Ineos Exits Restrictive Debt as Lenders Swarm: Corporate Finance
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By Stephen Morris and Krista Giovacco

May 2 (Bloomberg) -- Ineos Group Holdings SA is poised for credit-rating upgrades after obtaining the largest ever covenant-lite loan in Europe, breaking the yoke of restrictive terms when the company was forced to renegotiate debts in 2009.

Ineos, the provider of chemicals to such industries as construction and food packaging with 60 factories in 13 countries, refinanced $3.6 billion of debt last week with a $3.03 billion loan and $775 million of bonds. Standard & Poor’s upgraded the Rolle, Switzerland-based company to B from B- with a “positive” outlook on April 24, citing the refinancing and better-than-expected earnings. Moody’s Investors Service raised the outlook on its equivalent B2 rating to “positive” from “stable” last month.

Appetite from U.S. and European investors, driven by the company’s first profitable year since 2007 as demand for its chemicals rose, allowed Ineos to twice increase the size of its loan, while reducing its more-expensive bond sale. Obtaining the covenant-lite debt has paved the way for another upgrade.

“The positive outlook reflects the possibility of another one-notch upgrade over the next 12 months if Ineos completes the envisioned refinancing, shows further operating resilience, and reduces debt throughout 2012,” S&P analysts led by Oliver Kroemker in Frankfurt wrote in an April 24 report.

The company reduced its eight-year bond sale to $775 million, from $2.2 billion initially proposed, according to data compiled by Bloomberg. The notes have a 7.5 percent coupon and were sold at par, making the fixed-rate debt more expensive than the loan, which has a blended yield of about 7 percent.

Breaking Pattern

Richard Longden, a London-based spokesman for Ineos, didn’t return phone and e-mail messages seeking comment about the company’s finances.

Ineos is breaking a pattern in place since its 1998 founding in which it financed deals by increasing debt to about five times earnings, and then relied on profits to reduce leverage to three times before embarking on the next purchase, Group Director Tom Crotty said in a September interview.

“The refinancing will allow Ineos to achieve a much higher degree of financial flexibility and further improve its debt maturity profile,” Moody’s analysts led by Gianmarco Migliavacca and Olivier Beroudwrote wrote in an April 20 report from London. The deal will reduce the "vulnerability of Ineos's current capital structure in case of a downturn, especially given the tight financial covenants attached to all the outstanding bank facilities."

'Significant Improvement'

The ratio of Ineos net debt to earnings before interest, taxes, depreciation and amortization fell to 3.41 last year from as high as 9.1 in 2008, Bloomberg data show. It was 3.8 times at the end of the first quarter, when the company had 6.2 billion euros of debt, according to an April 16 statement. The company had debt of about 3.8 times Ebitda, it said in the statement, down from 4.75 times last year.

Ineos said in the statement that it's seen a "significant improvement in trading" as demand for chemicals recovered following the financial crisis that started with the collapse of the U.S. subprime mortgage market in 2007. An index of U.S. chemicals output was 7.5 percent higher on a seasonally adjusted basis in March than at the end of 2008 and European production was 20 percent higher in February, Bloomberg data show.

The chemicals maker reported 2011 net income of 376.4 million euros ($498 million), compared with a loss 617.3 million euros in 2009, underpinning demand for its new debt even as it was stripped of traditional creditor protections.

Covenant-Lite

"The concentration and amount of capital on the sidelines is enormous," Reuben Daniels, managing partner at EA Markets in New York said in a telephone interview. "Investors and certain financial institutions have cash to put to work in loan product, and that creates an environment where issuers can be more aggressive on covenants."

Companies in the U.S. and Europe sold a total of $20 billion of loans without typical lender protection such as financial-maintenance requirements in the first four months of this year, according to Standard & Poor's Capital IQ Leveraged Commentary & Data. Only $1.41 billion was sold in Europe.

"Clearly from a lender's perspective, one wants more covenants and tighter constraints to protect one's capital,"
Daniels said. "If the covenant package was the only decision- making factor, the Ineos deal might not have gotten done. Not only must lenders be looking beyond

the covenants, but they’re looking at other aspects of the relationship that are valuable to them,” he said.

‘Opportunistic’

Ineos, created as a management buyout of Belgian assets of BP Plc, renegotiated loans at more expensive rates and tighter conditions in 2009 after borrowing 7.5 billion euros to buy BP’s Innovene unit in 2005, before demand for chemicals collapsed in the recession.

The new term loans extend Ineos’s bank debt maturity as much as six years to 2018 and eliminate quarterly financial tests its current payment-in-kind loans are subject to under so- called maintenance covenants, three people with knowledge of the deal said on April 18. Instead, the debt will have incurrence- based covenants, which dictate the borrower cannot add debt unless a chosen financial ratio is within a stated range. Such packages are more commonly used for high-yield bonds and offer investors less protection than customary restrictions on loans.

“Ineos is being a little bit opportunistic here, but there’s nothing wrong with that,” Tim Polglase, global head of leveraged finance at Allen & Overy LLP in London, said in a telephone interview. “They’ve got the ability to get out of maintenance covenants that have caused them headaches in the past.”

Loans Rise

The largest term loan, for $2 billion, pays interest of at least 6.5 percent, or 5.25 percentage points more than the London interbank offered rate, whichever is higher. A 500 million euro-denominated portion pays 6.75 percent, or 5.5 percentage points more than Euribor, while a $375 million three- year slice pays 5.5 percent, or 4.25 percentage points more than Libor, the data show.

All of the loans were sold at discounts to face value, raising yields for investors. The six-year loans were sold at 98.5 cents on the dollar and rose to 100.625 cents yesterday, according to information provider Markit Group Ltd. The three- year portion, issued at 99 cents on the dollar, climbed to 100 cents, Markit said.

Ineos sold $1 billion of seven-year notes in February, part of a $1.6 billion dollar-and-euro issue that was doubled in size in response to investor demand. The 8.375 percent notes due 2019 were sold at face value and traded yesterday at

107.875 cents on the dollar to yield 6.9 percent, according to data compiled by Bloomberg.

Less Risk

The cost to insure Ineos's debt using credit-default swaps has dropped 13 percent to 702 basis points since it announced plans to refinance with a covenant-lite loan on April 16, extending the decline to 37 percent this year, Bloomberg data show.

That compares with a 5.4 percent rise in the price of contracts on BASF SE and a 4.3 percent drop for Dow Chemical Co., larger competitors. A fall in the price of the swaps indicates an improvement in perceptions of creditworthiness.

Derivatives traders were assigning Ineos almost certain odds of default in January 2009. The price of credit-default swaps tied to 10 million euros of the company's debt reached 8.28 million euros upfront plus 500,000 euros annually for five years.

Ineos also sold a 50 percent stake in a refining operation to PetroChina Co. for $1.02 billion last year to raise cash. Leveraged loans and high-yield bonds are rated below Baa3 by Moody's and lower than BBB- by S&P.

"Banks don't like incurrence-based facilities, so this is likely to have been primarily sold to fund investors in the U.S., and insurers are also quite big players in that market," said Allen & Overy's Polglase. "These loans are bought by investors who buy them in the same way as bonds; they don't expect to be getting frequent consent requests through and have confidence that the business will ride out any problems."

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