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## Panama's Encouraging Shot at Progress

By [Juan Carlos Hidalgo](#)

Since good news is rarely "news," the presidential election in Panama this Sunday has been largely ignored in the U.S., and even in Latin America. However, given that Washington still has pending business with Panama over the approval of a free trade agreement that has been stuck in Congress since 2006, this election matters.

The opposition candidate, Ricardo Martinelli, has a comfortable lead over the incumbent party candidate, Balbina Herrera. Martinelli is expected to win and become Panama's fifth president since civilian constitutional government was restored in 1989. Panama now boasts sound democratic institutions and the political campaign has unfolded like in any other mature democracy. This is quite a change from the authoritarian rule of strongman Manuel Antonio Noriega twenty years ago.

The Panama economy has been humming along nicely. From 2003-2007 its GDP per capita (Power Purchasing Parity) increased at an annual rate of 6.8 percent, the highest in Latin America during this period, higher than Peru, another country that has significantly liberalized its economy in the last two decades. The expansion of the Panama Canal will likely further boost the economy. But Panama's growth has also been underpinned by the current government's efforts to liberalize trade and reduce barriers to conducting business.

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Martinelli has made some low-intensity populist promises, such as creating a cabinet ministry for indigenous people and granting pensions to every single senior citizen "□□" including those who haven't contributed to the social security system. But his platform incorporates many elements of sound economic policy, such as cutting and abolishing some taxes, continuing the efforts to cut red tape, unilateral dismantling of trade barriers, and getting rid of energy subsidies.

The most significant proposal, however, is the introduction of a flat tax which, if implemented, would make Panama the first country in the Americas to institute it. A flat tax would rid the country of the complexity of the current tax system, reduce incentives for tax avoidance and tax evasion, and boost its competitiveness.

The introduction of a flat tax in one Latin American country will likely trigger a domino effect in the region such as the one that took place in Eastern Europe after Estonia took the lead with this policy in 1994. A second flat tax revolution might thus be in the making in Panama, which is good news for Latin America where high tax rates and complex rules force large portions of the economy into the informal

sector.

Finally, Martinelli is a staunch supporter of the free trade agreement (FTA) with the U.S. that is stalled in Washington's Congress. Current president Martin Torrijos made the strategic mistake of going alone in pursuit of an FTA with the United States, instead of joining other Central American countries in DR-CAFTA. The negotiations took longer than expected and an agreement was reached shortly after Democrats took control of Congress in November 2006. It's been stuck there ever since.

Now that President Obama has finally realized that the U.S. cannot take its friends in the region for granted, the administration has hinted at approving the FTA with Panama. However, leading Democrats in Congress, not satisfied with their efforts to rewrite the environmental and labor legislation of the countries that the U.S. signed trade agreements with, are now objecting to Panama's tax laws, in particular its banking secrecy provisions. Its liberal banking laws have made Panama a financial powerhouse in Latin America. Martinelli should resist any pressure from Congressional Democrats to rewrite Panama's financial and tax legislation so as to undercut this strength in exchange for a FTA with the U.S.

The next five years represent a magnificent opportunity for Panama to position itself as the hub of the Americas. The Obama administration is well aware that growth and economic opportunities are the best antidotes to populism in Latin America. That is why Washington should welcome the election of Ricardo Martinelli with the approval of the FTA with Panama.

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