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.

<table>
<thead>
<tr>
<th>Factors</th>
<th>Description</th>
</tr>
</thead>
</table>
| Economic Relation with the U.S. | • P.R. is a Top 20 trading partner of the U.S.  
• Resilient consumer sector  
• 41% of GDP is manufacturing / Top 5 pharmaceutical cluster in U.S. |
| Favorable Demographics        | • Population ~4.0 million.  
• Population ranks higher than 25 states; comparable to Oregon  
• Slightly younger: median age is 32 years versus 35 years in U.S. |
| U.S. Regulatory System        | • U.S. Constitutional and Legal Protection  
• U.S. Banking and Financial Regulatory System  
• U.S. Federal Court Presence and Intellectual Property Protection |

Source: PR Planning Board, U.S. Census and Bureau of Economic Analysis.
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

Financial Advisor
- Treasury and ALM*
- Asset Management
- Investment Strategies

Strategic Planner
- Macro & Regional Analysis
- Economic Modeling
- Statistical Reliability

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

Invested Assets $4,819
Loans 6,757
Other Assets 920
Total Assets $12,496

Deposits $5,972
Bonds and Notes 3,311
Other Liabilities 791
Total Liabilities $10,074

Net Assets $2,422
Net Assets/Total Assets 19.4%

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

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

General Fund since FY 2000
(recurring revenues and expenses)

$ millions

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:
     - 2005: 1.9%
     - 2006: 0.5%
     - 2007: -1.9%
     - 2008: -2.5%
     - 2009 E*: -3.4%

2. Fiscal Emergency
   - General Fund Data (Million)
     - Estimated Revenues FY 2009: $7,600
     - Budget Deficit: $3,241
     - Estimated Expenses FY 2009: $10,841

   - Deficit

We have responded with swift action

<table>
<thead>
<tr>
<th>Fiscal and Economic Challenges:</th>
<th>We have taken action:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Economy in recession</td>
<td>• Developed a</td>
</tr>
<tr>
<td>• Need of stimulus and</td>
<td>Reconstruction Plan</td>
</tr>
<tr>
<td>investment</td>
<td>for the next 4</td>
</tr>
<tr>
<td>• Fiscal deficit of $3.2 bn</td>
<td>years</td>
</tr>
<tr>
<td>• Multi-Year Budget Plan</td>
<td>• Have enacted 7</td>
</tr>
<tr>
<td></td>
<td>bills to</td>
</tr>
<tr>
<td></td>
<td>implement the Plan</td>
</tr>
<tr>
<td></td>
<td>• Enhanced investor</td>
</tr>
<tr>
<td></td>
<td>relations program</td>
</tr>
<tr>
<td></td>
<td>• Strong fiscal agent</td>
</tr>
</tbody>
</table>
1. Introduction and Action taken in the first 100 days

2. The Economic and Fiscal Reconstruction Plan

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

**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

**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.

**Economic Reconstruction**

1. Federal and Local Stimulus Packages
2. Public-Private Partnerships (PPPs)
3. Economic Development Supplemental Stabilization Plan

**Fiscal Reconstruction**

1. Expense reduction and government efficiency
2. Increased oversight and tax collection
3. Revenue Measures
4. Financial Measures

**Gross National Product**
The Fiscal Reconstruction Plan is based on a combination of measures.

Distribution of Fiscal Reconstruction Measures

- **Revenue Measures**: 20% (temporary & permanent)
- **Tax Enforcement**: 10%
- **Expense Measures**: 70%

Total: $3,200 million

Financial Stabilization Measures
## 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.

### Goal: $2,000 million savings

<table>
<thead>
<tr>
<th>Expense Reduction Measures</th>
<th>Public Employees Alternatives Program</th>
</tr>
</thead>
<tbody>
<tr>
<td>PAYROLL EXPENSES</td>
<td>Educational Voucher</td>
</tr>
<tr>
<td>• 30% reduction of non-career personnel</td>
<td>Retraining / Vocational Voucher</td>
</tr>
<tr>
<td>• Salary reduction of agency heads</td>
<td>50% salary subsidy for transition to private or non profit sector job up to $15,000</td>
</tr>
<tr>
<td>• Salaries freeze, ban of new posts and elimination of vacant posts</td>
<td>Self-Employment Voucher</td>
</tr>
<tr>
<td>• PHASE I: Incentivized resignations and work load reduction</td>
<td></td>
</tr>
<tr>
<td>• PHASE II: Transition of employees</td>
<td></td>
</tr>
<tr>
<td>• PHASE III: Temporary freeze in economic conditions</td>
<td></td>
</tr>
</tbody>
</table>

### Educational Voucher
- 50% salary subsidy for transition to private or non profit sector job up to $15,000

### Retraining / Vocational Voucher
- 50% salary subsidy for transition to private or non profit sector job up to $15,000

### Self-Employment Voucher
- 50% salary subsidy for transition to private or non profit sector job up to $15,000
<table>
<thead>
<tr>
<th>Event</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Enactment of Act No. 7 and effective day of Phase III (temporary freeze of economic conditions)</td>
<td>Mar-09-09: Completed</td>
</tr>
<tr>
<td>Creation of Fiscal Restructuring &amp; Stabilization Board (FRSB)</td>
<td>Mar-09-09: Completed</td>
</tr>
<tr>
<td>Release of Circular Letter with details on Expense Reduction Program</td>
<td>Mar-20-09: Completed</td>
</tr>
<tr>
<td>Public Agencies Notify Employees about Phase I (Voluntary)</td>
<td>Mar-27-09: Completed</td>
</tr>
<tr>
<td>Orientation about Transition Alternatives to Public Employees</td>
<td>Weekend Apr-18-09</td>
</tr>
<tr>
<td>Eligible Employees Submit Form for Phase I</td>
<td>Apr-27-09</td>
</tr>
<tr>
<td>Voluntary Resignations Effective</td>
<td></td>
</tr>
<tr>
<td>Notification of first round of Phase II (if necessary)</td>
<td>May-29-09</td>
</tr>
<tr>
<td>Voluntary Workday Reduction becomes Effective</td>
<td>Jun-01-09</td>
</tr>
<tr>
<td>First round of Phase II is effective (if necessary)</td>
<td>Jul-03-09</td>
</tr>
</tbody>
</table>

We are following a strict calendar in implementing the expense measures.
A combination of permanent and temporary tax measures and enforcement initiatives should increase revenues

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

Improvement in tax enforcement and collections is key for the Plan
The Economic Reconstruction Plan consists of significant stimulus and investment measures.

**Phase Ia**
- Federal Stimulus
  - Capital Improvements: $0.8 B (16%)
  - Tax Relief: $1.3 B (27%)
  - Relief for Individuals: $2.2 B (44%)
  - Budget Relief: $0.7 B (13%)
  - Total: $5.0 B

**Phase Ib**
- Local Stimulus
  - Capital Improvements: $0.21 B (42%)
  - Merchants Stimulus: $0.18 B (36%)
  - Gov. Expense: $0.02 B (3%)
  - Consumer Relief: $0.09 B (9%)
  - Total: $0.5 B

**Phase II**
- Supplemental Stabilization
  - Economic Development Investment: $2.0 B

Total: $5.0 B + $0.5 B + $2.0 B = $7.5 BN

12% of GNP

Public-Private Partnerships
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. Raimes, 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
1. Introduction and Action taken in the first 100 days

2. The Economic and Fiscal Reconstruction Plan

3. Financial Stabilization Measures
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

### FISCAL RESPONSIBILITY
- $4.5 Bn
  - Existing debts without an identified source of repayment

### DEFICIT FINANCING
- $0.8 Bn
  - Account payables to suppliers
- $2.3 Bn
  - FY 2009
  - FY 2010

### RECONSTRUCTION PLAN
- $1.5 Bn
  - Expense reduction cost
  - Local stimulus
- $2.0 Bn
  - Economic Supplemental Stabilization
    - (Stimulate private investment)

### Summary
- $9.1 Bn
  - 76%
    - $6.7 Bn
      - COFINA II (1.75% SUT)
  - 24%
    - $2.4 Bn
      - General Fund

Note: This slide describes the proposed financial stabilization measures and is subject to change and revision.
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:**

<table>
<thead>
<tr>
<th>Deal Component</th>
<th>Comments*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Initial Deal Size:</td>
<td>$3.0 - $4.0 billion</td>
</tr>
<tr>
<td>Timing of financing:</td>
<td>May 2009</td>
</tr>
<tr>
<td>Market access:</td>
<td>103 Market &amp; Puerto Rico markets</td>
</tr>
</tbody>
</table>

* Preliminary and subject to market conditions.
Each year, all of the 5.5% Sales Tax will continue to flow first to the COFINA I Bond Trustee until the Base Amount is satisfied.

- **Original (2006) – COFINA I**
  - 1% pledge

- **Act 1 2009 (Jan-15-09)**
  - 1% of additional pledge (COFINA II)

- **Act 7 2009 (Mar-09-09)**
  - 0.75% of additional pledge (COFINA II)

---

* 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

<table>
<thead>
<tr>
<th>Fundamental Factors</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Broad-based and Stability</td>
<td>• Broad based tax</td>
</tr>
<tr>
<td></td>
<td>• Demographics provide stability</td>
</tr>
<tr>
<td></td>
<td>• Excludes volatile items such as vehicle sales and others</td>
</tr>
<tr>
<td>Strong Consumer and Resiliency</td>
<td>• Large and resilient consumer sector</td>
</tr>
<tr>
<td></td>
<td>• Retail is strong in Puerto Rico</td>
</tr>
<tr>
<td></td>
<td>• Trend of resiliency in Sales Tax</td>
</tr>
<tr>
<td>Up-side Revenue Opportunity with Tax Enforcement</td>
<td>• Sales tax capture rate remains low</td>
</tr>
<tr>
<td></td>
<td>• Enforcement efforts will improve the capture rate and substantially increase annually recurring revenues</td>
</tr>
</tbody>
</table>
The Sales Tax is stable
Broad-based sales tax that includes services

Source: PR Treasury Department.
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**

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

* 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
We have responded with swift action through the Reconstruction Plan to address the economic and fiscal challenges.

We are already implementing the Reconstruction Plan and are committed to providing Progress Reports on the implementation process.

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.

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.

We are committed to protecting the existing COFINA bondholders.
# Investor Relations – Information

## Main Websites for Investor Information

<table>
<thead>
<tr>
<th>Government Development Bank</th>
<th><a href="http://www.gdbpr.com">www.gdbpr.com</a></th>
<th>English</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><a href="http://www.bgfpr.com">www.bgfpr.com</a></td>
<td>Spanish</td>
</tr>
</tbody>
</table>

## Other Related Websites

<table>
<thead>
<tr>
<th>Treasury Department</th>
<th><a href="http://www.hacienda.gobierno.pr">www.hacienda.gobierno.pr</a></th>
<th>Spanish</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(some English information at bottom right of the site)</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Office of Management &amp; Budget</th>
<th><a href="http://www.ogp.gobierno.pr">www.ogp.gobierno.pr</a></th>
<th>Spanish</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Planning Board</th>
<th><a href="http://www.jp.gobierno.pr">www.jp.gobierno.pr</a></th>
<th>Spanish</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Governor’s Office</th>
<th><a href="http://www.buengobiernopr.com">www.buengobiernopr.com</a></th>
<th>Spanish</th>
</tr>
</thead>
</table>
The Economic and Fiscal Reconstruction Plan of Puerto Rico

The Municipal Forum of New York

April 16, 2009