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DCP - Q1 2018 DCP Midstream LP Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Q1 2018 DCP Midstream LP Earnings Conference Call. (Operator Instructions)

As a reminder, this conference is being recorded. I would now like to introduce your host for today's conference, Irene Lofland, VP of Investor Relations. You may begin.

Irene Lofland - *DCP Midstream, LP - VP of IR*

Thank you, Jiggy. Good morning, and welcome to the DCP Midstream First Quarter 2018 Earnings Call. Today's call is being webcast and the supporting slides can be accessed under the Investor section of our website at dcpmidstream.com.

Before we begin, I'd like to point out that our discussion today includes forward-looking statements. Actual results may differ due to certain risk factors that affect our business. Please review the second slide in the deck that describes our use of forward-looking statements, and for a complete listing of risk factors, please refer to the partnership's latest SEC filings.

We will also use various non-GAAP measures, which are reconciled to the nearest GAAP measures and schedules in the appendix section of the slide. Wouter van Kempen, CEO and Sean O'Brien, CFO will be our speakers today. And after their remarks, we will take your questions.

With that, I'll turn the call over to Wouter.

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Thank you, Irene, and thanks everyone for joining us. We're off to a great start to 2018, and we delivered strong Q1 results that demonstrate the success of our diverse portfolio and our teams dedicated focus on innovation, operational excellence and growth.

During the quarter, we generated distributable cash flow of $171 million, driven by outstanding logistics and marketing results and continued cost efficiencies. Sand Hills had record throughput volumes and is ramping quickly with expansions coming online. We continue to strengthen our balance sheet with leverage of 3.8x, and our distribution coverage was 1.1x.

Our integrated asset portfolio provides us with significant opportunity to grow and extend our value chain, as we remain focused on our DCP 2020 strategy to become the most reliable safe low-cost midstream service provider.

On top of the strong financial results, our team continues to perform with remarkable safety outcomes. Building on our record setting safety performance in 2017, the GPA midstream Association recently honored DCP with a Chairman's award for safety improvement, and a second-place safety award for large companies. We are incredibly proud of our employee's consistent commitment to safety, and we thank them for their diligent efforts.

Today, we are extremely excited to discuss our substantial multiyear expansion in 2 of the most prolific basins in the country. Let me give you a snapshot into the things we'll be discussing on today's call.

Within our already extensive footprint in the DJ Basin, we are further establishing our leading position well into the next decade by announcing a comprehensive, integrated strategy. This plan includes up to 1.5 Bcf per day of capacity, inclusive of our new plan 12 and accelerations of both the Mewbourn 3 and O'Connor 2 plants. On top of that, we're expanding NGL take away capacity up to 220,000 barrels per day through the Southern Hills expansion via White Cliffs, and the Front Range and Texas Express expansions.

Lastly, we are in anchor ship -- in Cheyenne Connector, a $600 million cubic feet per day gas takeaway pipeline that is in development.

Now let's switch to the Permian, where we are also executing on strategic growth opportunities.

We recently completed an expansion of our Sand Hills pipeline to 365,000 barrels per day of NGL takeaway, and I'm proud to announce that we've already announced capacity to approximately 400,000 barrels per-day, solely through applied technology and innovation.

The next Sand Hills expansion is well on base and is now expected to increase capacity to 485,000 barrels per day by the end of 2018.

Additionally, the Gulf Coast Express gas pipeline is very close to being fully subscribed. This pipeline will transport approximately 2 Bcf per day of natural gas and is expected to be in service in the fourth quarter of 2019. We are continuing to execute on our laser focused capital allocation strategy that provides long-term solutions for our customers and significantly elevates our competitive advantage.

Turning to the next slide. I want to drive how -- just how substantially we are expanding every segment of our value chain as a fully integrated midstream provider. We are seizing tremendous opportunities for organic growth that highlight DCP's dedication to capital efficiency, portfolio optimization and disciplined diversification. All planned Greenfield capital projects are focused with strong returns and fall well within our target of multiple range of 5 to 7x or better.

Notably, expansion projects tend to have even better returns. And our upcoming NGL expansion project are no exception as you can see on the slide. We continue to leverage our G&P footprint to grow our logistics and marketing business, providing greater stability and financial returns within our value chain.

Let me put into perspective how we have changed DCP over the years. 7 years ago, 90% of our cash flow was driven by our G&P business with the consistent multiyear strategic approach to transforming our asset base, today we are a much more balanced company with our marketing and logistics business responsible for almost half of our cash flow.

On this next slide, I'm excited to take a deep dive into our DJ strategy. Our customers have had great success, producing incredible resources from some of the best rock in any basin, right under our feet here in Colorado. We're excited to announce that we're in lockstep with this prolific production as we are building the necessary capacity and infrastructure to unlock the basin's full potential.

Over gathering and processing site, we are adding up to 1.5 Bcf of capacity, with 0.5 Bcf coming online in the next year. We are accelerating the target in-service date of Mewbourn 3, our $200 million a day plant to August 2018. This is our second acceleration of this facility as we continue to exceed our timelines to ensure we provide our customers with needed capacity.

As a benefit of a producer significant agility and, therefore, remarkable production following the downturn, we expect this plan to ramp up very quickly. In response to these anticipated volumes, not only are we also accelerating our O'Connor 2 in-service date to Q2 2019, we are expanding its capacity by 50% to 300 million a day with up to 100 million a day bypass.

Additionally, today, we are announcing a new plant in the DJ. We've secured land and filed permit for Plant 12 to further meet the projected needs of our customers. Plant 12 will have up to 1 Bcf a day of capacity including bypass and is expected to begin initial phases of operation in 2020.

To remind you, let me quickly explain what a bypass does. Adding a bypass to a plant is a very capital efficient way to increase overall capacity without actually processing the gas. At the tailgate of the plant, we plant unprocessed gas from the bypass with a processed gas from the plant, while still meeting residue pipeline specs. Overall, we are pleased to announce that these strategic growth projects in the DJ will almost tripled our capacity in the basin, and this program will clearly establish DCP as the largest, fully integrated midstream service provider in the DJ for years and years to come.

But that's not all, in tandem, with advancing our upstream processing growth, we are increasing our downstream footprint with a multipronged approach to ensure our customers can rely for DCP to deliver throughout the full value chain.

NGL takeaway capacity in the basin will increase by up to 220,000 barrels a day via an expansion of the Front Range and Texas Express Pipelines and an exciting new opportunity we announced yesterday with Southern Hills via White Cliffs. We finalized a long-term 50,000 barrels a day capacity lease in the White Cliffs pipeline. This crude pipeline will be converted to a 90,000 barrels a day NGL pipe, with the ability to expand to 120,000 barrels a day.

Let me put this in perspective for you. This is a huge win-win. All volumes from the new White Cliffs NGL pipe are dedicated to flow into and through Southern Hills, giving us the opportunity to not only fill up all available capacity on Southern Hills, but also to potentially expand the pipe in the future. This is a highly, highly attractive capital efficient opportunity to add new volumes and increase utilization on Southern Hills. And as a result, our Southern Hills pipeline will basically extend from the DJ Basin all the way to the Gulf Coast market centers of Mount Bellevue, Sweeney and beyond.

And this project is expected to be in service in Q4 of 2019. Additionally, the Front Range and Texas Express Pipelines will be expended by Q2 of 2019, adding another 100,000 barrels of NGL takeaway capacity to the DJ. Finally, DCP has secured half of the capacity of the $600 million a day Cheyenne Connector, adding $300 million per day of gas Takeaway to our portfolio.

The Cheyenne Connector is another important step in extending market access to serve our customers, and we maintain the option to acquire 33% equity ownership stake in this project. All in all, we are talking about a massive, massive game changer in the basin as we continue to provide comprehensive solutions to fully support our customers continued success and record production.

From the wellhead to the NGLs market, DCP will be a reliable long-term partner to our producer customers, securing continued production growth for years and years to come.

The DJ isn't the only basin where we have exciting developments. Transitioning to Sand Hills on the next slide. Just 2 short years ago, Sand Hills capacity was 280,000 barrels per day. We recently completed our expansion to 365,000 barrels per day. And I'm incredibly excited to share that we have now further increased our capacity to 400,000 barrels per day through operational optimization requiring no incremental capital.

Putting that into perspective, this is a real outcome of our DCP 2.0 efforts innovation efforts. Our effective application of new technology resulted in 35,000 additional barrels per-day, which translates to tens of millions of new margin opportunity with strong returns and no incremental capital. On top of that, with the Q1 utilization rate of 95%, we are making excellent progress on our next 85,000 barrels per day expansion to capitalize and continued increase volumes.

In Q3 of this year, we will again expand Sand Hills by approximately 25,000 barrels per day, reaching an increased capacity of about 485,000 barrels per day by the end of 2018. This is 35,000 barrels per day above our previously reported size. To ensure DCP continues to be ahead of the growing demand for NGL takeaway in the Permian. These capacity increases will continue to drive fee-based earnings, well into the future. And we're proud to see the real tangible results of our DCP 2.0 efforts coming to fruition early in the year.

Our strategic growth opportunities in both the DJ and Permian underscore a competitive advantage among our midstream peers. We continue to prioritize projects and Permian basins that are low risk, provide strong returns and continue to diversify our portfolio.

With that, I'll turn it over to Sean to take you through our financial results.

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

Thanks, Wouter and good morning. Today I'm excited to share the details of DCP's strong first quarter driven by our diversified portfolio.

Turning to Slide 8, we delivered strong financial metrics with $171 million of distributable cash flow resulting in a distribution coverage ratio of 1.1x for the quarter.

Our logistics and marketing segment performed very well, driven by higher revenue from our NGL pipelines as well as strong cash generation from our gas storage in Guadalupe gas pipeline. We set record volumes on our Sand Hills asset in the first quarter. And have started to see some modest benefits due to increased ethane recovery, partially contributing to our increased pipeline volumes.

In our G&P segment, we had a solid quarter with continued record volumes and strong cash flows in the DJ, coupled with increasing volumes at Eagle Ford. In fact, in March, the Eagle Ford reached the highest volume level in almost 2 years. We continued to stay focused on driving cost efficiencies as we optimize our base business and corporate functions. And all of this strong execution around our diversified portfolio, more than offset the adverse impacts of our Discovery investment and higher maintenance capital.

Finally, no IDR giveback was needed in the first quarter or was anticipated for the entire year. Looking ahead, in Q2, similar to our historical trends, we will see higher levels of planned maintenance on our assets driving seasonal increases in our maintenance capital and operating costs.

Given consideration to this seasonality, we expect the shape of Q2 to be similar to last year as a result of the aforementioned plant maintenance as well as higher product replacement capital driven by volume growth in key basins. As we look after the second half of the year, we are forecasting it to be higher than the first half, as Mewbourn 3 and the additional Sand Hills expansions come online. Also, we expect to see volume growth in the Permian, Eagle Ford and the SCOOP regions of our G&P portfolio. These growth projects increase volumes will drive associated earnings and we're confident that we're on track to meet our 2018 guidance.

Now on Slide 9. I'll touch on our liquidity and financial flexibility. DCP continues to successfully execute its financial plan ending the quarter with the strong bank leverage ratio of 3.8x and distribution coverage of 1.1x. We've pre-funded our 2018 capital program via our $500 million preferred equity raise, we executed in November last year. And we have ample liquidity with approximately $1.3 billion available on our bank facility. We continue to demonstrate capital discipline.

With our growth focused on strong return capital efficient projects, like the recently announced White Cliffs and Front Range Texas investments that significantly grow our diversified portfolio and add fee-based cash flows. Additionally, DCP has substantial financial sustainability available to us via multiple financial alternatives to fund our growth. Including our banks facility, debt capital markets, preferred equity, our $750 billion ATM program and continued portfolio optimization.

Now I want to briefly touch on deferred policy revision. On March 15, Ford prevised its policy indicating that MLPs will no longer be able to recover an income tax allowance and their cost of service pipeline rates. As we've mentioned in our prior press release, we expect the associated impact to be de minimis, with only about $15 million of revenue, which could potentially be impacted.

Let me walk you through the math. If you take our 2017 transportation revenue of approximately $430 million, and then reduce that amount by revenues that are not impacted by deferred policy revision, you get only $15 million of revenue, which could be impacted. Then consider that a rate reduction would only be a small portion of that $15 million. This is why we are confident that any potential impact, which certainly be de minimis.

Now moving to Slide 10, let me provide you an update on our hedging program.

We've been active in layering on incremental crew propane and butane hedges as we work to further reduce our commodity exposure. Our 2018 estimated gross margin is now up to 78% fee-based and hedged. Weak gas prices have kept us from hedging the gas portion of our position. However, as I mentioned earlier, we are starting to see increased ethane recoveries reducing our gas equity length.

Finally, we've also taken advantage of the stronger crude in NGL outlook and have started to layer on 2019 crude and NGLs hedges.

With that, I'll hand it back to Wouter to provide an update on DCP 2.0.

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Thanks, Sean. On the next slide, I'll update you on how our digital transformation DCP 2.0 is differentiating our company.

We continue to not only see financial results but our customers gave us remarkable feedback that what we're doing is ahead of the curve. All around us, within almost every industry, the technological advancements of the fourth Industrial Revolution are totally and completely transforming the ways companies operate and how they make money.

DCP is no longer allowing that wave of innovation to pass by the midstream industry. We are utilizing real-time decision making with powerful and big data allowing us to optimize assets and seize market opportunities. And in the first quarter, we saw tangible benefits from DCP 2.0. Earlier, we noted the outstanding example of the capacity increases in Sand Hills. DCP 2.0 optimization efforts drove the capacity from 365,000 to 400,000 barrels per-day, resulting in tens of millions of potential margin opportunity. So how did we do that? Leveraging the innovative technology of dynamic set points, we are able to safely maximize our volume capability by knowing real-time conditions, whether they are operating under a set of static and assumed conditions. As a result, our smart control systems continuously implement needed changes automatically to maximize flows.

And the beauty of these efforts is that it did not require a single penny of incremental capital. As we revealed last quarter, our integrated collaboration center, known as the ICC, is executing the operations of the future. This is an industry that continues to rely heavily on SCADA. But we've put that strategy in our rearview mirror as it is a very limited approach. In our ICC, on top of SCADA, we incorporate comprehensive and real-time data from DCF, from engineering simulations, from operating KPIs, from our 8,000 different contracts, financial assistant and current real-time market practice. In Q1, we begin adding even greater functionality within these plant optimization models, which allows our plant operators to drive increased profitability and better reliability.

Ultimately, the ICC gives us the ability to make impactful optimization positions in real-time, rather than daily, weekly or monthly. Resulting in immediate improvements in our operations. Not to mention, the impact of the incredible arsenal of data that we're building as a foundation for predictive analytics.

Beyond our plans, our scope is now advancing to include our field operations, as we've worked to enhance our entire system. DCP operates a vast network of pipelines and maintains the largest fleet of compressors in the industry. As part of our commitment, to continually improve our liability and competitive edge, we plan to incorporate all major field assets into our 24/7 remote monitoring system by early next year.

Importantly, we're also driving innovation across every corporate and commercial function. Digitalization and robotics process automation are being utilized to streamline organization and add value. We have tremendous pride in how our people are stepping up to improve our internal processes and how we applied technology to see transition of the workforce of the future. Our outcome of Sand Hills and those across our entire system and organization are exactly why we're investing in this dramatic transformation, and working so diligently to build our culture of innovation. So let me sum it all up for you on our final slide.

Our portfolio delivered strong Q1 results. DCP has ample liquidity and strong coverage. We're taking a comprehensive and strategic approach to extending our integrated value chain throughout every segment of our business. Our tremendous, multiyear growth program in the DJ Basin will dramatically increase our existing capacity by adding up to 1.5 Bcf per day. We're accelerating our Mewbourn 3 and O'Connor 2 plants and adding Plant 12 to the basin.

Additionally, DCP is playing a critical role in adding up to 220,000 barrels per day of NGL Takeaway and $600 million cubic feet per day of gas Takeaway to the basin.

In the Permian, we've accelerated Sand Hills growth to operational optimization and continued to increase capacity as we moved to expand to 485,000 barrels per-day by the end of this year.

The Gulf Coast express pipeline is almost fully subscribed, which adds additional gas Takeaway within our Permian logistics business. And underpinning all of our operations, we're continuing to differentiating DCP in the midstream space through our DCP 2.0 transformation and our culture of innovation.

To close, I'm confident in our track record on executing and delivering on our commitments. As we continue to add value for our customers and investors. With that, Jiggy, please open the lines for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question is from Shneur Gershuni from UBS.

Shneur Gershuni - *UBS Investment Bank, Research Division - Executive Director in the Energy Group and Analyst*

Maybe we can start off with the White Cliffs conversion for NGL takeaway capacity. I was wondering if you can talk about the economics from DCP's perspective? Does it make sense to redirect some of the volumes from your other takeaway options towards the White Cliffs option? Do you receive better economics or said differently? Is that going to be the cheapest route to get from the DJ to Mount Bellevue versus the existing options?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Yes, it's Wouter. I think the White Cliffs project is a true win-win project. We've been talking with many of you that we were looking at basically 4 or 5 different opportunities and options to take our NGLs out of the DJ Basin into different areas. And I spoke with you all that we were going to most likely, 2 of those. Front Range and Texas Express and one other. And the one other was White Cliffs. As you know, Southern Hills has open capacity. We have about 60,000, 65,000 barrels a day of open capacity. For us, it was really important to what the other solution was going to be, is that Southern Hills was going to be part of that solution. So our base case initially was, we were going to extend Southern Hills from basically Kansas into the DJ Basin, that was probably about a 350-mile lay that we had to do. So could make that $350 million to $400 million in cost. We were also talking with White Cliffs about -- with Sand Group about repurposing their line. And I think this is one of those industry where industry comes together and is doing the right thing. If you think about this what is happening, is we are building about 25 miles or so of pipe in Colorado to connect into the White Cliffs system. At the other site on the Cushing site, what we're doing is we're extending Southern Hills from Cushing to Penova. There actually is already pipe in the ground there that we have, and that's about 45 miles. So for us, it is a massively, massively capital efficient way to do this. And like you're really talking about pennies on the dollars compared to the alternative of extending Southern Hills. So it's a great outcome for White Cliffs because they will -- and Sand Group and their partners because they're going to be able to fully utilize their pipe. For us, it is a tremendously good solution because it's very low capital. We are going to utilize and fill up that extra 60,000, 65,000 of capacity that we have on Southern Hills, and now this gives us an opportunity to potentially also expand Southern Hills into the future. And from an economics point of view, Front Range and Texas Express continues to be a great project, and we're flowing a lot of barrels on that.

From a Southern Hills point of few, we obviously own a lot more from as a percentage base on Southern Hills. So economically, for us and for the DCP unit holder, filling up Southern Hills is something that is very attractive to the DCP unitholders. So I think this is how you should look at that. We will continue to flow things -- barrels on Front Range and Texas Express. But I think you can feel pretty comfortable that 90,000 barrels of capacity on White Cliffs that can be expanded to 120,000 barrels of capacity, all of that is going into Southern Hills. And the routes that will be priced between White Cliffs and Southern Hills is going to be the same as the route on Front Range and Texas Express. For our producer customers, Southern Hills and Sand Hills and all our pipelines have great flexibility and I've spoken about that many times. The Sand and Southern Hills systems have open -- truly open access pipelines, which means that you can flow your barrels to any market that you want. If you want to flow to Sweeney, if you want to flow to Mount Bellevue, if you want to flow to any other market, we can take care of that. You have your choice of fractionators that you can use. So I think for the producers, this is also a very attractive project. So a truly win-win project.

Shneur Gershuni - *UBS Investment Bank, Research Division - Executive Director in the Energy Group and Analyst*

That makes sense. And just sort of to -- just sort of summarize or maybe paraphrase a little bit. So effectively, economically, it makes more sense for you to put the incremental gallons or barrels onto White Cliffs and then Southern Hills because you own a larger percentage of that. And from a producer's perspective, they should be really be indifferent from a net back perspective? And they have increased optionality?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

I think that's a great way of saying it, Shneur.

Shneur Gershuni - *UBS Investment Bank, Research Division - Executive Director in the Energy Group and Analyst*

Okay, perfect. It's good to understand it correctly. Okay. And then secondly, and this may be -- we didn't get our numbers totally squared away. But O&M seemed to have come in lower than expected and so did maintenance. I was just curious if a lot of that was related to the DCP 2.0 project?

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

Definitely -- Shneur, it's Sean. Definitely, 2.0, it continues to drive efficiencies. We spent some time with your team showing how we're reducing man hours, we're reducing overtime miles driven. We talked today, Wouter gave some additional color on the corporate functions, the use of robotics and RPAs and bots and those things. So we're definitely seeing efficiencies continue to be driven across the company. I'll remind you that in our guidance, for the third or fourth year in a row, we continue to guide to lower cost in 2018 than we had in '17. So I wasn't surprised by the reduced cost. But -- and they definitely were quite reduced from Q4. I think our Q4, we had a little seasonality. As I mentioned in my remarks, Q2, if you're thinking about shape, you ought to think about Q2 being a little bit higher, similar to last year because we're going to do more maintenance and we've got some things coming online. But by and large, a very good story for the company, I think our innovation efforts are helping drive that, and we'll continue to do that through the remainder of the year.

Shneur Gershuni - *UBS Investment Bank, Research Division - Executive Director in the Energy Group and Analyst*

In your experience over the last couple of years, I mean, maintenance is consistently coming less than people had expected. Are you still finding incremental opportunities where you're replacing certain parts earlier or other reports later? And are you having less downtime as a result? I mean, I was wondering if you can sort of talk about mechanics of it all?

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

We -- definitely maintenance is important to us. A couple of things to think through over the transfer of the company, obviously, we're extending this company more into the logistics side of the equation, the maintenance on that side of the equation and those are newer assets, tends to be lower. We have had a massive focus internally on improving the reliability, a big portion of that is improving our maintenance programs. I think we've been pretty good at doing that, has very efficient force in the very long run. I will tell you that I think our guidance on maintenance was 100, 120 this year, that's a little bit higher than last year. A trend to think about, and I mentioned it a little bit, is we are seeing additional product replacement in some key areas. The north, for instance, areas like the SCOOP and the Northern Delaware. So there is one area you may see some increases. But again, that's driven by volume growth, we like that. So we're driving efficiencies, yes. We're moving to more logistics assets. Those tend to be newer and less maintenance intensive. And then on the increase side, I think you will see a little bit as we move in and see volumes increase.

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

And then to maybe add to that and, like -- and we continue to obviously also add new assets. So not only are we absorbing those, we're still taking down the overall cost down as well. So it's a pretty remarkable effort by the team. And obviously, hey, the fruit gets higher and higher up the tree. But that's why you also got to continue to change what you're doing. That's why DCP 2.0 and what we're doing around technology and innovation is so important for the overall picture.

Shneur Gershuni - *UBS Investment Bank, Research Division - Executive Director in the Energy Group and Analyst*

Just to -- maybe to paraphrase, again. Look, I definitely understand that newer assets, obviously, have an impact on maintenance, in trends in general. But when I think about it from an apples-to-apples basis, if I sort of think about legacy asset, let's say, or older assets, is it fair to say that you're effectively spending less on maintenance yet you're seeing less downtime?

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

Yes, I think we are spending our money more wisely. We put a huge effort in place over the last couple of years, focused on maintenance at the company as part of our innovation efforts but also just as part of running the company better. So I think what you are saying, I think the short answer is yes. We are spending our money more wisely. We're trying to get better run times out of the assets that make us the most money. And then obviously, plug that into the ICC, whereas the technology comes into play.

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Let me maybe give you an example, Shneur. We have the largest compressor fleet in the industry. Historically, what would happen when you go through a downturn, like 2015 or 2016, people start pushing maintenance up, spending a little less. And that was really not a smart decision. During '15 and '16, we actually started spending much more money on preventative maintenance, and what that resulted into is that major failures on our compressors have gone down by over 70% over the last 3 years. So actually, spending a little bit more upfront and then not running into major failures that cost you much, much more down the line is one example of how we continue to take our cost down.

Operator

Our next question is from Michael Blum from Wells Fargo.

Michael Jacob Blum - *Wells Fargo Securities, LLC, Research Division - MD and Senior Analyst*

So I just want to think through the White Cliffs Southern Hills project. So I guess the first question is, so you're responsible for building the 25 miles into White Cliffs and then the 45 miles from Cushing? And so what's the cost of that and the timing of that spend? I guess, that's my first question.

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Yes. We haven't really laid out yet what the cost is. We're going to probably give all of you a little bit better insight in the different capital expenditures for the variety of projects that we announced over 2019, 2020 and beyond. In the end, I think if you take some round numbers, $1 million a mile, call it $25 million in the DJ Basin. On the other side, I told you that we, from Nova, where we interconnect with Southern Hills to Cushing, we already have large diameter pipe in the ground. So we are in the process of making sure that the pipe actually works. That it's tested, that, that works for this type of service. And it's going to take us another month or 2 to figure that's one exactly out. Worse case, we have to lay 45 million of -- 45 miles of pipe there. If you use the same rough numbers, you can get to a ballpark, and that's -- that the pipe is done 2/3 by DCP and 1/3 by Phillips 66, who owns 1/3 in the pipe. So that's roughly kind of how you should look at the capital outlay than some group and their partners are converting and paying for the capital to connect into Southern Hills and to convert the pipeline.

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

And Michael, maybe -- this is Sean. I'll just give a holistic view. We gave the range on our growth capital this year to $650 million to $750 million, clearly with some of the accelerations we're talking about. And in new projects, I would guide you more towards the higher end of the range. Having said that, if you listen to what Wouter said, a lot of this capital is fairly de minimis in '18. There is some capital in '19 for some of these projects. And then even as you think about, like, Plant 12, which we announced and talked about today, that's really '19, '20. So the good news is, yes, we're going towards the higher end of our range in '18, but we're starting to fill that pipeline in '19 and '20, and these are very accretive projects.

Michael Jacob Blum - *Wells Fargo Securities, LLC, Research Division - MD and Senior Analyst*

Okay, great. That's helpful. And then the other piece of this, just wanted to think through is, and you kind of touched on it before, but assuming White Cliffs fills the 90 and even the 120, does that all basically now have to flow into Southern Hills? And if so, then clearly, that suggests you need to expand that pipeline? Just wanted to check if I'm thinking about that correctly?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

You're absolutely correct. So White Cliffs flows into -- the only connection point from White Cliffs is into Southern Hills. So when we go out together, we will go out with a route that is an open season for White Cliffs and Southern Hills combined. That is the beauty of this project. You're absolutely right, we have today, 65,000 miles -- or 65,000 barrels or so of capacity into Southern Hills. So if we continue to fill this up and all the 90,000 or 120,000 are going to flow into Southern Hills, we, obviously, have to expand Southern Hills. To me, that goes into the category of luxury problems. I would love to deal with that. I think that would be terrific to have that. We have ample time to take a look at that because this is not coming into service until Q4 '19. So by the time we would get in a position where it truly fills up, you're probably looking at 2020 or a little bit later. So we have plenty of time to take a look at that and anticipate all those volumes and expense in Southern Hills.

Michael Jacob Blum - *Wells Fargo Securities, LLC, Research Division - MD and Senior Analyst*

Okay, great. And then my last question, turning to Sand Hills. Effectively, just wanted to get a sense for how full the pipeline is today? Like, where it's flowing today? And what you think the cadence is to fill up to get to the full 45 of capacity that you're expanding to?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Yes. So we're roughly kind of 95% full today. That's kind of where we were at Q1 '18. So at the end of the quarter, we're probably roughly the same there here today if you look real time. And the great thing what we're doing there, and I spoke about that in the prepared remarks is how the team found another 35,000 of additional barrels without spending a penny. And Michael, you know the math on this. So take gallons times rate times 42 times 365, which gets you the margin opportunity on 35,000 additional barrels a day, and, like, tens and tens of millions per year of additional capacity that we can put in. So that is great. So we're running it. We have the 400,000 barrels today. And then we're working on the expansion that now gets us to 485,000 versus the 450,000. The great thing about that expansion, it's not going to come all in at one time. 25,000 of that is going to come in somewhere in the third quarter. So that gets you from 400,000 to 425,000 of capacity in the third quarter. And then we're ramping the 425,000 to 485,000 in kind of step change throughout the quarters when we set additional pump stations, then those pump stations come online. So I feel very good about it. Continues to fill up really, really nicely and it's just pretty exciting.

Operator

Our next question is from Jeremy Tonet from JPMorgan.

Rahul Krotthapalli - *JP Morgan Chase & Co, Research Division - Analyst*

This is Rahul on for Jeremy. Just touching up on the ethane recoveries here. You talked about a $30 million to $40 million upside potential before, and like, I think Sean mentioned in his comments earlier about, like, material -- about recovery materializing some amount in first quarter. I'm just curious if you still expect to see a large amount of it coming out in second half of '18? And also, in context with your hedges around heavies, what's the stake gas for ethane?

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

So regarding the ethane uplift that we gave you, the good news is we are starting to see some. We saw -- to give you a round number, we were rejecting on our system about 60 to 65 a day last year as we came out of '17. We're down to 35 to 40 and a lot of that happens so it's towards the back end of the first quarter. That was worth about $3 million, $3.5 million to DCP in Q1. We do anticipate that to continue. We're seeing very strong recovery signals, and we're -- and that is continued into Q2. So you could probably take that and assume that, that at that level, that it's going to continue for the remainder of the year. That's our current assumption. What's driving that? The economics that are driving that? Obviously, gas prices have come off a bunch. Ethane's kind of hung in there, it hasn't increased a bunch. But that is really what's driving the push now to put more barrels into the pipeline and to pull more ethane out is the weakening of gas. I think your last question was fundamentals on the heavy side of the equation. Obviously, C5 has a very strong correlation with crude. Crude's moving pretty strongly and hanging in there. So we have seen the C5 portion of the NGL barrel, correlate and stay relatively strong this year.

Rahul Krotthapalli - *JP Morgan Chase & Co, Research Division - Analyst*

Got you. That's helpful, guys. And just shifting the focus to Permian a bit here. I mean, I think 1Q was slightly down or flat unlike the forecast for the rest of the year, it is flat to slightly up. Given that, in context, like, one of your competitors, (inaudible) partners talked about a potential second pipe out of Permian. Just curious thinking through the equity options you guys have, would it be something which you'll be interested at? Or just any thoughts there you can provide?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Yes, I think there's -- we continue to control a lot of gas in the Permian Basin. So there's a significant number of inbounds that come to our commercial teams around do we want to continue to -- or do we think there's an interest from our side to subscribe into a second pipe. We continue to look at all options and see what makes sense. I think we're pretty excited about Gulf Coast Express. That's going to be a great project, a project that needs to come online. The market needs that desperately, and I'm very excited that we've teamed up with Kinder Morgan really early to make that project work. So we'll continue to look at opportunities.

Operator

Our next question is from Jerren Holder from Goldman Sachs.

Jerren Holder - *Goldman Sachs Group Inc., Research Division - Associate*

What is the capacity in Guadalupe, given the ability to expand that pipeline, just given price-to-price holds in the Permian?

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

At the capacity, Jerren, it's 200 a day. I mentioned a little bit in our comments that we did with the Waha to Katy spread widening and having that physical asset, that definitely helped our L&M business. In terms of ability to expand it, I don't -- I'm not aware of any projects that we have on deck to expand it. So I'm not sure if we can get much bigger, but it is at 200 today and it's proving to be quite a good asset so far this year.

Jerren Holder - *Goldman Sachs Group Inc., Research Division - Associate*

And then maybe switching to the 50,000 barrels per day volume commitment on White Cliffs. Should we think of that as primarily based on the Mewbourn 3 and O'Connor 2 plants? And then as Plant 12 comes online and you do have capacity on White Cliffs and Southern Hills that, that's most likely where those incremental volumes will flow to?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Yes, you got it, Jerren. I'm, like,it's -- that's absolutely, Mewbourn 3 and O'Connor 2 will create well north of 40,000 barrels a day. So that basically takes those uncommitted barrels into Southern Hills and to the Gulf Coast. And then anything on top of that when we do a Plant 12 or could we do other things that obviously has the opportunity go into White Cliffs, Southern Hills as well. And then we'll be doing an open season. So we very well may see third parties come into the pipe as well. And that would bring additional volumes on Southern Hills as well. So I said it earlier, I think when Shneur asked a question, I'm like, "Is it truly a win-win?" It's a great project for Sun Group and their partners. And it's a great project for DCP and for our unitholders.

Jerren Holder - *Goldman Sachs Group Inc., Research Division - Associate*

Okay. And then lastly, it seems like you guys are pretty confident that Front Range would also be expanded. I think that's an open season right now and so nothing confirmed that has been expended yet. So I guess where the volume's going to come from just given that, like, all of your new plants are effectively sending volumes to White Cliffs?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Well, hey, remember that the parties that announced the expansion are also the owners of the pipeline. So I think you should feel highly confident that, that pipeline will get expended. We would not enter into an open season if we wouldn't know that this pipeline would get extended. So between ourselves, between Western, Anadarko, between Enterprise, we're very confident -- and Enbridge, very confident that Front Range will get expanded. The Texas Express will get done. There are -- we are putting a lot of barrels into that system, Western is putting a lot of barrels into that system as well. So highly confident that both these projects are going to get done.

Jerren Holder - *Goldman Sachs Group Inc., Research Division - Associate*

And maybe one more. On the bypass capacity, how should we think about CapEx and returns on that? Because obviously, you're not necessary providing the same services that you would for processing. So how should we think about that?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Yes. So bypass is really, it's a very capital efficient way to increase capacity without actually processing the gas. So -- and just to make sure that people understand, so what we're doing is at the plant tailgate, we blend the processed gas with unprocessed gas, and then we obviously got to optimize that so that we can meet pipeline specs. It is very capital efficient. I think the way you should think about this is O'Connor 2 plant goes from 200 million a day to 300 million a day, and it probably cost us 10% of the original capacity of O'Connor -- or the CapEx of O'Connor 2 to expand or to put a bypass in. And we have an arrangement with our producer customers, how we get paid on that. And it's another win-win. It's great for the producers. They will get to get their crude flowing. They will to have more capacity. And for us, we get paid on the capital that we put in and it provides us with very solid returns as well.

Operator

Our next question is from Chris Tillett from Barclays.

Christopher Paul Tillett - *Barclays Bank PLC, Research Division - Research Analyst*

I was just wondering if we could for a second dig into the increase in frac volumes year-over-year. You had a pretty nice uptick there. Just wondering if, I guess, which assets in particular saw that increase? And if that's at all related to some of the growing Sand Hills volumes that you guys have reported?

Sean P. O'Brien - *DCP Midstream, LP - Group VP & CFO of DCP Midstream, LLC*

That increase is predominantly related to investments that we have in Mont Belvieu in the Gulf Coast on those fracs. We have ownership percentage increases in those assets. I think if you're trending from last year, there was some downturn and some maintenance that occurred last year that lowered our volumes in Q4. So you saw that rebounding back, wasn't a huge -- I mean, we obviously like to see the volumes go up, it wasn't a huge driver of our earnings. But more back on par and back online. In terms of the Sand Hills driving it, I think the overall industry and the increased demand for the NGLs is driving it and the increase for export.

Operator

Our next question is from Jeremy Tonet from JPMorgan.

Jeremy Bryan Tonet - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Sorry, if it's already been kind of touched on here, but just want to check if there was anything out there that prevented you from directing volumes to Front Range and Texas Express, your equity volumes versus the new White Cliffs-Southern Hills JV that you're talking about here? Can you -- given that you own all of Southern Hills, is there any reason you can't just push as many volumes as you want to that line?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

Yes, Jeremy, it's Wouter speaking. So we have commitments that we have on Front Range and Texas Express. And obviously, we will continue to honor those commitments. But yes, there is a very significant number of barrels that we have under our control that -- where we have optionality. And that's why we were looking at, "Hey, what is the best way to do this? Should we expand Southern Hills and just do it all the way ourselves into the DJ Basin?" It was very attractive opportunity. But obviously, significantly more capital intense than what we're currently going to do where we're spending pennies on the dollars from a capital point of view but still continue to get the same transportation dollars and old barrels that are now coming out of the converted White Cliffs systems. So yes, you're absolutely right. There's a reason why we took out that 50,000 of capacity.

And we can potentially take out even more if we want to because we are very comfortable around the barrels that we're going to direct into that system.

Jeremy Bryan Tonet - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Got you. And just a quick follow-up there. Are you able to share any flavor as far as the duration of those commitments to Texas Express and Front Range? If that's kind of just near-term things that can roll or is it really later you get the contracts there?

Wouter T. van Kempen - *DCP Midstream, LP - Chairman, President & CEO of DCP Midstream LLC*

No, Front Range and Texas Express commitments are like they go, they go well into the next decade. They were long-term commitments when we put kind of one of the anchor shippers on that pipe. And we continue to love that pipe. And, like, its great. It's great to have that outlet. It's great to have this new outlet. In the end, I think the way you got to think through this and what is really important and what we're trying to do here is you want to make sure that you don't get into a place with the DJ Basin, where basically the Permian is today. Whether a shortage of all kind of capacity, you can't take your gas out. People will think about do we need to start flaring, producers thinking about flaring or having to shut in. You may see the same on the NGL side over time. So you have all these problems and bottlenecks that are created. What we are doing in the DJ Basin is to alleviate all of those in one big fell swoop deep into the next decade. It's a Cheyenne Connector that we've been working on. We knew that additional gas takeaway capacity was absolutely needed out of the DJ Basin talking to our producers. We knew that we were going to do something like Plant 12. That's why we worked together with our partners on the Cheyenne Connector, adding 600 million a day of gas residue capacity that's expendable to -- up to 1 Bcf, that's why we worked with our partners on expanding Front Range and Texas Express. But you want to have multiple outlets, and that's why we came to the solution of basically de facto extending Southern Hills all the way into the DJ Basin in a very capital efficient manner. And then on top of that, massive processing capacity that we're announcing by, once again, taking Mewbourn and accelerating it, by increasing and accelerating O'Connor, while filing permits, having all the land available and getting a -- building -- having the opportunity to build a plant that is up to 1 Bcf. So we can give our producer customers a very integrated one-stop shop solution to continuing to grow the DJ Basin, which is an unbelievably attractive basin. So that's really, I think, how you should take a look at this in a -- from a much more broader strategic point of view.

Operator

At this time, I'm showing no further questions. I would like to turn the call back over to Irene Lofland, VP of Investor Relations, for closing remarks.

Irene Lofland - *DCP Midstream, LP - VP of IR*

Thanks, Gigi. Thanks everyone joining us today. If you have any follow-up questions, please give me a call. Have a great day.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This concludes the program. You may now disconnect.
