

Boundless Koch

Downturn sets stage for expansion

Did you know?

KOCH INDUSTRIES



Charles Koch

The Wichita-based company has affiliates engaged in an increasingly wide range of economic sectors. Here are some of their major business interests.

Commodities trading

- Koch Supply & Trading LLC

Municipal finance and trading

- Koch Financial Corp.

Capital market investments

- Koch Capital Markets

Venture capital investments

- Koch Ventures LLC
- Koch Genesis LLC

Energy

- Entergy-Koch LP
- Gulf South Pipeline Co. LP

Petroleum and chemicals

- Refining and chemicals - Flint Hills Resources LP
- Canadian oil sands development - TrueNorth Energy LP
- Exploration and production - Koch Exploration Co. LLP

Asphalt

- Koch Materials Corp.
- Koch Pavement Solutions
- Koch Performance Roads

Pipelines

- Koch Pipeline Co. LP
- Koch Capital Investments Co./Colonial Pipeline Co.

Minerals

- Koch Mineral Services LLC
- Ferti Nitro

Hydrocarbons

- Koch Hydrocarbon Management Corp.

Chemical technology

- Koch Chemical Technology Group LLC

Ranching

- Matador Cattle Co.

Plastics and fibers

- KoSa BV

ROSEMOUNT, MINN.



Minneapolis Star-Tribune

Koch acquired a majority interest in the Pine Bend refinery in Rosemount, Minn., in 1969. Since then, the refinery has increased capacity from 50,000 barrels per day to 290,000 barrels per day. Even as the company diversifies, petroleum is still primary among Koch's businesses.

■ A restructuring and the battered economy have created opportunities for the Wichita company. Indeed, when the business cycle sours, Koch seems to say, "Bring it on."

BY PHYLLIS JACOBS GRIEKSPoor

The Wichita Eagle

Koch Industries is back in a serious growth mode. After extensive restructuring following an economic downturn and troublesome performance in the late 1990s, Koch has emerged ready to grow. It is, in fact, in negotiations for what could be its largest acquisition, the nylon fibers and resins business of DuPont, a deal analysts value at \$5 billion.

And after layoffs that numbered in the hundreds only a few years ago, employment is growing again.

More than 17,000 people work for Koch in some aspect of its far-flung empire of companies in 30 countries — a gain of 6,000 jobs since the late 1990s.

About 1,850 of those people work in Koch's headquarters in Wichita and another 100 work for Koch companies elsewhere in Kansas.

"Obviously as we grow through acquisitions and broadening of existing companies, our core employment in Wichita will also grow," spokeswoman Mary Beth Jarvis said.

Equally good news is that it is not likely the company will move its headquarters, at least not any time soon.

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“You never say never,” Jarvis said. “We are constantly re-evaluating all aspects of our business. But there are no signs that we’d be making that change any time soon. That doesn’t mean, of course, that it won’t be advantageous for some of our subsidiaries to have their headquarters somewhere else.”

In a time when the economy is sputtering and many companies are struggling, Koch is seeing opportunity, limited only by how fast it can identify and analyze potential properties to buy or develop ways to expand existing companies, executives say.

“We are in some ways a counter-cyclical company,” says Ron Vaupel, head of Koch’s business development team. “Historically, you’ll see Koch buying during a down cycle.”

The acquisitions of recent months — Colonial Pipeline, Farmland Fertilizer and Excel Paralubes — and the exclusive negotiations for DuPont’s nylon business are “just the tip of the iceberg,” in the words of president and chief operating officer Joe Moeller. He wrote about Koch’s growth plans in a recent company newsletter, describing the “deal pipeline” as “full and moving fast.”

Vaupel said Koch has worked hard to grow its capabilities. “We’re capability-constrained, not industry- or product-constrained,” he said. “We think that we can grow across the board in trading, in operations, as long as we stay disciplined and stay within our capabilities.”

Vaupel said the company philosophy is that a small group of core capabilities — including trading and operational excellence — will determine the growth of every Koch company.

Petroleum, including the handling of petroleum and the products made from petroleum, is still primary among Koch’s businesses. But trading, securities and finance, ranching and investments have emerged as key companies as well.

Through Koch Genesis and Koch Ventures, its venture capital and entrepreneurial support companies, Koch is looking for the right startup businesses to support — providing the basis for even more extensive diversity in the future.

Restructuring helped align businesses that could grow together and separated others that were likely to need to grow in a different direction, Vaupel said. For example, the split of Koch Petroleum Group created two separate companies, Flint Hills Resources, focused on refining, fuels and petrochemicals, and Koch Supply and Trading, focused on global trading of energy products and risk management tools.

Both have grown since the split.

Flint Hills Resources closed in July a deal that will give it a 50 percent interest in Louisiana-based Excel Paralubes, a company that produces and markets base oils, the primary ingredient of motor oils, transmission fluids and other lubricants.

It’s a new product line but one that fits

well within the refining capabilities the company already has.

“This is a great fit for us,” says Dave Robertson, president of Flint Hills Resources. “As an established player in the refining business, we know something about hydrocrackers. We also have a long history of trading refined products on the wholesale market.”

While the Paralubes deal is a major one, it’s not the end of looking for new properties for Flint Hills Resources.

“To some extent, our next move depends on the market,” Robertson said. “Who knows? We might buy another refinery or invest in a chemical asset. What matters most is that our growth efforts reflect our capabilities. We know what we do well.”

Koch Supply and Trading has added industrial and precious metals to its already substantial base of activities in crude oil and refined petroleum products.

Koch Nitrogen substantially increased its interest in the ammonia business when a Kansas City, Mo., bankruptcy court approved its \$293 million purchase of fertilizer plants and other assets from Farmland Industries in May.

The move was an example of Koch’s willingness to take a chance on expanding in tough times. High prices for natural gas, the primary feedstock for fertilizer, have caused tough times for the fertilizer industry in the United States, including plants already owned by Koch.

HOUSTON



Courtesy of Koch Industries

Houston is a hub for Koch Supply & Trading. The company is among the top five in the world for crude oil trading.

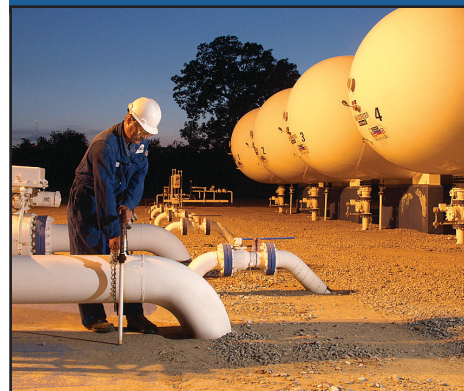
ENID, OKLA.



Brian Corn/The Wichita Eagle

The Farmland nitrogen plant in Enid, Okla., is among the Farmland assets purchased by Koch in a \$293 million deal in May.

TULSA



Courtesy of Koch Industries

Koch Pipeline Co. LP owns or operates about 8,000 miles of pipelines. Its operations include this pipeline terminal in Tulsa.

KOCH INDUSTRIES' GROWTH UNDER CHARLES KOCH

Koch Nitrogen, however, saw opportunity for long-term growth in the Farmland assets. At the time of the purchase, Koch said it expected to improve efficiencies at the former Farmland plants and make investments to move them to profitability.

Many Koch companies that have not made acquisitions have nonetheless grown through an increase in the scale of their transactions.

Koch Financial, for example, undertook its largest project when it provided \$91 million in financing for new transit buses in Pittsburgh, Pa. It has also increased its stake in municipal bond trading.

One thing that is not likely to happen, Koch officials say, is making any move toward becoming a publicly traded company.

Koch literature makes frequent reference to the "blessing" of being privately held by like-minded shareholders who have consistently poured 90 percent of the corporation's earnings back into the business.

"We don't have to impress analysts quarterly or create hype to enhance our outlook," Vaupel said. "We can concentrate on long-term value. Wall Street expects steady growth quarter after quarter and year after year. That's not the way it happens in the real world. Business tends to move in cycles. It's better to look at a 10-year or 20-year time period. Are you significantly ahead of where you were 10 years ago?"

At the same time, the company has not been averse to partnering with publicly traded companies as in the successful \$1 billion deal that formed Entergy-Koch Trading in 2001. Koch shares ownership with Louisiana-based Entergy, a publicly traded energy company.

Entergy-Koch is a private company that delivers, markets and trades power, natural gas, weather, energy-related commodities and risk-management products.

With its superior credit rating and extensive asset base, Entergy-Koch was well-positioned to make gains in the trading world following the collapse of Enron and other more speculative traders.

Vaupel said Koch is actively looking for acquisition opportunities, and those may well come from publicly traded businesses whose cyclical nature has left them

1969

- Acquires majority interest in Pine Bend Refinery in Minnesota

1970

- Natural gas liquids plant built in Medford, Okla.

1979

- Acquires real estate portfolio from Chrysler

1981

- Acquires refinery in Corpus Christi, Texas, from Sun Oil

1986

- Acquires C. Reiss Coal Co., a 100-year-old Great Lakes company

1988

- Construction of Texas Pipeline begins

1989

- Purchase of John Zink Co. of Tulsa

1992

- Acquires United Gas Pipeline, renamed Gateway, now Gulf South, an 8,000 mile system

1993

- Acquires Elf Asphalt

1997

- Acquires Delhi Group
- Acquires Glitsch

1998

- Forms KoSa, after acquiring 50 percent of Hoechst's polyester division
- Acquires Purina Mills
- Acquires Rotterdam splitter from Goldman Sachs
- Forms Koch Ventures, a venture capital firm with \$150 million invested

2001

- Acquires full ownership of KoSa
- Forms Entergy-Koch LP with Entergy Corp.

2002

- Flint Hills Resources, Koch Pipeline Co. and Koch Chemical Technology Group become stand-alone companies

2003

- Koch Nitrogen acquires fertilizer assets from bankrupt Farmland Industries for \$293 million
- Increases stake in Colonial Pipeline to 27.8 percent
- Enters lubricant base oils business with half-interest in Excel Paralubes, pending regulatory approval
- Enters negotiations for DuPont polyester business

in a "down cycle" in the current economy. He said private companies that want to stay private but are having trouble obtaining the money for investments that will stimulate growth would also interest Koch, which makes no secret of having plenty of cash and credit to pour into ventures that need only development to become profitable.

Koch Industries maintains long-term credit ratings of Aa1 from Moody's Investors Service and AA+ from Standard & Poor's Rating Group, the second highest rating possible.

Only 4 percent of rated entities worldwide, including banks and insurance firms, are at or above that level.

"If we see an opportunity for them to grow long-term with the right investment and management and if they fit within our capabilities, then we're interested," Vaupel said.



Dave Williams/The Wichita Eagle

Koch Industries' headquarters is in a prominent building on 37th Street North in Wichita. Employment at the headquarters now stands at 1,850 people. The company expects its Wichita employment to grow slowly over the next few years.

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Holdings growing at Koch

■ The second-largest privately held company in the U.S. could one day be No. 1.

BY PHYLLIS JACOBS GRIEKSPoor
The Wichita Eagle

Koch Industries often is described as the nation's second-largest privately held company.

At some point, it may shed that "second" designation.

Koch is growing rapidly, narrowing the gap in gross revenues between it and long-time No. 1, Minnesota-based Cargill Inc.

The designations have little meaning beyond conversation. Still, Koch growth is a bright spot for a Wichita economy still trying to recover from manufacturing job losses.

And Koch's expansion this year has been extensive:

Its subsidiary, Koch Nitrogen, bought a large portion of the fertilizer assets of Farmland Industries in May. It now is capable of producing more ammonia than any other company in the Americas.

Another subsidiary, Flint Hills Resources, closed a deal in July that gave it half of Excel Paralubes. That added a new product line: base oils, the type of oil used to make motor oil, transmission fluid and other lubricants.

Koch Capital Investments has increased its ownership share in Colonial Pipeline from roughly 7 percent to about 28 percent. It now is the largest shareholder in the largest refined products pipeline in the world.

The biggest deal of all may be announced any day.

Koch, through some unnamed subsidiaries, is in exclusive negotiations for

what would be its biggest purchase ever — the nylon fiber and resins business of DuPont, a deal analysts estimate at \$5 billion for a company that had more than \$6 billion in gross revenues last year.

Koch employs more than 1,800 people at its headquarters on North 37th Street. That number will grow with new acquisitions, said spokeswoman Mary Beth Jarvis.

"We can realistically expect that there may be some subsidiaries that it would make sense to have headquartered in other cities," she said. "But others will be in Wichita."

The Farmland acquisition, for example, brought around 25 new employees to Wichita. Farmland's headquarters were in Kansas City, Mo.

Jarvis said she sees nothing to indicate Koch could move its headquarters from Wichita.

"You never say never," she said. "But it's not something currently being considered."

Both Koch and Cargill are privately held companies, meaning they have a limited number of shareholders who own the company. Shares are not available to the general public.

Gaining that No.1 designation is not something that particularly concerns Koch, Jarvis said.

"It's just not something we're interested in," she said. "To us, growth is important; our own growth. But we're talking about strengthening, enriching, broadening. It's not about gross revenues. It's about doing things better, making our companies stronger."

The folks at Forbes Magazine, who annually do the math and the estimates to come up with a list of the world's largest privately held companies, say they see the gap between Koch and Cargill definitely narrowing, especially if the DuPont deal goes through.

Last year's numbers from Forbes put Cargill gross revenues at \$59.8 billion and

Koch's at \$40 billion. Cargill reports gross revenues in news releases, Koch does not. Net profits for either aren't something Forbes even tries to guess.

"Neither of them releases anything," said editor Vivian Woo, who oversees the compilation of the list.

She speculates, however, that Koch might already be the leader in that department.

"The margins are better in chemicals and oil and plastics and fibers than they are in commodities," she said. "Depending on just how much better they are, Koch could already be the more profitable of the two companies."

Cargill, the parent company of Wichita-based Excel, the nation's third largest beef packer, is also growing. Its meats side has added Taylor Beef, Empak and two turkey operations in the past year. Friday, Cargill announced it is bidding to purchase the assets of Farmland Foods' pork processing business.

By some measures, Cargill is much bigger. It has, for example, 98,000 employees worldwide to Koch's 17,000. It has affiliates in 61 countries around the world. Koch has companies in 30 countries.

Woo, however, says Koch may have a higher ceiling when it comes to growth opportunities.

"Cargill is primarily a commodities company," she said. "Koch is not limited by the market for any given product."

That is a point Koch also makes.

In a July newsletter, chairman and chief executive Charles Koch was quoted this way, "Unlike most companies, we see our growth as capability bounded, not industry or product bounded."

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