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Puerto Rico Not Too Broke to Pay Debt, OppenheimerFunds Says.

Puerto Rico's governor says the island's \$72 billion debt load is too big to pay. OppenheimerFunds Inc., the largest mutual-fund holder of the bonds, disagrees.

As Alejandro Garcia Padilla begins to make the case for delaying debt payments, the New York-based company is building the opposite argument. On a conference call this week, its money managers said data on sales-tax collections, unemployment and income growth indicate the economy is strong enough for the government to keep paying what it owes.

"The governor's new rhetoric, which we see as political cover after signing a budget that required unpopular spending cuts, is disappointing," OppenheimerFunds wrote in a summary of the July 6 conference call. "The ability to pay remains intact."

OppenheimerFunds has emerged as one of the earliest — and most vocal — opponents on Wall Street of Puerto Rico's unprecedented push to restructure its municipal bonds. The firm's comments provide a window into how others may seek to protect their investments in the cash-strapped island, which has amassed more debt than any state except California and New York.

Puerto Rico can't use bankruptcy to wipe out the debts of its publicly owned corporations, such as its teetering power provider, and its general-obligation bonds are protected by the commonwealth's constitution. That's forcing the government to negotiate, a process that's set to begin next week in New York.

Bonds Tumble

Puerto Rico bonds tumbled after Garcia Padilla last week said the commonwealth's debts are unpayable. A report by former International Monetary Fund economists released by Puerto Rico said the situation is dire, with high debt, unstable finances and a stagnant economy.

With speculation building about the island's solvency, Puerto Rico bonds have lost 9.5 percent in 2015, according to S&P Dow Jones Indices data.

No firm has felt the impact as much as OppenheimerFunds. It had about \$4.4 billion worth of uninsured obligations from the island as of July 9, according to data compiled by Bloomberg.

Puerto Rico obligations make up 13.8 percent of OppenheimerFunds's total holdings, excluding tobacco bonds, insured debt and pre-refunded securities, the money manager said in its statement.

OppenheimerFunds's state funds hold securities from Puerto Rico, which are tax-exempt nationwide. Its Virginia, Arizona, New Jersey, Maryland and North Carolina funds have the biggest losses among open-end, single-state muni funds this year, Bloomberg data show.

Fortune's Reversal

OppenheimerFunds predicts that the commonwealth's securities will rebound from record lows reached in the past two weeks.

"We believe Puerto Rico bonds will contribute to very strong total returns going forward and that, at current prices, there is far more upside than downside," according to the summary of the conference call. The speakers were fund managers Dan Loughran, Scott Cottier and Troy Willis, along with Digby Clements, the product director of OppenheimerFunds.

Ray Pellecchia, a spokesman for OppenheimerFunds, said the managers declined to comment further. He declined to comment on whether the money manager would be represented at a planned July 13 creditor meeting in New York.

That meeting, with Government Development Bank President Melba Acosta, will start at 3 p.m. in Citigroup Inc.'s New York headquarters, said Todd Hagerman, head of investor relations in San Juan for the development bank, which handles the island's debt transactions. It will focus on the IMF report.

Little Help

OppenheimerFunds disputes that the island's fiscal health would improve if some of its agencies were allowed to file for bankruptcy. Legislation to do so has yet to advance in the Republican-controlled U.S. Congress, even though key Democrats support it.

For one, the commonwealth's aqueduct and sewer authority probably couldn't prove it is insolvent, the money manager said, nor could Puerto Rico convince a court to reduce its sales-tax-backed bonds, known as Cofinas. Proving insolvency is a first step to seek court protection.

Additionally, the Puerto Rico Electric Power Authority, the cash-strapped agency for which legalizing Chapter 9 could be useful, is already working to renegotiate its \$9 billion of debt out of court, the company said.

"The financial and reputational costs associated with a Chapter 9 filing are such that most issuers see bankruptcy as the course of last resort," OppenheimerFunds said. "The administration needs to execute on the balanced budget, recognize its capacity to raise taxes, and continue to reduce the size of its underground economy, all of which should help the economy grow."

Bloomberg

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