CRECE
CENTRO PARA RENOVACIÓN ECONÓMICA, CRECIMIENTO Y EXCELENCIA

ROAD TO PROSPERITY NEWSLETTER

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The Center for Economic Renewal, Growth, and Excellence (CRECE, for its Spanish acronym) and Intelligent Economics have partnered to bring you the ***The Road to Prosperity Newsletter***. This periodic publication offers concise yet comprehensive economic analyses, providing insights for informed policy decisions that advance free entrepreneurship and economic freedom in Puerto Rico. From industry overviews to policy impacts, each issue is crafted to be an essential source of information with a primary emphasis on Puerto Rico's recovery efforts post-María and post-COVID, complemented by insights into U.S. and global trends.

US government spending is costing citizens

The US government is rapidly increasing spending and adding approximately $1 trillion to its debt every 100 days. On January 4, 2024, the U.S. government debt surpassed $34 trillion compared to $33 trillion on September 15, 2023 and $32 trillion on June 15, 2023.

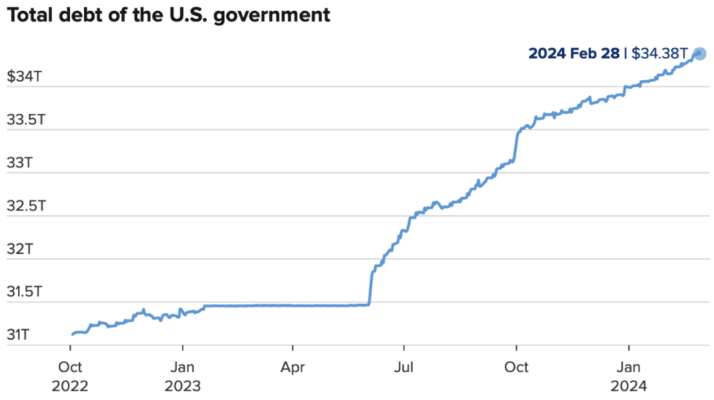
In the past three decades emergency spending has incurred nearly $2 trillion in accumulated interest costs. The United States faces a deteriorating fiscal outlook, with projected net interest costs surpassing the defense budget this year and public debt exceeding World War II levels by 2028.

Given the historical trend of deficit-driven emergency spending, it's imperative to adopt a fiscally responsible approach and offset new expenditures. While Puerto Rico has received over $60 billion in the past decade, the impact in the overall economy can be seen in higher interest rates and inflation.

How does excessive government spending affect the economy and the average citizen? First, it tends to crowd out private investment. When the government borrows funds from the private sector to finance its expenditures, it reduces the amount of capital available for private businesses and individuals, leading to higher interest rates and lower levels of private investment, which can hinder economic growth. Second, increased government spending typically leads to a higher tax burden. Because government expenditures are financed by taxes, when government spending increases, the toll on paying for the increase is on the citizens, who have to pay taxes to cover the increase in spending.

This type of continuous spending by printing money, including for emergencies, is based on the reallocation of needed resources. But unlike the private sector, which allocates resources based on consumer preferences and market signals, government spending is often driven by political considerations, leading to inefficient allocation and wasteful spending on projects that may not yield significant societal benefits. Citizens can demand for more responsible spending by advocating for sound policy that is backed by economic analysis.

Third, excessive government spending financed by borrowing or printing money can lead to inflationary pressures. When the government increases the money supply to finance its expenditures, it can erode the value of money, decrease purchasing power, and lead to price instability, ultimately harming savers and fixed-income earners.



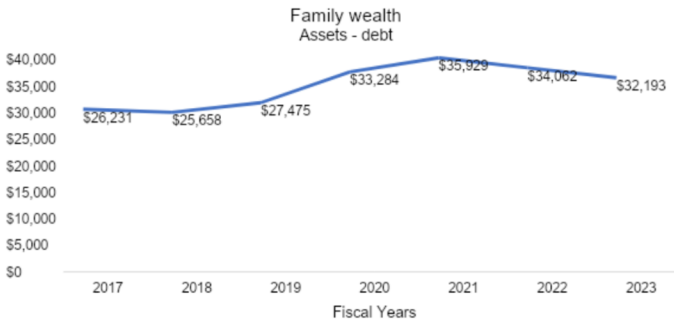
At the last meeting, on January 31, 2024. members of Open Markets Committee of the U.S. Federal Reserve had already warned that reducing rates would have to wait until inflation reached 2%. In March inflation stood at 3.5%, leading the Federal Reserve to delay plans for a reduction in interest rates for later in the year, or until inflation falls to the desired target of 2% or below.

The Federal Reserve has raised interest rates 11 consecutive times since March 2022 and has kept them unchanged since July 2023. Currently, rates are between 5.25% and 5.50%. With 2024 being an election year we will have to wait and see how tight of a leash can Congress keep the Executive Branch with spending.

Declining wealth of family's in Puerto Rico

According to the Economic Report to the Governor published by the Puerto Rico Planning Board, the financial wealth of families on the island, which is determined by the disparity between savings and debt, totaled $32.19 billion in fiscal year 2023, a 5.5% decline from 2022. The reduction in wealth can be attributed to a rise in debt levels and inflationary pressures. Still, family's wealth remains above pre-pandemic levels.

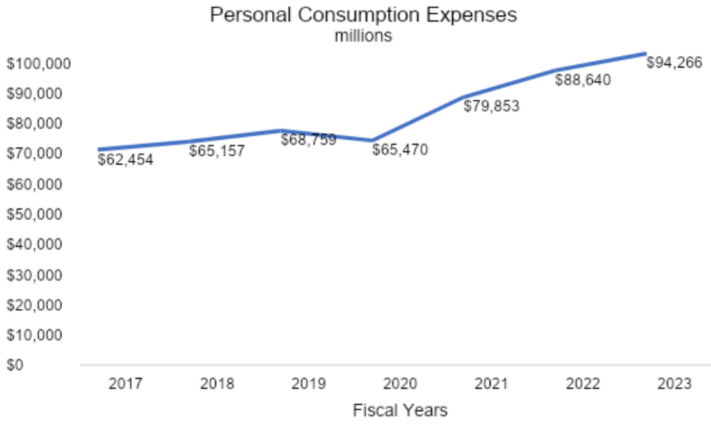
2023 is the second consecutive year of decline after a 21.1% increase in fiscal year 2020 and a 7.9% rise in 2021. The wealth level in 2023 is the lowest recorded since fiscal year 2019, predating the onset of the pandemic. In fiscal year 2023, household financial assets -- which include commercial bank deposits, credit unions, and reserves in pension funds -- reached $61.7 billion, representing a 1.0% increase compared to the preceding year.



Source: Statistical Appendix

On the other hand, family debt reached a record high of $29.48 billion in 2023, a 9.2% surge compared to the previous year. Thus, extending a four-year trend of continuous growth.

The savings rate for families also decreased in the past three years plummeting to -12.6% in fiscal year 2023. A negative savings rate means that families' consumption exceeds income. Meanwhile, personal consumption reached $94.3 billion in fiscal year 2023, an increase of 2.8%.



Source: Statistical Appendix

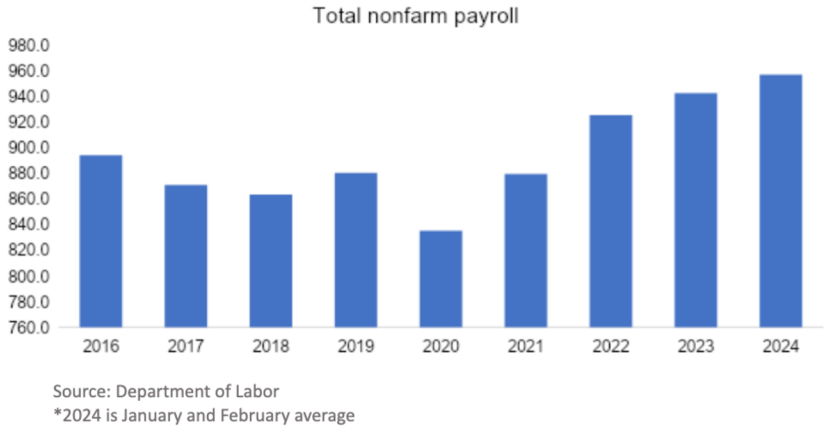
Inflation in Puerto Rico moderated in February

Inflation has moderated in Puerto Rico totaling 1.9% in February, according to data from the Department of Labor and Human Resources (DTRH). It is the second time in four months that inflation is below 2.0%.

Prices rose 0.4% between January and February, the largest month-on-month increase in six months.

Inflation rose due to a 4.1% increase in prices in the Medical Care group – mainly non-prescription medicines (7.0%) and health insurance (6.7%) – and a 4.0% increase in Entertainment.

Source: Department of Labor



Source: Department of Labor
*2024 is January and February average

The price of gasoline decreased 5.4%, clothing prices 3.2% and food prices rose 2.5%. The price of cereals increased 9.5% when compared to the month of February last year. The prices of fish and seafood (-9.7%) and eggs (-20.3%) continue to fall, while beef (5.1%) and fresh vegetables (2.2%) rise.

Inflation in Puerto Rico stood at 3.4% in 2023, below the 6.1% in 2022, the highest in more than 15 years.

Employment in Puerto Rico continues to grow

In February, employment grew by 23,000 jobs, or a 2.5% increase, when compared to the same month last year, totaling 957,600, according to the Department of Labor. Since the pandemic, there have been 35 months of growth.

Employment, which had slowed during the last two months of last year, has returned to growing at a stronger pace.

The unemployment rate stood at 5.7% in February, while the participation rate was 44.5%.

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