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Puerto Rico Bonds Rally as Rival Creditors Float Settlement.

- **Senior sales-tax bonds soar to 71 cents on the dollar**
- **While plan rejected, it moves toward settling major conflict**

Puerto Rico bonds rallied after a group of investment firms and insurers reached agreement on a restructuring plan that would allow them to receive larger-than-expected recoveries on their defaulted debt, marking a first step toward resolving a key clash between creditors who have been fighting in bankruptcy court.

The gains, which pushed some securities up by as much as 22 percent Monday, came despite the plan's rejection by Puerto Rico's federal financial overseers, who said it would leave the government facing budget shortfalls for years and was put together without their input.

But the framework hashed out by the owners of sales-tax-backed debt and general-obligation bonds shows progress toward resolving their disagreement over who has the highest claim to Puerto Rico's cash — an issue at the heart of the government's record bankruptcy. It also offers a baseline that investors could use to estimate what they stand to recover, which has been difficult given the divergent outcomes of previous bankruptcies and the toll on the island caused by Hurricane Maria in September.

"The big argument that everyone is waiting for is who gets the sales-tax money — who has control of that money," said Dan Solender, head of municipal investments at Lord Abbett & Co., which holds \$20 billion of state and local debt, including some Puerto Rico debt.

"That a good number of the bondholders have reached an agreement is pushing this forward," he said. "It's the first positive movement in that direction in a long time."

The plan received support from those who insure or hold about \$11 billion of Puerto Rico bonds, including Aurelius Capital Management, Monarch Alternative Capital, Fir Tree Partners and GoldenTree Asset Management. It also includes a group that represents residents who hold sales-tax debt.

The proposal calls for owners of sales-tax bonds, known as Cofinas, with the most senior claim on the revenue to recoup as much as 95 percent of their investments. Owners of subordinate Cofinas would get up to 43 percent, while general-obligation bondholders would receive almost 59 percent, according to a summary circulated by the group.

The rally was led by Puerto Rico's senior sales-tax debt, which was the most actively traded municipal security Monday, though general-obligations also gained. Senior sales-tax bonds due in 2040 climbed to as much as 72.5 cents on the dollar from 59.5 cents Friday, only to pare those gains by dropping to an average of 68.7 cents later in the day. General obligations due in 2035 rose to an average of 44.5 cents from 41.4 cents Friday.

Some investors expressed skepticism about the run up given that the plan was dismissed by the oversight board set up to oversee Puerto Rico's fiscal recovery. In a statement Monday, the panel

said that the restructuring proposal was “completely unaffordable” and out of step with the government’s latest fiscal plan because it would still leave Puerto Rico spending more than it brings in. The creditors said it would reduce the government’s debt by \$10 billion.

Dora Lee, vice president at Belle Haven Investments, which holds insured Puerto Rico bonds among its \$7 billion of municipal-debt holdings, said the creditor proposal isn’t a viable one for the island.

“It wasn’t a sustainable recovery plan,” she said. “It neglected the fact that the revenue has to come from a viable economic base. That core issue hasn’t been addressed.”

“Whenever there’s a glimmer of good news, the bonds trade up, reality sets in and people realize that again, we’re back at square one,” she said. “Whenever there’s good news out of Puerto Rico you need to take a deep breath and remind yourself you’re dealing with Puerto Rico.”

The rally pushed the price of the general-obligation bonds to the highest since early October. The bonds traded for as little as 21 cents in December, before Governor Ricardo Rossello began offering more optimistic assessments of the island’s recovery from the hurricane.

The island’s government and general-obligation bondholders have been allied against Cofina bondholders, who say sales-tax revenue should be used to repay them before it’s spent for other purposes. The commonwealth and the general-obligation owners want U.S. District Court Judge Laura Taylor Swain to throw out a law that transfers the sales taxes to a governmental agency, known as Cofina, whose only responsibility is to use the cash to pay its bondholders.

“Any kind of progress toward resolutions should translate into prices in some way,” said Matt Fabian, a partner at Municipal Market Analytics Inc. “It at least gives a theoretical anchor at which bond prices can trade.”

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