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Econews

Puerto Rico The Economy

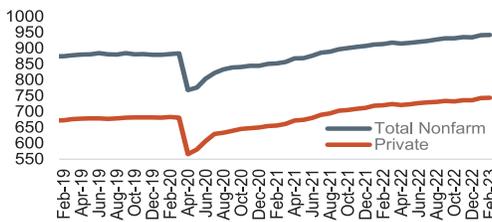
- The economy continued its path of modest recovery post-pandemic. The labor market is doing well and growth in economic activity is reflected in the Index of Economic Activity. Inflation is slowing down but still at high levels. Higher housing prices and interest rates are affecting the housing market.
- The implications of recent events, such as increased Chinese investments in the region and aggressive initiatives by Mexico, the Dominican Republic, and others, to benefit from the nearshoring strategy represent major competitive challenges for Puerto Rico. The CHIPS Act provides an opportunity for Puerto Rico, but it is not clear what actions are being taken to benefit from it.
- Puerto Rico's short-term outlook depends on the amount of federal funds disbursed and invested, particularly from the CDBG-DR and CDBG MIT programs. The CARES Act funds went mostly to consumption, not investment. There is now a great deal of uncertainty not only with respect to amounts, but also the timeline for disbursing the funds mentioned.
- The most recent survey by Estudios Técnicos, Inc. on business confidence for the Chamber of Commerce, the Puerto Rican Entrepreneur Confidence Index, reflected a less optimistic panorama, with businesses pointing to energy costs, persisting worker shortages, and the tax load, as the main pressing problems.

- As the island emerges from a drawn-out bankruptcy process, the FOMB certified a new fiscal plan, focusing on growth. It remains to be seen whether this fiscal plan will have a positive impact on growth.

EMPLOYMENT

Employment continued to expand during the first quarter (up to February), but at a slower pace, remaining at higher than pre-pandemic levels. Nonfarm private salaried employment increased 3.4% y/y, to 743,350, from 734,833 in the previous quarter. A total of 8,000 net new jobs were created during the quarter, reflecting the big expansion in January, of 6,900 jobs. That increase, though, is below the high of July 2021, when 9,700 jobs were added. So far, total private nonfarm salaried employment remains at its highest levels in years.

Private Nonfarm Salaried Employment (thousand)

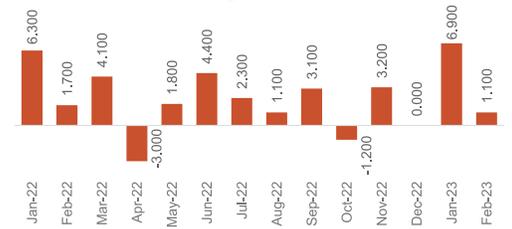


Source: P.R. Department of Labor and Human Resources, Establishment Survey (CES). SA = Seasonally Adjusted.

Employment increased the most in the Accommodation and Food Services sector, reflecting a continuing improvement in tourism, and in Professional and Business Services, Manufacturing, and Construction sectors. In February, 84.0% of the increase

in nonfarm employment came from private employment.

Month/Month Change in Private Employment



The unemployment rate increased slightly to 6.0% during the quarter, from 5.8% in August, as more people have joined the labor force. The participation rate rose to 44.2% in the quarter, from 42.4% in August.

MANUFACTURING

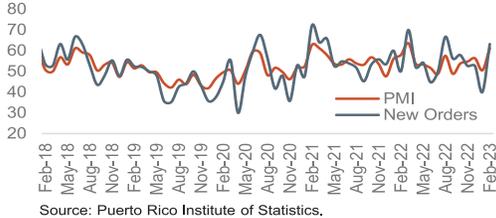
Activity in the sector expanded in the quarter. The sector's PMI averaged 55.8 (up to February), up from 54.9 in the previous quarter. That was as a result of the biggest monthly increase in February since March 2022, to 61.1, due to significant increases in the New Orders Sub Index, Production Sub Index, and Exports Orders. Still, compared to same quarter in 2022 the PMI was 2.0% below.

PMI Puerto Rico 2017-2022



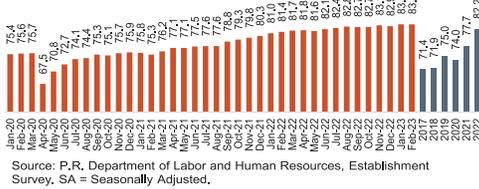
Source: Puerto Rico Institute of Statistics, * Up to February.

PMI Manufacturing



Employment in the sector continued to expand, increasing by an average of 2.7% y/y, to 83,400, from 82,183 in 2022. The rate of expansion has been slowing down. In 2022, employment increased 5.8% y/y, from 2.7% in the quarter.

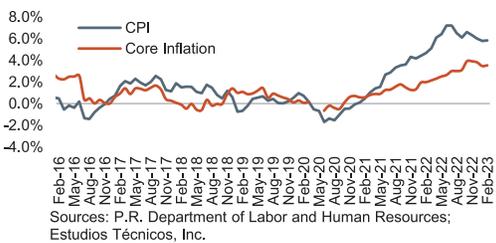
Manufacturing Employment (thousand)



INFLATION

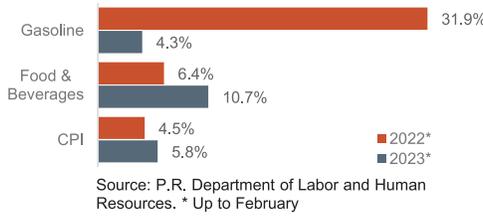
Inflation continued its moderating path, from a high of 7.2% in June of last year, to 5.8% in February, averaging 5.8% in the first quarter (up to February). Still, it remains above the historic lows of 2012 and 2013, when it averaged 1.2%. The Food and Beverage Index rose 10.7% y/y in the quarter, from 6.4% y/y in 2022, while the gasoline price index decreased to 4.3% y/y in the quarter, from 32.0% in 2022.

General and Core Inflation (December 2006 = 100)

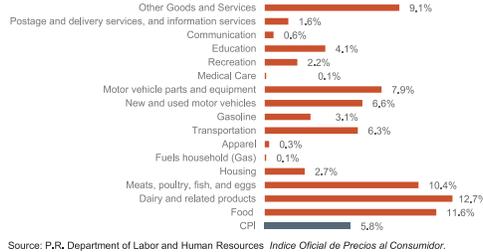


As energy prices moderated, the pace of increases in the inflation rate slowed down but increases in food and beverages prices are now the big drivers of inflation, with those on new and used motor vehicles, and parts and equipment contributing, too.

Inflation



Inflation in May by Main Groups

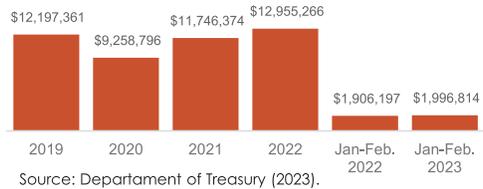


FISCAL REVENUES

Fiscal revenues (net revenues to the general fund) were up in the first quarter (up to February), rising at an annual average rate of 2.4%, to \$2.0 billion.

On a fiscal year basis, revenues were up by 3.4% y/y, as receipts from income taxes rose 12.0% y/y, and from the Sales and Use Tax (SUT) 2.5% y/y. Those from Law 154, on the other hand, decreased by 25.0% y/y, to \$654.0 million, from \$870.8 million in fiscal 2022. This is as expected, as starting in February the majority of the companies under Law 52 opted out, paying new income taxes at higher rates, which are reflected on the receipts from income taxes, which rose in the quarter.

Net Revenues to the General Fund



SHORT-TERM OUTLOOK

The year 2023 started with the economy returning to pre-pandemic levels, largely due to the funds disbursed related to COVID-19, about \$27.5 billion in all.

The disbursement of the federal reconstruction funds is essential to support

short-term economic growth. Investment on infrastructure projects will be the primary driver of growth. So far, about \$53.6 billion, of the \$81.5 billion allocated (including remaining COVID-19 funds) have been disbursed. The \$1.0 billion funds granted recently by the U.S. Department of Energy to the New Puerto Rico Energy Resilience Fund should provide a boost to improve and expand P.R.'s energy grid, with an important local impact.

At the beginning of April, a new Commonwealth Fiscal Plan was certified by the Federal Fiscal Oversight Management Board (FOMB). The Certified Fiscal Plan projects that the economy would decline (real GNP) in current fiscal year 2023 by -1.9%, with a modest growth in fiscal 2024 of 0.5%.

What to expect:

- Moderate growth in commercial and construction activity as FEMA's public assistance projects gain traction, although caution is recommended.
- Consumer spending will be supported by liquidity in transactional deposits, tax relief from the proposed tax reform, if approved, and new federal nutrition assistance funds.
- Increases in electricity and fuel tariffs due to PREPA's restructuring process, and upward movements in the price of oil.
- Further increases in short-term interest rate by the Fed, reaffirming their commitment to reduce inflation, but at the expense of greater volatility in the markets.
- Pressure on the consumers' financial position due to the negative effect of inflation and the increase in interest rates, which have a downward effect on spending and business investment.

Notes:

1. GRID Deployment Office. U.S. Department of Energy (2023). Department of Energy Announces \$1 Billion to Improve Energy Resilience for Puerto Rico's Most Vulnerable Households & Communities (February 20, 2023). At: <https://www.energy.gov/gdo/articles/departament-energy-announces-1-billion-improve-energy-resilience-puerto-ricos-most>
2. Federal Fiscal Oversight Management Board (2023). Restoring Growth and Prosperity (April 5, 2023). At: <https://aldia.microjuris.com/wp-content/uploads/2023/04/FOMB-Fiscal-Plan-for-Commonwealth-of-Puerto-Rico-Volume-3-Certified-as-of-April-3-2023.pdf>

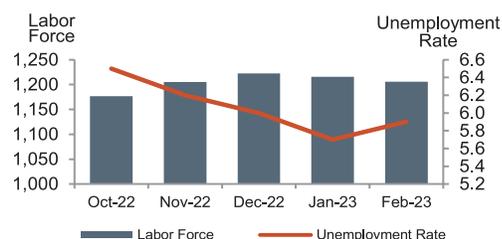
Puerto Rico

Economic Indicators

Employment

				Percent Change	
	Dec-22	Jan-23	Feb-23	Fiscal Year 2022-2023	Accumulated year to date
Labor Force (Household Survey, thousands)	1,222	1,216	1,206	1.0%	-0.1%
Employment (Establishment Survey)	950	935	942	-3.1%	3.3%
Private	749	736	742	-3.6%	3.5%
Construction	34	33	34	-8.3%	9.4%
Manufacturing	84	83	84	-4.0%	2.8%
Public Administration	201	199	200	-1.3%	2.7%
Unemployment Rate (Household survey, %)	6.0	5.7	5.9	24.0%	-6.5%

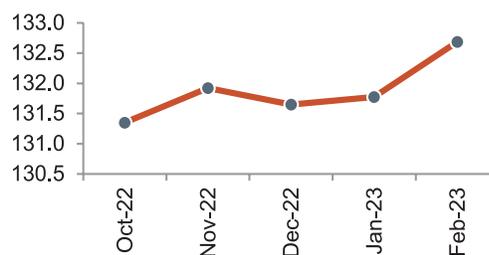
Total Employment (December 2006 = 100)



Consumer Price Index

				Percent Change	
	Dec-22	Jan-23	Feb-23	Fiscal Year 2022-2023	Accumulated year to date
All Items	131.7	131.8	132.7	6.3%	5.8%
Food & Beverages	153.6	154.4	154.8	10.2%	10.7%
Housing	121.2	121.5	121.7	2.9%	2.8%
Apparel & Upkeep	86.5	86.7	85.6	1.8%	0.8%
Transportation	125.2	124.6	127.4	8.3%	5.7%
Medical Care	160.4	160.3	160.1	1.4%	0.2%
Education	124.7	124.5	124.6	2.8%	2.6%
Recreation	118.7	118.8	118.9	2.2%	2.3%
Other Services	136.5	136.9	137.9	7.6%	8.8%

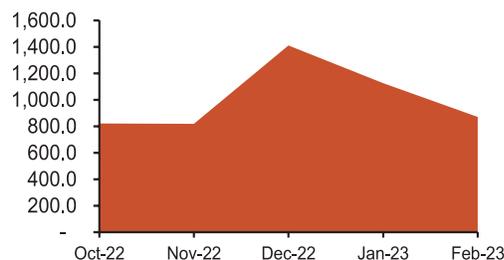
Consumer Price Index



Fiscal Revenues

				Percent Change	
	Dec-22	Jan-23	Feb-23	Fiscal Year 2022-2023	Accumulated year to date
Total Revenues (Mill.\$)	1,411.2	1,126.8	870.0	3.4%	4.8%
Taxes	1,353.0	1,064.6	809.7	3.9%	4.2%
Income Taxes	874.2	495.1	433.0	11.9%	8.3%

Net Revenues to the General Fund





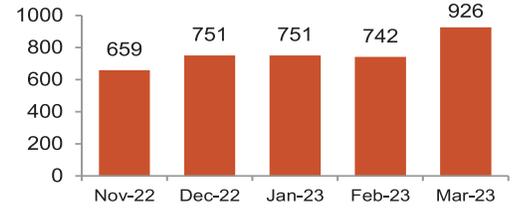
Puerto Rico

Economic Indicators

Construction

	Jan-23	Feb-23	Mar-23	Percent Change	
				Fiscal Year 2022-2023	Accumulated year to date
Cement Production (Thousand 94-lb Bags)	751	742	926	17.7%	30.0%
Cement Sales (Thousand 94-lb Bags)	1,103	1,217	1,463	-4.3%	1.9%

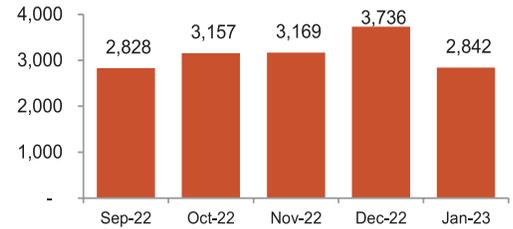
Cement Production



Retail

	Nov-22	Dec-22	Jan-23	Percent Change	
				Fiscal Year 2022-2023	Accumulated year to date
Total (Bill. \$)	3,169	3,736	2,842	3.4%	6.5%
Department Stores (Mill. \$)	1,071	1,275	945	5.0%	5.1%
Supermarkets (Mill. \$)	438	485	398	7.8%	2.2%
Used and New Autos (Mill. \$)	342	413	306	-12.6%	-7.6%
Gasoline Stations (Mill. \$)	148	207	179	8.0%	36.2%
Restaurants (Mill. \$)	211	235	213	15.8%	37.9%

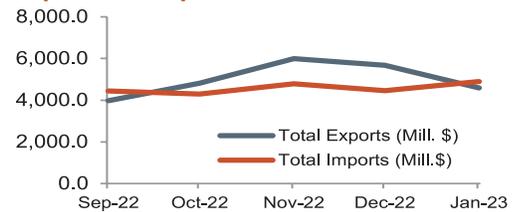
Retail Sales



Exports and Imports

	Nov-22	Dec-22	Jan-23	Percent Change	
				Fiscal Year 2022-2023	Accumulated year to date
Total Exports (Mill. \$)	5,995.4	5,670.3	4,594.4	9.5%	35.3%
Foreign Countries	1,588.1	1,919.7	1,502.7	23.8%	54.4%
Total Imports (Mill. \$)	4,785.0	4,462.8	4,895.5	12.0%	23.7%
Foreign Countries	2,102.6	1,871.8	2,257.4	5.8%	29.0%

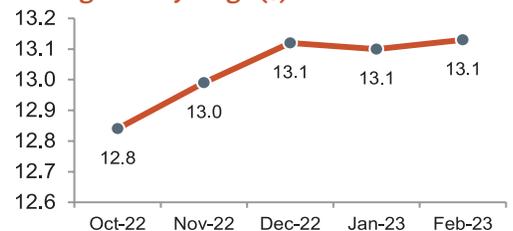
Exports and Imports



Manufacturing

	Dec-22	Jan-23	Feb-23	Percent Change	
				Fiscal Year 2022-2023	Accumulated year to date
Weekly Hours (#)	38.2	37.7	38.2	-1.3%	-2.1%
Average Hourly Wage (\$)	13.1	13.1	13.1	6.3%	5.6%

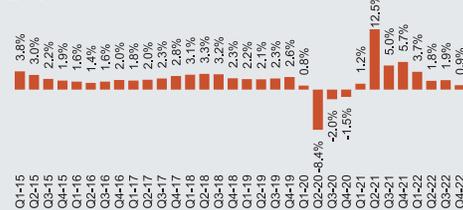
Average Hourly Wage (\$)



United States The Economy

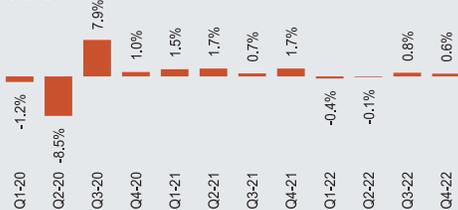
- The year started with positive indicators – inflation is down, the labor market remains strong. Although on a positive note, real GDP growth in 2022 was 2.1% y/y, with real growth in the last quarter decreasing to 0.9% y/y, from 3.7% y/y in Q1-22, pointing to a deceleration in the pace of economic growth. Consumer spending, a key driver in economic growth, increased by 1.7% y/y in Q4-22, moving into a lower growth path entering 2023.
- Yet, macroeconomic uncertainty exists – long-term inflation, decreasing consumption, high interest rates and the housing market, for example – contributing to the possibility of a recession.¹ There is a consensus of an economic slowdown, as the impacts of the Federal Reserve rate raises feed into the economy.² External geopolitical factors (for instance, the U.S.-China trade relations, and an escalation of the Ukraine conflict) still weight significantly.

Real GDP Growth (y/y)



Source: U.S. BEA.

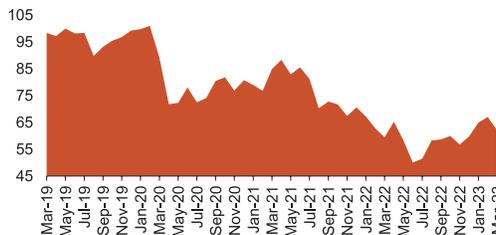
Quarterly Real GDP Growth (Q/Q)



Source: U.S. BEA.

- Consumer confidence in the first quarter reflected an overall positive note, with the University of Michigan/Reuters Index increasing to an average of 64.6, from 58.8 in the previous quarter. The index decreased in March, to 62.0, though, dropping by about 8.0 from February, reflecting the month's upheaval in the banking sector, but also increasing concerns about a recession ahead.

U.S. Consumer Sentiment Index

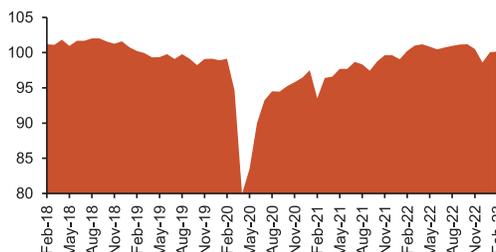


Source: University of Michigan/Reuters.

PRODUCTION - MANUFACTURING

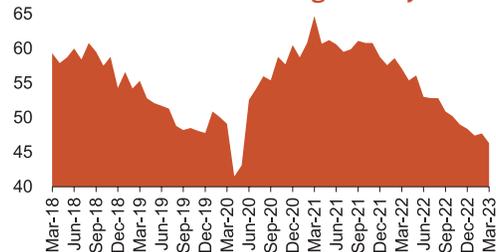
Overall, manufacturing production (up to February) barely increased in the first quarter, 0.1% y/y, from an average of 0.8% y/y in the previous quarter. Manufacturing production has remained rather weak in the past few months, after a high of 4.5% y/y in Q1-22. While computer and electronic products registered gains, nonmetallic mineral products registered the largest losses, with chemicals recording an increase.

US Manufacturing Production Index (2017 = 100)



Source: FRED (Federal Reserve Bank of St. Louis).

ISM Index of Manufacturing Activity



Source: Institute for Supply Management. **Note:** A reading above 50 points indicates that the manufacturing economy is generally expanding, and declining when the reading falls below 50 points.

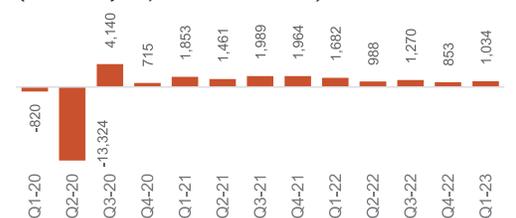
Economic activity in the manufacturing sector, according to its ISM Index, contracted in March for the fifth consecutive month, after a year above the expansion level of 50.³ The decline by the headline index partly reflected an accelerated contraction in new orders. In

March, the new orders sub index fell to 44.3 from 47.0 in February, below the threshold level of 50, which would suggest expansion in activity. The headline index averaged 47.1 in the first quarter, from 49.2 in the previous quarter, after a high of 57.8 in Q1-22. Among the industries that reported contraction were Computer and Electronic products, and Chemical Products.

EMPLOYMENT

Employment continued to project a bright picture, although the pace of expansion is slowing. During the first quarter, a total of 1.0 million new jobs were added, lower than those created in Q1-22 of 1.7 million. In March, the number of new jobs was 236,000, down from a high of 472,000 in January. The key sectors contributing to the new jobs in the quarter were leisure and hospitality, private education, health services, and retail trade.

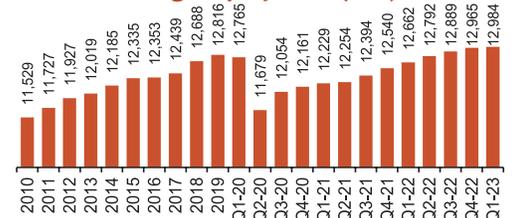
Quarterly Changes in Employment (Seasonally Adjusted - Thousands)



Source: U.S. BLS, Current Employment Statistics.

The unemployment rate averaged 3.5% in the first quarter, almost unchanged from the rate of 3.6% in March 2022.

Manufacturing Employment (th's)



Source: U.S. BLS, Current Employment Statistics.

Employment in the manufacturing sector expanded during the first quarter, but at a slower pace, too, to 12.9 million. The number of new jobs added has been decreasing, from a high of 146,000 in Q4-21, to 19,000 in Q1-23. All this is consistent with the slowing in manufacturing activity in the quarter. Employment increased in machinery

manufacturing and transportation equipment manufacturing sectors, while that in chemical manufacturing decreased.

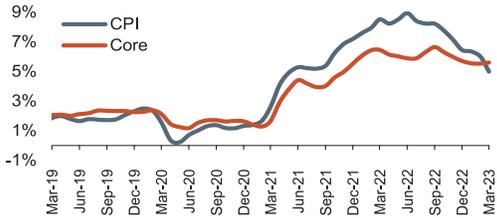
INFLATION

Headline inflation (CPI) has been trending downward since the summer of 2022, from a high of 8.9% in June, to 5.0% in March. For the first quarter it averaged 5.8%, from 7.1% in Q4-22.

On the other hand, core inflation, which excludes the more volatile components of the CPI (food and energy), although it averaged 5.6% in the first quarter, it rose in March to 5.6%, from 5.5% in the previous two months of the quarter. This points to a continuing problem of high inflation in the economy. That uptick in the core CPI will likely keep the pressure on the Federal Reserve to push ahead with another rate rise in May.

Annual Percent Change in CPI

(Y/Y, seasonally adjusted)

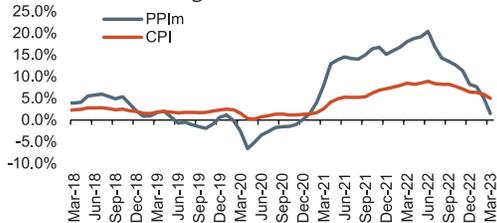


Source: U.S. BLS.

At the producer level in the manufacturing sector, the Producer Price Index inflation rate, another indicator of consumer inflation, that is, the final prices received for the industry's output, also trended down, increasing an average of 4.8% y/y in the first quarter, from 10.8% in Q4-22, lower than the increase in headline inflation.⁴ In March, the index increased by 1.5% y/y, another indicator pointing to cooling inflation.

Producer Price Index

for All Manufacturing Industries



Source: U.S. Bureau of Labor Statistics.

INTEREST RATES

Continuing high interest rates and worries about the banking system in the form of

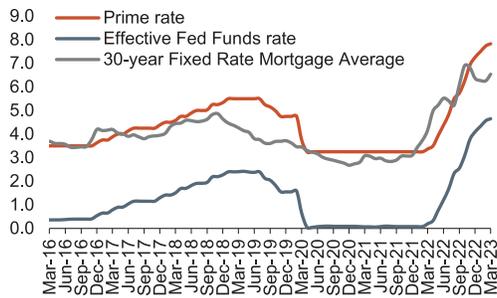
additional bank failures have dominated the financial scenario during the last month of the first quarter. Still, the Federal Reserve raised its short-term interest rates by a quarter-point on March 22nd.

Expectations are that it will raise again the federal funds rate by a quarter point at its May and June meetings. Its Chairman said that rate hikes will no longer be automatic. Close attention will be paid if a softening in the labor market and wage increases occurs, and slowing price increases, although the uptick in the core inflation rate in March could contribute to an increase. The federal funds target rate remains at 5.00 so far.

Mortgage rates are expected to remain elevated until inflation moderates.

Selected Interest Rates

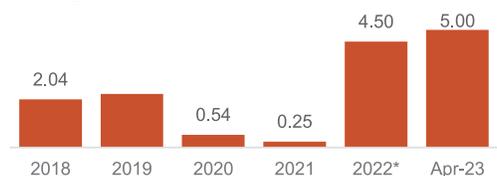
(Monthly averages)



Source: St. Louis Federal Reserve Bank (FRED).

Federal Funds Target Rate - Upper Limit

(Average)



Source: FRED. * Second half of year.

U.S./GLOBAL OUTLOOK

The global economy started 2023 with major uncertainties and downside risks, carried over from 2022 the geo-economic problems related to the continuing Ukrainian conflict, high inflation, an increased conflict between the US and China, and further financial sector stress related to the monetary and fiscal measures being adopted to fight high inflation. Add to these developments the banking crisis in the U.S. in March, which spread to Europe, and that the current scenario is worrisome.

Still, economic growth is expected, albeit at lower rates from those forecasted at the

start of the year. In its most recent forecasts (April 2023), the International Monetary Fund (IMF) now estimates global real GDP growth of 2.8% for this year, down from the January forecast of 2.9%, and 3.0% for 2024 and the following five years.⁵ Lower growth is expected for the developed economies, including the Euro Area, with India and China being the main contributors to global growth.

These are the lowest rates since the early 2000's. They reflect the increased interest rates and the strict policy measures adopted to fight high inflation levels, with an added uncertainty related to the volatility in the global banking sector.

Global and Regional Economic Outlook

2023 and 2024

	Projections				
	2022	2023f	January 2023 Forecasts	2024f	January 2023 Forecasts
World Real GDP	3.4%	2.8%	2.9%	3.0%	3.1%
Euro Area	3.5%	0.8%	0.7%	1.4%	1.6%
U.S.	2.1%	1.6%	1.4%	1.1%	1.0%
Latin America and the Caribbean	4.0%	1.6%	1.8%	2.2%	2.1%
Brazil	2.9%	0.9%	1.2%	1.5%	1.5%
Mexico	3.1%	1.8%	1.7%	1.6%	1.6%
China	3.0%	5.2%	5.2%	4.5%	4.5%
India	6.8%	5.9%	6.1%	6.3%	6.8%
Russia	-2.1%	0.7%	0.3%	1.3%	2.1%

Source: International Monetary Fund (2023). World Economic Outlook April 2023. Table 1.1.

For the U.S. a similar trend is expected for this year. Real GDP growth (y/y) for the first two quarters is expected to be higher than in Q4-22 but below the average for the three previous quarters, with 1.3% growth for the first quarter, and 1.9% for the second quarter, from 2.1% in 2022.⁶ A revision for the unemployment rate is part of the growth outlook. The unemployment rate is expected to average 3.8% in 2023, from 3.6% in 2022. The Congressional Budget Office (2023), on the other hand, projects an increase to 5.1% by the end of the year, declining to 4.5% in 2024.⁷

Notes:

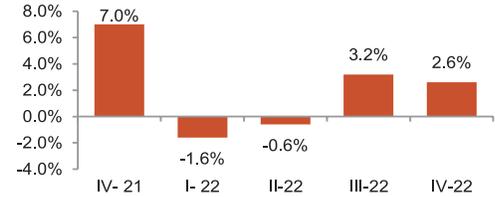
1. According to a Bloomberg survey, the probability of a recession during 2023 was 60.0%. IBISWorld - Recent Trends - Consumer Spending (March 6, 2023). At: <https://www.ibisworld.com/us/bed/consumer-spending/363/>
2. For example, higher interest rates will further slow growth via increased borrowing costs, and continuing high inflation will continue to erode consumers' real disposable income.
3. Institute for Supply Management (2023). ISM Report On Business - March 2023 Manufacturing ISM Report. At: <https://www.ismworld.org/supply-management-news-and-reports/reports/ism-report-on-business/pmi/march/>
4. The PPI and the CPI are different measures of price changes, the main difference being the types of goods and services they include, and types of prices they collect. The PPI index measures changes in prices received for the industry's output sold outside the industry (that is, its net output). PPIs measure price change from the perspective of the seller.
5. International Monetary Fund (2023). World Economic Outlook April 2023. At: <https://www.imf.org/en/Publications/WEO/Issues/2023/04/11/world-economic-outlook-april-2023>
6. Federal Reserve Bank of Philadelphia (2023). Survey of Professional Forecasters - First Quarter 2023 (February 10, 2023). At: www.philadelphiafed.org
7. Congressional Budget Office (2023). The Economic Outlook for 2023 to 2033 (February 2023). At: <https://www.cbo.gov/publication/58957>

United States Economic Indicators

GDP

	I-22	II-22	III-22	IV-22
GDP (% Change From Preceding Period)	-1.6	-0.6	3.2	2.6
Private Consumption	1.3	2.0	2.3	1.0
Fixed Investment	4.8	-5.0	-3.5	-3.8
Residential	-3.1	-17.8	-27.1	-25.1
Non-Residential	7.9	0.1	6.2	4.0
Government Spending	-2.3	-1.6	3.7	3.8
Exports	-4.6	13.8	14.6	-3.7
Imports	18.4	2.2	-7.3	-5.5

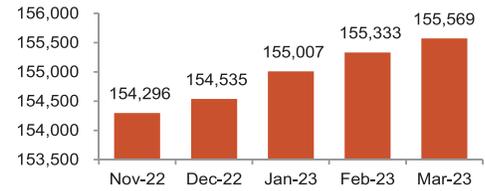
Gross Domestic Product (% Change From Preceding Period)



Employment

	Dec-22	Jan-23	Feb-23	Mar-23
Employees on Non-Farm Payrolls (SA) (Thousands)	154,535	155,007	155,333	155,569
Change (%)	0.2%	0.3%	0.2%	0.2%
Goods Producing	21,461	21,502	21,513	21,506
Change (%)	0.2%	0.2%	0.1%	0.0%
Service Industries	133,074	133,505	133,820	134,063
Change (%)	0.2%	0.3%	0.2%	0.2%

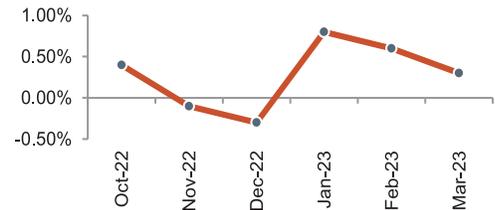
Employees on Non-Farm Payrolls (In thousands)



Consumer Price Index

	Dec-22	Jan-23	Feb-23	Mar-23
CPI - All Urban Consumers (1984=100)				
Change from preceeding month	-0.3%	0.8%	0.6%	0.3%
Change from preceeding year	6.5%	6.4%	6.0%	5.0%
CPI - Less Food and Energy				
Change from preceeding month	0.2%	0.6%	0.7%	0.5%
Change from preceeding year	5.7%	5.6%	5.5%	5.6%

Change in CPI



Interest Rates

	Dec-22	Jan-23	Feb-23	Mar-23
Effective Federal Funds	4.10	4.33	4.57	4.65
Three Month Treasury Bill (Constant Maturity Rate)	4.36	4.69	4.79	4.86
Prime Rate	7.26	7.50	7.74	7.83
Ten Year Treasury Bond	3.62	3.53	3.75	3.66
Moody's Seasoned Aaa Rate	4.43	4.40	4.56	4.60
30-Year Conventional Mortgage Rate	6.36	6.27	6.26	6.54

Selected Interest Rates (3month T Bills)

