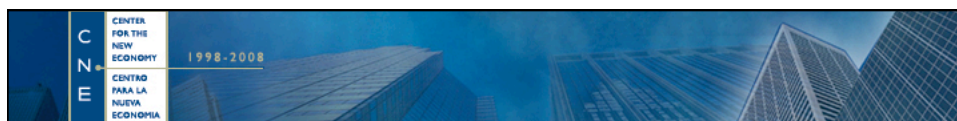


IS THERE LIFE AFTER ARRA? (Is there life during?...)

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Alphabet Soup Scenarios


- **Is it a V, or a U, or a W, or an L?**
- The recession is now in the late part of its fourth year
- The cumulative decline in real Gross National Product has been over 10%
- The consensus seems to be a rather wide U-shaped cycle.



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The Governor's Council of Economic Advisers:

- The Puerto Rico Economy is entering a stabilization phase, although not all indicators are in this phase of the cycle, especially those in the construction industry...
- This phase will last several months... before the economy reaches an inflection point and begins to grow again.
- In the first half of FY 2010 the Puerto Rico economy was not experiencing a recovery in parallel with the US economy...
- FY 2010 will still be a year of negative growth for the Puerto Rico economy



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What the Indicators Say

- **INDICATORS POINTING TO "STABILIZATION"**
 - Manufacturing employment and exports
 - Total employment
 - Employment in retail sales
 - Hacienda revenues
 - Electric power generation and consumption
 - Tourism indicators
- **INDICATORS POINTING TO CONTINUING CONTRACTION**
 - Construction industry data
 - Banking
 - Bankruptcy filings

Is There Life After ARRA?

- THE GOOD NEWS IS...
 - There are still about \$4.5 billion in ARRA funds available to Puerto Rico
- THE NOT-SO-GOOD NEWS IS...
 - Most of that money is not available for investment
- STILL, ARRA MAY BE A PRETTY GOOD THING...
 - It could be the force sparking a modest recovery in the second half of this year
- BUT, WHAT AFTER ARRA FUNDS RUN OUT?...
 - Recovery need not lead to sustained growth

Are PPPs the Solution?

NEEDED URGENTLY:

Large-scale private investment

- PPPs may be a good idea in principle, but...
 - Need profitable projects
 - Taking over existing public functions not good enough

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Other Growth Drivers

- The Pull of the US Economy is the only seemingly sure thing
 - Works for tourism, manufacturing
 - Doesn't work for construction, retailing, services, etc.

May be enough by itself to keep us growing at a 1% to 1.5% annual pace, which is grossly insufficient.

Must activate internal drivers like construction and banking.

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The Wrong Kind of Synergy

- BANKING AND CONSTRUCTION ARE TRAPPED IN A NEGATIVE FEEDBACK LOOP
 - A substantial unsold housing inventory
 - Non performing construction loans
 - Regulatory pressure on banks

ALL OF THE ABOVE CONSPIRE TO CREATE...

An economy-wide credit freeze
A virtual paralysis of private construction

And there are Other Housing Market Issues

Pressure building up in the “social” segment of the housing market

- No recent construction
- Demand for new low-income housing about 10,000 annually
- Repressed household formation → pent up demand

The Looming Tax Reform

- The danger of tax populism
 - Lower tax rates...
 - for everybody?...
 - for free?...
- Can we have a real tax reform, this time around?
 - Lower rates
 - More horizontal and vertical justice
 - A simplified system
 - Less evasion
 - Adequate revenues

The Criollo Plebiscite

- May end up being the Big Spoiler
 - A three-year election campaign
 - Policy paralysis
 - A referendum on Fortuño's popularity, not on the political status

IN ADDITION, IT WILL COST A LOT OF MONEY!!!