

# RatingsDirect®

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## Summary:

# Guam; Appropriations; General Obligation

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Rationale

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Credit Profile		
<b>Guam GO</b>		
<i>Long Term Rating</i>	BB-/Watch Neg	On CreditWatch Negative
<b>Guam (John F. Kennedy High Sch Proj)</b>		
<i>Long Term Rating</i>	B+/Watch Neg	On CreditWatch Negative
<b>Guam Ed Fincg Foundn, Guam</b>		
Guam		
Guam Ed Fincg Foundn (Guam) APPROP		
<i>Long Term Rating</i>	B+/Watch Neg	On CreditWatch Negative
<b>Phoenix Indl Dev Auth, Arizona</b>		
Guam		
Phoenix Indl Dev Auth (Guam) APPROP		
<i>Long Term Rating</i>	B+/Watch Neg	On CreditWatch Negative

## Rationale

S&P Global Ratings has placed its 'BB-' rating on the Government of Guam's general obligation (GO) debt and its 'B+' rating on the government's various certificates of participation (COPs) on CreditWatch with negative implications.

The CreditWatch placement reflects the government's disclosure that its cash flow will be extremely constrained over the next several months, and perhaps even longer, and also reflects our view that the government's ability to meet its ongoing obligations could be impaired. The CreditWatch placement affects about \$10 million of GO bonds and \$177 million of COPs outstanding.

The fiscal stress is due to an estimated \$67 million decrease in general fund revenue for fiscal 2018 due to the effect of The Tax Cuts and Jobs Act of 2017 (the act), signed into law by President Trump on Dec. 22, 2017. If not for the act, Guam's fiscal team indicates its general fund result was projected to break even for fiscal year-end (Sept. 30) 2018. Due to the act's provisions (Guam's tax code mirrors the federal tax code), Guam's corporate and individual income-tax collections are projected to be \$67 million lower in the current fiscal year. Therefore, the government indicates that it might be difficult to meet payroll in May 2018, and its ability to meet payroll in subsequent months is also uncertain. While the government has reaffirmed its commitment to treating debt service payments as its highest priority, we nevertheless believe that full and timely payment of debt service could be challenging. In distress situations, we have observed some cases where legal provisions in bond documents must be weighed against the other competing municipal obligations, such as maintaining critical services, including public health and safety services, and even public education.

In an effort to shore up the impact, but also to provide Guam Memorial Hospital (GMH) with a permanent, dedicated funding source (rather than rely on annual general fund contributions), Gov. Eddie Calvo introduced Bill 245-34, which proposed to raise Guam's business privilege tax (the island's second-largest general fund revenue source) to 6.0% from its current 4.0% rate. However, in a Feb. 28 legislative session, the bill was defeated by a 10-to-4 vote. Half the funds raised would have been directed to the general fund to cover the deficit, while the balance would have flowed to the Guam Department of Education (DOE) and GMH. The tax increase would have dipped to a 4.75% rate after 24 months, with the remaining tax increase to serve as a dedicated source of funding for GMH. We estimate the rate increase to 6.0% would have generated about \$10 million per month in additional revenues for the remainder of fiscal 2018, or approximately \$120 million per fiscal year. The government is now considering other revenue-raising measures with a similar or even greater impact, including a 2.0% sales tax and 6.0% internet sales tax. No public hearing on the sales tax measures is planned until March 8, so it is likely that no legislative vote is imminent.

On the expenditure side, the government has imposed a hiring freeze except for public safety and public health, and initiated cost-containment measures in utilities, fuel consumption, procurement, training, and travel, among other areas. Gov. Calvo's recent attempt to implement a 32-hour work week effective March 6 was postponed on March 1 after Attorney General Elizabeth Barrett-Anderson indicated the governor is required to follow furlough procedures, including a 90-day notice rule. Separately, the DOE board must approve the furlough plan and has its own 30-day notice rule. Adding to the uncertainty is the indication from the government that there are no internal borrowing resources, and no external borrowing is planned. In addition, the extent to which cost-cutting measures or revenue enhancements solve the government's cash flow issues is hard to predict.

Guam has a history of structural imbalance in its general fund, including recurring deficits, a very large negative general fund balance, and massive long-term liabilities. The negative CreditWatch placement reflects the possibility that these challenges will further diminish the general government's ability to meet its operational responsibilities and address its ongoing obligations, including debt payments. If we don't receive evidence from Guam officials addressing these rating considerations, we will likely lower the ratings.

Guam's financial position continues to be weak, in our view. The government's total general fund balance was negative \$106 million as of audited fiscal 2016 (ended Sept. 30), equal to negative 14% of expenditures, with the unreserved or unassigned portion growing for a third-consecutive year to negative \$215 million. Audited financial statements for fiscal year-end (Sept. 30) 2017 are not yet available.

We expect to resolve the CreditWatch placement following an analysis of management's plan to address the territory's current liquidity challenges as well as its overall financial position.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on the S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.



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