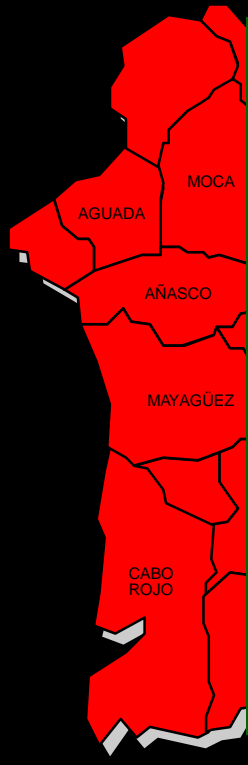


H. Calero
Consulting Group, Inc.

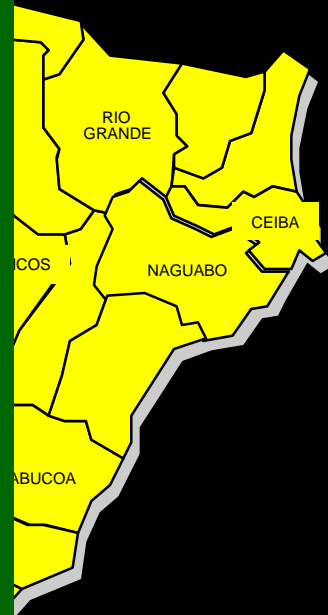
In the Eye of the Storm

Puerto Rico 2013 - 2015

Where is Puerto Rico today

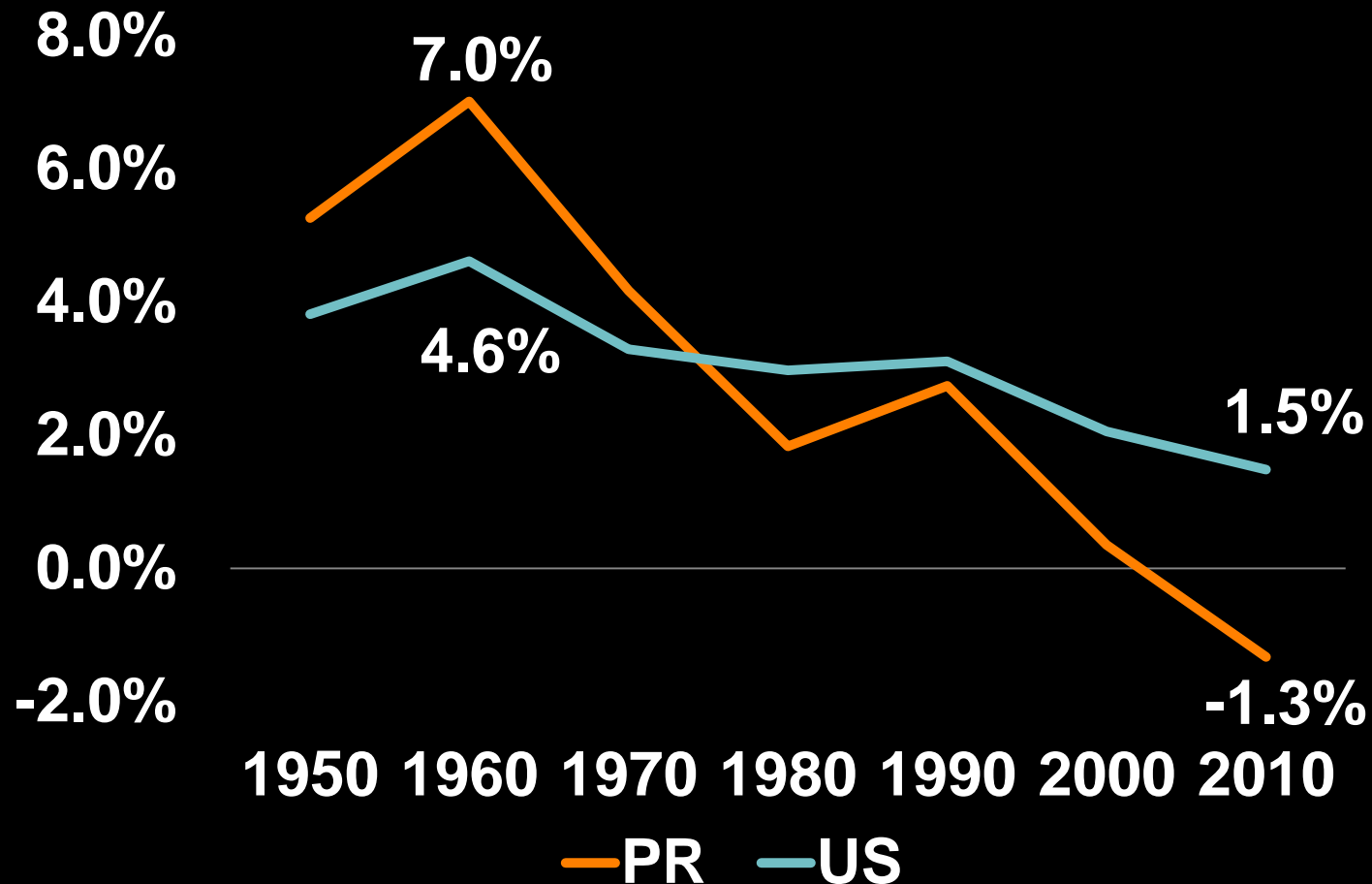


Gross Domestic Product 12	\$101.0b
Gross National Product 12	\$69.5b
Population Census 2010	3.7m
Share of Manufacturing in GDP	46%
Income Per Capita 12	\$16,934
Total Employment 7/13	0.9m
Inflation 7/13	1.9%
Unemployment rate 7/13	14.7%
Participation rate 7/13	41.0%



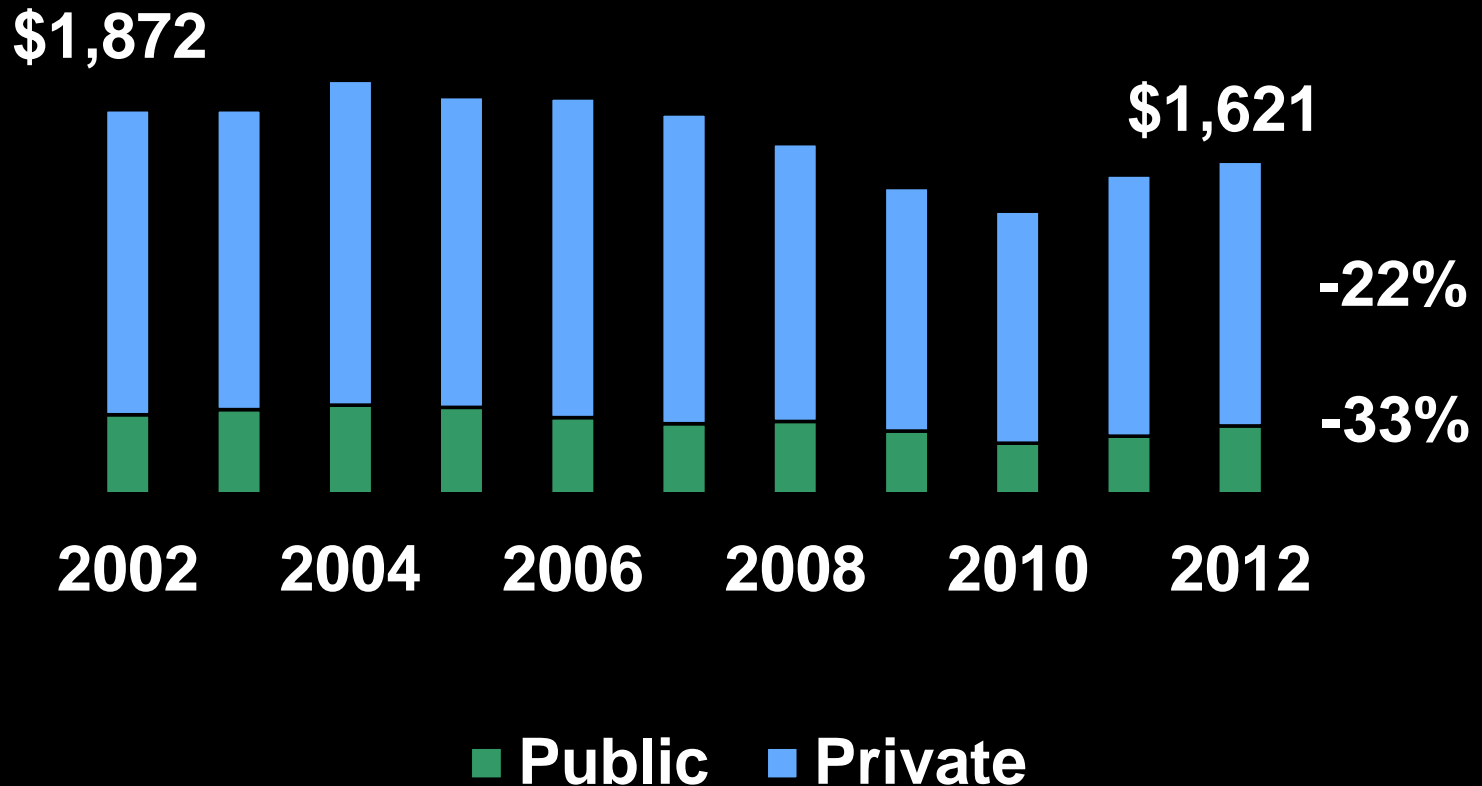
PR is a regional economy of US

10-year real GNP growth, %

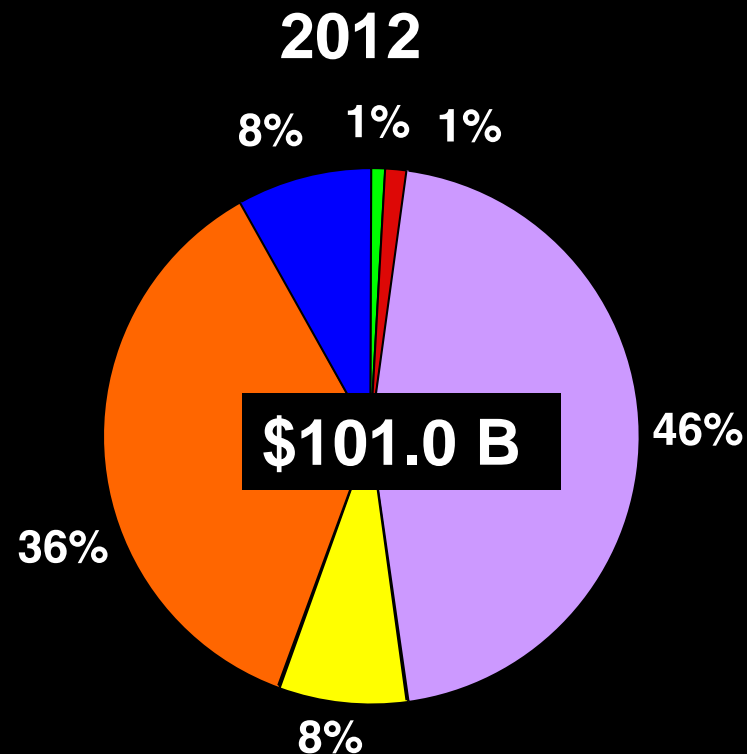
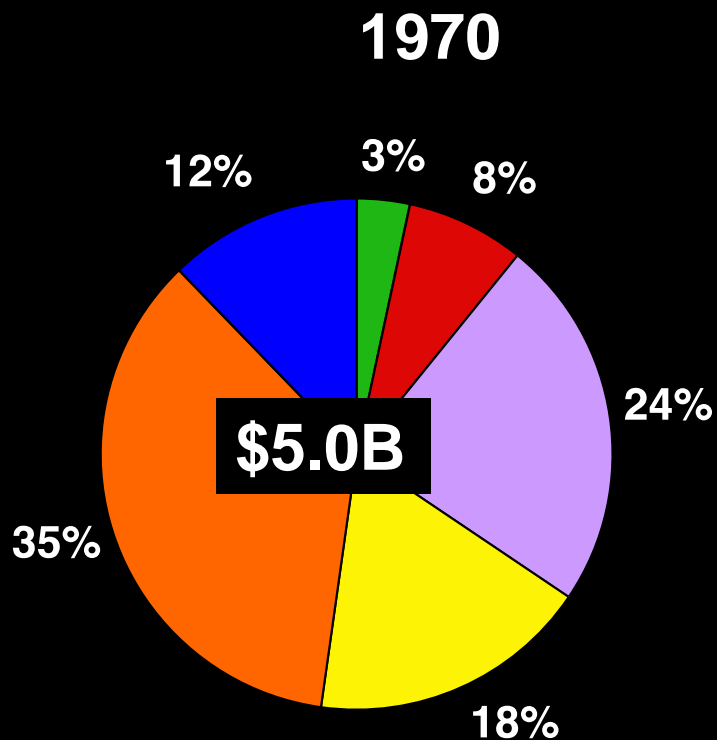


Investment went down

Public & private investment, real \$ million



Composition of GDP



Agric.

Trade

Constr.

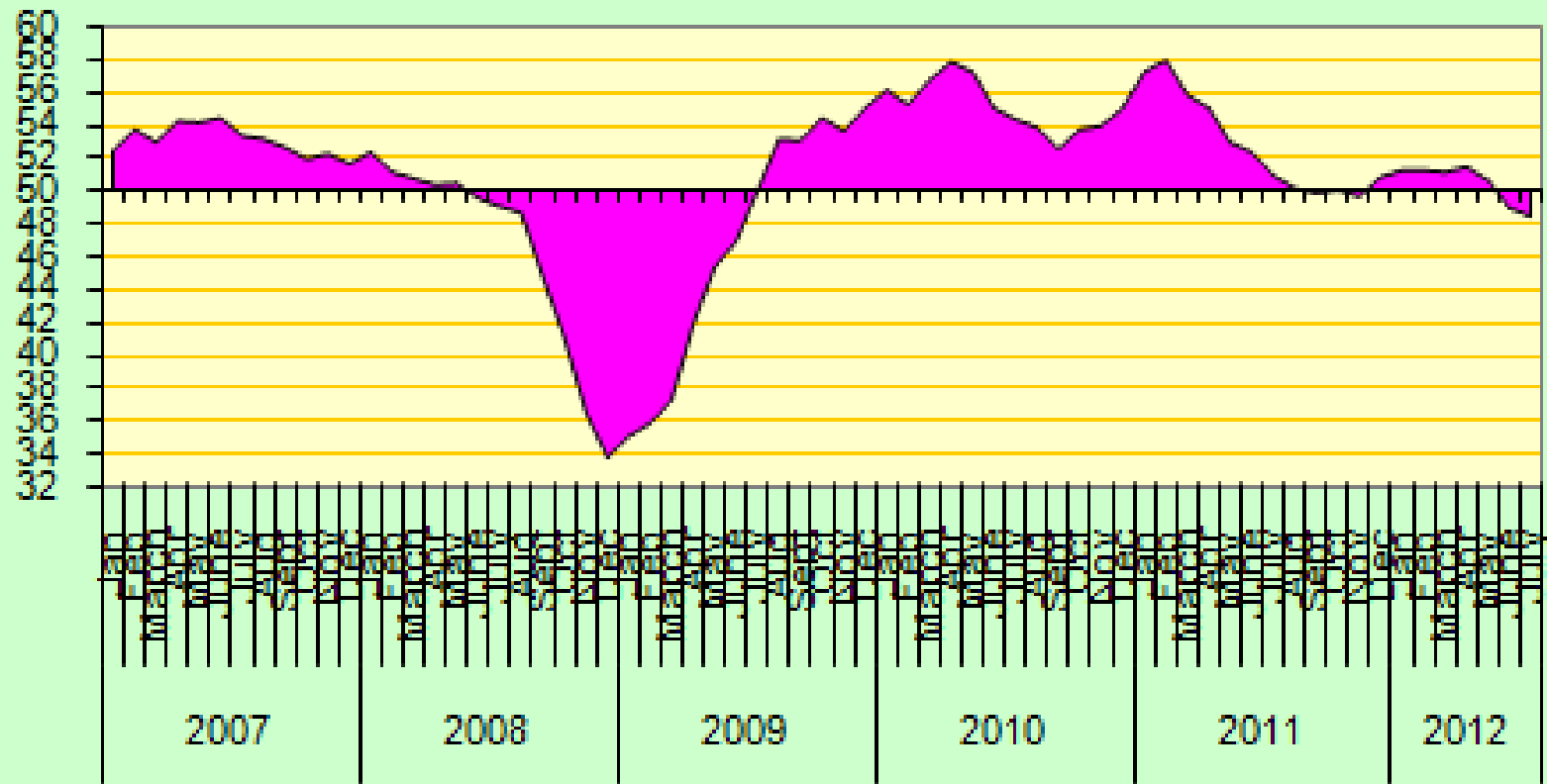
Services

Mfg.

Gov

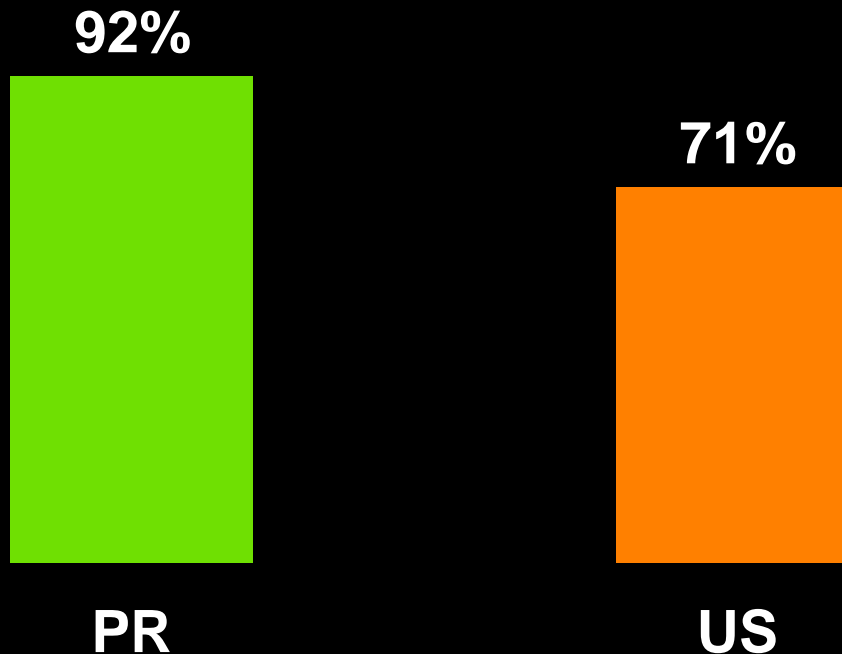
* Includes Transfers and Federal Grants

Global Manufacturing PMI

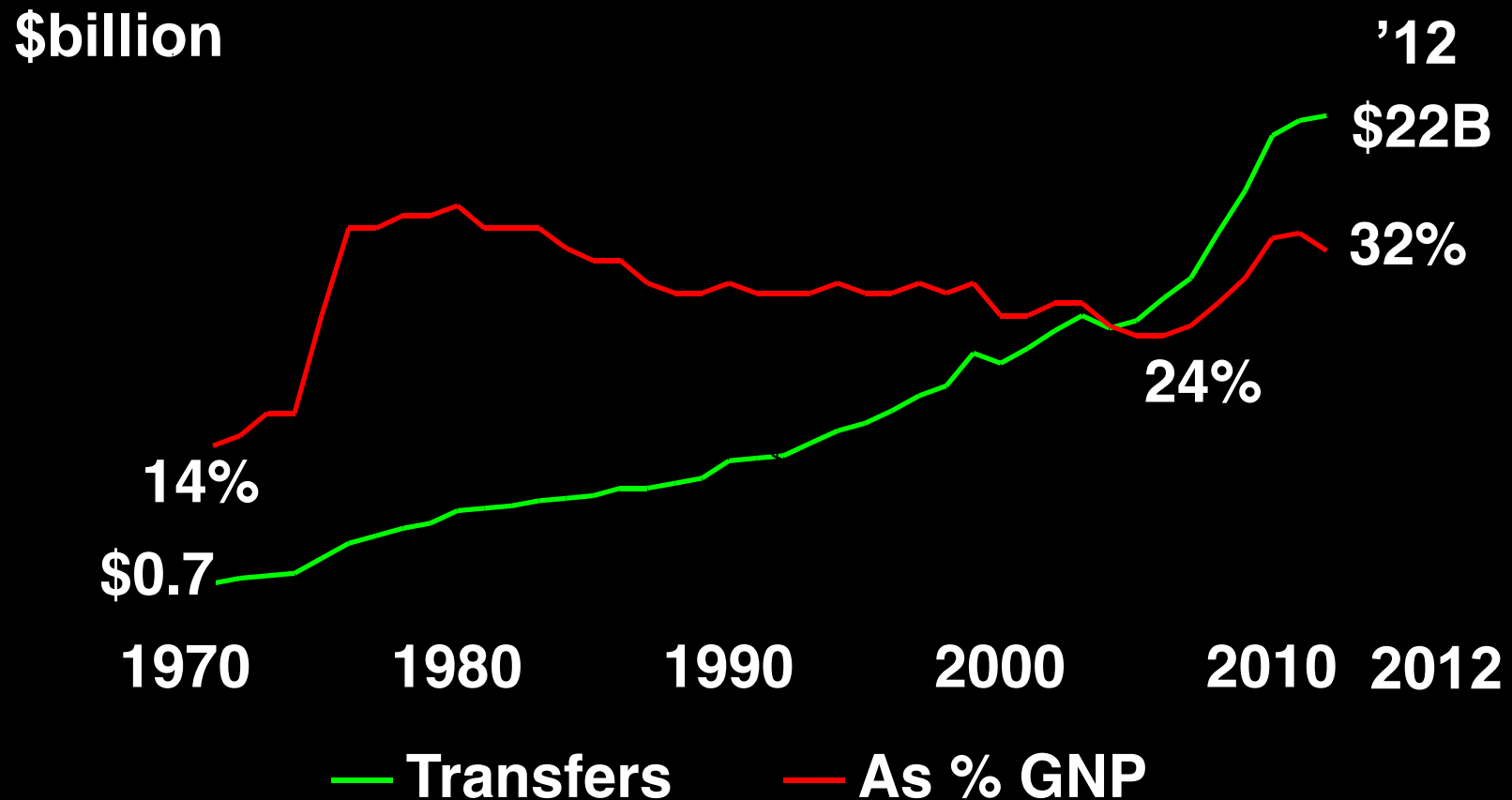


The economy relies on consumption

Real consumption as % of GDP, 2012

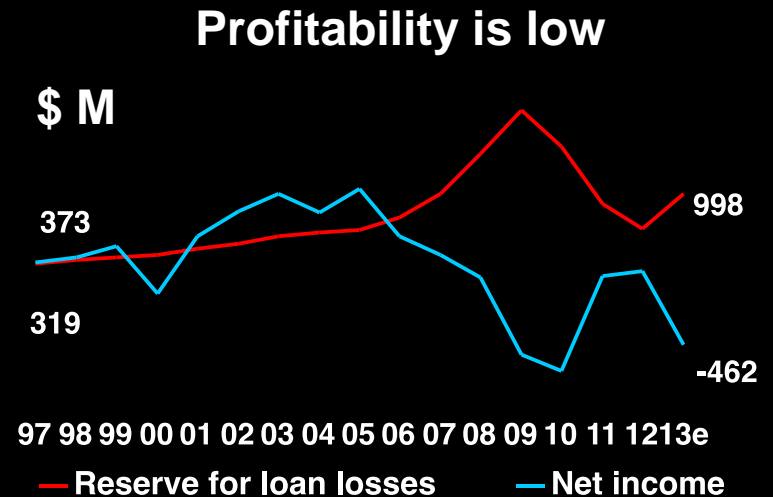
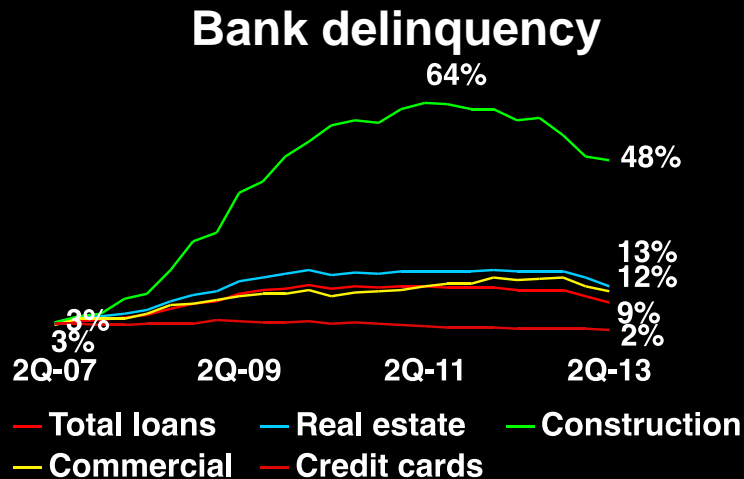
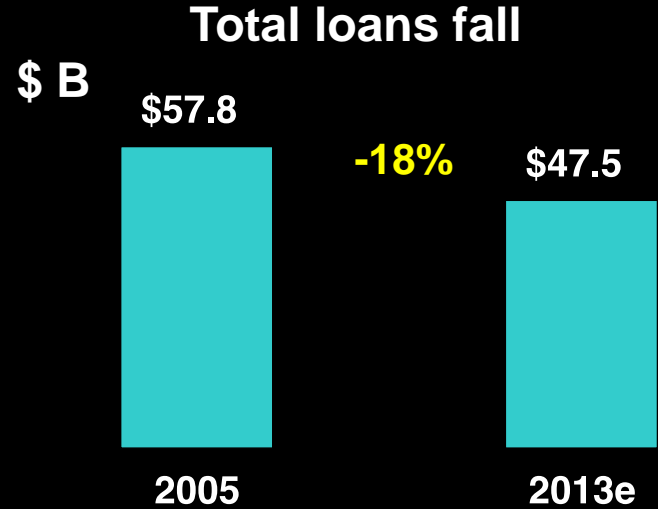
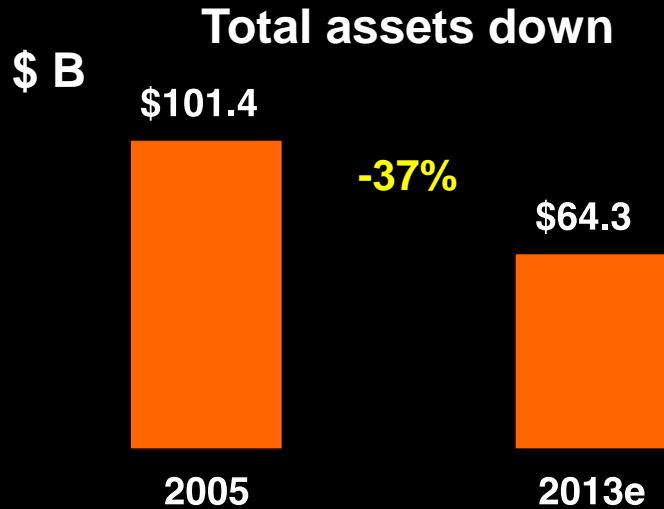


Living on transfers



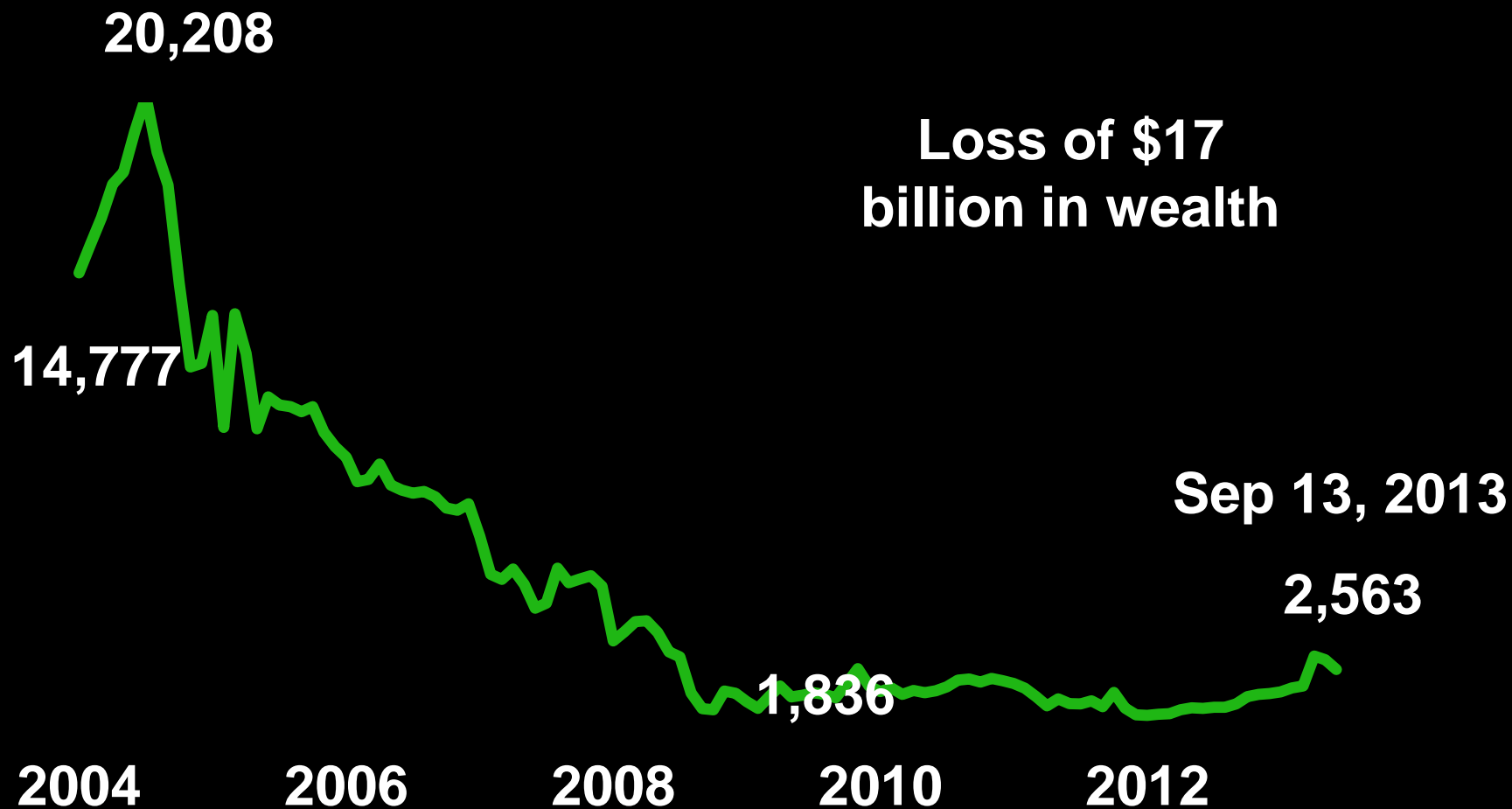
* Includes Transfers and Federal Grants

Banking performance

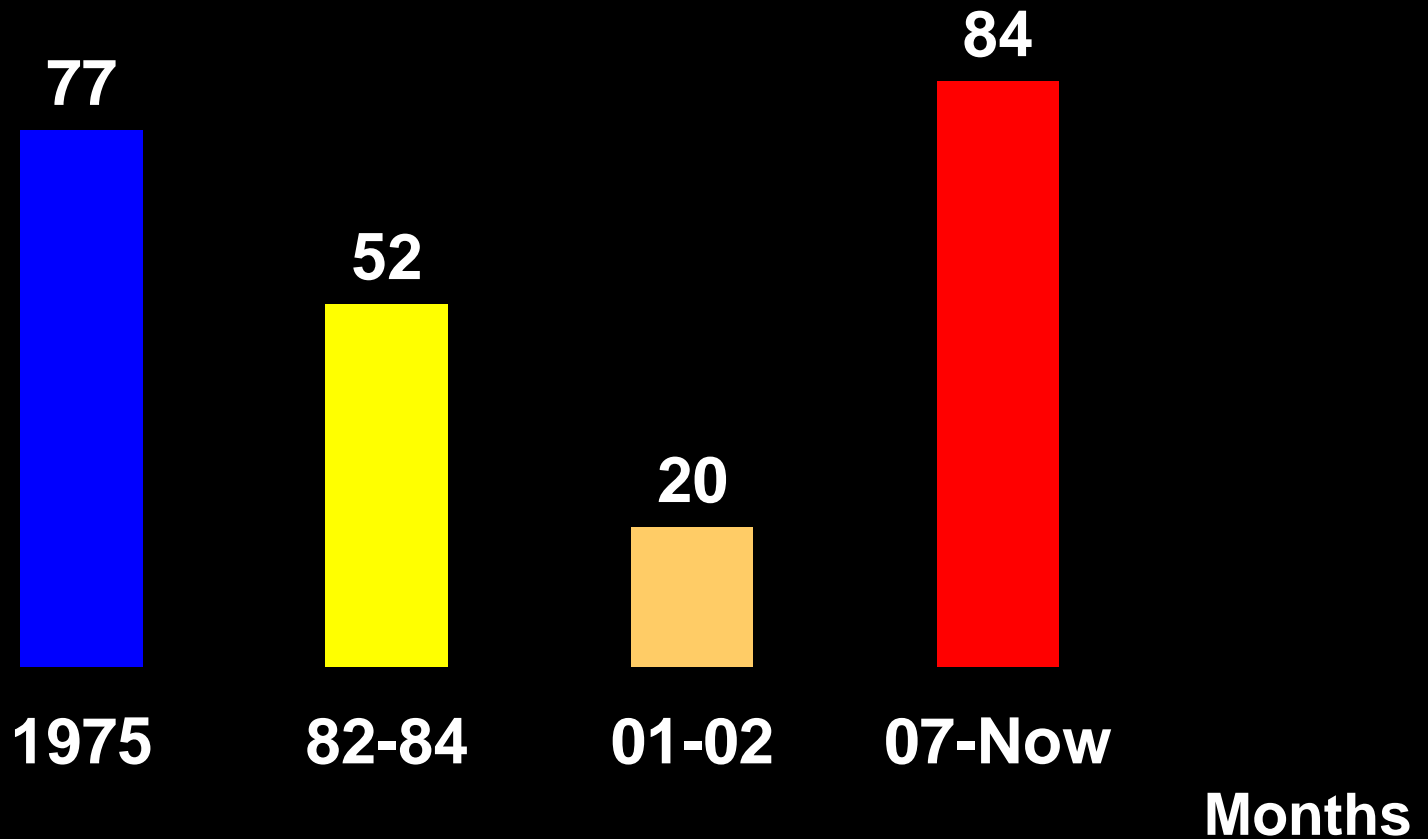


PRSI continues in recession

Monthly PRSI

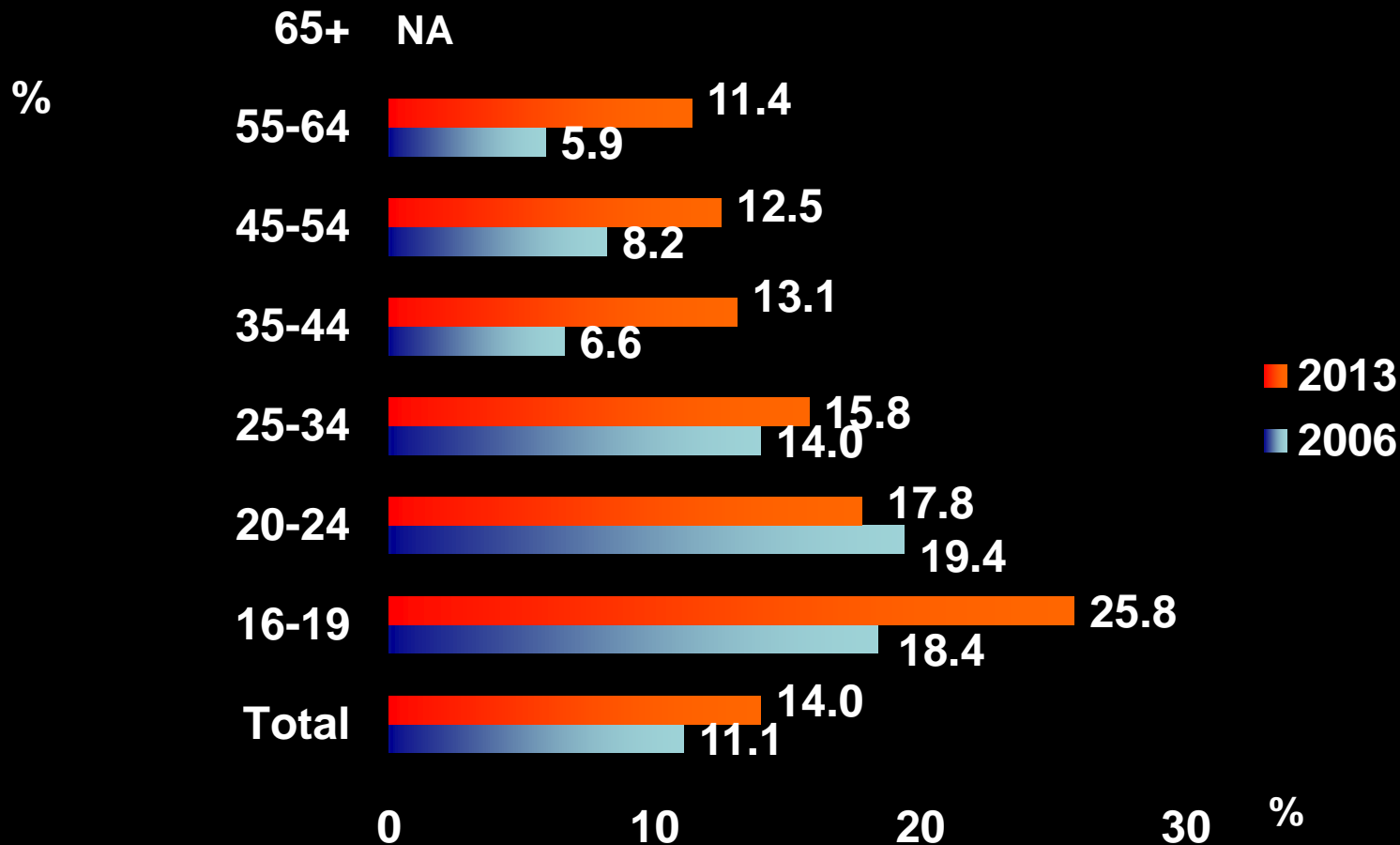


Duration of employment to return to pre-recession levels



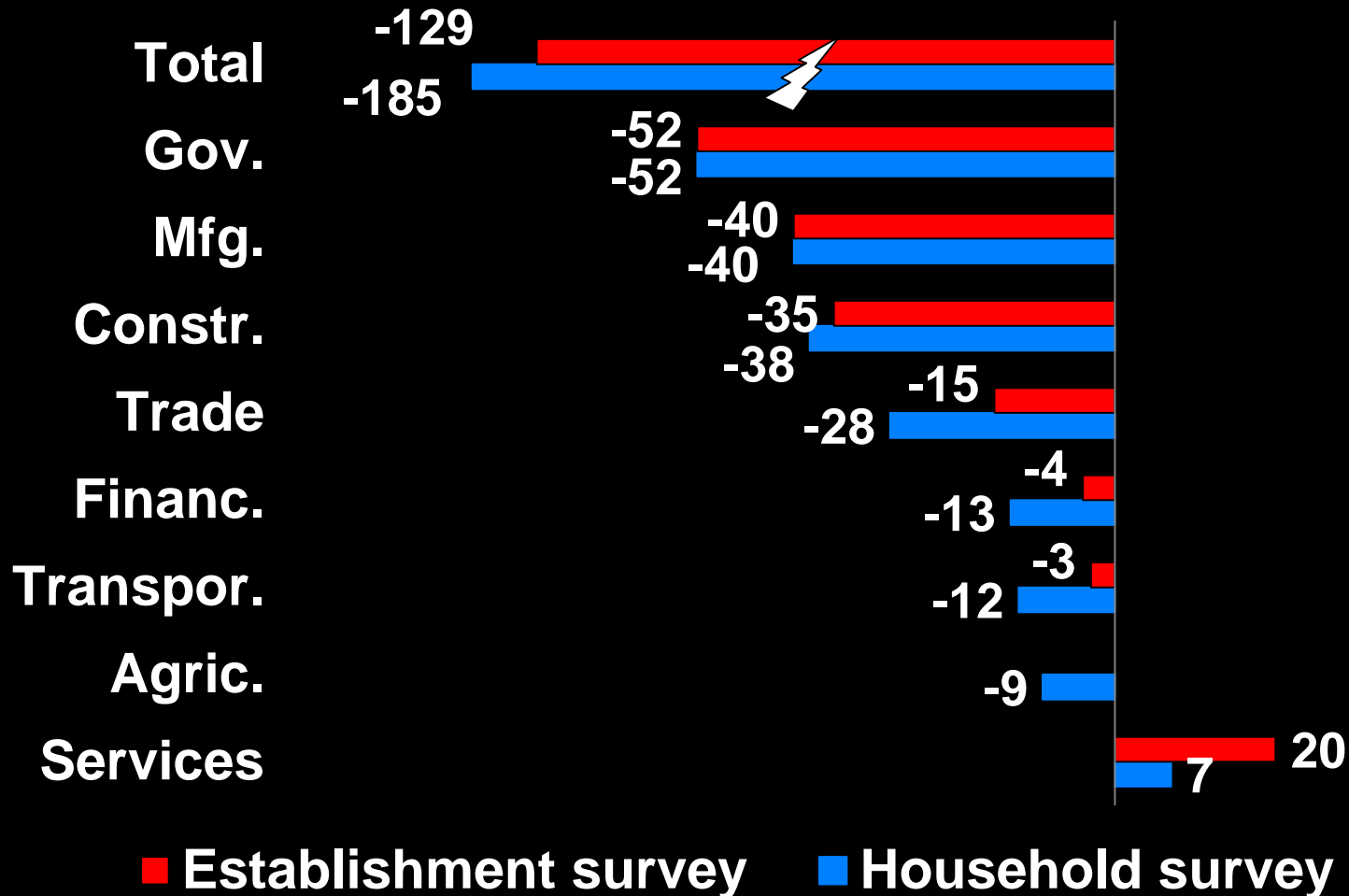
Higher Unemployment in 2013

Unemployment rate by age group, %

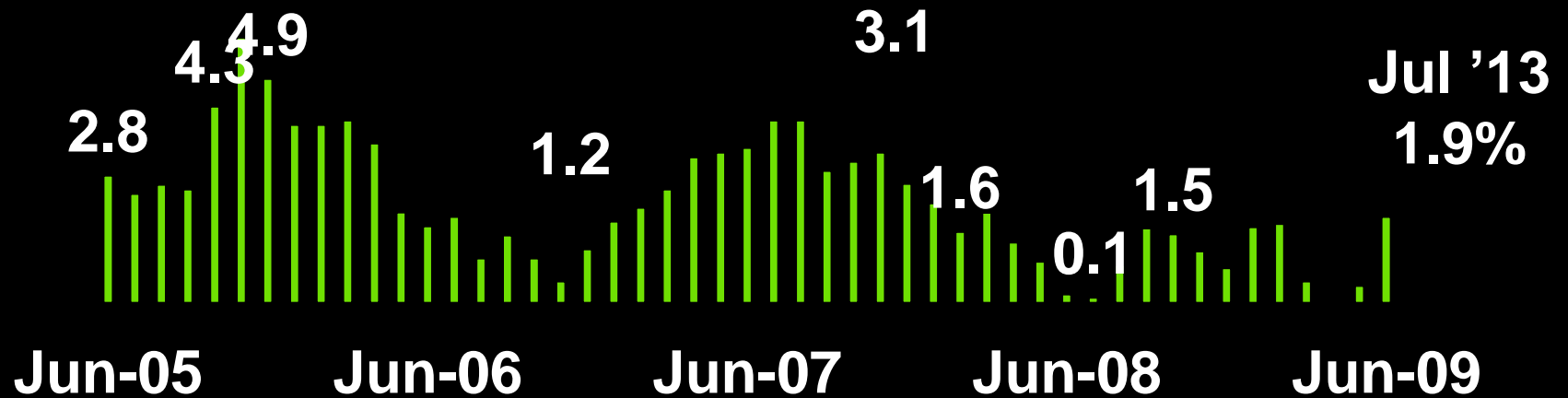


Most impacted sectors

PR employment by sector, FY '05 v. '13, 000s



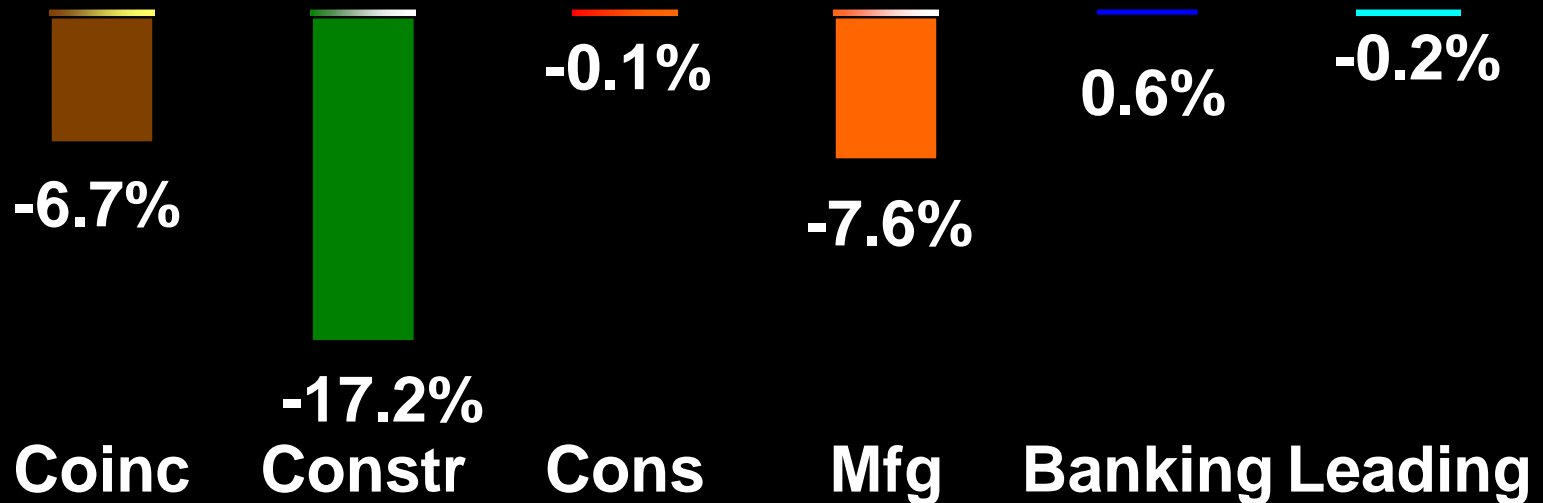
Expect higher inflation



Revised IPC

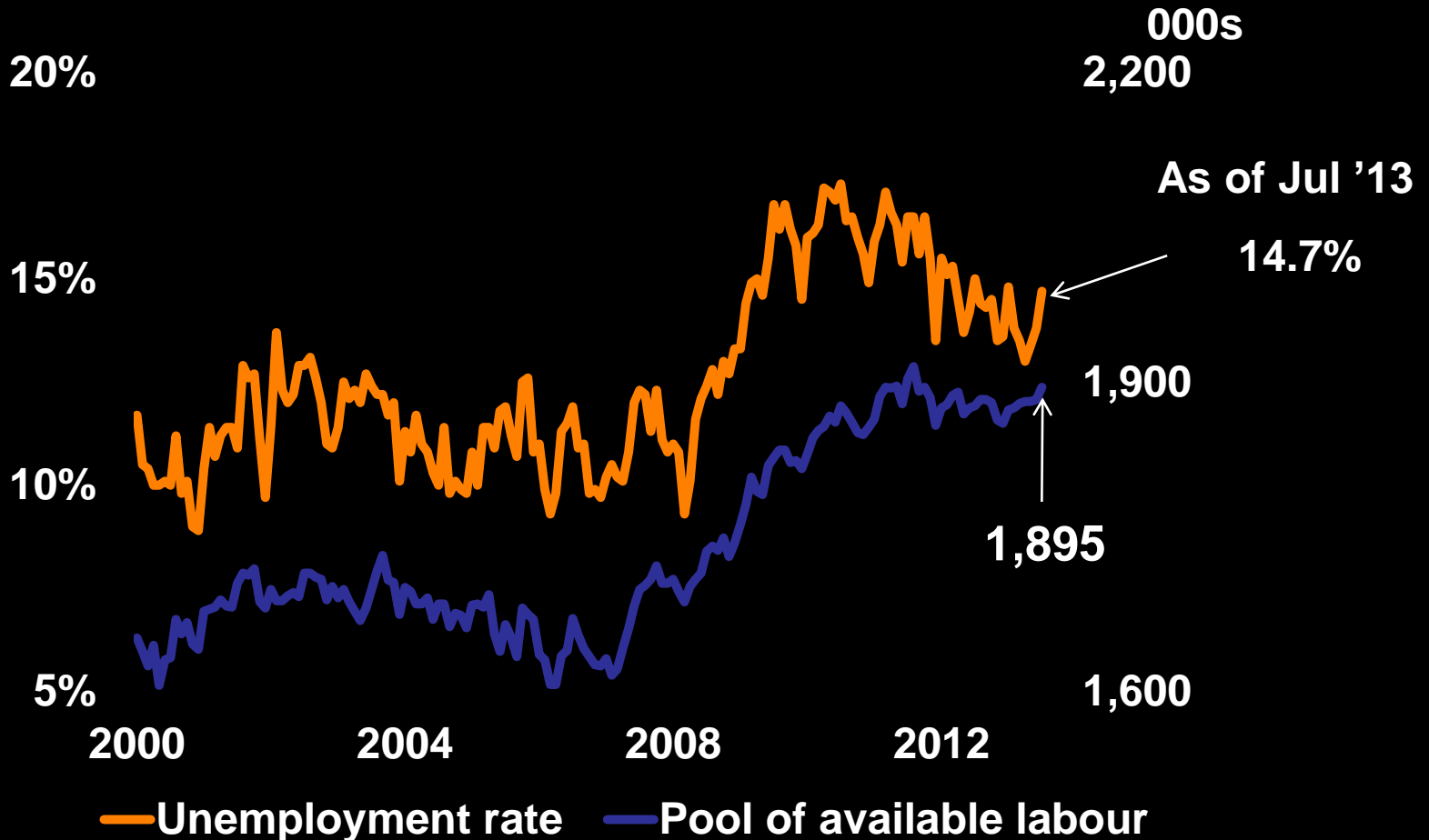
PR posts mixed results

HCCG quarterly economic Indices, 2Q 2013



The job challenge

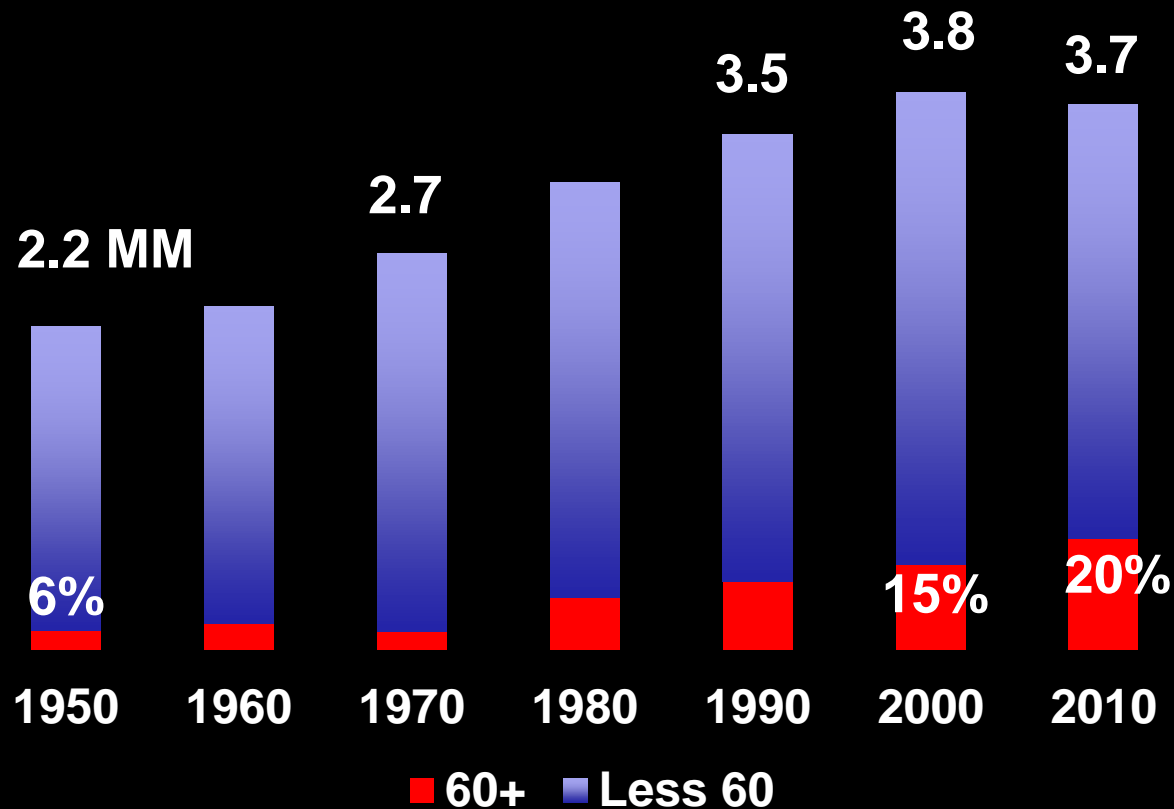
Unemployment still a major problem



Revised change in methodology (2010 Census population)

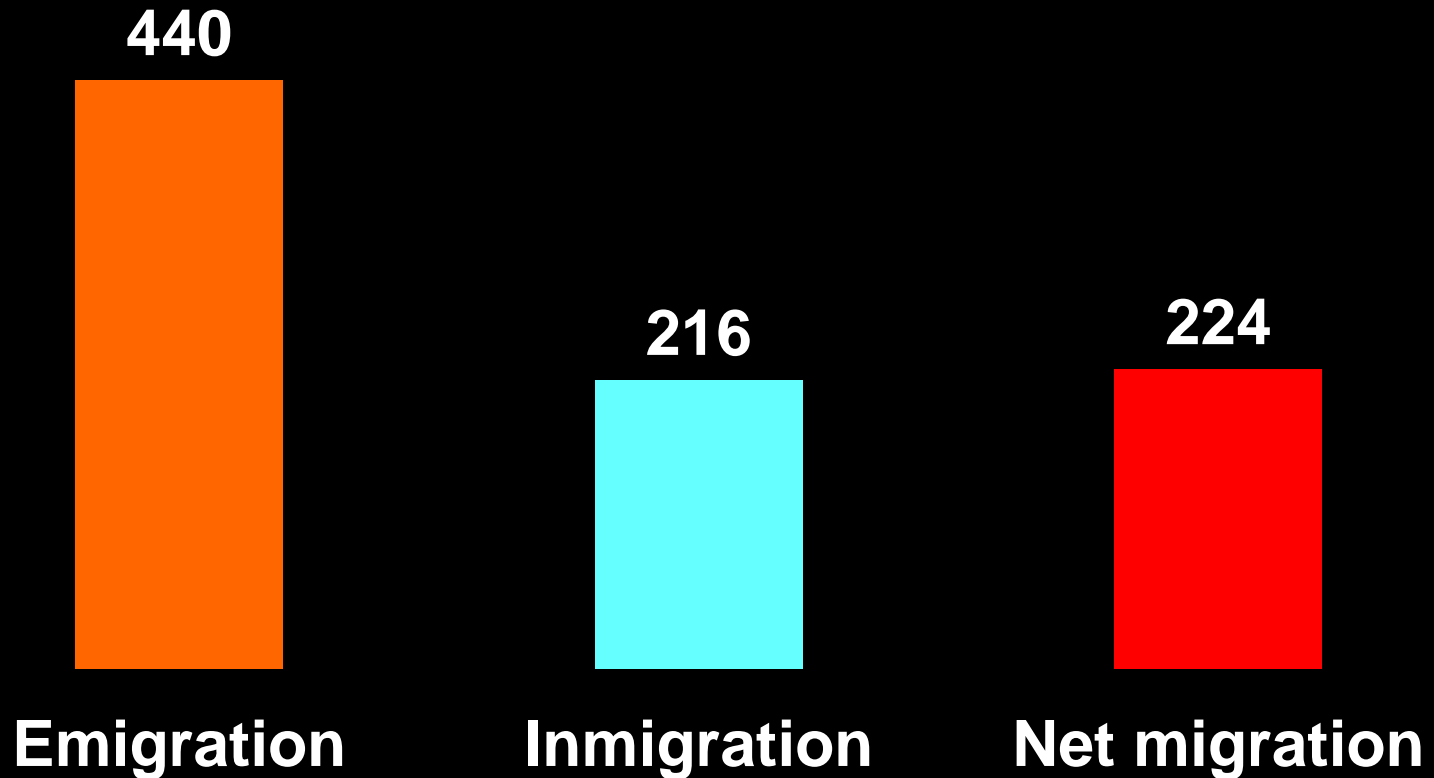
Demographic challenge

PR population, million



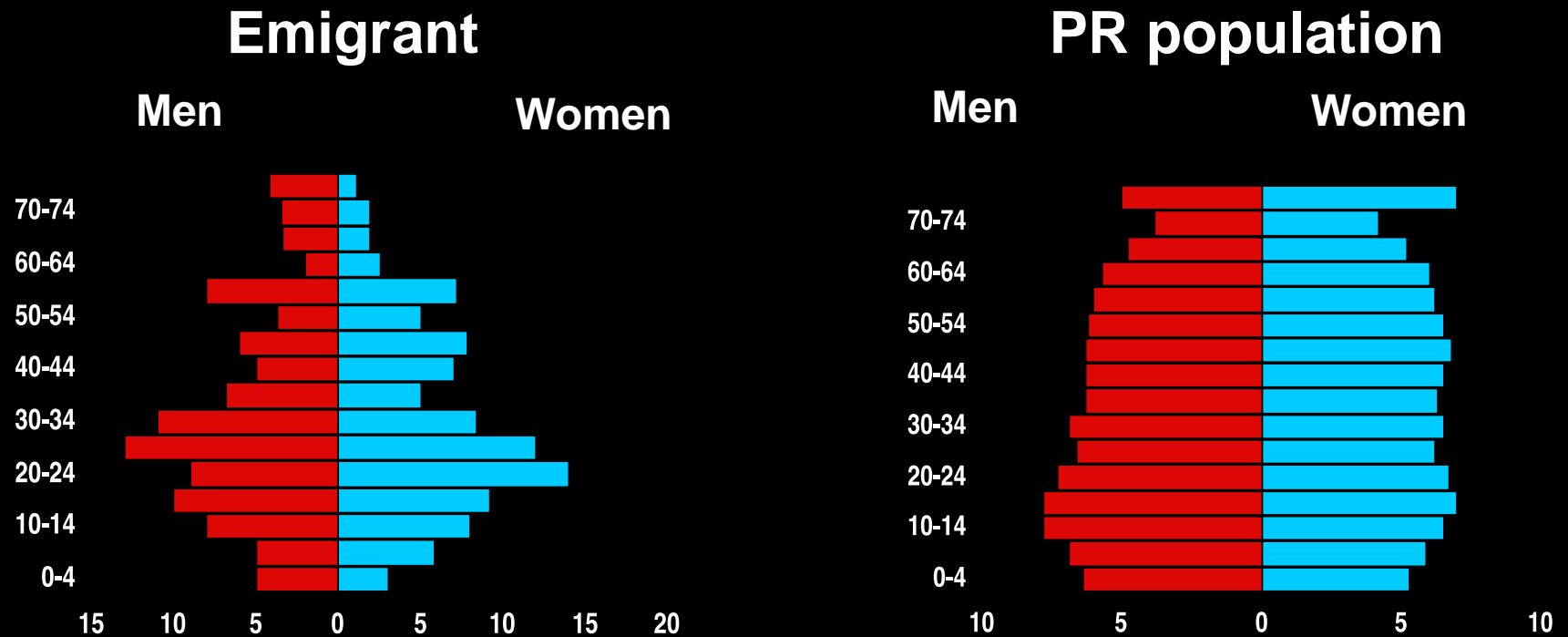
Migration challenge

2005-2011, 000s

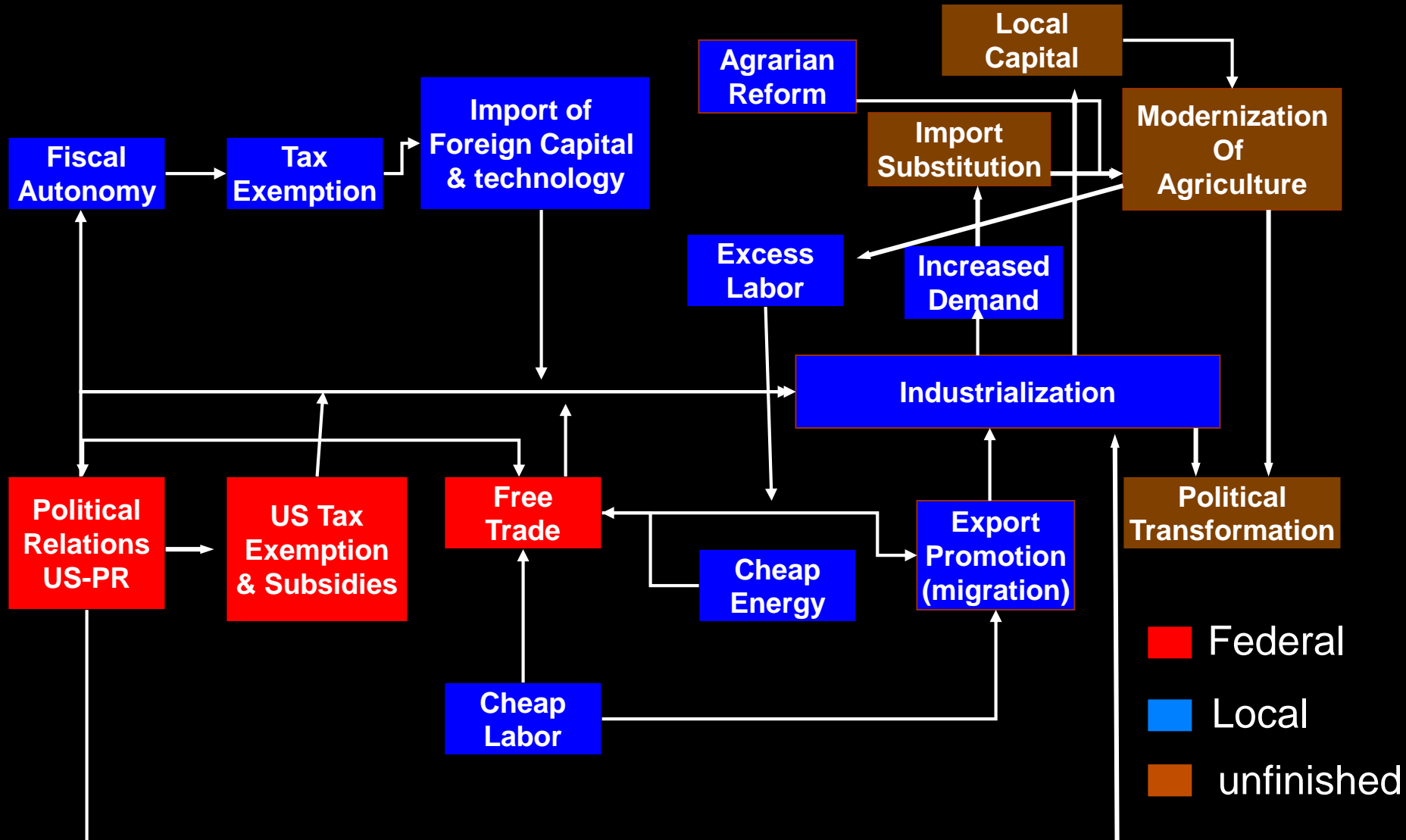


Young people are leaving PR

Population by age group 2011, %

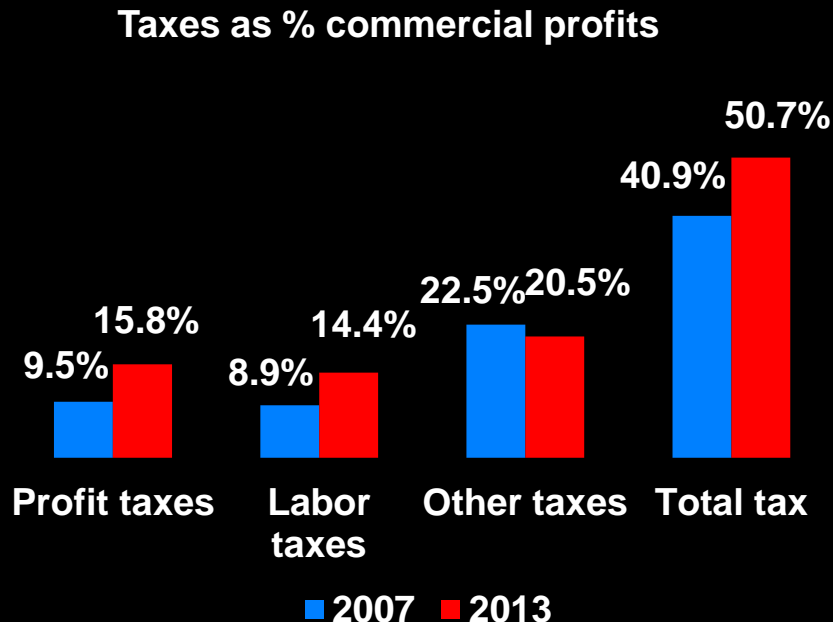


PR economic policy model



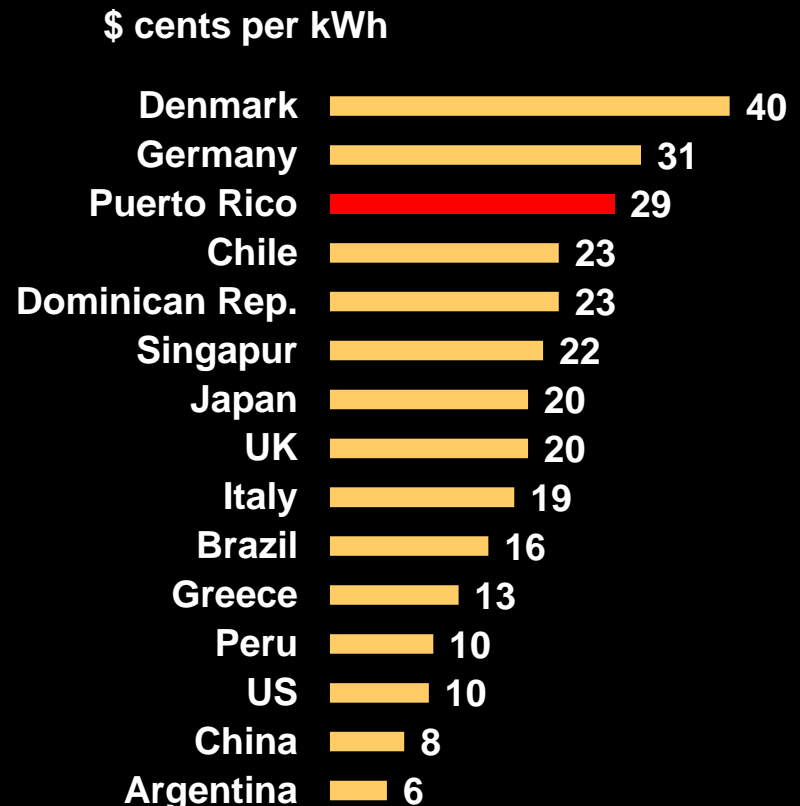
Challenge: Competitiveness

Higher taxes than 6 years before

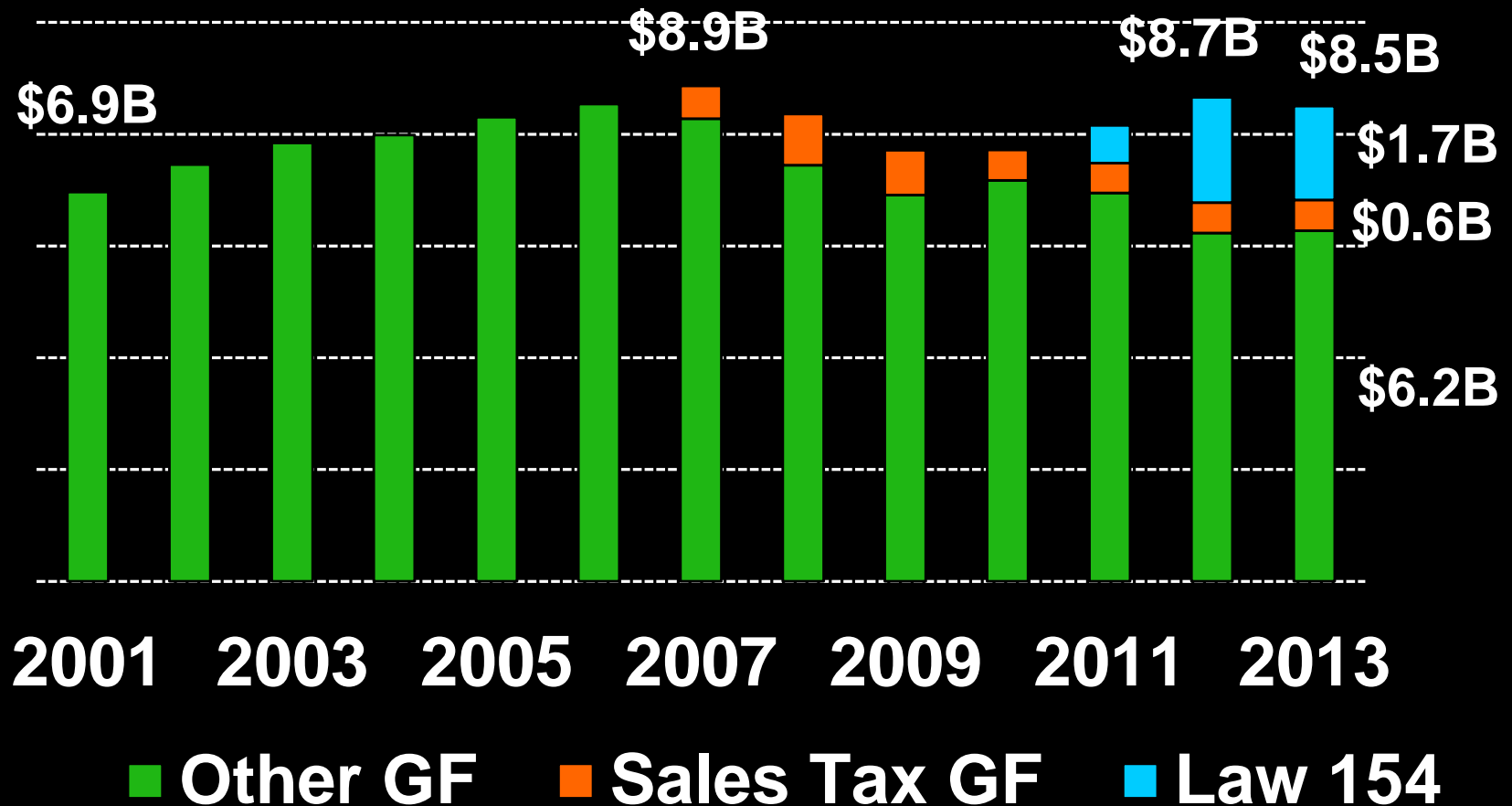


5th obstacle to Doing Business

Electricity cost

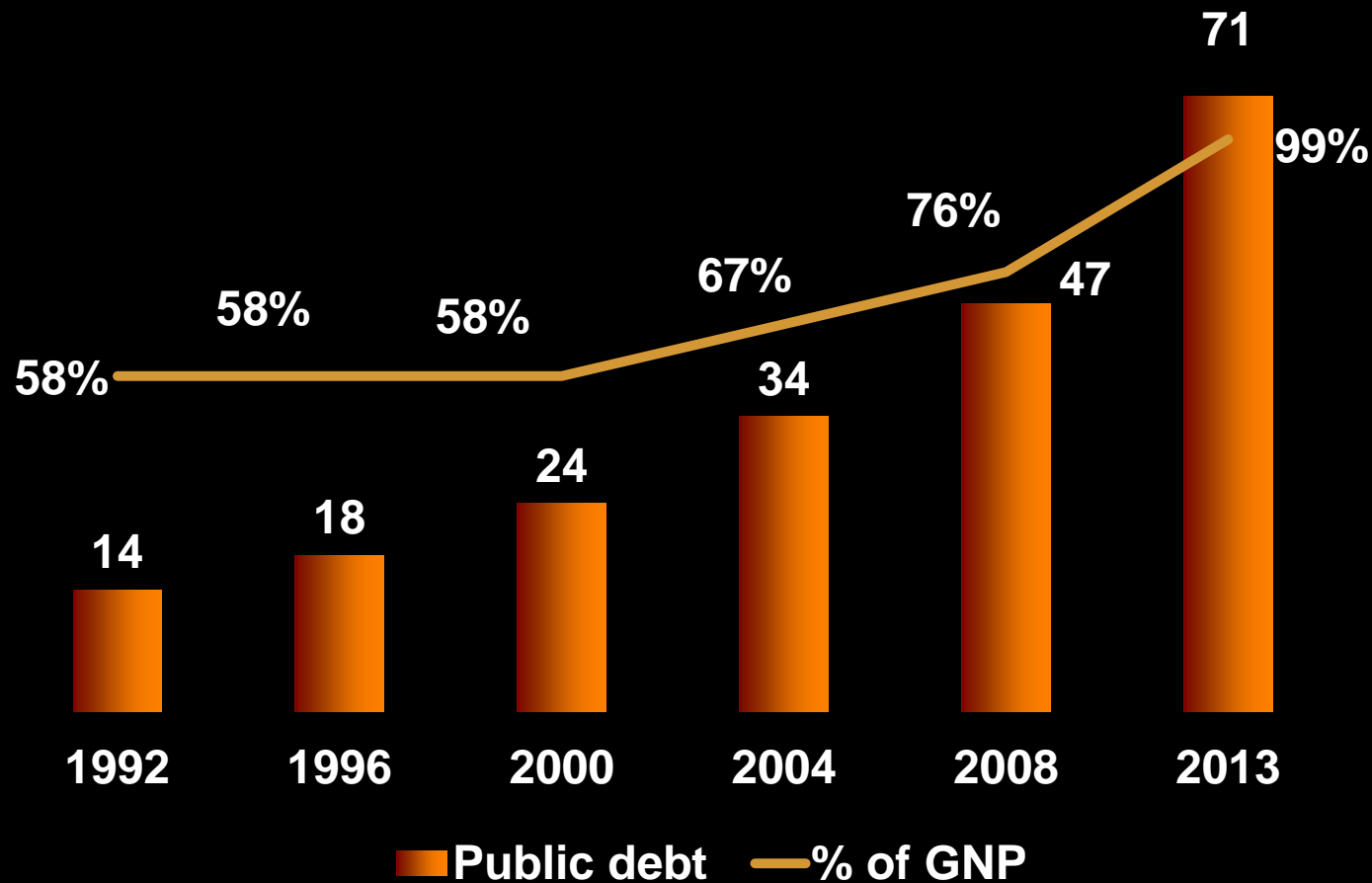


Fiscal revenues challenge



The public debt challenge

PR total public debt, \$ billion



One notch above junk

GO Bonds	Moody's	S&P	Fitch
Prior rating	Baa1	BBB	BBB+
Current rating	Baa3	BBB-	BBB-
Date	Dec-12	Mar-13	Mar-13
Outlook	Negative	Negative	Negative
Junk rating	Ba1	BB+	BB+

What challenges ahead?

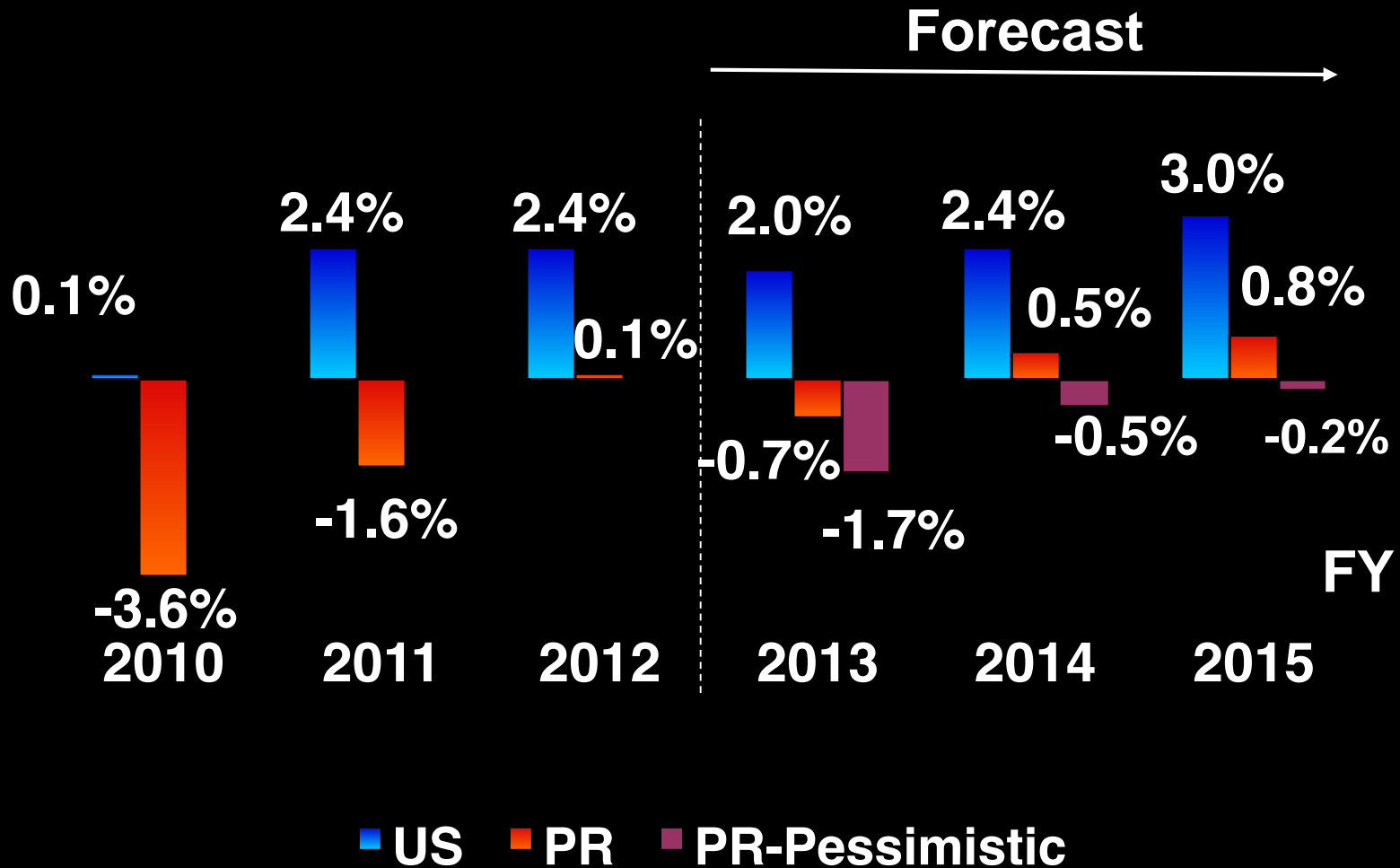
- ✓ **PR' s growth depends on manufacturing and investment**
- ✓ **Public debt must be reduced**
- ✓ **US fiscal woes threaten PR' s budget**
- ✓ **Banking is not jumpstarting the economy**
- ✓ **PR faces many challenges and a very mixed outlook**

In short:

- 1. PR is at a crossroad between fiscal discipline and economic growth**
- 2. Investment has not recovered.**
- 3. Credit remains tight.**
- 4. Labor market does not reflect more jobs.**
- 5. Structural change has not taken place.**
- 6. Road to recovery is uphill.**

Full recovery will take time...

Forecast of US and PR real GNP growth



Consumption & Income

Baseline

	History			Projected		
% change, real	2010	2011	2012	2013	2014	2015
Consumption	1.4%	0.7%	3.0%	1.5%	0.5%	0.7%
Dispos. Income	0.2%	1.8%	-0.4%	-0.6%	-1.6%	-0.2%

Investment

Baseline

	History			Projected		
% change, real	2010	2011	2012	2013	2014	2015
Construction	-14.1%	2.0%	11.0%	-2.8%	-1.7%	2.0%
Machinery	-2.3%	12.9%	1.0%	4.2%	1.2%	-1.8%
Investment	-7.8%	12.8%	4.4%	-1.1%	0.8%	-2.6%

Exports

Baseline

	History			Projected		
% change, real	2010	2011	2012	2013	2014	2015
Exports	-3.9%	1.7%	-4.1%	-1.0%	-1.7%	1.4%

Unemployment

Baseline

	History				Projected	
% change, real	2010	2011	2012	2013	2014	2015
Unemployment	16.3%	16.2%	15.2%	14.0%	14.1%	14.0%

Inflation

Baseline

	History				Projected	
% change, real	2010	2011	2012	2013	2014	2015
Inflation	2.0%	1.8%	2.6%	0.9%	2.4%	1.9%

Expected revenues from new taxes

\$ million

Total PR \$1,490 million

New tax on gross
sales



Higher corporate
income tax rates



Selected B2B

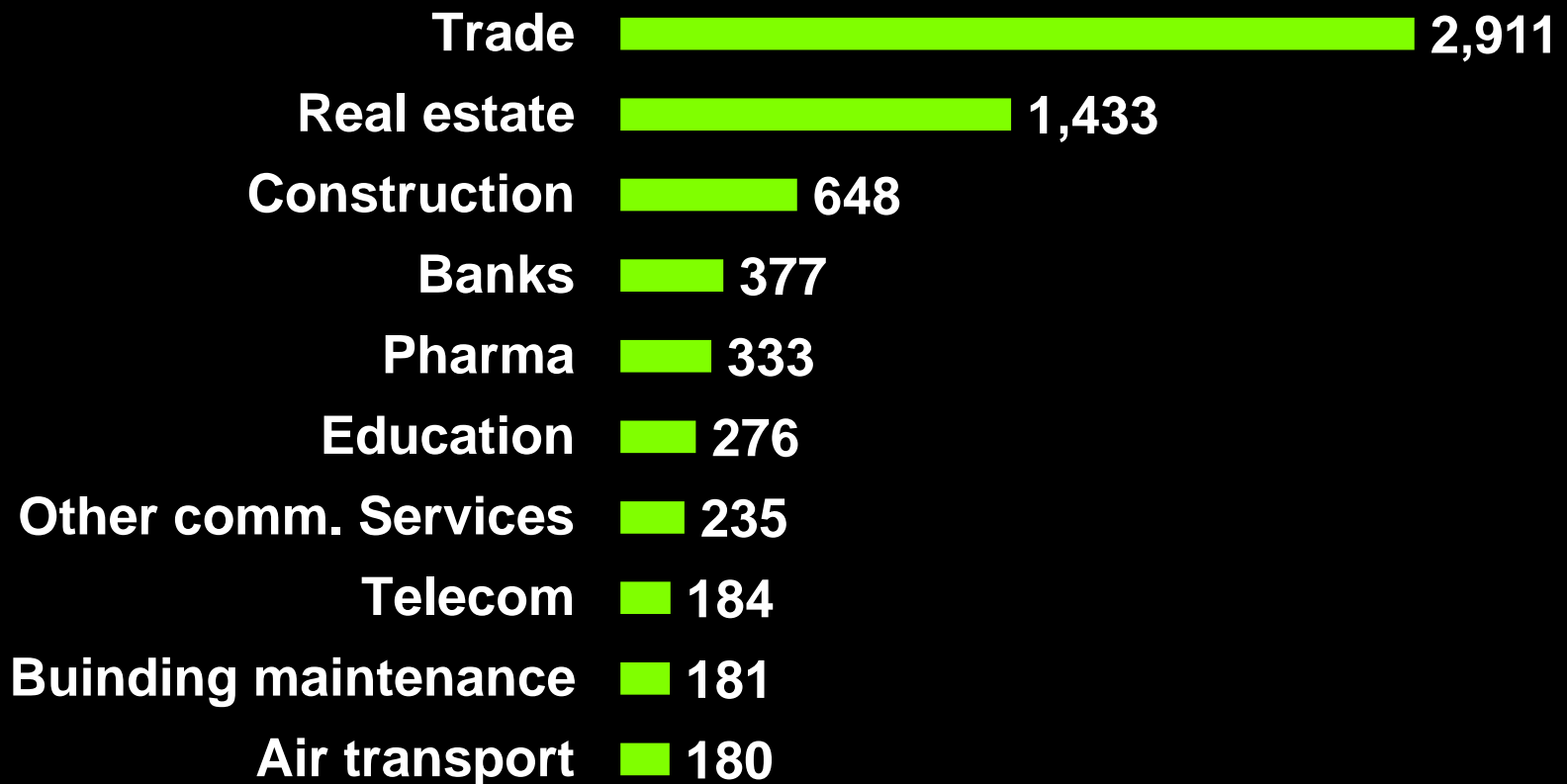


Other



Most impacted industries due B2B Sales Tax proposal

Service intensive Industries, \$ million (2002 prices)



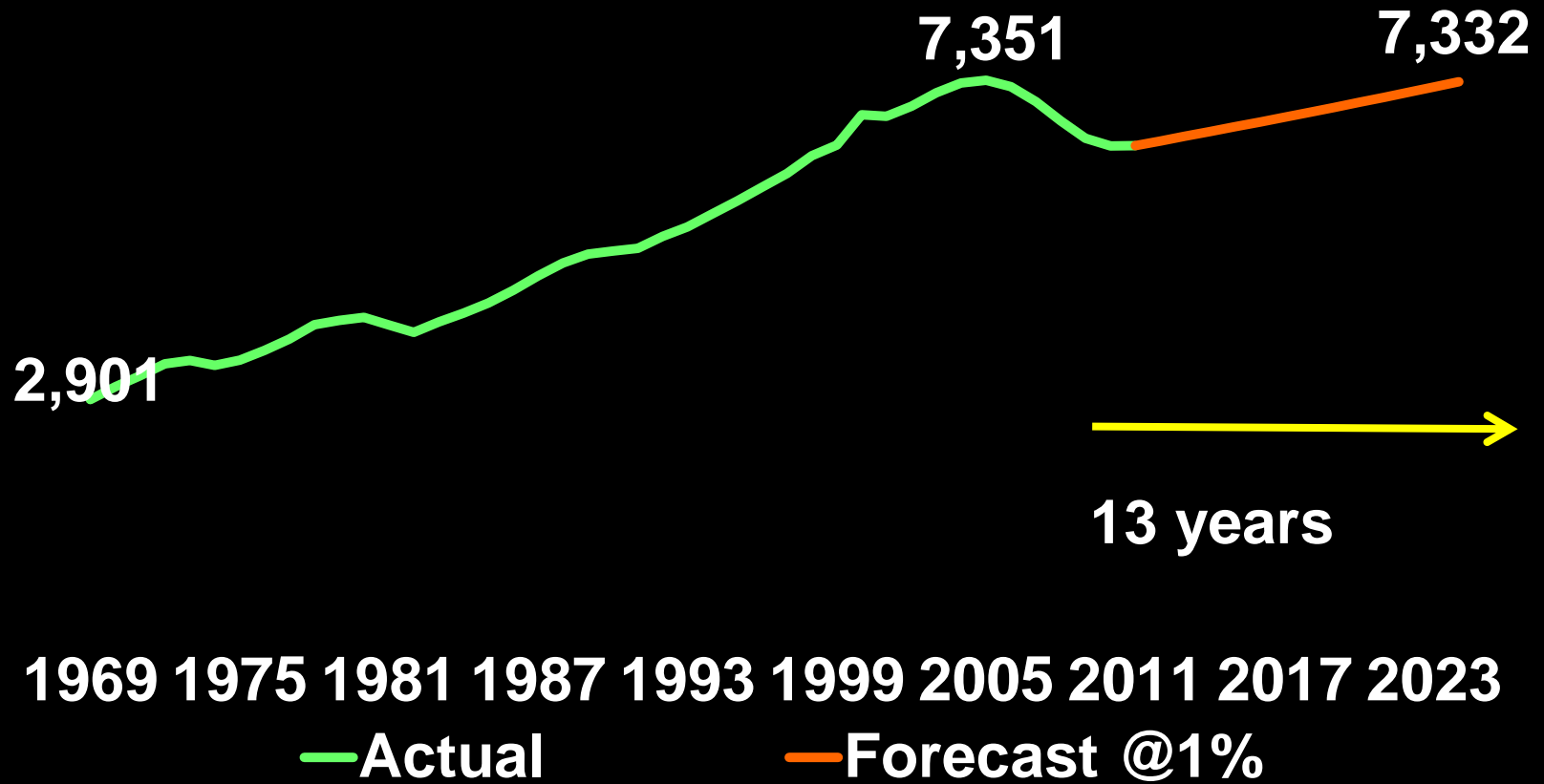
Source: Planning Board, Input-Output Matrix 2002.

Potential results

1. Revenues fall below estimates
2. SUT B2B is to businesses what Law 7 was to the labor market
3. Loss of competitiveness
4. Complex tax system
5. Incorrect use of sales tax
6. Downgrading of GO bonds to junk status

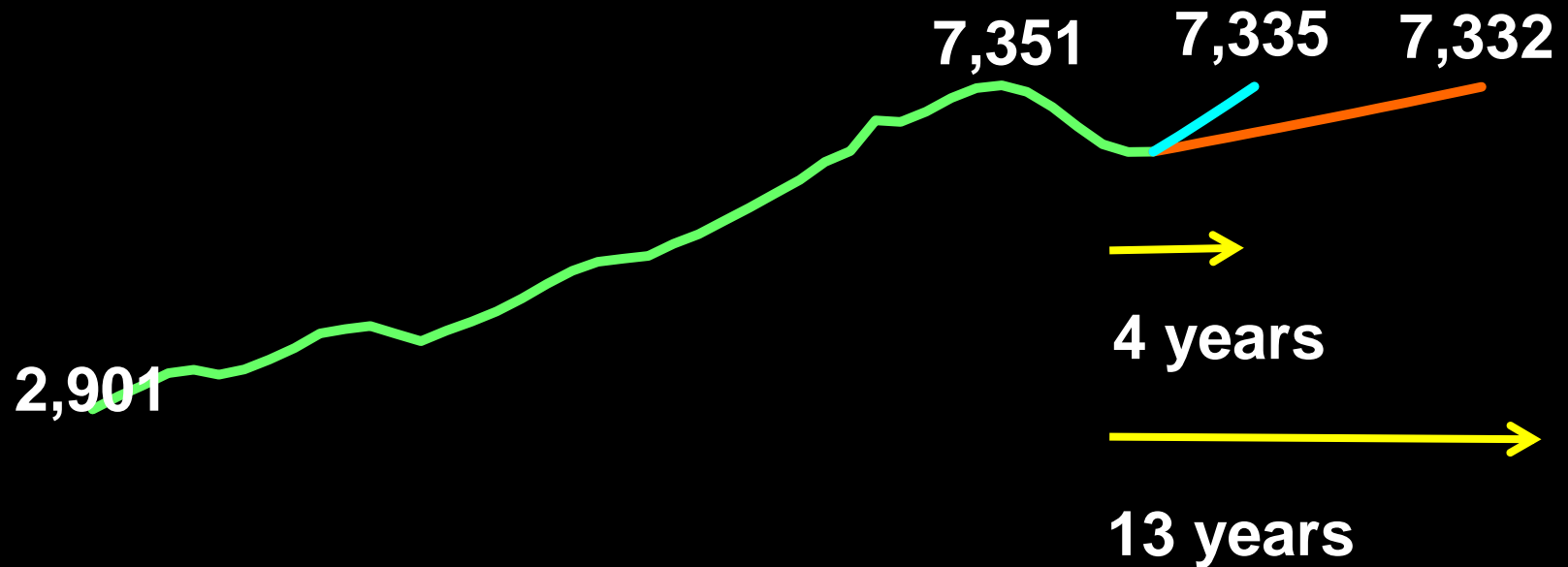
Years to return to 2006 GNP

Real GNP, \$ million



Years to return to 2006 GNP

Real GNP, \$ million

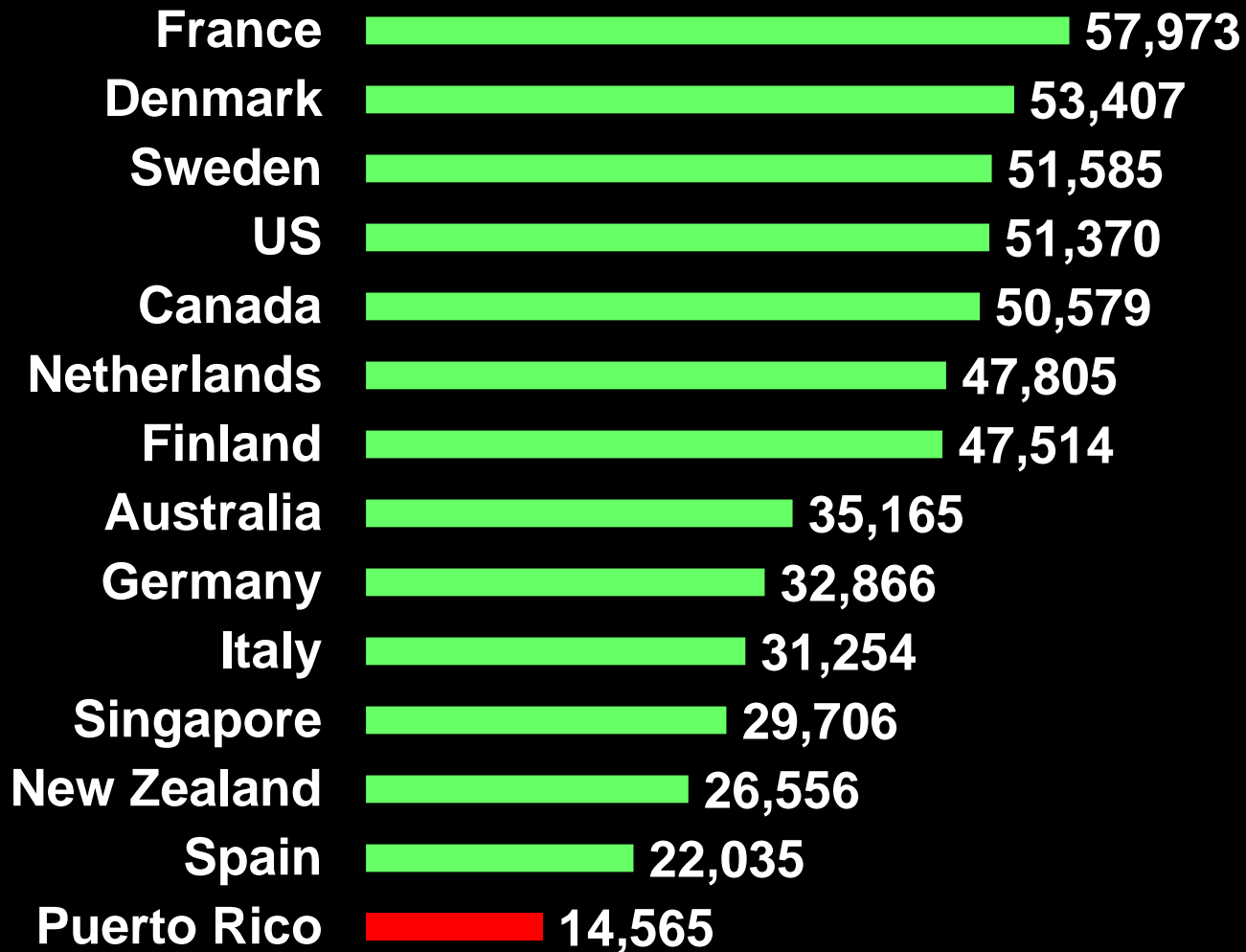


1969 1975 1981 1987 1993 1999 2005 2011 2017 2023

—Actual —Forecast @1% —Forecast @3.3%

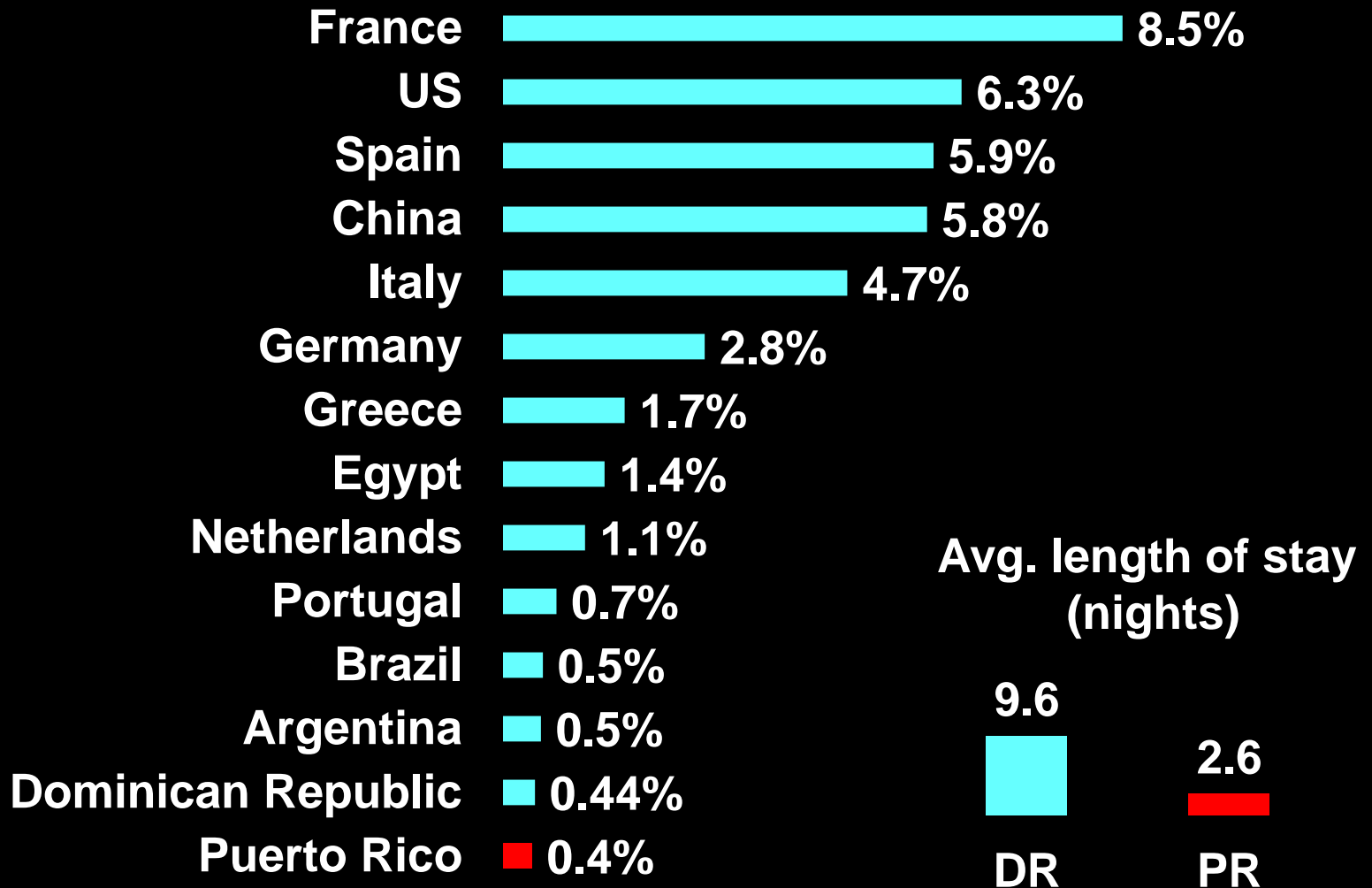
Potential for agriculture

Value added per worker (\$ constant) 2011



Potential for tourism

World tourism market share (% tourists) 2010



Puerto Rico has many assets but not leveraged effectively

Assets	Threats	Outcomes
Strong high-tech	<ul style="list-style-type: none"> • Limited R&D & local linkages • Cost disadvantages 	<ul style="list-style-type: none"> • Firms moving to lower cost locations
Strong services	<ul style="list-style-type: none"> • No promotion of services • Declining quality in education 	<ul style="list-style-type: none"> • Lose services; health & education to region
Hub for Caribbean	<ul style="list-style-type: none"> • Losing lead in infrastructure • Shrinking production industries 	<ul style="list-style-type: none"> • Lose port & exports to Jamaica, et al
Strong human capital	<ul style="list-style-type: none"> • Deteriorating education quality • Ineffective institutions 	<ul style="list-style-type: none"> • Squandering most critical asset
Attractive for knowledge workers	<ul style="list-style-type: none"> • Environmental degradation • Crime and drugs 	<ul style="list-style-type: none"> • Social & physical environment - liabilities
Entrepreneurial spirit	<ul style="list-style-type: none"> • Risk-aversion • Lack of support & Red tape 	<ul style="list-style-type: none"> • No basis for local innovation & industry
Bridge between LA and US	<ul style="list-style-type: none"> • Little focus outside the US • Even in the US, few linkages 	<ul style="list-style-type: none"> • “Neither here, nor there”