Methodology for Assessment of Procurement Systems
MEDUCA	Ministry of Education
MEF	Ministry of Economy and Finance
MiAmbiente	Ministry of Environment
MIDES	Ministry of Social Development
MINSA	Ministry of Health
MSMEs	Micro, small, and medium-sized enterprises
NDC2	Second nationally determined contribution
OECD	Organisation for Economic Cooperation and Development

OVE	Office of Evaluation and Oversight
PEG	Government of Panama Strategic Plan
PISA	Programme for International Student Assessment
PPP	Public-private partnership
R&D	Research and development
RENAB	Registro Nacional de Beneficiarios (National Registry of Beneficiaries)
RSU	Registro Social Universal (Universal Social Registry)
SDG	Sustainable Development Goal
SMART	Specific, measurable, achievable, realistic, and time-bound
TSP	Transport Division
UNESCO	United Nations Educational, Scientific, and Cultural Organization
WSA	Water and Sanitation Division

INTRODUCTION

A NEW APPROACH FOR IMPACT

Panama's potential

Panama is one of the most dynamic and resilient economies in Latin America. Its strategic location, linking two oceans through the Panama Canal, drives an economic model based on logistics and international trade, making it a key regional hub for financial services, transportation, and commerce.

Despite these economic advances, significant challenges persist. Social and territorial inequalities are reflected in major gaps in access to basic services, especially in rural and indigenous areas, where poverty reaches higher levels. Furthermore, Panama faces growing fiscal pressures stemming from a pension system with structural imbalances, low tax collection levels, and public management limitations.

At the same time, the country is highly vulnerable to climate change, particularly in terms of the availability of water to operate the Panama Canal. This necessitates strategic investments in environmental sustainability to ensure the Canal's competitiveness and economic stability in the future.

The Government of Panama Strategic Plan (PEG) 2025–2029 sets clear priorities in addressing these challenges through improvements in access to basic services, institutional strengthening, and sustainable management of natural resources. Panama has the potential to consolidate its status as an inclusive, diversified, and resilient economy, leveraging its unique comparative advantages to achieve balanced and sustainable growth.

New country strategy approach

The Inter-American Development Bank (IDB) Country Strategy with Panama 2025–2029[1] is aimed at maximizing the impact of the IDB Group (IDB, IDB Invest, and IDB Lab) in the country's development through greater selectivity and a long-term integrated approach. This new approach concentrates the IDB Group's resources, experience, and synergies while fostering strategic partnerships to address Panama's complex challenges, recognizing both the risks of operating in the country and the unique opportunities it offers.

The process of formulating the country strategy followed a structured selectivity framework. **The first step** was to align the national priorities—set out in the PEG 2025–2029, in the sector development plans, and in the Panama Canal Authority's investment plan—with the goals established in the IDB Group's Institutional Strategy, the IDB Invest and IDB Lab Business Plans, and the "América en el Centro" regional initiative. This step also included incorporating recommendations from recent independent evaluations. **The second step** was to analyze the positioning of the IDB Group vis-à-vis other multilateral agencies and financing sources,

[1] The IDB Group Country Strategy with Panama 2025-2029 will become effective upon its approval by the IDB Group Boards of Executive Directors and will remain in effect through 31 December 2029. This does not include the one-year transition period.

identifying areas in which the Bank has comparative advantages and greater impact capacity. **The third step** was to take into account the lessons learned from the preceding (2021–2024) country strategy and the operational and institutional capacity to implement the programs, with a view to ensuring the feasibility of the proposed interventions. **The fourth step** was to identify the main risks—macrofiscal, social and environmental, climate, and institutional—that could affect implementation, and to provide for mitigation measures to ensure the effectiveness of the country strategy and the sustainability of its outcomes over time.

This rigorous process made it possible to prioritize a small set of strategic areas in which the IDB Group can add value and achieve outcomes. As a result, the 2025-2029 country strategy focuses on three action pillars—improving access to basic services, strengthening public management, and promoting sustainable growth driven by the private sector—that address the country's most pressing needs. In implementing the strategy, the IDB Group will emphasize effective coordination with the government, the private sector, and other development partners, ensuring synergies that can optimize the use of resources and facilitate execution of the prioritized projects. At the same time, the new strategy will deepen internal collaboration within the IDB Group to take advantage of innovative financial solutions and mobilize larger investments, including by promoting public-private partnerships to assist in closing gaps in infrastructure and services.

Identified intervention pillars and expected impact

The IDB Group country strategy is built around three strategic pillars:

Basic services for vulnerable populations. The first pillar is aimed at improving the delivery of, and equitable access to, quality basic services, with an emphasis on health care, water, and sanitation. Narrowing the coverage and quality gaps in these services will boost Panama's human capital and help reduce the existing disparities between urban areas and rural and indigenous areas. Specifically, interventions under this pillar will be designed to: (i) promote equity through effective and equitable delivery of basic services such as drinking water, sanitation, and health care, particularly in rural and indigenous communities; and (ii) promote financial inclusion to make it easier for vulnerable groups to obtain access to tools that can improve their quality of life and economic capabilities, and institutional strengthening for the development of inclusive financial markets and infrastructure. These actions are expected to reduce territorial inequality, improve the living conditions of the most vulnerable groups, and strengthen the country's social cohesiveness.

Strengthening of public management and fiscal sustainability. The second pillar is centered on modernizing the public sector and consolidating macroeconomic stability. The strategy will support reforms aimed at making public expenditure more efficient, boosting tax collection, and improving the quality of public services. One of the priorities will be to ensure the financial sustainability of the pension system by promoting structural reforms to balance its accounts and ensure its future viability. Additional interventions will encourage the use of modern management tools—such as process digitalization and budgeting for results—to enhance effectiveness in public management. There is a need to develop and promote the State's digital infrastructure (data and connectivity infrastructure), supporting the digitalization of processes in all sectors, strengthening governance and protection of State data and services, and avoiding duplication of investments in computing capacity and cloud services. The specific strategic objectives of this pillar are to: (i) strengthen fiscal sustainability through comprehensive reforms designed to ensure the sustainability of the pension system, boost tax collection, and improve the quality of public expenditure; and (ii) enhance public management efficiency and make it easier to do business through regulatory reforms, digitalization of administrative processes, and red tape reduction. By implementing these advances, Panama will have a more effective, sustainable, and transparent public administration, helping to create an enabling environment for investment and inclusive growth.

Sustainable growth led by the private sector and by harnessing strategic assets. This pillar promotes a diversified, competitive, and environmentally sustainable economic growth model, with the private sector as the main driver of development. The pillar's specific strategic objectives, set out in the Results Matrix, are to: (i) strengthen the Panama Canal's resilience through effective management of its watersheds, ensuring water sustainability to enable the Canal to remain competitive and continue to contribute to the economy; (ii) support and enable private sector-led economic growth through productive diversification, strengthening of emerging sectors, and promotion of local linkages such as sustainable tourism and the digital economy; and (iii) protect the country's natural and cultural capital while at the same time expanding and promoting climate finance to move forward toward a resilient and low-carbon economy. These actions will make it possible to better harness the country's strategic assets, improve international competitiveness, and ensure an effective transition to a more sustainable economic model.

Crosscutting integration of institutional strengthening, sustainability and resilience, and inclusion and equality of opportunities across all pillars will reinforce the overall impact of the strategy.

Panama – IDB Group partnership

The IDB Group has been a key strategic partner for Panama all along the country's development path. The experience gathered over years of joint work, coupled with the Bank's continuous financial and technical support, has made a significant contribution in various priority areas for the country. During the 2021-2024 country strategy period, the IDB Group supported Panama's postpandemic economic recovery and institutional strengthening and social inclusion efforts. The Bank responded quickly to the COVID-19 crisis to maintain macroeconomic stability and protect the most vulnerable population groups. While the execution of some projects was met with challenges, noteworthy advances were made when there were synergies between the various IDB Group windows and coordination with other partners. The new, 2025-2029 country strategy recognizes that closing the existing gaps in access to public services, modernizing public management, and promoting sustainable growth under private sector leadership are core development objectives for Panama. Accordingly, the IDB Group stands ready to continue to operate as a key partner, boosting financial support in strategic sectors, fostering public-private partnerships, and mobilizing its overall experience and technical capacity.

I. BUILDING A NEW COUNTRY STRATEGY: PURPOSE AND APPROACH

A. SUSTAINED AND INCLUSIVE GROWTH FOR PANAMA

1.1 **Panama has maintained robust economic growth over the last two decades, standing out as one of the most dynamic economies in Latin America.** Its development model, based on trade, logistics, and construction, has enabled sustained growth in gross domestic product (GDP) per capita. However, this growth has not been equitable, and there are still significant challenges associated with (i) pronounced territorial inequality in access to basic services and economic opportunities; (ii) an economic model that is highly dependent on the construction sector, creating vulnerability to economic cycles; and (iii) a structural fiscal imbalance resulting from both a sharp drop in public revenue and major expenditure inefficiencies. To consolidate its position as a high-income country with inclusive and resilient development, Panama needs to close the structural gaps that limit the opportunities available to its population and adopt strategies that reinforce its ability to face economic, climate, and fiscal crises.

1.2 **Despite a reduction in poverty, Panama continues to exhibit significant inequalities in access to basic services.** In 2023, the poverty rate stood at 21.7% of the population, rising to 65.3%, 77.6%, and 87.2%, respectively, in the indigenous comarcas of Emberá, Guna Yala, and Ngäbe Buglé.[2] The country's comarcas and rural areas face significant gaps in basic services, as do some urban or periurban areas. For example, the province of Colón, which has the largest Afrodescendant population (61.6%),[3] has significant service access gaps.[4]

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[2] According to the Pobreza y Distribución de los Hogares (Poverty and Household Income Distribution) report based on the Household Survey. 2022–2023.

[3] According to the 2023 Population and Housing Census.

[4] These gaps have contributed to social protests. Executive Decree 176 of 21 June 2022 states that "for several decades, the province of Colón has been experiencing a serious crisis, basically in the social and economic sectors, frequently giving rise to social unrest in the form of acts of protest by the population."

Disparities in access to health care, education[5] and job training,[6] and water and sanitation[7] services continue to affect the most vulnerable segments of the population, and social investment remains lower than the regional average. Improving the coverage of basic services[8] is a priority with a view to ensuring equity in development and lowering the barriers that curtail social mobility.

1.3 **Fiscal sustainability and public sector modernization are key to ensuring long-term development.** Panama's tax intake of 6.5% of GDP in 2024[9] is lower than the average for Latin America and its own recent historical levels in this regard. This has resulted in higher external financing needs and increased debt, which coupled with external market conditions, have led to a rise in annual interest payments. Thus, between 2016 and 2024, interest payments went from 18% to 43% of tax revenue, constraining the State's capacity to finance strategic investments and social programs. In addition, the growing pressure on the Social Security Fund (CSS) and public debt creates a need for structural reforms to improve expenditure efficiency and optimize resource management. Strengthening governance and financial planning will ensure macroeconomic stability and give the State more leeway for action.[10]

1.4 **Panama has the potential to consolidate its position as a hub for innovation and economic diversification, reducing its reliance on the Canal, construction, and trade.** Despite its privileged geographic position, the country continues to exhibit low productive diversification, with national goods exports accounting for less than 2% of GDP. The lack of productive linkages with local sectors has restricted the creation of quality jobs and the growth of emerging industries. Efforts should focus on strengthening strategic sectors such as

5 According to the Regional Comparative and Explanatory Study (ERCE) 2019 (UNESCO-LLECE), 37.2% of Panamanian sixth grade students placed at the lowest performance level in the reading test, making Panama the country with the highest percentage of students at this level in the region. The results of the 2022 Programme for International Student Assessment (PISA) tests show that 68% of students are below level two (out of six levels), compared with an average of 27% of students in the Organisation for Economic Co-operation and Development (OECD) countries. Similarly, the 2018 Crecer tests highlight regional and income gaps (see Country Development Challenges (CDC) Panama).

6 Only 8.6% of Panamanian businesses invest in technical and vocational education and training for their workers, compared to more than 40% of businesses in Brazil, Costa Rica, and Mexico. At the same time, 77% of Panamanian businesses report being unable to find workers with the necessary skills.

7 The CDC document indicates that, according to the 2023 National Population and Housing Census, 75.9% of the country's population has access to solid waste collection services. This figure is low for Panama's income level and conceals large regional disparities.

8 There is a significant gap in drinking water coverage between urban and rural areas, amounting to more than 12 percentage points in terms of basic access to drinking water. Similarly, access to the public electricity network, which is about 90.8% for the country's population as a whole, is particularly low in the indigenous comarcas of Ngäbe Buglé (10.3%) and Guna Yala (6.2%), while it stands at 54.3% in the indigenous comarca of Emberá Wounaan (see CDC).

9 Taking into account tax revenues in cash. If the fiscal balance sheet revenue (which include tax documents) is used, the tax burden is 6.7%.

10 If the country achieves the efficiency level of its regional peers through improved performance, it could increase life expectancy at birth by 2.2 years and lower the infant and under-5 mortality rate to 7.6 and 12.8 per 1,000 live births, respectively (Goyeneche and Bauhoff, 2023).

logistics, agribusiness, the digital economy,[11] and sustainable tourism so as to boost competitiveness and create formal employment opportunities as well as the conditions needed to attract private investment.

1.5 **Climate change[12] and water security[13] pose urgent challenges to the country's sustainability.** The water crisis has affected the operational capacity of the Panama Canal, with direct implications for global trade and the country's tax revenue.[14] Proper watershed management, including the Canal's watershed, is essential in order to ensure the competitiveness of the logistics sector and preserve this strategic asset. In addition, the energy transition and climate resilience should be treated as priorities for maintaining the environmental and economic stability of the country.

1.6 **The Government of Panama Strategic Plan (PEG) 2025-2029[15] establishes a roadmap to improve access to basic services, strengthen public institutions and management, achieve responsible management of natural resources, and boost growth in key sectors.** With projected public investment of US$30.277 billion, the PEG prioritizes key areas such as access to water, sanitation, and electricity; social equity; transparency and accountability; competitiveness of the logistics cluster; innovation; financial system development; carbon footprint reduction; and adaptation to the new climate reality. Investment in the Panama Canal watershed is another core pillar of the plan, to ensure the sustainability of water resources and reinforce Panama's logistical advantage.

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[11] According to CISCO 2023, Panama lags behind overall, especially in areas such as human capital, ease of doing business, and technology use, with limited adoption of digital technologies in production processes. According to the Global Innovation Index 2022, Panama ranked 10th out of 18 countries in Latin America and the Caribbean, showing significant challenges in terms of business sophistication (innovation linkages and collaboration in research and development (R&D) are low), human capital and research, and generation of knowledge and technology products (WIPO, 2022).

[12] According to Executive Decree 3 of 8 June 2023, adopting the Política Nacional de Cambio Climático 2050 (National Climate Change Policy 2050), "Panama is highly vulnerable to climate change, primarily due to its physical characteristics, its social conditions, and the livelihoods of its population." According to the Índice de vulnerabilidad al cambio climático de la República de Panamá (Republic of Panama Climate Change Vulnerability Index), the areas most vulnerable to climate change are primarily located in the country's indigenous comarcas. So, there is a need for climate adaptation action in comarcal areas, such as the Guna Yala comarca, that are already experiencing problems due to the rise in sea level.

[13] According to the CDC, "efficient water management is vital for the Panama Canal, for tourism, and for human consumption. Expanding the Canal has increased water yield but also water demand, which has reached a critical point."

[14] The CDC indicates that the Canal has been affected by hydrometeorological events on several occasions. It mentions that in 2010, the storm La Purísima affected the operational areas and caused a suspension of vessel traffic for 17 hours, while in 2019 (the fifth-driest year on record at the time) and 2023 (the month of October of which was the driest in 73 years), the Canal's services were impacted by the drought. It is worth adding that in 2023, as a result of the drought caused by the El Niño phenomenon, the maximum permissible draught was lowered from 50 ft to 43 ft and vessel traffic was reduced from 36 to 22 vessels per day in order to save water. According to National Statistics and Census Institute (INEC) data, between November 2023 and May 2024, month-on-month freight volume (in long tons) fell by an average of 38% and month-on-month vessel traffic dropped by an average of close to 28%.

[15] Under the Ley de Responsabilidad Social Fiscal (Fiscal Social Responsibility Law) (LRSF), a five-year strategic plan, including an indicative economic and social strategy, financial programming, and public investment plan, is to be adopted by each government administration within six months after taking office. The PEG 2025-2029 was established accordingly by means of Cabinet Resolution 124 of 26 September 2024.

1.7 **The IDB country strategy for 2025-2029 is aligned with national priorities and IDB Group institutional priorities[16] and is built on three strategic pillars.** The first pillar is aimed at improving access to basic services to reduce inequalities in health care, water, and sanitation.[17] The second pillar focuses on improving public management and fiscal sustainability by promoting reforms to enhance the efficiency of the pension system as well as the quality of public expenditures and citizen services, thereby contributing to a better investment climate and macroeconomic stability. The third pillar promotes sustainable growth through the private sector and the use of strategic assets, with an emphasis on economic diversification, logistic modernization, and adaptation to climate change. In a crosscutting way, the strategy incorporates institutional strengthening,[18] sustainability and resilience, and inclusion and equality of opportunities to ensure inclusive and resilient development.

B. THE KEY LESSONS FROM THE 2021-2024 STRATEGY

1.8 **The 2021-2024 country strategy[19] was implemented in a challenging context, marked by the postpandemic recovery and growing fiscal constraints.** The IDB Group supported Panama throughout this period in key areas such as economic reactivation, institutional strengthening, and social inclusion. However, various factors, including limitations in project execution, governance challenges, and budgetary constraints, affected the expected impact of the program implemented by the IDB Group under this country strategy.

LESSONS LEARNED

1.9 **The implementation of the previous country strategy yielded lessons learned that guided the design, and will guide the implementation, of the 2025-2029 country strategy.[20]** The findings and conclusions of the Independent Country Program Review (ICPR): Panama, 2021-2024 prepared by the Office of Evaluation and Oversight (OVE) have been incorporated throughout the design of this strategy.

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[16] Priorities reflected in the IDB Group Institutional Strategy, including the IDB Invest Business Plan, the IDB Lab Business Plan, and the "América en el Centro" regional initiative.

[17] The Planes Estratégicos Distritales (District Strategic Plans) (PED 2025-2029), prepared by the municipios with technical support from the MEF's Territorial Development Directorate, are an important input to ensure the relevance and ownership of the interventions.

[18] Institutional strengthening includes digitalization, since the implementation of data infrastructure programs coupled with connectivity projects has a direct positive effect on productivity and economic growth. A 1% increase in the digitalization rate (with infrastructure, service connectivity, technology use, and regulatory framework variables) results in a 0.32% increase in GDP, a 0.26% increase in labor productivity, and a 0.23% increase in total factor productivity. Source: https://publications.iadb.org/es/el-impacto-socioeconomico-de-la-infraestructura-de-datos.

[19] IDB Group Country Strategy with Panama 2021-2024. May 2021.

[20] Information based on semiannual general portfolio reviews, performance and results of operations executed in the period, Project Completion Reports (PCRs), and the Panama 2021-2024 Independent Country Program Review (ICPR), among other sources.

1.10 At the strategic level, the following lessons are worth noting:

a. **Greater selectivity and programmatic approach in long-term strategic sectors help to make the Bank's support more effective.** During the implementation of the country strategy, even though the country program[21] was aligned with most of the agreed-upon objectives, the scattering of efforts across multiple sectors and systemic problems in the execution of operations limited the program's contribution to the expected results. The greatest contributions made by the program were associated with correspondence, long-term focus, and a complementary approach across interventions. The new strategy cycle should prioritize a small number of areas in which the IDB Group can generate more value added and have a long-term horizon, focusing on interventions that combine social impact, fiscal sustainability, and resilient economic growth.

b. **Synergies among the three IDB Group institutions and other development partners to address development challenges and maximize impact have become more important.** In the aftermath of the pandemic, the country's debt level increased, as consequently did its fiscal constraints,[22] affecting the government's ability to implement strategic investment programs. The IDB Group coordinated efforts to support key investments in relevant sectors such as micro, small, and medium-sized enterprises (MSMEs) and tourism, where the complementarity of its interventions yielded positive outcomes. Coordinating with other development partners mainly in the delivery of basic services made it possible to target the interventions. The new strategy should continue to prioritize synergies among the IDB Group windows in order to promote sustainable financing models that support the government in executing its public investment plan, foster public-private partnership (PPP) arrangements, and strengthen coordination with multilateral organizations to optimize resources.

c. **Strengthening the institutional capacity of the State helps to optimize resources and improve execution.** Implementation of the Bank's program with Panama has been affected by execution problems that include budgetary allocation constraints, low institutional capacity at some execution units, and high technical staff turnover. In particular, there are persistent challenges associated with the ex ante control function of the Office of the Comptroller General of the Republic (CGR),[23] which involves complex processes that translate into execution delays. Addressing this challenge is crucial, not only for execution of the Bank's portfolio in Panama but also for the country's

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21 "Country program" is the term used by OVE to refer to the portfolio in execution during the country strategy implementation period.

22 According to Ministry of Economy and Finance (MEF) data, the nonfinancial public sector deficit went from 2.9% of nominal GDP in 2019 to 10.2% of nominal GDP in 2020 (from 2.7% to 9.7%, according to GDP data modified by the benchmark year change), while public debt went from 44.5% to 64.8% of nominal GDP over the same period.

23 According to Law 32 of 8 November 1984, amended by Law 351 of 22 December 2022, "[t]he Office of the Comptroller General of the Republic is an independent, technical State agency tasked with the mission of overseeing, regulating, and controlling any movements of public funds and assets, as well as examining, auditing, and closing any accounts related thereto. In addition, the Office of the Comptroller General shall keep the national public accounts; prescribe the accounting methods and systems of public agencies; and direct and develop the national statistics."

economic development. Achieving the expected results under the country strategy will require focusing on strengthening the State's institutional capacity through a strategic, long-term approach and supporting the CGR in its modernization efforts.

d. **The private sector plays an essential role in economic recovery after an aggregate shock like the pandemic.** In the first place, instruments such as the Trade Finance Facilitation Program (TFFP) expand and diversify the financing available to export and import companies, ensuring their liquidity in periods of volatility and uncertainty and helping the global supply chains to recover more effectively. In addition, private-sector instruments deployed through IDB Invest successfully supported government-owned enterprises in their delivery of goods and services. In view of this, ensuring proper corporate governance is important inasmuch as it makes it possible to structure complex financing solutions that adequately capture the characteristics of a project; ensure the borrower's ability to execute the project; coordinate activities among multiple stakeholders; and maintain long-term financial balance.

1.11 **At the operational level, the following lessons are worth noting:**

e. **Strengthen coordinated dialogue among the authorities.** Early coordination between the authorities of the entities that take part in identifying, preparing, approving, executing, and closing operations is essential for improving project execution and results. During implementation of the country strategy, the Bank will continue to engage in ongoing dialogue with the authorities of the Ministry of Economy and Finance (MEF) as the IDB Group's main counterpart, and the Ministry of the Presidency, specifically the Secretariat of Presidential Goals, in order to follow up on the execution of operations and the prioritization of new investments. This process should be guided by the preparation and implementation of a medium-term fiscal framework.

f. **Reinforce the execution capacity of the counterparts for success.** Implementation of the portfolio's investment projects faces recurrent challenges arising from complex internal administrative processes, high turnover of key staff, low technical capacity within the execution units, and lack of up-to-date information. These challenges limit execution capacity, where an efficient use of public resources is essential in a context of growing fiscal constraints. Accordingly, there is a need to strengthen the execution capacity of the counterparts through technical assistance programs, simplification of procedures, and ongoing training in execution, monitoring, and evaluation tools.

g. **Improving financial and budgetary planning is crucial for accelerating project execution.** Weaknesses in the planning capacity of the execution units, fiscal management constraints, and review time required by supervisory entities have resulted in a slower pace of execution of sovereign-guaranteed investment operations. Reinforcing planning tools and knowledge of the budget cycle is key for getting results and reducing administrative expenditures.

h. **Training and strengthening the capacity of counterparts and clients are a priority for satisfactory project performance.** With regard to sovereign-guaranteed projects, challenges persist in the execution of procurement processes through Bank-financed contracts. The Bank should continue to provide training, knowledge transfer, and capacity-building to the execution units, ministries, and supervisory entities in order to reduce processing times, get better results from the processes, and improve execution. With regard to IDB Invest projects, building the clients' internal capacity is a prerequisite for satisfactory execution of social bonds. This capacity is related to a clear value proposition and the implementation of sound monitoring systems.

1.12 **At the development effectiveness level,** the following lessons will be taken into account:

a. **Improve the vertical logic of the country strategy and the selection of results indicators in the Results Matrix.** OVE's ICPR points out that the country strategy exhibited gaps in its monitoring mechanisms, inasmuch as 52% of the 25 progress indicators in the strategy experienced monitoring difficulties, which affected the tracking of country strategy objectives. The new country strategy includes SMART indicators, ranging from more ambitious ones that measure advances toward achieving expected results for the active portfolio to more modest ones that will help monitor advances in new areas under the strategy. This will require reliable and solid monitoring mechanisms, which in turn entails maintaining Bank support for strengthening Panama's country systems.

b. **Annually monitor advances in implementing the country strategy, including the soundness and validity of the Results Matrix, and make the required adjustments to this matrix to ensure that it remains relevant.** Under the previous country strategy, Panama was part of a 2023 pilot that analyzed the entire portfolio's alignment with the Results Matrix under the country strategy. In order to improve this alignment, the Bank proposed updating the Results Matrix in line with past OVE recommendations and the provisions of the country strategy guidelines (document GN-2468-9). During this strategy period, the Bank will annually monitor advances and propose the necessary adjustments to ensure that the matrix continues to be relevant.

c. **Scale the portfolio supervision pilot with a focus on results.** An environment of fiscal constraints, low institutional capacity, and multiple and simultaneous action fronts tends to affect both the theory of change and the premises on which the projects were originally designed, limiting the utility of the traditional portfolio review approaches (which are based on monitoring physical and financial progress). Under the country strategy, Panama will scale the results-based portfolio review model piloted in the country in 2024 with two loan operations, on which it will deploy an early tracking and risk monitoring system with effectiveness assessments with a view to implementing corrective measures in advance.

d. **Large investments in strategic logistics infrastructure can create considerable positive multiplier effects but can also give rise to negative externalities in the local communities.** To maximize the positive impact of large infrastructure projects on local development, it is important to carry out a comprehensive assessment of the project's environmental and social risks, understand the needs of the community (including vulnerable population segments and indigenous groups), and conduct periodic consultations to mitigate risks and safeguard sustainability.

C. FOCUS ON SELECTIVITY FOR TANGIBLE IMPACT

HOW DO WE SHARPEN OUR FOCUS?

1.13 **Strategic alignment of priorities.** The IDB Group country strategy with Panama 2025-2029 takes into account the country's development priorities, as established in the PEG 2025-2029, sector development plans, and the investment plan of the Panama Canal Authority (ACP). These priorities were harmonized with those of the IDB Group, as reflected in the IDB Group Institutional Strategy, the IDB Invest Business Plan, the IDB Lab Business Plan, and the regional initiative "América en el Centro,"[24] as well as with the OVE evaluation. Thus, the selectivity framework prioritized strategic sectors that can boost Panama's development. The initial alignment of priorities identified 11 potential areas of intervention: (i) water and sanitation; (ii) health and social protection; (iii) education; (iv) financial inclusion; (v) public management; (vi) fiscal sustainability; (vii) water resilience; (viii) logistics infrastructure; (ix) productive diversification; (x) energy transition; and (xi) climate finance.

1.14 **Strategic positioning.** The IDB has a relatively greater presence in Panama than other multilateral agencies, giving rise to comparative advantages and opportunities for collaboration with other development partners to mobilize financial resources and technical assistance. The IDB is the country's main multilateral partner, accounting on average for 46% of the multilateral debt in the 2021-2024 period. However, Panama's relationship with multilateral agencies has evolved in recent years. The country has gradually strengthened its relationship with the Development Bank of Latin America and the Caribbean (CAF), which has significantly expanded its portfolio in the country since 2018. In addition, the COVID-19 pandemic prompted increased interaction with the World Bank, the Central American Bank for Economic Integration (CABEI), and the International Monetary Fund (IMF) to obtain emergency support. As of year-end 2024, the IDB continued to be Panama's main partner, with approximately 44% of the multilateral debt, while the World Bank and CAF held 21% and 25%, respectively. CABEI's share has also edged up to 7%, while other multilaterals account for the remaining 3%. Between 2021 and 2024, the IDB was a key partner in the areas of health care, MSMEs, innovation, energy, water and sanitation, transportation, social protection and labor market, tourism, and integration. In terms of development finance through the private sector, IDB Invest was the most significant actor among its peers, exhibiting greater portfolio diversification and financing leadership in the trade, science and technology, health, sustainable tourism, and water and sanitation sectors. In addition, IDB Lab has promoted entrepreneurial innovation and the adoption of new technologies for the benefit of poor and vulnerable population segments.

1.15 **Operational evidence.** An operational evidence index was built to assess the performance of sovereign guaranteed operations, evaluating three issues: (i) portfolio performance, based on the execution alerts for operations throughout

[24] América en el Centro is a "regional development program designed as an umbrella to address common and cross-border challenges faced by countries in Central America, Panama, and the Dominican Republic (CAPDR). The initiative seeks to unlock the region's potential, promote sustainable development, and foster resilience." It is built on three pillars to address critical challenges: (1) productivity and economic integration; (2) climate adaptation and resilience; and (3) social development for young people. Source: https://www.iadb.org/en/who-we-are/country-offices/america-en-el-centro.

their life cycle; (ii) effectiveness, in terms of relevance, efficiency, and sustainability; and (iii) long-term programmatic vision. The analysis conducted led to the conclusion that support in the health care, water and sanitation, transportation, fiscal and social protection, and early childhood development sectors remains essential, given the Bank's programmatic vision and technical experience in the country. While these sectors have performed unevenly under the last country strategies, this has mainly been due to crosscutting factors, such as low institutional capacity, the lack of a medium-term fiscal framework, and the timeframes for resolution of CGR processes, which adversely affect the execution of portfolio operations and must be addressed to improve portfolio execution. Interventions are to be approved under a medium-term programmatic approach with operations that can be executed more effectively, given the fiscal constraints. With regard to non-sovereign guaranteed operations, IDB Invest identified lessons learned in terms of the private-capital mobilization capacity that investments in logistics infrastructure are able to generate, the broad scope of innovative financial solutions in target markets that face restrictions on access to adequate financing, and the development impact they entail. IDB Invest's new vision and business model is expected to result in a deepening of this impact through greater mobilization and a bolder risk management approach, collaboration in strengthening the regulatory and institutional frameworks, expansion of advisory services to promote critical development agendas, and implementation of innovative financial solutions and thematic investments.

1.16 **Risks.** The risks associated with implementation of the country strategy were identified using the new Risk Taxonomy of the Inter-American Development Bank (GN-2547-15), and mitigation measures were defined with a focus on early detection and active coordination to manage those risks. At the macroeconomic level, Panama faces pressures arising from a persistent deficit and a growing public debt. This situation could jeopardize the country's fiscal sustainability and lead to a credit rating downgrade. As a mitigation measure, the strategy will support strengthening revenue and expenditure management, keeping prudent macroeconomic policies in place to preserve financial stability and investor confidence. In addition, there are risks associated with institutional management capacity that could delay the implementation of the strategy. As part of the proposed mitigation measures, the strategy will support institutional strengthening and the State's operational efficiency through its interventions.

1.17 **Outcomes of implementing the strategic selectivity framework.** Implementing the four criteria of the selectivity framework made it possible to identify the areas in which the IDB Group windows can maximize their development impact in Panama, namely: (i) improving access to basic services, especially in terms of health care, water, and sanitation, for vulnerable population segments; (ii) strengthening public management and promoting fiscal sustainability through institutional, digital, and tax reforms; and (iii) fostering sustainable growth led by the private sector and leveraged by productive diversification, natural capital, and the country's strategic assets, such as the Panama Canal. In addition, the IDB Group will continue to provide support on projects in execution, health and social protection, financial markets (with a focus on MSMEs, vulnerable population segments, and foreign trade), and public management efficiency and sustainability. All of these areas incorporate institutional strengthening, sustainability and resilience, and inclusion and equality of opportunity approaches in a crosscutting way to boost their impact.

II. MAIN ACTION PILLARS AND EXPECTED IMPACT

PILLAR 1. ACCESS TO BASIC SERVICES FOR VULNERABLE POPULATIONS

2.1 **Panama continues to be one of the most unequal countries in the region in terms of access to basic services.** The economic progress of recent decades has not translated into equal wellbeing for all. Significant gaps persist between urban areas on one hand, and rural and indigenous areas on the other, in key health, education, drinking water, sanitation, and energy indicators. In other words, vulnerable population segments continue to face structural barriers in accessing essential services and development opportunities.

WHY IS IT IMPORTANT?

2.2 **Equity in the delivery of basic services remains a structural challenge for Panama.** Despite economic growth, vulnerable population segments face barriers in accessing essential health care,[25] social protection, rural electrification and connectivity,[26] sustainable transportation, and financing services.

2.3 **An example of these gaps is the lack of continuity and quality of health care services and the limited coverage of social protection programs.**[27] Panama faces complex challenges in its health care system as a result of deep-seated inequalities in development levels between urban, periurban, rural, and comarcal areas, the latter of which are characterized as hard to reach. The country's current

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[25] Maternal mortality, as documented in the 2023 maternal mortality status report issued by the Ministry of Health (MINSA), was 72.5 per 100,000 live births. Broken down by health care region, the four regions with the largest number of cases in 2023 were the Ngäbe Buglé comarca at 19%, Veraguas and Panama West at 14% each, and Coclé at 11%. According to INEC vital statistics, the nationwide infant mortality rate (i.e., for children under 1) in 2023 was 12.1 per 1,000 live births, broken down into 9.7 in urban areas and 16.0 in rural areas.

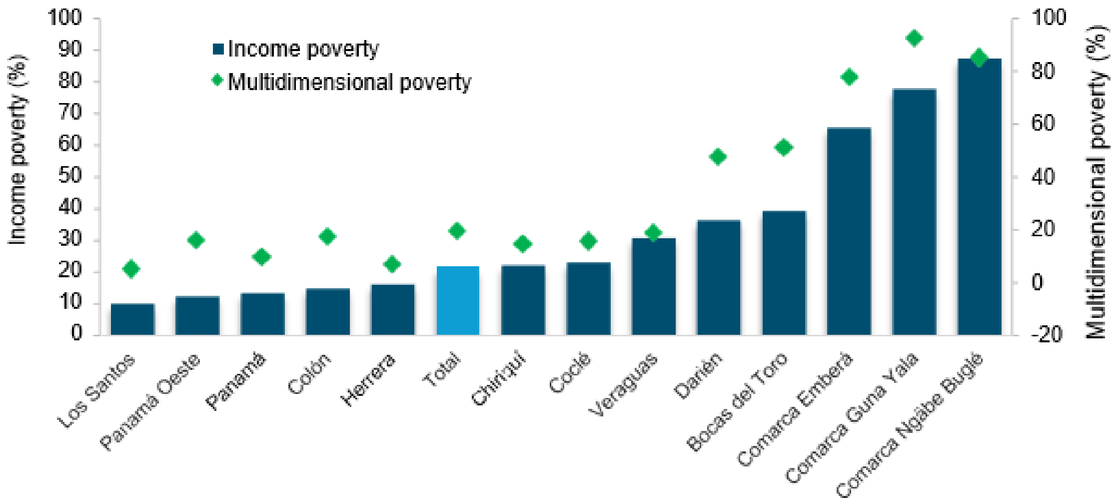
[26] In Panama there are 15 fixed broadband connections per 100 inhabitants (versus 17.7 in IDB countries and 37.8 in OECD countries), evidencing a household access gap. The affordability index shows that 40% of the country's low-income households have to spend 15% of their income to pay for a fixed broadband subscription. Source: https://publications.iadb.org/es/informe-anual-del-indice-de-desarrollo-de-la-banda-ancha-brecha-digital-en-america-latina-y-el-1.

[27] The CDC document indicates that the social protection system has limited capacity to respond to shocks. Although the Ministry of Social Development (MIDES) maintains a National Registry of Beneficiaries (RENAB), the country needs to implement a more dynamic and responsive social protection system that covers most of its population, as well as multiple instruments to assess and frequently update the vulnerability of each household to different types of shocks. The CDC document also highlights the challenges involved in updating the socioeconomic information on beneficiaries of conditional cash transfer programs to ensure proper targeting and the design of comprehensive social policies.

demographic transition and burden of disease, with an increasingly aging population,[28] necessitates better primary care and creates a more pressing need for specialized medical care, particularly care for noncommunicable chronic diseases, while testing the sustainability and efficiency of the health care system. Thus, a comprehensive approach is required to strengthen the infrastructure and make it more accessible, improve management, and ensure an equitable distribution of resources.

2.4 **In terms of social protection, many households living in extreme poverty are currently not receiving the benefits they need due to shortcomings in the targeting, physical accessibility, and scope of these programs.** This situation points to the need to strengthen the social registry and the beneficiary identification mechanisms in order to enable the aid to reach effectively those who need it most. Absent better targeting, significant vulnerable population segments are left out of the social protection network, especially in indigenous comarcas and isolated rural communities lacking road connectivity. Moreover, these population segments are also vulnerable to climate change, as they are generally exposed to hazards such as rises in sea level, floods, droughts, etc.

FIGURE 1. INCOME AND MULTIDIMENSIONAL POVERTY RATES IN PANAMA, BY PROVINCE AND INDIGENOUS COMARCA, 2023 (% OF POPULATION IN POVERTY)

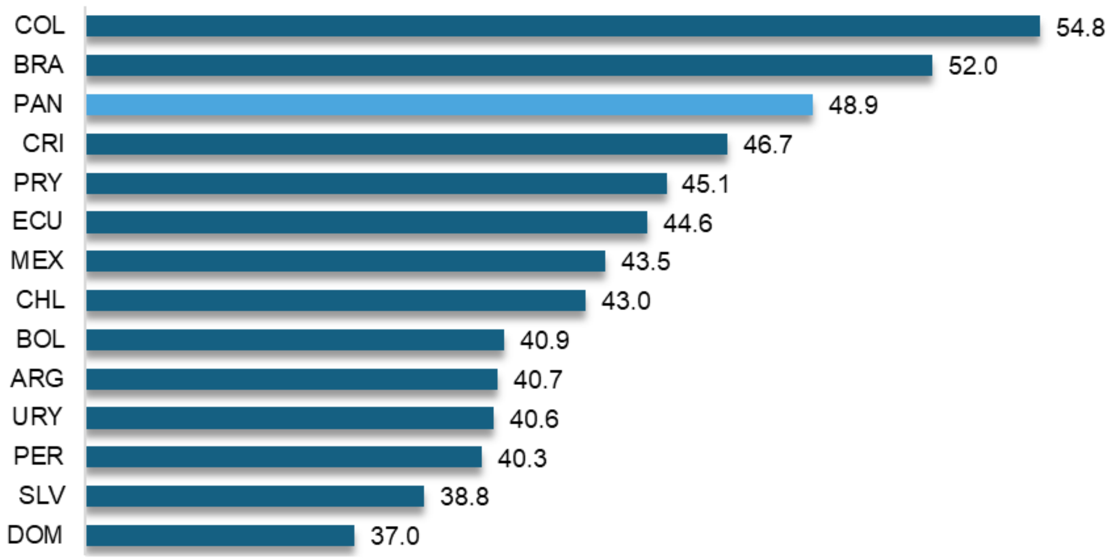


Note: The data on income poverty are drawn from the MEF and use information from the Household Survey. The data on multidimensional poverty were prepared by the authors using information from the 2023 National Population and Housing Census.

Source: Ministry of Economy and Finance (MEF) and the authors, using data from the National Statistics and Census Institute (INEC).

[28] By 2050, the proportion of the population over the age of 65 will have increased from 9.3% as recorded in 2024 to 17.6% (United Nations, 2024).

FIGURE 2. GINI COEFFICIENT FOR LATIN AMERICAN COUNTRIES, VARIOUS YEARS



Note: Information on countries with available data for 2021-2023. The datum for Bolivia is for 2021; the data for Ecuador, Costa Rica, and Panama, for 2023; the remainder, for 2022.

Source: World Bank.

2.5 **Early childhood education services continue to have low coverage, especially among children under 4.**[29] Early childhood education is a key determinant of long-term health, inasmuch as it influences children's cognitive, nutritional, and emotional development. However, gross enrollment among children in Panama up to age 3 is 5%, according to data from the Ministry of Education (MEDUCA) and the 2023 Population and Housing Census.[30] Although educational coverage for children ages 4 and 5 reaches 73.4%, there are still large gaps between the indigenous and nonindigenous population. Only 25% of indigenous children ages 4 to 5 have access to education, compared to 47% of nonindigenous children.

2.6 **To help enhance equality of opportunities and close regional gaps, it is crucial to act on several fronts in the education and job training sector.** The effort to expand coverage is evidenced by an improvement in the average presecondary school completion rate (fulfilling the mandate of providing compulsory education through the ninth grade), which rose from 73% to 89% between 2012 and 2021. Coverage has expanded, but the gaps between regions and income levels remain. At the same time, Panama performs poorly in international standardized tests such as the Regional Comparative and Explanatory Study (ERCE) and the Programme for International Student Assessment (PISA). According to the 2019 ERCE report (UNESCO-LLECE), 37.2% of Panamanian sixth grade students placed at the lowest performance level in the reading test, making Panama the country with the highest percentage of

[29] The CDC also refers to the existing gap between childhood poverty and overall poverty. It points out that, in 2021, the childhood poverty rate was almost double the overall rate.

[30] Considering students in kindergarten 1 and 2 in MEDUCA facilities and Comprehensive Early Childhood Care Centers (CAIPI) managed by MIDES.

students at this level in the region. Panama posted a slight improvement in the PISA 2022 results with respect to those of PISA 2018 on the three assessed competencies: mathematics, reading, and science. The progress made by Panama between PISA 2018 and PISA 2022 is meritorious in a context of general decline and in a period that encompasses the COVID-19 pandemic, when many schools were shuttered. The results of PISA 2022 show that, on average, 68% of students fall below level two (out of six levels), compared to 27% of students on average in the Organisation for Economic Co-operation and Development (OECD) countries.[31] These education quality gaps, coupled with problems in job training coverage and relevance, make it challenging for young people to join the labor market. Unemployment among young people ages 15 to 24 (23.7%) is three times higher than among adults ages 25 to 64 (7.8%), and in the case of young women (28.4%) the difference is even greater. Furthermore, young people who secure employment have lower-quality jobs than adults (SIMS, 2023). Only 28% of young people have formal jobs, compared with 49% of adults (SIMS, 2023).

2.7 **Similarly, rural and indigenous communities lack full access to basic infrastructure.** Panama continues to exhibit a gap in access to electricity, particularly in isolated areas. According to the 2023 Census, 95.2% of households had access to electricity, which means that more than 50,000 households still had no access as of that year.[32] While this coverage is an improvement from 89.1% in 2013, service expansion challenges persist, limiting the population's access to education and quality health care services as well as its ability to carry out productive activities for its economic and social wellbeing. At the same time, access to water and sanitation services is significantly lower in rural and indigenous areas than in cities (95% in urban areas and 66% in rural areas, according to the World Health Organization (WHO), 2023), affecting the health and quality of life of those communities. A comparable situation exists in terms of transportation services and infrastructure that provide access to basic services. According to 2023 Census figures, road density in the comarcas of Ngäbe-Buglé and Guna Yala, the only ones of the country's six comarcas that have this type of infrastructure, is 14 km and 1 km per 100 km^2, respectively, while the provinces of Panama West and Chiriquí have densities of 38 km and 48 km per 100 km^2, respectively, even surpassing the Latin America and Caribbean average of 30 km per 100 km^2. Similarly, the minor ports or piers located in comarcas and remote rural provinces such as the Darién lack the minimum infrastructure needed to support the teams providing health, education, and other government services, whose only point of entry is through these terminals. These deficiencies in basic infrastructure deepen the territorial inequalities that have historically been entrenched in the country. For example, more than 80% of the

[31] The 2018 PISA results show that the widest reading gap is between students who report speaking an indigenous language at home and those who report speaking another language at home. The difference in average score is around 80 points, which is equivalent to almost 3 years of school, according to the OECD. At the same time, the school dropout rate tends to be higher in indigenous areas, particularly in secondary school (in 2021, it was 7.0% versus 3.1% in urban areas and 3.9% in rural areas, according to MEDUCA) (https://www.meduca.gob.pa/sites/default/files/editor/49/ESTADISTICAS%20INDICADORES%202017-2022.pdf).

[32] INEC (n.d.) Census: Housing and Household 2023.

agricultural products harvested in the western region of Panama amount to less than 50% of the yields of many Central American countries.[33]

2.8 **Inequalities in access to urban services affect the quality of life of the population.** The sanitation, mobility, and waste management infrastructure continues to pose challenges in marginal and informal urban areas. Fast and disorganized urban growth, coupled with an absence of up-to-date regulatory frameworks, has given rise to an unplanned expansion, characterized by irregular land occupancy and a proliferation of improvised construction. This inadequate land management hinders the planning and delivery of basic services, disproportionately impacting the most vulnerable population segments. For example, in outlying areas of the city, which is where the vulnerable population lives, public transportation is not available and demand is met by informal carriers that charge unregulated fares and provide a service that is in most cases unsafe and uncomfortable for users. In addition, waste management in Panama is deficient: only 75.9% of the population has access to adequate collection services, and 74% of the waste ends up in open landfills such as Cerro Patacón, causing serious environmental and public health harm.

2.9 **In addition, persons with disabilities face substantial barriers in accessing essential services.[34]** The lack of accommodation and inclusion in public offerings makes it difficult for this population segment to fully enjoy health care, education, or employment programs, perpetuating its vulnerability. In addition, in marginal urban areas, many families live with deficient services; thus, the precariousness of the public transportation, waste collection, water supply, and sewage systems adversely affects their quality of life.

2.10 **Lastly, financial exclusion[35] limits the possibilities of progress for broad vulnerable population segments.** Access to finance is essential for economic inclusion, but in Panama many microenterprise and small business owners, as well as women[36] and low-income households,[37] lack access to the formal financial

[33] Deloitte – IDB, "Hoja de ruta para la Implementación de Cadenas Logísticas sostenibles, resilientes e inclusivas en El Salvador, Panamá y Paraguay" (Roadmap for implementing sustainable, resilient, and inclusive logistic chains in El Salvador, Panama, and Paraguay), September 2024.

[34] The CDC reports that persons with disabilities represented 4.3% of the population according to the 2023 National Population and Housing Census. It indicates that persons with disabilities, in addition to not receiving timely service and care, have higher poverty rates than those without disabilities. It also points to issues such as gaps in measuring and assessing disability, low coverage and quality in the delivery of health and rehabilitation services, limitations in implementing inclusive education, and an absence of strategies to promote personal autonomy.

[35] According to the IDB document "Inclusión financiera en Panamá. La importancia de la calidad institucional y las brechas territoriales, de ingreso y de género," prepared in April 2022, the global financial inclusion index (which includes service access, use, and availability variables) shows Panama as exhibiting a financial inclusion level equivalent to 45% of the average level in high-income OECD countries, and ranks Panama 73rd out of 134 countries. The document notes that the rank is relatively lower than would be expected considering the country's development level. In addition, it concludes that gender, income level, and rural area biases in financial inclusion were in almost all cases greater in Panama than in the high-income and middle-income countries considered. At the same time, Panama is ranked 110th out of 144 countries and 51st out of 77 countries, with and without digital wallet, respectively, in the digital financial inclusion indexes.

[36] Panama exhibits a significant financial inclusion gap between men and women, inasmuch as 37% of women are included in the financial system versus 48% of men. Source: Financial Inclusion Index, Credicorp Holding, 2023.

[37] In addition, there is a lack of disaggregated data on financial inclusion, especially data focused on gender and diversity.

markets and do not qualify for formal loans due to supply and demand barriers.[38] These credit constraints prevent local businesses from growing and erode household resilience to contingencies. Without access to adequate financial solutions, a sizeable portion of the population remains on the margins of the country's economic growth.[39] The credit constraints affect the growth of small businesses and the resilience of households living in poverty.

WHAT WE WILL DO

2.11 **To address these gaps, the IDB Group will support a comprehensive strategy aimed at expanding the coverage and quality of specific basic services for the most vulnerable population groups.** First, in the health care sector, primary care will be strengthened by institutionalizing the strategy of expanding coverage in rural and indigenous areas through improvements in the delivery, continuity, and quality of health care services, including support for digital transformation of the sector, staff training, and equipment and infrastructure. This action is aligned with Indicator 5 in the Results Matrix, which is aimed at improving effective access to essential health care services. IDB Invest will support private-sector projects designed to foster health care infrastructure modernization, facilitating investments that enhance the quality of health care services and their accessibility for vulnerable population segments. It will also be necessary to strengthen the organization and integration of the health care system and community engagement in order to boost the system's efficiency.[40] In the transportation sector, we will promote improvements in regional territorial (road, port, and air) connectivity with a view to expanding accessibility to the basic services that benefit the most vulnerable population groups.

2.12 **Second, the IDB Group will strengthen social protection and make it more targeted.** It will work with the government to expand coverage of the National Registry of Beneficiaries (RENAB) and enhance the targeting of conditional cash transfer programs to ensure that they identify and effectively reach people living in poverty, in extreme poverty, and in vulnerable situations, including climate-related vulnerability. These actions are aligned with Indicator 1 in the Results Matrix, which will help in targeting subsidies. This will entail modernizing the social information systems, including the interoperability of these systems, and training the institutions responsible for them. In addition, gender and diversity approaches[41] will be integrated into these programs to ensure that traditionally excluded groups equitably benefit from the social offerings. Cash transfer programs will be coordinated with the comprehensive early childhood care services available either in centers or in the home as a strategy to foster human capital growth starting in early childhood.

2.13 **In water and sanitation, drinking water and sanitation systems will be built to ensure access to safe and sustainable services.** In drinking water, the Bank

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38 According to the Evaluación del Sistema Financiero de noviembre de 2023, the overall MSME funding gap is estimated to be close to US$21.3 billion or 41% of GDP, making it the largest among the country's regional peers.

39 In Panama, the unemployment rate among young (15- to 29-year-old) Afrodescendants is 17% versus 13.6% for non-Afrodescendants in the same cohort (ECLAC, 2022. El futuro del trabajo y la población afrodescendiente en América Latina en el marco del COVID-19 y la recuperación transformadora con igualdad).

40 Particularly in the comarcas in the area of maternal and infant health.

41 Diverse individuals include Afrodescendants, indigenous peoples, and persons with disabilities.

will continue with its actions to expand the water distribution and conveyance networks and household connections to water service. In sanitation, Bank interventions will continue to expand sanitary sewerage networks and connectivity, while also expanding wastewater treatment to improve the quality of bodies of water and environmental conservation. In rural areas, which are home to vulnerable population segments such as indigenous communities, efforts will be made to find sustainable and appropriate solutions for water supply and safe management of excreta and solid waste.

2.14 **In education, to increase presecondary school coverage and close existing regional gaps, presecondary and secondary schools will be delivered in the Guna Yala comarca, and schools in hard-to-reach areas will be expanded using modular classrooms.** In addition, these schools will be equipped with solar panels to enable them to have electricity and receive computers and devices with pedagogic content to be used by students and teachers. Moreover, the country should continue to provide programs focused on essential skills (reading, writing, and mathematics)[42] in order to further improve the results of international assessments. Monitoring the implementation of programs, coupled with ongoing skills assessments, will make it possible to implement rapid improvement actions and enable gains in student performance. Distribution of materials or access to quality materials, as well as in-service training, are essential for consolidating the teaching and learning process and for enabling human capital development to provide better life opportunities for the country's students. IDB Invest will contribute by financing private-sector projects designed to improve access to educational technology and infrastructure, facilitating the implementation of innovative solutions in rural and hard-to-reach areas.

2.15 **At the same time, the strategy will emphasize eliminating the barriers encountered by persons with disabilities in accessing public services.** The IDB Group will support strengthening inclusion programs that adapt the infrastructure and delivery of health, education, sanitation, and transportation services to meet the needs of this population group. This may include investments in accessible equipment, training of public staff in inclusive care, and adoption of regulations that mandate universal accessibility in financed projects. The goal is to enable more Panamanians with disabilities to fully integrate into the educational system, job market, and community life, reducing the current exclusion gaps.

2.16 **In addition, we will narrow territorial gaps in basic infrastructure by means of targeted investments in lagging rural and indigenous communities.** The IDB Group will support implementation of the Sustainable Development Goals (SDGs),[43] particularly SDG 7, which seeks to ensure access to affordable, secure, sustainable, and modern energy for all. At the same time, it will help in reducing CO_2 emissions through decarbonization of the energy sector, enabling progress in fulfilling the country's commitments under the Energy Transition Agenda,[44] which

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42 In comarcal schools, it will be important to introduce bilingual intercultural education, pursuant to the recently issued implementing regulations to Law 88 of 22 November 2010 (Executive Decree 91 of 20 June 2024).

43 Sustainable Development Goals (SDGs). In September 2015, the United Nations adopted a set of global goals aimed at ending poverty, protecting the planet, and ensuring prosperity for all as part of a new sustainable development agenda. The 2030 Agenda, as it is also known, includes 17 SDGs.

44 The Lineamientos Estratégicos de la Agenda de Transición Energética 2020-2030 (Strategic Guidelines for the Energy Transition Agenda 2020-2030) were approved under Cabinet Resolution 93 of 24 November 2020.

is aligned with the framework of the Paris Agreement.[45] Furthermore, the Bank supports Panama in promoting sustainable development through a clean, fair, and equitable energy transition. Bank initiatives include rural electrification projects, which are aimed at bringing reliable electric power to communities that are not yet connected to the grid. These efforts will be supplemented by IDB Invest investments to support modernization of the country's energy infrastructure. The Bank will similarly promote regional territorial (road, port, and air) connectivity with the economy of the Canal corridor area and main border crossings, as well as logistics improvements to strengthen the primary value chains that benefit the most vulnerable population groups. Together, these investments not only will provide basic goods (electric power, transportation, clean water, primary health care) to previously unserved populations, but will lay the groundwork for productive development of these populations, from facilitating rural enterprises to improving child and maternal health indicators in indigenous comarcas.

2.17 **In tandem with the foregoing, we will improve essential urban services in low-income urban areas.** The strategy will support the relevant institutions and governments, as well as the private sector in coordination with governments, in implementing development plans and improving urban infrastructure in territories with high economic and climate vulnerability, including optimizing land use and management, expanding water and sanitation services, strengthening solid waste management, and improving urban transportation and mobility. For example, plans call for investing in the construction and rehabilitation of sanitation systems and in the renewal of community infrastructure (streets, public lighting, public spaces) in informal neighborhoods. In the transportation sector, the Bank will promote making improvements in urban mobility for all public transport users and extending public transportation (bus, metro, cable car) coverage to the areas where the most vulnerable communities reside. These interventions will make these areas more livable and safer, reducing health and environmental risks and enhancing the quality of life of their inhabitants.

2.18 **Another area of action will be to promote the financial inclusion of traditionally excluded sectors.** The IDB Group will design innovative mechanisms to facilitate access to credit and financial services for MSMEs as well as for individual entrepreneurs and low-income households and will support the capacity of financial authorities to further the development, integrity, and resilience of the financial markets and infrastructure. This will include supporting seed capital financing, financial institutions, microlenders, credit unions, leasing and factoring companies, fintech platforms, and development banks, which serve underbanked segments including migrants, women, and low-income and rural populations by providing them with capital and technical assistance to expand their services. We will also explore creating partial guarantee funds, risk-sharing structures that leverage private resources with public capital (first loss facilities), and financial products that reduce the risk for financial intermediaries when lending to small businesses. In collaboration with financial institutions, we will seek to support MSMEs through training in the preparation of business plans and bankable investment proposals, and to develop incubation and acceleration programs for innovative business models with scalability potential. Through these measures, the IDB Group will help to channel more resources toward MSMEs, limited-income households, and unserved population segments, boosting their capacity to invest,

[45] https://unfccc.int/documents/639829.

grow, and generate income. Financial inclusion will be a key component for a truly inclusive postpandemic economic recovery, down to the last link in the production chain. In addition, we will endeavor to strengthen the capital markets, particularly the corporate debt market, in order to expand financing to the private sector. IDB Invest could participate through guarantees, subscriptions, advisory services, and structuring of sustainable thematic emissions. The Bank's support will be essential for improving the regulatory environment, strengthening the capacity of the relevant authorities, and implementing public policy incentives to develop the market and promote sovereign issuances. Furthermore, the IDB Group plans to leverage regional market integration to facilitate crossborder issuances and diversify the sources of financing for investment projects in the country.

2.19 **Lastly, we will leverage digital transformation as a crosscutting tool to improve efficiency in the delivery of basic services.** The Bank will promote the digitalization of key processes, from electronic medical records and social registry management to the delivery of benefits and monitoring of field projects. This will include the development or expansion of technological platforms that enable, for example, improved traceability of health services, online enrollment of potential beneficiaries of social programs, electronic transfers using digital wallets or other mechanisms, or collection of georeferenced data on unserved communities to better target interventions.[46] It is essential to include the development of data infrastructure as an enabling factor for digital transformation across all sectors. This requires: (i) expanding the State's digital infrastructure; and (ii) bolstering the digital skills of the general public and public servants in using the State's infrastructure and digital services. Digitalizing and automating procedures is expected to reduce wait times, minimize leakage or duplications in beneficiary lists, and enhance accountability in project execution. In short, digital innovation will be an ally in expanding the scope of services with the same resources, and ensuring that aid reaches the target populations swiftly.

[46] According to the 2023 census, digital gaps in Panama are significant: only 40% of households have a computer, laptop, or tablet. The largest access gaps are in comarcal areas. Differentiated actions such as supporting the development of digital skills among women or indigenous peoples will be necessary as part of the digital transformation.

EXPECTED IMPACT

Expanding enrollment in the social registry for better targeting and strengthening of the social protection network, as well as supporting the inclusion of persons with disabilities. In social protection, improvements in social protection targeting and coverage (facilitated by having a larger percentage of the population enrolled in the Universal Social Registry (RSU)) are expected to significantly increase the number of poor households that receive the State transfers and support to which they are entitled, reducing the unserved proportion of vulnerable population groups. At the same time, the barriers that currently prevent certain disenfranchised groups from accessing essential services will begin to recede. A larger number of formerly isolated rural communities will have improved access to services and more persons with disabilities will be able to use public facilities tailored to their needs. In the long term, these improvements will help to boost living conditions and expand human capital in traditionally excluded population segments.

Improving water and sanitation service access and quality to reduce inequalities. In general, interventions will improve the infrastructure and accessibility of low-income communities, helping to close development gaps in vulnerable sectors. Similarly, improvements in urban services in less economically developed areas will result in healthier and safer environments for their residents. Thus, better sanitation, adequate roads, and accessible public transport are expected to lead to a decline in diseases associated with unhealthy conditions and greater integration of these areas into the rest of the main urban centers. Bank interventions will foster expanding and rehabilitating works in places in which the risk of hydroclimate events, exacerbated by climate change, is low, with a view to improving the volume, quality, and reliability of drinking water and sanitation services.

Improving access to essential health services and electricity in rural areas to enhance the quality of life and economic opportunities in isolated communities. In health, Bank interventions will promote expanding primary health coverage in lagging rural and indigenous areas to achieve development that is more equitable. In addition, bringing electric power to hard-to-reach areas will improve quality of life and foster economic development through new productive opportunities and jobs.

At the same time, increasing financing and efforts toward financial inclusion to assist in gradually narrowing the credit access gap. Expanding credit and financial services to a larger number of microenterprises, entrepreneurs, and low-income households, particularly among traditionally excluded population segments such as women, migrants, older adults, and rural dwellers, will boost investment in their productive activities to help invigorate local economies and create higher income as well as new jobs in vulnerable communities. These efforts will contribute to a more inclusive and equitable economic recovery.

PILLAR 2. STRENGTHENING PUBLIC MANAGEMENT AND FISCAL SUSTAINABILITY

WHY IS IT IMPORTANT?

2.20 The gap between high economic performance and institutional weaknesses significantly limits Panama's development potential. Despite being one of the most dynamic economies in Latin America, with sustained economic growth over the last decade, Panama faces challenges in terms of governance and effectiveness of the public sector. According to recent evidence set out in the document Country Development Challenges – Panama (CDC Panama), the country's institutional weaknesses are reflected in low capacity to execute efficient public investment, a tax system with limited and declining revenue collection capability (owing to high noncompliance levels[47] and numerous tax exemptions,[48] among other reasons), and critical sustainability problems in the pension system. This is coupled with public expenditure inefficiency, estimated at about 3.8% of GDP, aggravated by complex administrative mechanisms and limited institutional management capacity. In addition, Panama faces challenges in terms of economic governance, as evidenced by the country's inclusion on international lists relating to fiscal governance. In view of this, strengthening public institutions by modernizing the tax and pension systems, optimizing public expenditure, and improving the State's operational capabilities are essential conditions for sustaining the country's inclusive growth and its economic and social stability.

2.21 Low tax revenue collection limits the capacity of the State to finance essential services and respond to shocks. Panama has one of the lowest tax revenue levels in Latin America (close to 8.5% of GDP in recent years, versus a regional average of close to 16% of GDP). This poor performance results from a narrow tax base with multiple exemptions and special arrangements and from high noncompliance levels. It is estimated that tax expenditure stemming from income tax and goods and services tax generates annual collection losses on the order of 3% of GDP,[49] eroding the equity and sustainability of the tax system. A tax system with such low revenue restricts the government's ability to maneuver and increases its reliance on external financing and other nontax sources, such as the Canal's contributions or the extraordinary measures reported in recent fiscal years.

2.22 The pension system faces major financial sustainability, coverage, and sufficiency challenges, which are exacerbated by demographic trends. In the short term there is an urgent financial sustainability challenge, since the reserves of the defined benefit pension subsystem administered by the Social Security Fund

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[47] According to the Boletín Estadístico Tributario 2022, issued by the Internal Revenue Office (DGI), the noncompliance gap amounted to 7.9% of GDP in the case of corporate income tax; 0.4% of GDP in the case of personal income tax; and 2.3% of GDP in the case of goods and services tax.

[48] Contributing to this dynamic, the tax system exempts businesses from income tax if their revenues are derived from goods and services exports. This is a determining factor in the growing disconnection between economic growth and revenue collection.

[49] According to data from the DGI's Boletín Estadístico Tributario 2022.

(CSS)[50] were exhausted in 2025. This entails a cost that will quickly rise and reach 3.5% of GDP in approximately 20 years. With the increase in informal employment, the system's contributory coverage has declined over the past 10 years. The percentage of workers who contribute to social security has dropped from 56% in 2013 to 46% in 2023. Lastly, there is a sufficiency challenge in terms of pension amount since pensions are not indexed to price increases, which erodes their purchasing power over time.

2.23 **Public expenditure inefficiency places another constraint on development.** It is estimated that inefficiencies in Panama's fiscal spending, stemming from subsidy and cash transfer leakages and procurement cost overruns, amount to about 3.8% of GDP,[51] diminishing the social impact of public investment. Panama has doubled its spending on personnel and allocates the equivalent of one fourth of public expenditure to wages and salaries. It has recorded the region's second-largest wage bill increase as a percentage of GDP in the last decade.[52] In addition, public management weaknesses –such as limited technical capacity in some agencies and complex controls– slow the pace of execution of public and private projects. Panama's score in the Civil Service Development Index[53] fell from 29 points in 2012 to 24 in 2023, making it the only country in the region to experience a decline. This setback reflects decreased professionalization and broader discretion in human resource management. In addition, Panama ranks below the expected level in human resource management based on its GDP per capita, and its local governments need to strengthen their execution and evaluation capacity. Recent experience has shown that ex ante oversight processes that are not aligned with international best practices (such as procedures at the CGR) create inefficiencies that, coupled with a lack of interagency coordination, play a part in delaying the execution of strategic projects and investment in infrastructure. These administrative bottlenecks result in delays and cost overruns, reducing both the effectiveness of expenditures and the quality of services received by the public. Furthermore, monitoring and evaluation weakness and poor coordination with the planning and budget systems limit the quality of public management.

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[50] The Valuación actuarial del sistema panameño de pensiones, prepared by the International Labour Organization (ILO) in 2019, explains that, pursuant to Law 51 of 2005, the pension system was divided into two subsystems: (1) a defined benefit subsystem; and (2) a mixed subsystem, consisting of a defined benefit component and a personal savings component. Law 51, which became effective in 2008, established that workers who were over 35 when the law took effect would remain enrolled in the defined benefit subsystem along with current pensioners, while workers below that age limit would be moved to the mixed subsystem. The ILO report further explains that, since 2018, the defined benefit subsystem contributions have not covered benefit payments to pensioners, gradually exhausting the system's reserves.

[51] According to Better Spending for Better Lives, prepared by the IDB, public expenditure inefficiency in 2018 amounted to 3.8% of GDP, with inefficient procurement being equivalent to 1.5% of GDP, inefficiency in public wages and salaries amounting to 0.8% of GDP, and leakages in targeted transfers totaling 0.5% of GDP.

[52] According to the 2022 Article IV Consultation, improving the wage bill may help to enhance expenditure quality. According to the BTI (2023) Panama Country Report, high staff turnover, especially during changes in government administration, makes it difficult to learn how to improve public policies.

[53] The Inter-American Development Bank created a Civil Service Development Index for Latin America, which measures the quality of the civil service by means of diagnostic assessments of the civil service systems in the central government administration. The index is based on 33 variables taken from the Carta Iberoamericana de la Función Pública (Ibero-American Public Service Charter), which was signed by the region's countries in 2003 and sets out the foundations for a professional and effective civil service system. The scale ranges from 0 to 100, where the highest score reflects better performance. Source: https://blogs.iadb.org/conocimiento-abierto/es/que-tipo-de-historias-de-datos-con-el-nuevo-indice-sobre-servicio-civil-en-numeros-para-el-desarrollo/.

2.24 **Governance challenges have eroded public trust in institutions.** Dissatisfaction with public management has increased: surveys show that more than 80% of Panamanians mistrust the National Assembly and close to 77% mistrust the central government. Strengthening accountability and the institutional framework is crucial in order to build alliances conducive to pending regulatory and social changes. In addition, there is a need to strengthen the production, dissemination, and use of statistics for monitoring purposes (for example, the 2022 Open Data Inventory ranks Panama 111th out of 195 countries, reflecting the limited capabilities of the National Statistics and Census Institute (INEC)) to support evidence-based policy-making and thereby boost decision-making efficiency. At the same time, while insecurity in Panama is not among the highest in the region, the homicide rate increased by 30% between 2017 and 2024[54] (to 13 per 100,000 inhabitants), making it lower than the Latin American average of 20 but higher than the rate in Chile (6.8) and Argentina (4.3), both of which have a similar income level. In addition, the national police estimates that 70% of homicides are the result of clashes between local criminal gangs and are concentrated in the vicinity of ports or logistic areas, the territorial control of which is key for the development of illicit economies (in 2024, 75% of homicides in Panama took place in Panama City and Colón).

2.25 **In addition, various international indicators confirm the country's institutional weaknesses.** Panama has exhibited a decline in some governance, government effectiveness, and regulatory quality indicators, particularly when compared to similar-income countries.[55] These institutional challenges are reflected in a limited capacity to efficiently manage public resources, frequent budget modifications, and difficulties in implementing the fiscal framework effectively. This exacerbates investor uncertainty and affects the business climate. At present, the government administration is faced with shortcomings in budgetary planning, impacting the effectiveness of public management. Strengthening the civil service and digitalizing the public sector[56] can lead to improvements in State management. Institutional weakness is also evident in the insufficient concentration of police activity in insecure areas and the low use of evidence in police actions to deter violence. In view of this, enhancing institutional capacity is essential for boosting the efficiency of public spending, reducing fiscal risks, and creating greater trust among investors and the general public.

2.26 **Macroeconomic and fiscal stability is also being challenged.** Public deficits in recent years—exacerbated by the pandemic and rigid expenditures—have increased indebtedness and the perception of country risk. In 2025, Panama faces

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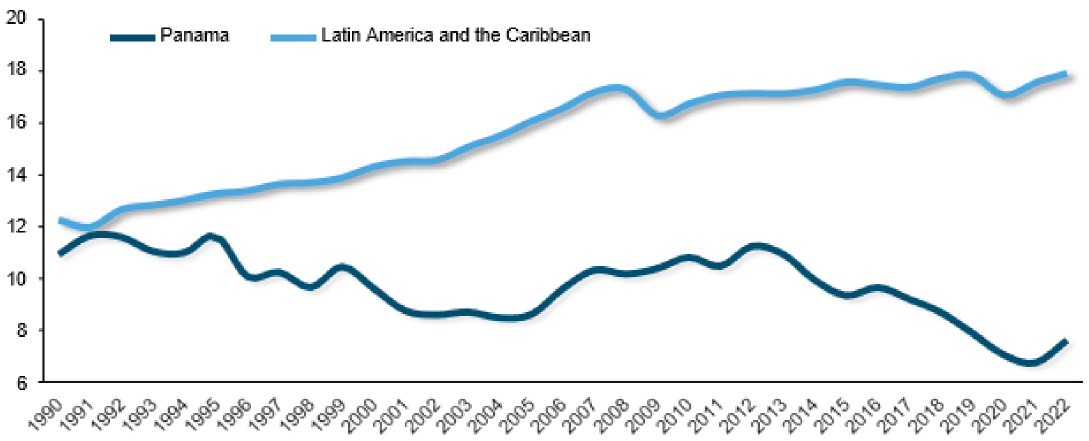
[54] In 2024, according to data from the Public Ministry, there were 23 femicides, 9 attempted femicides, and 25 violent deaths of women. These data show a 53% increase in femicides over 2023.

[55] World Bank Governance Indicators (WBGI) 2023.

[56] According to the CDC document, significant progress has been made on the digital transformation agenda, facilitating the response to the pandemic; however, challenges persist. As many as 20 new digital services were created during the pandemic, including vaccination and subsidy programs, with more than 16,000 people being trained in the use of the "Vale digital" (digital voucher). While this progress enabled Panama to climb 16 places on the United Nations E-Government Development Index between 2016 and 2022, the country continues to face digital government challenges and was ranked 79th out of 193 countries in the 2024 version of the index.

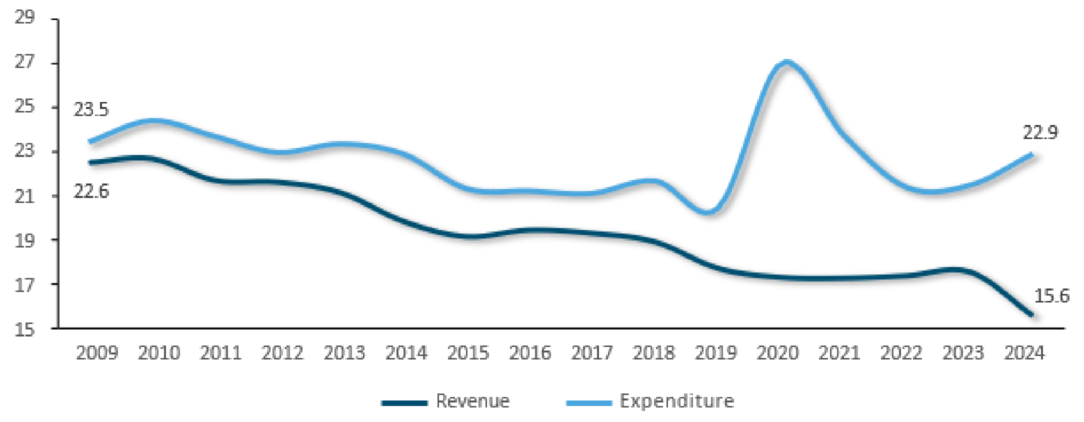
scenarios that jeopardize the investment grade status attained in 2010,[57] with the major rating agencies citing fiscal deterioration and governance shortcomings as key factors in the downgrade. This will make financing more expensive and adds urgency to the need for corrective action. Fiscal consolidation, in tandem with a more efficient State, is essential for maintaining the confidence of investors and the general public and for preserving the conditions for sustainable and inclusive growth in the medium term.

FIGURE 3. TAX COLLECTION IN PANAMA VERSUS LATIN AMERICA, 1990-2022 (% OF GDP)



Note: Excludes social security contributions.
Source: Organisation for Economic Co-operation and Development (OECD).

FIGURE 4. TOTAL NONFINANCIAL PUBLIC SECTOR REVENUE AND EXPENDITURE, 2009-2024 (% OF GDP)



Source: Ministry of Economy and Finance (MEF).

57 As of April 2025, Panama had a credit rating of Baa3 with negative outlook, according to Moody's Ratings; BBB- with stable outlook, according to Standard & Poor's Global Ratings (S&P); and BB+ with stable outlook, according to Fitch Ratings, which withdrew the country's investment grade.

WHAT WE WILL DO

2.27 **Support tax modernization to reduce tax noncompliance.** Implement measures to narrow the noncompliance gap across all taxes, facilitating tax compliance through digital transformation of the tax administration, risk analysis, and systemic compliance leveraged by process digitalization and the electronic invoice. In addition, in coordination with the authorities, we will study possible reforms to enhance the effectiveness and progressivity of the tax system. This will be reflected in Indicator 7 in the Results Matrix, which is aimed at reducing tax noncompliance.

2.28 **Strengthen the sustainability of the pension system by means of structural reforms.** The IDB Group will provide technical support for formulating and implementing structural reforms of the CSS aimed at improving the financial sustainability, coverage, and sufficiency of pensions. To this end, we will promote measures to improve the funding of the system, such as a review of contribution rates and an increase in coverage by eliminating barriers to the formalization of independent workers, and the sufficiency of pensions without compromising fiscal stability.

2.29 **Optimize public expenditure by means of budget evaluation and planning tools.** The IDB Group will endeavor to implement expenditure program evaluation and results-based budgeting tools to improve the efficiency of expenditures. It will incorporate public expenditure evaluation methodologies and monitoring systems to identify and reduce leakages, reallocating resources toward priority areas (education, health care, infrastructure) in territories in which their impact will be greatest. At the same time, it will reinforce internal control and audit mechanisms, using technology to prevent leakages and ensure that every balboa spent produces tangible development results.

2.30 **Strengthen public investment management to improve the execution of strategic projects.** Improve the prioritization, planning, and execution of strategic projects to accelerate the pace of investment in development. The IDB Group will work on simplifying and streamlining administrative processes (such as by optimizing the ex ante procedures at the CGR and modernizing public procurement) to reduce delays in the execution of works. In addition, it will promote transparency along the entire public investment cycle—from project prioritization to project procurement and monitoring—ensuring an alignment with national priorities and maximizing the socioeconomic yield of the investments.

2.31 **Boost the State’s public management efficiency.** The IDB Group will seek to strengthen the crosscutting public management systems by implementing more robust monitoring and evaluation mechanisms and a more professional, merit-based, and efficient civil service. It will boost digitalization and electronic government with a view to enhancing the State’s management efficiency in line with Indicator 10 in the Results Matrix, which is concerned with strengthening the digitalization of governmental procedures. In addition, the IDB Group will promote open government policies as an instrument for reinforcing transparency in the use of public resources, while at the same time supporting the adoption of best practices in governmental control systems. It will invest in strengthening the national statistics service, including open data platforms and interoperability of financial, procurement, and other systems, facilitating data exchanges between public sector entities. It will also invest in strengthening the national police capacity to bolster strategies for deterring violent crime, as well as the penitentiary system's capacity to improve its management efficiency. This will make it possible to automate processes, reduce administrative timelines and costs, and provide better-quality and more accessible public services, while at the same time strengthening traceability and electronic controls and improving citizen security.[58]

2.32 **The country strategy will focus on enhancing the efficiency of the public administration and facilitating a favorable business climate by comprehensively digitalizing governmental procedures,** lowering administrative costs, and boosting traceability in key processes for the general public and for businesses. In parallel, the IDB Group will strive to accelerate the pace of public investment execution and improve its effectiveness by optimizing critical administrative processes, simplifying complex procedures (particularly the ex ante procedures at the CGR) and modernizing public procurement to reduce delays in the execution of priority projects. These actions will make it possible to improve the quality of public spending, reduce leakage errors in social programs, and advance toward a more efficient management of fiscal resources.

2.33 **Promote the creation and operationalization of a Fiscal Board[59] to strengthen economic governance.** The IDB Group will support the establishment and operationalization of an independent Fiscal Board to strengthen economic governance. This technical body will advise on medium-term macrofiscal planning, assess compliance with fiscal rules, and foster budgetary discipline. It will play a key role in providing rigorous analyses to guide fiscal policy, strengthen public finance management, and reinforce the country's commitments to fiscal sustainability.

2.34 **Promote fiscal sustainability by means of efficient management of the public debt.** The IDB Group will strengthen financing strategies and fiscal risk management to enhance the country's macroeconomic stability. We will design medium-term financing strategies, diversifying sources and maturities to reduce vulnerability to external shocks. At the same time, we will improve the management of fiscal risks (including contingent liabilities) and reinforce the capacity to analyze debt scenarios in order to enable Panama to preserve its fiscal sustainability and gradually recover fiscal space to invest in development.

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58 Sexual and gender-based violence is a priority area for improving interagency coordination (in data capture and analysis, service coordination, etc.). In addition, we generally recommend continuing to strengthen the national statistics system in terms of its capacity to capture and analyze diversity-related demographic variables.

59 Under Law 68 of 26 December 2018, which amended Law 34 of 2008 on fiscal social responsibility and included other provisions, the Fiscal Board was created as an independent body tasked with providing technical analyses of macrofiscal policy by issuing nonbinding opinions in the form of reports on various aspects of public finance.

EXPECTED IMPACT

Reducing tax noncompliance and expanding fiscal space. The Bank's investment portfolio and technical assistance is expected to help sustainably boost tax collection and reduce evasion, providing the State with more self-sourced funds to finance quality public goods and services. A more efficient and broader-based tax system will also improve fiscal progressivity, fostering equity in corporate contributions.

Boosting the collection of social security contributions, thereby promoting the sustainability of the pension system and ensuring better conditions for retirees. The reforms will contribute to the sustainability of the pension fund, ensuring timely payment of current and future pension benefits under fair conditions. A financially better balanced social security system will reduce uncertainty for older adults and mitigate a significant long-term fiscal risk, strengthening social cohesion.

Enhancing public spending efficiency, thereby enabling a better allocation of resources in priority areas. Improvement in expenditure management will result in a more efficient use of public resources, allowing more to be done with the same budget. A reduction in leakages and superfluous expenditures is expected, freeing funds for investment in priority sectors (such as education, health care, and social protection). Thanks to a more efficient allocation, public policies will have a more tangible impact on the wellbeing of the population, narrowing social and territorial gaps.

Strengthening State digitalization and modernization, thereby enhancing the quality of public services. Adopting digital technologies will reduce administrative costs and boost the efficiency of the public sector. Institutional modernization and digitalization will enhance effectiveness and accountability in public management. More streamlined and open processes will improve the delivery of services to the public and reduce discretion in administrative decisions. Together, these actions should translate into greater public and investor confidence in Panamanian institutions and a stable business climate, laying the foundations for a virtuous circle of stability, investment, and sustainable development in Panama.

PILLAR 3. SUSTAINABLE GROWTH THROUGH THE PRIVATE SECTOR AND THE USE OF STRATEGIC ASSETS

2.35 **The core objective of this pillar is to promote sustainable, resilient, and competitive economic growth by enabling private investment and harnessing the country's strategic assets.**[60] Water management plays an essential role in the performance of the most important sector of the Panamanian economy: service exports, particularly logistics and transportation services, whose sustainability is directly dependent on the resilience of the watersheds, especially the Panama Canal watershed. This resilience is an essential precondition to activating and sustaining growth in other productive sectors. In this context, the IDB Group will support the strengthening of key sectors such as logistics, sustainable tourism, productive innovation, and digital technologies. This pillar will also incorporate resilience approaches to shocks, including climate shocks, by means of strategic investments and institutional strengthening to enable sustainable use of the country's natural and economic assets. To this end, the IDB Group will promote the use of complementary financing arrangements, such as PPPs, guarantees, and coinvestment funds, to expand private investment without creating new direct fiscal liabilities, thereby reinforcing fiscal sustainability while invigorating economic growth.

WHY IS IT IMPORTANT?

2.36 **Panama has unique natural and strategic assets, but there are pressing challenges to their sustainable use.** The Panama Canal and the national logistics infrastructure are drivers of growth: the Canal handles close to 3% of the world's maritime trade. However, the Canal's competitiveness is compromised by its water vulnerability, exacerbated in a context of climate change. Rainfall variability and recurrent droughts have reduced water levels in the lakes that feed the Canal, affecting its ability to operate. In recent years, the water crisis forced the Panama Canal Authority (ACP) to impose draught restrictions and limit vessel traffic, reducing the Canal's efficiency and causing delays in international trade. Ensuring the Canal's water resilience is essential to its long-term sustainability and to preserving this strategic asset. This requires innovative water management solutions that include, but are not limited to, new reservoirs, water reuse and operational efficiency, and forest restoration in water protection areas.

2.37 **Insufficient resilience[61] aggravates these challenges by threatening the country's infrastructure and development.** Panama is highly vulnerable to

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[60] For purposes of this strategy, "strategic assets" is understood to mean the key resources and infrastructure that support the country's sustainable growth and resilience. They include watersheds, biodiversity, and natural capital, as well as the associated logistics infrastructure.

[61] The CDC document emphasizes improving water resource management and natural capital protection to contribute to climate resilience. It is essential to support integrated management of water resources in all of the country's watersheds, aligning it with the Plan Nacional de Seguridad Hídrica 2015-2050. In the specific case of the Panama Canal watershed, the Panama Canal Authority has prepared a Plan Indicativo de Ordenamiento Territorial Ambiental (PIOTA) with IDB support with a view to guiding territorial, socioeconomic, and protection activities, sustainable development, and environmental control in the Panama Canal watershed. However, the actions set out in the PIOTA need to be operationalized.

extreme climate events and phenomena (floods, tropical storms, droughts) that are already affecting critical infrastructure—such as roads, bridges, and ports—, disrupting logistics chains, harming agricultural production, limiting access to drinking water service, and jeopardizing the wellbeing of the population. For example, the most severe floods have caused significant material damage and even forced temporary closures of the Canal, laying bare the vulnerability and exposure of strategic assets, while the droughts have impacted the availability of water supply for the population and for economic activities. Improvements in territorial planning and climate adaptation are urgently needed to mitigate these impacts and ensure long-term sustainable development. Similarly, the energy transition has become a priority. The current matrix relies on fossil fuels and large hydropower plants, which are vulnerable to rainfall variations, compromising energy security. Diversifying power sources to include nonconventional renewable energy (solar and wind) and promoting energy efficiency are essential for diminishing the carbon footprint, reducing vulnerability to climate change, and lowering energy costs in the future, strengthening the country's industrial competitiveness. Panama has taken steps to expand energy supply through auctions for power generation and bidding processes for transmission lines and associated substations. A renewed focus on auctions for renewable power generation or storage, or power purchase agreements, can diversify the electricity matrix, accelerate private investment, and enable businesses to obtain energy at more competitive and stable prices.[62]

2.38 **Panama's economic growth is concentrated in few sectors, increasing its vulnerability to external shocks.** Exports of domestic goods account for less than 2% of GDP, reflecting the country's limited productive base, which in addition is mostly of low or moderate complexity.[63] The economy has been concentrated in construction, commerce, the Canal, and logistics services, posing a risk in the event of disruptions in these sectors. Close to 46% of GDP[64] and 33% of employment[65] originate from those sectors.[66] Strengthening new, emerging sectors such as sustainable tourism and the digital economy is essential with a view to diversifying the productive structure, creating quality jobs, and reducing the reliance on traditional activities. A broader and more complex economic base will make Panama more resilient and strengthen its competitiveness regionally and globally. At the same time, diversifying the agribusiness sector is also important,

62 For example, as in the case of Brazil (Bloomberg NEF, 2024).

63 Panama is ranked 70th out of 145 economies on the Economic Complexity Index, which is a significant drop of 37 places from a decade ago. This major decline is primarily due to a lack of export diversification, particularly technology- and knowledge-intensive exports (Harvard's Growth Lab, 2025).

64 Refers to real GDP data published by INEC (with 2018 and 2007 as reference years, based on availability) between 2014 and 2024 for construction, wholesale and retail commerce, and transportation, warehousing, and communications.

65 Refers to INEC data on public sector, private sector, and other employees between 2014 and 2024 in construction, wholesale and retail commerce, and transportation, warehousing, and postal service.

66 In addition, more than 55% of economic growth was concentrated in construction, wholesale and retail commerce, and transportation, warehousing, and communications activities, taking into account real GDP growth data from 2014 to 2024 published by INEC (with 2018 and 2007 as reference years, based on availability).

since it employs one of every six Panamanian workers[67] and does so in regions of core significance for the resilience of the country's watersheds. However, its relative weight in the economy is low (the value-added of agriculture, forestry, and fishing totaled 2.5% of GDP in 2023), partly due to challenges that erode its productivity and have led to stagnant growth since 2015. These challenges include a concentration of activity in a limited set of low-complexity fields, limited access to inputs and services (including financial services), pronounced seasonality, high postharvest losses, tenuous industrialization, and highly fragmented land tenure.

2.39 **The country has untapped potential in the tourism sector.** Tourism revenue exceeded US$8.4 billion in 2023, and direct tourism-related employment accounted for 11% of total employment in 2024. Despite its proven contribution to exports, job creation, and attracting investment, the tourism sector faces major challenges that limit its competitiveness and hinder Panama's ability to compete in the regional market as a destination. Although Tocumen International Airport handled 19.2 million passengers in 2024, Panama received a mere 2.7 million visitors that year (well below the figures for its direct competitors in the region, such as Costa Rica and El Salvador), revealing a significant opportunity to increase the country's market share. Although Panama has innumerable comparative advantages in terms of the attractiveness of its natural and cultural resources, what prevails is limited diversification of quality tourism offerings[68] with concentrated investment, high vulnerability to climate events and other impacts that can degrade the ecosystems that motivate tourist visits, and weak governance as reflected in nonprofessionalized public management, low institutional capacity to supervise the sector, and an absence of business intelligence and data to inform strategic planning decisions.

2.40 **Lastly, there are persistent gaps in access to sustainable financing.** Despite a growing global interest in green finance, Panama faces difficulties in mobilizing sufficient funds for resilient and low-emissions infrastructure projects. Private investment in climate initiatives remains limited. Despite the capital market's adherence to sustainability principles, the launch of the sustainable finance taxonomy, the approval of guidelines for issuing social, green, and sustainable marketable securities, and a corporate sustainability policy at Latinex, innovative financial instruments such as green bonds, international climate funds, and blended public-private finance arrangements have yet to be fully utilized. The Panamanian capital market has made some recent progress, but it is still only an incipient source of long-term finance for productive investment. The debt market accounts for only a fraction of the banking system and GDP, with only limited secondary market activity and a high concentration in financial and real estate sector issues. While standing out for its low State participation in comparison to other countries in the region, it continues to have relatively little depth. Regional integration, support for sustainable bonds, and the presence of pension fund management companies create opportunities, but limited institutional investor participation and a weak pension system curtail its development. Adopting these mechanisms at a faster pace will be

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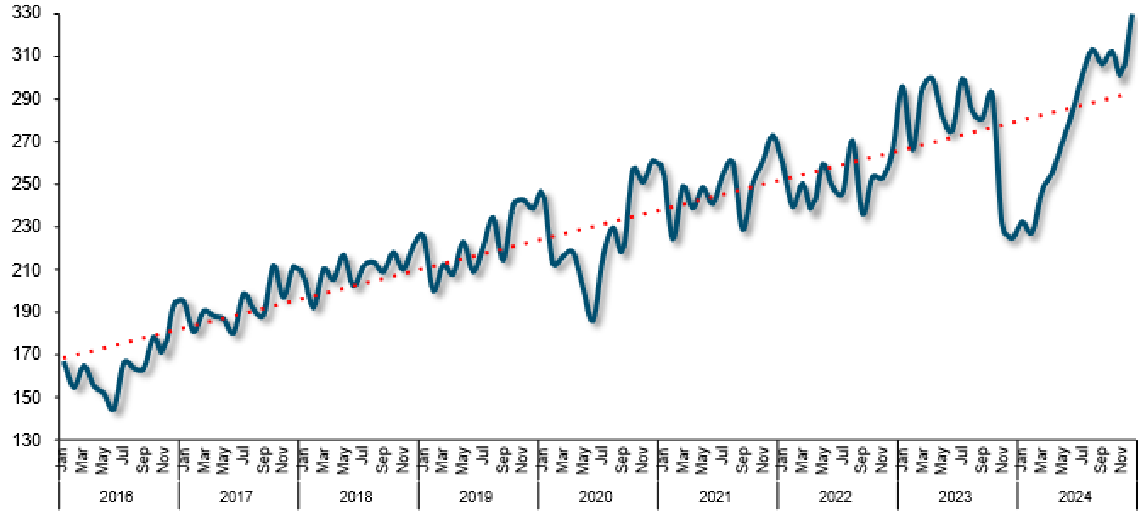
[67] The agricultural sector employs the largest percentage of the population in the country's comarcas: 81.4% in Ngäbe-Bugle, 66.8% in Emberá Wounaan, and 51.8% in Guna Yala (UNDP, 2016), according to the IDB report Análisis de Políticas Agropecuarias en Panamá, 2023.

[68] Worth noting in terms of the diversification of tourism offerings is Law 290 of 24 March 2022 on indigenous tourism and its implementing regulations, expected to be approved in 2025, giving the State the authority to support advances in indigenous tourism.

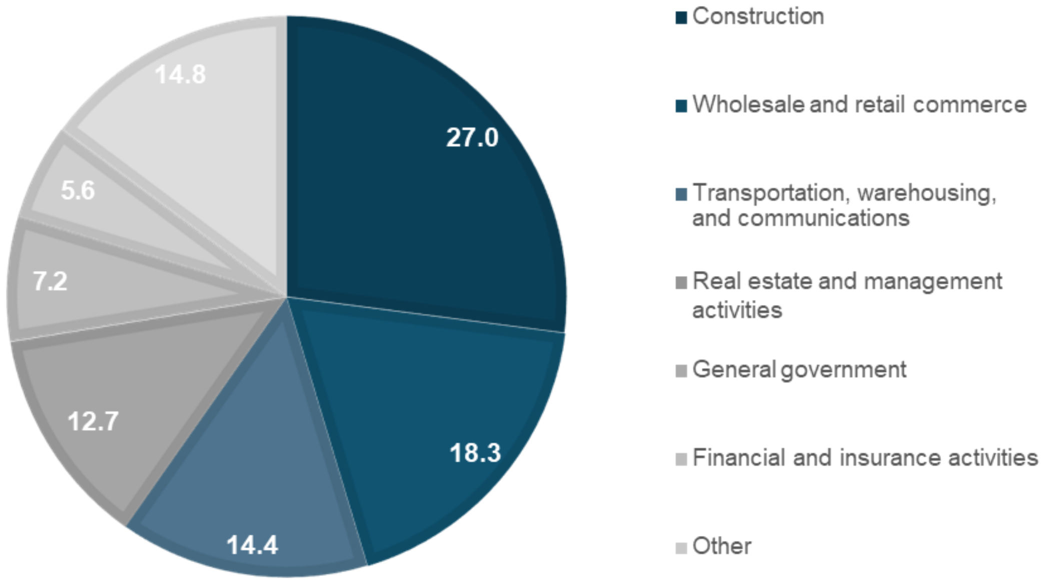
critical in order to channel capital toward the country's environmental priorities. In short, addressing these gaps will make it possible to sustainably harness Panama's natural and strategic assets, strengthening the country's resilience to climate change and boosting its competitiveness in key sectors.

FIGURE 5. IMPACT OF EXTREME CLIMATE EVENTS ON THE PANAMA CANAL WATERSHED. MONTHLY TOLL REVENUE, 2016-2024 (US$ MILLIONS)



Source: National Statistics and Census Institute (INEC).

FIGURE 6. CONTRIBUTION TO GDP GROWTH, BY ACTIVITY (2014-2024 AVERAGE, % OF THE TOTAL)



Note: Real GDP data are used, with 2018 and 2007 as reference years, based on availability.
Source: Prepared by the authors with data from the National Statistics and Census Institute (INEC).

WHAT WE WILL DO

2.41 To face these challenges and fully leverage Panama's strategic advantages, the strategy proposes a set of coordinated actions:

2.42 **Strengthen the country's water resilience, especially in the Panama Canal watershed, through investments aimed at improving water management.** IDB Group interventions will strengthen the water planning, measurement, and management systems for efficient water use and implement water infrastructure solutions, including the construction of new reservoirs, new water purification plants to ensure availability of water for various uses under a sustainability system, watershed protection, and water reutilization, optimizing watershed management, primarily in the Canal watershed. These measures, with public and private participation, will ensure a **sustainable water supply** for human consumption and for Canal operations and will **mitigate the effects of climate change** on shipping, ensuring the long-term continuity of this strategic corridor. The measures are aligned with Indicator 12 in the Results Matrix, which is focused on management of vulnerable watersheds.

2.43 **Modernize the basic and productive logistics infrastructure and adapt it to climate events to boost competitiveness.** The IDB Group will promote strategic investments in ports, airports, customs systems, and logistics services that incorporate advanced technology and climate resilience criteria. Logistics corridors will be modernized and progress will be made in digitalizing the sector to strengthen Panama's position as a competitive logistics hub. IDB Invest will seek to support private investments that address logistics gaps and will explore opportunities to expand the quality and capacity of strategic road corridors through private participation arrangements. The IDB Group will analyze the needs for new shipyards and infrastructure to handle solid and liquid bulk, exploring blended investment models for implementing them. In terms of energy, the IDB Group will contribute to a sustainable transition through policies and regulatory frameworks that encourage private investment in nonconventional renewable power generation, industrial and urban energy efficiency programs, and development of green hydrogen. These actions[69] will help to lower dependence on petroleum derivatives and on hydropower plants vulnerable to droughts, reducing the national carbon footprint and contributing to the goal of maintaining carbon negativity to 2050.[70] At the same time, the IDB Group will promote regional energy integration through electric interconnection with Colombia and by evaluating a linkage with the SIEPAC regional electricity market. The investments in digital infrastructure, coupled with logistics and energy development, will deepen both economic integration and productive diversification. These efforts will be bolstered by

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69 These actions will be aimed at advancing toward an inclusive energy transition, improving women's share in the Panamanian energy sector's labor force, which in 2021 stood at 33.6% versus 66.3% in the case of men. In this regard, the IDB supports the "Nexo Mujer y Energía" roadmap, an initiative aimed at pursuing gender equity in the sector.

70 Panama is one of the world's eight carbon negative countries thanks to the balance between its greenhouse gas emissions and the absorption capacity of its ecosystems. In Latin America and the Caribbean, only Suriname and Panama are on this list. The National Energy Secretariat, with IDB support, is analyzing the costs and benefits of the energy transition to decarbonize the energy and transportation sectors by 2050 (NDC2, 2024).

coordinating incentives for investment in R&D, specialized labor training programs, technology adoption, development of value chains, and foreign trade finance to facilitate the internationalization of Panamanian companies. In parallel, IDB Lab will foster an entrepreneurial ecosystem and the adoption of innovative solutions by means of regional and global connections.

2.44 **Protect natural capital and expand climate and green finance.** The IDB Group will foster the development of sustainable and high value-added industries, including tourism.[71] In this industry, Bank support will focus on substantially improving sector governance by updating the current regulatory framework and assisting in professionalizing public management and modernizing institutional management. The Bank will also promote improvements in sustainable management and protection of the country's natural and cultural heritage. In addition, jointly with IDB Invest, the IDB will support diversification and deconcentration of the country's tourism offerings with a view to expanding their socioeconomic footprint toward the provinces and comarcas. In terms of climate finance, the Bank will work to create a favorable environment by strengthening the local financial system's capacity to expand its green finance portfolios. It will actively promote the issuance of green and sustainable bonds and other climate finance instruments,[72] taking advantage of the new guidelines for issuing marketable securities in the domestic capital market. Furthermore, the Bank will develop innovative blended finance arrangements that effectively combine public, private, and international cooperation resources. This set of tools will make it possible to leverage strategic investments in resilient and low-emissions infrastructure, closing financing gaps and accelerating priority projects on climate mitigation and adaptation.

[71] Tourism activity takes place mainly in Panama City due to its well-developed service sector, the presence of the Canal and of stores that cater to the popular shopping tourism, and the existence of an important banking hub and conference tourism facilities.

[72] In all, 22% of the nation's territory is recognized as comarcal or indigenous collective territory. This territory contains large forest areas that can potentially benefit from climate finance instruments.

EXPECTED IMPACT

Strengthening the resilience of watersheds, including the Panama Canal, by mitigating the risk of floods, developing adaptation strategies in watersheds that are vulnerable to climate change, and improving efficiency and water conservation. The interventions will help to reduce the risks associated with water scarcity in the Canal, thereby strengthening the operational capacity of this key global commerce infrastructure and the sustainability of the services it provides. The investments supported by the Bank in the Canal watershed, combined with environmental conservation efforts, will improve the availability of water resources and help to progressively diminish the vulnerabilities related to extreme climate events. In addition, boosting management effectiveness in the targeted protected areas will help to reinforce watershed resilience.

Modernizing logistics infrastructure under climate and environmental criteria, thereby helping to deepen trade integration. The Bank's interventions will help to gradually reduce the cost and time associated with foreign trade, facilitating Panama's enhanced competitiveness as a regional hub. Trade integration will also be strengthened by expanding foreign trade finance and value chain finance, both of which are essential for internationalizing local businesses. Private investment financing will mobilize the skills of the private sector in asset modernization and delivery of infrastructure services. In addition, support for the development of emerging sectors, such as sustainable tourism, innovative agroindustry, and the digital economy, will help the country to gradually diversify its economic structure, grow in complexity, and expand the export basket of goods and services, partially mitigating risks stemming from the current concentration in a few sectors.

Implementing innovative financial mechanisms such as blended finance and public-private partnership (PPP) arrangements to help to reduce existing financing gaps in strategic areas, making it possible to develop the debt market, mobilize more resources for key environmental initiatives, and promote the development of a climate finance market. These efforts will help to mitigate risks, reduce critical gaps, and gradually reinforce the country's economic, social, and environmental sustainability. In addition, they will make it possible to diversify and expand the sources of financing for investment projects, contributing to economic growth and to a deepening of the Panamanian capital market.

CROSSCUTTING PILLARS

WHY IS IT IMPORTANT?

2.45 **Institutional strengthening.** Institutional strengthening is essential for improving public and private investment planning, prioritization, and execution capacity and ensuring effective management in Panama. At present, institutional weaknesses, bureaucratic delays, and poor interagency coordination impair effectiveness in the implementation of key projects, while also curtailing investor confidence. These difficulties highlight the importance of reinforcing strategic planning, public spending efficiency, and public management.

2.46 **Sustainability and resilience.** Environmental and climate vulnerability poses a critical challenge to sustainable development in Panama. The country regularly experiences floods, droughts, and climate hazards that jeopardize strategic sectors such as the Canal, agriculture, and public and private infrastructure. In addition, biodiversity loss and deforestation continue to affect long-term sustainability. Accordingly, this country strategy emphasizes a crosscutting integration of climate and environmental resilience into all operations.

2.47 **Inclusion and equal opportunities.** Panama continues to face deep inequalities which primarily affect women, indigenous populations, Afrodescendants, persons with disabilities, and LGBTQ+ communities. These inequalities are manifested in higher poverty levels, discrimination, violence, employment exclusion, and limited access to quality basic services, especially in rural areas and indigenous comarcas.

WHAT WE WILL DO

2.48 **Institutional strengthening.** The strategy will prioritize the adoption of innovative tools such as the Smart Fiscal Ecosystem[73] and the Integration and Technological Solutions of the Operational Management Model (ISTMO) system,[74] as well as the promotion of good corporate governance practices, boosting confidence in the capacity of public and private institutions to respond effectively to the country's development challenges. Similarly, strengthening the business environment, including regulatory and institutional frameworks, will create favorable conditions for boosting private investment. Under the appropriate conditions, instruments such as PPPs can become effective purchase modalities for the financing, construction, operation, and maintenance of infrastructure assets, while ensuring service standards. This will require strengthening the institutions associated with the Public-Private Partnership Law,[75] consolidating public administration capabilities and

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[73] The data ecosystem "will enable government agencies to share high-quality information in a secure and confidential way. It will also feature algorithms that analyze third-party databases in real time, helping agencies identify beneficiaries of social programs, verify eligibility and obligations, and take other actions." Source: https://www.iadb.org/en/news/panama-make-spending-more-efficient-and-equitable-20-million-loan-idb.

[74] The ISTMO system was presented by the MEF in 2014 as a "management system that will allow functional integration and administrative decentralization, preserving the duties and objectives of each entity and providing an integrated vision that will make governmental process more streamlined and improve how information is obtained and analyzed efficiently and in timely fashion."
Source: https://elcapitalfinanciero.com/mef-presenta-proyecto-de-gestion-financiera-istmo/.

[75] The PPP mechanism for development was created under Law 93 of 19 September 2019 as an incentive for private investment, social development, and job creation.

improving the structuring of bankable projects as well as project performance and impact evaluations. The possibility of using these instruments in nontraditional sectors such as health, education, and water and sanitation can also be examined.

2.49 **Sustainability and resilience.** The strategy will promote investments in sustainable infrastructure, renewable energy, and nature-based solutions in line with national policies such as the National Climate Change Policy and the second nationally determined contribution (NDC2),[76] thereby strengthening the nation's capacity to address environmental and climate risks and ensure sustainable growth.

2.50 **Inclusion and equal opportunities.** The country strategy will explicitly integrate a gender and diversity approach into all IDB Group interventions, promoting specific programs to boost financial autonomy for women and effective inclusion of diverse groups and vulnerable populations. This will help Panama move towards more inclusive development, ensuring that all population groups have equal opportunities for participation and progress.

[76] Política Nacional de Cambio Climático y la Contribución Determinada a Nivel Nacional actualizada (CDN2) (National Climate Change Policy and updated Nationally Determined Contribution (NDC2)). June 2024.

III. HOW WE WILL ACHIEVE THIS

A. PROGRAMMATIC APPROACH

3.1 **Programmatic approach for greater impact.** Implementation of the country strategy will be based on a programmatic approach, structuring comprehensive programs that encompass coordinated operations to achieve strategic sector transformations. This approach will prioritize coordinated use of multiple IDB Group instruments (investment loans, conditional credit lines for investment projects, policy-based loans, technical cooperation operations, and guarantees) to mobilize resources, strengthen institutional capacity, and promote private investment. We will work on policy reform programs in which the IDB Group actively supports the country through sector dialogue, investment loans, and technical assistance. The strategy will aim to replicate prior good practices, such as the Bank's track record in the social protection sector, where over the course of more than a decade it combined technical cooperation, investment instruments, and policy-based loans in sequential programs that strengthened the social protection system and the beneficiary registries. Efforts of this type are supplemented by other initiatives aimed at enhancing public management, enabling crosscutting improvements in the quality of expenditures. Through its portfolio, the Bank will support a consolidation of advances both in social protection and in the interrelated areas of public management described under the pillars, following a selectivity approach. At the same time, collaboration between the IDB, IDB Invest, and IDB Lab will be promoted to maximize the synergies among public interventions, private financing, and innovative solutions, particularly in sectors such as resilient infrastructure, climate finance, and sustainable tourism. In addition, the strategy will incorporate periodic monitoring arrangements to enable dynamic adjustments in implementation, identify lessons learned, and respond with flexibility to changes in the operational context, with an emphasis on progress indicators.

B. SYNERGIES AND COORDINATION ACROSS SECTORS

3.2 The IDB Group recognizes that solid internal coordination, coupled with a strategic alignment with national and international actors, is essential for maximizing the impact of this country strategy. In Panama, close collaboration will be fostered both within the IDB Group (including its public and private sector windows) and with the government, the private sector, civil society, and other development partners. This joint work will make it possible to leverage synergies, avoid duplication, and ensure that Bank interventions are fully aligned with the priorities of the country and the efforts of other cooperation agencies.

3.3 Under **Pillar 1**, opportunities for synergy between the various windows of the IDB Group in Panama enable coordinated action to strengthen the financial sector and promote financial inclusion, combining instruments for private sector support with reforms and institutional strengthening in the governmental sphere, in addition to public mechanisms for recalibration (absorption and mitigation) of risks. The main upstreaming opportunities include designing guarantee arrangements using public and multilateral resources to reduce risk in loan operations with the private sector, reducing information asymmetries and boosting competition in the financial system by expanding credit bureaus with positive and negative information, and implementing an inclusive and interoperable digital payments system or other public digital infrastructure. Additional key actions include comprehensively mapping the cooperatives system for better regulation and supervision, strengthening open finance to facilitate competition and customer mobility, and promoting the fintech ecosystem by institutionally strengthening the financial authorities, modernizing the regulatory environment, and creating incentives to foster its growth and penetration, especially in unserved market segments. The IDB Group will undertake concerted action—spanning from support for public initiatives to investment and technical assistance through IDB Invest and IDB Lab—to further integrate the population into the formal financial system, boosting its productive capacity and economic resilience and thereby also helping to reduce poverty.

3.4 For **Pillar 3**, sustainable watershed management and expansion and rehabilitation of drinking water and wastewater treatment service will require mobilizing significant financial resources. This includes the use of specialized financial vehicles such as climate funds and blended finance arrangements. Large-scale mobilization of such resources will in turn require close coordination between the IDB Group’s public and private windows. The complementary strengths of the IDB Group provide opportunities for structuring joint interventions that could channel public and private investment toward comprehensive management of watersheds. This synergy will enable the IDB Group to scale up initiatives for conservation and efficient use of water, ensuring sustainable outcomes in terms of climate resilience and water security for Panama. In addition, the IDB Group will support strengthening the legal and institutional framework of the water and sanitation sector, as well as a review of the criteria and formulas for determining rates, with a view to enhancing the efficiency and suitability of private financing. A clear and stable regulatory framework, combined with a well-defined allocation of responsibilities, can make the sector more attractive for private investment. In addition, the IDB Group will explore leveraging public-private participation mechanisms to finance critical infrastructure projects so as to properly mitigate the inherent risks in works of this type and attract capital market investors. The Bank’s upstream work on PPPs as a device for risk sharing and attracting private investment may include: supporting the government on regulatory changes to boost the efficiency of contracting through PPPs under Law 93; continuing to provide support in developing rules to account for, record, and measure the fiscal impact of projects; and supporting regulatory reforms to avoid a multiplicity of laws and overlapping responsibilities in solid waste management.

3.5 Also under **Pillar 3**, the IDB Group will promote synergies in other key areas, such as sustainable logistics infrastructure and the circular economy, including comprehensive management of urban solid waste at the regional level and wastewater reuse (in industry and agriculture), with private participation in introducing innovative treatment and smart monitoring technologies. In logistics, public-private coordination will be aimed at developing a resilient transportation infrastructure and cleaner and more efficient supply chains, reducing the carbon footprint and strengthening Panama's position as a regional logistics center. Similarly, boosting the circular economy will entail collaboration among industries, municipalities, and communities to implement waste recycling, reuse, and management practices designed to convert waste into new productive resources. Synergies will require strengthening some regulatory and institutional frameworks to create suitable conditions for attracting and facilitating private investment. At the same time, innovative financing alternatives with a high capacity for mobilizing institutional investor resources will need to be developed to move forward on key agendas, including the social and climate agendas. Public-private collaboration will be crucial for this purpose. For example, in sustainable tourism, long-term planning will be strengthened to diversify the country's offerings and adequately position strategic destinations and high-value segments. Opportunities are also foreseen for the development of integrated solutions to scale IDB Lab-supported innovative business models in productive activities. The IDB Group will facilitate these multisector collaborations by providing financing, technical knowledge, and platforms for dialogue. Through this integrated approach, the strategy will ensure that interventions under Pillar 3 are mutually reinforced, jointly generating economic and environmental benefits and avoiding isolated efforts on the path to a more sustainable development.

C. IDENTIFICATION OF PRIORITY REFORMS

3.6 **The Bank's country strategy with Panama highlights a set of priority reforms, each closely aligned with the strategy's pillars.** These initiatives are essential for promoting sustainable and inclusive development of the country, and implementing them successfully will require solid interagency coordination and overcoming major implementation challenges. The current political context poses challenges to advancing reforms that require legislative approval. However, the government has indicated that policy-based loans continue to be of interest and could be requested during the strategy period. Below is a description of the main identified reforms and their connection to the country strategy's pillars.

3.7 **Comprehensive reform of the social protection system (Pillar 1).** Panama faces significant social inclusion challenges, particularly in rural and indigenous areas, that have been exacerbated by the pandemic and other recent shocks. The current social protection network has major limitations in terms of coverage, effective targeting, and responsiveness. At the Bank, we have worked closely with Panama for more than a decade to consolidate its social protection system. To continue to overcome these challenges, Panama, with Bank support, will move forward on the second phase[77] of the comprehensive reform of the system, which includes expanding and strengthening the RSU, thereby enabling better targeting of benefits and faster response to social or economic crises. In addition, this registry expansion will indirectly help enhance the efficiency of public expenditure by reducing inclusion and exclusion errors (leakages) in social programs. Complementing this effort, the reform envisages specific interventions to promote

[77] PN-L1178 (phase one).

productive inclusion, particularly among rural and indigenous women, through the delivery of productive assets, culturally adapted technical training, and strengthening of local capacity to generate sustainable income. At the same time, the reform is aimed at expanding the coverage and substantially improving the quality of early childhood development services through investment in infrastructure adapted to bioclimate standards, staff professionalization, and family work programs, caring for vulnerable children to narrow early gaps in human capital. Lastly, the reform establishes a comprehensive model of care for the dependent population by creating specific pilot programs that strengthen the institutional framework and free up productive time, especially for women caregivers. Effective implementation of these measures will require significant technical and financial resources as well as close interagency coordination (among MIDES, local governments, and civil society) to consolidate a more robust, inclusive, and resilient social protection network aligned with the strategic priorities of the country. These reforms consolidate the advances made with Bank support in strengthening the social protection system through a program aimed at transparency and equity in social expenditure[78] and through the execution of technical cooperation operations. Initial strides made in expanding early childhood development services through the portfolio in execution,[79] with a view to helping make Panama's population less vulnerable, will assist the country in undertaking the investments required to implement the policy reforms, enhancing the sustainability of the results.

3.8 **Pension reform and health care sector integration (Pillar 2).** The recent approval of the pension reform in Panama (Law 462 of 2025)[80] marks a significant step forward in addressing the country's fiscal pressures and critical gaps in social protection. Previously, the system faced a pressing financial sustainability challenge brought about by exhaustion of the defined-benefit subsystem's reserves, insufficient coverage, and concerns among the general public regarding the future safety of their pensions. Through technical and strategic assistance provided by the IDB Group, the reform ensures the existence of funds for pension payments and improves financial sustainability by: establishing a Single Solidarity Fund that consolidates the contributions and reserves of the existing subsystems; gradually increasing employer contributions from 12.5% to 15.25% between 2025 and 2029; and introducing an annual fiscal subsidy of up to US$966 million to make public expenditure in pensions predictable, preventing this expenditure from rising from less than 0.2% of GDP to 3.5% of GDP in 20 years. In addition, the reform expands coverage by means of innovative mechanisms (such as simplified digital platforms for contributions) to incorporate informal and independent workers into the system, creates a minimum guaranteed pension (US$265 per month) to be annually adjusted for inflation, and ensures that pension savings will be converted to lifetime pensions, providing retirees with an assured income for life. It will be critically important to implement this reform effectively, and the Bank will continue to provide technical support to the Panamanian government to ensure a

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78 PN-L1103; PN-L1118; PN-L1152.

79 PN-L1105; PN-L1177.

80 Law 462 of 18 March 2025 amends, adds, and repeals articles of Law 51 of 2005, which amended the Organic Law on the Social Security Fund, and sets out other provisions.

sustainable, transparent, and fiscally responsible execution,[81] thereby contributing to the country's economic and social stability. It is equally critical to achieve adequate coordination between the CSS services and the Ministry of Health (MINSA) (pillar 1). The health care sector needs to update and develop mechanisms to facilitate the integration of the MINSA and CSS assistance services, including interoperability of electronic medical records, fee schedules, and service scheduling. Mechanisms should be implemented to make health care expenditures more efficient and monitor the implementation of these improvements. This includes updating or implementing digital platforms for public procurement traceability and auditing of funds allocated to the sector.

3.9 **Fair and sustainable energy transition (Pillar 3).** Under Pillar 3, associated with environmental sustainability and climate action, the Bank will continue to support the second phase[82] of key reforms to enable Panama to advance toward a fair and sustainable energy transition. These reforms are intended to accelerate the pace of decarbonization of the economy and contribute to fulfillment of the commitments made under the Energy Transition Agenda and the Paris Agreement. To this end, they promote the expansion of variable renewable sources, such as solar, wind, and hydro, reducing reliance on fossil fuels. They also promote digitalization of the electricity sector, facilitating network modernization and energy management efficiency. In addition, they foster electric mobility through the deployment of charging stations and expansion of clean public transport. These reforms support universal access to electricity, with an emphasis on rural electrification, and promote narrowing the gender gap in the sector. At the same time, they promote capacity-building in green jobs, preparing the workforce for the energy transition. To move forward on these objectives, they support introducing changes in the energy sector's regulatory framework to attract investment, strengthen sector planning, and ensure an enabling environment for the development of clean energy. The NDC2 commitment includes production of green hydrogen and its derivatives, adding a crucial dimension to the energy transition. The introduction of green hydrogen will help to lower industry emissions and reduce fertilizer and heavy transport use. Public and private financing will also be needed, as well as international support for the adoption of sustainable technologies. The Bank is providing technical assistance specifically to encourage solar renewable power generation;[83] transformation of technical training through a clean energy training program, especially focused on electric mobility and distributed power generation; and energy efficiency in public spaces and buildings. Interagency coordination among the Energy Secretariat, the Ministry of Environment (MiAmbiente), and other entities will be key for updating regulations, establishing incentives, and implementing strategic projects. The main challenges include creating a stable regulatory framework, efficiently integrating renewable energy into the matrix, and

[81] On the other hand, technical support to the MEF will be aimed at optimizing public expenditure and tax administration, ensuring that resources are allocated to areas with the highest social and productive impact, while revenue is progressively reinforced.

[82] PN-L1181 (phase one).

[83] According to data from the Autoridad Nacional de los Servicios Públicos (National Public Utilities Authority) (ASEP), in 2023, 64.5% of the installed power generation capacity was obtained from renewable sources (hydro, wind, and solar) and 35.5% from nonrenewable sources (thermal); solar energy alone accounted for 13% of the total. Advances have been made with respect to prior years, since in 1988, the respective percentages were 53.5% renewable, 46.5% nonrenewable, and 0% solar.

promoting sustainable consumption patterns, ensuring the competitiveness and reliability of the energy supply.

3.10 **Sustainable, inclusive, and resilient tourism (Pillar 3).** Under Pillar 3, the country strategy will continue the support provided during the previous strategy period, and complemented by technical assistance resources, to transform the Panamanian tourism sector into a competitive, sustainable, inclusive, and resilient model. Tourism is key for diversifying the country's productive matrix with impact and territorial equity. In view of the challenges described in the pillar, the second phase of the proposed reform[84] will be aimed at substantially improving these issues, promoting an updated regulatory framework under a new General Tourism Law that promotes environmental sustainability, closes gender gaps, and enhances ethnic inclusion. The success of this reform will require effective coordination among multiple actors, such as the Autoridad de Turismo de Panamá (Panama Tourism Authority) (ATP), the Ministries of Environment, Agriculture, Government, and Women, local governments, and the private sector. Key provisions include a regulation to protect sensitive ecosystems such as coral reefs, promotion of carbon-neutral practices, educational strategies to foster conservation of the natural and cultural heritage, and appropriate training of tourism staff for safe observation of biodiversity, among other things. Implementing these changes will require mobilizing significant public and private financial resources, in addition to specialized technical assistance, to ensure the tourism sector's competitiveness and resilience to climate and health hazards, optimizing its contribution to the country's inclusive economic development. The IDB Group will also work to support the ATP in diversifying the tourism portfolio by fostering the development of products, experiences, and productive linkages that showcase the potential of territories suitable for agritourism, indigenous tourism, and nature-based tourism, all of which are in high demand following the pandemic and predominate in rural environments where tourism can have a greater impact on improving the quality of life of the host communities. On the basis of a dialogue with the various stakeholders, it will be essential to assist in implementing the new Sustainable Tourism Master Plan 2025-2030,[85] including opportunities for the private sector in the deployment of support infrastructure. Strengthening the "country brand" will be key to positioning new destinations and high-value segments; similarly, it will be crucial to foster a sustained and participatory (public-private) strategy for promoting and marketing these offerings in outbound markets with the highest yield and potential.

3.11 **Sustainable water management (Pillars 1 and 3).** The country strategy will support strengthening governance in the water sector by consolidating the responsibilities associated with water management, now scattered across various institutions. This will enable data- and evidence-based decision-making, as well as long-term planning with a watershed vision that considers climate variability and economic development. In addition, the IDB Group will improve coordination with the ACP for consensus-based decision-making that benefits the country's economic and social development as a whole. At the same time, work will be done to transform and consolidate the delivery of water and sanitation services, currently

[84] PN-L1175 (phase one).

[85] Which will succeed the Plan Maestro de Turismo Sostenible de Panamá 2020-2025 (Master Plan for Sustainable Tourism in Panama 2020-2025).

dispersed among the Instituto de Acueductos y Alcantarillados Nacionales (National Water and Sewer Systems Institute) (IDAAN), the Panama Sanitation Program, and MINSA's Dirección del Subsector de Agua Potable y Alcantarillado Sanitario (Water and Sewer Subsector Bureau) (DISAPAS). The objective is to focus efforts on narrowing the service access gap and strengthening management capacity to ensure proper project execution, infrastructure operation and maintenance, customer service, and long-term financial sustainability.

3.12 **Urban solid waste management (Pillar 3, crosscutting).** As part of Pillar 3, Panama will move forward on a priority reform that promotes comprehensive and sustainable management of urban solid waste, directly tackling environmental, social, and public health challenges. In view of the challenges described in Pillar 3, this reform is aimed at implementing a modern and sustainable model based on Law 276 of 2021,[86] strengthening sector governance by developing specific technical and institutional instruments as well as through substantial investments in key infrastructure, including controlled landfills, recycling and waste treatment plants, and energy recovery initiatives. The Urban and Household Sanitation Authority (AAUD), which is the main executing agency, will need significant institutional capacity-building support, considering its limited experience with Bank-financed operations. Innovative financing arrangements are envisaged for the development of key infrastructure, such as concession models or PPPs, possibly with the participation of the Bank's Public Private Partnerships Unit and, if conditions allow, IDB Invest. In addition, the strategy envisages citizen awareness campaigns to encourage cultural changes toward waste reduction and separation at source.[87] The main implementation challenges include overcoming the institutional gaps, ensuring effective coordination among key actors (AAUD, MiAmbiente, MINSA, and local governments), and maintaining a firm commitment to environmental standards during the construction and operation of new facilities. The consolidation of this model will directly benefit the urban population, improve public health indicators, and significantly contribute to the country's climate goals by reducing greenhouse gas emissions.

3.13 **Together, these priority reforms reinforce the pillars of the country strategy and address critical bottlenecks for Panama's development.** Their coordinated implementation will be key for achieving the expected outcomes: a more equitable and better protected society; a growing, carbon-neutral economy; resilient productive sectors; and more sustainable urban environments. The IDB will support the country in this effort, providing financing and technical assistance and facilitating coordination among actors with a view to ensuring that these transformations translate into tangible benefits for the Panamanian population and sustainable long-term progress.

86 Law 276 of 30 December 2021 regulates comprehensive management of solid waste in the Republic of Panama. The CDC highlights advances, such as the implementation of Law 33 of 30 March 2018, which established the Zero Trash Policy and its framework for comprehensive waste action, as well as the action framework for comprehensive waste management. In addition, the Centro de Economía Circular de Panamá (Panama Circular Economy Center) was established (Panama's updated Nationally Determined Contribution (NDC), 2020). However, there is a need to establish that companies are fully responsible for their products during their entire life cycle and support MSMEs in the management of materials from extraction to postconsumption.

D. ALIGNMENT WITH THE IDB GROUP'S REGIONAL FLAGSHIP PROGRAMS ("AMÉRICA EN EL CENTRO")

3.14 **The IDB Group Country Strategy with Panama 2025-2029 is fully aligned with the Bank's regional program "América en el Centro,"** which is aimed at promoting sustainable, inclusive, and resilient development in Central America. The strategic priorities identified for Panama are directly linked to the three regional pillars of "América en el Centro": (i) productivity and economic integration through logistics modernization, digitalization, financial innovation, and fostering of regional commerce; (ii) climate sustainability and resilience, with an emphasis on climate adaptation, sustainable watershed management, and energy transition; and (iii) social inclusion, strengthening equitable access to basic health care services, comprehensive social protection, and financial inclusion for the most vulnerable population groups. This clear alignment will enable Panama to leverage regional synergies, exchange knowledge, and facilitate the mobilization of regional and external resources to fulfill its strategic objectives effectively.

E. STRATEGIC PARTNERSHIPS

3.15 **The IDB Group will continue to work in coordination with other development actors.** This will be done in three different ways: (i) identifying opportunities to leverage more resources through cofinancing or parallel financing; (ii) creating greater opportunities for technical assistance and knowledge generation in collaboration with actors with experience and a track record in key issues under this country strategy; and (iii) solidifying coordination with civil society stakeholders to maximize the scope of action of the IDB Group in the country. The Bank has the largest presence of any multilateral organization in Panama and will concentrate on promoting partnerships in accordance with the three priority areas identified in this strategy.

3.16 **Capital mobilization (financial partnerships).** The IDB Group will lead the creation of innovative investment vehicles and cofinancing arrangements aimed at mobilizing additional resources for Panama. By designing and piloting new financial instruments (such as blended financing platforms, public-private partnership frameworks, or social, sustainable, green, or blue bonds), the Bank will set precedents that other sources of financing can follow. This effort will focus on the country's considerable investment needs in strategic sectors such as transport infrastructure, water and sanitation, and energy. In collaboration with other multilateral, international, and domestic institutions and with IDB Invest, the IDB will seek to attract private investment to cover financing gaps in these priority sectors, ensuring that large-scale projects have the required capital. At the same time, IDB Lab will seek to strengthen local entrepreneurship support organizations and attract international innovation ecosystem and venture capital industry players.

3.17 **Knowledge and technical assistance (technical partnerships).** The IDB Group will deepen its collaboration with specialized partners to support the reform agenda and institutionally strengthen Panama. Key initiatives include a joint public finance review with the World Bank, aimed at assessing fiscal performance and identifying areas for efficiency improvement. In addition, studies on subsidy programs will be conducted to explore possible reforms aimed at improving targeting and fiscal sustainability. In coordination with the IMF, the Bank will analyze fiscal adjustment scenarios to guide prudent management of public debt and expenditure. At the same time, it will work with the Organisation for Economic Co-operation and Development (OECD) to support Panama, through technical assistance on tax transparency and money laundering prevention, in complying with international fiscal transparency standards, an important step toward resolving the issue of the country's inclusion on black or grey lists. These knowledge partnerships will provide the government with evidence-based recommendations, directly supporting policy actions aligned with the country's strategic pillars.

3.18 **Coordination with civil society (alignment with the strategic pillars).** The IDB Group will strengthen coordination with civil society and other relevant actors to maximize the impact, and ensure the sustainability, of its interventions. This includes working closely with nongovernmental organizations, community groups, academia, and the private sector to align development projects with local needs and foster broad support for the proposed reforms. Ongoing dialogue and collaboration with these actors will make it possible to include citizen feedback and strengthen social inclusion in all initiatives. By involving civil society in implementation and monitoring, the Bank ensures that its financial and technical efforts translate into concrete outcomes that help to advance Panama's three strategic pillars. The initiatives in which the Bank participates include the Think Tank for Education, which calls on all sectors of society to set clear priorities, promote specific solutions, and constantly monitor progress in the education sector. The Think Tank for Education is a permanent forum where students, parents, teachers, entrepreneurs, academics, teachers' unions, and civil society organizations converge to continuously monitor, promote, and support educational change.

IV. CONSIDERATIONS FOR IMPLEMENTATION AND CAPACITY-BUILDING

A. KNOWLEDGE GENERATION AND USE

4.1 **The IDB Group will prioritize the generation and systematic use of knowledge as an essential tool for evidence-based decision-making.** The experience of the IDB Group in Panama reflects knowledge generation achieved by promoting the preparation and dissemination of analytical studies, assessments, and specialized technical assistance in key areas such as: (i) digital transformation; (ii) climate resilience; (iii) social inclusion; and (iv) institutional strengthening. These activities will be carried out in close collaboration with domestic and international stakeholders, including universities, research centers, business associations, and labor unions. Furthermore, the IDB Group will strengthen local institutional capacity to ensure that the knowledge generated is appropriated effectively by the country's institutions. In addition to the central role played by the knowledge agenda in the diagnostic assessment of development challenges and in the design of this strategy, knowledge will be a key input in adapting and prioritizing interventions. Along with strengthening institutional capacity and informing the monitoring and evaluation system, the learning cycle will enable adjusting programmatic decisions on the basis of evidence generated in the field, thereby consolidating knowledge as a driver of the theory of change. The strategy will leverage prior experience and promote the dissemination of best practices at the regional and sector levels, ensuring continuous learning and ongoing dialogue on evidence-based public policies.

B. MONITORING AND EVALUATION CAPACITY

4.2 **The duties and responsibilities of the monitoring and evaluation systems are focused on the fiscal sphere and are mainly distributed across different areas of the MEF.** These areas notably include the Dirección de Presupuesto de la Nación (National Budget Directorate) (DIPRENA), responsible for preparing and managing the budget; the Dirección de Programación de Inversiones (Investment Planning Directorate) (DPI), in charge of public investment;[88] the Dirección de Políticas Públicas (Public Policy Directorate) (DPP), which together with DIPRENA monitors the evolution of public finance; and the Territorial Development Directorate (DDT), which provides territorial information for the decision-making process. The monitoring and evaluation system is fragmented and encompasses various additional initiatives and legal frameworks. These include: the Consejo de

[88] Which manages it through the National Public Investment System (SINIP) pursuant to Executive Decree 148 of 11 December 2001, under which the SINIP was created; MEF Resolution 779, which sets out the objectives of the Investment Planning Directorate as well as its structure and responsibilities; and the Fiscal Social Responsibility Law (LRSF).

la Concertación Nacional para el Desarrollo (Council on National Consensus for Development), which creates an avenue for dialogue where different sectors seek consensus on national goals;[89] the Secretaría de Metas Presidenciales (Secretariat of Presidential Goals)[90] which reports to the Ministry of the Presidency and is responsible for monitoring government priorities; and the Office of the Comptroller General of the Republic (CGR), which is the highest State oversight body. In addition, the MEF receives physical and budgetary progress reports from all governmental entities, some of which have their own monitoring systems. Duplication of responsibilities and lack of effective coordination among these entities curtail the system's efficiency.

4.3 **There is a significant opportunity to optimize Panama's monitoring and evaluation system by taking advantage of the current legal framework, maximizing the initiatives underway, and addressing the fragmentation and lack of coordination challenges.** Under the leadership of the MEF and with the collaboration of various key actors, it is possible to strengthen the monitoring and evaluation system and coordinate it with the planning and budget systems to improve decision-making and public management. Promising initiatives include implementation of **results-based budgeting** at 33 entities and promotion of the Smart Fiscal Ecosystem, with IDB support, to enhance data-based decision-making. In addition, the financial platform **ISTMO** is modernizing budget and accounting management by means of integrated technology. Despite these advances, the aforementioned initiatives operate in partial fashion and are not fully integrated with the planning and monitoring processes. This lack of integration creates a decoupling that weakens the public policy cycle and erodes the capacity for policy feedback. Furthermore, monitoring information is fragmented and manual, which prevents it from being used effectively in decision-making. The absence of formal mechanisms for consolidating and using this information is one of the system's major weaknesses. There is no single government entity responsible for assessments, and progress in this area has been limited.

4.4 **To address these gaps, the country strategy will support strengthening Panama's monitoring and evaluation capacity in line with the diagnostic assessment set out in the strategy's monitoring and evaluation annex.** In coordination with the government, the Bank will work on **three priority lines of action**: **(i)** establish formal mechanisms for coordination and governance of the monitoring and evaluation system, integrating its various components and linking it with the planning and budget processes; **(ii)** modernize and coordinate the institutions and information systems responsible for generating accurate, timely, and consistent data to facilitate decision-making; and **(iii)** strengthen institutional capacity and that of the staff responsible for monitoring and evaluation in public entities. In the short term, the Bank will provide technical assistance to create effective coordination mechanisms and reinforce existing bodies such as the **Secretariat of Presidential Goals**, the MEF's **Expenditure Management and Quality Unit**, and the CGR's INEC. In addition, the Bank's knowledge in emerging technologies (such as **microdata analytics and artificial intelligence**) will be leveraged to improve the public investment and expenditure monitoring platforms,

[89] Law 20 of 25 February 2008, approving the Mechanism for Verification and Monitoring of Agreements and Goals of the Council on National Consensus for Development, is aimed at creating a mechanism to verify and monitor such agreements and goals.

[90] Reestablished under Executive Decree 485 of 16 August 2024.

contributing to more efficient public management. In the medium term, these actions will lay the groundwork for implementing an integrated **planning-budget-monitoring-evaluation** framework to enable a better-coordinated implementation of policies and a more effective allocation of resources, while at the same time boosting the production of relevant, timely, reliable, and accessible official statistics.

4.5 **Fulfillment of the country strategy's objectives will be monitored through the Results Matrix (Annex I), which lists indicators, baselines, and targets associated with each strategic priority.** The Bank will continuously monitor these indicators in coordination with local authorities, issuing periodic progress reports. In addition, it will conduct a **midterm review** of the strategy, allowing adjustments to be made if needed to ensure attainment of the established goals. At the end of the strategy period, a rigorous **ex post evaluation** will be conducted with Office of Evaluation and Oversight (OVE) support to measure the results achieved, extract lessons learned, and report on the IDB Group's contribution to the development of Panama. These monitoring and evaluation efforts, both at the national level and under the strategy, will ensure that the Bank's interventions follow a **vertical logic**: the lessons learned will inform the decision-making and planning of new operations, thereby closing the virtuous cycle between evaluation and results-based management.

C. COUNTRY FIDUCIARY SYSTEMS

4.6 **During the strategy period, the Bank will continue to engage in dialogue with the government and support it through financial management, external control, and procurement initiatives.** In terms of financial management, the Bank will focus on: (i) supporting implementation of the action plan arising from the diagnostic assessment of gaps with International Public Sector Accounting Standards (IPSAS) and aimed at advancing toward full IPSAS implementation by the end of the strategy period; (ii) providing assistance and support in generating financial reports as required by the multilateral banks and bilateral lending institutions through the ISTMO system, the result of which will be reflected in an increase in the use of the country accounting and reports subsystem; (iii) providing IPSAS training and certification to National Accounting Directorate (DNC) officials / technical experts involved in the implementation of IPSAS; and (iv) participating in knowledge transfer events organized by domestic or regional networks (FOCAL, CreCER, and others). In the external control pillar, the Bank will: (i) provide IPSAS training and certification to CGR officials / technical experts involved in the implementation of IPSAS; and (ii) participate in knowledge transfer events organized by domestic or regional networks (OLACEF, CreCER, and others). In terms of procurement, the Bank will support the Dirección General de Contrataciones Públicas (Public Procurement Office) (DGCP) in implementing the action plan arising from the MAPS diagnostic assessment aimed at closing gaps with respect to international best practices, in the following lines of action: (i) moving forward on the implementation of version 3.0 of the PanamaCompra portal; (ii) providing technical support in relation to the contract management module to make contract performance information available to civil society; (iii) providing technical support for interconnecting the PanamaCompra portal with the financial administration system (ISTMO); (iv) providing technical support to promote greater civil society participation in the various stages of the public procurement process. In addition, with a view to boosting the use of country procurement systems in Bank-financed operations, the IDB's Guide for Acceptance of the Use of Country Procurement Systems will be applied, generating an improvement proposal if applicable. Lastly, to enhance the operational efficiency of the IDB portfolio, the Bank will work with the DGCP on standardizing bidding documents for national competitive bidding and shopping processes.

D. EMERGENCY RESPONSE

4.7 **The pillars of the 2025-2029 country strategy take emergency preparedness and response into account regarding natural and health-related disasters, with a view to contributing to the country's long-term resilience.**

4.8 **Access to basic services for vulnerable population segments.** The first pillar is centered on delivering and providing equitable access to quality basic services with the aim of reducing territorial inequality. In this regard, improving the quality of life of those who face barriers to accessing essential services in areas such as health, water, sanitation, electricity, and basic infrastructure will help to reduce their vulnerability to diseases and hazards associated with natural phenomena. In addition, expanding the coverage of the National Registry of Beneficiaries (RENAB) and better targeting conditional cash transfer programs will allow these programs to have a more effective reach and faster response time, helping to strengthen population segments living in poverty, extreme poverty, and vulnerability. Furthermore, the financial inclusion of microenterprise and small business owners will enable small businesses to participate more actively in the economy, helping them to generate greater economic, social, and climate resilience.

4.9 **Strengthening of public management and fiscal sustainability.** The second pillar is centered on optimizing public expenditure, strengthening investment, and boosting administrative efficiency, thereby promoting fiscal sustainability. It also addresses the need to reinforce fiscal financing and risk management strategies to ensure macroeconomic stability and reduce vulnerability to external shocks. Promoting efficient management of the public debt will make it possible to consolidate medium-term financial strategies, diversifying sources and maturities to preserve the fiscal space needed for strategic investments in development and natural disaster prevention. With proper planning, Panama can strengthen its emergency response capacity and ensure stable and resilient economic growth. In addition, interventions under this pillar will promote the use of ex ante financial arrangements, such as contingent credit lines and the inclusion of a deferred principal payment option in eligible loans. Furthermore, institutional strengthening will be promoted through the use of tools such as the Index of Governance and Public Policy in Disaster Risk Management (iGOPP), which can identify key regulatory and coordination gaps to improve disaster preparedness. Together, these tools will help to consolidate the national planning and response capacity while protecting the fiscal space upon the occurrence of extreme natural events.

4.10 **Boosting sustainable growth through the private sector and the use of strategic assets.** The third pillar promotes a diversified, competitive, and environmentally sustainable economic growth model, with the private sector as the main driver of development, in several ways. In the first place, strengthening the resilience of the country's watersheds, including the Panama Canal watershed, will help to reduce the risks associated with water scarcity in the Canal, improve the availability of water resources, and progressively diminish the vulnerabilities related to extreme climate events. In addition, improving the management effectiveness of the targeted protected areas will help to enhance the resilience of the watersheds. In the second place, modernizing the logistics infrastructure under climate and environmental criteria will help to deepen the country's trade integration, while supporting the development of emerging sectors—such as sustainable tourism, innovative agroindustry, and the digital economy—will help to partially mitigate risks derived from economic concentration, creating greater resilience to external events in general. In the third place, implementing innovative financial mechanisms will pave the way for mobilizing more resources toward key environmental initiatives and will propitiate the development of a climate finance market.

E. RISK ASSESSMENT

4.11 The **IDB Group's country strategy with Panama** recognizes the existence of various risks that could affect its implementation. Below is a description of the most significant risks and the respective mitigation measures.

MACROECONOMIC AND FISCAL RISKS

4.12 **Risk:** Panama faces pressures stemming from a persistent deficit and a growing public debt. This situation could compromise the country's fiscal sustainability and translate into a credit rating downgrade. A potential downgrade of the country's credit rating could in turn elevate the perceived risk to the returns on private investment, raise the financing cost for businesses, and possibly increase the level of nonperformance of financial commitments on the part of bank clients of IDB Invest (default) and their need to recognize additional loan loss provisions.

4.13 **Mitigation measures:** The government has reaffirmed its commitment to fiscal discipline by implementing the Fiscal Social Responsibility Law (LRSF),[91] strengthening revenue and expenditure management, and maintaining prudent macroeconomic policies to preserve financial stability and investor confidence. In this regard, it will be essential to provide continuous monitoring and support to the authorities and IDB Invest clients.

SOCIAL AND ENVIRONMENTAL RISKS

4.14 **Risks:** Implementing this strategy entails risks in the form of adverse environmental impacts (such as deforestation or pollution) and potential conflicts with local communities. Projects lacking proper environmental and social management can face community opposition and significant delays, and may even affect the rights of vulnerable population groups.

4.15 **Mitigation measures:** Strict environmental and social policies will be implemented in line with international standards,[92] (i) ensuring citizen participation (such as under the Escazú Agreement),[93] (ii) establishing rigorous environmental management plans, and (iii) expanding the mechanisms for environmental supervision. In addition, (iv) the Bank will promote early dialogue with the

[91] The LRSF was amended under Law 445 of 28 October 2024 with a view to strengthening public finance.

[92] IDB Environmental and Social Policy Framework and IDB Invest Environmental and Social Sustainability Policy.

[93] Regional Agreement on Access to Information, Public Participation, and Justice in Environmental Matters in Latin America and the Caribbean. Escazú, March 2018.

communities and close environmental supervision in projects to prevent conflicts and ensure the sustainability of the interventions as well as (v) identify the need to support adjustments and the implementation of social and environmental mitigation measures that benefit the vulnerable population.

CLIMATE AND DISASTER RISKS

4.16 **Risks:** Panama is highly vulnerable to extreme events such as floods, droughts, and landslides,[94] which could gradually become more severe.[95] These events could disrupt projects, damage critical infrastructure, including the Panama Canal, and adversely affect the population.

4.17 **Mitigation measures:** To reinforce resilience, the country is implementing its National Policy for Comprehensive Disaster Risk Management 2022-2030,[96] and has presented the following instruments to the United Nations Framework Convention on Climate Change (UNFCCC): (i) its long-term strategy, titled National Inclusive, Low Emissions, and Climate Change Resilient Socioeconomic Development Strategy, which is Panama's roadmap for fulfilling its commitment as a signatory to the Paris Agreement; and (ii) its second nationally determined contribution (NDC2), which is based on an integrated adaptation and mitigation approach under climate justice and equity principles and common but differentiated responsibilities, while also incorporating nature-based solutions. The government has included climate risk in environmental impact studies and has developed the Climate Risk Atlas,[97] which is a tool for mapping climate change hazards, vulnerability, exposure, and risks. The Climate Risk Atlas will inform land-use planning policies with an emphasis on natural capital and water protection and will contribute to the design and construction of resilient infrastructure, helping to ensure the operational continuity of investments in the face of extreme events. The IDB will continue to support Panama in strengthening disaster risk management by means of innovative products and services aimed at emergency preparedness and response. It will also continue to assess climate and disaster risks in its operations, ensuring that the risk analysis guides mitigation strategies and adaptation measures. IDB Invest will analyze the climate risks associated with its transactions as a basis for making investments in adaptation, including through the use of specific tools. In addition, it will provide technical assistance to potential investors in the form of information on potential environmental risks; will increase market awareness of this issue to complement the aforementioned national policies; and will boost value chain resilience, with an emphasis on suppliers. Lastly, IDB Invest will work with its clients in designing strategies to protect them from the effects of extreme climate events.

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[94] Located along the Pacific Ring of Fire, Panama is also exposed to seismic risks, landslides, and volcanic risks.

[95] According to the ND Gain index, Panama is ranked 94th in vulnerability to climate change and 108th in readiness to improve resilience. The ND Gain index assesses a country's susceptibility to climate change and its adaptation capacity. Vulnerability measures the likelihood of being adversely affected by climate risks, while readiness measures a country's ability to leverage investments in adaptation measures. This assessment shows a country's position out of more than 180 countries. A vulnerability position close to 1 indicates a higher likelihood of adverse impacts stemming from climate risks, while a readiness position close to 1 reflects a greater ability to leverage investments in climate adaptation effectively.

[96] Política Nacional de Gestión Integral del Riesgo de Desastres en Panamá 2022-2030 (National Policy on Comprehensive Disaster Risk Management in Panama 2022-2030).

[97] https://atlasderiesgoclimatico.miambiente.gob.pa/atlas.

INSTITUTIONAL AND EXECUTION RISKS

4.18 **Risks:** There are risks associated with institutional management capacity that could delay implementation of the strategy. They are posed by administrative and bureaucratic delays in key procedures, unclear roles in institutions, limited technical capacity in some executing agencies, and potential political changes that would alter the development priorities. Gaps in corporate governance of private sector actors could affect proper implementation of projects and adequate risk management.

4.19 **Mitigation measures:** The country strategy supports institutional strengthening and operational efficiency, fostering (i) greater interagency coordination and collaboration (including with the CGR to streamline validation procedures); (ii) simplification of administrative processes to make them more efficient; (iii) technical training for executing agency staff in issues of public management of investment projects; and (iv) planning, allocation, and timely management of resources at the project level. In addition, (v) the IDB Group will maintain an ongoing dialogue with the authorities to ensure that the members of execution teams have the requisite profile, experience, and skills, and that their continuity is ensured to provide project execution stability in the event of government transitions. On the private sector side, it will be essential to strengthen the corporate governance of companies, as well as their capabilities and controls to identify and mitigate financial and nonfinancial risks, including integrity and reputational risks.

ANNEX I – RESULTS MATRIX

Government priority	Strategic area	Strategic objective	Expected impact	Indicator	Baseline	Source
Equitable opportunities for all through relevant education and quality basic services	Access to basic services for vulnerable populations	Promote equity through the delivery of basic services	Expand enrollment in the social registry	Percentage of the Panamanian population enrolled in the RSU (%)	2024 Available in June 2025	Social protection project data. MIDES - RENAB
			Improve water and sanitation service access and quality	Households with new or improved access to water and/or sanitation services (#)	2023 77.4%	2023 census
			Improve access to electricity in rural areas	Electricity coverage in rural areas	2023 Available in June 2025	2023 census
			Support the social inclusion of persons with disabilities	Proportion of persons with disabilities certified as such under the ICF framework nationwide (%)	2024 Available in June 2025	Social protection project data. MIDES - RENAB
			Improve access to essential health services in lagging rural and indigenous communities	Percentage of the population in rural areas and indigenous comarcas benefiting from the strategy of expanding primary health care coverage	2025 0.25	Registry of population benefiting from the coverage expansion strategy (MINSA)
		Promote financial inclusion	Increase the financing provided to micro, small, and medium-sized enterprises (MSMEs)	Number of MSMEs financed (#)	2024 6,500	Banco Nacional de Panamá (BNP)
Efficient governance and institutional strengthening	Strengthening of public management and fiscal sustainability	Strengthen public finance and the sustainability of the pension system	Reduce tax noncompliance	Tax revenue / GDP (%)	2024 7%	MEF, CGR
			Boost collection of social security contributions	Revenue from regular contributions to the CSS (US$ billions)	2023 US$3.490 billion	CSS, CGR
			Boost expenditure efficiency by implementing the Smart Fiscal Ecosystem	Leakages in three major transfer programs: Red de Oportunidades (Opportunities Network), 120 a los 65 (120/65), Ángel Guardián (Guardian Angel)	2024 Available in June 2025	MEF, MIDES

Government priority	Strategic area	Strategic objective	Expected impact	Indicator	Baseline	Source
		Boost the efficiency of the public administration and the ease of doing business	Strengthen the digitalization of governmental procedures	Digitized governmental procedures (#)	2024 764	ICS project data / INEC
Strengthening of economic sectors for growth and quality job creation; environmental sustainability and responsible management of natural resources	Promote sustainable growth through the private sector and the use of strategic assets	Reinforce watershed resilience, including the Panama Canal watershed (watershed management)	Mitigate flood risk	New households protected against flood risks in the area of influence of the works financed through the program (#)	0	TSP / WSA project data
			Watersheds vulnerable to climate change that have developed adaptation strategies	Number of vulnerable watersheds that have developed adaptive planning of resources and territory (#)	0	ACP, MiAmbiente
			Improve water efficiency and conservation	Volume of water produced in water treatment plants	0	Project data (IDB Invest and WSA)
		Support strategic investments in key infrastructure and areas that foster trade	Improve the performance of the logistics sector and the urban transport sector	Panama's place on the Logistics Performance Index (#)	2023 57 out of 139, 3.1	World Bank
				Proportion of electric buses in the public transport fleet (%)	0%	TSP project data – MiBus reports
			Deepen economic integration, boosting international trade flows in goods and services	International trade promoted by IDB Invest (US$ millions)	2023 US$168.2 million	Development Effectiveness Matrix – IDB Invest
		Protect the natural and cultural capital and expand climate finance	Enhance management effectiveness in targeted protected areas	Visitors registered in protected areas (#)		Tourism project data
				Tourism revenue (US$ millions)	2024 US$6.0002 billion	ATP
			Increase the climate finance amount mobilized by the IDB Group	Climate finance provided under IDB Group operations (US$ millions)	2023 US$392.6 million	IDB Group climate finance data

ANNEX II – PORTFOLIO ALIGNMENT AND INDICATIVE PROGRAM 2025 - 2026[98]

Priority area	Strategic objective	Portfolio alignment	Indicative program 2025-2026
Access to basic services for vulnerable populations	Promote equity through the delivery of basic services	PN-L1072 PN-L1105 PN-L1115 PN-L1143 PN-L1155 PN-L1160 PN-L1170 PN-J0001 PN-L1177 PN-L1109 PN-L1121 IDB Invest: 14421-01, 13325-01, 13325-02, 13960-01	PN-L1189 “Water and Sanitation Program in Rural Communities in the Panama Canal Watershed” PN-LXXXX “Program to Support Efficiency and Equity in Panama’s Health Care System” PN-LXXXX “Universal Energy Access Program in Panama”
	Promote financial inclusion	PN-L1179 PN-L1174 IDB Invest: 11880-02, 12577-02, 13316-01, 12412-01, PN-L1030	
Strengthening of public management and fiscal sustainability	Strengthen public finance and pension system sustainability	PN-L1161 PN-L1172	PN-L1193 “Program for the Improvement of the Social Security Fund Pension System in Panama”
	Boost the efficiency of public administration and the ease of doing business	PN-L1148 PN-L1171 PN-L1180	PN-L1192 “Program for Institutional Transformation of the Office of the Comptroller General of Panama”

[98] Operations subject to formal validation by the Ministry of Economy and Finance as part of the programming dialogue with the Bank.

Promote sustainable growth through the private sector and the use of strategic assets	Strengthen the resilience of the Panama Canal (watershed management)	PN-L1150 PN-L1166	PN-U0001 “Development of Financial Solutions to Increase Access to Basic Services”
	Support strategic investments in key infrastructure and areas that promote commerce	PN-L1107 PN-L1153 PN-L1183 PN-L1185 IDB Invest: 12174-03, 12282-01, 14992-01, 12572-01, 13103-01, 13623-01, PN-L1027, PN-L1032, PN-L1065 PN-X1009	PN-L1190 “Program to Support a Fair, Clean, and Sustainable Energy Transition II”
	Protect the natural and cultural capital and expand climate finance	PN-L1146 PN-L1154 IDB Invest: 14095-01, 14505-01	PN-L1187 “Program to Strengthen Competitiveness and Improve the Sustainability, Inclusivity, and Resilience of the Panamanian Tourism Sector II”

Source: Prepared by the authors.

ANNEX III – DEVELOPMENT EFFECTIVENESS MATRIX

COUNTRY STRATEGY: DEVELOPMENT EFFECTIVENESS MATRIX

In August 2008, the Board of Executive Directors approved the Development Effectiveness Framework (GN-2489) to increase the evaluability of all Bank development products.

The Development Effectiveness Matrix for Country Strategies (DEM-CS) is a checklist of the elements for evaluating a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation" document.

COUNTRY STRATEGY: PANAMA

STRATEGIC ALIGNMENT

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

EFFECTIVENESS

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

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

* This analysis includes any potential diagnostic document used and prepared to inform.

** The Results Matrix is composed by indicators that are meaningful to, and capture progress towards, the expected results. The expected results stem from the strategic objectives.

ANNEX IV – COUNTRY SYSTEMS MATRIX

Strategic objective	Expected result during the country strategy period	Indicator	Unit of measure	Baseline	Base year	Main target	Period	Alignment with the Corporate Results Framework
Increase the use of country systems	Increased use of the ISTMO accounting and reports subsystem	Active portfolio using the accounting and reports subsystem	Percentage of the active portfolio	0%	2025	90%	End of country strategy period	Access to basic services for vulnerable population groups; strengthening public management and fiscal sustainability; and sustainable growth driven by the private sector and the harnessing of strategic assets
	Increased use of the individual consulting subsystem	Active portfolio using the individual consulting subsystem	Percentage of the active portfolio	0%	2025	20%	End of country strategy period	
	Increased use of the partial national competitive bidding (NCB) subsystem	Active portfolio using the partial NCB subsystem	Percentage of the active portfolio	0%	2025	20%	End of country strategy period	
Strengthen country systems	Closure of gaps with IPSAS	Progress in implementing the action plan arising from the diagnostic assessment of gaps with IPSAS	Percentage progress on the IPSAS implementation plan	0%	2025	50%	End of country strategy period	
	Closure of gaps in Panama's public procurement system with respect to international best practices	Progress in implementing the action plan arising from the MAPS diagnostic assessment	Number of action lines to be supported	0	2025	4	End of country strategy period	
Improve the operational efficiency of the IDB portfolio	Standardization of NCB and shopping documents	NCB and shopping documents standardized with the DGCP	Number of documents	0	2025	2	End of country strategy period	

ANNEX V – ESTIMATED LENDING FRAMEWORK

The sovereign guaranteed lending framework provides for approvals of US$1.5 to US$2.5 billion between 2025 and 2029, determined on the basis of the country's financing needs, strategic dialogue with the authorities, and operational dialogue the sectors hold with sector-specific institutions in the country. The IDB Group will continue to provide technical support in the strategic areas and explore resource leveraging opportunities with strategic partners and synergies with the private sector. These resources will be added to the IDB Invest and IDB Lab approval amounts for Panama, which totaled US$930 million during the 2021-2024 strategy period. In addition to positioning the Bank as a strategic partner in terms of technical support and knowledge generation for the country, the expected approvals and respective disbursements should allow the Bank to maintain a share of 6% to 7% of the country's total debt and 7% to 9% of its total external debt.

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US$ millions	2021-2024 strategy					2025-2029 strategy											
	2021	2022	2023	2024	Total	2025		2026		2027		2028		2029		Total	
						Min.	Max.	Min.	Max.	Min.	Max.	Min.	Max.	Min.	Max.	Min.	Max.
Approvals	521	390	425	320	1,656	300	500	300	500	300	500	300	500	300	500	1,500	2,500
Disbursements	608	388	321	157	1,473	300	600	300	600	300	600	300	600	300	600	1,500	3,000
Principal repayment	232	250	337	382	1,201	440	440	448	448	439	439	387	387	387	387	2,099	2,099
Net capital flows	**377**	**138**	**-16**	**-226**	**272**	**-140**	**160**	**-148**	**152**	**-139**	**161**	**-87**	**214**	**-87**	**214**	-599	901
Subscriptions and contributions	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Interest and fees	79	109	255	278	720	213	213	216	216	198	198	180	180	161	161	968	968
Net cash flow	**298**	**29**	**-272**	**-503**	**-448**	**-353**	**-53**	**-364**	**-64**	**-336**	**-36**	**-266**	**34**	**-247**	**53**	**-1,567**	**-67**

	2021	2022	2023	2024	2025	2026	2027	2028	2029
IDB debt	4,254	4,391	4,375	4,150	4,102	4,054	4,016	4,029	4,043
Multilateral debt	8,879	9,379	9,374	9,550	9,999	10,414	10,754	11,053	11,424
External debt	32,844	36,853	39,988	44,276	46,401	48,960	51,454	53,889	56,370
Total debt	40,488	44,274	47,025	53,737	57,204	59,809	61,669	63,680	65,886
IDB debt / Multilateral debt (%)	48%	47%	47%	43%	41%	39%	37%	36%	35%
IDB debt / External debt (%)	13%	12%	11%	9%	9%	8%	8%	7%	7%
IDB debt / Total debt (%)	11%	10%	9%	8%	7%	7%	7%	6%	6%

Source: FINSOL, MEF, and authors' calculations based on IMF and MEF data.