



# **The Economic and Fiscal Reconstruction Plan of Puerto Rico**

**The Municipal Forum of New York**

**Mr. Carlos M. García  
Chairman and President**

**April 16, 2009**



**1. Introduction and Action taken in the first 100 days**

**2. The Economic and Fiscal Reconstruction Plan**

**3. Financial Stabilization Measures**



# Puerto Rico is a Regional Economy of the U.S.

| Factors                                | Description  |
|--|--|
| <b>Economic Relation with the U.S.</b> | <ul style="list-style-type: none"><li>• P.R. is a Top 20 trading partner of the U.S.</li><li>• Resilient consumer sector</li><li>• 41% of GDP is manufacturing / Top 5 pharmaceutical cluster in U.S.</li></ul>              |
| <b>Favorable Demographics</b>          | <ul style="list-style-type: none"><li>• Population ~4.0 million.</li><li>• Population ranks higher than 25 states; comparable to Oregon</li><li>• Slightly younger: median age is 32 years versus 35 years in U.S</li></ul>  |
| <b>U.S. Regulatory System</b>          | <ul style="list-style-type: none"><li>• U.S. Constitutional and Legal Protection</li><li>• U.S. Banking and Financial Regulatory System</li><li>• U.S. Federal Court Presence and Intellectual Property Protection</li></ul> |



# GDB has a comprehensive role and an adequate capital base

## Comprehensive Role

### Banker

- Public
- Private

### Fiscal Agent

- Metrics and Monitoring
  - Fiscal Compliance
  - Public Corporations
  - Central Government

### Objectives

Fiscal Reconstruction  
Economic Reconstruction  
Sustainable Development

- Treasury and ALM\*
- Asset Management
- Investment Strategies

### Financial Advisor

- Macro & Regional Analysis
  - Economic Modeling
  - Statistical Reliability

### Strategic Planner

Ratings: **BBB (Stable) / A-2 S&P**  
Governance: **7 member board (6 from private sector)**

## Balance Sheet\*\* (millions) Mar-31-09

|                                |                 |
|--------------------------------|-----------------|
| Invested Assets                | \$4,819         |
| Loans                          | 6,757           |
| Other Assets                   | 920             |
| <b>Total Assets</b>            | <b>\$12,496</b> |
| Deposits                       | \$5,972         |
| Bonds and Notes                | 3,311           |
| Other Liabilities              | 791             |
| <b>Total Liabilities</b>       | <b>\$10,074</b> |
| <b>Net Assets</b>              | <b>\$2,422</b>  |
| <b>Net Assets/Total Assets</b> | <b>19.4%</b>    |

Source: GDB. Dollars in millions.

\*ALM = Asset and Liability Management.

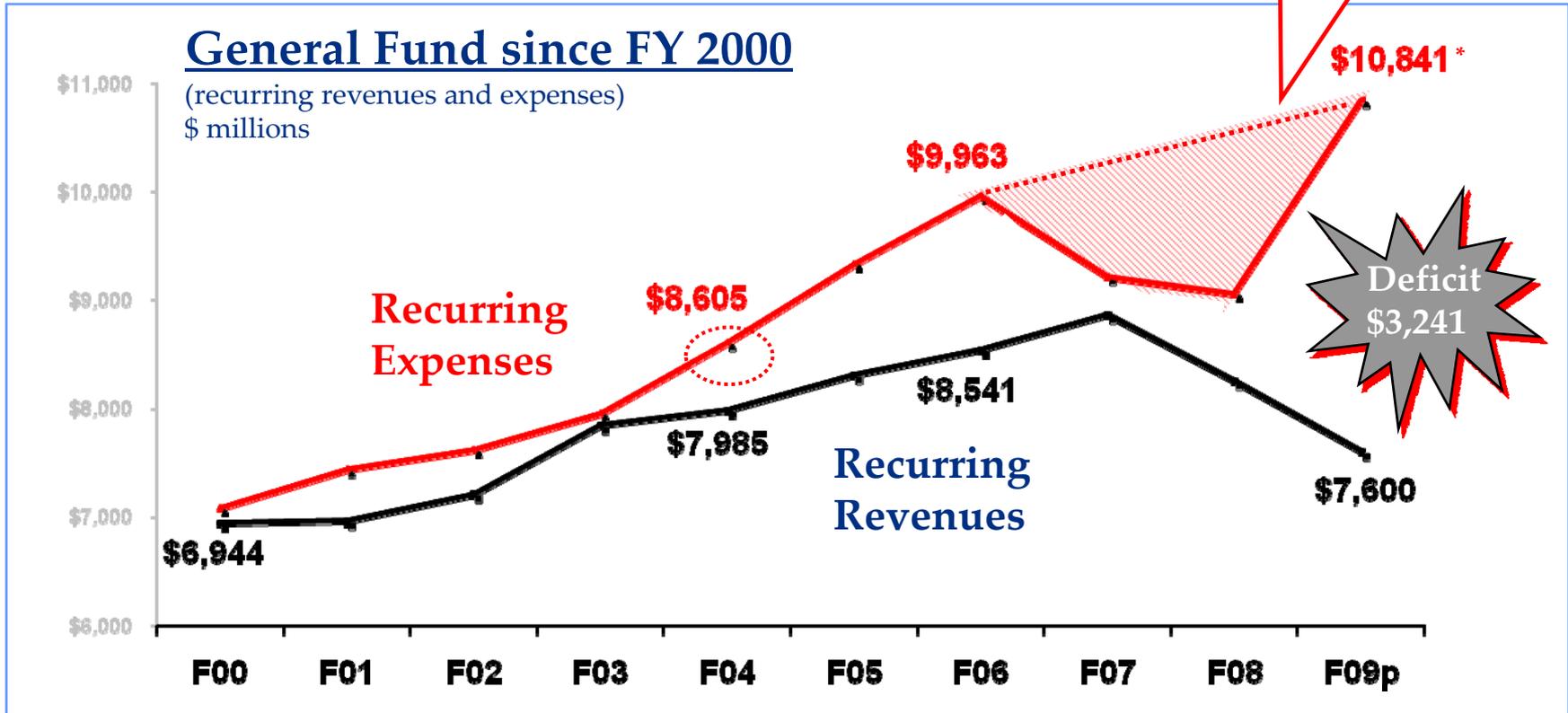
\*\* Consolidated GDB balance sheet. Preliminary and subject to change.



# Fiscal Emergency: due to a recurrent gap between revenues and expenses

- In FY 2004, expense growth accelerated
- Temporary measures to postpone expenses in fiscal years 2007 and 2008 exploded in 2009
- Reported deficits were covered with non-recurring measures that have run out

Expenses not taken into account in the budget



Source: P.R. Planning Board, 2008 Transition Reports.

\* Excludes payment for \$1,000 million of a portfolio of tax receivables from the PR Treasury Department.

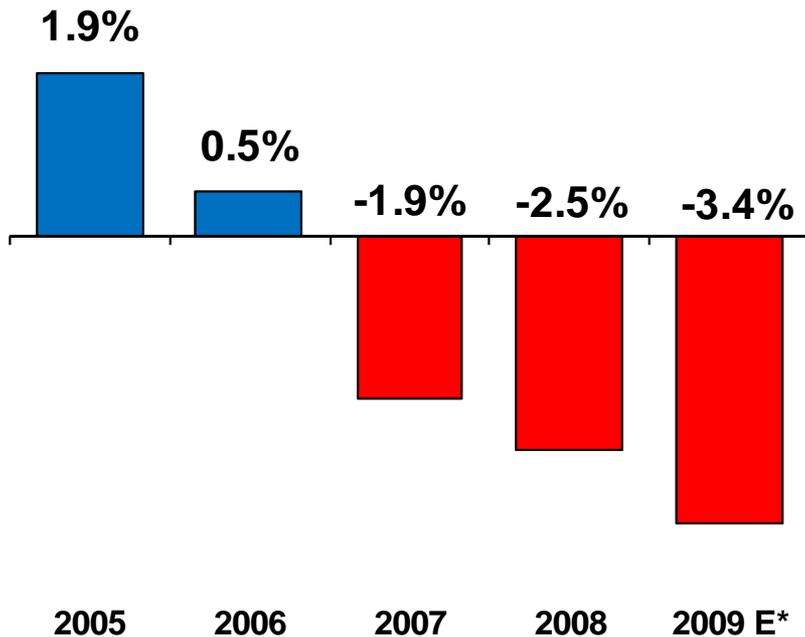


# We have recognized the challenges affecting Puerto Rico

1

## Economic Recession

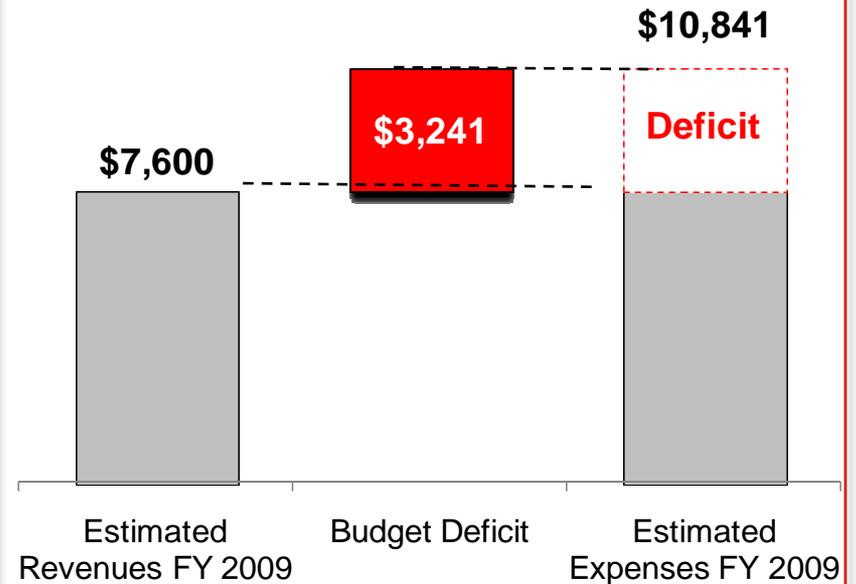
Real GNP Growth



2

## Fiscal Emergency

General Fund Data (Million)



# We have responded with swift action

## **Fiscal and Economic Challenges:**

- **Economy in recession**
- **Need of stimulus and investment**
- **Fiscal deficit of \$3.2 bn**
- **Multi-Year Budget Plan**

**SWIFT  
ACTION**

## **We have taken action:**

- **Developed a Reconstruction Plan for the next 4 years**
- **Have enacted 7 bills to implement the Plan**
- **Enhanced investor relations program**
- **Strong fiscal agent**

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3. **Financial Stabilization Measures**



The Executive and Legislative Branches worked together to successfully approve a Reconstruction Plan with three main goals

## Goals of the Reconstruction Plan

- 1. Stabilize the fiscal situation**
- 2. Safeguard Puerto Rico's investment grade credit**
- 3. Rebuild the local economy**

1

Enacted Legislation Jan-14-09

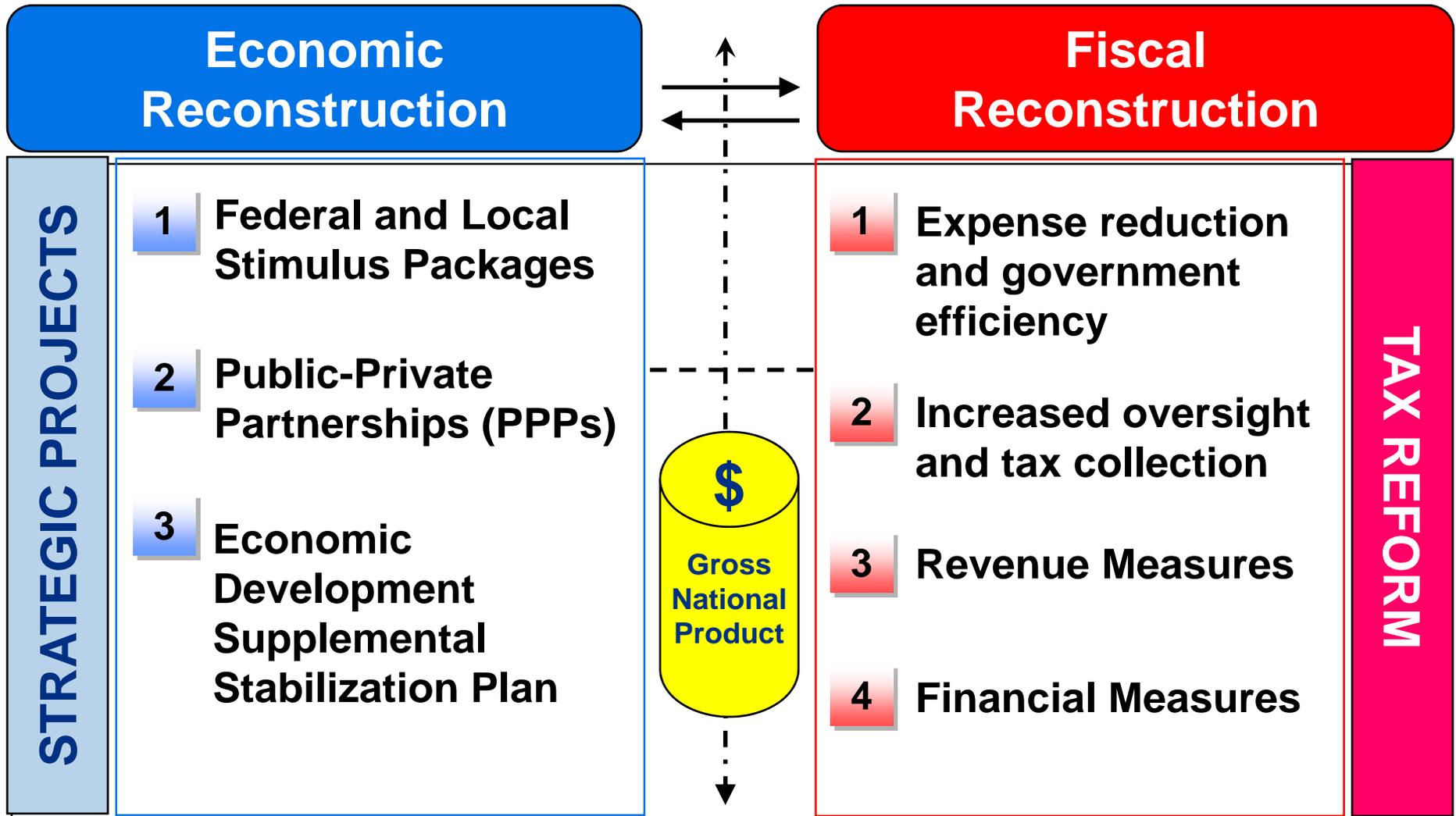
- Act # 1:** Additional 1% allocation to COFINA
- Act # 2:** Temporary use of deficit financing
- Act # 3:** PRIFA Corpus Account restructuring
- Act # 4:** Temporary increase in limit on GDB loans

2

Enacted Legislation Mar-09-09

- Act # 7:** Fiscal Emergency Act
- Act # 8:** PRIFA as Federal Stimulus manager
- Act # 9:** Local Stimulus Plan

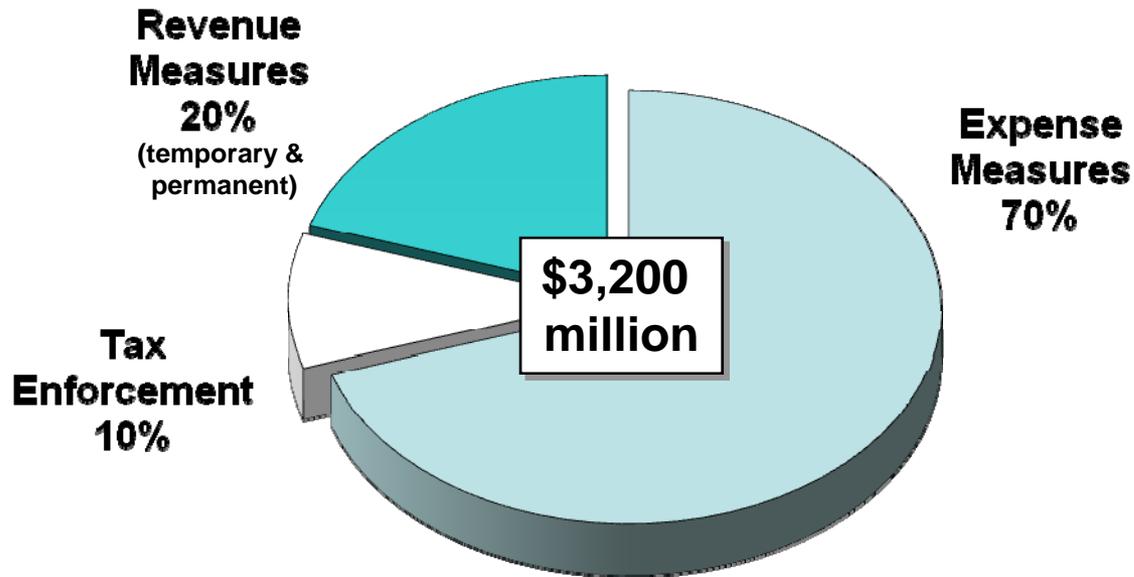
# The Administration has started implementing a balanced and comprehensive multi-year Plan





# The Fiscal Reconstruction Plan is based on a combination of measures

## Distribution of Fiscal Reconstruction Measures



Financial Stabilization Measures



# Expense Reduction Measures

**Goal: \$2,000 million savings**

## Expense Reduction Measures

### PAYROLL EXPENSES

- 30% reduction of non-career personnel
- Salary reduction of agency heads
- Salaries freeze, ban of new posts and elimination of vacant posts
- PHASE I: Incentivized resignations and work load reduction
- PHASE II: Transition of employees
- PHASE III: Temporary freeze in economic conditions

### OPERATIONAL EXPENSES

- Austerity: 10% of operational expenses, including cell phone use, credit cards and official vehicles.
- Executive Branch reorganization, supported by budgeting and accounting processes and IT.

## Public Employees Alternatives Program

**Educational Voucher**

**Retraining / Vocational  
Voucher**

**50% salary subsidy for  
transition to private or  
non profit sector job  
up to \$15,000**

**Self-Employment  
Voucher**

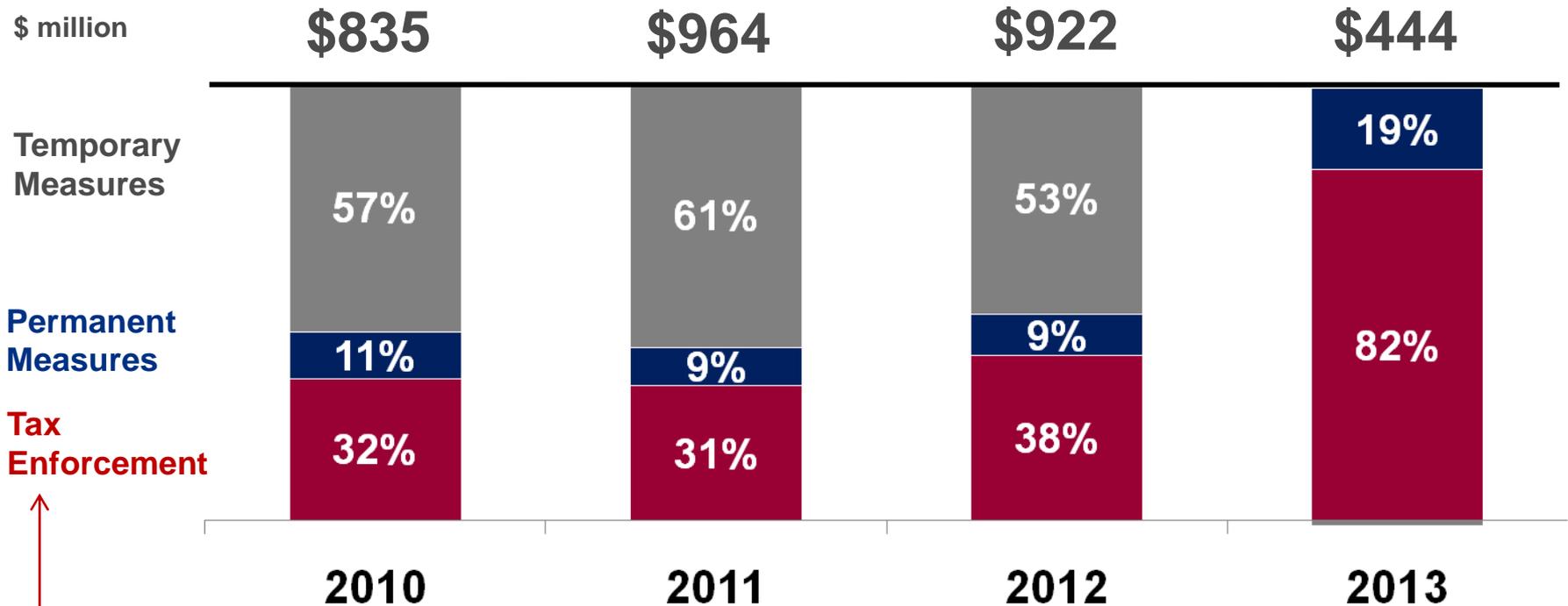


# We are following a strict calendar in implementing the expense measures

|  |                             |   |
|--|-----------------------------|---|
| • <b>Enactment of Act No. 7 and effective day of Phase III (temporary freeze of economic conditions)</b> | <b>Mar-09-09: Completed</b> | ✓ |
| • <b>Creation of Fiscal Restructuring &amp; Stabilization Board (FRSB)</b>                               | <b>Mar-09-09: Completed</b> | ✓ |
| • <b>Release of Circular Letter with details on Expense Reduction Program</b>                            | <b>Mar-20-09: Completed</b> | ✓ |
| • <b>Public Agencies Notify Employees about Phase I (Voluntary)</b>                                      | <b>Mar-27-09: Completed</b> | ✓ |
| • <b>Orientation about Transition Alternatives to Public Employees</b>                                   | <b>Weekend Apr-18-09</b>    |   |
| • <b>Eligible Employees Submit Form for Phase I</b>  | <b>Apr-27-09</b>            |   |
| • <b>Voluntary Resignations Effective</b>  | <b>May-29-09</b>            |   |
| • <b>Notification of first round of Phase II (if necessary)</b>  | <b>May-29-09</b>            |   |
| • <b>Voluntary Workday Reduction becomes Effective</b>   | <b>Jun-01-09</b>            |   |
| • <b>First round of Phase II is effective (if necessary)</b>   | <b>Jul-03-09</b>            |   |



# A combination of permanent and temporary tax measures and enforcement initiatives should increase revenues



Tax Enforcement

Improvement in tax enforcement and collections is key for the Plan

### Distribution of Measures

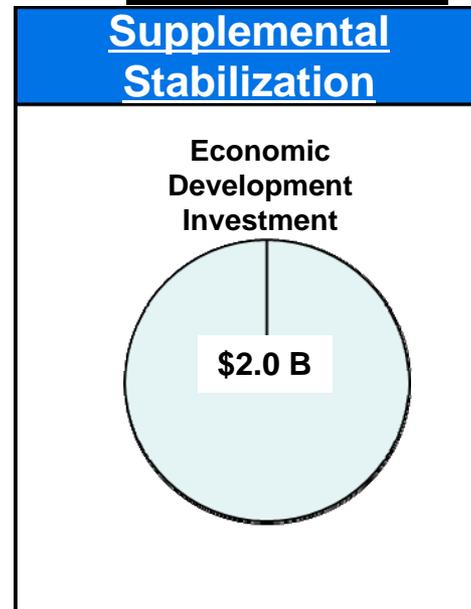
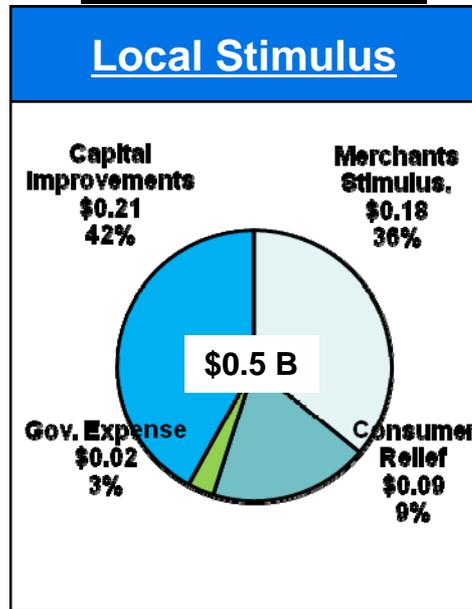
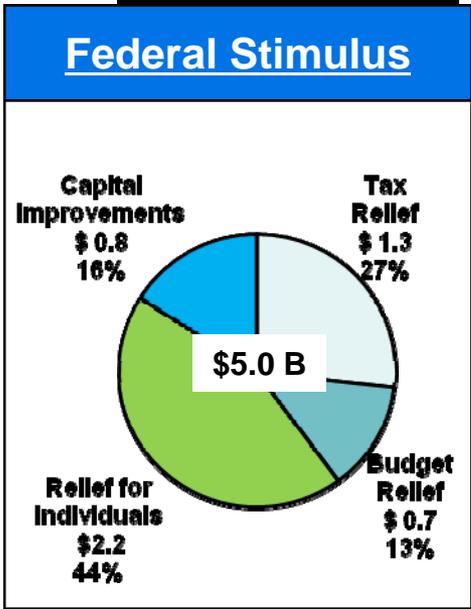
- 3 Permanent revenue measures
- 6 Temporary revenue measures
- 6 Tax Enforcement Measures

# The Economic Reconstruction Plan consists of significant stimulus and investment measures

Jun-09 -----> 2011

(\$ billions)

$$\begin{array}{ccccccc}
 \$5.0 & + & \$0.5 & + & \$2.0 & = & \$7.5 \text{ BN} \\
 \text{PHASE Ia} & & \text{PHASE Ib} & & \text{PHASE II} & & \\
 \text{Federal Stimulus} & & \text{Local Stimulus} & & \text{Supplemental Stabilization} & & 
 \end{array}$$



**12%**  
of GNP

Public-Private Partnerships



# Comments from Rating Agencies have been Positive

[Moody's Investors Service, March 2009:](#)

**“These measures... support plans to reestablish fiscal solvency for the commonwealth... it [is] a significant achievement that the administration and legislature have worked together to quickly produce a plan for recovery...”**

**E. Raimés, E. Behr and B. Kurtter**

[Standard & Poor's \(in Bloomberg News\), March 9, 2009:](#)

**“Puerto Rico is taking the right steps to preserve its investment-grade credit rating with a deficit-reduction plan ...”**

**Horacio Aldrete**

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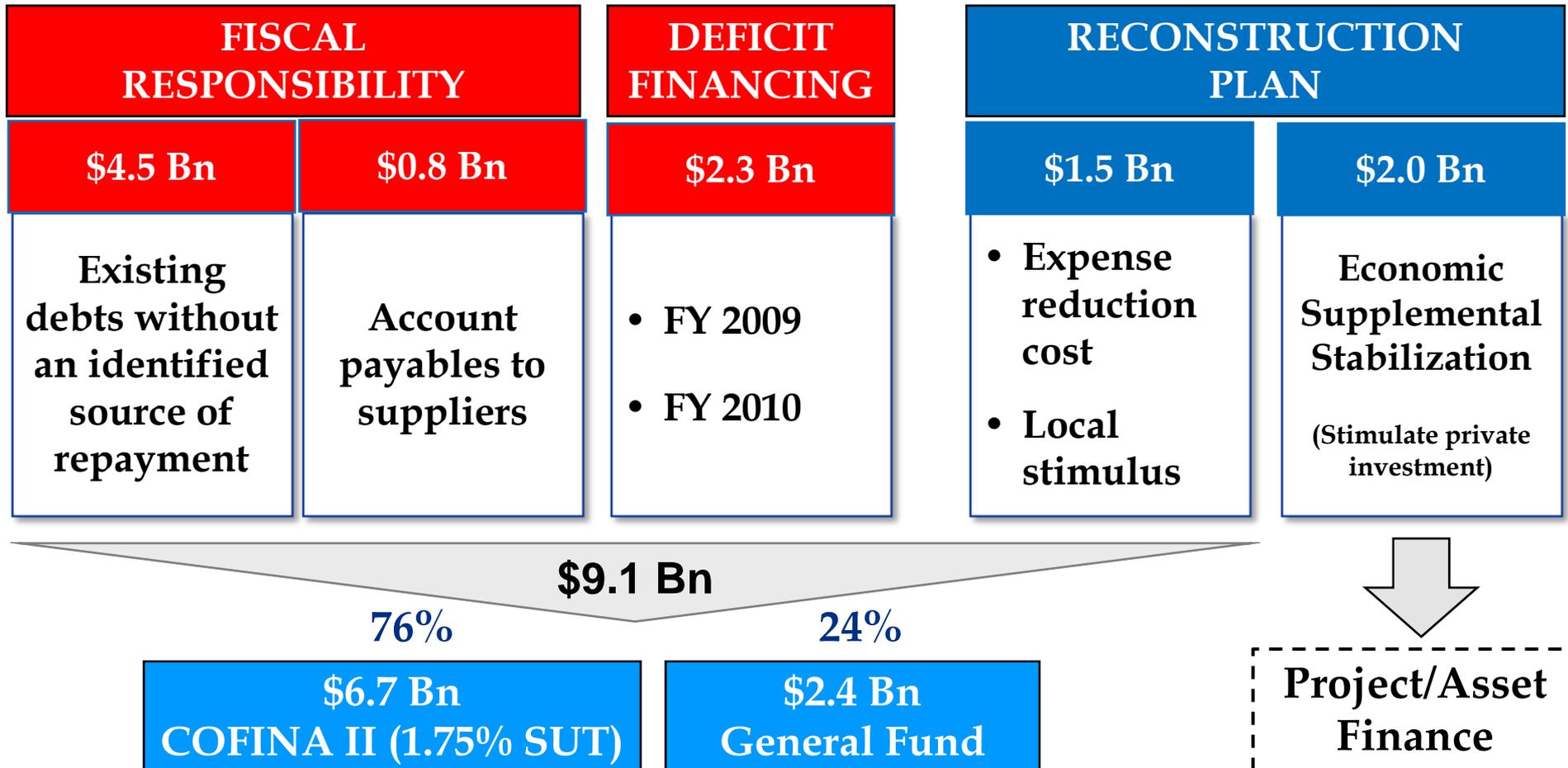
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# Financial Stabilization Measures

- Recognizing outstanding obligations/identifying a source of repayment
- Bridging the timing gap to a balanced budget
- Funding the Reconstruction Plan towards economic growth





# COFINA II is the financial “anchor” of the Fiscal Reconstruction Plan

**COFINA is a affiliate of the GDB that receives a dedicated portion of the sales tax and has the capacity to issue bonds.**

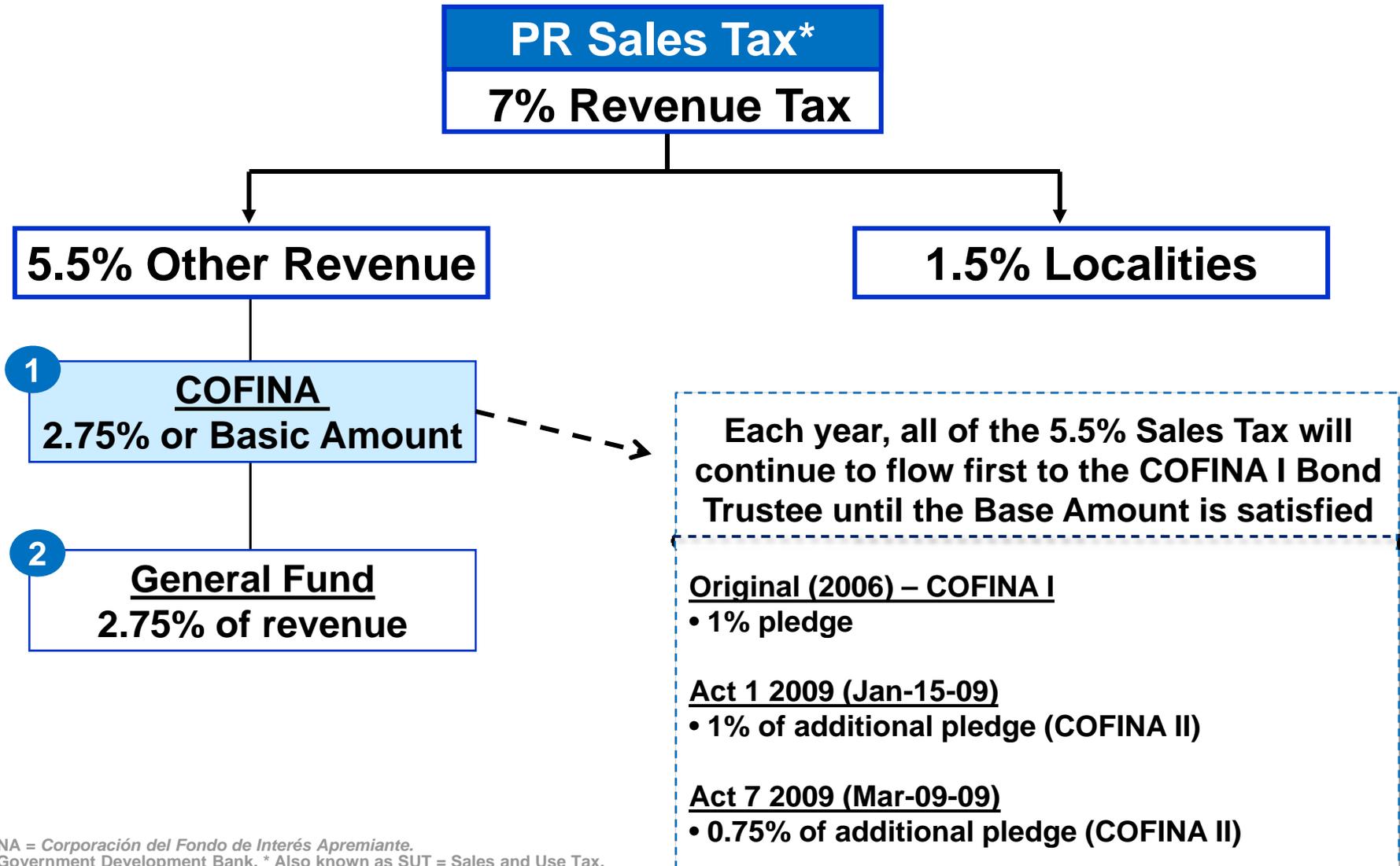
## Proposed financing of COFINA II:

| Deal Component       | Comments*                        |
|----------------------|----------------------------------|
| Initial Deal Size:   | \$3.0 - \$4.0 billion            |
| Timing of financing: | May 2009                         |
| Market access:       | 103 Market & Puerto Rico markets |

\* Preliminary and subject to market conditions.



# Dedicated tax revenue structure



\* COFINA = *Corporación del Fondo de Interés Apremiante*.  
Source: Government Development Bank. \* Also known as SUT = Sales and Use Tax.



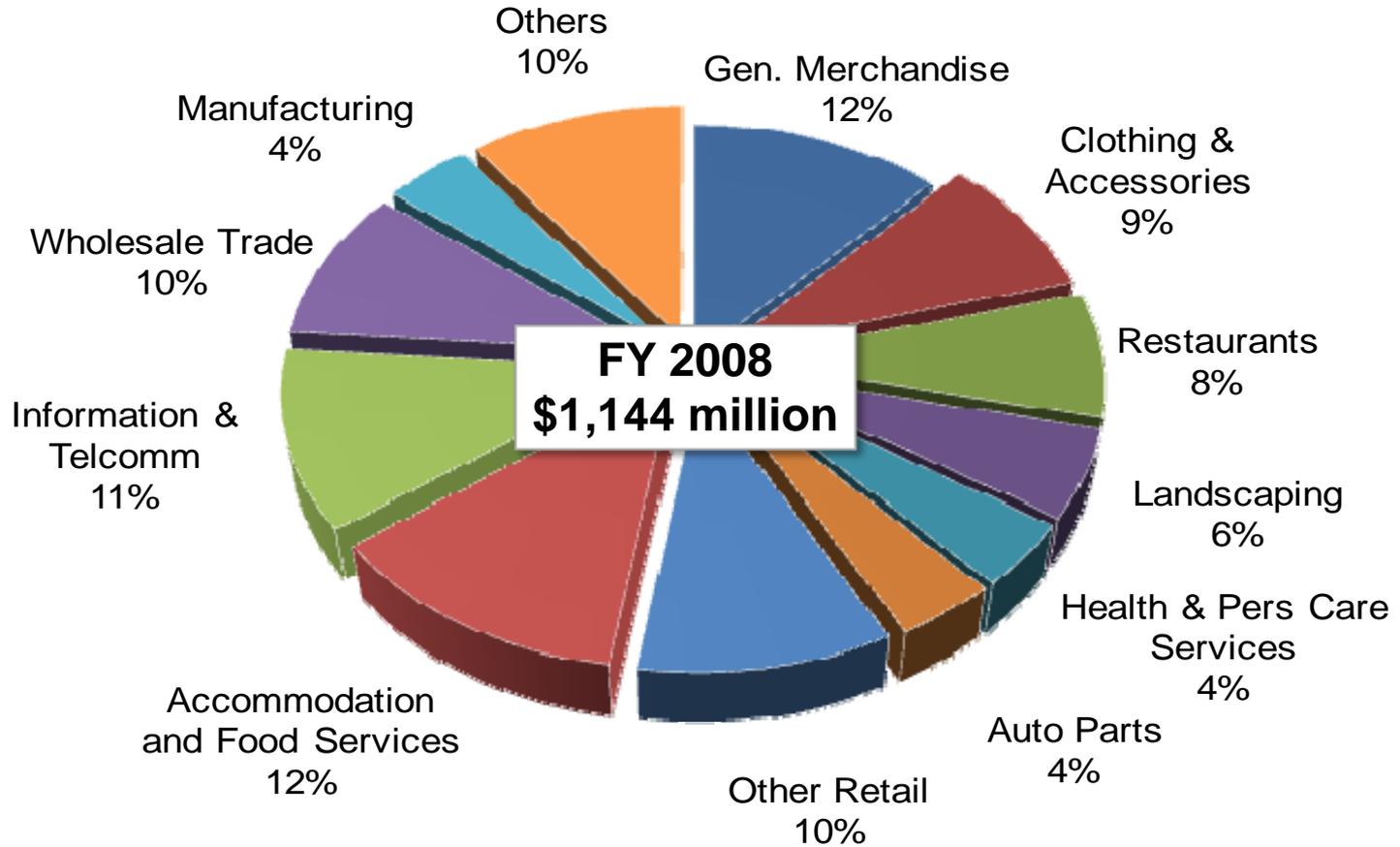
# The sales tax is Puerto Rico's single strongest tax pledge

| <b>Fundamental Factors</b>                              | <b>Description</b>  |
|---|---|
| <b>Broad-based and Stability</b>                        | <ul style="list-style-type: none"><li>• Broad based tax</li><li>• Demographics provide stability</li><li>• Excludes volatile items such as vehicle sales and others</li></ul>                           |
| <b>Strong Consumer and Resiliency</b>                   | <ul style="list-style-type: none"><li>• Large and resilient consumer sector</li><li>• Retail is strong in Puerto Rico</li><li>• Trend of resiliency in Sales Tax</li></ul>                              |
| <b>Up-side Revenue Opportunity with Tax Enforcement</b> | <ul style="list-style-type: none"><li>• Sales tax capture rate remains low</li><li>• Enforcement efforts will improve the capture rate and substantially increase annually recurring revenues</li></ul> |



# The Sales Tax is stable

## Broad-based sales tax that includes services

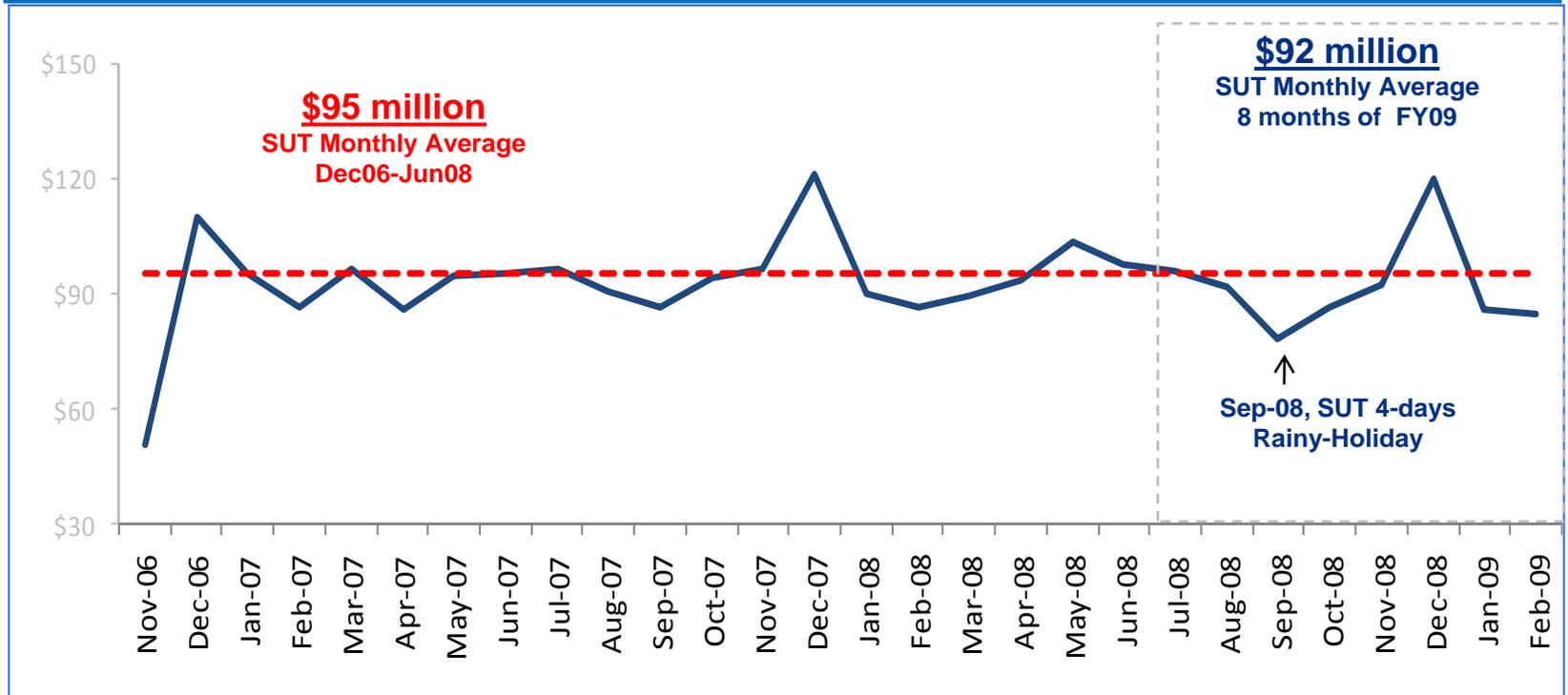




# The Sales Tax is Resilient

The Sales Tax collections remain in line with historical monthly average collections

## SUT monthly trend remains steady in spite of the recession



Source: P.R. Dept. of the Treasury

\* Gross revenues without excluding the assignment to COFINA.



# COFINA has a stronger coverage than comparable programs

| Program   | Coverage    | Rating        | ABT*        |
|---|-------------|---------------|-------------|
| Massachusetts Bay TA Sales Tax Bonds                            | 2.0x        | Aa2 / AAA     | No ABT      |
| Massachusetts School Building Aut. Bonds                        | 2.0x        | Aa2 / AA / AA | 1.4x        |
| California Economic Recovery Bonds                              | 1.1x        | A1 / A+ / A+  | 1.5x        |
| Nassau County Interim Finance Authority Sales Tax Secured Bonds | 4.5x        | Aa2 / AAA     | 3.0x        |
| <b>COFINA I</b>   | <b>5.5x</b> | <b>A+</b>     | <b>3.0x</b> |

\* ABT = Additional Bond Test



# Commonwealth Committed to Protecting Existing COFINA Bondholders

- No parity bonds except:
  - Refunding bonds, provided the refunding must produce annual savings
  - Refinance extra-constitutional debt, provided that debt service cannot exceed the Original Base Amount\*
- New, subordinate lien will be created to finance the fiscal stabilization measures
- Current COFINA bonds will have access to all of the increased dedicated sales taxes flowing to COFINA (\$550 million, up from \$200 million)
- Sales tax revenues in any year are pledged first to current COFINA bonds

Original Base Amount was \$185 million in 2007, escalated by 4% thereafter.



# Concluding Remarks



# Concluding Remarks

- 1** We have responded with swift action through the Reconstruction Plan to address the economic and fiscal challenges.
- 2** We are already implementing the Reconstruction Plan and are committed to providing Progress Reports on the implementation process.
- 3** COFINA II is the financial “anchor” of the Fiscal Reconstruction Plan. We are proposing an initial financing of \$3.0-\$4.0 billion for the month of May 2009.
- 4** The Sales Tax is Puerto Rico’s single strongest tax pledge due to broad-base and stability, consumer and tax resiliency and the opportunity to improve tax revenues through enforcement.
- 5** We are committed to protecting the existing COFINA bondholders.



# Investor Relations – Information

## Main Websites for Investor Information

|  |  |                |
|--|--|----------------|
| <b>Government<br/>Development<br/>Bank</b> | <a href="http://www.gdbpr.com">www.gdbpr.com</a> | <b>English</b> |
|  | <a href="http://www.bgfpr.com">www.bgfpr.com</a> | <b>Spanish</b> |

## Other Related Websites

|  |  |   |
|--|--|---|
| <b>Treasury<br/>Department</b>                   | <a href="http://www.hacienda.gobierno.pr">www.hacienda.gobierno.pr</a> | <b>Spanish</b><br>(some English information at<br>bottom right of the site) |
| <b>Office of<br/>Management<br/>&amp; Budget</b> | <a href="http://www.ogp.gobierno.pr">www.ogp.gobierno.pr</a>           | <b>Spanish</b>  |
| <b>Planning<br/>Board</b>                        | <a href="http://www.jp.gobierno.pr">www.jp.gobierno.pr</a>             | <b>Spanish</b>  |
| <b>Governor's<br/>Office</b>                     | <a href="http://www.buengobiernopr.com">www.buengobiernopr.com</a>     | <b>Spanish</b>  |



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