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The Williams Cos., Inc. (WMB)

Q4 2016 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, everyone, and welcome to The Williams and Williams Partners Fourth Quarter 2016 Earnings Conference Call. Today's conference is being recorded. At this time for opening remarks and introductions, I would like to turn the conference over to Mr. John Porter, Head of Investor Relations. Please go ahead, sir.

John D. Porter
Head-Investor Relations, The Williams Cos., Inc.

Thanks, Tony. Good morning and thank you for your interest in Williams and Williams Partners. Yesterday afternoon, we released our financial results and posted several important items on our website. These items include press releases and related investor materials, including the slide deck that our President and CEO, Alan Armstrong, will speak to momentarily.

Our CFO, Don Chappel, is available to respond to questions, and we also have the leaders of Williams' 2016 operating areas with us: Walter Bennett leads the West and Central; John Dearborn leads NGL & Petchem Services; Rory Miller leads Atlantic-Gulf; and Jim Scheel leads the Northeast Gathering & Processing area. Our Engineering Services leader John Seldenrust is also with us.

In our presentation materials, you will find an important disclaimer related to forward-looking statements. This disclaimer is important and integral to all of our remarks and you should review it. Also included in our presentation materials are various non-GAAP measures that we reconciled with Generally Accepted Accounting Principles. These reconciliation schedules appear at the back of the presentation materials.

We're planning on keeping our call to about an hour. If we miss any of your questions, feel free to follow up with Investor Relations later on today.

And with that, I'll turn it over to Alan Armstrong.

Alan S. Armstrong

President, Chief Executive Officer & Director, The Williams Cos., Inc.

Great. Well, thank you, John, and good morning, everyone. We're glad you could join us today. Let's jump right in here on slide two where we have an overview of what we're going to talk about this morning. We'll discuss our full year 2016 performance and also provide some perspective on where we see the business going and why we believe Williams is so well-positioned to continue on our growth trajectory.

And first, I'd like to recognize our teams across the Williams Companies for the strong performance that was turned in for 2016. They endured a lot of uncertainty and change but just kept on delivering both great performance and execution against our projects. Cash flows, as a result of their efforts, were up and we exceeded our adjusted EBITDA guidance for the year. Our performance reflects the decisive actions we began taking in early 2016 to focus on cost reduction, strengthen our financial position and align our workforce to execute against our more narrow strategy.

Very importantly, we continue to bring major new projects into service and make projects on others that are now permitted. We closed the sale of our Canadian assets in 2016 and we announced a restructured win-win gathering agreements in the Barnett and MidCon regions with Chesapeake. And we also announced the start of a process to monetize Geismar, which is on schedule. We also completed a board refresh process that saw the addition of seven new board members. We're very excited about the counsel and involvement of our entire board of directors that bring years of energy company experience and a solid track record of building and sustaining growth for stockholders.

Throughout 2016 and 2017, we continued to make progress in debt reduction, and we're also enabling the funding of significant growth portfolio of WPZ at the same time. And just this month, Atlantic Sunrise reached a major milestone with its FERC certificate, and we continue to make progress on both the regulatory and construction planning fronts for this important project. There is significant support for the project from both business, industry – general industry [ph] in the area (03:46) and as well big labor organizations who realized the value of the Atlantic Sunrise system to both Pennsylvania and to the U.S. economy.

But Atlantic Sunrise really is just one example of projects we're pursuing as we transform our asset portfolio to deliver fee-based predictable and stable cash flows from connecting prolific supply basins to growing markets.

On that note, we announced a transaction last week to increase our ownership in a Bradford County PA gathering operation. I'll discuss that a bit later, but we're very excited about the way that transaction worked out for us.

So, with the unique advantage position we're in across both demand and supply markets, we believe there is additional value in WMB and WPZ pricing, given our strong adjusted EBITDA growth since the oil price collapse at the end of 2014. And I'll show some detail of our perspective on that at the end – towards the end of this presentation about our growth versus our peers and our valuation against our peers.

So, with that, let's move on to slide three and discuss our overall full year 2016 results. Here, we look at the full year results for WPZ on GAAP measures of cash flow from operations. We were at about $3.7 billion, up nearly

$1 billion on cash from operations. On the full year 2016 GAAP measures, we delivered net income of $431 million at PZ, up over last year due to lower non-cash impairment charges, a little bit of help on commodity margins and of course increase on fee-based revenues.

On the non-GAAP measures, we look at 2016 adjusted EBITDA is up in every segment, all five of our segments here for 2015 (sic) [2016] (05:42) with a total overall increase of 8%, I think, really demonstrating the strength of our natural gas-focused strategy. And our DCF was also up about $151 million or 5.4% versus 2015, giving us a coverage ratio of 1.01 times. And of course, this is measured against the higher distribution rate of [ph] $3.40 a unit (06:07).

Our ongoing cost reduction efforts across the company are contributing to our strong performance, even as we brought new assets online. So we're continuing to grow the business, but as you look at our operating costs, we've been able to lower those in many areas and keep those flat in areas that we're growing. You can see some of the key drivers for the full year results by various operating [ph] years (06:32) on slide three, but let's turn over to slide four and I'll provide some color on each of the areas as we look at the 4Q 2016 results.

So, looking here at slide four, the simple headline here is, we do continue to deliver growth across the business here in the fourth quarter. And our CFFO for the fourth quarter was up nearly $1 billion, primarily driven by the Barnett contract restructuring as well as growth in our modified EBITDA.

Again, on the GAAP measures, similar story. Net income of $145 million was up over last year, once again due to lower non-cash impairment charges. And in the fourth quarter, EBITDA growth on adjusted EBITDA, we saw a growth of 5% over 4Q 2015. DCF for the quarter was down about 3% versus 4Q of 2015, and this is primarily driven by increase in maintenance capital and an increase in interest expense. Of course, we're beginning to take that interest expense down.

Overall, coverage for the fourth quarter came in at 0.92 times due to higher maintenance capital spending and, as I pointed out, the increased interest. But for the year, the coverage again was 1.01 times.

So, now, let me provide some perspective across all of our five operating areas. And just as a reminder, this would be the last time you hear about all five because we are consolidating those into three areas, which will be the Atlantic-Gulf, the West, and the Northeast G&P as we go into 2017.

So, looking at Atlantic-Gulf, we continue to deliver growth both year-over-year and in the fourth quarter. For the year, adjusted EBITDA was up $112 million with the increase driven by free-based revenue growth and embedded fee-based revenues in our Discovery JV. Of course, the Discovery JV was driven by natural gas volume growth from the prior year as we brought on some of the big systems in the deepwater. Great job by our Discovery team of continuing to operate safe with tremendous growth in their business there.

We saw higher fee-based revenues as well, but we had a nice lift from the Pascagoula opportunity in the second half of the year. And just lets you [indiscernible] (09:02) in a little tighter. We think that was about $24 million in the fourth quarter that came from the excess volumes coming in from the Pascagoula outage there in the fourth quarter. The Gunflint revenues were up as well, and we did see a partial offset of these increases due to some outages for well work-overs and repairs on the Tubular Bells field that flows into Gulfstar.

Overall for the year, cost related to new assets being placed into service and maintenance and modernization on our existing systems offset some of the fee-based revenue growth. But pretty impressive cost controls allowed a large portion of the revenues to be recognized in EBITDA. This Atlantic-Gulf team really has been managing tremendous growth and continuing to reign in costs the same time.

But I also would point to the fact that they also have tremendous amount of new business that they're developing at the same time. So, his team really is managing a lot of growth and doing it in an operationally prudent manner. So, very proud of the Atlantic Gulf team and their efforts there.

Looking to Central. The adjusted EBITDA increased $13 million to $912 million for the full year. In the fourth quarter, Central's adjusted EBITDA decreased by $25 million to $194 million. This adjusted EBITDA was unfavorably impacted by approximately $23 million due to a one-time year-to-date true-up of amounts previously recognized during 2016 related to Barnett Shale Minimum Volume Commitment, and that was caused by of course the Barnett restructuring and recontracting that occurred during the fourth quarter.

Moving forward, we're looking forward to working with Total to improve the performance of this important gas sale through their $40 million per year drilling commitment to the area. And overall, the restructuring has been viewed positively, and we think we're on track here to deliver steady continued growth in this area. And so, really excited to get to work in an area that's really been neglected for quite some time as it wasn't an area that was attracting any capital from Chesapeake.

Just to note about the Haynesville now, that's an area which is further advantaged if the Northeast takeaway capacity is unable to supply most of the coming demand in the Southeast U.S. So, we view our position here as very strategic. And I would just tell you, I think, as we look at production here in the U.S. right now, and we see that continuing to fall, it's going to be really hard for – as prolific as the Northeast is, it's going to be hard for it to make up all of the production decline that we're seeing across the U.S. without the infrastructure coming on here in 2017.

So, we really believe that any [indiscernible] (12:00) that has low cost reserves and existing infrastructure like the Haynesville are very well positioned here as we head into 2017.

So, let's look at the Northeast. In 2016, our Northeast G&P delivered a $43 million increase in adjusted EBITDA. These increases were due mainly to fee-based revenue growth as well as strong focus by Jim Scheel and our team there on cost reduction, including reduction of $36 million in our O&M expense. So, that team is really making the Northeast, which was just on a growth year there for quite some time, getting these big systems build out. And his team now is very focused on really getting our unit cost in line and continuing to be able to reign in costs there. So, it really impressed with the way the team has come together there.

As we've discussed, the Marcellus and Utica areas really hold the key for America's energy future, and we're working very hard on increasing not only our gathering position there but also getting – making sure we're connected to all takeaway capacities to unleash this tremendous resource that it will supply low cost, clean natural gas resource for decades to come. We did see some impressive volume uplift at the end of the quarter and set records on several of our big dry gas systems in January as [ph] local load (13:20) and the REX 3 expansion gave this bottlenecked area some relief. So, a little more on that later, but really seeing here towards the very end of the fourth quarter and in January, we're finally seeing some volume response [ph] to price up there (13:35).

And for the West operating area, the main story of 2016 was remarkably steady and predictable cash flows across the year with a very slight increase in adjusted EBITDA for the full year. The results were positively affected by a strong focus on cost controls and lower O&M and SG&A expenses. So, great job to Walt Bennett who leads that area for us as well and his team that really continue to put pressure on cost at the same time really driving our focus on process safety across all of our big gathering systems both in the West and now what's previously the Central area.

We can report that producers in the West staying a little more hopeful than they've been recently. So, we're cautiously optimistic based on some of the activities we're seeing out there, most recently in response to both better gas prices and better NGL margins for the [ph] Rockies (14:34), the fourth quarter volumes were a bit impacted by weather-related freeze-off, and we continue to see some impact from weather here in the first quarter.

On the NGL and Petchem Services area for the year, NGL-Petchem adjusted EBITDA was up $163 million, so a very nice increase over 2015. We had a significant accomplishment in 2016 when we completed the sale of our Canadian business. And as reflected in the quarter and year-end results, it was one of the big strategic moves we made to focus the business on our core capability of gathering, transporting and handling natural gas.

As you know, we're in the process of selling the Geismar facility and an anticipated announcement here in the first half of 2017. But I can tell you, the process is moving ahead as planned, and we expect final bids in late first quarter. The Geismar facility ran well in 2016, but we did have an interruption in production late in the year as we took facility down to make some repairs, which resulted in about a 12-day outage during the quarter.

This is a plant that's very strategically located on the Mississippi River, and we're really focusing on safe and reliable operations there as we're in the sales process. And it's a plant that is very well positioned to serve both Louisiana and the global market. Our other business, Conway and OPPL continued to generate very steady and growing cash flow. So, that area – that didn't get a lot of focus, will now be included in [ph] our list (16:09), but great job on our teams there continuing to deliver cash flow growth in Conway and OPPL.

Moving on to slide five. We regularly show how we are doing against the long list of projects and deals that support our very clear strategy. It's a really good measure of progress as we continue to steadily deliver these large complex projects and deals. It's critical to keep our eye on this list of high-priority items as it is pathway to growing high-quality, predictable fee-based revenues. And we think it's a great list for our investors to keep their eye on as well.

I think, any objective [indiscernible] (16:54) would have to agree that progress is being made as we pursue tremendous demand growth on Transco, which is both the largest and the fastest-growing pipeline system in the U.S. But we also are preparing for the tremendous follow on in volumes as the demand builds and the Northeast is called on to meet this very identifiable growth that's right before us. So looking at some of the recent developments, first of all, the Transco's Atlantic Sunrise, I mentioned earlier, we did receive a FERC Certificate on this 1.7 Bcf a day system. And we're continuing to now work with the State of Pennsylvania to get our final permits for that project. All is going well there, and the team is really excited about moving ahead with the construction after a very long permitting process there on Atlantic Sunrise.

On the Gulf Trace system, this is a system that most of the construction was done in Louisiana, and it's a 1.2 Bcf per day expansion that serves Cheniere Sabine Pass LNG export terminal, and this was placed in service ahead of schedule and under budget, and really nice I would tell you, I think a nice break for our teams that are used to building in areas that aren't so friendly. Nice to see what they can do in an area, in a energy-friendly state like Louisiana and Texas. So great performance by and great execution by our team there, I'm really excited to have that in service so early. And it is now up and flowing.

Also, several other expansions that are under construction, the 1.6 Bcf a day expansion in total, 448 million cubic feet per day for Dalton, 818 million cubic feet per day for the Hillabee Phase 1, 115 million cubic feet a day for the New York Bay system, and another 250 million cubic feet per day for the Virginia Southside 2. All of these projects are scheduled to be completed this year. So in total, five big Transco projects are scheduled to be placed into service this year. I might say, just because I think that sometimes it's hard to really put all this growth in perspective, that just the projects that I mentioned here brings on about 4.5 Bcf a day of expansion capacity on Transco, and I'll remind you that, that is all 100% contracted. So we do not have volume risk against that 4.5 Bcf a day.

Pretty impressive when you think back to 2010 with Transco being about a 10 Bcf a day pipeline back in 2010. So again, great work by our team, both capturing business and growing that system. And speaking of growth, Transco did set another delivery record for peak day and three-day average deliveries of 13.7 million dekatherm per day and 13.6 million dekatherm per day on January 7 through to January 9. And so these are measured as we deliver gas into our customers, and really impressive considering we had a fairly moderate winter here in 2017. That sounds something really easy to roll off my tongue is to talk about hitting that kind of peak day on a system.

But I'll tell you, it takes a tremendous amount of coordination and focus on operational excellence by our teams to reach brand-new levels of delivery off of this massive system, especially impressive when we have so much construction and maintenance going on, on the system to be able to coordinate those. So I think a lot of times, we all take for granted the extraordinary work that our workforce do to keep up with the kind of growth and volume and construction going on, but our Transco team has been doing it and doing it in stride.

Looking out west, our Northwest Pipeline, very quietly, our team moved ahead out there and got a rate case settlement or pre-settled rate case with FERC. And though that's been filed now with FERC on January 23, those new rates will be effective on January 1, 2018. I'll also note here that Northwest Pipeline set a monthly record for deliver in January of this year as well. So that was a whole month of January record. So new monthly record. In the Central area, Barnett, the new gathering agreement course executed on November 1 with Total, and really took the risk, of the collection risk we had on those MVCs, and exchanged it for large cash payments received at closing. We also improved our counter-party credit rating and received drilling capital commitment from Total. So a lot of activities starting out there, really excited to work with Total, that area has really been neglected, and certainly it's a very important gas resource to the nation and one that we think ultimately is going to get called on here as the demand picks up here in the U.S.

For our Marcellus-for-Permian transaction, this is really an important transaction for us. Great work by Frank Billings and the team to get that deal closed, and it really puts us in an area we really like. And in fact, the Bradford Supply area where these two systems that we acquired additional interest in, just set another record on February 10 of 2.725 Bcf a day, and that means for the Northeast PA, so this is just for our two big dry gas systems up in the Northeast PA, we exceeded 5 Bcf a day on that same day on February 10. So just to put that in perspective for you, on just two of our systems and in just two counties, we gathered over 7% of the entire U.S. production. So really starting to point out how incredibly important the Marcellus is, and these big dry gas systems are up here. So we're really excited about the acquisition there in Marcellus. And I think it's a great trade for Western and Anadarko as well. So a great example of a smart trade between two companies.

On the Northeast G&P volumes, daily volume records across the northeast systems with strong winter pricing. And so as I mentioned, we continue to see great records hit, Northeast PA was the most impressive of that. But I think as we enter into the fourth quarter here, we start to see some capacity open up in the southwest part of the play, and in the Utica we're going to start to see some increased volumes there as well. So on the coming soon list, of course we have the Geismar process, that final bid from the late first quarter. But I also, one thing is not on the page that I'd like to mention here, is that we just announced the new open season on the Southeastern trail project. And this is a project that will run from our existing Pleasant Valley receipt point near Dominion's Cove Point Pipeline in Virginian, down to the south, the location is far south as our existing station 65 Pooling Point, which is a very liquid pooling point in Louisiana in St. Helena Parish, Louisiana.

So another project, it's great to see this list of 20 or so projects who we're pursuing, start to come in fruition. But we're in the early stages of this project, but we've seen great evidence of continued strong customer interest, and pulling supplies off of Transco to meet their growing demands. So let's now move on to slide six. So just little bit of overview on the transaction we did there in trading out of the Permian system. That was a non-operated Delaware Basin joint venture. It was a joint venture with Western Gas and of course Anadarko then as the parent. And so we traded out of that area. And I'll tell you, it's certainly an area that has a lot of growth. It also had a tremendous amount of capital load against it. And so we're trading into an area that has tremendous free cash flow and growth that'll be associated in volumes as that area gets opened up to new takeaway capacity. So we think the timing of this transaction was really good, and very much meets our strategy. We also took in $200 million in the trade, and again, we're very excited to continue to double down on our focus on natural gas and natural gas market fundamentally.

If I move on to slide seven and look at the financial repositioning that we've done recently. We're really excited about this, and I just want to highlight some of the real positives that came out of this transaction. First of all, we really are getting to the point – no external equity financing need against our existing business plan. Certainly, the market risk, it's always easy for us to ignore market risk and market access risk. But I'll just remind you where we were a year ago in terms of access to the market risk. So we're really excited, I think that's a key risk to take off the table so that both we as a company and investors can really focus on our business performance, which we think has continued to be strong despite some ups and downs in the equity markets.

On the coverage side, a really interesting note here, and one I think that's being missed as people look at comparison of WMB to other entities, and we just point out here that the Williams economic coverage of 1.7 times is expected for 2017. Of course, that's driven off of the 1.3 times coverage at MB, plus 74% interest in the 1.2 times coverage at WMB. So we'll provide some detail on that in the back. But pretty impressive in terms of the kind of coverage that we're building that support to WMB dividend and yield. Looking at the strengthened credit metrics for both PZ and WMB, we note here the amount of debt that we've taken down here in the fourth quarter of 2016, as well as the first quarter of 2017. And we continue to really bring this down pretty dramatically, and in fact, if you look at where we were in just five months now with lower PZ debt by nearly $2.5 billion before asset sales, and WMB debt reduction down $75 million in the fourth quarter of 2016, and an additional $500 million expected here in 2017 as we execute our plan. So really bringing that down rapidly, and certainly that was a goal of a lot of the transactions that we've been taking on.

The PZ cash cost equity reduced by 50%. We now have a top quartile yield amongst our MLP peers. And while we don't have any plans to use that cost of capital any time in the direct future and within our existing business plan, we think it's very important to have that low cost of capital because just as I pointed out, we continue to find new places to invest money in new projects. And we think for the long term, having that little cost of capital is exactly what we think matches up with this low risk growing cash flow profile that we have at PZ and WMB. And so speaking of low risk cash flow deposit, if we look at slide eight here, very impressive look at our EBITDA growth at 8% year-over-year, EBITDA growth, and that is going to continue as we continue to invest about 68% of our 2017 capital in the regulated pipeline. And so we're really excited about how steady this growth in EBITDA has continued to perform. And that's with things like the sale of our Canadian assets as well in there. And so really think this perhaps gets overlooked a bit by investors in terms of how steady and predictable the cash flow growth has been.

And as we look at slide nine, really I think a very interesting picture here. So let me just quickly explain this to you. On the top chart there, you have the EBITDA growth. Now, this begins in Q1 of 2015. And why Q1 of 2015? A couple of reasons; one, that is right at the first quarter after the crude oil price collapsed in November of 2014. It also was where we consolidated and merged ACMP's operating numbers with us. So this is a nice, clean look at WPZ EBITDA growth. And then you can see below that our peers, you can see the peers listed down there in the footnote, and you can see the dash lines are peers that haven't reported yet, but that's their consensus EBITDA. So under any scenario here, I think it's safe to say that we have continued to perform extremely well against our peers in terms of EBITDA growth.

But if you look down on the slide below there, we don't really feel like that's being reflected in our valuation at WMB, you can see us trading there as eight out of nine peers, and in terms of the enterprise value to EBITDA. And so we really believe that if we continue to execute, continue to show this growth in EBITDA, we're going to move up that slide. I really think, if you look at the fundamental underpinning of our business plan, I don't think we should be anywhere but over towards the far left on this slide because I do think we have the most identifiable growth. I think we've got very solid financial picture underneath this now. And so we really, as a team, are very focused on moving this EV to EBITDA multiple over to the left, and we certainly think we deserve that.

So just in closing here, just to tell you, it really is hard to believe in the natural gas demand growth, and not believe in these kind of value that Williams is going to continue to generate. So we feel very strong about this natural gas fundamentals pictures. Obviously, we're continuing to double down on that through the transactions that we're taking, and we believe that even with the fairly mild winter that we've had this year, we're going to continue to see a need for natural gas market growth. We're certainly starting to see the LNG starting to pull. We're seeing supply is not really reacting yet. Certainly here through the third quarter and fourth quarter of 2016, we really haven't seen supplies react yet, but we know that they've got to, to keep up with all the tremendous amount of demand growth that's contracted for on our systems.

So we're going to be continuing to stay very focused on the strategy. We're going to continue to keep ourselves well positioned [ph] right in (33:17) between these very best supply basins, and the very best market growth. And we think that the advantage of our footprint will continue to shine over time, and the continued growth and opportunities that continues to fill in our pipeline of opportunities is going to continue for some time to come. So with that, we thank you very much for your attention this morning. And we'll turn it over for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you, sir. [Operator Instructions] We'll go first to Brandon Blossman, Tudor, Pickering, Holt & Company.

Brandon Blossman
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

Good morning, everyone.

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Good morning.

Brandon Blossman
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

I guess, let's start at Atlantic Sunrise, Alan. What determines, or what's the timeline look like from here? Is there a risk that the project [ph] lifts (34:11) from current in-service targets, and what would drive that risk?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah. Sure. Thank you for the question. Really, the primary risk at this point really remain around the permitting risk from the state of Pennsylvania. We've been working very closely with the state. They've been very cooperative, and they very much understand that we're going to do things right, and they are really doing the right job of keeping things on schedule on their side. So we're feeling very good about the work going on there with the State of Pennsylvania. Certainly, the Manor East 2 and the PennEast approvals this last week are good evidence of them continuing to execute on their side. So we're very thankful for the work that's going on with the pay debt there. They've got a lot of work on their plate, but they've continued to keep pace with us on our work. So that's probably the next big step, if you will, for us is to get that 102 and 105 permit from State of Pennsylvania. We still need to get the 404 permit from the core of engineers as well, but feel like that's moving along very handily as well. And of course, they've been heavily involved in the FDIS all along. So that's all part of moving that permit ahead. So really don't see the major risk on those two, but that is probably the risk that I would point to in terms of timing risk at this point.

Brandon Blossman
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

So best case, it sounds like you still think that you can hit the in service targets that you set out there.

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah. I think, of course, we still have it risked in our model. We still have it pushed out six months from that target date. But I would tell you, obviously, as we continue to click off things like the FERC Certificate, we continue to reduce the risk and the contingency that's built into that schedule. But right now, we still have it in there. But obviously, every permit we check off will start to pull that back. So I feel very comfortable about where we are, I would say, and feel good about being able to reach that target. But we all know that building pipelines these days is difficult, and we don't want to forget that as we lay out a financial forecast.

Brandon Blossman
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

Fair enough. And then a follow on related to the Bradford system. How should we think of that as it evolves with Atlantic Sunrise coming online? Is there more capital to be spent? Has it been fully capitalized? What the volume trajectory looks like over the next two years call it, and then earnings flat as a cost of service system, I believe, or should we expect [ph] uplift (39:58) there?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah. You know it well, the very little incremental capital required because most of the big systems have been out, so it's really just well-connect capital, there will [ph] be after the (37:20) activity to keep up with that, but the capital there, load, is very small. And it is, you are correct, it is a cost of service system. And so even though we may see some volume increase in pick up and some incremental capital, the base systems are cost of capital. I will say however though, that the positioning of those assets, and the opening up to those markets does allow us to bring in third parties to those systems. And so we do think that that will provide an opportunity for us out there to continue to expand our presence in the area. But generally, fairly moderate growth in earnings because of the rate base nature of those assets.

Brandon Blossman
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

Perfect. Good color. Thank you, Alan. That's all for me.

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Thank you.

Operator: We go next to Jean Ann Salisbury, Bernstein.

Jean Ann Salisbury
Analyst, Sanford C. Bernstein & Co. LLC

Q

Good morning. I wanted to ask more about the Southeastern trail project, Mountain Valley and Atlantic Coast are interconnecting to Transco. Is it targeting those volumes, and how much capacity do you have down there that could go south bound, like maybe 3 Bcf/d or so?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah. I would tell you that the amount of volume is – I mean, we can build and build and build, where we get – we have to get beyond the existing, right away existing capabilities of the pipeline the more expensive it gets. And so the first 400 million, 500 million cubic feet a day of capacity is fairly inexpensive. And as we get beyond that it gets more expensive. And so we're trying to make sure that we get the very best value for that, and that we know what the right size to build. I think the biggest challenge we have, frankly, is really picking that right size. It's not whether or not there is a project there, it's a question of making sure we pick the exact right size, and we get the very highest return available to us based on that. So said another way, the larger the project may get, the lower our return may get. And so we've got to pick, really, what the perfect project is there. In terms of who those volumes are coming from, I would tell you the market will decide that. And certainly, that would be an area to pick it up, but it's looking like there's demand well in excess of that in terms of the market demand. So I'm not going to get real specific on that, and the open season, of course, will tell who's going to pick up that incremental capacity. But that's, of course, the purpose of the open season.

Jean Ann Salisbury
Analyst, Sanford C. Bernstein & Co. LLC

Q

Got it. That's very helpful. Thanks. And then secondly, you've had kind of talk to a lot of investors about the IDR transaction last month. I'm just wondering if there's anything in hindsight that you would have done differently or anything that you think investors may not have necessarily seen the same way that you [indiscernible] (40:27).

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah. Thank you. Well, I would just say, I think we really are focused on the long-term benefit of sustaining growth in the business. And getting the IDR put away, I think, what was going to continue to be a level of uncertainty about whether or not that IDR could be met, how much waiver was going to be. So we felt like there's a lot of market inefficiency that was going to come with that. We also felt like we needed to move quickly to both take down debt. And importantly, I think probably this is the piece that you can have varying opinions on, is getting ourselves in a position where we're not having to be reliant on access to the markets over time and the volatility of those markets. We certainly saw that, that really damaged us last year as we had a lot of growth obligations, a lot of capital obligation, and yet we were having to issue debt at a very high cost, and the equity markets were extremely expensive as well. And so we feel like getting that risk out in a way that we can fund all this great capital in front of us is a really nice way to lock in margin between our cost of capital and these great projects that we have. So I would say, it's probably [ph] dealt (41:47) and thinking about the risks that are out in the markets long term, and very much a focus on a sustainable model that can grow dividend for years and years to come.

Jean Ann Salisbury
Analyst, Sanford C. Bernstein & Co. LLC

Q

Thanks for that. That's all from me.

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Thank you.

Operator: Next is Shneur Gershuni with UBS Financial.

Shneur Z. Gershuni
Analyst, UBS Securities LLC

Q

Hi. Good morning, guys.

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Good morning.

Shneur Z. Gershuni
Analyst, UBS Securities LLC

Q

I was wondering if we can sort of shift focus a little bit here and talk about the sales process that you have ongoing. I kind of guess I have a two-part question here. You've had a couple of recent asset sales. Is there anything left besides just Geismar in that process? And then has the sales exceeded or they in line with your expectations. And I guess, what I'm really asking is how should we think about that $2 billion target that you put out there? Could you be above that number at this stage with how you [ph] perceive it (42:43) thus far?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah, Shneur, thanks for the question. First of all, one thing I want to remind people is, is that target that we put out there is a $2 billion after-tax number. And so I think we've been pretty clear on that. But that is what we've said and will continue to say. And I would just say that the Geismar process is going very well, and gaining confidence as the days go by on that. And so I feel very good about that. In terms of other assets, I would tell you that there are some other assets in and around Geismar. For instance, some of the pipeline, the NGL and Petchem pipeline systems in the Gulf Coast, that will not be all that strategic to us. And so I think we're going to be kind of an [indiscernible] (43:39) of looking at opportunistic purchases of assets.

And so whether there are players that have great synergies with some of our assets and are willing to put some of those synergies on the table to be the right buyer, then I think that's going to be the kind of sales that we're going see, and whether that's Mid-Continent, the stuff that's in the central region today in the Mid-Continent area, or whether it's the NGL and Petchem liquids line, it's really going to be a matter of somebody that might be a better buyer for those assets. So I don't think we're going to be in a [ph] much sale (44:16) mode at all. I think we're going to be very much in an opportunistic mode, and looking to see if somebody can make better use out of the asset than what see it. And so I think that's kind of the two areas you should think about. And to whether or not we'll blow pass that $2 billion number is very dependent on how hungry the market is and how nice the pricing [indiscernible] (44:40).

Shneur Z. Gershuni
Analyst, UBS Securities LLC

Q

Okay. And just a couple of follow up. Once Geismar is sold, I believe you've talked about your commodity exposure would be around 3% going forward. So kind of the recent spike in NGL prices shouldn't necessarily have much of an impact. But when you think about the impact on your producer customers, are you seeing economics improving in some regions as a result, are there some green shoots where customers are starting to step up? And maybe in some specific areas, possibly the Eagle Ford and the Northeast, I was wondering if you can sort of [indiscernible] (45:16) of the land as to where you see opportunities and where things are going to roll from here?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah. I think it's very interesting to me right now looking at the natural gas picture. And we continue to see U.S. production continuing to fall. And yet, the market doesn't seem to be responding all much that yet. That is going to come home to roost. But I will say that when we did see some length in the market in 2017, we did see some activities in the west. We start to see a few rigs come back in the west. Walt and his team has done a great job of capturing business out there as that's occurred. And we also saw quite a bit of activity in the northeast. I think the number of pad connections that are being requested right now in the northeast is really catching my attention, and Jim Scheel and his team have been doing a good job of capturing that business.

So I'd say it's more than green shoots in places like the northeast because those are [ph] no firm add (46:26) request. But it's going to have to come on stronger, I think, in what we're seeing so far to [ph] arrest (46:33) the kind of production declines that we're seeing in the U.S. right now. And so yes we're seeing some resurgence, but I don't think it's enough, frankly, because I think we're kind of got spoiled leaning on [ph] docks (46:46) and tie-ins with existing – of new production during 2016, and we've kind of been lulled to sleep on the fact that our productions continue to decline pretty dramatically on U.S. natural gas. So I feel, I think 2017 is going to be a very interesting year for U.S. natural gas, and I definitely think we're going to have to see some resurging activity in [indiscernible] (47:10), in the Rockies, and we have seen some resurgence in the Haynesville as well.

Shneur Z. Gershuni
Analyst, UBS Securities LLC

Q

Great. And one final question on constitution. Given the recent changes in Washington, do you see the odds of success increasing with this project? Are there things that we should be looking for out of the FERC, or should we be focused on the state in this scenario?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

I'm very, very encouraged about Constitution as we sit here today. I think it's becoming very evident that it's a critical pipeline in terms of serving gas demand and power generation needs for the northeast. That issue is getting louder and louder, and it's going to continue to be because there's no way to ignore it. In addition to that, I would tell you, the labor unions who obviously have had a pretty big voice in the Trump administration are very much on our side, and I think are going to be really pressing hard on the administration on that issue. And so, I think, there's a lot of people with their hands in the air right now in DC, and trying to get attention drawn to their particular projects or their particular issues they need to resolve, and we're certainly one of those. And I think Constitution is going to be a great example of one that can bring jobs and critical infrastructure. And so, I think, it's extremely well positioned to get some attention at the Federal level, and hopefully we'll be able to work something out with the state and do that in an amicable way. But I think there are several avenues that that can be impressed at the Federal level if the state does not want to cooperate.

Shneur Z. Gershuni
Analyst, UBS Securities LLC

Q

Thank you very much. Appreciate the color.

Operator: Next is Ted Durbin with Goldman Sachs.

Theodore Durbin
Analyst, Goldman Sachs & Co.

Q

Good morning. If I can just talk about the – I think, in your slides in January, you talked about 20 prospective projects that are not in the backlog right now. Can you just talk about the returns you would expect to get on this? I think, you're building your current backlog at around 6 times to 7 times EBITDA build multiples. Is that kind of what you're looking at for the next wave?

And then, if you can give us some sense of the capital there, again, I think of $100 million to $200 million. So, if we get them all, are we [indiscernible] (49:23) $2 million to $4 million or could the number be higher than that?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Yeah. So, just few things here. First of all, as I mentioned, the Southeast trail project is a good example, the one I mentioned we have an open season on. We'll be able to – I don't need to make this sound too easy, but we basically will be making decision between size and return on that project. And so, the larger it gets, the lower our return will go. But at the smaller level, we can make a very high return.

So, obviously as we look at our cost of capital, that's a critical analysis for us to look at. But I would say, we certainly have the opportunity on that project to be in the 6 times to 7 times level, maybe even higher than that. But then, you also have projects, for instance, on – big projects up in the Northeast that are fully cost of service, so like the Rockaway Beach lateral – sorry, the Northeast Supply Enhancement project. Some of those projects are cost of service projects. Hillabee is a good example of a cost of service. We make a lower return on those projects because they are – I mean, we don't have any construction risk on those projects. And so, those are more in the 8 multiple level but, I would say, probably the mix is probably more like 80% of higher return and 20% at our [ph] full (50:58) cost of service projects that are out there.

And in terms of the size, yeah, that number is probably about right. I think, we certainly see capabilities of continuing to invest in the $2.5 billion range for quite some time on an annual basis based on these projects coming in.

Theodore Durbin
Analyst, Goldman Sachs & Co.

Q

That's great. Very helpful. Thank you. Next question. So you've got these targets out there for leverage for 2017. I guess, I'm wondering what the targets are beyond that, if you can help us both on WPZ standalone and then WMB consolidated?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.

A

Don, do you want to take it?

Donald R. Chappel
Chief Financial Officer & Senior Vice President, The Williams Cos., Inc.

A

Hey, Ted. It's Don. No, we haven't disclosed the specific targets. But certainly, we want to be squarely solid within our ratings. So, I'd say, somewhere in that 4.0 to 4.5 is kind of the right zip code. And again, we're trending down, and I think that's directionally where we're heading.

Theodore Durbin
Analyst, Goldman Sachs & Co.

Q

4 to 4.5 for WPZ. And then, for WMB?

Donald R. Chappel
Chief Financial Officer & Senior Vice President, The Williams Cos., Inc.

A

Again, we have a sort of target out there. We have disclosed that we plan to pay down some debt, $500 million this year, and we would expect some excess coverage again in 2018 that would enable us to pay down some additional debt. So, that consolidated leverage would be coming down at the same time as PZ leverage.

Theodore Durbin
Analyst, Goldman Sachs & Co.
Q

Got it. And then, again, with the big change in the restructuring, just economically WMB is of course much more dependent on what WPZ does. I guess, again longer-term, what are your target coverage levels for WPZ? Is there any reason why you would retain excess cash flow there and not pay it up in distribution that would then come up to WMB?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

I think [ph] it's important (53:02) to maintain some excess coverage to fund your capital as well as to provide a buffer against risk, whether it's delays in projects or anything else. And we think that the market provides attractive valuation when the market doesn't worry much about coverage. So, I think, we'll plan to maintain a sufficient amount of coverage that the market doesn't worry about it, and as well to provide some level of funding for capital.

Theodore Durbin
Analyst, Goldman Sachs & Co.
Q

Great. And then, last one for me. You've sort of spoken about the Northeast gathering business and kind of the uplift you could see. It looks like we've got better visibility now on Rover maybe and [indiscernible] (53:51) and some other big takeaway projects. How much of an impact does that have on your volumes in the Northeast there, Southwest Pennsylvania and the Utica?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

Yeah. Really excited about that project pushing ahead, really excited about winning all takeaway projects just because we've got so much leverage in the Northeast in terms of our gathering systems. So, I could see that [indiscernible] (54:15). And yes, I would say, the areas that are going to be enhanced by that, certainly the dry gas Utica is going to get a nice pick-up off of that. That's where a lot of that gas will come from [indiscernible] (54:30) as the Southwest Marcellus area as well. And so, we're starting to see a lot of those assets fall in at the hands of better capitalized and really great operators up in the basin there in the Southwest PA area. And so, we really think we're going to see some big [ph] pull and overcome (54:49). We saw a little bit of improvement from REX 3. We see TETCO M2, Zone M2 creating up a little bit over the Northeast Pipeline index as that opened up. And so – but I think, with Rover coming on, we'll see a lot of people preparing to meet their obligations on Rover, and we're excited to see our volume [ph] lift off of that (55:13).

Theodore Durbin
Analyst, Goldman Sachs & Co.
Q

Great. I'll leave it at that. Thank you.

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

Thank you.

Operator: We'll go next to Tom Abrams with Morgan Stanley.

Tom Abrams
Analyst, Morgan Stanley & Co. LLC
Q

Hi, thanks. Just a follow-up on that balance sheet questioning. If you could start from scratch, would you have any debt at the MB level?

Donald R. Chappel
Chief Financial Officer & Senior Vice President, The Williams Cos., Inc.
A

I think it's a theoretical question. So I'm not sure how to answer that, because we...

Tom Abrams
Analyst, Morgan Stanley & Co. LLC
Q

Okay. Let's put it this way. As time goes by, why wouldn't you just continue to pay WMB down [ph] towards zero (55:44)?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

I think that's a policy question. I think the board will have to take on in time. I think, right now, we're focused on paying down debt with our excess coverage, I think, beyond our guidance period. I think, we'll have to wait and see what direction the board choose to take. We don't have, just to kind of point out, we do have a revolver balance that is efficient to pay down. We don't have bonds that reduce, so anything we do in the bonds would be open market purchases or tenders, which would likely be pretty inefficient. So, again, I think, the near-term focus will depend on the WMB revolver.

Tom Abrams
Analyst, Morgan Stanley & Co. LLC
Q

All right. And then, also on the, I recall, a month or two ago that your tax payer status was out – no taxes through 2025, maybe 2024 with the Geismar sale. In slide 12, we have a footnote there about – at least through 2020, that is what – that's the nature of your new guidance, so something has changed in the general picture.

Donald R. Chappel
Chief Financial Officer & Senior Vice President, The Williams Cos., Inc.
A

I think, our prior guidance was, we do not expect to be a tax payer through 2020. Beyond that will be a function of future capital investment. I think, we do have significant capital opportunities to invest, which would provide a tax shield beyond 2020. But we've not provided any guidance beyond 2020.

Tom Abrams
Analyst, Morgan Stanley & Co. LLC
Q

All right. Thanks a lot.

Operator: Next is Faisel Khan with Citi.

Faisel H. Khan
Analyst, Citigroup Global Markets, Inc.
Q

Yeah, thanks. Good morning. Thanks for taking my question. Now, Alan, most of the restructuring now out of the way, and sort of the balance sheet sort of getting close to where you guys want it to be, how are you thinking about acquisitions, either bolt-on acquisitions on larger transactions or are you even thinking about these sort of opportunities at all?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

Yeah. Faisel, we certainly are. We're certainly looking at areas up in the Northeast where there are some great synergies between various operating systems up there. And so, we certainly have got our eyes on that. I think that the market vantage points have to come together to get to a trade there. But certainly there's a lot of operational synergies to be had up there. And as any basin does as it matures, those opportunities come together.

And so, I think, right now, we're continuing to focus on honing our unit operating cost being as low as we can where we are, but with an eye to the future for what kind of capital efficiencies can be gained between us and some of the systems that we have joint ventures in. So, pretty excited about the way the Northeast will roll up there. But I'd say, that's probably the primary area that we've got our eyes on, because we see so much operational synergy. It's not necessarily a financial transaction for us. It's really just the improvement in operating cash flows that we think we can get out of those areas.

So, we'll continue to look at those, but obviously we have to come to the meeting of the minds between the buyer and the seller to get there.

Faisel H. Khan
Analyst, Citigroup Global Markets, Inc.
Q

Okay. And then, last question for me. Just – after the financial repositioning announcement you guys made on January 9, is there any significant change to your deferred tax asset from doing that transaction in terms of what we'll see in the 10-K when it comes out?

Donald R. Chappel
Chief Financial Officer & Senior Vice President, The Williams Cos., Inc.
A

No, but we did pick up a higher share of the depreciation deductions. So, again, depreciation deductions are now 74% claimed by Williams versus the 58% that we had previously. So, we will pick up somewhat higher shield.

Faisel H. Khan
Analyst, Citigroup Global Markets, Inc.
Q

Okay. Understood. Thanks.

Operator: To Jeremy Tonet at JPMorgan.

Jeremy B. Tonet
Analyst, JPMorgan Securities LLC
Q

Good morning. Thanks for sneaking me in the end here. And just want to touch based on the Central segment that had stepped down a bit quarter-over-quarter. And I was just wondering if you could dive into that, maybe a little bit more granularity? [indiscernible] (01:00:02) could be bouncing back a bit in the first Q, also knowing that you had sold some of those assets there?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

Yeah. I think, Jeremy, probably the primary issue there was the $23 million impact that was a pretty complicated story there. But we basically were taking a charge from the fact that we booked the MVCs from prior periods. And so, once that MVC was paid down, so there's a $23 million one-time impact there in the fourth quarter that certainly impacted Central that you wouldn't see on an ongoing basis.

I don't know, Walt, do you have anything to add to that?

Walter J. Bennett
Senior Vice President, West, The Williams Cos., Inc.
A

No, I think, there were some volume declines, but I think we'll see if that's holding pretty flat going forward with additional activity [indiscernible] (01:00:58). We'll keep it – any declines [indiscernible] (01:01:01).

Jeremy B. Tonet
Analyst, JPMorgan Securities LLC
Q

Great, thanks. And then, maybe just touching on the West transaction a bit there, if you could give a little bit of color as far as how you think the volumes are trending there or any synergies that you can bring to that asset with your increased ownership or other plans you might have?

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

Yeah. Not a whole lot of synergies to be gained further there as we sit here today because we are the operator already on those assets. Certainly, I'd say, we're extracting all we can there today. So I don't really see a big pick-up in synergies. I think, really the big story there is, as Atlantic Sunrise and other projects and hopefully Constitution now start to open up that Northeast PA to market see volume growth outside of just the current JVs that we have that can utilize some of our presence in the area. And so, I think that will be a real positive for us as that area gets exposed to the market.

We're very convinced that that area is going to have to come alive in a big way to keep up with the market demand once the takeaway infrastructure is built. So, we're very bullish on the area. But there's not really a whole lot to be said about operational synergies that we're not capturing.

Jeremy B. Tonet
Analyst, JPMorgan Securities LLC
Q

That's helpful. That's it from me. Thanks.

Alan S. Armstrong
President, Chief Executive Officer & Director, The Williams Cos., Inc.
A

Thank you.

Operator: That concludes our question-and-answer session for today. Mr. Armstrong, at this time, I would like to turn the conference back to you for any closing or additional comments.

Alan S. Armstrong

President, Chief Executive Officer & Director, The Williams Cos., Inc.

Okay. Well, thank you all very much for joining us. Really pleased to report another strong quarter. And again, just want to thank the organization here at Williams and employees for their dedication to continuing to perform so well despite a pretty rocky year. I would tell you, we are all very excited and looking forward to 2017 and really putting the focus on growing the business as we deliver some of these big projects here in 2017. So, thank you very much for joining us. We look forward to speaking with you next quarter.

Operator: This concludes today's conference. We do thank you for your participation. You may now disconnect.