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# PUERTO RICO CONFERENCE

Entrepreneurship for Growth

# 2010

March 24, 2010 | Conrad San Juan Condado Plaza | 7:30 a.m. - 5:00 p.m.

P u e r t o R i c o C h a m b e r o f C o m m e r c e



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# **The Current Outlook for Puerto Rico**

**Puerto Rico Conference 2010, Entrepreneurship for Growth**

# Agenda

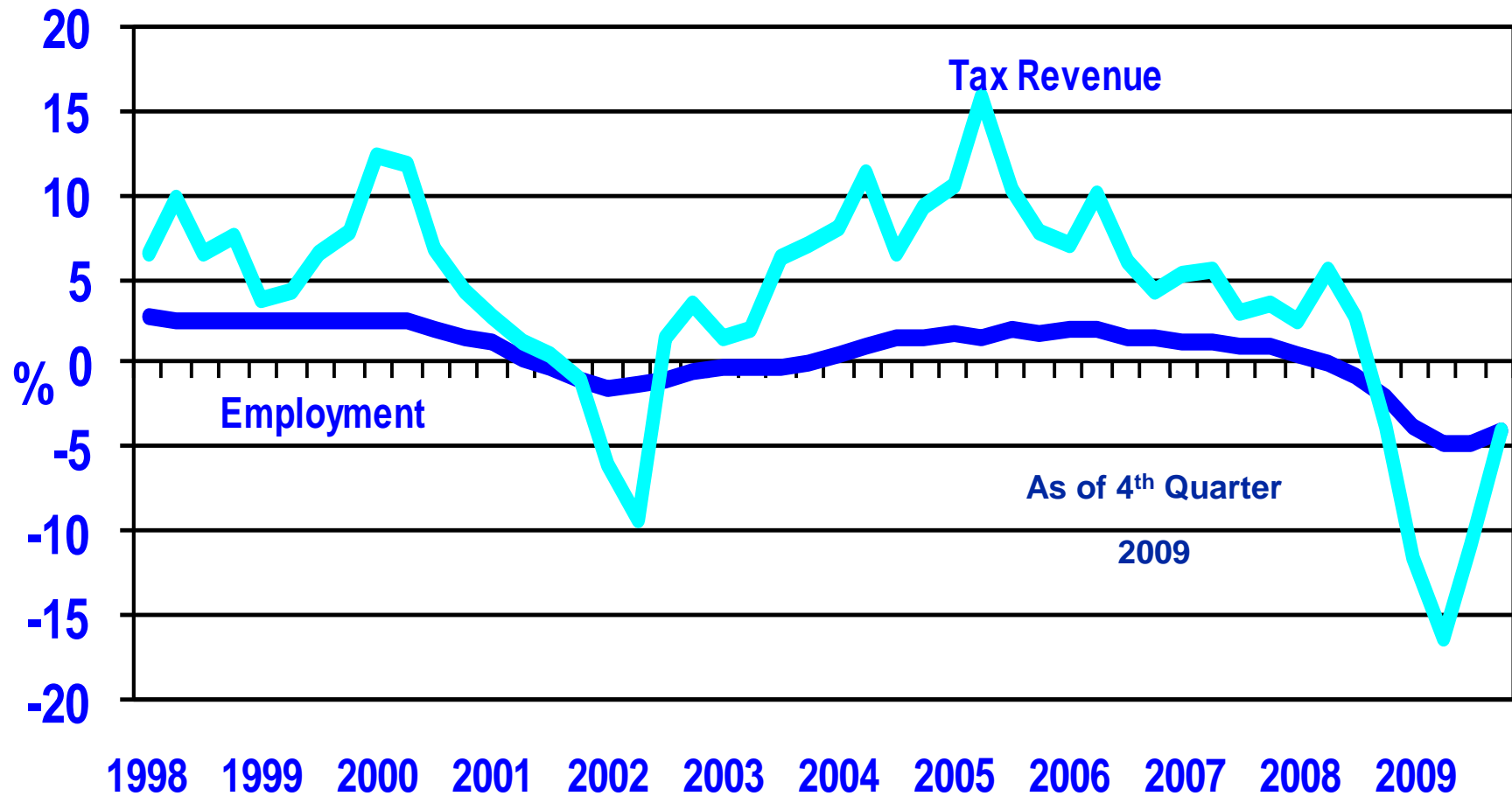
1. States Big Picture—Economy and Finances
2. Outlook for the Future
3. Puerto Rico in the Current Environment
4. Puerto Rico Going Forward
5. Municipal Rating Recalibration



# 1. States Big Picture—Economy and Finances

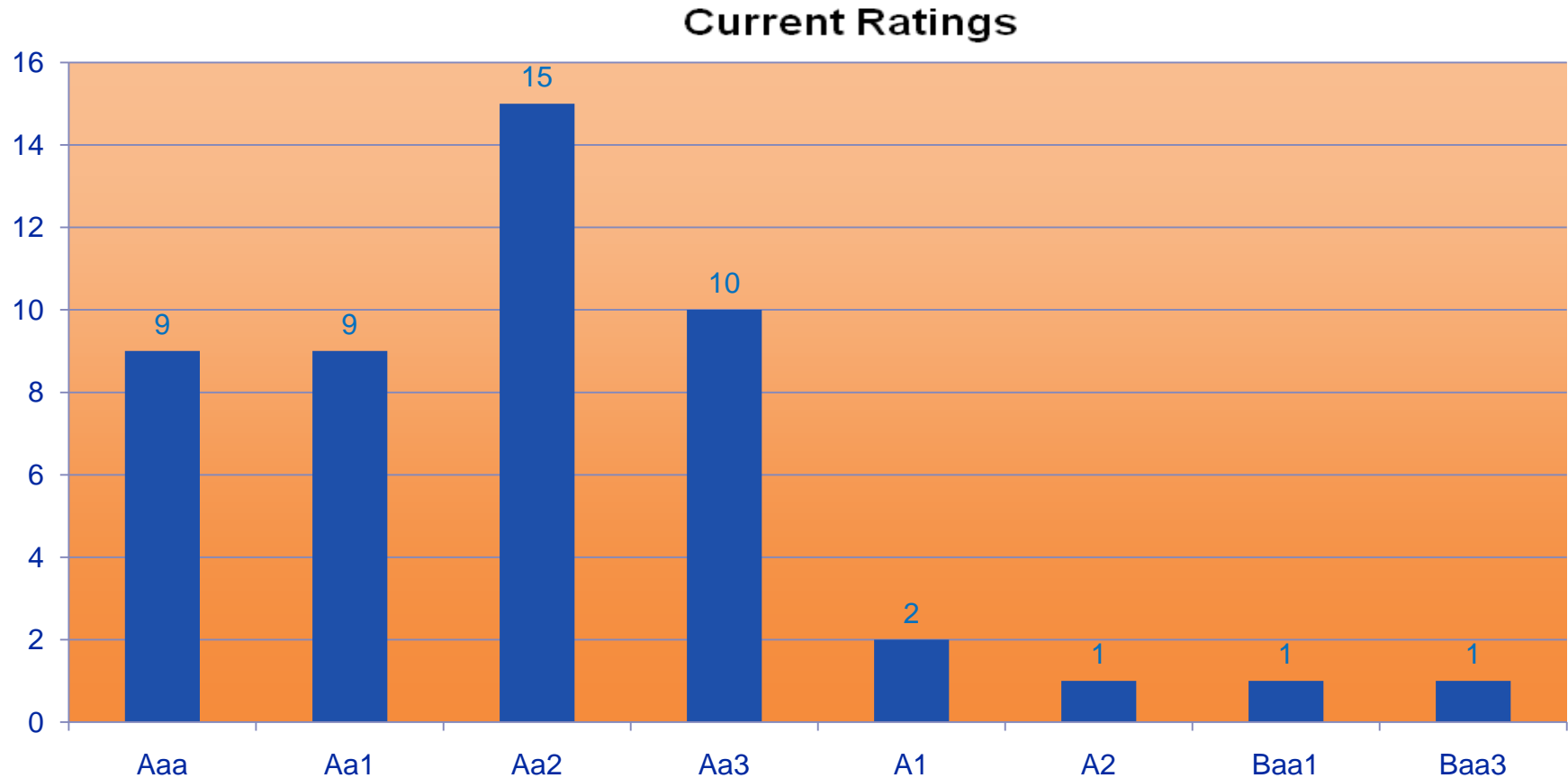


# State Tax Revenue Falling (through December 2009)



Source: Rockefeller Institute and Bureau of Labor Statistics

# Distribution of State and Puerto Rico G.O. Ratings



» **40 General Obligation Ratings**

» **8 Issuer Ratings**

## Rating Downgrades Reflect Recessionary Pressure

Rating Actions	2001	2002	2003	Subtotal		2007	2008	2009	2010	Subtotal
Upgrades	1	0	1	2		5	1	0	0	6
Positive Outlook Changes	0	3	0	3		5	0	4	0	9
Positive Watchlist Actions	2	1	3	6		0	0	0	0	0
<b>Downgrades</b>	<b>4</b>	<b>2</b>	<b>8</b>	<b>14*</b>		<b>1</b>	<b>0</b>	<b>6</b>	<b>0</b>	<b>7**</b>
Negative Outlook Changes	12	8	3	23		6	5	7	2	20
Negative Watchlist Actions	2	2	6	10		0	0	5	0	5

» **2001-2003: Sudden sharp decline; rapid rebound**

» **2007-2009: Slower, but deeper decline; slow rebound expected**

» **Federal fiscal stimulus has cushioned the fall**

\* affecting 10 states

\*\* affecting 5 states



## 2. Outlook for the Future





# State and Local Government Outlooks

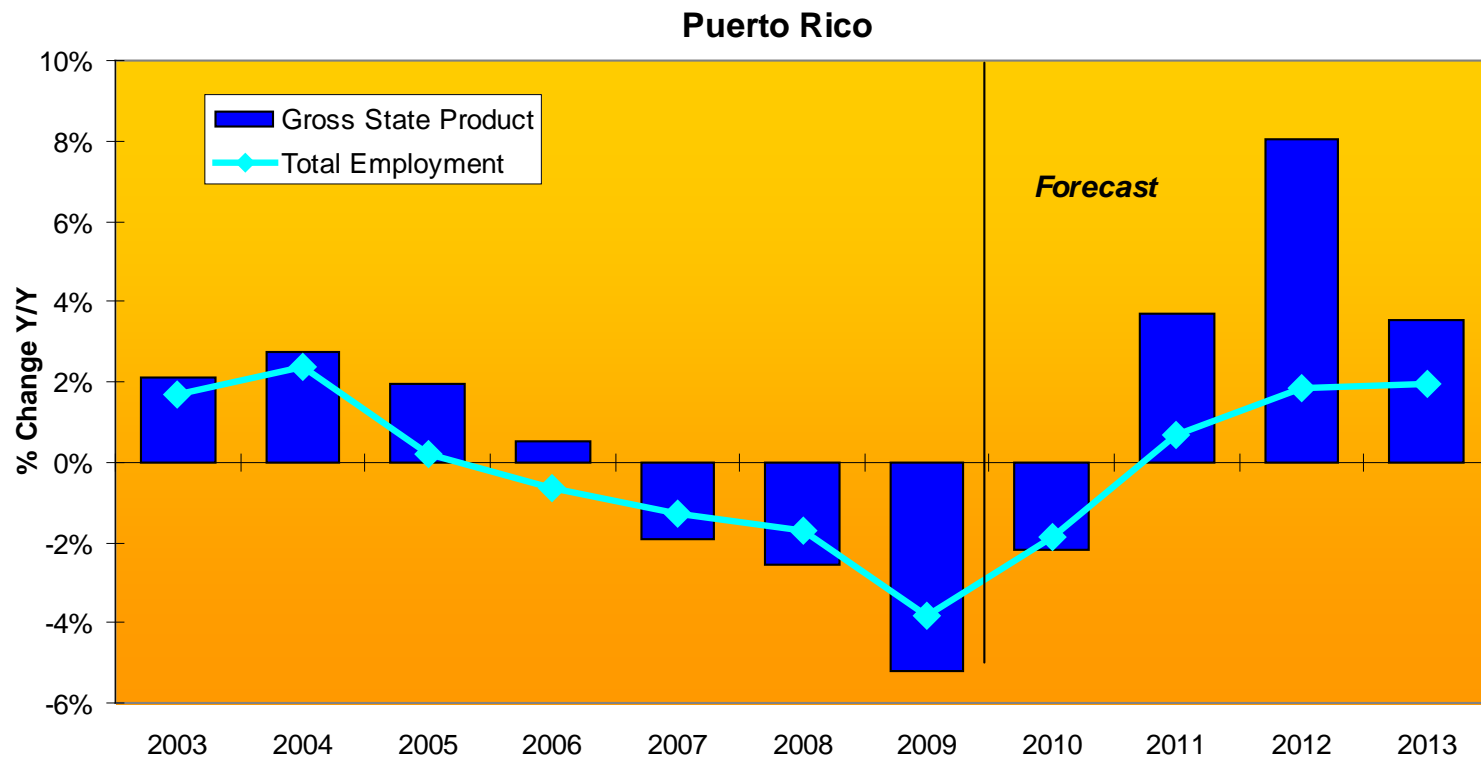
- » Outlook for state governments and local governments both negative
- » While there are signs that the U.S. economy has begun to recover, fiscal recovery for state and local governments will lag the economic recovery
- » Despite the continuing credit stress, the majority of state and local government issuers are expected to manage through the next 18-24 months with no more than a modest rating impact

### 3. Puerto Rico in the Current Environment



# Puerto Rico Economy and Finances

- » Economy still in recession
- » Moody's Economy.com projects negative GSP and employment growth in 2010, followed by modest growth in 2011

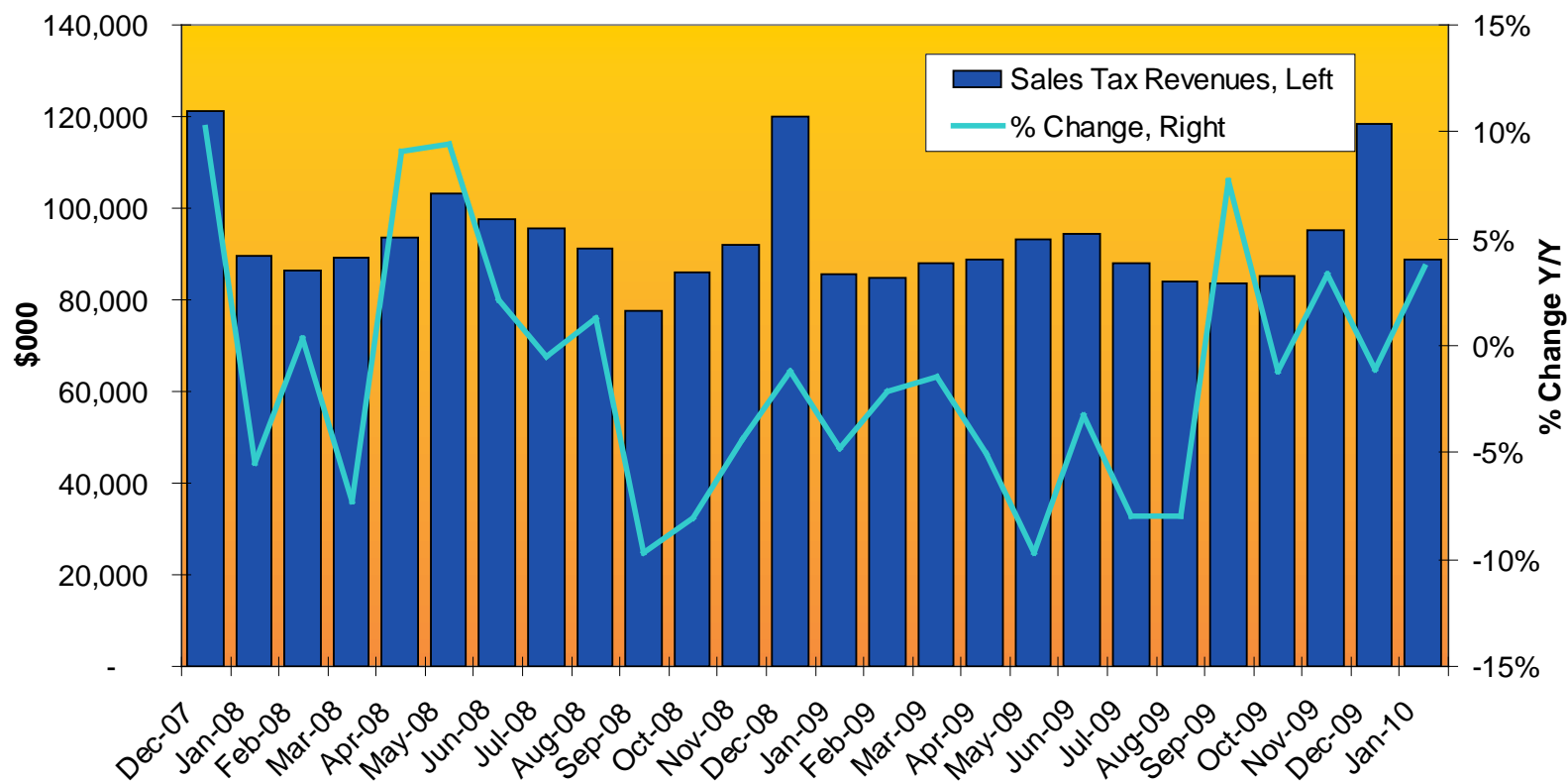


Source: Moody's Economy.com

# Puerto Rico Economy and Finances

» Despite weakness in economy and finances, sales tax performing relatively well

– Up 3.7% in Jan 2010 vs. Jan 2009



# Puerto Rico Budgeting

- » **Conservative budgeting of tax revenues**
- » **Expenditure control primarily through employment measures**
- » **Deficit financing used for budgetary relief**
  - Sales tax revenue bonds
  - Restructuring GO bonds to push out debt service payments
- » **Measures of success include:**
  - Revenue collections very close to expectations for July-December 2009
  - Employment measures enacted
  - Cash balances (December 2009) exceeding projections

## 4. Puerto Rico Going Forward



# Puerto Rico Going Forward

- » Puerto Rico's plan for fiscal stability and structural balance is ambitious
- » Passage and implementation has been speedy thus far
- » Continued resolution to stick to plan will be essential
- » Once outcome of tax reform committee is known, tax revenue details and impact on commonwealth general fund will be considered
- » Having a good plan is a positive rating factor, but even more important than the plan is the *result*



# Puerto Rico Going Forward

- » Success of government's plans will depend upon:
  - Global and national economy
  - Local economic recovery (federal stimulus and local economic stimulus may play a role)
  - Employment measures leading to expected savings
  - Close management of debt
  - Continued efforts toward structural balance
    - » Conservative budgeting of revenues
  - Continued market access


## 5. Current Status of Moody's Municipal Rating Recalibration



# Current Status of Moody's Municipal Rating Recalibration

- » **Moody's will recalibrate its ratings of U.S. municipal bond issues and issuers to its global scale beginning in mid-April**
- » **Result will be comparability of Moody's municipal ratings with ratings in other sectors such as sovereign, sub-sovereign, corporate and financial institutions**
- » **More information on [www.moodys.com/gsr](http://www.moodys.com/gsr)**

MARCH 2010
U.S. PUBLIC FINANCE



**RATING METHODOLOGY**

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## Recalibration of Moody's U.S. Municipal Ratings to its Global Rating Scale

### Overview

Beginning in April 2010, Moody's plans to recalibrate its long-term U.S. municipal ratings to its global rating scale. The global rating scale is used to rate sovereign, sub-sovereign, financial institution, project finance, structured finance and corporate obligations. This recalibration will enhance the comparability of ratings across the Moody's-rated universe. Historically, Moody's municipal ratings have been calibrated on a separate rating scale that emphasizes the ordinal ranking of credit risk within the municipal sector only and measures distance to distress. Upon recalibration Moody's will maintain a single global scale rating system for municipal issuers, and we will no longer assign municipal scale ratings to municipal obligations.

Our benchmarking analysis of municipal credits against global scale ratings across the Moody's rated universe will result in an upward shift for most state and local government long-term municipal ratings by up to three notches<sup>1</sup>. The degree of movement will be less for some sectors, most notably in the enterprise sectors<sup>2</sup> which are largely already aligned with ratings on the global scale.

*Market participants should not view the recalibration of municipal ratings as rating upgrades, but rather as a recalibration of the ratings to a different rating scale.*

This recalibration does not reflect an improvement in credit quality or a change in our credit opinion for rated municipal debt issuers. Instead, the recalibration will align municipal ratings with their global scale equivalent. A key driver for the recalibration is the market's increasing desire for rating comparability between municipal and non-municipal sectors given the growing number of "cross-over" investors active in both tax-exempt and taxable markets.

The following summarizes our conclusions by broad municipal sector:

» State and local government general obligation (GO) ratings: will change by an average of about two notches higher than their current ratings on the municipal scale, with a range of zero to three notches. Ratings at or above Aa3 on the municipal scale will receive less upward movement than those rated below Aa3.

<sup>1</sup> A notch is defined as a step on Moody's alphanumeric rating scale (e.g., from A2 to A1).

<sup>2</sup> The enterprise sectors include healthcare, higher education, housing, not-for-profit organizations, public power, transportation, and other infrastructure projects.

# Conclusion

- » **Broad and deep recession**
- » **Major state revenues hit very hard**
- » **Federal fiscal stimulus cushioned the blow**
- » **Jobs will lead us out of the recession**
- » **Revenue growth will lag economic recovery**
- » **More negative pressure on state ratings**
- » **Puerto Rico's rating will reflect its ability to handle its economy, budget, and finances relative to its peers**

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