

ECONOMY

Who do we trust?

THINK STRATEGICALLY:

A Life that Cannot be Tested is a Life that Cannot be Trusted

As Gov. Rosselló Steps Down, Stocks Finish Week at Record Highs, GDP Slows from Trade Tensions, Weaker Growth Globally

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Gov. Rosselló steps down

The TelegramGate scandal that sent Gov. Ricardo Rosselló on a downward spiral began July 8, 2019, when nearly 900 pages of communications between him and his inner circle were made public. Initially, the governor stated he had no reason to resign, but after massive protests and demonstrations arose across Puerto Rico, the public outcry reached its highest point when, on July 22, up to 700,000 protesters shut down Luis A. Ferré Expressway, an 11-lane highway in the heart of San Juan.

The protests sprung up like wildflowers, attacking with massive support, including from some of Puerto Rico's most prominent stars, such as Ricky Martín, Residente and Bad Bunny, all calling for Gov. Rosselló to resign. As the protests continued, most former Puerto Rico governors requested his resignation, as well as prominent members of U.S. Congress, such as Rick Scott, Raúl Grijalva, Nydia Velázquez and even the House and Senate leadership. As the crisis ensued, the mayors and resident commissioner asked Rosselló to step down, and the governor was left all alone with no one to support

him. It became evident that having Rosselló as governor would be a liability to the island. Every day there were follow-up mass protests. Finally, Rosselló caved under the pressure and resigned July 24, 2019, via Facebook Live, with an effective date of Aug. 2, 2019, at 5 p.m.

Puerto Rico and the world watched the conclusion of what at first glance appeared to be a bright political career. The island now knows that Rosselló was unfit to serve as governor, and these are some of the traits that led him to fail.

- He never achieved any personal victories of any significance before leading his team as governor.
- He surrounded himself with people who did not have unconditional love and respect for him; if he had, such a chat would never have been created.
- He had less influence than any other governor.
- His inability to hire brilliant people was evident, with certain exceptions.
- He could not prepare his team for the journey of governing.
- He sold his vision and plans short.
- He paid little attention to fundamentals.

In short, to sum it all up, what we learned most from having Ricardo Rosselló as governor is that before choosing any leader, we have to say to any leader: "A life that cannot be tested is a life that cannot be trusted."

As I was writing this column, I thought about some great advice from my grandfather, general contractor Tito Castro. When I started my career in business, he told me, "Before you make any decision or consider any action, stop for a second to think, is this decision I am making, will it make my wife, my parents, my children or family proud or would it embarrass them. If you have a single doubt, do not do it. This simple thought process has served me well all my life, and even though like all human beings, I am not perfect, it has allowed me to consider decisions by recognizing all constituents in my life.

Week in markets: U.S. GDP down, markets at new highs

U.S. stocks finished the week at record new highs, as earnings season delivered much-better-than-anticipated quarterly earnings, and considering that the U.S. gross domestic product (GDP) slowed somewhat, mainly due to trade tensions and weaker-than-expected growth globally.

The GDP, which is the most comprehensive measure of goods and services produced by an economy, grew at a 2.1 percent annual rate in the second quarter (2Q), according to data released by the Commerce Department.

The most recent GDP numbers are a far cry from the 3.1 percent growth rate recorded in the 1Q; it is noted, however,

that consumer spending increased 4.3 percent, signaling that the economy is still strong. As recent corporate results are reviewed, and we examine with more detail the reporting companies, we note that trends in critical sectors such as financials and industrials are quite robust and offer a telescopic view on the economic outlook. For example, in the U.S. Purchasing Managers' Index (PMI) released last week, it showed manufacturing activity stagnated in July, partly due to slowing global growth and continued trade tensions. As we review stocks in the industrial sector, we confirm that challenges are comprehensive and extensive.

The Dow Jones Industrial Average closed the week at 27,192.45, for a gain of 38.25, or 0.14 percent, and a year-to-date (YTD) return of 16.6 percent. In addition, the S&P 500 closed above the 3,000 mark for the week at 3,025.86, for a gain of 49.25, or 1.65 percent, and a YTD return of 20.7 percent. The Nasdaq closed the week at 8,330.21, for a gain of 183.72, or 2.26 percent, and a YTD return of 25.5 percent. Meanwhile, the U.S. Treasury's 10-year note had a slight increase during the week, closing at 2.07 percent, a gain of 0.98 percent, with a YTD return of minus-0.61 percent.

One of the most widely recognized phrases in film history comes from the 1996 movie "Jerry Maguire," when Cuba Gooding Jr.'s character, NFL player Rod Tidwell, uses the phrase "show me the money" to keep his agent, Jerry, on his toes.

Most investors who follow this column would note that we often have advised staying invested during this complex market cycle. That advice has proven to be quite effective, especially after 4Q18. So far this year, we have seen double-digit returns as follows:

- Dow Jones Industrial Average 16.6 percent YTD;
- Standard & Poor's 500 20.7 percent YTD;
- Nasdaq Index 25.5 percent YTD.

Stock increases are a product of several factors that combine over a longer-term period. Although low-interest rates are a factor, the overall health of the economy, labor market, corporate earnings and investment climate combine to create the adequate growth prospects. The best barometer of an economy is incremental corporate

earnings that provide a reliable source of analysis for overall performance.

Even as the overall growth of earnings has slowed, there are plenty of opportunities for investors to realize good returns. As we review the revenue targets from 2016 to YTD 2019, we note the following:

- The target annual revenue for 2017 was \$70.27 billion, a 4.76 percent decline from 2016.
- Target annual revenue for 2018 was \$72.71 billion, a 3.48 percent increase from 2017.
- Target annual revenue for 2019 was \$75.36 billion, a 3.63 percent increase from 2018.
- Target revenue for 2019, updated April 30, was revised to \$76.2 billion, a 4 percent increase.

With U.S. stocks trading slightly over their long-term average valuation levels, our analysis leads us to believe corporate earnings growth will provide the lift for market gains as we advance in the current market cycle.

Final word: A word of caution to manufacturing

Not all is well in the manufacturing sector; please note some of the critical statistics we are monitoring.

The U.S. Manufacturing PMI fell to 50 in July, which is below the hoped for 51, reaching its lowest rate since September of 2009.

Overall output has contracted at a rapid pace similar to August 2009.

New work from abroad declined at the fastest pace since April 2016.

Employment decreased in the sector for the first time since 2013.

The resulting weakness in the manufacturing sector is the result of the U.S.-China trade war and its impact on overall global trade, having a significant effect on manufacturing.

What is ahead for U.S. economy

The week of July 29 to Aug. 2 will focus on the earnings season and possible rate actions from the Federal Reserve Bank. With nearly 50 percent of the S&P 500 reporting 2Q19 earnings and the Fed is widely expected to cut rates for the first time since the Great Recession of 2008. In addition, critical data to be released Aug. 2 include consumer spending and the July jobs report.

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Market Close Comparison	7/26/19	7/19/19	Change	YTD
Dow Jones Industrial Average	27,192.45	27,154.20	0.14%	16.60%
Standard & Poor's 500	3,025.86	2,976.61	1.65%	20.70%
Nasdaq	8,330.21	8,146.49	2.26%	25.50%
U.S. Treasury 10-Year Note	2.07%	2.05%	0.98%	-0.610%

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