



4 FORECASTS,
3 THEMES &
3 REACTIONS FOR

The Trumpcession



As we share this issue of The Zenith Investor, I would like to first thank Francisco “Paco Pepe” Rodríguez Castro, President & CEO of Birling Capital for his valuable contributions to the Puerto Rico Chamber of Commerce all these years, with his collaboration and leadership in various successful investor conferences. This time, we have the opportunity to collaborate in an area where our members need timely information regarding the international markets, in line with this year’s motto of taking you “Mas Allá del 100x35”, taking us well beyond the boundaries of the 100x35 miles of our beautiful island. The Chamber has some stimulating activities with regards to international efforts, and we are planning significant events for this year.

Notwithstanding the uncertainty brought about by the recent government scandals, we remain confident that Puerto Rico is a viable and attractive investment destination. We continue working with the state and municipal governments to create a framework for implementing various programs, such as Opportunity Zones, and direct investment as a result of the new Incentives Code approved on June 30.

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President and Chairman of the Board
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As we publish this issue of The Zenith Investor, we may have dodged Hurricane Dorian, but we could not avoid the Dow Jones Industrial Average finishing August with a 460.99 point drop, and we may not be able to prevent a recession thus we need to start using the term Trumpcession, to define the path on which President Trump has appeared



to be heading not only the U.S. economy but the global economy with the protracted U.S. and China Trade war.

As the month was ending and the president was due to leave on Air Force One for the G-7 Meeting in Biarritz, France, the president announced he would increase tariffs on China even further. The duties, at a rate of 30 percent, would be implemented on Oct. 1 on about \$250 billion of Chinese goods. Another \$300 billion in Chinese goods will be taxed at a 15 percent rate starting Sept. 1. These new tariffs raise the taxes between 20 percent and 50 percent, and that price increase has a direct effect on U.S. consumers.

This latest move by President Trump follows China’s response to impose

tariffs on another \$75 billion of U.S. products, including crude oil, cotton, pork and soybeans.

Some political analysts have pointed out that the most recent Chinese tariffs are markedly pointed toward President Trump’s base of support, which includes farmers and factory workers across the Midwest and South.

The financial markets, which had recovered during the from a previous loss of 623.24 points, closed with so much political interplay that it is becoming quite challenging to avoid the current volatility.

As it seems the President may be taking us to a Trumpcession and, meanwhile, are creating new all-time image lows for the United States, which was once the beacon of hope, democracy and leadership in the world.

Forecast 1: Trump holds stock market hostage!

With President Trump’s trade war with China, what is an investor to do, and what to look for?

- **U.S. economic growth:** The U.S. economy should continue growing steadily over the next few years, outpacing many other western countries with a growth forecast for Q3 2019 of 1.81 percent as of Aug. 23, using now-cast.
- **Key economic releases:** Last week, PMI Manufacturing slowed to minus-1.17, and the PMI Services Business Activity Index

also slowed to minus-0.13 and the Kansas City Fed Manufacturing Survey even contracted by minus-1.81.

- **Key economic released during the week of Aug. 26-30: Aug. 26-Manufacturers' New Orders of Durable Goods:** New orders for the US manufactured durable goods rose 2.1 percent from a month earlier in July 2019, the most since August 2018.

Aug. 27-Consumer Confidence Index: U.S. Consumer Confidence slipped to 135.1 in August from 135.8.

Aug.27 Manufacturers' Inventories: Durable Goods:

Inventories of manufactured durable goods in July, increased \$1.5 billion or 0.4 percent to \$427.3 billion. This followed a 0.3 percent June increase.

- **Strong jobs growth, low unemployment rate:** Robust jobs market has slowed but increased by 164,000 jobs in July, and the unemployment rate stood at 3.7 percent.
- **The solution to U.S.-China trade saga:** Even though exports only represent 13 percent of the U.S. gross domestic product (GDP) and trade disruptions have a small effect, they do have an impact on the overall business sentiment and may curtail investments across the board in the U.S.
- **Inverted-yield curve continues to show up, signaling a recession:** The inverted-yield curve occurs when 10-year treasuries are yielding less than 2-year treasuries, and usually is indicating a signal of an imminent recession.

We advise investors to also monitor consumer spending because it comprises more than two-thirds of U.S. GDP. Another critical element is corporate earnings because they are usually the source of power for any stock-market growth. This past earnings season was a testament that the economy is still stable and U.S. corporations may continue to support economic expansion. We continue to predict that the Federal Reserve will lower interest rates further. Investors need to have predetermined goals, a balanced, diversified portfolio that allows one to navigate periods of volatility, downturns and uncertainty.

Forecast 2: Wave of Healthcare Mergers and Affiliations to grip Puerto Rico Hospital Sector with a more frugal consumer

As healthcare moves toward value-based care, there have been 850 mergers and acquisitions (M&As) and 925 affiliation and partnership announcements since 2018, which means that consolidations were taking place almost every single business day of the year.

There are several views on what all of the consolidations mean. The consolidation trend goal is to move to lower costs and improved care, as smaller hospitals become affiliated with larger healthcare systems and better technologies. This will be the new normal, and we believe it will increase over the next few years.

The Frugal Healthcare Consumer

A recent KcKinsey's survey shows how the healthcare consumer has changed noting that they are now

- **Frugal-** 65% of them select cost as the top factor when choosing healthcare.

- **Technologically Prone-** just like most of us do with trip advisor, Patients are now looking for online reviews, transparent prices, and local service providers to seek their healthcare services.
- **Heavy on Convenience-** shows the growing proliferation of post-acute environments, like retail clinics. In fact, over the past four years, consumers who report using retail clinics has climbed from 9 percent to 24 percent in younger generations.
- **Waiting Averse-** north of 50% of patients are against waiting for Doctors to receive care, In most polls patients that wait more than 1 hour in a doctors office in 80% of the times receives less than 5 minutes of actual Doctor face time.

As the healthcare sector continues moving to a value-based system, we find some interesting trends that will guide the next few years:

- Stronger collaboration between health systems and health plans.
- Reaching for preventive and wellness rather than curing illness
- Harnessing technology to help patients improve their health.
- Increase adoption of virtual care options.

These, as well as other factors, will drive the Healthcare Industry.

Forecast 3: Countdown to the 'Trumpcession'

Since what we now know as the United States of America became an independent nation, there have been more than 47 recessions in the United States dating back to the Articles of

Confederation and Perpetual Union. For many of us, who started to work in the late 1980s, we have seen three U.S. recessions, namely the following:

- The Early 1990s Recession from July 1990 to March 1991.
- The Early 2000s Recession from March 2001 to November 2001.
- The Great Recession from December 2007 to June 2009.

The last three recessions persisted between eight months and 18 months. Why are we talking about recessions? On Aug. 14, 2019, the Dow Jones Industrial Average fell 800.49 points, closing at 25,479.42. Again on August 23, 2019, the Dow Jones Industrial Average lost another 257.11. The main drivers were, on one hand, the fact that an inverted-yield curve showed up and the two-year Treasury note was yielding more than the 10-year note and the escalation of the Trade War with China as announced by President Trump and the slump in the global economy.

- **What does an inverted yield curve mean?**

An inverted-yield curve is an indicator that a recession is looming. Most recession experts agree there's a long and variable lag between initial inversion and the start of recessions: 22 months on average, ranging from 10 to 36 months for the past five recessions. The inverted-yield curve by itself has a limited economic impact. However, for the financial markets, it is a crucial warning signal that a recession is coming. It also signifies that the health of the U.S. and overall global economy may be weakening.

- **The U.S.-China trade war has taken a turn for the worse-the current consensus from many**

economists is that the chances for a recession have increased and some see the probability of an economic meltdown at as high as 40 percent.

Drivers of the Trumpcession:

- **The U.S.-China trade war:** The U.S. and China have fractured the global economy with the trade war that has imposed 25 percent tariffs on \$250 billion worth of products. The result, for now, is that global economic growth for 2019 is only slightly above the 2.0 percent threshold for a world recession.

- **The German economy is crumbling:** Economic data released Aug. 14 reveals that the German economy shrank 0.1 percent in the second quarter of 2019 as that nation's industrial output posted a 1.9 percent quarterly decrease. The decline of Germany's gross domestic product (GDP) shook markets to the core because this European powerhouse is the world's third exporter after the U.S. and China.

- **Jobs growth:** The U.S. economy has added jobs for more than 105 months in a row, the longest ever. Unemployment is at 3.7 percent, which is very close to 1969 numbers. Should the economy turn, this jobs growth would immediately diminish.

- **GDP:** Having two-consecutive quarters of economic growth is needed to create a recession. So far, the U.S. has continued to grow its GDP, albeit at a slower 2.1 percent rate.

The "Trumpcession," may be coming. We must be prepared to face an economic downturn. By now, investors should have made their portfolios

recession-proof to ride out the current volatile period.

Forecast 4: The European Union In Economic Transition

The Eurozone economy is on route to reaching seven years of uninterrupted growth in 2019, as all the member nations economies are on course to end



the year with positive economic growth. The EU is projected to grow at 1.3% for 2019 and 1.6% for 2020, however some countries their issues are complex a challenging.

Let's look at the challenges of some of the nations in the Eurozone to see their outlook:

- **Germany-** its economy shrank 0.1% in 2Q19 as the industrial output was much weaker than expected.
- **France:** Implemented several fiscal measures that are expected to support
- **Italy:** With the resignation of the Prime Minister and marred with an uncertain budgetary outlook with weaker investment and local demand.
- **Spain:** Has produced an upswing in investment and weak imports.
- **United Kingdom:** the UK is set to grow in 2019 by 1.3% and 1.4% in 2020. This forecast contemplates an orderly Brexit.

Overall the EU is expected to end the year in with net growth and a strong comeback in 2020.

Theme 1: G-7 meeting update on Biarritz 2019

The G-7 is composed of France, Canada, Germany, Italy, Japan, the United Kingdom, and the United States. The G-7 rotates its presidency, with French President Emanuel Macron currently holding the top position since Jan. 1, 2019.

Moreover, the United States will hold the presidency starting Jan. 1, 2020.

The G-7 goal is to combat inequality, and their work has focused on:

- Responding to the worsening bias within countries, through coordination of tax issues, social protection, labor norms, trade policy, and corporate social responsibility.
- Combating global inequality by forging a new partnership with Africa
- Eliminating gender inequality by generating international momentum to amend legislation and act tangibly to combat violence and foster economic empowerment.

One of the issues surrounding President Trump before leaving for the G-7 summit was the news reports that relations between the G-7 nations were very tense and divisive and allegedly President Trump thought the meetings were a waste of time.

Once at the gathering, the president tweeted, “Well, we are having excellent meetings, the leaders are getting along very well, and our country, economically, is doing great—the talk of the world!”

President Trump, who proclaimed himself “The Chosen One,” has created the basis for a global economic downturn of epic proportions, which

was very much on the minds of the heads of state at the G7 meeting.

Theme 2: The Month in markets: August 2019 arrived with a bang with increased volatility and sharp market downturns.

The Dow Jones Industrial Average closed the month of August at 26,403.28 for a loss of 460.99 or -1.72 percent and a year to date return of 13.20%. The S&P 500 closed the month at 2,926.46 for an loss of 53.92 or -1.81 percent, and a year to date return of 16.70%; The Nasdaq closed the month at 7,962.88, for a loss of 212.54, or -2.60 percent, and a year to date return of 20.00%; meanwhile, the U.S. Treasury's 10-year note lost during the month with an inverted yield curve, reaching 1.49% and losing -26.24% and the U.S.

Treasury's 2-year note lost during the month reaching 1.50% and losing 20.53%. The stocks losses are a result of the protracted U.S.-China trade war that as recently as last week President Trump doubled down on the

Monthly Market Close Comparison	8/30/19	7/31/19	Change	YTD
Dow Jones Industrial Average	26,403.28	26,864.27	-1.72%	13.20%
Standard & Poor's 500	2,926.46	2,980.38	-1.81%	16.70%
Nasdaq	7,962.88	8,175.42	-2.60%	20.00%
U.S. Treasury 10-Year Note	1.49%	2.02%	-26.24%	-1.180%
U.S. Treasury 2-Year Note	1.50%	1.89%	-20.63%	-1.060%

imposition of the tariffs, and while at the G7 the President seemed to flip-flop by second-guessing himself. Meanwhile, his staff attempted to allege that what the President meant was that he "Should have imposed more tariffs sooner." Following the G7 meeting, China's top trade negotiator Vice Premier Liu He stated that China "firmly opposes" the recent escalation of the trade war. He also said the increase of the trade war was "against the interest of China, the U.S., and the entire world."

U.S. President Donald Trump later told the media, "China called last night our

trade people and said, 'let's get back to the table,' so we'll be getting back to the table, and I think they want to do something."

In our view, the U.S.-China Trade war is a losing economic proposition for all. For the political arena is winning a position in the opinions of many experts. President Trump is convinced that the Chinese have taken advantage of the U.S. for many years, that is a fact that no one can dispute.

However, how the President has taken to rework a new trade deal has been quite byzantine and unconventional.

The trade war impacts not only China, but it also hurts the U.S. and now the rest of the world's economy.

Increasing tariffs means someone must pay these new taxes, and it is usually the economies in which the duties are being imposed.

For a reason, we have seen the significant impact the trade war has had to the U.S. stock market every time a deal appears near the swings of the market upwards, and on the flip side every instance the trade war escalates the stock markets suffers significantly. As it has become evident, China is under immense pressure to finalize a deal as it is impacting in a very significant way their economy, investment climate, and overall industrial development.

However, in the political arena, the President finds the trade war not only

appealing he finds it in line with the Make America Great Again message which has been his campaign promise since the outset of his political career. When the trade war has resolved any changes, any concession, any deal will be spun as a significant victory for the President. Until the time comes that a trade deal is finalized, you will experience increased volatility as a direct response to trade tensions.

However, investors should note that this just one risk in a mixed bag of threats that surround the markets. We must also consider other risks such as liquidity, concentration, credit, inflation, among other risks that all investors should be mindful of them.

Theme 3: Warren Buffett's Berkshire Hathaway is keeping a cash hoard of \$122 Billion it may signal a Market Crash, let's examine why:

As the Oracle of Omaha's Berkshire Hathaway's reported the second-quarter results that resulted in a significant rise in profits and with its cash hoard increased to \$122 billion and the overall value of its now-famous investment portfolio rose to new highs reaching \$200 billion in value. Without any reservation, Warren Buffett and Berkshire

Hathaway are probably the best value investing guru's in the market. Mr.

Buffett has often used what is named as the Buffett Indicator." The Buffett indicator is a metric used to measure the overall health and valuation of U.S. Stocks and like all things Buffett is simply a calculation of the total market capitalization of all U.S. public stocks by the most recent Gross Domestic Product (GDP). As a matter of historical reference, the Buffett indicator surpassed 145% just before the dot.com bubble burst, and it reached 110% the week before the financial crisis. One must not confuse that the Buffett indicator is a signal that stocks are cheap and they may get even less expensive, just as it happened during the financial crisis or the dot.com burst. Currently, the Buffett Rule is at 138.4%, which US Total Market Capitalization is at 138.4%, compared to 147.4% last year. This is higher than the long term average of 82.85% and indicates levels that we higher than the dot.com bust and just below the financial crisis. However, before jumping to any conclusion, we must consider what has changed, for one the Tax Reform of 2017 has provided companies with a lower tax rate and that translates into increased valuations. What the Buffett indicator is signaling is that the U.S. stocks are primarily expensive and to that point, we have not seen Berkshire make any significant acquisitions lately.

Notable Berkshire Hathaway Holdings:

1. American Airlines (AAL)
2. Apple (AAPL)
3. American Express (AXP)
4. Bank of America (BAC)
5. Goldman Sachs (GS)
6. JPMorgan Chase (JPM)
7. Mastercard (MA)
8. Moody's Corp. (MCO)
9. Coca-Cola (KO)
10. Wells Fargo (WFC)

In just five stocks they hold a whopping \$137.4 Billion and they are Apple at \$52.1 Billion, American Express \$18.2 Billion, Bank of America \$26.1 Billion, Coca-Cola \$22.0 Billion and Wells Fargo \$19.0 Billion.

In summary, we must be mindful of the Buffett indicator as it is telling us most stocks have not been as high or near their high as right now. So indeed a market crash may be approaching.



“Oh, and now who can defend us”- The role of the Federal Reserve Bank (FED):

by CPA Cesar Hernández-Monagas, Principal Birling Capital



During 1970 (there are still re-runs going around) there was a famous Mexican TV Hero called, Chapulín Colorado.

In all the shows, there was always a person in distress who will exclaim “Oh, and now who can defend us” (“Oh, y Ahora quien podra defendernos”), the hero will appear and respond “Me, the Chapulín Colorado” (“Yo, el Chapulín Colorado”).

As we approach what we are calling the Trumpcession, the Federal Reserve System will be the hero that will come to the economy’s rescue. Let’s explain. The FED created by Congress, in 1912, its role is to provide the U.S. with a stable monetary and financial system.

The Federal Reserve System is the central bank of the United States. It performs the following general functions to promote the effective operation of the U.S. economy:

- Conducts the nation’s monetary policy;
- Supports the stability of the financial system;
- Implements the safety and soundness of individual financial institutions;
- Fosters a safe and efficient payment and settlement system;
- Promotes consumer protection and community development

How does the Federal Reserve manage a Recession?

In conjunction with the Department of Treasury, the Fed is responsible for maintaining economic stability. Both entities are more connected than it appears in the news. Also, to keep the financial stability, the Fed sends cash from its operations to the Department of Treasury. It should be noted that the Fed transferred around \$80 billion to the Treasury Department in 2017. So, the Fed not only helps to make and implement policies, but it also produces a significant amount of revenues for the U.S. Government.

The main methods used by the Fed to fight recession are:

- **Change in interest rates:** Recently, the Fed cut interest rates by a quarter-point for the first time in more than a decade. This cut is designed to make borrowing less expensive for businesses as well as the general public.
- **Sell/Buy U.S. government debt:** during the 2008 recession; the Fed implemented a process known as quantitative easing (“QE”). The purpose of the program was to increase the money supply to stimulate the economy. This program was in place for most of the last decade. However, in late 2017 the Fed implemented a reverse program to QE known as quantitative tightening (“QT”), in which the Fed was selling previously purchased securities to reduce the availability of funds in the markets once the economy was stable. Recently, the Fed decided to stop the QT program, but it has not implemented the QE program, yet.
- **Extend cash/credit to financial institutions:** during the years, the Fed has led several initiatives to save the economy by bailing out different corporations and industries. In 1979, the Fed provided financing to maintain the Chrysler Corporation afloat, in the 1980s the bail-out was to help the savings and loan industry. In 2001 it saved the airline industry, and in 2008 it helped financial institutions, such as Bear Stearns (financing was used by JP Morgan to purchase Bear Stearns) as well as AIG, the largest insurance company in the world.

In Conclusion

The Fed acts at the macro level by addressing economic weakness by stimulating the economy and at the micro-level, by saving failing corporations. Interest rates were already adjusted to address this Trumpcession, and everyone is in the watch to what will be the Fed's next step to prevent the downward spiral and to stabilize the economy as it did after the last recession. One thing is for sure; the Fed an apolitical entity must not allow itself to be lured into the Trump Trade War with China, even as it faces numerous attacks from the President, doing so it would only diminish the Fed's luster and independence and will set a dangerous precedent for this and others Presidents to follow.

If you need specific information, please contact CPA Cesar E. Hernandez, Esq. chernandez@birlingcapital.com.

The Final Word: We belong to an Island.... A Call to action! by Francisco Rodriguez-Castro, President & CEO

For the past thirty years we have handed out the blame for Puerto Rico's problems, we have blamed the government, the unions or the private sector, in the end, we are all to blame for our troubles, but no one assumes the responsibility for the direction Puerto Rico has taken. We all must share the blame.

We either elect the politicians, chose the union leaders, or chose the private sector leaders, and they all represent us. It has become quite evident that the problem is not the politicians, the unions, or the private sector; the problem is Puerto Rico as a people. Yes, the culprits are all of us that constitute the civil society.

- We belong to an Island where newspapers will never sell like in other countries because we can't pay just one and leave the others there for others to enjoy.
- We belong to an Island where people feel successful if they steal water, electricity, and cable.
- We belong an Island where the successful man is humiliated, and the Drug Lord is both admired and celebrated.
- We belong to an Island where there is no awareness, and reading is not encouraged nor promoted.
- We belong to an Island where saving for a rainy is not supported, on the contrary, excessive consumerism is encouraged
- We belong to an Island where the legislature works too little, speaks too much and earns the salary of senior executives.
- We belong to an Island where our sensitive environment is unprotected by throwing garbage in clandestine landfills or on the streets or all kinds of trash in our beaches, and when storm drains are full of waste and debris, we criticize the government for not cleaning them.
- We belong to an Island where the right of way is for the car and not for the pedestrian.
- We belong to an Island where we can see an older adult or a pregnant woman and not give them the seat in the bus, public car, or the urban train.
- We belong to an Island where the common good is often ignored for the individual right.
- We belong to an Island where we are full of faults, but we prefer to criticize our politicians.

These Actions must stop; that's enough!

The time has come to refuse to continue to follow the paths and behaviors that have brought us to this juncture and create new pathways and determine our renewed social responsibility.

Allow Puerto Rico to support a better quality of life, abolish inequality, distribute wealth, not poverty, and create a new class of citizen that protects preserves, and cherishes the Island.

It is therefore imperative to create a permanent dialogue to unite Puerto Rico in search of the common good. In search of prosperity, in search of solutions, in search of offering a peaceful life to the people and growing loyalty to the Island where we have been born or chosen to live.

We invite you to look for those responsible for placing Puerto Rico in such a bad shape and find them to demand; Yes, request to correct their behavior. The search will not be extensive; in fact, I'm sure we're going to find them this afternoon when we look ourselves in the mirror. As we view ourselves in the mirror, we must demand that you help us make a better Puerto Rico.

As we see it, we are stronger together, the changes we need will not come if we do not seek them, we are the ones called to find them, protect them, support them and maintain them.

We hope that you have enjoyed this issue of The Zenith Investor © and we very much welcome your comments, thoughts, and ideas; you may reach us at frc@birlingcapital.com or 787-247-2500



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