

Puerto Rico: Six Months After Hurricane Maria

“Puerto Rico Needs Economic Recovery First, Not “Structural Reforms” and Debt Service Extraction”

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Six months after Hurricane Maria devastated Puerto Rico, the island is still a long way from recovery. But perhaps most disturbing is the inadequacy of US federal support, and the unrealistic fiscal plan that has been put forth for the next six years.

In the limited time here, I want to focus on the 2018 fiscal plan, some version of which is likely to be approved in the near future by the Financial Oversight Management Board (FOMB), and is therefore likely to have a major role in shaping Puerto Rico’s economic future.

First, it is important to understand that Puerto Rico was already in a prolonged, deep slump for a decade prior to the hurricane. And the first fiscal plan approved by the FOMB in 2017 was a plan without a future for Puerto Rico. It implied another lost decade, and probably more, without economic growth. So, even before the hurricane hit, Puerto Rico was headed for an economic experience that is rare in the history of modern capitalism: more than 20 years without economic growth. Unemployment was already almost 12 percent and about half of the population was living in poverty. Child poverty was at 58 percent, about three times that of the United States. And it was obvious that Puerto Rico’s debt was unsustainable.¹

Then came the hurricane, which destroyed much of Puerto Rico’s already crumbling infrastructure, with some \$94 billion in damages, according to the governor’s estimates.

¹ Merling, Lara, Kevin Cashman, Jake Johnston, and Mark Weisbrot. 2017. “Life After Debt in Puerto Rico: How Many More Lost Decades?” Washington, DC: Center for Economic and Policy Research. July.
<http://cepr.net/publications/reports/life-after-debt-in-puerto-rico-how-many-more-lost-decades>

Now we have a new fiscal plan, which purports to show a significantly better future than the pre-hurricane plan. The economy is forecast to have positive real GNP growth for 5 years, after a big plunge for 2018.² In this plan, there is a cumulative budget surplus of \$3.4 billion over the next six years.³

How is this possible? Did Puerto Rico receive so much federal aid that its economic future has been transformed? No, that didn't happen: in fact, expected post-hurricane assistance has only covered about half of the estimated damage, and has been slow to materialize.⁴

The answer to this puzzle is mostly contained in a section of the fiscal plan on “structural reforms.” Over the next six years, these “structural reforms” are expected to yield \$13 billion in new savings to the government, or about 3 percent of GNP during this period.⁵ These are reforms such as a “New Government Model” that reorganizes and shrinks the executive branch; as well as spending cuts in health care, corrections, education, and other government services.⁶ But there is little evidence that such reforms would produce the alleged efficiency or revenue gains. If even one quarter of the fiscal surplus that the plan projects from these “structural reforms” does not materialize, then the projected \$3.4 billion fiscal surplus over the next six years disappears. And for most of the spending cuts, we would expect a further negative impact on economic growth, including a multiplier effect.

Furthermore, a separate plan for the privatization of PREPA (the government-owned electric utility) is a risky venture, especially in consideration of Puerto Rico's past experience with privatization; in particular, the privatization of water services turned out to be a terrible failure.⁷

And there is no basis in the research on economies damaged from cyclones that their long-term growth trend would increase after such damage. This includes one study that looked at 6,700 cyclone events

2 Cumulative real growth is still projected to be negative, at -3.5 percent for the six years; however, this is considerably more optimistic than the -11.25 percent growth for these years projected by the 2017 fiscal plan.

3 Puerto Rico Fiscal Agency and Financial Advisory Authority (FAFAA). 2018. “New Fiscal Plan for Puerto Rico.” February 12. <http://www.aafaf.pr.gov/assets/newfiscalplanforpr-02-12-2018.pdf>

4 Russ, Hilary. 2018. “Puerto Rico asks Congress for help with delayed disaster relief loan.” Reuters, February 27. <https://www.reuters.com/article/us-usa-puertorico-liquidity/puerto-rico-asks-congress-for-help-with-delayed-disaster-relief-loan-idUSKCN1GB33R>

5 There are also revenue losses or costs from other reforms, so the net savings are less; the \$13 billion is the total from measures that are projected to have a positive fiscal impact. FAFAA (2018), 38.

6 Ibid, 53–64.

7 See Merling, Lara. 2018. “Privatization Won't Fix Puerto Rico's Broken Power Utility.” NACLA, February 1. <https://nacla.org/news/2018/02/01/privatization-won%E2%80%99t-fix-puerto-rico%E2%80%99s-broken-power-utility>

over almost 60 years, and found that for all countries, regardless of initial income levels and relief efforts, growth trends were negatively affected for at least 20 years.⁸

Another huge part of the present state of denial is the refusal to recognize the need for debt cancellation. A debt that was not payable before the hurricane damage is even less sustainable now. Economists Pablo Gluzmann, Martin Guzman, and Joseph E. Stiglitz estimated that even before the hurricane, Puerto Rico would still need debt cancellation of between 47 and 80 percent of the public debt stock — and that was under the overoptimistic assumptions of the 2017 fiscal plan.⁹

In sum, the first priority for the Puerto Rican economy must be a return to economic growth. And that is precisely what the new fiscal plan, despite its wildly overoptimistic assumptions, cannot provide. After the economy returns to growth, then we can talk about what “structural reforms” might help sustain that growth. But the fiscal plan’s continued austerity and the attempt to squeeze debt service out of this devastated economy is a recipe for disaster. It makes no economic sense, especially when the economy is caught in a trap of falling demand, shrinking population (projected 19 percent decline from the hurricane to 2023, after falling 10 percent in the decade prior), and creditors still menacing the recovery with legal actions.¹⁰ If implemented, this plan will most likely lead to an even more prolonged economic decline than was projected by the first (2017) fiscal plan.

8 Hsiang, Solomon M., and Amir S Jina, “The Causal Effect of Environmental Catastrophe on Long-run Economic Growth: Evidence from 6,700 Cyclones,” National Bureau of Economic Research (2014).

9 Gluzmann, Pablo, Martin Guzman, and Joseph E. Stiglitz. 2018. “An Analysis of Puerto Rico’s Debt Relief Needs to Restore Debt Sustainability” Espacios Abiertos. January. <http://espaciosabiertos.org/wp-content/uploads/2018/01/Final-Report-DSA-2018.01.pdf>

10 FAFAA (2018).