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Research Update:

Government Development Bank for Puerto Rico Downgraded To 'CC' From 'CCC-' On Imminent Default; Outlook Negative

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Overview

- The Government Development Bank for Puerto Rico (GDB) made an official announcement, on Friday, July 10, of its intent to purchase or exchange, from "time to time," its outstanding senior notes in the open market and in privately negotiated transactions at a price the bank expects to be "materially less than par."
- In addition, the president of GDB, Melba Acosta, has been quoted in recent press alluding to ongoing discussions to restructure debt below par. She also alluded to a "consensual adjustment" on a portion of Puerto Rico's debt in her address to creditors in New York yesterday.
- Although the details, including the timing, are unclear at this point, we very likely would classify an exchange offer or similar restructuring as tantamount to default, in line with our criteria, as investors would likely receive less than the par value of the securities.
- We are therefore lowering our rating on GDB to 'CC' from 'CCC-', reflecting our view that a default is virtually certain.
- The rating outlook is negative. We will lower the issuer rating to 'SD' if GDB executes a debt exchange, and we will lower the issue-level rating on any exchanged debt to 'D'.

Rating Action

On July 14, 2015, Standard & Poor's Ratings Services lowered its long-term issuer credit rating on the Government Development Bank for Puerto Rico (GDB) to 'CC' from 'CCC-'. At the same time, we are affirming our 'C' short-term issuer credit rating on GDB. The rating outlook is negative.

Rationale

This downgrade reflects our view that a default by GDB in the near term is a virtual certainty. GDB has announced its intent to purchase its outstanding senior notes in the open market and in privately negotiated transactions through cash or exchange with new securities at a price the bank expects to be "materially less than par." We would deem such an exchange as distressed and consider it a default under our criteria. We affirmed our short-term rating because we believe it already reflects our expectation for default in the near term.

We lowered our general obligation (GO) rating on the commonwealth and its debt

to 'CCC-' on June 29, reflecting our view that a default, distressed exchange, or redemption of the commonwealth's debt appears to be inevitable within the next six months absent unanticipated, significantly favorable changes in the issuer's circumstances. At present, we understand the potential debt exchange relates only to GDB debt, and hence our ratings on the Puerto Rico GO and appropriation debt remain unaffected.

We continue to monitor GDB's financial performance and believe its fundamental credit quality, including its business position, risk position, and funding and liquidity, are very weak. Moreover, we expect credit metrics to continue to be weighed down by the commonwealth's inability to access funding markets, and the overall deteriorating business, financial, and economic conditions in Puerto Rico.

GDB faces nearly \$900 million of notes maturing in fiscal 2016, and it had net liquidity of roughly \$778 million as of May 31, 2015. We believe, in light of its tight liquidity conditions and limited ability to raise capital, GDB will have difficulty meeting its debt service requirements.

Outlook

The rating outlook is negative, reflecting our view that a default on GDB's debt is virtually inevitable. We expect we will lower the issuer rating to 'SD' if GDB executes a debt exchange, and we will also lower the issue-level rating on any exchanged debt to 'D'. When GDB has completed the planned restructuring of its debt, we expect to update our assessment of the banks stand-alone credit profile.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	CC/Negative/C	CCC-/Negative/C
Anchor	bbb+	bbb+
Business Position	Very Weak (-5)	Very Weak (-5)
Capital and Earnings	Very Strong (+2)	Very Strong (+2)
Risk Position	Very Weak (-5)	Very Weak (-5)
Funding and Liquidity	Below average and very weak(-5)	Below average and very weak(-5)
Support	0	0
GRE Support	0	0
Group Support	0	0
Sovereign Support	0	0
Additional Factors	-2	-1

Related Criteria And Research

Related Criteria

- Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings, Oct. 1, 2012
- Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Banks: Bank Capital Methodology And Assumptions, Dec. 6, 2010
- Rating Implications Of Exchange Offers And Similar Restructurings, Update May 12, 2009

Related Research

- Puerto Rico's Latest Financial Disclosure Confirms Precarious Liquidity Position, July 9, 2015
- Government Development Bank for Puerto Rico Long-Term Rating Lowered To 'CCC-'; Outlook Negative June 30, 2015
- Puerto Rico GO Rating Lowered To 'CCC-' From 'CCC+'; Outlook Is Negative On Likelihood Of Default Or Distressed Exchange, June 29, 2015
- Ratings On Four Puerto Rico-Based Banks Placed On CreditWatch Negative Following The Downgrade Of Puerto Rico's GO Debt, Feb. 13, 2015
- Under Pressure: Puerto Rican Bank Ratings Face Several Major Hurdles, May 19, 2014

Ratings List

Downgraded; Ratings Affirmed

	To	From
Government Development Bank for Puerto Rico Issuer Credit Rating	CC/Negative/C	CCC-/Negative/C

Downgraded

Government Development Bank for Puerto Rico Senior Unsecured	CC	CCC-
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