

# Puerto Rico Financial Security Research

## An Expert View

ROXANA TRABANCO

IPSOS Connect

HECTOR ORTIZ

Kranios Marketing

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# Puerto Rico Financial Security Research

# ABSTRACT

# Introduction

- In the last 10 years many Puerto Rico residents have suffered from a serious depletion of their retirement savings and for many others a secure retirement is out of reach. Lack of savings expose individuals to poverty on retirement.
- People of all ages have bought Puerto Rico government secured and unsecured bonds and 30% of the government bond debt is owned by middle class Puerto Ricans. <sup>1</sup>
- Many Puerto Ricans face a triple whammy of pain: their bonds are worth a lot less, their taxes are going up and their home values are plunging because of a mass population exodus from the island. In the midst of the Puerto Rico government financial crisis, island residents have faced enormous pressure in the form of loss of property value which has been the traditional form of saving of the working class. The value of housing stock in Puerto Rico has dropped by 25 percent since 2007 due to the recession and excess supply. The director of the economic consulting firm Estudios Tecnicos, Jose Villamil, reports that the “loss of net worth among Puerto Ricans from the drop in real-estate prices is close to \$30 billion”. <sup>2</sup>
- The Puerto Rico Financial Security Research comes at a time where the factors detailed before have set back the savings and job security of many Puerto Ricans of all ages and social segments and seeks to understand factors influencing savings habits, employer availability of savings programs and to test a savings concept.

1. Heather Long, “I’ve lost over \$200,000 on Puerto Rican bonds”, CNN.com, <http://money.cnn.com/2016/02/22/investing/puerto-rico-debt-bondholders>

2. Staff writer, “House Prices Down 25% in Puerto Rico”, Latin American Herald Tribune, <http://www.laht.com/article.asp?CategoryId=14092&ArticleId=363336>

# Background

- The Puerto Rican debt crisis is an ongoing financial crisis related to the amount of debt owed by the government of Puerto Rico. The island has more than \$70 billion USD of outstanding debt, with a debt-to-GDP ratio of about 68%. In February 2014, various American credit rating agencies downgraded the government's debt to non-investment grade. <sup>1</sup>
- Four factors spearhead the PR financial crisis; 1) reduction of employment since 1976 and large population exodus to the US since 2000, 2) Puerto Rico has a much lower labor force participation rate, at around 40%, than the U.S., where the rate is around 63%. This partly reflects a large informal economy in Puerto Rico, 3) Construction crunched since 2011, 4) Growth in public sector debt, dramatic reduction in tax revenues, increase of tax rates and base, private sector stagnation, and the government's inability to understand the root cause of their problems. <sup>2</sup>
- The crisis has caused Puerto Rico's government to adopt policies that will ideally reduce costs drastically, increase revenues, and spark economic growth so that it can better fund its debt obligations. Puerto Rico's economy has been described as precarious, weak, and fragile, and aggravated by social distrust and unpleasantness. On August 3, 2015, Puerto Rico defaulted on a \$58 million bond payment to the Public Financing Corporation, a subsidiary of the Government Development Bank, while other financial obligations were met. <sup>1</sup>
- The Financial Oversight and Management Board for Puerto Rico was created under the Puerto Rico Oversight, Management and Economic Stability Act of 2016. The Board consists of seven members appointed by the President of the United States and one ex officio member designated by the Governor of Puerto Rico and is tasked with working with the people and Government of Puerto Rico to create the necessary foundation for economic growth and to restore opportunity to the people of Puerto Rico. <sup>3</sup>

1. "Puerto Rican government-debt crisis", Wikipedia [https://en.wikipedia.org/wiki/Puerto\\_Rican\\_government-debt\\_crisis](https://en.wikipedia.org/wiki/Puerto_Rican_government-debt_crisis)

2. Nick Timiraos, "Puerto Rico's Economic Crisis in Five Charts", The Wall Street Journal <http://blogs.wsj.com/economics/2016/06/29/puerto-ricos-economic-crisis-in-five-charts/?mod=e2tw>

3. Puerto Rico Financial Oversight Board Website: <https://juntasupervision.pr.gov/index.php/en/home>

# Objective

- The AARP is interested in understanding better how the current economic environment promotes or detracts from saving, and identify barriers and opportunities for the implementation of a portable savings plan that can be made available to employees through small businesses owners and to independent workers across all sectors.
- To achieve this, our research explored the experiences and knowledge of several experts on: the prominence of retirement savings alternatives, preference by employers and employees, predisposition to save by individuals, and the behavioral and circumstantial reasons that shape the local savings habits.
- A savings plan concept was presented to the experts and input was gathered about its perceived differentiation from the available alternatives, contribution to the financial wellbeing of individuals and the interest of employers, employees and the government in supporting the initiative.

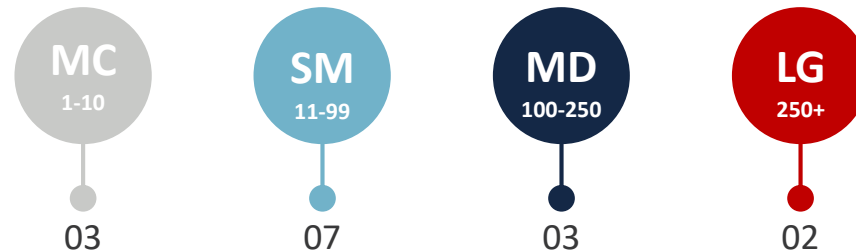
# Methodology

- The research was conducted by IPSOS in collaboration with Hector Ortiz, Senior Strategist of Kranios Marketing Think Tank. Hector has over 35 years of experience in strategic marketing communications, research and planning.
- Fifteen (15) incentivized, one to one interviews were conducted in person among experts in the topic of financial planning. The interviewees were chosen based on availability from a list of pre-approved experts that live in Puerto Rico and who influence or are responsible for policy making, development and/or implementation of financial planning in their businesses and organizations. The sectors included were: financial education, economists, distribution, trade associations and government officials.
- Contact to the experts was initiated with a telephone and personalized email request for a recorded, anonymous in person interview with a short description of the research purpose attached. Interviews were conducted individually and all of them were blind interviews, where AARP was never revealed as the research sponsor.
- Interviews lasted from 45 to 60 minutes, were recorded and transcribed, and utilized a semi-structured guide that allowed interviewees to respond to the requested information while promoting the sharing of related personal perspectives and experiences.

15 FACE TO FACE INTERVIEWS – DECEMBER 6-20, 2016

# Interviewee Profile

Name	Sector	Title	Organization / Company	Empl./Memb.
Benito Morales, CPA	Corporate Consulting	Managing Partner	Pricewaterhouse Coopers - PWC	250
Marta Candelas	Distribution - Foods	VP Administration	Caribbean Produce	160
Yamile Rashid	Distribution - Provisions	VP Human Resources	V. Suarez Group	541
Lcdo. José R. Del Valle Bigelow	Distribution - Beverages	Sr. HR Manager	Coca-Cola Puerto Rico Bottlers	1500
Antonio Rosado	Economist	President	VCF Management	1
Joaquín Villamil	Economist	Chairman & CEO	Estudios Técnicos	28
Myrna Rivera, CIMA	Financial Advisor	CEO	Consultiva Internacional, Inc.	25
José Medina	Financial Educator	Presidente	Finanzas Al Máximo	4
Kurt Schindler	Financial Educator	Education Management	University of Puerto Rico	1
Eugenio Alonso, Esq.	Financial Educator	President & CEO	Consumer Credit Counseling	35
Manuel Cidre	Gubernatorial Candidate 2016	Past President	Los Cidrines Bread & Pastries	1
Rafael Blanco, Esq.	Government/Regulatory	Commisioner	Commisioner of Financial Institutions	94
David A. Rodríguez-Ortiz, CPA	Trade Association - Business	President	PR Chamber of Commerce - CCPR	14/1200
Manuel Reyes, Esq.	Trade Association - Food	President	Cámara Mercadeo, Industria y Distribución de Alimentos - MIDA	6/200
Jesus Vazquez	Trade Association - Retail	Treasurer	Centro Unido de Detallistas (Retailer's Assoc.)	18/5000



Classified by employee count: micro, small, medium and large

# Summary of Findings

## The current state of savings

- Our experts coincide in that saving, “our lifeline for retirement”, has taken a step back to spending for the moment and that our society in general may not have the means to avoid poverty upon retirement.
- Property ownership by the average worker was the principal means of reducing the largest perceived expense upon retirement. This has become a challenge for young workers today who stay at home longer. Property devaluation and lack of market for resale is also challenging the older population owning property.
- The availability of social saving alternatives from the Federal and local government, the vanishing profit sharing plans, the 401K's in large companies and the shrinking industrial sector encouraged saving among a small segment of the population. Contrary to these, SMB's (Small and Medium Business) who provide work to a large sector cannot afford the cost of saving plans while the self-employed face the challenge of lack of discipline or sufficient income to make ends meet and save. Living in the moment has become the norm for many.
- The impact of an insolvent government retirement plan, defaulted and undervalued municipal bonds, poor financial management, distrust, lack of discipline, unemployment or deficient salaries to match cost of living threaten young and old alike.
- When asked about what's missing in the market an expert proposed: a profit sharing plan not based on market share growth, but on future business valuation.

# Summary of Findings

## Feasibility of a portable savings plan

- At first sight our concept was perceived similar to the SS, local government retirement and 401k's programs that roll with you with the plus that it's portable and self-managed with no government involvement which promotes transparency. Special care must be taken to avoid manipulation by special interest groups in favor of their own interests.
- Government could be the big winner since a successful plan could attenuate poverty and help ignite the economy if strategic private local investments are included. The plan must be presented in easy to understand terms that can help the worker to visualize the benefit.
- SMB's could accept and promote if the plan is not a burden in terms of added management expenses. Some even suggested to initiate the saving as the next automatic wage increase but warned that early financial education, an exemplary government, a stronger economy and better wages among the working class are key to its success.
- Some larger employers may consider it unnecessary and could restrain from promoting this plan since a decrease in employee participation in active 401k's may increase overall management cost.
- Not being mandatory became the most frequent barrier, followed by the need of a transparent and credible reporting and management system. A big plus would be the incorporation of a balanced offering of funds and making contributions tax exempt or distributions not subject to income tax.
- Government must be seen as a facilitator but all stressed that must keep hands off its administration. Also, CPA Society, the Retailers association and the large food sector must support this plan. Surprisingly, SHRM who was invited but declined participation in the study was seldom mentioned as a resource.

A WORD FROM OUR EXPERTS

# Puerto Rico Financial Security Research



- “Government has failed the working class”
- “The bad habit of overspending and misspending is evident in workers as well as in our own government”
- “It takes too long to see my savings become anything meaningful, so I’d rather spend in wearables and feel good spending”



- “Boomers had stable work and developed a habit of saving in many ways such as buying property and acquiring government bonds which eventually lost value making many somewhat poor”
- “Gen X have become big spenders and focus mainly on spending to sustain a lifestyle of apparent prosperity vs. the life they can really afford”
- “Poor savings habits among Gen X and Millennials in PR have resulted from the lack of government interest in the topic given that the government revenue is highly dependent on continued consumption across key categories such as retail, automobiles, housing, and utilities”



- “A savings program like the one presented may serve some but will fall short of reaching a the many Puerto Ricans living week by week on minimum wage”
- “The unemployed and parallel economy will be left out of this savings program. These people do not contribute while in their productive stage and become a burden to the system when they become old and unable to work”
- “SMB’s and retail sector employees could benefit most from the proposed savings program if wages improve and the prospect of savings and its role in wealth accumulation is taught in clear terms”



Planning and Saving

# LIFELINE FOR RETIREMENT

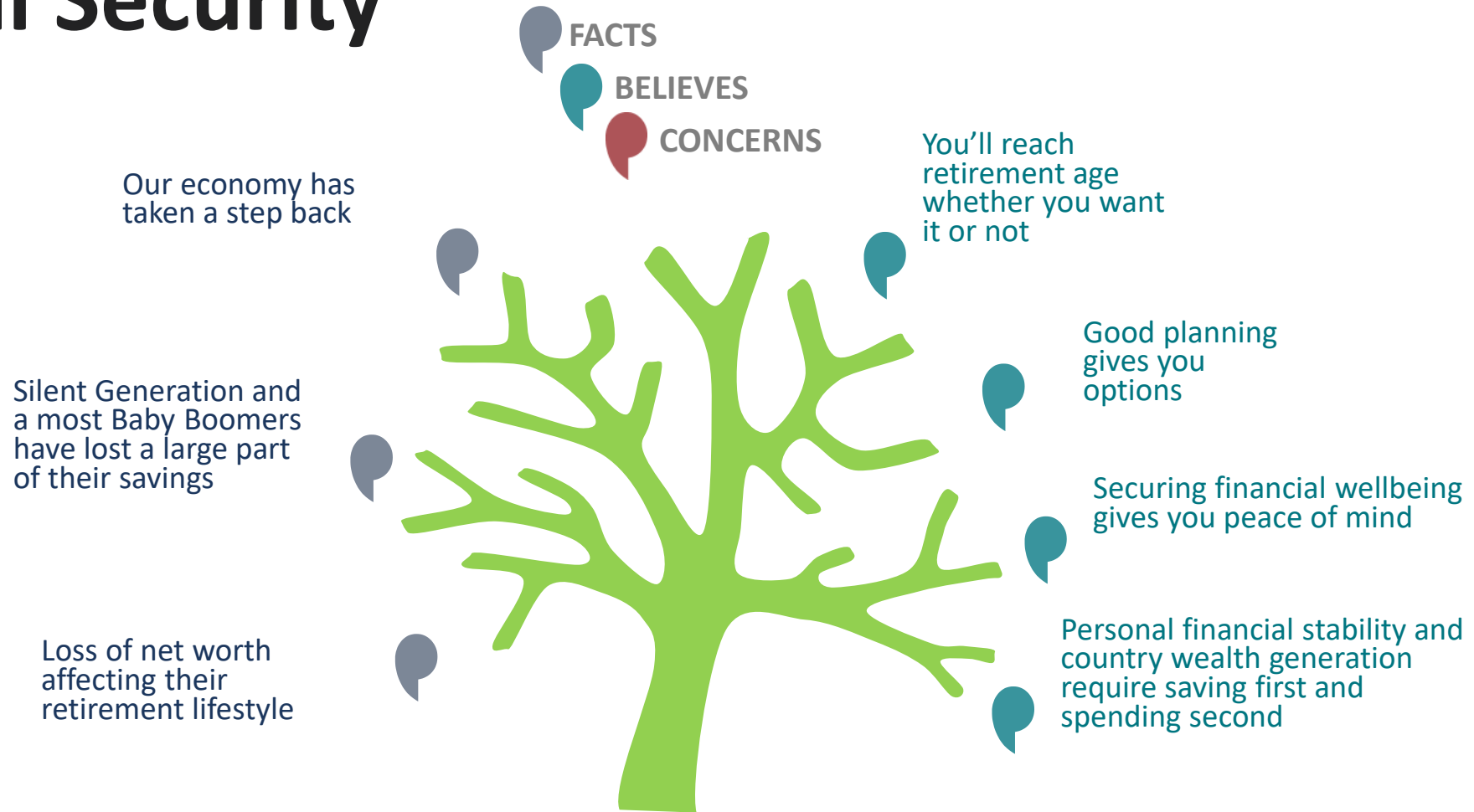
## MEANING

# Financial Planning and Security

- “ Accumulation of resources from an early age to achieve a reasonable quality of life upon retirement
- “ Plan capital accumulation per your expectations upon retirement
- “ Saving to achieve long term security.
- “ Capitalize productive years to achieve sustainability on retirement.
- “ Preventive measures to pay for fixed costs upon retirement.
- “ Accumulation of resources for when you have less.

# Financial Security

## Views and Concerns



- Newer generation will be unable to sustain themselves
- The trend of self-employment may thwart saving.
- Not sure where to place their retirement money safely.
- Government may not be able to stand up to their commitments.
- We're under saved and compromising our future income now.

# Psychology of Dependence

Why aren't we saving more for retirement?

## OUR REALITY

- For over 50 years the state has been the largest employer and a pension plan was instituted. Today that plan is at risk.
- We've been taught that the state, Federal funds, the casinos or horse betting or a winning Lottery ticket would solve our problems.
- The savings message has been inconsistent and the government has not lived up to it.

## RATIONAL FACTORS

- Income may not be enough to meet obligations and still save.
- Easy access to credit promotes excessive spending vs. saving.



Myrna Rivera, Consultiva  
Internacional



## EMOTIONAL FACTORS

- Too many hoping to be saved by the numerous available government programs.
- Poor realization on the consequences
- Living the moment "will not look there"

# Our Population is Under Saved

- Government has and continues to have an important role in employment in PR but the government retirement plan is at risk.
- Add the industrial and service sectors that offer some kind of retirement income and you still have more than 50% of our working



## OUTCOME

LESS MONEY FROM SAVINGS FLOWING INTO THE ECONOMY, MORE WELFARE AND STAGNATION



## KNOWN RETIREMENT INSTRUMENTS

# Top Mentions

Top mentions	401K, IRA, Keogh, Pensions, CERS*, Coops
	<small>*Commonwealth Employee Retirement System</small>
📍 Positive Mentions	📍 Commonwealth Retirement and SS - mandatory
📍 Negative Mentions	📍 Payroll deduction for an IRA – available, not mandatory 📍 IRA too expensive for most small businesses
📍 Most popular retirement plan ✓ Why	📍 401K is the preferred retirement plan ✓ Allows for employer contributions making them more competitive to job seekers
📍 Why aren't retirement plans offered?	📍 Small business, especially, cannot afford them. They give bonuses when possible instead

## EDUCATION AND EXPERT RECOMMENDATION

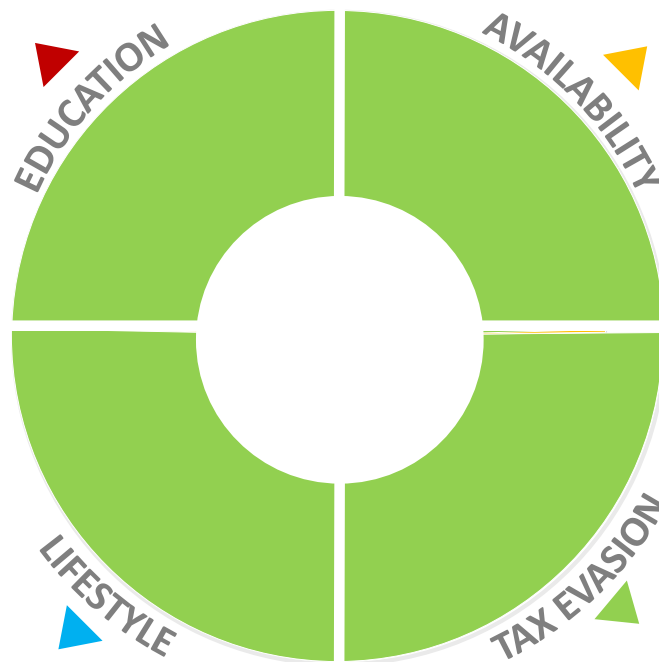
# Top Mentions

Educational Tools	Hiring orientation, annual talks, individual help
<ul style="list-style-type: none"> <li>Method of Implementation</li> </ul>	<p>Most offering a 401K would enroll employee automatically and remove if required</p>
<ul style="list-style-type: none"> <li>Barriers to 401K</li> </ul>	<ul style="list-style-type: none"> <li>Lower income employees do not participate</li> <li>Occasional inability to make contributions</li> </ul>
<ul style="list-style-type: none"> <li>Expert Recommendation</li> </ul>	<ul style="list-style-type: none"> <li>401K is the most recommended.</li> <li>Educators and advisors recommend diversification when possible.               <ul style="list-style-type: none"> <li>✓ Maximize tax deferral benefit of 401K's and IRA's</li> </ul> </li> <li>Savings strategies vary per level of income and type of employer               <ul style="list-style-type: none"> <li>✓ Government employees dream of a life supporting pension are gone and must explore complementary options.</li> <li>✓ High earners in companies prone to benefits can opt for 401K's and IRA's</li> <li>✓ Mid wage earners lacking retirement savings options will keep exploring properties as their way of securing rent income upon retirement.</li> <li>✓ Low wagers lack alternatives.</li> </ul> </li> </ul>

# Barriers to Saving

- Deficient personal finance education.
- Lack of knowledge, discipline, or non-availability from employers.
- Not realizing challenges to be faced upon retirement.

- High spending and level of debt.
- Burdened by extended family needs.



- Limited and inconsistent offering across sectors
- Retailers of all sizes “small to large” not providing options to workers.

- Participants in the underground economy keep most cash stashed to avoid tracking.


EXPERT ADVISE

# How to Promote Saving

**1**

## LEADERSHIP


- A comprehensive HR strategy aligned with a new economic development vision in the government and private sector to improve productivity, wages, and our way of living.



**2**

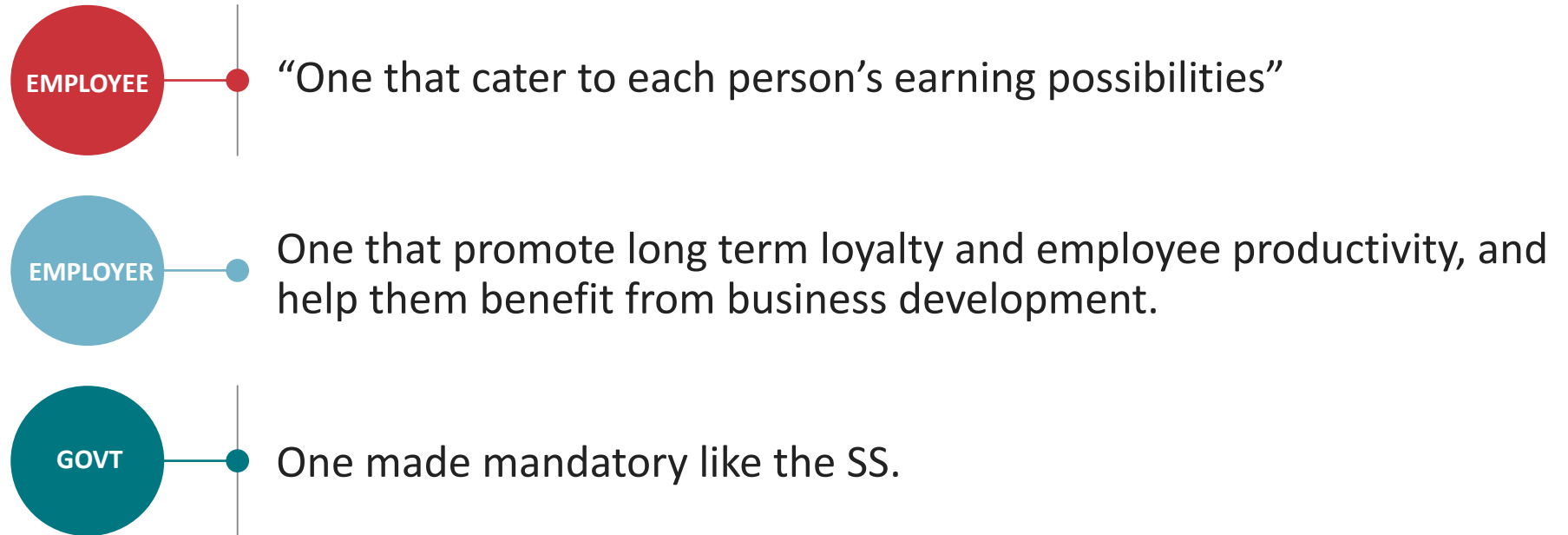
## EDUCATION

- Help workers become aware of where they need to be and start to save now. By showing in simple, easy to visualize ways, and provide support along the way.



EXPERT ADVISE

# The ideal retirement savings plan



## What’s Missing

- 📍 A profit sharing plan not based on market share growth, but on future business valuation:
  - Aimed to build employee engagement, interest in business results and vested with a higher yield of shared revenue.

Retirement Saving Plan

# CONCEPT TEST

## CONCEPT STATEMENT

One way to help more puertorriqueños save for their futures is for the state to promotes a retirement savings plan that would be available to all workers.

More employees in the private sector and in small businesses would have the option to save for retirement automatically out of their regular paycheck.

Participation would be voluntary and if someone chooses to participate, they could have the same retirement savings account at any job.

## DESCRIPTION

- **Promote Financial Freedom:** Social Security alone isn't enough to depend on. These accounts make it easier for workers to grow the additional savings they will need to live a secure and independent future.
- **Give Employees a Choice:** Accounts are voluntary. It's up to employees to decide if they want to participate.
- **Give Employees Control:** Accounts are portable. When employees switch jobs, they can take their accounts with them.
- **Save Taxpayer Dollars:** Giving employees a simple way to save for retirement will mean fewer people will need to rely on government safety net services, which will save taxpayer dollars.
- **No Risk:** Would be easy for employers to set up, and there would be no ongoing costs or risk to the employers or the state.

# Compared to Other Programs

## SIMILARITIES

- Commonwealth Retirement Programs, the SS and an IRA in that they roll with you.

## LIKES

- Open to everyone
- Perceived transparency and control over savings

# Can this program help solve a problem?



YES






- In the long term it could attenuate poverty in the Golden years.
- If the economy flourishes and financial planning is promoted across all sectors.
- Local economy could benefit if some of the funds include investments in local business such as bank shares and in low risk strategic development initiatives.
- Good Complement to Social Security



NO

- No savings plan can be achieved on minimum wage.

# Who Benefits Most

-  SMB's who do not have the capacity to pay high administrative costs for managing a savings program
-  Retail and wholesale employees, especially sectors of high rotation such as supermarkets and mass merchandisers
-  Higher waged employees of SMB's who lack employer sponsored programs. Employees who feel that the close monitoring capability allowed by this program make them feel in control of their savings vs. other alternatives
-  Companies in competitive sectors such as agribusiness, small businesses and independents could consider this an alternative to the non-availability of a 401K
-  The government who gets to reduce dependency

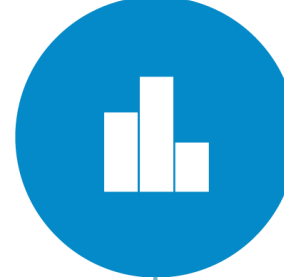
# How does Puerto Rico benefit from this initiative



Could be the beginning of a turnaround in savings habits.



Somewhat reduce dependency on government later in life.



Making money available upon retirement would help keep the economy healthy.



An alternative to a government plan that is proving impossible to sustain.

# Level of interest in a plan like this



Employees of larger companies may not be too interested since their limited savings capacity would split between employer sponsored plans and this personal plan.



Why consider this plan if they have the option of making post tax contributions to their 401k plan or get a tax deferred IRA and end up better up.



Would depend on interest rates compared to traditional savings accounts.



Support will depend on the level of continuous education and promotion.

## THE EMPLOYER'S PERSPECTIVE

# Opportunities



● Cautious with the administrative cost and burden to service.



● Could be a viable alternative that many SMB's cannot provide



● Employers should be allowed to deposit to an employee account on their behalf as a giveaway. Can be portrayed as a salary increase helping to gain employee goodwill and loyalty.



● Pooling up savings from many employees could result in very low management costs thus increasing yield

## THE EMPLOYER'S PERSPECTIVE

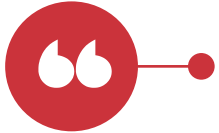
# Barriers



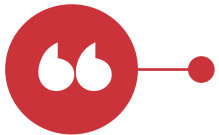
Given the economic constraints of most workers, if not mandatory, a low level of participation can be expected.



Lack of knowledge of the average employee of how the markets work.  
Comparable IRA alternatives provide a tax advantage but aren't being capitalized by workers.



Transparency and credibility of fund managers given the high profile of bad news related to poorly managed government retirement funds and the local bond market losses.



Lack of ability to save given that low base of compensation in PR. Family of 4 earns Avg. \$28K or \$7K per capita.

## THE EMPLOYER'S PERSPECTIVE

# Barriers

- “ Financial markets delivery of very low yields may deter savings.
- “ Comparable IRA alternatives provide a tax advantage but aren't being capitalized by workers.
- “ Administrative costs and competition with employer sponsored plans.
- “ Unsophisticated businesses with few employees that do not have adequate accounting practices.

# Should the government support this plan?

Historically, healthy economies have relied greatly on the capacity of workers to save in their productive years and inject those savings back into the economy later in life.

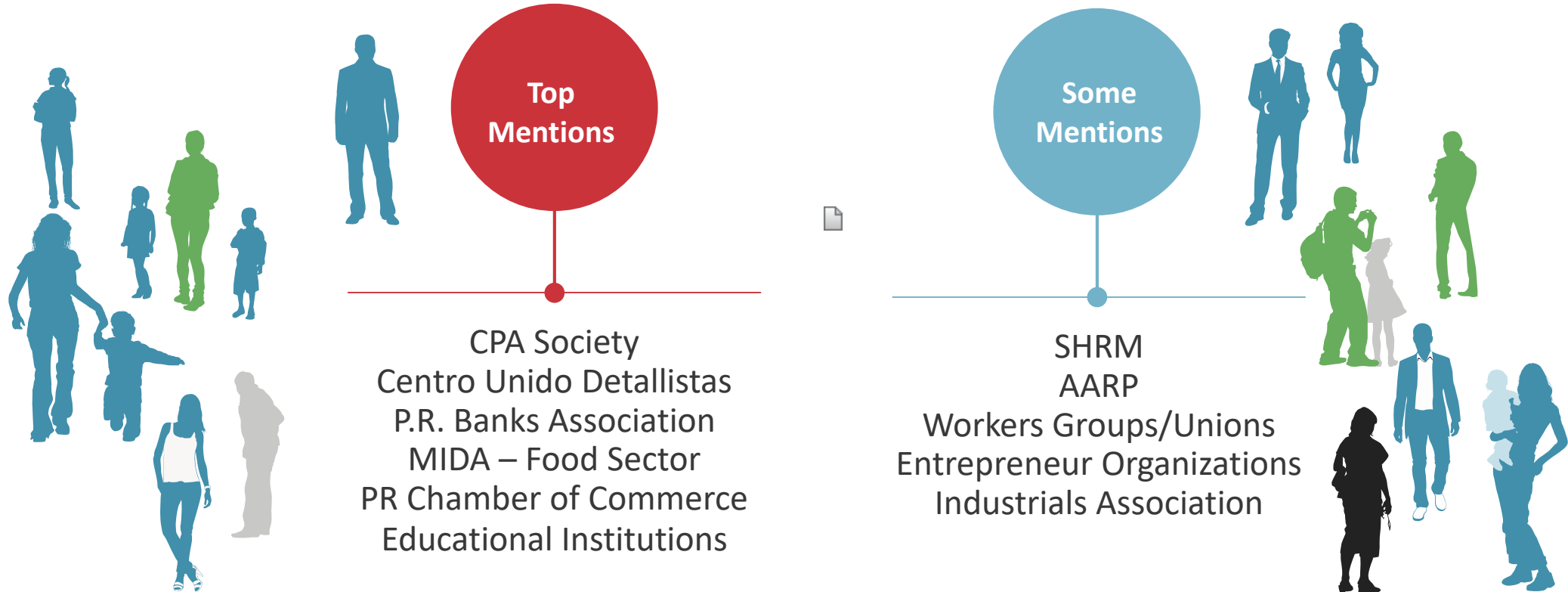
**“We’re faced by the opposite right now”.**

**“SOMETHING LIKE THIS COULD OFFSET NEGATIVE EFFECTS OR HELP GOVERNMENT GET OUT OF THE PENSION BUSINESS WHICH THEY DO VERY POOR AT”.**



SEEKING SUPPORT

# Who should support this program?



Very few mentions of people: Kurt Schindler (educator), Ojeda (radio personality)

# Contacts



**Héctor Ortiz**

Senior Strategist, Kranios

✉ hector@kranios.com

📞 787-406-0054



**Luis Garay**

Country Manager

✉ Luis.garay@ipsos.com

📞 787-753-8370



**Roxana Trabanco**

Account Director

✉ Roxana.trabanco@ipsos.com

📞 787-753-8370