Par Pacific Holdings, Inc.

Third Quarter 2023 Earnings Conference Call

Tuesday, November 7, 2023, 10:00 AM

CORPORATE PARTICIPANTS

Ashimi Patel – *Director, Investor Relations*

William Pate – *Chief Executive Officer*

Will Monteleone – *President*

Shawn Flores – *SVP and Chief Financial Officer*

Richard Creamer – *EVP, Refining and Logistics*

CONFERENCE CALL PARTICIPANTS

Ryan M. Todd - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Matthew Robert Lovseth Blair - *Tudor, Pickering, Holt & Co. Securities, LLC, Research Division - Managing Director of Refiners, Chemicals & Renewable Fuels Research*

Neil Singhvi Mehta - *Goldman Sachs Group, Inc., Research Division - VP and Integrated Oil & Refining Analyst*

Jason Daniel Gabelman - *TD Cowen, Research Division - Director & Analyst*

John Macalister Royall - *JPMorgan Chase & Co, Research Division - Analyst*

Manav Gupta - *UBS Investment Bank, Research Division – Analyst*

PRESENTATION

Operator
Good morning, and welcome to the Par Pacific Third Quarter 2023 Earnings Conference Call.

All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the “*” key, followed by “0”.
After today’s presentation, there will be an opportunity to ask questions. To ask a question, you may press “*’, then “1” on a touchtone phone. And if you need to withdraw your question, please press “*”, then “2”.

Please note, this event is being recorded.

And now I would like to turn the conference over to Ashimi Patel, Director of Investor Relations. Please go ahead.

Ashimi Patel
Thank you, Marlise. Welcome to Par Pacific's third quarter earnings conference call. Joining me today are William Pate, Chief Executive Officer; Will Monteleone, President; Shawn Flores, SVP and Chief Financial Officer; and Richard Creamer, EVP of Refining and Logistics.

Before we begin, note that our comments today may include forward-looking statements. Any forward-looking statements are subject to change and are not guarantees of future performance or events. They are subject to risks and uncertainties, and actual results may differ materially from these forward-looking statements.

Accordingly, investors should not place undue reliance on forward-looking statements, and we disclaim any obligation to update or revise them. I refer you to our investor presentation on our website and to our filings with the SEC for non-GAAP reconciliations and additional information.

I'll now turn the call over to our Chief Executive Officer, William Pate.

William Pate
Thank you, Ashimi. We're pleased to share outstanding third quarter results with you this morning. Key highlights include record earnings, an improved capital structure and achievement of our principal Billings integration objectives. We recorded record quarterly adjusted EBITDA of $256 million. The accretive impact of Billings was illustrated by our third quarter adjusted net income of $3.15 per share, 10% above the comparable result in 2022.

This was our first full quarter of ownership of the Billings refining and logistics system, which contributed quarterly adjusted EBITDA of more than $85 million. As previously noted, our principal acquisition objective is to increase annual throughput through consistent, reliable operations. In this regard, we exceeded our acquisition target of 50,000 barrels per day with quarterly throughput above 55,000 barrels per day. We are also well ahead of our acquisition synergies target, due to commercial activities and corporate overhead reductions.

Our other refining and logistics units recorded strong profits due to solid operational execution and favorable market conditions. Despite the pressures of rising wholesale prices on street margins, our retail system continued to post excellent same-store sales growth and strong profitability. Across the board, our team continues to exhibit near flawless operational and commercial execution.

With the strong earnings, we also improved our capital structure. During the quarter, we were able to build liquidity, reduce debt and refinance one of our intermediation facilities, while also repurchasing $27 million of our common stock. We have also retired all prior year RIN obligations. At this point, we have a strong balance sheet with limited financial obligations, other than investing in our base assets and pursuing our strategic growth initiatives.

On the growth front, we are focused on low-cost, high-return renewables projects. In Tacoma, we successfully tested our co-feeding operation, and we're also moving forward with the engineering of our green hydrogen and SAF units. In Hawaii, we remain on schedule with our renewable fuels project. Overall, we continue to invest and expand in this critical sector, aligning with our long-term sustainability goals.

As we enter the winter, distillate cracks continue to be strong across our markets and gasoline cracks have declined with the conclusion of the summer driving season. While our Rockies markets remain well above Gulf Coast cracks, Billings and Wyoming have strong seasonality profiles due to the winter decline in Upper Rockies demand. However, the strong distillate orientation of our Hawaii operations will continue to reduce our sensitivity to winter seasonality, and it leaves us well positioned for the winter quarters.

I'll now turn the call over to Will to provide a detailed analysis of our commercial and operational performance.

William Monteleone
Thank you, Bill. The Refining and Logistics business units delivered strong asset reliability during peak season, driving a record quarterly financial contribution. Total throughput was 198,000 barrels per day, which included a full quarter contribution from Billings of 55,000 barrels per day.

In Hawaii, third quarter throughput was 82,000 barrels per day, and production costs were $4.50 per barrel. The quarterly Singapore Index averaged $23.39 per barrel, and our landed crude differential was $5.50 per barrel, consistent with our guidance. We expect our fourth quarter Hawaii crude differential to average between $6 and $6.50 per barrel. Third quarter capture to the combined index was approximately 75%, reflecting unfavorable price lag, crack spread hedging and previously mentioned reformer maintenance.

In Washington, third quarter throughput was 41,000 barrels per day and production costs were $3.77 per barrel. The PNW Index averaged $35 per barrel during the quarter. Capture improved to 35%, reflecting a reversion to the typical capture range despite rising prices impacting asphalt netbacks.

The Wyoming team set a quarterly throughput record of 19,500 barrels per day, driving production costs to $6.46, per barrel. The quarterly U.S. Gulf Coast index was $29.65 per barrel and Wyoming capture was approximately 125%. The adjusted gross margin result includes a favorable FIFO impact of $13 million and strong seasonal Rockies market conditions versus the Gulf Coast.

Montana throughput was 55,000 barrels per day and production costs totaled $10.83 per barrel, which was elevated by approximately $1.25 per barrel due to coker maintenance. Capture to our Gulf Coast index was 89%, slightly below what we would expect in the seasonally strong third quarter, due to reduced asphalt and secondary product netbacks in a rising price environment.

Four months into our ownership of the Billings system, we're as excited as we were on day one. We're pleased with the operations and commercial execution. The resourcefulness, creativity and dedication of the operations and commercial teams have been excellent. Total synergies are exceeding initial expectations, and we remain focused on improving plant reliability.

As you can see from the team's strong operational results, the plant is more than capable of running above 50,000 barrels per day. Our objective is running consistently above 60,000 barrels per day. Looking forward, we are laying the groundwork for delivering consistent reliability. When we made the Billings acquisition, we guided to amortized turnaround expenditures of approximately $20 million per year. Given a 5 to 6-year turnaround cycle, this implies approximately $120 million over the course of a cycle. During 2024 and 2025, we expect to turn around all major units, broken down roughly between the two years. During the 2024 turnaround, we will also be making $25 million of capital investments to improve reliability. Based on modest improvements in reliability, these investments should result in a 1 to 2-year payback in mid-cycle market conditions.

The Retail segment generated a strong financial quarter with growing fuel volumes and expanding merchandise revenues. Third quarter same-store sales fuel volumes and merchandise revenue grew 9% and 7%, respectively, versus 2022 levels. We also recently opened our first new to industry site in the Spokane market, and initial results are promising. In addition, we have one new site coming online during the fourth quarter in Hawaii.

For the fourth quarter, we expect Hawaii to run between 83,000 and 88,000 barrels per day, Montana between 47,000 and 50,000 barrels per day, Washington between 38,000 and 40,000 barrels per day and Wyoming between 16,000 and 18,000 barrels per day. As we look across our capital project portfolio, we see many high-return projects that will allow us to consistently deliver annual throughput of 200,000 barrels per day or more.

In addition, we are progressing our renewables initiatives. The Hawaii project remains at the forefront, and we expect the renewable fuels unit to come online in 2025. The majority of long-lead equipment items have been ordered and returns continue to look robust on the project given the attractive low capital conversion costs of less than $1.50 per gallon of capacity.

I'll now turn it over to Shawn to review our financial results.

Shawn Flores
Thank you, Will. Third quarter adjusted EBITDA and adjusted earnings were $256 million and $194 million, or $3.15 per share.

The refining segment reported record quarterly adjusted EBITDA of $234 million in the third quarter, compared to $129 million in the second quarter. Our third quarter refining results included unfavorable price lag impact of $22 million and a product crack hedge loss of $26 million in Hawaii, partially offset by a $13 million FIFO benefit in Wyoming. We have continued our crack hedging framework in Hawaii with approximately 25% of our fourth quarter sales hedged at $22 per barrel premium to Brent.

Our Logistics segment reported adjusted EBITDA of $29 million in the third quarter, compared to $26 million in the second quarter. The sequential improvement was driven by increased throughput across our system and a full quarter contribution from the Montana business.

The Retail segment reported adjusted EBITDA of $17 million in the third quarter, compared to $18 million in the second quarter. Despite rising wholesale prices, our stores generated strong profitability on growing fuel volumes and merchandise revenue.

Cash provided by operations in the third quarter totaled $269 million. Net changes in working capital resulted in a cash inflow of $70 million, most of which we expect to reverse during the fourth quarter. Cash outflows from investing activities totaled $6 million, including capital expenditures of $23 million and an inflow of $13 million related to the final working capital settlement for Par Montana. Strong free cash flow during the quarter drove record ending liquidity of $778 million.

With gross term debt at the midpoint of our stated target of $500 million to $600 million, we are focused on streamlining and reducing our cost of working capital. During the quarter, we closed a $120 million letter of credit facility that will support our Hawaii refinery. We expect the LC facility to reduce our crude funding costs by approximately $3 million per year, or $0.10 per barrel.

In early October, we terminated the intermediation agreement at our Washington refinery and increased our ABL capacity from $600 million to $900 million. With the Washington working capital folded into the ABL, we expect to reduce annual funding costs by approximately $6 million, or $0.40 per barrel. Our expanded ABL facility now supports all three mainland refineries and our retail business.

Through the end of October, we have repurchased $37 million, or 1.1 million shares, at an average price of $33.44. As we head into the new year, our balance sheet is well positioned to achieve our strategic growth objectives, while opportunistically repurchasing our common stock at attractive prices.

This concludes our prepared remarks. Operator, we'll turn it back to you for Q&A.

QUESTION AND ANSWER

Operator
Thank you very much. We will now begin the question-and-answer session. To ask a question, you may touch “*”, then “1” on your touchtone phone. If you are using a speaker phone, please pick up your handset before pressing the keys. If at any time your question has been asked and you would like to withdraw your question, please press “*”, then “2”.

At this time, we will pause, momentarily, to assemble our roster. Our first question comes from Ryan Todd from Piper Sandler. Ryan, please go ahead.

Ryan Todd
Great, thanks. Maybe starting out, I mean, margin capture was solid, and the numbers are good in the third quarter. Can you talk about some of the moving pieces as we think about, as we look at the fourth quarter? WCS differentials have widened out quite a bit. You've got a reformer back up and running. Secondary product trends, particularly in asphalt. So, how should we think about directional trends in margin capture as we look into the fourth quarter?

Shawn Flores
Yeah, thanks, this is Shawn. I'll hit each region separately.

I think starting in Hawaii, we would reiterate our guidance of 100% capture over the medium to long term. As you noted, we booked a pretty sizable headwind on price lag and crack hedging in the third quarter. And then we also had the reformer activity. I think when you back all of that out of the Q3 capture, it would imply about 120% gross margin capture in the third quarter. So, we still feel very good about our 100% guidance in Hawaii, given the moving pieces there.

For Tacoma, we've guided towards a mid-40% capture. Obviously, the WCS widening out will be a boost in the quarter. And I would also point to the sort of headwinds that we're continuing to see on the secondary product market, namely asphalt.

In Wyoming and Montana, I think Bill and Will both mentioned the seasonality of both of those businesses. It's not unusual to see capture in the 60% to 70% range in Q1 and Q4. Although I will say, the Upper Rocky market really Spokane, Billings, Missoula, have fared quite well, quarter-to-date. So, I suspect the Montana capture will hold in a bit better than Wyoming.

Ryan Todd
Okay. That was really helpful. And then maybe on free cash flow, I mean generation was strong in the quarter, supporting both debt reduction and share buybacks. As we look forward, can you talk about how you think about priorities for the use of cash going forward? Is there more debt reduction that we should anticipate? And then how do you look at balancing shareholder returns and growth capital, going forward?

William Pate
Hey, Ryan, this is Bill. Certainly, as I mentioned in my prepared comments, we have a balance sheet at this point where we've got a lot of flexibility. We really have minimal obligations with respect to financial needs. So, the question really is, how do we want to invest in growth? And when we think about share repurchases, we really look at that as another opportunity to invest, and it's an opportunity to invest in our own company.

And so, I think what you'll see is if the market is weaker, you're probably going to see us investing--repurchasing more equity, over time. And as the market strengthens, you'll probably see less of that. And then we will continue to pursue our strategic growth initiatives. And that's everything from some of the retail locations that Will mentioned that are proving to be quite successful, to investing in our refineries to improve reliability.

We continue to be in markets that are short product. And so, improvements in reliability translate directly into profitability for us, at this point. And obviously, we'll be looking at strategic opportunities to the extent that they are apparent and available within our existing markets.

Ryan Todd
Perfect. Thanks, Bill.

Operator
And our next question comes from Matthew Blair from TPH. Matthew, you may proceed.

Matthew Blair
Thank you. Congrats on the strong operations in Montana. Could you talk about what you're doing, today, to run at 55,000 barrels per day versus the original target of 50,000. And then moving up to the 60,000 mark, could you give any sort of examples of projects they'll be implementing or things that will be changing in order to raise production further?

William Monteleone
Sure, Matthew. This is Will. So, I think as we've demonstrated, I think you saw the June results where we were above 60. And you can see for the quarter, we averaged 55. And so, I think the story in Montana really is not about mechanical availability, right? We can--we've demonstrated we can run the plant in the 60s; it's really about doing it reliably and through the season.

So again, our focus is not so much on expanding the capabilities at the facility but focusing on identification of areas that have been reliability challenges in the past where you've experienced unplanned outages.

And so--this could be everything from really improving, I'll just call it the design of certain pieces of pumps and compressors, to metaling up certain units that we think will reduce corrosion risks. So again, a lot of this comes down to not necessarily reengineering the plant so you get more throughput, but really making sure we just experience fewer unplanned events.

Matthew Blair
Sounds good. And then on the retail side, that same-store volume number of up 8.6% year-over-year was pretty eye-popping. Could you talk about what's driving those gains?

William Monteleone
Sure, Matthew, it's Will, again. So, I think it's really two factors I'd point to. I think in Hawaii, you're still seeing us lapping some softer comparable periods in the 2022 time frame, where Hawaii at least was still somewhat impacted by COVID. So, it was a little bit slower to come out than the Mainland. So again, I think you're seeing some benefit on the macro side there for Hawaii. That's a bit idiosyncratic to that market.

And then I think secondarily, on the Mainland, we have rebranded all of our stations in the Pacific Northwest region. And I think we we're seeing a nice response and I think are growing an attractive brand in that region. So, I think both markets are growing nicely, and I think those are the two major factors driving the attractive and consistent same-store sales growth that we've been delivering.

Matthew Blair
Great, thanks for your comments.

Operator
We have a question from John Royall from JPMorgan. John, go ahead.

John Royall
Hi, good morning. Thanks for taking my question. So, I was hoping for your view on refining in China. We've been reading there have potentially been some run cuts there. And I know there are limits on crude imports, right now. Do you expect that to tighten up the supply market in Asia? And just any thoughts on your outlook for the product market in Asia would be helpful.

William Pate
Hey, John, this is Bill. Certainly, the run cuts in China, which I think are related to crude imports, is related to export quotas but, ultimately, just related to how the economy is managed. And what you've seen there is consistent with some of the conversions. I think you've had a number of larger new refineries come online in the last three to four years. They're all really integrated into the petrochemical chain.

And then at the same time, you've seen closure of lending facilities in teapot, simpler refineries. And as a result, there's been a balanced production change with respect to transportation fuels and a fairly significant increase in terms of feedstocks for the petrochemical chain.

And I think what we're seeing, today, is the government managing their refining complex to supply their local market. While their economy is weak, I think a lot of it is related to global demand, and the reopening of the economy for the local consumers actually resulted in probably more demand for transportation fuel.

So, we've seen, I think through the year, fairly consistent exports and then a recent tightening, but I don't know that there's any major changes. They tend to be not as active in the Singapore market as they were a couple of years ago. I mean a lot of the teapots have really withdrawn in terms of their export capabilities.

And so, you're really left with Chinese national companies that are managing the exports of any excess product in the Chinese market out into the international market. And that all results in just a more balanced and a kind of a more rational entry into the market of any excess production they may have.

John Royall
Great. Really thorough and helpful. Thank you. And then apologies if this one is maybe more housekeeping, but just on interest expense, there are a couple of moving pieces there. You talked about $6 million in savings annually from essentially moving the intermediation agreement into your ABL, but you did have an increase in 3Q, which is obviously related to the Billings acquisition.

So, is that $21 million quarterly run rate minus, I guess, $1.5 million for the intermediation, is that the right way to think about the quarterly run rate, going forward?

Shawn Flores
Hey, John, it's Shawn. I think the quarterly run rate going forward as we get into early next year will be closer to the $15 million to $16 million per quarter level. The $6 million of funding savings from flipping from an intermediation to an ABL is really split between interest savings and a reduction in cost of sales, just due to the elimination of the intermediation fee. But as we guide towards interest expense for next year, it will likely hold around $15 million.

John Royall
Great, thanks very much.

Operator
Our next question comes from Neil Mehta from Goldman Sachs. Neil, please go ahead.

Neil Mehta
Thank you so much. Bill, you've done a great job around M&A, particularly around the Billings transaction where you timed that very well. I'm just curious what your thoughts are around the market, right now. Are there other opportunities for opportunistic bolt-on, or a better opportunity when refining margins are below mid-cycle?

William Pate
I think the latter is definitely the case. Frankly, with the market as strong as it is right now, every refinery is profitable. And I think it's really challenging for parties who might think a refinery is

nonstrategic to think about parting with that asset. The other thing is our footprint is just bigger. And I think we've been very clear about where we want to operate and where we don't want to operate.

I don't think we would be very competitive on the East Coast or the Gulf Coast or even the Mid-Con. We want to be supplying transportation fuels in the upper Rockies, in the Pacific, in PADD IV and PADD 5. And so, it's harder for us to get transactions done going forward. But certainly, the market environment is not very receptive to that.

And as I was noting earlier, if you think about most of our strategic growth objectives, and I should have included renewables, by the way, which is a very significant part of how we think about our growth. They're really all organic. It's putting capital to work in and around our existing asset base and investing in our plant and our people.

Neil Mehta
Yeah, that makes a lot of sense. So, a big picture question in the last five years, the stock has done very well. You kind of repaired the balance sheet, you scaled the business. and now are a very competitive refining footprint. Talk about how you're setting up the business for the next five years. What does Phase 2 of this company's development look like?

William Pate
Well, it's exactly what I just said. I think we have the footprint. We have the assets and the people, and we're going to invest in and around that footprint. So, it's things like the Tacoma project or it's the conversion of the hydrotreater in Hawaii to start to producing renewable fuels in Hawaii. It's bolting up our retail business. As Will mentioned, our Northwest retail business is ramping very nicely and growing, well. And it's building on what we have.

I mean, I think there's also logistics opportunities, but within our asset base, there are plenty of opportunities to put capital to work. And then more broadly, the best opportunity to put capital to work may be simply repurchasing our stock.

Neil Mehta
Okay, great. Thanks, Bill, appreciate it.

Operator
We have a question now from Jason Gabelman from TD Cowen. Jason, please go ahead.

Jason Gabelman
Hey, good morning. Thanks for taking my questions. I wanted to first ask a couple of specific financial questions on the quarter. You mentioned that you paid down your entire RIN liability. Was there any cash that came out of the system in 4Q related to that, and if so, how much? And then also, was there any lost profit opportunity in Montana from the coker outage? I know you had mentioned OpEx impact. So, I'm wondering if there's anything on the margin side. And I have a follow-up. Thanks.

Shawn Flores
Hey, Jason, it's Shawn. I can cover both of those. On your second question on the LPO and margin for the coker outage, there was an impact of roughly $10 million to $15 million. And so, I think when you pull that out, it would imply capture in the high 90% range.

And on the settlement of all of the prior year RIN obligations, we did tackle some of this in the fourth quarter, and that really sort of is why I referenced the reversal of the working capital inflow of $70 million during the fourth quarter.

Jason Gabelman
Got it. Understood. And then my follow-up is just on the outlook for the West Coast market with another refinery expected to close early next year. Can you talk about your ability to sell more products into that market, both from Hawaii and Tacoma and, potentially, take advantage of what could be more margin volatility of the upside, particularly in the summer?

William Monteleone
Sure, Jason, it's Will. So, I think just broadly, I think West Coast markets really function together between the Pacific Northwest and down into California. There's clearly some spec differences, but there are a fair amount of points of integration there across the systems that each of the major players operate.

So, I think just tangentially, I think we're going to participate in the changes in supply and demand that are occurring on the West Coast as you think about potential refinery closures. And so, I think that's probably the best way to think about it versus our specific ability to manufacture, say, CARB spec gasoline or something like that.

That said, we do operate marine equipment and do pretty consistently participate and play in the physical markets in both California, Portland and the Pacific Northwest broadly and through Hawaii and also Tacoma. I think we'll continue to actively participate as that market changes.

Jason Gabelman
Okay, understood. Thanks.

Operator
Now let me remind you, if you would like to get into the question queue, please press “*”, “1”. And now we have a question from Manav Gupta.

Manav Gupta
I just specifically wanted to ask you about--you mentioned earlier that the gasoline demand is acting very seasonally. And I was just wondering if that's how you feel or have you seen anything which could be a structural issue for gasoline going ahead? In the various regions that you operate, do you believe that as we clear these winter months, the demand would act in a seasonal way and rebound from current levels?

William Monteleone
Manav, it's Will. I would say we haven't seen anything structural. The seasonal trends that we're observing are consistent with our experience operating in the Upper Rockies. So again, we've been actively participating in that market through our Wyoming refinery for the better part of the last seven or eight years.

And so, I think it's not unusual to see a tapering in demand, as you see, really tourism and just overall activity start to taper off and also weather, again, becomes a little softer. I would say on the flip side of that, we're seeing positive trends on the diesel demand side, particularly as you're in October and November time frame where you're in the harvest cycle. So overall, I think demand in each of our markets is strong, structurally, and the seasonality is nothing new.

Manav Gupta
Okay. And my quick follow-up here is, can you tell us a little more about the green hydrogen project stuff that you're doing?

William Monteleone
Sure, Manav. This is Will. So, we're looking at developing a facility that would be co-located with our Tacoma refinery where we would pair a green hydrogen production facility with a sustainable aviation fuel plant. And again, I think we would co-locate it so that we could share and utilize the logistics assets that we have on site there that we think are particularly strategic.

So again, I think our view is we've got some attractive ingredients here for a project that should be successful in a market that's focused on decarbonizing with strong credit incentive schemes, strong logistics assets to access feedstock and some of the lowest cost power in North America.

So again, that's why we're spending time on this. And ultimately, I think we've got a particularly competitive project here that is worth getting smarter on and getting the engineering in a place where we can make a decision.

Manav Gupta
Thank you so much.

CONCLUSION

Operator
Thank you very much. And this concludes our question-and-answer session. I would like to turn the conference back over to William Pate for any closing remarks.

William Pate
Thank you, Marlise. We're very pleased with the accretive financial contribution of the Billings acquisition, as well as the impressive performance of all our business units. The trailing 12-month adjusted net income of $9.34 a share signifies the value that we've created for our shareholders, and I want to thank you for your support today. Have a good day.

Operator
The conference has now concluded. Thank you very much for attending today's presentation. You may now disconnect.