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Muni Pros Scold P.R. For Lack of Financial Disclosure.

Municipal investors said Puerto Rico's $355 million Government Development Bank note payment and claw-back debt management plan did little to resolve the island's debt crisis.

Buyside experts on Wednesday said the commonwealth remains in a precarious situation, as a now-crucial $1 billion debt service payment looms on Jan. 1. Some said Tuesday's plan merely postpones an inevitable default, while jeopardizing future payments to some bond holders by clawing back revenue from lower-tier debt to pay general obligations.

"It's robbing Peter to pay Paul," said Alexandra Lebenthal, co-chief executive officer at Lebenthal Holdings in New York City. "If I'm Peter I'm not very happy."

James T. Colby III, senior municipal strategist and portfolio manager at Van Eck Global, which owns a variety of Puerto Rico credits in two municipal high-yield exchange traded funds, said the firm viewed Gov. Alejandro Garcia-Padilla's testimony to Congress this week with "heightened sensitivity" to the potential repercussions for the debt.

"While we were encouraged by the near-term decision to make payment and meet their near-term obligations, by failing to give greater clarity on any plan for addressing their cash needs — save the comment about a possible 'claw back' to provide some working capital — holders such as ourselves were left no better off than 24 hours earlier," Colby said on Wednesday afternoon. "We are left to wonder if this gesture was one of recognition of the GO full faith and credit pledge or just the play of a bargaining chip."

Others reiterated the need for increased financial disclosure.

Even though the commonwealth has the ability to claw-back revenue to secure the repayment of general obligation debt service, Peter Delahunt, managing director at Raymond James & Associates, said there needs to be more clarity as Puerto Rico manages its future debt responsibilities and strives to recover from its overall fiscal malaise.

"What is unclear is an actual audited accounting of the commonwealth's finances," Delahunt told The Bond Buyer, noting that the commonwealth has not produced audited financial statements for the past two fiscal years. "The lack of audited financials discredits the accuracy of the commonwealth's recent Financial Information and Operating Data Report, which was reinforced last week when the administration published an Errata Notice that disclosed this report had included erroneous data," Delahunt said.

"Claims have been made that the report overstates the commonwealth's general fund debt service burden by as much as 30% to 60%," Delahunt continued.

"The lack of audited numbers enables a good deal of ambiguity. Until the ambiguity is cleared up, a proper debate for resolution is pointless," he said.

Michael Comes, a portfolio manager and vice president of research at Cumberland Advisors, said the actions of the commonwealth reflect “one step in many of the process by which Puerto Rico will deleverage its balance sheet and shore up its liquidity in the absence of an orderly resolution process.”

The firm only owns P.R. debt insured by Assured Guaranty and MBIA, Comes said. He said there is concern in the market over the Jan. 1 payments as well as other future debts.

“I don’t think they’re going to be able to make the payment,” Comes said. “They simply do not have the money. The collective unwillingness of creditors and the issuer to achieve consensus has led to a worse outcome than if they had.”

While the commonwealth is faced with limited liquidity, it also must place a high priority on providing services to its citizens, said Peter Hayes, head of the Municipal Bonds Group at BlackRock Inc., which oversees $111 billion in municipal assets and does not own the direct debt of Puerto Rico in its municipal funds.

“This means that it will be more difficult to find sources of funds going forward, making each payment date more tenuous, particularly as markets are closed to them,” he said. “Puerto Rico is clearly trying to pay debt service and avoid litigation, while buying time for consensual negotiations.”

Overall, municipal experts agreed the negatives still outweigh positives for Puerto Rico investors.

“For those credits subject to the claw back, this is clearly a negative credit event – but one that is already being factored into current pricing levels,” Jeffrey Lipton, managing director and head of municipal research and strategy at Oppenheimer & Co. said.

He said while the executive order comes as no surprise and is consistent with the governor’s prior statements and actions, it also underscores the severity of the commonwealth’s liquidity crisis.

At the same time, he said, “it is very difficult to gauge just how serious the cash erosion is given the transparency issues and systemic shuffling of monies that have been characteristic of Puerto Rico for many years.”

Hayes said the commonwealth will need to suspend payments for other issuers in the future, unless there is “a quick settlement with bondholders on a restructuring that includes postponing debt service payments.” He said such a solution seems unlikely.

“Time is running out and the current debt levels are unsustainable,” Lipton said.

“Without broad restructuring capability or access to Chapter 9, the only course of action would be to pursue a PREPA-like restructuring, which as we know has consumed a great deal of time and expense,” Lipton said. He referred to the Puerto Rico Electric Power Authority’s efforts for more than a year to complete a business and debt agreement.

“Multiplying this by several more credits will likely create much greater uncertainty,” Lipton added.

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