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As Junk Rallies, Tribal Startup Sets Riskiest Muni Bond in Years.

In a municipal-bond market flush with cash chasing the riskiest securities, a new business created to sell propane to American Indian tribes is planning to issue debt that, from the start, is seen only a few steps away from a default.

The venture, set up by a Dallas-based company, is aiming at a problem that's vexed remote reservations in the Great Plains: winter fuel scarcities, which have led to price spikes and left some impoverished residents unable to heat their homes. The $22 million sale, which is slated for sometime in the next two months, would be used to buy propane when prices are low, store it and truck it in when needed. Revenue from those sales would repay the debt.

Bondholders may be out of luck if the business fails to get enough tribes to sign on, according to Moody's Investors Service, which said only three had by early May. So it rated the securities Caa2, eight steps into junk, the lowest grade it has given a new bond offering in at least six years. The rank indicates "very high credit risk."

"Anyone who buys will have had to have done extensive due diligence," said Peter Block, managing director with Ramirez & Co., a New York bond underwriter that isn't working on the deal. "Hard to say who will be interested in this."

Now is a good time to find anyone who is. With municipal-market yields the lowest since the 1960s, investors have been snapping up the worst-rated bonds, which have bigger payouts because of the risk. That has fueled a rally in speculative securities issued by state and local government agencies, including bonds repaid with tobacco-company settlements that rating companies say are almost certain to default.

Individuals added $310 million to funds focused on the riskiest municipal debt in the week ended May 11, the most in about four months, according to Lipper US Fund Flows. With money coming in, the assets of such high-yield funds have climbed to a record $82 billion from $58 billion at the start of 2014, according to data from Morningstar Inc. and Lipper.

The debt for the Infrastructure Development Cooperative's energy business would be sold through the Madison, Wisconsin-based Public Finance Authority. The agency, which rents out its access to the tax-exempt market for a fee, has raised money for charter schools, real estate developments and other projects in more than a dozen states. Scott Carper, the authority's program manager, declined to comment.

L. Steven Haynes, the founding partner of Haynes Investments, an affiliate of Highland Park Management LLC — which Moody's says is overseeing the project — didn't respond to telephone calls seeking comment. Haynes Investments, which is based in a hangar next to Dallas's Love Field airport, describes him as "one of the leading business executives in Native American project finance."

Gabe Doney, executive director of Tribal Infrastructure Development Cooperative, a Valentine, Nebraska, supplier of products and services to American Indians, said in an e-mail that he is Haynes' partner on the deal. Doney said the group's goal is to sell the bonds within the next 60 days.

"We are still working toward our bond," said Doney. "Once we have everything taken care of we would be willing to discuss it."

The business may fill a chronic need. In winter, those living on reservations are routinely squeezed by propane shortages that push retail prices to unaffordable heights, said Gavin Clarkson, American Indian finance scholar at New Mexico State University.

In 2014, the governors of several states signed emergency declarations making it easier to truck in supplies after a shortage led to at least one death at the Standing Rock Sioux reservation, which straddles the border of North Dakota and South Dakota.

"People can't afford to heat their homes so they risk freezing to death," said Clarkson. "It's a solid business concept, but the question is whether the tribes can execute."

The business' ability to generate revenue adequate to repay the bonds is the biggest challenge. Though it identified "significant" demand among 37 tribes, it has only signed agreements with three of the 10 it has targeted as initial customers, Moody's said in a May 11 report. Borrowing without enough agreements makes the deal "highly speculative," even though some of the proceeds will be used to cover the first three years of interest payments, according to the credit-rating company.

"The potential exists for significant shortfalls in net revenues," Moody's said.

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