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## Research Update:

# Government Development Bank For Puerto Rico Long-Term Rating Lowered Three Notches To 'B-' From 'BB-'; Outlook Negative

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## Research Update:

# Government Development Bank For Puerto Rico Long-Term Rating Lowered Three Notches To 'B-' From 'BB-'; Outlook Negative

## Overview

- We believe the Government Development Bank for Puerto Rico's ability to access the capital markets under reasonable terms has become uncertain as a result of several factors, including a recent lower court decision invalidating its debt restructuring law as well as persistent economic weakness in Puerto Rico.
- We lowered the ratings on the Commonwealth of Puerto Rico's general obligation and appropriation debt to 'B' from 'BB' because of what we view as significantly increased near-term liquidity risks for the Commonwealth. The outlook is negative. (See "Puerto Rico General Obligation Debt Rating Lowered To 'B' From 'BB' On Potential Inability To Meet Debt Commitments," published Feb. 12, 2015.)
- We are lowering our long- and short-term issuer credit ratings on GDB to 'B-/C' from 'BB-/B', given our view of its constrained market access and its substantial exposure to the Commonwealth and its public corporations in the form of loans and investments.
- The outlook on GDB is negative, reflecting the potential that it will be unable to raise sufficient funds to meet debt maturities or other funding needs of the Commonwealth over the next several quarters, as well as its substantial credit exposure to three public corporations.

## Rating Action

On Feb. 12, 2015, Standard & Poor's Ratings Services lowered its long-term issuer credit rating on the Government Development Bank for Puerto Rico (GDB) to 'B-' from 'BB-'. The outlook is negative. We also lowered our short-term issuer credit rating on GDB to 'C' from 'B'. We revised our stand-alone credit profile (SACP) on GDB to 'b' from 'b+'.

## Rationale

The downgrade reflects our view that GDB faces persistent economic weakness in Puerto Rico and increased liquidity risk resulting from a recent decision invalidating its debt restructuring law, which threatens GDB's ability to access capital markets under reasonable terms. Additionally, our downgrade reflects the potential that GDB will suffer material losses given its substantial outstanding loans to three public corporations with weak creditworthiness. The rating action on GDB is in conjunction with our

downgrade of the Commonwealth of Puerto Rico's general obligation debt to 'B' from 'BB'.

We believe that GDB has a limited ability to cover its liquidity needs, which includes nearly \$900 million of notes due in fiscal 2016, over the next 12 months without accessing the debt markets. Currently available funding options are limited and will likely be significantly more expensive than what GDB has been able to obtain in the past. Given this increased near-term liquidity risk, we lowered our liquidity assessment on GDB to "weak" from "adequate," which resulted in lowering our SACP one notch to 'b' from 'b+'.

Additionally, GDB has loans aggregating more than \$2 billion to three public corporations. The Highways and Transportation Authority (HTA) is GDB's largest borrower and has about \$2 billion outstanding as of Sept. 30, 2014. This is quite substantial relative to GDB's equity capital of \$2.3 billion. These exposures also include loans to the Puerto Rico Electric Power Authority (PREPA), which has \$35 million outstanding to GDB, and Puerto Rico Aqueduct and Sewer Authority (PRASA), which has \$99 million outstanding to GDB. Given GDB's heavy lending concentration to the Commonwealth and to Puerto Rico's public entities, whose creditworthiness is weak, we believe there is uncertainty of the degree to which GDB's capital and financial condition could decline.

We consider GDB a government-related entity (GRE) based on our view that the link between GDB and the Commonwealth is very strong and GDB plays a very important role for the government. GDB provides funding to the Commonwealth and other Puerto Rican public corporations and is a fiscal agent to the Commonwealth and its instrumentalities. Because we lowered the rating on the Commonwealth's general obligation debt to 'B', we no longer incorporate one notch of uplift from our SACP to arrive at our issuer credit rating on GDB, based on our GRE criteria. We also believe that GDB is structurally subordinated to the Commonwealth, so we continue to include a one-notch distinction between the ratings on the entities.

## Outlook

The outlook is negative, reflecting the potential that GDB will be unable to raise sufficient capital to meet debt maturities or other funding needs of the Commonwealth over the next several quarters, as well as its substantial lending exposure to three public corporations with weak creditworthiness. We could lower our ratings on GDB if it is unable to raise capital well ahead of upcoming debt maturities or if we expect material losses to occur at its largest borrower, the HTA, to a degree that it would weaken GDB's capital or financial profile. We could also lower our ratings on GDB if we downgrade the Commonwealth's general obligation debt further. In our view, GDB remains vulnerable given its high lending concentration and interconnectedness to the Commonwealth.

Alternatively, we could revise the outlook to stable if GDB is successful in

accessing the capital markets on reasonable terms to raise capital to meet its liquidity needs over the next couple of years.

## Ratings Score Snapshot

	To	From
Issuer Credit Rating	B-/Negative/C	BB-/Negative/B
SACP	b	b+
Anchor	bbb+	bbb+
Business Position	Very Weak (-5)	Very Weak (-5)
Capital and Earnings	Very Strong (+2)	Very Strong (+2)
Risk Position	Weak (-2)	Weak (-2)
Funding and Liquidity	Below average and weak(-2)	Below average and adequate(-1)
Support	0	0
GRE Support	0	+1
Group Support	0	0
Sovereign Support	0	0
Additional Factors	-1	0

## Related Criteria And Research

### Related Criteria

- Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions, Jan. 29, 2015
- Group Rating Methodology, Nov. 19, 2013
- Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework, June 22, 2012
- Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- Bank Capital Methodology And Assumptions, Dec. 6, 2010

### Related Research

- Puerto Rico General Obligation Debt Rating Lowered To 'B' From 'BB' On Potential Inability To Meet Debt Commitments, Feb. 12, 2015
- Puerto Rico Electric Power Authority, Puerto Rico Aqueduct and Sewer Authority Ratings Unaffected By Court Ruling, Feb. 10, 2015

## Ratings List

### Downgraded

	To	From
Government Development Bank for Puerto Rico		
Counterparty Credit Rating	B-/Negative/C	BB-/Negative/B
Senior Unsecured	B-	BB-

### Ratings Affirmed

Government Development Bank for Puerto Rico	
Senior Unsecured	AA-

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