

TRANSCRIPT

**2020 BUSINESS UPDATE
CONFERENCE CALL**



PHILLIPS 66 (NYSE: PSX)

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PHILLIPS 66 BUSINESS UPDATE CALL TRANSCRIPT

PHILLIPS 66 PARTICIPANTS

Jeff Dietert, *Vice President, Investor Relations*

Greg C. Garland, *Chairman and Chief Executive Officer*

Brian M. Mandell, *Executive Vice President, Marketing and Commercial*

Timothy D. Roberts, *Executive Vice President, Midstream*

Robert A. Herman, *Executive Vice President, Refining*

Kevin J. Mitchell, *Executive Vice President, Finance and Chief Financial Officer*

MEETING PARTICIPANTS

Roger Read, *Wells Fargo Securities*

Neil Mehta, *Goldman Sachs*

Phil Gresh, *JP Morgan*

Paul Sankey, *Mizuho Securities*

Justin Jenkins, *Raymond James*

Spiro Dounis, *Credit Suisse*

Brad Heffern, *RBC Capital Markets*

Matthew Blair, *Tudor, Pickering, Holt and Company*

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Operator

Welcome to the Phillips 66 Business Update Conference Call. My name is Sharon, and I will be your Operator for today's call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. Please note that this conference is being recorded.

I will now turn the call over to Jeff Dietert, Vice President, Investor Relations. Jeff, you may begin.

Jeff Dietert

Good morning and welcome. Today we will provide an update on Phillips 66 and our responses to the current business environment. Then we will open the line for questions. Participants on today's call include Greg Garland, Chairman and CEO; Kevin Mitchell, Executive Vice President and CFO; Bob Herman, Executive Vice President, Refining; Brian Mandell, Executive Vice President, Marketing and Commercial; and Tim Roberts, Executive Vice President, Midstream.

We will be making forward-looking statements today. Actual results may differ. Factors that could cause results to differ are included in the press release and in our SEC filings.

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

Greg C. Garland

Okay, Jeff. Thanks. Good morning everyone and thank you for joining us today.

Earlier today we announced actions that Phillips 66 is taking in response to the challenging business environment. The press release outlines our specific actions. We thought it would be helpful to provide you with some context for our decisions and to answer your questions.

First and foremost, our commitment remains to operating excellence; it's steadfast. Our top priority continues to be the health and well-being of our employees, their families, our communities, as well as to safe and reliable operations. This has always been our focus, and this will not change.

Phillips 66 is well positioned to persevere through this tough environment with a diversified portfolio of high-quality assets and a strong balance sheet. We believe it's appropriate for us to take action to preserve liquidity, maintain our strong investment-grade credit rating and be well-positioned for the future.

We are reducing our 2020 consolidated capital spending by \$700 million to \$3.1 billion. We are doing this by deferring and cancelling some projects. The \$700 million reduction will be partly offset by a \$400 million increase as DCP Midstream will not be exercising its option to participate in Fracs 2 and 3 this year at Sweeny. Phillips 66 Partners capital spending forecast is little changed at approximately \$900 million.

In our Midstream business, the Red Oak Pipeline and Sweeny Frac 4 projects as well as the Phillips 66 Partners Liberty Pipeline will all be deferred. Phillips 66 Partners has also postponed its final investment decision on the Ace Pipeline. These projects will be reevaluated at a future date.

Across our business, we are reducing operating and administrative costs by \$500 million in 2020. For the near term, we have suspended our share repurchases to provide additional liquidity and preserve our strong balance sheet. We will reevaluate resuming share repurchases in the future.

We recently entered into a new \$1 billion 364-day term loan facility. This is incremental to our existing \$5 billion revolving credit facility. Phillips 66 Partners also has a \$750 million revolving credit facility.

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The actions we have taken are to preserve the continued security of our dividend, maintain our strong investment-grade credit, provide us with additional liquidity and financial flexibility. We are ensuring that we make the right business decisions to position the company appropriately as we navigate through this challenging business environment. We are closely monitoring global market conditions and will be prepared to take additional action as needed.

We will continue to execute our strategy with a focus on disciplined capital allocation and long-term value creation for our shareholders.

Before we open the line for questions, I'd like to reinforce that while the current environment presents great challenges to us, we'll get through this together. We have a long history and have successfully managed through many events and down cycles. This will be no different. We remain committed to providing energy and improving lives.

I want to thank you for your support, your interest in our company and now we'll open the line to questions.

Operator

We will now begin the question-and-answer session. As we open the call for questions, as a courtesy to all participants, please limit yourselves to one question and a follow-up. If you have a question, please press star, then 1 on your touch-tone phone. If you wish to be removed from the queue, please press the pound key. If you are using a speakerphone, you may need to pick up the handset first before pressing any numbers. Once again, if you have a question, please press star, then 1 on your touch-tone phone.

The first question comes from Roger Read with Wells Fargo. Please go ahead. Your line is open.

Roger Read

Thank you. Good morning and thanks for the detailed update here on I know what had to be a short amount of time to put all this together.

I guess, Greg, if I could, really can we just talk about the macro here? What you're seeing on the fuels side of the business, thinking particularly gasoline and jet, and how maybe that compares to the more steady operations in the Midstream and the Chemicals businesses here.

Greg C. Garland

Sure. Brian, I'll let you start on the product side.

Brian Mandell

Okay. We have line of sight basis, our retail and wholesale business in several markets in Europe including Austria, Switzerland, Germany and U.K. In those markets, we're seeing demand destruction as much as 70% in Austria, down to the U.K. of about 10%. This is based on government isolation procedures; Austria started first and so their demand destruction is greater.

In the U.S., we – kind of hot off the presses yesterday, we did our demand basis this week versus last week. We're seeing around the U.S. about 20% demand destruction and in some markets, particularly the West Coast where they've been isolating longer, about 30%, so a lot of demand destruction. We're seeing gasoline cracks at negative margins. We're seeing jet cracks even worse. Distillate cracks are still holding up around the U.S., but we're seeing even our Latin American customers asking us if they can back out of cargoes now, so we see that the demand is starting to move toward – demand destruction is starting to move toward Latin America.

It's a tough market out there, and we're seeing refiners start to have run cuts, including Phillips 66, and that's kind of the way to help clean up this demand in the short-term.

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Jeff Dietert

Roger, if I could, at the fourth quarter earnings call we provided refining utilization guidance of about 90% for the first quarter and obviously we did not envision this type of environment. Given the current environment, we expect first-quarter refining utilization to be in the low to mid-80% range.

Greg C. Garland

Maybe a quick comment on petrochemicals, Roger. I think we had guided to low mid-90s in terms of operating rates, and I think we're in that rates on petrochemicals. Margins have kind of hung in there. Full chain ethane to polyethylene margins are between \$0.18 and \$0.19 today, so the volumes are hanging up well globally on the petrochemicals side.

Roger Read

Okay. Then I guess as we think about run cuts, I know each unit is different and even within a facility, whether you run the FCC a certain way, but at what point do you reach a decision on like a full shutdown of the unit relative to throttling back on the runs that you're doing. In other words, if we're thinking 80% utilization for the company, some units running harder than others, is 60% utilization a break point we should think about or can you go as low as 40%? Is it higher than that? I was just curious if there's any sort of rule of thumb to think about there.

Robert A. Herman

Hey Roger, this is Bob Herman. I think when you think about how low can we go, it really is refinery by refinery specific and really geared toward the market. We're trying to stay out in front of the demand as it comes down and cutting back at some point. I don't think a good rule of thumb would be down in the 60% range for refiners. Most refineries can't turn down that far. Within an individual refinery, you'll see us shut down conversion units because if we lower crude in, say, a refinery where we've got multiple hydrocrackers and cat crackers, we won't have enough feed to keep all of those units online, so it's a specific step by step. I think you can expect the state everybody has had to go to quickly, we're nearing kind of minimum crude rates in many of our refineries today.

Operator

Next question we have is from Neil Mehta with Goldman Sachs. Please go ahead. Your line is open.

Neil Mehta

Good morning team, and thanks for the update this morning.

The first question is around balance sheet and can you just walk us through again liquidity position, how we should think about the 2020 maturity and how you guys are managing to keep the balance sheet strong?

Kevin J. Mitchell

Neil, it's Kevin. From a liquidity standpoint, the starting point is the \$5 billion revolving credit facility we have in place at PSX. We also have \$750 million at PSXP. We have just recently put in place a \$1 billion-dollar term loan facility, and what I'd emphasize on that, it's not that – we didn't do that because the \$5 billion isn't enough. What we've seen – and as you can probably appreciate this – as we cycle through the month, the different payment cycles, the monthly cash flow, the daily cash flow varies quite a bit. And so we can be in and out of commercial paper markets, and we use the revolving credit facility to backstop the commercial paper program.

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What we've found in this environment is there are days where CP markets can be really tight, and so we put in place the term loan to provide additional facility to us in the event that there's times where we may want to be in the CP market and we're actually struggling to do that.

Just to put it into context where we are today, of that \$5 billion revolving credit facility, we've got \$450 million of CP outstanding, so that leaves \$4.55 billion still available. We've got the billion-dollar term loan, and we're sitting on about \$900 million of cash. A lot of liquidity available to us, and so we feel that with the term loan we're just shoring up the balance sheet just to help ensure that we're always in a good spot in terms of having the liquidity to make sure that as we go through the month, the daily cycles, that adequate cash flow is there.

Neil Mehta

Appreciate that additional color, Kevin. The follow-up is just around capital spend. A couple of questions around that. You took down the cap ex decently, but if the conditions continue to remain adverse, do you have additional flexibility in 2020? Then, any comments specifically on Liberty and Red Oak from a Midstream perspective in terms of how we should think about whether this is a deferral of the project or walking away? Two questions there.

Greg C. Garland

Well, probably around 2020 most remaining cap ex is to finish these projects in flight, Neil. Around the edges, probably in sustaining cap ex, we can probably find another couple of hundred million if we were pushed. That would not be our first choice obviously to go in and cut sustaining capital, but you can always do that for a year. You just can't do that for multiple years.

Another thing I would point out is that as we get to 2021, we have quite a bit of flexibility in terms of our capital profile and then I'll let Tim kind of give the update on Red Oak and Liberty.

Timothy D. Roberts

We thought at this point with regard to these two projects that they're early enough in the project cycles, and we like the projects. I got to tell you we think they're good projects, or we wouldn't have sanctioned them, but with the current uncertainty in the marketplace and what's happened is quite a shock to the system, we thought it was a good time to go ahead and pull up, pause and then we can reevaluate. Our investment isn't lost, but we will defer to a later point in time on whether we continue the projects, or we cancel the projects. But at this point in time we've been in discussion with our partners and discussion with our shippers on this, and we just think it's the prudent thing to do with the amount of uncertainty going on in the market right now.

Operator

Next question comes from Phil Gresh with JPMorgan. Please go ahead. Your line is open.

Phil Gresh

Just a few follow-up questions. First one is just around the capital spending flexibility as we look ahead to 2021. Following up on Neil's question, if this environment were to remain in place for a more extended period of time, how are you thinking about committed capital above and beyond sustaining capital?

Greg C. Garland

Phil, we finished up most of the big projects that we have underway in 2020. That's not much that really carries over into 2021. If you go back to 2016, let's say, Refining kind of had a break-even year net income, \$1.4 billion of EBITDA for that year. We pulled capital down to \$1.7 billion, so \$1 billion dollars worth of sustaining capital and kind of \$600 million to \$700 million of growth. Certainly, we could see 2021 being

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and under \$2 billion-year total spend for us. It depends on how long these economic conditions go on and then how soon the economy recovers coming out of the time that we're in.

Phil Gresh

Okay, thank you. That's helpful. Second question, I guess this one would be for Kevin. You mentioned the cash balance today. Part A of that is, is there any working capital impact here in the first quarter that is embedded in how the cash balances end up given what's happened with crude prices? Then if I were to extend that to the second part, just how you think about the balance sheet more broadly, what your leverage targets would be, whether it's net debt to EBITDA or I think you usually look at more of a consolidated net debt to cap. Obviously, this environment seems like as we move through the trough, the dividend would have to be funded by the balance sheet, so how long would you be willing to do that? Thank you.

Kevin J. Mitchell

The first question is around working capital. Our usual cycle is one of a working capital as a use of cash in the first quarter. A lot of that is driven by the timing of inventory builds and draws, and so you typically see a use of cash in the first quarter and we're certainly seeing that, although I will say, given the dropping crude prices and some efforts we've made to look for opportunities to optimize inventory levels and bring cash back through working capital, so we're sort of optimizing around that.

Obviously, that number, those numbers I quoted were as of this morning and reflect any working capital impact through the year-to-date, through this morning. But if you look broader at balance sheet and ability to fund, I mean the reality is in the near term, as we're going through a significant down cycle here and the balance sheet is there, we've got the balance sheet to enable us to carry through this down cycle. So, for a period, if you think through say the end of this year, yes it means we'll add debt, but we've got adequate capacity to be able to do that without having a detrimental impact around our credit ratings. Our typical leverage target that we talk about, that sort of 30% debt-to-cap ratio, we will go beyond that. We will go above that, but it never was a hard target; it's a level we're very comfortable being at, and we'd expect that once we come through the other side of this we get the balance sheet back to the kind of condition that it was before the start and we'd be back at our sort of targeted leverage levels.

Greg C. Garland

I think it's important to say, though, we want to maintain an investment grade rating as a company.

Kevin J. Mitchell

Oh, absolutely.

Operator

Next question comes from Paul Sankey with Mizuho. Please go ahead. Your line is open.

Paul Sankey

Hi, good morning everyone. I appreciate your comments there on maintaining investment grade. Thank you, Greg. Could we just think about the cash flow for a little bit here? I think in the past you've talked about 2016 as a trough year. Where are we at relative to that? I know that you see on a day-to-day basis in this extraordinary circumstance how things are moving around out there and that you've got a couple of countercyclical businesses. Could any of you just frame that for me? Thank you.

Greg C. Garland

Well, Refining probably feels a little worse than 2016, Paul. If you go back to 2016, we were doing \$1 billion of EBITDA Midstream. We've doubled the Midstream EBITDA since 2016. I think the Chemicals business was \$1.3-ish billion of EBITDA in that year, and maybe we're a little lighter there. And then our Marketing

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and Specialties business was – perennially, it's \$1.2 billion to \$1.5 billion. It was \$1.3 billion that year. That feels about right for us. So there's some ins and out and takes and puts I would say versus a 2016 year, but 2016-year trough EBITDA we were kind of \$4-ish billion dollars, and we could be in a range of \$3 billion to \$4 billion this year, I would guess.

Jeff, I'll let you come in on that one, too.

Jeff Dietert

Yes. It's a very challenging period to determine the depth and duration of the impact of the double-demand and supply shocks that we've got underway. We're working to maximize profitability and minimize losses as best we can while continuing to focus on operating excellence with safety, reliability, environmental, but I think it's tough to know exactly how this is going to play out. It's a more severe environment than that 2016 bottom of the cycle environment. As Greg said, Marketing and Midstream are stable contributions that help our cash flow and our credit quality.

Paul Sankey

Absolutely understood. Then, this is a bit of a wildcard question but there could be major opportunities out there for a company of your strength in terms of M&A. Is there anything you can say about that? Thank you.

Greg C. Garland

Well, I don't know, Paul. These are interesting times. We have a saying here, "never try to catch a falling knife," and the folks that have gone out in our industry and have done M&A transactions and paid big premiums that really hasn't worked out well. There's nothing on the horizon for us today.

I would tell you that the longer this goes on, it's my personal feeling the more likely that people will be willing to do no-premium deals, and I think that could be an interesting time in the industry, but there's nothing on our radar today other than managing our cost structure, watching our liquidity every day and making sure every dollar that we're spending on behalf of our shareholders is going to the right place, being disciplined allocators of capital.

Operator

Next question comes from Justin Jenkins with Raymond James. Please go ahead. Your line is open.

Justin Jenkins

Great. Thanks. Appreciate the color this morning. I've just got one question on the Midstream side, and it's one we're getting a lot in Midstream land. It's around the credit quality of your customers, and I'm thinking maybe more for PSXP. I don't know if Kevin or Tim, if you could maybe outline what you're thinking in terms of the counterparty risk that you've got in the business.

Kevin J. Mitchell

Yes. Justin, it's Kevin. When you look at PSXP, the business is really split between the assets that PSXP owns and operates, and then all the joint venture assets, and the joint venture assets have grown significantly over the last few years. The owned and operated assets are predominantly it's something like 97% PSX is the counterparty on that. And so you've got – and most of those assets are integral to PSX running its refining and marketing business. And so you're really exposed – you've got high credit quality. Your potential exposure is to the minimum volume commitments around that if you think about potential for refineries running below full utilizations. So you have some exposure there. It's not credit exposure but from an EBITDA and from a cash generation exposure.

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Then on the JVs, we're looking at about 75% – as best as we can tell, when you look through the JVs, about 75% of the EBITDA at minimum volume levels is investment grade. When you combine all of that, if you take the owned assets and the JVs, you get about 85% at minimum is investment-grade credit. We're looking to put something together that we'll probably publish the next time we do an Investor Update that just provides a little bit more granularity around the credit quality of the PSXP customer base, just to help provide some of that.

Justin Jenkins

Perfect. Thanks, Kevin. Be well, everyone.

Operator

Next question comes from Spiro Dounis with Credit Suisse.

Spiro Dounis

Hey, good morning everyone. Kevin, appreciate the comment on the credit counterparty risk, but you did mention the MVCs, so just had a follow-up question there. Just with respect to any near-term refined product demand hit or refinery utilization downturn. Can you give us a sense for how protected the EBITDA is as a result of those MVCs? I think just using some of your figures from the 10-K, I think I back to a number of around 70% of consolidated revenue seems to be about MVC protected. And I'm just wondering if that's maybe consistent with what your numbers say and then what that looks like across the joint venture portfolio.

Kevin J. Mitchell

Yes, I think the MVCs are actually a bit higher than that. No every asset is the same. Most of the MVCs are set at 80% to 85% levels. There are certain assets where it's actually a full capacity commitment that PSX is making to PSXP and so the minimum, if you like, is something closer to 100%. There are probably a – well, there are a handful of assets where there are no minimums but those are few and far between, so I actually think in terms of this 80% to 85% as a reasonable guide in terms of how to think about that.

Spiro Dounis

Okay, perfect. That's it from me. Thanks, Kevin.

Operator

Next question comes from Brad Heffern with RBC Capital Markets.

Brad Heffern

Hey, good morning everyone. I just wanted to touch up on jet fuels. Can you talk about the percentage of your distillate yield that goes to jet and then how much of that can be shifted into the diesel pool?

Brian Mandell

We currently make about 225,000 barrels a day of distillate – of jet, rather. We think about half of that jet we can push into gasoline or distillate, so we're left with a relatively small amount at most of the refineries. That's a nonissue. We're working with the airlines and others to take the jet we have, so we don't feel that that's a problem for us. It's a small amount versus the whole roughly 1.8 million barrels a day of production currently.

Brad Heffern

Okay, got it. Thanks for that.

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Then on the \$500 million cost savings number you guys have given, is there any way that you can sort of categorize that? Is there overlap between that number and the AdvantEdge66 program? Thanks.

Greg C. Garland

Well, I mean certainly AdvantEdge66 has provided the basis for us to recover some of these costs and opportunities. Part of this is deferral as we looked at pushing some of our turnarounds. This is a quite active turnaround year that we had scheduled. A lot of it was accomplished in the first quarter. As we're thinking about Q2, Q3 and Q4 turnarounds though, I mean one of the concerns that we have is just around the contract labor force that would be there to help us do a turnaround. And you're bringing a couple of hundred to multiple hundreds of people into your facility, you don't know and you think about the risk and the spread of virus and all that, and so we think there's really good reasons beyond just the cost side to think about which turnarounds could we push or defer, and so that's been an element of this. Certainly, as we're reducing rates there's less chemicals and additives associated with that, but I'd probably let Bob talk about his business a little bit.

Robert A. Herman

Yes, I think Greg hit most of it. We've really sharpened our pencil around our turnarounds this year, and we get about three sizeable turnarounds that we're able to shift into next year and we've gone through all kind of the safe operations reviews of those and our ability to do that we think is very strong.

Some of that just comes from – some of the units are driven by catalyst changes and as we run lower rates, we're not burning up the catalyst as fast; it allows us to push out, and specifically, we have pushed turnarounds because of worries about getting the workforce in. So, if you think about that, that actually helps us on the capital side too because we usually have a lot of sustaining capital associated with our bigger turnarounds, so as we move turnarounds we get a double play there in that we push expenses into next year and we defer capital out of this year into next year.

Kevin J. Mitchell

Brad, it's Kevin. I would just – just to supplement the AdvantEdge66 comment, I would say a lot of that activity underway anyway and what this initiative, what this is doing is forcing us to look critically at how can we accelerate some of those benefits? How can we bring forward some of those AdvantEdge66 cost benefits that we're pursuing anyway, but we just need to get more aggressive over.

Operator

We have a question from Matthew Blair with Tudor, Pickering, Holt.

Matthew Blair

Hey, good morning everyone. I wanted to clarify on the 20% demand destruction number for the U.S. What products does that encompass? Is it just for gasoline or is that for total U.S. oil demand?

Brian Mandell

Yes, we're seeing – when I talked about 20% to 30% depending on the location that's predominantly for gasoline. We've seen distillate demand much less affected. As you can imagine, you have Amazon trucks rolling around and other businesses, so it's more of a gasoline issue currently. It's why the distillate cracks on the screen today are \$20, and the gasoline cracks are negative.

Matthew Blair

Got it, okay. Then any comments on the export market for products? Are you able to shift barrels out of the U.S. and over to Latin America at attractive rates?

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Brian Mandell

We continue to ship products out of the U.S. Latin America has been the biggest sink for products for the U.S. for a long time now. As I mentioned earlier though, we're getting questions from our Latin American customers asking us can we back off on some of the term deals that they have, term purchases that they have from us. So, you can start seeing that the coronavirus is moving in that direction, and they have the same concerns we do about that lower demand and too much product. More to come. We'll see how the coronavirus affects Latin America over the next few weeks.

Matthew Blair

Got it. Thank you.

Operator

Thank you. We have now reached the time limit available for questions. I will now turn the call back over to Jeff.

Jeff Dietert

Thank you, Sharon, and thank all of you for your interest in Phillips 66. If you have further questions, please call Brent or me. Thank you.

Operator

Thank you, ladies and gentlemen. This concludes today's call. You may now disconnect.