ECONOMY

Senate Amendments Are a Poison Pill

THINK STRATEGICALLY:

Ten Amendments Derailing P.R.'s Exit from Bankruptcy

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Since we became involved in the economic development of Puerto Rico more than 25 years ago, I have been advocating for the creation of what is called a "country project." The country project includes the strategic guidelines, objectives and indicators that address the challenges faced by the nation and around which all public and private sectors must act and execute to fulfill the intermediate goals of the country's vision.

None of the parties that have governed Puerto Rico has raised, discussed or executed a country project. Without the political actions for the country project that go beyond the elections of the politicians, Puerto Rico will not be able to implement the changes it needs to create sustainable economic progress.

For these reasons, the same political system mostly undertook processes that would not impact their elections or getting re-elected. This type of governance did not allow leaders to properly fix what was wrong in Puerto Rico and made the island's bankruptcy the most significant in U.S. history.

The Financial Oversight and Management Board, or FOMB, exists because our politicians could not avert the crisis that led us to bankruptcy. The FOMB, with the highest cost to our democracy, has made the necessary steps to create a better financial planning process for the finances of Puerto Rico with more careful analysis. The FOMB has become a referee of sorts between the government and Judge Laura Taylor Swain, who oversees the proceedings under Title III of the Puerto Rico Oversight, Management and Economic Stability Act, or Promesa. While the FOMB has not been perfect, and a strong dose of ethnocentrism is needed, it has provided a balance that would have never occurred without it.

Late last summer, discussions began to surface that a measure would be introduced in the Legislative Assembly, the Law to End the Bankruptcy of Puerto Rico, or House Bill 1003.

According to the commonwealth's certified fiscal plan, this bill would set the stage to allow Puerto Rico to end the bankruptcy process and eliminate more than 50 percent of its bonded debt, allowing the island to exit bankruptcy with a fighting chance and a new beginning.

It appeared that the necessary negotiations between the FOMB, executive and legislative branches had occurred, and thus HB 1003 was filed. Suddenly this week, the Popular Democratic Party-controlled Senate presented 10 amendments to HB 1003 that are poison pills for the process.

We will discuss the three that, in my view are either controversial or cost-prohibitive:

1. To protect retirees' pensions, an agreement was reached that only cut pensions above $2,000. Now the Senate is reneging on that agreement, and is calling for no pension cuts whatsoever. Retirees are unsecured creditors in the bankruptcy, and the government of Puerto Rico collapsed the Employee Retirement System because it became insolvent.

2. Establish the goal of 100 percent of the population having medical coverage: The health reform and its plan, Vital, is a system the island cannot afford and has made its finances more delicate. Extending medical coverage to 100 percent of the Puerto Rico population would cost more than $6 billion a year, and is an unrealistic proposal.

3. A Fixed allocation of $500 million in the budget for the University of Puerto Rico over five years, freezing programmed cuts: The UPR needs to be revamped entirely. It only produces less than 3.5 percent from tuition, while its stateside peers get well above 25 percent. It has created a bloated operational system of 11 campuses with staff that exceeded 14,000 people for 57,000 students. While we support the UPR mission, its operations need to be updated; look at how private universities have grown by offering modern curriculums and solutions without the turmoil present in the UPR.

These three items could add north of $8 billion, if not more, to the yearly budget of Puerto Rico, a figure we cannot afford. The other seven amendments include fewer problematic matters like the University Scholarship Trust Fund, protecting medical plans, among other mechanisms that, in our view, can be dealt with later, when Puerto Rico is no longer in bankruptcy.

In conclusion, former Gov. Rafael Hernández-Colón said: "Historically, a country's project is forged in a democracy when the electoral majorities arrange to face adversity, hunger, injustice and hopelessness, as happened in the United States under the presidency of Franklin Delano Roosevelt."

Puerto Rico has been spared such a test because of Promesa. Instead of using that opportunity to change our circumstances, our political system continues to operate in the same ways that drove us to bankruptcy. These amendments send the worst possible message to current bondholders, hedge funds and other constituents.

Week in Markets: Debt Ceiling, Volatility, Jobs Stall, Energy Rises, and Supply Chain Disruptions

As last week ended, we experienced a lot of volatility caused mainly by the debt ceiling standoff in Congress, the lower than expected labor numbers, and the energy crisis engulfing Europe. However, the week delivered an increase in all indices, while bonds fell.

As Congress hashed out a short-term deal to keep the government operating and allow the debt ceiling to rise until December, this was enough to improve investor confidence; however, volatility will remain.

The continued global supply chain dislocation, rising energy prices, and labor force shortages will continue to impact the markets.

Let us discuss each item in detail:

– Energy Prices on the rise: Oil's price increased to a seven-year high, and natural gas prices are also on the rise, causing an energy crisis in Europe and China. Europe is blaming Russia for the price increase, saying it may be withholding gas supplies, making prices soar, to force the approval of the much-debated Nord Stream 2 pipeline, which would deliver gas directly into Germany. In China, authorities ordered coal mining to increase at least 98 million metric tons, or 30 percent of the total production, to avert the rising power outages.

Don't expect this to impact the United States materially as we are now less reliant on oil than in years past, and we have gained energy efficiency

– Danger Labor Alert: U.S. job numbers fell 46.99 percent compared with the previous month. Estimates pointed to 500,000 jobs but only 194,000 were filled in September. However, on a positive note unemployment fell to 4.8 percent, from 5.2 percent, marking the third consecutive monthly drop. With an outsize number of job openings, the elapsing of the pandemic benefits, and fewer COVID-19 infections, we believe the labor markets will pick up considerably. One last thing we must mention is that we do not see a stampede of workers returning to the labor force, and we note the labor participation rate fell 0.1 percent

– Global Supply Chain Disruptions: The constant material shortages, including computer chips, are affecting the world's supply chains in a very material way, and with it, millions of products of all kinds. One of the best examples is U.S. automobile manufacturing shipments, which fell to $5.54 billion, down from $7.44 billion one year ago, a 25.51 reduction and 1.9 billion fewer vehicles sold. The supply chain disruptions will last as long as COVID-19 remains a problem globally.

In conclusion, the symmetrical labor and material shortages impacting the global supply chains are affecting economic activity, forcing prices to rise and, with it, inflation.

We believe these economic conditions will become temporary in nature and will sort themselves out soon. Our outlook for the year's end into 2022 remains positive with growth across most sectors; however, be advised that a market rotation will quickly occur, and we must all prepare our portfolios for the sizable opportunities.

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Weekly Market Close Comparison	10/8/21	10/1/212	Return	YTD
Dow Jones Industrial Average	34,746.25	34,326.46	1.22%	13.53%
Standard & Poor's 500	4,391.34	4,357.04	0.79%	16.91%
Nasdaq Composite	14,579.54	14,566.70	0.09%	13.12%
Birling Puerto Rico Stock Index	2,973.47	2,924.13	1.69%	45.40%
U.S. Treasury 10-Year Note	1.61%	1.48%	8.78%	0.70%
U.S. Treasury 2-Year Note	0.32%	0.27%	18.52%	0.63%