STANDARD & POOR'S
RATINGS SERVICES
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Summary:

Puerto Rico Electric Power Authority; Retail Electric

Primary Credit Analyst:
Jeffrey M Panger, New York (1) 212-438-2076; jeff.panger@standardandpoors.com

Secondary Contact:
Peter V Murphy, New York (1) 212-438-2065; peter.murphy@standardandpoors.com

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Summary:

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Credit Profile		
Puerto Rico Elec Pwr Auth pwr (AGM) (SEC MKT)		
Unenhanced Rating	CCC-(SPUR)/Watch Neg	Downgraded
Puerto Rico Elec Pwr Auth pwr (ASSURED GTY) (SEC MKT)		
Unenhanced Rating	CCC-(SPUR)/Watch Neg	Downgraded
Puerto Rico Elec Pwr Auth		
Long Term Rating	CCC-/Watch Neg	Downgraded
Puerto Rico Elec Pwr Auth retail elec		
Unenhanced Rating	CCC-(SPUR)/Watch Neg	Downgraded

Rationale

Standard & Poor's Ratings Services has lowered its rating on Puerto Rico Electric Power Authority's (PREPA) power revenue bonds to 'CCC-' from 'CCC'. The rating remains on CreditWatch with negative implications.

The downgrade reflects our view of the following:

- Repeated draws on the debt service reserve fund and uncertainty regarding any future draws that could result in its depletion;
- A structural imbalance between revenues and expenses without a pathway to meeting debt service obligations if and when the debt service reserve is depleted;
- Our concern about the authority's access to capital markets; and
- The uncertainty whether money on deposit with the Government Development Bank (GDB) could be diverted from PREPA.

As a result, we believe a default, distressed exchange, or redemption appears to be inevitable within six months, absent unexpected significantly favorable changes in the authority's circumstances.

On April 1, 2015, PREPA used $8.8 million from its debt service reserve to help make a quarterly bond payment, the third such draw. In July and October 2014, the authority withdrew $41.6 million and $8.8 million, respectively, from the reserve. In our opinion, the draws suggest that despite falling oil prices, the authority has a continuing structural imbalance between revenues and expenses. We also believe Puerto Rico has very limited access to either the public or private debt markets. PREPA's next scheduled debt service payment totals $400 million and is due July 1.

Legislation enacted in 2014 requires PREPA to deposit with the GDB certain non-operating funds, including construction funds and the debt service reserve, which currently has $236 million on deposit. It is unclear whether the government could divert this money.

PREPA's inability to successfully negotiate renewal of liquidity facilities needed to purchase oil has compounded its weakened financial position. The negotiating deadline for the revolving credit facilities has been extended several times and is set to expire April 30. The extensions are part of an agreement with insurers and bondholders controlling more than 60% of the authority's bonds to amend the existing bond documents to provide it with liquidity and time to work with its creditors to develop a restructuring plan.

In accordance with the agreement, PREPA hired a chief restructuring officer to assist it develop a restructuring plan proposal acceptable to at least two-thirds of forbearing bondholders.

Liquidity is the immediate risk. The forbearance agreement requires the authority to provide an initial 13-week cash flow forecast with monthly updates. It also allows PREPA to use cash in the construction fund to provide some additional interim liquidity. The bank lines used to purchase oil are almost fully drawn but are paid down as revenue associated with fuel costs comes in, and then redrawn to purchase additional oil.

Although missing credit facility payments is not a default under the revenue bond indenture, we believe the authority's inability to repay the amounts outstanding will increase the likelihood that it will restructure its debt. We will lower the rating if PREPA restructures its debt by extending maturity dates to reduce annual debt service payments, which we would view as a default under our criteria.

CreditWatch

We expect to resolve the CreditWatch placement in the next three months after we have evaluated PREPA's plans and the actions it will take to resolve the imbalance between revenues, expenses, and debt service. We will lower the rating if the authority restructures the debt by extending maturity dates.

Related Criteria And Research

Related Criteria

- USPF Criteria: Electric And Gas Utility Ratings, Dec. 16, 2014
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011
- Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings, Oct. 1, 2012

Related Research

- U.S. State And Local Government Credit Conditions Forecast, April 2, 2015

Ratings Detail (As Of April 24, 2015)		
Puerto Rico Elec Pwr Auth pwr (MBIA) (SEC MKT) (National)		
Unenhanced Rating	CCC-(SPUR)/Watch Neg	Downgraded
Puerto Rico Elec Pwr Auth retail elec		

Ratings Detail (As Of April 24, 2015) (cont.)		
Unenhanced Rating	CCC-(SPUR)/Watch Neg	Downgraded
Many issues are enhanced by bond insurance.		

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