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NOV - Q4 2015 National Oilwell Varco Inc Earnings Call

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**OVERVIEW:**

Co. reported 4Q15 revenues of $2.7b and GAAP net loss of $1.5b or $4.06 per fully diluted share.





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## CORPORATE PARTICIPANTS

**Loren Singletary** *National Oilwell Varco, Inc. - VP IR*

**Clay Williams** *National Oilwell Varco, Inc. - Chairman, President, CEO*

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**Marshall Adkins** *Raymond James & Associates, Inc. - Analyst*

**Bill Sanchez** *Howard Weil Incorporated - Analyst*

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**David Anderson** *Barclays Capital - Analyst*

**James West** *Evercore ISI - Analyst*

## PRESENTATION

**Operator**

Good morning and welcome to the National Oilwell Varco earnings conference call. My name is Kevin and I will be your operator for today's call. (Operator Instructions)

I will now turn the call over to Mr. Loren Singletary, Vice President Investor and Industry Relations. Mr. Singletary, you may begin.

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**Loren Singletary** - *National Oilwell Varco, Inc. - VP IR*

Thank you, Kevin; and welcome, everyone, to the National Oilwell Varco fourth-quarter and full-year 2015 earnings conference call. With me today is Clay Williams, President, CEO, and Chairman of National Oilwell Varco; and Jose Bayardo, Senior Vice President and Chief Financial Officer.

Before we begin this discussion of National Oilwell Varco's financial results for its fourth quarter and fiscal year ended December 31, 2015, please note that some of the statements we make during this call may contain forecasts, projections, and estimates including but not limited to comments about our outlook for the Company's business. These are forward-looking statements within the meaning of the federal securities laws, based on limited information as of today, which is subject to change. They are subject to risk and uncertainties, and actual results may differ materially. No one should assume that these forward-looking statements remain valid later in the quarter or later in the year.

I refer you to the latest Forms 10-K and 10-Q National Oilwell Varco has on file with the Securities and Exchange Commission for more detailed discussions of the major risk factors affecting our business. Further information regarding these as well as supplemental financial and operating information may be found within our press release on our website at www.NOV.com or in our filings with the SEC.

Later on this call we will answer your questions, which we ask you to limit to two, in order to permit more participation. Now let me turn the call over to Clay.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Thank you, Loren. National Oilwell Varco faced deteriorating market conditions during the fourth quarter to cap off a very challenging year. The Company reported fourth-quarter net income of $85 million or $0.23 per fully diluted share, excluding other items, down from $0.61 per fully diluted share in the third quarter of 2015 on a comparable basis.

Other items included pretax charges of $1.6 billion in goodwill and intangible asset impairments; $139 million in restructuring, inventory write-downs, severance, and facilities closures; and $7 million in FX losses in Argentina. GAAP net loss for the quarter was $1.5 billion or $4.06 per fully diluted share.

Fourth-quarter 2015 revenues were $2.7 billion, down 18% from the third quarter of 2015. Operating profit for the quarter was $141 million or 5.2% of sales, and EBITDA was $308 million or 11.3% of sales, excluding other items from both.

Decremental operating leverage was 35% from the third quarter to the fourth. Our management teams across our business units are responding quickly to lower revenues, which fell further than we expected in the fourth quarter, by reducing costs and accelerating restructuring plans, which enabled us to hold decremental leverage to 35%, ex-charges, despite the sharp volume decline and renewed intense pricing pressure we are seeing.

As we have stated for the past few quarters, our focus is to manage what we can -- namely costs -- while continuing to advance our longer-term strategic goals. It nevertheless remains a very challenging time for everyone in the oil and gas industry and our visibility remains limited.

For its full-year 2015, National Oilwell Varco posted a GAAP loss of $1.99 per fully diluted share, including restructuring, asset impairments, facility closure costs, and other charges of $2 billion pretax. Excluding these items, earnings were $2.80 per fully diluted share, down 54% from $6.07 per fully diluted share earned in 2014.

Operating profit was $1.6 billion or 11.1% of revenue. And EBITDA was $2.3 billion or 15.5% of revenue for the full year, excluding charges.

Decremental operating leverage was 32% from 2014 to 2015, excluding charges from both years, a commendable result in view of the severe downturn and pricing pressures we faced throughout the year.

Cash flow from operations for 2015 totaled $1.3 billion, with $614 million of that coming in the fourth quarter with improving working capital liquidation. We continued to invest in our future, closing seven acquisitions through the year which, among other benefits, enhanced our presence in Saudi Arabia, our wellsite services offering in Asia, and brought in new composites technology. We continued developing new products with our new test rig, which we spudded at the beginning of the year.

We also continued investments in the world's most promising regions, adding new facilities in Saudi Arabia, Abu Dhabi, Russia, and West Texas.

We returned to $.9 billion to shareholders in 2015 through dividends and share repurchases.

With regards to costs, we were able to match to good decremental operating leverage on our 31% decline in revenues, ex-charges, by close attention to costs and efficiency. We insourced tens of thousands of hours from outside suppliers to our workforce to preserve our team wherever possible. Nevertheless, our global workforce including contract labor declined 21% through the year, and we closed 75 facilities since mid-2014 to retrench to a smaller, more efficient footprint. We expect restructuring will continue through the first half of 2016, perhaps longer in view of the challenging market.

A second major decline in oil prices last year deepened and intensified late during the fourth quarter and continued throughout January, when oil traded into the high $20 range, levels not seen since 2003. This, combined with hedges rolling off for E&Ps and term contracts expiring for drilling contractors, ratcheted up financial stress on our customers and increased pricing pressure on NOV.

We believe the present level of activity is insufficient to supply the longer-term demand for oil and note that, unlike the three most recent downturns through the past 20 years, OPEC has not curtailed production to defend pricing. This has made the present downturn far more severe, but will perhaps lead to a sharper eventual recovery.

With producers pumping furiously to maximize their cash flow, the relentless march of depletion, the deferral of 68 projects representing 3 million barrels of oil per day of planned future production, and the unfolding of severe capital austerity will help bring supply and demand into balance. But we are not planning for recovery in 2016. Instead we will continue to manage costs to the reality of the marketplace in the short term.

Even with a rebound in oil prices, it will take time for our customers to repair balance sheet, reactivate crews, and to ramp up the activity that drives our business. But each day that passes means we are a day closer to the inevitable rebound. Our plan is to emerge with new products, new business models, and new efficiencies.

Our Completion & Production Solutions segment fell 7% sequentially in the fourth quarter and posted 56% sequential decremental operating leverage, excluding restructuring and other items. Orders declined from 99% book-to-bill in the third quarter to 59% in the fourth, which led backlog down to $969 million at year-end.

Strong sequential improvements in our XL Systems conductor pipe connections unit in the fourth quarter capped off a solid year for this unit, with higher year-over-year margins. However, these failed to fully offset sequential double-digit declines in our other products within the segment.

In North America, customers delayed picking up well stimulation equipment previously ordered, and some are now buying frac spreads at distressed pricing to use for spare parts, which further reduced sales but will ultimately help erode the equipment overhang. In North America, sales of spares and consumables like coiled tubing declined with reduced activity, but the FSU and the Middle East remain comparatively strong.

Sales of composite oilfield pipe declined as the cost of competing steel flowlines have plummeted 35% or more, and our sales into the marine construction market slowed. Our value proposition for the composite pipe that we manufacture is much lower lifetime cost, due to its corrosion resistance, but E&Ps under duress are opting for the lowest investment option to bring on wells and their associated cash flow.

About 20% of the segment's mix is in production equipment: pumps, separators, and artificial lift, which also fell in the quarter as distributors slowed purchases. We have six major facility consolidations underway within this business unit, which will drive better efficiency going forward.

Within our offshore production-related businesses we saw rising pricing pressure on flexible pipe, but were pleased to post a 111% book-to-bill as we landed some significant orders for presalt applications in Brazil. Our floating production vessel unit continues to pioneer new business models we launched a few years ago that leverage NOV's unique vessel construction capabilities to improve construction costs and reduce risks. Our new vessel concepts, which seek to accelerate production from certain types of deepwater fields are being met with high enthusiasm from our customers so far.

We are encouraged by new designs that are steadily whittling costs, but operators remain slow to sanction major deepwater projects. It is nevertheless a promising target, with 400 discoveries in the offshore.

Our Wellbore Technologies segment revenues fell 9% sequentially in the fourth quarter and posted 69% sequential decremental operating leverage, which resulted in a negative 4.1% operating margin, excluding restructuring and other items. EBITDA margins were 9% for the segment, ex- other items.

Two-thirds of the sequential decline in revenue came from North America, where operators stacked major drilling programs, intensifying pricing pressures and reducing volumes. Rentals of solids control equipment, rig instrumentation, and downhole equipment declined at high variable margins. Nevertheless we were able to increase share in our bits business, owing to new Tectonic designs which we are successfully packaging with our ERT drilling motors.

In the FSU we expect to begin production in our downhole tools facility at our new Kostroma plant within a few weeks to supply the local market which, along with Asia, posted higher sequential revenues in the fourth quarter. Latin America saw a significant decline for this segment across Brazil, Mexico, and Argentina.

Our Tuboscope pipe coating business held up well through the quarter on drillpipe strength in China. But pipe mill inspection activity in North America declined, with nine months of casing on the ground, the highest level of inventory seen since the 1980s.

Rising activity around tubing, pipeline, and line pipe helped offset this somewhat. But we are even seeing workover activity fall in West Texas, which is unusual. Prior downturns have seen workover activity hold up better, owing to quick paybacks.

Drillpipe sales increased modestly from the third quarter into the fourth quarter, but still remain low and under price pressure. Growing operator interest in closed-loop automated drilling technology drove higher revenues for our IntelliServ wired drillpipe unit in the fourth quarter, to produce solid year-over-year improvements for the group. This innovative service grew 6-fold in 2015 as compared to 2014, and we have lots of interest from E&Ps as well as drilling contractors eager to differentiate their rigs by enabling high-speed data transmission from the bottom of the hole through their drillpipe.

Our Rig Aftermarket segment posted flat sequential revenues, but margins fell due to mix. A decline in spare parts sales was offset by higher repair revenues, which came in at lower margins partly due to rising discounts to win repair work. As rigs come down, particularly onshore, they are being cannibalized for parts, impacting our spares business for the quarter.

SPS activity on offshore rigs rolled over in the fourth quarter, but remains active nonetheless. The Rig Aftermarket segment is actively working on about 40 projects either underway or in the bidding stage, but these are fluid as drilling contractors are curtailing scope or, in some instances, electing not to proceed with an SPS without a clear line of sight on a contract for the rig.

Service and repair work in the US Gulf of Mexico improved sequentially for Rig Aftermarket, and BOP repair work in the Middle East remains strong.

Rig Systems revenues fell 32%, at 24% decrementals in the fourth quarter, driven by sharply lower shipments out of backlog. Customers are delaying acceptance of uncontracted newbuilds to avoid stacking costs and to slow their CapEx as they face falling dayrates and utilization, as their contracts roll off.

Revenues from new offshore rig construction fell to about 20% of our consolidated revenue mix in the fourth quarter. We are working closely with our shipyard customers to navigate challenges and requests for delays and to improve our collections, but these situations remain fluid. At this point we expect revenues out of backlog for all of 2016 to total about $2.1 billion or $2.2 billion.

Rig Systems saw a 76% decline in new orders in the fourth quarter, which fell to $89 million and totaled $1 billion for the full year. Quoting activity plummeted late in the year, and while we still see interest for new land rigs for the Middle East and some other selected markets, we expect orders to again be very low for the first quarter. Importantly, we expect the land rig market to eventually resume its efforts to retool to more efficient AC technology; but the fourth-quarter downturn in dayrates for Tier 1 rigs will certainly delay that trend.

As we disclosed in December, we reached a confidential settlement with one of our shipyard customers in Brazil to cancel seven floating rigs being constructed there, which reduce our backlog by nearly $1.2 billion and led to a year-end backlog of $6.1 billion for all of Rig Solutions segment. At year-end that backlog includes $1.75 billion for the remaining 15 rigs across three shipyards in Brazil.

I would stress that the situation in Brazil with regards to these remains uncertain and continues to evolve, owing to the failure of our shipyard customer to secure long-term financing for these projects. We suspended work within two of these remaining three shipyards early last year, and we are in discussions with all three yards regarding the resolution of their programs. We recognized only $10 million in revenues from the remaining newbuild rigs in Brazil during the fourth quarter of 2015.

As we wrap up a challenging year in 2015, we recognize we are facing increasing headwinds in 2016, but we also recognize that extraordinary opportunities will arise as a result of the stress our industry is under. I'm pleased with the execution of our experienced leaders, who are cutting costs and improving efficiency, but also continuing to advance our long-term strategic initiatives -- like closed-loop automated drilling opportunities, which we expect to grow in 2016; new FPSO business models and designs to improve deepwater economics; and new products to improve drilling operations, completion techniques, and more profitable production.

Our E&P customers' business models simply don't work in this low oil price environment, and therein lies the opportunity for NOV to once again pioneer new, more efficient ways of extracting oil and gas to reduce their cost.

Importantly, NOV represent a diverse portfolio of market leaders that participate in every major oilfield market around the globe. We examine the major global sources of oil, which make up the 90-plus-million barrels of oil per day global industry. We see 10 million barrels of oil per day coming out of each of Saudi Arabia and Russia, both areas where we have invested heavily through the past few years, with our investments continuing to support relatively high levels of activity. Another 10 million barrels of oil per day comes from the Gulf States where, again, we are expanding our presence and the oilfield remains comparatively busy.

Nearly 10 million barrels per day has been achieved from deepwater production, where we have benefited disproportionately from the deepwater and offshore rigs we have built and expect to pioneer better methods of production in the future. Another 10 million barrels per day, roughly, comes from North America, which is dominated by shale production techniques.

Each of these major productive areas has been enabled by NOV technology, and we continue to help our customers adapt to lower oil prices across them all. NOV remains well positioned globally for when the eventual recovery comes, wherever it shows up first.

Our leading market positions have been assembled through a combination of organic investments and acquisitions, and we are actively pursuing several targets now. It has been challenging and sometimes frustrating to reach agreement with potential sellers; but as the downturn lengthens, everybody in this space is becoming a lot more realistic.

We remain patient and disciplined on values and realistic in our outlook as the option value of our capital flexibility steadily rises. I am pleased that NOV has the balance sheet and financial resources to pursue these. But I am more pleased that we have tough, capable, experienced managers who can skillfully integrate acquisitions and execute our business plans.

To all of the NOV employees, I congratulate you for navigating such a challenging year in 2015, and I thank you for your contributions in building such a strong enterprise. We have a tough road ahead, but we are laying the groundwork for our future success. Jose?

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**Jose Bayardo** - *National Oilwell Varco, Inc. - SVP, CFO*

Thank you, Clay. I'll next provide some additional detail on our segment operating results for the fourth-quarter and full-year 2015, and provide some commentary on the near-term outlook.

Our Rig Systems segment generated revenue of $1.0 billion, down 32% from the $1.5 billion earned last quarter, and down 60% from the $2.6 billion generated in the fourth quarter of 2014. For the fourth quarter, the split between offshore- and land-related revenue was 73% and 27% respectively.

Revenue out of backlog was $843 million, down 35% sequentially. As Clay indicated, sliding delivery schedules and limited new order intake have contributed to the decline in revenue.

You may recall that in the first quarter of 2015 we announced we were negotiating certain customer-requested delivery delays for offshore newbuild rigs. Although not our first choice, modifying delivery schedules allowed us to better manage our cost structure and level-loading across our operations, as we began sizing our business to support reduced levels of demand. The success of our cost management measures are seen in our decremental operating profit margins, which were 23.9% on a 32% sequential revenue decline, and which were 22.7% on a 60% year-over-year revenue decline.

Fourth-quarter operating profit for the Rig Systems segment was $160 million, yielding operating margins of 15.8%, down 260 basis points from Q3. EBITDA was $184 million or 18.1% of sales; and EBITDA margins decreased 200 basis points compared to the third quarter of 2015.

During the fourth quarter, we received $89 million in new orders, resulting in a book-to-bill of 10%. Q4 bookings were composed entirely of discrete pieces of capital equipment, as we received no new rig orders in the quarter. Bookings included topdrives and blowout preventers for international land rigs and cranes for offshore construction vessels.

We ended the quarter with a backlog of $6.1 billion, down 24% sequentially, of which approximately 89% is for the offshore market and 92% is destined for international markets.

As Clay mentioned in his commentary, our customers are under increasing pressures related to falling dayrates and utilization associated with the cyclical downturn. Our global portfolio of offshore rig equipment contracts typically incorporates significant downpayment and progress payments which minimize our working capital investments throughout the life of the agreement. While we do not expect meaningful charges from potential future breaches of contracts, cancellations, or other similar issues, the impact would vary, dependent upon the specific contract, timing of the event, and other circumstances.

For full-year 2015, Rig Systems generated revenue of $7 billion, down 29% in comparison to 2014, as slowing project progress and declining orders drove revenue out of backlog down $2.6 billion from the $8.7 billion earned in 2014. With a resolute focus on execution and a commitment to continued cost reductions, Rig Systems generated $1.4 billion in full-year EBITDA and maintained EBITDA margins just over 20%, despite revenues declining almost 30% over the same period. Full-year 2015 operating profit was $1.3 billion or 18.9% of revenue, down 140 basis points from the previous year, representing decremental leverage of 23.5%.

As we move into the first quarter of 2016, at this point we expect Rig Systems revenue to decline in the high-single-digit percentage range and revenue out of backlog to decrease to around $775 million, but I will stress that our visibility remains limited.

We plan to deliver on our current backlog while continuing to resize the business aggressively to meet a much lower level of demand. We are actively scaling facilities to single shifts, consolidating locations, and implementing other cost-control initiatives. Despite these efforts, reduced volumes will work against us, and we anticipate some margin erosion on lower activity levels and continued delays, in the range of 200 to 300 basis points.

Declining energy prices will negatively impact our order book for the foreseeable future, and we expect new orders for large equipment packages both on- offshore to remain low.

We continue to win in the marketplace do our commitment to technology, capacity, and operational service and support, but orders are scarce. As such, we do not expect this quarter's bookings to improve materially from the fourth quarter.

Our Rig Aftermarket segment generated $559 million of revenue during the fourth quarter 2015, roughly flat sequentially and down 33% year-over-year from a record $850 million in the fourth quarter of 2014. Customers curtailed spending as rig utilization declined in both land and offshore markets. Land-related sales were approximately 21% of total segment revenue, down slightly from 22% in Q3, but up on a percentage basis from 18% in the fourth quarter of 2014.

EBITDA for the segment was $135 million or 23.7% of sales. Operating profit was $127 million or 22.3% of sales, down 330 basis points from last quarter on higher proportion of lower-margin service and repair work as well as incremental pricing pressure on repair and select spare parts.

Overall, 2015 results reflected an increasingly uncertain environment in which our drilling contractor customers reduced spending in an effort to preserve liquidity. Throughout the year our customers chose to deplete existing spares inventories rather than pursue new, and did de minimis repair work and maintenance on their rig fleets, deferring more expansive work except where absolutely necessary.

For the full year, Rig Aftermarket generated revenue of $2.5 billion, down 22% from a record 2014. For full year, EBITDA was $647 million or 25.7% of revenue, down 250 basis points from 2014. In 2015, operating profit was $617 million or 24.5% of sales, down 290 basis points from the prior year.

Looking into the first quarter of 2016, we expect Rig Aftermarket will see revenues decline in the mid- to upper-teens percent range. Due to the seasonal nature of the aftermarket business, we typically expect lower activity with a better mix of spares to service and repair work in the first quarter than in the fourth. However we anticipate a steeper than usual decline in Q1, reflecting current market conditions.

Although reducing costs will be at the forefront of our response efforts, pricing pressure may push margins around 100 basis points lower in the first quarter. Longer-term, we believe our Rig Aftermarket segment will be a strong early-cycle beneficiary of the eventual recovery. We believe drillers will rush to return sub-optimally maintained, stacked, partially cannibalized rigs to proper operating condition once they gain confidence that the market has reached a bottom and they see early indications of a recovery.

For the fourth quarter of 2015, the Wellbore Technologies segment generated revenues of $757 million, down 9% sequentially from $834 million, and down 50% from a record $1.5 billion in the fourth quarter of 2014. Reduced drilling activity negatively impacted all of our businesses within the segment.

Average rig counts declined by 13% sequentially in the US, 9% in Canada, and 2% internationally. Segment revenue by geography closely mirrored the sequential fall in rig count.

Pricing pressure continued into the fourth quarter across most all product lines. For the fourth quarter of 2015, EBITDA was $68 million or 9% of revenue, down 530 basis points from last quarter; and the segment posted an operating loss of $31 million.

For the full-year 2015, Wellbore Technologies generated revenue of $3.7 billion, down 35% in comparison to 2014, consistent with the year-over-year average decline in global rig count. 2015 EBITDA for the segment was $562 million or 15.1% of revenue, down from 26% in 2014; and operating profit was $162 million for the year, for 2015, or 4.4% of sales as the speed of activity and revenue decline outpaced our reduction efforts.

Like our Rig Aftermarket business, we expect our Wellbore Technologies segment to be an early-cycle beneficiary of the eventual recovery. However, near-term we have limited visibility, and the activity-driven nature of the business contributes to variability. Just four weeks into 2016, US rig count is down 18% from the average in Q4 of 2015, so we expect revenues to fall 8% to 10%, with decremental margins in the 40% range.

We continue our efforts to optimize our Wellbore Technologies segment, resizing our business to meet lower levels of demand, improving our manufacturing processes to become more efficient on a lower cost base, and shortening our commercialization processes to bring new value-adding technologies to market.

Our Completion & Production Solutions segment generated revenues of $746 million for the fourth quarter of 2015, down 7% sequentially and 44% compared to the fourth quarter of 2014. Businesses related to onshore completion and production were some of the most negatively impacted, with customers delaying receipt of finished orders as operators' inventory of drilled but uncompleted wells rose in response to commodity price declines.

EBITDA for the segment was $86 million or 11.5% of sales. Operating profit for the segment was $34 million, resulting in operating margins of 4.6%, down 330 basis points sequentially and 1,160 basis points year-over-year as a result of lower volumes and pricing pressure.

During the quarter, Completion & Production Solutions received orders of $272 million, down $194 million or 42% sequentially, as a substantial flexible pipe order won in the third quarter did not repeat. We recognized $460 million of revenue out of backlog, resulting in a book-to-bill of 59%. The segment ended the quarter with a backlog balance of $969 million, of which approximately 75% is offshore and 87% destined for international markets.

For full-year 2015 the segment generated revenue of $3.4 billion, down 28% in comparison to 2014, as revenue out of backlog declined $501 million or 20%, and non-backlog revenue decreased 37% from 2014 to $1.3 billion. Full-year EBITDA was $507 million or 15.1% of revenue, down 480 basis points from 2014.

Operating profit was $286 million or 8.5% of revenue in comparison to $700 million and 15.1% in 2014, representing decremental leverage of 32.3%. Record or near-record margin in some of our offshore production-related businesses, including flexibles and large-diameter XL Systems conductor pipe connections, were overshadowed by lower year-over-year contributions from our higher-margin intervention and stimulation equipment businesses, given reduced demand for hydraulic stimulation, coiled tubing, and wireline capital equipment and consumables.

With oil at 12-year lows, orders for new capital equipment will remain challenged as we move into the first quarter of 2016. Opportunities that do emerge will face continued pricing pressure. As a result, we anticipate revenues will decrease by approximately 15% and expect revenue out of backlog to fall to the $350 million to $370 million range. We anticipate decremental operating leverage in the 30% to 35% range.

Now let's discuss some additional detail regarding our consolidated financial results. Working down the consolidated statement of income for the fourth quarter of 2015, gross margin declined 210 basis points to 19.1%. SG&A increased $25 million or 7% sequentially, due in large part to increases in bad debt and other year-end-related items, which more than offset overhead reductions.

Despite the slight sequential increase, we reduced SG&A 28% year-over-year, which translated into an annualized cost savings of approximately $600 million. Other items for the quarter equaled $1.8 billion and resulted primarily from goodwill and indefinite lived tangible asset write-downs of $1.6 billion, and restructuring and other charges of $139 million.

EBITDA was $308 million or 11.3% of sales. Net interest expense remain flat for the third quarter, and equity income was a loss of $3 million as demand for OCTGs or green tubing associated with our voestalpine joint venture remains muted, given the low demand for new drillpipe. Other expense for the quarter decreased $3 million sequentially to $17 million, and the effective tax rate for the fourth quarter excluding the impact of other items was 18.7%, affected by a taxable loss in the US and taxable income in foreign jurisdictions among other things.

Net income excluding other items was $85 million or $0.23 per fully diluted share. Working capital excluding cash and debt totaled $5.5 billion at December 31, 2015, down $422 million from the prior quarter. We generated a total of $614 million in cash flow from operations.

After dividend payments of $173 million, investments in our business of $136 million, and FX impact on our cash balances and other items totaling $18 million, we were able to decrease our net debt position by $287 million during the quarter. We ended the quarter with a cash balance of $2.1 billion, $4 billion in debt, and our net debt-to-capitalization was 11.2%. We also have $3.6 billion of undrawn capacity on our revolving credit facility.

Overall, 2015 was a challenging year under the backdrop of market uncertainty, falling energy prices, declining drilling activity, and reduced customer spending. In spite of these conditions, NOV generated $1.3 billion in cash flow from operations, bought back to $2.2 billion in our shares, paid out cash dividends of $710 million to our shareholders, invested over $450 million in organic growth opportunities, and completed seven acquisitions for approximately $85 million -- all while preserving a very strong balance sheet.

2016 will prove to be another challenging year. However, the actions we took during 2015 have positioned us well to weather the storm and capitalize on opportunities that we identified during this down-cycle.

Now let me turn it back to Clay.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Thank you, Jose. I think at this point we're ready to open it up to questions. Kevin?

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) Marshall Adkins, Raymond James.

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**Marshall Adkins** - *Raymond James & Associates, Inc. - Analyst*

Good morning, guys; thanks, Clay. Obviously the industry, these oil prices coming to a screeching halt, I'm curious. How do you balance the massive cost-cutting that you seem to be doing with the ability to meet a recovering market in 2017 and 2018? How much cutting is too much?

I guess the corollary to that is I presume we should expect margins to continue to decrease through the year. At what point in time do we stabilize?

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

That's a great question, Marshall. We were hoping to find stability early 2016, and then oil headed down another $10 and all the E&Ps are coming out with sharply lower CapEx forecasts than we had been planning for. So things remain fluid.

But to your original question, what's the right balance, I've got to tell you one of the really necessary skill sets in oilfield services for those of us that have been in it a while is the ability to flex up sharply when called upon and flex down sharply when called upon.

The good news for NOV is we have a very experienced management team running our business units around the globe. They know how to do this. We've been called on in the past to double and triple and quadruple production over a short period of time, and we successfully navigated that very well and maximized profitability and returns through that.

This is the flip side of that. As orders fall away, as spending comes to a screeching halt, we have to cut costs in lockstep. So I have an abundance of confidence in the capabilities of this team to do both: to respond to this market that is slowing down dramatically, as well as speed up and flex upwards when we're eventually called upon to do that.

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**Marshall Adkins** - *Raymond James & Associates, Inc. - Analyst*

Okay. One unrelated follow-up. Obviously M&A is a focus here with things coming back. That has always been your strength.

How is that market looking? And what geographic areas -- I mean generically; I don't want you to give away anything. But where are you going to focus acquisitions?

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

We're in the enviable position I think of going into such a sharp downturn with a very strong balance sheet. To recap some of the liquidity items that Jose mentioned just a moment ago: a $2.1 billion cash balance, a $5.5 billion of working capital, which has begun liquidating, a $3.6 billion revolving line of credit. So we have a lot of capital flexibility.

We stepped up our efforts, as we talked about on prior calls, to be very vigorous in looking for opportunities to deploy capital in what we see as becoming more of a buyers' market. So we are pretty excited about that and have a lot of flexibility to pursue those.

As you know, we really fundamentally pursue competitive advantage and really fundamentally pursue evolving trends that we see in the oilfield as attractive areas to deploy capital. So specifically, I think in my comments just a month ago I mentioned places like Saudi Arabia, which has committed to increasing activity; they want more local content.

We've talked a lot in the past about areas like the FSU, where we have done more organic investment than acquisitions. But that's an area of interest.

Argentina, the excitement around the Vaca Muerta shale, which was down in the Q4 but longer term we are pretty excited about the potential there -- those are the sorts of things that we look to, to be potentially interesting when it comes to potential M&A targets.

**Marshall Adkins** - *Raymond James & Associates, Inc. - Analyst*

That's helpful. Thanks, guys.

**Operator**

Bill Sanchez, Howard Weil.

**Bill Sanchez** - *Howard Weil Incorporated - Analyst*

Thanks; good morning. Clay, I was curious -- or perhaps Jose, just given what appears to be I guess accelerating deferrals here of Rig Systems orders, I guess both offshore and onshore, you've laid out a revenue range out of backlog for 2016. I know you fell short of your view in 4Q.

Just your level of confidence, Clay, right now given what seems like the further deterioration in terms of recognize that level of backlog revenue, if you will? If you have pretty high confidence on that, and given the cost reductions you've continue to make in Rig Systems, do you have any visibility in terms of when possibly a margin trough level could occur, and at what level that could be?

**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Bill, I'm hesitant to give guidance beyond what we just did, given the situation is pretty fluid, like we mentioned in our comments. We were disappointed in the fourth quarter that revenue out of backlog fell so sharply. It fell about $460 million sequentially out of Rig Systems, a couple of hundred million short of what our expectations were for the fourth quarter.

That's due precisely to what you highlighted with regards to drilling contractors really getting more aggressive on trying to delay acceptance of rigs and pushing back. As you know, the food chain that we work within -- drilling contractors sign up for the construction of these new rigs; the shipyards are their customers; and then we work for the shipyards.

We have been very diligent over the years about demanding very strong contracts, very strong down-payments, progress billings, and the like. But given our focus on monetizing the profit in that backlog, we have slowed our progress on revenue out of backlog to better match payments and to minimize our working capital exposure in those programs.

That's what you saw in the fourth quarter, as we slowed down that revenue recognition out of backlog. But ultimately it's really caused by a lot of drillers trying to delay acceptance of rigs. A couple of situations I think have been made public, and a couple of situations remain a little tense.

Contributing to that was the one shipyard we continued working for in Brazil also slowed in the fourth quarter. I mentioned in my call that we only did $10 million in revenue out of Brazil, and so progress on that particular program slowed as well.

So really across the board things have slowed down. It remains fluid. We have haircut our guidance for revenue out of backlog into Q1 and are working to respond to the market week by week as we see things unfolding.

**Bill Sanchez** - *Howard Weil Incorporated - Analyst*

Okay; thanks for that. Just curious on Rig Aftermarket, Clay. You had a very resilient 4Q on the top line, and I know we've got a pretty significant guide down for 1Q in terms of revenue expectations. Just where do we go from here in that business?

What is a bogey you would tell us to use to think about overall top line as we think 2016 versus 2015 potential declines? Is there something we should be looking at that could help us gauge where that could go?

Is there something in 1Q that would suggest, just given the significant decline, that Q2 actually could stabilize a bit from 1Q? Or how do we think about that?

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**Jose Bayardo** - *National Oilwell Varco, Inc. - SVP, CFO*

I can jump in first, Bill. On the guidance regarding Q1, basically as we talked about on the last conference call and I think it's been mentioned before, Q4 often sees an uptick, a meaningful uptick in service- and repair-related revenue. And we certainly saw that during the quarter, offset by continued decline in orders for higher-margin spare parts.

As we go into Q1 -- essentially during the course of Q4 we saw obviously quick deterioration in a number of the product offerings, spare parts included. So we're expecting a good fall-off not only in that seasonal-associated service and repair work but also a continuing fall-off in spares.

As I mentioned in my commentary, this is a business that we are certainly excited about for the future, as it is tightly tied to the front end of the cycle. And we really do believe that once there are some glimmers of hope out there, things stabilize a little bit, our customers can call bottom and start seeing any sort of optimism to gain some confidence, there will be a rush to deliver new orders, which will result in a nice pickup for us.

The exact timing of that is really difficult to say. We are obviously in an environment where there's very little near-term visibility. But again we are confident about the prospects for that business when things rebound.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Bill, worth pointing out too, you've seen probably three or four steady quarters of drillers beating estimates, land and offshore, and pointing to lower costs. They consistently have lower cost than guidance.

Well, their lower costs equal our Rig Aftermarket revenues. They've slowed down spare parts purchases or, as we talked about before, cannibalizing. They are deferring maintenance wherever possible. I think it's safe to say that no piece of capital equipment across the oilfield globally is being well maintained right now.

What that sets up for the future is when activity does turn, when we find bottom and then it starts to go up, is a lot of work for our Rig Aftermarket folks to repair, to maintain, to replenish spare parts. So the deeper this goes and the longer this goes, I think the sharper the rebound and the more positive the rebound.

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**Bill Sanchez** - *Howard Weil Incorporated - Analyst*

Clay, given that, is there any reason that we should expect discounts to rise further from here?

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Yes. I would say this isn't just Rig Aftermarket, but across the board the level of price pressure on all of our businesses rose to new levels of intensity, if you will. We saw that particularly late in the fourth quarter and certainly continuing into January.

It's almost -- in a lot of ways it almost felt a second shoe dropped in the fourth quarter. I think you had hedges rolling off E&Ps. I think you had some term contracts expiring on rigs out there that were priced in a much higher dayrates. I think you had a new round of fiscal or financial pressure on our customers that came to bear in the fourth quarter and it just -- we hit a whole new level of pain.

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**Bill Sanchez** - *Howard Weil Incorporated - Analyst*

I appreciate the time. I'll turn it back.

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**Operator**

Byron Pope, Tudor, Pickering, Holt.

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**Byron Pope** - *Tudor, Pickering, Holt & Co. Securities - Analyst*

Good morning. Clay, trying to get a feel for the potential structural changes in the businesses as we progress through this downturn. As I think about Wellbore Technologies, it seems as though some of that work might be shifting from sales toward rentals. So as I think about downhole tools, bits, are there any shifts there in terms of how you think about the structural nature of that?

And are you relatively agnostic between sales and rentals within that segment? Just curious as to your thoughts there.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Yes, rentals carry a higher operating margin. As I mentioned in my call, late in the quarter we had a lot of rental equipment return, not just in general tools but in other rental businesses within Wellbore Technologies.

With respect to our Drilling & Intervention business we've seen a steady progression in our business over the last few years of working more closely with the E&Ps. Across North America is mostly what I'm talking about, but also elsewhere around the globe, where they're more interested in being involved in the selection of the bottomhole assemblies that go into their complex directional drilling.

So our mix of customers, let's say, has shifted to work more directly with the exploration and production companies to help them optimize their well pads. But that has been sort of a steady progression. I'm not sure we have seen a big change here lately that changes the trend of that.

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**Byron Pope** - *Tudor, Pickering, Holt & Co. Securities - Analyst*

Okay. Then just a question as it relates to Completion & Production Solutions, given that you touch essentially all the equipment on the well side as it relates to frac spreads. I guess I can infer this from the Q4 book-to-bill ratio, but it certainly feels like the anecdotal data points about chewing up frac spreads, it feels like you guys are seeing it with regard to within your orders; but at some point that turns.

So I'm just curious as to the anecdotal data points that you all are seeing with regard to, at some point, there's a call on the equipment on the frac side.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Yes, I am not sure I can tell you the day or wrap numbers around this. But I would tell you anecdotally nobody is really maintaining their fleets very well. In fact as I said I think in my comments, there's a lot of equipment auctions underway where you can pick up fleets at pennies on the dollar, and that becomes a source of spare parts. And that's how it affects our business: rather than buying consumables, fluid, and things from us those are being purchased at auction.

So I think the cannibalization of the existing fleet, the erosion of the equipment overhang is well underway in that space. And when it does turn again, NOV is going to be called upon to step up and boost production to satisfy future demand.

**Byron Pope** - *Tudor, Pickering, Holt & Co. Securities - Analyst*

Thanks for that; I appreciate it.

**Operator**

David Anderson, Barclays.

**David Anderson** - *Barclays Capital - Analyst*

Clay, your balance sheet remains one of the best in the sector with a really healthy cash position, which really stands out in this downturn. Can you talk a bit about -- obviously you are navigating through a pretty severe downturn, one of the worst we've seen. But can you talk about your priorities in terms of that?

Maybe remind us in terms of capital allocation; and also remind us what types of leverage ratios you are comfortable with getting up to.

**Jose Bayardo** - *National Oilwell Varco, Inc. - SVP, CFO*

David, it's Jose. I will jump in on that one. Yes, we are obviously very pleased to have the balance sheet that we have today. As Clay mentioned earlier, having optionality in the capital structure in this current environment is becoming more and more valuable day by day. We're also seeing a narrowing of the bid-and-ask spreads on some compelling acquisition opportunities coming forward.

So as we think about capital allocation, for us it's really all about ultimately driving maximum value to the shareholders. Obviously, historically organic investment has been a very good use of capital; but in the current environment when we're overcapacitized, M&A tends to be front and center in our minds. Everything is going to be opportunity-specific, outlook-dependent, in terms of how we think about using the capital structure related to M&A and our other capital requirements.

So I don't want to get into any sort of specifics on ratios, etc. But I think the Company has historically maintained a fairly conservative balance sheet; we intend to keep it that way.

But again, it really depends on the specific opportunity, cash flow it brings into the organization, as well as exactly where we feel we are in the cycle and outlook for the combined businesses.

**David Anderson** - *Barclays Capital - Analyst*

Okay; thanks, Jose. I heard all your guidance and we have to digest it all for the first quarter. But as I think about decrementals for the full year, if I use 2015 as a starting point, is there any guide you can help us out with, to say maybe which segments may be a little better, a little worse?

Obviously with less revenue coming out of backlog in Rig Systems, I'd have to think maybe decrementals looking worse. On the other hand, C&P and Wellbore I think have a pretty high level of amortization in there; so maybe that gets a little bit better.

Can you just help us out with some of the trends that you are thinking from a full-year basis on the decremental side?

**Jose Bayardo** - *National Oilwell Varco, Inc. - SVP, CFO*

This is Jose. It's a really challenging question, David. I think we gave -- there are ebbs and flows. Every business has its own unique components, and things don't always cycle perfectly.

As an example, last quarter we saw decrementals that were an 18%, 20% range. This quarter we're at 35%. So the cost and revenues unfortunately don't always go hand-in-hand.

But I think we gave some pretty detailed thoughts that will take some time I'm sure to digest regarding first quarter. And beyond that visibility really is pretty murky, so I hesitate to give any specifics on that.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Yes. I think I'd add, it gets a little tougher from here. As backlog dwindles down, absorption becomes a little more challenging, and we are managing cost in response to that as closely as we can. But our backlog-driven businesses that are mostly manufacturing, certainly their decrementals will be affected by that picture.

On the other hand we do have a number of businesses that are exposed directly to the drillbit. So you finally find bottom on rig count, and maybe have just a little bit of help on rig count, we will immediately for instance get wellsite services jobs. We will immediately see a turnaround on our downhole tools and bits business. We will immediately see rig instrumentation work pick up.

And those are three rental businesses that I mentioned earlier that come at high variable margins. So just a little bit of activity help I think would help put up much better decrementals for Wellbore Technologies.

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**David Anderson** - *Barclays Capital - Analyst*

Okay. Thanks, Clay.

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**Operator**

James West, Evercore ISI.

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**James West** - *Evercore ISI - Analyst*

Good morning, guys. Clay, as you think about -- just another question on M&A, I guess the obligatory M&A question for Clay or Jose. Are there certain areas or product lines that you are looking at maybe to diversify away from your core competencies, where you dominate businesses, so you can become a more full-cycle type player?

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Yes, James, as you know, we operate through 15 business units. Two of those 15 build new rigs, one for land, one for shore. But 13 of our business units do other things. So we do a lot across the oilfield, probably more than we get credit for, and already have more diverse exposure.

What I would say is the thinking here with regards to M&A and corporate development, which I think the Company has a lot of that in its DNA, really is focused on identifying opportunities to make money. What are the trends in the oilfield? Where can we drive better industry structure? Where can we offer a better package of products and services for our customers?

It's really a little more granular than trying to globally arrive at some sort of diversified portfolio mix. I think we've ended up at a very diversified portfolio mix already; but at the end of the day this business is about making money, right? So where can we put capital in, into an opportunity, get that capital back as quickly as possible? I.e. get a quick payback and a good return and really do something different to drive higher capital returns in an industry where we have all spent our careers and I think have a lot of insight into, which is global oilfield services at large.

So that's kind of our approach to M&A and looking for those sorts of opportunities. Honestly, Jose and Lauren, I wish we could tell you more this morning; but as you understand, these things are never a deal until they're a deal.

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**James West** - *Evercore ISI - Analyst*

Of course, yes.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

We are enthusiastic about what we're starting to see out there. And again, great to have a lot of balance sheet flexibility and capacity, and I think there's a lot of optionality right now embedded in NOV.

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**James West** - *Evercore ISI - Analyst*

Has there been a significant change in the sellers' asking prices here as we've taken this third dip down in oil prices?

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Yes, there's a lot of shellshock out there. We're not the only ones seeing this.

I would tell you on down-cycles, having been through a few, it's really hard to get the bid and the ask to converge on the way down. Because the seller is looking backwards and seeing: Hey, a quarter ago, two quarters ago, a year ago we did much better financially.

And as a buyer, you're looking forward into a deteriorating P&L, wondering: Where is bottom? And trying to discount appropriately.

So the bid and the ask tend to widen early in a down-cycle. I think if we're -- I'm not calling bottom; I don't know if we're there yet. But as you start to get close to bottom, time passes, reality sets in, folks recognize this may go -- be lower for longer, and I think that's where the industry is coming to now.

I think it brings a much more sober, realistic outlook on the part of potential sellers. And I think we're starting to approach that kind of world.

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**James West** - *Evercore ISI - Analyst*

Good, okay. We'll look forward to your next move. Thanks, Clay.

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**Operator**

Ladies and gentlemen, this does conclude today's question-and-answer session. I would now like to turn the call back over to Mr. Williams for closing remarks.

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**Clay Williams** - *National Oilwell Varco, Inc. - Chairman, President, CEO*

Thank you very much, Kevin. I appreciate everyone joining us this morning, and we look forward to sharing our first-quarter results with you in April. Thank you.

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**Operator**

Ladies and gentlemen, this does conclude today's presentation. You may now disconnect and have a wonderful day.

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