S&P Global
Market Intelligence

Murphy USA Inc. NYSE:MUSA

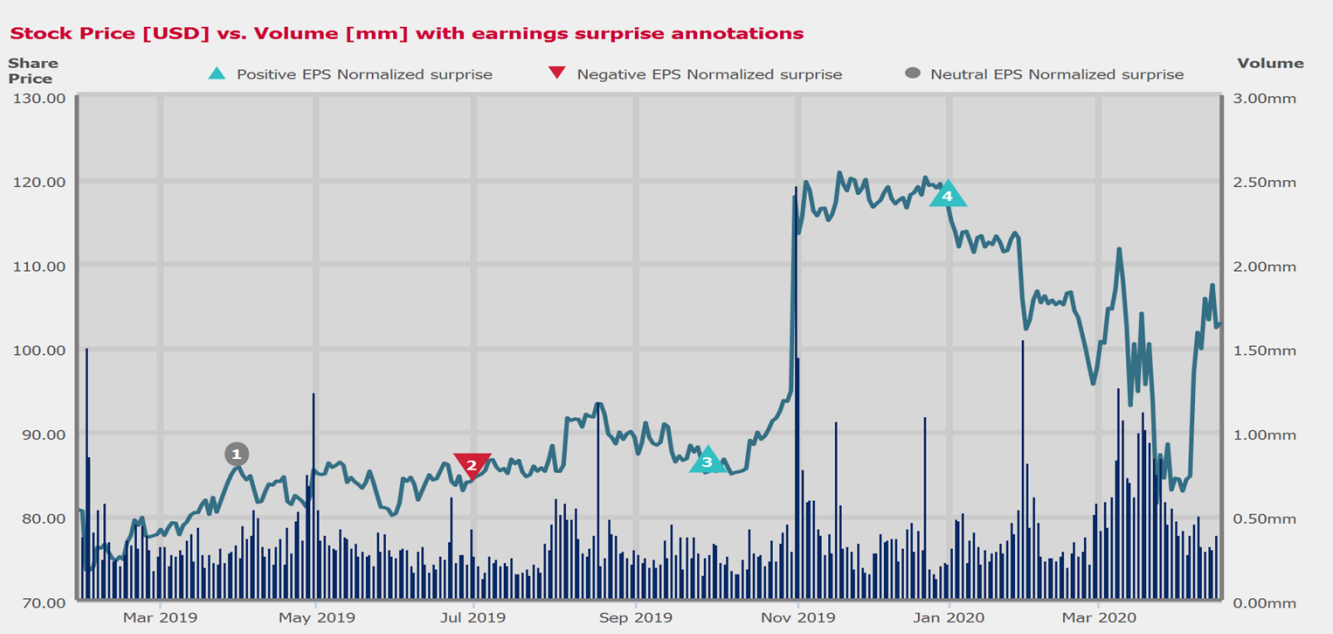
FQ1 2020 Earnings Call Transcripts

Friday, April 17, 2020 3:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2019-	-FQ1 2020-			-FY 2019-	-FY 2020-
	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS
EPS Normalized	1.46	2.22	2.96	▲32.74	5.04	6.24
Revenue (mm)	3569.53	3042.33	3184.80	▲4.68	14143.99	12403.16

Currency: USD
Consensus as of Apr-17-2020 12:55 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2019	0.17	0.17	1 0.00 %
FQ2 2019	1.08	1.03	2 (4.63 %)
FQ3 2019	1.46	2.55	3 74.66 %
FQ4 2019	1.46	1.54	4 5.48 %

COPYRIGHT © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved

Table of Contents

Call Participants	.....	3
Presentation	.....	4
Question and Answer	.....	10

COPYRIGHT © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved

Call Participants

EXECUTIVES

Christian Pikul
Senior Director of Investor Relations & Financial Planning and Analysis

Malynda K. West
Executive VP of Fuels, CFO & Treasurer

R. Andrew Clyde
President, CEO & Director

ANALYSTS

Benjamin Shelton Bienvenu
Stephens Inc., Research Division

Bryan Cecil Hunt
Wells Fargo Securities, LLC, Research Division

Christopher Mandeville
Jefferies LLC, Research Division

John Macalister Royall
JP Morgan Chase & Co, Research Division

Robert Kenneth Griffin
Raymond James & Associates, Inc., Research Division

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Presentation

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Murphy USA First Quarter 2020 Earnings Conference Call. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Christian Pikul. Please go ahead.

Christian Pikul
Senior Director of Investor Relations & Financial Planning and Analysis

Hey, good morning, everyone. Thanks for joining us. With me, as usual, are Mr. Andrew Clyde, President and Chief Executive Officer; Mindy West, Executive Vice President and Chief Financial Officer; and Donnie Smith, Vice President and Controller. After some opening comments from Andrew, Mindy will provide an in-depth overview of our financial results and outlook, and then we will open up the call to some Q&A.

Please keep in mind that some of the comments made during this call, including the Q&A portion, will be considered forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. As such, no assurances can be given that these events will occur or that the projections will be attained. A variety of factors exist that may cause actual results to differ. For further discussion of risk factors, please see the latest Murphy USA Forms 10-K, 10-Q, 8-K and other recent SEC filings. Murphy USA takes no duty to publicly update or revise any forward-looking statements.

During today's call, we may also provide certain performance measures that do not conform to generally accepted accounting principles, or GAAP. We have provided schedules to reconcile these non-GAAP measures with the reported results on a GAAP basis as part of our earnings press release, which can be found on the Investors section of our website.

With that, I will turn the call over to Andrew.

R. Andrew Clyde
President, CEO & Director

Thank you, Christian. Good morning, and thank you to everyone for joining us today. I hope everyone joining in live or listening in or reading later is doing well as we go through this unprecedented period in our country. I hope that you and your loved ones are healthy and safe. Most of us have been through periods of disruption where similar unsettling cloud surround us. I personally think about the 2008 Great Recession and the crude price fall off that precipitated it, the dot-com crash as we saw new but less proven business models collapse, and the terrorist attacks on 9/11 and the change in the American psyche as we worked together back towards normalcy knowing full well some things would never be the same again.

In my personal view, what makes this period in our history so dramatic for so many people and for so many businesses is that we have compounded on top of one another somewhat similar types of events but a significantly larger magnitude, compressed the combination of their impacts into shorter periods of time and have far less certainty on what the eventual recovery looks like for the everyday life of individuals as well as more proven established businesses. As I noted in my outreach calls to our 1,500 store managers and field personnel last week, many of them have been battle-hardened from hurricanes, tornadoes and other events, but nothing quite compares to what we are going through now.

At Murphy USA, our business has been specifically impacted by the combination of 3 historic events: the rapid and steep fall in crude oil prices that resulted from the price war between Saudi Arabia and Russia and the resulting oversupply in domestic and global markets; the global COVID-19 pandemic that introduced the dangerous fires throughout our country, shutting border, cities and many businesses, leading to significant demand destruction for most of the products that we sell to our customers; and the large-scale government response and intervention to provide for safeguards for our people and for our economy, shoring up liquidity for businesses and for individuals who have found themselves out of work.

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

What I would like to do on today's call, to the extent I can, is to use these events to frame how our business has responded to and is performing in the current environment, and how our business is positioned to endure through this period of uncertainty, knowing full well we can't predict the future. What I hope you take away from today's call is that the principles upon which we have designed and built our business model has enabled Murphy USA to rise to the challenges of these events. And at the heart of this business model is an incredibly engaged and dedicated team of close to 10,000 employees who rise to the occasion each and every day to meet the needs of our customers.

As an essential service business, we are indeed very fortunate to be able to serve the needs of our customers across the communities in which we operate during this period. We are extremely grateful for our employees and our key supply chain partners who are at the front lines making this happen. As shareholders, we can never lose sight of who really makes this business tick because without our customers and the teams that serve them, we have nothing.

I would like to start our performance discussion by talking about the impact the dramatic falloff in the price of oil had on our business. While the drop in crude prices from around $62 a barrel in January to just below $20 a barrel in late March was not of the same magnitude as we saw in 2008, it occurred in a much, much shorter time frame. The immediate result of this rapid drop was the generation of total fuel margins of $0.225 per gallon, which in turn led to our record Q1 financial performance. It is important to remember the falloff in crude prices was largely driven by geopolitical events that led to the high-margin environment going into the COVID-19 crisis. And in that period, we were experiencing fuel volume increases of approximately 2.7% through February on a same-store basis as our fuel pricing initiatives were delivering exceptional results.

March became a story of 3 periods. In the first 10 days of March, before the COVID-19 crisis became widespread, consumer demand was very strong, and we were seeing per-store volumes up 6.2%. However, the pursuant demand shock as shelter-in-place orders across the country took hold had a significant impact on the second half of March performance. During the middle 10 days of the month, as schools closed and more people started working from home, we saw some prebuying behavior. And as a result, per-store volumes remained relatively strong at 2.7% over the prior year period. The last 10 days of March, however, exhibited the full effects of shelter-in-place orders with per-store fuel volume showing year-over-year declines of 31.7%.

April month-to-date fuel volumes have leveled out at an average decline of 31. 6% with the variance of daily levels reflecting a variety of factors, including paydays and government stimulus payments as well as prior year effects.

Higher total margins endured throughout the quarter as crude prices continued to fall. What should no longer be a surprise to anyone is that our net supply margins offset some portion of the retail margins in this price environment. Strong margins have endured in the first half of April but continue to trend down. How quickly margins return to normal levels will be a function of how and when crude prices restore, demand recovers and local market and competitive dynamics respond. That said, we believe we should expect to earn higher total fuel contribution than many of our peers during this important -- during this period for 2 important reasons. First, assuming our stores continue to perform at around 70% of normal volumes, we will fare better than the average industry store, which, based on third-party sources, suggest a national average decline of around 50% of normal volumes.

Second, given our normal fuel margin is much lower due to our everyday low price position, the relative percent increase in our fuel margin is significantly higher than the relative percent increase of the average firm. When you multiply our relative volume change times our relative margin improvement, we expect to be at or above 100% of normal total fuel contribution levels for a longer period of time versus our peers.

Last, given our very low fuel breakeven cash margin requirement of less than $0.01, the impact of lower-loss gallons has significantly less impact to us than the average industry site, let alone the marginal industry site, which has a breakeven requirement of over $0.25, which after losing half its gallons rises to $0.50 per gallon.

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

As I wrap up the discussion on fuel performance, I want to especially thank our fuel carriers and suppliers who have worked with us through so many challenges, including the destruction of 1 carrier's headquarters in Jonesboro, Arkansas, from a recent tornado.

Next, I would like to discuss how COVID-19 has impacted our business beyond fuel demand, particularly our merchandise sales. As most of us are personally aware, the implementation of social distancing and shelter-in-place orders has created a stockpiling mentality. If we look at March through the same 3 periods, we were having an excellent quarter-to-date in the merchandise business with per store sales up 7.1% in the first 10 days of March versus prior year, building on the strength we saw in January and February performance, which was comping very well in both tobacco and nontobacco, erasing Q4 2019 headwinds. In the middle of the month, merchandise sales per store increased to 29%, above prior year sales as consumers stocked up on essential items, particularly cigarettes. In the last 10 days of March, per store sales were flat versus the year ago period with continued strength in tobacco sales showing a 6% year-over-year improvement, offset by a reduction of nontobacco sales, which were down 13.3% as both fuel and tobacco traffic was lower.

Again, based on Nielsen and other third-party sources, we believe our performance in our core categories is outperforming what the industry is seeing on average. We believe 3 factors really drive this. First, there's absolutely no doubt in our minds that our proximity to Walmart supercenters and the uplift in traffic they are experiencing is having a positive and differentiated impact on our business. The strategic relationship has always been important to our model, but it is even more so in the current environment.

Second, our value-conscious customers have become more loyal to us, and we have added customers and share of wallet, as evidenced by new Murphy Drive Rewards members. We are seeing trip spike on key dates, like the most recent government stimulus check payments, and other payday events where more customers are stocking up with us before or after stocking up at Walmart.

Third, exceptional operational execution from our store associates along with support from our incredible supply chain partner, Core-Mark, and our manufacturing partners have allowed us to maintain high in-stock levels as we quickly stocked up and built inventory early on our highest-selling items.

As a result, performance in categories like cigarettes have remained positive throughout, and we have seen material shifts in carton buyers going from 48% to 58% of purchases. As some competitors do not even offer cartons, this has led to notable share gains.

Through the first 2 weeks of April, total merchandise sales are up 8.3% with tobacco up 13.3% and nontobacco down 4.3%. Beer and alcohol sales were up 9.1% and general merchandise is up 6.5%, in part due to standing up a new hand sanitizer supply chain in short order. While we have temporarily eliminated prepared food, like roller grill items and our mug refill program, for customer safety considerations, these categories represent a small part of our overall product mix today.

The third and last discussion topic relates to the unprecedented steps our government has taken to limit and manage the spread of the virus and provide liquidity to the overall economy. Let me start by stating clearly that at this time, Murphy USA does not anticipate the need for government financial assistance. As Mindy will elaborate on further, our cash position is strong; we continue to generate significant operating cash flow; our credit facilities have capacity; and our debt maturities are well down the road, thanks to our well-timed refinancing last year at very attractive rates.

Our conservative balance sheet is yet another strategic asset that was an intentional design element of our business model. As a result, we continue to invest in our new stores and raze-and-rebuild opportunities. And while we have the flexibility, if necessary, to adjust our capital plans for the second half of the year, we have no plans to do so at this time. Our current projects are all on track with only 1 delay due to weather.

As I said before, we are very fortunate to be an essential service provider and we remain open for business. As such, we have taken significant measures to ensure the safety of our customers and our associates. We have added labor hours to our stores for more thorough and frequent cleaning procedures, and we now self-stock some items that are simply dropped off by certain distributors. We have provided

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

various PPP -- PPE items to our staff and, when available, to our customers, including designing, sourcing, installing protective sneeze guard barriers for our walk-in stores in less than a week. We are meeting and, in some cases, exceeding the standards and guidelines set by various national, state and local governments.

The results of our efforts is that we have kept our network up and running with no store closures currently. We have temporarily closed 43 stores to date for deep cleaning, which typically last a few hours. Opening hours have been reduced at 74 stores due to mandated curfew restrictions, and we have reduced opening hours at another 79 stores on a discretionary basis for safety or security concerns. We continue to hire new associates, and we have a record low 8 store manager vacancies across the entire chain.

The benefit of maintaining opening hours and increasing operating hours, labor hours, is that we are at least able to provide our store associates with the ability to maintain their income. We have provided assurance around Q2 commission levels, and we are ensuring schedules give our managers time to balance demands at work and at home. We have also added a variety of benefits, including an expanded paid sick leave policy for COVID-related matters. I hosted calls last week with all our store and district managers where they continue to provide direct feedback to me, my leadership team on how we can best work through this together. In return, our associates are doing what they are famous for, delivering friendly service and upselling, even in the face of lower demand, keeping their stores clean and in stock and engaging their customers. We couldn't be prouder of our team. Their relationship with their customers is truly what defines our brand.

Our customers have noticed the steps we are taking in our stores for their safety and for the benefit of our staff, and it is reassuring to hear their direct feedback daily through a variety of channels.

Our commitment to helping the communities in which we do business hasn't stopped with our employees and our customers. We recently announced a partnership with the Boys & Girls Club of America that had been in the works well before the current crisis began where we made an annual commitment of at least $500,000 to help provide essential skills and tools for the next generation. We kicked off the partnership with a voluntary customer roundup campaign, which our store associates got enthusiastically behind. Since its launch on April 1, we have raised over $350,000, which speaks volumes for how even in these challenging times, our customers are always willing to look out for those in greater needs.

As investors and shareholders, we have the benefit of owning a piece of a company that has shown resilience and agility in the current environment. We started the quarter firing on all cylinders, and in that context, we executed $141 million of share repurchases in alignment with prior statements around our intent to front-load our up to $400 million repurchase program in order to accelerate expected benefits for long-term investors as we continue to grow and improve the business. We believe this amount closely approximates full year 2020 expectations. And I want to point out, we did make the decision to halt our repurchase activity as the social impacts of COVID-19 became to make themselves known. Coupled with robust margins, we still ended the quarter with a very strong cash position, and we wanted to proactively preserve liquidity to ensure we had the resources to enable our strategic objectives, preserve future options and support our employees, no matter what scenario we might find ourselves facing in the second half of the year.

Mindy and I were reflecting the other day about many of the key principles that we first shared with investors as we were going public in 2013. I summarized those in my recent annual shareholder letter. While we could in no way even imagine what we are all going through today, we take pride knowing Murphy USA's business model was built for times like this, to not only endure but to emerge better and stronger.

And now I'll turn the call over to Mindy.

Malynda K. West
Executive VP of Fuels, CFO & Treasurer

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Thank you, Andrew. Hello, everyone. I'm going to change my narrative a bit here to address the COVID-19 environment and its impact on our business and move away from summarizing some of the financial information that is already provided to you in the release.

During this time, I know how important the balance sheet and liquidity is to investors. It's important to me, too. So let me provide some additional color around our financial position. But first, let me take care of some standard items. CapEx approximated $45 million for the first quarter, most of which was allocated to retail growth; our EMV upgrade initiative; and, to a lesser extent, maintenance capital. Average retail gasoline prices per gallon during the quarter were consistent with the year ago at $2.14 versus $2.15 in 2019.

Based on our debt outstanding, the leverage ratio we report to our lenders approximated 1.9x for the first quarter of 2020, down slightly from the 2x in the first quarter of 2019 and down even more significantly from the 2.4x in the fourth quarter of 2019.

At this time, we have $134 million remaining under our up to $400 million repurchase authorization by July 2021. Given the current environment, however, we do not expect to be in the market during the second quarter for any repurchase activity. We did end the quarter with 29.2 million shares outstanding.

We are all impacted and will continue to be impacted by COVID-19, but despite the challenges to our people and our customers, I'm happy to say that, financially, we are in good position at Murphy USA to endure this extraordinary situation, thanks to our strong balance sheet, our low-cost model and solid fundamentals underpinning our high-volume fuel business. As Andrew mentioned, we are entering the second quarter in a position of strength with $200 million in cash on our balance sheet. I can tell you that after the first 2 weeks of April business, our current cash balances remain consistent with that amount, although they do fluctuate daily depending on day of week and timing of certain payments. But broadly speaking, this is a free cash flow positive business, and with current margins and volumes, we would expect cash balances to grow over time.

Our balance sheet is well-structured and strong. As you may recall, in September of 2019, we redeemed our 6% notes due 2023 and replaced those with new 10-year notes due 2029, lowering our coupon rate to 4.75%. We also topped up our term loan, adding $250 million of debt that has an amortization rate of $12.5 million per quarter, the first payment of which occurred in -- on April 1, leaving a balance of $237.5 million and the next amortization payment scheduled for July 1. Aside from these fixed $12.5 million quarterly term loan repayments, we have no near-term debt maturities.

In addition to cash on hand, we also have our ABL facility to draw on with current available borrowing base of $91 million, and that reflects historically low receivables and inventory value due to the low commodity price environment. This facility was put into place largely to supplement working capital needs in a high-price and low-margin environment. And in the current low-price environment, the natural offset that we would expect are higher retail margins, as is the case today. Should prices move higher, we would expect increased availability under this facility.

If the need arises, we have added flexibility with respect to our capital program and can defer much of our raze-and-rebuild program and NTI store growth into 2021, which would reduce our capital program by at least $100 million. However, given our strong cash position, at this time, we intend to move forward with our high-quality organic growth program to continue upgrading our network with bigger and better stores in 2020 while preserving our land pipeline for higher growth in 2021. In fact, we may actually be able to capitalize on real estate opportunities for our future store pipeline as retail-related deal flow for high-quality locations has become even more attractive in this environment.

The bottom line is we have a strong cash position and remain cash positive in all but the most conservative scenarios that we have tested, which would require a rapid deterioration in fuel margins and persistent demand destruction throughout the entire year of 2020, and that's an outcome we see as unlikely. We remain confident that our ABL will support any short-term liquidity needs without having to interrupt our organic growth programs. And for the record, again, we are not seeking any government assistance, nor do we intend to seek any such assistance in the future.

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Next, I want to briefly discuss our cost structure with respect to the fixed and variable cost components. We have always endeavored to maintain a low-cost model at Murphy USA, but we do have a meaningful component of what I would call fixed cost. While we have some flexibility around labor hours, there isn't a one-to-one correlation with transactions that will drive operating expenses lower by 30% to 40% to match our fuel volumes. We still have to maintain and provide upkeep for our stores. We have to pay property taxes and utilities, and we will continue to support our employees. Nevertheless, we would expect some modest swing of between $5 million and $15 million of OpEx and G&A reductions should the current abnormally low demand environment persist into the second half of the year. However, with labor hours relatively flat and incremental costs rising to provide a safe and clean environment for our employees and our customers, we might actually see a slight uptick in store operating expenses in the second quarter. That's the one drawback of running a lean organization, there simply isn't a lot of room to eliminate costs when you already have an efficient operation.

As a reminder, we own 86% of the land under our sites, and thus have low fixed payments for rent. Additionally, we should experience a benefit from lower payment fees in the low-price environment, and our stores require less labor than some other larger-format food-based models, so we are less exposed to higher-margin revenue shortfall as our merchandise performance clearly shows.

Finally, if we step back and look at our performance so far in April, we continue to generate positive merch sales comps. And while fuel volumes are running between 60% and 70% of prior year figures, given total demand destruction that we have seen globally and here in the U.S., we appear to be holding on to our customers and market share better than the national average would suggest. And as long as the fuel environment generates margins sufficient to offset lower volumes, our business is not financially compromised.

So that is the end of my comments. Thank you to everyone. Stay safe. And I will return the call back to Andrew.

R. Andrew Clyde
President, CEO & Director

Thanks, Mindy. Let me close with a very brief discussion around 2020 guidance. Clearly, our fuel volume for the next few months is going to be challenged by the current environment. As discussed, the fuel margin offset is more than making up for that and should continue to do so for the near term. With no clear view on when demand will return to normal, we are withdrawing our fuel volume guidance, and we will come back and update it when we can provide a solid future view.

As to our other operating guidance metrics, we are maintaining them as we continue to see strength in our merchandising sales and contribution and have sufficient levers to manage any near-term pressure on operating costs and SG&A.

With respect to our capital spending in NTI and raze-and-rebuild program, we designed our capital structure to be able to invest in both good times and bad times. As such, we plan to continue to invest in the future growth of our business, knowing that we have the flexibility, if conditions change significantly.

I know we've covered a little more than usual in our prepared remarks, but wanted to make sure we proactively address the key issues that are on everyone's mind.
And with that, operator, we will open up the lines for our Q&A.

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Ben Bienvenu from Stephens.

Benjamin Shelton Bienvenu
Stephens Inc., Research Division

I want to ask first on some of the commentary you gave on April, which, frankly -- so I was having some difficulty hearing you, but I think I heard you say tobacco was up 13.3% through the first 2 weeks of April. Nontobacco was down 4.3%.

R. Andrew Clyde
President, CEO & Director

That's correct.

Benjamin Shelton Bienvenu
Stephens Inc., Research Division

I want to ask about the tobacco side. Frankly, that's kind of remarkable to me in light of what it sounds like the rest of the industry is doing. And so I'm just curious if you could expound on why you think your tobacco sales are still so strong into April.

And then also, the 1Q results were really strong as well. So I'd just be curious to hear a little bit more about what you're doing that's working. And maybe you'll tell us it's more of what you've already been doing, but I'd just be curious to hear any detail that you can offer.

R. Andrew Clyde
President, CEO & Director

Yes. Ben, I would say it's really building on our strengths. We're known as everyday low price for fuel and tobacco, we are a destination for that. We're a destination for cartons. And so where we have seen sales and units up, we've actually seen trips down. So people are definitely coming less often but buying more and adding to their baskets. And so I noted cartons were up just under 50% to just under 60%. I think the industry average is somewhere around 20%. In a lot of our markets, you have smaller c-stores that don't even sell cartons.

We have an incredible supply chain partner with Core-Mark, and we work very closely with our manufacturers. You noted that we had a working capital increase as we built inventory in anticipation of this to have the key selling items in stock, and our associates did a great job of keeping those products in stock.

And so, I mean, those are just the basics, right? You've got a customer brand proposition. You've got a supply chain that keeps it in stock. You keep your price where it needs to be and it's available for the customer, and then you have the additional value of Murphy Drive Rewards. I think we added something like 400,000 new members, participants to Murphy Drive Rewards in the month of March. And we've been looking at people that are showing up for the very, very, very first time, and it says a lot about share gains that we're getting from our competitors.

I mean I'll give you a couple of numbers that also just highlight the fact that paydays and government stimulus numbers are pretty impactful. We've had 6 days in April where we sold over 1 million packs. And we had to go back to August 2015 to see numbers like that. On the government stimulus day, cigarettes were up 30% versus 10% the day before, and smokeless and other tobacco products were up 25% and 38%.

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

So what you're seeing is paydays, key dates, et cetera, customers going to their chosen outlets to stock up, either at Walmart or at our stores, et cetera. And so I think we're at the right place at the right time with the right products at the right price.

Benjamin Shelton Bienvenu
Stephens Inc., Research Division

Okay. That's helpful. My second question is related to fuel. We've obviously seen the big drops in wholesale gasoline prices over the last month or so. But given all the dislocations in the fuel markets across the country, I'd be curious to hear what opportunities exist in the market for you specifically to leverage your proprietary sourcing to procure attractively priced gasoline, maybe in excess even of what the market would present on surface.

R. Andrew Clyde
President, CEO & Director

Sure. So as we were watching prices go down, we were short to our LIFO targets, which is generally a good practice. As they've come down lower, we've invested in inventory and are now more balanced to those targets. I think there were some racks in the Midwest and areas contracts, we were able to acquire products for $0.20 a gallon. And so we're seeing opportunities across the board to take advantage of that. And Mindy and Greg and the team are doing an exceptional job doing that.

I think one of the challenges is I'm not sure prices can't get lower, if you start looking at prices for crude, WTI, shut-in economics in West Texas, et cetera. And so there's a lot of concerns about logistics systems filling up, no place to put it and the kind of netbacks you would need to move that product. So we want to be thoughtful even in this low-price environment about inventory exposure. But we certainly manage the downward fall well and have gotten back to balance.

Operator

Your next question comes from the line of Bobby Griffin from Raymond James.

Robert Kenneth Griffin
Raymond James & Associates, Inc., Research Division

I hope everybody is safe and your families are doing well. I guess, first, I want to ask Andrew, in kind of your history of the industry and stuff, when you see a falloff like this in crude prices to this magnitude, how long do the outsized margins usually last for before we turn into some type of normal year-over-year cadence?

And then maybe as a second part of that, given that this is so different with volume trends and everything, do you think, competitively, a lot of the local competitors that you see will hold on to these outsized margins for a longer period of time right now?

R. Andrew Clyde
President, CEO & Director

Yes. I think it's a great question. I haven't seen anything like this before, but I think we can go back and look at prior periods to build some analogies. I mean I think about 2008. I mean it went from $140 a barrel to $40 a barrel, but it took a while to get there. And so that was a -- you never had periods where national margins were $0.50, $0.60, $0.70, but they were $0.20, $0.30 plus for an extended period of time. And while we saw, I can't remember, 10% demand destruction between '08, '09 as the economy fell off, that was gradual, too. And so it was this steady downward progression week over week over week that allowed that period of extraordinary profits for the industry with a very gradual decline on the demand.

What's happened here is fundamentally different, right? You had a less significant falloff in a greater period of time, but it was accompanied by an unprecedented demand shock. And the comments I made about the simple math, if we're currently running sort of the last 4, 5 days 70% of prior year planned volumes. But if normally, we're making $0.10 to $0.15 this time of year and you're earning margins of 3x or 4x that, your contribution margin is significantly higher than that. So your question is right, how long

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

does that last? I think you had to go back to really what sets margins in markets, which is going to be kind of the average independent out there, the marginal player. And if they've got a $0.20 to $0.25 fuel breakeven cash margin requirement and they've lost half their gallons, their cash breakeven requirement has just doubled to $0.40 to $0.50 per gallon. And that's ultimately what is going to set the -- some of the competitive dynamics, market competitive dynamics around the margins.

I think the other thing I would say is because their relative margin was already high, the increase in margin to them as a percentage may only be 2x. And at half the volume, they're only earning 100% of their prior contribution. So as margins fall off, now they're earning less than 100% of their prior contribution, and many of them invested in food and other things that are being curtailed. And so you could imagine one or two scenarios. One in which there's some discipline around that, and that creates the -- a foundation for the margin structure or it breaks through that, and then that puts significant pressure on the independents. And I think what you'll see is a combination of both depending on the local markets, and we're actually seeing a combination of both. And I think this is where just the market and competitive dynamics will play out differently in different markets. But I think we're in a unique position because we're starting with a high-volume position, we haven't lost as much volume. We're starting with a very low-margin position relative to others. And on a percent increase basis, that relative increase is so much higher, we're going to be able to weather this with positive free cash flow generation for a much, much longer time.

Malynda K. West
Executive VP of Fuels, CFO & Treasurer

And Bobby, I can kind of add a little bit of color on the competitive environment to what Andrew said. We're seeing competition really behave differently depending on who they are. Bottom-of-market players, in general, we've seen them reduce their prices fairly steadily. We've seen branded dealers, however, they tend to take more large moves down, and we suspect this is primarily due to load pricing where they're building in fixed margins to the latest load of gasoline that they've received. And then when we look at the hypers and grocers, the results are more mixed. Some are discounting, while many appear more concerned with running the operations in their big box. So for us, we're relying on our fully staffed fuels pricing department and also our precision of our store-level tactics to reassert our bottom-of-market position, and we're doing it really thoughtfully and deliberately. And fortunately, our processes and controls have improved dramatically within the last year, which are enabling us to do that quite well in this environment.

Robert Kenneth Griffin
Raymond James & Associates, Inc., Research Division

I appreciate that. That was very, very helpful. I guess my second question is maybe just on the wholesale supply side of the business. Clearly understand how it reacts when oil falls off as quickly as it does. In an environment where oil is down at this level, levels we haven't seen in a long time, but just is stable and flat, how does that business recover? Does it start to get backwards normal EBITDA dollars? Or how should we think about how that would trend in 2Q if we were at a flattish oil environment from the crude side?

R. Andrew Clyde
President, CEO & Director

So I think if the question is how does the product supply wholesale net of RINs behave in a flat market environment, I think this just gets back to our proprietary supply advantage, right? And so you would look to areas like the Colonial Pipeline system in the Southeast and other areas where we're able to deliver proprietary barrels into those markets. With refinery runs being cut, you may see certain areas that are very loose and long with product in which that supply advantage may get competed away at the racks as folks are trying to move product, but you may also see other dislocations where that advantage is helpful.

One of the challenges, as you can imagine, is when you start dialing back refinery runs, closing, shutting in crude units, distillation units, et cetera, turning those things on isn't a simple act. I mean most of the

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

unplanned outages that occur in the refining industry occur on the other side of a planned outage. And so you could see disruptions taking place there that create some localized shocks that improve our business.

I saw where 5 state governors were asking for waivers on biofuel blending. And so it's -- there's still some uncertainty about how some of that will play out as well. But certainly, ethanol prices are very low, and some of the ethanol producers and refiners with ethanol plants have shut in a high number of their plants as well.

Operator

Your next question comes from the line of Chris Mandeville from Jefferies.

R. Andrew Clyde
President, CEO & Director

Operator, we'll just put him back in the queue and go on to the next question.

Operator

Your next question comes from the line of Bryan Hunt from Wells Fargo Securities.

Bryan Cecil Hunt
Wells Fargo Securities, LLC, Research Division

I was wondering, and you called this out earlier, Andrew, I was wondering if you could talk about the relevant performance of your stores that are within a couple of mile radius of the Walmart relative to stores that aren't?

R. Andrew Clyde
President, CEO & Director

They performed at a higher level. Certainly, at the beginning of the kind of the panic buying period, if you will, in the middle 10 days of March, we saw that distinction very clearly. It continues today. And I think when you see key paydays or government check issuance days, you see that as well. But the reality is that represents the majority of our stores, and so they most benefit from that. But again, it's very much a positive.

Bryan Cecil Hunt
Wells Fargo Securities, LLC, Research Division

Is there a way you can give us a magnitude of difference in the performance of the stores you have, those half of the, roughly, stores that are near Walmart versus the other?

R. Andrew Clyde
President, CEO & Director

Yes. We may have to come back with the exact number. I think recalling at some point, it was anywhere from 5% to 8%, depending on the categories.

Bryan Cecil Hunt
Wells Fargo Securities, LLC, Research Division

All right. And then my last question is a lot of grocery and/or big-box retail have dramatically changed their promotional and marketing tactics in this environment. So can you talk about what you all may be doing different from promotion and marketing standpoint?

R. Andrew Clyde
President, CEO & Director

Well, I think when you're everyday low price, that's one of the objectives is to try not to win customers through promotional pricing but everyday low pricing and then surprise the customer with additional value on top of that. And so I think, one, for some of our core categories like tobacco, being in stock was a

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

huge advantage, number one. Having the everyday low price is a second advantage. Having the Murphy Drive Rewards program on top of that. And when we drew these new customers in from competitors, we gained significant number of members from that to the extent the manufacturers have programs. When they call and say, "Hey, we've got a program, how quickly can you launch that?" If they're trying to move product or address an issue, we can typically turn it on within 48 to 72 hours, and so the customers will see additional value there. And we've got some new programs that have been launched in the last week or so that reflect that. So that's part of the beauty of being everyday low price. You don't have to resort to new promotions all the time to win. I will say on candy and some of the other ones, there's a cadence of buy 1, get 1 or various things, and those were doing extremely well. In Q1 also, if you recall, last year, we diverted a lot of that associate time to launching Murphy Drive Rewards.

Bryan Cecil Hunt
Wells Fargo Securities, LLC, Research Division

And you -- and I'm sorry, just to touch on one of the topics you addressed in your answer. Given your relative performance to the industry, are you seeing, in your opinion, greater opportunities to run unique promotions with your vendors relative to what your peers are seeing? And that's it for me.

R. Andrew Clyde
President, CEO & Director

Absolutely. We absolutely are because they know that we can step up with the working capital to take on the inventory, take on keep the product in stock, sell through the promotions with excellence, et cetera. And so if you've got a manufacturer, regardless who it is, and they want to tack the largest-possible audience with the fewest amount of dollars with exceptional execution, we're going to be at the top of that list.

Operator

Your next question comes from the line of Chris Mandeville from Jefferies.

Christopher Mandeville
Jefferies LLC, Research Division

Andrew, can you happen to hear me?

R. Andrew Clyde
President, CEO & Director

We can. Was that a work-at-home challenge?

Christopher Mandeville
Jefferies LLC, Research Division

Yes. It's a wonderful world of working from home these days, apologies for that. I was hoping I could build off of what Ben had brought up a little bit earlier with respect to just the continued impressive tobacco results. Be it that the margins, the contribution as well as on a percentage basis being up year-on-year were even more impressive than just the sales dynamics in my mind. So I guess, just outside of the greater carton mix that you realized in the quarter, can you offer up any other puts and takes on how you managed to drive the margin in that category?

R. Andrew Clyde
President, CEO & Director

Yes. So we talk about cigarettes, but it's also smokeless and the other tobacco products as well. They're all up double digits, and it's really for the same reasons, right? It's high in stock, it's great value, and we're at the right place at the right time with that product. So it's really all of the categories and subcategories performing at a really, really high level. I mean we've had tobacco sales in the month of April that were up double digit most of the days. And I think Easter Sunday was the only negative day when traffic was down generally across the board for the network.

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Christopher Mandeville
Jefferies LLC, Research Division

Okay. That's helpful. And then I do appreciate the commentary surrounding some level of sustainability in the margin profile on fuel for the foreseeable future and just what you've been seeing with respect to some of your lower quality of competitors, if you will. But if we think about matters longer term and how over the last 20 to 25 years, we've seen structural improvements in the industry of fuel margin capture, coming out of coronavirus, I guess I'm just kind of intrigued to get your perspective on how you think COVID influences matters permanently? And how a few retailers at large are looking at fuel margins?

R. Andrew Clyde
President, CEO & Director

Yes. I think some of the fundamentals aren't going to change that much in the sense that it's kind of the margin in a market is set by that almost 75th percentile retail store, we can expect their breakeven requirements to continue to go up. And even if we see a fallout to an event like this where we go from losing 1% of our stores to, I don't know, let's say you lost 5% to 10% of the stores in the industry over a multiyear period, you would still look at those cash margin requirements to set up the margin structure for the industry. And so I think you're going to continue to see a lot of pressure on the smaller stores and those that decide to exit. And hopefully, they can get a lot of value for their real estates and be successful doing something else.

There's going to be another set of retailers on the margin that are facing the same set of challenges. They may not have invested in EMV, now they've got the credit card liability. They haven't been able to keep up with their investments in their stores, and so they don't attract as much traffic and so forth. And so I think that's really the fundamental that we've seen over time, as that breakeven requirement gets higher and higher and higher, the average pool margin goes up. And then that's where you've got bottom-of-market retailers, like us, who can operate on a less -- much lower margin and still have attractive returns, reinvestment economics and new-to-industry economics. And so I think it's just this gradual, continual cycle or format evolution that takes place, and I really don't see that changing.

What would be dramatic is if our industry was like the video industry where all of a sudden, you lost an entire format called the video store, and that happened in a very short period of time. And I don't think that's really going to be the case here because of the role convenience stores, gasoline stations play in the economy and the established base. So I think this is likely going to continue to play out as a process over time.

Operator

Your next question comes from the line of John Royall from JPMorgan.

John Macalister Royall
JP Morgan Chase & Co, Research Division

So you mentioned a couple of times maintaining your capital program throughout the environment and recognizing that you're ending 1Q on a strong balance sheet position. I guess what would you need to see to pull back on growth a little here and exercise that $100 million flex that you mentioned?

R. Andrew Clyde
President, CEO & Director

We'd have to see a really sharp deterioration both in Q2 performance and performance outlook for the second half of the year. We've run a variety of models and scenarios for the second quarter to get a sense of what that end-of-Q2 cash balance would be, and then on top of that, run a set of scenarios for the second half of the year. And you have to believe our worst of Q2 assumptions and our worst of the second half of the year assumptions to end the year with a 0 cash balance, right? And at that point in time, we still haven't touched our ABL, which probably is going to be valued at a much higher level because what would contribute towards a lower second half performance would be rising prices, and so the value of that would be higher. So we got to believe the worst of the second quarter and the second half scenarios to do

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

that. The challenge, of course, with CapEx flexibility is every 30 to 60 days that goes by, you've already now committed and started on product -- projects where it's too late to pull back on certain projects. So we're looking at Q2 very closely. Everything is going very positively from that standpoint versus our scenarios. And then as we come towards the end of Q2, seeing where we're at, we can then make a decision on, "Okay, are we going to be in a situation where we need to do that." But I would handicap that as the lowest-possible scenario right now. We just wanted to note that we do have that, flexibility should the need arise. But that flexibility goes away the longer into the year. Certainly, you've got 2021 CapEx flexibility if this thing went on and on and on.

And what I would say is we're starting to see signs of the economy reopening. We don't know if -- exactly when and how this is going to play out. I will note that just 1 day, if you look at the government stimulus impact in taxpayers receiving checks, yesterday, we only had 4 states where our volume was below 70% on a planned basis and our own state of Arkansas was at 95.7% of plan with a dozen states over 80%, right? And so it's just kind of a note that says, "Okay, that was stimulus to the economy, and taxpayers got a check and they went and spent it, and they've spent a lot of it with us." But it does give you a sense that there's a lot of pent-up demand out there, and when it comes back, we expect to see it come roaring back like this, and we will get more than our fair share of it because of how we've treated customers and worked with customers to keep them safe and give them value during this period.

John Macalister Royall
JP Morgan Chase & Co, Research Division

Okay. And then on the merchandise side, I was just wondering how the fuel side is affecting the comps inside the store in this environment. So if fuel volumes were down a certain percentage lower than you expected, I guess, what portion of that would you expect to flip through to inside the store? If I'm thinking about this right, I would assume that correlation might be a little bit lower than normal. But I'm not sure if I'm thinking about that right.

R. Andrew Clyde
President, CEO & Director

Yes. So a lot of the stocking up on tobacco was completely independent of the trends we saw on the fuel side. Our -- as I noted, the first 10 days of March, our fuel volumes were up something like 7% year-over-year. And so the stocking up period was only 2.7% where the merch numbers really spiked during that period. So they're becoming less correlated probably on a trip basis. We're probably having more stand-alone merch trips as people are going back to the Walmart, coming back to our stores to stock up. So not seeing some of that same correlation as we've seen before. But a good example would be where we were at down 30% Monday and Tuesday of this week on fuel gallons, we were only down 20% Wednesday with the stimulus. And so you do see some continued correlation that's taken place.

Look, we're at the top of the hour. And certainly, we had a little bit longer prepared comments than normal, but we thought it would be important to try to give you as much clarity as possible on what we were seeing on the 3 periods in March and in the month-to-date period in April to give you line of sight to how our business is performing.

But we thank you for your time today, your questions. And certainly, please follow up with Christian with any follow up. Stay safe, everyone. Thank you.

Operator
This concludes today's conference call. You may now disconnect.

Copyright © 2020 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Copyright © 2020 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

These materials have been prepared solely for information purposes based upon information generally available to the public and from sources believed to be reliable. No content (including index data, ratings, credit-related analyses and data, research, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of S&P Global Market Intelligence or its affiliates (collectively, S&P Global). The Content shall not be used for any unlawful or unauthorized purposes. S&P Global and any third-party providers, (collectively S&P Global Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Global Parties are not responsible for any errors or omissions, regardless of the cause, for the results obtained from the use of the Content. THE CONTENT IS PROVIDED ON "AS IS" BASIS. S&P GLOBAL PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Global Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages. S&P Global Market Intelligence's opinions, quotes and credit-related and other analyses are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P Global Market Intelligence may provide index data. Direct investment in an index is not possible. Exposure to an asset class represented by an index is available through investable instruments based on that index. S&P Global Market Intelligence assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P Global Market Intelligence does not act as a fiduciary or an investment advisor except where registered as such. S&P Global keeps certain activities of its divisions separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain divisions of S&P Global may have information that is not available to other S&P Global divisions. S&P Global has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P Global may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P Global reserves the right to disseminate its opinions and analyses. S&P Global's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P Global publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.
© 2020 S&P Global Market Intelligence.