

Economist: Time for PR control board

By CB Online Staff, Saturday, October 25, 2014



Economist Arturo Porzecanski has added his voice to scattered calls in Washington for Congress to consider creating a federal oversight board to manage Puerto Rico's fiscal crisis.

“A renewed slide in investor confidence, on the heels of worsening economic and budgetary trends in Puerto Rico, raises the specter that in the absence of enlightened political leadership in San Juan, the U.S. Congress may soon have to establish a federal oversight board to manage the Commonwealth's grave fiscal situation,” Porzecanski said in column for The Hill.

The Uruguayan, director of the International Economic Relations Program at American University's School of International Service in Washington, D.C., argued that “investors have become pessimistic,” pointing out that Puerto Rico's junk rated bonds have slumped while investment-grade municipal paper has rallied in recent weeks. Meanwhile, Puerto Rico's borrowing costs have surged, with a syndicate of banks getting a 7.5 percent interest rate to buy \$900 million in short-term notes from the commonwealth earlier this month. Benchmark issuers pay well less than 1 percent and the commonwealth has generally paid in the 1 percent to 2 percent range for such issues.

“The market action suggests that sophisticated investors are beginning to realize that Puerto Rico's economic and fiscal situation is unlikely to turn around anytime soon,” he said.

A key gauge of Puerto Rico's economy posted another drop in August, remaining in negative territory for a 22nd straight month and settling at its lowest level in two decades as the island struggles to pull out of a recession dating back to 2006.

The Government Development Bank's Economic Activity Index closed fiscal 2014 (ended in June) down 2.9 percent compared to the previous fiscal year. The EAI had returned to growth in December 2011 for the first time since Puerto Rico's recession began in 2006. It showed small but consistent year-over-year gains for nearly a year before beginning to retreat again in December 2012.

Unemployment rose to 14.1 percent in September, higher than any U.S. state and far above the national average of 5.9 percent. The island's labor participation rate, meanwhile, dropped back below 40 percent last month.

“Indeed, the fundamentals of Puerto Rico resemble those of New York City in the mid-1970s and of other municipalities on which a financial control board has been imposed,” Porzecanski said. “NYC lost a chunk of its middle class and 16 percent of its jobs between 1969 and 1977. It was also saddled with too much debt – Puerto Rico's tax-supported debt amounts to nearly \$12,000 per inhabitant, twelve times the median of state debt per capita in the continental United States – and NYC's access to financing came to an end when the leading banks resisted underwriting any more bonds.”

The economist is sharply critical of the administration of Gov. Alejandro García Padilla for a “shortfall of political skill and forceful leadership.”

“His plan to balance the budget by tinkering with revenue measures and curbing employee compensation, while avoiding layoffs and the restructuring with intent to privatize inefficient state-owned companies, is insufficiently aggressive,” Porzecanski said. “Three months into the new fiscal year, the plan is already falling short. On the funding side, meantime, the strategy is to pledge ever-greater portions of earmarked taxes to back new indebtedness, despite undermining the obligations that are not similarly supported.”

He argued García Padilla's recent shuffling of his fiscal team — with Melba Acosta presiding the GDB and Juan Zaragoza replacing her in the Treasury Department helm — doesn't represent an improvement.

“The time is rapidly approaching when the U.S. Congress may well have to take matters in its own hands and, empowered by Clause 2 of the Constitution, establish a financial control board to take the unpopular austerity and reform measures that circumstances warrant,” Porzecanski said.

He is the second Washington figure in less than a month to go public with the idea.

Last month, former high-ranking U.S. State Department James K. Glassman made a similar call in pushing for more attention from Washington on Puerto Rico's debt crisis.

“It's about time American officials criticized what's happening in Puerto Rico, a U.S. territory since 1898,” Glassman, former U.S. undersecretary of State for Public Diplomacy & Public, said in a column published in the Capitol Hill newspaper Roll Call “If action isn't taken soon — either by the Obama administration or the Congress — U.S. taxpayers could end up holding the bag.”

Glassman said the federal government should establish a financial control board, similar to the one that was set up in the Clinton administration and ran the affairs of the District of Columbia for six years. The board had authority over spending, borrowing, hiring, and contracts.

“Puerto Rico is no longer a disaster waiting to happen. The disaster is happening. The New York Fed should be ringing the alarm bells, and Congress and the White House should be laying the groundwork for a control board,” he wrote.

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