Fireside Chat with Don Baldridge, EVP Midstream Phillips66 (PSX) | Barclays | January 28, 2025

Theresa Chen:

Good afternoon everyone. My name is Theresa Chen. I'm the Midstream and Refining Analyst here at Barclays. Joining us today to discuss their midstream outlook and strategy is the Phillips 66 executive management team. With us, we have Don Baldrige, EVP of Midstream and Chemicals, and Jeff Dietert, VP of Investor Relations. Welcome.

Jeff Deitert:

Thank you.

Don Baldrige:

Thank you. Really appreciate your interest and appreciate the opportunity.

Theresa Chen:

Likewise. Before we get started, as a matter of housekeeping, if any of the listeners on the line would like to ask a question, please email me at teresa.chen@barclays.com and I will facilitate in asking the questions towards the end of our fireside chat if time allows. So maybe we kick it off with a more big picture, broader question. Phillips 66 clearly has been active in rotating and optimizing the midstream portfolio within the past year. So guys, if we fast forward 10 years and all of your plans and strategic initiatives came to fruition, what would PSX's midstream business look like in your mind?

Don Baldrige:

Sure, yeah. I'd probably start out and say, look, our vision is to be the leading integrated downstream energy provider. And you think about that, we operate in two value chains. One is our clean to crude products, which really encompasses our refining, marketing and transportation business. And then we also are in the NGL value chain, which is our wellhead-to-market midstream strategy. And where we see the business growth is primarily in that midstream NGL value chain. And so we see, from an organic standpoint, the ability to grow that in a mid-single digits CAGR out the future years. I'll have you look back from 21 to today, we've practically doubled our EBITDA in this segment. So we really had, I think, a great growth trajectory already. And if you look at just the macro fundamentals, we do expect that this part of the business to continue to be a real primary growth vehicle for Phillips 66. I hope at the end what people take away is they see us as a best in class service provider with really safe, reliable operations providing a really good value proposition for our customers as well as our shareholders.

Theresa Chen:

Got it. So with this growth in front of you, and keeping in mind the diversified nature of Phillips's assets as they exist today, what percentage of Phillips do you think the midstream segment should ideally be?

Don Baldrige:

Yeah, obviously we've been growing our midstream business, but I'd probably have you think about it as the way we look at it is not so much a segment look, but really how we think about our integrated business and think about the value chain margins that are really what are driving our investment decisions. It's driving our business strategy. So what that means is we want to make the right capital allocation, the right investment decisions that grow earnings and grow our EBITDA for the assets that we have that are across all of our value chains. So I think that's the context. Now we see the midstream growth as being a primary vehicle of growth for Phillips 66. Again, that's driven by the macro fundamentals, but also just the NGL value chain asset base that we have created over these last three, four years and really see a lot of organic backlog of opportunities that allow us to continue to grow this part of the business.

Jeff Deitert:

I might add just a couple of things, Theresa, you'll recall in 2015, we had about a billion dollars of EBITDA a in our midstream segment. And between 2016 and 2019, we really built out the Sweeny fractionators and the export facility and the pipelines feeding the Sweeny hub. In the last few years, we rolled up PSXP and DCP and now we've added the EPIC transaction, and that's increased EBITDA from 2019, it was 2 billion a year to with the EPIC transaction, we'll get to 4 billion a year annual run rate later this year. And as we think about the macro environment, the growthy part of the barrel is in NGLs and petrochemicals. And so those are our two primary growth areas.

Theresa Chen:

Makes sense. So on the NGL front specifically, the market at this point has had some time to digest the Epic transaction. Do you think there's anything over the past weeks of meetings and calls that you've had, do you think there's anything that the investment community is missing related to that transaction in particular?

Don Baldrige:

Yeah, we've actually spent quite a bit of time over the last couple of weeks at investor conferences and meeting with investors. I'd say overwhelmingly, we have had a lot of positive feedback around the transaction. I think the market really understands the industrial logic, the strategic rationale around that transaction, see how well it fits with our existing business and how complementary the asset base is. Some of the questions we've fielded are about our supply portfolio and how we think about that in context of our G&P capacity as well as the expansion around the EPIC pipeline. So I think the three things that we really highlight around those questions are one, our existing supply portfolio at Phillips 66 is long-term in nature. I think over 80% has five year plus terms. When you think about our supply portfolio, it is much larger than our existing Sand Hills capacity out of the Permian, so that drives some of the need for additional capacity as we are utilizing space on third parties.

And then when you backdrop our G&P activity, we are growing that side of the business. And so we've got existing plants today that aren't connected to our system, as well as we've got a new plant coming online this year, as well as another from a third party that's committed to us. And so it really helps support the overall acquisition and the logic with that kind of supply portfolio. And then when you factor in for where EPIC is and its expansion program, it's currently at 175,000 barrel a day going through an expansion to get to 225,000 barrels a day mid-this year, and then eventually getting to 350,000 barrels a day.

And when you think about our supply and that growth that we have that's coming online and the strength of the contract portfolio, as well as just EPIC has its own contract portfolio with high quality customers and good terms, that's really what supported the acquisition. It's what supports the expansion. One of the things that we think about is it not only fit us well from an asset base, but it fits us really well from a timing standpoint because we're in that phase of growth where this expansion capacity comes online just at the right time for us. I think the final points I'd say that folks, it really resonated with them was when you look at our combined system, we really offer, I think, a compelling value proposition for our shippers. Our customers, as well as the EPIC customers, are going to get a real broad access to the Gulf Coast. We're connected to a significant number of the fractionators along Gulf Coast, all of the operators at Mont Belvieu. So that's a great story on the NGL side.

And then when you think about the purities coming off these fractionators that we have, the EPIC, plus our system, it really creates this shuttle system of purity product flows from Corpus through Sweeny up to Mont Belvieu. So it's just a great market access that these two systems together will be able to provide.

Theresa Chen:

Okay, got it. And we're going to touch on several components of what you just mentioned, Don, but maybe on the supply of Y-Grade into your Y-Grade pipelines to begin with. So based on slide six of that EPIC presentation, there was that helpful stacked bar of how the supply is coming. There seems to be a significant amount of long-term third-party supply agreements that make up the Y-Grade flowing through Sand Hills and EPIC. This, in some ways, stands in contrast to the strategies deployed by some of your Permian NGL competitors who are rapidly expanding their G&P assets so they can control and direct the Y-Grade coming off of their own processing plants. So can you tell us a little bit more about what underlies the strategy in securing the Y-Grade volumes over the long term without owning the processing? Or do you hope to deploy more capital in building out that processing and that's how you bridge that gap? Any thoughts around that would be great.

Don Baldrige:

Sure. So you step back and you think about where we have been and where we are. So in '23, we bought in DCP, captured over $400 million of synergies through that. In 2024, we acquired Pinnacle Gas Assets, which had a gas processing plant in the Permian. And then we are in the process of expanding that facility, adding a second train that will come online this year. And when you think about that pace, I also expect probably this year we'll announce an additional Permian gas processing plant in West Texas. You add all that together, add as well as last year it was announced that we contracted for a 200 a day of processing capacity in the DJ from Western. You add all that together, I mean, we're well over a Bcf a day of processing expansion in flight since we acquired or bought in DCP in 2023. So certainly G&P growth is an important part of our strategy and we see that continuing to grow given just again, the backdrop and the opportunities that we have around our footprint.

But I'd also say that our third party supply activity, it'll always be an important part of our business. When you think about how we started Sand Hills Pipeline 10, 12 years ago, it's really a customer centric pipeline that has broad connectivity all along the Gulf Coast. Our customers, our shippers really value that access. It creates great logistics flexibility for them. And so that part of our business, I think, will continue to be strong. I'd have you think about, you look at the overall Permian Basin, I think about 40% of that processing capacity is held by parties that don't have a downstream NGL network. And so the producers behind those systems, again, they're looking for good placement for their product. That's what we offer. We continue to have real good success in contracting for those volumes. We have, like I said, a really long-term portfolio of supply. So I think both of those combined really set us up well for continuing to fill Sand Hills as well as filling in the EPIC expansion.

The other thing I think people forget sometimes is we do have a northern route of our NGL network that goes Southern Hills up through the Mid-Continent into the DJ basin, and we're restarting our Powder River NGL pipeline that goes up north all the way into Wyoming. And you think about all of that is all also connected to our Sweeny hub. All those barrels are able to flow there. It's all connected to our network. So adding that volume that comes from the north, which is primarily from our G&P plants...

Don Baldrige:

... from the north, which is primarily from our G&P plants. It really creates a strong portfolio of supply that feeds, not only our pipelines, but also our FRAC and export facility.

Theresa Chen:

Understood. I guess from a growth perspective on the pipeline piece, specifically, so since midstream competitor, MPLX, consolidated to MPC on the refining competitor side, since that entity owns a significant portion of BANGL, and BANGL ties into Epic NGL, how do you see BANGL's UJI with Epic NGL evolving over time? Specifically, as each owner contemplates expansion commensurate with growth upstream, what would that process look like?

Don Baldrige:

Yeah, I'd say Epic has had a real successful partnership with BANGL. They've been able to optimize capital, optimize capacity as they've developed the system. I think that's been a real success, a successful relationship between the two. I expect we'll continue to have opportunities post-close. With Epic, we'll continue to have opportunities to partner with BANGL, be able to continue to provide our respective customers great service. I think, MPLX has done a good job building out their Permian asset base. I think they see BANGL as likely continuing to be an important part of their midstream value chain.

We'll continue to have, at times, aligned interest on how we think about capacity development and being able to serve customers. So I'm optimistic that that's going to continue to be an advantage of having the UJI in place.

Theresa Chen:

Got it. The downstream of the FRAC... I'm sorry, of the pipe, can you tell us about the rationale behind building an additional FRAC train at Corpus, following the Epic close versus building an expansion or another train at your existing Sweeney FRAC complex?

Don Baldrige:

Yes, we are definitely in that evaluation process, thinking about where the next fractionation facility ought to be located. I think it'll be really be driven by the cost efficiencies and value creation between the two locations. I think, one, it's great to have options. Certainly, the ability to expand at Corpus was something that was interesting to us and was attractive to us as part of the Epic transaction. More to come as to how we think about sequencing and maybe what location makes the most sense next. I'd say, at Sweeney, we enjoyed a lot of synergies by continuing to add trains there, being able to take advantage of the infrastructure around there.

I think Corpus has some of that same benefit in terms of synergies because of what's currently there, the Epic has, and some of the scale that's there that we can take advantage of. So we'll take a hard look at it.

The Corpus market is a good market for additional fractionation facility. One of the things that I think is different with our ownership of Epic is just the ability of its connection with our Sweeney facility. We already have a lot of pipes that go back and forth between the facilities.

So being able to site a fractionator in Corpus, we'd still be able to take advantage of a lot of the infrastructure that we have around Sweeney, whether that be Clemens, our storage facility, or Freeport, our export facility. So more to come on that, but we certainly are excited for the potential of expanding into a Corpus as well.

Theresa Chen:

Okay. On the consideration of where that incremental train is going to be located, and to your point about utilizing some of the existing infrastructure, Don, do you think you're going to need to expand storage as well? Is there an expansion opportunity at Clemens Caverns, or would you entertain building above ground storage, which would likely come with a different set of economics if you have to build around Corpus? What are your thoughts around that?

Don Baldrige:

Yeah, I mean, our existing Clemens facility has about 16 million barrels of storage capacity. It certainly has room for expansion. It serves a lot of products already. It will probably be something that we look at in association with whether we do an export expansion or whether we think about more staging of storage in our shuttle system. I think that'll be what drives something at Clemens. But we don't see necessarily a driving need to do that on its own. It's really be whether it's complimentary to some of the other activity that we see around fractionation and export. But I mean, it's, again, a good place to have storage. It's very well-connected already with the Epic system. It's very well-connected with our downstream systems into Mont-Bellevue. So we definitely think it's an advantaged location for us, and we'll definitely grow it as we see the opportunity that unfolds.

Theresa Chen:

Okay. Then similar to the question on storage, it's just thinking about the infrastructure necessary to move that molecule further downstream. You touched upon this earlier, Don, but clearly, NGL exports in the U.S. Gulf Coast is a visible area of necessary investment going forward. Many of your peers have projects of their own to expand the export infrastructure. Do you have expansion capability at Freeport? Is that likely? Or as you're evaluating all of this, would you rather build and expand export infrastructure at Corpus Christi instead?

Don Baldrige:

Sure. Probably, to start off again, it's great to have options post-close with Epic. So we like that. I probably first just highlight at Freeport; we've been doing some pretty great expansions around Freeport just through the way we operate. The team has really, over the years, been able to extract more capacity out of that facility. So that has been a real benefit to our midstream business to be able to get more product through that facility. I do think our next page of expansion is probably more substantial in and around Freeport.

We'll definitely look at something that is probably more than just our LPG, but look at our broader integrated footprint around Sweeney and the various products that we handle. But Freeport is definitely expandable. It's something that we have folks evaluating. I do think, with Epic, we'll take a hard look at Corpus and what makes sense there from an export expansion. Currently today, there's two facilities operated by third parties that are LPG export capable. Epic is tied to one, and product flows into that one. I think Corpus is an interesting port for LPG expansion there. From an export standpoint, it's an area that's very friendly to export expansion.

I think whether we do that Greenfield or whether we do that partnering with some of the existing incumbents there, I think, you know, more to come along that line. But one of the things that, again, I think connecting the Epic system with our system that is so powerful is that with the shuttle system between our assets, the Clement storage, I think we really provide kind of a game changing setup for Corpus, for LPG exports because, again, we can use Clemens for staging and for better ship scheduling and better ship loading, whereas, you don't have a lot of storage in around Corpus for that kind of activity. So bringing our asset to the Clemens asset to bear around Corpus, will really help facilitate expansion of the LPG exports there.

I'd also say Corpus is in a great location just for export customers. It's easy access to Blue Water and it's far less congested than the Houston Ship channel. So there's some real benefits in and around Corpus and we're going to look at opportunities to take advantage of in the future.

Theresa Chen:

Okay. Maybe a follow-up, just to clarify that point a bit, so if you are streamlining operations in a more flexible way, offering more optionality to your customers, how are you seeing the economic uplift? Like, how does that commercially come to fruition? Will you be charging different fees to your customers funneling in more volumes or, you know, getting better netbacks from a marketing perspective? How does that increase midstream EBITDA as you streamline the Corpus side of things?

Don Baldrige:

I think it's some of all the above. Providing better netbacks to our producers, providing good logistical presence for our downstream customers, both domestic and international. I think all of that comes to fruition through enhanced throughput, enhanced fee, enhanced just utilization of the assets, as well as follow-on investment opportunities that we think will be accretive, and generate nice returns for our midstream segment.

Theresa Chen:

Okay. One of the competitive advantages of Phillips midstream, the offering that you have, is having CPChem as a ready, captive downstream customer. So, Don, asking you to put it on your chemicals hat for a second, can you tell us about the integration between CPChem and your midstream assets? Is there anything formal in place? Does CPChem get a first look or something similar at the purity products? If not, if the answer is no, you know, why would CPChem buy from PSX midstream versus enterprise, Targa Energy Transfer, and the like?

Don Baldrige:

Sure. I would say, CPChem, is definitely a differentiator as part of our Phillips 66 Integrated Platform. It's clearly a top performer in the PetChem space. I grimaced a little bit when you said captive. We operate with CPChem, definitely, at an arms' lengths basis in terms of how we contract for NGLs. But I'd say we have a very strong vested interest in making sure that CPChem has a robust, secure, reliable supply of feedstock. Given the operational synergies we have around Sweeney and the proximity of location as well as just our relationship, CPChem will always be a very important customer of ours.

We'll always be an important supplier to CPChem. But at times, they may have access to advantage feedstock. We might have advantage markets. We'll take advantage of those opportunities in our respective companies. At the end of the day, if that happens, we're all to benefit from that. So I think it's just important to think about that as the overall context. I think our growth with CPChem will continue to be there as they bring on their Golden Triangle project in 2026, that world-scale cracker. They're going to need more ethane.

I think we'll continue to be an important supplier to them, and they'll continue to be an important market. But I think it's a great relationship. It's working quite well, and I mean, at the end of the day, I just say we have a lot of shared vested interest and alignment in how we operate.

Theresa Chen:

Okay. If I can just clarify your comments or ask a question for clarification, so since they're not a captive customer, then is it fair to say there's no formal agreement in place? You compete fairly independently with...

Theresa Chen:

... Agreement in place, you compete fairly and independently with any other third-party midstream entity?

Don Baldrige:

100%. I mean, we contract independently, so that is a very fair representation that you just laid out. But again, we have very aligned interests, but we contract, for sure, we contract independently.

Theresa Chen:

Understood. And using your analogy, Don of the shuttle system on the purity product side, we all kind of understand the integrated NGL offering, gathering to processing, long-haul transportation, storage fractionation, all the way to export. On the purity product pipelines that you have in the Gulf Coast, can you just tell us a little bit more about this system and how that offers a competitive advantage to your assets?

Don Baldrige:

Yeah, I mean, I think you take a step back. I think we're pretty unique in that we are both in the NGL value chain as well as accrued to clean products value chain, and that breadth of operation, that scale really enables us to offer, I think a robust service to our customers. We're able to really stand beyond just the Gulf Coast. You think about our global scale with where we have trading offices in Singapore, London, Calgary, and Houston, the commodity logistics business that we're able to provide really captures a lot of opportunities that are multi-commodity in context and be able to bring to bear all the assets that we operate within the Gulf Coast.

And then you factor in the global presence that Phillips has. We're very active in the marine logistics, that enables us to really talk to customers on a global basis about multi-commodity deliveries. We can help customers get through bottlenecks, help improve netbacks deliver prices. I think that's a differentiator that Phillips 66 brings to bear as an integrated energy company that has such a strong refining presence as well as the NGL value chain that we have around Sweeney and the rest of the midstream assets. That's really where we see a lot of opportunities. That's what's driving I think a lot of the organic opportunities that we're going after is what gives certainly me a lot of confidence and a lot of excitement as to what the future holds.

Theresa Chen:

Okay. In addition to the integration and the diversified nature of your assets through multiple commodity value chains, since you are investing in the NGL portion, the Permian supply push NGL portion in particular, what else does your midstream business offer the customers at the wellhead as you're competing for those incremental molecules that your competitors do not?

Don Baldrige:

Sure. I mean, I think about it as there's really only three other companies like us that have this wellhead to market capability from gathering and processing through the pipeline, through fractionation and export. And I think what we bring to bear is a really strong access of capacity and throughput, reliability for our customers. Surety of flow is very important with our customers and the way we can partner with our customers. Again, the broad market that we are playing in, which is not only in the NGL value chain but also the crude to clean products. There's just a lot of touch points that we have with our customers that are across a broader array than just NGL. And so I think that's where we have opportunities to partner with customers to bring, I think, good win-win solutions that we're getting a lot of opportunities, a lot of discussions around.

Theresa Chen:

Got it. And maybe just to follow up on that, operating in multiple portions of the value chain and having the refining footprint as a demand center for those crude barrels, do you bundle your services? I mean, if you ask a producer to move their molecules with you on the Y-grade front, can you also offer some sort of commercial offtake for their crude barrels at Sweeney and Lake Charles for example? Is that how it works or are they completely different independent processes?

Don Baldrige:

Sure. You think about how we're organized at Philips, we have one large commercial group that really spans across all the commodities. So we are able to talk to customers about a broad breadth of commodity services and where it makes sense and where the customer has interest and where we have capability, those are definitely conversations and opportunities that we execute on and will continue I think, to grow as we really start to build out this midstream platform. I think those are the types of opportunities that are going to continue to grow not only here within the US, but also just globally. The conversations and the activity that we're having overseas I think will continue to be something that's of interest and will yield some really nice benefits for our business.

Theresa Chen:

Got it. So looking at your asset composition within midstream at this point, 2024 was not only a busy year of midstream acquisitions, but also divestitures. You still have a considerable amount of what I will call less strategic, maybe less strategic midstream assets in your portfolio, minority interest in a variety of liquid pipelines, for example. So can you just help us think about what inning are you in as far as your midstream asset divestiture program goes? Do you anticipate much more to come? Are you pretty much done based on the prevailing bid-ask spreads that you see today?

Don Baldrige:

I mean, I certainly wouldn't characterize us as being done. I think what I would probably have you think about is we continually evaluate our portfolio of assets, thinking about the degree of fit with our strategy and business opportunity. As we go through that process, assets that are not as core, that don't have as great a strategic fit, we certainly look at them as candidates for divestiture, but it also comes to timing. When's the right opportunity, the right valuation to execute on those divestiture opportunities? I think there's certainly more that we can do there and we'll continue to evaluate that as we go forward. But I think as you saw, we'd announced a target of $3 billion of divestitures.

We've had a tremendous amount of success over the last year and a half executing on that. I think we'll continue to have a real keen eye as to, hey, what fits in the portfolio and what doesn't? Being able to bring that capital back and redeploy it in beneficial ways is something that I think is just a continuous process that we'll have. I think it's a healthy process. So I wouldn't characterize it as certainly not as done. And from an inning standpoint, I think it's just a continuous process that we will be under.

Theresa Chen:

Okay, got it. So as we think about the Phillips 66, some of the parts valuation, I think it's generally speaking, important to delineate between affiliate source revenues versus true third-party payments. At this point, thinking about the different components within midstream itself, pipeline transportation, NGLs and such, what proportion of your midstream EBITDA or EBIT today consists of third-party customer payments versus Phillips's refining or M&S segments paying midstream?

Don Baldrige:

Sure. I think if you look at our midstream disclosure, we break that up into two kind of sub-segments, the transportation and logistics and our NGLs. And I think an easy way to think about it is our NGL sub-segment underneath midstream, that's almost entirely a hundred percent third-party activity. And then if you think about our transportation and logistics side, that has a much higher percentage of Phillips 66 affiliate activity, probably in the order of magnitude 70, 80%. And you think about the relative size between those two, I think we've been tracking our NGLs probably two-thirds.

Our transportation logistics are about a third of EBITDA. You kind of go through that math. It's pretty easy where you can get to about 70% of our midstream or so business is third-party type business as opposed to Phillips 66 affiliate business around our refineries. That's obviously grown tremendously over the last several years as we've brought in DCP and continue to grow on the NGL side of the midstream segment, I think that you can probably assume that that'll continue to grow at a faster clip than our transportation and logistics side. So that waiting will continue just to increase from a third-party versus a Phillips 66 affiliate.

Theresa Chen:

Okay, great. So I am going to filter through some of the client questions at this point. The first one kind of goes back to what we discussed earlier about having long-term third-party supply agreements as a conduit for Y-grade. To feed your long-haul Y-grade transportation versus G&P, the physical processing plants. So the question goes, why wouldn't third-party customers go to EPD, ET, Targa given that they're expanding export capacity versus more limited space at Freeport and would need further expansion. So as far as ultimate deliverability goes and the ability to put that molecule across the water, can you maybe educate us on where you stand versus your competitors and how your mousetrap competes with theirs from a soup to nuts perspective?

Don Baldrige:

Sure. I think maybe the context to have is you look at our supply portfolio, again, we've got long-term contracts that feed into that system. We are going to continue to grow our G&P presence. So you're going to see a shift over time where G&P becomes a larger supply of our NGLs. But you think about just the tenor and term of our portfolio, we're still able and continue to attract additional volumes, new contracts, but we still have a solid base that really supports the expansions that we're looking at on EPIC from a transportation standpoint and then also from a frack and export standpoint.

So as we contract additional volumes, I think where we see the opportunities is just further expansion opportunities downstream greater than what we already have today. I mean, what we're doing today is really geared toward the growth that we have that's already under contract. And we see as we look at opportunities to expand from an export standpoint and from a frack, we'll definitely reach into the market for additional supply opportunities. I think we compete quite well with our peer midstream companies from a service offering, from a reliability, from a cost to service, so very comfortable with where we stand and excited for I think what we provide with the kit that we've put together.

Theresa Chen:

Got it. Next question has to do with build multiples and evaluation of organic build-

Theresa Chen:

... Multiples and evaluation of organic build versus some of the acquisitions that you made. So when evaluating the Epic transaction, did you also look at looping Sand Hills and building just another frack on your own? What would those economics have looked like versus the Epic transaction?

Don Baldrige:

Yes, and I would say that our base case is definitely an organic build opportunity. And so when we think about acquisitions, really the filter we go through is it accretive to our return on capital employed within Midstream against our current plan of self-build? And that's obviously a high screen. And what tends to play out with Pinnacle and now Epic is the acquisitions that make sense for us are ones that we can bring in-house, capture synergies, but also have a real follow-on growth capability that is a real improvement to the overall economics.

And so that's what drives these last couple of acquisitions for us is that we can acquire and expand these assets in an accretive manner compared to what some of the alternatives would be, like a complete loop of Sand Hills. Those are definitely the evaluative process that we go through.

So very good question, and that's how we think about acquisitions; it's got to be better than what our organic opportunity is.

Theresa Chen:

Okay.

Another question about the acquisition thought process from a different angle. So upstream growing G&P, would you grow G&P primarily through M&A given the acreage dedications and the, I guess if I'm paraphrasing correctly, higher hurdle in moving those dedications over if you were to build organically in certain areas?

Don Baldrige:

Yeah, I think about our growth plan within Midstream, and even specifically around gathering and processing, I mean, again, I think we see a pretty clear line of sight of being able to grow our business organically at that kind of mid-single digit CAGR on an annual basis.

That is because we do have already such a big footprint from a G&P standpoint with a lot of good acreage and a lot of good connectivity. We offload a fair amount of gas to process through third parties. As we build out additional gas processing plants, we bring in that gas into our new plants. We really believe our contract base and where our footprint is, it affords us the ability, again, probably to be on pace of building an expansion gas plant basically on an annual basis within the Permian for the next several years.

So acquisitions, I think we'll definitely take a look. It's a high hurdle. It's got to be better than or it's got to be accretive to what our existing growth strategy is. But we feel like within our own control we have a good line of sight of organically developing our gathering and processing capacity there in the Permian. So comfortable with where we stand. Certainly we'll take a look at acquisition opportunities. We always do. It's a high hurdle, but if it makes sense, we'll pursue further.

Theresa Chen:

Great.

Okay. Another question related to this. So if there's no more M&A, based on your base assets today and the organic plans you have in place, what percentage of your Y-grade volumes do you expect to come from your own processing plants over the next three to five years?

Don Baldrige:

Yeah, I mean, if you look at where we are as our total company portfolio, about 60% of our Y-grade supply comes from our own gathering and processing assets. And that's system-wide.

If you look at just the Permian, which I think is where a lot of the questions and the focus is, that's probably about 35% today. We see that just through organic growth, that getting to a 50/50 type ratio here by the end of the 2020s, if you will. So over the next kind of four years, we expect that shift in the ratio between third party supply and our own G&P plant production.

Theresa Chen:

Right.

And I know that we touched upon the supply agreements going through your pipelines, and there's seemingly, to your earlier points, Don, of incremental processing, processing changing hands, a lot of volumes up for grabs over the next few years.

Don Baldrige:

Yeah.

Theresa Chen:

Can you maybe give us some sense of what the re-contracting looks like on your Y-grade pipelines over the next five years pro-forma for Epic?

Don Baldrige:

Yeah, I mean, we feel ... If you think about our portfolio, like I said, about 80% of our supply portfolio has terms that are beyond five years. So we don't have a lot of re-contracting exposure over the next five years. We see obviously there's a lot of opportunities to go get incremental barrels because there are just a lot of RFPs, if you will, out there, a lot of activity. We think we're going to get our fair share of those re-contracting supply. But as I look at our portfolio, those are much more accretive to our existing supply than say rolling off volumes. We just don't have a supply portfolio that has, here in the near term, a lot of volume that rolls off from a term standpoint. We're in really good shape from that perspective.

Theresa Chen:

Great.

And looking at the broader Midstream segment, can you tell us what proportion is truly fee-based at this point versus more commodity exposed?

And maybe if I can put a finer point to this question. I imagine your transportation and logistics is going to be largely fee-based; within the NGL business, how much is fee-based versus POP or keep whole and some of the legacy contracts? And I imagine whether it be pipe or frack or export, that is also fee-based. So if you can just help us think about where the commodity exposure lies, that'd be great.

Don Baldrige:

Yeah, if you look at our Midstream segment, about 80% of our earnings is fee-based. That's why we have such a high level of comfort with how secure and stable that earnings profile is within the Phillips 66 portfolio. So that's an order of magnitude from a fee versus commodity exposure.

Jeff Deitert:

And Teresa, you're aware of this, but we've got sensitivities available if people want to look at the impact of crude natural gas and NGL pricing. I know you're aware of that, but for everybody's benefit.

Theresa Chen:

Absolutely.

And Don, to your earlier point about overseas opportunities, can you just expound a little bit more about that, what that means for Phillips 66 from a Midstream perspective?

Don Baldrige:

Sure. You think about the activity that Phillips 66 has already from a global standpoint; already moving a lot of clean product, crude, just a lot of activity and capability in terms of time charters, moving product on ships ourselves. And so how that translates then into the Midstream space is when we look at our freeport export facility, there's a good portion of that portfolio or a good portion of that capacity that we just sell across the dock, but we also take and have the capability of taking product onto ships and actually offering a delivered service and being able to deliver product to our customers in Southeast Asia.

By doing that, that creates just a lot of follow-on opportunities, whether it be redirecting volumes based on the opportunity set on a spot basis; whether that brings to bear bundled commodity services where a lot of our customers look at not only importing LPGs, but other products that we manage and have logistics capabilities.

So I think that's a bit of the differentiator that Phillips 66 brings to bear with our Midstream platform; something that I think from a opportunity set continues to grow. As you think about all the incremental production that comes out of the US, it really needs to hit the water, it really needs to go to international customers, we're very well situated to play and be an active participant in delivering those products to our overseas customers. So really see that as continuing to be a growth opportunity for us.

Theresa Chen:

And just to clarify, that activity marketing to overseas customers, is that cashflow living within the Midstream segment or is that within the marketing segment, but utilizing synergies across Midstream assets to further that activity?

Don Baldrige:

That activity flows into Midstream. We have a commercial group that manages a lot of this activity, but that activity really goes to the other business segments. So that activity will flow into Midstream earnings.

Theresa Chen:

Okay, perfect.

I have received a number of questions on capital allocation, on dividends, on leverage. Clients, I hear you, but we are going to defer those questions to Friday for the earnings call.

Don Baldrige:

A few days. Just a few days.

Theresa Chen:

Indeed.

Thank you both so much for joining us and for all the color and insights. Really appreciate it. Thank you.

Jeff Deitert:

All right.

Don Baldrige:

Thank you, Teresa.

Jeff Deitert:

Thanks, Teresa.

Don Baldrige:

Thank you.