

ECONOMY

Is Puerto Rico Ready?

THINK STRATEGICALLY:



Economic Healing Takes Time and Courage

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We have already gone through more than 15 years of economic contraction, and despite having used numerous tools to reactivate the economy, the efforts have not paid off. After more than two decades of fiscal imprudence, excessive spending, and wage and benefits increases for public employees that drove Puerto Rico into bankruptcy, we now have the opportunity for complete economic healing.

A recurring theme in Puerto Rico's economic analysis has been its poor performance for at least three and a half decades. In that period, the economy had an annual growth rate of about 2 percent, well below the rates achieved by our competitors. We are now basing most of our growth on a combined federal funding allocation of about \$94 billion. Healing forces us to develop a new sustainable economic model aside from those funds to develop a new sustainable economic model.

Joseph Schumpeter, the great Austrian economist, used the phrase "creative destruction" to describe the forces of

the market in its function of provoking constant changes and adjustments to promote innovation.

Now that the Financial Oversight and Management Board (FOMB) has restructured most of Puerto Rico's debt from \$70 billion to \$34 billion, the question is how we create an investment climate of trust.

This juncture is a logical time to commit to a higher level of economic growth while reducing government even further; there are diverse opinions on this subject, but we must agree to a plan and stick to it; the healing of a nation is often tricky and hurtful. However, there cannot be shortcuts to achieving success.

What we can do as citizens to move our country forward is to create a comprehensive country plan and establish a set of goals that I call the Puerto Rico First Goals. Goals that go beyond any political or governmental consideration are goals that the entire country can recognize and support. From my point of view, I would initially like to propose that we adopt the following:

Puerto Rico First Goals

- Transform Puerto Rico with robust economic development and sustain a consistent growth of no less than 4 percent within the next 10 years;
 - Promote the knowledge-based economy in which employment is no less than 25 percent of GNP within 10 years;
 - Create 300,000 new jobs in the private sector within 10 years;
 - Increase the labor participation rate to 55 percent within 10;
 - Reduce the unemployment rate to 4 percent within 10 years;
 - Reduce the government apparatus by transferring to the private sector any corporation, operation or service that it can run more efficiently;
 - Increase median household income by 30 percent to reach at least \$27,200;
 - Transform the educational system from primary to university level into one focused on entrepreneurship, trades and transformation.
- These goals would add more than \$15.5 billion in new economic activity, wealth creation, job growth and education; the Puerto Rico First Goals are the key to the island's economic healing.

The Week in Markets: One Quarter Down, 3 to Go, Wall Street Searches for Growth

The U.S. stock market closed the week with mixed results. Investors welcomed the second quarter with gains amid news that the U.S. economy added 431,000 new jobs and the unemployment rate dropped to 3.6 percent.

The U.S. economy added nearly 1.7 million jobs during the first quarter of 2022. The U.S. economy averaged 562,000 a month, similar to the first quarter of 2021. These results further evince that the U.S. economy is close to a full recovery.

All of the indices we follow finished the quarter with losses: the Dow Jones Industrial Average fell 4.18 percent; the S&P 500, 4.62 percent; the Nasdaq Composite, 8.84 percent; and the Birling Puerto Rico Stock Index, 4.88 percent.

Despite the current results over the last several weeks, the market has risen close to 10 percent from the lows of the first quarter. The Russia-Ukraine war has had an impossible impact as significant as the inflation pressures that have made the Federal Reserve react more aggressively.

The key to the continuation of the U.S. stock market's growth are three segments of the U.S. economy:

- Inflation Pressures: During the week, the U.S. Core PCE Price Index year over year (YOY) rose to 5.4 percent, compared with 5.17 percent last month, higher than the long-term average of 3.2 percent, as the Fed's preferred inflation indicator continues to reflect higher than historical inflation; while the highest in 40 years, it was below the estimated 5.5 percent. We see prices beginning to normalize by the third quarter of 2022; supply chain issues would be behind us, and commodity prices that rose due to the conflict would have dropped.
- The Health of Consumers: The recent unemployment report, which fell to 3.6 percent, the lowest in recent history, signals that even with the inflation headwinds and increasing prices, the U.S. consumer continues to see positive economic growth.

Also, another key indicator that has continued to rise is the participation rate, which grew at 62.4 percent, an important barometer that the labor force situation is slowly normalizing.

— Corporate Earnings Growth is Expected to Continue: We expect the first-quarter earnings to report on April 14; beginning with Goldman Sachs and JP Morgan Chase, we continue to see earnings revisions for 2022 to climb higher. We expect significant upward revisions in corporate earnings signaling a growing U.S. economy.

The Final Word: Looking for Opportunities

- We evaluate the year to date returns and price targets for each stock as of April 1 for our banking portfolio of stocks:
- Wells Fargo (WFC): had a first quarter return of 1.52 percent and has a price target of \$62.55.
 - OFG Bancorp. (OFG): had a first quarter return of 0.23 percent and has a price target of \$35.33
 - Popular Inc. (BPOP): had a first quarter return of -1.33 percent and has a price target of \$110.92
 - First Bancorp. (FBP): had a first quarter return of -3.58 percent and has a price target of \$17.88
 - Bank of America (BAC): had a first quarter return of -8.07 percent and has a price target of \$50.95
 - Morgan Stanley (MS): had a first quarter return of -11.38 percent and has a price target of \$111.58
 - Citigroup (C): had a first quarter return of -13.35 percent and has a price target of \$70.50
 - Goldman Sachs (GS): had a first quarter return of -13.68 percent and has a price target of \$434.69
 - JP Morgan Chase (JPM): had a first quarter return of -14.55 percent and has a price target of \$167.68

While we transition onto other investments for our portfolios, it serves you well to investigate some of these stocks, which could deliver welcome news beginning April 14.

Weekly Market Close Comparison	4/1/22	3/25/22	Return	YTD
Dow Jones Industrial Average	34,818.27	34,861.24	-0.12%	-4.18%
Standard & Poor's 500	4,545.86	4,543.06	0.06%	-4.62%
Nasdaq Composite	14,261.80	14,169.30	0.65%	-8.84%
Birling Puerto Rico Stock Index	2,738.64	2,785.80	-1.69%	-4.88%
U.S. Treasury 10-Year Note	2.38%	2.48%	-4.03%	0.85%
U.S. Treasury 2-Year Note	2.44%	2.30%	6.09%	0.95%

Francisco Rodríguez-Castro is president and CEO of Birling Capital LLC. Think Strategically© is a publication by Birling Capital LLC that summarizes recent geopolitical, economic, market and other developments. This report is intended for general information purposes only and does not represent investment, legal, regulatory, or tax advice. Recipients are cautioned to seek appropriate professional counsel regarding any of the matters discussed.