

CHAPTER I: GENERAL INFORMATION

1. Geography and Climate

The Republic of Panama is located between the Republic of Costa Rica and the Republic of Colombia, in the isthmus connecting Central and South America. It borders to the East with the Republic of Colombia and to the West with the Republic of Costa Rica, to the North with the Caribbean and to the South with the Pacific Ocean. The Panama Canal crosses the Republic from North to South, at the Isthmus narrowest point.

The country has an approximate area of 30,000 square miles (77,083 square kilometers), and is subdivided politically in nine Provinces (Bocas del Toro, Coclé, Colón, Chiriquí, Darién, Herrera, Los Santos, Panamá and Veraguas) and two Special Administrative Regions (Kuna Yala, Ngöbe Buglé, Emberá-Wounaan, Madugandí, and Wargandí).

It has a tropical climate throughout the year with two seasons: the dry season, which runs from January to April and the rainy season that continues from May to December. The average daily temperature is 27°C (81°F) in the lowlands, and 18°C (64°F) in the highlands. The relative humidity varies from a low 52% in March to a high of 98% in October. The average yearly rainfall during the rainy season is approximately 3,270 millimeters (128.74 inches) on the Atlantic (Caribbean) side of the isthmus and 1,750 millimeters (68.70 inches) on the Pacific side, with little or no rain during the dry season.

2. History and Government

The Isthmus of Panama was discovered by Rodrigo de Bastidas in 1501. In 1513, Vasco Núñez de Balboa launched from Panama the expedition that discovered the Pacific Ocean.

Panama was valued as a commercial route from Peru to Spain until 1671, when the main city of the route in the Pacific side was destroyed by fire during a raid of the pirate Henry Morgan. Panama remained as a Spanish colony until 1821, when it became independent of Spain and joined Colombia. In November 1903, after several attempts to achieve emancipation, Panama broke its alliance with Colombia to become a fully independent Republic.

The Republic of Panama possesses a democratic system of government divided into three separated branches, the Executive, the Legislative and the Judiciary. The Executive Power is exercised by the President and the two Vice Presidents, who are elected for a five-year term and cannot be reelected for the same post in the following term. Election is by direct popular vote. The Legislative Branch is unicameral and is actually composed of 71 Senators, elected by direct popular vote, and responsible for passing laws. The Judiciary Branch is composed of the Supreme Court, Superior District Courts and other lower courts established by law. Supreme Court Justices are appointed by the Executive Branch, subject to the confirmation of the Legislative Branch. Government participation in economic activities is limited to those areas where private capital is not available or investment is non profitable.

The Panamanian legal system is assembled along axes of formal sources derived from the Political Constitution as the main doctrine stream, flowing throughout the framework of the State. Subordinately are the Republic's statutes, organic or regular in character, followed by decree-laws and Cabinet decrees. Thereafter, rank all Executive decrees, regulations, ordinances and resolutions publicizing decisions (administrative or

judicial). Treaties and international agreements rank alongside the laws.

The Panamanian system is informed by a notion of legality, which suggests that all acts exercising the authority of the State should be grounded in previously enacted legal norms. This is to say that public officials cannot execute acts not expressly authorized by the Law.

In contrast, private parties are governed by their autonomous will and endowed with contractual freedom; they can do what the Law does not expressly forbid.

3. Population, Cities and Languages

With an estimated population of approximately 2,845,647 (2001 est.), and as a real World crossroads, Panama is a multicultural hub, where different human groups interact harmoniously.

The City of Panama is the most important, with about one million two hundred thousand habitants. This high concentration of population places considerable strain on housing, educational and public services on this metropolitan area.

Colon, the second most important city, is located on the Atlantic Coast, and is the site of the Colon Free Zone. The Colon Free Zone is a center of international free trade, considered the principal trading area in the Western Hemisphere due to its trade volume and value.

David, the third largest city in Panama, located in the westernmost area of the country, has a strong agricultural, cattle rising, industrial, and commercial economy.

Panama's official language is Spanish. However, English is widely spoken as a second language in the main cities, especially by the service sector located mainly in the cities of Panama and Colon. The majority of Panamanians are Roman Catholics; however, complete freedom of religion exists. Panama's educational level is higher than those of most Latin American countries. The illiteracy rate is less than eight percent. The government invests a significant portion of its capital budget in education.

4. Economy

Economic activities fall mainly on private parties. Panama's economy is heavily service-oriented, with more than 75 percent of the Gross National Product (GNP) and 50 percent of the country's employment results from this sector.

In 1991, the Gross National Product was US\$2,042.7 million. This represented a 9.3% growth compared to the previous year, and reflected the dynamic ability of the local market sectors to recover after the years of negative growth (1987-1989).

As of 2001, the Gross National Product (GNP) has been estimated at US\$7,365.2 million at 1982 prices (11,319 millions at 1996 prices).

The tendency in many Latin American countries to open their markets has favored re-exports from the Colon Free Zone.

The official monetary unit is the Balboa (B/. or PAB), which is at par value with the United States Dollar (US\$), as the currency that circulates freely and with convertibility in the country. The constitutionally mandated absence of officially issued paper currency accords the circulation of the US dollar, which holds immense importance for both local and international transactions.

Based primarily on private enterprise, the service sector, including banking and finance and the Panama Canal, makes up a very large portion of the country's Gross Domestic

Product. Principal exports, other than services, include agricultural and marine products (mainly bananas, coffee, sugar and shrimp), clothing articles and oil byproducts. Foreign investment, to which very little restrictions are applied, has traditionally been welcomed in the country and plays a very important role in several sections of the economy.

Considered a “tax haven” because of its territoriality concept, Panama has been able to attract a number of multi-national companies, banks, re-invoicing operations, light manufacturing companies, and other activities.

Since 1990, the government has initiated a series of privatizations. All state-owned companies dealing with agriculture, including sugar mills, have been sold or closed. Air Panama, the state-owned and operated airline was sold and later closed; Cemento Bayano, the state-owned cement plant was sold to CEMEX; the ports of Cristóbal and Balboa were placed under the administration of an international consortium; the international airport at Tocumen is being privatized via management contracts, as are the gambling operations, including casinos and horse racing; and 49% of INTEL, the state-owned telephone company, was sold in May, 1997 to the British consortium Cable & Wireless. The Electric Power Company (*Instituto de Recursos Hídricos y Electrificación-IRHE*) was also privatized. The administration of the railroad joining the cities of Panama and Colon was recently granted to Kansas City Railroad.

5. The Panama Canal

After the independence of Panama in 1903, this country and the United States executed a treaty to construct an inter oceanic navigation canal. Ten years later, the project was finished at a cost of US\$ 387 million. It opened for transit in 1914 and is still considered an engineering wonder.

Currently, total investments in the Canal amount to US\$ 3 billion. Since 1914, the Panama Canal had provided services to more than 725,000 vessels.

The 1977 Canal Treaty embarked Panama and the United States on a partnership for the management, operation, and defense of the Panama Canal. Consequently, the Panama Canal Commission, a U.S. Government agency, operated the canal until December 31st, 1999, when management was transferred to Panama.

The waterway is the largest employer in the country, after the National Government and its agencies. It takes a vessel an average of eight hours to travel from one ocean to the other, using 50,000,000 gallons of fresh water which are unloaded unto the oceans each time a vessel goes through. Approximately 14,000 ships transit the Canal annually, and this figure is projected to grow 2% annually over the next decade. The average toll paid is about US\$27,000.

6. Colon Free Zone

Located on the outskirts of the city of Colon, on the Atlantic side of the Isthmus and only fifty miles from Panama City, the Colon Free Zone offers an area where merchandise may be imported, modified, repacked and held until its final sale, on a duty free basis. Trade in the Zone must be carried out strictly on a wholesale basis. Because of its special income tax status and its convenient location, the Colon Free Zone is used by companies from all over the World as a Latin American warehousing center. Light manufacturing and some assembling are also carried out in the Free Zone area.

The Colon Free Zone offers a well-trained and experienced (usually bilingual) work force, ample facilities, government cooperation, and easy access to sea, railroad and air

transportation facilities.

Free Zone authorities shall approve the specifications of buildings within its area, and, according to needs, buildings or warehouses may be built or leased. Warehousing facilities administrated by the authorities of the Free Zone are also available for companies initiating activities in the area or for those companies with small or varying inventories, that do not justify owning or leasing a facility.

Tax laws, which apply to income generated in Panama, do not apply to Free Zone operations. As of January 1st, 1997, income generated by re-exporting activities is totally tax free. No taxes are levied on the export of capital, or the payment of dividends on earnings derived from re-exporting activities. However, and also after January 1st, 1997, Companies operating in this, or any other free zone, must put together financial statements in accordance with Panamanian legal standards, duly countersigned by a Panamanian Certified Public Accountant, and must file tax returns.

With Hong Kong, Japan and the United States of America being the principal suppliers, total annual trade in the Colon Free Zone exceeds US\$10 billion, which represents approximately 15% of GDP. South American countries are the biggest customers of this Free Zone. Companies wishing to establish operations in the Colon Free Zone must first obtain an operation permit from the Free Zone Administration, which is an autonomous entity of the Panamanian Government. No business license is required for companies operating in the Colon Free Zone.