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Earnings Call

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Call Participants

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Donald A. Baldridge
Executive Vice President of Midstream & Chemicals

Kevin J. Mitchell
Executive VP & CFO

Mark E. Lashier
CEO & Chairman

Richard G. Harbison
Executive Vice President of Refining

Sean M. Maher
VP of Investor Relations & Chief Economist

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Jason Daniel Gabelman
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Presentation

Operator

Welcome to the Second Quarter 2026 Phillips 66 Earnings Conference Call. My name is Hillary, and I will be your operator for today's call. [Operator Instructions] Please note that this conference is being recorded.

I will now turn the call over to Sean Maher, Vice President, Investor Relations and Chief Economist. Sean, you may begin.

Sean M. Maher
VP of Investor Relations & Chief Economist

Hello, everyone. Good morning, and thank you for joining Phillips 66 Second Quarter 2026 Earnings Conference Call. Participants on today's call will include Mark Lashier, Chairman and CEO; Kevin Mitchell, CFO; Don Baldridge, Midstream and Chemicals; Rich Harbison, Refining; and Brian Mandell, Marketing, Commercial and Renewable fuels. Today's presentation can be found on the Investor Relations section of the Phillips 66 website, along with supplemental financial and operating information.

Slide 2 contains our safe harbor statement. We will be making forward-looking statements during today's call. Actual results may differ materially from today's comments. Factors that could cause actual results to differ are included here as well as in our SEC filings.

With that, I'll turn the call over to Mark.

Mark E. Lashier
CEO & Chairman

Thank you, Sean. This quarter's operating results reflect the dedication and work that our teams have delivered throughout the company's transformation over these past several years. Our system is operating well. Our assets are well positioned and the market environment is constructive. While there's more work to do, we believe our organization's earning power is becoming clear as we continue to drive execution and return capital to shareholders.

Safety, reliability and operational excellence remain at the center of everything we do. We recently earned industry recognition for exemplary safety performance in Midstream, Refining and Chemicals. Due to our steadfast focus on reliability, our integrated businesses are available to supply U.S. and global energy needs. At Phillips 66, operational excellence is foundational. We remain focused on disciplined execution and continuous improvement.

Our Midstream business continues to execute on its growth plan as expected. Over the past 2 years, we've increased fractionation capacity to over 1 million barrels per day and achieved greater than 100% average frac utilization. During the quarter, we also achieved record LPG export volumes. Our complete wellhead to market system allows us to move products across our integrated value chain and offers customers valuable optionality and global access.

In Refining, our deliberate focus on operational improvement continues to deliver results. We have enhanced the portfolio, increased clean product yield, improved our cost structure, led the industry in utilization and increased our nameplate capacity. Supported by a strong contribution from our commercial organization, we captured 98% of our market indicator in the second quarter.

In Renewables, we have scale, flexibility and strong operations at one of the largest renewable diesel facilities in the world. As the uncertainty over renewable credit regulations unfolded in 2025, we engaged constructively with state and federal regulators and continue to do so. We also focused on taking costs out of the system and improving reliability and flexibility. To that end, we ran above nameplate capacity during the quarter.

In Chemicals, our industry-leading position is clear. These are advantaged assets positioned at the low end of the feedstock cost curve. Across all of our businesses, we continue to raise the bar. Make no mistake, we must compete every day. Our teams continue to find new ways to maximize value through improving operations, increasing yields, expanding margins and lowering costs.

Moving to Slide 4. We process low-cost hydrocarbons from the U.S., Canada and Latin America and turn them into higher-value usable products for customers. As global supply and demand dynamics become more complex, our integrated model positions us for long-term value creation. We are investing for the next decade, not just the next quarter.

The Midstream and Marketing and Specialties businesses deliver reliable cash flows while Refining, Chemicals and Renewables generate attractive incremental returns with commodity upside. We've built an integrated North America infrastructure system. We'll continue to focus on being the best in every segment of our portfolio, all while maximizing shareholder returns. That's what makes Phillips 66 unique. We have a resilient business model, advantaged assets, strong commercial capabilities and significant earnings potential.

Now I'll turn the call over to Kevin as we move to Slide 5.

Kevin J. Mitchell
Executive VP & CFO

Thank you, Mark. Last year, we committed to reduce total debt to $17 billion by year-end 2027 and to return greater than 50% of net operating cash flow, excluding working capital to shareholders. Our focus on these priorities has not wavered, and we expect to deliver on our debt commitment ahead of schedule.

In the second quarter, we made significant progress on strengthening the balance sheet. We ended the quarter with total debt of $20.6 billion and net debt of $16.5 billion. This positions us better than where we started the year. And using current consensus estimates, we expect net debt to be less than $16 billion by the end of this year.

We expect to achieve our debt target, while also returning greater than 50% of net operating cash flow to shareholders through dividends and share repurchases. This is a core strategic priority, and we expect to increase share repurchases in the second half of this year.

Our disciplined capital allocation framework allows us to enhance our shareholder value proposition. We remain committed to a secure, competitive and growing dividend and to creating value for our stakeholders through disciplined capital investment, dividends, share repurchases and debt reduction.

On Slide 6, second quarter reported and adjusted earnings were $3.8 billion. Reported and adjusted earnings per share were $9.55 and $9.41, respectively. The company's second quarter financial results were impacted by mark-to-market gains of approximately 50% of the first quarter mark-to-market losses.

Operating cash flow, excluding working capital, was $4.3 billion. Capital spending for the quarter was $726 million. We returned $887 million to shareholders, including $379 million of share repurchases and $508 million of dividend payments.

I will now cover the segment results on Slide 7. Total company adjusted earnings were $3.8 billion. Midstream results increased mainly due to higher margins as well as higher volumes, largely driven by the absence of last quarter's Winter Storm Fern impacts.

In Chemicals, results increased mainly due to higher polyethylene margins driven by higher sales prices.

Refining results increased mainly due to higher realized margins driven by an increase in market crack spreads.

Marketing and Specialties results increased mainly due to higher global marketing margins.

In Renewable Fuels, results increased mainly due to higher regulatory credits from higher pricing and renewable fuels production. Also included in the results are approximately $450 million of favorable mark-to-market impacts in the Refining, Marketing and Specialties and Renewable Fuel segments.

In Corporate and Other, the pretax loss decreased primarily due to lower net interest expense and employee-related costs.

Slide 8 shows cash flow for the quarter. We started the quarter with a $5.2 billion cash balance. Cash from operations, excluding working capital, was $4.3 billion. There was a $2.9 billion working capital benefit due to a reduction in inventory as well as the timing of tax payments. Total debt reduced significantly during the quarter as we paid off all outstanding commercial paper and repaid $1 billion of the March 2027 term loan. The remaining $1.25 billion balance on the term loan was paid off in July. We ended the quarter with $4.1 billion in cash and $6.4 billion in committed capacity, giving us total committed liquidity of $10.5 billion.

Looking ahead to the third quarter on Slide 9. In Chemicals, we expect the global O&P utilization rate to be in the low 90s. In Refining, we expect the worldwide crude utilization rate to be in the mid-90s. Turnaround expense is expected to be between $100 million and $120 million. We anticipate Corporate and Other costs to be between $325 million and $350 million.

Moving to Slide 10. Mark will now provide some final thoughts. We will then open the line for questions.

Mark E. Lashier
CEO & Chairman

Volatility in the first half of the year created both challenges and opportunities, and our team was prepared, agile and focused on execution. This enabled us to navigate the market and capture value through strong Refining performance, disciplined Midstream growth and flexible, opportunistic commercial execution across our portfolio. Looking ahead, the macro environment remains constructive. We are focused on continuous operating improvement, and our people are helping drive that progress as they leverage the advantages of our asset footprint.
In any market, including this one, we will continue to maintain capital discipline and stay focused on the balance sheet while pursuing meaningful opportunities to drive long-term value. Our integrated model, together with our employees, provides resilience and opportunity, positioning us to manage through volatility and capture the benefits of a strengthening macro environment for shareholders.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Steve Richardson from Evercore.

Stephen I. Richardson
Evercore ISI Institutional Equities, Research Division

Mark, I was wondering if you could talk a little bit about the environment and what you're seeing. The last time, Refining profitability was at this level for you and the industry was 2022. And I wonder if you could talk a little bit about what you're seeing versus that time. What the path to normalization looks like, if that's even possible to kind of envision at this point? And then how is Phillips 66 differentially positioned versus that time would also be helpful.

Mark E. Lashier
CEO & Chairman

Yes, Steve, that's a great question. When you think back to 2022 versus today, there are really a couple of major differences. You think about 2022, there was a demand surge coming out of COVID. Right about the time when the entire refining complex was getting its act back together, recovering from COVID, we were reluctant to take shutdowns. We were reluctant to do all the maintenance we needed to do during COVID for fear of an outbreak, and we had to catch up. And so those 2 things collided in 2022. And it's different than today because the resolution of those 2 things happened more quickly.

Everyone got their maintenance completed. Actually took advantage of the run-up in margins to make the investments they needed to be more robust and the demand normalized a bit. And now when you look at what's going on, it's more of a supply shock than a demand shock. You've had significant refining capacity off-line and stocks are low. And so we see it taking a lot longer for that situation to normalize than what we saw in 2022.

But the second piece of the story is Phillips 66. We're a very different company than we were in 2022. A big part of it during the business transformation, our culture evolved pretty dramatically. And we are a leaner company, we're more agile and more focused on continuous improvement in competition. We're embracing AI out at the front line level. We're doing a lot of things that are AI-enabled. So it's really enhanced how we respond to the market and how we do things.

Refining has dramatically improved its performance. We've streamlined the portfolio. We've added capacity by rolling up WRB. And Rich and his spokes have cut over $1, headed towards $1.50 per barrel of cost of the Refining. And in the meantime, while we're cutting costs, we've been improving yields and improving utilizations. Underlying that, the Midstream portfolio is now a wellhead to market strategy fully in place and it's been growing. And so we've got a lot of strengths there and a great foundation. So the company is focused on driving and leaning into that integration value, focus on general interest, not just our functional earnings.

And I would say that Phillips is positioned better than ever to successfully execute in this in any environment. And the headline should be that at this point in time, this is the case where preparation meets opportunity, and we're delivering.

Stephen I. Richardson
Evercore ISI Institutional Equities, Research Division

That's great. I'd love to follow up just a little bit more if we could on commercial. Could you give us a sense of incrementally at least in the quarter and year-to-date what -- how the commercial teams are attacking this environment in terms of refining, anything incrementally on freight, transport, crude sourcing, the entire value chain would be helpful from a commercial perspective.

Brian M. Mandell

Executive Vice President of Marketing & Commercial

Thanks, Steve. This is Brian. Appreciate the question on commercial. Maybe I'll start by saying I'm incredibly proud of the commercial team, particularly through this period of historical volatility. The team has done an excellent job. And for P66, commercial is kind of a key source of optimization value because it connects our physical assets to market dislocations and opportunities around the world.

As you know, we have 6 global offices. The organization optimizes feedstocks, moves products into the highest value markets and also captures value from optionality from arbitrage, captures value from market structure opportunities as well. And our model at Phillips is an asset-backed model, which means we use our physical footprint. We use our logistics capabilities and integration and our market access to capture value when markets dislocate.

So maybe just to give you some examples. In today's market, we can substitute lower-cost domestic grades for more expensive international grades in our U.S. refining system and then sell those more expensive international grades at a profit. Or as you talked about on freight, our time charter freight position has given us a lot of optionality in tight logistics markets. We've expanded our fleet fourfold in the past 2 years. And now it supports roughly 40% of our asset-backed demand while also generating a new third-party business.

And then Jones Act is another example of how commercial creates value. We've been granted about 20% of the Jones Act waivers issued since the current waiver took effect in March. And combined with our freight position, these waivers have improved our ability to optimize feedstock and product flows from our Refining business, Marketing business and Midstream businesses.

And then finally, as a result of our time charter fleet growth and increased Panama Canal transits, we now hold a favorable canal ranking. You haven't heard a lot of people talk about this. We're 26 out of 556, which allows us to schedule transits well in advance, avoid high auction fees and reduce waiting times and improve on-time reliability. So ultimately, I'd sum up by saying commercial is focused on creating value across our integrated businesses by capturing the embedded optionality within and across the system.

Operator

Your next question comes from the line of Doug Leggate from Wolfe Re -- pardon me, from Wolfe Research.

Douglas George Blyth Leggate
Wolfe Research, LLC

These are probably for Kevin. I apologize in advance. But Kevin, the step down in your net debt this quarter takes your net debt at least below your $17 billion total debt target. Now you've got line of sight to the end of the year. Previously, you justified this on a multiple of, call it, stable EBITDA. But I think whether you agree with elevated margins or not, elevated free cash flow currently, it seems to us that you've got an opportunity to reset that net debt target or that debt target substantially lower. So that's my question. What -- where do we go after the end of 2027 and maybe even before then?

Then my follow-up very quickly is to Mark. You've had this 50% or more than 50% of operating cash flow target return to shareholders for a while. But there's 2 pieces to that, Mark. There's the buyback always at risk of being procyclical and there's a dividend. So how do you think about this debate of whatever mid-cycle and whatever Phillips 66 owned free cash flow potential might be going forward? What's the right dividend strategy for Phillips as you fulfill, for example, your Midstream growth and so on? And I'll leave it there.

Kevin J. Mitchell
Executive VP & CFO

Yes, Doug. So you're exactly right in terms of where we were on debt target. And I will reiterate the $17 billion debt target that we had was a good target. We had sound logic for how we developed that, and it was a sub-3x multiple on the Midstream and M&S EBITDA that can comfortably support that debt level. But I do agree with you that in a period of strong cash generation, like we are in right now, we have the opportunity to go lower than that. $16.5 billion at the end of the second quarter, I expect that to go down between now and the end of the year.

And so on a net debt level, I think of a next sort of target is something around about $13.5 billion, which would equate to a $15 billion or thereabouts balance sheet debt number. I don't want to reset the target in absolute debt level terms just because we're also restricted by the -- or impacted by the maturity schedule of the debt we have out there. And what I'm not going to do is make uneconomic decisions to retire debt early. So we'll manage that as best we can. But from a net debt standpoint, I think in terms of this sort of $13.5 billion to $14 billion as an appropriate next target that is certainly achievable based on the kind of environment that we're looking at right now.

Mark E. Lashier
CEO & Chairman

Yes, Doug, your second question, I think that I'd take you back to 2022, we made some pretty aggressive commitments to deliver returns to shareholders. We set our 50% target, but we also committed to dramatically improve Refining performance to roll up DCP and create a wellhead to market presence and to improve Refining, grow Refining, grow Midstream, all of those things required us to use the balance sheet as a tool along with asset sales. And if you look at what we did quite effectively over that time frame, it really positioned us to excel today when the macro is favorable. And so the payoff is that we're going to be able to lean into both share repurchases and debt reduction. And the share repurchases will allow us to keep pace with our dividend increases even more dramatically. So we'll be taking a close look at that and having conversations with our Board how best to go forward there.

Douglas George Blyth Leggate
Wolfe Research, LLC

Does anyone would think you were an oil major, Mark?

Mark E. Lashier
CEO & Chairman

Thank you, Doug.

Operator

Your next question comes from the line of Manav Gupta from UBS.

Manav Gupta
UBS Investment Bank, Research Division

Congrats on a strong quarter. I was wondering if I could do some quick maths with you. Your guidance for year-end run rate Midstream EBITDA is about $4.5 billion for 2027 year-end. If you take out the tax and interest expenses, it's about $3.3 billion in free cash that, that business generates. Now that number strikes us because that's exactly your dividend burden plus your sustaining CapEx. So what I'm trying to understand is, once you are at this $4.5 billion run rate EBITDA, can your Midstream fully support your sustaining CapEx for the full company and the dividend burden? And what I'm trying to get to is if that grows at like mid-single digits, the Midstream business from these projects that you're announcing, would that mean that Midstream could then support like a 4% to 5% dividend growth just on its own? If you could talk about some of those dynamics.

Mark E. Lashier
CEO & Chairman

Manav, first of all, you're quite good at math, and we appreciate you doing that for everyone. You're absolutely right. That's why we like the Midstream business. We think of the Midstream business as the foundation under our fortress of the rest of our portfolio that Midstream along with Marketing and Specialties provides that consistent cash generation to cover the sustaining capital and the dividends. And today, a significant portion of our interest expense, and we see that only getting better. And absolutely, as you look forward, that will contribute to our ability to drive that competitive growing and sustainable dividend.

Manav Gupta
UBS Investment Bank, Research Division

Perfect. My quick follow-up here is your partner was indicating that you are very close to the FID of Western Gateway. So I wanted to understand the benefits of that project, if you could reiterate? And should we expect FID sooner than later because it does add in a big way to your Midstream backlog when it does FID?

Donald A. Baldridge
Executive Vice President of Midstream & Chemicals

Manav, this is Don. I appreciate the Western Gateway question. We do expect that we would be able to FID the Western Gateway project here in a month or so. We are finalizing the definitive documents and finishing up the details around scope and ensuring we have a solid project execution plan. So with a summer FID, what we would expect is to be able to deliver reliable, secure fuel from the Mid-Continent to the Western U.S. by the latter part of 2029. We think that's a tremendous benefit to the market in the Western U.S., where the need for reliable, secure supply coming from the Mid-Continent of the U.S. will be a benefit. It's a great addition to the market. It will help the Mid-Continent set up as well. So I think as we've talked about, it's the right project at the right time. It will generate the right returns for Phillips 66. So very excited to advance the project and looking forward to its completion.

Operator

Your next question comes from the line of Justin Jenkins from Raymond James.

Justin Scott Jenkins
Raymond James & Associates, Inc., Research Division

I'd like to start maybe on the line of Steve's first question on Refining. Obviously, the macro has been incredibly favorable, but you've seen pretty solid capture rate momentum for a few quarters now. Mark, you touched on some of the internal drivers of that in your first answer, but how much more running room do we have with both self-help and maybe some quick hit projects in Refining to drive even more momentum here?

Mark E. Lashier
CEO & Chairman

Yes. Rich has a long list of self-help and quick hits. We're looking for high-return, quick-payout projects, but he can run through that with you.

Richard G. Harbison
Executive Vice President of Refining

Justin, thanks for the question. And we've obviously been on a journey here for a couple of years on this particular subject. And that's really around growing our ability to capture the marketplace and be flexible in the marketplace and also controlling what we can control. That's the other part of this. So we've been keenly focused on molecule management inside of the fence. And then maybe after this, I'll turn it over to Brian a little bit, and he can talk about outside of the fence parts that we're doing to stabilize and lock in a high market capture rate for the assets.

Inside the fence, we've done a series of actions. One, one is we've taken the time to evaluate every key process unit we have and look for opportunities to better manage the molecules inside of those. And that process has been completed. It was a very detailed exercise, and it has come up with a number of good opportunities that we have implemented or will be continuing to implement, which will improve the molecule management across the system.

The other thing we've done as well is we've increased our -- restructured our organization. And the purpose of the restructure was really to focus key parts of the organization on key success points inside the operation of the plant and avoid distractions and really just focus that organization on achieving world-class operations.

And then, of course, as you indicated, we've done a number of small capital projects as well. And these projects have very high returns on a very low capital base. And maybe just a couple of those, I'll rattle off here, and there's many of them. So I won't be able to touch on all of them, but one project we've got active right now, and it's due to start up next year is a low sulfur gasoline project at the Humber facility. And that's very timely actually for us as we've also picked up the Prax assets there, which provide great logistics for us, enhanced logistics to reach the inner markets of the U.K. and the London market. So the timing of those 2 asset purchase as well as the project is very good.

We see some opportunities at the Ferndale facility as well. There's a project to increase jet production. It's a 2-phase project. We'll actually get first phase done this year. Second phase will finish up next year. And once that second phase is finished up, that will actually produce about 12,000 barrels a day of jet fuel out of the Ferndale facility. And Ferndale is also producing CARB gasoline as well. So it's become a nice point for us to pick up supply to bring into the California market from the West Coast, supported by a number of activities that Brian is doing. And maybe that's a good bridge over to Brian here, and you can talk about outside of the fence, what we're doing to harden the capture rate.

Brian M. Mandell
Executive Vice President of Marketing & Commercial

Sure. Justin, maybe you've given me a chance to talk about our value chain optimization team because that's a core team that kind of looks at opportunities to drive market capture. They maximize profitability across regions, across segments and across our integrated value chains as opposed to just looking at individual assets. And we were an early adopter of the VCO model, and we continue to strengthen the team. And they use data-driven decision-making, clear accountability and look for execution to drive this kind of market capture.

And so I'll just give you some examples of kind of what the team has been working on and some of the things they've been doing. A relentless focus on lowering feedstock costs to improve market capture, including building a leading position in advantaged crudes, such as Canadian crude, PMI fuel oil and now becoming the third largest buyer of Venezuelan crude worldwide. They've utilized our marine time charter fleet in conjunction with the Jones Act waiver to substitute foreign crudes with WTI-based crudes at our Bayway Refinery and that helped mitigate the impact of Middle East conflict. And then while continuing to maintain strong crude utilization, VCO also has strengthened integration across intermediate feedstock activity and refinery execution, enabling us higher confidence decisions to optimize intermediate purchases and drove record high secondary unit utilization in 2Q.

And then finally, the team increased along with our refinery brethren, increased the distillate production by approximately 35,000 barrels a day in Q2. So all these examples demonstrate VCO's ability to translate market opportunities into commercial, operational and financial results.

Operator

Your next question comes from the line of Arun Jayaram from JPMorgan Securities LLC.

Arun Jayaram
JPMorgan Chase & Co, Research Division

I wanted to see if we could get a little bit of an update on your 2027 strategic priorities. You guys highlighted thoughts on shareholder returns and the balance sheet. But I wanted to see if you could maybe update us on your goal to reduce your operating costs by $500 million as well as the $1 billion growth in mid-cycle Midstream and Chemicals earnings power.

Richard G. Harbison
Executive Vice President of Refining

This is Rich. I'll start with the Refining part of the 2027 goal. And that goal in Refining is to target an annualized $5.50 a barrel operating cost ex turnarounds. And as you can see in the second quarter here, we came in at $5.57, pretty close, pretty striking -- within striking range of the $5.50 number. But the annualized number is really what we're targeting, and that's what we want to -- our goal is to achieve next year.

So with that, what are we doing to achieve that and hit that annual goal. And this will incorporate the volume impacts associated with turnarounds and all the seasonal changes and still achieve the $5.50 assuming a $3 MMBtu of Henry Hub price.

So the project -- the organization is working on over 200 initiatives, targeting operating expense reduction. And these are really focused in a couple of areas. One is energy efficiency. And I'm often asked, "Well, give me an example of that." And the 2 examples that come to mind here that I recently saw were at our Bayway facility. We operate very large boilers there, especially associated with the FCC. And they've come up with a unique process to clean the tubes and make the boiler much more efficient through the run while it's online.

And the second one is a heat recovery project, a nice project for Ferndale Refinery. Each of those 2 projects reduced operating expense by over $1 million a year independent of each other, right? So these are fantastic projects that the organization has been coming up with and working and executing.

We're also trying to simplify our work processes out there and eliminate waste and other things that we got. And one of the key projects there that comes to mind is the acid consumption project at the Wood River refinery. And that, like those previous 2 I mentioned, also reduces well over $1 million from operating expense. So we have 200 of these projects we're working throughout the system to drive cost out.

The other thing I'll mention, and this is, I think, helpful is we're an organization that is full of data. And the AI revolution here has really opened up our ability to analyze this data and look for trends. So we're actively engaged in doing that as well. And that's also bringing a lot of opportunities to light that I don't know that we otherwise would have seen because of the data -- the fog of too much data almost.

Of course, on the other side of that equation, you got to run well. And having your equipment running reliably and assure it's ready to run, we're keenly focused on that as well. And then Brian's group is working hard to support filling up the downstream units that have available capacity to them and really working towards that, increasing the total process input for the site.

So what I see in summary is that $5.50 is well within range and I fully expect us to achieve that goal next year. And those cost improvements that we are driving for our stock owners, these are structural. They're not going to work their way back into the system. There's structural changes that we're doing, and we're not done yet with this.

Donald A. Baldridge
Executive Vice President of Midstream & Chemicals

Arun, this is Don Baldridge. I'll take the $1 billion growth in Midstream and Chemicals that you asked. And really, we split that into 2 parts, 50-50, if you will. The first is the $500 million growth in Midstream. That's really their $4.5 billion run rate target by the end of '27. The 2 things I'd highlight there is the -- first, the execution on our large expansion projects. And then second is the successful optimization efforts that we're having around the footprint. First, the large expansion projects that we've announced already, like the Iron Mesa gas plant and our Coastal Bend NGL pipeline expansion. They remain on time and on budget and will be meaningful contributors in 2027 and allow us to meaningfully grow our earnings.

But I'd also highlight the second one, which is just the execution on the smaller optimization opportunities around our footprint where we are continuing to see how we can grow our capacity in a very capital efficient way. You saw that in this quarter with our growth of record NGL fractionation, record NGL exports. Our operations teams continue to find ways to grow the capacity very capital efficiently and the commercial team readily fills it. So that's the strong team execution that's happening around Midstream.

That gives me a lot of confidence in not only hitting our 2027 earnings growth target, but also just the growth rate beyond that.

Within the Chemicals, that's really our CPChem business. And that's even a simpler story. We've got 2 large world-scale crackers that will meaningfully come online and contribute in 2027, and that's the predominant growth for that $500 million on the Chemical side.

Arun Jayaram
JPMorgan Chase & Co, Research Division

Great. And my follow-up, I was wondering how we should think about, obviously, really good results in Refining. But how does this quarter's Refining, even Midstream strength, how does that influence how you think about the mid-cycle earnings power of each of those segments?

Mark E. Lashier
CEO & Chairman

I would say at a high level that given what's going on in the world, that there's some resilience in Refining. The macro looks strong. Even if peace broke out tomorrow, we saw strengthening fundamentals before the Iran conflict kicked in. And so we think that it will even be stronger coming out of that conflict. And so whatever your view of mid-cycle was, we think it will be stronger going forward, and we think that it will be persistent going forward.

So we think it's very constructive and has some legs under Refining. Midstream has been very consistent. And I think that, that's the beauty of the Midstream business. Like I said earlier is that it's that solid rock foundation under the rest of our businesses. And the growth there will be our organic growth and delivering on those projects and enhancing that.

Operator

Your next question comes from the line of Theresa Chen from Barclays.

Theresa Chen
Barclays Bank PLC, Research Division

I appreciate some of the comments related to long-term structural drivers for the Refining macro. I wanted to ask near term, are we -- as we move through the remainder of summer driving season into the fall, which factors do you view as the most important upside or downside risk to crack spreads over the next quarter? Is it demand elasticity? Is it Chinese exports? And maybe putting a finer point on the capture discussion, what are your expectations at this point for third quarter capture?

Brian M. Mandell
Executive Vice President of Marketing & Commercial

Theresa, it's Brian. Maybe I'll start with just a list of things that give us a lot of confidence, list of tailwinds for kind of higher cracks going into Q3 and carrying on through the rest of next year. Refining fundamentals, as Mark talked about, are very tight and getting tighter with the issues in Russia and the Mid East. We have 7 million barrels a day of refineries down in Asia and the Mid East and another 1.4 million barrels down in Russia. And the refineries, depending on the damage and the ability to get spare parts, are going to take a good long time to get back online.

We have low product inventories in the U.S. and around the world. Chinese exports of products have been low, half of what they have been over the last 2 years. And the Chinese have shown discipline over the last number of years. We've seen -- we'll see the need to refill SPRs over time, and there will likely be new SPRs that develop to protect against these type of geopolitical problems.

We're also forecasting high turnarounds in '27 and '28 and likely more unplanned turnarounds in the near term as refiners push work out to take advantage of the higher margins. You have the typical inflationary pressures on operating expenses and CapEx. We have high RIN prices. We have elevated our freight rates. And the marginal refining barrels in Europe where structural costs are higher, carbon is higher, electricity is higher, labor is higher, all much higher than the U.S. So with the opening of the Strait, we also see crude supply will exceed product supply, and that drives stronger margins, too.

And the final point that we've been talking about for a while is net refinery additions are lower over the coming years and importantly, lower-than-expected demand increases. So this really sets us up for stronger margins through Q3 and the rest of perhaps next year.

Theresa Chen
Barclays Bank PLC, Research Division

Super helpful. With one of the large Canadian infrastructure operators proposing a project that would shift incremental WCS volumes from the Mid-Con to the Gulf Coast, potentially tightening heavy crude differentials in the Mid-Con while improving availability in the Gulf Coast, how would you expect that to affect the capture rates and Refining profitability across your system? And more broadly, how do you see WCS egress evolving over time? And what do you view as the most likely pathways for incremental barrels to reach market?

Brian M. Mandell
Executive Vice President of Marketing & Commercial

Well, our general view on WCS is that differentials are going to wider structurally over time, driven primarily by growing heavy crude supply out of Canada and Venezuela. Canadian production, which has been offline from weather and turnarounds was back online mostly by the end of last month, and we're heading into a diluent blending season. Also Venezuelan imports into the U.S. are already up 300% since January, which should add downward pressure on heavy crude pricing over time.

And then we expect the strong pull of U.S. barrels and higher freight rates and lightering costs to contribute to wider WTI/WCS differential as the inland heavy crude lags the export-driven strength of WTI and competes with Venezuelan barrels. But -- and I think once there's clarity on the movements from the Strait, we'll see increased supply of barrels moving into the market. Those will be primarily medium sours, but they'll also support wider heavy differentials. And just as a reminder to all of you on the phone, every dollar the WTI/WCS spread widens is an incremental $140 million impact to our annual EBITDA.

Kevin J. Mitchell
Executive VP & CFO

Theresa, this is Kevin. In your question, you had asked about capture in the third quarter, and Brian went through a lot of factors that we see in terms of how this market is going to play out. But just specifically, as we think about capture rates, we've historically guided to about 95%, and we don't see any reason why that would be any different this year in terms of where we are -- in terms of what we see currently with regard to third quarter.

Operator

Your next question comes from the line of Neil Mehta from Goldman Sachs.

Neil Singhvi Mehta
Goldman Sachs Group, Inc., Research Division

Just wanted your perspective first on Renewable diesel. Even if I was to normalize for margins closer to that $1.50 mid-cycle, you'd probably be above the $700 million that you guided to a while ago. And so just love your perspective on that business? And is there a new run rate of profitability at this level of utilization? And any perspectives on how we should be thinking about the modeling of it going forward?

Mark E. Lashier
CEO & Chairman

Yes, Neil, great question. I think that, first, it starts with the existential crisis that asset had a year ago when there was uncertainty around what the RVO would be, what any of the incentives to run that place would be. And the team there took it quite seriously. They readjusted their logistics opportunities. They cut costs, dramatically streamlined and they are operating extraordinarily well. So that really sets the base for what is possible. And Brian can talk about the fundamentals going forward. But when you look at the distillate macro, just that in its own right, provides another good, solid layer underlying the value of that asset.

So Brian, you can talk about the other.

Brian M. Mandell
Executive Vice President of Marketing & Commercial

Yes. I certainly agree with Mark. We had strong earnings in Q2, driven by credits and strong diesel margins, largely a function of the Iran war. Renewable diesel prices in RINs roughly doubled versus 2025 due to the Iranian situation. RINs remain an important driver to the segment's profitability. And there's ongoing regulatory policy risk, including the concern that foreign feedstock RIN generation will be cut in half after the end of next year.

We also had a onetime help in Q2 of $100 million, primarily due to tariff refunds. As Mark mentioned, Rodeo ran above nameplate capacity with record utilization of 106%. And then our Renewables segment isn't just Rodeo. And outside of the Rodeo complex and within the segment, we had good performance from our U.K. and our Asian businesses in the quarter. And in the segment also, we had mark-to-market pretax gain of $47 million carried over from Q1. So we continue to engage with state and federal administrations to ensure the long-term viability of that facility.

And just one point of clarity for modelers. We've updated our Renewable diesel indicator beginning this month to reflect the new 2026 45Z guidelines released in June to include $0.40 per gallon of PTC benefit in the indicator.

Neil Singhvi Mehta
Goldman Sachs Group, Inc., Research Division

That's great. So from one hard market to another, I just wanted your perspective on China. It is probably something that we have really tough time getting visibility into as an investment community. And we know runs are down a lot from the beginning of the year in China, and there's some talk of the quotas growing back. And so just your perspective on that in the context of your bullish refining view. Does this represent a risk?

Brian M. Mandell
Executive Vice President of Marketing & Commercial

Yes. I think as you said, it is tough to get information about China. We have seen their refineries about 2.5 million barrels a day of refinery runs offline. They're buying about 4 million barrels of crude -- less crude than they had been 12 million barrels of imported crude to about 8 million barrels. Their exported products are now about 400,000 barrels a day from 800,000 barrels a day. So it is possible that they could increase the exports of products. They haven't been doing that in a number of years past. They've been pretty disciplined, but it's hard to tell what they'll do going forward. So I think our guess will be, just like yours, do they want to help manage the worldwide product shortage or not.

Mark E. Lashier
CEO & Chairman

And I would add to that, you have to recall that China is coming off of a materially lower crude pricing basis than the rest of the world because they were buying huge quantities of deeply discounted Venezuelan crude, Iranian crude, Russian crude, anything they could get their hands on. That's gone now. So that changes their perspective on their ability to supply products to the rest of the world, both, I think, on a refining basis as well as petrochemicals. And our petrochemical folks are seeing them already respond to higher cost basis in petrochemicals and raising the prices of polyethylene, for instance. So they are very price sensitive, and they will respond to price signals. And I think that their price basis is much, much higher in crude than the impact the rest of the world has seen post war.

Operator

Your next question comes from the line of Matthew Blair from TPH.

Matthew Lovseth Blair

I was hoping you could talk about the appeal and refining environment in the Atlantic Basin. If I look at your July indicators, Atlantic Basin was up the most quarter-over-quarter. And of course, you have more exposure than a lot of your peers to the region. Is Russian downtime the main drivers here? Any other factors that you'd call out? And is this something that you'll be able to capture in Q3?

Richard G. Harbison
Executive Vice President of Refining

Yes. I'll start with the answer to that, Matt, and then turn it over to Brian. This is Rich here. When we looked at the Atlantic Basin, Q1 capture rate was pretty high at 182%. And then Q2 was on the other end of that spectrum at 79%. I really think the way you have to look at this with all the noise in the system over those 2 quarters is you got to look at it on a first half basis. And the first half capture rate was just well over -- not well over, but 112% on average. So it's a decent capture rate. And so I think the assets are performing well. And that also includes the effects of the Humber turnaround during that time frame.

And when we look at that first half annual average of 112%, we did go back and look at it from '23 to 2025, and we averaged about 96% in this. So I would say the assets are running well. They've been operating reliably. And it's been pretty impressive to increase that capture rate with the strong backwardation in the marketplace.

And maybe that's a good bridge over to you, Brian, on the market.

Brian M. Mandell
Executive Vice President of Marketing & Commercial

Yes. I think one of the things I'd say in Q3 is that backwardation has started to come off some. And certainly, from Q2, the historic crude differentials we saw in Q2 have come up as well. A lot of the crude that we buy for Bayway is Brent-based, so that will help in Q3. And as I mentioned, we were also moving barrels through the Jones Act of crude -- U.S. crude around to Bayway, too, and that helps also. So we'll continue to do that as well.

Matthew Lovseth Blair

Sounds good. And then the $450 million mark-to-market impact in Q2, I think you might have said that Renewable Fuels was $47 million boost. Do you have the same breakout for Refining and M&S?

Kevin J. Mitchell
Executive VP & CFO

Yes. Matt, it's Kevin. So that $450 million, I'll give you the breakdown by segment. So Refining was about $240 million of that. And just -- I think as everyone knows, but just to emphasize, that is built into the indicator and so not a variance from a capture standpoint. So $240 million Refining, Marketing and Specialties is about $160 million. And then Renewables is just shy of $50 million. And so you put those together, you get that $450 million total.

Operator

Your next question comes from the line of Joe Laetsch from Morgan Stanley.

Joseph Gregory Laetsch
Morgan Stanley, Research Division

So I wanted to follow up on the Chemical side. Can you just talk about what you're seeing in the market currently? It looked like margins have come in a bit from the peak earlier this year. Can you just talk to how you're thinking about the macro set up? And then it also looked like utilization rates during Q2 came in above guidance as well.

Mark E. Lashier
CEO & Chairman

Yes. Thanks, Joe. Yes, certainly, Chemicals saw a surge during the height of the crisis around the Straits of Hormuz. And they've come back down a bit with peace breaking out and that being factored in a bit. There's still considerable oversupply in the market that will come back into play once things normalize around the Straits. We think that will take some time. But even when that happens, we see a higher floor kicking in because, as I mentioned earlier, China is -- has lost its access to deeply discounted crude, so they're going to have to reset where they are from that perspective.

And we see that impact of about $0.07 per pound over where we saw the kind of the bottom of the cycle in 2025 at about $0.07 per pound. Put that in perspective, at the bottom of the cycle, our portion of CPChem's EBITDA was about $845 million at that $0.07 per pound. So they still have relatively robust performance. And so you'll see considerable upside even just resetting at that higher floor going forward. And so we see things relatively more stable, though they'll be below mid-cycle. They shot above mid-cycle temporarily. They'll be coming back down to something around $0.14, $0.15 a pound.

Joseph Gregory Laetsch
Morgan Stanley, Research Division

Mark, that's helpful. And then I wanted to ask just on M&S. So this is one of the segments that came in a bit above our expectations during the quarter. I think a falling crude environment and the strong summer driving season probably helped the volumes are up a little bit year-over-year. Could you just unpack some of the drivers in 2Q and talk about the outlook for the back half of the year as well?

Brian M. Mandell
Executive Vice President of Marketing & Commercial

Yes. This is Brian. I'll give you kind of a chat on M&S. One of the things that helped us was just margins in the business were very, very strong. I think M&S is going to be also a function of spot prices. Whether spot prices are moving up or moving down, that also affects our business. We had some favorable regulatory credits in the quarter. And also our lubricants business, which we don't talk about all that much, benefited from stronger base oil spreads with roughly about 1/3 of the global Group 3 base oil production offline. So I just think going forward, the tailwinds are going to include a favorable market, particularly with the ongoing Iranian war and the RIN prices. We also see some regulatory upside in Q3 as well. Tailwinds, again, are the rising spot prices.

Operator

Your next question comes from the line of Jason Gabelman from TD Cowen.

Jason Daniel Gabelman
TD Cowen, Research Division

The NGL segment within Midstream has been pretty volatile over the past few quarters. So just wanted to level set where we are right now if 2Q kind of represented a normalized environment for that segment just given the moving parts with commodities moving higher, projects coming online? Any color would be helpful.

Donald A. Baldridge
Executive Vice President of Midstream & Chemicals

Thanks, Jason. This is Don. Yes, I think we're still hovering around in the Midstream segment around that $1 billion a quarter mark with some ups and downs depending on commodity prices and depending on just some volume variances. But largely, we're solid in that run rate. Certainly, first quarter, we were impacted from Winter Storm Fern that impacted volumes. We also saw impacts of shut-ins when we had really low negative prices in the Permian. That is largely a pass-through. We've got new pipelines coming -- that have come online. We're seeing positive prices in Waha. As a point of reference, our June Permian volumes on our gathering and processing were a record high. I think that's a testament to producers turning on more volumes and having comfort of continuing to drill and grow now that there's good egress out of Waha. So we're on track to hit that $4.5 billion by 2027.

What gives me confidence of that is we've got these large capacity projects that are going to come online in 2027. And we already have a lot of that volume that we're processing with third parties or moving on third-party pipelines. So when Iron Mesa turns on, I expect us to be able to readily fill that capacity within the first part of 2027. And then those NGLs would obviously flow into our Coastal Bend pipeline expansion that comes online end of this year and fills that capacity up. So on track with hitting the targets and continue to see the growth trajectory from where we are today.

Jason Daniel Gabelman
TD Cowen, Research Division

Great. My follow-up is just on the Marketing segment. And I think in the past when Rhine River levels have been low, the international Marketing business has done extremely well. There have been some changes in the portfolio. So wondering if you still retain that upside exposure given Rhine River levels are currently low.

Mark E. Lashier
CEO & Chairman

Because Germany is no longer short diesel, the Rhine impact is much smaller going forward. So you won't see that like we've seen in the past.

Operator

Your final question comes from the line of Phillip Jungwirth from BMO.

Phillip J. Jungwirth
BMO Capital Markets Equity Research

Great. I was hoping you could talk about the Midstream portfolio and just current thoughts around optimizing here, whether it's divesting noncore assets or bolt-ons across core areas. And generally, do you see value in Midstream M&A? Or do you feel like with the organic projects you have like Zeus, Coastal Bend frac, which were announced intra-quarter plus Western Gateway are sufficient enough to drive competitive EBITDA growth beyond the $4.5 billion annualized run rate by year-end '27?

Donald A. Baldridge
Executive Vice President of Midstream & Chemicals

Thanks, Phillip. This is Don. And we are excited about the organic growth projects. We do think they are the best returns. The opportunity set that we have around the portfolio is dominated by the organic growth. We're seeing the customer response from a producer standpoint with volumes that are filling our system and enabling us to add capacity and grow that business. So it's a high bar when we think about M&A or bolt-ons. They have to be something that is highly strategic. It has to be of a bolt-on size that would be something that we could readily scale. Pinnacle was a great example. EPIC was a great example, where we could do something that was -- make our system more competitive as well as be able to scale it up quickly. But right now, we -- our focus is executing on the organic growth plan that we have in front of us. That's where we think the best opportunities are.

In terms of the overall portfolio, we've always said that, hey, there's certainly some nonoperated Midstream assets that aren't necessarily core, but they're nice assets. If they're worth more to others than to us, we'd certainly consider that. But we don't have any predetermined divestiture targets, but we're always looking at ways to make the portfolio more competitive, more durable and drive the earnings profile that we like in Midstream.

Phillip J. Jungwirth
BMO Capital Markets Equity Research

Great. And then, Mark, you sounded excited about this in the script. So just wondering different ways Phillips is implementing new technologies or AI across the Refining business just as it relates to optimizing commercial operations, executing or predicting turnarounds or lowering operating costs. And if it is more broad-based across the other businesses, I'd also love to hear about that also.

Mark E. Lashier
CEO & Chairman

Yes, Phillip, it is broad-based. We've implemented an AI program that really is normalizing the use of AI inside the company. We have people focused on use cases and then extrapolating those use cases across the organization. I think it's pretty exciting to see what's going on out in the front lines with the engineers out of the front lines using AI to -- as Rich alluded to it, capturing the data and extracting the data and getting solutions out deployed faster than we've ever thought about being able to do before. So it enhances the performance of the assets in almost real time. And to see their intellectual capacity just augmented by their use of AI to drive performance that they would normally drive over time, but it may take months or years to get to the same place they're getting to in days and weeks. And that is being spread across every part of the organization.

And we've been at it for a long time with machine learning to enhance maintenance, to enhance our ability to shorten our turnarounds and increase the duration between turnarounds, but we're just building on that with really this human-centered approach to AI deployment.

Operator

This concludes the question-and-answer session. I will now turn the call back to Sean Maher for closing remarks.

Sean M. Maher
VP of Investor Relations & Chief Economist

Thank you for your interest in Phillips 66. If you have any questions or feedback after today's call, please reach out to Kirk or myself. Thank you. Have a great day.

Operator
This concludes today's call. Thank you for attending. You may now disconnect.