Suburban Propane Partners, L.P.
Q3 2020 Earnings Call
August 6, 2020

Officers
A. D'Ambrosio, Vice President, Treasurer
Michael Stivala, President, Chief Executive Officer
Michael Kuglin, Chief Financial Officer, Chief Accounting Officer

Presentation

Operator: Good morning, and welcome to the Suburban Propane Partners, L.P., Fiscal 2020 Third Quarter Results Conference Call. (Operator Instructions)

Please note, this conference call contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 as amended, relating to the partnership's future business expectations and predictions and financial condition and results of operations. These forward-looking statements involve certain risks and uncertainties. The partnership has listed some of the important factors that could cause actual results to differ materially from those discussed in such forward-looking statements, which are referred to as cautionary statements in its earnings press release, which can be viewed on the company's website. All subsequent written and oral forward-looking statements attributable to the partnership or persons acting on its behalf are expressly qualified in their entirety by such cautionary statements.

Please note this event is being recorded.

I would now like to turn the conference over to Davin D'Ambrosio, Vice President and Treasurer. Please go ahead.

A. D'Ambrosio: Thanks, Ian. Good morning, everyone. Thank you for joining us this morning for our Fiscal 2020 Third Quarter Earnings Conference Call. Joining me this morning are Mike Stivala, President and Chief Executive Officer; Mike Kuglin, Chief Financial Officer and Chief Accounting Officer; and Steve Boyd, Chief Operating Officer.

This morning, we will review our third quarter financial results along with our current outlook for the business. Once we've concluded our prepared remarks, we will open the session to questions.

Our annual report on Form 10-K for the fiscal year ended September 28, 2019, and 10-Q for the period just ended June 27, 2020, which will be filed by the end of business today, contain additional disclosure regarding forward-looking statements and risk factors.

Copies may be obtained by contacting the partnership or the SEC.

Certain non-GAAP measures will be discussed on this call. We have provided a description of those measures as well as a discussion of why we believe this information to be useful in our Form 8-K which was furnished to the SEC this morning. Form 8-K will be available through a link in the Investor Relations section of our website at suburbanpropane.com.

At this point, I will turn the call over to Mike Stivala for some opening remarks. Mike?

Michael Stivala: Thanks, Davin. And welcome. Thank you all for joining us this morning. I hope that you and your families remain safe and healthy. And once again our hearts go out to those that have lost loved ones or who may be suffering from the consequences of the COVID-19 virus that has plagued our entire nation over the last 5 months.

At Suburban Propane, our business has been essential service throughout this crisis and our personnel have done an outstanding job supporting the needs of our customers and local communities while also adapting to the new business protocols developed to help protect our employees, our customers and the workplace.

As I indicated back in May during our fiscal second quarter earnings call, we expected to experience some challenges in our business as a result of job losses and the dramatic slowdown of the economy, particularly in our commercial and industrial customer sectors. We developed operational and manpower plans to adapt our business model to the shifting customer demand patterns and the potential for an extended period of demand softness.

As the fiscal third quarter progressed, we did experience lower demand from our commercial and industrial customers with volumes that were 9% below the prior year third quarter. However, that decline in volumes was more than offset by strong demand from our residential customers as a result of a combination of cooler average temperatures in the April-May time frame and the higher usage resulting from the stay-at-home measures instituted by government leaders throughout our operating footprint in order to help mitigate the spread of the virus.

In fact, in our residential sector, volumes increased more than 21% over the prior year. As a result, the physical 2020 third quarter was an exceptionally strong quarter for Suburban Propane. Adjusted EBITDA of $32.2 million, was $12.1 million or 61% higher than the prior year third quarter and, in fact, represented the highest level of adjusted EBITDA for any third quarter in our history.

During the quarter, we also repaid more than $35 million under our revolving credit facility from excess cash flows, which resulted in a significant improvement in our leverage metrics compared to the second quarter.

So while we have certainly faced some tremendous challenges managing through this unprecedented crisis and adapting to the ever-changing circumstances, we are proud of the way our people have responded to those challenges, how they have remained focused on safely meeting the needs of our customers and how we have positioned the business to be nimble as the country continues to wrestle with the virus for the foreseeable future.

In a moment, I'll come back for some closing remarks. However, at this point, I'll turn it over to Michael Kuglin to discuss the third quarter results in more detail. Mike?

Michael Kuglin: Thanks, Mike, and good morning everyone. To be consistent with previous reporting and to discuss our third quarter results, I am excluding the impact of unrealized non-cash mark to market adjustments on derivative instruments used in risk management activities which resulted in an $861,000 unrealized gain in the third quarter of 2020 compared to a $138,000 unrealized gain in the prior year. Excluding these items as well as a $900,000 pension settlement charge in the third quarter of this year, our net loss for the third quarter improved by $13.6 million or $0.22 per common unit compared to the prior year.

Adjusted EBITDA for the third quarter was $32.2 million, an increase of $12.1 million or 60.5% compared to the prior year. The improvement in earnings was driven by a combination of higher volume sold resulting from strong residential customer demand, hiring in at margins and savings from various cost-containment efforts. While the unprecedented health crisis had a varying impact on customer demand and volume sold during the third quarter, it did not materially impact bottom line earnings.

There's still a fair amount of uncertainty about the future impact from the economic slowdown resulting from COVID-19, but we will continue to adapt our business and take steps to help mitigate the potential negative consequences of lower demand to the extent we experience prolonged sluggishness in the economy.

Retail propane gallons sold in the third quarter were 75.4 million gallons, which was 2.2% higher than the prior year. Although weather during the third quarter typically has less of an impact on volume sold than it does during the heating season, volumes in the third quarter benefited from cooler temperatures during April and May that resulted in strong residential heat-related demand. Average temperatures for the month of April and May were 17% cooler than the same period last year and 5% cooler than normal. Overall, average temperatures across our service territories for the third quarter are comparable to normal and 12% colder than the prior year. The combination of the cooler weather and temporary stay-at-home governmental measures help drive residential propane usage that more than offset the decline in commercial and industrial volumes.

From a customer mix perspective, residential volumes increased 21% compared to the prior year, whereas commercial and industrial volumes decreased 9%.

In the commodity markets, wholesale propane prices remain relatively low compared to historical levels, but increased steadily during the quarter with the price of propane, basis

Mont Belvieu, rising from $0.27 per gallon at the start of the quarter to $0.46 per gallon at the end of June. Overall, average wholesale prices for the third quarter were 26% lower than the prior year third quarter and 11% higher than the second quarter of fiscal 2020.

In the early part of the fourth fiscal quarter, propane prices continue to remain relatively low and range bound resulting from U.S. inventory levels that remain considerably above average levels for this time of the year.

Total gross margins of $146.4 million for the third quarter increased $10.9 million or 8% compared to the prior year, primarily due to higher propane volumes and higher average unit margins. Overall, propane unit margins increased $0.09 per gallon or 5.2% compared to the prior year due to favorable volume mix and from the year-over-year decrease in commodity prices.

With respect to expenses, despite the 2% increase in volume sold, combined operating and G&A expenses decreased $1.1 million or 1% compared to the prior year. The savings reflected the operational plans that we developed and implemented to address different customer demand scenarios resulting from COVID-19, including a temporary reduction to our manpower. The savings from these actions were partially offset by higher variable operating costs to support higher volume-related demand and an increase in accruals for self-insurance liabilities and reserves for potential doubtful accounts.

Net interest expense of $18.5 million for the third quarter decreased $400,000 compared to the prior year, primarily due to a decrease in benchmark interest rates on borrowings under our revolver.

Total capital spending for the third quarter of $5.6 million was $2.1 million lower than the prior year, due to a lower level of spending on vehicles and tanks.

Turning to our balance sheet. During the third quarter, we repaid more than $35 million under our revolver with cash flows from operating activities. Despite a modest delay in collection activities resulting from the impact of the economic slowdown on our customers and from government (implemented) restrictions in certain states that limited some of our traditional means of helping ensure customer payments, the collection of accounts receivable was a significant source of cash during the third quarter. In the early part of the fourth quarter, our collection activities continue to improve and are nearing the historical levels that we would generally experience for this time of the year. While we're encouraged by the improvement, this is something that we continue to closely monitor.

From a leverage perspective, the increase in adjusted EBITDA coupled with the debt repayment during the third quarter resulted in our consolidated leverage ratio improving to 4.83x at the end of June compared to 5.22x at the end of the second quarter.

Our borrowings on the revolver at the end of Q3 were $109.7 million, which was $17.5 million lower than June 2019 and $3.8 million lower than the level at the beginning of the

fiscal year.

We remain well within our debt covenant requirements. We'll continue utilizing excess cash flows in a balanced fashion to strengthen the balance sheet and to invest in strategic growth.

Back to you, Mike.

Michael Stivala: Thanks, Mike. On the top of the strengthening the balance sheet and our overall leverage, let me first address our recent announcement on July 23, regarding our decision to reduce the quarterly distribution from $0.60 per common unit in the previous quarter to $0.30 per common unit in respect to the third quarter of fiscal 2020.

After a thorough assessment of the potential for shifting demand patterns as a result of the economic uncertainties associated with the ongoing efforts to mitigate the spread of COVID-19, we decided to take this proactive step to reduce our annual cash requirements. This reduction will provide an incremental $75 million of excess cash flow. It will significantly enhance our distribution coverage. It will provide excess liquidity to accelerate our debt reduction efforts. And importantly, it will provide enhanced financial flexibility to support our growth initiatives.

Conservative balance sheet management has always been a core philosophy of ours, one that has served us well in managing through challenging environments. All that being said, our business fundamentals remain strong. Operationally, we remain focused on providing exception service to our customers, driving efficiencies and cost savings, implementing additional protocols to protect the health and safety of our employees, executing on our customer base growth and retention initiatives and positioning the business for long-term growth.

While we may experience continued softness in demand from our commercial and industrial customers in the near term, our efficient and flexible business model leaves us well-positioned to support our customers and local communities as they recover.

Interestingly, what we are also seeing is a recognition that propane is a part of the solution in the recovery as a result of its clean burning attributes and the portability and dependability of propane to support new applications as businesses and local communities adapt to the new social distancing guidelines with more outdoor activities.

As we have stated before, we take a long-term view on managing this business. And having the financial strength, flexibility and access to adequate capital to support our growth plans are all key to our long-term success.

Finally, I am extremely proud of the more than 3,200 employees of Suburban Propane for their continued resiliency and commitment to safety and outstanding service to the customers and communities they serve, while adapting to the ever-changing circumstances and new operating protocols to help protect their health and safety. Thank

you for all that you do every day.

And as always, we appreciate your support and attention this morning, and now we'll take questions. And Ian, if you could help us out with that.

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Questions and Answers

Operator: (Operator Instructions) At this time, we have no questions.

Michael Stivala: Okay. Great. Ian, thank you very much. Thank you all for your attention today. Appreciate all the support. We look forward to talking to you again in November as we get to close out the fiscal year and prepare ourselves for a new fiscal year and a new heating season in 2021. Stay healthy. Stay safe. Thank you all.

Operator: And just a final announcement. To access the replay for this call, please dial (877) 344-7529 or (412) 317-0088 and enter the code 10145783. The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.