

Testimony submitted to “*Puerto Rico’s Ongoing Financial and Humanitarian Crisis: Economy, Debt-Restructuring, and Options for Recovery*,” a forum organized by members of the House Natural Resources Committee and the Congressional Hispanic Caucus, Tuesday, May 2, 2017, at 2:00 p.m. in Room 1310 of the Longworth House Office Building. (Embargoed until the hearing begins.)

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- 1) Puerto Rico is in the midst of one of the most serious debt crises ever experienced in the United States or in any developed country.
- 2) When any political entity has borrowed more than it can pay, it is imperative to restructure that debt in an orderly and fair manner. Ideally, this restructuring will be done once – and only once – and the reduction in interest and principal payments will be sufficient to support essential government services and public infrastructure.
- 3) When debt is not restructured sufficiently or when the degree of austerity imposed is excessive, the reaction of any population is straightforward and completely understandable – they seek to move elsewhere.
- 4) Residents of Puerto Rico are US citizens, with the right to live and work anywhere in the 50 states. Relevant regional job markets are strong, for example in central Florida, and considerable out-migration is already underway. Anyone who moves to the US will likely earn more income, have access to a stronger publicly-supported healthcare system, and also become eligible for the earned income tax credit.
- 5) Creditors to Puerto Rico should focus on this fact: people are the ultimate the tax base and they are mobile. Any attempt to impose onerous terms or to force further austerity will result in more people leaving the island – further reducing Puerto Rico’s ability to repay.
- 6) Similarly, squeezing the income pensioners or government employees further will reduce their spending power and have a contractionary effect on the local

¹ Also a member of the Federal Deposit Insurance Corporation’s Systemic Resolution Advisory Committee, the Office of Financial Research’s Financial Research Advisory Committee, and the independent Systemic Risk Council. All the views expressed here are mine alone. Underlined text indicates links to supplementary material; to see this, please access an electronic version of this document, e.g., at <http://BaselineScenario.com>. For important disclosures, see <http://baselinescenario.com/about/>.

economy. This, in turn, will have a negative impact on local business, with further adverse consequences for tax revenue.

- 7) Undermining essential government services will cause a further deterioration in public infrastructure, including schools and public safety. There is nothing about such a strategy that will help with economic recovery or fiscal capacity. Under this scenario, the humanitarian crisis in Puerto Rico will only worsen.
- 8) Congress passed PROMESA in 2016 in order specifically to allow Puerto Rico access to an orderly and fair debt restructuring process. An oversight board was created in order to facilitate this process.
- 9) The Congressional intent in PROMESA was clear. Puerto Rico should negotiate in good faith with its creditors but, if this did not quickly succeed in creating the basis for a sustainable economic recovery, Title III of PROMESA creates a process through which debts can be restructured subject to court supervision.
- 10) An automatic stay on the payment of debts and on legal action was created by PROMESA, in order to allow time for negotiation – and for the governor to prepare a fiscal plan that would be credible. The oversight board was allowed to – and did – extend this stay until May 1, 2017.
- 11) Given that a voluntary restructuring has not been possible, and with further legal actions by creditors imminent, it is now time to move to the next stage – the court supervised process under Title III of PROMESA.
- 12) Any further delay in debt restructuring will create a greater additional burden on the people of Puerto Rico. More of them will leave the island to seek a better and more stable life elsewhere in the U.S.
- 13) If Congress wishes to provide additional resources to Puerto Rico, for example to address the unfair and unsustainable way that Medicaid (and Medicare) are funded, it is important to do this after the debt restructuring. Money is fungible and it is plausible that creditors may wish to delay the restructuring process if they hope additional funding from Congress will be forthcoming in such a way as to boost debt payments.
- 14) Puerto Rico needs a recovery in private sector activity, supported by essential local government services and robust investment in public infrastructure. This can only take place after a substantial and comprehensive debt restructuring has taken place.