

Puerto Rico's economy starts coming out of depression

Governor announces historic Economic Development Summit between Puerto Rico and New York



Luis G. Fortuño
Governor of Puerto Rico



José R. Pérez-Riera
Economic Development &
Commerce Department Secretary

By John Marino
pages 14-19

TOP STORY

Aggressive expansion to U.S. Hispanic payment-processing market by Paytech
page 2

INSIDE

Fortuño raises eyebrows with bid to exempt natural gas from Jones Act

page 4

Smooth sailing for bill to protect local business from stateside competition

page 8

Private-security industry offers guards, high tech, to help authorities fight crime

page 22

SPECIAL REPORTS

CARIBBEAN BUSINESS
Special Report

Fastest Growing Companies

CARIBBEAN BUSINESS
Special Report

Innovations in Healthcare

February 16, 2012 Pages S1-S16



For up-to-the-minute local, national, international and economic news in English, go to

caribbeanbusiness.pr
now on



Historic Puerto Rico-New York Economic Development Summit set



Signs abound
Puerto Rico's
depression is
finally ending

BY JOHN MARINO
marino@caribbeanbusinesspr.com

While Puerto Rico's economy is finally approaching positive terrain, the administration of Gov. Luis Fortuño is pushing forward with new initiatives to help local businesses thrive and ensure that the island's recovery grows increasingly stronger.

One of the most compelling is the first Economic Development Summit between New York and Puerto Rico taking place next month that aims to foster partnerships between local

firms and New York-based minority companies to win large state and federal contracts, Economic Development & Commerce (DDEC by its Spanish initials) Secretary José R. Pérez-Riera announced during an exclusive interview with CARIBBEAN BUSINESS.

The event, a trailblazing initiative between U.S. jurisdictions, is backed by both Fortuño and New York Gov. Andrew Cuomo, who wants to improve the state's track record on providing contracts to minority firms.

There are billions of dollars in government contracts in New York City

and New York State available to minority firms, but many of the small minority firms in New York City and New York State lack the financial might, bonding capacity and experience to be able to bid on or handle large contracts. That is where the Puerto Rico firms come in, many of which have the experience, expertise and financial strength to handle such major contracts.

"There is a great tie between Puerto Rico and New York. We need to take advantage of that," Pérez-Riera said. "This is the beginning of integration between the Puerto Rico and

New York economies. We give them something they need, we take something we can't get without their help and ultimately we both benefit."

The New York-based minority companies together with the Puerto Rico companies will be bidding together. This will help these New York minority companies get involved in multimillion-dollar projects instead of just getting the tiny contracts they get now because of a lack of big projects. These government agencies together spend billions of dollars each year.

Continued on next page

Continued from previous page

The Puerto Rico-New York Economic Summit initiative is part of a central goal of the Fortuño administration to integrate Puerto Rico more fully into the global economy, a key strategy of its New Economic Model for Puerto Rico, but it will also help find work for local firms, especially construction industry related, that aren't working at full capacity here in Puerto Rico because of the island's long economic downturn.

The initiative will be aimed at all sorts of companies that can provide goods and services to the New York and federal governments, but it will have the largest immediate impact on construction firms, Gov. Fortuño's economic development chief said.

Each New York government agency will be making a presentation of the type of contracts they have or will be coming up and how to access the bidding process. There will be several networking opportunities with the officers of these agencies.

While the local economy is now moving in the right direction, it will take some more time for the overcapacity of homes and commercial buildings to be absorbed by the market, allowing for a new wave of construction investment to take place. So looking offshore for opportunities is key to the local construction industry's growth right now.

"We have extraordinary services to offer. We have highly qualified people who have the expertise, the bonding capacity and the financial strength to undertake projects that go above and beyond what we can offer in Puerto Rico right now," Pérez-Riera said. "There is no reason in the world why we shouldn't use those resources as an advantage to bring economic development to Puerto Rico."

While the effort can serve as a "bridge" for these firms to find work until local demand for their services increases, the administration envisions Puerto Rico transforming into a huge exporter of professional services, encompassing diverse fields such as engineering, architecture, legal services and financial services.

Puerto Rico not only has the expertise, but also its professional services are often priced below U.S. rates, giving local professionals a competitive advantage. Because locally owned



Saying that investors sense an economic turnaround on the island, Gov. Luis Fortuño is moving ahead with new initiatives to drive growth such as the first ever Economic Development Summit between New York and Puerto Rico that will take place next month.

firms qualify as minority firms, they have an added advantage in competing for government contracts.

In an effort to seize on this opportunity, Gov. Fortuño recently enacted the Economic Incentives for the Development of Puerto Rico Act, which provides incentives, including a 4% tax rate, for firms that export professional services from Puerto Rico. This adds to Puerto Rico's cost advantages in this area, the DDEC chief said.

"The work done outside Puerto Rico is going to generate revenue coming back to the island, but you need to get the work," Pérez-Riera said. "That is where this summit comes in."

The summit, which will take place March 15-17 in New York City, will gather together at least nine New York city, state and federal government agencies, Puerto Rico officials, and a large group of contractors from Puerto Rico and New York.

Participating agencies include the Metropolitan Transportation Authority (MTA) of the State of New York, the New York State Thruway, the New York State Transportation Authority, the New York State Dormitory Authority, the Port Authority of New York/New Jersey, the Empire State Development Corp., the U.S. General Services Administration (GSA), the U.S. Small Business Administration (SBA) and the U.S. Army Corps of Engineers. Several other city, state and federal agencies are interested in joining the effort.

Govs. Fortuño and Cuomo are slated to attend, and other participating officials include Pérez-Riera; Michael Garner, MTA chief diversity officer; Nick Lugo, president of the New York City Hispanic Chamber of Commerce and a member of Gov. Cuomo's Regional Economic Council; GSA Regional Administrator Denise Pease; Fernando Ferrer, MTA board member and former Bronx borough president; and SBA Regional Administrator Jorge Silva-Puras.

The event is sponsored by the New York City Hispanic Chamber of Commerce, the MTA, DDEC and Casiano Communications.

For information:

If interested in attending this Summit meeting in New York, call the DDEC at: 787-268-0140, from 8 a.m. to 6 p.m.

OUT OF THE DEPRESSION

Meanwhile, Fortuño administration officials are seizing on the latest economic indicators from December 2011, which they say is now showing the beginning of the end of Puerto Rico's depression.

The latest Government Development Bank-Economic Activity Index (GDB-EAI) showed overall economic activity in December 2011 up 0.5%, when compared to the same month the previous year, the first time the index has shown year-over-year growth since Puerto

Rico's economic downturn went into zero growth in March 2006.

Most private economists say we must wait for more data before a clear trend of economic growth and a definitive end to the extended economic downturn can be called, but a growing chorus of experts contend that we are returning to modest economic growth and that Puerto Rico will continue to post positive numbers in the future. Many believe the GDB-EAI's performance is the best economic news in a very long time, especially as other economic indicators are painting a similar picture, with signs of a return to economic growth multiplying.

"We are starting to grow again," Fortuño told CARIBBEAN BUSINESS in an exclusive interview. "With the closing of the government during the previous administration in 2006, we fell into our deepest and longest recession in history. In our three short years, we were able to start turning things around."

Added Pérez-Riera, "We have been waiting for this from the very beginning...different sectors of the economy breaking into positive territory. In the grand scheme of things, we have come back quickly at a time when the global economy has been imploding."

Most U.S. economists define a recession as at least two quarters of economic contraction, so a general rule of thumb is to call one over after at least two quarters of growth, according to some local economists.

In the U.S., the National Bureau of Economic Research's Business Cycle Dating Committee is the authority for calling the start and finish of a recession, which it defines as a "significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP [gross domestic product], real income, employment, industrial production and wholesale-retail sales."

No matter how you measure it, however, Puerto Rico's tough economic times have added up to not just a recession, but a full-blown depression, which is most often defined as entering a depression after two years of recession.

Puerto Rico qualifies on both counts, as the economic downturn,

Continued on page 16

Continued from page 15

which began in March 2006, will complete six years next month and has already resulted in a total contraction of nearly 14%, economists say.

"This is a positive development and in line with other indicators that show that the depression is bottoming out," said Vicente Feliciano, president of Advantage Business Consulting, pointing to the latest GDB-EAI report. "The depression will end after we have several months of solid year-over-year growth."

We will still remain in a recession until we break into positive GDP growth. But going back to recession is the first step after coming out of depression, according to some economic observers.

"The numbers don't lie. They look pretty good. Things are much better than they were over the past few years," added economist José Joaquín Villamil, president of Estudios Técnicos. "It is a clear trend that

you will continue to see over the next few months and quarters."

Government officials are betting that the improved economic picture will instill confidence in both consumers and investors, which will only work to bring greater improvements to the economy over the next few years.

"This is already happening," the governor said. "Investors are already sensing the turnaround. Every day last week, I visited businesses that have created jobs as a direct result of private sector investment."

Pérez-Riera concurred that "people are starting to gain that confidence."

"We are finally at the point where if you have been sitting on the sidelines waiting to make a bet on yourself and Puerto Rico, this would be the time to do it," he said.

Economists agree that positive economic news, by boosting consumer and investor confidence, can lead to a further brightening of the economic picture.

"The confidence factor is critical. People feeling that the worst is over will absolutely help the economy move forward," Feliciano added. "If you have a job, you will start to feel confident about keeping it and start spending more. If you are in business and have survived, it is time to start making some judicious bets on the future."

THE NUMBERS SPEAK

The December 2011 GDB-EAI, at 127.7 points, showed growth in three of four of its main indicators.

Total payroll employment hit 934,600, a 0.2% improvement over the year-prior period and the first month reflecting positive growth since early 2006.

Cement sales, another GDB-EAI indicator, totaled 1.618 million bags in December, a 13.9% increase over the same period in 2010. Total cement sales for calendar year 2011 ended 5.4% above 2010.

Meanwhile, gasoline consumption reached 95.3 million gallons in

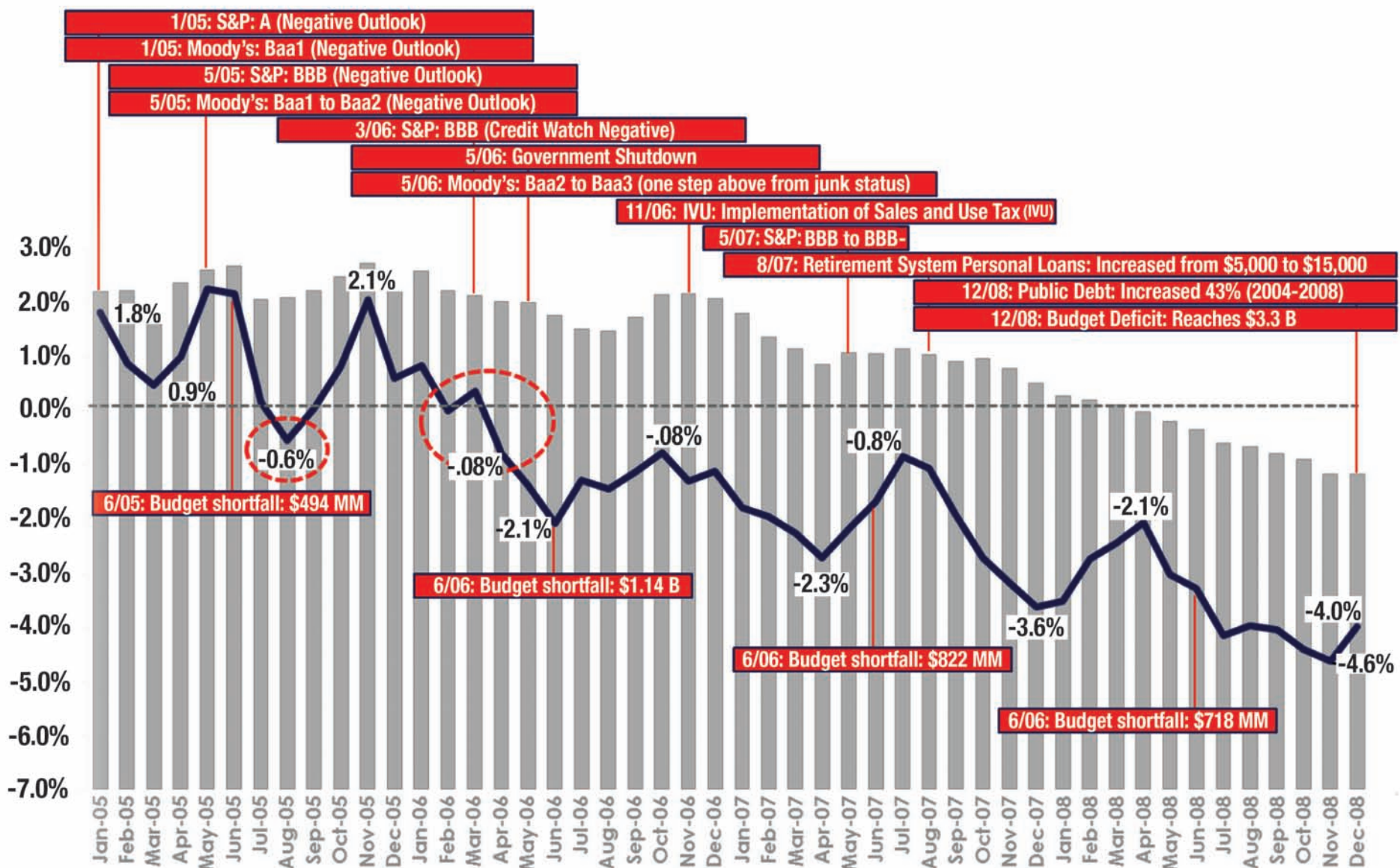
December, a notable increase over the average 87.1 million gallons consumed monthly during 2011, GDB officials said.

Only one of the four indicators—electric power consumption—declined compared with last year, with December consumption registering a 1.7% decline over the same period the previous year. Officials attribute this to increased conservation efforts by citizens and businesses and a colder than normal December, which led to less use of air conditioning.

"There is a direct relationship. When the weather is more agreeable, energy consumption falls," GDB President Juan Carlos Battle told CARIBBEAN BUSINESS. "Also, all the promotion about energy conservation and the use of green energy, both by the government and the private sector, is having an impact on consumption. A 1.7% decline isn't dramatic."

The positive year-over-year growth

Continued on next page



Continued from previous page

follows three straight months in which the GDB-EAI showed month-to-month improvements, and in November it fell a mere 0.1% when compared to the year-prior period.

Because of the GDB-EAI's 98% degree of correlation with real gross national product levels, officials expressed hope that after a stabilization period of more than a year, the Puerto Rico economy will finally reach positive growth terrain.

The GDB-EAI plummeted 13% from June 2005, when it was at 153.9 points, to June 2009, when it registered 134.1 points. From June

2009 to December 2011, it lost an additional 4.7%.

The Planning Board is projecting 0.7% growth for the current fiscal year, which runs through June 30, but will revise its outlook next month.

"We know we will have positive growth," Battle said. "The behavior of the GDB-EAI and positive news from the U.S. mainland will have an impact, but we still don't know whether the projection of 0.7% will change."

OTHER SIGNS OF

ECONOMIC IMPROVEMENT

Government officials are particularly upbeat because more, much more,

than just the GDB-EAI is showing that things are getting better.

The Banco Popular Economic Activity Index (BPOP-EAI), which is based on different components than the GDB-EAI, including bank deposits, imports and hotel registrations, surged 1.8% in November 2011 compared to the same period the prior year, according to the latest issue of Progreso Económico, a quarterly report published by Puerto Rico's largest bank.

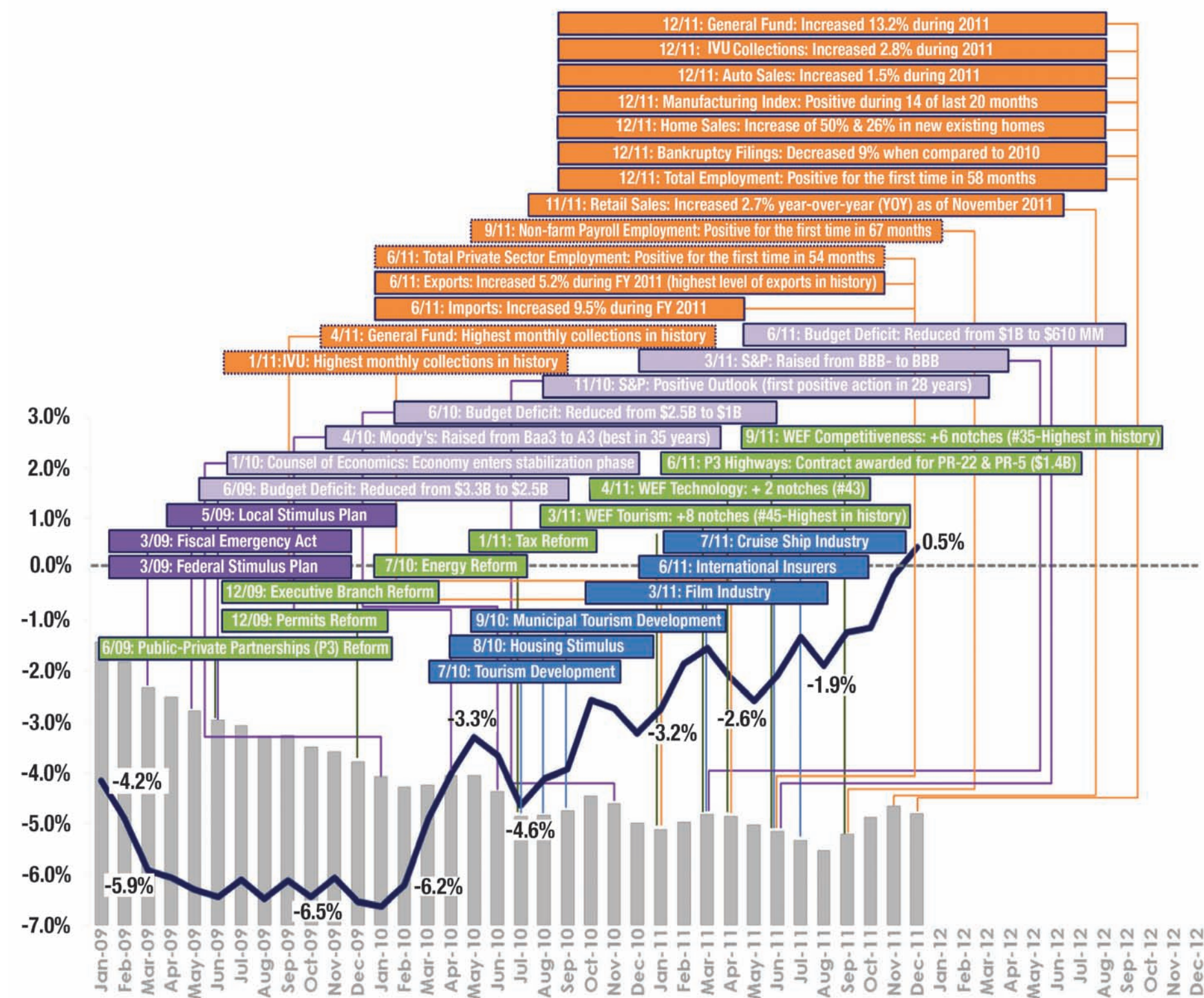
Prior to that, the BPOP-EAI registered a positive 0.7% year-over-year improvement in June 2011 for the first time since the recession began. In July 2011, it registered a positive

3.1%. Over the next three months it registered an average 0.9% decline before returning to positive turf in November.

"The increases that both the BPOP-EAI and the GDB-EAI are showing compared to last year is a positive development, but we have to wait for more data before determining whether there is a clear trend of economic growth," said Mario Marazzi, executive director of the Puerto Rico Institute of Statistics, which produces the quarterly report for the island's largest bank.

The indexes are springing to life following months of improvements

Continued on page 18



Continued from page 17

in individual economic sectors.

Home sales, for example, totaled 15,573 last year, a 30.4% improvement over the previous year. New-home sales surged 49.7% to 3,465, while existing-home sales grew 25.7% to 12,108.

Cement sales, a big indicator of construction activity, have plummeted throughout the economic depression, dropping 13.5% in 2008, 29.6% in 2009 and 20% in 2010, before turning the corner last year to increase by 5.2%.

Exports, meanwhile, have been on the upswing for an even longer period of time. They fell 4.9% in 2009, but then climbed 1.4% in 2010 and 5.2% in 2011, when, at \$64.876 billion, they registered the highest level in Puerto Rico history.

Car sales have also been driving up the confidence of officials that an economic turnaround has begun. After falling by 12.9% in 2007, 11.6% in 2008 and 15.6% in 2009, car sales increased 17.3% in 2010 and 1.5% in 2011. Likewise, retail sales began improving with a 1.54% increase in 2010, and are projected to increase by 2.7% in 2011.

Meanwhile, Puerto Rico's Purchasing Managers Index (PMI) has shown that the all-important manufacturing industry has been growing rather than contracting in 13 of the past 19 months.

The tourism industry has also been doing better. Hotel occupancy dropped 1.8% in 2009, but then increased 1.2% in 2010 and 2.2% in 2011 to reach a 69.2% level, according to the Puerto Rico Tourism Co. The number of cruiseship visitors, using Puerto Rico as a homeport, also jumped 21.5% in 2010 and another 1.9% last year.

The all-important RevPAR metric, which measures a hotel's revenue per room, finally turned positive last year, surging 7.1% to \$118.22, after sliding 14.9% in 2009 and 0.1% in 2010.

Revenue generated from the local sales & use tax (IVU by its Spanish acronym) has been on the rise for the past 11 months, and it jumped 2.8% in 2011 compared to the previous year.

Net tax revenue, another broad indicator, crashed along with the economy, dropping 6% in 2008 and 9% in 2009 before increasing 3.4% in 2010 and 11.3% in 2011.

In further signs of improvement, new



Economic Development & Commerce Secretary José R. Pérez-Riera said next month's event is the beginning of the integration between the Puerto Rico and New York economies and part of the drive to transform the island into a big exporter of professional services.

corporation registrations increased 14% last year, while bankruptcies are down, dropping 9% in 2011 compared with the previous year.

"It is very evident that things are getting better," Pérez-Riera said.



"There is light at the end of the tunnel, and you honestly see the economy of Puerto Rico beginning to kick on all cylinders."

JOBS, JOBS, JOBS

Perhaps the biggest, brightest sign of them all that things are getting better is the improvement in the island's jobs picture, with the unemployment rate dropping to 13.2% in December 2011. The rate has come down in seven of the past nine months compared to the same periods last year.

"We have stopped the loss of jobs and begun to create new jobs,"

Pérez-Riera said.

In the first six months of the current fiscal year, from July 1 through Dec. 31, 2011, some 34,000 new jobs were created, which is the largest amount of jobs created in the first

half of a fiscal year in more than a decade, he said.

Some 159,200 jobs were lost from fiscal 2006 through fiscal 2009, with most of those jobs—95,300—being shed in fiscal 2009, which coincided with the last six months of the administration of former Gov. Aníbal Acevedo Vilá and the first six months of the Fortuño administration. In 2010, 31,800 jobs were lost and in 2011, just 1,000 jobs were lost.

Private sector employment increased 2.6% in December, the biggest increase since January 2007, and total employment was up by 0.1% during

the final quarter of 2011, when compared with the previous year period.

"All the jobs numbers look better," Villamil said. "There is a clear trend. The one area of concern is manufacturing employment."

The 13.2% unemployment rate in December was the first time it had dipped below 14% since January 2009, when it was 13%. It provided more evidence that Puerto Rico is finally pulling out of its long economic doldrums.

The jobless rate in December 2006, when Puerto Rico's lingering recession was still taking root, was just 9.5%. It rose to 10.5% in 2007, to 13.1% in 2008, to 14.4% in 2009, and to 14.7% in December 2010, according to local Labor Department statistics.

Meanwhile, the Fortuño administration has reduced central government employment by 36,360 since it has been in office.

THE U.S. BOUNCE

Since late 2008, Puerto Rico has been largely on its own in trying to turn around its economic fortunes, as the U.S. and world economies got caught in steep downturns of their own following a global financial crisis.

However, the U.S. mainland economic picture has brightened in recent weeks, which should bolster the island's prospects of entering a recovery period, economists and officials say. The U.S. unemployment rate fell in January to 8.3%, a three-year low, as 243,000 jobs were created, the most in nine months. Manufacturing activity has been up for the past three months, with a growing backlog of orders suggesting the surge will continue and consumer confidence is up.

The numbers have snuffed many of the concerns of economists and analysts that the U.S. economy, which grew at about 1% last year, would slip back into recession, according to several reports. Instead, several financial firms are revising their economic forecast for the year upward from 2% to 2.5% and 2.8%.

Economists and officials say because the local economy is tied into the U.S. economy, the better economic picture stateside will only serve to help improve things here.

Feliciano said that an improved U.S. economy would give a kick to two important economic sectors on the

Continued on next page

Continued from previous page

island, manufacturing and tourism.

"This gives us more confidence that this recovery has some legs," Pérez-Riera said.

At the beginning of the depression, when the Puerto Rico economy was in decline, and the U.S. economy still growing, the gap between local economic performance and stateside economic performance grew to historic levels.

While the local economy historically has lagged behind that of the U.S., it would closely follow its ebb and flows and stay within its range. The divergence in the fortunes of the local and stateside economies was "scary" and sparked fears that the two economies were delinking, Pérez-Riera said.

"When we came into office, the gap between the growth here and the national growth was abysmal, seven to eight percentage points, and we have been able to get much closer to the level of growth of the national economy," Fortuño said.

That has had a direct impact on the financing costs that the Puerto Rico government pays. At the start of this administration, Puerto Rico bonds were about 150 basis points above the national average, and today interest costs are much lower and closer to the national average, the governor added.

"Those are savings that go straight into people's pockets," Fortuño said.

DIGGING OUT OF THE DITCH

While there is growing agreement that Puerto Rico is beginning to dig out of the large economic ditch left by the depression, there is also consensus that much more needs to be done to get the economy back to healthy levels of growth, and regain the ground of the "lost decade."

"The economy has been shrinking for the past five years, and it is almost 14% smaller. That is a huge contraction that isn't the sort of the thing you can shrug off," Villamil said. "We are coming out of recession, but there are still risks out there."

"Looking forward, there is a much better government fiscal platform than there was in 2006 when the depression started," Feliciano said. "Other than that, we face many of the structural deficiencies that led us into the depression, such as



New York Gov. Andrew Cuomo wants to double minority contract awards in his state and believes partnerships between Puerto Rico firms and New York State minority firms can help achieve that goal.



Government Development Bank President Juan Carlos Batlle said the most recent economic indicators support the administration's forecast of a return to economic growth this fiscal year.

inflexible labor laws and expensive electricity."

Villamil said he is "100% certain" that the Fortuño administration's swift action upon entering office to shore up the government fiscal situation was the right thing to do, even though many of the austerity measures it was forced to enact, including firing thousands of government workers, actually had a negative immediate impact on the economy.

Tax reform and the government public-private partnerships (PPPs) program will also work to strengthen the economy going forward, the



José Joaquín Villamil, president of Estudios Técnicos, said that positive economic indicators form a "clear trend that you will continue to see over the next few months and quarters."

economists say, but Villamil said that incentives specifically aimed at spurring investment need to be enacted.

Fortuño said the tax reform is a "key" initiative that helped buoy the economy, but he said the PPP program, the fiscal measures, and the energy and permitting reforms were also essential ingredients in the brightening economic picture.

The aggressive pursuit of federal funding under the American Recovery & Reinvestment Act, which has brought \$7.5 billion to the island, and the creation of a local \$500 million economic stimulus fund, also

helped buoy an economy in freefall during the early days of the administration. Further contributing to the stabilization of the local economy was the Federal Deposit Insurance Corp.-driven consolidation of the local banking industry.

Government officials say that in the darkest days of the depression they received a lot of pressure to "artificially" boost the economy, but they resisted, believing that their efforts aimed at getting the private sector to be the engine of economic growth would lead to a sustainable recovery, which they say is beginning now.

"I never doubted the policy, but we did receive a lot of pressure," Fortuño said.

Pérez-Riera is the first to admit that much more needs to be done to get the economy back to optimal levels of growth. He, however, is convinced



Vicente Feliciano, president of Advantage Business Consulting, said Puerto Rico's public finances are stronger than they were at the beginning of the economic depression, but the island still suffers from high electricity costs and inflexible and costly labor laws.

that the various incentives enacted by the government, in the areas of energy, tourism and film, and additional incentives aimed at the exportation of professional services from the island and new ones that will be introduced in the future, will create the conditions for a return to solid growth.

"We are making a compelling case to the rest of the world that we should be looked at as a beacon of growth in a very turbulent time," Pérez Riera said. ■