Company Name: Marathon Petroleum Corp
Company Ticker: MPC US
Date: 2016-04-28
Event Description: Q1 2016 Earnings Call

Market Cap: 21,748.43
Current PX: 41.095
YTD Change($): -10.745
YTD Change(%): -20.727

Bloomberg Estimates - EPS
Current Quarter: 1.483
Current Year: 3.853
Bloomberg Estimates - Sales
Current Quarter: 16924.000
Current Year: 63113.571

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Q1 2016 Earnings Call

Company Participants

- Lisa Wilson
- Gary R. Heminger
- Timothy T. Griffith
- Raymond L. Brooks
- Donald C. Templin
- Anthony R. Kenney
- C. Michael Palmer

Other Participants

- Evan Calio
- Edward George Westlake
- Brad Heffern
- Neil Mehta
- Douglas Terreson
- Chi Chow
- Paul Sankey
- Phil M. Gresh

MANAGEMENT DISCUSSION SECTION

Operator

Welcome to the First Quarter 2016 Earnings Call for Marathon Petroleum Corporation. My name is Katie and I will be your operator for today's call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. Please note that this conference is being recorded. I now turn the call over to Lisa Wilson, Director of Investor Relations. Miss Wilson, please go ahead.

Lisa Wilson

Thank you, Katie. Welcome to Marathon Petroleum Corporation's First Quarter 2016 Earnings Webcast and Conference Call. The synchronized slides that accompany this call can be found on our website at MarathonPetroleum.com under the Investor Center tab.

On the call today are Gary Heminger, Chairman, President and CEO; Tim Griffith, Senior Vice President and Chief Finance Officer; and other members of the MPC executive team. We invite you to read the Safe Harbor statements on slide two. It's a reminder that we will be making forward-looking statements during the call and during the question-and-answer session. Actual results may differ materially from what we expect today. Factors that could cause actual results to differ are included there as well as in our filings with the SEC.

Now, I will turn the call over to Gary Heminger for opening remarks and highlights.

Gary R. Heminger

Thank you, Lisa. And if you please turn to slide three. Earlier today, we reported first quarter earnings of $1 million, which included charges of $0.06 per diluted share related to a goodwill impairment recorded by our consolidated subsidiary, MPLX, and a lower cost or market inventory charge. The lower earnings this quarter were largely attributable to weak crack spreads, especially in the first two months of the quarter, as well as high turnaround activity.

We completed significant turnaround activity at the Robinson and Galveston Bay refineries, ahead of schedule and under budget. As part of these turnarounds, we commissioned the light crude upgrade project at our Robinson, Illinois, refinery to increase light crude processing and overall crude capacity. This upgrade will improve the refinery's flexibility to optimize its crude slate and product yields in a variety of market conditions.

We also implemented additional process improvements and synergy projects at our Galveston Bay refinery in Texas City in an ongoing initiative to enhance margins at that complex. Even with the challenging market conditions in the first two months of the year, we remain encouraged by the strengthening of frac spreads late in the quarter, as gasoline inventories declined and refiners responded to market conditions.

In addition, we're also encouraged by the supply and price competitiveness of sour crude oil as we enter into the summer asphalt season. Heavy Canadian crude oil is still growing, and it's attractive for both our Midwest and U.S. Gulf Coast refineries. Medium sour crude also looks very promising. U.S. Gulf of Mexico sour production is growing, and we are seeing more foreign sour cargo opportunities than we have for some time, as OPEC competes for market share.

MPC can capitalize on these opportunities, since we can process even the very heavy high-asset and high-sulfur crude oil at both our Galveston Bay and Garyville refineries. We are also well- positioned to take advantage of the expected strength in gasoline demand, given our high gasoline yield and pure leading alkylation and reforming capacity.

We reported strong financial results from our Speedway and Midstream segments, which underscored the value of our ongoing strategic objective to grow the more stable cash flow segments of our business. Speedway continued its exceptional performance in the first quarter. In addition to higher light product sales volume, Speedway's merchandise margin increased in the quarter, reflecting progress toward our goal to generate two-thirds of our profitability from merchandise sales. This approximates the earnings contributions of merchandise sales prior to the acquisition of East Coast and Southeast locations at the end of September of 2014.

We are focusing on the significant marketing enhancement opportunities at our recently converted retail locations, further optimizing the value of these assets and building out the earnings power of the entire Speedway business. We are also pleased with our Midstream segment, including MPLX's financial and operational results this quarter. MPLX completed several key operational projects this quarter, while generating strong, distributable cash flow for the partnership. Despite the challenging environment from midstream MLPs, we remain enthusiastic about the quality of the partnership's gathering and processing assets and the diversified customer base they support, particularly at the prolific Marcellus and Utica Shale regions. We believe the partnership is very well positioned to take advantage of the continued volume growth as NGL prices improve.

Over one-third of the total U.S. gas rigs currently in service are in the rich and dry gas areas where MPLX operates and enjoys acreage dedications. Over the last year, the partnership commissioned almost 1.5 billion cubic feet per day of processing capacity to support its customers' growth plans. This year, MPLX anticipates its processing facilities in the Marcellus and Utica to average approximately 80% utilization, as it expects its overall processed gas volumes from this region to increase by approximately 15%, a notable increase in light of the current commodity environment.

At the end of the quarter, we completed the contribution of our Inland Marine business to MPLX at a supportive valuation in exchange for additional MPLX equity. Our near-term support of the partnership in this challenging environment for MLPs is intended to contribute to the long-term value MPLX creates for our shareholders through our limited partner and general partner distributions, dropdown proceeds and the overall value of our equity interest in MPLX.

We continue to believe the addition of the MarkWest business will be a powerful value driver for MPC and its shareholders over the long term. We will continue our disciplined investment strategy across all segments of the business, balancing value-enhancing investments with returning capital to shareholders over the long term. We also remain committed to strong liquidity and an investment-grade credit profile through all cycles.

In the first quarter, we returned $244 million of capital to shareholders through dividends and share repurchases and announced a significant reduction of nearly 30% of our 2016 capital expenditure plan. MPLX announced yesterday its $1 billion private placement of convertible preferred securities with third-party investors. The partnership elected to take advantage of very strong investor interest in convertible preferred securities by privately placing $1 billion with a select group of investors. Originally contemplated as a transaction with MPC, the private placement provides an attractive funding source for the partnership, while preserving MPC's capital and financial flexibility.

The combination of some opportunistic ATM issuances in the first quarter, combined with this private placement, provides for the partnership's anticipated funding needs for the remainder of 2016 and into 2017, therefore enabling MPLX to continue its execution of attractive organic growth projects that will contribute to distributable cash flow and long-term value for the partnership. The transaction is expected to close in early May.

MPC is well-positioned to benefit as market conditions improve. In addition to our financial strength, we have a sustained competitive advantage from our refining system, premier retail assets and an enhanced logistics and storage network, with the addition of the MarkWest assets to MPLX. We remain bullish about the prospects for the enterprise as we go forward this year and beyond.

And with that, let me turn the call over to Tim, who will walk through the financial results for the quarter.

Timothy T. Griffith

Thanks, Gary. Slide four provides earnings on both an absolute and per share basis. MPC had $1 million of earnings for the first quarter of 2016 compared to $891 million in the first quarter of last year. As Gary mentioned, first quarter earnings included charges of $0.06 per diluted share to impair a portion of the goodwill recorded in connection with the acquisition of MarkWest, as well as the lower cost or market inventory charge. The impact of the goodwill impairment charge on diluted earnings per share only includes the impact of our then 21% equity interest in MPLX.

The chart on slide five shows by segment the changes in earnings from the first quarter last year. The primary drivers for the change were the $1.4 billion decrease in refining and marketing income and the $129 million goodwill impairment charge, partially offset by lower income taxes and higher income from our Midstream segment, which reflects the first full quarter of results from the combination of MPLX and MarkWest.

Turning to slide six, our Refining and Marketing segment reported a $62 million loss in the first quarter of 2016, compared with income of operations of $1.3 billion in the same quarter last year. The decrease was primarily due to weaker crack spreads in both Chicago and Gulf Coast, higher cost related to the turnaround activity at Robinson and Galveston Bay, and a narrower LLS-WTI differential. In addition, we had less favorable crude oil and feedstock acquisition costs relative to our market indicators, resulting from narrow crude differentials, which is included in the $199 million of other gross margin negative impact highlighted on the slide.

The lower blended crack spread had a negative impact on earnings of approximately $869 million. The blended crack spread was over $5 per barrel lower at $4.62 per barrel in the first quarter of 2016 compared to $9.69 per barrel for the same period last year. The LLS-WTI differential narrowed $2.57 per barrel from $4.23 per barrel in the first quarter of 2015 to $1.66 per barrel in the first quarter of 2016. This had an approximately $81 million negative impact on earnings based on the WTI-linked crudes in our slate.

The $231 million year-over-year increase in direct operating costs related primarily to higher turnaround activity during the first quarter. Turnaround and major maintenance costs increased $1.64 per barrel or about $260 million compared to the first quarter of 2015. The higher turnaround activity also impacted throughputs, which were 78,000 barrels per day lower than the first quarter last year. Partially offsetting these negative impacts was favorable market structure

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during the quarter. This contango effect is reflected in the $117 million favorable difference on the walks and relates to the difference between the prompt crude prices we use for market metrics and the actual crude acquisition costs.

Moving forward to the other segments, slide seven provides the Speedway segment earnings walk compared to the first quarter of last year. Speedway's income from operations was consistent with last year's first quarter at about $167 million. Last year was a record first quarter for our Speedway business, even before including the retail assets acquired along the East Coast and Southeast. So we are very pleased to see the continuing strong performance in the first quarter of this year.

Gasoline and distillate margins were about $0.03 lower than the first quarter of 2015. This was offset by higher merchandise margins, higher gasoline and distillate sales volumes and a $24 million gain from the sale of a retail location in the quarter. Gasoline and distillate margins averaged $0.168 in the first quarter of 2016 compared to $0.197 in the first quarter of 2015. This decline reflects some the stickiness in price at the retail level, when crude prices move rapidly, as we experienced later in the first quarter. On a same-store basis, gasoline sales volumes increased 1% over the same period last year.

Merchandise margins were $19 million higher than the first quarter of 2015, due to overall higher merchandise sales and the higher margins realized on those sales. Merchandise sales in the quarter excluding cigarettes increased 3.1% on a same-store, year-over-year basis, reflecting some of the progress we're making in merchandising across the entire business. In April, we've seen an increase in demand with approximately 1.4% increase in same-store gasoline sales volumes compared to last April.

Slide eight provides changes in the Midstream segment income versus the first quarter last year. Please note that we changed our operating segment presentation this quarter in connection with the contribution of our Inland Marine business to MPLX. Previously, the Inland Marine business and our investment in Crowley Ocean Partners were included in our Refining and Marketing segment. First quarter and going forward, we include all of the marine related businesses in the Midstream segment.

The $90 million shown here for the first quarter of 2015 has also been adjusted for comparability between periods. The $77 million increase quarter-over-quarter was primarily due to the combination with MarkWest at the end of last year, which contributed $72 million of incremental segment income to the first quarter. The remaining increase of $5 million was primarily due to an increase in income from our equity affiliates and higher transportation revenues, partially offset by higher operating expenses versus last year.

Slide nine presents the significant elements of changes in our consolidated cash position for the first quarter. Cash at the end of the first quarter was $308 million. Core operating cash flow was a $604 million source of cash. The $277 million use of working capital noted on the slide primarily relates to a decrease in accounts payable and accrued liabilities, partially offset by decreases in accounts receivable and inventory. The decreases in these accounts were primarily due to the drop in crude oil and refined product prices during the quarter versus the fourth quarter of 2015, which led to the net use of cash, given the generally longer terms on the crude purchases.

Net debt repayments resulted in the $372 million use of cash during the quarter. This net reduction resulted from some opportunistic ATM issuances at MPLX in the quarter, generating equity proceeds of about $315 million. These funds were used to pay down a portion of MPLX's then outstanding revolver balance. The equity proceeds are also reflected as part of the $281 million of other cash flows in the quarter shown on the walk.

We continued delivering on our commitment to returning cash to our shareholders. We repurchased 75 million of shares and paid $169 million of dividends in the first quarter. While the share repurchase activity may vary based on the needs and the cash flow characteristics of the business in any particular period, our commitment to continue returning capital remains a fundamental element of our strategy and an important part of the value proposition for our investors.

Share count at the end of the quarter was approximately 530 million shares, reflecting repurchasing activity of about $7.3 billion, retiring about 28% of the then outstanding shares since the spin. In addition, the $0.32 per share dividend announcement by our board yesterday contributes to the 28% compound annual growth rates in our dividend since the

spin.

Slide 10 provides an overview of our capitalization and financial profile at the end of the quarter. We had $11.6 billion of total consolidated debt, including $4.7 billion of debt at MPLX. Total consolidated debt-to-book capitalization was about 37% and represented a manageable 2.1 times last 12 months adjusted EBITDA of just over – close to $5.6 billion. Operating cash flow for the quarter was $604 million before reflecting the $277 million use of cash for working capital in the quarter.

Slide 11 provides updated outlook information on key operating metrics for MPC for the second quarter this year. We are expecting second quarter throughput volumes to be down slightly compared to second quarter 2015 due to more planned maintenance in the quarter. Total direct operating costs are expected to be about $6.75 per barrel on total throughputs of 1.875 million barrels per day, which reflects the impact of higher turnaround activity. Our projected second quarter corporate and other unallocated items will be about $75 million.

With that, let me turn the call back over to Lisa.

Lisa Wilson

Thank you, Tim. As we open the call for your questions, we ask that you limit yourself to one question plus a follow-up. You may re-prompt for additional questions as time permits. With that, we will now open the call to questions. Katie?

Q&A

Operator

Thank you. We will now begin the question-and-answer session. [Operator Instructions] And our first question comes from Evan Calio from Morgan Stanley. Please go ahead.

<Q - Evan Calio>: Hey. Good morning, guys.

<A - Gary R. Heminger>: Good morning, Evan.

<A - Timothy T. Griffith>: Good morning, Evan.

<Q - Evan Calio>: Gary, my first question, I know you've been constructive on the refining margin outlook and curious you've got any updates there, particularly on Mid-con for the balance of the year, and then diesel? And somewhat related, I mean is your system currently at a maximum gasoline versus distillate yield?

<A - Gary R. Heminger>: I will let Ray talk about whether or not we're maximum gasoline, and diesel, I believe we are. But I'll let Ray Brooks talk about this. But let me speak to the overall Refining segment first within the industry, Evan. I guess I step back and look at it from an inventory position and this week's inventories for the first time, you see – and as I said in my script, I'm very pleased how the industry really has, I think, [indiscernible] (20:41) into balance. If you look at Pad 2, we are now spot on the same inventory levels as we were same time last year across Pad 2. The zero increase in gasoline and zero increase in ultra low sulfur diesel same periods. So I see that as very positive from where we were coming into the year. And I think that is really – should provide for strength, as we go into the gasoline season here at the end of Q2 and Q3.

Secondly, the Gulf Coast, while gasoline is still little bit up, there's still some turnarounds being finished in the Gulf Coast, and with the exports, I think the Gulf Coast can get into as we go into the summer grade gasoline, they will get into balance very quickly.

Lastly, the thing to really watch is the significant demand in asphalt across the country. And specifically, we're the largest manufacturer of asphalt in the refining system, and we're expecting a big asphalt season. And with our ability to

run a lot of sour crude oil, and what we've been seeing widen out the Mars spreads, and not only Mars, but if you look at several cargo opportunities, the sour crudes have really started to improve here in the second quarter. And we see that as very positive going into the balance of the second quarter and Q3.

So Ray, do you want to talk about max gas versus max diesel?

<A - Raymond L. Brooks>: Sure, Gary. We've completed all of our planned turnaround work, which was heavy in the first quarter, and we're back up running all our refineries at plan and at maximum. And our swing streams right now are directed to the gasoline stream. We have the capability to swing about 10% between gasoline to diesel, and that's all pointed to gasoline right now.

<Q - Evan Calio>: Great. That's very helpful. I'll keep my second question to the macro, just shift it to maybe your NGL outlook, where I know you've got significant direct exposure now, and there's [ph] what, six (23:00) new ethane crackers starting up in 2017 and 2018, it's almost 550,000 barrels a day of ethane demand exports in the third quarter. New propane exports have lowered the inventories there in line with the 5-year average. I mean any thoughts on the NGL outlook? Where things look to be improving? And as you think about sensitivities at the MPLX level, I'd appreciate it.

<A - Gary R. Heminger>: Sure. Don, do you want to it please?

<A - Donald C. Templin>: Sure. Evan, we do see improving pricing around NGLs, and we are optimistic and look favorably upon what's happening in the market. I think as it relates specifically to MPLX and our producer customers particularly in the Marcellus and Utica, absolute prices are important, but so is basis differential. And one of the challenges that they had particularly last summer was there were discounts from other markets. And so, our goal right now and the activities that we are undertaking are really focused on relieving the excess volumes in the Basin and allowing them to get to markets that are either more liquid or international markets.

So, our projects like rail to the East Coast, our projects like – and this will be a little bit longer-term, but a consideration of butane to alkylate, our efforts to load unit trains, are the positive news about ethane being shipped from the Basin over to the East Coast and making its way onto an international shipment. Those are all very positive in our view for the producer customers that we have a regular interaction with and that impact our business the most.

Operator

Thank you. And our next question comes from Ed Westlake from Credit Suisse. Please go ahead.

<Q - Edward George Westlake>: Hey. Good morning. And I guess a broader care question to begin with. Obviously you've made a lot of strategic changes and the quarter was quite tough because of maintenance and then some of the environment issues, you end up with $300 million of cash. Can you just talk about what you think are the main levers that you're going to pull to rebuild that cash balance? Clearly the summer may be good, but we're 7 years into a business cycle.

<A - Gary R. Heminger>: Ed, let me [indiscernible] (25:41) Tim will cover the balance sheet part, but let me talk about our strategy. And you're right, we have – since we spoke at your conference, in fact in February, we've rolled out our plans to reduce capital this year. We made a significant headway in reducing capital. We are making tremendous headway in self help and reducing operating expenses across all segments of our business, and that's going to happen, and we're going to continue to do good job of that.

But as we go forward to release any distraction within our businesses, as you recognized yesterday, we announced the convertible preferred, I thought it was important, the whole team thought it was important, that we get any distraction, as I outlined at your conference when I spoke, to get any distraction between MPC and MPLX off the table and we've accomplished that with the billion dollars of convertible preferreds that will take care of the capital budget of MPLX into 2017.

Secondly, as we continue to digest this acquisition, Tony and his team have done a tremendous job in being able to digest the Hess acquisition, is that we are going to get into a mode and into a rhythm of being able to harvest the cash from these businesses and build up that stockpile of cash, and clearly intend to get back into a more robust share repurchase program as we go down the road. Tim?

<A - Timothy T. Griffith>: Yeah. With regard to the cash balances, as you may recall for the Analyst Day last year, we highlighted the fact that as we go through our core liquidity analysis and how much we need to support the business and protect for all the potential contingencies, there's a number of elements of that analysis that are a function of absolute crude prices, and the amount of core liquidity in the form of cash that we would keep at $100, $80, $60 oil is much higher than where it is at oil between $30 and $40 and $45. So, I think we are very comfortable at the $308 million number. We expect it's going to be anywhere between sort of zero and $0.5 billion. And with the committed capacity we have on the facilities and the sort of tools we have available to us with working capital and otherwise, I think we are very comfortable that if these absolute price levels that we're at appropriate levels to protect the business on a going forward basis. So there's – I don't think there's a notion, at least at these crude prices, that we necessarily need to build cash balances back. I think we're comfortable with where we're at. But as Gary said, a lot of opportunity for sort of earnings enhancement as we go forward. And we'll certainly have those levers available to us, so.

<Q - Edward George Westlake>: Okay. Second question, briefly. We'll ask your customers too in MarkWest how they're feeling. But are you – with oil having picked up a little bit and perhaps the fears of [indiscernible] (28:54) having receded, are you seeing any appetite to move forward any quicker on the upstream side of the MarkWest business?

<A - Gary R. Heminger>: Don?

<A - Donald C. Templin>: When you say move forward more quickly at, and I guess a little bit of clarification there?

<Q - Edward George Westlake>: Oh sorry, in terms of upstream customers wanting to get back in terms of activity and you know your just-in-time approach therefore needing to be speeded up a little bit.

<A - Donald C. Templin>: Okay. Yeah. I would say that we are monitoring and are in regular constant dialogue with our producer customers. I do think, obviously, the uptick in pricing is a very positive sign for them. Our capital budget that we have currently, the billion-dollar capital budget, I think is reflective of what we believe our current drilling plans for our customers, our producer customers. We obviously – we think there is some flex there. But I don't anticipate that there would be any significant movement from the number that we've publicly quoted.

<Q - Edward George Westlake>: Thank you.

Operator

And our next question comes from Brad Heffern from RBC Capital Markets. Please go ahead.

<Q - Brad Heffern>: Good morning, everyone.

<A - Gary R. Heminger>: Good morning, Brad.

<Q - Brad Heffern>: Gary, I guess previously you sort of touched on this. But I was hoping you could provide a little more color. I'm just curious the billion-dollar private placement, MPLX, how that frees up MPC. And the extent to which that reduces the support that maybe you thought you might have to provide to MPLX. And I'm thinking about specifically in the context of are we going to continue to see drops at very advantageous multiples for MPLX? And does it take some of the things like maybe IDR givebacks off the table?

<A - Gary R. Heminger>: Well, Brad, as you know, this is a – well, the MLP markets, the way they are today, it's a very dynamic situation. And it's – my answer has to be – address those dynamic cases. But certainly that is our expectation and our goal. As we did the drop of the Inland Marine system, it was at a very supportive drop and that was to be able to bridge MPLX over this time of challenge within the MLP market. MPLX has responded very, very well

since early February, and very pleased with the support and the improvement in the yield since that point in time.

Secondly, as I said in my prepared remarks, we thought it was very important to get this distraction at any overhang. Your question is spot on. In order to be able to be supportive to the MLP, what did the sponsor need to do? You're right. We dropped at a supportive multiple. We certainly don't expect to be dropping at those type of multiples going forward. And that was a bridge to get to where we are today. The same thing with the convertible preferred here. A very strong support for MPLX, but it takes that overhang and takes that distraction outside of MPC. And I believe as we go forward and look at any next drops, I think where we're situated now, we don't need to make anymore drops in 2016. We'll see how far out into 2017 before we would need to consider that. But our plan is as MPLX continues to improve and the yields continue to improve, which I'm confident they're going to, I think we're going to be able to cure this bridge or try to rebuild this bridge that we've been working on for the last three months or four months. Tim, you want to add anything to that?

<A - Timothy T. Griffith>: No. I would just reiterate the notion that, Brad, I think as we assess things, the convertible preferred provides a very efficient form of equity capital in a market that's been sort of volatile with elevated yields. Obviously, through the first quarter you saw common unit yields, which were extraordinarily high. And I think we were careful thinking about exactly what that could mean for the partnership on a long-term basis. So, with the amount of inventor interest around these securities and structuring of securities that we think makes sense that, as Gary said, provides a fantastic funding source. It takes 2016 off the table right into 2017.

And again, allows the focus on the business to be the continued growth in production, the organic projects and positions the partnership well. What this will mean for sponsor support, I think MPC stands ready in all of its varying forms and all the varying tools to step in to help support the partnership. When there's efficient capital available in the marketplace, we'll avail ourselves of that. And when that's not available, MPC will stand ready.

So we're pleased with getting this security done. As Gary said, there was some thought that MPC would provide this funding. MPC is still prepared to do so, but with the third-party money available, at terms that we found attractive, we thought that was a very good decision to move forward on.

<Q - Brad Heffern>: Okay. That's great color. Thanks for that. And then as my follow-up, I'd like to touch on Speedway. I was curious, you had a very good quarter in terms of growth, both in terms of volumes and in terms of merchandise sales. Is there a breakdown that you can provide of that for the legacy stores versus the Hess stores? I'm just curious if one side of that is driving the growth, or another, if it looks broadly similar across the portfolio.

<A - Gary R. Heminger>: Tony?

<A - Anthony R. Kenney>: Yeah. Brad, as we've moved through the integration of the two businesses and the focus on capturing synergies, we've stopped keeping track separately of the two businesses. And if you integrate all the functions of the business, I mean, the difficulty and the challenge to keep separate books on each is tremendous. So, we do not have a breakdown as to where the contributions are coming specifically.

<Q - Brad Heffern>: Okay. I'll leave it there. Thank you.

<A - Gary R. Heminger>: And Brad, I'll – Brad, let me just say, while we don't report individual segments from inside Speedway, Tony's team did a tremendous job and they now have re-ID'd all of the stores that were going through re-ID; way ahead of schedule on the synergies, way ahead of the schedule on the cash flow that we expected from this acquisition. But at the same time, their legacy assets performed very, very well. So, both sides I would say are running on all cylinders.

Operator

Thank you. And our next question comes from Paul Cheng from Barclays. Please go ahead.

<A - Gary R. Heminger>: Good morning, Paul.

Operator

Paul, if you're on mute, please un-mute yourself. Okay. We'll go to the next question. We have Neil Mehta on the line from Goldman Sachs. Please go ahead.

<Q - Neil Mehta>: Good morning, Gary.

<A - Gary R. Heminger>: Hi, Neil. How are you?

<Q - Neil Mehta>: Doing great here. So, Gary, want to touch – start off on retail and the right structure for it to be in. I know I've asked you this in the past. But what do you think about doing a retail spinoff? We just keep on seeing these marks out there of these retail C-Corps that are trading at 11 times, 12 times EBITDA. Does that make sense to monetize that asset?

<A - Gary R. Heminger>: Neil, and you're right, we have talked about this before. And as we look at that question, the answer has to be what – how do we think shareholders are valuing Speedway inside of MPC today, and therefore what is the delta? When I step back and really look at the delta that may be available, it certainly is not a number that I think gives credence to separating from the long-term strategic value that we see and having Speedway under the control of – or I should say not under the control, but inside the value system and inside the supply chain system of Marathon. It's always been one of our key value quotients with inside Marathon.

We've gone back and done a lot of work on some other transactions that have happened historically where companies spun off their retail and it appeared to be a pretty small bump in share value that can be eroded for many different reasons across the value chain. With all that said, we continue to look at it. We continue to analyze it. And I clearly, as you and I have spoken, I clearly see what the values that are being garnered inside the retail-only space. And, as always, we will continue to analyze this as we go down the road.

<Q - Neil Mehta>: I appreciate that. And then, Gary, just wanted your perspective on the crude markets on two different fronts, first, on your views on the differentials which continue to be tight, certainly for these inland differentials, but favorable on the light heavies and the medium sours. And then also just on the flat price, I know you were in Saudi Arabia a couple of weeks ago. Just any thoughts in terms of how you think OPEC acts through the balance of the year.

<A - Gary R. Heminger>: Right. Neil, as I spoke at your conference earlier in the year, I made a prediction that crude would be somewhere mid-$50s to mid-$60 by the end of the year. Brent topped $47 yesterday and looks to have a momentum going into today. And I still believe that crude will continue. And what's so important is that this inches up slowly. You do not want to spike on a very short-term basis, because I think the pain on a spike and then coming off that spike would have longer lasting effects on the marketplace. So you want to have a very slow, gradual move. And we're seeing that happening. And I still stand by our thoughts that the crude is going to continue to move. And I think that's beneficial across the entire energy sector. I think that it improves demand. If you get prices up and get people back working in the oil fields, I think it's important, again, for the entire worldwide global demand sector.

What I said in my remarks that – I'm glad you brought it up, is that we're starting to see the medium sours, the Mars, and some other cargos of Mars, medium, and other lookalike type barrels over the last month or so, we're starting to see that Mars spread, that medium sours spreads widen out. And I think that is very supportive to the industry, very supportive to those refiners who have the ability to run this medium sour crude and have the residual processing capability to handle [indiscernible] (41:14) and us being the largest manufacturer of asphalt in the country, it really helps us as we went to the asphalt season.

So I see crude continuing to move up for the balance of the year. I think it's very good for the medium and heavy sour refiners. And at the same time, we'll see what happens. I would expect that there's going to be another meeting of the OPEC numbers here in May. And at that time, I would expect to see these [indiscernible] (41:43) put into place. And if that happens, I think it'll continue to have some pressure on the [indiscernible] (41:56). But I think it will continue to benefit the medium sour players.

<**Q - Neil Mehta**>: Thanks, Gary.

Operator

And our next question comes from Doug Terreson from Evercore ISI. Please go ahead.

<**Q - Douglas Terreson**>: Hi, everybody.

<**A - Gary R. Heminger**>: Hi, Doug.

<**A - Timothy T. Griffith**>: Good morning, Doug.

<**Q - Douglas Terreson**>: Guys, distillate consumption has been weak so far this year, even considering weather effects. And so I wanted to see if you could provide some color on the commercial or on-road aspect of this demand that you're seeing this year, and whether or not improvement's likely later on in the year?

<**A - Gary R. Heminger**>: Tony, you want to cover that, please?

<**A - Anthony R. Kenney**>: Yeah. Distillate demand is down. It's just a combination of a number of things when we look at the overall numbers that we're looking at on diesel. The over-the-road component is soft. It's probably down in the neighborhood of about 2%. That's the large 18-wheel freight business. And then some of the regional business is down a little less than that, probably in the 1% area. And there're some other factors that are affecting overall distillate as well. Demand for U.S., for example, all the shale production that was shut in, there were some large consumption on distillate for that activity, which has obviously slowed down significantly.

<**Q - Douglas Terreson**>: The negative numbers like that historically correlate to a particular GDP figure? And if so, what would be the read through to the U.S. economy? Or do you guys not take it quite that far?

<**A - Gary R. Heminger**>: Doug, we've always – you've heard me say many times that over-the-road diesel is a, I think, a precursor to the overall economy.

<**Q - Douglas Terreson**>: Yeah.

<**A - Gary R. Heminger**>: Due to some of the – if you go back to the first quarter, we just analyzed our diesel demand, over-the-road diesel demand in the first quarter. And there were times across the Eastern Seaboard, we lost four days and five days of diesel demand because of severe weather. But...

<**Q - Douglas Terreson**>: Okay.

<**A - Gary R. Heminger**>: ...you have severe weather in different pockets of the country every year. But it seem to be more severe in the markets in which we operate today. But you're right. It has always historically been somewhat of a predictor of the overall economy. I look at some of our big, big customers on the diesel side and they're down probably 2% to 3% on a same-store basis on diesel demand. Yet in talking to a lot of the big trucking companies, the trucking companies' books, they say looks strong going into Q2 and for the summer months. So, it remains to be seen. I expect that diesel, I don't think for the year, we're going to be down 3%. But we may – as you know, we've had tremendous growth in diesel the last three years or four years. And I think some of that is just leveling off of what the demand has been. But we still – if you go back and look the last three years or four years, probably in total up around 10%. So, when you average this out, I think the market's still fairly good.

<**Q - Douglas Terreson**>: Okay. Let's just hope it's a soft patch. And then also, condition seem to be worsening in Venezuela, although it's unclear as to whether it's affected refined product flows based on the data that we've seen. And so, I want to see if you can provide insight into that market if you have any? And also the outlook for exports into the other possible export markets in the Atlantic Basin this year?

<**A - Gary R. Heminger**>: Sure. Mike Palmer handles all of our exports. So, Mike?

<A - C. Michael Palmer>: Yeah, Doug, I don't know that we have any particular insight into the troubles that Venezuela is seeing right now other than you do.

<Q - Douglas Terreson>: Okay.

<A - C. Michael Palmer>: I can tell you that it is difficult doing business with them. They have a lot of trouble trying to keep their upgraders, for example, going. And there hasn't been a lot of spot opportunities from Venezuela for us so far this year. So, that's certainly been difficult.

<Q - Douglas Terreson>: And just the overall thing on export markets? Yeah?

<A - Gary R. Heminger>: But the other thing, Doug, due to the export markets, our export markets, as Tim said in his remarks, of course, we had turnarounds in the first quarter that will have dropped our export volume. But we've come back strong, and the book looks good throughout the balance of the second quarter, up over 300,000 barrels per day in exports, which would suggest that Venezuela continues to struggle.

<Q - Douglas Terreson>: Okay. Great. Thanks a lot, everybody.

Operator

And our next question comes from Chi Chow from Tudor Pickering, Holt. Please go ahead.

<Q - Chi Chow>: Thanks. Good morning. Tim, it looks like you've repurchased around $75 million worth of shares in the quarter. Do you have a buyback target for the share?

<A - Timothy T. Griffith>: Well, Chi, I don't know that there's a hard target. Again, this is something that we'll sort of assess as we go. Obviously, a relatively weak quarter on the earnings side and the resulting cash flows. So I think you'd expect that the activity would have been lower in first quarter. But again, I think our focus is that, we've talked about 100% of free cash flow through cycle as the business generates cash and we're sort of carefully looking at capital. We expect that the activity is going to vary based on any given quarter. So, I wouldn't say that it's a hard target, but a continued long-term focus on making that an important part of our overall capital plans.

<Q - Chi Chow>: Okay. Thanks. You talked about the Robinson crude project in the release. I guess in addition to the crude slate flexibility, is there going to be a corresponding increase in the production capacity of light products out of the plant?

<A - Gary R. Heminger>: Ray?

<A - Raymond L. Brooks>: Yeah. With the Robinson turnaround, we completed the project to increase our light crude processing capability. And what that allow us to do is increase our handling of light crude by 30,000 barrels a day on a stream day basis, and at the same time, that gives us an overall increase in total crude throughput of about 20,000 barrels a day at that refinery. So significant improvement in that refinery.

<Q - Chi Chow>: Can you talk about the yield impact on the product side?

<A - Raymond L. Brooks>: Well, the yield impact would just basically follow our normal distribution of about between gasoline and diesel there. There wouldn't be a large change there, overall. One thing that we've done at that refinery too at the end of last year is we increased our hydrocracker capacity by about 10,000 barrels a day. So this plays along with that too.

<Q - Chi Chow>: I guess along those lines, it just seems like a lot of your current refining projects are focused on increasing ULSG production. And maybe this is back to Doug's question, with demands soft, how concerned are you about not only your increases on ULSG capacity, but just the broader global increase that we've seen over the last couple years? And how do you think that's going to play out on the cracks for diesel going forward here over next maybe even couple years?

<A - Gary R. Heminger>: Well, Chi, I would say that if you go back and look at our exports and look at the exports of the industry, still about 2 to 1 the global demand for diesel in the export market is what we're seeing. As I said earlier, we're back to all the diesel inventories across Pad 2 are balanced to where we were same period last year. Still up about seven million barrels of inventory in Pad 3. I think that can be cleared relatively easy as we go into the balance of the quarter. It's all going to come back to the question Doug had on, what is overall the over-the-road diesel demand equation? What happens to that in the near-term?

But as we see – and it's always been our position. We work very hard to always balance the diesel inventory in Pad 2. Pad 3 diesel inventory moves into Pad 1, moves into Pad 2 with the demand and any dislocation that may happen in the marketplace. But most importantly is the export demands for diesel.

Going back to Doug's question about Venezuela, and I think some other markets, we're continuing to see very strong demand. But we're also seeing improvement in gasoline demand at some of those export markets as well.

So, I understand your question, and I think the entire industry is continuing to assess and be very careful in any incremental diesel projects. But as you know, Chi, you don't do one of these projects overnight. They're long-term in the planning and long-term that generally these small upgrades or creep that you get in that supply commonly [indiscernible] (51:58) do have a major turnaround cycle plan. So, it's all going from back down to the balance of over-the-road demand and the balance of export demand going forward.

<Q - Chi Chow>: Yeah. I think we're all trying to figure out how that's going to go here. But thanks for the comments, Gary. Appreciate it.

Operator

And our next question comes from Paul Sankey from Wolfe Research. Please go ahead.

<Q - Paul Sankey>: Hi, guys. Gary, I had a question on...

<A - Gary R. Heminger>: Hey, Paul.

<Q - Paul Sankey>: Hi. I had a question on MPC that I want to come back to, but just briefly you mentioned somewhat casually in passing that you thought OPEC was going to meet in May and set a freeze. I don't know if that was kind of a throw-away comment or if you could just expand on that a little bit. And then I'd like to come back on the subject of CapEx, please. Thanks.

<A - Gary R. Heminger>: Well, no, it wasn't a throw-away comment. It's just – you read the same things I do. But I go back in history and look at how all these discussions play out. There's a tremendous amount of disappointment in the number of the OPEC members that this wasn't solved at the April 17 meeting. And the expectation is, there'll be another meeting here in May. And this goes along with my entire thesis of where we think crude prices are going to go. I, of course, don't have any inside knowledge of whether there will or will not be. But it certainly comes from my years of experience that I would expect that you'll see another meeting.

<Q - Paul Sankey>: Thanks for the clarification, Gary. Gary, you talked several times about the [audio dip] (53:42) CapEx. Could you talk about the outlook for MPC CapEx? Update us on the major projects that you're undertaking? And you mentioned that you're hoping to bring CapEx down further. And I think fairly strongly said that you're going to be prioritizing cash return to shareholders. So if you could give us the CapEx side of that balance outlook for MPC, I'd be grateful. Thank you.

<A - Gary R. Heminger>: Sure, Paul. And we stated in early February, we reduced the capital – that we've reduced the capital budget around $1 billion across both MPLX and MPC side of the equation. Our major projects, we are just embarking on very, very early stages of the Big Star project. And that goes out six years for the South Texas asset redevelopment project. So that goes out for a number of years, and we do not have any large projects or large capital expenditures in any individual projects all at once. We will continue to look at the capital.

Don has done a very good job in being able to squeeze capital out of the midstream side, as well as Tony has on the retail side to be very efficient and probably to backload some projects where we saw was opportunistic to reduce some of our capital spend. And we continue to look at that every month as we close our books.

My comments on capital deployment and getting back into share repurchases was that, as we went through this big acquisition at Speedway, now a year-and-a-half ago, and that's, as I said earlier, we're way ahead of schedule on the EBITDA that it is generating. And MPLX, I believe that we really have that going in the right direction that our plan is, as conditions improve, and Tim just answered the question from Chi on share repurchases, we do not have a month-by-month plan on what we're going to do. But our strategy – or I mean we know what we want to do, but not a plan on exactly any share buybacks and when that might happen. But we want to get back into a rhythm as we log into the next few years of being able to harvest from these businesses that we've acquired and really set this company up very, very strong across all three segments of the business that we will be able to harvest and get back into a strong share buyback program over the long term.

<Q - Paul Sankey>: Thanks.

<A - Gary R. Heminger>: Yep.

Operator

And our next question comes from Phil Gresh from JPMorgan. Go ahead.

<Q - Phil M. Gresh>: Hey. Good morning. My first question actually is just a follow-up to what Paul was just asking. At the – in the December Analyst Day, you had talked about something around a $3 billion growth investment target for 2017. And obviously, you've been [indiscernible] (57:12) on 2016. A decent chunk of that's at MPLX. But as you noted, there's some increased spend in refining as well. So, could you just talk about maybe the level of flex capital invested within that $3 billion growth number? And just are we thinking about the same level of flexibility as what you saw this year looking ahead?

<A - Gary R. Heminger>: Tim, you want to cover that?

<A - Timothy T. Griffith>: Sure. Phil, obviously, as Gary indicated, we have and will continue to look very carefully at capital. There's a certain portion of the capital budget at MPC that is, what we'll probably describe it as a little bit more maintenance in nature, a little bit more sort of regulatory pieces. But for all the pieces, and certainly when we think about some of the investments in Speedway, in T&L, obviously the Star project we announced, we've sort of extended that and pushed it out. There are elements and good pockets within the capital budget that probably would continue to have flex capability to them, depending on how things go. I mean there are a number of things that we can sort of set up and pursue more rapidly if conditions improve and we see the earnings and cash flows that could support the investments there, or frankly, defer further, defer into 2017 and potentially beyond as the needs of the business sort of migrate over time. So there is, I think, with any refining business, you'll see an element of capital that maybe has a little bit less flexibility to it. But we still have significant elements that we'll continue to look at over the course of this year and into next in terms of where we may want to make some adjustments.

<A - Donald C. Templin>: And Phil, this is Don. On the MPLX side, or Midstream side, our budget this year has been reduced or we're going to manage it down to something closer to $1 billion. Of that, probably 60% or so was G&P and 40% was logistics and storage. And in that 40% were a couple projects that were underway that we are going to complete this year, that won't continue on into next year, to give us some flexibility. So, for example, that Cornerstone project will be completed by the – we're projecting that it will be completed by the fourth quarter of this year. And that was roughly half of the budget that we had for the L&S business.

On the G&P side of the business, this year, in our budget, about 60% of the total year budget was around gathering, and 40% was sort of processing and fractionation. The remainder of the year it's actually a higher proportion of gathering than processing and fractionation. We've essentially completed the major projects that we were undertaking. So, we have the ability to flex that capital next year, really dependent upon how our producer customers and what they're

planning to do and how quickly they continue to grow their volumes. So, I believe there's a lot of flex. I believe that the – on the MPLX side, particularly, capital is probably closer to a number that we had this year. But we'll continue to manage that as the year progresses.

<Q - Phil M. Gresh>: Okay. Thanks. That's very helpful. The second question is just around on the refining side, Tim, probably your favorite topic. On an absolute basis, the other gross margin was only about $15 million in the quarter. You mentioned crude differentials as a key variance factor year-over-year. I was just wondering, was there anything else maybe one-time in the quarter because it was a big downturn quarter? Obviously it was a weak margin quarter to begin with. But if there's any additional color there, that might be useful. Thanks.

<A - Donald C. Templin>: Yeah. So I don't know that there's any very unique one-timers. I mean again, a lot of what we've seen on the other gross margin sort of [indiscernible] (01:01:08) over time, has really been a function of where absolute crude prices are, because obviously at lower crude prices, you'll see things like volumetric gains decline in terms of the value ascribed to the gain within the refining system as absolute refined product prices are lower.

You'll see with a lot of the differentials having come in, you also see a lot of the benefits that we had seen historically on the blend stock and feedstock into the system. Those spreads relative to L&S have come in as well. There is a little bit less opportunity, again, at these absolute levels to garner the benefits of feedstocks and blend stocks into the system as well.

So, again, a lot of that has been trending that way just at the absolute levels and with some of the differentials coming off. And those are probably the biggest drivers of it. There's nothing in first quarter that was particularly unusual relative to the trends that we've seen really over the course of the last year.

<Q - Phil M. Gresh>: Okay. Thanks.

Operator

This concludes the question-and-answer session. I will now turn the call back to Lisa Wilson for closing remarks.

Lisa Wilson

Thank you, Katie. And thank you for joining us today and your interest in Marathon Petroleum Corporation. Should you have additional questions or would like clarification on topics discussed this morning, Teresa Homan and I will be available to take your calls. Thank you.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating, and you may now disconnect.

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