PUERTO RICO’S WORST CASE SCENARIO:
BUT ARE THERE “SHARKS” CIRCLING THE MARKET?

WHAT A DIFFERENCE A YEAR MAKES

It’s been 12 months since my last comprehensive HJ Sims credit report on Puerto Rico, when I declared that there were 10 reasons to consider Puerto Rico bonds as a good investment. The bad news since last October is that recession continues for the Island, and a brief period of recovery noted last October almost immediately turned into another sizeable decline in economic activity through August of this year. In addition, the Commonwealth’s general fund deficit for 2013, expected to improve after major tax increases and major government spending cutbacks, doubled in size to over $2 billion. Bad news, indeed, and chronicled in blaring headlines from Barron’s, to Forbes, to this week’s Wall Street Journal, which trumpeted growing concerns in the White House over Puerto Rico’s debt and impact on the nation’s financial markets. The Journal’s speculation over the possibility of a federal “bailout” of Puerto Rico is just that, as no one is willing to come out of anonymity to confirm or deny such a plan. Lost in everyone’s rush to a judgment of bankruptcy was the major news that Puerto Rico’s 1st quarter revenue collections were less than ½% below its projections (only $7 million out of over $1.8 billion). In a financial crisis, just as in war, truth is always the first casualty. (See http://www.hjsims.com/news-views/puerto-rico-remains-a-sound-investment-for-income/ for my commentary on news media coverage of Puerto Rico’s economy and financial position.)

For a major leaguer, continued deficit stress and economic downturn would be two big strikeouts, but as Yogi Berra would say, “it ain’t over ‘til it’s over”. Puerto Rico is in the middle of a big, but crucial, rally. From just a year ago, Puerto Rico has pushed some mighty important runs
over the plate, and there are still plenty of innings to play before this game is going to be forfeited. Bond default or a forced “cram-down” of reduced repayment restructuring is not in the “game plan”, as some would have you believe.

**PUERTO RICO’S FISCAL RECOVERY PLAN OVER THE LAST 12 MONTHS IS UNPRECEDENTED**

On Monday, October 7th, the Municipal Analysts Group of New York (MAGNY) convened four fiscal authorities on Puerto Rico: three well respected all-star municipal analysts, and the current President of the Puerto Rico Senate, Eduardo Bhatia. Mr. Bhatia offered a challenge to the panel and the audience of New York’s leading municipal bond analysts: name a U.S. state that has ever implemented a fiscal recovery plan that was as large and comprehensive as Puerto Rico has done since new Governor Padilla took office. He is right; you can’t find one.

Despite stubborn economic malaise, Puerto Rico enacted over $1.3 billion of new taxes, designed to shrink ongoing deficit operations that have spanned ten years. The new budget also targets additional spending to strengthen its pension funds and kick-start the island’s economy. The tax increases amounted to about 10% of the government’s general fund spending. To put that in perspective, that would be like California raising taxes by $13 billion in one year. Comparing it to the federal government, President Obama would have to raise taxes by $378 billion in one year’s time to match what Puerto Rico has accomplished. The two largest federal tax increases in history were both less than $80 billion in one year. To say that Puerto Rico’s tax increase for 2014 was monumental is an understatement.

The Commonwealth also made major changes to its pension system, which is easily the least funded plan of all state-level governments. It won’t radically improve the system’s funding levels quickly, but it accomplishes several important goals which put pension funding in the right direction. It increases Commonwealth contributions by about 1% of payroll in each year for the next 10 years. It effectively freezes growing benefit demands by shifting most
employees to a defined contribution plan similar to a 401K (unlike the old plan with open-ended benefit increases). It increases retirement ages, and increases employee contributions.

As for the Commonwealth’s major essential service providers (the electric system, the water and sewer system, and the highway department), the administration has implemented substantial rate increases, implemented better enforcement of fee collections, and eliminated general fund subsidies which have contributed to deficit operations in the past.

Frankly, it’s a remarkable achievement that has gotten short shrift from the business and news media.

**PUERTO RICO’S AUSTERITY MEASURES HAVE NOT BEEN WITHOUT ECONOMIC FALLOUT**

As impressive as these measures are, they have not been without economic impact. In the past, Puerto Rico has been criticized by financial analysts for its dependence on government employment. While total employment in the last 4 years has declined across the board (except for trade and services), the single biggest contributor to job losses has been the government’s austerity plan, accounting for 76% of payroll jobs lost between 2010 and August 2014, and 40% of jobs lost in the last year alone. While the labor force has been dropping over the period, the 40,000 government job reductions contribute about 3-4% of the Commonwealth’s above average 14+% unemployment rate.

**THE MUNI ANALYTICAL COMMUNITY WEIGHS IN AT MAGNY**

As I’ve said in the past, Puerto Rico’s credit picture is not a pretty one. But listening to the other three panelists at the MAGNY conference (David Hitchcock of S&P, Joe Rosenblum of AllianceBernstein, and Alan Schankel of Janney Montgomery), I couldn’t help but notice the more measured tones of these bond pros with the bombast of the financial news and general media. Mr. Schankel, for one, was noted in late July of 2012 as recommending that investors keep their portfolio exposure to Puerto Rico debt at 10% or less. At the conference, even he had to say that “These guys down in Puerto Rico, they’re determined to make this work.”. In my opinion, the harshest criticism of the Commonwealth came from Messrs. Rosenblum & Hitchcock, who reminded the audience that the Commonwealth has been saying that their deficit would be eliminated within 2 years for about the last 10 consecutive years. The moderator, Bob Donahue, put it best when he asked Mr. Bhatia “why should we analysts believe that story when it’s been repeated without success for the last 10?” And even though I am more positive than most about Puerto Rico’s fiscal fortunes, I have to agree with that criticism.
With that as background, let me reiterate my reasons why I still believe that Puerto Rico investors should not be panicking and selling off their Commonwealth bonds into this depressed market, whose flames have been fueled by bombastic and unbalanced reporting of the island’s economic and government financial factors.

Puerto Rico has long endured below average personal income and an economy built on relatively low paying tourist and service jobs, and above average government employment. Puerto Rico’s economy is heavily dependent upon the U.S. economy, so when national headwinds blow, they often blow harder in Puerto Rico. It has had a history of modestly balanced budgets in good times and above average deficits during downturns. In that respect, its financial performance resembles third-world countries more than one of the domestic United States. Deficit financing is not characteristic of the 50 states that Puerto Rico would like to be compared to (although as we have seen in the past from California, Illinois and Connecticut, deficit financing has been used during economic times of stress).

These are not new developments; they are long-term characteristics of a unit that has not significantly changed its economic drivers or its financial policies for decades. These characteristics were in evidence when Moody’s had Puerto Rico rated “A” in the 1970’s, and “A” by S&P as late as 2005. In fact, Moody’s recalibrated ratings and raised Puerto Rico to A3 in 2010. In March 2011, S&P actually raised Puerto Rico’s rating to BBB, when deficit borrowing was beginning to peak. Fitch, in a first-time rating assignment, assigned a BBB+ to Commonwealth general obligation debt during the same period.

While Puerto Rico’s problems have been chronic, the length and depth of the Great Recession has exacerbated these problems to unprecedented levels. The annual budget deficits became unprecedented, totaling $9.5 billion over the period from 2005 through 2012. The same kind of deficit growth could be said for both California and Illinois. Unemployment also exceeded expectations, much as it did in the U.S.

Unlike California and Illinois, however, Puerto Rico developed a multi-year plan to attack and reduce deficits, avoiding the annual squabbles and budget stalemates that marked both California and Illinois. The plan included significant tax increases and new taxes, but also included a curb on annual spending and a 17% reduction of the government work force. Puerto Rico’s administration faithfully stuck to that plan under former Governor Fortuno. Unfortunately, the island hasn’t caught an economic break, and current Governor Padilla inherited a $2 billion deficit when he took office in January 2013.

THE SHORT & THE LONG OF PUERTO RICO’S FINANCIAL BIND AND SOLUTIONS

Puerto Rico’s major credit risks on its high debt load can be summarized into 5 main components:

1. The basic economy continues to be shallow, and is dependent on cyclical and competitive tourism with other Caribbean resort destinations, lower paying manufacturing jobs, and above average dependence on government employment (although that dependence has been reduced dramatically over the last two administrations);
2. The Commonwealth has had a checkered history of managing its financial operations, culminating in unprecedented deficits and deficit borrowing;
3. Income levels remain well below the averages for states in the U.S.;
4. Debt levels are high, and have been exacerbated by the recent deficit borrowing done to stabilize the budget, finance employee layoffs and firings, and provide a start to funding economic development programs; and finally
5. An extremely low pension funding level between 6-8%, whereas most states are at levels of 70% or more.

PENSION UNDERFUNDING

Pension underfunding is the current buzzword in municipal finance. It is being used increasingly as a reason for rating downgrades, and has been described as a “ticking time bomb” that will lead to unprecedented defaults on municipal bonds. I wrote a piece 3 years ago saying that pension funding is not an immediate cash crisis for most issuers, but a problem that is long-term and can be solved gradually, without requiring that public pension funds need to be fully funded at all times.

In Puerto Rico’s case, however, underfunding reached a crisis stage. Historically underfunded at low levels (a fact known by analysts and rating agencies for a decade), investment losses of nearly $800 million in 2008 & 2009 clobbered Puerto Rico’s Employees Retirement Fund assets, bringing their actuarial funding level to an unprecedented low of 6.8%. Until then, the Fund’s expenses generally matched revenue, and in 2008, the Fund sold about $3 billion of pension obligation bonds to shore up Fund reserves. Unfortunately, the bonds were sold at the outset of the financial crisis, leading the fund to lose money on its borrowing. And because of early retirements, pension payout benefits were expected to rise rapidly after 2011.

<table>
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<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>TOTAL CONTRIBUTIONS</td>
<td>$722</td>
<td>$758</td>
<td>$799</td>
<td>$885</td>
<td>$1,001</td>
<td>$919</td>
<td>$1,021</td>
<td>$909</td>
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<tr>
<td>TOTAL NET INVESTMENT INCOME</td>
<td>$259</td>
<td>$316</td>
<td>$454</td>
<td>$(63)</td>
<td>$(315)</td>
<td>$406</td>
<td>$652</td>
<td>$266</td>
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<tr>
<td>TOTAL ADDITIONS</td>
<td>$982</td>
<td>$1,074</td>
<td>$1,253</td>
<td>$822</td>
<td>$686</td>
<td>$1,349</td>
<td>$1,716</td>
<td>$1,194</td>
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<tr>
<td>TOTAL DEDUCTIONS</td>
<td>$795</td>
<td>$860</td>
<td>$903</td>
<td>$1,106</td>
<td>$1,451</td>
<td>$1,526</td>
<td>$1,658</td>
<td>$1,681</td>
</tr>
<tr>
<td>NET INCREASE (DECREASE)</td>
<td>$186</td>
<td>$213</td>
<td>$350</td>
<td>$(284)</td>
<td>$(765)</td>
<td>$(177)</td>
<td>$(59)</td>
<td>$(487)</td>
</tr>
<tr>
<td>TOTAL CASH &amp; INVESTMENTS</td>
<td>$1,954</td>
<td>$2,140</td>
<td>$2,217</td>
<td>$4,338</td>
<td>$3,558</td>
<td>$3,291</td>
<td>$3,499</td>
<td>$3,286</td>
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Unattended, this would precipitate a cash crisis within only 3-4 years.
In 2011, The Commonwealth passed a law that would require it to raise its contribution rate by 1% annually for 5 years, and by 1.25% annually for the next five years. This would result in Puerto Rico raising their contribution from 9.75% in 2011 to 20.525% by 2021.

This year, the Legislature approved more stringent pension reforms that will boost income and slow the growth of benefit payments. Employees’ share of contributions to their pensions was raised from 8.75% of salary to 10%. Minimum retirement age was increased for many segments, in some cases from 58 to 61 years old, and for new employees, the minimum retirement age for most general employees will be 67, and for new public safety officers, the minimum retirement age will be increased from 55 to 58. These changes will slow the growth of existing and new pensioner benefit payments. In addition, the Commonwealth extended its shift of employees from costly defined benefit plans to plans that emulate 401K plans, where pensioners’ benefits will be determined and limited by contributions grown through investing. As seen in the chart below, projections show that despite these reforms, current pension assets will continue to decline, even if the pension fund earns 8% annually on its cash and investment balances, before reaching break-even in 2021.

Finally, despite the contribution increases more will need to be done. From 2005 through 2011, the Fund averaged 8.4% returns on its investment, despite losses in 2008 & 2009. Even assuming 8% investment returns, the unfunded liability will continue to grow, but the pension fund would still remain solvent and capable of meeting pension benefits promised. Not pretty, but a good start that avoids running out of pension assets in 3 to 4 years had the pension reforms not been adopted.

Despite these daunting challenges, Puerto Rico has many basic strengths that will keep finances stable until an elusive economic recovery takes place.

**DICK LARKIN’S CONTINUING REASONS FOR HOLDING PUERTO RICO BONDS**

1. **PUERTO RICO STILL HAS STATE-LIKE SOVEREIGN POWERS.** States as a category have had the lowest default rates of any municipal bond. Although Puerto Rico is not a state, it has many of the same sovereign powers that a state has, including the power to tax and legislate without
interference from a higher authority. Unlike some states like California and Massachusetts, there are no constitutional or voter approved tax limitations that Puerto Rico is subject to. And as S&P’s Dave Hitchcock reminded us at MAGNY, Puerto Rico is not authorized to be able to file for bankruptcy.

2. **THE ECONOMY STILL BENEFITS FROM NO FEDERAL INCOME TAX ON RESIDENTS.** Puerto Rico’s low income levels can provide a cost-efficient working base for corporations willing to invest in the island’s economy. The Puerto Rico Industrial Development Company (PRIDCO) estimates that labor costs in Puerto Rico are about 20% lower than in the States. In addition, bona fide residents of Puerto Rico do not have to pay U.S. Federal Income Taxes, unless the income is earned outside of Puerto Rico or they are employees of the Federal Government. While the U.S. federal income tax burden is low or zero for many residents, the Commonwealth must maintain high taxation rates to offset the lack of federally funded spending programs. However, studies have indicated that the total per capita tax burden in the Commonwealth is lower than in the U.S. I recently calculated the total income tax burden for a family of 4 that rents (no itemized deductions) and has Puerto Rico’s median family income of about $35,000 to be about $1,545; in Mississippi, the state with the lowest average income, federal and state taxes combined for about $1,740 on the same median family income, or a tax premium of about 12% to live and work in the U.S..

3. **PUERTO RICO RETAINS TAX ADVANTAGES FOR BUSINESS** There remain some corporate tax advantages for locating business to Puerto Rico, even after increases imposed to address the deficit. For example, 16 of the 20 top selling pharmaceutical drugs in the United States are made in Puerto Rico. And the recent excise tax hikes have allowed some reductions in individual and business income taxes starting in 2011; those tax incentives, however, are now significantly reduced under the adopted tax increases for fiscal 2014.

4. **HIGH PER CAPITA COMMONWEALTH DEBT MASKS THE FACT THAT MOST RESIDENTS ARE NOT PAYING FOR THE UNITED STATES NATIONAL DEBT.** Studies show that per capita debt in Puerto Rico is more than 2 times the average for U.S. States; an argument can be made that debt is higher because it doesn’t receive the same federal spending benefits that states enjoy, so it must be funded at the local level. Moreover, it could also be argued that because bona fide Puerto Rico citizens do not pay federal income taxes, the crushing burden of the Federal Government’s debt of over $50,000 per capita does not weigh on most Puerto Rico residents. That puts Puerto Rico’s high debt burden in a different perspective. As in the earlier example, Commonwealth income taxes are still below comparable taxes within the United States, so the argument that Puerto Rico’s debt load is higher than for states holds no water.

5. **FISCAL REFORM HAS PUT THE COMMONWEALTH CLOSE TO BUDGETARY BALANCE.** While Puerto Rico’s financial operations are checkered, fiscal discipline that started with former Governor Luis Fortuno has escalated under Governor Padilla. Besides an unprecedented package of tax increases, Puerto Rico has adopted substantial pension reforms that will improve funding and rein in growth of benefit costs. (It must be noted that these pension reforms cost money, and have increased the budget imbalance that already existed.) In addition, fee increases and
restructuring for the island’s major enterprise systems (electric, water/sewer and highways) will eliminate general fund deficit pressures into the future. While the annual imbalance has been reduced to a few hundred million dollars, (compared to the multi-billion dollar deficit that met the Governor upon taking office), the Commonwealth deserves criticism for continuing to put off full deficit elimination for two fiscal years instead of “biting the bullet” and eliminating borrowing for operating costs completely.

6. **DESPITE OPERATING DEFICITS, SOME BORROWED MONEY IS BEING USED TO JUMP START THE ECONOMY.** The deficit funding in the 2014 budget includes about $260 million for new initiatives to improve operations and spur economic development. There are an additional $100 million of non-general funds dedicated solely to new economic initiatives. While meager compared to the costs of maintaining annual government operations, investment into growing and diversifying the Commonwealth’s economy are important if long term fiscal stability can ever be reached. A return to stimulating the economy by increasing government employment would just undo all of the long-term benefits of balancing the budget. Private sector growth and employment must be a goal, within the parameters of getting Puerto Rico’s financial house in order.

7. **THE GOVERNMENT DEVELOPMENT BANK BRINGS ADVANTAGES TO PUERTO RICO THAT MOST STATES CANNOT AVAIL THEMSELVES.** Puerto Rico has another advantage over most states because of its relationship with Puerto Rico’s Government Development Bank. This has been an important stabilizing factor and a facilitator of debt financing, including short-term seasonal cash flow notes. More recently, the GDB was able to lend money temporarily to the Commonwealth when the municipal debt market was being roiled this summer by Detroit’s bankruptcy and the negative headlines over Puerto Rico’s long-term problems. The GDB has also led efforts to improve the transparency of Puerto Rico debt and financial operations, transparency which is crucial for investors.

8. **STRINGENT LONG TERM PLAN TO BALANCE RISING PENSION COSTS.** While funding for Puerto Rico’s Employees Retirement fund is abysmal, the Government has taken a firm stance, passing a law which will require the Commonwealth to increase its contribution rate another 1% each year for the next 10 years, bring the employer contribution rate from 9.75% to 20.5% of employees’ covered salaries. In addition, more employees are being shifted to lower-risk defined contribution funding, while retirement ages were increased and higher employee contributions were enacted.

9. **COFINA (PUERTO RICO’S SALES TAX BOND AUTHORITY) GIVES THE COMMONWEALTH FLEXIBILITY TO MEET ITS WELL-ADVERTISED BOND ISSUE NEEDS WITH BETTER MARKET ACCESS AND LOWER BORROWING COSTS.** Janney’s Alan Schankel pointed out the better marketability and higher ratings of COFINA compared to the Commonwealth. S&P’s Hitchcock also characterized COFINA as a stronger credit in the muni bond market than the Commonwealth itself. I commented that the new plan to replace normal Puerto Rico general obligation bonds with COFINA debt was a decided positive in my report of September 25, when the borrowing plan was first announced. (See Sims’ September 27 report [http://www.hjsims.com/news-views/hj-sims-dick-larkin-updates-puerto-rico-tobacco-bonds/](http://www.hjsims.com/news-views/hj-sims-dick-larkin-updates-puerto-rico-tobacco-bonds/) )
BUT ARE THERE “SHARKS” CIRCLING THE MARKET?

10. PUERTO RICO’S WORST CASE: R-E-C-O-V-E-R-Y. Finally, I’ve come full circle to my report’s title. But in this case, I am not talking about fiscal or economic recovery, but a more esoteric concept in the municipal bond industry—the likelihood that an investor will recover most, if not all, of his or her investment in Puerto Rico debt were there to be a default on its debt. Last year, I made the argument that Puerto Rico may be “too big to fail”. I’ll repeat that I don’t believe that there is a likelihood of a federal bailout, although a recent Wall Street Journal article detailed behind-the-scene discussions in Washington of just such a notion, if anonymous spokesman are to be believed. If such a move took place, Puerto Rico bondholders would surely benefit from such protection, but in my opinion, it is not only unwarranted, I think it would set a bad precedent in a municipal bond market that has functioned exceedingly well without federal government intervention. In fact, given the current impasse between Congress and the President, I don’t think I would want to take the fed as a partner if I were governing the Commonwealth.

Pundits have likened Puerto Rico to Greece, or Detroit Michigan; these comparisons are ill-informed. The problems faced in Greece, and the actions necessary to solve that crisis are unfathomable when compared to Puerto Rico’s situation. And as for Detroit, whose emergency manager is seeking to “cram-down” 80% losses to bondholders in its bankruptcy, I’ve already demonstrated that, by following methods used by other cities in severe fiscal stress, a “PLAN B” is possible to allow that city’s bondholders to be paid in full. (See http://www.hjsims.com/news-views/plan-b-for-detroit/ for more detailed discussion.) To put the Detroit/Puerto Rico comparison to rest, let me put it as Yogi Berra would: when Puerto Rico came to a fork in the road, they took it. In Detroit’s case, the driver hit the median, so the fork is still “untaken” for that poor city.

In the worst case, Puerto Rico could be compared to NYC in the 1970’s--high debt, large deficits, and a weak economy. New York defaulted on short term debt obligations, under what was thought to be a legal “moratorium” law that the state enacted to prevent a run on the City’s dwindling cash. NYC was eventually rescued by the lenders that originally caused NYC’s debt to go unchecked. By investing in a newly created conduit borrower (the Municipal Assistance Corporation) with extra legal provisions to protect investors, these lenders returned to lending funds—the alternative would have been to write-off significant amounts of debt on their balance sheet. Puerto Rico has already created a safer conduit borrower called COFINA, which has a first legal claim on Commonwealth sales taxes. Because of the breadth and depth of Puerto Rico’s indebtedness, lenders would probably act the same way in order to protect their existing investment of over $60 billion of Commonwealth debt. And the Commonwealth has the ongoing incentive to repay in full because of its demonstrated need for external borrowing.

History shows that investors that panicked and sold their New York City debt at losses of 50 cents on the dollar lost their hard-earned savings; those investors that could see beyond the doomsday headlines and political hysteria of 1975 were richly rewarded for keeping their heads, while all around them were losing theirs. A substitute borrowing authority, the Municipal Assistance Corporation for New York (M.A.C.) had to be created to buy time and provide an alternative borrowing entity for that beleaguered city. Puerto Rico already has one in its back pocket in the form of COFINA.
THE BOND RATINGS

The rating agencies all have a negative outlook on Puerto Rico with ratings just above the “Great Divide” of non-investment grade. Yet at the height of the Commonwealth’s financial problems in 2010 & 2011, Moody’s recalibrated the rating upward to A3 in 2010, and S&P upgraded the rating from BBB-to BBB in 2011. Throughout the last six years, low pension funding was acknowledged within the ratings. Yet it appears that, as the government has taken actions to reduce deficit borrowing, improve its pension systems and bring Puerto Rico to its best operating state in over 10 years, more downgrades and junk-bond status may be on the horizon. Their timing seems to be way off. I continue to worry more that the Commonwealth will keep on course as it has for the last four years, than what might come out of the rating agencies.

THE INSTITUTIONAL INVESTOR MARKET & ITS IMPACT ON PUERTO RICO BOND PRICES

As I’ve cautioned in the past, investing in Puerto Rico debt is not for those that will be seeking to liquidate their holdings during this period of high interest rate volatility. It’s been reported that many bond funds, which have been seeing money outflows for months, have been liquidating their Puerto Rico investments, sometimes at distressed prices. While regulations no longer require funds to maintain positions based only on public bond ratings, it’s likely that some funds use bond ratings as at least one benchmark or criteria for selling off portfolio investments. A downgrade of Puerto Rico’s debt to below investment grade may trigger more sell-offs; it’s also possible that many funds may have already reduced or eliminated their Puerto Rico exposure in anticipation of more downgrades. It’s also been reported that hedge funds have become active buyers of Puerto Rico debt at today’s distressed prices. If this is true, it is a disturbing trend because the motivations of a hedge fund looking for above average returns in a short period are markedly different than the motivations of long-term investors seeking safe steady income. I am amazed at how suddenly hedge fund managers, who have never seen an actual municipal bankruptcy, have suddenly become quotable authorities, stirring up irrational fears for reasons that may not be altogether altruistic. Shades of Meredith Whitney and her famous prediction of a municipal bond Armageddon that has never materialized, not even in this year of Detroit’s bankruptcy.

I’ve tried to make the case that retail investors concerned with income and not prices have a sound investment in Commonwealth-issued debt. There is evidence all around that the make-up of institutional investors of Puerto Rico debt is changing significantly. With all that in mind, buyers and sellers of the Commonwealth’s debt, beware of the sharks.

ABOUT THE AUTHOR

Richard Larkin is a Senior Vice President and Director of Credit Analysis, joining HJ Sims in February 2008, where his first assignment was to testify before the House of Representatives on the Bond Insurance Crisis. Dick worked at J.B. Hanauer from 2003-2008, where he performed high-yield municipal bond analysis for traders and brokers in Hanauer’s five offices in New Jersey, Pennsylvania and Florida. Prior to joining Hanauer, Dick was a Managing Director in Fitch’s public finance group and served as the Co-chairman of its Public Finance Criteria Committee. He covered high-profile taxsupported and revenue bond credits and had
supervisory responsibility for credit surveillance and the training and development of the public finance staff. Prior to joining Fitch in 1998, Dick was a Managing Director and Chief Municipal Rating Officer at Standard & Poor’s where he was responsible for municipal rating policies, practices, governance and criteria. Following a twenty-one year career at S&P, Dick served as a financial advisor to Fairmount Capital Advisors where he developed credit enhancement programs for public pension funds. Later, he helped found Reliance SRL, a rating agency that performed local credit ratings in Uruguay.

From 1988-1992, Dick was a charter member of the Anthony Commission on Public Finance, which was created to consider the effects of federal tax law on the ability of state and local governments to carry out their responsibilities to their citizens and to recommend improvements to those laws. From 1995-1998, Dick served on the National Advisory Council on State & Local Budgeting (NACSLB). This industry task force, comprising representatives from the private sector and officials from all levels of local government, identified and fostered 60 of the best budgeting practices that have been implemented by our best-run state and local governments.

Dick earned his BA in economics from Iona College and a Masters in economics from Fordham. In 1999-2000, he was a key participant in the implementation of Fitch’s Default Study and revision of its criteria and ratings. During the same period, he authored the definitive study on the impact of municipal government’s management practices on credit ratings, defining for issuers a rating agency’s relative evaluation of best management practices. Dick has had hands-on rating experience in 42 states, at all levels of state and local government covering virtually every type of debt structure and security pledge. He has been a frequent speaker at state and national Government Finance Officers’ Association (GFOA) conferences, and has articles published in national media and public finance textbooks. Dick has appeared frequently on CNBC, Bloomberg Television and Fox Business News, and has been widely quoted in the Wall Street Journal, BusinessWeek, the Bond Buyer and Bloomberg reports, as well as many other media outlets. Dick serves on the Policy Committee for the Securities Industry and Financial Markets Association (SIFMA), and is on the Technical Committee of Municipal Bonds For America (MBFA), a public/private coalition charged with educating government officials about the benefits of tax-exemption for municipal bonds for government issuers as well as the investment market. He was also awarded the National Federation of Municipal Analysts’ Award for Excellence in 1996, and in 2008, 2009, 2010 & 2011 was elected the First Team Special Revenue Bond Municipal Analyst by Smith’s Research & Ratings.

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