TRANSCRIPT
Q2 2015 EARNINGS CALL

PHILLIPS 66 PARTNERS (NYSE: PSXP)
July 31, 2015 AT 2 pm EDT

PHILLIPS 66 PARTNERS PARTICIPANTS

Kevin Mitchell, Vice President, Investor Relations

Tim Taylor, President

Robert Herman, Senior Vice President, Operations

Greg Maxwell, Vice President and Chief Financial Officer

Tom Liberti, Vice President and Chief Operating Officer

CALL PARTICIPANTS

Elvira Scotto, *RBC Capital Markets*

Jeremy Tonet, *JPMorgan*

Kristina Kazarian, *Deutsche Bank*

Brian Zarahn, *Barclays*

TRANSCRIPT

Operator

Welcome to the Second Quarter 2015 Phillips 66 Partners Earnings Conference Call. My name is Leanne 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 Kevin Mitchell, Vice President, Investor Relations. Kevin, you may begin.

Kevin Mitchell – Phillips 66 Partners – Vice President, Investor Relations

Thank you, Leanne. Good afternoon and welcome to the Phillips 66 Partners Second Quarter Earnings conference call. With me today are Tim Taylor, President of Phillips 66 Partners; Greg Maxwell, Vice President and CFO; Bob Herman, Senior Vice President, Operations; and Tom Liberti, Vice President and Chief Operating Officer. The presentation materials we'll be using during the call can be found on the Events section of the Phillips 66 Partners website along with supplemental financial and operating information. We'll have time for questions at the end of the presentation.

Slide 2 contains our Safe Harbor statement. It's a reminder that we will be making forward-looking statements during the presentation and the question and answer session. Actual results may differ materially from what we present today. Factors that could cause actual results to differ are included here as well as in our filings with the SEC.

With that, I'll turn the call over to Tim Taylor for some opening remarks.

Tim Taylor – Phillips 66 Partners – President

Thank you, Kevin and good afternoon everyone. As you can see from the graph on Slide 3, Phillip 66 Partners continues to deliver on our objective to achieve a 30% compound annual growth rate on distributions from fourth quarter 2013 through 2018. We've increased our limited partner distribution every quarter since the IPO and maintained a sound coverage ratio. We plan to continue to grow our distribution supported by dropdown acquisitions from our parent, Phillips 66, organic projects constructed at Philip 66 Partners and strategic acquisitions that benefit both the LP unitholders and the GP owner.

In the second quarter earnings benefited from three months of contributions from our ownership interest in the Sand Hills, Southern Hills and Explorer pipelines which were acquired in March of this year. This acquisition helped support the recently declared second-quarter distribution of $0.40 per unit, which is 8% percent higher than the first quarter of 2015 and a 33% increase over the second quarter of 2014. Since the IPO, we have increased distributions at a compound annual growth rate of 44%.

Turning to operations, total pipeline throughput volumes for the quarter excluding the volumes from equity affiliates were 728,000 barrels per day down 2% from the last quarter. Total terminaling throughput volumes were 942,000 barrels per day, 5% lower than in the first quarter. These decreases were primarily due to lower volumes in the Sweeny to Pasadena Products System and the Clifton Ridge

Crude System, resulting from maintenance activities at the connecting Phillips 66-owned refineries. Similar to the first quarter, downtime at the Borger Refinery continued to limit volumes shipped on the Gold Line Products Pipeline.

NGL volumes on our Sand Hills and Southern Hills JV pipelines increased from the first quarter, reflecting higher throughput and a full quarter of PSXP ownership. Sand Hills volume should continue to ramp up as several new facilities begin to deliver NGLs into the system and pipeline expansions underway increase capacity. Average pipeline revenue per barrel remained unchanged from the first quarter at $0.44 while average terminal revenue increased $0.01 per barrel to $0.39. Both of these rates exclude equity affiliates.

Now I'll turn the call over to Bob Herman.

Robert Herman – Phillips 66 Partners – Senior Vice President, Operations

Thanks Tim. Turning to Slide 4, we are making good progress on our organic growth projects. The second phase of the Eagle Ford Crude Gathering System remains on track for scheduled completion in the third quarter of 2015 and the Cross Channel Connector Products System should finish shortly after, early in the fourth quarter of this year.

In April our refined products pipeline to the Hartford Terminal Dock experienced a diesel fuel release. Our response teams mobilized quickly and worked to ensure safe, timely and effective cleanup of the incident. The Hartford Terminal is back to normal operations and we are utilizing third-party dock facilities and other logistics options to meet our customer needs. As a result of the incident we are planning to install a new 8-inch and 14-inch pipeline connections at the facility and we are negotiating new contracts with minimum volume commitments that will support this investment. We expect the project to be completed during the fourth quarter, cost about $3 million and yield typical midstream returns.

The Palermo Rail Terminal is also progressing well and is on schedule to begin taking truck deliveries and loading railcars by year end. Permitting delays have affected the work on Sacagawea Pipeline which will push completion into 2016.

Through the second quarter we've had capital expenditures of $97 million, $94 million of, which is growth capital. Going forward as PSXP executes its growth plans, we expect the Partnership to take on more and larger organic projects to supplement acquisitions from Phillips 66.

Now I will turn the call over to Greg Maxwell to provide a more detailed update on the financial results for the quarter.

Greg Maxwell – Phillips 66 Partners –Vice President and Chief Financial Officer

Thanks Bob. Good afternoon everyone. Beginning on Side 5, second quarter revenues and other income were $83.8 million, up $13.7 million from the first quarter. The increase primarily reflects three months of equity earnings from the ownership interests acquired in the Sand Hills and Southern Hills NGL pipelines as well as the Explorer products pipeline.

Total costs and expenses were $41.9 million, up $7.4 million from the prior quarter, mainly driven by additional interest expense associated with the additional $1.1 billion of debt that was issued in February. We also had higher operating costs due largely to the Hartford Terminal dock incident as well as higher property taxes. G&A expenses were lower compared to last quarter.

The general partner's Board recently declared a second quarter cash distribution of $0.40 per limited partner unit which will be payable on August 12. This represents an 8% increase over the $0.37 per unit distribution last quarter.

This next slide shows our Adjusted EBITDA and distributable cash flow growth since the second quarter of last year. We continue to execute our aggressive growth plan which has resulted in an Adjusted EBITDA increase of 52% year-on-year. Over this same time period, distributable cash flow is up almost 40%. We are continuing to deliver on our plans for a five-year 30% compound annual growth rate for our unitholders.

Turning to Slide 7, Adjusted EBITDA for the second quarter was $57 million and distributable cash flow was $47.8 million. During the quarter, PSXP received minimum volume deficiency payments of $2.2 million from Phillips 66. These payments were primarily triggered at the Gold Line Products System due to downtime associated with turnaround activities at the Borger Refinery. We had maintenance capital expenditures of $1.5 million during the quarter and total cash distribution will be $41.5 million, resulting in a coverage ratio of 1.15.

Slide 8 shows our current financial position. We ended the quarter with $104 million of cash and no outstanding borrowings under our $500 million revolving credit facility. On a revolver covenant basis, our debt to EBITDA ratio at the end of the quarter was 4.2 times. Long term, we expect this ratio to decrease to our targeted level of 3.5 times as organic growth projects come online.

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

Operator

Thank you. We will now begin the question answer session. If you have a question, please press star, then the number one on your touch-tone phone. If you wish to be removed from the queue, please press the pound key. If you are using a speaker phone, you may need to pick up the handset first before pressing the numbers. Once again, if you have a question, please press star, then one on your touch-tone phone.

Our first question comes from the line of Elvira Scotto with RBC Capital Markets. Your line is open.

Elvira Scotto – RBC Capital Markets

Hi. Good afternoon. I want to start with a macro question and I know PSX addressed this earlier today but maybe you could expand a little bit here. Given the recent large M&A announcements, can you talk about third-party M&A? Specifically how PSX and PSXP think about it, and I ask because given PSXP's

cost of capital, PSXP could probably acquire anything and make it accretive. So maybe just walk through how PSX and PSXP evaluate third-party M&A and what types of assets would you consider.

Tim Taylor – Phillips 66 Partners – President

Yes, Elvira, it's Tim. I always like to frame this by saying with a $20 billion plus backlog of organic projects at PSX, there's a great backlog of organic growth to really drive a lot of value and this is an MLP that we position to be a high growth MLP. So we've got organic growth, we've got a lot of options across refining and marketing at PSX. We've got gathering and processing tie-ins with our chemicals business, so a nice integrated downstream business where logistics play a very, very important part. So there's a lot of options there to play.

That said, I think when we think about M&A, we want something that is; (a) if we did that, it would have to be fee-based, it would have to be complementary and create additional options to continue that growth and drive that growth story for PSXP, and it has to be good for PSXP unitholders as well as benefit PSX.

Elvira Scotto – RBC Capital Markets

Great that's very helpful. Then my next question is on natural gas liquids. Now given the weakness in NGL prices, can you talk about the impact, if any, that these weak prices are having on Sand Hills, Southern Hills pipelines? It sounds like volumes are good and you're still moving forward with expansion plans, but just any color there would be helpful.

Robert Herman – Phillips 66 Partners – Senior Vice President, Operations

Elvira, this is Bob. I think we've continued to see NGL volumes come to the market and appear to be growing a bit. We see continued interest from the producers to place NGLs. The price, since they are kind of a tag-along from gas drilling and other drilling, kind of in the core areas of Eagle Ford and Permian and some of those areas, NGL volume continues to appear to be increasing out there and we've seen volumes, particularly on Sand Hills, continue to grow quarter-on-quarter. So we're feeling very good about NGL supply to our NGL business.

Tom Liberti – Phillips 66 Partners – Vice President and Chief Operating Officer

Elvira, it's Tom. I'd add a little bit more color. We've actually increased capacity on the Sand Hills line from 200 to about 240 going to 250 right now and we still have plans to put a little bit more capital into the pumping capacity and connections to increase that capacity even further.

Elvira Scotto – RBC Capital Markets

Okay. Great. Thanks a lot.

Operator

Jeremy Tonet from JP Morgan is online with a question.

Jeremy Tonet – JP Morgan

Good afternoon. I was wondering as far as Bayou Bridge is concerned—congratulations there—it seems like there could be an expansion in St. James, you have that open season going there. But I'm wondering

about moving in the other direction. Is there potential to expand that pipeline further into Texas? Possibly tap into condensate or the light production from the Eagle Ford?

Tim Taylor – Phillips 66 Partners –President

Jeremy, it's Tim. I'm going to address Bayou Bridge. Today the plan is that pipe will go from Beaumont to St. James. There's a supplementary open season, expansion open season to see the size of the pipe that would go from Lake Charles on over to St. James. It really is a long pipe from the Beaumont-Nederland terminals that we have into the St. James, so I think that's a key point. So that's going to happen. There's other options that perhaps extend that system further as we assess additional shipper interest. So I wanted to make sure that we were clear on that and I think Bob, you wanted to talk about the west part of that.

Robert Herman – Phillips 66 Partners – Senior Vice President, Operations

Yes. I think if you kind of look at the crude condensate system we've been looking at and talking about for Texas and Louisiana, this fits in real nice and kind of gives us the Eastern leg of that. One of the projects we have under development now is a crude condensate pipeline and splitter system that would reach into the Eagle Ford and certainly come to Sweeny, and then if you look at it there's not much of a jump to get from Sweeny over to our Beaumont terminal and all of a sudden you've taken Eagle Ford condensate and you've put it into St. James, Louisiana. So that continues to be a focus area for us and we think that's a good development opportunity for PSX.

Jeremy Tonet – JP Morgan

Great, thanks for that. It seems like you guys have gotten a pretty good partnership with Energy Transfer family going with some of the joint ventures you've announced so far. Do you see more opportunities for kind of joint development with them?

Tim Taylor – Phillips 66 Partners –President

I just think the asset overlay that we've had has really fit that. So I think they're a good partner and we'll continue to look where we have overlap and the ability to drive value projects. We'll look at partnering with them, and of course, with other people and then we've got our own set of organic opportunities as well.

Jeremy Tonet – JP Morgan

Great, thanks. Then just one last one. If you could refresh us on the size of the EBITDA dropdown pool upstairs and how do you see the current environment impacting that? Is it getting smaller or larger or what are your thoughts there?

Tim Taylor – Phillips 66 Partners – President

Well, you know, I started today with looking at Midstream and then including refinery logistics, we start with $1 billion of EBITDA at PSX. So it's a PSX perspective. Under construction we have about $7 billion of capital projects with the Sweeny Frac, the LPG terminal, the joint ventures with Energy Transfer and Sunoco, Beaumont terminal, et cetera, and that adds—if you have seven times multiple, it would add about $1 billion of EBITDA, so you're at 2, and then we are still in the early engineering phase, an

additional $2 billion to $3 billion of capital in that 2018/2019 timeframe. That would add again another $300 million to $400 million of EBITDA. So I think we still see the 2.3 pool at PSX developing at a run rate basis at the end of '18 and we can see expansion beyond that as we continue to develop new projects.

Jeremy Tonet – JP Morgan

Great. Thanks for that. That's it for me.

Operator

Kristina Kazarian from Deutsche Bank is on the line with a question.

Kristina Kazarian – Deutsche Bank

Hey, guys. Greg—well, the other Greg—mentioned on the PSX call this morning about $2 billion of Midstream capex at the PSX level and the potential for that over the next couple of years. Can you guys talk a little bit about some of the projects that would potentially drive this magnitude of capex and what it takes to move these projects? Maybe like Sweeny Frac 2, condensate splitters, pipes, LPG expansion from the backlog into the current project queue.

Robert Herman – Phillips 66 Partners – Senior Vice President, Operations

Sure. This is Bob. I can take a shot at that. When we look at spending $2 billion to$2.5 billion of capital for Midstream over the next few years, we've still got work to do; obviously next year to finish the LPG export terminal that will be done second half of next year and start exporting LPGs. We've got really the next year and a half is kind of the heavy left for Dakota Access and ETCOP, Bayou Bridge. We just announced it last night but we are already out working to lay the first leg of that pipe so next year is a good look for that. Beaumont expansion, we've identified several projects over there that really take us out over the next four or five years of incremental expansion opportunities and income streams. Then when we look at Frac 2 for the Sweeny complex, a crude condensate line out of Eagle Ford over to Sweeny and probably a natural fit then with a condensate splitter at Sweeny, those are projects we are actively working today. As Tim just said they are in the early stages of engineering and I think we would see those coming for final investment decision sometime next year and getting right into that queue, so I would say those are active projects right now for us.

Kristina Kazarian – Deutsche Bank

Great, and then follow-up on that. Now that PSXP has the IG -rated balance sheet, how do I think about which projects are at the PSX level versus the PSXP level over the next couple of years, and what is the right run rate on PSXP capex should be?

Tom Liberti – Phillips 66 Partners – Vice President and Chief Operating Officer

Kristina, this is Tom. We look at each project individually and one is going to be the timing of the project, when the EBITDA actually comes online, the size that we have, the situation we are in as we get into a growth mode of how much capital we can handle and still keep into our debt covenants. But you saw this year we will be in the $160 million to $200 million kind of number and things, depending on how much of the Paradigm Pipeline shifts over into 2016. Those same kinds of rates now going into next year, we have

not given a capital outlook yet, but those kinds of things you can kind of count on. Again, we will look each time at each individual project and see whether it fits into PSXP for organic growth or not.

Kristina Kazarian – Deutsche Bank

Just last one on my side is I know Greg talked on the call this morning about how the vision for PSXP is to remain a fee-based entity with high growth rates, but can you guys talk about and provide a little more color on what fee-based actually means in your mind?

Tim Taylor – Phillips 66 Partners –President

I think when you think about fee-based for us it's really the throughputs deficiency underpinning the commercial side, so there's both a component of say a tariff or a fee and there is a volume piece because you've got to work both pieces of that. So we are still looking for contracts and commercial arrangements that really underpin these investments with those I would call throughput and deficiency types of agreements that give a great deal of assurance around the cash flow around the asset as you build that.

Kristina Kazarian – Deutsche Bank

So does that mean if there was an asset that we might not traditionally think of as fee-based, but PSX could do something to offset or take off the risk and structure those contracts that way, that could potentially be the PSXP qualifiable asset or a fit for the MLP?

Tim Taylor – Phillips 66 Partners –President

From an MLP perspective--from PSX perspective or PSXP perspective it would be qualified income, but as long as it met that definition, yes, you could structure something that fits that definition to then be part of an MLP-able pool.

Tom Liberti – Phillips 66 Partners – Vice President and Chief Operating Officer

If you're asking, Kristina, if there's an asset that has both fee-based and commodity risk to it could we split that between parent and PSXP, the answer is yes, we could obviously do that.

Kristina Kazarian – Deutsche Bank

Perfect. Thanks guys. Nice job today.

Operator

Michael Blum from Wells Fargo is online with a question.

Michael Blum – Wells Fargo

Thanks. My questions were already addressed.

Operator

Brian Zarahn from Barclays is online with a question.

Brian Zarahn – Barclays

Good afternoon everybody. Just following up on Bayou Bridge. I think on the parent call you gave a cost estimate and return expectations. On the return expectations, are those based on contracted capacity or just expected utilization of a mix of contracts and spot volumes?

Tim Taylor – Phillips 66 Partners –President

It's really based on what we see as contracted commitment at this point. I think there can be some upside depending on the success of the open season and of course the spot business has a component that we have not built into our thinking about the base driver.

Brian Zarahn – Barclays

In terms of the shippers, I'm assuming PSX is one of the anchor shippers?

Tim Taylor – Phillips 66 Partners – President

We don't disclose the shippers or the shipping terms at this point.

Brian Zarahn – Barclays

Okay. Then in terms of the project costs, does that include any potential storage expansions. Will you need any additional tankage at Lake Charles?

Robert Herman – Phillips 66 Partners – Senior Vice President, Operations

No, we won't need any additional storage at Lake Charles because this pipeline will run right into the Lake Charles crude system now at Clifton Ridge where we have storage to supply the refinery. It will originate barrels out of our Beaumont terminal from our standpoint and we are already currently building additional crude storage there.

Brian Zarahn – Barclays

On the leg from Lake Charles to St. James, I know you've been in discussions previously with potential shippers on that leg. It sounds like you feel fairly confident that that section of the project will move forward. I guess any commentary on any bottling issues you are seeing from shippers?

Robert Herman – Phillips 66 Partners – Senior Vice President, Operations

Yes. I think we are absolutely confident that the leg from Lake Charles to St. James is moving. The expanded open season that we announced yesterday is to really set the size of the pipe. We think there's enough interest now that we might want to upsize that pipe from the base project.

Tim Taylor – Phillips 66 Partners –President

The base is 24-inch and we are looking can we go to possibly 30-inch pipe because of the demand side on that.

Brian Zarahn – Barclays

So the cost estimate you gave around $800 million, does that include or exclude the Eastern leg?

Robert Herman – Phillips 66 Partners – Senior Vice President, Operations

It includes the Eastern leg. We give a range I think $700 million to $800 million and the range really is the difference between 24-inch and 30-inch pipe.

Brian Zarahn – Barclays

Okay, and I guess on a small item in the second quarter, the taxes is that—the increase there to about $3 million, is that property taxes and is that more of a one-time item or is that a good run rate?

Greg Maxwell – Phillips 66 Partners –Vice President and Chief Financial Officer

This is Greg. It was more or less a one-time item. Basically it's catch up accrual for about six months worth of property taxes and then the normal monthly accrual will occur as we go forward.

Brian Zarahn – Barclays

Last one for me. Any updated view on maintenance capex for the remainder of the year?

Tom Liberti – Phillips 66 Partners –Vice President and Chief Operating Officer

Yes. Maintenance cap ex will be up a little bit in the second half of the year, basically because we are down a little bit from forecast in the first half. So we should end the year right around $9 million from the 3/3.5 that we're at today. So I guess it's more like $5.5 million or $6 million in the second half of the year.

Brian Zarahn – Barclays

Thank you.

Operator

We have no further questions at this time. I will now turn the call back over to Kevin Mitchell for closing remarks.

Kevin Mitchell – Phillips 66 Partners – Vice President, Investor Relations

Thank you very much for participating in the call today. We do appreciate your interest in Phillips 66 Partners. You'll be able to find a transcript of the call posted on our website shortly and if you have any additional questions, please feel free to contact me or CW. Thanks again

Operator

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