

# **Bond Case Briefs**

*Municipal Finance Law Since 1971*

---

## **Puerto Rico's Troubles Create New Opportunities for Investors.**

Puerto Rico entered its own form of bankruptcy in early May, and the financial crisis there is still getting worse. But even as the restructuring process devolves into more lawsuits, defaults, and downgrades, some ripple effects are creating surprising opportunities for investors.

Consider what's going on with MBIA the parent of bond insurer National, which insures about \$4 billion in par value of Puerto Rico bonds. (That's about \$8.5 billion in total debt exposure, including all scheduled interest payments and principal.) MBIA's business plans were torpedoed by a two-notch rating downgrade by S&P Global Ratings in late June. The firm laid off employees and said it would give up trying to write new business, as bond insurers have to be rated higher than municipalities for the insurance to add any value.

Yet, MBIA's shares have been rising ever since. On Tuesday, management told investors to expect shareholder-friendly moves, such as more stock buybacks and perhaps a special dividend—even as it had to increase accounting for losses related to Puerto Rico. Executives say the firm, which has the ability to pay claims equal to \$4.6 billion, is now “unshackled from most of the limitations imposed by the rating agencies,” by not writing new business. The stock has risen to \$10 from \$8 in the past two months.

Investors expect MBIA to be acquired by fellow bond insurer Assured Guaranty. Deal speculation has fueled the gains. CreditSights analyst Josh Esterov thinks it will be challenging for the two companies to reach a deal, but calls the logic behind it “sound.”

Such special situations aren't normally the purview of municipal-bond investors. But the bonds insured by MBIA and Assured may be. Richard Daskin of RSD Advisors believes that investing in insured Puerto Rico paper can be a good opportunity, even though he qualifies that it “should probably be done with professional help.”

Mark Taylor, portfolio co-manager of the Alpine High Yield Managed Duration Municipal fund, has recently added to his fund's stake in insured Puerto Rico munis, raising his allocation to 6% from about 5%. He won't touch uninsured Puerto Rico paper, and he keeps maturities to within five years. For example, he owns some general-obligation bonds maturing in 2020 that now yield 3%, equivalent to a 5% taxable yield for investors in a high tax bracket.

Mr. Taylor was surprised by MBIA's downgrade, which he calls “draconian.” He believes the firm has adequate reserves for at least the next several years. Plus, if MBIA is sold, the bonds it insures would climb in price, he says.

Other muni-fund managers are avoiding Puerto Rico bonds altogether. “I think the ultimate outcomes will be significantly worse than where the bonds are trading now,” says Nicholas Venditti of Thornburg Investment Management. While Puerto Rico's GO bonds are trading at about 60 cents on the dollar, he believes they could ultimately be worth as little as 25 cents. And if Assured, which has higher reserves than MBIA does, has to pay out large amounts in claims, it could get

downgraded.

“These entities live and die by their credit ratings,” Mr. Venditti says. Yet if bond insurers get through Puerto Rico’s restructuring, pay all their claims, and don’t get downgraded, they could have a great sales pitch to boost their business, he notes.

Puerto Rico’s road to restructuring is going worse than expected for creditors so far. “The judge is the one picking winners and losers, and that isn’t a good place to be,” says Mr. Taylor. But for owners of insured Puerto Rico bonds—and even shareholders of beleaguered MBIA—things may turn out just fine.

## **The Wall Street Journal**

By Amey Stone

July 17, 2017 12:05 p.m. ET

Write to Amey Stone at [amey.stone@barrons.com](mailto:amey.stone@barrons.com)

Copyright © 2025 Bond Case Briefs | [bondcasebriefs.com](http://bondcasebriefs.com)