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PAYING DOWN WITH PIPES

Stock Surge Helps Companies Eliminate Debt

by Max Frumes

As the stock market surges, more companies are issuing private placements to pay off maturing or high-interest debt.

Many of those companies may be rescued by the market rebound from the risk of defaulting on their debt. There are 1,154 companies listed on U.S. exchanges that reported net losses in their last annual filings and have more than $1 million in long-term debt coming due by the end of this year, according to data provider Capital IQ. This compares to 794 such companies in the same situation a year ago.

Meanwhile, the market's gains this year have fueled a 54% rise in the Russell 2000 index of small cap stocks through June 6 from the six-year low it touched in March.

At least 45 companies this year have said they would use proceeds from a PIPE to repay debt, according to PrivateRaise, DealFlow Media's data service. That compares with 42 companies over the same period last year, even though there were 40% fewer PIPEs this year.

"I can't think of a better use of proceeds in this environment than to pay down debt," says Aaron Gurewitz, the head of investment banking at Newport Beach, Calif.-based placement agent **Roth Capital Partners**.

The management of gold and silver mining company **Hecla Mining** didn't want to face the nightmare situation of having to raise money at $1 a share. That's where Hecla stock had traded since March after hovering above $13 a year earlier. So in a deal announced June 2, the Coeur d'Alene, Idaho-based company got a $60 million commitment from investors to pay down a portion of an increasingly expensive outstanding loan. The PIPE was arranged by **Rodman & Renshaw**.

Hecla sold shares for $3.45 each, taking advantage of a tripling of the company's stock price since March.

Investors included **Heights Capital Management**, **Rockmore Capital**, and **Downsview Capital**.

When Hecla had taken on the debt, it had planned to replace it with longer-term financing, but that option disappeared as markets crumbled, said Don Poirier, the company's vice president of investor relations.

Now that Hecla has seen a marginal recovery, it doesn't want to risk having to raise money at a lower price.

"Last year, we didn't see the market risk that came," Poirier said. "We just don't want to take that kind of risk again … Precious metals are going on a tear of late; to me [financing now] seems to be a reasonable thing to do."

Hecla had a $380 million loan that **Bank of Nova Scotia** arranged in April 2008. The loan consisted of a $140 million three-year term facility and a $240 million bridge facility. The bridge facility charged interest of LIBOR plus 6% or an alternative base rate plus 5%. Hecla had paid part of it off with public and private offerings, but still had a balance of more than $100 million by the end of the first quarter, according to filings with the Securities and Exchange Commission.

The PIPE reduced the debt to $55 million.

Rodman hopes to arrange more of these placements for companies looking to pay down debt, said John Borer, the firm's head of investment banking. Rodman has been reaching out to companies that have bank debt or high-yield debt, and finding it to be "fertile ground," Borer said. The effort has been going on since the fall. Since that time, Rodman has arranged at least four PIPEs for companies that will use at least some of the proceeds from their placement to pay back debt, according to PrivateRaise.

"There are so many of these companies where everything but one toe was at the gates of Hell," Borer said. "They're looking back now, and don't want to go back that way…We're seeing a lot of that psychology."

Many companies looking to pay down more expensive loans still can't get better rates from banks.

Firms like Victory Park, an asset-based and bridge lender to small companies, have been able to take advantage of the fact that banks have not been lending over the past year. That in turn means that there may be more PIPEs as soon as a company sees its stock recover enough to pay off bridge loans.

For example, **Jamba Inc.**, the parent company of the Jamba Juice chain, is issuing a $35 million private placement of convertible preferred stock to pay off a loan from Victory Park.

Jamba's lender before Victory was Wells Fargo Foothill. When Wells tightened its lending, Jamba had to resort to issuing a $25 million note to Victory in September, secured by a first priority lien on all of Jamba's current and future assets, according to an SEC filing. Those notes carried a rate of the six-month LIBOR plus 8%, with a floor of 12.5%.

Companies will turn to Victory Park when they'd rather pay a high interest rate than dilute the value of their stock.

But dilution is less of a concern in situations where recent investors will still have a profitable investment even after a dilutive financing, as was the case with Hecla.

"Having a higher share price made it easier," Hecla's Poirier said.

In Jamba's private placement, the Emeryville, Calif.-based company raised $19.55 million from private equity firm **Mistral Equity Partners**. The other $15.45 million came from a company controlled by the Serruya family of Canada, Jamba said in statement.

The preferred stock from the Jamba PIPE is convertible into common stock at $1.15 a share. That was a 15% premium to where Jamba shares traded before the deal was announced.

Jamba shares rose 9 cents to $1.09 on June 1, the day of the announcement.

Roth's Gurewitz said that it is not uncommon for fundamental investors to be receptive to companies that are raising capital to pay off debt.

That was the case in a deal by **IMAX Inc.**, the operator of giant-screen movie theaters. The Mississauga, Ontario-based company had $160 million in outstanding senior notes as of March 31, according to an SEC filing. The unsecured notes, due December 2010, charged a rate of 9.63%.

Roth Capital arranged a privately negotiated equity deal for $65.1 million that IMAX announced on June 2. The placement was structured as an underwritten public offering marketed on a confidential basis with pre-registered shares sold similarly to in a registered direct PIPE.

"Investors have been very receptive to issuers raising capital to pay off debt," Gurewitz said. "It's basically a lot of the fundamental and long-type investors that are participating here."

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