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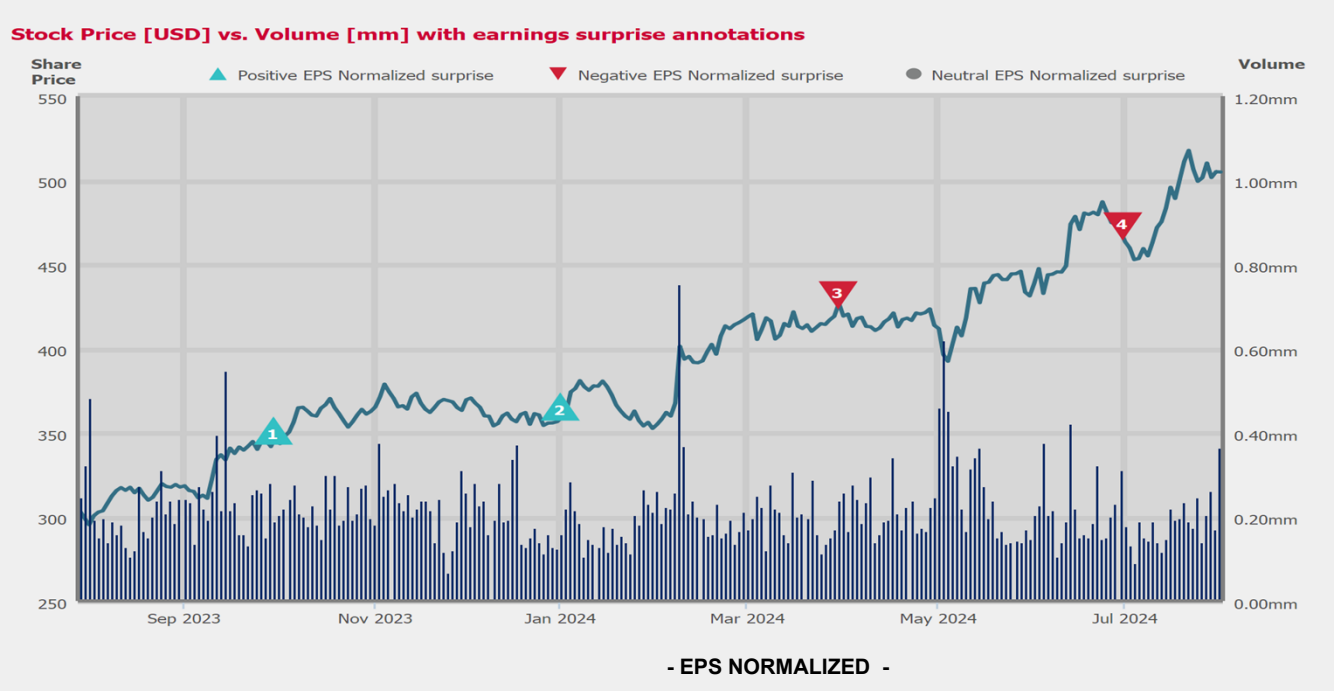
FQ2 2024 Earnings Call Transcripts

Thursday, August 1, 2024 3:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ2 2024-			-FQ3 2024-	-FY 2024-	-FY 2025-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	7.05	6.92	▼ (1.84 %)	7.60	24.91	NA
Revenue (mm)	5691.35	5451.70	▼ (4.21 %)	5834.78	21646.92	NA

Currency: USD
Consensus as of Aug-01-2024 2:33 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2023	6.55	7.69	1 17.40 %
FQ4 2023	6.65	7.00	2 5.26 %
FQ1 2024	4.46	3.12	3 (30.04 %)
FQ2 2024	7.05	6.92	4 (1.84 %)

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Presentation

Operator

Thank you for standing by. My name is Bailey, and I will be your conference operator today. At this time, I would like to welcome everyone to the Murphy USA Second Quarter 2024 Earnings Conference Call. [Operator Instructions] I would now like to turn the call over to Christian Pikul, Vice President of Investor Relations. You may begin.

Christian Pikul
Vice President of Investor Relations & FP&A

Thank you, Bailey. Good morning, everybody, and thank you all for joining us today. With me are Andrew Clyde, Chief Executive Officer; Mindy West, Chief Operating Officer; Galagher Jeff, Chief Financial Officer; and Donnie Smith, Chief Accounting Officer. After some opening comments from Andrew, Galagher will provide an overview of the financial results, and then we will open up the call to 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 those 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'll turn the call over to Andrew.

R. Andrew Clyde
President, CEO & Director

Thank you, Christian, and thanks, everyone, for joining us today. We're very pleased with Murphy USA's second quarter results. We believe our flywheel is clearly in motion, delivering advantaged results to our business and creating value for our investors. Let's start today's call by taking stock of how the business as a whole is performing. Our core fuel business is delivering excellent results in a low volatility environment, which is historically when it is more difficult to grow volume. The structural dynamics that support higher breakeven economics in the industry persist, as evidenced by all-in margins of $0.317, $0.022 per gallon higher than the prior year period. As a result, second quarter retail fuel margin contribution dollars were the highest Q2 in company history, underscoring the sustainable and enduring success of Murphy USA's advantage model.

Turning to merchandise performance. Same-store sales and margin growth were strong, driven by exceptional performance across tobacco categories. While total merchandise margins were up nearly 5% in the second quarter, year-to-date results are falling short of our high expectations. Given the slow start in Q1, softness in some discretionary center store categories and lighter-than-expected traffic in QuickChek markets resulting in fewer transactions that were built into our internal plan, total full year merchandise margin growth will be around 4%, as reflected in our adjusted guided range from $830 million to $840 million.

Our initiatives are on track, but the early results will not overcome the impact of these drivers. Inflation is real and remains impactful to our customers. We have especially seen the effects in the Northeast markets, where we see lower inflation for food at home versus food away from home, and that remains a challenge. We also note that QSR promotional intensity has increased, where many QSRs are pivoting back to value and competing per share in prepared food and beverages, which are core traffic-driving categories at QuickChek. As a result, year-over-year sales comps remained down about 2% at QuickChek in the second quarter, with similar performance into July. This represents the largest variation to our total merchandised plan, where we anticipated more of a rebound in transactions year-over-year at QuickChek.

Similar to MDR members, QC Rewards members remain very active, shopping with greater frequency and with larger baskets. But with 1 less trip or a trade down, it adds up. With our commitment to value pricing, the new QC Rewards rollout coming up and other initiatives, we are well positioned to get that incremental trip and trade up back. That said, there are some incredible bright spots on the merch side that highlight where we not only win in the current environment, but sustain the wins thereafter. We continue to invest and reinvest in the tobacco category from a price, promotion and capability perspective, driving strong growth across all products within the broader nicotine ecosystem.

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Our leadership in combustible products has built a strong foundation upon which we continue to grow share in vapor, oral nicotine and other noncombustible products that are not only growing sales and margins in the low double-digit range, but also come with higher margins. We intend to support our customers as they transition to noncombustible products, leveraging our advantaged volume position and promotional strength to continue to drive growth in the nicotine category.

In the first state that has actually cracked down on illicit vapor products, we have already seen a strong resurgence in our volume to the products that the FDA has approved. Hopefully, more to come on that front. In the center store, results were mixed between nondiscretionary and discretionary products, but one thing remains clear. The Murphy USA customer spend on nondiscretionary products in our store remains very strong. Make no mistake, our customers are not immune to the inflationary pressures impacting household budgets of Americans living paycheck to paycheck, which we believe to be a growing customer segment. As such, they are making choices in their discretionary spend at our stores. Yet their spend on what we consider categories that remain core to our customers, such as fuel, tobacco, beer, salty snacks and packaged beverages remains strong. Thus, overall spend at Murphy stores is not only stable and resilient, it's growing.

In the Murphy footprint, traffic-driving categories and fuel -- including fuel and tobacco are bringing people to the store and growing the basket in the center store categories attached to the visit. Remarkably, total tobacco margin dollars were up 12% and nontobacco margin dollars were up 4.8%, material improvements against what was a very strong second quarter in 2023. The 2-year stacks were up 17.8% and 15%, respectively, in tobacco and nontobacco margin growth, illustrating the powerful impact of Murphy's advantaged model and the resilience of our customer.

Unpacking results at the category level, customer spend remains strong in beer and salty snacks, product that customers not only don't want to forego, but are buying more of, compelled by our value offer. Per store margin growth in beer and salty snacks were up 11% and 9%, respectively, offsetting softness in candy and lottery, where customers are making different choices.

Packaged beverage, the largest center store category from a sales and margin perspective, has improved sequentially from the first quarter, exhibiting seasonal momentum, up 2.4% in per store margins, outpacing the Nielsen data and gaining market share in our footprint, driven by higher promotional intensity and carbonated soft drinks. General merchandise margin growth, the second largest center store category, was more robust, up 5.6%, reflecting improvements from our initiatives and cost of goods that are margin accretive. Of note, general merchandise is 1 of the areas we reimagined with our in-store experience campaign focused on enhancing performance at our larger format stores, adding 200 additional SKUs and 700 additional facings to optimize selling space. Early results are promising across center store categories as we enhance the customer experience, improve sales velocity and improve employee productivity.

Looking at operating expenses. Second quarter OpEx on a per store basis was up 6.2% year-over-year, down sequentially from up 6.7% in the first quarter and remains on track to finish within our internal plan and the 2024 guided range. The primary drivers of OpEx growth remains the larger stores we are building, including raze-and-rebuilds, intentional wage investments we made in 2023, including elevating the assistant manager cohort and higher maintenance costs largely attributable to warranty expirations on dispensers we replaced for a large part of the network in 2018 and '19 as part of our EMV compliance.

Like the headwinds we are seeing in certain parts of the business, we're very confident in the future growth drivers that will create value, including maintaining a relentless focus on EDLP and value pricing, generating additional value and efficiency from our stores as part of our store productivity excellence campaign, leveraging the benefits of digital transformation to address and offset pockets of weakness in discretionary categories and ramping up new store additions in 2024 and 2025 and beyond.

These are the building blocks of sustainable growth that are the material drivers of our $1.3 billion EBITDA target in 2028 and the catalyst to our flywheel. Our core fuel and tobacco categories continue to outperform, and our customer remains resilient, giving us further assurance we can meet this goal and continue our track record of delivering top-tier shareholder returns.

I'll now turn the call over to Galagher to give you more color on how we are allocating our cash flow to grow the business and create value for shareholders. Galagher?

Galagher Jeff
Executive VP & CFO

Hello, everyone. Thanks for joining today, and thank you, Andrew, for that setup. This morning, I'm going to provide some color on our new store program, talk about our capital spending and cover what we're doing with our free cash flow. Starting with store growth. We opened 3 new stores in the second quarter, bringing our year-to-date openings to 6, including 1 QuickChek store. We also reopened 9 raze- and-rebuilds, transforming small kiosk into 1,400 square foot stores, bringing us to 11 year-to-date.

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Our current construction activity is robust with 22 new stores under construction, including 3 QuickChek stores and 25 raze-and-rebuilds also underway. We expect another slate of new store construction to begin in early September. And I want to emphasize, we will achieve our guided range of 30 to 35 new stores this year, accelerating our pace of store growth from 28 openings in 2023.

As I mentioned last quarter, the new store pipeline is in great shape, and we remain highly confident that new store growth will increase again in 2025, becoming a more sustainable and significant contributor to EBITDA going forward. From a capital spending perspective, we spent $123 million in the second quarter, with about $96 million of that for new store growth and the rest largely going to maintenance capital and technology investments. As referenced in the press release, we are able to push through more raze-and-rebuild projects this year and are now targeting 47 stores, up from a range of 35 to 40 in our original guidance. Keep in mind, timing may impact the final in-service dates, but we are certain to get at least 40 over the finish line open for business and serving our customers in 2024.

For perspective, the raze-and-rebuild projects are generally easier to permit and build versus the new store. We do like this program as it enhances customer offers, improves the appearance of our stores and comes with high reinvestment returns. So along with share repurchase, this remains a highly effective way for us to deploy our free cash flow. Given the higher level of construction activity this year and our ability to get a head start on the 25 new store build class, we expect our full year 2024 capital spending to be at the high end of our $400 million to $450 million guided range. But this also means we can expect many more new store openings in the first quarter of 2025, which will add some balance to the new store pipeline and contribute more to 2025 EBITDA.

Turning to share repurchase, which remains preferred use of free cash flow beyond growth capital. We continue to be active repurchasers of our own shares. We bought back 238,000 shares in the second quarter and remain committed to ongoing share repurchase. We continue to execute against the existing Board authorization to repurchase up to $1.5 billion of our stock, which extends through 2028. Year-to-date, we have bought back 454,000 shares for $193 million, leaving about $1.2 billion remaining under our board authorization.

To summarize, as Andrew mentioned, Q2 was a good example of how we get more from our customers and more from our stores. It creates strong free cash flow we can invest in accelerating our flywheel. In Q2, we invested in our technology initiatives and store maintenance. We accelerated our new store growth. We allotted $107 million for share repurchase. We paid our dividend and closed the quarter with nearly $80 million of cash. This free cash flow enabled us to invest in our advantaged model and maintain a balanced capital allocation of accelerating new store growth and returning cash to shareholders. We expect to continue the strategy, which we believe maximizes long-term shareholder value for the foreseeable future. With that, I will turn the call back over to Andrew.

R. Andrew Clyde
President, CEO & Director

Thanks, Galagher. Let me close with a preliminary view of July performance. Per store fuel volumes are largely flat to prior year at retail only margins of about $0.28 per gallon, several pennies above July of 2023. Whether or not we see a steep falloff in prices that will present a bigger opportunity for margin capture remains to be seen. Geopolitical uncertainty persists. Oil prices remain range-bound. High refinery utilization following turnaround season is boosting gasoline inventories, yet fewer imports are coming into New York Harbor, so line space values are high.

There's a whole set of market dynamics playing out, as always, and the ultimate impact on the future direction of fuel prices remains unknown at this time. Will there be a significant fall-off in the third quarter? All we can say with certainty is that it hasn't happened to date, yet we remain certain that the structural dynamics supporting higher retail margins are in place, while volatility has been limited due to high inventories and lack of any material shocks to the market.

Merchandise trends largely reflect the same customer dynamics we have seen in the first half, with stronger performance in nondiscretionary categories outpacing softness in discretionary choices. In QuickChek markets, traffic remains softer than planned, as we have seen in the first half. However, the core Murphy network continues to perform broadly in line with first half results.

I'll end with a simple message. In times of significant consumer distress, consumers change their purchase behavior, and more of them come to Murphy. When that stress subsides, we find that most stay loyal customers because of the incredible value we deliver on the same products and the empathetic service and smiles they receive from our associates who understand their pain points. For fuel, the severe distress of high prices witnessed in 2022 has subsided, only to be replaced by persistent inflation in other categories.

Looking at the 3-year fuel volume stack to 2022, we've gained over 4% average per store month gallons, demonstrating the sustainability of growth experienced during that difficult period. On the other hand, continued price increases on tobacco and other in-store products have created distress that has not subsided.

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Looking at the multiyear stacks of the overall tobacco category highlights the ability to continue to grow and sustain margin dollars and share. Other categories fall in between, as they are most often a part of the basket of a fuel or tobacco destination trip. Or in the case of QuickChek, of food and beverage trips.

The point is, we are well positioned to win in the current environment that challenges our core paycheck to paycheck consumer, and we are making the investments to keep them when conditions moderate. Indeed, the way we make our flywheel spin faster is to make these investments in value, capabilities and store growth across the economic cycles, especially in times of consumer distress, as we have the balance sheet and free cash flow to do so. Let us end this, and we'll turn the call back to the operator to open up for questions.

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Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Anthony Bonadio with Wells Fargo.

Anthony Bonadio
Wells Fargo Securities, LLC, Research Division

So I just wanted to start with the new insight guidance. So peeling that back, it seems to imply that your year-over-year contribution growth decelerates by close to 50 bps in the back half from what you just put up in Q2. So understanding the overall demand, backdrop is pretty choppy right now. But on the flip side of that, you've got a pickup in both NTIs and raze-and-rebuild, easier compares. And then all the self-help stuff you've been talking about. So can you just help us think about the different puts and takes in that forecast? And just maybe how you're thinking about the shape of consumer demand in the back half?

R. Andrew Clyde
President, CEO & Director

Sure. So as I mentioned in the prepared remarks, the merchandise contribution from QuickChek is the single biggest driver of the adjusted guidance. And this largely reflects a view in our internal plan where we expect the transactions to rebound year-over-year where we've actually seen some continued softness with this persistent inflation, QSR competition, value mill pricing, et cetera. And so we continue to see the same pattern for the rest of this year.

The initiatives that we have in place, some of which that are driving improvements at QuickChek, are therefore on a lower transaction base than what is planned as well. And most of those initiatives are second half weighted. You're right around the NTIs. In fact, we're about to start on a large tranche of those, but those will be ramping up towards the very end of the year and not contributing as much, and the same with the extra raze-and-rebuilds.

So as I said, the biggest driver is what we've seen in terms of velocity of transactions in QuickChek, it's more a function of the aggressive plan that we've built in that's causing the guidance chain versus just a 2% decline that we witnessed this quarter.

Anthony Bonadio
Wells Fargo Securities, LLC, Research Division

Got it. That's really helpful. And then switching gears to gas margins. I guess as we think about modeling that out in the back half, a lot of uncertainty, but just maybe some thoughts on how much of Q2 was maybe a function of more temporary price dynamics versus strong underlying fundamentals? And just any updated thoughts on that $0.30 to $0.34 per gallon range you guys talked about starting the year?

R. Andrew Clyde
President, CEO & Director

Sure. Look, I mean, every quarter is different, and we always just got to remember what are the biggest drivers of outsized fuel margins. The first 1 is, are you going to have a steep run-up and then a sharp falloff in prices? And we haven't seen that yet. We often see that in Q3. We've seen Q3 where it's been exceptional falloff like 2022, but it took something pretty material for that run up. And I think going back to 2016, we've seen run-up in prices based on some OPEC changes in Q3, but then we saw the big fall off in Q4. So Anthony, I wish we had a crystal ball. It would make all our lives a lot easier, but we don't.

What we can say is that, again, there was nothing really exceptional about Q2. There's a lot of inventory -- lot of inventories built up, but we are seeing stronger line space. And so those inventories work down, we continue to see line space, we could see some strength there. There's nothing in what I would call the competitive dynamic that creates any concern. So if you think about this quarter's margins, July's margins that we noted in a period of low volatility, that remains strong. So I think the biggest driver of a $0.30 low end of the range to $0.34 of the range, $0.34 a high end of the range is are we going to see a sharp fall off or not in prices and something geopolitically or logistically in the U.S. infrastructure would have to happen for that to occur.

Operator

Your next question comes from the line of Bonnie Hergoz (sic) [Bonnie Herzog] with Goldman Sachs.

Bonnie Lee Herzog

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Goldman Sachs Group, Inc., Research Division

I wanted to ask about the consumer. In light of the pressures that we're seeing and then certainly, your comments on the environment, Andrew, I guess I'd be curious to hear what additional levers you can pull to drive improved traffic in the back half of the year, whether that is stepped up promotions, et cetera? And I'm curious, why do you think the Northeast is -- maybe consumer there, I guess, having a more significant impact than maybe what we're seeing or you're seeing in other regions?

R. Andrew Clyde
President, CEO & Director

Sure. I mean if you just start with the Northeast, I mean, the rate of inflation is higher there than some of the other regions. And fact, we had a Goldman economist to present some information to us the other day that showed those exact same factor. So all the economic regions are faring a little differently. Murphy just happens to be in regions where the inflation hasn't been as high. As I noted, the food at home inflation to date has been lower than the food away from home. And so we see our QC Rewards members coming back. We are not losing guests, but they are making on the margin one less trip, for example, or they're trading down from a 12-inch sub to a 6-inch sub or they're taking value of something from our 2 for 5 made to stock warmer items.

So that's the behavior that we're seeing. And I think it's pretty normal trade down behavior on something they need to subsist from a food standpoint. I think on the Murphy side, we're seeing the behavior that we've continued to see, right? Nondiscretionary items, people are trading down to lower-priced retailers. We're getting more Murphy Drive Rewards customers every month, every quarter, year-over-year, and they are ramping up and accelerating their growth, the newest customers, faster than the prior year cohort. So I think that's a consumer behavior that benefits us.

And we don't have to get super extra aggressive from a promotional standpoint because the players in many of those products continue to raise their prices, sometimes with price increases where they keep more of the pennies and we share more of them with the consumer. So our just natural differential widens over time. And I think that's led to some of the outsized gains that we've had there. I think the center store categories are just another discretionary choice. And on the margin, if someone's feeling $1 short, they're just 1 less thing they're going to put in their basket on that trip. But I think the important message is we are not losing guests. We are keeping or gaining guests because of the value proposition, but those guests are making some choices.

Galagher Jeff
Executive VP & CFO

Okay. Could I add one thing, Andrew? Bonnie, thank you for spending time on our QuickChek stores this quarter. And hopefully, you saw some of the technology that's really resonating with customers. We are seeing a lot of good traction from our QuickChek rewards members. There's over a 10-point difference between their behavior versus the nonmembers. And we're seeing mid- to high-single-digit growth in transactions and sales from our QuickChek reward members. And as we grow that program and realize in the second half, we really think we're going to make more of an impact on that business. So the trips, most of the transactions we're losing are not from those that know us best. And as we expand that program and grow it, we expect the loyalty to even be stronger.

Bonnie Lee Herzog
Goldman Sachs Group, Inc., Research Division

Okay. That's a good point. And I think that's an opportunity, too, just to touch on that in terms of sharing best practices, right? As you have a lot of learnings that you can kind of implement throughout the broader store base, I guess. Okay. If I may, just one last question for me on a different topic. Just sort of on capital allocation, M&A, one of your peers announced a pretty large acquisition recently. So just curious how active or not you've been in the M&A market? And where are you seeing multiples trend versus last year and really maybe versus historical levels? And then lastly, I guess, where are you seeing the greatest returns right now? Is it buying back your stock, M&A, new store growth, raze-and-rebuilds, et cetera?

R. Andrew Clyde
President, CEO & Director

Sure. I mean in terms of the M&A context, we see most of the transactions as they rise. And as we've talked about before, many consist of either portfolios that have a pretty varied mix of quality performance, age and investment that has to be put back into them. I think one of the most fundamental things we look at is, one is, how does the EBITDA store compare to the extremely high productivity of our stores where we do not have a tail of low-performing stores like most commodity retailers do?

And then secondly, would you be able to take that entire chain to an everyday low price position consistent with your value proposition? And so when you see chains that are highly concentrated in certain markets, you recognize, it just doesn't meet the

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criteria on many, many dimensions. When we look at our organic growth opportunity, we just see that as a better capital return because you're getting a new store designed the way we want it, the way our customers want it that works for our employees, where we don't have to then go in and take out 20- to 30-year-old tanks that are sitting in the ground. You don't have to spend significant capital on rebranding the stores or getting out of unbranded or getting out of branded fuels contracts, et cetera. So our preferred approach is our organic strategy.

With the share price improvement that we've had, it's pretty hard to say that hasn't been our highest return investment. But the only reason it's a high-return investment is we continue to grow our EBITDA position, that growth in front of investors so it shows up in the multiple and buy back the shares. And so if I put into context where we expect to be in 2028, we will have grown EBITDA by $1 billion since the spin. We will have almost doubled our multiple, and we bought back over 60% of the float.

And so it's really a combination. Is that balanced capital allocation. And as long as we see very high returns and improving enhanced returns in our new to industry stores and raze-and-rebuild stores and the investments we're making in our capabilities, those are probably some of our highest return on investment, capability-building investments. It's really that combination. And so unless there is something perfectly unique unicorn about the M&A opportunity, we're going to stay focused on our way to play and our way to win.

Operator

And your next question comes from the line of Corey Tarlowe with Jefferies.

Corey Tarlowe
Jefferies LLC, Research Division

Great. I was wondering if you could talk a little bit about the promotional intensity that you're seeing in your stores? I think you highlighted some higher promotional intensity in carbonated soft drinks. I'm curious about your willingness and/or need to pull that lever to potentially boost merchandised sales inside the store and how you think about the ability to do that to drive traffic and volumes.

R. Andrew Clyde
President, CEO & Director

Look, we're always going to be known for everyday low price. And across the various center store categories and packaged beverages, you're always going to see some promotional activity going on in our store. We represent such a significant baseload volume for so many providers that, that type of promotional activity is just part of the value pricing that we do. So I would not say that there's anything unique or onetime or difficult to comp over in terms of our promotional activity.

Corey Tarlowe
Jefferies LLC, Research Division

Got it. And then just on the OpEx per store. I mean you mentioned that you're opening larger stores, and you've certainly been making some wage investments as well. How should we be thinking about the shape of the OpEx curve as you continue to open new stores and then again, make these investments in some of these larger stores and in your people?

R. Andrew Clyde
President, CEO & Director

Yes. So the component that relates to new larger stores will increase because we're increasing the number of new larger stores that we're building. The numbers associated with raze-and-rebuilds will increase as we increase the raze-and-rebuilds. The amounts related to kind of onetime catch-up wage investments that we needed to do for some of our most important cohorts will normalize because we've made those investments, and they'll go back to a normal merit-type increase. And the increase attributable to dispenser maintenance coming off of warranty will normalize as those cycle over our EMV period.

So those were the main drivers. And the biggest part going forward will continuing to be the new store. The important thing to always remember is the enhanced merchandised performance of those new stores, which largely outstrips the increase in wage rates. So that's why we look at our coverage ratio, our old fuel breakeven metric, et cetera. It's really the expansion of the merchandise contribution and doing that efficiently is the key metric that you want to be looking at, not just the pure OpEx by itself.

Operator

And there are no further questions at this time. I will now turn the call back over to Andrew for closing remarks.

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R. Andrew Clyde
President, CEO & Director

Great. Thank you, everyone, for joining us today. As we know, these are challenging times for many consumers. And I think as we've illustrated, Murphy's long-term commitment to serving those customers with value, doing it in better ways with our new capabilities and continuing to grow, not only wins for them, but wins for all of us as investors as well. Thanks for your time today.

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

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