# Par Pacific Holdings' (PARR) Q4 2016 Earnings Call Transcript

Par Pacific Holdings, Inc. (NYSEMKT:PARR)
Q4 2016 Earnings Conference Call
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**Executives**
Christine Laborde - Director of Investor Relations
William Pate - President and Chief Executive Officer
Joseph Israel - President and Chief Executive Officer of Par Petroleum, LLC
Will Monteleone - Senior Vice President of Mergers & Acquisitions
Chris Micklas - Chief Financial Officer

**Analysts**
Chi Chow - Tudor, Pickering, Holt & Co.
Tim Rezvan - Mizuho Securities
Andrew Shapiro - Lawndale Capital Management

**Operator**

Greetings, and welcome to the Par Pacific Holdings Fourth 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 Laborde, Director of Investor Relations for Par Pacific Holdings. Thank you, Ms. Laborde. You may begin.

**Christine Laborde**

Thank you, Doug, and welcome, everyone, to Par Pacific Holdings fourth quarter and full-year 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.

Before we begin this discussion, please note that some of the statements we make during this call may discuss plans, expectations and estimates including but not limited to our outlook for the company. These are forward-looking statements which are subject to change. They are subject to risk and uncertainties, and actual results may differ materially. Because of this investors should not place undue reliance on forward-looking statements. We disclaim any intention or obligation to update or revise any forward-looking statements.

I refer you to the latest Forms 10-K and 10-Q Par Pacific Holdings filed with the SEC for a more detailed discussion of the major risk factors affecting our business. Further information regarding these as well as supplemental financial and operating information, including reconciliations to GAAP may be found within our press release and our investor presentation on our website at www.parpacific.com or in our filings with the SEC.

Now, let me turn the call to Bill Pate.

**William Pate**

Thank you, Christine, and good morning to our conference call participants. We had a strong fourth quarter to cap 2016 with adjusted EBITDA of approximately $36 million. We enter 2017 with a much better Pacific market outlook, no major planned refinery outages, a full-year of contribution from our Wyoming operations, and a more significant drilling program at Laramie.

Our Hawaii operations had particularly strong results in the fourth quarter due to a buoyant market and solid management execution. In large part, these results were due to a return to mid-cycle cracks and excellent operational performance at all of our Hawaii business units.

Our Hawaii retail business completed the conversion of 32 retail locations to our new Hele brand, business has been brisk and we had another strong quarter at the pump. In Wyoming, we experienced weaker refining cracks like most mainland refiners, but operational performance was very strong, and we were able to generate positive EBITDA in the fourth quarter.

The fourth and first quarters for Wyoming will always be difficult quarters, given the seasonality in PADD IV. During the quarter, we also received approval to operate and completed a rail loading facility in Newcastle. In both markets, we had key refined product contract wins to maintain our market share in our local markets as we enter 2017.

Laramie continues to perform very well with the completion of most of its drilled but uncompleted well inventory, as well as the initiation of a single-rig drilling program in December. With the current market environment, we anticipate that Laramie will be able to grow its production profitably and increase its drilling program without additional capital. We expect to see a growing production and cash flow profile from Laramie in 2017.

And now, Joseph will provide more details on our downstream business.

**Joseph Israel**

Thank you, Bill, and good morning, everyone. First, I would like to congratulate our employees for achieving two years with no lost time injuries in our Hawaii refinery and one year with no lost time injuries in our Wyoming refinery. This is a testament to our safety culture at the Par family.

Our Refining segment adjusted EBITDA in the fourth quarter was $30 million, compared to $23 million in the fourth quarter of 2015. In Hawaii, back to mid-cycle environment with combined Mid Pacific index at $8.48 per barrel compared to $8.25 per barrel in the fourth quarter of 2015. The favorable market conditions in the fourth quarter were mainly driven by Singapore gasoline and fuel oil crack spreads. Low global refining utilization rates combined with healthy gasoline demand in Asia and Latin America have shifted inventories away from Asia and supported crack spreads.

On the fuel oil side, lower supply from upgraded refineries, especially in Russia and higher demand from refineries and power plants resulted in lower fuel oil inventories and improved cracks. In the fourth quarter, our refinery throughput in Hawaii was 75,000 barrels per day with 99.8% operational availability. Adjusted gross margin was $7.26 per barrel, and direct production costs were $3.07 per barrel. We sold 75,000 barrels per day, including 63,000 barrels per day of on-island sales.

Our net margin performance in the fourth quarter is reflecting $0.50 to $0.75 per barrel of stronger than average capture rate, mainly driven by the following items. Number one, hydrocracker performance post the third quarter turnaround. Number two, low cost operations driven by reliability. And number three, solid commercial execution. So far in the first quarter, our combined Mid Pacific index has averaged over $9 per barrel, and our first quarter planned throughput in Hawaii is approximately 78,000 to 80,000 barrels per day.

In Wyoming, our 3-2-1 Index was $13.69 per barrel in the fourth quarter compared to $19.03 per barrel in the fourth quarter of 2015. The weak market environment for Rocky Mountains and Midwest refineries was driven by high products inventories. Our refinery throughput averaged 15,000 barrels per day in the fourth quarter.

Adjusted gross margin was $5.85 per barrel, and direct production costs were $3.86 per barrel. Excluding a pension liability adjustment in the fourth quarter, the production cost in Wyoming would be approximately $6.20 per barrel, implying close to break-even net margin result.

On the commercial front in Wyoming, we extended our rail loading capabilities in the fourth quarter to handle light products. This project increases our footprint and provides us with greater flexibility to optimize sales and leverage our high octane capabilities in different markets. So far in the first quarter, our Wyoming 3-2-1 Index has averaged under $15 per barrel. We continue to position our refinery and system inventories in Wyoming for the gasoline season, and planned throughput for the first quarter is 14,000 to 15,000 barrels per day.

At this point, I'll turn the call over to Will to review Laramie's activities.

**Will Monteleone**

Thank you, Joseph. 2016 has been a transformational year for Laramie with major improvements to nearly every aspect of the business. This transformation started in March with Laramie closing on a strategic acquisition of adjacent properties with the primary objective of reducing unit operating costs. The Laramie team has done just that, repeating past exceptional performances on this front.

In review, the year one target we set for cash operating costs per Mcfe, including G&A when we completed the acquisition was $1.52 per Mcfe, or a reduction of approximately 40% from Laramie's 2012 to 2015 unit operating costs. Looking at the last three quarters of 2016, since the acquisition closed, unit operating costs were $1.67 per mcfe.

Most notably, Laramie delivered lease operating expenses per Mcfe of $0.44 compared to the prior operators standalone lease operating expenses of $0.74 per Mcfe. We believe there is more improvements to come on this front and we're making further steps to achieve the targets set that I will discuss below.

Quarterly production averaged 137 million cubic feet equivalent and December exit production was 140 million cubic feet equivalent. As of year-end, 50 of the 58 drilled uncompleted wells were online. In addition, during December, Laramie commenced a one rig drilling program and four wells were drilled for the quarter.

Price realizations continue to improve and during the quarter gas realizations were $2.87 per Mcf, Natural Gas Liquids $0.36 per gallon, and condensate $44 per barrel. On the hedging front, Laramie added 10 million cubic feet a day for 2017 and 2.5 million cubic feet a day for 2018, keeping roughly 80% of existing gas production hedged through 2018. A portion of these hedges were collars with a floor of $3 and ceiling of $3.25 per Mcf.

Laramie is unhedged on Natural Gas Liquids from January 2017 forward. See details in our updated investor presentation. Laramie generated approximately $13 million in Adjusted EBITDA for the fourth quarter, spent approximately $14 million in CapEx leaving a revolver balance of $118 million as of December 31. Since March 31, Laramie paid down first-lien bank debt by more than $13 million and ended the year with a debt to EBITDA of 2.7 times, below the 3 times debt to EBITDA target set when announcing the strategic acquisition.

During the fourth quarter, Laramie renegotiated one of its gathering and processing contracts, reducing gathering and processes expenses, and improving netbacks on Natural Gas liquids. These improvements will largely materialize starting in the fourth quarter of 2017. These changes materially improve Laramie economics in certain locations and drive the expectation for further declines in unit operating costs down to $1.47 per Mcfe. In addition, Laramie expects Natural Gas Liquids netbacks to improve further.

Proved reserves and Proved PV10 based on SEC conventions increased 84% and 174%, respectively. This increase reflects the acquisition completed during Q1 of 2016, as well as lower prices in the 2016 case.

I would also call out, we've provided in our updated investor deck an alternate reserve case based on NYMEX Strip prices as of 12/31/2016. Under this pricing scenario, Proved Developed PV10 is approximately $400 million and Proved and Developed PV10 is approximately $187 million. The booked PUD locations in this case reflect 342 gross drilling locations.

Regarding future plans, Laramie is running a one rig program and anticipates adding a second rig during the second quarter of 2017. Laramie is evaluating adding a third and fourth rig in the second-half of 2017. Based upon a staggered two-rig program, Laramie anticipates exiting 2017 with production between 160 to 180 million cubic feet a day equivalent.

Laramie expects to fund capital expenditures in excess of cash flow with availability on its revolving credit facility, while maintaining a 3 times debt to EBITDA ratio at year end.

At this point, I'll turn the call over to Chris to review our financial results.

**Chris Micklas**

Thank you, Will For the fourth quarter 2016, Par Pacific reported a net income of $14 million, or $0.30 per share compared with a net loss of $67 million, a $1.72 per share loss in 2015.

Our adjusted net income was $11 million, or $0.23 per share compared to an adjusted net loss of $38 million, or $0.99 per share. Adjusted EBITDA for the fourth quarter was $36 million compared to $23 million in 2015. Our earnings release details our non-GAAP adjustments for arriving at adjusted net earnings and adjusted EBITDA.

The Refining segment's adjusted EBITDA was $30 million compared to $23 million for the same period last year. Included in the 2016 results is a favorable non-cash pension adjustment of $3 million.

As Joseph has mentioned, the fourth quarter Hawaii refinery results benefited from crack improvements to slightly above mid-cycle and we were able to achieve a higher capture rate. As a result of the weak market environment in the Rocky Mountains and Mid-continent, the Wyoming refinery was close to break-even in the quarter.

Our Retail segment generated adjusted EBITDA of approximately $7 million, which is consistent year-over-year. During the fourth quarter, our Logistics segment posted adjusted EBITDA of $10 million, a $4 million increase from the same period last year.

The Hawaii logistics improved profitability of $3 million was a result of higher utilization of our assets and reduced maintenance expense. Wyoming contributed approximately $1 million to our year-over-year improvement.

In the fourth quarter 2016, G&A expense was $10 million. This was flat with the third quarter this year and a $2 million reduction compared with the same period last year. The Wyoming acquisition integration has progressed as plan, with the closure of the Houston, Denver and Austin offices, a system conversion in November, and we are on track to exceed our projected $5 million of annual synergies.

At the end of the year, our cash balance totaled $48 million and our total liquidity was $92 million, an improvement of $16 million from the third quarter. Looking forward to 2017, we anticipate our CapEx spend to be $42 million to $46 million. This comprises of maintenance and regulatory CapEx in our Refinery, Logistics, and Retail segments of between $23 million and 25 million, $12 million to $14 million in profit improvement project that we've identified, and $6 million to 7 million in new information system.

Now, I will turn the call back over to Bill.

**William Pate**

Thank you, operator. We'd be happy to take any questions at this time.

**Question-and-Answer Session**

**Operator**

Thank you. Ladies and gentlemen, at this time, we will be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Chi Chow with Tudor, Pickering, Holt. Please proceed with your question.

**Chi Chow**

Hey, thank you. Good morning, everyone. Well done on the Q4 results there. Joseph, a couple of questions for you. The operating costs performance at both refineries was very good in the quarter. Can we expect Q4 trends on both a per barrel and absolute dollar basis to be representative, or indicative of the expected cost pressure going forward at both plants?

**Joseph Israel**

I'll start with Wyoming. Chris mentioned in his prepared remarks, the pension adjustment at $3 million, this will translate to $2.30 per barrel with implied $6.20 per barrel kind of OpEx. And I expect our ongoing OpEx with higher rates in the season to be closer to $6.50 per barrel more of a trend going forward. And then for Hawaii, I think about $3.07 per barrel is like record low as many things went our way, I think 3.25, 3.30 is probably more of the steady state going forward.

**Chi Chow**

Okay, great. Thanks. You talked about the new rail loading facility, can you talk a bit more about the strategy there? Is that really to push products to different markets, or any details on that end?

**Joseph Israel**

Yes. In Padd 4, the name of the game is isolation and small markets, so going outside of the Wyoming and South Dakota boundaries required logistic initiative on our side in order for us to access other markets with rail and take advantage of our long octane position in the refinery. And we have done just that and extremely happy with the result and it will continue to serve us and give us additional markets to optimize our refining capacity.

**Chi Chow**

What kind of volumes are you talking about on moving out by rail?

**Joseph Israel**

It's going to be a very dynamic answer there. Each month, it depends on the market condition in our area and market opportunities outside..

**Chi Chow**

Okay. Thanks, Joseph. Maybe one question – final question for Bill. Can you give us an update on what you've seen in the M&A market? Are there any increase visibility and acquisition opportunities and how you feel about the balance sheet position to fund any opportunities going forward?

**William Pate**

Sure. We always have a robust acquisition pipeline. I wouldn't say that it's more significant or less significant than it has been in the past. And as you know, our growth has really been built upon a string of successful acquisitions, and I'm pretty confident that we can extend that track record with time.

We obviously just completed the Wyoming acquisition and we're really focused on improving the value of that and other units right now. But I can assure you as soon as we have something to notify you and the shareholders regarding any growth-related capital investments, we will be out in the market.

As to the balance sheet, we have plenty of capital for our current business. I think as we mentioned in the last call, we expected in Q4 to be generating liquidity and we did that. I expect that we'll generate cash based on current market conditions for the year. I don't think we have balance sheet capacities to pursue major acquisitions, so we'd obviously be looking to the equity markets with respect to any acquisitions. But we would have to evaluate that in the context of our equity cost of capital. And at the current share prices, I think, we need to see exceptional opportunities to justify the dilution associated with any equity raise.

**Chi Chow**

Any particular share price targeted have to be more comfortable on issuing equity?

**William Pate**

No.

**Chi Chow**

Okay. Thanks, Bill, I appreciate it.

**William Pate**

Yes.

**Operator**

Our next question comes from the line of Tim Rezvan with Mizuho Securities. Please proceed with your question.

**Tim Rezvan**

Hi, good morning, folks. I had a couple questions on Wyoming. I guess probably intended for Will. I saw in the presentation you talk about getting clearly the completion cost down to $800,000, which is a pretty impressive improvement. Do you have any update on kind of EURs that you're seeing, or should, we're trying to think about as we look at full cycle cost, how we should be thinking about F&D, especially given that you're drilling where you have a 100% net royalty interest?

**Will Monteleone**

Sure. So included in the investor presentation that we recently posted, we did get our cost down an additional amount down to $800,000 from $900,000, or we're expecting it to that level. And then I think with regards to EURs, we have also included details to some spacing changes that were proceeding on beginning with the rig that commenced drilling in December. So I think on the original three column designs, we were seeing close to 1.3 BCF EURs. And our belief is, as I referenced in the – our investor presentation, we're going to actually increase spacing to 15 acres and we're going to drill two columns per section.

So we think that that the target there is 1.7 to 2 BCF EURs off of an $800,000 cost. And again, I think one of the elements here that we are cognizant and watching is, there is obviously a concern service cost inflation is starting to creep up. But I think one of the competitive advantages that we have is, we're using sandless fracs. So sand is not a component of our completion cost as you would see versus other operators and we continue to see drilling days and efficiencies improve and the team is doing a great job on capital efficiency.

**Tim Rezvan**

Okay. And just to classify, are you still drilling in the areas where you're not paying royalties?

**William Monteleone**

I think our development plans for 2017 have us in the southern acreage, which is, we do have small sections, where we have elevated net revenue interest. But I think on average, we're going to be in the 85% to 88% in our range for our 2017 development plan.

**Tim Rezvan**

Okay, all right. Thanks for the color.

**William Monteleone**

Sure.

**Operator**

[Operator Instructions] Our next question comes from the line of Andrew Shapiro from Lawndale Capital Management. Please proceed with your question.

**Andrew Shapiro**

Hi, good morning. I think if I heard Joseph correct, Hawaii has been – is running at a, call it an optimized cost level, and if that's the case and where you're sitting at mid-cycle cracks, let's say, that continued. To what level could the Hawaii refinery increase its throughput on a sustainable level rather than, a short gunning that for a brief time period to get a feel for what kind of as further economies could be derived, as well as in a maximized throughput from what you're running at?

**Joseph Israel**

Yes, we have demonstrated in the past several days of 90 plus when we needed to catch up. So we definitely have this capability. But over a month's period of time, over a quarter, we haven't seen really a higher need than 81,000, 82,000 barrels per day, which included the export opportunities. So, we'll continue to monitor margins and then choose the right throughput accordingly. At this point, this is optimization.

**Andrew Shapiro**

Okay. And then with respect to Wyoming, you might have said this in your script earlier, I might have missed it. But to what extent is the integration of the assets in the Par and extracting the synergies that you had projected or planned, to what extent is that integration complete and what is left to complete?

**Joseph Israel**

Yes, I'll let Chris start on the administration – the administrative level and continue with the operations.

**Chris Micklas**

Yes, from an administration and back-office standpoint, we have closed the Houston, Denver, and Boston offices and have consolidated all of the back-office functions here in our Par, Houston offices. We have converted the Wyoming business from their old ERP system on to our ERP system, so they're functioning now completely on our ERP system and we are on track. We had said during the acquisition that we were shooting for $5 million of synergies and we are on track to exceed the $5 million of synergies.

**Joseph Israel**

And then beyond operation, we have a great team in Wyoming. It’s really a matter of adopting best practice, giving them access to our refinery team in Hawaii, share information, start tracking KPIs, and all the good things that we do in the industry and this is going very well.

**Andrew Shapiro**

And then – and when you talked about the administrative, the closing the offices and those consolidations; were those effective in the middle of the fourth quarter, the end of the fourth quarter, I’m just wondering to what extent the fourth quarter’s performance already reflects those synergies, or it’s primarily going to be seen in the Q1 that we’re in now?

**Chris Micklas**

The majority of the activity happened at the end of the fourth quarter, so you…

**Andrew Shapiro**

Okay, [Multiple Speakers] yes.

**Chris Micklas**

… holding in the first quarter.

**Andrew Shapiro**

Thank you. And the last question here is, can you – what do you have on the calendar for your upcoming investor presentations, conferences that you’re coming out with?

**William Pate**

Christine?

**Christine Laborde**

And we have a conference in late March in New Orleans and in July in Dallas and we will put out details to those as we get closer to them.

**Andrew Shapiro**

Outstanding. Thank you very much.

**Operator**

There are no further questions in the queue. I’d like to hand the call back over to management for closing comments.

**William Pate**

Thank you, operator. We want to thank everyone for joining us today. Refining is a cyclical business and the key for us is to know how to generate modest cash flow when times are bad and run exceptionally well in the good times. And this is exactly what we’ve done this year. We found a way to execute a major turnaround in Hawaii, acquire the Wyoming downstream operations, establish a new retail brand, all as we were navigating through some pretty challenging margin environments during the first three quarters of the year.

Today, we’re delighted to report strong fourth quarter financial results with a return to mid-cycle cracks in the Mid Pacific. We look forward to speaking with you in the future. Thank you.

**Operator**

Ladies and gentlemen, this does conclude today’s teleconference. Thank you for your participation. You may disconnect your lines at this time and have a wonderful day.