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HEP - Q4 2016 Holly Energy Partners LP Earnings Call

EVENT DATE/TIME: FEBRUARY 21, 2017 / 9:00PM GMT



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Rich Voliva *Holly Energy Partners LP - SVP & CFO*

CONFERENCE CALL PARTICIPANTS

Theresa Chen *Barclays Capital - Analyst*

Jerren Holder *Goldman Sachs - Analyst*

PRESENTATION

Operator

Welcome to Holly Energy Partners' fourth-quarter 2016 conference call and webcast.

(Operator Instructions)

Please note, that this conference is being recorded. It is now my pleasure to turn the floor over to Craig Biery. Craig, you may begin.

Craig Biery - *Holly Energy Partners LP - IR*

Thanks, Devon, and thanks to each of you for joining this afternoon. I'm Craig Biery, Investor Relations for Holly Energy Partners, and welcome to our fourth quarter 2016 earnings call. Joining us today are George Damiris, President and CEO, and Richard Voliva, Senior Vice President and CFO.

This morning, we issued a press release announcing results for the quarter ending December 31, 2016. If you would like a copy of today's press release, you may find one on our website at hollyenergy.com.

Before George and Rich proceed with their remarks, please note the Safe Harbor disclosure statement in today's press release. In summary, it says statements made regarding management expectations, judgment or predictions are forward-looking statements. These statements are intended to be covered under the Safe Harbor provisions of federal securities laws.

There are many factors that could cause results to differ from expectations, including those noted in our SEC filings. Today's statements are not guarantees of future outcomes.

Also please note that information presented on today's call, speaks of only as of today, February 21, 2017. Any time-sensitive information provided may no longer be accurate at the time of any webcast replay, or reading of the transcript.

Finally, today's call may include discussion of non-GAAP measures. Please see today's press release for reconciliations to GAAP financial measures. And with that, I'll turn the call over to George Damiris.

George Damiris - *Holly Energy Partners LP - President & CEO*

Thanks, Craig, and thanks to each of you for joining the call this afternoon. HEP had a very successful 2016, led by significant operational and financial achievements.



We continued our history of steady growth, by increasing total throughput volume by 8% versus 2015. Our strong and stable cash generation allowed us to accelerate our year-over-year distribution growth, and maintain our record of continuous quarterly distribution increases. With over 90% of our revenues tied to long-term fee-based contracts with minimum volume commitments, HEP has a solid business model that will continue to drive financial results, while supporting our positive growth outlook.

In 2016, we continued to execute on our growth strategies, by completing several acquisitions and current sponsor dropdowns. During the year, we successfully acquired a 50% interest in the Osage and Cheyenne pipelines, increasing our equity income by \$5.6 million annually.

We also expanded our storage footprint, with the acquisition of our Tulsa crude tanks in March, taking our total storage capacity to 14 million barrels. The largest transaction of 2016 was the addition of the newly constructed refinery processing unit at HollyFrontier Wood Cross refinery, which were dropped down in October, providing an estimated \$32 million in annual EBITDA. Overall, our internal and external growth initiatives resulted in a 17% increase in annual EBITDA versus 2015.

Going forward, we're optimistic about the year ahead, and continue to explore acquisition opportunities. Given the quality and location of our asset base, the talented employees, and support of General Partner, HEP has a strong foundation for growth. With that, I'll turn it over to Rich.

Rich Voliva - *Holly Energy Partners LP - SVP & CFO*

Thanks, George. On January 26, Holly Energy Partners announced a quarterly distribution of \$0.6075 per unit, a 7.5% increase over the same period in 2015. This distribution marks the 49th consecutive increase for HEP unitholders since our IPO in 2004, and represents an acceleration in year-over-year distribution growth, as well as progress towards our 8% distribution growth rate target.

For the fourth quarter of 2016, HEP generated distributable cash flow of \$59 million, \$4.9 million higher than the same period last year. We ran a distribution coverage ratio of 1.07 times for the quarter, and 1.09 times for the full-year of 2016.

Net income attributable to HEP for the fourth quarter was \$41.4 million, compared to \$40.5 million for the same period in 2015. This increase in earnings was primarily driven by the newly acquired Wood Cross refinery processing unit, and partially offset by higher interest expense associated with our 6% notes, as well as inflation-driven tariff decreases.

Operating expenditures in the period totaled \$35 million, including \$850,000 of OpEx reimbursed by HollyFrontier. Our capital expenditures for the quarter were \$12 million, including approximately \$2.6 million in maintenance CapEx, and \$2.7 million of CapEx reimbursed by HFC. In 2017, excluding CapEx reimbursed by HFC, we expect to spend approximately \$9 million for maintenance CapEx, and approximately \$30 million for expansion capital, excluding acquisitions.

HEP successfully participated in the capital markets in 2016, providing us with the necessary funding to take advantage of asset opportunities. We raised \$400 million of 6% notes, and upsized the capacity of our revolver by \$[350] million, in order to strengthen our balance sheet. Additionally, we issued \$[103] million of equity through a private placement, and \$24 million through our ATM program. Our current liquidity, and ability to access the capital markets will enable us to achieve future growth, both organically and through M&A.

As of December 31, 2016 HEP had approximately \$1.2 billion of total debt outstanding, comprised of \$300 million of 6.5% notes due in 2020, \$400 million of 6% notes due in 2024, and approximately \$550 million drawn on our \$1.2 billion credit facility. On January 4 of this year, we redeemed our 6.5% note, by using revolver borrowings, thereby reducing our quarterly interest expense by roughly \$2.6 million. Including cash and revolver availability, our current liquidity stands over \$330 million at the end of January 2017.

For the fourth quarter of 2016, we recognized \$2.7 million of the deferred revenue from prior shortfalls billed to shippers. And as of December 31, HEP carried \$5.6 million in deferred revenue on our balance sheet. In the first quarter of 2017, we anticipate recognizing approximately \$2.9 million in deferred revenue. And with that, I'll turn the call over to Devon for the Q&A period.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Theresa Chen, Barclays.

Theresa Chen - *Barclays Capital - Analyst*

Good afternoon.

George Damiris - *Holly Energy Partners LP - President & CEO*

Hey, Teresa.

Theresa Chen - *Barclays Capital - Analyst*

Hi, I had a question related to your expected contribution on UNEV. Now that you have about a full winter's of volumes behind you, are you still comfortable with that \$15 million number for 2017, versus 2014 levels?

Rich Voliva - *Holly Energy Partners LP - SVP & CFO*

So Teresa, I think, it may be a little short of that number. That pipeline is going to be very driven, by the arbitrage between Salt Lake City and Los Angeles ultimately, but really that shows through in Las Vegas. So we saw that swing pretty hard, for example, in the fourth quarter, when [ARB] was closed in October and November, and we did not see the volume growth we were hoping for during those months. That [ARB] opened up in December, and we saw more than what we had expected on a run rate basis.

So we're expecting that to be volatile, when that [ARB] is open, that the \$15 million number on an annualized basis is very good. But I don't have a crystal ball on whether that ARB is going to be opened or closed day to day. So I think \$15 million is the upside, is probably the short answer.

Theresa Chen - *Barclays Capital - Analyst*

Got it. And then on your internal initiatives, the operational improvements that you've given in your previous Analyst Day, can I just get an update on how that's going, and if you're hitting those run rates?

George Damiris - *Holly Energy Partners LP - President & CEO*

Yes. I'd say we're probably three-quarters of the way, through hitting those run rates. That's really going to show up in two places, and it's kind of hard to call out, right, because part of it's operating expense that's avoided. But yet, because we're growing, we're still seeing operating expense growth in total. And part of it, is capital that's avoided. And you can see obviously, our maintenance capital number is set to be down 2017 versus 2016. So as you can see it tangibly there. But we're very pleased with the progress on those initiatives.

Theresa Chen - *Barclays Capital - Analyst*

Great. Thank you very much.

Operator

(Operator Instructions)

Jerren Holder, Goldman Sachs.

Jerren Holder - Goldman Sachs - Analyst

Hi, good afternoon. I was just wondering, was there anything that happened in the quarter unplanned, sort of like a turnaround, or a disruption in the pipes that may have led to lower year-over-year volumes?

Rich Voliva - Holly Energy Partners LP - SVP & CFO

Yes, Jerren, so I think we called this out in the press release. We had, Holly Frontier had some down time during the quarter at the Navajo refinery, which did hit our crude system, and some of the intermediate lines. It wasn't not extensive, but versus, certainly, versus the rest of the fourth-quarter of 2015 would show up.

Jerren Holder - Goldman Sachs - Analyst

Anything else we should expect, maybe year-to-date, as we kind of compare numbers between last year and this quarter so far?

Rich Voliva - Holly Energy Partners LP - SVP & CFO

Well, I think, in the first quarter, HollyFrontier has a scheduled turnaround at the Navajo plant. That is a full refinery turnaround, basically taking the plant offline for 45 days. If memory serves, the vast majority of which will be in the first quarter, so we do expect to see some impact there in the year-over-year.

Jerren Holder - Goldman Sachs - Analyst

Okay. Nothing in the Utah sort of area, none of those your -- like Frontier pipeline or SLC pipeline?

Rich Voliva - Holly Energy Partners LP - SVP & CFO

Sure, Darren. So obviously, I'll defer to Plains for details, as the operator and our partner in those lines. We have had some down time on the SLC line, in the last -- one to two weeks, and that has backed up and impacted the Frontier line.

There is some impact there, and if you look at our 2016 equity and income, we had about \$4.5 million for the year on SLC, and a little over \$4 million for the year on Frontier. So depending on how long this downtime goes, we'll see some impact there. We're very optimistic that we're going to get those resolved shortly though.

Jerren Holder - Goldman Sachs - Analyst

Okay. And that has no flow-through to UNEV, just given that you guys are pretty much -- are expected to be at MVC levels,?



George Damiris - *Holly Energy Partners LP - President & CEO*

Yes, I mean, maybe a little bit. In my earlier comments on the arbitrage, the crack spreads, and the product prices between Salt Lake and Las Vegas are very volatile at the moment, as you would expect given what we're seeing on the pipe. So it's probably a little early to say, frankly.

Jerren Holder - *Goldman Sachs - Analyst*

Okay. That's it for me. Thank you for the time.

George Damiris - *Holly Energy Partners LP - President & CEO*

Sure.

Operator

If there are no further questions, I will turn the floor back over to Craig for any closing remarks.

Craig Biery - *Holly Energy Partners LP - IR*

Thanks again for joining the call today. If you have any follow-up questions, please reach out to Investor Relations. Otherwise, we look forward to sharing our first-quarter results with you in May.

Operator

This concludes today's conference call. You may now disconnect. Thank you for joining, and have a great day.

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