

PLAYING THE BORDER GAME

Anthony Catachanas explains why a sustainability fund bought two storage terminals in the US for the cross-border market in Mexico



> IN MAY 2021, Victory Hill Global Sustainable Energy Opportunities (GSEO), bought two operating storage terminals in Brownsville, Texas, US, for US\$61 million (€52 million).

The terminals store high-sulphur, more polluting fuels from Mexican refineries, from where they can be transported to modern, efficient refineries in the US, for further refining into low-sulphur, less polluting fuels, such as ultra-low sulphur diesel (ULSD), compliant with US and European standards. GSEO's new terminals then act as a distribution point to ship these cleaner fuels back to Mexico.

Keen to find out why a sustainability-focussed investment company would buy petroleum terminals, *Tank Storage Magazine* spoke to Anthony Catachanas, the CEO of Victory Hill Capital Advisors (Victory Hill), GSEO's investment advisor.

A SUSTAINABILITY FUND IS NOT A RENEWABLES FUND

'We are a sustainability fund. What sustainability doesn't mean necessarily is that we're going to be doing renewables only,' says Catachanas. 'Renewables means predominantly power generation, which requires a lot of capital. Much of this goes into places like the US and Europe, causing an oversupply of intermittent power generation. It's fantastic, we do want more, but it's intermittent, so then you go back to other, more reliable forms of generation, which often means coal. Pouring tens of thousands of dollars into renewable power generation while still relying on coal to balance the grid doesn't make any sense. We're about trying to

understand the balances and trying to understand the gaps.'

A renewables fund is therefore not necessarily sustainable. Catachanas says that the company also needs to educate an investor community more used to obvious renewable projects about local conditions and realities. A solar farm in a developing country connected to an unreliable grid isn't going to help anybody or indeed, generate good returns. So far, investors have been receptive.

STEPS ALONG THE WAY

In Mexico, one of the biggest gaps is the need for cleaner fuels. Victory Hill identified a 'fundamental need' to improve the Mexican fuel market. The Mexican economy is extremely transport-orientated and dependent. The rail network is underdeveloped, so cars, buses and trucks are vital. Mexican refining capacity, run by state-owned company Pemex, has not seen significant investment since the 1970s, with some major refineries more than 100 years old. Locally produced fuels do not meet newer Euro 5 and Euro 6 standards, and the country is reliant on US refining capacity, shipping out its dirtier fuels for further refining.

Cleaner fuels are undoubtedly better, for the climate and air quality, but sustainable? Catachanas believes that sustainability is a goal, and achieving it will require all the available options.

'Mexico needs to get rid of its dirty fuels, because if they don't do that, they're going to continue burning the fuels that they produced locally. If we don't facilitate this process of adaptation and transition, we're not helping the transition at all, we're actually curtailing it,' he points out.

In affluent, more developed countries, with more reliable electricity grids and infrastructure, as well as the money for upgrading vehicles, electrification is the ideal, but in many places, including Mexico, this is not currently an option. With lower incomes, people will buy whatever car they can and fill it with the cheapest fuel they can find. While a new solar or wind farm would tick all the right environmental, social and corporate governance (ESG) boxes, it wouldn't help, given the unreliable, inefficient Mexican grid.

'We have to deal with the realities on the ground and the reality on the ground is

that they have a need to make a switch first from highly emitting fuel and migrate that into lower emitting fuels. Eventually they will migrate that at some point to electric vehicles, but it's a journey, it's a process. We try to recognise that process and facilitate that process instead of saying get into electric vehicles right away,' he says.

FINDING A USP

Having identified the investment gap, Victory Hill needed to work out how to contribute.

'There is a northbound market [heavier, high-sulphur fuels out of Mexico] and the southbound market [more refined fuels back] and if you do what everybody else does in terms of terminal storage, which is to go for the most fungible product, the product that has the greatest ability to be traded, you're going to have a lot of competition. There's a lot of people that can store ULSD or gasoline product but that doesn't really help. You're not really adding value to the chain if you do everyone else does,' says Catachanas.

What Victory Hill decided to do instead was facilitate both the north- and southbound supply chains, helping to perpetuate and encourage the constant flow. For that, it needed a facility that could handle the heavier products.

THE BENEFITS OF BROWNSVILLE

Victory Hill was spun out of Mizuho, and between them, the team already had extensive experience in global conventional as well as renewable energy assets, in 33 jurisdictions, having deployed collectively US\$217 billion of capital. Already at Mizuho, Brownsville had been identified as a good, strategic location for the Mexican markets by the team. It is much closer to the border than major hubs like Corpus Christi and Port Arthur, and has direct rail connections into Mexico, making transport simpler and quicker, not to mention cheaper real estate costs.

Victory Hill identified a suitable site and approached owner Howard Energy Partners which agreed to the sale, and the deal was signed on 31 March 2021.

The 525,000 bbl of capacity is split over two sites, one focussed on fuel oil, with two 150,000 bbl tanks, and one on lubes,

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waxes and some ULSD, with nine tanks ranging in size from 20,000 to 50,000 bbl. The sites each have a rail hub, and dock access, with a draught of 36' (11 m), pipelines to the tanks and hoses for loading.

WORKING WITH MOTUS AND CUSTOMERS

'The one thing you need when you offer these types of assets is a good management team which knows how to contract these tank spaces, can get customers to come in as tenants and use the tanks and turnover the tanks. That's where the revenue line predominantly comes from,' says Catachanas.

Victory Hill found this team in Motus Energy, the founders of which come from BP, JP Morgan, Itero Energy, TransMontaigne and had worked with the previous owners. Motus also took on the Brownsville sites' existing staff of 10.

'We've known this particular team at Motus for a very long time. They have been doing a lot of trading southbound into Mexico through their trading company called Metrix Energy and we've decided to put together Motus by combining them with some former members from the Howard Energy team for the purposes of managing the two sites. These guys have quite a bit of experience and we're very happy with the management team there. I think they will probably be managing other midstream assets that we pick up through this fund,' says Catachanas.

Customers can obviously put whatever they like in their leased tanks, but Victory Hill and Motus are very careful about who they partner with, to ensure that they choose companies that understand the desired sustainability purpose of the

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Brownsville operations, and have cross-border experience. Friction at the border is common.

'It's our choice what kind of tank we build and what purpose we want to render for the tank. These are choices that we want to consciously make. The partners that we have at the moment certainly understand our intentions,' says Catachanas.

FUTURE PLANS

The Brownsville sites, which, while in a very good condition overall, have 'tremendous potential' for further development, according to Catachanas. Victory Hill plans to expand one of the rail hubs to accommodate a second unit train, as requested by a customer, and it is also investigating pipeline connectivity for the sites.

'We plan to expand both terminal sites with an additional 200,000 bbl of capacity, probably one 100,000 bbl tank on one site and two 50,000 tanks on the other to accommodate lighter products,' he says.

'We like working across the US and Mexico border. Since 2013, the Mexican market has been reforming the fuel

market bring in more refined products, and we see an avenue to bring in more products. The import infrastructure in Mexico is pretty underdeveloped, so the US Gulf Coast ports in Texas tend to act as aggregation hubs for rail export into Mexico,' says Catachanas. 'That's why we want to expand our activities.'

Midstream assets have always been attractive to investors, as they offer steady yields and good returns. The engineering is simple and the technology risk low. Catachanas says they are also good in the longer-term.

'We believe that midstream assets will always have a place going forward even if we shift into biofuels and other products that act as a stepping-stone towards a more electrified world. There will be an intermediary step, maybe even two, and we will need tank capacity. Midstream assets are simple assets and can be repurposed easily. If you have a natural gas storage facility it can be repurposed to store hydrogen. If you have a gas pipeline you can repurpose it for hydrogen as well. If you have liquid storage tanks you can put biodiesel in them,' says Catachanas. 'These assets have a role to play in the energy transition.'

For more information:

www.vh-gseo.com
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