November 2012

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NOTHING TO FEAR: Through credit enhanced bond financing, John May has given risky projects access to capital.

PHOTO: WHITNEY CURTIS

Meet the Biobanker

How John May and bond-based financing are commercializing bioenergy.

BY LUKE GEIVER

The unemployment rate in the rural region surrounding Lake Providence, La., hovers around 18 percent. Thanks to Massachusetts-based Myriant Corp., the term biobased succinic acid will soon be synonymous in the struggling region, however, with the term employed. By the time Myriant begins operations at its 30 MMgy biobased chemical plant, 250 people in the area will have been employed to build the plant, and for everyday operations, another 50 will call the Lake Providence facility their full-time employer.

Although the creation of 50 jobs may not impress someone outside the region, for the biobased chemical industry, the story of Myriant's Lake Providence facility is significant. The story reveals what the future of biobased project finance looks like, why a town with a population under 4,000 is the new capital (unofficially) of the biobased chemical industry, and, why every new or future hire at Myriant's facility, or any other biobased facility that may soon begin operations, should thank a particular investment banker from St. Louis.

The Right Idea, the Right Time

John May calls St. Louis home, but his job requires a grueling travel schedule that takes him to places in South America, southern Florida and in the case of Myriant, Lake Providence. As the managing director at investment banking firm Stern Brothers and Co., May knows well what it takes for a company to secure funding to build a bioenergy plant. His client list includes nearly all of the advanced biofuel production companies who've applied for and secured commitments for guaranteed loans from USDA for commercial plant build-out in the last two years, including: ZeaChem Inc., Chemtex International, Ineos Bioenergy, Fulcrum Bioenergy, Enerkem Inc., Fiberight LLC and others. According to May, to May, his success at Stern Brothers wouldn't have happened if his team hadn't decided to test a new financing strategy in 2002.

PHOTO: MYRIANT CORP.

THE CAPITAL: Myriant's Lake Providence facility is a job creator that exemplifies how commercial construction projects can be paid for.

"Stern Brothers took a risk of its own in trying to create a demand in the bond market for bioenergy project finance among different types of funds," he says, including mutual, insurance and hedge funds. The result of May's attempts to create a demand for project debt in the bond market has proven, he says, that Stern Brothers was at the right place at the right time with the right idea.

May's idea on bond-based financing was first created in 2002 but is also the same financial model used today by nearly all of his clients in bioenergy, including Myriant, and as May explains, there's one huge reason why: risk. The five major banks in the U.S. currently hold nearly 60 percent of all total bank assets in the U.S., meaning that if large-scale projects over $25 million, receive traditional debt financing, one of the big five will be the source. But, banks haven't been willing or able to lend signficant sums of debt for the past 10 years, especially for projects that come with inherit risks like commercially unproven tech-

PHOTO: MYRIANT CORP.

ALL LINED UP: Over 250 construction jobs will be created during build out. The plant will come online in early 2013.

nology, feedstock input uncertainty or a lack of end-user contracted agreements.

"The bank market of the U.S., and really around the world," May says, "is such that commercial banks aren't capable of handling a large, sophisticated transaction (like the Myriant project), because they simply do not have the risk appetite."

In the past, if U.S. banks were unwilling to provide project debt to bioenergy companies, developers could turn to European banks such as WestLB of New York. But, that office has closed and sold its renewable energy practice due to the exposure it faced in the European financial crisis. And, when May says U.S. banks don't have the risk appetite, it's because those banks simply can't take on projects with the risk profiles that many bioenergy project finance transactions represent. Upcoming Basel III new capital and liquidity standards, from the globally recognized banking standards committee that most globally recognized banks adhere too, could soon force large banks to adopt a strategy that some are already using: holding more cash or liquidity on hand, while avoiding (due to regulations that limit the ability of banks to invest in risk intensive deals) loans that are too risky and could result in a significant loss to a bank if a loan recipient defaulted.

And unless a company is willing to give up a significant portion of its collateral to strategic partners, venture capitalists or private equity providers through financing rounds, equity financing in exchange for company control is not an option.

Because May and his team knew that the bond market was not, and would not be under the same regulations of major banks or require a company to option off portions of its company, he went to the bond market.

Bioenergy firms however, haven't succeeded solely on bonds issued to mutual or hedge funds, in part, because May and his team realized something else: that investors looking at projects with higher risk profiles would need some element of certainty that their investment would pay off. To appease investors, May developed a project finance strategy that involves credit-enhancing tools similar to a USDA loan guarantee which pushes a poorly rated bond up by assuring through the guarantee that a bond will be paid out if the loan recipient defaults, with a complex bond-placement structure that brings bond investors looking for small returns in the 4.5 to 6 percent range together with investors that are actually looking for riskier investments that could potentially return 14 to 17 percent.

GOT A REGIMEN: Stephen Gatto, CEO of Myriant, will deploy the same financial regimen on future projects.

Myriant, like nearly all of May's previous clients, is a prime example of what the bond-based, credit-enhanced, structurally complex project finance model of today, and tomorrow, looks like. The Lake Providence facility is the first-ever biobased chemical plant to receive a USDA Business and Industry Rural Development loan guarantee, a program that has been around since the 1970s, and more importantly, offers a loan-backing provision that will guarantee up to 60 percent of the loan amount issued.

In Myriant's case, that meant $15 million of the bonds the company placed in the market were guaranteed by the USDA. Here is where the structure gets complex. In order to appease the investor who also wants higher yields (willing to underwrite the riskier investment), while also offering a bond package to the investor looking for a less-risky investment, May used the $15 million in guaranteed bonds, in combination with another $10 million worth of unguaranteed bonds to achieve a placement for $25 million with a very competitive blended rate. In short, May achieved a sweet spot rate that can attract risk-averse investors (who like the guaranteed portion), and risk-seeking investors (who are all about the unguaranteed, 16 percent yielding portion).

Typical projects of this type have installed bond tenure's in the 15- to 20-year range, allowing the bioenergy companies enough time to build the equity and produce fuels or chemicals and also comfortably manage amortization of outstanding principal and accrued interest. In the end, May has found a way to offer hope to project developers strapped with technology, feedstock or any other risk, by pairing an investment market (bonds) that has and will always have an appetite for the potential earnings created by a unguaranteed investment, with those in need of investments that hold a perceived risk. Although several of the transactions that May is working on in the bioproduct space will use USDA loan guarantees, he believes the bond market is viable even without credit enhancement.

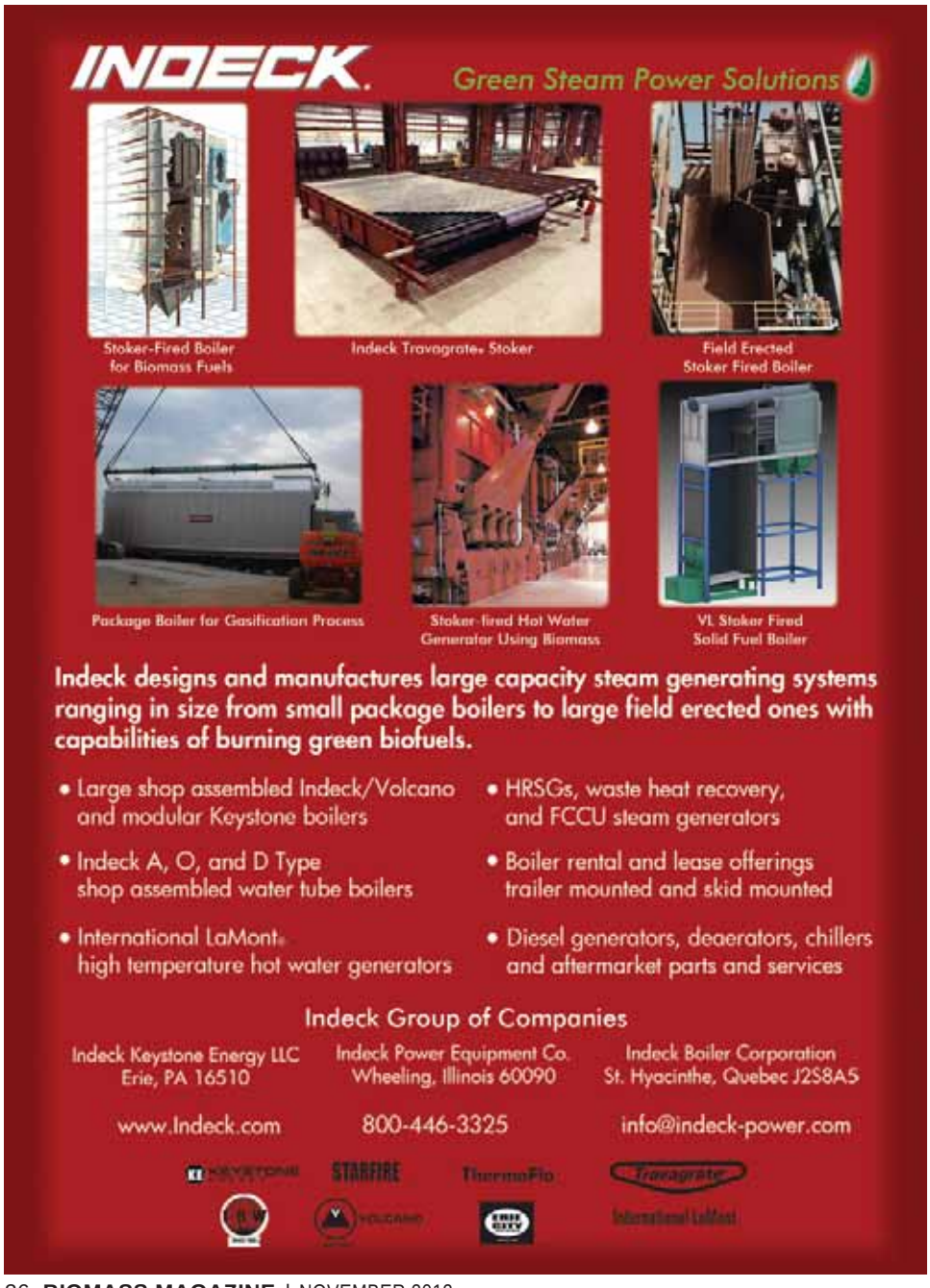
Myriant's success at using the bond-based financing approach wasn't just about the ability of May to explain the story of Myriant or the circumstances surrounding the bioenergy industry to investors, a message he says most bond investors understand. Feedstock requirements, off-take agreements, terms of debt and technology risk, he says, are all issues in other markets, but according to May, the bond market understands those factors may not all be answered in the world of bioenergy and be neatly wrapped and accounted for.

The Project Finance Regimen

Stephen Gatto, chairman and CEO of Myriant, is no stranger to bioenergy or project finance. He's already built and sold a biofuel production company and for the last 25 years, he's been working on project finance for office buildings, labs or fuel production plants. "My experience over the last 25 years is that project finance regimens, if utilized by themselves," Gatto says, "lower the cost of debt because they effectively lower the risk profile." That is exactly why Gatto says, in addition to performing independent engineering and technology analysis on Myriant's biochemical production process prior to seeking out funding, he decided to follow the bond-based financing approach for his Lake Providence project.

May and Gatto share the same understanding of the bioenergy market, as evidenced through their history together. Gatto was the first person to let May deploy his bond-based financing method in the early 2000s. "Going into a project today, where you can mitigate the risk through contractual elements… is probably the only way you get these deals done," he says.

Gatto believes that if Myriant had attempted to use a traditional debt-style financing, the weighted cost of capital received for the project, if any capital were



received at all, would have been around 18 percent (almost 10 percent higher than that achieved by Stern Brothers for the Lake Providence project). "That is a very high cost of capital, certainly for a first of its kind plant," he says. If the success of Myriant's Lake Providence facility, or others who've worked under the guidance of May on bioenergy installations isn't enough to prove why bond-based financing is the new normal for project finance, then Gatto's future expansion plans should. "We will not change our financial structure regimen," Gatto says, on plans for new plants. The company's future regimen will include a third-party process evaluation that allows investors to see that the company can do what it says it will, and the regimen will also go to the $1 trillion bond market for financing, a place where typical regulations don't exist and risk is welcomed.

Although the complex nature of issuing a renewable-energy-linked bond placement might sound as if an aspiring company would need a previous relationship to work with May and his team, it's not the case. May says he takes all calls from project developers, and is willing to pursue any type of bond-based project. The team is currently working on roughly 30 projects for 30 separate clients, the lion's share of which, he says, are in the biomass industry. Over the next 18 months, he believes at least six deals will go through, ranging in size from $25 million to $250 million. Typically, at any given time, his team has at least two bond placements on the market.

The life of a bond placement for a biobased company can be broken down into two parts. The first part involves a financial advisory relationship between a company such as Stern Brothers and the bioenergy firm. The first stage can last roughly two to three months. The second part is the execution, when May sets up an online data room offering investors a chance to view a company's profile, technology and overall risk. That step can take roughly one year.

May and his team earn their compensation through monthly retainer fees and a placement fee that is paid when the bonds are sold to investors. The compensation can vary he says, but typically is based on three to four percent of the total amount of the bonds sold.

For companies interested in pursuing a bond-based financing package but are worried about expiring loan guarantee programs, May says his firm is already working to develop, or has developed other credit enhancing tools like insurance guarantees for certain technology. May believes that over the next few years his travel schedule will not decrease, and his bond-backed strategy will continue to offer the best alternative to traditional debt-financing and in most cases, a better alternative. Comments from Gatto also show just how important the first-ever biobased project in the U.S., and its ability to deploy a bond-based financing regimen, truly is for the entire industry. "The good news," Gatto says of his Louisiana plant, "is that the construction will be completed shortly. Not only do you prove to investors that the plant and the operations are viable, but you have effectively de-risked your second plant."

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