

Research

Of Islands & Tariffs

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AUTHOR: CECILIA THON

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Will the new US tariffs apply to Puerto Rican exports to the US?

Puerto Rico, a small tropical island in the Caribbean, became a US territory after the Spanish-American War of 1889, along with Guam and the Philippines. However, unlike the last two, Puerto Rico is currently under a unique and somewhat paradoxical legal reality as an “associated free state” or “Estado Libre Asociado.” It is a commonwealth with special status but not considered one of the 50 states. It is not, however, considered a sovereign foreign country. Its citizens are all US citizens from birth with a US passport. Its government works independently, but according to Article 4, Section 3 of the US Constitution, known as the territorial clause, the US Congress has broad authority to govern territories. Moreover, it is represented by a resident commissioner who is a House of Representatives member who advocates for the island's interests but lacks voting power.

It is not, however, considered a sovereign foreign country. This begs the question: Will President-elect Donald Trump's promise of a 20% tariff on all US imports apply to goods originating from Puerto Rico? **The answer is no.**

The United States is Puerto Rico's leading trading partner, accounting for more than half of all the island's imports, while more than 75% of the island's exports are destined for the mainland. Technically speaking, since Puerto Rico is part of the US customs territory, these are not considered exports but rather commercial exchanges. The island also carries on significant trade with Japan, Ireland, and other European countries.

A Strategic FDI Destination

Puerto Rico has much potential to attract FDI and other business partnerships. On the one hand, the island offers various incentives, primarily through its unique tax structure that provides additional tax benefits to foreign investors who decide to establish operations or relocate to Puerto Rico. (Puerto Rico Incentives Code 60). Additionally, foreign vessels can deliver directly to Puerto Rico from foreign countries, despite the "Jones Act" that regulates the island's maritime shipment.

"ACCORDING TO ICEX DATA, ALL SECTORS ARE OPEN TO FOREIGN INVESTMENT, WITH THE EXCEPTION OF THE EXPLOITATION OF OILFIELDS, MINING, AND OTHER EXTRACTIVE INDUSTRIES, WHICH ARE RESERVED FOR THE GOVERNMENT OF PUERTO RICO"

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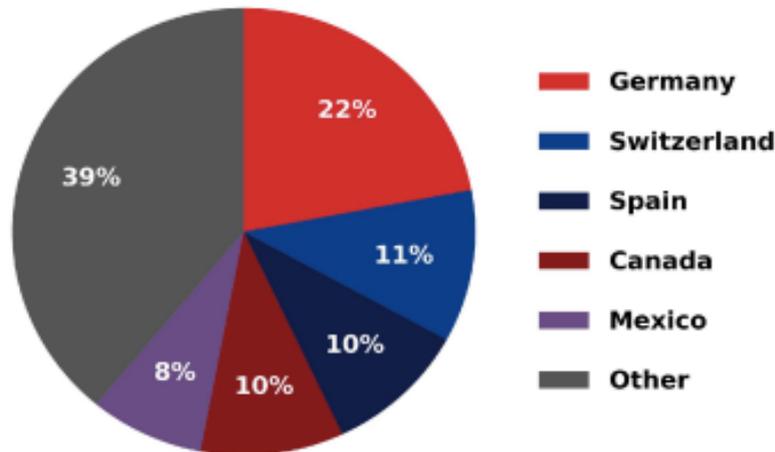
In 2023, the island reported an annual growth rate of 3.8% and an 11% average annual growth rate since 2019. Most opportunities are found in well-established and well-performing sectors such as pharmaceuticals, biotechnology, and medical devices. Other sectors include infrastructure, energy and water supply projects, aeronautical, and tourism.

Various examples of foreign investment use the island as a production base, with the US states as the intended market, leveraging tax incentives, duty-free shipment, and federal shipping regulations. The German companies Siemens, which operates facilities focused on medical and industrial equipment, and B. Braun Medical, which produces medical devices and pharmaceuticals, have products manufactured in Puerto Rico that are later shipped to the US and global markets.

Other examples include the Swiss pharmaceuticals Novartis and Roche; the Irish Allergan (acquired by AbbVie) and Medtronic; Japan's Sony and Omron Healthcare; and Spain's Santander Bank.

Top Sources of FDI in Puerto Rico

(62 Total Announced Greenfield Projects)



Source: *Foreign Direct Investments (FDI): Puerto Rico* 2024

Potential Sector Opportunities

Export Destined Products

Puerto Rico's main exports are pharmaceuticals, which account for over 50 percent of all exports. Other exports include medical equipment, computers, apparel, rum & other beverages. The Puerto Rican government has implemented various incentives to boost exports from the island. Known as export services, they account for eligible services rendered to a foreign natural or juridical person located outside of Puerto Rico. Businesses providing services to markets outside Puerto Rico benefit from low tax rates and exemptions (Act 60). Among the commercial activities eligible for these tax rates and exemptions are:

- Assembly, Bottling, and Packaging of Products for Export
- Commercial and Mercantile Distribution of Products Manufactured in P.R.
- Commissions on the Sale of Products to Customers outside P.R.
- Purchase of Products for Resale to Customers outside P.R.
- Sale of Intangible Products to Customers outside P.R.
- Storage and Distribution Centers

Advanced Manufacturing

Businesses in advanced manufacturing, biosciences, and information technology enjoy a 4% fixed corporate income tax rate, an exemption from property taxes, and a 50% exemption on municipal taxes. According to US Trade Statistics, most exports from PR are in Pharmaceutical and Medicine Manufacturing, accounting for 17.9 billion US dollars in 2023, followed by Medical Equipment and Supplies. Most FDI activity on the island focuses on these two subsectors. Although it is already a global leader in pharmaceutical and medical device manufacturing, there is still untapped potential in various niche areas, such as advanced biotechnology, cell and gene therapies, and AI-driven diagnostic tools. The aerospace and automotive sector is also a well-established sector experiencing significant growth. American global giants such as Collins Aerospace and Honeywell Aerospace have manufacturing sites on the island. Future opportunities could include establishing manufacturing hubs for specialized parts in the aerospace sector. Meanwhile, EV and hybrid vehicle parts and related infrastructure could present opportunities in the automotive sector.

Information and Communications Technology (ICT)

Puerto Rico is gaining recognition as the Caribbean's ICT regional hub, with some ICT giants, like Cisco, Oracle, and Hewlett-Packard, establishing themselves on the island. There are opportunities in digital assets, like fintech, insuretech, and blockchain, as well as in cybersecurity and software development. Moreover, substantial organizational support exists, including the PR Science, Technology, & Research Trust (PRSTRT), the IT Cluster, and the public Blockchain Advisory Board. As well as government support through Act 60's tax incentives.

Renewables and CleanTech

Thanks to its 100% renewable energy by 2050 pledge, Puerto Rico has seen significant advances, and various energy companies and research institutions have established themselves on the island. There are ample opportunities for innovation and development in the renewable energy sub-sector, especially for products and services related to utility-scale projects and energy storage. Cleantech development also presents significant opportunities, such as energy storage systems, microgrids, energy-efficient technologies, waste-to-energy projects, waste management systems, and water management technologies. Under Act 60, foreign companies investing in renewable energy and cleantech may benefit from tax exemptions.

Luxury Items

San Juan, the capital, has multiple locations for luxury shopping, including exclusive boutiques and high-end stores, which focus on fashion, jewelry, cosmetics, artisanal, and lifestyle products. The Mall of San Juan, located a few minutes from the island's airport, offers a curated selection of luxury stores. Fashion-wise, its stores boast names such as Gucci, Versace, and Salvatore Ferragamo. Its Condado area also has various fashion and fine jewelry boutiques.

Food & Beverage

There is demand for imported specialties, especially for unique international cuisines, including Asian, Mediterranean, and European foods. There are significant opportunities in gourmet and premium offerings such as premium cheeses, wines, olive oils, and other high-end products that appeal to a segment of affluent consumers. There is also a strong demand for organic and natural foods, especially gluten-free and plant-based products. Concerning the beverage sector, there is a burgeoning craft beverage market. Craft beer, wine, and spirits exporters could find opportunities, especially with high-quality or niche products. There is also a significant opportunity for food service industry partnerships. Hotels, restaurants, and cafés demand imported specialty ingredients and beverages driven by tourism. Franchise development is also an option; establishing or expanding global casual dining chains presents opportunities.

Real Estate

There is a wide variety of real estate options for foreign companies and investors on the island, from greenfield sites and warehouse facilities to traditional offices and co-working spaces. The Puerto Rico Industrial Development Company (PRIDCO) has a portfolio of more than 1,500 public commercial properties throughout the island, including industrial buildings, lots, and undeveloped land. Moreover, there are multiple opportunities for building rehabilitation and tourism-focused real estate.

Agribusiness & Farming

Agriculture in Puerto Rico is easily one of the most understated sectors on the island. Various agricultural powerhouses and small-scale local businesses with growth potential are operating on the island. Some opportunities can be found in local farming and fishing ventures. Puerto Rico is keen on boosting local agriculture, which creates investment opportunities in producing exportable tropical fruits (pineapples, mangoes), coffee, and cacao. There are various incentives for Bona Fide Farmers and agricultural businesses, such as exemption from paying income taxes on 90% of income directly from the agricultural businesses.

Moreover, there is an increasing need for innovative and sustainability-driven agricultural technology with ample institutional and government support. R&D is also highly supported: Act 60 provides tax credits for up to 50% of R&D expenditures. Various research facilities are also focused on developments in bioinformatics, especially the University of Puerto Rico's ARL Lab, which is currently conducting research on artificial intelligence for biomedical sciences.

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www.harringtonblue.co.uk

info@harringtonblue.co.uk

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