



COMMONWEALTH OF  
PUERTO RICO

Government Development Bank  
for Puerto Rico



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Good afternoon. My name is Melba Acosta and I am the President of the Government Development Bank for Puerto Rico. Thank you for taking the time this afternoon to meet with us. Puerto Rico appreciates the partnership that many of you have provided over the years, and welcomes the opportunity to discuss the process that we will be undertaking in partnership in the coming months.

As you are aware, Puerto Rico faces an economic and financial crisis. Our economy has been stagnant for many years, and our structural deficits have persisted notwithstanding the efforts of recent administrations. This administration has been focused on putting Puerto Rico on a path to economic recovery and long-term fiscal sustainability by tackling long-standing structural challenges. In particular:

- We have sought to significantly increase Commonwealth revenues to reduce budgetary deficits. These measures have included an increase of 4.5% in the rate of the sales and use tax and a material expansion of its base; a material increase in our petroleum products tax, and a pledge to consider implementation of a value added taxation system.
- We have significantly reduced expenses and taken measures to stabilize the Commonwealth's cost-structure. Act 66 of 2014 fixed formula based appropriations and froze hiring, collective bargaining agreements and other labor benefits.
- Since 2006, public employees of the Commonwealth and its instrumentalities have been reduced by over 25%.
- We reformed our largest pension system by moving all existing employees to a defined contribution plan, eliminating non-core pension benefits and increasing employee contributions and the retirement age.
- We have embarked on a restructuring of the power authority, constructively engaging with our creditors in an effort to develop a consensual restructuring that enables PREPA to attract

additional investment and implement significant upgrades to its system so as to provide cost efficient electricity to the island's residents and businesses.

Even though we have taken bold action to improve our fiscal situation, our work is not yet complete. As you will hear from Dr. Krueger today and as Governor Garcia Padilla outlined two weeks ago, we continue to face significant challenges.

- Declining investment in the island
- Continuing decrease in housing prices
- High labor costs and low labor participation rates
- Negative demographic trends, including a declining population
- High energy and transportation costs
- Significant federal and Commonwealth legacy regulations constraining business activity

This persistent economic stagnation has resulted in recurrent budget deficits, which have been financed in part by a significant increase in debt over such period to fund the difference between collected revenues and incurred expenses. For example, in 2013 and 2014, based on the broader methodology used by Dr. Krueger, we had \$4.2 and \$4.7 billion of aggregate financing needs, respectively. More than half of those funding gaps were filled with incremental debt financing. This cycle of recurring budgetary deficits financed by long-term debt in the context of a stagnating economy cannot be sustained any longer; Puerto Rico must achieve economic growth in order to achieve the primary surpluses necessary to support its debt. In any case, doubts about the sustainability of our existing debt have made market access for new financings at reasonable terms difficult, if not impossible.

Therefore, in order to rebuild market confidence in Puerto Rico and ensure that the island regains market access and the economic vitality necessary to satisfy the needs and demands of all its stakeholders, we are embarking on a broad reform package that is targeted at structurally reforming the Commonwealth's economy, reducing the financing gap based on a credible fiscal adjustment plan, and implementing the necessary institutional reforms to execute such plan and make our financial situation more transparent to investors.

Dr. Krueger's report identifies various alternatives to address our structural challenges and close our projected financing gaps. The Commonwealth is committed to using Dr. Krueger's report as the starting point for the development of a long-term economic recovery and fiscal adjustment plan. With that said, we don't expect to implement each measure identified by Dr. Krueger and other alternatives will be considered as we develop the plan. Relying upon Dr. Krueger's expertise and drawing upon our internal resources and those of our other advisors, we are committed to developing a comprehensive package of reforms that will enable us, over time, to reinvigorate our economy and permanently address our fiscal challenges. We want all our stakeholders, including our creditors, to be partners in, and contributors to, a successful outcome to this process. Today's meeting is the first of what we hope will be a series of productive conversations with our creditors towards the end of revitalizing Puerto Rico's economy and making its debts sustainable over the long term.

The implementation of this plan will not be easy. The reforms needed will require sacrifice by and contributions from all of our stakeholders. That includes, first and foremost, the people of Puerto Rico, who have endured a decade of economic stagnation and fiscal retrenchment and are willing to continue doing their part in the context of broader solution to the current crisis. It includes Government employees, local and multinational businesses, as well as the municipal and Commonwealth governments. It also needs to include the Federal Government, who, as Dr. Krueger's report highlights, can aid our economic and fiscal recovery through necessary and long-demanded changes in federal policy. And it must include our financial creditors, who have invested in Puerto Rico, and must now help Puerto Rico return on that investment.

We have made many tough decisions up to this point, but our recovery depends on participation from everyone who is invested, either personally or financially, in the success of Puerto Rico. We expect the economic recovery and fiscal adjustment plan to be comprehensive and to include structural and institutional reform, revenue and expense measures and, as Dr. Krueger's report foreshadows, a temporary adjustment to the terms of the Commonwealth's accumulated debt load. The fiscal adjustment required is simply too large for any single group of stakeholders to bear alone without having a negative effect on what we are all trying to achieve: a turnaround of the economic fortunes of Puerto Rico so that it can thrive economically again for the benefit of its citizens and our investors.

The projected financing gaps we face are very large. A credible economic recovery and fiscal adjustment plan is central to our turnaround effort and while that plan remains in development, it would be premature for me to suggest the manner and extent the debt of the Commonwealth and its various related issuers may need to be adjusted. When our economic recovery and fiscal adjustment plan is completed, the contribution required from each of our investors will be made clearer. We have no fixed, unalterable designs on how to achieve this level of contribution from our creditors; we are committed however for such contribution to be sufficient to achieve the plan's goals. I ask for your patience while we develop a credible plan that meets all of our stakeholders' objectives.

We are fully aware that, for any plan to be credible, we will need to provide creditors and other stakeholders with reasonable comfort that the Commonwealth will honor the commitments and achieve the milestones outlined in such plan. Any credible plan will take many years to fully implement and span beyond the current term of this administration. In order to ensure that the plan is implemented and enforced throughout the adjustment period, this Administration, after consultations with the Puerto Rico Legislature, will propose that a financial control board be created to monitor ongoing compliance by successive Administrations with the plan's targets. The financial control board would be charged with ensuring that the Commonwealth, and each of its agencies and instrumentalities, meets the targets set for it in the economic recovery plan. And, if those targets aren't met voluntarily by this administration, or future administrations, the control board will be given the tools necessary to compel compliance with those targets. We are conscious of the fact that, in order for any control board to provide the necessary comfort to all stakeholders regarding the credibility and execution of a fiscal adjustment plan, the membership and powers of such commission will have to be designed with care, in consultation with our legislature. We are committed to working with all our stakeholders to design an institution that has the necessary credibility and authority to ensure Puerto Rico is on a path to fiscal and economic recovery.

I'd like to spend a few moments discussing the process by which the economic recovery and fiscal adjustment plan will be developed. The Governor has appointed a Working Group of five members, which includes the Governor's Chief of Staff, the Secretary of Justice, the President of the Senate, the Speaker of the House and myself. The Working Group is charged with overseeing the development of

the plan. We have engaged advisors and consultants to assist us with the development of this plan and the Governor has asked that the Working Group provide a draft plan to him no later than September 1st. We have a lot of work to do in a very short period of time, but the Working Group is committed to meeting that deadline and doing the best we can to meet all of the objectives the Governor set out for us. After the plan is complete, the Working Group will work with our legislature and Governor to develop the necessary legislative framework to implement the plan. As we work through this process, we will endeavor to update our investors from time to time and will welcome ideas from all our stakeholders. With a credible plan in hand, we expect to sit down to negotiate a consensual adjustment of that part of the debt necessary to ensure that we have adequate time and resources to turn Puerto Rico's economy around so that we can honor our financial commitments over the long term. This consensual negotiating process must be successful. As evidenced by examples elsewhere in the world, a contentious, drawn-out adjustment process will not be in the best interests of the Commonwealth or of its creditors. I am confident that we will work together constructively towards our common goals.

Thank you for your continued support of the Commonwealth. There is no more important project to the people of Puerto Rico and we look forward to working with you during this critical period.