

# Bond Case Briefs

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## Puerto Rico Bond Buyers Wait for 'Teens' Price Before Jumping In.

- **Investors wait for benchmark G.O. bond to fall below 20 cents**
- **Lower price could bring back tax-exempt mutual funds who sold**

How low will it go? That's what investors are wondering as they contemplate at what price Puerto Rico's most actively-traded security becomes a buy.

The price of the 8 percent general obligation bond due 2035 dropped nearly 60 percent since Hurricane Maria struck the island. It traded Thursday at an average price of 23 cents, down from 56.7 cents before the storm hit. Some investors are waiting for a price in the teens before buying.

While that may seem cheap, the commonwealth has yet to restructure its \$74 billion of debt and faces continued economic decline and persistent population loss. The bonds were sold in March 2014, the government's last long-term debt sale, and hedge funds bought most of the \$3.5 billion issue at 93 cents on the dollar.

A lower price on the G.O. bonds would help offset the island's financial challenges, said David Tawil, president and co-founder of Maglan Capital LP, who bought commonwealth bonds in 2013 and has since sold them. If the debt drops below 20 cents, he's back in, Tawil said.

"Once it goes below 20, I think people will see that as a threshold for capitulation," Tawil said. "And at that point it becomes investible."

A lower price could bring back tax-exempt mutual funds after most of those investors reduced their exposure over the past few years as the island inched closer to bankruptcy. Pacific Investment Management Co. last month said the commonwealth's general obligations were looking more favorable as prices declined. The lower the price, the more the municipal market is eyeing the debt, said Peter Hayes, head of municipal bonds at BlackRock Inc.

"As they continue to fall, it certainly gets more interesting and you have less downside," said Hayes, who helps manage \$124 billion of municipals. "The risk, reward — that changes the lower the prices go and I think it's certainly getting toward that point even for muni bondholders."

Puerto Rico has defaulted on most of its debt. The value of its securities has fallen since former Governor Alejandro Garcia Padilla in 2015 said the commonwealth was unable to repay all of its obligations. The island's bankruptcy filing in May and Hurricane Maria pushed prices down even more.

The storm's devastation has changed anticipated bondholder recoveries. Before Maria, Puerto Rico said it could direct \$8 billion for principal and interest payments through 2026, far short of the \$33.4 billion of debt service owed during that time. Island officials have said the commonwealth can no longer afford to pay even the \$8 billion amount. Puerto Rico may need to suspend debt payments for five years, a lawyer for Puerto Rico's federal oversight board said in court last month.

That has left investors wondering how much they'll get repaid and when. It's difficult for mutual funds to wait years for repayment while they allocate investment income to their clients. "It means you have a bond that doesn't accrue," Hayes said. "It's not additive to the income to your shareholders."

Puerto Rico Governor Ricardo Rossello is set to submit to Puerto Rico's federal oversight board a revised fiscal plan by Jan. 10 that will include how much the commonwealth estimates it can repay. Investors are eager to see how much lower those numbers are and which type of security will get more money for repayment, general obligations or debt backed by sales-tax receipts. Bad news for general obligation debt could push prices lower.

"If the prices get low enough, it might look attractive for the portfolios that can accept that type of risk," said Rob Amodeo, who manages \$25 billion as head of municipals at Western Asset Management.

While other Puerto Rico securities, including general obligations, trade below 20 cents, investors focus on the 8 percent G.O. because it's the most actively traded. It's easier to get in and out of that bond compared with the island's other securities.

Some general obligations have been trading in the teens for the past month, data compiled by Bloomberg show. Junior sales-tax bonds, which get repaid after senior bondholders, have been trading below 10 cents on the dollar in the past few weeks.

It's not just an additional potential price drop on the 8 percent G.O. that keeps investors poised for a possible opening on Puerto Rico's debt. At some point the island's economy and finances will improve, Tawil said.

"There will be some turning of the corner in terms of the fundamental story," Tawil said.

## **Bloomberg Markets**

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