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Puerto Rico Avoids Second Default, but Future Payments Uncertain.

NEW YORK/SAN JUAN — Puerto Rico made a crucial debt payment on Tuesday but warned that its deteriorating finances could trigger future defaults, as the governor granted the U.S. territory power to take revenues from public agencies.

There had been speculation Puerto Rico would default on all or part of the \$355 million notes issued by its financing arm, the Government Development Bank. The U.S. territory said in a statement that it made the Dec. 1 bond payment despite “extreme fiscal challenges.”

While Puerto Rico first defaulted in August, failure to make the payment on Tuesday would have been more significant because part of that debt was protected by the commonwealth’s constitution.

Another default could have triggered lawsuits, further spooked investors and undermined the island’s efforts to climb out of \$72 billion in debt and forced it to take drastic measures to keep public services running.

But Moody’s said the ratings agency would “continue to view default as likely on future commonwealth debt payments.”

Puerto Rico’s next deadline is \$945 million in total bond payments on Jan. 1, including \$363 million in general obligation debt service, Moody’s said.

A Puerto Rico executive order signed on Monday by Governor Alejandro Garcia Padilla said it gives the commonwealth the ability to claw back revenues from certain government agencies, including the highway authority HTA and the infrastructure authority PRIFA.

Garcia Padilla told a U.S. Senate Judiciary Committee that Puerto Rico would have to “claw back revenues pledged to certain bonds issued in order to maintain public services” and to repay bonds issued with the full faith and credit of the commonwealth.

An imminent default “looms large,” Garcia Padilla said.

“In simple terms, we have begun to default on our debt in an effort to attempt to repay bonds issued with the full faith and credit of the commonwealth and secure sufficient resources to protect the life, health, safety and welfare of the people of Puerto Rico,” the governor said in written testimony.

Justice Secretary Cesar Miranda said that the clawbacks “could be interpreted as a technical default, in the way that we retain money destined to eventually pay a debt when due” and said it could open the door to litigation.

Puerto Rico’s 8 percent General Obligation Bond rallied to trade at an average price of 74.9 cents on the dollar, with a yield dropping to 11.2 percent versus a yield of 11.8 percent on Monday, on news that it did not default on the GDB debt.

With 45 percent of its 3.5 million population in poverty, Puerto Rico is a meteorological paradise mired in economic purgatory. Years of over-spending and the expiration of corporate tax incentives stuck it with debt that gets harder to pay as residents increasingly emigrate to the United States.

“Puerto Rico’s debt crisis didn’t happen overnight, it’s been years in the making,” said Senator Chuck Grassley, who chaired the committee at Tuesday’s hearing. “The starting point is to identify the problem.”

Puerto Rico is in the process of trying to negotiate a debt restructuring with investors which could involve a so-called superbond that provides just one credit for various existing bonds. One source familiar with the situation said negotiations had been going slowly and will now probably drag into next summer as the GDB payment buys some time.

“This just really buys a bit more time for the Commonwealth, but the Puerto Rico leadership better act fast with respect to bond holder negotiations if they want these payments to have been worthwhile,” said David Tawil, president at hedge fund Maglan Capital.

Of the \$355 million paid on Tuesday, \$81.4 million was to service non-general obligation-backed debt and \$273.3 million was for notes backed by the commonwealth’s general obligation guarantee.

The payment on bonds issued by the GDB was crucial as Puerto Rico tries to stretch its liquidity into 2016 to provide more time to restructure debt.

In August, Puerto Rico paid only \$628,000 of a \$58 million payment due on its Public Finance Corp bonds.

By REUTERS

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