

ECONOMY

Transparency eclipsed in legal harangue under Promesa



Think Strategically: The Darkness Always Lies

Markets Brush Aside Trade War, Labor-Participation Rate Remains Below Pre-Economic Crisis Levels

BY FRANCISCO RODRÍGUEZ-CASTRO
frc@birlingcapital.com

The Markets: Jobs growth & tariff war impact markets

The much-awaited jobs report came out last Friday, July 6, showing total nonfarm payroll employment increased by 213,000 in June versus 244,000 in May, and the unemployment rate rose to 4.0

percent versus 3.8 percent in May, as stated by the U.S. Bureau of Labor Statistics.

There are three key takeaways from the jobs report:

- **How much room is there for continued jobs growth?** If one measures the U3 rate (or the official unemployment rate) versus the U6 rate, which measures unemployment but also adds part-time workers for purely economic reasons, the rate is 7.8 percent. The labor-participation rate remains below pre-economic crisis levels.
- **Wages are growing less than expected.** Most economists had forecast wages growing by 2.8 percent in June. While wages rose 2.7 percent, inflation is also on the rise, causing workers not to see the growth on their pay stubs.
- **Manufacturing is on the rise.** With growth of 36,000 jobs during June. Manufacturing almost doubled its jobs growth from May's 19,000. Even as the unemployment rate rose slightly by 0.2 percent, if we compare

year-over-year numbers, June 2017 unemployment stood at 4.3 percent and now is at 4.0 percent.

We must remain vigilant about what effect the trade war with China, Canada and the European Union will have on manufacturing and net job growth.

The three main market indicators began in positive territory, with the Dow Jones Industrial Average standing at 24,732.56, or a gain of 276.08 from the previous close. The S&P 500 opened at 2,778.34, or an increase of 18.52, and the Nasdaq opened at 7,731.36, or a gain of 42.97 from the last close. The markets are reacting with a rally that began in Asia as most investors appear to have brushed aside the implementation of U.S. tariffs on imports.

We feel most investors are in the market awaiting the July earnings season that is about impacting the market. The earnings seasons fall in January, April, July and October, following the end of each fiscal quarter.

Top 10 July stock earnings poised to produce notable results:

Company	Ticker	Report Date
Citigroup Inc.	C	7/13/18
Delta Airlines	DAL	7/11/18
Fastenal	FAST	7/11/18
First Republic Bank	FRC	7/13/18
JP Morgan Chase	JPM	7/13/18
Oriental Bancorp	OFG	7/20/18
PepsiCo	PEP	7/10/18
Popular Inc.	BPOP	7/23/18
Wells Fargo	WFC	7/13/18

The Final Word: The darkness always lies

The absence of light or darkness is what we perceive when faced with insufficient light relative to our visual field. That is why the dark is always black. When we were children, most of us dreaded going to bed and facing The Darkness. I, for one, could not sleep without a nightlight that my mom would dutifully turn on as my brother and I were tucked into bed.

In those days, The Darkness always provided an array of responses in our minds that made us see shadows, things, noises or even monsters. Thus, I have always stated that "The Darkness Always Lies." As our thoughts are prepared to adjust to the absence of light, it plays tricks on our visual sensory perception.

We found it fitting to use "The Darkness Always Lies" as the headline of this week's column because the current standoff between the Government, the Senate and the Financial Oversight & Management Board (FOMB) is creating such darkness in our already tricky fiscal problems, which is another step in the wrong direction.

The Government of Puerto Rico opted to sue the FOMB over a recent budget impasse, when the FOMB rejected the \$8.7 billion budget passed by the Legislature. The budget, however, was not the complaint. The issue was that it did not also include the repeal of Act 80 of 1976, better known as the wrongful termination law.

What is surprising about this lawsuit is that until the Senate rejected the Governor's requests—not once, but twice—to repeal Act 80, the Governor had been in line with the FOMB and the deal that both parties had agreed upon to stave off further budget cuts.

In its argument, the Government states, "The FOMB cannot obligate the Governor to comply with its policy recommendations, whether those recommendations are freestanding

or advanced in a fiscal plan. The FOMB cannot impose mandatory workforce reductions, change the roles and responsibilities of certain government officials, criminalize certain acts under Puerto Rico law and otherwise seek to micro-manage Puerto Rico's government."

Puerto Rico is facing the same situation I experienced as a child and, as you now know, "The Darkness Always Lies."

What eludes Puerto Rico is not our ability; it is our willingness to act.

Through this process, there has been little willingness to implement austerity measures to adjust Puerto Rico's mushrooming budget and bad practices. As we said in the past, we need look no further than Detroit. Not only had the city created a 10-year budget forecast to ensure continued stability, but they obtained approval from the credit rating agencies, which upgraded the city's bond rating.

Detroit's fiscal position

- Three-consecutive years of balanced budgets and operating surpluses.
 - Two credit rating upgrades in less than three years.
 - Income-tax revenue has increased 15 percent over four years.
 - The property-tax collection rate increased to more than 80 percent in FY 2018.
 - Finished FY 2017 Comprehensive Annual Financial Report (CAFR) four months earlier than the prior two years.
 - Executing strategy to address legacy pension contributions that resume in FY 2024.
 - Creation of the Retiree Protection Fund (RPF), an irrevocable U.S. Internal Revenue Code Section 115 trust, to gradually build up assets and budget capacity of the RPF.
- Between bonds, unfunded pensions and other claims, Detroit's record-setting debt upon bankruptcy was \$18.8 billion. Puerto Rico has far surpassed that amount. Its comparable debt is \$122 billion, or 6.5 times greater than Detroit's, with \$74 billion in bonds and \$48 billion in unfunded pensions.
- Our relaxed sense of urgency is completely unacceptable, and as we fall deeper into the darkness, we will continue to see that "The Darkness Always Lies."

Francisco Rodríguez-Castro, president & CEO of Birling Capital, has more than 25 years of experience working with government, and multinational and public companies.