TRANSCRIPT
2Q 2021 EARNINGS CALL

PHILLIPS 66 PARTNERS (NYSE: PSXP)
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PHILLIPS 66 PARTNERS PARTICIPANTS

Jeff Dietert, *Vice President, Investor Relations*

Kevin Mitchell, *Director, Vice President and Chief Financial Officer*

Casey Gorder, *General Manager, Operations*

Tim Roberts, *Director and Vice President, Operations*

MEETING PARTICIPANTS

Spiro Dounis, *Credit Suisse*

John Mackay, *Goldman Sachs*

Michael Blum, *Wells Fargo*

Jeremy Toney, *JPMorgan*

TRANSCRIPT

Operator:

Welcome to the Second Quarter 2021 Phillips 66 Partners Earnings Conference Call. My name is Hillary, and I will be your operator for today's call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. Please note that this conference is being recorded.

I will now turn the call over to Jeff Dietert, Vice President, Investor Relations. Jeff, you may begin.

Jeff Dietert:

Good afternoon, and welcome to Phillips 66 Partners First Quarter Earnings Conference Call. Participants on today's call will include Kevin Mitchell, Vice President, Finance, and CFO; Tim Roberts, Vice President and COO; and Casey Gorder, General Manager, Operations.

Today's presentation materials can be found on the Events section of the Phillips 66 Partners' website, along with supplemental financial and operating information. Slide 2 contains our safe harbor statement. We will be making forward-looking statements during today's presentations and our Q&A session. Actual results may differ materially from today's comments. Factors that could cause actual results to differ are included here, as well as in our SEC filings.

With that, I'll turn it over to Kevin.

Kevin Mitchell:

Thank you, Jeff, and good afternoon, everyone. In the second quarter, Phillips 66 Partners delivered solid financial results and reliable operating performance across the business. Our earnings reflect higher throughput on our wholly owned and joint venture assets. During the quarter, we advanced our capital program. We continued construction of the C2G Pipeline connecting the Clemens Storage Caverns to the petrochemical facilities in the Corpus Christi area. The pipeline is expected to be operational in the fourth quarter of this year.

The Bakken Pipeline optimization project continues to progress with the next phase of incremental capacity commencing service this month. The C2G Pipeline and the Bakken Pipeline are both supported by long-term commitments.

In July, the board of directors approved a second-quarter distribution of the $0.875 per common unit unchanged from the first quarter of 2021. Phillips 66 Partners remains committed to safe, reliable operations, a strong balance sheet and disciplined capital allocation.

Moving to slide 4 to discuss financial results. Phillips 66 Partners reported second-quarter earnings of $225 million compared with a first-quarter loss of $18 million. Our first-quarter results included a $198 million impairment resulting from the partnership's decision to exit the Liberty Pipeline project.

Adjusted EBITDA was $337 million this quarter, an increase of $48 million from the prior quarter. The improvement in earnings and adjusted EBITDA reflects higher volumes and lower utility costs following the first- quarter winter storms, as well as higher pipeline and terminal volumes due to increased utilization of Phillips 66 operated refineries.

Second-quarter distributable cash flow was $267 million, up $34 million from the prior quarter. The increase reflects improved earnings which were partly offset by higher maintenance capital in the second quarter.

Slide 5 highlights our financial flexibility and liquidity. We ended the second quarter with $2 million of cash and $734 million available under our revolving credit facility. We funded $44 million of growth capital during the quarter. This included spend on the C2G Pipeline and funding for the Bakken Pipeline optimization project.

The debt-to-EBITDA ratio on a revolver covenant basis was 3.0, which is consistent with our target to remain below 3.5. Our distribution coverage ratio was 1.34. In April, we repaid $50 million of tax-exempt bonds and borrowed $450 million under a new term loan agreement. Proceeds were primarily used to repayments borrowed under the partnership's revolving credit facility.

This concludes our prepared remarks. We'll now open the line for questions.

Operator:

Thank you. We will now begin the question-and-answer session. As we open the call for questions, as a courtesy to all participants, please limit yourself to one question and a follow-up.

Your first question comes from Spiro Dounis with Credit Suisse.

Spiro Dounis

Hi guys, good afternoon. Kevin, I know you’re generally not in the practice of providing firm guidance, but I was hoping maybe if you could help frame up what the second half of the year might look like relative to the first half. It would be helpful to hear your thoughts on the macro environment, maybe any specific drivers, performance, as we head here into the second half?

Kevin J. Mitchell:

Yes, Spiro. I think Tim is going to make a few comments on that.

Tim Roberts:

Yes, Spiro. With regard to the macro, I mean, obviously, the first quarter was impacted by, one there is a seasonal element coupled with the fact that we had winter storms. So, as things have picked up and there's been a recovery in the overall market from the COVID-19, we've benefited clearly in the 2Q with regard to refining utilization. Then, also, we've seen some increase in production out in the basins. I mean, nothing too extreme, but you are seeing a normalization going on as demand is picking up globally. We would expect that to continue through the third quarter. And then, through the fourth quarter, obviously, there are some elements, where you see some seasonality. But generally speaking, second quarter moving into the third quarter, we feel very constructive, especially as demand continues to pick up globally.

Spiro Dounis:

Great. That's helpful. Thanks for that. And the second question is just around capital return. It seems some peers now have started to recommence distribution growth and formalize some buyback programs just given that stabilization and macro outlook. And so, I'm just curious how you guys would describe your capital return goals as we sit here today. What do you sort of need to see first to either recommence distribution growth or initiate a buyback program? And on buyback specifically, I think we're seeing some peers buy back at DCF levels or yields of around 11%. Phillips 66 Partners is, of course, trading north of that right now. So, I'd imagine that stream is attractive, but I'm sure you've got the operations there that will be helpful to sort of layout?

Kevin Mitchell:

Yes, Spiro. As you look at the overall capital allocation priorities, it all comes down to how we manage coverage and leverage. in terms of the committed outflows, we've got the maintenance capital, which — that's going to continue. So, this year, I think the maintenance capital budget is $135 million or so. And I don't anticipate that being dramatically different as you look into future years. The growth capital this year, the budget is $165 million. There are more limited opportunities than we've had historically or in the earlier years of the MLP, and that probably continues to be relatively low compared to historic levels. But at the same time, if you look at where we are from a coverage standpoint, this quarter 1.34, which for Phillips 66 Partners is quite strong, but in the overall scheme of things that doesn't actually give you that much flexibility. I think one of the reasons that was strong in the second quarter is because we had lower maintenance capital, so you can revert to some of the more normal maintenance capital. In absolute dollar terms, that's maybe $50 million a quarter of coverage to basically fund the growth capital and then whatever other discretionary uses of capital you might have out there. So, I don't think there's a lot of room to do much for a period of time, at least beyond some modest amounts of growth capital within the sort of overall construct of the available cash that we have available.

Operator:

Your next question comes from Michael Blum with Wells Fargo.

Michael Blum:

Good afternoon. I wanted to maybe stay on this topic and see if you can expand a little bit on your comments on growth capital. Do you see any large or small potential projects on the horizon, whether it comes in the nature of those? And if the answer is not really, then I'd just love your latest thoughts on just how you view the MLP within the structure of the Phillips 66 family if there really isn't a need to finance any growth in Midstream. Thanks.

Kevin Mitchell:

Yes. I think that you'll see continued, I'll call them, optimization projects around the existing infrastructure because Phillips 66 Partners has a really nice portfolio of assets. There will continue to be opportunities to invest around those. They tend to be relatively small projects, but they also tend to be very attractive economics. And so, we'll continue to do that. Given where — if you just step back and look at the sort of macro midstream environment, where generally there is — the sort of major pieces of infrastructure are already in place to feed the needs that are right there. So, I think it's much less likely that you're going to see significant investment in organic growth projects. So, I think it will be more of a continuation of some of these smaller optimization-type projects from that standpoint. I don't know, Tim, if you've got any other perspective on that?

Tim Roberts:

No, I think you covered it. To give you a little bit of context on the smaller projects, Michael, it will be at one of our sites, maybe on Gay Oak, where we add a connection in, and we may have to add 10 miles of pipe. We add a storage tank. In some of our terminals, we may add truck racks, but that's the type of scope we're talking about as far as the incremental optimization opportunities.

Operator:

Your next question comes from the line of John Mackay with Goldman Sachs.

John Mackay:

Hi, everyone. Thanks for the time. I just wanted to follow up on the part of Michael's question that didn't quite get an answer there. Just curious if we can spend a minute or two talking about how Phillips 66 is looking at Phillips 66 Partners from a strategic standpoint here and kind of what that outlook there could be?

Kevin Mitchell:

Well, I think given that this is a Phillips 66 Partners call, I think all we can do is reiterate what we've said in the past, and in reference to the 13D filing that was done, I think it must be coming up to a year ago now, it was about a year ago. And that was — it basically gave Phillips 66 the flexibility to consider alternatives around the path forward for the MLP, but it certainly does not obligate any particular decisions or path forward. And I think we just leave it at that. Those statements still hold true that the 13D gives Phillips 66 flexibility to consider alternatives. But there's no more to say on that at this point.

John Mackay:

All right. That's fair. I think it feels like a year, though that would have been like six months ago. So, that's fine. A lot is going on. Maybe just one smaller one. Just in terms of the smaller projects that could come up, I'm just thinking, in terms of messaging, are these things that you guys expect to keep talking about in releases or is it the thing where, hey, if we don't start to see something in the next couple of releases, maybe it looks like 2022 CapEx could be a lot lower?

Tim Roberts:

Yes. Look, I think at this point, it will depend on really the size of the project. It's hard for us with regard to our release to be talking about maybe a $3 million project. So, I would say it depends on what the size of the project would be. I mean, some of these — if you're adding a pipeline or pipe, some stub, a lateral on to an existing pipe with some tanks, I mean, you can get up into the tens of millions of dollars there, but not hundreds of millions of dollars. So, depending on where that is, and it's hard for me to give you that cut-off, if we feel it’s material to Phillips 66 Partners, obviously we would have some sort of release. But certainly during earnings calls or even in our Qs, we'll talk about projects that are underway and — or projects that — well, projects that are underway or being completed.

Operator:

Your next question comes from Jeremy Tonet with JPMorgan.

Jeremy Tonet:

Hi. Good afternoon. I want to start with the DAPL expansion there. I was wondering if you might be able to provide some color as far as this first expansion came online. What was the cost for Phillips 66 Partners on that? What type of capacity was coming online with this first expansion here? And are there any regulatory approvals that need to put that capacity into service?

Casey Gorder:

Yes, Jeremy. Thanks for the great question. The expansion takes capacity up to around 750,000 barrels a day. The spending relative to Phillips 66 Partners in 2021 is a little bit under probably $50 million. We think that through next year it will be kind of $325 million or so — is kind of a capital number where we zero in on the capital invested front.

Tim Roberts:

And on the regulatory approvals, those have already been received. So, nothing outstanding at this point in time.

Jeremy Tonet:

Starting up this month?

Tim Roberts:

Yes, that commenced the capability and the commissioning, and it’s starting.

Jeremy Tonet:

That's very helpful. Thanks for that. And then with the C2G Pipeline here being pushed back a bit, is it tied to the Exxon, SABIC cracker, or just any other drivers to that timeline shift?

Casey Gorder:

No. It's really weather-related with the timeline shift. And we have said all along the real kind of commercial in-service date would be year-end. And then there may be some potential to flow some barrels northbound between kind of mechanical completion and commercial in-service at the end of the year. With weather delays, that window for kind of northbound volumes has narrowed. But I think we said last quarter we didn't expect those to be material anyway and still wouldn't expect it to be material. So, no change to the ultimate in-service date of the larger project or the MVCs underpinning that project.

Jeremy Tonet:

That's very helpful. Thanks. And last one if I could sneak it in. It seems like the midstream landscape has changed a bit. And there has been maybe a little bit more activity on the M&A side particularly as it relates to liquids, logistics, terminals, what have you. And just wondering, I guess, Phillips 66 Partners’ thoughts on consolidation in the midstream sector at all if there are any thoughts you're willing to share there.

Kevin Mitchell:

I think what you've — Jeremy, you've probably heard us say in the past that we do think that if you just take a sort of big picture view that across the midstream sector, you will see consolidation take place. You're seeing that happen in the upstream. And based on this morning, you're starting to see some of that happen in the downstream. And so, there's a lot of players out there in midstream.

And I think part of one of the impediments to more consolidation or at least easier consolidation is just the capital structure across the midstream space with so many MLPs with different governance models, which I think precludes some of that potentially happening. But ultimately, I think for the midstream business to compete well, it needs to be — there needs to be some consolidation when you drive efficiencies, shutdown idle plants and leverage the infrastructure that's available and create some value that way.

Operator:

We have reached the end of today's call. I will now turn the call back over to Jeff.

Jeff Dietert:

Thank you. We appreciate your interest in Phillips 66 Partners. And please follow up with Shannon or me if you have any further questions. Thank you.

Operator:

Thank you, ladies and gentlemen. This concludes today's conference. You may now disconnect.