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Puerto Rico's Defaulted Debt at Record Low as Recovery Rate, Legal Battle Weigh.

NEW YORK (Reuters) – Puerto Rico’s benchmark government bond slumped to an all-time low on Monday after competing groups of bondholders stepped up their legal battle over who should be paid first out of a smaller-than-expected pool of cash.

Benchmark Puerto Rico general obligation (GO) debt maturing in 2035 and carrying an 8 percent coupon, fell 5.15 points in price to 61.35 on Monday, according to Thomson Reuters data.

The U.S. commonwealth is in the midst of trying to pull itself out of a financial quagmire that leaves it with \$70 billion in debt it cannot pay without a massive restructuring.

It is also fighting a 45 percent poverty rate and islanders fleeing for the mainland in search of a better life.

The debt, which has been in default since last year when the U.S. Congress passed a rescue law known as PROMESA that suspended debt payments, has dropped 11.4 points in price since a new fiscal rescue plan was accepted on March 13. Defaulted debt trades more like an equity and is not typically quoted with a yield.

Investor sentiment turned more negative when so-called COFINA bondholders, whose debt is backed by sales tax revenue, asked a federal judge in San Juan on Sunday to deny the GO bondholder group’s effort to stop the island’s government from making payments on COFINA debt.

GO debt traditionally is considered senior to all other debt obligations as it is backed by the good faith and credit of a municipality. A larger amount of COFINA debt is held on the island than GO debt, which is held widely in U.S. municipal bond portfolios.

The Financial Oversight and Management Board for Puerto Rico, established by the PROMESA law, certified a revised fiscal turnaround plan on March 13 that set aside less money for servicing debt payments than originally planned.

A lower-than-expected amount of money set aside to service debt under the new plan, \$800 million per year versus \$1.2 billion a year over a 10-year period, puts the recovery rate for bondholders, in aggregate, around 30 cents on the dollar, according to analysts.

“The most liquid bond prices have dropped after the acceptance of the fiscal plan by the PROMESA board and the recovery rate being on the low side,” said Joe Rosenblum, director of municipal credit research at AllianceBernstein in New York. “I’m not making a comment on whether it is correct or final, but at least sets up from Puerto Rico’s side a much lower recovery rate.”

“That is carrying forward and over the weekend the COFINA creditors committee went hard against the GO bondholders. We knew all along that was going to be a tough battle,” he added.

Municipal analysts at Barclays Capital estimated that even if 100 percent of the additional revenue and expense measures are met, “the debt stack would need to be reduced to about 31 percent in order to achieve a stable debt-to-GNP ratio.”

“We assume exit yields of \$4.9 percent post restructuring, consistent with where 10 year single-B high yield municipal bonds trade,” Barclays said in a March 15th research note.

Reuters

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