SemGroup Corporation

First Quarter 2018 Conference Call

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CORPORATE PARTICIPANTS

Alisa Perkins - *Vice President and Treasurer*

Carlin Connor – *Chief Executive Officer*

Robert Fitzgerald - *Senior Vice President and Chief Financial Officer*

David Minielly - *Vice President Rose Rock Midstream*

PRESENTATION

Operator
Good morning, ladies and gentlemen. Welcome to the SemGroup's First Quarter 2018 Earnings Conference Call. As a reminder, this call is being recorded. All participants will be in listen-only mode. Should you need assistance, please signal a Conference Specialist by pressing the star key, followed by zero.

After today's presentation, there will be an opportunity to ask questions. To ask a question you may press star, then one on your touchtone phone. To withdraw your question, please press star, then two.

I would now like to turn the conference call over to SemGroup's Head of Investor Relations, this Alisa Perkins. Ms. Perkins, the floor is yours, Ma'am.

Alisa Perkins
Thank you, Mike. Good morning everyone. Before we being today, I would like to remind you that our earnings release and presentation for today's call include projections, forward-looking statements, and certain non-GAAP financial measures. We encourage you to read our full disclosures in our latest press release, slide presentation, and SEC filings for a discussion of those items, including conciliations to GAAP financial measures.

Hosting the call today is Carlin Conner, our CEO, and Bob Fitzgerald, our CFO. We also have David Minielly, Vice President of our Crude Division.

With that, let me turn the call over to Carlin.

Carlin Connor
Thank you, Alisa, and good morning everyone. We are pleased to be here today to review SemGroup's financial performance for the first quarter and provide an update on our direction and strategy.

Starting with Slide 4, our execution so far on our 2018 operating plan has been on target. We are growing high-value organic earnings and increasing the security of these cash flows. At the same time, we are well-positioned in project-rich areas of the Gulf Coast, Canada, and midcontinent to deliver strong capital returns.

From an earnings perspective, we finished the first quarter with Adjusted EBITDA of just over $93 million, up $33 million from this time last year. Excluding a one-time instruments claim loss at HFOTCO, our results are right in line with expectations. With the addition of secure refinery-driven cash flows from HFOTCO and Maurepas pipeline, we're announcing nearly 60% of our gross margin supported by Take-or-Pay business compared to about 40% last year. We are affirming the financial guidance we provided in February. We expect strengthening in the second half of the year as projects like HFOTCO's crude expansion come online. Bob will cover more details of our first quarter results in a few moments.

During the first quarter, we were very focused on executing our capital raise plan. We completed the previously announced sale of our Mexican Asphalt business in January and also sold our U.K. SemLogistics business which closed in April. These non-core divestments, when coupled with the sale of Glass Mountain pipeline in December and our $300 million preferred equity offering in January, raised approximately $800 million to date. In April, we made the final HFOTCO payment of $580 million and were able to capture an early payment discount of approximately $20 million.

We've also been busy finalizing our plans to improve our asset position in the DJ Basin. On Monday we announced an exciting new project to convert a portion of the White Cliffs pipeline system to NGL service, which is described in more detail on Slide 5. This project is backstopped by a long-term contract with DCP to provide a much-needed market solutions serving growth in the DJ Basin. The 10-year agreement provides DCP with 50,000 barrels per day of NGL transportation capacity on the converted pipeline. The commercial agreement includes firm volume commitments that are consistent with our drive to have more secure cash flows. We will move the NGLs from the DJ to Cushing on the converted White Cliffs line and then interconnect with Southern Hills pipeline with final delivery into Mont Belvieu.

White Cliffs and Southern Hills pipeline will soon conduct a joint open season to attract additional shipper commitments in the basin. Ship is removed product under our published joint tariff. The project is estimated to cost between $60 million and $66 million, of which SemGroup will fund 51% with minimal spending in 2018. The project is estimated to be constructed at less than a four times EBITDA multiple based solely on the committed portion of DCP's capacity lease.

As an Operator in White Cliffs, we will convert one of the existing 12-inch crude lines, taking it out of service late first quarter 2019 and bringing it into NGL service during the fourth quarter 2019. The pipeline will have an initial capacity of 90,000 barrels per day and will be expandable up to 120,000 barrels per day. This repurposing of White Cliffs is an excellent way to diversify the pipeline's capabilities beyond crude and de-risk its profile. At the same time, we have a clear path to retaining crude volumes.

Now I will hand the call over to Bob.

Bob Fitzgerald
Thanks, Carlin. Turning to first quarter results on Slide 6, SemGroup reported a debt net loss of $33 million compared to net income of $2.6 million in the prior quarter. The decrease from the prior quarter is primarily due to a $27 million reduction in net gains and losses related to divestitures and impairments. SemGroup's first quarter 2018 Adjusted EBITDA was $93 million compared to $112 million in the fourth quarter 2017. Excluding nonoperating or nonrecurring items in both quarters, our Adjusted EBITDA is essentially flat at just under $100 million per quarter. These items include about an $8.5 million of annual deficiency payments recorded in the fourth quarter, the absence of Glass Mountain pipeline earnings following its sale in December of $4 million, and the $4.2 million write-off this quarter of an insurance claim receivable at HFOTCO.

Moving to Slide 7 for a look at our first quarter results by segment, you'll remember that starting in the fourth quarter 2017 we revised our segment reporting performance measure from Adjusted EBITDA to segment profit. Overall, segment profit is down sequentially for the same reasons mentioned earlier.

Crude Transportation's first quarter segment profit was $34 million compared to $42 million during the previous quarter. The decrease was driven by the absence of Glass Mountain pipeline earnings, as well as lower field services volumes due primarily to weather-related issues. White Cliffs pipeline volumes increased 16% over the prior quarter due to the success of our temporary tariff which went into effect last December. Group facilities reported first quarter profit of $9 million compared to $14 million last quarter, which benefited from a $5 million deficiency payment.

Crude Supply and Logistics reported a current quarter segment loss of $6.6 million, down from the prior quarter due to the impact of adverse timing issues, the absence of Contango earnings, and narrow basin differentials.

Looking forward, we're seeing margin improvements in several key areas and still expect to post full-year segment results consistent with our initial guidance of negative $10 million to $15 million.

HFOTCO posted first quarter profit of $31 million compared to $33 million during the fourth quarter of 2017. Operationally, HFOTCO's results improved slightly quarter-over-quarter on higher volumes, but this was offset by the write-off of a claim receivable. We continue to forecast completion of Ship Dock 5 and the related crude storage facilities by midyear, contributing to a growing second half cash flow contribution.

Turning to the SemGas segment, first quarter 2018 profit was a little over $14 million compared with the previous quarter. Growing STACK volumes more than offset the decline in Mississippi Lime volumes. We expect Mississippi Lime production to have bottomed out during the first quarter, as Moch Resources started drilling on their newly acquired acreage in April.

SemCAMS segment profit was $22 million for the quarter, relatively flat compared to prior quarter. The slight decrease was due to the absence of $3.5 million in producer recoveries last quarter, partially offset by the recognition of Take-or-Pay deficiency revenues this quarter. The plant KA turnaround began in April and we expect to have the plant back up later this week.

Moving to Slide 8, our leverage and liquidity position, during the quarter we completed a preferred equity offering of $350 million. This offering was executed at attractive terms and contributed to our overall capital raise initiative. We ended the quarter with a total consolidated net leverage ratio of 4.1 times and consolidated available liquidity of nearly $1.3 billion. On a pro forma basis, factoring in the SemLogistics sale and the final HFOTCO payment, pro forma consolidated net leverage would have been 5.2 times at the end of the first quarter.

We continue to target consolidate leverage of five times or lower which we expect to achieve by the end of 2019 and continue to evaluate numerous capital funding options. However, we do not have any plans to issue common equity in 2018.

I will now turn the call over to Carlin for some closing remarks.

Carlin Connor
Thanks, Bob. As promised, we're delivering on our strategy this year. The transformation of our portfolio is largely complete. Our capital raised initiatives have been successful and we've made the final payment on HFOTCO. Our portfolio it now supported by significantly more Take-or-Pay business. It is providing strong coverage to pay attractive dividends for Shareholders while naturally de-levering our balance sheet.

We are also building the means to continue to invest in high-value organic growth in our core areas. We have a clear path to year-over-year growth with projects coming online this year and more in 2019. We continue to capture new opportunities as well, like the White Cliffs pipeline repurposing. We're very excited to partner with DCP on the growing NGL market in the DJ Basin, and at the same time significantly de-risk one of our core assets. It is another great example of how we are leveraging our footprint to serve customers in a changing market while at the same time maximizing the utilization of our assets.

Finally, I would like to recognize our Crude Team for winning PennWell's Oil & Gas Project of The Year for the engineering and construction of our Maurepas pipeline. In our drive success culture, we emphasize excellence, safety, environmental respect, and value creation. All of these elements were found in the execution of Maurepas, and are expected in all projects and operations across our organization.

With that, I'd like to thank you for your time this morning and now turn the call over for questions.

QUESTIONS AND ANSWERS

Operator
Thank you, Sir. We will now begin the question-and-answer session. To ask a question you may press star, then one on your touchtone phone. If you're using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you'd like to withdraw your question, please press star, then two. Again, it is star, then one to ask a question. At this time, we will just pause momentarily to assemble our roster.

The first question we have will come from Elvira Scotto with RBC Capital Markets. Please go ahead.

Elvira Scotto
Hey. Good morning, everyone. I'd like to start with the conversion of one of the White Cliffs lines to NGL service. My first question is, how does that cash flow ramp from DCP's 50,000 barrel a day commitment? What's sort of that timeline for that ramp period?

Carlin Connor
Hello, Elvira. This is Carlin. We'll be taking the pipeline out of service first quarter 2019 and then we'll be coming back into service fourth quarter '19 with NGL. The ramping of the cash flows, Dave?

David Minielly
Yes. I mean, ramping of the cash flows will start right as the pipeline is put in service, and commissions start in the fourth quarter of '19. At the Take-or-Pay commitments.

Elvira Scotto
So, you'll start receiving that full cash flow on day one?

Carlin Connor
The contracted portion.

David Minielly
The contracted portion, correct.

Elvira Scotto
Right. Okay. Great. Then can you just run through your thought process on your margin

opportunity for converting the line versus keeping the line in Crude Service? I mean, I think the incentive crude rates are about $1.75 per barrel. I think converting to NGL service, it seems like the committed rates may be a little below that, but just can you talk about the margin opportunity there and just the thought process you went through?

Carlin Connor
Well, we do not look at projects solely on margins. We also look at projects on risk. What we really liked about the conversion was the 10-year contract and the diversification away from being only a crude takeaway project. We also, as you probably picked up when running your models, we have—the project can expand out to 120,000 barrels per day, so even on a margin basis, we think we can do very well in a full service with NGL and, most importantly, I think we've reduced a tremendous amount of contract risk that we were facing in 2019 and 2020.

Elvira Scotto
Okay. Great. Then just kind of switching to the S&L business, the first quarter was a loss of $6.6 million, you guys are seeing margin improvement and you maintain that guidance. Can you provide a little more detail around that and what gives you confidence that you can hit those numbers? Have you locked in some margins?

Bob Fitzgerald
We haven't locked in the margins, but we are seeing strengthening in the margins in a couple of our key areas, notably in the North Dakota market where we're seeing some strengthening there. Also, in and around the Oklahoma-Kansas Cushing's footprint, we're seeing some strength in it going forward. So, given where we're at and what we've seen so far this quarter, we have a fair amount of confidence that we'll see that improvement and we won't have some of the timing issues that we saw also in the first quarter.

Elvira Scotto
Okay. Great. Then just a last one for me for now, on crude oil storage, I don't think you have significant contract rollovers this year, but I believe you have a fair amount next year. Do you expect much impact to your rates given the shape of the crude oil curve?

Carlin Connor
This is Carlin. As we sit here today, we continue to see some support for that low $0.30 renewal. Our tanks in Cushing are very operationally driven tanks and we feel pretty confident that we'll be able to do some renewals next year in that range.

Elvira Scotto
Great. Thanks a lot.

Operator
Next, we have Justin Jenkins of Raymond James.

Justin Jenkins
Great. Thanks. Good morning, everyone. I guess real quick, following up on Elvira's stuff on White Cliffs, can you remind us what the capacity is going to be just on the standalone crude oil line?

Carlin Connor
Well, as you know, we have two 12-inch pipelines and we're taking one out for NGL, so that leaves us the 12-inch. Currently today, depending on the gravity of crude oil, it really drives how

much you can push through. We have a plan in place to further debottleneck some of the receipt infrastructure for that White Cliffs crude pipeline and we think we have the ability to basically handle the same amount of crude we're handling today on that one pipeline.

Justin Jenkins
Perfect. Appreciate that, Carlin. Then it looks like SemGas ramped up pretty nicely quarter-over-quarter. I think you mentioned that in the prepared remarks, but is that almost exclusively due to the new pipeline servicing the STACK?

Bob Fitzgerald
In the first quarter that was all driven by the STACK volumes coming online and we do see growth in the future quarters coming from both the STACK as well as some improvement in Mississippi Lime.

Justin Jenkins
Perfect. Then last one for me, any updates or thoughts on potentially extending or even bringing in a partner to the Maurepas pipeline?

Carlin Connor:
This is Carlin again. We continue to pursue refiners that we believe are interested in pipeline supplied crude from St. James. We believe a major triggering event for them to take space will be the Capline reversal, at least that's for the next expansion. As you know, that is a project that is continuing to be going through an open season and, if successful, probably will not be converted until I think 2021 and 2022. So, we have some time. We still see an opportunity there. We're not too worked up about it. We think it's an obvious solution for some of the refiners in that area, and we'll just continue to collect on the Shell contract in the meantime.

Justin Jenkins
Perfect. Appreciate the time. Thanks, guys.

Operator
Next we have Craig Shere with Tuohy Brothers.

Craig Shere
Good morning and congratulations on the successful White Cliffs repurposing. Speaking of White Cliffs, Carlin, you had alluded to reducing risk of the contracts rolling over the next couple of years, and obviously you're having the size of your capacity materially reducing the oversupply in the market. Do you think by the end of '19 that walk-up tariffs on the crude side could move closer to the original $3.25 to $4.65 levels from the current $1.75 incentivized rates?

Carlin Connor
Well, it probably wouldn't be smart for me to signal where we think those tariffs are going; it's still a competitive environment. I think you have to look at the production in the Basin. It is ramping up. We see Anadarko and Noble both increasing their capital allocation towards the Basin and so we see production coming online that I think is going to be supportive of tariffs maybe moving north. In the meantime, we continue to just block and tackle and serve our customers and hit our forecast on those volumes.

I think clearly taking one pipe out of the mix does a couple of things. It reduces the takeaway capacity that's going to be fighting for whatever production that is needed to leave, but then for us, just as important, is the fact that we've diversified ourselves away from that situation and are really quite happy with now being a supplier of services to the growing NGL part of that development.

Craig Shere
Understood. I was really happy to hear about no plans for 2018 equity issuance, given the wind-down in CapEx and ramping EBITDA. Do you feel comfortable that there's unlikely to be any equity issuance in '19 to maintain your five times coverage, or do you really need to kind of see how those tariffs kind of shake out and out of the DJ?

Carlin Connor
Well, of course, the base business and its earning potential will drive some of those decisions going forward, but as we sit here today, we feel very comfortable with the plan we have and without common equity in that plan. Of course, the caveat to that would be any big projects, any new projects which would be additive to the story may change that calculus. But as we sit here today, we feel pretty confident in saying that no common equity in the foreseeable future with the base plan.

Craig Shere
Understood. As far as additional opportunities, I think you already addressed Maurepas prospects for additional bolt-ons for HFOTCO. Were you guys still trying to upsize Smoke Lake?

Carlin Connor
We continue to look at the demand around that plant, as well as our other plants in Canada. We have, I think, good development opportunities in Canada, not only around Smoke Lake but also around Wapiti and Pipestone area.

Craig Shere
Okay. Do you think in coming quarters we might see some additional tens of millions of dollars of kind of mid-single-digit accretive growth projects that can be announced?

Carlin Connor
Well, as we said in our scripted remarks, we're very happy with our footprint now and it's a more focused footprint and we think it's high growth areas that we're serving, and we have great assets. We hope to leverage that in developing high return on capital, low multiple organic projects, so, yes, hopefully we'll see more of that coming.

Craig Shere
Great. Last question for me, just kind of seconding, nice to see the SemGas volume uptick. Obviously, there's a nice turnaround with the connection of (inaudible 23:20) STACK pipeline, but you're going to have to average close to 400 a day through the rest of the year to meet the low-end of 2018 guidance. Are you still comfortable with that?

Carlin Connor
Yes. Right now, we have one rig in our plan, but we see the back half of the year. Fortunately, we see Mok Resources who bought the Chesapeake acreage. They're moving in rigs that be probably will see some impact to that maybe—I'm looking at Bob—in the second quarter, potentially. We'll hopefully see Mississippi Lime volume growth over the next six to nine months.

Bob Fitzgerald
I'll just add, we expect to see some of those volumes starting up in the second quarter for Mississippi Lime, but growing towards the end of the year when we start to see more activity.

But we also see growing volumes coming in through the STACK as well, so between the two of them we're still very confident in our forecasting guidance on the volumes.

Craig Shere
Great. Thank you.

Operator
Next, we have Michael Blum with Wells Fargo.

Michael Blum
Hi. Good morning. Question on the delinquent NGL conversion project. I guess the question is really just you've got the 50,000 a day coming in from DCP; do you expect further commitments during the open season? Do you have other kind of indications that you know about that will probably stand out? In other words, how much of the 90,000 do you think actually gets committed?

David Minielly
Hi, Michael. This is David. Yes. I mean, we certainly plan to go out to an open season and we do think that we will have some success with that, and we have had some preliminary discussions and feel good about where we're at as we go into the open season.

Michael Blum
Okay. Great. Then second question, just on SemGas, obviously you're seeing a bit of an improvement there; you have a new producer behind one of the systems. Is there any thought now of looking at a sale of SemGas or is that really off the table at this point?

Carlin Connor
Well, as you know, we went into that process—this is Carlin, by the way, Michael—we went into that process and didn't get the value that we felt was warranted for that asset. Some of the arguments we made to potential buyers back then, it's happening, right, and we're seeing more activity around the lime with Mok coming in and we're also seeing our STACK play continue to develop. So, we're extremely confident in the plan the Gas Team has put together, and we're a public company, so we have to take into consideration the value of that asset relative to our plan. But, as I sit here today, we're not running an active process and we will continue to operate and develop it going forward.

Michael Blum
Great. Thank you very much.

Operator
Next, we have Jerren Holder of Goldman Sachs.

Jerren Holder
Thanks. Good morning. Can you guys discuss your White Cliffs re-contracting strategies to when those volumes do come up for renewal in 2020? How are you guys thinking about it at this point?

David Minielly
Well, certainly what we want to do is put ourselves in the best position to re-contract the pipeline. I think we've gone a long way with de-risking the pipeline with just what we've done here with DCP and we'll be certainly moving with not only our anchor shippers but our other

potential shippers to work to re-contract that pipeline moving forward.

Jerren Holder
So we should think about more focus on a longer-term contract, lower margin as opposed to pushing for a higher margin?

David Minielly
Yes. I think we're going to look at whatever makes sense for both parties.

Jerren Holder:
Okay. In terms of the NGL pipeline, any initial thoughts in terms of extending that deeper into the Rockies or the Bakken?

David Minielly
No. I mean, not at this point. I mean, we're focused on just working with DCP out of Weld County.

Jerren Holder
Okay. Thank you.

CONCLUSION

Operator
Well, this concludes our question-and-answer session. I would now like to turn the conference call back over to Mr. Carlin Conner for any closing remarks. Sir?

Carlin Connor
Thank you all very much for joining us today. We appreciate your continued interest and support. Have a great day.

Operator
We thank you, Sir and to the rest of the Management Team also for your time today. Again, the conference call has now concluded. At this time, you may disconnect your lines, everyone. Thank you again. Take care and have a great day.