

The Jones Act

With Cumberland's quarter-end publishing cycle coming to conclusion, we will use this missive to deliver a bullet aimed at the Jones Act. (Readers may have noted that we try to have most of our folks offer comments at the end of each quarter, which is why there has been a flurry of missives.)

The Puerto Rico story has been front-page news and has been discussed several times by my colleagues [John Mousseau](#) and [Shawn Burgess](#) and myself. See [cumber.com/munis-in-third-quarter-2017-all-about-storms/](#), [cumber.com/quick-note-on-hurricane-maria-and-insured-puerto-rico-bonds/](#), and [cumber.com/a-marshall-plan-for-the-caribbean/](#).

The Marine Merchant Act of 1920 is nearly a century old. Created by Sen. Wesley Jones of Washington, it requires that all goods shipped between US ports be carried on US-built ships owned and operated by Americans. In the wake of Hurricane Maria some members of Congress sent a letter to the Dept. of Homeland Security, asking for a temporary suspension of the Jones Act. Here is the link to that letter: [velazquez.house.gov/sites/velazquez.house.gov/files/09252017_FINAL_Letter_to_DHS_JonesAct_Federal_requirements_waivers.pdf](#). (Note that the US Virgin Islands is already permanently exempt from the Jones Act. Source: Fox News)

The Trump Administration granted the waiver. Better if sooner, but it has been done.

Sen. John McCain, R-Ariz., who urged Trump to waive the law, said shipping costs to Puerto Rico are approximately twice as high as to other nearby islands that allow foreign ships to dock. "It is unacceptable to force the people of Puerto Rico to pay at least twice as much for food, clean drinking water, supplies, and infrastructure due to Jones Act requirements as they work to recover from this disaster," McCain said, as he

also called for the “full repeal” of the “archaic and burdensome Act.” McCain has called for repeal of this law before and has offered repeal legislation without success.

We believe Senator McCain is correct. A hundred years ago, the law had one purpose. It was right after World War I, and US shipping needed bolstering. The impact today is to raise prices and slow down shipping. The law protects a few special interests in shipping and labor, who make a spurious argument based on homeland defense and who are bent on economic protectionism, while imposing costs on most of society. We seem to tolerate these politics normally, but every time there is an emergency we use temporary suspension of the Jones Act to overcome obstacles that wouldn't be there if the act were repealed.

So the law is currently waived because of Hurricane Maria, and it was waived because of Hurricanes Harvey and Irma. It was previously waived after Hurricane Sandy. Most analysts want the law repealed. Hawaii and Alaska officials want the law repealed.

Note, too, that many shipping companies use a workaround method to avoid the Jones Act and ship from the US to a foreign place and then transship to a US port so they are not directly shipping US to US. That practice adds costs and reduces efficiency.

Please understand that we do not want to compromise our nation's defenses. A Jones Act replacement law could achieve the national defense purpose in times of emergency but not impose higher costs and procedural delays such as we saw for a week during the Puerto Rico crisis.

We should also bear in mind that Puerto Rico has been hurt by the Jones Act for decades. See money.cnn.com/2017/09/28/news/economy/jones-act-puerto-rico.

Here is a modern metaphor. Suppose today the Congress were to

pass a law that every commercial airplane flight from a US airport to a US airport had to be on a plane made in the US. Airbus and Bombardier, and others would not be permitted unless they flew from the US to a foreign airport and then had a separate flight from that airport back to the US. The same would be true for delivery of goods by the US Postal Service or FedEx or UPS. What would happen? Costs would skyrocket. Prices of aircraft would rise. Global competition, which has the effect of lowering costs for all of us, would be reduced.

The new law would be couched in an argument that all US aircraft needed to be available for defense purposes first – but that waivers could be granted in emergencies. We wouldn't for a moment tolerate such a law today for air transport, yet we permit it to continue with shipping.

Our country has trouble repealing bad or unneeded laws. For example, we had a national prohibition on alcoholic beverages, but the method resorted to for repeal of that law was to pass jurisdiction to the states. Now, we are engaged in a fierce debate over healthcare, and the default approach seems to be to pass jurisdiction to the states. We seem trapped in a paradigm that allows the federal government to say yes but not to say no. Once a yes is granted, special interests become embedded, and they then achieve enough influence and financial power to protect their niches. When we have finally had enough or when we come to a real crisis, we end up passing jurisdiction to the states. If the Jones Act were passed to the states and Puerto Rico, it would be repealed by nearly all of them that had seaports.

It usually takes a crisis to get laws like this changed. Puerto Rico is an American territory with American citizens and is in deep trouble. It ranks higher in population of US citizens than 20 of the 50 states (source: US Census Bureau). Not one of those 50 states would tolerate the Jones Act's doubling its food prices and hampering its gasoline deliveries if that state were hit by a crisis like the one that Puerto

Rico is presently enduring.

Let's get the Jones Act repealed and replaced. Then, when the next hurricane strikes, there won't be as much needless suffering as the federal process grinds toward a costly temporary waiver.

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Puerto Rico Needs a Plan

Excerpt below:

President Donald Trump suggested last week that Puerto Rico's \$74 billion in debt would be wiped out. In response, Puerto Rico's bonds, which had been surprisingly resilient up until Maria hit, plummeted.

Even some insured municipal bonds fell, after initially trading above par post-Maria. Yields, which move inversely to prices, rose from about 4.1% to 4.75%, and then fell back to 4.3%. "That's a lot of gyrations off of one statement that didn't mean anything," says [John Mousseau](#), director of fixed income at Cumberland Advisors. His firm owns insured Puerto Rico debt and bought more during the panic.

What's next? Puerto Rico needs emergency aid—whether in the form of grants or very low-cost loans—and Congress has no choice but to step up. After that, a comprehensive plan to [rebuild and modernize its infrastructure is needed](#). That could halt the dire problem of outmigration by creating new jobs and boost the economy by allowing tourism to flourish, says Mousseau.

Read the full article here:
<http://www.barrons.com/articles/puerto-rico-needs-a-plan-1507351565>

Bond expert: Trump's Puerto Rico debt comments have 'little merit'

In a bizarre moment on Tuesday, President Donald Trump told Fox News that he was “gonna have to wipe out” Puerto Rico’s debt.

The exchange sent Puerto Rico general obligation bonds into a tailspin, with bonds maturing in 2035 dropping over 13% to \$0.38 on the dollar, according to Bloomberg data.

“I wouldn’t start to guess with Trump,” John Mousseau, director of fixed income at Cumberland Advisors told Yahoo Finance. “The pace of rebuilding efforts will tell a lot.”

With an impetuous president often hazy on policy and details, many professionals like Mousseau have hesitated and remained calm in the face of wild, head-scratching statements.

“We take these comments as an unclear off-the-cuff response with little merit,” wrote Shaun Burgess, a fixed-income analyst for Cumberland in a note.

Read the full article here:
<https://finance.yahoo.com/news/bond-expert-trumps-puerto-rico-debt-comments-little-merit-194556127.html>

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Trump sends Puerto Rico bonds reeling

The stock market has gotten pretty good at discounting some of President Trump's more freewheeling rhetoric on North Korea, taxes and other issues. But the bond market had no idea what to make of Trump's comments late Tuesday that the U.S. might have to wipe out Puerto Rico's \$74 billion in publicly held debt.

Cumberland Advisors' David Kotok emails on Trump: "No idea what he means. It certainly threw a curve at markets. There is a federal oversight system already in place. The pre-hurricane debt needs restructuring and this is widely known. Trump is an enigma."

Read the full article here:
<http://www.politico.com/tipsheets/morning-money/2017/10/05/trump-sends-puerto-rico-bonds-reeling-222655>

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Shaun Burgess speaks with CNN

about the current state of Puerto Rico Debt and Bonds

Shaun Burgess speaks with CNN about the current state of Puerto Rico Debt and Bonds in response to recent comments by President Trump.

Trump said “we are going to work something out. We have to look at their whole debt structure. They owe a lot of money to your friends on Wall Street. We will have to wipe that out. It’s going to have to be. You can say goodbye to that”. He added, “I don’t know if it’s Goldman Sachs but whoever it is, you can wave goodbye to that. The debt was massive on the island”.

Watch below or on [Snappy TV](#).

President Trump’s Puerto Rican Debt Comments Have Spooked Investors

Excerpt below:

“The biggest risk for Puerto Rico and the creditors is that the rebuilding of basic infrastructure takes so long that the out-migration worsens, and you see people put roots down in other places,” said Jim Millstein, CEO of financial advisory firm Millstein & Co. Millstein recently advised Puerto Rico on managing its debt.

So far, the emigration is already happening. An estimated 7,000 people have already left via the Luis Munoz Marin International Airport, with “tens of thousands more” likely to follow, a recent Municipal Market Analytics note read. But on a more optimistic note, investors such as John Mousseau, the director of fixed income at Cumberland Advisors, says he waiting for financial aid from the federal government to help rebuild and strengthen Puerto Rico’s economy.

“If you get this rebuilding underway, you start seeing Puerto Rico turning the other way,” he told [Fortune in late September](#).

Read the full article here: <http://fortune.com/2017/10/04/puerto-rico-donald-trump-debt-bankruptcy>

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A Marshall Plan for the Caribbean

“George Catlett Marshall, Jr. (December 31, 1880 – October 16, 1959) was an American statesman and soldier. He was Chief of Staff of the United States Army under presidents Franklin D. Roosevelt and Harry S. Truman, and served as Secretary of State and Secretary of Defense under Truman.” Source: Wikipedia.



His brilliance on behalf of the United States was multi-dimensional, military and diplomatic. But he is most remembered for his initiative after World War II when the eponymous Marshall Plan helped rebuild defeated enemies. That remarkable initiative has created some of the strongest allies for the present day United States. It blunted the spread of communism during the Cold War era. It provided financing and assistance to destroyed countries and their citizens. It allowed them to become friendly and durable allies of the United States and not our enemies. For details see: https://en.wikipedia.org/wiki/Marshall_Plan.

So let's take some editorial Sunday morning risk and propose the Tillerson Plan on behalf of the current Secretary of State. And let's prospectively credit President Trump with supporting a Caribbean initiative that would become a modern day American hurricane response that honors the memory of

George Marshall. Not only would this be a funded initiative for the American territories of the Virgin Islands and Puerto Rico but it would also extend aid and assistance to other Caribbean island nations. Of course, there could be collaborative efforts with other countries (like France or Netherlands) that have sovereign history with one island or another. And there are the independent Caribbean island nations to be included as well.

Imagine the huge positive response America would obtain with a US program to help the victims and their rebuilding effort. Imagine a modern day Marshall Plan for the Caribbean that includes the US citizens and also extends beyond American borders to our hemispheric Caribbean neighbors.

Funding requires Congress. My colleague [John Mousseau](#) envisions a special bonding authority for the American geography similar to those that were used in other circumstances. Funding sources for such an initiative can include a lateral segue of repatriated monies currently sitting abroad in special treasury bills under a tax code that has severe disincentives to their repatriation. In other words, the money is already there, sitting, waiting. And now we have a one-time, targeted, program opportunity.

All of that initiative requires a plan and a Trump Administration request for a one-time program. President Trump and Secretary of State Tillerson can do the asking. My best guess is they would get it through Congress since the politics incur little cost and reach into households of millions of Americans.

There would be conditions, of course. They can include a requirement that the money must be spent with American firms. That is now typical of foreign aid programs anyway.

And for the American geography a small percentage of the two trillion dollars currently now sitting abroad that awaits a

repatriation tax law change could be used to fund this program. Instead of sitting in short term treasury bills and waiting for a law change, that same money could be immediately directed toward this initiative.

And there could be soft loan repayment structures. There can be rules and oversight. There are a lot of details to be determined once the concept is accepted.

The political benefits to our current president are huge even as the cynics would depict him negatively as opportunistic given our dysfunctional current political climate. But there are many who would applaud such an effort as a Trump equivalent of the Marshall plan.

Some personal notes are in order. In our Cumberland office are several folks whose families originate from Puerto Rico. We have personally heard and seen their familial stories of which there are many. The vastness of the damage allows us to project those stories to many thousands and maybe millions of others we do not know personally. We have other interactions to the Virgin Islands. And there are still others within our Cumberland business associations that encompass Caribbean nations and their consultants and advisors. So we believe that this full disclosure is necessary since some may accuse us of a conflict of interest by writing this commentary.

We wouldn't write this if hurricane damage were not as deep as it is. Here is an example that my friend, and a serious economist, Joel Naroff noted in an email to me about Puerto Rico. Joel wrote: "according to reports, 1,360 of the island's 1,600 cellphone towers were downed, and 85 percent of above-ground and underground phone and internet cables were knocked out. Most roads are covered with debris and few gas stations have power."

Please take that single data fact and extend it broadly to all elements of a society with three and half million people

(American citizens) who are living under a financially bankrupt government. That's right, our fellow citizens in dire circumstances, living under a financially bankrupt government.

Joel asks if this Congress and President can be called into action and deliver. Others ask if it is recognized by Washington that these are American citizens as are those in the Florida Keys or Houston.

Our view is that the "America First" policy must include all of its citizens. That recognition must take place quickly in Washington.

But we would also recommend the initiative go beyond our territory and adopt the Marshall Plan heritage and legacy for the entire Caribbean. It seems to us that our country would benefit enormously from this approach.

George Marshall and Harry Truman saw devastation and acted. Can Rex Tillerson and Donald Trump see it as well? We hope so.

David R. Kotok

Chairman and Chief Investment Officer

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