

# MARKET CHATTER: WHAT'S NEXT FOR PUERTO RICO BONDHOLDERS?

NEPC Research  
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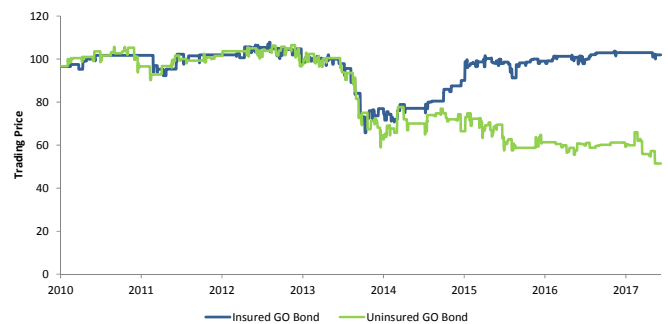
There's no playbook for this one: Puerto Rico is essentially **seeking bankruptcy protection** as it has no way to meet its financial obligations—including over \$70 billion of debt issued by local agencies—making it the largest municipal restructuring in US history.

Its bondholders include some of Wall Street's savviest investors, ranging from hedge funds to retirement accounts. Mutual funds hold about \$14 billion of Puerto Rico's outstanding debt, according to Morningstar; hedge funds hold a similar amount, according to estimates, but exact numbers are difficult to come by due to limited disclosure requirements. Given the substantial stakes, there is little doubt that the **restructuring will prove to be complex and messy** as creditors mount expensive legal defenses in efforts to secure their place in the pecking order. What is in doubt is the outcome for investors. While the end result is likely to be some form of haircut for most bondholders, the range of recoveries could be a wide one, ranging from 80 cents on the dollar to as low as 35 cents, according to Moody's Investors Service.

The largest volumes of Puerto Rico bonds outstanding are general-obligation issues, or GOs, and sales-tax based COFINA bonds; GOs make up roughly 18% of the total debt outstanding and COFINAs account for around 24%. A GO bond with a 5% fixed-rate coupon maturing in 2024 recently traded at 102 cents on the dollar, while an-

other GO issue with the same coupon and duration is trading at 54.50 cents. The sole differentiating factor: the bond trading at a premium is insured and the other one is not. This difference will likely prove to be significant as investors of the insured debt should be protected leaving bond insurers on the hook should Puerto Rico default.

Markets are differentiating between bonds



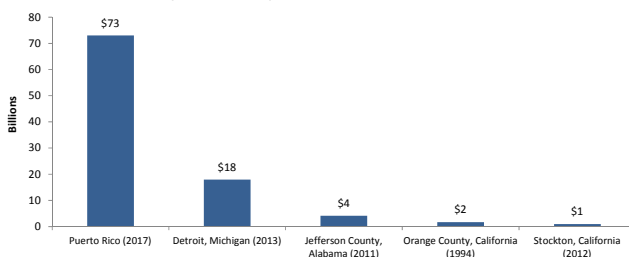
Source: Bloomberg, FINRA

As with other distressed or stressed assets, there will be winners and losers. We believe an actively managed credit strategy that has really done its homework could benefit from these turn of events. Here, at NEPC, we are closely monitoring the situation and exploring potential investment opportunities and managers. We will be sure to provide timely updates as events unfold.

## Disclaimers and Disclosures

- Past performance is no guarantee of future results.
- All investments carry some level of risk. Diversification and other asset allocation techniques do not ensure profit or protect against losses.
- The information in this report has been obtained from sources NEPC believes to be reliable. While NEPC has exercised reasonable professional care in preparing this report, we cannot guarantee the accuracy of all source information contained within.
- The opinions presented herein represent the good faith views of NEPC as of the date of this report and are subject to change at any time.

Municipal Bankruptcies - Estimated size of debt



Source: Bloomberg, FINRA, Moody's