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Forbes: Wall Street's Vultures Are Circling Puerto Rico's Bond Market.

The vulture hedge funds are circling Puerto Rico's $70 billion municipal bond market and are about to swoop. This is another round of disturbing news for Mom and Pop investors who own UBS closed-end Puerto Rico bond funds as well as the tens of thousands of other investors who own Puerto Rico debt in Municipal bond funds that brokers sold to them as safe, steady and reliable investments.

A huge issue facing Puerto Rico is whether it can borrow money and issue more debt in an attempt to buy time to get its tremendous fiscal problems in order. Puerto Rico officials are desperate to prevent a downgrade to "junk" bond status, which could potentially whipsaw the $3.7 trillion US municipal bond market.

Puerto Rico's current debt levels, however, appear unsustainable. If you add in all government debts and unfunded pension obligations, Puerto Rico has a staggering $46,000 debt load per person.

That's where Wall Street's vultures come in.

The New York Times last week first reported that "Puerto Rico is under pressure to show investors and credit-rating agencies that it can still borrow money from the capital markets. A group of hedge funds and private equity firms may help it do just that, but at a high price," according to Michael Corkery.

"Bankers at Morgan Stanley have been reaching out to about a dozen hedge funds, private equity firms and other large investors to gauge their interest in providing up to $2 billion in financing to Puerto Rico," Corkery reported, citing Wall Street sources.

The cost of the vultures' so-called "investment" in the island's bonds is charging Puerto Rico interest of course. In this case, Morgan Stanley and its investors could take a 10% rate of return, or "vig" as the loan sharks call it.

What a sorry state of affairs that the Commonwealth needs to pay 10% just to borrow enough money to prevent default for what would likely be just days or weeks. The island commonwealth appears to be fighting the inevitable.

According to a CNBC report on Friday, Moody's and the other rating agencies are watching the terms that investors will require for the debt offerings, which UBS Puerto Rico will likely underwrite. "If the interest rate Puerto Rico has to pay is considered too high, that too could spark a downgrade" to junk bond status which itself would trigger a bloodbath for the island.

CNBC's Michelle Caruso-Cabrera compared Puerto Rico's needed debt refinancing to "refinancing a 15-year mortgage into a 30-year mortgage" which would have a higher interest rate and a lower monthly payment, "making it easier to manage cash flow," she reported.

All eyes are on a scheduled February debt offering, according to a Bloomberg report. Moody's threatened a downgrade by March if it doesn't like the deal.

A few months ago, this blog noted that Wall Street has made billions from Puerto Rico's debt market. Now, it's looking to make more. This is a blueprint of how Wall Street works. It gets fat on the fees and commission from underwriting and selling municipal bonds or hot stocks, and then, after the deals blow up, a bank like Morgan Stanley steps in to buy the bonds for pennies on the dollar or lend at usurious rates.

Puerto Rico's strategy is like a desperate consumer trying to stave off the debt collector by opening a new credit card account to pay interest on his other credit cards. In this case, I believe the cost will end up being passed on to the poor Mom and Pop "bonistas" – bondholders – when their supposedly safe bond funds turn to junk.

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