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HFC - Q4 2015 HollyFrontier Corp Earnings Call

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OVERVIEW:

Co. reported 4Q15 net loss attributable to HFC shareholders of $44m or negative $0.24 per diluted share.

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PRESENTATION

Operator

Welcome to HollyFrontier Corporation's fourth-quarter 2015 conference call and webcast. Hosting the call today from HollyFrontier is George Damiris, President and Chief Executive Officer. He is joined by Doug Aron, Executive Vice President and Chief Financial Officer.

(Operator Instructions)

Please note that this conference is being recorded. It is now my pleasure to turn the call over to Julia Heidenreich, Vice President, Investor Relations. Julia, you may begin.

Julia Heidenreich - *HollyFrontier Corporation - VP of IR*

Good morning, everyone, and welcome to HollyFrontier Corporation's fourth-quarter 2015 earnings call. I am Julia Heidenreich, Vice President of Investor Relations. This morning, we issued a press release announcing results for the quarter ending December 31, 2015. If you would like a copy of today's release, you may find one on our website, hollyfrontier.com.

Before George and Doug proceed with prepared remarks, please note the Safe Harbor disclosure statement in today's press release. In summary, it says statements made regarding Management expectations, judgments, or predictions are forward-looking statements. These statements are intended to be covered under the Safe Harbor provisions of federal securities law. 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. Today's call may also include discussion of non-GAAP measures. Please see the press release for reconciliation.

Also, please note that information presented on today's call speaks only as of today, February 24, 2016. Any time-sensitive information provided may no longer be accurate at the time of any webcast replay or rereading of the transcript. With that, I'll turn the call over to George Damiris.

George Damiris - *HollyFrontier Corporation - President & CEO*

Thanks, Julia. Good morning and thank you for joining us on HollyFrontier's fourth-quarter earnings call. Today we reported a fourth-quarter net loss attributable to HFC shareholders of $44 million, or negative $0.24 per diluted share. Excluding the $144 million non-cash pre-tax inventory valuation charge, net income attributable to HFC shareholders was $44 million, or $0.24 per diluted share.

Fourth-quarter EBITDA excluding the inventory valuation charge was $161 million, 21% above the comparable quarter last year due to higher crude throughput. Fourth-quarter throughput was approximately 407,300 barrels per day versus our revised guidance of 395,000 to 405,000 barrels per day. We ran 26% sour and 18% WCS and black wax crude.

Our average [laid in] crude cost under WTI was $0.93 per barrel in the Mid-Con, $4.35 in the Rockies, and $0.91 in the Southwest. Consolidated refinery gross margin was $9.91 per produced barrel, 8% below the $10.76 per barrel recorded in fourth quarter of 2014.

Contributions from strong winter gasoline cracks and a $19 million bio-fuel tax credit were more than offset by a $12.5 million RIN charge associated with the November 30 increase in RFS targets, a $26 million hit from negative ethanol blending economics, and a $36 million year-end inventory revaluation charge. Combined, these effects [smacked] approximately $1.50 per barrel off realized margins on a consolidated basis.

Full-year 2015 operational results highlight the benefits of our reliability and process safety initiatives. We achieved a record 97.6% refinery utilization rate, 6 percentage points above 2014. The Southwest and Mid-Con systems recorded full-year utilization rates in excess of 100% and the Rockies showed a 5% improvement compared to 2014.

2015 earnings benefited from gasoline market strength. Our 52% weighting towards gasoline production drove a 15% increase in our full-year realized margins of $16.07 per barrel. Optimizing our refining system to maximize gasoline production, along with the contribution from recent refinery investments at El Dorado, contributed to the 2 percentage point increase in gasoline production compared to previous years.

Despite current gasoline inventories and margins, I remain encouraged by the record vehicle miles travel data and vehicle mix shift towards SUVs and trucks seen in 2015. A heavy PADD 2 spring turnaround schedule with approximately 20% of upgrading capacity due to be offline in April, combined with continued demand strength, should drive a recovery in gasoline cracks from current levels. Given our gasoline weighting, we are well-positioned to benefit from strong gasoline margins, which we expect for the remainder of 2016.

Realized 2015 margin capture represents a 6% increase relative to average capture achieved since our merger. This result demonstrates the benefits of the first phase of execution on our business improvement plan. During 2015, we estimate we achieved approximately $200 million of the $700 million in annual EBITDA improvements targeted by 2018. Over $100 million of our goal was achieved through improved operational reliability and reduced operating cost. We reduced 2015 [loss] profit opportunity by approximately 40%, from 8% of gross margin to 5%.

Controllable operating costs, net of expenses associated with increased throughput, decreased by $38 million, driven by lower maintenance costs. Over $60 million in annualized commercial EBITDA improvements were realized last year. Increased Mid-Continent premium sales facilitated by expanded market access and the refining value benefit from running Permian crude at El Dorado rather than WTI alternative are just two of the many initiatives being executed.

Execution on our opportunity capital investment program is underway. Modernization work on our Tulsa FCC is currently in progress and our list of opportunity capital investment opportunities under evaluation continues to improve in both quality and quantity. While the current crude and margin environment differs from 2014 levels set at our baseline, we still see ample opportunity to execute on our plan and generate value.

For first quarter 2016, we expect to run between 380,000 and 390,000 barrels per day of crude. We currently have a 48-day FCC alky turnaround underway in Tulsa resulting in reduced rates. Additionally, we are optimizing our system to take the current margin environment into account. We will begin a similar turnaround in the Cheyenne FCC alky in April and we also have an FCC alky turnaround schedule at Woods Cross in October. With that, let me turn it over to Doug Aron, our Chief Financial Officer.

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Thanks, George, and good morning. For the fourth quarter of 2015, cash flow provided by operations totaled $76 million. Turnaround spending in the fourth quarter totaled $33 million, taking our full-year turnaround expense to $89 million. In 2016, we expect to spend approximately $116 million on turnarounds.

Fourth-quarter HollyFrontier standalone capital expenditures was $193 million, taking our full-year capital expenditures to $609 million compared to our $600 million to $650 million budget. For 2016, we expect to spend about $500 million on CapEx. Included in that is some carryover spending that was not completed in 2015 and approximately $50 million in additional environmental costs associated with Tier 3 compliance.

As of December 31, 2015, our total cash and marketable securities balance stood at $211 million, a $416 million reduction from September 30 levels. Cash outflows in the quarter included $321 million in dividend and share repurchases and $193 million in CapEx. Through 2015, we returned a significant portion of our cash earnings to shareholders.

During the fourth quarter, we repurchased 5.2 million shares at an average price of $48.22. For the full year 2015, we spent $743 million on share repurchases, reducing our overall share count by 16 million shares. Year-to-date 2016, we have executed an additional $129 million on share repurchases, buying back 3.7 million shares at an average price of approximately $35 per share.

We have $179 million remaining on our existing share repurchase authorization. Last week, we announced our $0.33 per share quarterly regular dividend, which puts our total cash yield at 4.3% as of last night's close on the dividend. As a reminder, HollyFrontier owns 39% of Holly Energy Partners, including 22.4 million common units, plus the 2% general partner interest. The current market value of our LP units is approximately $630 million as of last night's closing price. Fourth-quarter general partner incentive distributions were $11.2 million, a 20% increase over the same quarter last year. For the full year 2015, we have received approximately $90 million in cash distributions from HEP.

Lastly, a reminder that you can find monthly WTI-based 3-2-1 indicators for our Mid-Con, Rockies, and Southwest regions posted on HollyFrontier's Investor page. These regional indicators do not reflect actual sales data and are meant to show monthly trends. Realized gross margin per barrel may differ for indicators for a variety of reasons. You can find the data on our Investor page at hollyfrontier.com. With that, Shelly, we are ready to open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Blake Fernandez.

Blake Fernandez - *Howard Weil Incorporated - Analyst*

Hey, guys. Good morning. I wanted to talk a little bit about the buyback pacing. At your analyst day, I know you weren't given guidance, but you did outline an outlook into 2016, something around maybe $1 billion or so. In 4Q, you certainly ramped it up as promised. I'm just curious, Doug, how you are thinking about that continuing into 2016 here as some of the margins have begun to roll over a little bit?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Sure, Blake. What I would say is -- I will start by reiterating that we already bought back about $130 million worth of stock, or 3.7 million shares so far in January and February. So as we look at the balance of 2016, I would say it's certainly our expectation we complete our current $1 billion authorization, of which about $180 million remains outstanding.

Then beyond that, it will be largely dependent on three things: first, our cash flow generation; second, our ability to raise public debt at a reasonable price; and then, third, our ability to drop assets down to HEP for cash. All three of those metrics are worse or have deteriorated from September levels, but it's important to remember that it's still February and the refining business often looks weaker in January or February every year.

So I would say that, in summary, we remain laser-focused on executing our business improvement plan that we outlined last September as you referenced and that share repurchases are a key component of that plan. But the volume of repurchases is going to depend some of the refining margin environment and the availability of capital in the market.

Blake Fernandez - *Howard Weil Incorporated - Analyst*

Understood. Okay. The second question, if -- it's a question on Pad 2 cracks and some of the economic run cut that's been announced by industry, but secondly, if you could maybe tie in what you're seeing there with some of the guidance? I heard 380,000 to 390,000 in 1Q, which is little bit below what we were thinking, although I know George mentioned some downtime at Tulsa, which -- I am sorry to ask so many -- but can you tie in -- I thought some of the Tulsa issues were taken care of in Q4, so I'm just try to understand, is that a different turnaround than what you've already completed at Tulsa?

George Damiris - *HollyFrontier Corporation - President & CEO*

No, the turnaround that we have right now Tulsa was our planned event. We did have an unplanned event in the fourth quarter in Tulsa and that was due to trying to extend our cycle between turnarounds from five years to six years in order to incorporate the project that we are implementing at Tulsa to modernize our FCC, so again, fourth quarter was an unplanned event.

This turnaround that we are currently in is the planned event to implement our turnaround and the project. So that's our primary reduction in crude rates, and it's primarily at Tulsa. We have trimmed a few thousand barrels a day here and there at El Dorado and Navajo, but nothing major.

Blake Fernandez - *Howard Weil Incorporated - Analyst*

Okay great. Thank you.

George Damiris - *HollyFrontier Corporation - President & CEO*

Thanks, Blake.

Operator

Neil Mehta.

Neil Mehta - *Goldman Sachs - Analyst*

Hey. Good morning, guys.

George Damiris - *HollyFrontier Corporation - President & CEO*

Good morning, Neil.

Neil Mehta - *Goldman Sachs - Analyst*

George, I know this was preliminary and Doug always warned me to not [type] $700 million number as gospel, but I just want to think about this a little bit. At the analyst day, you came out with the $700 million number in terms of refinery operations optimization and capital investment in terms of average annual EBITDA uplift.

As you guys think about the business plan for 2016 and 2017, which of these different -- the five different pockets that you outlined there do you think we should say is commodity agnostic if that makes sense, as opposed to ones which would be sensitive, and how much risk is there to that $700 million number?

George Damiris - *HollyFrontier Corporation - President & CEO*

Well, I would say most of the $700 million is agnostic to price. The element that's probably the most dependent on price and cracks is the opportunity capital component because obviously at $30 per barrel, you have less impetus to do yield improvement type projects. It take something from petroleum coke or fuel gas value up to crude oil value than what you do the price of crude is $60 to $80 a barrel.

But I don't think any of us expects crude to be $30 per barrel for the next 20 years, which is the typical term we use for project life in our analysis. So it might start out a little bit on the slow side, but over the long haul, these opportunity capital investments we are pursuing are going to be economical and justifiable.

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

And Neil, what I would add to that is, as you think about being agnostic to the price, the level set here is on that $700 million of improvement against 2014. So if margins are substantially lower or higher for that matter or different, then we're trying to back that out of what we call our business improvement plan capture.

So if we get to the end of year and we say, look, we feel like we've captured a lot of these things, we've lowered OpEx, we've seen commercial optimization, but EBITDA is flat to [2014] or worse, that will be because of crack spreads being worse, not necessarily because we didn't execute on our business plan. And that's, as we outlined in September, would always be the challenge in trying to show that, but we think we've got a very good program to be able to do that, and know that we are achieving what we expected to achieve so far in our plan.

Neil Mehta - *Goldman Sachs - Analyst*

I appreciate that. The second is more of a macro questions, the three layers of the cake. If you could just talk about each of them. First on diesel, what the impact of some of the slowdown in rig count has been as you look at your Mid-Con operations. In gasoline, you cited a constructive outlook going into the summer, but what you're seeing from an inventory level at this point and what ultimately works it down? And then finally, any thoughts on differentials? All three would be greatly appreciated?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Doing differentials?

George Damiris - *HollyFrontier Corporation - President & CEO*

We will start with diesel first. There's no question diesel is weaker currently than has been in the recent past and that's due to a number of issues both domestically and internationally. A lot of new refineries built overseas for the explicit purpose of making diesel. And then in the US, we've got some hydrocracker start-up that increased diesel production.

At the same time, the demand is weak. You mentioned [develop patch], obviously with the one-third of the rig count we had not too long ago, all the activity associated with that was diesel-driven, that demand is gone. There's a lot less railcars and stuff moving around, especially with -- of coal. I know we've done a good job of killing the coal industry in this country and so those railcars aren't moving as much as they used to.

And there is on-the-road truck traffic is down as well. So lower demand and higher supply is resulting the cracks by about $10 a barrel versus $20-plus historically. On the gas side, there's no question inventories are high at this point in time. That's primarily been supply-driven. Refining fleets run in the high 90% of utilization.

At the same time, demand is still relatively strong. The vehicle mile driven data is very strong, 2.5% year-on-year. Can't ask for much more than that. Employment is strong. So we still see the demand side of the equation being relatively strong, and it's going to be a matter of people getting their turnarounds done in April as we highlighted. We have our 52% gasoline weighting that should play in our favor here when cracks improved starting with the turnaround season here.

As far as crude dips, there's not much to talk about on crude dips in the $30 environment. There's just not that much room or spread at $30 as there is at $60 or $80 or $100. We are still very encouraged by the Canadian crude dips. We're seeing double-digit crude dips in a $30 WTI crude world. That's pretty encouraging.

We run about 80,000 to 100,000 barrels a day of heavy Canadian crude, so about 25% of our slate can be heavy Canadian crude. So that plays well. But as far as Permian dips and Rockies dips and all those dips, with all the pipeline pads that has been put in place, they are very compressed and we expect them to be for the foreseeable future until price picks up and production picks up accordingly.

Neil Mehta - *Goldman Sachs - Analyst*

All right. Thank you, George and Doug.

George Damiris - *HollyFrontier Corporation - President & CEO*

Thanks, Neil.

Operator

Phil Gresh.

Phil Gresh - *JPMorgan - Analyst*

Hey. Good morning.

George Damiris - *HollyFrontier Corporation - President & CEO*

Good morning, Phil.

Phil Gresh - *JPMorgan - Analyst*

First question is just on the Southwest region. If we look at the capture rate that you have seen in that region, it's been down for four consecutive quarters. Obviously, there are some variables here in the fourth quarter that perhaps were one-time, but maybe you could just help us calibrate that fourth-quarter performance and how you would think about what a reasonable cash rate is considering tightening of crude differentials, et cetera in that region?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Yes, Phil -- capture right is such a what I'd call an analyst concept although I appreciate that the way you guys model it. As we think about what's gone on there, the biggest issue trending negatively has been compression of the TI and CS spread and then the Midland to Cushing pushing spreads, the plant is actually running extraordinarily well.

I knock on wood as I say that superstitiously, but Navajo has done great in debottlenecking some problems in terms of running crude that they have had and average crude rate for 2015 was north of 100,000 barrels a day. So in terms of the trend, as George highlighted, we had a few things that worked against us in the fourth quarter that were significantly pronounced.

On really some RINs and biodiesel, a few other things that are likely one time in nature, certainly we hope that to be the case. In terms of modeling capture going forward, Julia has pretty got a better handle. Julia, do you have anything to add or subtract from that?

Julia Heidenreich - *HollyFrontier Corporation - VP of IR*

Yes, I do just think I would reemphasize the fourth-quarter capture was pretty sloppy because of an inventory year-end write-down. Most of that $36 million impacted Navajo, and again, the RINs and biofuel. If you adjust for all of those things, it's far more normalized, and in fact, slightly better than the third quarter, which was 69%.

Again, just looking here going out, the crude differentials are certainly going to keep that at a lower level versus when you had that $6 and $7 benefit, but nonetheless, I do still think that, depending on how the gasoline diesel cracks weigh in, because we you will have to look -- we do make a little bit more diesel in the Southwest due to the some improvements we made there, being able to pull some more distillate out of that stream, so you do have to keep an eye on the inversion between diesel and gasoline, which could also plan into capture rates.

Phil Gresh - *JPMorgan - Analyst*

Okay, thank you. I appreciate all the color on that. Second question, just coming back to the buyback, at the analyst day you talked about a willingness to take leverage to roughly 1 times. Obviously, the macro backdrop has changed. Is there still a willingness to use the balance sheet to the same degree if things are worse? And related to that, where do you feel things are with respect to the $200 million of dropdown capital you're expecting to get per year from HEP in 2016?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Yes, as to the debt question, first, I would say, yes, we very much do expect to put leverage on the balance sheet. As I said in answering Blake's initial question, that market has backed up a little bit, but I would like to believe that's somewhat temporary. I am not sure we can be in the 4.5% level that maybe we might have seen October, November of last year for a 10-year, but yes, you should expect to see us put some leverage on the balance sheet in the first half of 2016.

Again, the uses of those proceeds will be for a CapEx program this year, and then free cash flow generated for share repurchases, so no change there. In terms of the dropdowns, what I would say is, yes, we still very much see 2016 as an opportunity to dropdown Phase 1 of the Woods Cross expansion. That said, we do see some deals in the market, and when I say we, I mean HEP really predominantly, that we had not seen for a good while.

So I would say that dropdowns are still very much part of the story. There might be acquisition opportunities in the market that compete with that in the near term given some of the distress in the MLP markets that we've always got the ability to time the dropdowns from HFC, and so do I think $200 million of cash sales to HEP in 2016 is still possible? Yes. Likely I might back off of that number some just because HEP may see a few other deals that it hasn't seen in the last few years that you have got to take advantage of while they're there.

Phil Gresh - *JPMorgan - Analyst*

Sure, understand. Okay, thank you.

Operator

Brad Heffern.

Brad Heffern - *RBC Capital Markets - Analyst*

Hey. Good morning, everyone.

George Damiris - *HollyFrontier Corporation - President & CEO*

Good morning, Brad.

Brad Heffern - *RBC Capital Markets - Analyst*

Doug, just following on, on the repurchase questions. I'm curious, at year-end, the cash balance is really quite low and you said you have repurchased a decent amount in the first quarter, as well. What is the minimum cash level in this environment, and given that I would assume cash flow generation has been relatively weak given where cracks are, have you been funding those repurchases off the revolver?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

No we have not. We use cash flow generation through the fourth quarter and cash on the balance sheet for share repurchases. We haven't borrowed yet for that. As you point out, we had a $1 billion undrawn revolving credit facility, which provides certain liquidity to us and we've always said a targeted $500 million of cash on the balance sheet was what we had anticipated having as go-forward safety capital.

Some combination of that and revolver capacity, particularly in a lower crude price environment, gives us some comfort. So I don't want to be pinned down to a specific number, Brad, but somewhere in this geography, in that, call it, $250 million of cash and $500 million of revolver availability, where your liquidity was never below $0.75 billion or so.

It feels comfortable to us. There might be 90-day periods of time where we are above that are below that, but again, that gets back to us talking about more wanting to add a little bit more permanent capital to the balance sheet and that's something we would expect to do in the first half of this year.

Brad Heffern - *RBC Capital Markets - Analyst*

Okay, thanks for that. And then circling back to the first-quarter guidance, understand there's some turnaround activity in that. Have you guys chosen to make any pure economic run cuts, just given the context and the environment?

George Damiris - *HollyFrontier Corporation - President & CEO*

Yes again, relatively minor. A few thousand barrels a day here, there at El Dorado and Navajo.

Brad Heffern - *RBC Capital Markets - Analyst*

Okay. And then one more if I could. On the ethanol blending front, you called out the headwind that, that had in the fourth quarter. Is that something that you see bleeding into the first quarter, as well?

George Damiris - *HollyFrontier Corporation - President & CEO*

No question. We've got ethanol trading at a premium to gasoline, roughly $0.20 a gallon. So for every gallon of gasoline you blend, you use 10% ethanol, about $0.02 on a blended gallon basis.

Brad Heffern - *RBC Capital Markets - Analyst*

Okay. I will leave it there. Thanks.

George Damiris - *HollyFrontier Corporation - President & CEO*

Thank you.

Operator

Ryan Todd.

Ryan Todd - *Deutsche Bank - Analyst*

Thanks. Good morning, guys. Maybe if I could ask a couple on the capital side. Could you give us an update on the status of some of the projects that were targeted for a year-end start -- the Woods Cross expansion and maybe the additional scope work that you talked about during the first quarter of 2016 and the Cheyenne hydrogen plant. Are those up and running and any change in outlook to the EBITDA contribution from those?

George Damiris - *HollyFrontier Corporation - President & CEO*

Yes, we will start with the big one first on the Woods Cross expansion project. There is no change from the last guidance we provided. We said we were going to finish construction and start commissioning in the first quarter, ramp up the plant in the second quarter, and get to full run rates and EBITDA potential in the third quarter. We're still on schedule there.

Same thing for the incremental projects around the expansion to allow us to run alternative crudes to the Black Wax baseline which the project was based. The Cheyenne hydrogen plant is up and running, as is the El Dorado Naphtha fractionation project. Both of those two are doing what they are supposed to be doing and operating quite well, and we look forward to further optimization based on the increased capability those two projects give us.

Ryan Todd - *Deutsche Bank - Analyst*

Great, thanks. Then maybe a follow-up to an earlier question on the opportunity capital program. If you look -- you had given some level of guidance in terms of the opportunity capital and the EBITDA generation over a three-year view. Given the environment that we are in, both -- you referenced before about the crude environment and the product environment, as well -- is there is there any shift to the pace of that?

Should we expect to see the pacing be the same? Do you -- as long as crude prices remain at $30, do you just defer some of the capital on that? Do you spend it now on the view that crude prices will recover relatively soon or is there opportunities within that bucket that would allow you to accelerate those versus maybe other commodity-sensitive ones?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Yes, we don't see much change due to the current pricing environment for those projects. We are still thinking in terms of putting $100 million a year to work to get $15 million per year of EBITDA, so roughly again, two-year simple paybacks. Yes, the current crude environment makes you double clutch a little bit on some of these projects, but you have to take a longer term perspective, again, that crude is not going to be $30 per barrel forever. These projects are very economic and give us a lot more capabilities than we would otherwise have without them.

Ryan Todd - *Deutsche Bank - Analyst*

Great. I appreciate. I'll leave it there. Thanks.

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Okay, Ryan.

Operator

Doug Leggate.

Clay Augumini - *BofA Merrill Lynch - Analyst*

Hey, guys. This is actually Clay [Augumini] on for Doug. A couple of questions. First one just on marketing and maybe this is for George. Refineries are generally bullish on gasoline in 2016. I just wonder if you could [trust] the record level of gasoline stocks that we have currently?

And are you guys finding gasoline storage or takeaway becomes tighter at this point? And maybe, could you explain how the switch from winter to summer's spec could exasperate this trend? And finally, how this may frame your expectation for the seasonal margin in the summer?

George Damiris - *HollyFrontier Corporation - President & CEO*

Okay. Again, we do have a lot of inventory in the system currently. That is primarily due to the efficiency of the industry refining fleet, been running at nearly 100%, high 90%s anyway, utilization rates. And as you say in the summer -- or in the winter, you can make more gasoline due to butane blending and other high RVP blending components. This is nothing new. We go through this every year, every winter, to varying degrees.

It seems like every other year, the Magellan system, to pick out a specific one, for Mid-Continent refinery, spills and inventories get high, but as soon as the RVP changes, those high RVP barrels that are inventoried have to come out, and when they come out and the butane blending ceases, that decrease the supply and underlying demand is still strong, as evidenced by the vehicle miles traveled again, we view that as all positive for the crack going forward in the second and third quarters.

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

I would add something to George's commentary because obviously there's been a lot printed and a lot of concern about gasoline inventories and concern over the outlook for refineries. Did a little work this week in looking and comparing ownership of refining assets in the United States in, say, 2008, 2009 time environment, the last time we really saw a downturn in this business and an oversupply for extended period of time in the market and compare that to today.

You guys might all already realize this, but by our estimation, there is about 4.2 million barrels of capacity that's gone from being owned by integrated oil companies to now being owned by independent refiners. The two big ones there are Marathon and Phillips, which came public as independent companies in 2012. Then you saw Tesoro by Carson; you've seen PBF by Chalmette recently, as well as Torrance.

That adds up to about 25% of the refining capacity in the United States that used to be owned by integrated oil companies, now owned by independents. So, you look back to just two weeks ago and some announcements when we saw margins get pretty weak on gasoline for very short period of time, and you saw Phillips and others make announcements about discretionary run cuts. We mentioned a few thousand barrels a day within our own.

I would say, perhaps different from some of our peers in other sectors in the energy space, refining has gotten to be extraordinarily disciplined. You couple that with, as George has talked about, what we think will be very good demand for gasoline, especially at this lower price heading into the summer. Sure, again, we've got to be reminded, it's February, there's seasonal weakness, but those dynamics will carry us through to what should be maybe a better gasoline margin than certainly the forward strip or most of those that are looking expect right now.

Clay Augumini - *BofA Merrill Lynch - Analyst*

Thanks for that, guys. Second question, just want to throw another one at the buyback. Just looking at Q1, obviously the margin environment has deteriorated and it's likely going to affect your cash generation ability, but your stock is at the lowest level in a year. Can you just talk about your appetite for buybacks with this in mind? Thanks.

George Damiris - *HollyFrontier Corporation - President & CEO*

Yes. I'm not sure how I could say it much differently than I already have. We've again already bought back 3.7 million shares so far this year, acknowledging that price is obviously lower. We've got an intent to put something on the balance sheet.

Then again the pace of the buybacks is going to be dependent on our cash flow generation, the ability to raise debt, and then the ability to fund dropdowns at HEP. It's not a matter of if we will be buying back shares; it's just going to -- the pace will be dependent, again, on cash flow generation, which is what I would think you guys would expect and hope from us.

Clay Augumini - *BofA Merrill Lynch - Analyst*

Thanks appreciate it.

Operator

Jeff Dietert.

Jeff Dietert - *Simmons & Company International - Analyst*

Good morning. Jeff Dietert with Simmons.

George Damiris - *HollyFrontier Corporation - President & CEO*

Hey, Jeff.

Jeff Dietert - *Simmons & Company International - Analyst*

Hey. Was curious, you did see a little bit of an increase in your medium and heavy crude feedstocks in the fourth quarter. I assume that's probably continuing in the first quarter as those discounts have been more attractive than the lighter crudes. Can you talk about your flexibility to shift incrementally towards medium and heavy crudes that are trading at better discounts?

George Damiris - *HollyFrontier Corporation - President & CEO*

Sure. Most of that flexibility resides at El Dorado and Cheyenne where we have decent sized cokers. Like you said, to the extent that we can, we are running as much WCS as we can at both those facilities. Navajo doesn't have access to WCS, and we don't run WCS at Tulsa; we run the WTI primarily for our lubes business, so again, those are two plants that give us the flexibility to run the Canadian crude and we can run some other Canadians as well, but primarily it is WCS.

Jeff Dietert - *Simmons & Company International - Analyst*

Got you. You talked about economic run cuts, some barrels at El Dorado and Navajo. Can you talk about some of the challenges, perhaps logistical challenges associated with cut and runs. I am assuming you are buying crude 30 to 60 days in advance, and your crude inventories, I assume, are relatively high, so if you're not going to run, you either have to sell the barrels or store the barrels. Could you just talk about that complexity a little bit?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Yes, it really hasn't been much of an issue for us, especially at El Dorado where we are connected to Cushing. We can either store it in our tankards there or sell it, and then -- again, these aren't big cost. A few thousand barrels a day here or there, so we've been able to contain them, and we have had a positive role that gives us economics to tank them and use them for future months.

Jeff Dietert - *Simmons & Company International - Analyst*

Got you. You talked earlier about your high gasoline yield relative to peers. Has this been an intentional strategy or are you more just doing the best with the legacy assets that you have in making investments there that are most advantageous?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

It's a combination of being lucky and being good. We take what we have, as you said, and we had a good project to modernize our FCC that played out regardless of the gasoline diesel spread and we implemented the project and a positive gasoline diesel differential just made that project even better.

Jeff Dietert - *Simmons & Company International - Analyst*

Thanks for your comments.

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Thank you.

Operator

Chi Chow.

Chi Chow - *Tudor, Pickering, Holt & Company Securities - Analyst*

Great, thanks. Doug, the effective tax rate for the quarter appears to be very low. You mentioned that the biodiesel blending credit is slowing some margins. What are the other factors that were impacting tax rate in the quarter?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Yes, Chi, the biggest impacts for us there were, we had been accruing through September at a higher expected statutory rate. Fourth quarter was lower than expected, so ended up with a lower -- what feels like a lower effective tax rate. So think HFC earnings a little lower in fourth quarter, HEP actually a little higher, but as you know, that's a pass-through to unit holders there. So think that, that is a one time anomaly that was a function of where we were through the first nine months versus where we ended up in the fourth quarter.

Chi Chow - *Tudor, Pickering, Holt & Company Securities - Analyst*

Okay. And what's the guidance on tax rate going forward here this year?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Statutory 35% is what we are modeling.

Chi Chow - *Tudor, Pickering, Holt & Company Securities - Analyst*

Okay. Great. And then on -- any growth at HEP, whether it's drops or acquisitions, with the yield where it's at, how do you think about financing growth there in the current MLP environment? And on any drops, it sounds like you are definitely focused on bringing cash back to the proceeds at HFC. Is that correct?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

To the last question, on new assets -- take example the Woods Cross Phase 1, yes, it would be a preference to take cash because you've got a high basis asset where by taking cash you don't have any tax leakage, whereas on more legacy assets you maybe even prefer to take units so you don't have the fraction of the tax. What I would say is, the yield environment or the unit price has improved certainly at HEP, but still not at a level where you would be real excited about issuing units.

We've still got a fair amount of debt capacity there. We are at just north of 4 times debt-to-EBITDA so there is some additional capacity. We wouldn't need to be issuers of equity in 2016 at HEP. Certainly for a Woods Cross dropdown, there would have to be an equity component, and whether that was to the market or to HFC, it's just going to depend on a number of different factors.

That market is starting to show a little bit of, again, positive reception to those like HEP that have a steady stream of growth and are starting to be better recognized than they were in the last 30 to 60 days. But listen, we are like everybody else. We're going to have to watch that market and look at what the opportunity set is, what the capital looks like, and that's certainly more uncertain today than it was a year ago.

Chi Chow - *Tudor, Pickering, Holt & Company Securities - Analyst*

All right. Okay. Thanks, Doug. Appreciate it. Thank you, Chi.

Operator

(Operator Instructions)

Johannes Van Der Tuin.

Johannes Van Der Tuin - *Credit Suisse - Analyst*

Hi. Thank you for taking my call. A couple of quick questions. First on the balance sheet, given the additional worries people have about the macroeconomic environment, I know you're not here right now, but if you did ever become a bit more balance sheet-constrained, how would you go about managing that through the cycle? Would you look at first maybe slowing down the pace of buybacks or would it be a slowdown in growth CapEx or are there other levers that you would pull?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Yes, all of those are possibilities. As you say, today we have zero debt on HFC's balance sheet, so we're not at all constrained. But that being said, of course, you've got to look, even when you are or are not capital constrained, it's been our history to be good stewards of capital. You've got to look hard at your CapEx programs and do the projects that are the most advantageous to you going forward.

There are -- as George mentioned there's lots and lots of more good ones that we have started to evaluate and see as possible. We would love to do all of them in 2016, but that's not realistic first from an execution standpoint and secondly from an available capital standpoint. So, we said at our analyst day, projects like Woods Cross Phase 1, of that nature, are few and far between, and we're going to be more focused on projects in that $25 million to maybe up to $50 million capital range.

Is there a possibility of one or two that could be higher than that in the next few years? Yes, but otherwise, we're going to be cautious in what feels like a tougher environment than we've been in the last few years. On the buybacks, reiterating, yes, to expect $750 million of buybacks, which is what we did last year or $780 million, it's going to be dependent on free cash flow generation.

If you look back through really all of the history of Holly and Frontier and then the predecessor companies, you'll find us to be on the more conservative side in the industry. That still stands true today. When we talk about adding leverage, we would expect that to be in the 1 times EBITDA range, so you just don't find yourself having to manage the balance sheet beyond that. I'm not sure if I've answered your question, but most would agree we are among the very best and most conservative and understanding that this can be a cyclical business.

Johannes Van Der Tuin - *Credit Suisse - Analyst*

That's very helpful. Thank you. Second question goes to winter grade gasoline. There is a sense that in the market currently a lot of those inventories are really winter grade inventories that were built up in December and January when runs were much higher. My understanding -- and this could be incorrect -- is that winter grade gasoline, like all gasoline, the molecules deteriorate over time.

It can't be preserved from a year-to-year basis on an indefinite period of time. Is that the case, and if that's so, is it really just a all oil inventories must go situation in which everybody really needs to push those winter grade inventories into the market basically now while they can? Or are there some ways that you can preserve the value there for some future period?

George Damiris - *HollyFrontier Corporation - President & CEO*

Let's start with the shelf life question. I don't think that what you have been led to believe is true, that there is a limited shelf life on gasoline. The bigger issue is the cost of continuing to store that gasoline. If you don't get it out by the time the RVP changes, you have to take that barrel for a whole year or almost a whole year till the RVP season gets back to that spec, so it's really the cost of carrying that through a whole year that drives people to sell the barrel rather than continue to store it.

Johannes Van Der Tuin - *Credit Suisse - Analyst*

Okay, but you think that the net effect is still the same where people just really want to sell it now because the cost is too prohibitive to carry it into the next season?

George Damiris - *HollyFrontier Corporation - President & CEO*

That's true. Tanks cost money, at the end of the day. It's round numbers, call it $0.50 per barrel per month. So if you're going to store it for a year, it's going to cost you roughly $6 a barrel to store the barrel for a year.

Johannes Van Der Tuin - *Credit Suisse - Analyst*

Okay. That makes sense. Thank you very much.

George Damiris - *HollyFrontier Corporation - President & CEO*

Sure.

Operator

Roger Read.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Good morning. I thought I hit star-one earlier, but I messed up on that. Anyway, a couple of questions to ask you just because it hasn't been hit on this call and it's been on every other one. As you think about the octane issues out there, can you give us an idea of what may have changed a little bit? Maybe an idea of how much of some of the gasoline that's in storage might be more octane than something else and how we should think about sourcing that as we go into this summer?

George Damiris - *HollyFrontier Corporation - President & CEO*

Yes, as far as octane, I don't think much has changed year-on-year for octane. We still view octane as going to be at a premium going forward. A lot of that has been driven by the composition of the crude slate the US refining fleet is processing has more naphtha in it and it tends to be a lower quality naphtha that basically means it's lower octane or produces lower octane gasoline as a result.

So we still view octane as going to be tight this year. I don't think anything much has changed from last year to this year to change that forecast. As far as what's in storage now, some higher octane gasoline components could be in storage, especially since they tend to be lower RVP so can make the transition from the high RVP winter to the lower RVP summer, but I don't see that being as a big percentage of what's in storage now.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Okay, thanks. Then you talked earlier about the economic run cuts just being a few thousand barrels. I was curious if you had made any changes in the yield in that environment as well, so not just moving removing barrels from the market, but also moving barrels to a different part of the yield?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

No question. Like all refiners, we use our LP models daily if not more frequently than that to optimize our crude slate, as well as our product mix, not only between gasoline and diesel, Roger, but also between light products and heavy products. There are times when asphalt has been a very good product for us, especially when the heavy sour crude dis is wide enough and asphalt can be a better product for us at times and even light products.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

Thanks. That was where I was going to go with the next. Any thoughts on the asphalt market as you go into this summer?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

No, I really don't see much material change there either year-on-year. The supply of high-quality asphalt is less than it had been, say, the last five years or so, again, due to the crude slate. The lighter shale oil crudes don't make good asphalt, so as they have made their way into the US crude slate, they don't produce as high-quality asphalt so the supply of high-quality asphalt is not as prevalent as it used to be. We still run again a lot of WCS, primarily at Cheyenne and El Dorado, again, and we make a lot of high-quality asphalt at those two facilities.

Roger Read - *Wells Fargo Securities, LLC - Analyst*

All right. That's it for me. Thank you.

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Thank you.

George Damiris - *HollyFrontier Corporation - President & CEO*

Thanks, Roger.

Operator

Jeff Dietert.

Jeff Dietert - *Simmons & Company International - Analyst*

Maybe quickly, regionally, could you talk about when you make the shift from winter grade to summer grade? How much time is left to bring these winter grade inventories down?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

I can't quote all the RVP timing changes by region, Jeff, but it's just safe to say that it's happening now, and it will continue to ramp up over the months to come. We can get you the RVP schedules by region or by state if you would like, but I just can't recite them off the type of my head.

Jeff Dietert - *Simmons & Company International - Analyst*

In the south, don't they start in March or is it more of an April event?

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

It's -- go ahead, Tom.

Tom Creery - *HollyFrontier Corporation - VP of Crude Supply*

This is Tom Creery. You are correct. We get varying layers on when the grade changes start, and you're current, we're going to start gearing up for March change-over. That will be the first [tranche] and then go from there.

Jeff Dietert - *Simmons & Company International - Analyst*

Okay.

Tom Creery - *HollyFrontier Corporation - VP of Crude Supply*

But why don't you let us, Jeff, get you the exact schedule so that you know for a fact rather than just from poor memory?

Jeff Dietert - *Simmons & Company International - Analyst*

Okay. I got you. But generally speaking, it's earlier in the south and later in the north, correct?

George Damiris - *HollyFrontier Corporation - President & CEO*

That's right.

Tom Creery - *HollyFrontier Corporation - VP of Crude Supply*

That's correct.

Doug Aron - *HollyFrontier Corporation - EVP & CFO*

Yes.

Jeff Dietert - *Simmons & Company International - Analyst*

All right. Thanks for your comments.

George Damiris - *HollyFrontier Corporation - President & CEO*

Sure.

Operator

The are no further questions at this time. I would like to turn the call back over to Julia for closing remarks.

Julia Heidenreich - *HollyFrontier Corporation - VP of IR*

Thanks everyone for joining us this morning. If you have any follow-up questions, please reach out to Investor Relations. With that, have a good day.

Operator

Thank you. This does conclude today's teleconference. Please disconnect your lines at this time and have a wonderful day.
