North American Petrochemicals Deal of the Year 2013: Iowa Fertilizer

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Cheap natural gas prices are encouraging a rebirth in industries where the US has not been competitive in decades. Orascom Construction Industries $1.8 billion nitrogen fertiliser plant in Wever, Iowa, is the first new US plant of its type in 20 years. It is the largest direct investment ever in Iowa, taking advantage of being close to both to low-cost fuel and its target market.

The financing was also able to take advantage of a tax-exemption bond allocation on offer to sponsors that develop new projects in areas affected by flooding. By raising all of its debt requirement in the tax-exempt bond market, it also became the largest-ever non-investment grade financing in the municipal market.

The tax-exemption dates back to flooding that hit the Midwest in 2008. The floods inspired the Heartland Disaster Tax Relief Act, which made allocations of Midwestern Disaster Area Revenue bonds available to projects that would not normally be eligible for a tax exemption, as long as they were located in the 30 counties affected.

Henry Hub gas prices peaked at $12.69 per million btu in June 2008, when the floods hit. Since the start of 2009, however, they have only gone beyond $5 once. Orascoms interest in developing a project dated back to 2012, when it became clear that the bond allocations might expire unused.

In September, Orascom bought The Weitz Company, which is based in Iowa, essentially so Weitz could perform the engineering, procurement and construction (EPC) contract for the Wever plant. The acquisition was Orascoms second in the US, after it had bought the mothballed Beaumont methanol plant in Texas in 2011. In 2010, Orascom launched an American depositary receipt progamme in the US.

So, as Orascom prepared to put together the financing, it was able to boast familiarity with both the US petrochemicals and construction markets. Many US investors, meanwhile, would have been exposed to Orascom, a power in African and Asian markets, through its equity.

This additional experience helped Orascom assemble the financing quickly. The sponsors biggest challenge, according to Dalia Khorshid, group corporate treasurer at Orascom Construction Industries, was negotiating an acceptable arms-length EPC contract.

Orascom E&C USA holds the $1.2 billion contract with its sister company, and offers a suite of liquidated damages, a 98% plant capacity guarantee and 5% performance security. The EPC contractor, unlike the project company, benefits from a parental guarantee, though it took care to make its subcontracts, with a group of providers that includes KBR, Tecnimont, Stamicarbon and ThyssenKrupp Uhde, as tight as possible.

Iowa Fertilizer Company LLC

STATUS
Closed 15 May 2013

SIZE
$1.8 billion

DESCRIPTION
2 million tonnes-per-year nitrogen fertiliser plant located in Wever, Iowa

SPONSOR
Orascom Construction Industries

DEBT
$1.185 billion three-tranche tax-exempt bond issue

UNDERWRITERS
Citigroup; Bank of America Merrill Lynch

AGENT BANK
Citi

GAS HEDGE
Merrill Lynch

BOND COUNSEL
Dorsey & Whitney

UNDERWRITERS COUNSEL
Nixon Peabody

SPONSOR LEGAL COUNSEL
Orrick

INDEPENDENT ENGINEER
Nexant

MARKET CONSULTANT
Integer

EPC CONTRACTOR
Orascom E&C USA

EQUIPMENT SUPPLIERS
KBR, Tecnimont, Stamicarbon and ThyssenKrupp Uhde

Up until the launch of the bonds, Orascom always had the option of using a financing from its relationship bank lenders. But it found explaining the plants economics to bond buyers relatively straightforward. The US is a net importer of fertiliser, and prices reflect both fuel costs and transport costs. Unless the transport element disappears altogether, notes Khorshid the Wever plant will enjoy a consistent advantage even over producers with cheaper feedstock.

The financing benefits from a seven-year hedge of 50% of gas costs with Merrill Lynch, a hedge that was as much about increasing sponsor comfort as lender comfort. Additional enhancements include a six-month cash-funded debt service reserve account, a major maintenance reserve and a $96.7 million contingency.

The bond issue, for which Citigroup was senior manager and Bank of America Merrill Lynch co-manager, attracted ratings of BB-/BB- (S&P/Fitch), and orders of $3.5 billion. The issue broke down into $390 million of 5% 6.5-year bonds yielding 4.8%, $366 million 5.5% 9.5-year bonds yielding 5.1%, and $429 million of 5.25% 12.5-year bonds yielding 5.3%.

The weighted average interest rate on the debt was 5.25%, an extremely attractive rate for any fertiliser producer, let alone one making its debut in the US.