Enterprise Products Partners LP Q3 2007 Earnings Call Transcript

Question-and-Answer Session

Operator

Thank you. We will now begin the question-and-answer session. [Operator Instructions]. Our first question comes from Mr. Darren Horowitz of Raymond James. You may ask your question.

Darren Horowitz - Raymond James

Good morning guys. My first question has to do Randy, with what you said a little bit about the NGL mines fractionation, based on what's going on with cargo deferral over to Europe and looking at your volumes as they reported this quarter end and what's your experience in currently. What's your expectation for that to improve hopefully into the fourth quarter and into the early parts of 2008.

W. Randall Fowler - Executive Vice President and Chief Financial Officer

Jim... I will let Jim Teague, Executive VP that runs our NGL business to respond to that.

A.J. ("Jim") Teague - Executive Vice President

The question was, what was import volumes?

Darren Horowitz - Raymond James

Yes

W. Randall Fowler - Executive Vice President and Chief Financial Officer

As far as I guess with the import volumes being diverted over to Europe, do you see... what you're seeing there, do you see any relief over there.

A.J. ("Jim") Teague - Executive Vice President

No, no you know if you look at what's going on in the rest of the world you've got naphtha prices. We saw in northwest Europe at a record level of $720 a ton within the last couple of weeks, which suggest that those guys are going to crack in the LPG that can lay their hands on. So that's what we are seeing being diverted. I will hasten to add, we are not seeing any of our contractors to move us back from their contracts because the expectation is still with new production coming on in the Middle East that we will see import volumes and these guys continue to sign up the contracts with minimum obligations. The other side of that is whenever we've had, with this slow down in imported volumes its created a pretty tight U.S. marketplace and is probably one of the reasons that we see frac spreads up north of $0.60 a gallon on the Bermuda Henry Hub basis, so you can look at the import issue in isolation and say, what's going to happen, there is some knife cuts both ways.

Darren Horowitz - Raymond James

Okay so could you also take and imply that to Duncan as the reason why you the NGL petrochemical storage down about 40 % frequently, is that pretty much the same thing?

Michael A. Creel - President and Chief Executive Officer

NGL storage was --

Darren Horowitz - Raymond James

Is it due to lower NGL impact activity here?

Michael A. Creel - President and Chief Executive Officer

Yes, I think the stores facility I mean if you look at it in total, it's... the import, the reduced import is a contributor to it, its not the only thing, but it is a contribute to that decline. We just got lower volumes in general in storage throughout the month and throughout the country right now. I mean it goes back to what Randy said earlier about the lower propane inventories, I mean all of that has an effect in terms of just reducing overall profitability on that storage facility.

Darren Horowitz - Raymond James

Okay.

A.J. ("Jim") Teague - Executive Vice President

This is Jim Teague again. The other thing is you've got that chemicals running at pretty high rates and with ethane, profane, normal butane being the preferred feedstocks, relative to condensates and naphtha they are pulling a heck a lot more than you would typically see them pull, consequently less they are holding less in storage.

Michael A. Creel - President and Chief Executive Officer

And this has been... let me add a little bit of color to TEPPCO deal. The storage revenue at Mont Belvieu has always been this way. We have what we call base storage out there which is up this year over any prior year. So our base storage and what we call our tanker base storage is there. What happens they get a one throughput deal to that storage, what's happened on the NGL and import markets that's what we call extra throughput. So every time a barrel moves to the storage, I think we get like $0.10 barrel. The difference between this year's third quarter revenue and the third quarter revenue of '06 and '05 was that we had large volume coming in through the imports and in effect I think this time last year, we probably had over 800 million gallons or 800 million barrels that we were holding still with TEPPCO deal. So it's a throughput deal not the base storage that vision is down.

Darren Horowitz - Raymond James

: Okay, that's helpful, I appreciate it. And my final question is really one on a housekeeping note. When you are looking at the high depreciation that you experienced in the quarter, what should we use as a run rate for 2008 with lot of these new projects online? And the second part of the question is with that being said what does that mean for your maintenance CapEx lines sequentially over the course of next year?

Michael A. Creel - President and Chief Executive Officer

Well, I think in terms of depreciation we don't have a real good number for you to use in 2008. But third quarter includes a couple of new assets, it includes Independence and Trial. It also includes the Hobbs fractionator and our now PB splitter at Mont Belvieu. The only other significant asset going in service this quarter would be Pioneer.

Darren Horowitz - Raymond James

So we probably shouldn't be to much of a variance relative to what you reported this quarter then in D&A?

Michael A. Creel - President and Chief Executive Officer

I'm sorry.

Darren Horowitz - Raymond James

We would have... Hobbs will be the only incremental project that hits the D&A line this quarter crack.

Michael A. Creel - President and Chief Executive Officer

The Meeker plant was in there for a part of the and in the third we've got a few thousand dollars, but you will see a full quarter of Meeker as well.

Darren Horowitz - Raymond James

Okay. And then may be an initial shot at what you think does for maintenance CapEx in the next year?

W. Randall Fowler - Executive Vice President and Chief Financial Officer

I think we've put here that we think our run rate for sustaining capital for this year was approximately $160 million. I thing we are still comfortable with that number. Right now what sort of putting together where our sustaining cap is for next year. But I don't really at this point of time see it exceeding that number. In fact if anything, it might be a little bit lower.

Darren Horowitz - Raymond James

Okay, thanks guys I appreciate it.

Operator

Our next question comes from Mr. Sam Arnold of Credit Suisse. You may ask your question.

Samuel Arnold - Credit Suisse

Hi guys, I guess the first question would be in the octane enhancement in the petrochemical services, it looks like that was kind of down from prior quarters and it looks like typically you know third quarter has been one of the strongest quarters that you typically have in this segment. I was wondering is this attributable to kind of a flood of competition from ethanol or, can you give us a little more color on that.

Gil H. Radtke - Senior Vice President

Yes, Sam, this is Gil Radtke. The real reason that that is down compared to last year is that you've got a spread between normal and gasoline has really compressed. The normal butane prices itself with crude and the finished product that we sell out of there is priced against RBOB. So what happened here over the last quarters is we had a big compression in the crack spreads that the refiners have enjoyed, so that's really what happened there. We are seeing plenty of demand for the product, it's just that the value between crude and gasoline has compressed. So I mean going forward, you can look at the fundamentals and you can see that we're still well below where we normally have been on gasoline inventories, so I think seasonally we're kind of where we think we should be, or where we expect to be this time of the year. But I think going forward and looking in 2008, we are going to see a better gasoline season next year.

Michael A. Creel - President and Chief Executive Officer

Hey Sam, this is Mike. As I mentioned before it's difficult to compare the third quarter this year with the third quarter of last year a bit...

Samuel Arnold - Credit Suisse

. But even going to the last several years beyond that?

Michael A. Creel - President and Chief Executive Officer

No, I understand. But remember in isooctane, the second quarter last year was very strong and we hedged those margins through the end of last year and so we've got a caught a peek in terms of the Isooctane margins to lock in and that's what you are comparing the third quarter this year again.

Samuel Arnold - Credit Suisse

Sure. Okay, so my understanding would be I mean Octane enhancement is just obviously something you are doing to add to the gasoline to bring up the octane. Some... I am having a little bit of trouble understanding how that's exactly tied to the frac spread. Because it should be an independent supply demand phenomenon correct and only competing with other octane enhancement?

Michael A. Creel - President and Chief Executive Officer

well I think one thing that you got to consider is that we use butane as a feedstock for that, so that contributes to the margins.

Samuel Arnold - Credit Suisse

I see, Okay, so its really just a perhaps the NGL prices being booed by the crude oil price. So it's a separate market but because your feedstock has increased that's the real reason. Correct?

Michael A. Creel - President and Chief Executive Officer
Correct. The field stock has increased relative to the value of gasoline.
Samuel Arnold - Credit Suisse
Got you. Okay and the field stock primarily getting broader because it's more like propane and because...
Michael A. Creel - President and Chief Executive Officer
It follows crude oil.
Samuel Arnold - Credit Suisse
Yes, and it has been brought up by crude oils well as the correlation. Okay, that makes lot of sense. And, if I could ask just one more, you guys stated that you had some better margins with the crude oil transportation and were able to re-negotiate some tariffs and you expect that tariff to be always sustainable, kind of what you saw on the quarter going forward and then can you talk about, you talked about a couple of projects with [indiscernible], how is that going to offset, kind of your natural decline rate in those production going forward?
Michael A. Creel - President and Chief Executive Officer
Its the same, I guess, we're the question that you had on crude oil and tariffs, if you could embellish on that, a little confused on that one?
Samuel Arnold - Credit Suisse
Okay.On the off shore pipe lines and services, you had page 3 number B says, you had $5 million from higher revenues from high and offshore as a result of new tariff that went into effect in March 2007.
Michael A. Creel - President and Chief Executive Officer
Yes Sam, that's a gas pipeline.
Samuel Arnold - Credit Suisse
Okay. Highland Offshore.
Michael A. Creel - President and Chief Executive Officer
Bit of a rate increase there.
Samuel Arnold - Credit Suisse
Okay I see, all right. My mistake and then I guess following that would be kind of what's your natural decline on the gas and crude oil lines?
Dan L. Duncan - Chairman
Sam, this is Dan Duncan. Let me answer the other on the crude oil. Our crude oil pipelines, the capacity of the [indiscernible] Cameron Highway, that was designed with the liners and Genghis Khan and Marco Polo, all 11 being there. None of those fields have come on stream yet. Yet I think the BP Atlantis deal and also the BHP Australian company, the deal went in fourth quarter beginning to be ramped up on the deal. So those two pipeline today is running about 200,000 barrels a day each, we all know approximately 35% to 50% of those two pipelines. The actual capacity of those two pipelines is about 600,000 a day. That's because the product itself hadn't came on there is no decrease in the volume of that were finally moved to it its never come out to start with, so there is not a decline on the crude oil side.
Samuel Arnold - Credit Suisse
Right. Okay, so you'll have that ramp up and then you will start the national decline so we just --.
Unidentified Company Representative
Let me add to that, we mentioned several field names and certainly Genghis Khan will benefit, the Marco Polo platform in our gathering line it goes up to tie into Cameron Highway and Poseidon, so we have a very good value chain with that. With Cameron Highway and Poseidon, Cameron highway

with some additional pumps can do 600,000 barrels a day, Poseidon, with some additional pumps can do 400, so combined they are moving around 200,000 barrels a day right now, but you've got 800,000 barrels a day of additional capacity, and a lot of that was designed in with knowing that Atlantis and Atlantis has been late coming on, but we still believe it's a very strong field. Atlantis is dedicated to Cameron highway. On top of Atlantis Genghis Khan, we mentioned Neptune. That is coming on either late this year early 2008 and that access is Cameron highway as well as Poseidon and then in late 2008 early 2009 we are building a major gathering for the Shenzi field, which is 100,000 barrel a day field.

That is going to come on at that time period and our gathering line is going to connect to Poseidon and Cameron Highway, so that's revenue to not only the gathering line but to our downstream oil pipeline. On top of that there is numerous discoveries out in that corridor and then if you look at the leasing activity and what people paid for blocks in the last lease sale not only in that Green Canyon area, but if you move a little bit west of there, kind of in the western central Gulf there is a major BP discovery called Kaskida. There was a tremendous amount on new leasing over in that area and the way our oil pipelines way out they hug the shale from northern east west before they turn up to the market, so we're not only well positioned for what's going in Green Canyon, but also this future activity a little bit to the west of that area. So taking what's going on in the oil side northern central and then Mike mentioned the leasing around Independence Hub, which we believe is the major gas area. We think we are well positioned for the gas growth in the Eastern Gulf as well as the oil growth in the Central and west Central Gulf.

Samuel Arnold - Credit Suisse

Okay, great, thank you

Operator

Our next question comes from Mr. Yves Siegel of Wachovia. You may ask your question.

Yves Siegel - Wachovia Securities

Thanks, good morning.

Michael A. Creel - President and Chief Executive Officer

Good morning Yves.

Yves Siegel - Wachovia Securities

Can you just elaborate, James on those comments, at what of time do you need to start thinking about incremental growth CapEx offshore and so the flip side is that as when you think of the incremental 800,000 of capacity on Poseidon and Cameron highway. It sounds like within a couple of years that might get fully utilized. How should we think about incremental cash flow that you could see without necessarily having to invest any incremental capital?

James H. Lytal - Executive Vice President

Well, Yves, let me say one thing, a lot of the pumps are already in on Cameron Highway in anticipation of Atlantis ramping up, we are probably a little bit ahead of the curve just because it's a little late. The incremental capital for both Poseidon and Cameron highway to get to the levels I talked about is very small because we already we own the platforms where we are going to put the pumps, we have the space available, lot of the piping is already been done in anticipation of it, so its just a matter of adding a little bit of pumps, so it's a very small number.

Unidentified Company Representative

I think he is trying to give a sense for the potential additional gross operating margin without --

Unidentified Company Representative

Let me give you a feel on 100,000 barrels a day on Cameron highway you are looking at $17 million to $18 million a year of additional gross operating margin in round numbers.

Unidentified Company Representative
You have built it in, that value in that BP and the two bigger ones, BP coming on and BPH and Exxon on those fields, this is like James said, each one is 100,000 barrels a day is net to about $80 million a year. That's the kind of price is ownership out there. So in theory, if we can get up to what they have announced is around 500,000 barrels a day increase that's about $60 million of revenue on top of what we're doing like now.
Unidentified Company Representative
Without spending very little additional capital because we are there.
Yves Siegel - Wachovia Securities
Okay. That's great. But then when you think about growth CapEx next year and beyond in what you've announced already, where do you think the opportunity is for incremental growth CapEx and do you think the Gulf of Mexico is there opportunity as well in the Gulf of Mexico or would you be thinking more the Rockies and where you are today?
W. Randall Fowler - Executive Vice President and Chief Financial Officer
Yes Yves, I think the answer is yes. We're looking at all of those areas and we're frankly looking at some priced exit, we happen to announce, maybe premature to talk about now, but suffice to say that we got some pretty exciting prospects, both onshore and offshore, perhaps a little weighed a little more heavily onshore.
Yves Siegel - Wachovia Securities
Okay any terms of timing?
W. Randall Fowler - Executive Vice President and Chief Financial Officer
You know we've already got projects in our capital budgets for next year that are quite in the $1.2 billion to $1.4 billion range and we haven't even finished this year yet so next year is looking pretty robust. In terms of announcing any other growth projects, we're probably still 3 to 6 months out.
Yves Siegel - Wachovia Securities
I know I am pushing it Sharon Lui has a couple of questions on Duncan, but before I turn it over to her, could you just also, what would you think the time lag is on $1.2 billion of investments next year before you start recognizing cash flow?
W. Randall Fowler - Executive Vice President and Chief Financial Officer
Those, we don't have a big project in that number like an Independence Hub that takes 3 years to build, so a lot of these projects are going to be finishing up projects like Meeker 2 for example, and that's already well underway. The Sherman Extension is another one, so a lot of these are finishing projects that we've already done. These project by and large are smaller in scope than an Independence type of project, so you're looking at probably on average maybe 9 to 12 months.
Yves Siegel - Wachovia Securities
That's great, thanks guys and here is Sharon.
Sharon Lui - Wachovia Securities
Hey, good morning.
Unidentified Company Representative
One correct and one mistake I made. The ramp up of crude oil going in to Poseidon and into Cameron Highway is $90 million annualized, not 60 I gave that one.
Sharon Lui - Wachovia Securities
Okay, thanks. I guess on the Duncan side, if you could may be give some color on the higher OpEx cost, it looks like you guys are incurring its higher integrity cost for both the natural gas pipeline and the NGL storage segment?
Michael A. Creel - President and Chief Executive Officer

Yes I guess from the context of the pipeline integrity cost, primarily at Acadian, those are related to what we have to do associated with regs in Louisiana and those are really, we accelerated some projects from the first quarter of 2008 into 2007 because we have to. So, when we look at that, its money we knew we're going to spend anyway, we just had to accelerate it and so that's why our expectation is that going forward, those operating cost levels will be lower than where they are today and really the same thing, its not pipeline integrity out of the storage facility but its just a maintenance capital that we decided that we need to do now and not wait and do when it was, some of that was also scheduled in 2008, its just it's the prudent thing to do. So, again we don't see that, those high rates continuing, it's just we're getting the work done now.

Sharon Lui - Wachovia Securities

But is it fair to say that, it will be at the similar rate for the fourth quarter?

Michael A. Creel - President and Chief Executive Officer

There is a good chance of that. Yes, it again comes down to timing and getting everything done but yes, I think that's a fair assessment.

Sharon Lui - Wachovia Securities

Okay and I guess, if you guys have an update on potential drop down for Duncan in terms of timing?

Michael A. Creel - President and Chief Executive Officer

We don't have anything to really talk about right now. When we did the IPO back in February, obviously we said that Enterprise would not have formed Duncan Energy Partners, it was only for a one-time transaction. We've certainly had discussions internally about what might make sense for both partnerships but again it's a real premature to talk about it.

Sharon Lui - Wachovia Securities

Okay, thank you.

Operator

our next question comes from Mr. Ross Payne, Wachovia Capital Markets. You may ask your question.

Ross Payne - Wachovia Capital Markets

How are you doing guys?

Michael A. Creel - President and Chief Executive Officer

Hey Ross.

Ross Payne - Wachovia Capital Markets

First question, Independence Hub, it did 124 for the quarter, the 640, is that where it is today or your expectations for the average throughput in Q4 and on top of that if you can throw out any kind of thoughts on EBITDA contribution from the ramp up sequentially there because it is petty significant.

Michael A. Creel - President and Chief Executive Officer

Yes Ross. The Independence Hub and Trail, as we talked about before, we've got $44 million a year demand charge on the platform and the addition to gross operating margin for the Hub and pipeline is about $17 million for every 100 million cubic feet. We are at 640 today, producers have indicated that they might even get closer to that Bcf a day by early December. So you can do some math to figure out what that means in terms of additional cash flow. But it's a much faster ramp up in production than we had counter played when we honestly sanctioned the project and even much higher than we had thought six months ago.

Ross Payne - Wachovia Capital Markets

Great, great. Also Mike, can you comment on what you thing start up cost might have been at Meeker and some of these other plants, just you know forget that there is going to be substantial increases in cash flow here. But what kind of cost much you be incurring in this quarter with all the ramps up that are ongoing?

Michael A. Creel - President and Chief Executive Officer

Yeah, it's difficult to say. In the third quarter, we had between $2 million and $3 million of start up cost there. Frankly, these plans when you start them up, you always run into some unexpected issues and then we are working through those now. We did have delays in the construction of the facility. We had some issues with the manufacturer of the valves that we had to work through and we'll certainly be looking for a reimbursement from them. But I think in terms of additional startup costs they are going to be relatively low.

Ross Payne - Wachovia Capital Markets

Okay, on this --

Dan L. Duncan - Chairman

If you go back and look at when we... if they would have came on in less than 30 days after we initiate the deal, often third quarter between Meeker and the fractionator Hobbs it is probably close to $40 million to $50 million.

Ross Payne - Wachovia Capital Markets

Okay, thank you. Also on the distribution coverage, with the ramp up in cash flows in '08 what are the expectations on that coverage ratio being maybe tail end of '08?

Michael A. Creel - President and Chief Executive Officer

It all depends on what we do with distribution right, but frankly with the ramp up in volumes on Independence, the Meeker and the Pioneer plants, cash flows could ramp up pretty quickly. What we've told investors both on the equity end and fixed income side is that when we look at our distribution, we not only look at distributal cash flow but we also look at our capital program, we look at the projects that we have and how long the construction cycle is to make sure that we have or prudent in the way that we increase our distribution and while we clearly expect to continue increasing distributions we don't want to get ahead of ourselves and put our balance sheet in jeopardy.

Ross Payne - Wachovia Capital Markets

Okay and one final question, equity NGL were down a bit and San Juan was down, if you could just touch based on those two items. Thanks.

Michael A. Creel - President and Chief Executive Officer

Yes, on San Juan we had a plant turnaround in August that our Chaco plant, so we were down for five days and that's large plant, over 600 million a day. So, that had an impact to San Juan in the third quarter.

Unidentified Company Representative

Yes, and were also equity NGL production. It was only down about 3000 barrels a day, I know part of it, when that first hurricane came through the Gulf Mexico when actually went in, over around... well the other one that went towards Mexico, that there was some evacuation of platforms and I think we had offshore production that was offline for call it 3 or 4 days. So that impacted gross operating margin both, on some of the pipelines, on the processing plants which would hit equity NGL production and then also in some of the fracs too, so that may be part of it.

Unidentified Company Representative

You also had produced your elections in South Texas where they elected the type of processing position rather than unconditionally.

Ross Payne - Wachovia Capital Markets

Okay, all right. Very good, that's it from me. Thanks guys.

Michael A. Creel - President and Chief Executive Officer

Thank you, Ross.

W. Randall Fowler - Executive Vice President and Chief Financial Officer

Thank you, Ross.

Operator

Our next question comes from Ken Liyal [ph] from J.P. Morgan. You may ask your question.

Unidentified Analyst

Hi my question is regarding the Independence Hub, when do you think you need to come at additional wells to keep this full or near full when the initial 16 wells start to decline? And what do you see in the pipeline or how many wells are in the completion stage that you can comment them to the Hub?

Unidentified Company Representative

This is James. Well, I will... the producers have indicated they have other wells that they plan to drill. I think what you are going to see or the tenants kind of watch your volumes, project declines and drill wells accordingly to try to keep the platform as full as possible over the next five years at least. And they find that these wells are fairly quick to grow and they have laid out this major subsea gathering system. So as opposed to having a way of homely system up to the platform, they'll just drill a well and tie it into their existing system so the timing as well as the capital required to get the wells on is going to be low. So I think you are going to see the existing... they have a lot more blocks out there than what's flowing from today, you're going to see those people continue to drill wells to work to keep there capacity full. Over the long-term, I think you're going to see people start to drill in these blocks there, new leases that they have taken in the recent lease sale and if you look out over the next five to 20 years you're going to see areas around the platform as well as these new areas that have been leased up is providing the gas for the Independence Hub and these people are going to EBIT incentivised to use the Hub because one, its there and you can get your gas on a lot quicker. And the cost of building a subsea pipeline to the platform compared to building a new platform is significantly cheaper, so you get the present value benefit to getting on quicker and then obviously the benefit to lower capital to get wells on.

Unidentified Analyst

Thank you.

Operator

Our next question comes from Mr. John Edwards, Morgan Keegan. You may ask your question.

John Edwards - Morgan Keegan

Yes, good morning everybody.

Michael A. Creel - President and Chief Executive Officer

Good morning, John.

John Edwards - Morgan Keegan

Yes, just I think Dan already mentioned this number, but I just want him to assert I have it straight on the incremental equity and earnings we should expect from Cameron and the Cameron and Poseidon are pipelines and I think you said for Cameron about $18 million or so, is that correct understanding, and what's the... what's your expected timing on that?

Dan L. Duncan - Chairman

John that 18 million was each 100,000 barrels a day.

John Edwards - Morgan Keegan

Each 100,000 barrels a day.

Dan L. Duncan - Chairman

It's a 1,00,000 barrels a day comes on, we own Cameron Highway 50%, so it's $1 tariff, so that is $36 million, our share would be $18 million of that.

Unidentified Company Representative

Let me add one thing, because I gave you a revenue number. There is a little bit of expense to pumping and I think you're looking at about $16 million on a gross operating margins or added cash per 100,000 barrels.

John Edwards - Morgan Keegan

Okay so you're... so that's why because you saw the producers were coming on with about 500,000 that or I guess more than that, I tell you're getting to the incremental $90 million?

Dan L. Duncan - Chairman

I was using 500,000 barrels a day at the 18 well in 16, under that scenario it would be $80 million. This BP coming on with their production, they say now end of '08. BHP of Australia coming on with their production and I hope IS coming in at the end of the year or early

Unidentified Company Representative

So we have several fields over the next year that are being --

Dan L. Duncan - Chairman

One other field is

Unidentified Company Representative

BHP in Atlantis, they are in Genghis Khan, Neptune and then Shenzi.

John Edwards - Morgan Keegan

Okay so BHP's production is coming on, how much production are they contributing there?

Unidentified Company Representative

You know what, well they are working interest owner in all those fields. Atlantis, their share and BP share of Atlantis is dedicated to Cameron Highway. You know if you add it up, Atlantis is projected to be 200,000 barrels a day, Neptune is projected to be 50. Shenzi is projected to be a 100,000 barrels a day and Genghis Khan BHP has projected at 55,000 barrels a day.

John Edwards - Morgan Keegan

Okay. Okay and then the incremental contribute... you may have mentioned, Dan, I think you may have mentioned this. The incremental contribution you are expecting from Meeker when it is fully ramped up?

Michael A. Creel - President and Chief Executive Officer

Dan, you want to answer that one?

Dan L. Duncan - Chairman

What we've done is we have looked at what the market says these plants will produce is terms of the quoted prices in the forward market, quoted basis. We look at 2008 just the contracts that we have in place not including those that we were highly confident of, taken into account some of the hedging we've already done, the marketplace is saying that Meeker and Pioneer together will produce gross operating margin next year of north of $300 million, what we are saying is that with those that we are confident will get, which is another 300 million a day, we could see that beam toward $350 million.

John Edwards - Morgan Keegan

Okay so 300 to 350?

Unidentified Company Representative

Again that's based on the forward prices that we are looking at today.

John Edwards - Morgan Keegan

Right, based on forward prices and that's just for Meeker 1, it doesn't count Meeker 2?

Unidentified Company Representative

That includes Pioneer.

John Edwards - Morgan Keegan

And includes Pioneer?

Unidentified Company Representative

And a portion of Meeker 2. Meeker 2 is scheduled to come on in the third quarter.

John Edwards - Morgan Keegan

Okay. And then could you talk a little bit about the NGL fractionation, it was at least we are not... we are looking at all variance analysis, is a little bit below what we were expecting? Can you talk a little bit... give us a little color on what happened there. I think you mentioned it in the press release as well, but there were some... it was associated with the fractionation decrease in fractionation volumes at the Norco fractionator.

Unidentified Company Representative

Yes John, really three things in there, probably the largest thing is in the third quarter of 2006 we had some measurement gains around... measurement gains principally around some wells they were probably about into $12 million. And then that's the biggest piece, and then you did have the decrease in volumes at the Norco fractionators and again that is sort of our highest margin fractionator. And then finally, you had Hobbs that was probably another $1.5 million of start up expenses.

Unidentified Company Representative

You also had some business interruption proceed, about $10 million more in BI proceed in third quarter of '06 for them.

John Edwards - Morgan Keegan

Okay. So you are expecting that performance to come back up in the fourth quarter and beyond then?

Unidentified Company Representative

Yes.

John Edwards - Morgan Keegan

Okay. And then I guess similar question with San Juan. I mean for the natural gas pipeline segment, you indicated in the press release that there was an offset of more of a totaling $10 million due to lower volumes of revenues in the San Juan system and some other issues you list there. Can you talk a little, just give little more detail on what was going on there in and why that came in not as well as you expected?

James H. Lytal - Executive Vice President

I mentioned, its James Lytal. I mentioned we did have some downtime days in August due to our processing plant going through part of their turn around and actually impact us a little more than 5 days just getting well back on afterwards. Also I think we've talked in the past that the San Juan, a lot of our gathering contracts are based on the percentage of gas price. That can impact the revenues from San Juan although having link to gas over there is an a nice hedge to our shore position of gas, where we buy gas at Mont Belvieu and also for our pumps on our Maple liquid system. So where we may lose some at San Juan, we are getting some in some other areas when processors are little lower, so volume and then the frac gas prices were little lower which affected our gathering fee.

John Edwards - Morgan Keegan

Okay, great

Unidentified Company Representative

Yes, John gas pipes out in the San Juan were up $0.35 per MBtu lower in the third quarter 2007 compared to the third quarter of 2006

John Edwards - Morgan Keegan

Okay. And then, these future storage projects that are going to be coming on and I realize you mentioned they are out quite a ways in the future, 2010 and 11. Have you... what's the capital budgets you've got associated with some of those?

James H. Lytal - Executive Vice President

This is James Lytal again. It ultimately depends on the total amount we build and also we are developing a new cavern at Belvieu initially the first five will be less than $100 million. To do that, that we are designing the path on that first five to give us capacity for to expand up to 20 Bcf in the area. So your capital is going to be a little higher on the front end because you are oversizing facilities in preparation for the other so, when we start adding the incremental 15 Bcf, total capital and then returns and I've talked about our storage business in the past and we've looked at it from the standpoint of depending on how much pipe and compression you have to add, you are probably looking at anywhere from $15 million to $20 million per Bcf of storage that you add. With the market rates that we're seeing in the storage business, it leads you to projects to pay out in 5 to 8 years typically, when these contracts are mainly domain charge contracts and on top of that we can do interruptible business. So, I know I may not be giving you the exact number but I think we're confident we're going to build another ten at Petal, but we could go a lot further than that, we have a lot more land that we're able to develop lot more caverns which could lead to additional pipeline expansions at Petal.

John Edwards - Morgan Keegan

Okay, thanks very much.

Randy Burkhalter - Director of Investor Relations

Marsha, this is Randy. We have time for one more question.

Operator

Thank you. Our next question comes from Mr. Luis Shemy [ph] of Zimmer and Lucas. You may ask your question.

Unidentified Analyst

Hi everybody. I guess, two things that I wanted to ask. So, first off, if you can give a little bit of a more detailed break out of how you expect to generate margin on Meeker, in terms of what economics you are assuming there? And then, second question was regarding your financing?

Unidentified Company Representative

The question is how do we expect to generate margin on meeker?

Unidentified Company Representative

I think to look at what kind of port prices we are looking at?

Unidentified Company Representative

You are talking about, is this related to what our earlier answer?

Unidentified Analyst

Yes, exactly. So in terms of what the volume assumptions are, operating expenses and then kind of your forward price assumptions?

Unidentified Company Representative

Our forward price assumptions are a function of what we see uploaded in the market place. Forward price assumptions are not, they are really not assumptions, but they are actual quotes in terms of what we can sell the product at and what we can buy the gas at and what the quoted basis is to the Rockies. For example, we are operating on somewhere or near $1.50 basis to the Rockies for calendar '08.

Unidentified Company Representative

And volume --.

Unidentified Company Representative

The volume we're looking at, we expect Meeker 1 to be fill topping that in the mid year, we think when Meeker 2 comes on, we will need Meeker too right at the time it's coming n on. So we see a ramp up in Meeker 1, right now, I think we are at about 450 million a day throughput producing 25,000 barrels a day. We see that ramping up to the full 750 by mid year next year at 35,000 barrels a day and having gas left over to go into Meeker 2. We see Pioneer, right now if you look at our silica gel, we are running 525, 550 in the silica gel, so whenever Pioneer comes up, we automatically have around 550 out of the 750 capacity.

Unidentified Company Representative

I think in the lower number we have Meeker ramp up from the 470 it is today to about $800 million at the end of the 2008, if on the higher numbers of 350 Jim mentioned that would have Meeker ramping up to about a Bcf a day by the end of 2008. And Pioneer on the lower number goes from about 525 or 550 there to 650 or so by end of '08 and higher number probably adds about 50 to that and takes us to about $700 million by the end of '08.

Unidentified Analyst

Okay, great thanks a lot. And then on the financing, just wondered if you guys could give me an overview of how you internally look at your various financing options and which are looking most profitable at this point for whatever CapEx budget you are going to announce for 2008?

Unidentified Company Representative

Well, I think some of what we are... last year, in 2006 we really front end loaded our 2006-2007 capital expenditure program with a large amount of equity and 2006 with two follow on equity offerings with the $550 million of hybrid being issued. We also had a $100 million of distributable cash flow that we reinvested. Coming into this year, that in fact that gave us a lot of flexibility coming into this year. We came in and issued another $700 million of hybrid securities that brings the hybrids up to about a little less than 10% of our total capitalization, so we still have some flexibility on the hybrid side going forward as far as equity content is concerned.

The other thing that we also have... the other component in there is off our dividend reinvestment plan we are probably running on a run rate right now about $60 million a year of the new equity being issued to that program. I think finally, the thing we look at is when you look at the ramp up of the distributable cash flow that we expect coming on in 2008 with Independence ramping up, with these processing plants and fractionators that Jim talked about. I think we will throwing off a huge amount of distributable cash flow in and as we come in and set our cash distribution policy. I think one of the things we have done historically is we retained... just historically if you look at it, we probably retained about 15% of our distributable cash flow to use to fund capital investment, so really as we go into next year we think we've got a lot of flexibility in coming in and financing that growth.

Unidentified Analyst

Okay great. And in terms of looking at cost of capital kind of between but they are issuing more hybrids and that kind of tapped at 10% of budget I guess, but between that and unless they are doing a drop into DET or issuing more conventional debt or issuing equity, how do you look at your various cost of capital between those few options?

Unidentified Company Representative

Well, I don't think we are completely tapped out on the hybrids and certainly markets change frequently and we look at things on a pretty dynamic basis, so to the extent we felt a need to raise equity, which we don't right now, we would look at all 3 methods whether it is additional hybrids, whether it is a drop down, whether it is traditional equity and determine what makes the most sense for the partnership given the current market conditions. But again, we don't have a lot of pressure to do any of that right now.

Unidentified Analyst

Sure. And have you considered doing any kind of convertible security or is that kind of not on the horizon?

Unidentified Company Representative

It's not at the forefront for us now.

Unidentified Analyst

Okay great, thanks a lot.

Unidentified Company Representative

You bet, thanks

Randy Burkhalter - Director of Investor Relations

Marsha, if you would you give our listeners the replay information?

Operator

Thank you. If you would like to listen to the replay, you may dial 1800-728-5839. Once again that's 1800-728-5838, excuse me, 5839. Once again 1800-728-5839.

Randy Burkhalter - Director of Investor Relations

Thank you, Marsha and thank you every one listening to our call today and have a good day. Good bye.