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November 29, 2010

Outlook On Puerto Rico Revised To Positive From Stable On Balanced Budget Progress; GO Rating Affirmed At 'BBB-'

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DALLAS (Standard & Poor's) Nov. 29, 2010--Standard & Poor's Ratings Services has revised its outlook on its general obligation (GO) 'BBB-' rating on the Commonwealth of Puerto Rico to positive from stable. At the same time, we affirmed our 'BBB-' rating on the commonwealth's appropriation debt. The outlook on the commonwealth's appropriation rating remains stable because even if the GO rating is raised in the next two years, the appropriation rating would remain one notch below the GO rating.

"The outlook revision is based on our view of the commonwealth's recent implementation of significant expenditure controls and revenue enhancement measures that we believe could help restore budget balance within the next two years," said Standard & Poor's credit analyst Horacio Aldrete-Sanchez.

The 'BBB-' ratings continue to reflect our opinion of the commonwealth's history of chronic budget deficits. Governor Luis Fortuño's fiscal stabilization plan, which included an unprecedented 17% reduction in payroll expenditures, along with the recently approved tax measures is aimed at eliminating a decade-long trend of budget imbalances. The implementation of these measures has received broad legislative support. While we view the current administration's measures as an important step toward budget stability, we do not anticipate the achievement of a structurally balanced budget until fiscal 2013.

Factors that continue to support the ratings include our opinion of the commonwealth's strong ties to the U.S. economy, resulting in a significant flow of trade and income transfers, with exports to the U.S. accounting for approximately $46.4 billion (76% of GNP) in 2008. According to the U.S. Census Bureau, total income transfers from the U.S. to Puerto Rico totaled $13.5 billion (22% of GNP) in 2008.

The positive outlook is based on our view of the commonwealth's recent implementation of significant expenditure controls and revenue enhancement measures that we believe could help restore budget balance within the next two years. Standard & Poor's could raise the rating if over the upcoming two years in conjunction with an improvement in the commonwealth's economic performance, budget controls remain in place and we believe there is significant progress toward achieving balance between ongoing revenues and expenditures as well as in addressing its unfunded retirement benefit obligations. We could revise the outlook to stable if the effectiveness of the recently approved tax and budget measures is impeded by either continued economic deterioration or a loosening of the expenditure discipline exhibited to date, and the commonwealth fails to make progress toward addressing its unfunded retirement obligations in the next two years.

The outlook on the commonwealth's appropriation rating remains stable because even if the GO rating is raised in the next two years, the appropriation rating would remain one notch below the GO rating.

RELATED CRITERIA AND RESEARCH

- USPF Criteria: GO Debt, Oct. 12, 2006
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007

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