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HFC - HollyFrontier Corp to Acquire Sonneborn - M&A Call

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OVERVIEW:

On 11/13/18, Co. announced that it has entered into a definitive agreement to acquire Sonneborn US Holdings Inc. and its international affiliate for $655m or $583m, net of working capital of approx. $72m.

CORPORATE PARTICIPANTS

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Roger David Read *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

PRESENTATION

Operator

Good morning. My name is Mariama, and I will be your conference call operator today. Welcome to the HollyFrontier Corporation Management Update Call. I would like to now turn the call over to Craig Biery.

Craig Biery - *HollyFrontier Corporation - Director of IR*

Good morning, everyone. I'm Craig Biery, Director of Investor Relations. Thank you for joining us to discuss the transaction we announced this morning to acquire Sonneborn. A slide deck for the conference call can be found through the webcast link provided in the press release and also in the Investor Relations, Events and Presentations section of our website at hollyfrontier.com. Joining us today are George Damiris, President and CEO; Rich Voliva, Executive Vice President and CFO; and Mark Plake, Global Executive of Lubricants and Specialty Products.

Before Rich, George and Mark proceed with their remarks, please note the safe harbor disclosure statement in today's press release. We will be making forward-looking statements on today's call. There are many factors that can cause results to differ from expectations, included those noted in our SEC filings. Today statements are not guarantees of future outcomes. Please also note that any comments made on today's call speak only as of today, November 13, 2018, and may no longer be accurate at the time of any webcast replay or transcript rereading.

And with that, I'll turn the call over to George.

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Thank you, Craig. Good morning, everyone, and thank you for joining us. As Craig mentioned, you can follow the presentation through the webcast, and it is also available on our website. We will run through the highlights in the deck, and we'll take questions after the presentation.

Starting on Slide 3. This morning, HollyFrontier announced that it has entered into a definitive agreement to acquire Sonneborn US Holdings Inc. and its international affiliate for $655 million or $583 million net of working capital of approximately $72 million. HFC expects to fund the transaction entirely with cash on hand and anticipates it will be immediately accretive to both earnings and cash flow per share. We expect the transaction will generate approximately $85 million in annual EBITDA, including approximately $20 million in annual synergies, which we will discuss in more detail in a little bit. This represents a very attractive multiple of 7x EBITDA net of working capital and synergies. The transaction is subject to regulatory approval and customary closing conditions, and we expect it to close in 2019.

Moving to Slide 4. Sonneborn is a global producer of high-purity specialty products and one of the world's largest dedicated suppliers of white oils; petrolatums, more commonly known as petroleum jelly; waxes and sodium sulfonates. Sonneborn has manufacturing plants in Pennsylvania and the Netherlands, with a combined processing capacity of roughly 5,300 barrels per day. Both locations have R&D facilities with experienced staff as well as blending and packaging capabilities that distribute premium quality of specialty products through a global distribution network.

Turning to Slide 5. This acquisition will further our downstream integration and significantly grow the Rack Forward part of our lubricants business. 100% of Sonneborn earnings are attributable to our Rack Forward segment. And the acquisition of Sonneborn will significantly expand our specialty products portfolio. HF LSP currently supplies a portion of Sonneborn's base oil feedstock. This provides opportunity for additional uplift from our Tulsa and Mississauga base oils, increases operational flexibility and allows for feedstock optimization. Sonneborn strengthens our global footprint by increasing processing and blending capabilities in both North America and Europe and expanding our global sales organization and distribution footprint.

I'll now turn the call over to Mark Plake to talk about Sonneborn's operations and products.

Mark Plake

Thanks, George and good morning, everybody.

Moving to Slide 6. Specialty hydrocarbons are highly purified and specialized derivatives from base oils. Sonneborn formulates and manufactures highly purified hydrocarbons, such as petrolatums, white oils, waxes, sodium sulfonates and industrial specialties, such as metalworking fluids. Sonneborn's operations offer a world-scale and flexible formulation platform. The hydrotreating unit in Pennsylvania provides unparalleled flexibility to run a wide range of Group I and II base oils, which gives it a competitive advantage on feedstock.

The sulfonation and purification units in the Netherlands have the ability to produce unique product formulations with a high degree of customization due to their feedstock flexibility and advanced processing technology. Their strong global distribution and sales team enables us to efficiently place a broad line of products around the world.

Turning to Slide 7. HF LSP is an integrated business with 2 components, Rack Forward and Rack Back. The Rack Back component is the process of converting refinery intermediates, such as vacuum gas oils and Hydrocracker Bottoms, into base oils. Rack Back earnings and cash flows are similar to refining because it captures the value between feedstock costs and the market prices of base oils. The Rack Forward component is the process of converting nonadditized base oils into an assortment of finished products. This segment captures the value between the base oil market prices and the sales of finished products. The distinction between the 2 components is whether we are producing base oil, which is Rack Back, or using base oil as our feedstock, Rack Forward. As George mentioned, 100% of Sonneborn's earnings are attributable to our Rack Forward segment.

Now looking on Slide 8. Sonneborn products are tailor-made solutions for blue-chip customers representing industries such as personal care, pharmaceutical, food, telecom and metalworking. White oils are used to lubricate, smooth, soften and retain moisture across a variety of uses in personal care, pharmaceutical and food applications. Petrolatums provide lubricity and moisture retention with superior performance and longer shelf life than competing products. Microcrystalline waxes and blends act as natural bases to harden, lubricate, carry pigments and protect against moisture in lipstick, cold creams, ointments and cheeses. Natural sodium sulfonates are used as detergents, emulsifiers and anticorrosion rust-prevention agents. Sonneborn's industry-leading research and development and formulation process has resulted in loyal customers with relationships that have lasted many decades.

Turning to Slide 9. Sonneborn's diversified specialty product slates complements our existing portfolio while achieving our goal of shifting our product mix from base oils to finished products. Sales of finished products receive higher margins and are much less volatile than base oils. Sonneborn adds significant scale to HF LSP by growing our Rack Forward portfolio.

Now we'll turn the call over to Rich

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

Thank you, Mark.

On Slide 10, you'll see Sonneborn's business has shown tremendous stability with EBITDA margins averaging 18% since 2015. This provides an uplift to the healthy EBITDA margins of our existing Rack Forward business. We expect this addition of Sonneborn will consistently add between 100 and 500 basis points to HF LSP's pro forma EBITDA margins.

On Slide 11, you'll see that we have identified $20 million in potential synergies, consisting of $5 million of SG&A; $3 million of logistics savings through transportation and blending cost reductions; and $12 million of production-optimizing opportunities across Tulsa, Mississauga, Petrolia and Amsterdam. We are also evaluating several low-cost, high-return projects that will provide incremental earnings. An example of such a project is a potential expansion of capacity in the sulfonation unit in the Netherlands.

Turning to Slide 12. The consistency of Sonneborn's earnings will add stability to HollyFrontier. As you can see, with the exception of a production issue in 2016, Sonneborn has consistently generated $60 million to $70 million per year of EBITDA. And as discussed, we believe synergies over the next few years will drive this number north of $80 million.

On Slide 13, you can see our ability to fund this transaction with cash on hand, which is a testament to our strong balance sheet. As you can see, we have plenty of cash on the balance sheet to fund the transaction and maintain a healthy liquidity position and capital structure. We are confident that we will maintain our investment-grade ratings from S&P, Moody's and Fitch.

Looking ahead, we continue to expect to generate strong cash flow, and we'll follow our capital allocation strategy of, first, defending the balance sheet and assets; second, paying a competitive regular dividend; third, growing our business through both organic investments and acquisitions, such as Sonneborn; and fourth, returning excess cash to shareholders in the form of stock repurchase. In line with these priorities and our prior guidance of a target of $0.5 billion of minimum cash, we expect to hold $1 billion to $1.2 billion of cash on the balance sheet until closing.

Slide 14 illustrates why specialty product companies trade at higher multiples than refining companies. Some of you are familiar with this chart from our Analyst Day in 2017, which shows historical EBITDA margins and the range of those margins for the lubricant comp group. HF LSP's Rack Forward business compares favorably to these peer companies in both absolute EBITDA margin and margin stability. With Sonneborn, our pro forma Rack Forward business has an average EBITDA margin of 11% to 16% over the trailing 3 years. Using 2019 consensus earnings estimates, these comps are trading in the range of 9x to 14x.

Let's take that to Slide 15. We believe that with its margins and stability, HF LSP's pro forma Rack Forward business should carry an EBITDA multiple of 11x using an [EBITDA] margin of 11% to 16%. That takes our pro forma lubricant business valuation to over $3 billion. We expect to average through the cycle annual CapEx at HF LSP of $60 million to $70 million, with DD&A of $60 million to $70 million (sic) [$40 million to $50 million] and SG&A of $145 million to $155 million.

And with that, I'll turn the call back to George.

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Thanks, Rich.

We'll finish up on Slide 16. The map shows our consolidated asset footprint, including Sonneborn's processing and blending and packaging assets in Petrolia, Pennsylvania and Amsterdam, Netherlands. We're excited about this opportunity that exists to combine Sonneborn with our current lubricants business. This transaction demonstrates our continued commitment to the finished lubricants business and is expected to bring outstanding value to our shareholders and to the customers and employees of both companies.

And with that, Mariama, we're ready to open the floor to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Manav Gupta with Crédit Suisse.

Manav Gupta - *Crédit Suisse AG, Research Division - Research Analyst*

George, I know you guided to $88 million in EBITDA including $20 million in synergy. I'm trying to understand the factors that could drive this to, let's say, $120 million in EBITDA, and at the same time, the risks that could push this to $70 million in EBITDA. Basically, if you could talk about some of the factors that we need to watch carefully to understand the sensitivity of EBITDA in this business.

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

You're talking about the synergies, Manav, more than anything? I think...

Manav Gupta - *Crédit Suisse AG, Research Division - Research Analyst*

The total EBITDA of $88 million, I'm just trying to understand the upside and the downside and what could drive the -- could be the driving factors to that guidance.

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Okay. So with the base EBITDA here, as Rich highlighted in his portion of the discussion, the EBITDA is very stable here. And I think that speaks to the nature of the end markets that we're talking about, personal care products, pharmaceuticals, food applications, things that are relatively stable and recession-proof. So we think again the base EBITDA of this business is very stable, very solid. So we don't see much concern or volatility there. Then as far as the synergies that we're going to layer in on top of that, that just speaks of to now having a 4-facility lubricants network versus the 2 that we have currently and the synergies that will result from that, as Rich highlighted on the SG&A side, the logistics side, the opportunity to optimize between, again, 4 facilities versus 2, make the right products in the right processing unit closest to the customer and/or closest to the supplier.

Manav Gupta - *Crédit Suisse AG, Research Division - Research Analyst*

Excellent, George. I just have one quick follow-up. The Rack Forward business has worked very well for you. You have delivered stable margins. And this acquisition is basically Rack Forward again. So from here on, when we look at HFC, do we think when you're growing your PCLI business, even the going-ahead acquisitions will mainly be focused on the Rack Forward? Or you are still open to doing some Rack Back acquisitions also?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Well, I think we're open to both segments but our higher priority is on the Rack Forward. I think we've been pretty consistent with our messaging here and our strategy in the lubricants business. Again, we like both segments but we like the Rack Forward better because, again, the margins are higher and more stable over time.

Operator

Your next question comes from Phil Gresh with JPMorgan.

Philip Mulkey Gresh - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Congratulations on the transaction. First question, I guess, maybe a bit following up on Manav's second question. How do you see the pipeline of opportunities today? Is this the one kind of bigger opportunity you've been looking at? Or do you feel like you still have a pretty good pipeline of opportunities in the lubs business looking into 2019?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

No. We're very pleased with the pipeline of opportunities we're seeing in the space. As we've said before, this business is highly fragmented. It's a lot of small private companies, a lot of private equity companies, such as Sonneborn, in this space. It's such a large global market that we see lots of opportunities across all of these segments, finished lubricants, specialty products, waxes, white oils, greases with diverse customer bases as well. Again, customer segments like personal care, pharmaceuticals. So that's what we like about this space is the diversity of products with diversity of end markets that, again, contribute to the EBITDA margin profile that was talked about.

Philip Mulkey Gresh - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Okay. Second question, I guess this one's for Rich. Rich, I think you made the comment that you want to maintain $1 billion to $1.2 billion of cash in the balance sheet, roughly I think where you ended the third quarter. So I guess that we should interpret from that, that you might pause on the buybacks until the deal closes. But then thereafter, it seems like you still have a pretty good cash flow profile to perhaps, I believe, after this acquisition, continue to maintain some amount of buybacks moving forward. Is that a reasonable way to think about things?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

No. Actually, Phil, I think it's kind of, I'd argue, the other way. So we've got the cash on the balance sheet now to fund the acquisition and continue to generate good cash flow across all 3 businesses. So we'd expect to be buying back stock.

Philip Mulkey Gresh - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

Okay. So do you think you can continue at the 3Q run rate essentially moving forward?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

I think we've been pretty clear about the run rate will be largely dictated by what the market gives us at the end of the day. So we'll buy back -- again, we'll target that $1 billion to $1.2 billion. We do plan, obviously, to spend organic capital on our business as well. But beyond that, we'll go ahead and be repurchasing stock.

Operator

Your next question comes from Roger Read with Wells Fargo.

Roger David Read - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

I guess, let me just ask about Sonneborn. You said the business is real stable here. How have they been in terms of introducing new products? In other words, are we looking at stability and no real change? Or that stability is built by the fact that they introduce new products, and that's maybe not included in synergies but something we should be focused on down the road?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

I think this business has a proven track record of introducing new products, Roger. They work very well with their customers to understand their needs and to customize solutions to those needs through -- given their R&D capability.

Roger David Read - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

And is that something new to the overall organization for you? Or if you compare it to your other Rack Forward businesses, it's very similar that way? I guess, I'm just trying to understand maybe the upside value of the acquisition as opposed to just looking at it from a Rack Forward EBITDA only.

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Yes. No, I think to your point, this is -- what Sonneborn's R&D capability brings is very similar to what the PCLI R&D capability brought to us when we acquired that in February of '17. So it's very similar, slightly different markets and products but the capability, again, of working with your customer, having them share what their specific needs are and tailoring a customized solution through the variety of base oil feedstocks and processing capabilities. And that's what we're really excited about is being able to bring, again, 4 facilities versus the 2 we have now. And we think those opportunities really open up geometrically as you add more facilities and more base stock, feedstock options.

Roger David Read - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Okay. And then as we look at the synergies, I would imagine G&A is fairly quickly realized. The other 2 maybe take a little bit longer. Can you give us an idea of maybe of what some of the optimization is? And is this a 12-, 24-, 36-month goal on the synergy front?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

Roger, it's Rich. So I think your impression is fair. The SG&A synergies will come quickest. I think the logistic synergies will probably take 12 to 18 months to fully realize. The optimization synergies will be longer, call it, 24 months, give or take. That, as George has mentioned, right, it's a lot of optimizing feeds and production across 4 facilities, making the right products at the right plant at the end of the day.

Operator

Your next question comes from Blake Fernandez with Simmons Energy.

Blake Michael Fernandez - *Piper Jaffray Companies, Research Division - MD & Senior Research Analyst*

Congrats on the deal. Rich, if I can just go back and clarify real quick on Phil's question. I realize you're going to get down to about $400 million post the deal closing. The $1 billion to $1.2 billion of cash, are you saying you need to build back up to that level? Or are you comfortable holding roughly $500 million of cash on the books?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

Yes. So we've said and we continue to believe that all things being equal, $500 million of cash on the balance sheet is the correct number. Given the transaction, effectively, what we're saying is we would add the purchase price to that $500 million. That gets you to $1 billion, $1.2 billion. We're there right now, so we're funded as far as we're concerned. So again, excess cash over and above that, we will return to shareholders from here on out.

Blake Michael Fernandez - *Piper Jaffray Companies, Research Division - MD & Senior Research Analyst*

Okay. So you're -- okay. In our previous travels, you had talked about the fragmentation of this market, and I think you alluded to that. If I'm not mistaken, I think you were marketing products in Europe or internationally before but this is your first real manufacturing in Europe. And so I'm kind of curious to see if a lot of the opportunities -- I always thought of it as like privately held businesses here in North America, are a lot of those opportunities in Europe as well? I'm just wondering if this is like a launching pad for a broader international kind of growth?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Yes. I think, Blake, our focus is primarily North American. But this business obviously has both the North American and European components. So I think this is a logical extension of our production capability. But again, it's not a primary focus to broaden into Europe and Asia. Again, never say never. When the right opportunities come along, we'll pursue them. But it's not the major thrust of our growth initiative to look for international opportunities.

Blake Michael Fernandez - *Piper Jaffray Companies, Research Division - MD & Senior Research Analyst*

Okay. And if I could just clarify one thing. I know you had the CapEx mid-cycle $60 million to $70 million. Is it fair to assume that, that just lands into 2019 spending?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

No. So Blake, that's mid-cycle. Obviously, we've got a fairly chunky turnaround every 4, 5 years at Mississauga, which we just had in 2018. So we'd expect a lower capital number in our lubricants business in 2019.

Operator

Your next question comes from Matthew Blair with Tudor, Pickering, Holt.

Matthew Robert Lovseth Blair - *Tudor, Pickering, Holt & Co. Securities, Inc., Research Division - Executive Director of Refining and Chemicals Research*

Rich, you mentioned that $500 million is a good run rate on cash going forward. But what about the debt side of the equation? As you add these specialty businesses that provide more stable EBITDA, would you be, I guess, interested in levering up?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

No. I think where we're at right now is we feel comfortable with our debt profile today. We intend and expect to maintain our investment-grade rating. To your point, as we add more stable businesses and cash flows that gives us some more flexibility going forward, so we'll continue to reevaluate. But right now, no intention to add additional debt.

Matthew Robert Lovseth Blair - *Tudor, Pickering, Holt & Co. Securities, Inc., Research Division - Executive Director of Refining and Chemicals Research*

Okay. And then, I think it was Slide 9, it showed approximately, let's call it, $53 million in EBITDA for this business in 2016. In 2017, it jumped up to $70 million. Could you talk about the drivers behind that move? Was it more related to the changes in feedstock base oil pricing or more related to changes in, I guess, end market demand in pricing?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

No. This is actually a pretty easy one, Matthew. In 2016, Sonneborn did have a production issue at the Petrolia facility. They had a fire, and they were not able to produce for a period of time. So that drove the dip you saw in 2016. So actually we really view this as kind of a legacy of the last year, so $60 million to $70 million a year run rate EBITDA business.

Matthew Robert Lovseth Blair - *Tudor, Pickering, Holt & Co. Securities, Inc., Research Division - Executive Director of Refining and Chemicals Research*

Is there any turnaround, I guess, planned turnaround impacts in these numbers here?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

Not really, Matthew. The way -- these are -- turnarounds are not -- these units don't really turnaround the same way as you'd think a refinery would. So the way we think about it is the maintenance capital of this business should run $8 million to $12 million a year pretty ratably, without much production volatility year to year.

Operator

Your next question comes from Jason Gabelman with Cowen.

Jason Daniel Gabelman - *Cowen and Company, LLC, Research Division - VP*

I have a question about the product mix. So I believe white oils are kind of in the middle of the margin profile for specialty product. Are the other products that you list on Slide 8 and specifically the petrolatums, are those kind of higher margins, lower margin or similar to white oil? And just as a follow-on to that, you list a handful of products that you [can't] produce. Is there a challenge in managing the product mix to kind of realize the maximum potential margin on these products?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

So I'll take the first question. I think the best way for -- to think about these Sonneborn products is that they're the next step forward or downstream in the value chain for white oils and waxes. So the petrolatums are products from white oils and other feedstocks. And similarly, the microcrystalline waxes that Mark Plake mentioned, it was shown in the middle of that slide, the microcrystalline waxes, those are the next logical step downstream from the wax products that we make from both Tulsa and Mississauga. So again, that's what we really like about this business. It shores up existing product lines and then again takes us the next step, the next logical step downstream with these value chains.

Jason Daniel Gabelman - *Cowen and Company, LLC, Research Division - VP*

Got it. And then -- sorry, and then on the product mix part of the question?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Yes. I think this business again is similar to PCLI. It makes a variety of products, a lot of SKUs. There is a challenge to managing it but as with PCLI, Sonneborn has demonstrated the capability to be able to manage the diverse product portfolio and the diverse set of customers. And their ability to manage that manifests itself in the high stable margins that we see in these businesses. So yes, it's challenging but again, it's very doable, and the end product has a great margin profile.

Jason Daniel Gabelman - *Cowen and Company, LLC, Research Division - VP*

Got it. If I could just ask a follow-on on the feedstock side, it looks like on Slide 7, you guys are kind of short base oil feedstock. I'm not sure if I'm reading that correctly. But does this increase your shortage in base oil to feed, the specialty plants? And if so, how are you thinking about kind of the base oil feedstock market moving forward over the next few years?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Yes. So we're still net long base oils even with this acquisition. So the purchases that are coming in are specialized purchases that we don't make either at Tulsa or at Mississauga. Or if they are products that we make at Tulsa and Mississauga, it's one of the reasons why we made this acquisition is to forward integrate those base oils to finished products as part of our strategy of forward integrating again. So I don't think this acquisition has a material impact on our view of the base oil market. It does allow us again, as we mentioned earlier, to pull through some of our folks in Mississauga base oils through this business. And we will continue our strategy to, again, forward integrate.

Operator

(Operator Instructions) Your next question comes from Doug Leggate with Bank of America.

Douglas George Blyth Leggate - *BofA Merrill Lynch, Research Division - MD and Head of US Oil and Gas Equity Research*

So I was trying to -- my apologies. I'm sitting in an airport. Can you hear me okay?

Craig Biery - *HollyFrontier Corporation - Director of IR*

Yes, sir.

Douglas George Blyth Leggate - *BofA Merrill Lynch, Research Division - MD and Head of US Oil and Gas Equity Research*

Okay, good. So guys, I wonder if you could help me with the tax, the after-tax cash flow? Because obviously, you're bringing an international business into the mix. What does the $65 million of EBITDA translate to as a kind of average cash flow number after tax?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

So Doug, the way I'd answer that question is it's coming pretty low tax basis. In this case, the tax rate is roughly similar. So we have no change on our overall tax rate guidance. So I think about $65 million, $70 million of EBITDA; a 20%, 25% tax on that number, and then back out the -- we talked about maintenance capital $8 million to $12 million a year, that kind of gets you $40 million to $50 million of free cash flow a year.

Douglas George Blyth Leggate - *BofA Merrill Lynch, Research Division - MD and Head of US Oil and Gas Equity Research*

Okay. So the implied cost of capital is 6%, 7%, something like that, as an annuity?

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

It would be -- are you trying to get to a free cash flow? Or...

Douglas George Blyth Leggate - *BofA Merrill Lynch, Research Division - MD and Head of US Oil and Gas Equity Research*

Yes. I'm trying to think -- so if it does about -- so $40 million of free cash on your acquisition price. I'll probably assume this is like an annuity. I'm trying to back into an implied -- yes, an implied earnings yield for this thing.

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

Yes. So I think before any synergies, yes, you're talking 6% to 7%. Obviously, we expect to generate synergies and growth beyond that.

Douglas George Blyth Leggate - *BofA Merrill Lynch, Research Division - MD and Head of US Oil and Gas Equity Research*

Good stuff. My follow-up is very quickly. It's on the range -- I think it's on Page 15, the range of multiples for the peer group. What is behind the variability there? It's about 7x to 15x. What do you see as the attributes of those different businesses that drive such a wide range of multiples? And what do you think is the right -- and we said 11x is an average. But where in that range do you see the quality of this business sitting, the high end or the low end? And I'll leave it there.

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

So Doug, I think we'd say mid- to high end. I think if you look at this peer group, obviously, the low end of this range is driven by balance sheet issues, not by the business itself. And so I think you can count, if you take the attitude of throw out the high and throw out the low, and then the high end of this range, that's a pretty closely held company at the end of the day, a very excellent business but it's got some technical issues that probably drive at least a portion of that multiple. So again, in our mind, you throw out the high end, you throw out the low end, that gets you that range of 9 to 14x. We think our business is mid- to high end of that range.

Douglas George Blyth Leggate - *BofA Merrill Lynch, Research Division - MD and Head of US Oil and Gas Equity Research*

Great stuff. And sorry, guys, if I could just squeeze one last one, just on the debt of the acquisition. Is that higher cost or lower cost than you guys? And would you intend to refinance that? And I'll leave it there.

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

We'll be getting the business debt-free, cash-free, Doug.

Operator

The next question comes from Paul Cheng with Barclays.

Paul Cheng - *Barclays Bank PLC, Research Division - MD & Senior Analyst*

I tuned in maybe late, so you may have already addressed it. Rich and George, any time when you do a reasonable-sized acquisition, it's going to take some management time and integration and all that. So from that standpoint, do you think at this moment, you have your hands full and you're not going to make a similar-sized acquisition like that? Or that you think your management capability is still capable for you to take on this type of acquisition within the mix [trauma]? Or do you think that it's going to be maybe at least 2 or 3 years, you have opportunity come for this kind of acquisition? So I'm trying to understand how you look at the time you'd take for you to be comfortable that you can take on additional asset?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Yes. I'll only answer the question this way, Paul. I don't view management and integration constraining our ability or desire to do future acquisitions. And that's [if] we have a good management team now. I think we're acquiring some excellent talent with this acquisition. And I think between what we have now and what will be coming to us with Sonneborn, I think we can quickly and efficiently integrate that business. And I think our pace of future acquisitions will be dictated by what we see in the marketplace. And if we see something that's attractive, like Sonneborn or PCLI, I don't think we'll be afraid to pull the trigger and do another deal while we're integrating Sonneborn in the HFC family.

Paul Cheng - *Barclays Bank PLC, Research Division - MD & Senior Analyst*

George, is the Sonneborn acquisition, do you intend to attribute it as a standalone business to run here as it is? Or that is really going to be fully integrated in with the rest of your lubricant business? And do you have to maintain different systems? Or how long the process is going to take for you to fully integrate?

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Yes. I think we're going to fully integrate this acquisition into our HF LSP business. I think it fits real well in that portfolio. And I think it's well suited to bring into the fold again. I'll let Rich comment on any back-office system issues that he might see.

Richard Lawrence Voliva - *HollyFrontier Corporation - CFO & Executive VP*

No. I think we spoke about this a little earlier. We'd expect to realize some SG&A synergies pretty quickly but we don't see any issues or hurdles with the integration.

Operator

There are no further questions at this time. I will now turn the call back over to the presenters.

George J. Damiris - *HollyFrontier Corporation - CEO, President & Director*

Thank you all for joining the call with us this morning. As always, if you have any questions, please feel free to reach out to Investor Relations.

Operator

This concludes today's conference call. You may now disconnect.
