STANDARD & POOR'S RATINGS SERVICES
McGRAW HILL FINANCIAL

RatingsDirect®

Puerto Rico Electric Power Authority Revenue Bonds Downgraded To 'CCC' On Nonpayment Concerns, Remains On Watch Negative

Primary Credit Analyst:
Judith G Waite, New York (1) 212-438-7677; judith.waite@standardandpoors.com

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

NEW YORK (Standard & Poor's) July 31, 2014--Standard & Poor's Ratings Services has lowered its rating on Puerto Rico Electric Power Authority's (PREPA) power revenue bonds two notches to 'CCC' from 'B-'. The rating remains on CreditWatch with negative implications, where we originally placed it June 18, 2014.

PREPA has $8.3 billion of power revenue bonds outstanding. A pledge of the electric system's net revenues secures the bonds.

The lower rating indicates that, in our opinion, the authority's debt is vulnerable to nonpayment, and depends upon favorable business, financial, and economic conditions for the obligor to meet its commitment. In the event of adverse business, financial, or economic conditions, PREPA is not likely to have the capacity to meet its financial commitment on its obligations.

"We believe that the absence of an overarching solution to liquidity issues and the structural imbalance among its revenues, operating expenses and debt service commitments suggests an increasing likelihood that the authority will not be able to satisfy debt service obligations on time and will avail itself of the Puerto Rico Public Corporation Debt Enforcement and Recovery Act, signed into law June 28, 2014, and restructure all or portions of its debt," said Standard & Poor's credit analyst Judith Waite.

The law "allows public corporations, among other things, to adjust their debts

1350600 | 302008878

in the interest of all creditors affected thereby; provides procedures for the orderly enforcement and, if necessary, the restructuring of debt in a manner consistent with the Commonwealth Constitution and the U.S. Constitution; and maximizes returns to all stakeholders by providing them going concern value based on each obligor's capacity to pay."

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 that matured in January was extended to July 31, and if the facility is not renewed, the authority will have to repay the $146 million outstanding, and probably relatively quickly. PREPA also has $525 million outstanding under a second revolving credit facility matures Aug. 14, 2014. If not renewed, the authority will have to repay the $525 million outstanding on that date. Normally, it repays the lines with revenue associated with fuel costs recovered from customers. However, PREPA does not have surplus liquidity to repay the amounts.

Although not making 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.

The CreditWatch placement reflects an ongoing structural imbalance among revenues, operating expenses and debt service commitments, compounded by liquidity pressures. We could lower the rating further if these mismatches remain unresolved and the likelihood of meeting debt service obligations erodes. We expect to resolve the CreditWatch placement within the next three months.

RELATED CRITERIA AND RESEARCH

Related Criteria
- USPF Criteria: Electric Utility Ratings, June 15, 2007
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011

Related Research
- U.S. State And Local Government Credit Conditions Forecast, July 8, 2014
- Puerto Rico analysis, July 31, 2014

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.