COMMONWEALTH OF PUERTO RICO
Government Development Bank for Puerto Rico

COMMONWEALTH OF PUERTO RICO
Puerto Rico Fiscal Agency and Financial Advisory Authority

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Government Development Bank for Puerto Rico and Puerto Rico Fiscal Agency and Financial Advisory Authority Joint Statement on Proposal Released by Bonistas Del Patio

San Juan, P.R. – The Government Development Bank for Puerto Rico (GDB) and the Puerto Rico Fiscal Agency and Financial Advisory Authority (FAFAA) jointly released the following statement on the debt restructuring proposal issued yesterday by Bonistas Del Patio, Inc.:

"The Commonwealth appreciates the proposal made by the advisors to Bonistas Del Patio and their goal of protecting local holders of the Commonwealth's debt. Bonistas Del Patio (Bonistas) is a group that recently formed and is currently believed to represent holders of approximately 1 to 2 percent of the total debt the Commonwealth has targeted for a restructuring. Like the advisors to Bonistas, the Commonwealth has always recognized the burdens that a restructuring of the island's debt would place on local holders, and every one of the Commonwealth's restructuring proposals has offered consideration to local holders well above the prices at which the bonds trade in the market today. At the same time, the Commonwealth has been conscious of the fact that a restructuring that overburdens the island with debt service will have disastrous consequences for all of its residents, not just the creditors that Bonistas represents. While the Bonistas proposal is well-intentioned and the Commonwealth welcomes the opportunity to engage in a constructive dialogue with the group and its advisors, the specific proposal offered on June 27 cannot be accepted by the Commonwealth, as it is not only based on clear calculation errors and unfounded assumptions, but, more importantly, would ultimately harm the people of Puerto Rico in favor of creditors, the vast majority of which are non-residents.

"The calculation error contained in the Bonistas proposal undermines their central claim that 'the Puerto Rico Fiscal Crisis is [only] one of liquidity [necessary] to meet principal maturities.' In arriving at this claim, Bonistas calculates that the five-year deficit facing the Commonwealth, excluding principal payments, is only $2.8 billion. This calculation, however, very obviously counts the benefits of one of the fiscal measures identified by the Commonwealth twice. As publicly explained by the Working Group for the Fiscal and Economic Recovery of Puerto Rico (the Working Group), one of the measures identified and included in its financing deficit estimates is the extension of Act 154. [1] On page 12 of its proposal, Bonistas begins with the Working Group's estimate of the financing deficit *after measures* and then proceeds to add the benefits of extending Act 154, effectively double-counting the possible benefits from the extension of Act 154. Once this error is corrected, the deficit Bonistas projects before the payment of any principal *nearly doubles* to $5.5 billion.

"The Bonistas proposal makes no attempt to explain how it would solve this $5.5 billion shortfall or even how to solve the incorrectly calculated $2.8 billion shortfall. Instead, Bonistas implies that the Commonwealth has made no attempt at expense reductions by stating that the Bonistas holders will agree to principal haircuts 'if and only if [the] Government is willing to restructure all expenses, not only debt service.' This demand ignores the very real expense cuts that are already included in the Fiscal and Economic Growth Plan (the FEGP) developed by the Working Group—which are, in fact, the very same projections Bonistas relies upon in developing its proposal. For example, the FEGP expense reduction measures, which total approximately $14 billion over ten years, include consolidation of schools (measure 2.6), an extended freeze on all government salaries (measure 2.4), annual attrition targets for government employees (measure 2.4) and large cuts in subsidies to the university system and the municipalities (measure 2.5). In addition, the FEGP's projected level of spending includes direct payments to local businesses that are owed money from the Commonwealth, continued funding of the healthcare system and vital capital expenditures to restore the Commonwealth's decaying infrastructure and return the island to growth. Bonistas makes no attempt to identify where the incremental $5.5 billion of cuts its proposal requires would come from. It is left to the imagination of the reader whether Bonistas would prefer that more schools be closed, more teachers be laid off, more civil servant salaries cut, healthcare spending be reduced, more local businesses go unpaid, or that the island's infrastructure be allowed to further deteriorate.

"The most unfortunate part of the proposal's call for incremental cuts in government spending is that the savings would be used to pay creditors, 78 percent of which, according to Bonistas, live *outside* of Puerto Rico. The Bonistas proposal assumes participation from *all* creditors, not just those who reside in Puerto Rico. So while Bonistas claims it is working to protect the people of Puerto Rico, in reality it is demanding greater sacrifices from those who depend on the Commonwealth government for essential services, in order to benefit predominantly non-local creditors.

"This is made even worse by the fact that Bonistas does not even attempt to show that, in exchange for these spending cuts, the people of Puerto Rico would be left with a debt service burden they could actually afford. The Bonistas proposal only shows its projections through fiscal year 2020 — that is to say, only through the period when solely interest would be due and Puerto Rico would have a so-called "principal holiday." Even though the Working Group provided ten-year projections, Bonistas makes no attempt to show how the Commonwealth would afford the large principal payments that would come due under the Bonistas proposal starting in fiscal year 2021. The likely reason for this is that the only way the projected revenues would be sufficient to support the debt burden that Bonistas proposes is by making incredibly optimistic assumptions about economic growth. For the debt service under the Bonistas proposal to be paid, not only would the U.S. Government have to replace over $2 billion per year of Affordable Care Act funding, but the Commonwealth economy would have to grow at a long-term rate roughly in line with the projected growth rate of the United States, or 4.5 percent nominal growth per year.[2] In developing its restructuring proposals, the Working Group

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1 Page 32 of Puerto Rico's FEGP published on September 9, 2015 clearly explains that one of the "measures" included in its estimate of financing deficits is the extension of Act 154 (see also page 30 of the FEGP Update Presentation published January 18, 2016 showing the same measure).

2 Over the five-year projection period shown by Bonistas, the "Estimates After Measures" that serves as the starting point for Bonistas' analysis incorporates the estimated benefits of growth in the case where the long-term growth rates approximate that estimated for the U.S. This is clearly explained in multiple Commonwealth publications (see, for example, the sources contained in footnote 3 below). If Bonistas were not to continue this assumption past 2020, it would require even greater spending cuts than discussed herein, none of which are identified by Bonistas.

publicly stated that such an assumption 'is optimistic given the Commonwealth's real GNP growth has been below that of the United States since 2001.'[3] Further, all of the economists with whom the Commonwealth has consulted in developing its plan agree that it would be unwise to formulate a restructuring proposal that requires this growth rate to be achieved. As a result, all of the restructuring proposals released publicly by the Working Group have assumed moderate nominal growth in the economy of 2 percent per year, but did not burden the Commonwealth with debt service that could only be paid in the most optimistic of scenarios.[4] It is exactly this type of financial sophistry—which paints a picture of an easy debt restructuring built on unrealistic spending cuts and optimistic economic growth assumptions—that led Puerto Rico to the fiscal and economic crisis it faces today.

"The Bonistas proposal provides that all of the bondholders, most of which do not live in Puerto Rico, receive even greater recoveries on the backs of the people of Puerto Rico who would suffer greater cuts in services than already proposed by the Commonwealth. It further positions Puerto Rico for a second restructuring given that debt service could only be sustained under the most optimistic growth assumptions. The Commonwealth would be happy to engage with Bonistas, as it has with all its bondholders, but only if the goal is a restructuring that will actually be beneficial to all of Puerto Rico's residents, rather than a proposal that just claims to be."

3 See page 6 of the FEGP Update Presentation published January 18, 2016.
4 See page 19 of the Puerto Rico Restructuring Proposal published February 1, 2016.

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The information included in this statement contains certain forward-looking statements. These forward looking statements may relate to the fiscal and economic condition, economic performance, plans and objectives of the Commonwealth of Puerto Rico or its agencies or instrumentalities. All statements contained herein that are not clearly historical in nature are forward looking.

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