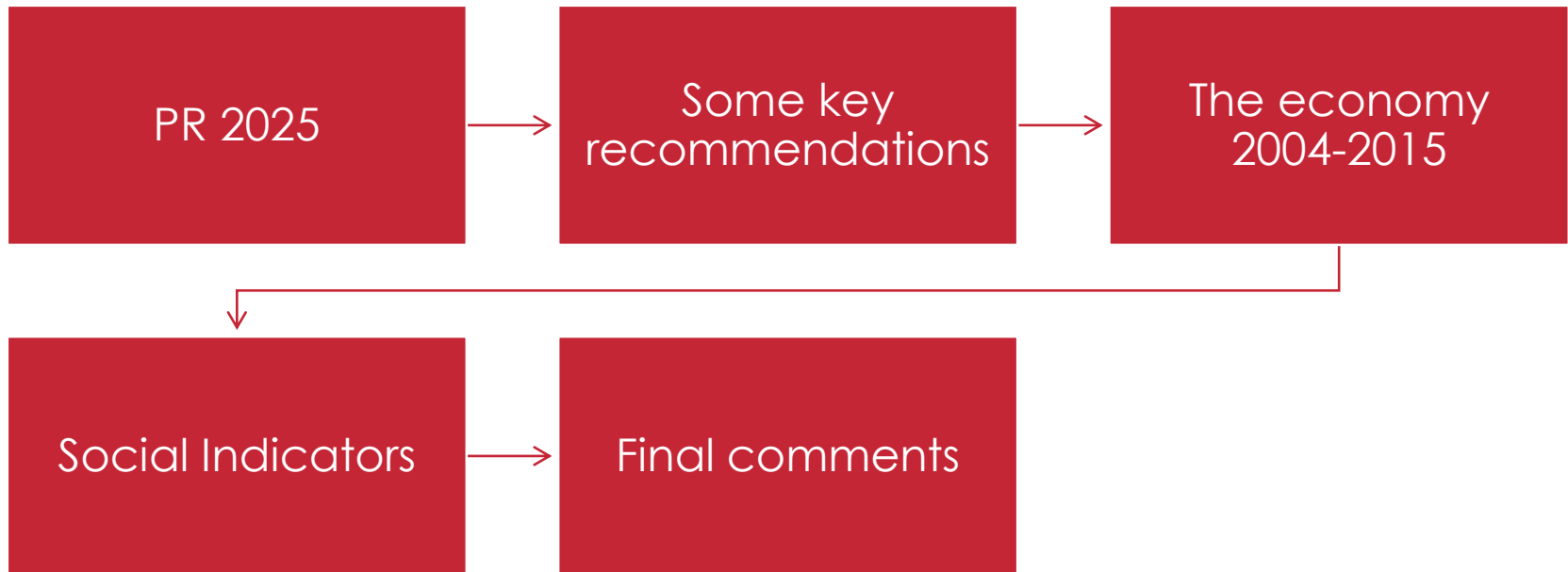




PR-2025: An Update

José J. Villamil
June 26, 2015

Presentation Plan





PR-2025

PR-2025

Background



- An initiative of Governor Sila M. Calderón
- The Project began in 2003 and was completed in mid-2004
- A.T. Kearney was the principal consultant
- A Steering Committee was appointed to oversee the project.
- When a draft was completed a distinguished group of economists was invited to comment on the report
- A non-profit entity was created to provide continuity but was short lived.

PR-2025

Content



Ten key areas were chosen as the focus of the Project

- Innovation and Enterprise
- Competitiveness and Connectivity
- Opportunity and Income
- Education
- Health
- Public Safety
- Culture and Recreation
- Land-use and Environment
- Utilities
- Transportation



PR-2025

Approach

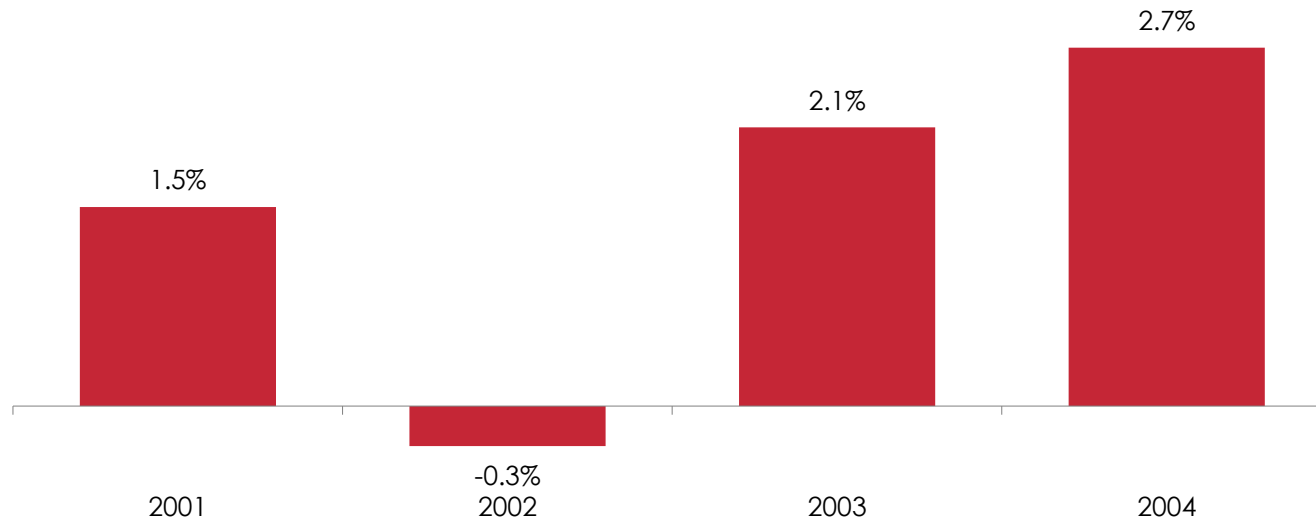
Stripped down to its essentials, the Vision for 2025 consists of four fundamental elements:

- 1 An advanced, globally-connected, knowledge-based economy
- 2 A just and secure society with responsible citizens, communities and institutions
- 3 A healthy and attractive environment
- 4 A diverse and dynamic culture – respected locally and internationally

PR-2025 Context



**Real GNP Growth, Puerto Rico
Fiscal Years -- 2001 - 2004**

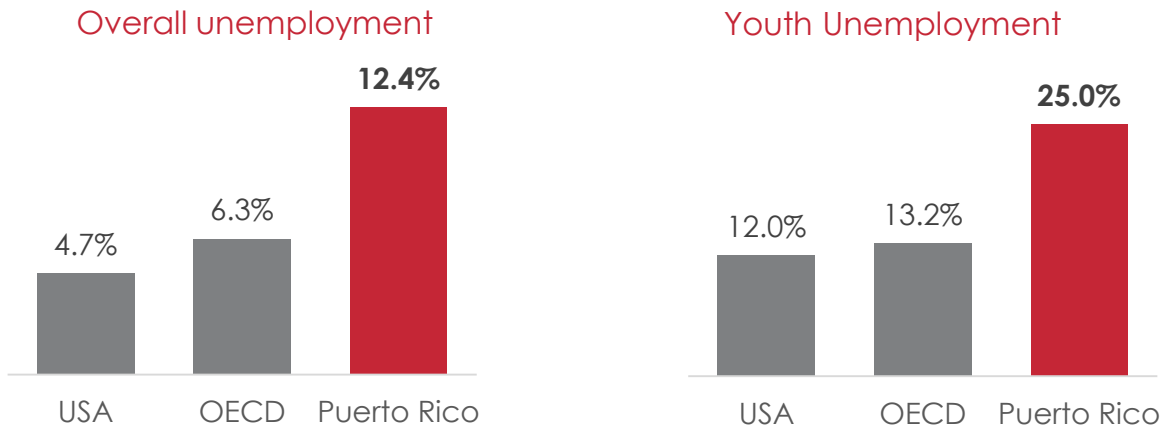


The PR-2025 report was drafted after a period of economic growth only slightly interrupted in 2002.

PR-2025 Context

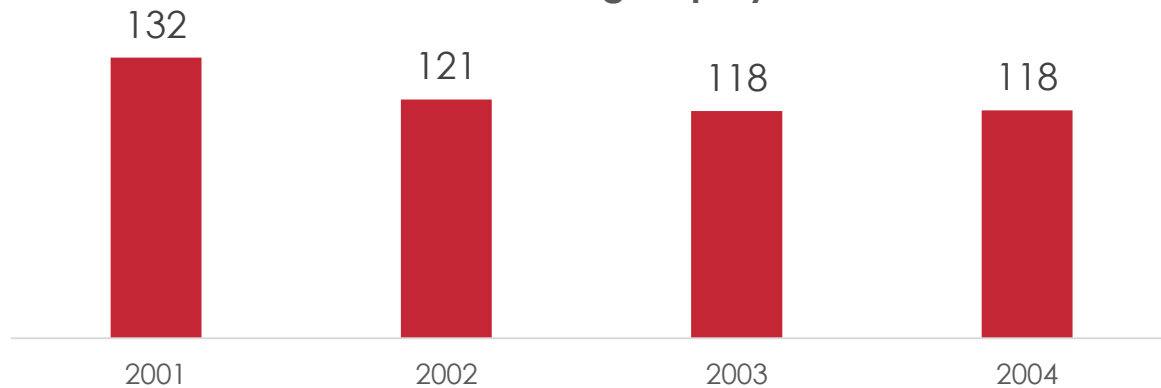


Unemployment- overall and youth rates 2002



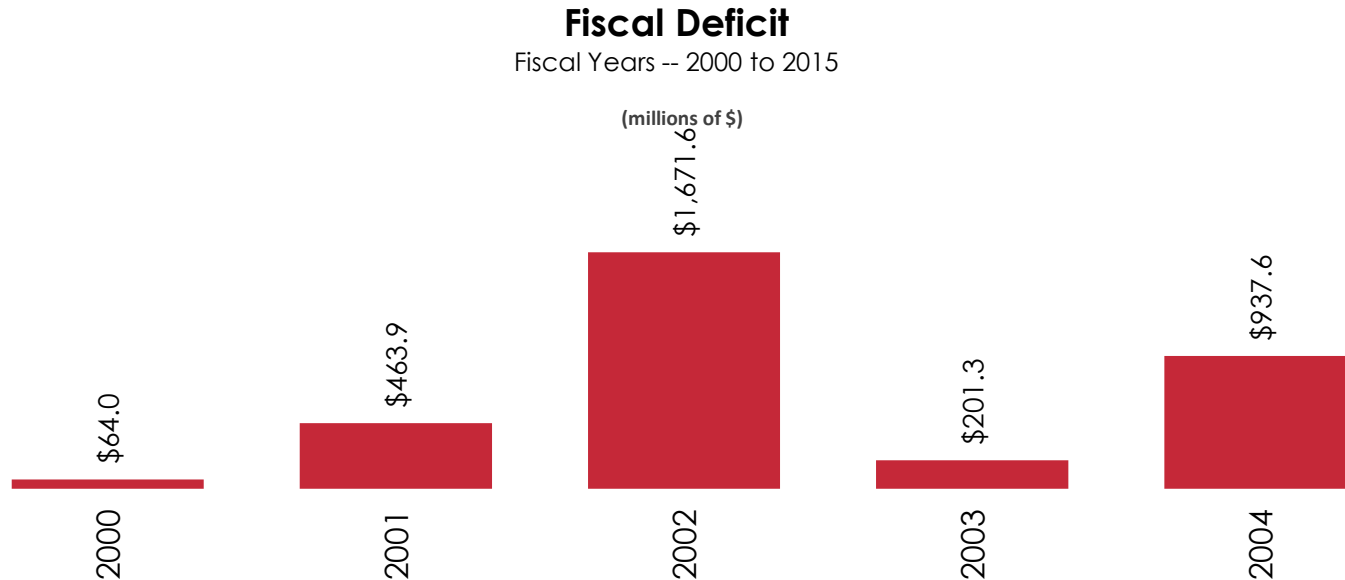
- Unemployment was at a level not too different from the present.
- 936 was terminated and the transition period extended from 1996 to 2005. Manufacturing employment was substantially above present levels. No urgency was reflected in government policies concerning the future of manufacturing, although employment had fallen significantly since 1996.

Manufacturing Employment



Source: PR Department of Labor and Human Resources (2015). Current Employment Statistics: Nonfarm

PR-2025 Context



Sources: Office of Management and Budget (2015). *Budget Petition (various years)*. Office of Management and Budget (2015). *Approved Budget Fiscal 2015*. The fiscal 2015 statistic corresponds to the estimated cash flow deficit upon the fiscal year's closing (May 20, 2015).

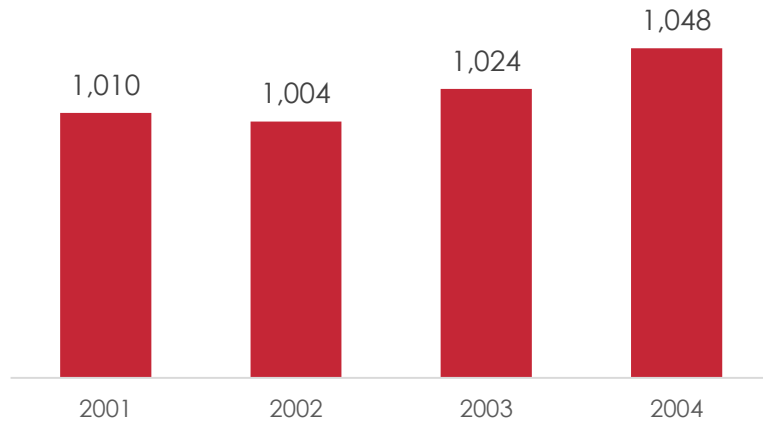
The fiscal situation was already in critical shape but the Commonwealth had access to capital markets, and debt grew in order to deal with operational deficits and finance projects from the 1997-2001 period.

Rating agencies were already expressing concern by 2004 (negative outlooks), but bond ratings remained positive.

PR-2025 Context

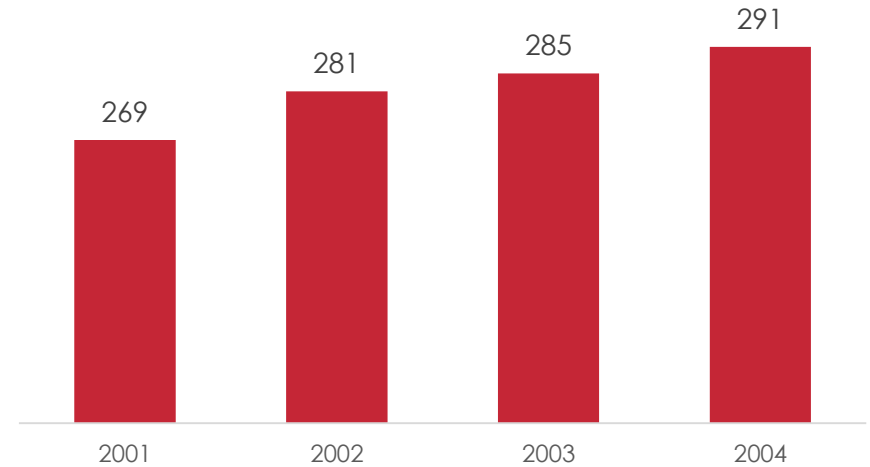


Non-Farm Salaried Employment



Source: PR Department of Labor and Human Resources.

Public Employment



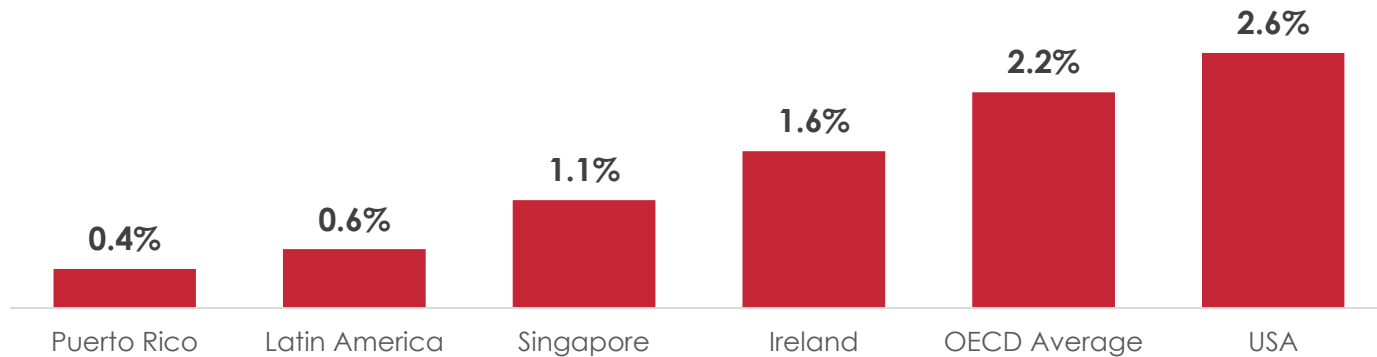
Source: PR Department of Labor and Human Resources.

Both total salaried and government employment grew between 2001 and 2004.

PR-2025 Context



R&D Spending as % of GDP - 2001

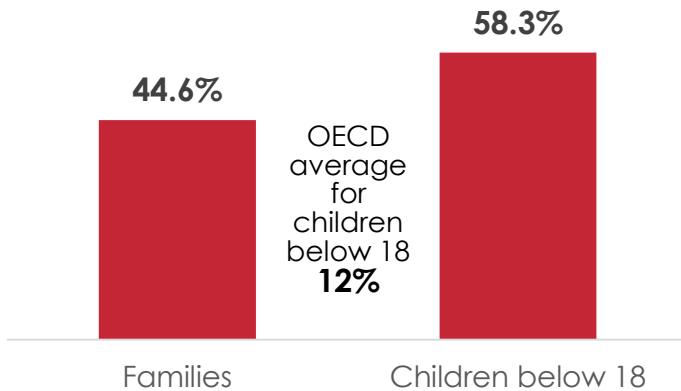


A Public Policy on Science and Technology had been adopted in 1996 with specific goals for increasing R & D spending, but it remained very low when compared to other jurisdictions.

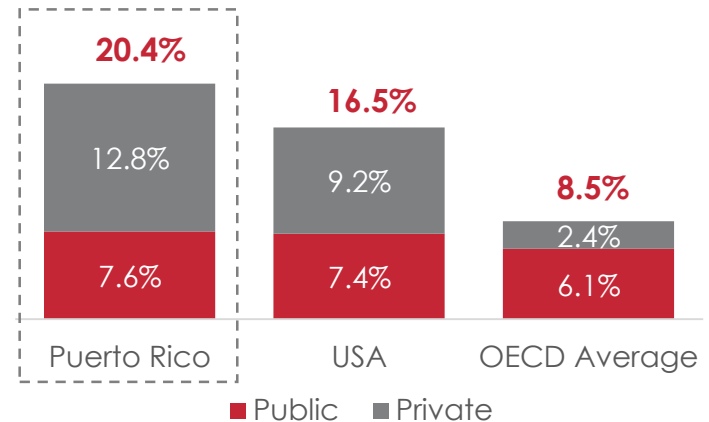
PR-2025 Context



Families and children living in poverty
% living below national poverty line, 2000



Health Expenditures as a % of GNP
2000



Poverty was a major concern in the early part of last decade, as was the health system, that was consuming large amounts of public fiscal resources.

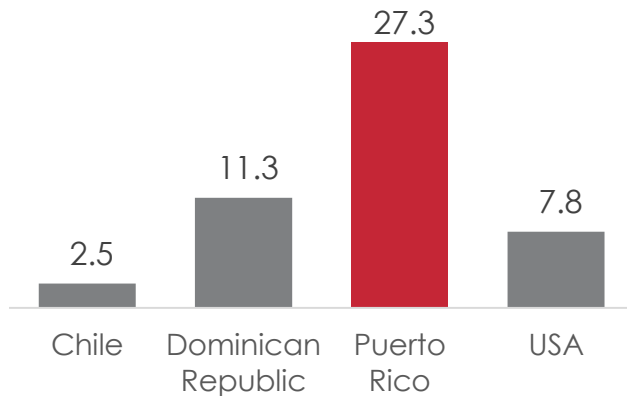
PR-2025

Context



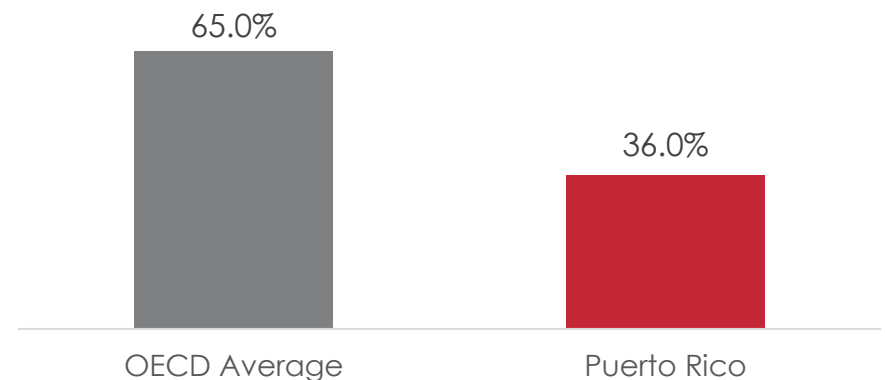
Mortality Rates due to AIDS

Number of deaths per 100.000 population, 2000



% of Education budget on teaching staff salaries

2001



Some health indicators reflected serious problems and the Department of Education, although still with an enrollment of over 600,000 was showing signs of serious deterioration.

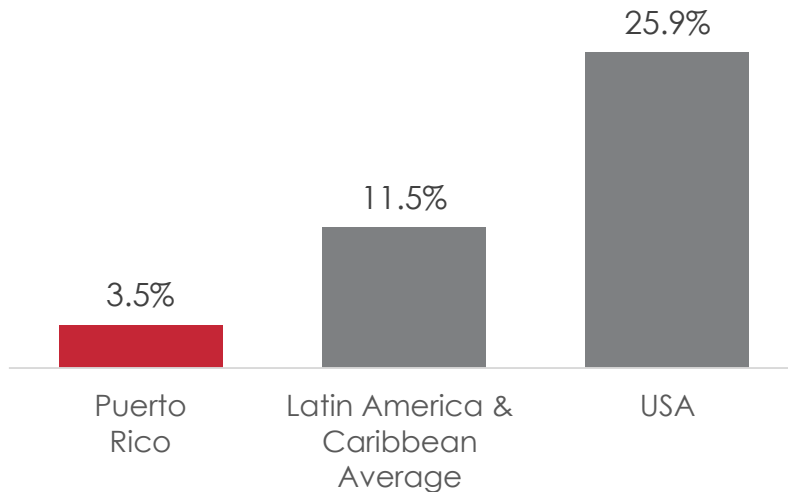
McKinsey was asked to assess the Department and come up with recommendations.



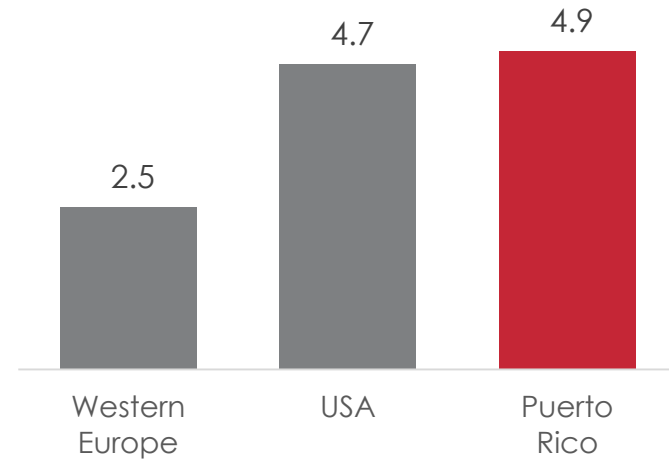
PR-2025

Context

Nationally Protected Areas
% of total land area, 2002



Waste generated
Pounds per person per day, 2002



Environmental and infrastructure issues were present and the Calderón Administration directed efforts to deal with them. The PRASA privatization effort failed.

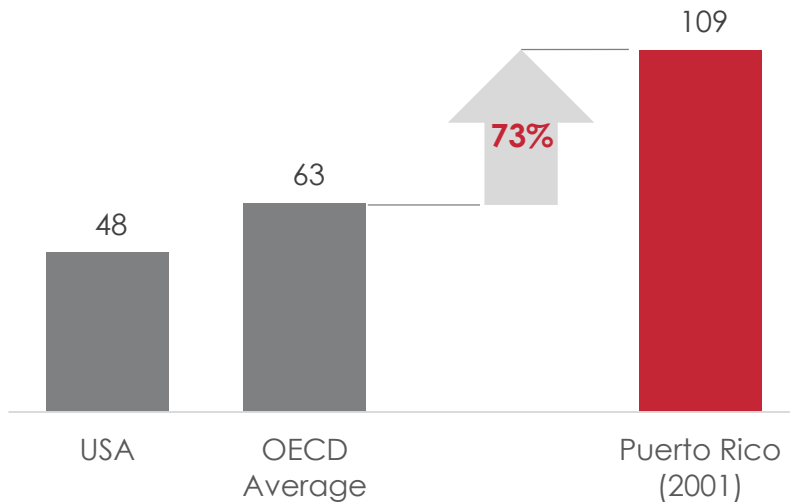
PR-2025

Context



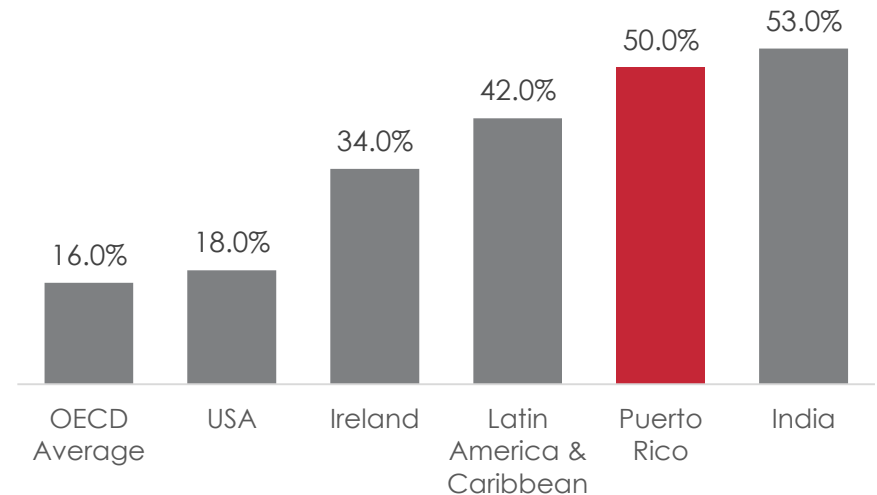
Industrial Electricity Costs

Cents per MWh, 2003 (unless stated otherwise)



Water unaccounted for

As a % of total water produced, 2002



The cost of energy was already a major issue with cost in Puerto Rico being well in excess of the U.S. and the OECD countries.



SOME KEY RECOMMENDATIONS



Some key recommendations

ECONOMIC VISION

In 2025, Puerto Rico is a prosperous, productive, and innovative society, capable of generating knowledge with an entrepreneurial spirit and supported by an efficient public sector.

Globally integrated, Puerto Rico creates a fertile and dynamic environment for internal growth and provides its population with ample opportunities to reach its potential and to equitably share the benefits of such growth potential. This results from:

- A country that fosters entrepreneurial activity;
- A fiscal policy that facilitates and encourages productivity, income generation, and savings;
- A legal framework that protects the balance between production and natural wealth;
- Knowledge and technology are the main drivers of the economy;
- An agile, accessible, and reliable public system of economic, social, and geographical information.

Economic development increases profits, reduces unemployment, inequality, and poverty rates, allowing all members of society to achieve their full potential using their knowledge and talent.

Puerto Rico offers workers, entrepreneurs, and investors (local and foreign) the most competitive location to generate wealth in the Americas, in terms of:

- Human capital, knowledge and productivity;
- Quality of life;
- A natural environment capable of sustaining economic activities;
- A built environment and technology;
- Social harmony and professional ethic;
- Political and legal stability;
- Access to capital;
- A fair regulatory framework and fiscal policy.

Some key recommendations



In the Puerto Rico 2025 Report

Economic Development

- Launch a coordinated campaign, with the support of all public and private organizations (like the *Illinois Coalition* and similar entities in other locations) to double international R&D investment in Puerto Rico within the next 2 years, and reach the US and European average within 5 years.
- ...appoint a commission bringing together leaders of all existing initiatives to agree on a unified S&T policy.
- Create a taskforce bringing together the JRT, telecom and IT providers, economic development and business interests to develop a strategic plan to catapult Puerto Rico's ICT infrastructure to world-leading status:
 - Identify relative infrastructure gaps and weaknesses.
- ...put in place a permanent coordinating team to track and evolve Puerto Rico's international image
- Involve a cross-section of business and community leaders, in addition to representatives from the main image-building agencies (PRIDCO, PromoExport, Tourism, Convention, Rums, etc.)



Some key recommendations

In the Puerto Rico 2025 Report

Economic Development

- Focus on Puerto Rico's fundamental assets (human capital, infrastructure, stability, environment, culture), and not so much on transient factors like low costs and tax incentives.
- Bring together a taskforce of business leaders to initiate a comprehensive review of Puerto Rico's investment promotion organizations and processes
- Building on the work of PromoExport and the Exporters' Council, bring together a taskforce of business leaders to initiate a radical expansion of Puerto Rico's export activities.



Some key recommendations

In the Puerto Rico 2025 Report

Social Issues

- Mobilize the combined assets of government, business and communities to launch an all-hands effort to support the unemployed in accessing the information and skills they need to find and secure jobs.
- Provide support and incentives to non-profit organizations to create more job opportunities.
- Reform social-assistance programs to encourage employment.
- Encourage saving and asset building among low-income populations.
- Organize a multi-disciplinary task force (Education, Health, Public Safety, Family, Sports) to address three objectives:
 - Guarantee all children access to high quality public primary education.
 - Develop multi-agency plans to guarantee the provision of important health and nutrition enablers.
 - Develop multi-agency plans to provide for the education of special-needs students.
- Building on the recent studies undertaken by the Department of Education, launch a comprehensive overhaul of the financial structure and management of the education system.

Some key recommendations



In the Puerto Rico 2025 Report

Social Issues

- Bring together a public/private taskforce on crime prevention that will dedicate resources to defining the role that citizen groups, as well as each citizen, can play in crime prevention efforts in Puerto Rico.
- Encourage non-governmental organizations, public and private entities tasked with the development of crime prevention programs to share information on their work to raise awareness.
- Bring together the various law enforcement agencies to improve collaboration and sharing of information and best practices across agencies and with international counterparts.
- Develop a juvenile criminal justice plan.

Some key recommendations



GOVERNMENT

- In the context of the larger review of regulatory burdens that hinder business growth, undertake a special review of the regulations and government processes that act as a deterrent to small business start-up and growth.
- Review all government procurement processes to identify areas where it may be made easier for local SMEs to win government business:
 - Survey local SMEs to understand what local business they feel excluded from.
- Create a public/private commission to:
 - Conduct an independent review of each public entity (central, municipal, public authorities) to identify areas of obsolescence, overlap and inefficiency and make recommendations to increase the agility of each entity.
 - Implement comprehensive tax reform, shifting the focus from incremental revenue generation to economic development and ease of administration.

Some key recommendations



GOVERNMENT

- Rationalize unproductive subsidies distorting competition and resource allocation in key economic sectors.
- Reinforce regulatory mechanisms overseeing use of public/private power to minimize abuses and to adapt it to the changing needs of society.
- Promote the observance of standard international behavior codes and ethical norms by both public and private office holders. Examples would include the United Nations Code of Behavior for law enforcement officers; the principles of medical ethics in the health profession; the International Code of Behavior for public officials, among others.

Some key recommendations



CULTURE, ENVIRONMENTAL AND INFRASTRUCTURE

- Establish a public commission that will:
 - Study the potential economic impact of cultural industries, including potential exports of arts and crafts, music, and film
 - Evaluate the effectiveness of current public funding and other support programs for artistic and cultural activities and advocate appropriate reforms.
- Create a public/private commission consisting of music industry performers, technicians, producers, distributors and associations, along with government ministries to:
 - Study the potential export market for music created and/or produced in Puerto Rico
- Create and enact into law a unified set of municipal, regional and island-wide land-use plans, which are sufficiently detailed to guide and facilitate development:
 - Form an interdisciplinary group led by the Planning Board to guide the process of creating the integrated plans

Some key recommendations



CULTURE, ENVIRONMENTAL AND INFRASTRUCTURE

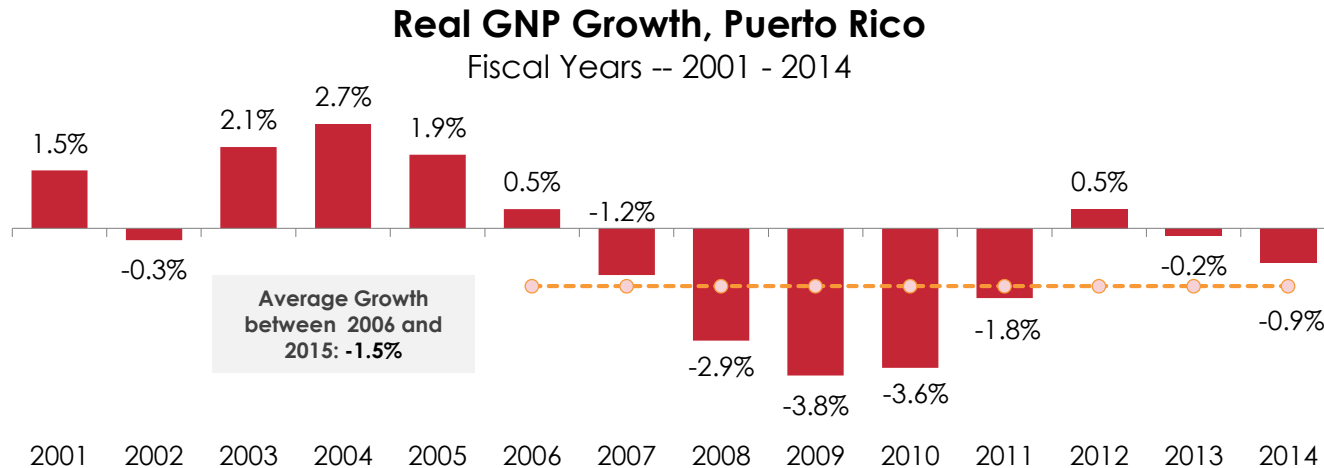
- In parallel with the completion of the integrated land-use plan, establish a formal communication process to ensure broad community input to, and understanding of the new land-use plans and permitting process.
- Develop a long-term comprehensive water and sewage management plan:
 - Create an interdisciplinary taskforce bringing together all relevant public entities, community and business representatives.
- In conjunction with the Economic Strategy Taskforce, develop a long-term plan for establishing Puerto Rico as an air passenger and cargo hub on the scale of major US and global cities:



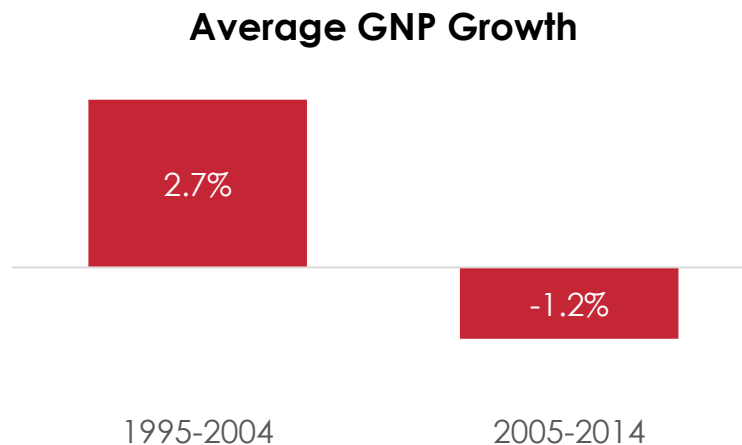
THE ECONOMY 2004-2015



The economy 2004-2015

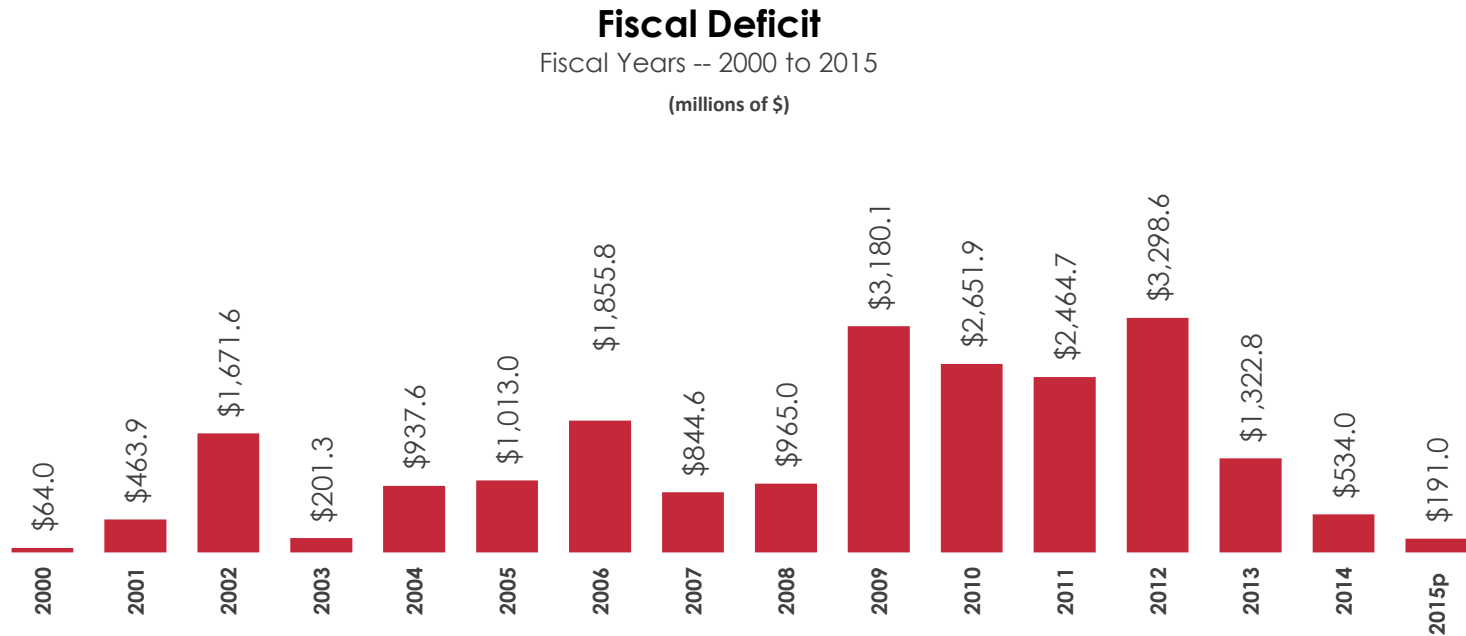


Source: Puerto Rico Planning Board (2015). *Statistical Appendix*.



Beginning in 2005 a downward trend in GNP began, changing significantly the economic context that characterized the previous period. Puerto Rico's economy became a totally different one. A major change in direction occurred beginning in 2006.

The economy 2004-2015



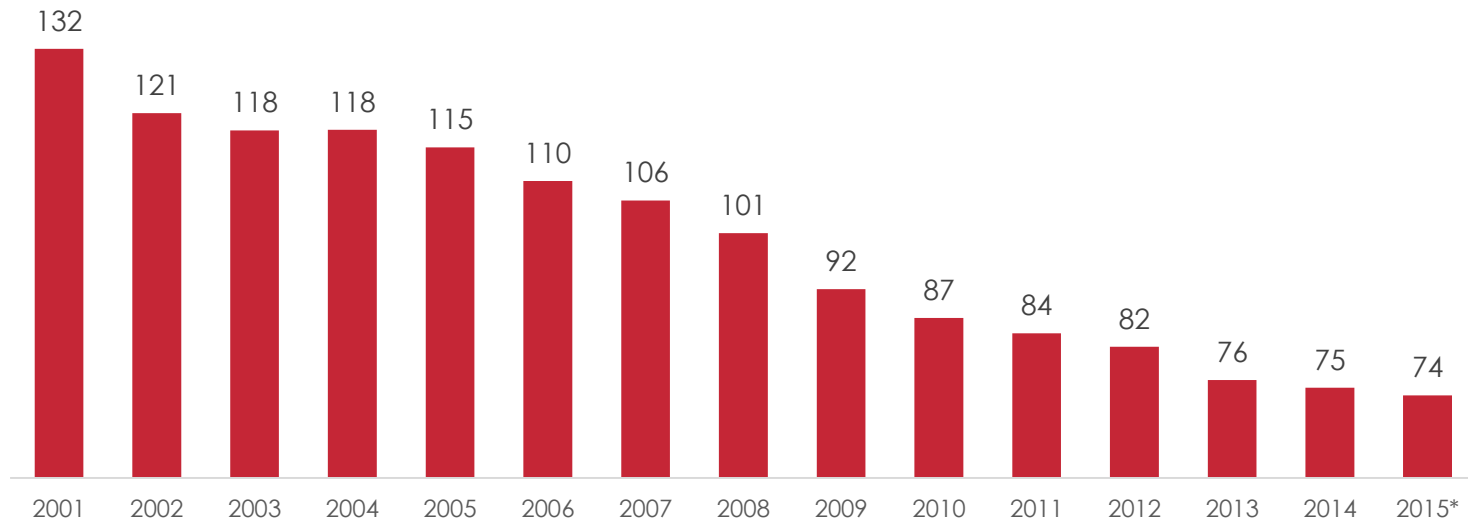
Sources: Office of Management and Budget (2015). *Budget Petition* (various years). Office of Management and Budget (2015). *Approved Budget Fiscal 2015*. The fiscal 2015 statistic corresponds to the estimated cash flow deficit upon the fiscal year's closing (May 20, 2015).

- The government's fiscal situation worsened significantly, particularly after 2009, until last fiscal year.
- A major warning was issued by rating agencies in 2005 primarily because of the growth in appropriations debt.



The economy 2004-2015

Manufacturing Employment

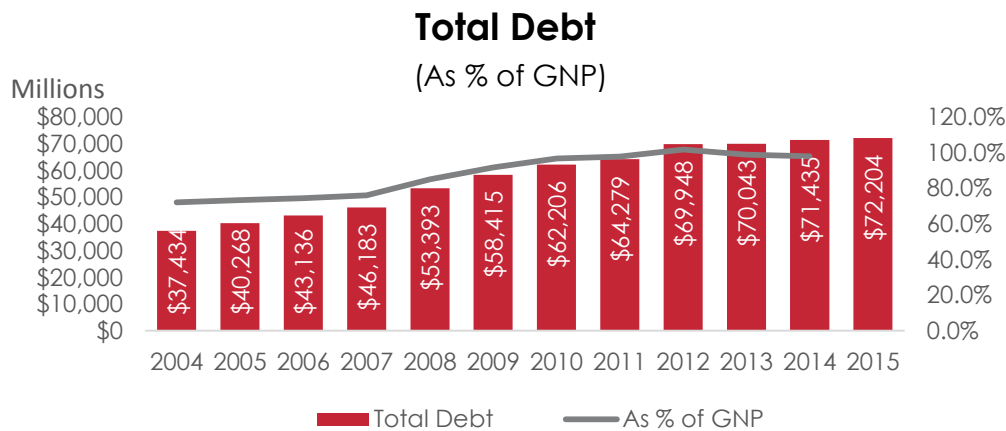


Source: PR Department of Labor and Human Resources (2015). Current Employment Statistics: Nonfarm Employment (Seasonally Adjusted). *Yearly average includes up to April 2015

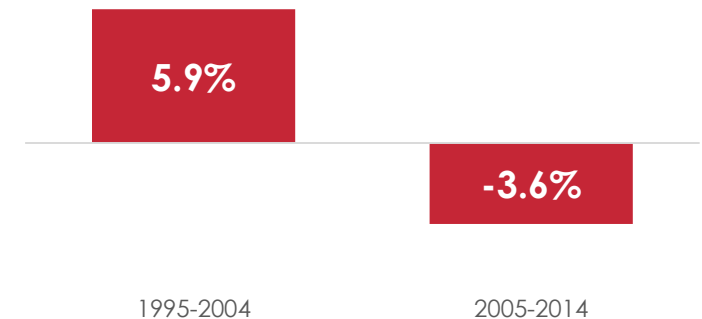
- Manufacturing employment, a key indicator, fell from 118 in 2004 to 74,000 in 2015, reflecting a major restructuring of the Island's economic structure and specifically its manufacturing sector.



The economy 2004-2015



Average Total Gross Domestic Investment Annual Growth



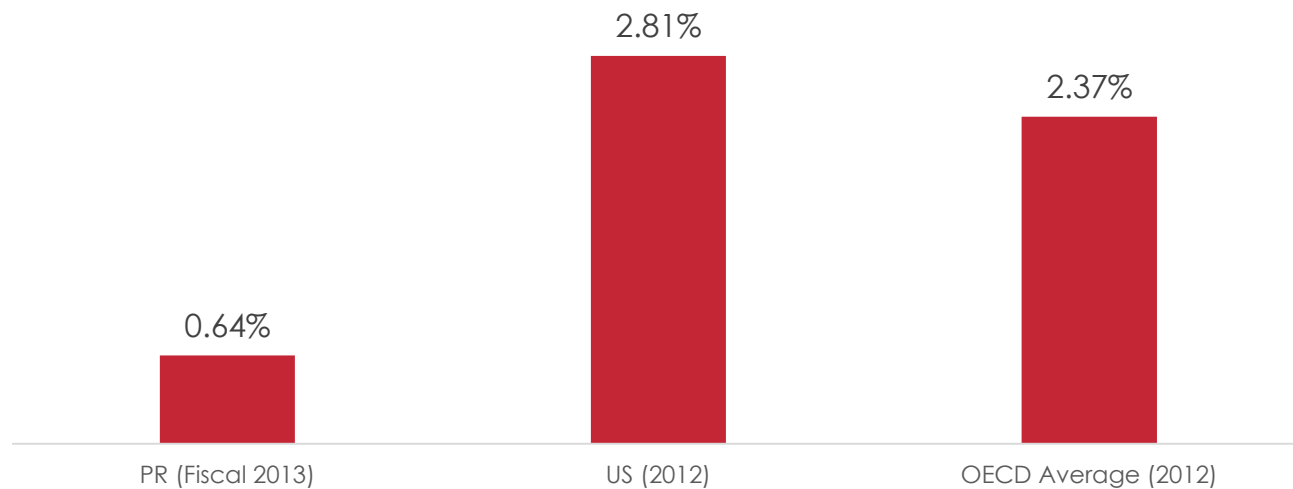
Source: Office of Management and Budget (2015). Budget petition for fiscal 2009, 2010, 2011, 2012, 2015; Government Development Bank; JPR Planning Board, Statistical Appendix (2015); Estimates by Estudios Técnicos, Inc.

- Debt in the amount of \$42 billion was issued between 2001 and 2012.
- As debt increased, investment fell, a combination that spells disaster as far as economic growth is concerned.

The economy 2004-2015



Spending on Research and Development as % of GDP/GNP for Selected Regions



Sources: PR Statistical Institute (2015). *Encuesta Sobre Ciencia y Tecnología: Investigación y Desarrollo*. OECD Stats Database (2015). *Main Science and Technology Indicators*.

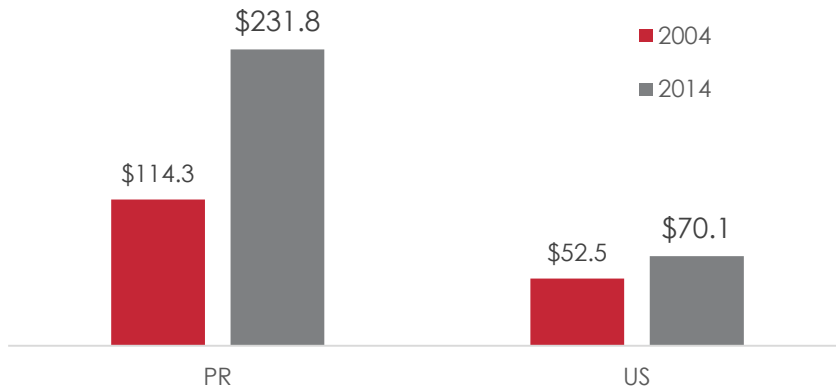
- Spending on R & D grew and more attention was paid to S & T issues with the creation in 2004 of the Science, Technology and Research Trust Fund.

The economy 2004-2015



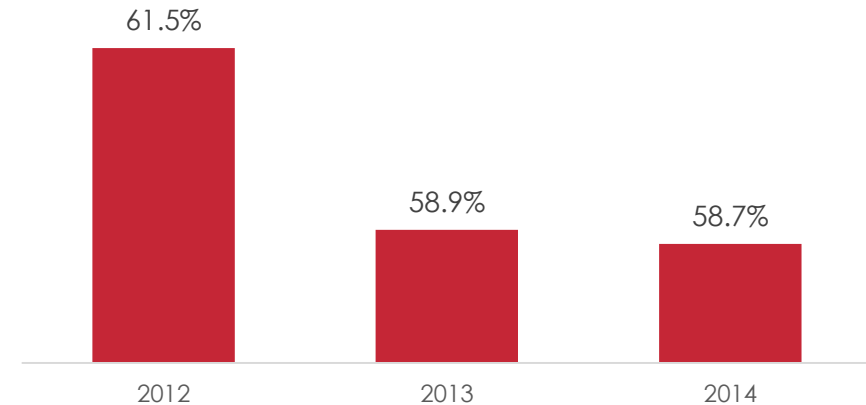
Electricity Rates for Selected Regions 2004 & 2014

(dollars / MWh)



Sources: Puerto Rico Electric Power Authority (2015). US Energy Information Administration (2015).

Non-Revenue Water in PRASA, as a Percentage of Total Water Generation



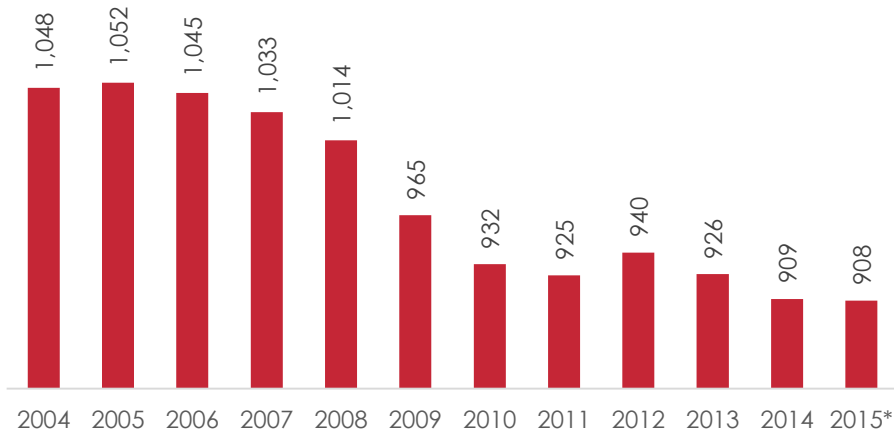
Source: Puerto Rico Aqueduct and Sewer Authority (2015). *Final Report of Consulting Engineers 2014*.

- PREPA and PRASA problems became worse in the period since 2004 and the cost of electric power became a major issue in terms of Puerto Rico's competitiveness.

The economy 2004-2015

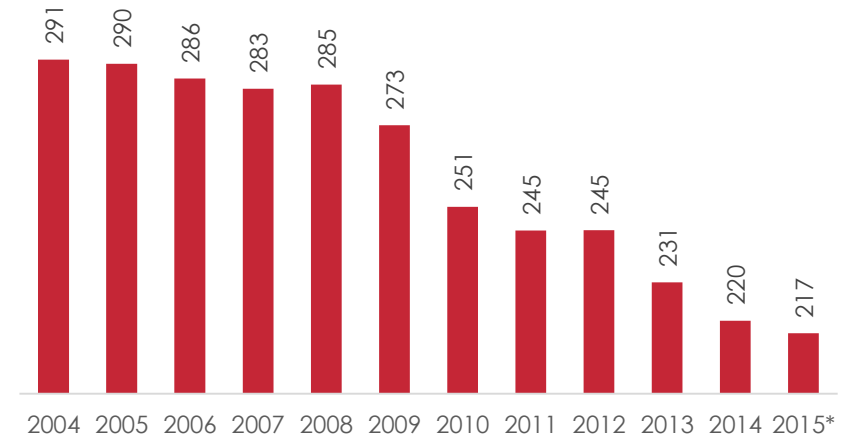


Non-Farm Salaried Employment



Source: PR Department of Labor and Human Resources (2015). Current Employment Statistics: Nonfarm Employment (Seasonally Adjusted). *Yearly average includes up to April 2015.

Public Employment



Source: PR Department of Labor and Human Resources (2015). Current Employment Statistics: Nonfarm Employment (Seasonally Adjusted). *Yearly average includes up to April 2015. Excludes Federal Government employment.

- The employment issue became critical with some 140,000 salaried jobs lost since 2004. Prospects for recovering these jobs are not positive given actual and projected growth rates in GNP.

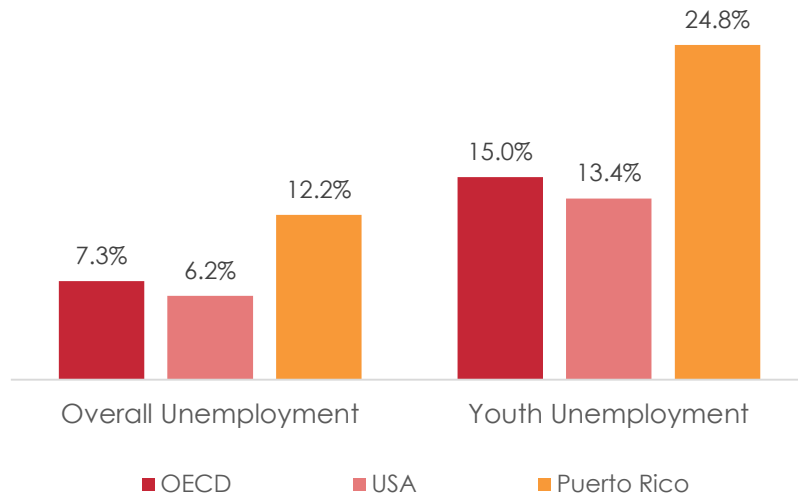


SOCIAL INDICATORS

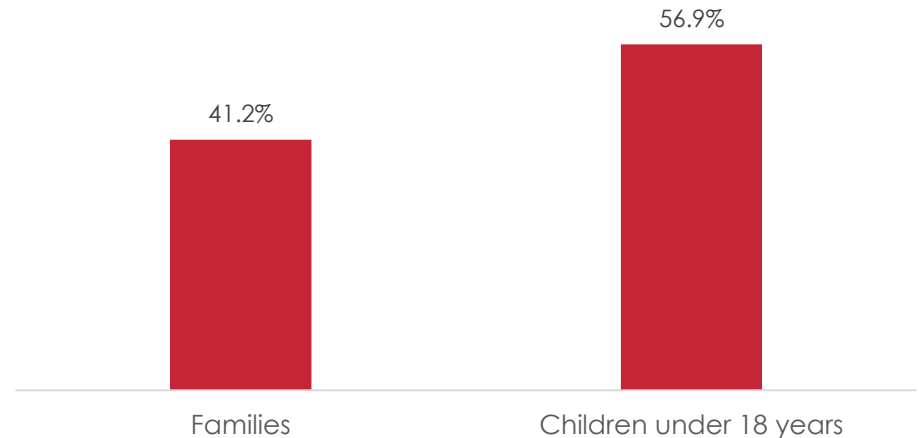


Social Indicators

Overall Unemployment and Youth Unemployment 2014*



Poverty Rate for Puerto Rico (2013)



Source: OECD Library 2014 unemployment. *PR Department of Labor and Human resources April 2015 unemployment. Puerto Rico youth Unemployment rate is for the ages 16-24 for April 2015. OECD and US rates are for 2014, with youth unemployment for the ages of 15-24

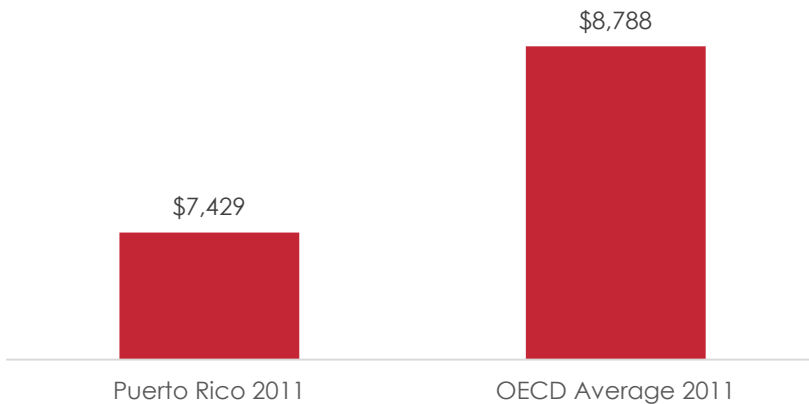
Source: U.S. Census Bureau, 2009-2013 5-Year American Community Survey

- Poverty rates improved slightly from earlier numbers but youth and overall unemployment remain at essentially the same levels.



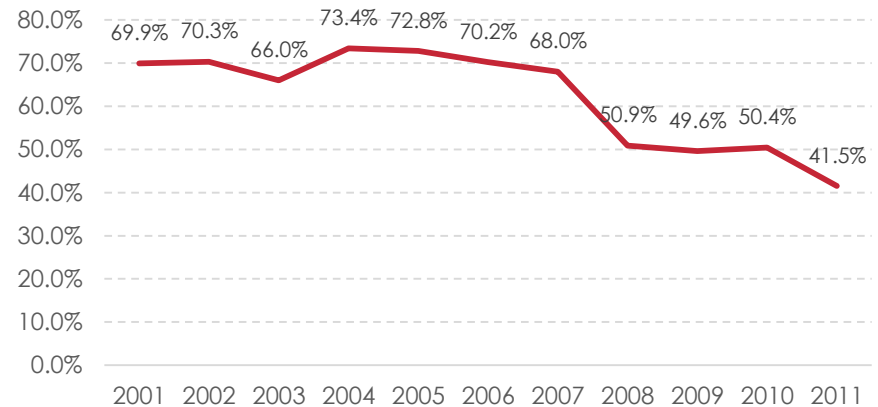
Social Indicators

**Public Expenditure per Student in USD
Elementary and Secondary -- 2011**



Source: National Center for Education Statistics (2015). *Elementary and Secondary School Information*.

**Expenditures in Instruction, as % of
Education Expenditures
2001-2011**

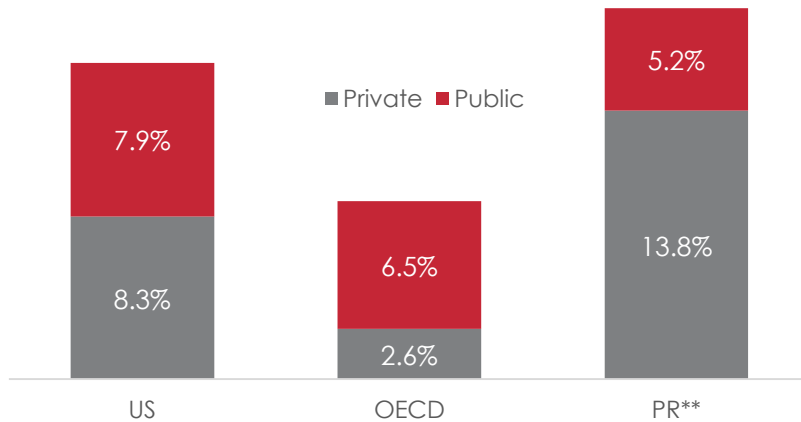


Source: National Center for Education Statistics (2015). *Elementary and Secondary School Information*.

- A worrying condition with respect to public education is the cost per student, not too far below that of the U.S. and the fact that a smaller proportion of the cost goes towards teaching, below what it was earlier.

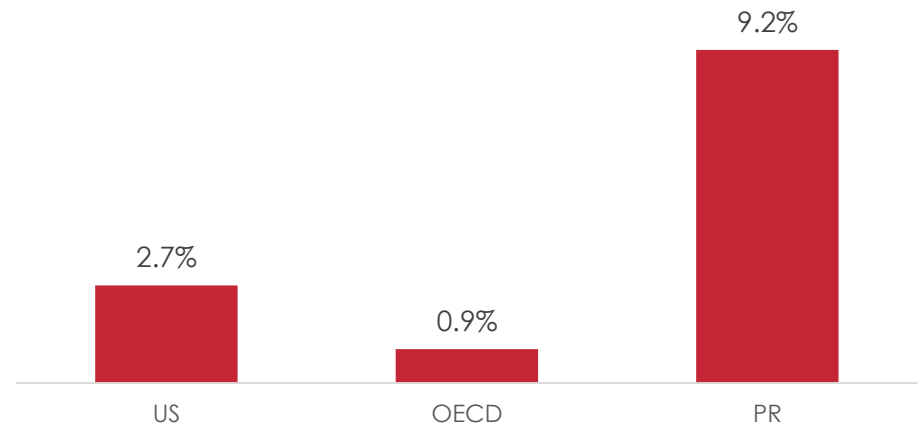
Social Indicators

**Health Expenditures as % of GDP
2011***



Source: OECD Library, data for 2011 for US and OECD average. Office of Management and Budget (2015). *Puerto Rico data is for fiscal 2014
**Health spending as % of GNP

**Mortality rate for AIDS
2010**



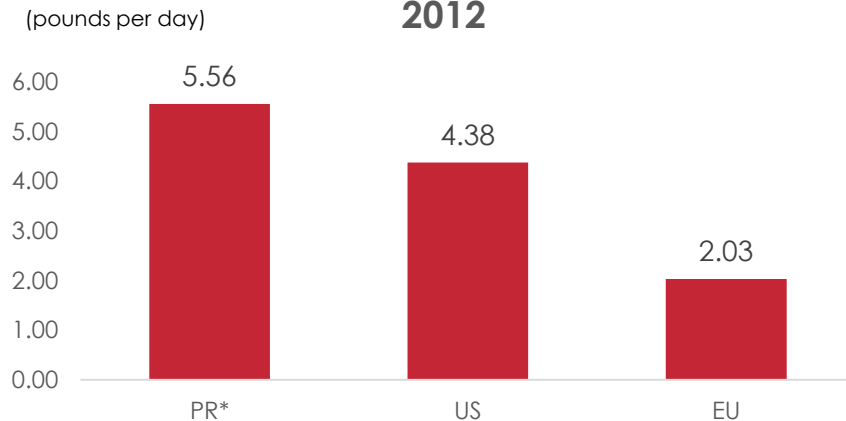
Source: Health Report for Puerto Rico (2014). PR Department of Health.

- Health expenditures in Puerto Rico as percent of GNP continue to exceed those of the U.S. and the OECD countries and AIDS mortality rates continue to exceed those of the U.S.



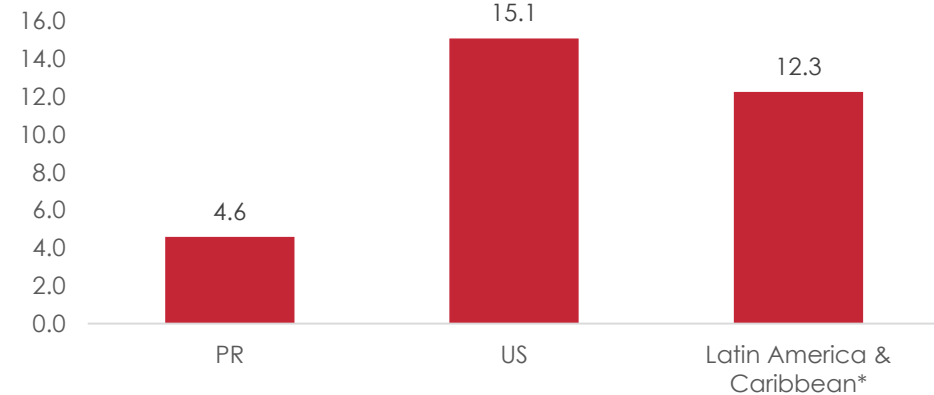
Social Indicators

Daily Per Capita Waste Generation for Selected Regions 2012



Sources: PR Solid Waste Authority (2015). US Environmental Protection Agency (2015). EuroStat (2015).

Percentage of Protected Maritime & Terrestrial Territory 2012



Source: World Bank (2015). *World Development Indicators*. *Some jurisdictions omitted due to lack of available data for 2012.

- Per capita waste generation in Puerto Rico exceeds that of the U.S. Given the limitation of space to dispose of such waste and the critical state of many of the landfills, waste disposal has become a key problem.



FINAL COMMENTS



Final comments

NEW CHALLENGES

- Many of the existing problems were either present or beginning to make themselves known in 2003/2004: fiscal issues, poverty, unemployment and some others.
- Compared to 1995-2004, the period beginning in 2005 reflects not only a temporary change in rates of growth, but a totally different direction for the economy.
- There are new challenges that were not present or that were not foreseen:
 - The sudden decrease in population due to out-migration
 - The consequent aging of the population
 - The accelerated erosion of the productive base
 - Cuba's opening as of December, 2014
 - Absence of access to capital markets due to rating agencies' debt downgrades
 - Increased uncertainty from a rapidly changing and volatile external context



Final comments

IMPLEMENTING 2025

- Throughout the 2025 report what stands out is the insistence on private participation in public policy issues as the solution to a host of problems, among others:
 - Puerto Rico's promotional strategies
 - Export promotion
 - Stimulate R & D and adopt a S & T policy
 - Branding
 - Crime prevention
 - Institutional reform
 - Cultural development

Final comments

IMPLEMENTING 2025



- Some recommendations have been implemented fully or partially.
 - The Land Use Plan for Puerto Rico is being prepared, but the process has not been as inclusive as 2025 suggested it be
 - Integrating data bases for juvenile delinquency has recently been completed through the Juvenile Information Sharing System
 - Governor García Padilla created a Commission on cultural development and it did analyze culture as an economic sector as suggested in PR 2025
 - A Committee was created by law to develop and manage Puerto Rico's Brand, it is still not operational
 - Legislation to rationalize subsidies has been submitted in 2015

Final comments



NEXT STEPS

Puerto Rico has a long way to go to be near the 2025 Vision for the economy. In order to achieve this vision, we need to:

- Develop a tax system that stimulates investment and economic activity, something that the recently approved tax legislation does not do.
- Overhaul Puerto Rico's institutional framework which is mostly obsolete, and which has generated the widely recognized absence of the capacity to execute strategies.
- Rethink the Island's promotional strategies in line with changing global conditions, including renewed efforts to stimulate the intangible economy.
- Improve transparency in government as recently suggested by the Director of the Statistics Institute and others, including an accessible, agile and timely statistical system.
- Have the private sector assume a more pro-active role in determining Puerto Rico's economic agenda.
- Increase internal linkages through explicit policies that stimulate the creation of local supply chains.
- Insert risk management considerations in economic policy-making in recognition of a changing and uncertain external context.
- Make better and more effective use of the PPP instrument, created in 2009.

Thank you



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