Company Name: Murphy USA Inc. (MUSA)
Event: Raymond James 37th Annual Investors Conference
Date: March 8, 2016

<<Benjamin Brownlow, Analyst, Raymond James Financial Inc.>>

Good afternoon. I'm Ben Brownlow, the Raymond James analyst covering midstream fuel suppliers and convenience retailers. And I'm pleased to introduce Andrew Clyde, the CEO of one of the largest convenience retailers in the country, Murphy USA. Andrew.

<<Andrew Clyde, President and Chief Executive Officer>>

Great. Thank you, and good morning. And thanks to Ben and Raymond James for hosting us today. As always, we have a cautionary statement around forward-looking statements in the presentation. For sake of time, I won't go through those, but please do take note of those. I'm joined today by Mindy West, our Chief Financial Officer, and Christian Pikul, our Head of Investor Relations. And we'll be available for Q&A when we're done here. And then our breakout session, I know it'll be a tough choice between that and lunch.

We hope that some of you can join. We are webcasting this. So we thank the folks that have joined by webcast. And we'll have a transcript of this available on our IR site. So Murphy USA spun off from Murphy Oil Corporation in late August of 2013. We came out with a very differentiated strategy, and over the last three years we've really proven out that strategy. For those that know us, we are a low- price, low-cost fuel and convenience retailer. The majority of our 1,335 sites are located in very close proximity to Walmart Supercenters, probably the best demand aggregator for price-sensitive consumers you can have.

Our strategy to compete in a very competitive market has five elements, and they're very coherent and hang together. Our growth story is about organic growth versus acquisitions. We started with a strong tobacco base. And so we've been taking steps to diversify our merchandise mix. We have a cost leadership position that we've been sustaining. We are in the fuel business. It's volatile, but we have capabilities that allow us to create advantage from that volatility.

And we believe in investing for the long term, both in our real estate and our assets, our people, and our shareholders. And the free cash flow from this business allows us to demonstrate significant shareholder distributions that we've done since the spin, as well as invest in growth. When you take that strategy together, we have a business model that's been resilient to and takes advantage of the underlying fuel price volatility. And earlier this year, we announced an independent growth plan where we will be pursuing locations in front of supercenters, purchasing from third parties as we've done in the past for many years, but not acquiring more land from Walmart.

And we describe that as our independent growth plan, and it combines modest unit level growth along with shareholder-friendly distributions. We think since the spin we've executed and demonstrated a strong track record. And you can see on the right our relative share performance

versus two of the large indices. And as we'll go through today, we believe we have a very bright future ahead of us. This is a really simple business at the end of the day. And so we like to think about our value creation formula in real simple terms as well. So how do we grow earnings and earnings per share?

First, it's about growth. And as we said, it's organic growth at the unit level, and with this independent growth plan selecting sites that are going to be in the highest return markets, which we'll be pursuing. But at the same time, we're making meaningful upgrades to our network which are adding to our per-site cost. If that's the force multiplier, you've got to have something worth growing, and that's our core business, which is made up of our fuel contribution, the fuel breakeven requirement, which is the merchandise margin offset by the cost, and then all your other corporate costs, SG&A, taxes, interest, and the like.

And from a fuel contribution standpoint in a flat to declining fuel demand environment, growth is largely about growing share through new units. The advantage we have is in our cost of goods acquired through our proprietary supply chain, and we capture margin through volatility. Our fuel breakeven is a function of our merchandise gross margin growth and cost leadership. Where last year we grew store operating costs, we held them flat and we're guiding to lower site operating costs this year. And we're continuing to make very active step-level improvements to our business.

In our corporate costs, the things we'll be talking today are about our scalable systems and process initiatives and tax efficient asset sales. So that drives the core earnings. Then you've got the denominator of EPS, which is your share outstanding. And since the spin, we've been very active. We've had share repurchases totaling $300 million. And as part of our independent growth plan, we announced $500 million in share repurchases through 2017. And so now, with clarity on our future, we also have the balance sheet flexibility to add the appropriate leverage to our business.

And so these key points we've illustrated, basically make up the framework for today's presentation that I'll go through quickly. So unit growth, this will continue with our express-branded stores. And so the difference between a Murphy USA store and a Murphy Express store is whether we acquired it from Walmart and whether it's tied into the credit card and gift card program. The USA stores are. The Express stores aren't. And as you will see, we did 73 stores in 2015, including one raise and rebuild. We have 58 stores left from the up to 200 Walmart deal we did in 2012. And so the balance of our growth this year and the majority of our future growth is going to be in Express stores where we acquire stores, locations from third parties, but they are still in proximity to supercenters, which is this great demand aggregator, traffic generation for these price-sensitive customers.

One of the key questions we got when we announced the independent growth strategy was, well how do the return profiles compare between a Murphy USA store directly on the Walmart parking lot or on the out lot in front of it, to an Express store, which is often typically in the out lot in front of it, across the street, or no more than a half a mile to a mile down the road. And we know from a consumer behavior standpoint they're very similar. We did 100,000 consumer

intercepts last year, and we found in both occasions 50% of the customers say they are going to our store before or after a trip to Walmart.

And so not surprisingly, the traffic and the contribution from fuel and merchandise is similar. This example of stores are stores that were built and started operations by the end of 2014, and they represent our top three market clusters the way we segmented sites. These are the stores, type of stores we're going to be focused on going forward. And so you can see the Express stores have higher total contribution. They have slightly higher operating expenses, which, in part, reflects the credit card mix because they're not on the Walmart gift card or credit card program where we would have an advantage interchange.

And as a result, they end up with a higher after- tax cash flow. And when you divide that cash over the cash investment, they generate very similar unlevered returns. And so we feel very confident going forward with this independent growth plan based on these returns. We're also continuing to reinvest in our network, and that provides great growth opportunities. Most of our stores that were built starting in 1997, were built on four-tenths of an acre, they had four pumps, and they had 112 square-foot kiosk in front of them.

And while we've added to them over time and our new stores are 200 square-foot kiosks with coolers in front of them, and most of our stores now are the 1,200 square-foot stores, there's a great opportunity to do raise and rebuilds on the older stores. We did our first in 2015. We replaced the kiosk with 1,200 square-foot stores, more fuel dispensers. And the initial candidates have a great profile. They have higher traffic. They have better-than-average fuel margins. They have great potential for merchandise uplift.

And we can increase our fuel volume with more diesel dispensers and a better fuel mix at those stores. We've identified 135, so about 10% of the portfolio. We're going to do 10 stores in 2016, and then moved to 20 stores a year after that. And given the premium locations, the after-tax IRRs are between 15% and 35%. The refresh program is a program we've been doing for a while, but, really, as Walmart upgraded a supercenter, we would do a slight renovation on our existing store.

What we realized once we became a standalone company is we under invested in our network. And it was starting to show, especially given the higher than industry average throughput of our locations. And so to get out in front of that, we launched a refresh program of 300 stores in 2015, which we will continue for the next two to three years. It updates the look and feel. It makes it a better look and feel for the customer. And we've been able to demonstrate 1% improvement in our store fuel volumes, as well as our merchandise sales. And because of some of the improvements, we will have lower maintenance cost over a 10-year period.

And on slide 8, we have a picture of the before and after of that program. And you can see the key differences on the right. You've got a new canopy wrap. The exterior of the building, which was metal paint before, that was repainted, has a brick veneer on it. We've done bathroom upgrades and the like. We have other programs that go on at the same time - LED lighting, Super Coolers. We installed a new security system across our network last year as well. And so we believe this is a business in which you have to continue to invest. In many of the old legacy sites

you see out there, their owners have taken more of an invest-and-forget approach. And if you want to stay vital in this business, you have to continue to invest. The good news is, our reinvestments generate good returns and paybacks.

So let's switch gear to fuel. And what does the fuel environment look like? What this chart shows is what the cumulative demand has done over the last decade. And if you look at the red line, that's U.S. fuel demand. And on a cumulative basis from the last decade, it's down 1%. It's been trailing up the last two years. We expect this year, and 2015 last year, will probably be happy 2.5% to 3%. But on a cumulative basis, it's down 1%.

If you look at EIA or any of the other forecasts, it's projected to be flat or down for the foreseeable future. But we just know there'll be some ups and downs depending on what fuel prices are and what's the mix of new cars going into the fleet? Murphy USA's average per site fuel volume has been 0% over that same time. In 2006, 2007, and 2008, as fuel prices were rising rapidly, low-price retailers like Murphy USA got more consumer demand as people became more and more frugal.

And as prices moderated, that customer on the margin shifted back to other outlets. We also saw in this same period increased competitive pressure from grocery store chains with their promotions and the cross subsidy between fuel and groceries. And while we were early with Walmart on the discount program, we didn't have as good a response to that. And so you can see over the last three years, our volumes have moderated and have been basically plus or minus 1%. On a cumulative basis though, we've grown our volumes by 57% over the last decade. And so the headline message here is, per-store volumes are going to be plus or minus 1%, and the way you're going to grow fuel volume is largely through adding new stores.

What makes Murphy USA unique? One of the things that truly makes us unique is our differentiated advantage fuel supply capabilities. If we were a big box retailer or 7-Eleven or someone that was more focused on the merchandise side, you would expect us to be talking about our own central distribution system, our commissary systems, our food offer, et cetera. But that's not our business with our small kiosks and our small stores. So what's the differentiated capability that sets us apart? It's our fuel supply chain.

And the way we do that is 50% of the gallons we sell are sourced through proprietary barrels, meaning we buy them from the refiners in the refining centers, we ship them through the pipeline systems for which we have access through our historical shipper status. And that takes decades to build. If you wanted to get in this business tomorrow, you could not go and get pipeline access on most of these pipelines. We take that into mostly third- party terminals.

We blend it with ethanol. That captures the RIN. And that leaves us with a landed cost of supply when you add that supply advantage plus the RINs, that's going to be advantaged over our competitors. 42% of our volume is through third-party contracts but is with refiners sourced on a spot price basis. So say Gulf Coast plus the transportation differential to the terminals, and where we've been able to negotiate the RIN value in that transaction.

Why do we have an advantage? Because we have an alternative. We could ship our own barrel into that market instead of having that spot index contract. The advantage for the refiner is, they would prefer to keep our barrel out of that market, keep that market in equilibrium. So they're more willing to discount to Murphy USA because of that alternative we have versus their next-best alternative of shipping a barrel out of that market. So we've got access to line space. We have access to terminals. We have access to the RINs through the blending. We have the credit. We have the scale and scope to hold the working capital and manage through the volatility that smaller competitors don't have.

As we've said, this is a volatile business, and the margin capture follows the underlying volatility. And what you typically see is a period of up and down spot prices, which is illustrated in the red, with a lagging retail price. And if you look down at the bottom, we've got the retail price the way we report it, and you can kind of eyeball the trends. When spot prices go up, retail margins are compressed. When spot prices fall, retail margins expand. When they fall really hard like they did in Q4 of 2014, retail margins expand by a lot.

And then you see the additional contribution from product supply, wholesale, and RINs. It is also a function of rising and falling prices, but there's other factors like, is the market long or short? Are inventory levels high or low? Are the ARBs to New York Harbor and other markets out of equilibrium or are the ARBs open? And so forth. But when you add that up, it leads to a very strong margin profile. It is going to be volatile. And we've projected that the retail margins will be $0.12 to $0.13 over time for our business, and then you add product supply and wholesale plus RINs to that.

When you add it all together, and this has been sort of a source of complexity for people to project the product supply, wholesale, and RINs piece, it is consistently accretive to the total fuel contribution. And so if you look at the retail margin in blue, typically around $0.125 to $0.13, with a couple of periods of outsized margins. The PS&W plus RINs, has been adding about $0.025 to $0.03 consistently to that business. And you can see even before 2013, before RINs were on the map, it added at least $0.015 to the business.

So let's talk about our core operations. The way we measure that is in our fuel breakeven requirement. And you see the definition at the bottom. It's basically the merchandise margin minus the site operating expenses minus your field G&A divided by volume. And for us, the merchandise margin covers most of that but not all of that. So this breakeven number's really expressed in a negative number. So what it says is, in 2013, the year of our spin, we needed $0.034 per gallon fuel margin to break even. And so if we earned $0.13 in that year, if you subtract the credit card fees that would be the residual profit.

So this is an important measure of any firm's competitiveness. And what you can see is, since the spin, we've improved our competitive by a cent per gallon. And you may say, a penny well, what does that mean? When you sell 4.2 billion gallons of fuel a year, that's worth $42 million to the bottom line EBITDA. And so our projections for 2016 are to get below $0.02. And we believe that we have lots of runway left to continue to improve that.

So in some ways people have gotten more concerned about plus or minus 1% in fuel volume, when there's a lot more opportunity in improving your merchandise margin and your side operating cost. So how have we done that? Well, first is our merchandise margins have expanded as we've enhanced our product mix. As I said before, early in this business, we had a large proportion of our sales on tobacco. And it still represents a significant portion of our gross margin dollars.

To put it in context, we sell four to five times the tobacco products that the average competitor does. And so you may not like the 10% margin, but if you sold their level of sales, you'd be getting a 40% to 50% margin equivalent on that, which you would all find very attractive. And so what you've seen is, since 2013 when you had the tobacco contracts, MLP and others, that clawed back some of the benefits and changed some of the competitive dynamics, we've been able to hold our tobacco gross margin dollars constant to slightly rising.

And as I'll talk about, our new Core-Mark contract is going to allow those to expand in 2016 and beyond. But what we've really been able to do is improve our non-tobacco gross margin dollars. And you see that both reflected in the gross margin dollars per site as well as the percent of gross margin dollars going from 32% to 41%, and the unit margin growing from 12.5% to 14.4%.

We're never going to be a retailer that's going to have 30% unit margins, in part, because we don't have the stores to have the 50% to 60% unit margins on fresh food and those offers, but we're also going to have a large proportion of tobacco in our mix. We have not been standing still. We've been very active since the spin. One of the things that we worked very hard on in 2015, was negotiating a supply contract with Core-Mark, having been with our previous supply chain partner for 20 years.

We implemented a five-year contract. It's more transparent. It has a fixed rebate structure. We're going to see the improvements in both enhanced margins for both tobacco and non-tobacco, as well as lower delivery fees. And we've already completed the nationwide rollout in 30 days starting in late January. Core-Mark has already met or exceeded its service level and fill rate metrics. And so investors will be able to start seeing those benefits in Q1.

In front of our older kiosks, we've been adding Super Coolers, which doubles the capacity of the beverages at the store. We get more higher-margin items in the mix, as you see carbonated soft drinks coming down. We're seeing beverage sales increasing by 15% at those kiosks. We added 60 in 2014 and 2015, and we're going to double that number in 2016. And this just gives you a picture of the left side, what we had before, and on the right. So it makes a significant impact. The other thing is, when we have our promotions where you buy three beverage items and get $0.10 off. The sales go up pretty dramatically. This allows us those beverages chilled quicker and store more, and so it allows us to be more effective with those promotions.

Cost leadership remains the hallmark of a low-price retailer. And this just shows what our site operating expenses have done. I think the trick in this business is, if you can grow merchandise margins and hold site operating costs constant, that is a huge win. Last year we held our site operating costs flat, 0%, so beating inflation. And with our ASaP initiatives where we're going to

optimize our store labor and other activities, we've guided to 2% to 4% lower store operating expenses.

We're also focusing on our SG&A. And a lot of the ASaP initiatives this year will be targeted towards improved system, whether it's in fuels management, information management and dashboards, or back office accounting. We have $40 million program that we've been spending over a three-year period. That will wrap up in 2017. So we'll not only see the cost of that initiative fall out of SG&A, but we'll start seeing SG&A benefits flow through as well. The one-time gains for merchandise inventory reduction pay for 75% of that initiative. And that's just getting a week's worth of excess inventory out of the stores on a one-time basis.

Another thing we've been busy doing since the spin is discovering the value and monetizing a number of non-core assets. And we're excited to have completed the turnaround on our Hereford Ethanol Plant last year, realizing $98 million for that. And then discovering the true value of the CAM Pipeline system was a crude pipeline that was part of the old Murphy Oil Meraux refinery. And the value of that asset increased significantly with some of the shale approved plays. So since the spine, we've generated $362 million in non-core asset sales, and we're pursuing efficient tax free exchange treatment to the more recent sales.

Capital allocation is probably my most important job and that of our Board's. And we've been very balanced in our approach to date, balancing growth with shareholder returns. The big difference in terms of whether we did the big Walmart deal or not would have meant how much capital would have been allocated to growth if you ramped up to 120 to 150 stores a year versus staying at a more modest levels? And so not surprisingly, with that clarity in sight, knowing we would continue to grow at the modest level we've been growing at, we announced another large share repurchase $500 million through 2017 that we've started on.

Our balance sheet remains very conservative. Prior to the announcement, we kind of held the dry powder, not knowing what the requirement might have been had we pursued that transformational growth opportunity. Again, with clarity on that growth opportunity, we can take steps to add leverage to our balance sheet in a prudent and effective way. We want to maintain our debt-to-EBITDA target of below 2.5 times.

We believe that having a conservative balance sheet, as the low- price retailer in a volatile business, especially if you look at where crude prices are and the likelihood they will experience some run-ups where you have some compression on your margin, you want to have a business model that stays resilient to that environment. But if you think about what we've done since the spin, we've paid back $150 million of the term loan. We've executed $300 million in share repurchases. And now we've announced up to $500 million through 2017. So we'll be able to start taking the appropriate steps to add leverage to our balance sheet in a way that's thoughtful.

If you take all of this together, we're really excited about our independent growth plan. And when we were giving the guidance for 2016, as you see here, you can see how the sum of all of our efforts really start to play out. And I guess it's best reflected in the EBITDA guidance of $400 million to $440 million, up to $100 million improvement over 2015. The biggest variance in terms of hitting our guidance last year was largely in the trade-off between product supply and

wholesale in RINs, and we expect this year as well, if RINs continue to stay at $0.75, there's probably some pressure on product supply and wholesale that offsets that, but the two of those together should be able to generate an incremental $0.025 to $0.03 per gallon.

So as we conclude, we believe Murphy USA has a bright future ahead for our shareholders. Our strategy remains largely as it is. Our business model stays resilient and our commitment to our shareholders remains strong. The independent growth strategy really provides clarity on how we choose to do sites and how we allocate capital between growth and shareholder distributions. That's really it. Our core strategies, those other five elements, remain intact. We remain internally active with a very continued focus on performance improvement, as you see through initiatives like Core-Mark and ASaP, and making this business more competitive.

And so we look forward to building on that track record of performance, executing our strategy, and delivering on the commitments we made to our shareholders. So with that, I'll conclude my prepared remarks. Thank everyone for joining the webcast. If we have time for Q&A, we can do that, and we'll have more Q&A in the breakout session.