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<<Ben Bienvenu, Analyst, Stephens Inc.>>

Okay. I think we'll go ahead and get started. Thanks everybody for being here. I'm Ben Bienvenu. I cover the Convenience Store and Grocery Industry with Stephens. Thrilled to have with us here today, Murphy USA, one of the leading convenience store operators in the U.S.

And pleased to have with us from the company CEO Andrew Clyde. I think maybe to kick things off – I'd be remiss if I didn't say congratulations on a great quarter, but I think if we look back at something that you guys have kind of been building to for better part of the year, so if you could just give us some background on what that building process has been, what do you think it allows you to do going forward?

<<Andrew Clyde, Chief Executive Officer>>

Right. Well, thanks Ben. It's great to see some familiar faces in the room and some new faces. We are webcasting this as well for other investors who may listen now or at a later time.

Yes, I guess if you think about our journey since we spun off in 2013 we tackled a number of big initiatives that you could do at the corporate level, renegotiated supply chain contract, moved from McLane to Core-Mark, attacked store labor, a number of things that, we were using an analogy this morning, kind of slow-twitch muscles, right? And we got a lot of benefit out of those and as we started laying out what the next several years needed to look like, we recognized there were more opportunities in front of us, but they really relied on what I'd call fast-twitch muscles, right? Optimization.

Since the spin, we had seen volume deterioration in fuel, one of our core traffic drivers. And we knew what we needed to do from a strategic pricing – price optimization standpoint, which is getting the people mindset leadership coupled with the systems and know-how and process to do that. And so we made a change in June, a year ago Mindy West our CFO is here and another gentleman took charge of this process and really started focusing on those key disciplines that we needed to be excellent at fuels pricing.

And we really established re-established with the customers and the competitors, our bottom of market mindset, our every day low price leadership position regaining share and had demonstrated in Q3 to build or gain market share volume and margin through those disciplines. And so that's something we're going to be able to continue to build on. But that was something that requires a great deal of precision day by day, if you build a playbook for every store in the network, every product, how are you going to price against every competitor? And that's hard work. But it's really paying off.

Strategically, about three years ago after we, stopped getting stores from Walmart and kind of moved our independent growth plan. At the same time, we realized we really don't have a loyalty program. And we'd had the summer discount programs with Walmart, prior to me joining the firm in 2013 and for couple of years after. But they worked until they didn't, and they weren't economic for Walmart, they weren't economic for us and they drove some traffic but the juice just wasn't there.

And the biggest challenge for us was as an everyday low price retailer. How do you make loyalty work? And if you look out among consumer retail companies that are commodity retailers, you don't see a lot of loyalty programs, is there going to be low price retailer. You can't price up to some and discount for others.

And you got to be really careful about not giving value to already loyal customers. And so, we went about figuring out what's the calculus and the strategy to actually make that work, built and designed a system seeking to solve that problem, which was different than any of the other loyalty programs out there we're trying to solve.

They were trying to solve a, if you buy six, can I give you a seventh cup of something for free? And they were proprietary high margin items in our small stores. We only have dispensed beverages or that opportunity. We knew that we needed to price discriminate based on targeting very distinct behaviors. If you bought one of these, can I get you to buy three of them? But I'm only going to target the people who are buying one, not the three. If you buy these products like tobacco, but you've never bought fuel from us.

And what we discovered was we've got millions of customers, transactions that are, buying tobacco from us every week, but have never bought a gallon of fuel from us. And so being able to target those very specific behaviors and not rewarding anyone else and then getting the uplift from those behaviors is the way we've cracked the code on that.

What's especially powerful is because we built something from a unique position, we built the backbone and the analytics engine behind that. We've got longitudinal data on consumers and their transactions that if you're a tobacco manufacturer or a consumer packaged good company being able to see what you're buying and you should think about tobacco and the poly use - people who smoke also dip and vape - are you staying within the brand? Are you going outside of the brand, et cetera?

We are finding that we can get 15% to 35% participation in surveys that we send consumers. And we don't have to offer our consumers a lot to participate in a survey. So imagine if you're a consumer packaged good company and you've got longitudinal data on all the products you're buying, right? You're introducing new products, you don't know anything about that consumer, we can provide that and then we can target specific surveys against them.

So, there's a lot of upside, I think, in 2020 and beyond to figure out how do we get the most value out of that. So, that's another example of what I'd call a fast-twitch muscle that we've

started to build and exercise and now take advantage of. And I think some of the things that we're really good at around the store process optimization, we had higher costs in the first half of the year as we implemented our maintenance program. We acknowledged that and said cost would moderate in Q3 and they did.

So, I think it was one of those quarters where we're able to demonstrate upside in volume and margin on the fuel side. We continue to hold tobacco units flat where the industry is declining 6% to 7% and grow margin there. Keep our cost discipline and then reiterate our commitment to capital discipline with the share buy backs.

<<Ben Bienvenu, Analyst, Stephens Inc.>>

Perfect Andrew. Any questions in the audience?

Q&A

<Q>: How are you keeping that out-performance on the tobacco side?

<A – Andrew Clyde>: So a number of ways. One is if you're every day low price and now you're getting three price increases a year from the tobacco manufacturers by two, everyone's prices are going up as your consumer, right? And so on the one hand, consumers are price sensitive and so they can either trade down their brands or they can trade to a different retailer. And so we're getting more consumer traffic from that.

We'd started participating in a manufacturer program in October, 2017 where all you had to do is append a unique identifying number to a transaction to get those loyalty funds. There's only so many retailers that are on that program. With our loyalty program, what we found is by being able to earn points on tobacco and we're the only retailer in the country that allows you to do that and then burn it on fuel, we've created stickiness in the periods where those manufacturer programs roll off for a month or two and are able to hold onto that volume more so than when they rolled off the programs previously.

One of the things retailers in this business face, whether it's fuel or tobacco it's just the volume headwinds from competition and the like. And at some point you realize, look, I'm on a tobacco everyday low price contract, but I'm really not getting the volume associated with that. And there are certain restrictions on those contracts in terms of selling tier four products for example.

Many of the retailers we've seen in the tobacco side have consciously moved away from those contracts. And so we have less competition at the bottom of the market. And by the way, we've seen the same thing on the fuel side as well. Some retailers realizing, you know what, I really can't price down at the bottom of the market with you. I'm not getting the three times, four times volume, you're getting. I'm much better off pricing up, shedding some volume, making it in margin and it's fine.

And for a convenience oriented retailer that works well for them. So, we're seeing retailers concede bottom of market to us with our everyday low price position. And when you couple that with an everyday low cost position that we have in our super low breakeven at the store level, it's a sustainable position.

And so some people worry about the exposure to fuel and tobacco as two of our biggest categories. These are multibillion-dollar categories that are going to be around for a really long time, right? We see fuel demand being flat plus or minus 1% for the very foreseeable future. And so we're gaining share in those categories. And then as the retailers are getting weaker and weaker and you just have to look at the NACS data, the bottom two or three quartiles break-even performance, their margin requirement keeps going up whether you look at fuel or tobacco.

And so there's pressure upon them to price up. And then as an everyday low price retailer, you've got the option, can you maintain your price, increase your differential grow volume or get price – price up and get volume and margin.

<Q>: [Question Inaudible]

<A – Andrew Clyde>: At our store, so we do need more pumps, which is why we've been doing the raze and rebuild program. And when this business was started 20 years ago, I don't think the founders had any idea what a everyday low price fuel offer would generate in terms of traffic because there weren't a lot of those out there. And there's this huge latent demand segment that wanted low price.

And so 15, 20 years later, we're going through the portfolio, 25 stores a year, razing and rebuilding those stores, taking out all the tanks and pumps, and underground any remediation. And building brand new 1,400 square foot stores that still fit on the Walmart pad where we have all that traffic, putting six to eight dispensers maybe where we had four, diesel at every dispenser, a niche product like an ethanol free gasoline if you're in a boating or an ATV recreational vehicle type environment, and we're able to do that.

Our favorite example was Eagle Pass, Texas. We were doing 500,000 gallons of regular out of one, –out of four dispensers and a 100,000 gallons of diesel out of one dispenser. And so with the raze and rebuild, we're doing well north of 600,000 there. So, people will wait in line also, but at some point more dispensers helps.

<Q>: [Question Inaudible]

<A – Andrew Clyde>: It's a better problem to have than an empty parking lot.

<Q>: On the fuel side. What is it that makes you all distinctive on the fuel procurement side of things and how do you think the market, if at all, tries to replicate that? And do you think there's been any philosophical change downstream in your competitor set to try to replicate what you do?

<A – Andrew Clyde>: Sure. So being more fuel oriented and having the history pre-spin of a company with refineries, terminals, supply positions. We're one of the largest shippers on the Colonial pipeline, which many of you know, goes from the Gulf coast to the New York Harbor and probably the largest gasoline pipeline system in the U.S.

We buy 50% of our product direct from the refineries in shipping on the pipelines. We have the space to be able to do that. So, we have an advantage there, we take it into a few of our own product terminals, but mostly the third parties where we provide that anchor tenant base load volume to them and get an advantaged rate for that.

So, the result of that is our laid down costs to get gasoline and diesel to our markets is $0.02 to $0.03 or more below the OPIS unbranded low price, which is another $0.01 below the OPIS average price and another $0.02 or $0.03 below the branded price you would pay in that market.

And that more than covers the cost of the working capital in the infrastructure or the fair market value of the line space et cetera. So it allows us to have low cost product. It allows us to have secure and a rate-able product as well. And so we could just buy-off the rack. And there've been times where that would have been advantaged, but we've also had times where a backhoe causes a Colonial pipeline to stop and they turn off the racks. And if you didn't have allocation and product in terminals along the way, you would be out of luck.

I think this last week, the Colonial line space has been trading for $0.025 a gallon, ARB has been open to the Harbor. We've seen some challenges in that area. So that's become an advantage. Again, there's probably a period over the last couple of years where that advantage wasn't as great as it was when you had excess refined product.

But markets like these ultimately go back into equilibrium. And so that advantage is showing back up again. Others could emulate this practice. They could buy line space, they can rent line space. There was a period where it was selling for a premium and then when the advantage went away, people stopped doing that. So, you've really got to be committed to it and have the volume or the ratable secure aspect of it is important as well.

We have supply spot index contracts for the majority of our other barrels. So it's basically a agreement with a refiner on a spot basis where we then pull at a differential from different terminals and others can certainly mimic that as well. And there's plenty of retailers who have the scale and scope to be able to do that and get some advantage.

So, I would say there's nothing unique about anything that we're doing, but the combination of all the things we're doing at the scale we're doing it across all the markets is a real capability and allows us to just take advantage of shifts in the marketplace when needed.

So, it's just something as a capability, we've decided to focus more on others that may have a bigger merchandise business and geographic concentration decide they're going to get into a merchandise distribution centers and commissaries that's a similar capability

they've decided to focus on whereas we have such a larger distribution area for our stores in more rural areas that wouldn't make as much sense for us.

<Q>: So, Merch margins compressed maybe 50, 60 bps the last two quarters on a year-over-year basis. Anything in particular you could flag as to what's behind that?

<A – Andrew Clyde>: Yes, two things that are driving that. One is tobacco sales and contributions is a bigger part of the mix. Right? And so the important thing is merchandise contribution dollars increased significantly. And that's what you take to the bank. The percentage mix is a function of the relative mix of the products. So, tobacco was a higher proportion of that as we continue to take share in that category.

The second thing was the discounts and deferrals on Murphy Drive Rewards, which was about 30 bps of that is as well. And so as you're earning on the merchandise items in those burn discounts get allocated to the merchandise and those were the two biggest components of that.

<Q>: So, in this most recent quarter, I don't know, from our perspective, it looked from a fuel margin perspective environment, relatively unremarkable, but you managed to put up really strong gallon growth and above what has been kind of characterized as historically average fuel margins. What are you all doing and fuel to get both?

<A – Andrew Clyde>: Yes, so usually the third quarter is a quarter in which you would see high demand in the driving season. But, at some point of it, price is coming down somewhat seasonally. And so we expect some downward movement and that's really good for our business as spot prices come down. The retail price lags and we're able to widen our differentials and get both volume and margin. I'd say there was one episode when the Saudi refinery got bombed, we saw a sharp spike in the market and it came down right away. And the market restored prices fairly quickly in that period. But otherwise there was nothing remarkable about it.

So it really gets down to this store-by-store pricing, really understanding the competitive dynamics, knowing where and when to go after volume by widening your differentials where – frankly, by widening my differentials I'm going to get mashed immediately. And I get no volume juice from it and I give away all the margins. And so it's just being thoughtful at that level of granularity to be able to achieve those kind of margins and the volume.

So the overall third quarter environment should have been favorable for volume and margins. I think the way we executed it helped and I think Murphy Drive Rewards also helped because we are seeing more trips, higher gallons from our members versus participants or nonmembers as people only burning on fuel and then on the tobacco burning on there as well.

<<Ben Bienvenu, Analyst, Stephens Inc.>>

Where are we with Murphy Drive Rewards? It seems like you're using the basic functionality today, driving engagement, but in terms of when you start to think about making more tactical targeted use of that tool, what should we be thinking about?

<<Andrew Clyde, Chief Executive Officer>>

Yeah. So 2019 was definitely an investment year, we stood up the systems and a lot of those today was SaaS applications and so forth are part of SG&A, that are part of the ongoing. We invested a lot of non-transactional points in the first year for people to sign up and the Rev Up and all of that and really focused a lot of our associate time on getting customers to sign up.

So I think as of this week, we're at 11 million participants, well over 2.6 million members. And that's really what, seven months after national launch. There's plenty of companies out there that have been doing this for 10 years and maybe have 4 million members. So we're really excited about the efforts to gain that kind of traction. I think one thing I would note is we have a little over 6,000 engaged customers per store on the program.

And that's about four to five times what we see as the typical per store number in the industry. But it really shouldn't surprise you because we sell five times the industry average tobacco and three, four times the industry average fuel per store. So I think from an acquisition engagement standpoint, we feel really good about that.

On the targeted offers, we've done a lot of experiments as I mentioned. Okay. Here's an incentive to buy a three pack when you've only bought a one pack. And when you do it the second – when you do it, we're going to hit you again with a different offer two days later because you're going to a pack a day. Here's the next incentive and so forth. And with tobacco-only purchasers who've never bought fuel, here's $0.15 off just to them using kind of customer lifetime economics math to justify a discount to get them to come into the store.

And so we've proven ourselves, we can do all of those things one-off. But right now from the technology standpoint, it's a lot of work. And so we've identified several areas in which we're going to dedicate the resources in 2020 to focus on specific types of behavior changes to see how much we can move the needle in terms of gallon growth, merchandise growth, the efficiency of the program and various things that impact the entire P&L for the MDR part of the business.

And I think from that, we'll have a much clearer understanding of what is it this capability wants to be, right. What we don't want to do is spend a lot more money year-after-year building it into something it doesn't want to be. The customers don't want it to be that as well. We're also going to be looking at the ways to monetize the insights in a way that's appropriate with the customers and respects the privacy and all the arrangements we have with them.

Because we do believe the way we can organize the data in the analytics and the consumer insight that we can get from that is one of the most powerful tools out there. And when we've talked to our consumer package goods providers, they have told us specifically no one else can provide what you are providing in terms of insights. And there's a real value there.

So I think that's really our goal for 2020 is we've built it, the members came, now its like, how do we get the most value out of it. And from there we can determine what's the next wave of investments that we want to make from it.

<<Ben Bienvenu, Analyst, Stephens Inc.>>

There's been a lot of headlines around vapor, Juul in particular. I'd love to get your thoughts on the dynamics, your exposure to it, how you think about that as a risk or headwind to your business and how you mitigate that risk?

<<Andrew Clyde, Chief Executive Officer>>

Sure. So the vapor category in its entirety represents about 16 million of contribution for us. So that's kind of the value at risk. Flavors is a little more than half of that. We were very late getting into Juul because we were not confident that the supply chain capabilities could actually keep up with our demand and volume, so when we got in, there's always some – already some pressure around flavors. We sold through that very quickly when they got out. A lot of that transferred over to mint and menthol.

And now of course, I think Juul's announced that they're exiting mint. And so we'll have to see how that all plays out. So mitigation strategy in Q3, we introduced a third manufactured product, NJOY and it sold through very well. It had an aggressive starter pack price but that's now translated into repeatable, sustained refill sales.

And by the way, the other manufacturer's products didn't go down in that process. So that was an end, so we've mitigated, tailwind – headwinds around one specific manufacturer by introducing another. And I guess, the next thing you worry about is okay, what are the other regulations that could go on vapor.

If you eliminate menthol as well, then you'd have to see, okay, how many consumers are going to switch to a tobacco vapor product, how many are going to switch to an IQOS product? How many are going to switch back to a combustible product? There's a House of Representatives bill that's being tossed around currently that would ban, as a law, menthol cigarettes and menthol vapor products as well.

And so they would just completely change the landscape versus the master settlement agreement that tobacco manufacturers had with the Department of Justice and, given the FDA oversight on it, if the FDA overstepped its bounds, the manufacturers could sue and claim they've overstepped their bounds and they'd go into protracted litigation. If you pass a new law that says menthol tobacco products are banned, that's the new law of the land.

And so that's a whole different game. And of course, the tail end of that process, they'd slip in a federal excise tax increase. So those are the sorts of things that we have to navigate around. We'd estimate the flavor impact if they included mint and menthol could be $5 million to $10 million exposure to our business. We've been growing merchandise contribution $20 million a year. So what would you replace that with while, you've got the other products like IQOS that have gotten a FDA approval. There's other products coming in the market like CBD that we're looking at very closely.

But frankly, we need to make sure that it doesn't become like vapor 2.0 and becomes the Wild West in terms of people selling products that they have no idea what the ingredients are. So we're never going to be kind of just a first mover jumping into that. We're going to be a responsible retailer. We're trialing CBD at a few stores. We're treating as an age-restricted product, even though that's not a requirement to do so.

So we're going to be one of those responsible retailers only selling legitimate products. I think by example, if someone said, well, what would happen if minimum wages went to $15. It's about a $5 million to $10 million impact on our business as well. And so if you think about two of the biggest regulatory headwinds that we could face, that's the order of magnitude. And just remember $0.01 swinging gasoline margins is $45 million. So on a relative basis, those were things that could impact the business, but you would quickly make that up in a year or so.

<<Ben Bienvenu, Analyst, Stephens Inc.>>

Capital allocation is an important element of Murphy's story. It's just your philosophy on capital allocation, I know you and Mindy and the Board think about the way to maximize shareholder returns with the balance sheet as well, kind of appended onto that.

<<Andrew Clyde, Chief Executive Officer>>

So this is an industry sector where for decades retailers have typically overinvested on low return projects. And so you've got to hold a high bar to your capital returns. When we had the Walmart 200 and we look at that as a portfolio and then we look back as a portfolio. It got returns that more than met our expectations.

But then as we look beyond that and say, okay, most of the good and great supercenter locations have been built. We need to think about what format do we have the right to win with in our markets with consumers that can give us the best returns. And we stepped back and said, okay, let's look at our 2,800 square foot format, it is still modular build. We have experience with that and that's what we're proceeding forward with.

But we still anticipate doing that with this balanced capital allocation notion of 50% growth, 50% share buybacks, which has been our history since the spin. This was a volatile business so if you think about share buybacks versus dividends, a very small dividends,

not that meaningful. And from all the research and investor feedback and the investor perception studies we've done, we don't get a lot of credit for having a small dividend.

So we think it's just – it's tax efficient and effective to do the share buybacks. The way we think about the share buybacks is simply, given our view of what is the potential of this business. If you step back at any point in time and look back three to five years, are you going to be happy buying shares at that price.

And so we've got a very robust shareholder value model, all the initiatives that we talk about, we have a view of what the value potential of those are and what we can get from those. We know the benefit of the organic growth that we have built in. And so when we crank our shareholder value model, it spits out a number every year of what the share price should be.

And so that gives us a level of confidence buying shares in the current market. It may not look great, one month later or two months later on an earnings call, but we have a high level of confidence that three years, four years, five years later, everyone's going to look back and say that looked really smart. And so in the last quarter we bought back 1 million shares, paid a little over $85, I think for the shares.

We bought back 36% of the company since the spin. The average price is $67. I think it's trading around 115, 116 right now. And so I think it's just the level of conviction the management team has, the Board has, I think the market gave us some credit for in the last couple of weeks, guides us to how we think about share repurchase. I think in the current – in the next five years, our capital spend is going to be more back weighted in that five year period than front weighted, which is why the Board approved the $400 million program at the end of Q2.

And then, within any quarter, we're going to try to be thoughtful about when we buy, the pricing parameters, et cetera, other factors that may be out in the market. And I'll be the first to tell you that sometimes we get too cute with that. We probably thought too hard about IMO 2020 in terms of what the potential risk could be. It looks like they're going to get a lot of get out of jail waivers and small ports from the harbor-master, so it doesn't look like it's going to be as big a deal as maybe we thought it would be.

But anyway, that's a little bit of our sense. It's an important part of our overall model. I think from a balance sheet standpoint, this was a business that doesn't want to have a lot of fixed costs. It doesn't want to have a lot of exposure to inflation. So if we can maintain a two to two and a half times debt level and stay within that with the EBITDA growth we've had, we can take out a little bit more debt every few years and just continue this formula, if you will, for growing shareholder value.

Q&A

<Q>: [Question Inaudible]

<A – Andrew Clyde>: That's a really good question and we've thought about that a lot as well, just in terms of their performance when we turn them around. And so that's one of the things we'll evaluate. We certainly have the capital to do that. If we did that, we'd dial back on the share repurchase. So it's nice to have the balance sheet and the free cash flow, operating cash flow and the leverage to be able to do that.

<Q – Ben Bienvenu>: You all did a bond refinancing, it was well over subscribed, very successful. What is the bond – this is a business with volatility quarter-to-quarter, what is the bond market focused on for you guys, how are the questions you get from them different from the questions you get from the equity markets?

<A – Andrew Clyde>: Yeah. So they're not concerned about the next quarter or the next quarter. It's a much longer term view. I mean, I think they really think about capital discipline, use of proceeds, long run margin et cetera. And I think what we've been able to do since the spin is execute consistently, do what we say we're going to do. So it allowed us to get some upgraded ratings from the agencies that's then translated into the bond investor confidence. It's a lot of the same kind of questions, but it's just with a longer term view.

I think they want to make sure that you're not growing for growth sake. You're staying within certain guardrails around the business that we've described. And I think they've consistently seen us do that. They're confident we're going to have the cash flow to pay the interest and the principal and the like. So I think 4.75 on a 10-year unsecured for non-investment grade was pretty good, and I think it was trading up 102% within a few days. So we probably left a little money on the table, even though the bankers told us we didn't.

<<Ben Bienvenu, Analyst, Stephens Inc.>>

Any other questions from the audience? Andrew, thanks so much for your time. Appreciate it.

<<Andrew Clyde, Chief Executive Officer>>

Great, thanks Ben.