Company Name: Murphy USA
Company Ticker: MUSA US
Date: 2018-05-02
Event Description: Q1 2018 Earnings Call

Market Cap: 2,223.22
Current PX: 66.90
YTD Change($): -13.46
YTD Change(%): -16.750

Bloomberg Estimates - EPS
Current Quarter: 1.208
Current Year: 4.608
Bloomberg Estimates - Sales
Current Quarter: 3480.000
Current Year: 13881.833

Q1 2018 Earnings Call

Company Participants

- R. Christian Pikul
- R. Andrew Clyde
- Malynda K. West

Other Participants

- Benjamin Bienvenu
- Christopher Mandeville
- Bonnie L. Herzog
- Ryan J. Domyancic
- Ben Brownlow
- Carla Casella
- Damian Andrew Witkowski
- Bryan C. Hunt

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, good afternoon. My name is Kim, and I'll be your conference operator today. At this time, I would like to welcome everyone to the Murphy USA 2018 First Quarter Results Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

I'll now turn the call over to your host, Christian Pikul, Senior Director of Investor Relations. Please go ahead, sir.

R. Christian Pikul

Hey. Good morning. Thank you, Kim, and thank you, everyone, for joining us today. With me are 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 overview of the financial results, and then we'll 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 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.

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

R. Andrew Clyde

Thank you, Christian. Good morning, and welcome to Murphy USA's first quarter 2018 conference call. I trust you have all reviewed the earnings release, so I will start by adding some color to the quarterly results before Mindy provides some additional financial details, and we open up the call to Q&A.

We all recognize Q1 is the most challenging quarter of the year, and last year truly brought that point home. We also know that Q1 performance is the weakest predictor of full-year performance as 2017 also proved out. So, when looking at first quarter 2018 performance, I want to highlight three components of our strategy that are relevant to both our financial results and our long-term competitive positioning in the industry.

First point is that our fuel business showed resilience on many fronts this quarter. From a year-over-year perspective, we saw higher all-in margins on a cents-per-gallon basis, $0.114 per gallon versus $0.101, which led to higher total fuel contribution dollars of $114.6 million versus $102.7 million in the first quarter of 2017. This increase was largely driven by results from our product supply and wholesale business, which posted $0.03 of margin on a retail-equivalent basis, well above the prior-year contribution of $0.00.

More importantly, we delivered this performance in an environment not entirely dissimilar to last year, particularly with respect to a significant mid-quarter sell-off and RIN prices due to actions or speculation of actions related to the RFS program. But unlike last year, due to different market conditions impacting different parts of the supply chain, we witnessed an offsetting improvement in our spot-to-rack margin as we have often argued as what we would expect when RIN values decline all else being equal.

From a within the quarter perspective, January stood out as an exceptionally poor month, which has already been discussed by multiple retailers and analysts. Year-over-year volumes were down significantly because of lower traffic as fewer vehicle models were driven. On the other hand, fuel volumes were just under 100% of prior year in the month of March where there were few externalities.

From a longer term perspective, we saw the benefits of investments we have made in our supply asset positions and capabilities. Our Colonial position create an advantage when the pipeline allocated shippers for maintenance and the system tightened. This benefited long-term shippers like Murphy USA and led to both stronger internal supply margins and third party wholesale margins.

Our prior year investments in butane blending at our own terminals generated higher than planned uplift as we blended more barrels at higher margins. The rising price environment and associated price and timing variances offset in part the lower retail margins. While some have suggested the value of our supply models at risk, we believe Q1 demonstrated once again the benefit of our model and its resilience.

My second point about the quarter is that we continue to ruthlessly focus on performance improvement initiatives across the business. Through continued efficiencies from our labor model and store supply and maintenance cost, along with improvements to the merchandise business, we reduced our fuel breakeven metric by nearly 50 basis points to $0.0147 per gallon from $0.0195 per gallon in the first quarter of last year. We continue to fill questions from investors who ask whether there are continued opportunities to extract further potential from our stores, and the answer remains an unequivocal yes, as we once again showed this quarter.

For instance, we just launched scan-based trading for some items in our general merchandise category in the center of the store. This initiative strengthens our product mix, improves our margins, eliminate shrink, further reduces store labor as the vendor manages the merchandise activities, reduces working capital and eliminates inventory complexity both at the store level and back office functions resulting in lower SG&A. This initiative continues the trend of what Murphy USA has become distinctive for, growing our merchandise contribution, while lowering cost at the same time. This form of internal investment contrasts sharply with where the c-store industry is putting most of its efforts and

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energy, which brings me to my third point about the quarter.

We are maintaining a disciplined approach to capital allocation. While not attending the NACS conference myself, I too read the downbeat reports on the sector coming out of the event, and with all the capital cost and efforts being invested into food service models, it's not a surprise to see many firms worried about their profit outlook because not everyone is going to execute that model at the highest level needed to succeed.

Consequently, we continue to see more evidence of private companies attempting to exit the business ahead of looming capital requirements around EMV compliance in hopes of getting a high multiple. The task to transform their legacy networks of stores is indeed daunting. That said, our opinion of the opportunities in the industry from Murphy USA remain unchanged, and we remain upbeat about our potential. Yes, the business will continue to face a variety of headwinds, but when we look at our EBITDA per store, which has among the highest of our publicly-traded peers and 1.5 times to 2 times higher than some of the companies we've seen on the market, we see opportunity.

In fact, this quarter we received a one-time cash benefit, which we redirected towards share repurchase because we remain confident in our ability to make our business more competitive over the long-term. And while others are looking to sell, we remain active buyers, and the business we want to be buying is our own business, which is why we repurchased close to 1 million shares in the quarter.

While we believe our strategy and actions will create significant shareholder value over time, there will continue to be volatility in the business. Rising crude prices in April are setting up another challenging environment for Q2, which in our eyes inevitably sets the stage for a larger fall-off in prices that could result in a period of above-normal margins, volume and contribution for the back half of the year.

The point is the industry will continue to have highs and lows, disruptions and dislocations, externalities and headwinds, and periods of compressed retail fuel margins that all companies will have to endure. In our view, the productivity enhancements and associated innovation we continue to generate are the greatest source of value for any large-scale mature retail operator, and we have invested wisely to develop our capabilities and improve our margin and cost structures that enable us to be agile and resilient in any environment, which will ultimately benefit our long-term investors.

With that opening, I will turn things over to Mindy to discuss the financials and discuss Q1 capital spend for growth and share repurchase.

Malynda K. West

Thanks, Andrew, and hi, everyone. Revenue for the first quarter was $3.2 billion versus $3 billion in quarter one of 2017. This was largely attributable to higher product prices and to a lesser extent, higher merchandise sales. Average retail gasoline prices during the quarter were $2.34 per gallon versus $2.11 in 2017. Adjusted earnings before interest taxes, depreciation and amortization, or EBITDA, as previously mentioned, was $45.1 million in the first quarter versus $30.3 million in the same quarter last year.

Net income was up significantly for the quarter due to a $35.3 million after-tax benefit from the settlement of damages due to the Deepwater Horizon oil spill in 2010. The effective tax rate for the first quarter was 16.8%. That was lower than our 25% expected rate due to resolution of a discrete state tax matter during the period. We do still expect an all-in tax rate close to 25% in future periods.

Total debt on the balance sheet as of March 31, 2018 was $875 million broken out as follows: long-term debt of $856 million consisting of $494 million carrying value of our 6% notes due 2023, $295 million carrying value of our 5.625% notes due 2027 and $68 million remaining on our $200 million term loan. In addition to that, we are carrying $19 million of expected amortization under the term loan and current liabilities on the balance sheet. Using these figures and trailing 12 months EBITDA of approximately $480 million, which includes the net settlement proceeds, our leverage ratio approximates 1.9 times.

Our ABL facility remains in place with a $450 million cap subject to periodic borrowing base determination, currently limiting us to approximately $225 million at quarter-end, and at the present time, that facility is undrawn. Cash and cash equivalents totaled $144 million as of March 31, excluding the $1.1 million of restricted cash, resulting in net debt of approximately $730 million.

During the quarter we repurchased 929,000 common shares for $71.7 million at an average price of about $77 per share. Echoing the sentiment from our fourth quarter conference call, we remain committed to share repurchases and we expect to conduct future repurchases in the same disciplined way framed by our shareholder value model and for quarterly amounts consistent with our past history, subject of course to available cash balances and other demands on capital. There were 33.2 million common shares outstanding at the end of the first quarter.

Moving to CapEx. CapEx for the quarter, approximately $44 million. And at this time, we do expect our capital spending to remain within our guided range of $225 million to $275 million.

And that concludes the financial update, so I will now turn it back over to Andrew.

R. Andrew Clyde

Thanks, Mindy. With that, we can go ahead and open up the call to Q&A, Operator.

Q&A

Operator

Thank you. [Operator Instructions] Your first question comes from the line of Ben Bienvenu with Stephens. Your line is open.

<Q - Benjamin Bienvenu>: Hi. Thanks. Good morning.

<A - R. Andrew Clyde>: Good morning, Ben.

<Q - Benjamin Bienvenu>: I want to ask about the margin profile of the tobacco business, as well as the non-tobacco business. Non-tobacco business margins, under pressure, but tobacco business margins are considerably stronger than we would have thought. Just understanding the mechanics and the dynamics of what's going on there and how sustainable you think the all-in merchandise margin strength that we've been seeing in recent quarters is going forward?

<A - R. Andrew Clyde>: Yeah. So, I think on tobacco, we see the continued trends around the secular decline in cigarettes offsetting in part by smokeless and other tobacco products and some of the new innovation there. We continue to see ratable price increases from the manufacturers that when we pass those along, net-net, we end up improving our margins overall. So, it's a category that while you miss the decline in units and the traffic associated with that is it continues to grow margin dollars in contribution. And so, I think we'll continue to see more of that same trend in the future, as well.

<Q - Benjamin Bienvenu>: Understood. And then, thinking about the remainder of the year, particularly on the fuel business. 1Q hampered by weaker fuel margins on the retail side of the business in particular, and while higher than year-over-year on the all-in cents per gallon contribution, the remainder of the year requires all-in fuel margins to be considerably above the high end of the range. I'm just curious about how you guys are thinking about that in light of your all-in EBITDA dollar guidance that you guys have provided for the year thus far and haven't touched today.

<A - R. Andrew Clyde>: Sure. I think there's two things that we look at when we set up our plans for the year. What is the typical price structure that you would see in a normal year, and what's the range in which you would expect to see absolute prices fall within. And so, while the past isn't a good predictor of the future when we set up the plans, we do expect to see rising prices in the Q1 early Q2 environment. At some point, that peaks and falls off and then you start seeing significantly stronger demand, falling prices, better margins and the like at the end of Q2 and Q3.

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And so, that's effectively what we've built in. And so, how we achieve those margins is – usually, the biggest driver of it is what is the structure of the market itself and how are we pricing within that. 2017 was a year where volatility was pretty flat, right, in terms of the rise and fall. And so, without the kind of the hurricanes in the impact there, it was a much flatter profile. We're seeing this year crude prices rising and actually rising above some of the ranges set by experts in the industry several months ago. So we expect to see that rise and fall pattern.

The other thing, Ben, that you know, is that we continue to make improvements to our business. So whether it's carrier optimization, whether it's improving the diesel performance at our stores, which are up year-over-year at higher margins, that all contributes towards a strong cool margin as well. And we've seen years where Q3 has responded in a very strong way. And so, as we see prices going up, that actually bodes well for a stronger Q3. I'd be more concerned if prices were flat and we weren't seeing a whole lot of movement because that would undermine the ability for the sharp fall-off where you get the volume and the margins later in the year.

<Q - Benjamin Bienvenu>: Okay. Thanks for that color. And then, one quick question on calendar timing. Easter fell a little bit earlier this year and the year relative to last year. We've heard other retailers pointing to that as a benefit to the sales. Did you guys see any discernible implications as it relates to Easter falling into 1Q versus 2Q this year?

<A - R. Andrew Clyde>: We didn't. March was a really strong month. We talked about the fuel volumes being close to 100% and that was coming after 2017. March was well over 102.5% higher than 2016 that certainly translated into really good traffic in the stores for March, but we didn't attribute any of that to the Easter holiday per se moving up.

<Q - Benjamin Bienvenu>: Okay. Thanks. Thanks for taking my questions.

<A - R. Andrew Clyde>: Thanks, Ben.

Operator

Thank you. And your next question comes from the line of Chris Mandeville with Jefferies. Your line is open.

<Q - Christopher Mandeville>: Hey. Thanks for taking my questions. Andrew, just on the OpEx less CC fees, you had very solid results relative to guidance in that negative 1.4% range. How should we think about that going forward for the rest of year? Is the expectation that OpEx will ramp to meet that zero to 2% range or are you possibly ahead of your internal expectations?

<A - R. Andrew Clyde>: So, Q1 was solid. And the improvements we saw, as we talked about, maintenance, supply cost, were sustained. We've got some maintenance initiatives, though, that are going on that may lead to some kind of one-time cost there, so there could be some offsets. But we would expect, over the course of the year maintenance, supplies or a couple of areas, we're going to see improvements.

We continue to generate labor savings and efficiencies by better adherence to the labor model and the like. So, we got off to a head start. There's always gives and takes over the course of the year, but we certainly feel very confident about that part of our guidance for sure.

<Q - Christopher Mandeville>: Okay. And then, my second question being, while small in nature, I'm sure you've seen that Walmart wants to install roughly 100 EV chargers into their Supercenters by the end of 2019. Are you at all aware of the potential overlap with your sites? And then, maybe thinking more broadly about the competitive intensity today, how are Walmart and/or anyone else that you'd characterize as a high-volume operator acting these days compared to the last six months ago?

<A - R. Andrew Clyde>: So, on electric vehicles, I'm still waiting to see my first electric vehicle in a Walmart parking lot. And then no, I haven't been to all of them, but I don't expect that to create a lot of overlap, and we continue to update our views on electric vehicles and all the other factors that impact fuel demand. And actually, when we compare where we are sitting here today versus a year ago when we provided some insights on long range demand, the factors are more bullish than they were a year ago whether it relates to the economy and its impact on vehicle miles traveled,

whether it's the relaxation of the CAFE standards by the current administration, whether it's the challenges of electric vehicle manufacturers, the loss of subsidies in some states, et cetera. So, charging stations ought to be where people park their cars for a long time, not a very short period of time, and that makes sense. I'll look forward to seeing how that works out.

I think your second question was just largely around the competitive intensity of Walmart and other retailers. I think as we've alluded to, we've seen that pressure come down quite a bit in terms of new store additions. If you compared last year to the year before, to the year before that, we're all aware of the announcements they've made about the number of new Supercenters and neighborhood markets for their fiscal year 2019, which is largely our calendar year 2018. So, I think those new additions have diminished. And, as we've noted before as well, once new competitors come in and establish their position, they typically act very rationally once that position's been established. And so, if you see fewer new additions, then, you ultimately get back to a position where you've got more rational behavior in the marketplace. So, nothing new really to report on, on that side.

<Q - Christopher Mandeville>: All right. Thanks for taking the questions, and look forward to seeing you next month.

<A - R. Andrew Clyde>: Thank you.

Operator

Thank you. And your next question comes from the line of Bonnie Herzog with Wells Fargo. Your line is open.

<Q - Bonnie L. Herzog>: All right. Thank you. Hi. I have a question on the overall traffic, and what you guys are seeing for the industry in terms of stepped-up competition, whether it's from QSRs, dollar stores, grocery, et cetera, and then, also, what I might call the Amazon effect. And then, Andrew, could you also touch on the number of trips you saw in your store during the quarter, and if you're seeing that slow at all? Thank you.

<A - R. Andrew Clyde>: I can't comment on the Amazon effect impacting our store. I don't know what percent of our customers are Prime members, but I know that the segment of our demographic that aren't Prime members. What we are seeing though is the continued investment by Walmart in their pickup points and the success there, and as they continue to roll that out, as well as the towers they're looking at, and the parking lots.

And so, as we noted from the 100,000 customer intercepts we did a few years ago, 50% of our customers were coming to were from a trip to Walmart. And so, these trips to Walmart may look different that they did five years ago. But there're still trips to Walmart and they're passing by our store. And then, what we're seeking to do is get more of those customers who are going there to come in to our store whether it's through our loyalty program, or through our refresh stores, or our better offers, and the like.

So, I'm not seeing any negative effect from that, and as more and more people move online, and many of our markets that online models are going to be walmart.com and getting picked up at their stores, which means there's a high likelihood that means a trip to our stores. We're not impacted, really, by the QSRs because we're not in the food business. And I appreciate sort of the report you wrote about the NACS Summit and...

<Q - Bonnie L. Herzog>: Thank you.

<A - R. Andrew Clyde>: ...if I'd invested hundreds of millions of dollars in the food service business over the last few years with the stepped-up pressure on the QSRs, I'd be pretty downbeat as well. But we didn't. We invested our money in productivity improvements, rebuilding our older stores at the end of their useful life and building technology and capabilities to allow us to scale and grow our business. So, not seeing the impact of the QSRs. And other than the few really good private companies that have – many of them started as a hoagie shop or whatever and sell gasoline, we don't see a whole lot of impact from that.

Your last comment about sort of trips in general, I mean, you're well familiar with the trends in tobacco and the units decline there, but the ability to make up for that in margin dollars. Higher gas prices. I mean if you buy with the $20

bill, you're going to have fewer gallons per trip so you have more trips associated with that. And we're absolutely seeing that as well.

And so, there're pluses and minuses to a higher price environment. One is, more trips, right. Second is that customer on the margin who wasn't as price-sensitive when prices were below $2 are starting to get a little bit more price-sensitive, and below price retailers will get their extra share of that because we all know there's more low price retailers out there today than there were 5 or 10 years ago. And so, there'll be pluses or minuses when it comes to trips and who gets their fair share of them.

<Q - Bonnie L. Herzog>: Okay. That's helpful. And then you made some comments earlier about your position and I'm thinking about in the broader context and do you feel at all that you're possibly structurally challenged in any way versus your peers especially given the limitations you have with your box sizes. And, I guess, I'm thinking about this in the context of the opportunities that many of your c-store peers have as they try and premitize their in-store offerings as well as the customer experience. And, I think, what you guys have built is on the other end of the spectrum. But could you maybe just touch on that for us and help us think about what you see your company evolving to in the next three to five years?

And also on that, I'd love to get your thoughts on any stepped-up M&A. I know that hasn't been a priority, but you did make a comment this morning about a lot of operators are getting out of the business, and could that be an opportunity for you to expand your store base? Thanks.

<A - R. Andrew Clyde>: Okay. I'll try to remember all of those questions. So, I think if you go back to the chart we use a lot of our analyst days about the competitive models at scale, I would say they're different, certainly the hypermarket model and the big box model, but they're both seeking to achieve the same thing, which is standalone economics, which mostly means a zero breakeven. So you need no margin from fuel to be able to break even and cover your costs.

So, are we structurally disadvantaged versus the others? Absolutely not. We're structurally advantaged when you think about that ultimate measure, but in a different way than they're trying to get there. They're trying to get it by selling more food and higher margin items to cover the significantly higher labor and other cost associated with that model to generate standalone economics for their business. No one's ever going to be selling fuel at a loss, right. It's a profit center. It always has been for every retailer out there.

And so, I would say, we're structurally advantaged similar to the way the best large big box firms are, but just in a different way. The structurally disadvantaged players are these small boxes retailers, the 2,000 square foot ones with the legacy formats, the ones that are selling 80,000 gallons a month, which is the industry average, a 100-something out of the store, and they got $0.10, $0.12, $0.15, $0.20 breakevens. So, I think that bottom quartile breakeven figure you cited from the NACS data, which isn't the industry average, but it's their poll of companies. Comparing our $0.01 breakeven to their $0.20 breakeven, we're absolutely advantaged. If you compare our $0.01 breakeven to a $0.01 breakeven that a big box with food would have, we're at structural parity. We're just serving a different customer on different missions that are coincident with other trips that they're making. So, we see that as a core reason behind continuing to build that strength.

On the M&A side, look, we look at things from side – from time to time. And what I will tell you is when you see a chain that is 90% legacy stores, that's built their handful of bright shiny objects on 2 acres to 3 acres that cost millions and millions of dollars that aren't generating superior returns, and the bottom-line EBITDA per store is 50% to 60% of our EBITDA per store. It's really hard to get excited about that. The amount of capital that then has to go into refurbishing those stores, the EMV compliance, if there was a truly distinct capability that came with that we could then at some point maybe pivot towards a different model, that might be interesting, but most of the stuff you're seeing sold out there doesn't bring along with it some distinctive capability that you would pay a premium for.

<Q - Bonnie L. Herzog>: Okay. Thank you.

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Operator

Thank you. And your next question comes from the line of Ryan Domyancic with William Blair. Your line is open.

<Q - Ryan J. Domyancic>: Hey. Good morning, Andrew. Thanks for taking my questions.

<A - R. Andrew Clyde>: Good morning.

<Q - Ryan J. Domyancic>: So, were there any pricing or other actions that you proactively took in March that resulted in that strong fuel gallon performance?

<A - R. Andrew Clyde>: None in particular. No. I mean I think it was just a month with less externalities, if you will. We had a price falloff at the beginning of the month and then a price increase towards the end of the month, so you had some structural advantage as you were coming into the month from pricing structure standpoint. And so, we didn't do anything in that environment different than we would have done in any other similar type environment.

So, we put some additional margin on the street when it's appropriate on the way down and we have to take our foot off the gas on the way up, be responsible so that we don't find ourselves with negative margins. It was just a good example finally of a month without a lot of noise and disruption around it and it comped well, it flowed through to the stores and we still generated operating cost savings in that same period. So, I'd like to see more months like that, and I'd certainly like to see more of the back half of the year without those major externalities.

<Q - Ryan J. Domyancic>: Well, hopefully, more to come for those months. And then just quickly on the second question, is the timeline for the loyalty program pilot still in place with testing in a few larger metros this summer and then maybe a larger national rollout towards the end of the year?

<A - R. Andrew Clyde>: Absolutely. So, we're doing a beta test with our employees here in El Dorado at our headquarter store and our El Dorado store. And so from that, we're testing the technology, we're looking at the data and analytics that come out of that to say are we going to be able to get the insights and data to be able to generate the dynamic levers that we will pool in this program, which is what's key to make it work for an everyday low price retailer like us. We're still planning our two pilots in June.

The amount of time that we run the pilot for is one of those things that depending on the early findings we may accelerate it. But given that a big part of this program is about attracting a low share of wallet and new customers that don't already shop with us we need to make sure we give that the right amount of time to develop those insights. And so, we'd be content running the pilot throughout the rest of the year with a more likely launch in 2019 nationally.

And as we've stated before, we haven't built in any upside from a margin standpoint into our guidance this year, but we have built the cost of the program into our SG&A numbers.

<Q - Ryan J. Domyancic>: All right. Thanks for the detail. Thanks, Andrew. Thanks, Mindy.

Operator

Thank you. And your next question comes from the line of Ben Brownlow with Raymond James. Your line is open.

<Q - Ben Brownlow>: Hi. Good afternoon. Just going back, Andrew, you touched on the non-tobacco side and was hoping you give a little bit more color on that in terms of the same-store sales and the contrast with what you're seeing on the decline in the non-cigarette gross profit per store. Is that a mix, is it promotion? Just give a little bit more color around that.

<A - R. Andrew Clyde>: Yeah. It's a mix and I'll use March as an example. March same-store sales for non-tobacco were up 5.9%. Margins were up 7.1%. Those are really good numbers, lotto/lottery was a big part of that. And so, we continue to see just the way those programs are structured, higher jackpots. We are also increasingly a destination for that because of our offer and the participation in that programs. Beverages, we're strong in that month and – as well as

beer, wine, liquor being added to more and more stores, as well. There are some products that we've gotten out of. We've talked about the additives, some of the card programs and the like. And so, we've had to overcome that mix shift as well from the negative side with these other improvements.

Promotion effectiveness is something we continue to work on. Some of the incentives that we've had designed for our store employees in the past around the circle of stars, and having kind of three main items being the focus. We look at measures now percent sold on deal, which has a much broader range of products. And so, changing how we're motivating folks, incentivizing folks and measuring those as well. And that also helps improve the mix as well.

<Q - Ryan J. Domyancic>: Great. That's very helpful. And on PS&W segment, it seems like the spot-to-rack spread is improving a little bit quarter to-date, albeit still very volatile. Any color on what you're seeing in the second quarter on PS&W excluding RINs? And do you think, if that's true, do you think that there's more of a seasonality aspect to that or you think it's some of the market response to lower RIN values?

<A - R. Andrew Clyde>: Yeah. So, I firmly believe, and that was our submission to the EPA, the White House and others that we interacted with around the point of obligation. And, I think, the EPA came back unequivocally and said, yeah, there is a relationship between RIN prices and the refinery gate supply price. And so, as we have seen in periods where RIN prices aren't kind of dislocated, if you will, based on speculation and rumors and all of that, that the product supply and wholesale margin improves. And so, we've seen that relationship.

And we expect to continue see it. We'll also expect to see both of those have dislocations from time-to-time based on independent facts. Colonial had allocation due to the maintenance, and so that tightened the system up. That's generally good for long-term shippers like us, and we remain a committed long-term shipper. Some of the smaller players who got line space as part of the lottery and were making money off of that, they got tired of writing checks with negative line space. And so, like any other long-term capital asset like that, things come back into equilibrium over time and we're seeing that with the Colonial as well.

So, it's essential to us for ratable secure supply, but we also believe that assets like this return to equilibrium. A good example of that is three years ago, we were seeing evidence of open seasons on expansion programs and those discussions have pretty much dried up. So, I think that is – you're going to see sort of temporal shifts in value across the value chain and then they come back to you. We just have to be adaptive and responsive to those changes.

I mentioned the butane blending. It's a seasonal opportunity where you get to blend butane into the gasoline pool. We made those investments in 2016-2017. We generated significantly higher uplift from that due to the market pricing structure, but also how we manage the inventory in the blending around that. So, there're little things on the margins, but we've talked about this is a penny profit business. Those things that are a $0.001, can start adding up over time.

<Q - Ryan J. Domyancic>: Great. Thank you.

Operator

Thank you. And your next question comes from the line of Carla Casella with JPMorgan. Your line is open.

<Q - Carla Casella>: Hi. On the stores that you have in development right now, have you set the timing of the opening and then what's the – in terms of the timeline for your opens for the remainder of the year?

<A - R. Andrew Clyde>: Yeah. So, we kind of have a two-fronted effort. So, we start a bunch in the first part of the year which we've got 10 raze-and-rebuilds under construction and 12 new stores. We've opened two or three year-to-date. And as that program gets wrapped up, then they'll get opened and then we'll kind of start the second tranche of raze-and-rebuild and newbuilds that then tend to open more in that late October/November, and some slip into December timeframe. So that's kind of the two-pronged window. And we try to minimize a whole lot of openings during the June, July, August time period, if we can.

That's our busiest time period, that 100 days of summer and the driving season. So we want everyone all hands on deck focused on that. So the most stores we can get opened, especially the raze-and-rebuilds to benefit from the summer

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program, we want to do that and then get the other raze-and-rebuilds to new stores started so that they can open by the kind of November time period.

<Q - Carla Casella>: Okay, great. My other questions have been answered, so thank you.

<A - R. Andrew Clyde>: Thank you.

Operator

Thank you. [Operator Instructions] Your next question comes from the line of Damian Witkowski with Gabelli & Company. Your line is open.

<Q - Damian Andrew Witkowski>: Hey, Andrew. So at minus 4% for same-store sales volume, are you losing share, market share?

<A - R. Andrew Clyde>: Well, in January, we're minus 8%, right? With the winter storms, I think people – that's fewest number of vehicle miles traveled in any month for some extended period of time. And so, I'd have to look to see total January demand when the official data comes out, I guess, in June on that standpoint, holding flat on a same-store basis and March is strong. So, if we think about the industry now, probably growing fuel demand at kind of 1-plus percent.

If we grow total volume in our markets including new stores at greater than 1%, which I think we would expect to do with the new stores, we would actually gain share. So, if you get it down to an individual market where we're not building a new store and someone else is, we're losing share in that market or holding our own. So, really, it's a function of what's the total demand, what's the total number of industry build, how many builds are we doing and the volume, we get from that.

We did an analysis that looked over every decile of our stores. And whether it was the top decile or the bottom decile, half the stores maintain share or grew volume over the period and half declined on some basis, some more than others and so forth. So, it's really kind of a mix when you get down to the store-by-store basis because in some markets, it may be two or three other competitors that are closing shop or after an M&A activity, someone decides to rationalize part of the portfolio they get or change their tactics there.

<Q - Damian Andrew Witkowski>: I mean I can't imagine that someone is entering your market who is actually selling fuel below where you're doing except for maybe Costco or someone like that. But is it just that that's not the only thing that matters., and so, any new entrants?

<A - R. Andrew Clyde>: Yeah. So, if you take a market like Dallas, our Dallas West store used to be our highest volume store until we opened one in Florida. But if you have two QuikTrips that open on I-30 on the interstate exits before and after that, that store instead of doing 600,000 gallons is doing north of 500,000 gallons, so it's down.

<Q - Damian Andrew Witkowski>: Yeah.

<A - R. Andrew Clyde>: But I'd love that store doing 500,000 gallons. Now, you've got two stores, a half a mile or a mile away, that are both probably doing 400,000 or 500,000 gallons as well. The fact that we only lost what we did either meant there's a lot more people in that area or some other competitors are getting hurt a lot worse. And given the competitor I just named, when you ask consumers why do they go there, it's based on convenience and food. They also have low price.

And so, I think we're going to continue to see what I describe as the haves and the have-nots in this space. There are two different models for the haves. There's the big box models like the QuikTrips, the Sheetz, the Wawa's that have developed their programs that work and there's the hypermarket models like us.

And then there's the have-nots who have the high fuel breakeven requirement. They're hanging on. They can hang on for a long time. And ultimately, they get acquired and you're also seeing some acquirers at the bottom end of the market

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as well that are kind of rolling up some of the weaker chains. So, I think we're going to continue to see rationalization of the have-nots in this industry.

<Q - Damian Andrew Witkowski>: And then from a consumer perspective, with gas prices going up, are you seeing anything there that is discernible and how they behave? I mean, you'd pointed out that they actually come in more frequently because they have $20 to spend on a fuel. They have to...

<A - R. Andrew Clyde>: Yeah. It's too early. It's too early to tell, Damian. In my former life, we looked at this, but we had monthly data from like panel data research companies where you could look back over a really long extended period like 2005 to 2008, and you could discern those patterns. And so we just haven't been able to pick that apart at this point. We know that behavior should exist. The other issue is there is just a lot more low-price outlets out there. So, it gets redistributed.

<Q - Damian Andrew Witkowski>: Yeah. Thank you.

<A - R. Andrew Clyde>: You're welcome.

Operator

Thank you. And your next question comes from the line of Chris Mandeville with Jefferies. Your line is open.

<Q - Christopher Mandeville>: Hey, thanks for the follow-up. Andrew, just in terms of recent new store performance, as you kind of pivot entirely to the express format, is there any observable difference that you could call out in terms of how they're ramping versus prior vintages?

<A - R. Andrew Clyde>: Yeah. So, I think the new stores, if we look at the 2015, 2016, 2017 class, they all – they're all continuing to ramp up. So, we're seeing year-on-year performance improvement on those. I think the tobacco ramp up, you see differences that if it's in a minimum tax state versus not because those customers go somewhere else for those few months, and it's a lot easier to get them back if you don't have price restrictions in the market. As we continue to focus on the most attractive markets, I think we've got the three USA stores left from the Walmart portfolio this year to build out. We would expect to see a better mix from a geographic standpoint than we did if you looked across the 2015, 2016, 2017 class.

We can also continue to refine our store opening processes. And one of the things we're even looking at is the stores that we opened during the hurricane period last year when you had severe supply shortages and anomalies, you couldn't open them the same way, you did. Do we need to think about doing some other promotional activity at those stores to make sure you gain the customer acceptance for those.

So bottom line, the more recent class has continued to ramp up, nothing new versus what we've talked about before. The current raze-and-rebuilds also continue to meet or exceed the expectations in terms of delivering a better format, more dispensers, more product offers on those. So we continue to be very encouraged about the returns on those, especially given these are stores at the end of their useful life.

And again, we talked about the haves and the have-nots, we're reinvesting back in those stores because we have the structural advantage, because we have the low breakeven, because we can achieve those reinvestment returns. The weaker stores chains out there would be unable to rebuild what they have and get those kind of return economics.

<Q - Christopher Mandeville>: Okay. And then just maybe lastly as it does relate to the raze-and-rebuilds, is there anything notable the call out from the downtime that you have currently in terms of how that's impacting volume trends and/or is there anything to which you could help us think about going forward?

<A - R. Andrew Clyde>: No, I think – and that's why we really wanted – we report both the same-store sale and the average per store month numbers, and we've got tables in the earnings release on that. We tend to focus a lot more internally on the same-store number now that raze-and-rebuilds is a much bigger part of the portfolio. And some of the stores that we take down are 400,000, 500,000, 600,000 gallon stores that are 15 years old that are doing this out of

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four or five dispensers, right?

And so the one thing I would say is it really bites to take those stores out of the fleet for that period of time. But it's great when they come back performing the way they do. But that's why we look at the same store metrics, and we break all our analysis down here by build class for the new stores by race-and-rebuild class and then have a pretty consistent basis stores we look at that are like 2014 class and older.

<Q - Christopher Mandeville>: All right. Thanks again.

<A - R. Andrew Clyde>: Yes.

Operator

Thank you. And your next question comes from the line of Bryan Hunt with Wells Fargo. Your line is open.

<Q - Bryan C. Hunt>: Thanks for your time, Andrew. When you look historically, I mean, you chase Walmart, you mentioned earlier in the call they're opening a lot fewer stores. I was wondering could you give us an idea of what you're looking for in new store opening strategy and whether there is a retail or two that you find attractive to follow around?

<A - R. Andrew Clyde>: Yes. The thing that made it so productive following Walmart around and many others had the same strategy is they are just the world's greatest aggregator of price-sensitive customers. And grocery stores on average have about a third less traffic there. So, there – it's a great proxy for traffic. And so there are other good proxies for that. If you've got other big boxes, whether it's home improvement or other chains along a thoroughfare that generates the same traffic. And so again, if you go back historically, 70% to 80% of our fleet is in rural markets, right.

And so, that's why it also made sense to follow them as the rural market attractive locations have been built out and saturated, you're left with the urban and suburban ones, so there are more inter-sections there, as we discussed in our prior calls, we're continuing to target five key markets in which we would be building the larger 2,800 square foot modular store. And by definition, that's going to be more of an infield at those high traffic locations away from the Walmart Supercenter. So, it's less about saying, hey, we're going to go attach our reins to grocery store A or mass merchant discounter B or home improvement store C. It's about traffic. The Supercenter has just been a great proxy for that, but it's not the only proxy for that.

<Q - Bryan C. Hunt>: And just as a follow-up. I mean you talked about breakevens earlier across the whole business. For that modular box 2,800 square feet, is the breakeven materially different than it is for the higher velocity locations from a fuel perspective?

<A - R. Andrew Clyde>: It is. The sales are higher, the margin is higher, the mix is higher, the labor is higher but not that much higher. And so, you end up with kind of all the benefits. And when you had a Beer Cave and just a broader set of offerings and categories, you can strike that balance and you're coming just short of having to then step over that chasm to get into the 5,000 to 7,000 square foot models where you've got a kitchen, you need to have a commissary or you need to have a different type of program. And we looked at that model versus the 3,500 square foot model which is stick-built. We actually find this as kind of the right way to maximize the footprint for us.

<Q - Bryan C. Hunt>: And then my last question is, when I think about greenfield locations, how many – can you give us an idea what the inventory looks like?

<A - R. Andrew Clyde>: Yeah. So, we don't talk about the inventory. We typically just say, look, here's our plan – newbuild pipeline, and we expect to continue to do up to 50, 55 stores with the mix between newbuilds and raze-and-rebuilds and allocate capital at about those levels, and then have the balance for share repurchase on our kind of balanced approach.

<Q - Bryan C. Hunt>: Thank you for your time, and best of luck.

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<A - R. Andrew Clyde>: Thank you.

Operator

Thank you. There are no further questions at this time. I'll turn the call back to the presenters for closing remarks.

R. Andrew Clyde

Great. Well, thank you for your time today and interest, and all the best. Thank you.

Operator

Ladies and gentlemen, this concludes today's conference call. You may now disconnect.

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