THE BOND BUYER

Payment pressures drive bond exchange offer for Iowa fertilizer project

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CHICAGO – The Iowa Fertilizer Co. LLC is seeking a tender exchange for up to $435 million of bonds from two maturities in its nearly $1.2 billion 2013 issue that funded construction of its nitrogen fertilizer production plant.

The exchange would ease near-term payment pressures.

The company had always planned to extend repayment on some of its junk-rated private activity debt -- sold with a tax-exemption under the federal government's Midwestern Disaster Area designation – after the project was up and running. It accelerated its plans to late last year due to the threat tax reform posed to future private activity borrowing.

The final version struck by the House and Senate preserved PABs but with the exchange plans well underway the company decided to move forward. Officials did decide to push off the solicitation deadline from late December into the New Year.

"The tax reform bill enacted by Congress and signed by President Trump does not impact private activity bonds, unlike an earlier version. As a result, the company has extended the deadlines for responses to the consent and exchange solicitations to 5:00 p.m., January 5, 2018," said a notice filed on the Municipal Securities Rulemaking Board's EMMA website.

The company is seeking approval for both an exchange solicitation and a consent solicitation with the latter permitting the first. Citi is the dealer.

The company wants to exchange up to $190 million of 2019 bonds and $246 million of 2022 bonds "for an equivalent principal amount of the corresponding Series 2017 bonds," reads the exchange notice.

The bonds currently are valued above their original face value, so a cash payment is being offered as part of the exchange equal to 3.77% and 2.12% on the respective 2019 and 2022 bond tendered. The new 2017 bonds mature in 2050 with a choice “of a final mandatory tender on December 1, 2033” on the new A series or “a final mandatory tender on December 1, 2037” on the B series.

The consent solicitation alters some bond terms allowing for the new borrowing to fund the exchange, allowing for changes in the construction contract, altering various credit and collateral agreements, and giving the company more flexibility in how it funds some reserves.

Holders of a majority of the outstanding principal amount of the existing 2013 bonds and a subsequent 2016 issue must consent. The company completed a $150 million bond exchange in 2016 on a portion of the 2019 maturity that eased fiscal strains on the project which has struggled with financing and construction obstacles.

“The 2016 bond exchange and project completion relieve very near-term financial concerns while extending the ultimate revenue bonds' maturity to 2027,” Fitch Ratings wrote in its last report in May, when it affirmed its B-minus rating. “Fitch's analysis suggests that IFCo's ability to meet ongoing mandatory debt payments is vulnerable to deterioration of operating margins.”

The original 2013 bonds sold in three terms – the 2019 bond totaled $390 million, the 2022 bond totaled $366 million, and the 2025 totaled $429 million, with yields between 4.8% and 5.3%. Citi and Bank of America Merrill Lynch were underwriters and Dorsey & Whitney LLP was bond counsel.

The short maturities were aimed at luring investors with plans to eventually extend maturities after construction was completed and production had begun, at which point the finished project would be in a better position to persuade investors to take the risk of a longer-term investment, said one market participant familiar with the project.

In addition to the bonding, the owners have contributed $1.4 billion to the more than $3 billion project, according to the notices. The project also received $100 million in state and $30 million in local subsidies.

The project launched production in the spring of 2017 after a series of construction struggles. The Internal Revenue Service also closed an examination of the nearly $1.2 billion interim and nearly $1.2 billion permanent financing without a change in their tax-exempt status.

Officials touted the project as one of the largest private sector construction projects in Iowa’s history and the first world-scale, greenfield nitrogen fertilizer facility built in the country in more than 25 years, saying it was worth the tax breaks because it creates thousands of jobs. Critics countered the money could have been better invested elsewhere.

The interim financing was sold in 2012 through the Iowa Finance Authority for the project that was developed by Orascom Construction Industries, which was originally based in Egypt and is now based in the Netherlands. The permanent financing sold in 2013.

The deal was one of the largest ever junk-rated private activity bond issues. It sold under the state's share of $14.6 billion of private-activity borrowing authorized by Congress for qualified projects in designated counties hit hard by storms in the spring of 2008.

The bonds are secured by a first priority security interest in all tangible and intangible assets of the project and a pledge by Iowa Holding LLC of its membership interests in the Iowa Fertilizer Co.

The bonds were originally rated BB-minus by Fitch and S&P Global Ratings but have since been downgraded. S&P affirmed its B rating in May, while shifting its outlook to stable from positive. Fitch in May removed the credit from negative watch but assigned a negative outlook.

The removal from watch reflected “the fact that the project has alleviated short-term liquidity concerns, has reached completion and is in position to start generating operating cash flow, while also benefiting from continued shareholder undertakings to meet upcoming debt payment obligations,” Fitch said.

“The negative outlook reflects the potential for further negative rating action due to early operational performance below expectations or weakening in product prices,” Fitch added.

S&P revised its outlook based on its “expectation that U.S. nitrogen fertilizer prices in the near term will remain at similar levels to those in 2016, which will affect the project's cash flows.”

“Our outlook also reflects our view that IFCo would be able to achieve provisional acceptance, satisfy the lenders' reliability test, and ramp-up in line with our expectation,” S&P added.

The market is volatile for the nitrogen products which are sold to farmers, distributors, wholesalers, cooperatives, and blenders. Nitrogen fertilizer pricing is tied to the price of feedstock, which may be oil, coal, or natural gas depending on the region and producer. Substantial declines in oil and natural gas prices have sharply driven down nitrogen prices.