

Panama

Election into the last stretch

Panama is preparing for general elections on May 5. Although polls agree on likely outcomes, legal challenges to Mulino's candidacy cloud the electoral outlook heading into the last week of campaigning. We reiterate the next administration will need to embark on an ambitious agenda for growth and fiscal consolidation ahead.

- The country is heading towards general elections on May 5 where it will elect a president, 71 deputies and more than 700 local representatives. Polls show Mulino leading voter preferences while Congressional polling points toward higher fragmentation.
- The focus is on a potential ruling on the constitutionality of Mulino's candidacy. It is not clear what the legal outcome would be or if it would come before May 5. Our base case is that Mulino will indeed be allowed to run given the AG's opinion and tight timing ahead of election day.
- The next administration will face an uphill course with several inherited economic challenges such as the need for tax and pension reforms, water management at the Canal and a decision on the copper mine's future. No action amid a tight social and political context would increase risks of losing IG at another rating agency down the road.

Polls show clear lead for Mulino

The latest polls from La Prensa and CID-Gallup paint a very similar picture, with Mulino leading by about 15-17pp on preferences (Figure 1). These also show that second place is being contested between Martin Torrijos, Romulo Roux and Ricardo Lombana, all around 11-14%, while the rest of candidates do not poll more than 6% support. Furthermore, these numbers are not that different from March's La Prensa poll, showing that Mulino's popularity is not being affected by scandals around the Martinelli jail sentence standing firm and seeking asylum at Nicaragua's embassy or the decision not to attend the presidential debates.

The undecided voters seem to be around 22-23% but fragmentation could leave small space for major surprises. It is unlikely that just one of the three candidates jockeying for second place could be identified as the only alternative to Mulino. Hence, it could be difficult to see one candidate grabbing the required votes to surpass Mulino.

The March La Prensa poll indicated that the next Congress will likely be fragmented, with no clear majority (Figure 2). The poll also showed discomfort with current political forces, as "Independent" led the polling while the undecided were as high as 30% of respondents. If

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#Elections

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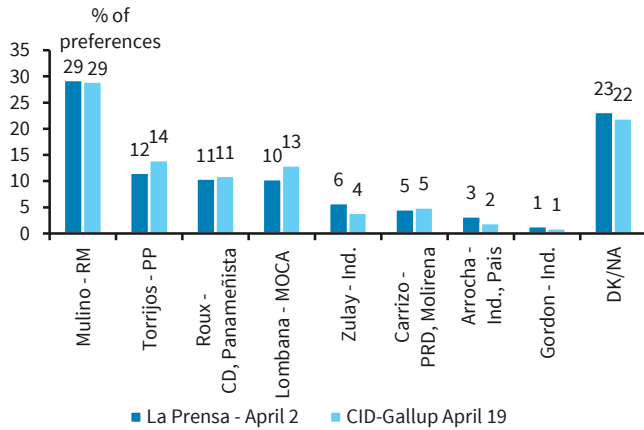
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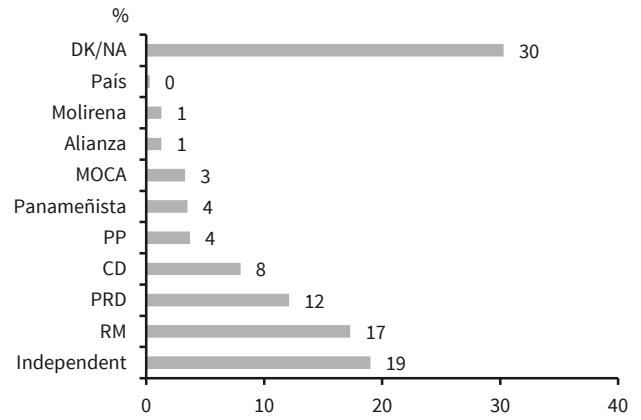
fragmentation materializes, this could also result in an increase to nine political forces in Congress from five in the current legislature.

FIGURE 1. April polls showed similar scenarios ahead of May 5 vote



Source: La Prensa, CID-Gallup, Barclays Research

FIGURE 2. Responses to which party would you vote for Congress in March 12, La Prensa poll



Source: La Prensa, Barclays Research

The risk into the last week: Constitutionality of Mulino's candidacy

Mulino is running on Martinelli's popularity. Mulino was first running for Vice President as ticket companion to Ricardo Martinelli. However, in early February the Electoral Court (TE) disqualified Martinelli from the race after the Supreme Court did not accept appeals for Martinelli's 10 year jail sentence on a money laundering case. The same TE also ruled on March 4 that without Martinelli, Mulino became Realizando Metas' presidential candidate. In prior polls, Martinelli was performing closer to 40% (CID Gallup, October poll) so it seems there was a strong transfer of preferences from Martinelli. In fact, in a recent poll from Doxa, 65% of respondents said that Martinelli is likely to actually be in charge if Mulino wins.

There is an ongoing legal challenge against Mulino's candidacy arguing it is unconstitutional. The voices against Mulino's candidacy mainly argue two things: 1) Mulino was not elected through primaries like the rest of the candidates, thus, did not receive an official electoral act; and 2) the law requires a President and a Vice President, but Mulino's ticket does not have anyone as VP.

The legal outcome is not clear . As part of the Supreme Court hearing process, the National Attorney General Javier Caraballo published an opinion on March 26 saying that Mulino's candidacy is not unconstitutional. There he argued that Mulino's registration as VP was legal and accordance to law. Furthermore, although there is not legal guidance for the specific case where a presidential candidate is not allowed to run, the AG mentioned that Mulino's registration is not only to fill the position of vice president of the Republic, but also to address the event of the vacancy of the main position due to resignation, disqualification or death. On April 16, President Cortizo also mentioned that all candidates should be allowed to run in May 5 including Mulino.

Overall, we think it is unlikely that the Supreme Court could rule against Mulino. Furthermore, there is not certainty that a final ruling could come before elections. There were press reports that five out of nine magistrates on the Supreme Court were on vacation or on business trips this week. We think that as there isn't pressure from the current administration on the Court to rule against Mulino and given the AG's opinion, it is more likely that Mulino is allowed to run, even if there is a last-minute ruling on the case.

Risks cannot be ignored. If a last-minute ruling against Mulino materializes as soon as next week, there could be concerns on how election day is organized and how this could affect voter perception of electoral authorities. In that case, Mulino's supporters are more likely to move towards Zulay Rodriguez, who has been close to Martinelli, although she is perceived as less market-friendly option (Figure 3). Furthermore, if a negative resolution came only after election day and Mulino was elected, the Supreme Court would need to be clear on the implications as it would be unprecedented for current law.

Challenges are identified, recipes are not

In our view, there are no radical platforms among the main candidates or proposals that could shake Panama's economic model. Per our Figure 3, most of the candidates have policy experience and do not lean to the extremes in the political spectrum. The two profiles most concerning to the market could be Zulay Rodriguez, who is perceived to rely on high public expenditure and proposals like unifying pensions systems without tackling sustainability, and Maribel Gordon, who is a leftist candidate and has openly criticized the current economic model,¹ but both are performing low in polls.

However, the key could be willingness or capacity to tackle some of the inherited economic challenges. The focus of the next administration needs to ensure fiscal sustainability among concerns regarding structural growth deceleration amid risks of international arbitration around mining. Furthermore, after a recent Fitch downgrade to high yield, the next administration would be working against the clock to deliver a credible plan that could tackle those topics and ensure that it does not lose investment grade status from another agency. Nonetheless, the campaigns brought forth generic proposals, perhaps understandable, as most of them, in the specifics, could be unpopular:

- **Fiscal reform:** It is likely that the fiscal responsibility law will be modified again, as it would be very hard to comply with the target 2.0% deficit in 2024; our forecast is at 4.4%. It is likely that the government could follow the IMF's recommendation and target 1.5% by 2027, in order to ensure some debt convergence into the medium term, as we currently forecast that debt to GDP will start to increase as soon as this year to about 60%. However, in order to regain credibility around those targets, tax reform will likely be needed. Panama has historically relied on the Canal's revenue while tax-related revenue has been as low as 7.7% of GDP. Such reform could address current exemptions or low VAT rates, at 7%.
- **Pension reform:** There is uncertainty on when the subsystem of defined benefits of the pension system will run out of reserves. Some local analysts think that it could materialize as soon as this year,² while authorities, as mentioned in the last IMF article IV report, say that will actually not happen until 2025. Nonetheless, the government's need to cover that deficit of about \$1.2bn at some point, and which is only increasing in coming years, is unavoidable. The next administration will need to think of parametric changes, such as age retirement or contributions, or ways to fund that subsystem to provide some sustainability, with the latter more commonly cited by candidates.³
- **Canal and water management:** The Canal has started to ease transit restriction in past months, with the latest announcement saying that the limit would increase to 32 vessels per day starting in June, up from 27 in April. However, that is still low compared to 38 reported a year ago. The low rain levels reported in the past year highlight the need to support the Canal

¹ Maribel Gordón: 'Si la izquierda representa el cambio que demandamos en este momento, sí, soy de izquierda', La Estrella de Panama, May 21, 2023

² Emergencia pensionaria en 2024: Reservas agotadas y la inacción del Gobierno, La Prensa, December 31, 2023

³ Candidatos se comprometen a inyectar dinero fresco al programa del IVM de la CSS y no hablaron de elevar las cuotas ni la edad de jubilación, La Verdad Panama, February 26, 2024

and the importance of securing its activities. This could be the easiest pending task, as most of the candidates have agreed that the government needs to provide the Canal water access. In addition, the plans are likely to include water management programs to also improve water for human consumption increases. The focus is on potential announcements around the legislation needed for the Canal to have access to the "Rio Indio."⁴

- **Mining:** This could be the most-troubled topic for the next administration. If it decides to reverse the decision to reopen the copper mine, it will likely need some time to build political capital before acting. Right now, and as shown by the February La Prensa poll, 90% responded as against mining but that could be biased by the unpopularity of the Cortizo administration. Therefore, a new administration would likely need to build consensus, which would take time and involve planning to undo the moratorium set by the Congress and be sure that any new project could not be declared unconstitutional again. If it decides to stick with the closure plan, there would be a lot of environmental challenges to an orderly closing of the mine, with uncertainty on who would fund such costs, while an arbitration process potentially costing as much as \$20bn would continue to weigh on Panama's outlook. For now, most of the candidates try to avoid the topic and limit themselves to saying that the "people have already spoken."

We maintain our view that political and social space is tight, so no action could bring downgrade discussions in 2025 (see [Panama: Fitch strikes first, will the others follow?](#)). We do not discard that Moody's (BBB-, Stable outlook) places it on Negative outlook or S&P (BBB, Negative outlook) executes a downgrade before year-end, but they will likely provide some space to know the next administration's agenda, its credibility and medium-term implications before deciding to actually strip off Panama's investment grade rating. Indeed, there could be a path to avoid a downgrade if a market-friendly candidate wins the presidency on May 5 and starts to build the consensus needed to tackle politically contentious economic reforms. However, the complex social situation, as shown in street protests over the past two years, uncertainty on structural growth and a fragmented political landscape could make such a path too difficult and eventually lead Panama to lose its IG status at another agency.

⁴ Proyecto en río Indio buscaría solucionar crisis del Canal de Panamá, pero se necesitan cambios en la legislación, Voz de América, February 8, 2024

FIGURE 3. Main presidential candidates

Name	Main political party	Short-description	Main policy proposals
Raul Mulino	Realizando Metas	- Lawyer and Political Scientist and holds a master's degree in Maritime Law.- Foreign Minister in Guillermo Endara's administration (1994) and Security and Interior Minister in Martinelli's Presidency (2009-2014).	- Prioritize macroeconomic stability. He has vowed for fiscal austerity while at the same time maintaining public investment as the growth driver. The CSS situation requires more analysis and dialogue. - He has proposed calling a constituent assembly as a mechanism to reorganize the Panamanian State.- He has been somewhat ambiguous about the mining situation and but considers it a closed topic. Before the contract was declared unconstitutional, he was in favor of mining activity.
Martin Torrijos	Partido Popular	- Economist and political scientist. - Former president during 2004-2009. The economy grew 7.6% on average before the global crisis by the end of his administration.	- He is calling for a six-month discussion of how to fix the CSS, but the people will ultimately decide. His slogan says that he has reformed it before and he can do it again. - No mention of tax reform, but to contain expenditure growth and make subsidies more efficient. - On mining, he said that the people had spoken and the mine should not exist in Panama. He has recognized that the mine's closure would be a long and complex process.
Ricardo Lombana	Movimiento Otro Camino	- Lawyer with a master's degree in International and Comparative Law. - The most "outsider" of the main candidates, he has been focused on diplomacy, private law and journalism. He was an independent candidate in the 2019 elections and placed third.	- Fiscal adjustment focused on the expenditure side, reducing government size and tax exemptions. Fiscal savings would help to save the CSS subsystem, he is against parametric reforms.- New constitution to reform the State and Justice system. - He has been very vocal that the mine should cease operations, while arguing that Panama can win the arbitration process.
Romulo Roux	Cambio Democrático	- He holds a bachelor's degree in marketing, an MBA, a master's in Commercial Law and a PhD in Law. - Former president at the Panama Canal and foreign minister during Martinelli's administration. He came in second place in the 2019 elections.	- He has mentioned that the government needs to make sacrifices to help the pension system, not the workers. - He has also mentioned the for of a Constituent Asembly to reform the State and Justice System. - After the mining contract was declared unconstitutional, he warned that the next decisions should be responsible and minimize the environmental and economic effect. His previous law firm was related to the mining company.
Zulay Rodriguez	Libre Postulación (Independent)	- Lawyer and political scientist with master's degrees in Procedural Law and Environmental Law. - She made a career at the judicial power in the lower courts and has been elected deputy under the PRD party in latest two legislatures: 2014-2019 and 2019-2024.	- She proposes to return to one basic solidarity pension system without parametric changes.- She also proposes a new extension to the Canal so it can allow bigger vessels. - She has been very vocal against the mining contract and even voted against it in October.

Source: Local newspapers, Tribunal Electoral, Barclays Research

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