



# 2<sup>nd</sup> PROMESA Conference

**January 31, 2018**

## **Fiscal & Economic Update: A View of Two Islands: The Private & Public Sector**

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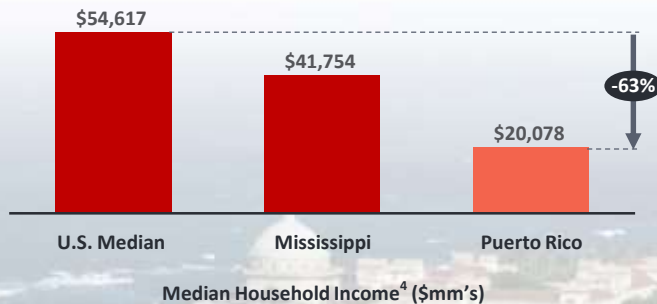


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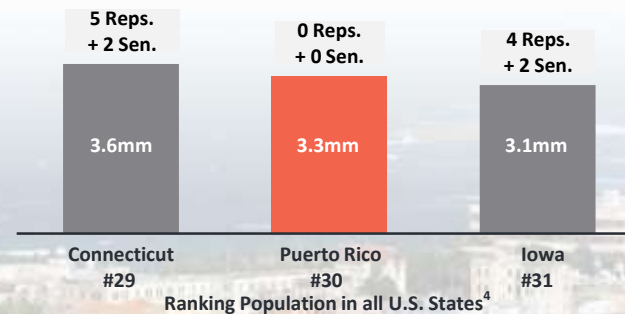
The net effect of the territorial status is inequality, a driving factor in our decade-old fiscal and economic crisis

- Since 2006, Puerto Rico's real GNP has shrunk by more than 14%.
- In the past decade more than 300,000 people left Puerto Rico. The impact of Hurricanes Irma and Maria accelerated this trend with an additional 600,000 people or 19% decline expected by FY22.
- Student population has declined by over 40% since 2000 with an additional 16% decline expected by FY22.<sup>1</sup>
- More than 45% of Puerto Rico residents live in poverty, which is the highest poverty rate of any U.S. state (Mississippi is the next highest at 21.9%). Puerto Rico's 10.9% unemployment rate is almost three times the national level.<sup>2</sup>
- Concerns about quality of life, poor delivery of public services and high unemployment have led to a historic population outmigration.
- Puerto Rico is treated unequally under key federal programs such as Medicaid as compared to states. For example, the Census Bureau has reported that Oregon, a relatively prosperous state with a population size similar to Puerto Rico, received over \$29bn from the Federal Government, whereas Puerto Rico received \$19bn for the same year.<sup>3</sup>
- As discussed further, the impact of Hurricanes Irma and Maria requires that Puerto Rico's fiscal plan provide a roadmap to fiscal recovery and long-term sustainability.

*Inequality created by the territorial status is one of the primary causes of the severe disparity in personal income that exists between residents of the U.S. mainland and Puerto Rico.*



*Puerto Rico ranks 30<sup>th</sup> in terms of population, but because Puerto Rico is not a state it has no voting representation in Congress.*



<sup>1</sup> Department of Education, official public school registry

<sup>2</sup> US DOL Bureau Labor of Statistics

<sup>3</sup> GAO Report United States March 2014: Information on How Statehood Would Potentially Affect Selected Federal Programs and Revenue Source

<sup>4</sup> United States Census Bureau, 2016



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Our vision for the socioeconomic transformation is led by a new Government model to drive fiscal and economic stability

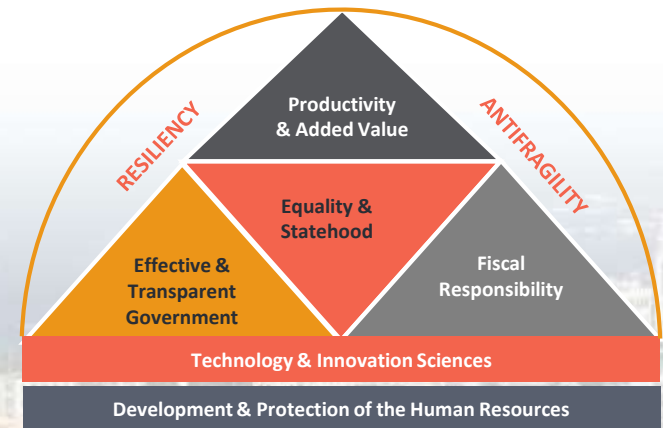
The devastation caused by Hurricanes Irma and Maria creates an opportunity to redesign major components of the Island's critical infrastructure, invest in the quality and resiliency of public and private buildings, and restructure and modernize and reevaluate delivery of services to residents.

### Strategic Goals:

- To establish a new Government which facilitates and implements strategies that achieve sustainable economic growth and provides opportunities for job growth and personal advancement.
- To develop an educated, healthy, productive and vibrant society, observant of law, order and integrity.
- To establish effective, efficient, and responsible government policies and practices that remain sensitive to the needs of Puerto Rico's most vulnerable residents.
- To incorporate practices and operations based on scientific- and performance-based models into Government; where evidence and results matter; and where resident participation, collaboration, and trust in government are the main focus of its validation.

### Main Objectives:

- Develop and **protect human capital**.
- Correct structural issues, **bolster economic growth** efforts, and utilize areas of opportunity.
- Improve **Puerto Rico's competitiveness** through less regulation, energy reform and other various structural reforms.
- Position Puerto Rico as a **global investment** destination.
- Upgrade policies of **public private partnership** investment in energy, water, waste management, and other infrastructure projects.
- Increase labor force flexibility and create **high quality jobs**.
- Develop a **safe, educated, healthy and sustainable society**.
- Achieve **equality** for all residents of Puerto Rico in tune with other U.S. states.
- Remove **inequality** at the local level.
- Use **science and technology** as a driver for transformation.



Source: Plan Para Puerto Rico, Government Program and a Model for the Socioeconomic Transformation of our Island.



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The New Fiscal Plan integrates the devastation caused by the Hurricanes as well as updated facts and assumptions underlying Disaster Relief Assistance and private insurance claims proceeds

The FOMB approved the Certified Fiscal Plan covering a 10-year period on March 13, 2017. Thereafter, the Government began the difficult task of implementing the proposed initiatives to achieve structural balance by FY20. In the aftermath of Hurricanes Irma and Maria, the FOMB directed the Government to revise the Certified Fiscal Plan. The New Fiscal Plan is built upon the pillars of fiscal and structural reform with the main objective of revitalizing the economy and critical infrastructure.

Devastated  
Puerto Rico



Altered  
Macroeconomic  
Outlook



Transformative  
Moment in  
History



A Critical Path  
Forward



External Help  
Critical to  
Support  
Recovery

- Air Worldwide, a global leader in catastrophic risk modeling, estimates that the infrastructure and economic damages correspond to a storm that happens once every 250 to 1,000 years.
- In addition to the 11 years of recession and significant economic decline, the Hurricanes severely impacted the infrastructure and economy of Puerto Rico.
- The Hurricanes had a significant negative impact on the economy; however, Disaster Relief Assistance outlays in the coming years will help rebuild the infrastructure destroyed by the storms and provide a foundation for economic renewal.
- Population is expected to decline by 10% over the next two years with the downward trend continuing, but at a moderated level, over the following years.
- Build Back Better represents a bold and innovative vision on how the Government will rebuild portions of the Island's infrastructure, housing, and economy in a way that makes Puerto Rico stronger, better, and more resilient.<sup>1</sup>
- Puerto Rico established the CRRO to manage the reporting and use of recovery funding with stringent controls following proven past disaster recovery structures.
- Fiscal reforms, such as implementing the New Government Model and improving tax collections, will help to achieve cost efficiencies and enhance revenues. Structural reforms, such as energy and welfare reform, will be implemented to stimulate sustainable economic growth and employment opportunities.
- Obtaining financial support from the Federal Government is vital to rebuild Puerto Rico and to continue providing core services while the Government implements its transformational strategy.

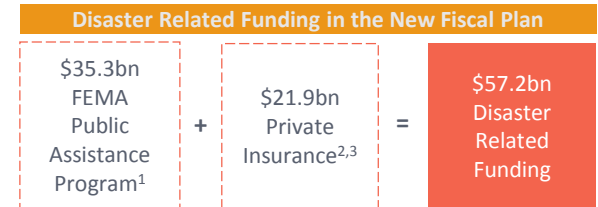
<sup>1</sup> Build Back Better Puerto Rico, Request for Federal Assistance for Disaster Recovery November 13, 2017.



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Although, Puerto Rico anticipates significantly more Federal Disaster Relief Assistance, \$35.3bn of assistance is included in the New Fiscal Plan

- Puerto Rico has requested \$94.4bn in Federal Disaster Relief Assistance.
- However, as required by FOMB guidelines, the New Fiscal Plan assumes only \$35.3bn under FEMA's Public Assistance Program as per current law.<sup>1</sup>
- In addition, \$21.9bn from private insurance companies is included.<sup>2</sup>



- The Government's cost-share is estimated at 10% or \$1.4bn, with \$1.3bn to be spent during the five years covered by the New Fiscal Plan, excluding the amounts related to PREPA and PRASA which are addressed in their respective fiscal plans.
- Puerto Rico is requesting a cost-share adjustment for FEMA's programs under the Stafford Act to 100% Federal. To the extent the cost-share is not eliminated entirely, we seek authorization to use CDBG-DR funds to cover the cost-share match requirements. Historically, either FEMA or Congress have authorized a 100% Federal cost-share for catastrophic disasters such as Hurricanes Andrew and Katrina.
- Congress has approved \$4.9bn of liquidity funds for Puerto Rico and the U.S. Virgin Islands in the form of a CDL. Terms have been the subject of negotiation since October 2017. This loan is not additive to the economy.
- Property Claims Services, a subsidiary of Verisk Analytics, estimates \$21bn of private insurance funds, with 75% spent over the first five years.<sup>4</sup>

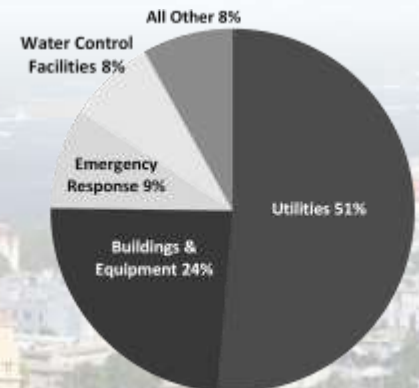
### \$35.3bn FEMA Public Assistance Funding

The FEMA funding need is \$35.3bn based on FEMA Public Assistance program guidelines with a damage assessment by category.

Proposed funding uses:

- 51% – Repairing, modernizing, and strengthening Puerto Rico's water and power infrastructure.
- 24% – Reconstructing critical publicly mixed buildings and fixing of equipment.
- 25% – Rebuilding and strengthening emergency response capabilities, water control facilities and other.

### \$35.3bn of FEMA by Category



<sup>1</sup> PR Government estimates reviewed by third party subject matter experts.

<sup>2</sup> Property Claims Services Estimate, dated October 2017.

<sup>3</sup> Includes FEMA individual assistance

<sup>4</sup> Based on outlays of Hurricane Community Development Fund during Hurricane Katrina recovery.





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### Cash Flows Post Measures, Excluding Debt Service

By FY22 the accumulated deficit is \$3.4bn, requiring a liquidity facility to maintain the ability to provide basic services to residents of Puerto Rico.








<sup>1</sup> Component units are legally separate from the Government, but are discretely presented as component units in the Government's financial statements



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Government Transformation and better revenue management is expected to yield annual savings of \$3.0bn by FY22

			FISCAL MEASURES IMPACT (\$mm's) <sup>1</sup>				
New Government Initiatives	Objective		FY18	FY19	FY20	FY21	FY22
 <b>NEW GOVERNMENT MODEL</b>	<ul style="list-style-type: none"><li>New Government Model is the blueprint for the optimization of government agencies and services while improving quality of services offered.</li></ul>		1	334	784	1,046	1,264
 <b>PROCUREMENT REFORM<sup>2</sup></b>	<ul style="list-style-type: none"><li>Build a centralized, transparent, and efficient procurement function that ensures best value for money by acting as a single customer, rather than separate entities, when buying goods &amp; services.</li></ul>		0	12	33	43	43
 <b>REDUCTION OF APPROPRIATIONS</b>	<ul style="list-style-type: none"><li>Reduce appropriation levels for UPR and Municipalities, while revamping Incentives Code, will stimulate the necessary adjustments and lower dependency from the Central Government.</li></ul>		0	161	302	428	506
 <b>NEW HEALTHCARE REFORM</b>	<ul style="list-style-type: none"><li>By streamlining policy and institutionalizing controls, healthcare expenses will be reduced and benefits optimized.</li></ul>		49	199	500	750	795
 <b>TAX COMPLIANCE AND FEES ENHANCEMENT</b>	<ul style="list-style-type: none"><li>Enforcement of Tax Compliance measures is the main Government lever to enhance revenues while not increasing taxes.</li></ul>		65	210	298	366	415
<b>TOTAL</b>			115	916	1,917	2,633	3,023

<sup>1</sup> All measures reflect gross savings. Estimated total net costs to implement are \$132mm over the five year period.

<sup>2</sup> Third party consultants are currently conducting a thorough analysis of all applicable expense categories. Estimated savings will be updated and are anticipated to be higher than current estimates.



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### Debt Sustainability Overview

The debt sustainability analysis is intended to provide an informative guideline for the long-term financial capacity of the Government and to minimize future default risk.

- 1 The objective of the Debt Sustainability Analysis is to provide forward-looking and transparent analysis of borrowing capacity to regain and maintain capital market access in compliance with PROMESA requirements.
- 2 This analysis is intended to be “creditor agnostic” and does not take any position on the allocation of debt repayments to any particular constituency.
- 3 Borrowing capacity is analyzed using benchmark average U.S. state debt metrics to imply a range of potential debt capacity.

The Government will adopt the following elements generally regarded as key components of a debt affordability study:

1



#### Actual Comparables

Benchmark against peers considering the appropriateness of the comparison group and using multiple metrics to get a full picture of where Puerto Rico stands.

2



#### Projects obligations

Forecasts debt obligations and/or capacity to repay beyond the current fiscal year, considering various issuance and revenue scenarios and looking at multiple measures of future debt levels.

3



#### Comprehensive debt analysis

Consider the majority of debt outstanding from both the primary Government and major component units, and discuss the impact of other long-term obligations on debt affordability.

4



#### Produced regularly

Require regular completion of a debt study which contains a clear statement of remaining debt capacity.





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The new structural reforms package seeks to complement and extend the structural reforms that have already been implemented to drive private sector investment and economic growth



### Ease of Doing Business

#### Tax Reform and Incentives Code

- Local Tax Reform will provide the necessary modifications to help counteract the Tax Cuts and Jobs Act.
- The new Incentives Code will rationalize all economic development incentives, exemptions, subsidies, grants, and credits, based on the ROI to Puerto Rico.
- The Code will conform to the Tax Cuts and Jobs Act to protect and enhance Puerto Rico's competitiveness.
- The Code will establish a new digital and transparent process for the application, award, and compliance of all incentives.

#### Regulatory Reform

- Reduce unnecessary regulatory burdens to reduce the drag of government on the private sector.
- Consolidate all public service & utility regulatory agencies into one.
- Deregulation of land freights to help reduce the price of consumer goods and improve carriers/shippers service.
- Deregulation of occupational licensing to reduce unnecessary hurdles for individuals entering the labor market.
- Modify the condominium law to accelerate decision-making.



### Human Capital

#### Welfare Reform

- Implement a Local EITC program to drive integration into the formal economy.
- Update the welfare structure protect vulnerable segments while promoting self-sustainability.

#### Workforce Reform

- Focus the Workforce Innovation and Opportunities Act (WIOA) incentives to high-priority sectors and capabilities.



### Energy Reform

#### Utility Reform

- Leverage and facilitate expedited private sector investments in modern, cost-efficient, and environmentally compliant energy infrastructure; reform PREPA operations and services to clients; and allow for greater competition in energy generation.



### Government Transformation

#### New Government Model

- Establish a right-sized, integrated, and agile government that facilitates the growth of the private sector.
- Consolidate & externalize the production of economic statistics to the Federal Government.

#### Digital Services Reform

- Maximize the use of technology to streamline all citizen services.
- Modernize the property registry by leveraging the use of technology through a public-private partnership.

#### Transparency Reform

- Approve and implement the Administration's transparency and public documents bill (PS0561 / PC1095).



### Partnering with the Federal Government

#### Executive & Congressional Measures

- Provide equal treatment to Puerto Rico in Federal funding and programs and implement the recommendations of the PROMESA Congressional Bi-Partisan Task Force Report.



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