

# ECONOMY

Challenges to be met  
loom on the horizon

THINK STRATEGICALLY:

## Rosselló 20 Months On

Even With Obstacles, Improvements  
Are Present; On Agenda: Hurricane Relief,  
Healthcare Parity, Reconstruction Funds

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### Measuring government with unbiased benchmarks

This issue of Think Strategically is dedicated to evaluating how the Puerto Rico economy has performed after 20 months under Gov. Ricardo Rosselló Nevares. Measuring a successful governorship takes much more than these metrics but allows us to measure the overall direction of the island's economic well-being.

On Inauguration Day Jan. 2, 2017, Rosselló inherited the following benchmarks. In the chart to the right are the results. →

### Even with headwinds, improvements present

We see improvements in unemployment with a decrease of 24.7 percent over the past 20 months. In addition, the labor-participation rate increased almost 0.25 percent during the same period. It is worth mentioning that by October 2017, the participation rate had stood at 38.5 percent due to the impact of Hurricane Maria. The median household income also increased 2.87 percent, and the results for gross national product (GNP) growth for fiscal year (FY) 2018 showed positive or

near-zero growth, reflecting much better performance than the previously projected minus-13.0 percent.

Maria's aftermath has exposed the fragility of most essential services. As the most devastating hurricane in Puerto Rico's modern history, we experienced 2,975 deaths from the event. It appears Maria's economic impact was initially overstated, and the following aid package reflects this stance.

### Benchmarks for Puerto Rico

	Oct-18	Jan-17	Change
Price Per Liter Regular Gasoline	\$0.76	\$0.65	23.27%
P.R. Stock Index	2,420	2,552	-5.17%
Unemployment	8.40%	11.70%	-28.21%
Average GNP Growth Rate in Office	-1.27%	-2.20%	73.23%
Labor-Force Participation Rate	40.60%	40.50%	0.25%
Home Ownership Rate	62.90%	62.90%	0.00%
Median Household Income	\$20,078	\$18,826	6.65%
National Debt	\$69 Billion +	\$69 Billion+	Unchanged
Credit Ratings	D	D	Unchanged
Access to Markets	No Access	No Access	Unchanged

Sources: Bureau of Labor Statistics, Federal Reserve Bank of NY, Junta de Planificación, Estudios Técnicos

### Rosselló's advances

•**Placing P.R. hurricanes, FEMA relief on D.C. agenda.** For decades, Puerto Rico was absent from the Washington agenda, and Gov. Rosselló and Maria changed that.

•**Seeking Medicare and Medicaid parity.** Puerto Ricans pay 100 percent of Medicare and Medicaid insurance costs, yet we receive less than 40 percent of our benefits, which is a discriminatory practice. The governor has moved that message to the point that parity may be on the horizon.

•**Inflow of reconstruction funds significant.** More than \$54 billion in federal recovery funds and an additional \$8 billion from private insurance have been approved. As of August 2018, the Federal Emergency Management Agency (FEMA) estimates it has disbursed or approved \$8.1 billion in public and private assistance funding. The total expected over 10 years is \$62.4 billion.

•**Total employment, including self-employed.** Had been declining since 2007. This trend continued into 2017, as total employment reached 964,000 in August 2017, just before Hurricane Maria. This trend has reversed since Maria, with total employment increasing. In July 2018, more than 1 million residents reported having work, which is the highest level since February 2017.

•**Manufacturing increasing.** Post-Maria, Purchasing Manager's Index (PMI) has averaged more than 53, which suggests an expansion in manufacturing activity, and has been particularly noticeable over the past six months. The New Orders index has averaged over 55 post-Maria. This means further increases in manufacturing activity are expected over the coming months.

On the negative side, the governor's challenges came into full light after the hurricanes.

### Some observations

•**Establishing 95 percent of P.R. would have electricity by Dec. 15, 2017.** Even as hopeful as this initial goal was, it created expectations for people that were desperate. A less aggressive goal would have been better. Power was restored entirely by Aug. 24, 2018.

•**Not working as a team with the Legislature, FOMB.** The best way to cure the financial crisis is by reaching agreements with the FOMB, Legislature and U.S. Congress. Doing so will allow Puerto Rico to accomplish the needed five years of balanced budgets and eventual return to the capital markets. This will imply significant budget cuts and changes in the way Puerto Rico conducts its operations.

•**P.R.'s GNP growth may be temporary.** Favorable growth rates of real GNP are anticipated for FY 2019 and FY 2020. Nevertheless, with current and expected growth rates, according to Estudios Técnicos Inc., "It will not be until FY 2026 that the level of real GNP will approach that of FY 2006." Former NY Fed President William Dudley warned: "Don't be seduced by temporary reconstruction dollars." Puerto Rico must find a more permanent economic growth model.

•**P.R.'s debt burden.** The still mostly unresolved issues related to the government's debt will affect its advances in other areas.

•**P.R. at systemic risk in healthcare.** Puerto Rico hospitals are being forced to either reduce costs at the expense of creating potentially devastating impacts on the communities served or take less aggressive cost-cutting measures and risk facing severe financial hardships. The scenario with this indubitable Hobson's Choice (which is a "free" choice in which only one thing is offered) has developed through profound public policy and market moves that transfer financial risk to the local healthcare systems. With little or no financing available, we have considerable similarity to the 2008 systemic risk crisis. Despite detailing the need to improve health services, there is no stronghold activity within the plan to use reconstruction funds (i.e., Community Development Block Grant-Disaster Recovery).

•**Demographic changes, loss of population.** Although recent data suggest it will not be as severe as expected, there is consensus that by 2025 the population of Puerto Rico will be nearly 3.1 million people. The difference is some 700,000 individuals from the population in 2000 and nearly 1 million below projections made that year for 2025 of about 4.0 million. The consequences related to demand

are significant but given a much older and a very low-income population, the need for government healthcare and social services will be higher and will require considerable changes.

•**The federal tax reform.** A new challenge for Puerto Rico is the federal tax reform approved in December 2017, which will require the island to radically alter its industrial promotion approach and take steps to mitigate the impact on the industrial sector and overall economy. Much of what will occur in the mid- and long terms depends on how successfully we reinvent our economic growth and development strategies.

•**Governor's recent executive order increases minimum wage for construction workers to \$15 an hour.** At the lowest base level, this increase produces a cascade effect on all other payroll levels and industries closely related to the construction sector. The effect increases average labor costs for any government construction project by more than 85 percent.

•**The P.R. Tax Reform.** This tax reform is ill-timed; it would have been more advisable to postpone it until 2020.

•**The 2,975 deaths from Maria.** It took the government one year to accept this number of deaths, instead of the 64 initially reported.

### Final Word: What challenge will make us work harder and faster?

We must find processes to strengthen the ways government is managed, and this can be done if we have the appropriate metrics. Benchmarking is a necessary function of government because it can enhance oversight and accountability of programs, improve effectiveness and efficiency of services, and assess what works and what does not while providing critical information for difficult policy decisions.

As for the challenges, we should begin to wonder: "what will be the next test for the island? What will be the challenges that will make us work harder and faster?" Nothing is more important than rising to the response to these questions.

Puerto Rico needs all the help it can get to emerge from this crisis, and it takes more than one person with a familiar name to do it. Industrialist Efraín D. Vassallo, may he rest in peace, used to say, "Last names do not make the person; it is the person who makes the last name." The Governor has a once-in-a-lifetime opportunity to make his mark on Puerto Rico's history.

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