Par Pacific Holdings' (PARR) Q1 2016 Earnings Call Transcript

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Par Pacific Holdings, Inc. (NYSEMKT:PARR)
Q1 2016 Earnings Conference Call
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Executives
Christine Thorp - Director of Investor Relations
William Pate - President and Chief Executive Officer
William Monteleone - Senior Vice President of Mergers & Acquisitions
Christopher M. Micklas - Chief Financial Officer
Joseph Israel - President and Chief Executive Officer of Par Petroleum, LLC

Analysts
Scott Levine - Imperial Capital
Thomas Mitchell - Miller Tabak
Andrew Shapiro - Lawndale Capital Management

Operator

Greetings and welcome to the Par Pacific Holdings First Quarter Earnings Conference Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host Christine Thorp, Director of Investor Relations and Public Affairs for Par Pacific Holdings. Thank you Ms. Thorp, you may begin.

Christine Thorp

Welcome, everyone, to Par Pacific Holdings' first quarter 2016 earnings conference call. With me today is William Pate, President and Chief Executive Officer, Chris Micklas, Chief Financial Officer, Joseph Israel, President and Chief Executive Officer of Par Petroleum and Will Monteleone, Senior Vice-President of Mergers and Acquisitions.

This call is also being webcast and can be accessed through the audio link under the investor relations section of our website. Information recorded on this call, speaks only as of today May 5, 2016.

Before we continue I would like to remind you that this call contain forward-looking statements made pursuant to applicable Security Laws including statement of, expectations, future events, or future financial performance. Forward-looking statements involve inherent risks and uncertainties, and we caution investors that a number of factors could cause actual results to differ materially from those contained in any such forward-looking statements.

These factors and other risks and uncertainties, are described in detail in the company's most recent quarterly report on Form 10-Q, annual report on Form 10-K and in the company's other filings with the Securities and Exchange Commission. Par Pacific assumes no obligation to publically update or revise any forward-looking statements.

I would now like to turn the conference call over to Bill for his opening remarks.

William Pate

Thank you Christine. And thank you for joining us this morning. I'm pleased to report positive EBITDA for the first quarter of 2016 despite a very difficult market with declining crack spreads. Distillate crack spreads in the first quarter 2016 were the lowest in more than five-years. We also incurred some one-time expenses and losses associated with the downsizing of our Texadian operations and Chris will go into these items and our financials in more detail later.

In Hawaii, we continue to have solid execution at all of our business units. Our retail and logistics operations are doing quite well, and we are very pleased with their financial contribution. The refinery performed well in spite of the declining crack spreads and the typical inefficiencies of units that are operating with catalysts near the end of their useful life. We look forward to having a fresh refinery in August after our turnaround. Joseph will go into operations in Hawaii in a second.

On the strategic front, we increased our investment in Laramie Energy to support their first quarter acquisition of largely contiguous acreage with significant natural gas production and drilling inventory in the Piceance basin. We are very happy with this acquisition, and Laramie management is moving rapidly to integrate those assets and capture the cost savings associated with the transaction. In addition, our commodity price hedges have proved to be valuable in the midst of the current natural gas supply glut, permitting Laramie to realize positive cash flow even in this difficult time.

I also wanted to comment on the recent announcement by our competitor in Hawaii that they were selling their refining, retail and logistics operations to a private equity firm. Some of you may have questions regarding the recent announcement. I would like to say we know little of the buyer's strategy and have no comment on the transaction other than to reiterate that we are pleased with our competitive profile in Hawaii and look forward to the future as we continue to enhance our position supplying fuels vital to Hawaii's economy.

At this time, I would like to turn the floor over to Joseph who will provide more detailed perspective on our refining, retail and logistics business.

Joseph Israel

Thank you Bill, and good morning everyone. Our Refining segment adjusted EBITDA in the first quarter was $6 million. Our combined 4-1-2-1 crack spread and Mid-Pacific crude differential index in the first quarter was $6.58 per barrel, approximately $1.85 per barrel below five-year's average or mid cycle environment. The weak index was mainly driven by low

Singapore and Pacific Northwest distillate crack spreads, basically at a five-year low for both jet fuel and diesel.

In the first quarter, our on-island sales were 61,000 barrel per day. Export sales were 20,000 barrel per day, for total sales of 81,000 barrel per day. On-island sales were 9% lower than plan, mainly driven by timing and lower jet fuel and Low Sulfur Fuel Oil demand. However, we continue to target 65,000 barrel per day of on-island sales for the rest of the year, based on existing supply contracts with military, airlines, utilities and other customers.

Our export sales included high value mixed aromatics to Asia, as we continue to take advantage of our long reformate position in a short global octane balance. On the feedstock side, we continue to benefit from the oversupplied market and build our crude oil supply flexibility by introducing new crude oil grades and optimizing transportation costs.

Solid refinery safety performance with zero Total Recordable Incident Rate or TRIR, combined with 98.9% mechanical availability for the quarter, have allowed us to continue to optimize our assets and execute our operating plan. Margin realization in the first quarter, and second quarter plan, is approximately $0.50 per barrel below average due to the hydrocracker catalyst reaching the end of its useful life.

Our refinery throughput in the first quarter was 74,000 barrels per day, consistent with our guidance. Our planned throughput for the second quarter is approximately 77,000 barrels per day. Our production cost in the first quarter was $3.74 per barrel. So far, in the second quarter, the combined index has averaged approximately $5.50 per barrel. However, the global octane shortage and the gasoline blending dynamics continue to present opportunities in the Pacific North West and Asia.

Our refinery turnaround is scheduled to start in the second week of July with an estimated 30-days oil-to-oil. Scope includes the execution of routine maintenance, including hydrocracker catalyst change, as well as regulatory consent decree works. Our estimated cost for the turnaround is in the $30 million to $35 million range.

Our retail segment has performed well with $8 million adjusted EBITDA contribution in the first quarter. Mid-Pac has generated through 12-months of operations under Par $16 million EBITDA in retail, $6 million EBITDA in logistics and additional $8-16 million EBITDA at the refinery level. Our Logistics segment adjusted EBITDA in the first quarter was $6 million.

In summary, we are happy with our operations results in the first quarter of 2016. This is a cyclical business and the margin environment is low now. We remain focused on what we can control, benefiting from our integrated and diversified business profile.

And now, I’ll turn the call over to Will to review Laramie operations and results.

William Monteleone

Thank you Joseph, as a reminder, Laramie closed its previously announced acquisition on March 1 and more than doubled its production and cash flow profile. Simultaneously, Par Pacific infused an additional $55 million of equity capital and increased its stake in Laramie to approximately 42%. The integration of the acquired properties is well underway and cost reduction activities are proceeding well. We're excited about the opportunities we are seeing to reduce costs and unlock value through this highly accretive transaction.

The Laramie team remains focused on lease operating expense reductions roughly 60-days into consolidated operations. Opportunities that we identified during our acquisition evaluation continue to look as large as we thought prior to taking control, and our confidence in execution on these initiatives continues to grow. For example, Laramie has renegotiated rental compressor contracts and is preparing to re-pipe gas flows to utilize excess Company-owned compression while moth-balling multiple rental units.

Headcounts are down significantly, excess equipment that came with the acquisition is being liquidated or incorporated into ongoing facility expansions, well chemical treatment programs have been simplified all to drive costs down to target levels. As we've detailed before, the acquired properties' LOEs totaled approximately $0.73 per mcfe during 2015 while Laramie's existing properties ran at $0.56 per mcfe.

If we can close the gap, the $0.17 per mcfe reduction would reduce our costs by approximately $5 million annually. This would be a significant uplift from our previously disclosed $24 million five-year average annual cash flow from the acquired properties. This amount would be realized without any additional benefit from economies of scale and field operations density.

I would like to remind everyone that Laramie's assets are more than just a dry gas play. Approximately 80% is dry gas, 20% is natural gas liquids and condensate. A significant portion of its Laramie's gathering, processing and treating costs are to strip out liquids and receive incremental revenue. Up until recently, NGL prices have been depressed and we weren't receiving much of a lift in pricing. However, we're starting to see that change for the better as ethane and propane prices improve.

Laramie has remained relatively unhedged on NGL pricing, however, during the quarter Laramie took advantage of some of the strength in the NGL market and hedged approximately 25% of existing NGL production through the end of December 2016. Laramie elected to hedge approximately 875 barrels per day of propane at $0.46.5 per gallon and 270 barrel per day of C5 plus at $0.85 per gallon. Excluding any impact from NGL hedges, every $0.01 per gallon move in natural gas liquids prices impacts Laramie's revenue and cash flows by approximately $800,000 annually based only on existing production only.

Production has held up a little better than we expected and exit production as of March 31 was approximately 151 million cubic feet equivalent per day. Laramie completed eight wells during January and then ceased activity leaving 58 wells that are drilled but uncompleted. Depending on gas prices through the balance of the year, we are assuming modest completion activity in the second half of the year.

At this point I will turn the call over to Chris to review our financial results.

Christopher M. Micklas

Thank you, Will. During the first quarter, Par Pacific reported Adjusted EBITDA of $5 million dollars. However, our first quarter adjusted EBITDA was negatively impacted by special items that totaled approximately $5 million. These special items include $4 million related to timing from the liquidation of inventory and severance costs associated with the downsizing of our Texadian operations and approximately $1 million of additional costs incurred with our company's SAP implementation.

We reported a net loss of $19 million, a loss of $0.46 per share, but these results include a $21 million non-cash inventory adjustment, $5 million for the previously mentioned special items, a $2 million loss from our investment in Laramie, an unrealized loss of $1 million on our derivative contracts and $700 thousand of acquisition and integration expense. Partially offsetting these items were a $6 million reduction in the value of the Tesoro earn-out contingency and a decrease of $2 million in the value of our common stock warrants. After adjusting for these items, our net income for the first quarter is $3 million.

I would like to take more time to provide more color to the $21 million non-cash timing differences that relates to the valuation of our refining inventory and related liability. Our supply and off-take agreement with J. Aron creates timing differences between GAAP reporting and the cash paid for inventory. For GAAP reporting, our inventory is maintained on a FIFO basis at the third-party purchase price. Also, we eliminate crude price risk by hedging cargoes on the water.

Hedge gains and losses as well as actual cash paid for the sale and repurchase with J Aron do not impact our GAAP inventory valuation. However, our calculation of Adjusted EBITDA reflects the actual cash cost for the crude run and adjusts for these impact in timing. In the first quarter, the adjustment was $17 million or approximately $2 per barrel. In addition, we record a liability in the amount we expect to pay J Aron as if we repurchased the inventory at current market prices. During the quarter, due to price rises, the change in this liability was a non-cash expense of $4 million.

Now, I will briefly review the segment performance. In our Refining segment, the refining adjusted margin was $32 million compared to $44 million for the same period last year. This was primarily impacted by lower crack spreads and lower on-island sales as Joseph previously discussed. Our Retail segment generated a gross margin of $19 million a $5 million or 40% increase over the first quarter of 2015. This increase reflects a full quarter's contribution from Mid-Pac of $8 million and continued growth in fuel volumes, offset by lower margins.

Our Logistics segment posted a gross margin of $8 million, a 13% decrease from the same period last year. This was primarily due to higher costs related to the acquired Mid-Pac assets coupled with a decrease in on-island sales volumes and the refund of insurance premiums received in the first quarter last year.

Texadian's gross margin was a loss of $4 million after adjusting for a loss of $3 million due to the sale of crude inventory stored at our leased terminal. As we have previously disclosed, we have downsized our Texadian operations to minimal activity levels by closing our Canadian office, exiting the terminal lease and allowing our credit agreement to lapse. Therefore, going forward, Texadian's remaining activities will be maintaining our pipelines' historic shipper status and subleasing rail cars.

General and Administrative expenses were $11 million which includes over $1 million of severance costs, the majority of which was non-cash stock vesting, related to the closure of our Texadian office in Canada and approximately $1 million of additional expenses relating to consolidating our systems and implementation of SAP.

Turning to liquidity, during the first quarter, we generated $12 million of cash from operations, and we continued to strengthen and improve our balance sheet. At the end of the first quarter, our long-term debt balance, including current maturities was $163 million. You may recall that we completed a stock offering of $76 million in the fourth quarter and repaid the $35 million term loan that was scheduled to mature in March of this year.

Our cash balance totaled $122 million at the end of the first quarter and our total liquidity position was $153 million, including $5 million available under the retail revolver. During the quarter our cash interest was $3 million and our capital expenditures totaled $4 million.

Our capital budget for the remainder of 2016, including maintenance CapEx, remains in the $45 million to $50 million range. As we have previously mentioned, the bulk of these expenditures relate to the scheduled refinery turnaround, which is expected to require cash expenditures of $30 million to $35 million including new catalyst.

Additionally, within the Logistics segment we expect to have a one-time operating expense of between $5 million and $10 million for maintenance projects. During the turnaround, we will also perform certain regulatory upgrades pursuant to Tesoro's Consent Decree with the EPA that is subject to reimbursement by Tesoro.

Now, I will turn the call over to Bill for his closing comments.

William Pate

Operator, this concludes our prepared remarks. Would you please check for any questions?

Question-and-Answer Session

Operator

Thank you. We will now be conducting a question-and-answer session [Operator Instructions] Thank you. Our first question comes from Scott Levine with Imperial Capital. Please go ahead.

Scott Levine

Hey good morning guys.

William Pate

Good morning.

Christopher M. Micklas

Scott Levine

So I was hoping if you can elaborate on the on-island sales, you've indicated they were little bit late in the quarter. I think you discussed some of the reasons why, but indicated that you expect 65,000 barrels a day for the remainder of the year. Will that ramp through the remainder of the year or do you expect to be there in the second quarter and maybe a little bit more elaboration as to what was going on there in the quarter that caused you to fall short of your target?

Joseph Israel

Yes, Scott good morning, it is Joseph. On-island are contractual by nature. So normally when we are over or under, it's more of a timing related than really structural demand. What happened to us in the first quarter, the jet fuel were short 3,000 barrels per day for On-island sales. Half of it was military, half of it was commercial and we're expecting catch-ups in inventories.

The military contract has also a minimum volume target for the year. So we should probably see some volume move up later in the year. And then, 2000 barrels per day we were short on the LSFO or Low Sulfur Fuel Oil, and this is related to a utility plant that we supply and that plant went through a turnaround in the first quarter and was short 2,000 barrels per day in consumption. So we are holding and expecting to be back to a 65 level for the rest of the year because this is where our contracts are.

Scott Levine

Okay. So you expect to be back at that level in Q2.

Joseph Israel

Yes.

Scott Levine

Okay. And then could you quantify, did you see a benefit from the declines in crude oil during the quarter, is that something you can quantify in terms of the impact on your results in 1Q.

Joseph Israel

And what do you mean by decline Scott?

Scott Levine

The crude oil price dropped pretty significantly during the - in the first quarter there, I didn't know whether your received the benefit associated with that drop.

Joseph Israel

Actually for the quarter, the price increased slightly if that helps. It was minimum impact, so we didn't see an impact of change.

William Pate

Scott this is Bill. If you recall, it went down in the first half of the quarter and then it came back up and the changes overall were offsetting.

Joseph Israel

Yes.

Scott Levine

Were offsetting, okay so negligible there. Got you. And then with regard to the acquisition landscape, I know you're limited in terms of what you can say Bill, in terms of your appetite there. But maybe an update on the market in general and does the transaction with one lock-in Hawaii effect any way your strategic plans either from this perspective or from a business perspective as far as you can tell?

William Pate

Yes, well first of all transactions they always take some time and bear in mind that we signed the Laramie deal in December and funded it just a month ago and we're obviously very pleased with that. We have a robust pipeline of opportunities, but we want to be very careful, our main objective is to identify opportunities that to us are attractive from a strategic, operational and financial context, and I can assure you we're going to remain disciplined as we're looking at transactions.

And if they don’t meet those criteria, we’re going to walk away. We’ve done that on a couple of occasion and we’ll continue to do that because we want to be patient in our strategy yet, at the same time, I do think this environment is going to yield opportunities for us to grow inorganically.

Scott Levine

Fair enough. Thank you very much.

Operator

The next question comes from Thomas Mitchell from Miller Tabak. Please go ahead sir.

Thomas Mitchell

Hi. I guess I just want to double check, if we take the entire refining gross profit that was about $10 million, if the on shore was $32 million does that mean you lost about $22 million in export on the gross profit basis.

William Pate

Could you handle it?

Christopher M. Micklas

Yes, I'm not sure I follow your question Tom. This is Chris the adjusted refining margin was $32 million not $9 million, $9 million is before you back out the adjustments for the inventory valuation so.

Thomas Mitchell

So that’s the inventory valuation okay fine. And then secondly, I think one or more of you may have had some experience in going into an industry where basically you are or your guiding investors - take up private equity point of view. Is a private equity buyer for the Chevron Refinery essentially inclined to make you believe that pricing discipline will remain on the island or are you concerned about potential new competition or I guess we could say reanimated competition from the refinery?

William Pate

I really can't comment on their strategy, I don’t know that much about it, but bear in mind Hawaii is a competitive environment and we think we are winning out fair share of the business and continue to believe that that will be the case going forward.

Thomas Mitchell

Okay. Thank you very much.

Operator

The next question comes from Andrew Shapiro with Lawndale Capital Management. Please go ahead.

William Pate

Hi Andrew.

Andrew Shapiro

Hi. Correct me if I'm wrong, but I don't think the FTC [BMA Trust] (Ph) delays on the Mid Pac acquisition concern the retail. So with the shifting of ownership of several retail outlets on-island, do you see any acquisition opportunities for further increase your on-island demand in economies of scale in the retail segment?

William Pate

I think it would be difficult to grow our retail segment through acquisition, we are obviously focused on trying to grow organically with new sites and we are going to be aggressive in that regard and we believe we can build the business on-island. But bear in mind it's a relatively small market and our ability to grow our share even at the grassroots level is somewhat limited, but we think it's a great franchise and we want to continue to try to grow it.

Andrew Shapiro

Right and when you say your ability to grow it through acquisition maybe problematic, is that because of your sizeable share already?

William Pate

Yes. And when we acquired Mid Pac, really the FTC focus was on the retail, it wasn't on the logistics.

Andrew Shapiro

All it was. Okay. Then I was wrong okay.

William Pate

And I think the FTC was really focused on market share in that region and it's already a fairly consolidated market between ourselves, Chevron and Sunoco [or Aloha].

Andrew Shapiro

Yes they have got Aloha. Okay, and then retail sales on the same-store sales basis, I don’t recall if you guys mentioned it, if you did can you at least remind so I don’t have to pick it up from the transcript.

Joseph Israel

Same-store basis is up 2%.

Andrew Shapiro

Okay and that is, do you have a breakout between I guess the gas versus everything else?

William Pate

That 2% was for fuel actually.

Joseph Israel

But it's really 95% gas we move and minimum diesel move through the stores.

Andrew Shapiro

Alight. Thanks a lot.

William Pate

Thank you.

Operator

[Operator Instructions] The next question is a follow-up from Scott Levine with Imperial Capital. Please go ahead.

Scott Levine

Hey good morning. Was hoping for just a little bit more color on the LOE savings, you guys there are hoping for with Laramie and the cost reduction. Seems like you have a good business plan there. I mean can you give us a sense, I don’t know if you have formal targets, I'm guessing not. But just maybe informally, what kind of timeframe we should be thinking about to achieve the types of cost savings within the business that you are anticipating that’s going be gradual process or maybe we've seen accelerated process early on and then it kind of tapers off from there, maybe a little bit more color there would be helpful.

William Monteleone

Sure, good morning Scott, this is Will.

Scott Levine

Good morning Will.

William Monteleone

I think it's the later kind of description that you gave which would be, I think we see a significant realization kind of within the first 60 to 90-day and then it's going to take the balance of probably the year to get it to where we need it to be kind of on a target basis. And again, I think from a more detailed standpoint if you look at the acquired assets a decent chunk of the production an acreage came from the north area that we refer to as Cascade Creek. And then a large chunk of the upside and integration opportunity was actually acreage that's correctly adjacent to where Laramie operates today in Collbran Valley.

So we don't have any reason to believe that the way that Laramie operated historically, its cost around $0.50 to $0.55 of LOE per mcfe is an unreasonable target for us to be pursuing here. And again, it's giving limited benefit to economies of scale or field operation density that we would see. So a bit differently we're not thinking about this in the context of it actually lowering Laramie's base LOEs either, we're just showing you kind of what it's worth on an annual basis if we can hit the target, but we feel it's reasonable.

Scott Levine

And to be clear, your timing in terms of hitting that target. You're thinking year end is reasonable there?

William Monteleone

Yes.

Scott Levine

Okay, great and then just one housekeeping or clarification for the turnaround. So are peaking to $30 million to $35 million in CapEx in the third quarter associated with that and then $5 million to $10 million in OpEx or P&L in direct associated all-in the 3Q?

Joseph Israel

Yes.

Scott Levine

Okay, just want to be sure I understood that correctly. Thank you.

Operator

The next question is a follow-up from Andrew Shapiro from Lawndale Capital Management.

Andrew Shapiro

Thanks. Quick follow-up what are the upcoming investor presentations and conferences you guys have on the calendar for the upcoming quarter or two?

Christine Thorp

This is Christine. We will release them, we haven't publicly announced any coming up, but as soon as we get them on the schedule, we'll let the market know.

Andrew Shapiro

So the conference call isn't one of the forums to do that then?

William Pate

I don't think we have anything right now, because a lot of the season as you probably know we just passed through and then we'll have some more in the fall, which we will obviously be attending.

Andrew Shapiro

Okay. That's great.

William Pate

We don't have anything through the summer schedule Andrew.

Andrew Shapiro

Okay. [indiscernible] the conference call seems to be - this is regular FD Forum that you can do.

William Pate

Yes.

Andrew Shapiro

Great. Thanks.

Operator

Ms. Thorpe, gentlemen, there are no further questions registered at this time. I would like to turn the floor back to you for closing comments.

William Pate

Thank you operator and thank you everybody for joining us. We appreciate your time. Have a good day.

Operator

Ladies and gentlemen, thank you for your participation. This does conclude today's conference call. You may disconnect you lines and have a wonderful day.