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# Andeavor Logistics LP (ANDX)

Q4 2018 Earnings Call

## CORPORATE PARTICIPANTS

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*Analyst, UBS Securities LLC*

Tristan Richardson

*Analyst, SunTrust Robinson Humphrey, Inc.*

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Welcome to the ANDX Fourth Quarter 2018 Earnings Call. My name is Elan, 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. [Operator Instructions] Please note that this conference is now being recorded.

And I would now like to turn the call over to Kristina Kazarian. Kristina, you may begin.

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Kristina A. Kazarian

*Vice President-Investor Relations, MPLX LP*

Good afternoon, and welcome to the Andeavor Logistics' fourth quarter 2018 earnings webcast and conference call. A synchronized slide that accompanies this call can be found on [andeavorlogistic.com](http://andeavorlogistic.com) under the Investor tab.

On the call today are, Gary Heminger, Chairman and CEO of Andeavor Logistics; Don Sorensen, President of Andeavor Logistics; Greg Goff, Executive Vice Chairman of MPC; Tim Griffith, CFO of MPC; and Andy Woodward, Vice President of Finance of Andeavor Logistics; as well as other members of the management team.

We invite you to read the Safe Harbor statements and non-GAAP disclaimer on slide 2. It's a reminder that we will be making forward-looking statements during the call and during the question-and-answer session that follows. Actual results may differ materially from what we expect today. Factors that could cause actual results to differ are included there as well as in our filings with the SEC.

Now, I will turn the call over to Gary Heminger for some fourth quarter and full year highlights.

## Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

Thanks, Kristina. And thank you for joining our call this afternoon. This morning we reported fourth quarter and full year results, which included many milestones for Andeavor Logistics. Andeavor Logistics delivered EBITDA of \$333 million for the quarter, an increase of \$52 million over the prior year. Full year EBITDA of \$1.2 billion increased \$252 million over 2017.

The primary drivers of the year-over-year increase in earnings were the August Drop Down of Midstream assets, the acquisition of the SLC Core Pipeline System and execution of several organic growth projects in the Permian and then Bakken regions.

Full distributable cash flow attributable to common unitholders was \$907 million, up 36% year-over-year. This provided distribution coverage of 1.02 times for both the quarter and for full year. The company ended the year with a \$5 billion of debt which is approximate 3.8 times last 12 months pro forma EBITDA.

As we look forward into 2019, the dynamics in the Permian Basin continue to be compelling and we believe will continue to support attractive organic growth opportunities. In the Bakken, crude production continues to increase and with our line of sight on well connects across our footprint and associated gas production in the region, we continue to see opportunities for our business.

As we move into 2019, we remain focused on enhancing the financial profile of Andeavor Logistics on a standalone basis and plan to carefully manage our leverage levels and focus on meaningfully increasing our distribution coverage in the coming quarters.

Lastly, as stated [indiscernible] (00:03:11) earlier conference call, MPC is currently reviewing the various options for its two MLPs. Our comments will be limited on this, as we work through our evaluation process and we expect to provide an update to investors once this process is complete.

With that, let me turn the call over to Don Sorensen to review ANDX's operational highlights. Don?

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## Don J. Sorensen

*President, Andeavor Logistics LP*

Thanks, Gary. Slide 4 provides an overview of our three business segments. Terminalling and Transportation reported fourth quarter segment EBITDA of \$186 million, an increase of \$40 million year-over-year. Full year segment EBITDA was \$660 million, which represents a 25% increase year-over-year. Compared to the prior year, results were primarily driven by contributions from the 2018 Drop Down, which contributed \$29 million and \$48 million of segment EBITDA during the quarter and full year, respectively.

Terminalling throughput was 1.7 million barrels per day, a decrease of 2% from last year and pipeline transportation throughput was 1.1 million barrels per day, an increase of 13% year-over-year. Terminalling volumes were impacted by a turnaround at MPC's Martinez refinery, which reduced marine movements over our dock infrastructure. Pipeline transportation volumes were impacted by refinery maintenance at third-party facilities in Salt Lake City, Utah and Billings, Montana. These maintenance outages reduced supply in the region leading to lower volumes on our Northwest Products System.

During the quarter, we completed the Los Angeles Refinery Interconnect Pipeline project, which was part of the 2018 Drop Down. This project [ph] with (00:04:55) final step of MPC's Los Angeles Refinery Integration and

Compliance or LARIC project, which formally connects the Carson and Wilmington portions of MPC's Los Angeles refinery.

Moving to Gathering and Processing, segment EBITDA was \$146 million, a decrease of \$1 million from the prior year. Fourth quarter 2017 results benefited from a final minimum volume commitment payment received from one of our customers in the Bakken. Full year segment EBITDA was \$537 million, which represents a 20% year-over-year increase. The year-over-year increase was primarily driven by contributions from Permian Basin crude oil volume growth and the 2018 Drop Down, which contributed \$21 million and \$28 million of segment EBITDA during the quarter and full year respectively.

Crude oil and water gathering volumes was 522,000 barrels per day for the fourth quarter, an increase of 18% from last year, driven by year-over-year volume growth in the Permian and Bakken regions. This increase was partially offset by lower volumes from the Four Corners region on our TexNew Mex System due to frac protection where production is shut and ahead of completion activities.

During the quarter, we completed construction on our Conan Crude Oil Gathering System in the Permian. For the fourth quarter, volumes on this system were approximately 126,000 barrels per day. Volumes exited the year at 139,000 barrels per day, exceeding our expectations of approximately 125,000 barrels per day.

Switching to Natural Gas and Natural Gas Liquids, for the quarter, gas gathering and processing throughput was 716,000 MMBTUs per day, a decrease of 28% year-over-year. Please note that due to the adoption of a new revenue recognition standard, reported gas volumes were lower by approximately 193,000 MMBTUs per day, but had no impact on earnings.

On a comparable basis, volumes decreased approximately 8% from the prior quarter, driven primarily by natural production decline in the Rockies and a contract expiration, as well as temporary operational issues with the producer customer. This volume decrease was partially offset by increased volumes in the Bakken due to the recently completed Robinson Lake gas processing facility expansion, which is already operating at record levels and full capacity.

NGL sales volumes were [ph] 11,400 barrels (00:07:33) per day, flat with the prior year. Similarly, we remained in ethane recovery for a portion of the quarter. We made substantial progress on the North Dakota NGL Logistics Hub during the quarter and we've had our first rail shipment in November. We expect full operations in the second quarter 2019, as some aspects of construction moved into early 2019.

Shifting to Wholesale, segment EBITDA for the quarter – for the fourth quarter of 2018 was \$7 million, a decrease of \$1 million from the prior year. This decrease was due to weaker, unbranded wholesale pricing impacting margins with retailers in the Southwest region. Full year segment EBITDA was \$38 million, an increase of \$18 million from 2017.

With that, let me turn the call over to Andy to cover our financial highlights.

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## Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

Thanks, Don. Turning to our financial highlights on slide 5, we reported EBITDA of \$333 million and distributable cash flow attributable to common unitholders of \$243 million for the fourth quarter, a 19% and 29% increase, respectively over the same quarter last year. Total Terminalling and Transportation segment EBITDA was \$186 million, while the Gathering and Processing, and Wholesale segments contributed \$146 million and \$7 million of

EBITDA, respectively. Full year EBITDA was approximately \$1.2 billion with nearly 55% generated by the Terminalling and Transportation segment.

2018 distributable cash flow attributable to common unitholders was \$907 million, which was almost \$250 million higher than the prior year. This significant year-over-year increase was driven by Drop Downs in both the Terminalling and Transportation segment and Gathering and Processing segment and organic growth primarily in the Gathering and Processing segment.

The bridge on slide 6 shows the change in EBITDA from the fourth quarter of 2017 to the fourth quarter of 2018. EBITDA was \$52 million higher than the same period last year. The 2018 Drop Down in the third quarter of 2018 generated an increase in EBITDA of \$50 million, which contributed to both the Terminalling and Transportation, and Gathering and Processing segments. The \$16 million decrease in Gathering and Processing segment EBITDA was primarily driven by lower gas gathering and processing volumes, partially offset by a higher crude oil gathering volumes. Results also benefited from lower G&A expenses due to transaction costs as compared to the fourth quarter of 2017.

The bridge on slide 7 highlights the elements of the change in full year EBITDA versus 2017. The 2018 Drop Down generated a \$76 million increase in EBITDA for the year, which is reflected in both the Terminalling and Transportation, and Gathering and Processing segments.

Terminalling and Transportation segment EBITDA also benefited from higher volumes and earnings from the SLC Core Pipeline System acquisition and other organic growth investments such as the Stockton terminal expansion and a new pipeline connection on our Southern California Pipeline System.

Gathering and Processing segment also benefited from the growth from our Permian assets as well as the completion of the Robinson Lake gas processing facility expansion, offset by decreased gas gathering and processing volume in the Rockies. Wholesale segment EBITDA increased by \$18 million year-over-year, which was primarily driven by a full year of contribution of the business.

And slide 8 provides a summary of key financial highlights and select balance sheet information. ANDX ended the year with approximately \$1.4 billion of liquidity with approximately \$855 million available on our bank revolvers and \$500 million available on the intercompany loan with MPC that we [indiscernible] (00:11:49) during the quarter. We are committed to leverage levels at or below 4 times and end of the year with a leverage ratio of 3.8 times.

Now, let me turn the call back over to Kristina.

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**Kristina A. Kazarian**

*Vice President-Investor Relations, MPLX LP*

Thanks, Andy. As we open the call for questions, we ask that you limit yourself to one question, plus a follow-up. You may re-prompt for additional questions as time permits. With that, we'll now open the call to questions, Elan?

## QUESTION AND ANSWER SECTION

**Operator:** Thank you. [Operator Instructions] Our first question for today is Jeremy Tonet from JPMorgan.

Jeremy Bryan Tonet

*Analyst, JPMorgan Securities LLC*

Q

Hi. Good afternoon. Just want to dial back to when ANDX acquired QEP Field Services and there were a certain kind of contractual commitments or backstops that the parent provided at that point in time. And I was wondering if those contracts had started to lapse about now? And if they were kind of recurring on the same terms or different terms, or if there's any other contracts between ANDV and ANDX had and if those are continuing in the same fashion as they expire?

Gregory James Goff

*Executive Vice Chairman-Marathon Petroleum Corporation, Andeavor Logistics LP*

A

Jeremy. This is Greg Goff. When the QEP business was acquired, at the time Andeavor acquired the gas liquids from the Midstream business to take the commodity risk out of the business and those gas liquids were acquired at a certain level that was set in place for a five-year term that could be renewed each year through a negotiation process between the two companies, because Andeavor takes some of those liquids and puts it into its refining system. That was the only agreement.

Jeremy Bryan Tonet

*Analyst, JPMorgan Securities LLC*

Q

Okay. Thanks. Thanks for that. And then, I was just wondering, in the press release, you guys talk about meaningfully increasing the distribution coverage in the coming quarters. And coming quarters seems to indicate kind of a near-term event there and it seems like the past to achieving that are either reducing the distribution or a combination. Am I thinking about that the same way, or is there something else to read into kind of what you were saying here?

Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Well, you can increase revenue, lower expense, slow down CapEx if necessary. We can do all of the above, or combinations of the above.

Jeremy Bryan Tonet

*Analyst, JPMorgan Securities LLC*

Q

Okay.

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

Yeah. And this is Andy. I mean, we have a plan in place with where the current distribution is today to meaningfully increase distribution quarter-after-quarter. So, we feel, with our model that we laid out and plan that we laid out during the 2018 Analyst Day that we are on path to meaningfully higher distribution or coverage.

Jeremy Bryan Tonet

*Analyst, JPMorgan Securities LLC*

Q

Got you. I guess, when I saw meaningfully, I thought it was like towards MPLX levels, which seem to – like it would be an extended path unless you took one of those two options. So, maybe I was kind of reading that the wrong way then.

Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Yeah. I think you were overreading that, Jeremy. We plan to meaningfully over time, but it's not immediate. And Andy is right, we have a plan. One of the things is that when investments are made and then you start filling those investments up by underutilized space in those assets that just drops straight to the bottom line.

Jeremy Bryan Tonet

*Analyst, JPMorgan Securities LLC*

Q

Great. Thanks. I'll stop there. Thank you.

Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Okay.

**Operator:** Thank you. Our next question is from Theresa Chen from Barclays.

Theresa Chen

*Analyst, Barclays Capital, Inc.*

Q

Hi. Thank you for taking my questions. I'd like to follow-up on something that Jeremy asked and maybe take a different cut at it. So, specific to those keep-whole contracts that were swapped for fee upon the QEPFS acquisition within Gathering and Processing, I believe they end at the end of this year, that's the termination of the five-year period. And when we look at that 2020 EBITDA guidance of \$1.6 billion for the whole company, can you just help us quantify how much of that consists of the keep-whole contract that was swapped for fee that I'm assuming has been rolled over into that guidance?

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

Yeah. This is Andy. So, if you look at when that contract was first struck back with the QEP back in 2015, the NGL spread was right around \$5.50 at that point in time. So certainly, over the last – right after that, over the last couple of years, that spread was closer to the \$3 range. And so, where we are today and what we forecasted going forward is back in that sort of \$4.50 to \$5.50 range. So, we assumed in our 2020 guidance that that contract would remain in place. But even if it didn't, we don't think that the impact would be that material in this price environment.

Theresa Chen

*Analyst, Barclays Capital, Inc.*

Q

Got it. And shifting gears to your organic projects. Can you help us quantify how much further ramp you expect on the Conan Gathering asset and any update related to the non-Canon Permian Gathering projects?



Don J. Sorensen

*President, Andeavor Logistics LP*

A

Yeah, Theresa, this is Don Sorensen. So, relative to where we at on Conan, when we talk about having put it in service, it's really kind of the core base system with our anchor customer. We are continuing to work with that customer to add additional gathering and Central Tank Battery connections. That customer is also continuing to drill out some of those pads and add additional well flows in through existing systems we've connected. As we look forward to the year, we are seeing continued growth not only with our anchor customer, but with several customers around that.

Relative to that Conan area itself, we look at from where we're at in fourth quarter of 2018 to first quarter of 2019, we expect to see those volumes grow by about 20%. And then throughout the year, we'll continue to add additional volumes from new customers.

Theresa Chen

*Analyst, Barclays Capital, Inc.*

Q

Thank you.

**Operator:** Thank you. Our next question is from Shneur Gershuni from UBS.

Shneur Z. Gershuni

*Analyst, UBS Securities LLC*

Q

Long time no speak, guys. Just a couple of follow-up questions to some of the questions that were just asked and maybe to approach it in a different way. Can you quantify for us what the actual support was for the QEP assets in 2018?

Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Yeah. So, the support around the QEP assets was exactly what Greg had said before. It's taking the commodity exposure around the keep-whole arrangements and having that at legacy Andeavor now Marathon and keeping – and then translating that volume into a fixed fee contract for ANDX, which is much more appropriate for an MLP structure.

Shneur Z. Gershuni

*Analyst, UBS Securities LLC*

Q

I'm just looking for the dollar amount, like what would be – like if there was no support what would be the difference to ANDX's EBITDA?

Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Are you looking for today or...?

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

No, for 2018, it was probably close to zero.



Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Yeah. I would say, very close to zero.

Shneur Z. Gershuni

*Analyst, UBS Securities LLC*

Q

So, zero support. Okay. Got it.

Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Well, it's not support, it's a purchase agreement to acquire the liquids and at a set price that was negotiated when the assets were acquired. And because of the frac spread, it was close to that differential – last year, it was basically almost zero.

Shneur Z. Gershuni

*Analyst, UBS Securities LLC*

Q

Okay. So, almost zero [indiscernible] (00:19:49), got it. Okay. And if I remember correctly with the agreement, it was for five years and there was a one year auto renewal, so I can assume that's still in place for next year?

Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

A

Yeah. Yes it is.

Shneur Z. Gershuni

*Analyst, UBS Securities LLC*

Q

Okay. Got it. And then finally, you have said in your response to Jeremy's question about having a plan to meaningfully improve the coverage ratio, do you mind sharing the details of that plan or the targets?

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

Really, the plan that we shared during the Analyst Day is the guidance we're providing today. I will say, to get there at a flat distribution, you're going to, quarter-after-quarter, have meaningfully higher coverage.

Shneur Z. Gershuni

*Analyst, UBS Securities LLC*

Q

Okay. So, the way we should think about it is that the coverage ratio that's implied by your guidance is what you mean by meaningfully improving coverage, correct?

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

Correct.

Shneur Z. Gershuni

*Analyst, UBS Securities LLC*

Q

Perfect. Thank you very much, guys. Really appreciate the color.

**Operator:** Thank you. And our final question today is from Tristan Richardson from SunTrust.

Tristan Richardson

*Analyst, SunTrust Robinson Humphrey, Inc.*

Q

Hey, good morning, guys. Just wanted to ask, Andy, just talking about your plan to grow. You talked about sort of the organic backlog of projects and spend in 2019 and in 2020. Can you talk about sort of the components of that, the major projects within that, sort of where those opportunities are over the next couple of years?

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

Yeah. So, getting to 2020, certainly, the NGL Hub for this year is going to be a major contributor to our EBITDA growth. Now, as Don pointed out in his prepared remarks, we're expecting – we're already generating EBITDA from it. But we expect full EBITDA sometime in 2Q. So, that's going to be a major driver going into for 2019.

Robinson Lake expansion, which includes not only expanding the facility, but a lot of the gathering that's around that area. It's core of the core in the Bakken with most of our rig count. And so, that's going to be a major growth area for us in 2019. Outside of that, in the Bakken and the Rockies, it's going to be primarily well connects in both areas versus where they were back in 2017. Our up rig count and the producers are drilling much more. So, we expect some good growth in those areas, just from a well connect standpoint.

And then on the Permian side, and as we provided remarks previously on, for Conan, we're still expecting about \$50 million of capital to be spent on that project at very attractive returns. We've built most of the facilities, so we're talking returns much more attractive than the full project itself and this is Central Tank Batteries that we're continuing to connect for producers in that area. And then on the Terminalling and Transportation side, not a lot going on in 2019 related to that, but we are in the process of working on the Carson crude terminal expansion, which would generate EBITDA for us closer to 2020.

Tristan Richardson

*Analyst, SunTrust Robinson Humphrey, Inc.*

Q

So, just to clarify that the \$600 million in 2019 and in 2020 is largely GMP-oriented projects and a lot of it is Robinson-like, is that fair?

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

I would actually call it more a third Terminalling and Transportation, a third Permian and a third Bakken. Slightly more in the Permian, because that's where a lot of the growth is today, but those are probably good rough numbers to use.

Tristan Richardson

*Analyst, SunTrust Robinson Humphrey, Inc.*

Q

Helpful. Thank you, guys, very much.

Andrew Woodward

*Vice President-Finance, Andeavor Logistics LP*

A

Thank you.

## Gary R. Heminger

*Chairman and Chief Executive Officer, Andeavor Logistics LP*

Great. And with that, I think that was our last question. So, thank you for joining us today and thank you for your interest in Andeavor Logistics. Should you have additional questions or would you like clarification on any of the topics we discussed this afternoon, we'll be available to take your calls. Elan, I'll turn it back to you.

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**Operator:** Thank you. And this does conclude today's conference. You may disconnect at this time.

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