OVERVIEW:

NOV reported 3Q15 revenues of $3.3b, operating profit of $346m and GAAP fully diluted EPS (including certain items) of $0.41.
CORPORATE PARTICIPANTS
Loren Singletary National Oilwell Varco - VP IR
Clay Williams National Oilwell Varco - CEO
Jose Bayardo National Oilwell Varco - CFO and SVP

CONFERENCE CALL PARTICIPANTS
David Anderson Barclays - Analyst
Jim Crandell Cowen Securities - Analyst
Bill Herbert Simmons & Company - Analyst
Jeff Tillery Tudor, Pickering, Holt - Analyst
Jud Bailey Wells Fargo - Analyst
Marshall Adkins Raymond James - Analyst
Bill Sanchez Howard Weil - Analyst

PRESENTATION
Operator
Good morning and welcome to the National Oilwell Varco earnings 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.

Loren Singletary - National Oilwell Varco - VP IR
Thank you, Kevin, and welcome everyone to the National Oilwell Varco third-quarter 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 third quarter ended September 30, 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 upon 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 a more detailed discussion 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.
Clay Williams - National Oilwell Varco - CEO

Thank you, Loren. National Oilwell Varco continued to face a very challenging market during the third quarter. The Company reported GAAP earnings of $0.41 per fully diluted share including restructuring, asset impairments, facility closure costs and other items of $112 million pretax or $0.20 per share after-tax. Excluding these, earnings were $0.61 per fully diluted share, down 21% from the second quarter of 2015 and down 62% from the third quarter of 2014, excluding restructuring and other items from all periods.

Third-quarter 2015 revenues were $3.3 billion, down 15% from the second-quarter 2015. Operating profit for the quarter was $346 million or 10.5% of sales, and EBITDA was $511 million or 15.5% of sales, excluding restructuring and other items from both. Decremental operating leverage was 18% from the second quarter to the third, as cost reductions across the organization helped minimize the margin impact from lower sequential volumes.

A second major decline in oil prices from the high $50 range back into the low to mid $40 range since June has increased financial stress and led to a second round of rig activity reductions, sending the US rig count down by almost 60% since late 2014 peaks. We expect to see further activity reductions and pricing pressures continuing into the fourth quarter.

Visibility is limited, but we believe most producers will further reduce their 2016 CapEx plans after cutting spending significantly in 2015. The industry has not seen two years of declining CapEx since the 1980s, signaling the severity of the downturn we find ourselves in.

We believe many, if not most, North American producers and OPEC countries are producing existing fields close to maximum levels, trying to offset lower revenues due to oil price declines with higher volumes, while sharply reducing drilling activity. OPEC and non-OPEC production are up year-over-year.

This is not sustainable. Production will begin to decline naturally as it has begun to in the United States, and therein lies the seeds for a recovery. However, with swollen inventories moderating demand growth with economic weakness in Asia and elsewhere around the globe, and an uncertain trajectory for incremental oil exports from Iran, we don't expect a recovery anytime soon.

Nevertheless, it will come, and our plan is to manage what we can, namely costs, through the downturn while continuing to position and strengthen our franchise for the inevitable upturn. We expect to accomplish this through a combination of organic investment in new technologies and capabilities, as well as extraordinary acquisition opportunities that we expect to emerge.

Through the first part of this downturn we deployed $3 billion of capital into our share repurchase program, retiring 1 out of 8 shares over the past year, while maintaining capital flexibility through our $4.5 billion revolving credit facility. As the downturn has lengthened, we believe values of potential target companies will become more and more compelling.

Thus far it has been challenging to bring the bid and the ask on potential acquisitions into alignment, but we remain patient and disciplined in these discussions. As we move into 2016, we believe sellers are likely to reduce their expectations and better capital returns on M&A will follow.

Consequently, our capital deployment strategy is shifting from share buybacks to an external focus on potential acquisitions. This is a sound capital deployment strategy that we will continue to execute in a disciplined way. NOV closed small four acquisitions during the third quarter of 2015. The strategic goal of these and other transactions will continue to focus on cultivating market leadership in selected subsectors within oilfield services and manufacturing.

As we have said many times before, market leadership yields competitive advantage, economies of scale, purchasing leverage; the ability to leverage R&D and introduce new products through a larger revenue base; the more rapid accumulation of experience within a subsector; our global aftermarket support network, etc. Our market positions make us a trusted, efficient, low risk supplier to our customers.

These are the types of opportunities that we look for, and the businesses we have built employing this strategy are leaders in their respective fields. In short, NOV represents a portfolio of market leaders with the deepest experience and the most expertise.
Within these businesses, we have assembled discrete packages of equipment and services to drive higher efficiency in ways that our customers really want and in ways that really improve their businesses. This means we take a view on where the logical boundaries of these packaged offerings should lie.

Our acquisitions are of enterprises where NOV can be a better owner, to accelerate growth, drive efficiency and fully unlock their potential to create value for our customers and our shareholders.

This view on product groupings or package boundaries rest on questions like, “what products have complex technical interfaces that are difficult for our customers to manage; interfaces where a single vendor can and should undertake the interface management challenge?” “What proprietary technology can we build a logical package of products and services around?” “What trends do we see amongst customers as they all seek to reduce costs and risk around their operations?”

The development of our corporate strategies within our business units guides both our M&A strategy as well as our research and development strategy. Both work in concert. In the near term, we will continue to focus on managing costs to the marketplace, and our shallow decremental margins speak to the great job NOV’s business unit managers have done in this effort.

SG&A is down 34% year-over-year and down 15% sequentially. Rig Systems posted decremental leverage of 28% on a 23% sequential sales decline. Rig Aftermarket held operating profit flat, despite unexpectedly high 13% revenue decline. Wellbore technologies held decrements to 21%, despite a 13% sequential sales decline. And completion and production solutions held decrements to 24% in the face of a 9% sales decline.

I am extraordinarily grateful to these business leaders who are skillfully reducing our capacity, managing costs, and leading our core team through this challenging time. They are providing their teams with the vision of better days ahead to make sure that our folks see the prosperity that will follow for NOV. That's critical in a downturn.

We are fundamentally a service business, even in our manufacturing units. And ensuring our workforce continues with our long tradition of taking care of our customers and not getting distracted during stormy weather is critical. I want all of our employees to know that I am very proud of what you are doing.

Difficult market conditions will persist for the foreseeable future. We supply a highly capital-intensive industry and have benefited from decade-plus period of retooling with improved levels of technology and automation. But the industrial transformation is far from over. Our view is that we are currently in a cyclical pause. Recent oversupply of oil exacerbated by weak economic demand growth has demonstrated the power of newer, more capable rigs and completion equipment and techniques.

During such a cyclical pause, our biggest competitor becomes the overhang of products and consumables and equipment that our customers cannibalize extremely effectively in their Darwinian quest to preserve cash. The idle rigs and pressure pumping fleets and wireline units and a myriad of other units we sell are being systematically stripped of spare parts and components to keep the much smaller fleet of units that remain under contract working.

This remains a highly capital equipment consumptive industry. The life expectancy of mechanical equipment is tied to the footage it drills or the volume of profit it pumps. The ability of the industry to increase borehole created per year or stages fracked per year means that the physical consumption of mechanical equipment per year has also risen sharply, probably linearly.

NOV will be called upon again to resume capitalizing the critical fleets of equipment required to supply a growing population with rising energy needs once we pass through the cyclical downturn. And as I said, we will emerge better and stronger.

Our Completion and Production Solutions segment held operating margins of nearly 8%, despite a 9% sequential sales decline. The group benefited from strong performance from our floating production unit and our flexible subsea pipe unit in the quarter. We also posted good orders in the quarter, helped by a large deepwater flexible pipe order arising from our proprietary heated pipe solution. This resulted in an ending backlog level of $1.2 billion.
We expect orders to decline in the fourth quarter as the market faces an overhang of fracture stimulation equipment across North America and as operators seem in no hurry to sanction many deepwater developments at the moment.

Nevertheless, we are engaged in several FEED studies around the globe and meeting with a lot of operator interest in standardized, more industrial efficient solutions to improve deepwater development economics. We are encouraged by a handful of public statements from major oil companies on meaningful double-digit cost reductions on deepwater projects, driven by the combination of design simplification, supplier participation in design, and supply chain deflation. "Fit for purpose solutions" rather than, "perfect", solutions.

We continue to develop new products within the group in areas like composites, spoolable piping systems for corrosive produced fluids. In fact, we shipped our first string of spoolable composite pipe into Saudi Arabia this quarter, and we expect to install our first string of our proprietary Smart Pipe for shallow well dewatering in Australia in the fourth quarter.

Nevertheless, with 30% plus declines in prices for steel pipe has made steel pipe more competitive for our composite pipe unit. However, as fields mature and water cuts rise, we expect our customers to gravitate to our corrosion proof solutions.

We were also pleased to see higher sales of coiled tubing in the quarter on gains with key accounts and our new service center in the Northeast pulling sales through.

Our Wellbore Technologies group is driven by rig activity, and we are now facing a second rising wave of price pressure across all our products and services as rig activity declines.

The group saw demand for almost all of its products and services decline except for our IntelliServ wired drill pipe technology, which has seen growing interest from operators in conjunction with our automated drilling solutions. This technology enables microsecond data from downhole sensors to control rig machinery much more effectively than human drillers, and increases rates of penetration significantly. We have several programs scheduled to spud with this later this year and into 2016, and are excited about the transformative capabilities of high-speed data from the bottom of the well.

New Tectonic bit technologies we’ve introduced are helping drive market share gains, and we are pressing forward with new products in managed pressure drilling and wide-catch fishing tool technologies. The operation of our test rig is helping accelerate time to market for many new products and new condition monitoring technologies.

We’ve seen our customers aggressively reposition and utilize their own fleets of equipment wherever possible to preserve cash, and our mix of drilling tools shift from sales to rentals as a result. Demand for drill pipe has been very weak, as drillers cannibalize streams from idle rigs to support working rigs, but we have reduced capacity to match the current market. Our Tuboscope unit has held up reasonably well as its work has shifted from drill pipe to line pipe and tubing.

The Rig Aftermarket segment declined 13% sequentially, as more and more rigs went idle and became fresh sources of spare parts for their owners, driving sales of spare parts and manifolds lower. Nevertheless, the group held operating profit flat, and operating margins increased 350 basis points.

We saw our count of SPS projects on offshore rigs flatten this quarter after increases through the first half, as many planned-for reactivation/recertification programs are being shelved by drillers due to growing concerns about the near-term outlook for offshore rig demand. Nevertheless, SPS activity is up year-over-year, and we are also seeing rising inquiries around maintenance services we can provide on stacked rigs.

Rig Systems demand remains weak overall, and we are downsizing to address this reality. We still see certain markets moving into the 21st Century to employ proven technologies - Argentina, the CIS, the Middle East - and we are aggressively pursuing these opportunities. We also know many North American drillers continue to high-grade their fleets to AC Tier 1 capabilities once prosperity returns.
Orders in Rig Systems included land rigs for international markets and two jackup packages and were up modestly from the second quarter, resulting in an ending backlog of $8 billion for the group. We expect orders to remain low through 2016 when scheduled outflows from backlog will be in the $2.4 billion range. Those are orders that are scheduled right now in the backlog.

In certain instances, we continue to work with customers to systematically delayed deliveries of rigs, which is improving our project margins as we were able to reduce overtime and source components more efficiently. Brazilian rigs totaled $3 billion of the $8 billion in our September 30 backlog, and accounted for only $53 million of revenues during the third quarter.

As we reported previously, we have suspended or delayed work on certain of these 22 rigs. Our shipyard customers are continuing to work with their customer, Sete, to address overdue funding needs and future funding to move the projects forward. In the meantime, we are reducing costs in-country.

Within Rig Systems, third-quarter revenues associated with new offshore rigs, both floaters and jackups, totaled $860 million or 26% of consolidated revenues during the third quarter. While we expect some new specialized offshore rigs to be built by the industry over the next couple of years and we are developing new designs and capabilities around these, we do not expect the level of building that we have seen over the past decade to resume for quite a while.

Like many, we are waiting an increase in scrapping of older units across the fleet, which seems inevitable at this point.

Finally, I’m delighted to welcome our new Chief Financial officer, Jose Bayardo, to our team. Many of you know Jose from his time at Complete Production Services and more recently at Continental Resources. Let me turn it over to Jose to discuss our third-quarter performance and outlook in more detail. Jose.

Jose Bayardo - National Oilwell Varco - CFO and SVP

Thank you, Clay. It’s great to be here with everyone this morning. Our Rig Systems segment generated revenue of $1.5 billion, down 23% from the $1.9 billion earned last quarter, and down 44% from the $2.7 billion all-time high revenue generated from the segment in the third quarter of 2014.

Revenue out of backlog was $1.3 billion, down 24% sequentially, in line with total revenue for the segment. Revenues declined as we continued to adjust to our project schedules and manage output to navigate effectively through fewer orders of lower backlog and customer requested delivery delays on certain projects. For Q3, the split between offshore and land related revenue was 78% and 22% respectively.

Operating profit as adjusted per the reconciliations in our earnings release for the Rig Systems segment was $275 million, yielding operating margins of 18.4%, down 210 basis points from Q2. Decremental operating profit margins were 27.6% sequentially and 22% year-over-year. Low decremental margins demonstrate the effectiveness of our efforts to improve process efficiencies and resize the business to anticipated production levels.

EBITDA was $300 million or 20.1% of sales, and EBITDA margins decreased 160 basis points compared to the second quarter of 2015. During the third quarter, we received $367 million in new orders, resulting in a book to bill of 28%. Orders for the quarter were fairly evenly weighted across offshore and land, and included two high-spec jackup drilling equipment packages and two 3000 HP land rigs for the Middle East.

FX adjustments of $77 million resulted in quarter ending backlog of $8 billion, down 11% sequentially, of which approximately 90% is offshore and 93% is destined for international markets. We expect orders to remain subdued as activity continues to decline on land and offshore, and uncertainty regarding the timing of a recovery persists. We are seeing some demand for a few jackups from NOC’s. And while opportunities for floaters are generally scarce, meaningful conversations on 20,000K PSI floaters and other application-specific rigs continue.

As we move into the fourth quarter of 2015, we expect total Rig Systems revenue to decline approximately 10% into the $1.3 billion range, and revenue out of backlog to decrease to about $1.1 billion as we see reductions in new order activity work through existing projects and work with customers to accommodate certain requests to extend delivery dates.
Resizing the business to reflect market activity remains critical to margin preservation, and we will continue to focus on cost-reduction opportunities including process efficiencies, vendor pricing, and facility consolidations to better align our resources with anticipated production levels.

That said, cost control will not be enough to fully offset the impact of lower volumes, and we anticipate segment margins will decline into the mid-teens during the fourth quarter.

Despite the current challenges and customer capital constraints, longer-term fundamentals remain solid for our Rig Systems segment. Land rig customers continue to show a strong preference for rigs which utilize the latest technologies to most efficiently and precisely drill longer lateral wells from multi-well pads. And offshore exploration and production companies are committed to utilizing new rigs and equipment that enhance their ability to more safely and economically access hydrocarbons in increasingly challenging environments.

NOV will continue to make long-term investments in the development of the best technological solutions that provide industry-leading quality and reliability to most effectively address the needs of our customers.

Our Rig Aftermarket segment generated revenues of $570 million during the third quarter of 2015, down 13% sequentially and down 32% year-over-year, driven by lower spare parts sales as drilling contractors continue to focus on reducing their expenditures amid activity declines. The reduction in spare parts sales was partially offset by a slight increase in service-related work.

Despite the low teens revenue decline, the segment maintained flat operating profit at $146 million, resulting in operating margins of 25.6%, a 350 basis point improvement sequentially due to effective cost controls and inventory charges incurred in the second quarter, which did not repeat.

EBITDA was $154 million or 27% of sales. Consistent with second quarter, land-related sales were approximately 22% of total segment revenues. Near-term we expect the segment will continue to ebb and flow as our customers try to identify the bottom of this current cycle. As we move into the fourth quarter, we believe the pickup in service and repair revenue we have seen the last quarter of prior years will be much more modest this year, as uncertainty leads to more cautionary spending by our customers.

However, we do anticipate Rig Aftermarket revenues will be up slightly in comparison to Q3.

Operating margins are expected to be similar to the third quarter, as increases resulting from incremental revenues will be offset by product mix.

In our rig businesses we distinguish ourselves through service after the sale. We are committed to the success of our customers and driven by a sense of urgency in maintaining and supporting our equipment and technology in the field. The capabilities of our global service network our unrivaled.

The mid-to long-term outlook for the Rig Aftermarket segment remains bright, and we anticipate sales will begin to improve as soon as customers work through their limited existing inventories of spare parts. We also anticipate the improvement will accelerate once overall industry activity levels begin to increase, causing a rush to return sub-optimally maintained, stacked and partially cannibalized rigs to proper operating conditions.

For the third quarter of 2015, the Wellbore Technology segment generated revenues of $834 million, down 13% sequentially and down 43% compared to the third quarter of 2014. Almost all business units within the segment were impacted by the overall decrease in drilling activity levels, with production-oriented businesses realizing slightly better performance.

Customer interest continues to grow in our technologically advanced products and services, which reduce drill times and lower operating costs, such as our Tectonic drill bits, ConneXion drilling performance software, and our SoftSpeed stick slip prevention services.

One of our Tectonic bits was recently paired with our HellCat motor and Agitator drill system to drill a 2.5 mile long lateral in the Bakken, in what we and our customer believed to be a record time of 4.5 days.
Operating profit for the third quarter was $22 million or 2.6% of sales, down 230 basis points from last quarter. Sequential decrements were limited to 20.5%, as we continue to focus on expense reduction and process efficiencies to develop a leaner cost structure for the business. Q3 EBITDA was $119 million or 14.3% of revenue.

Looking into the fourth quarter of 2015, many of our North American customers are bracing for a further falloff in activity during what they anticipate will be a prolonged year-end holiday slowdown. Fewer rigs running will result in weaker demand for Wellbore Technologies products and services, and we are seeing a new wave of pricing pressure which may offset our cost reduction efforts. As such, we believe revenues in our Wellbore Technologies segment will decline in the mid-to-high single percentage range with incremental margins in the mid-20s.

Longer-term we anticipate continued market share gains from our advanced products and services designed to enable the drilling of more complex, productive and safer wells at a faster rate, thereby enhancing the economics. We believe our strategy to help our customers achieve their objectives is succeeding, and we will continue to invest in solutions our customers value today and which will further enhance our position for the eventual recovery.

Our Completion and Production Solutions segment generated revenues of $798 million for the third-quarter 2015, down 9% sequentially and 33% compared to the third quarter of 2014. Revenues declined across most businesses on lower backlogs and customers delaying pickup of finished work, with some offset coming from higher sales of floating production related equipment and flexible pipe.

We also saw increased coiled tubing sales as our investments in placing tubing centers closer to our customers' operations enable us to provide better service.

Operating profit for the segment was $63 million, resulting in operating margins of 7.9%, down 140 basis points sequentially and 750 basis points year-over-year. Sequential decrements were 24%, and third-quarter EBITDA for the segment was $170 million or 14.7% of sales.

Operating margins were negatively impacted by volume pricing pressure and product mix, but most cost-control initiatives helped to offset some of the margin decline, resulting in improved decrements versus prior quarters.

Turning to our capital equipment orders and resulting backlog for Completion and Production Solutions, the third quarter saw a much improved order intake of $467 million. That's an increase of $212 million or 83% sequentially, led by improved bookings for floating production related equipment and fiberglass pipe as well as a large order for subsea flexible pipe.

We recognized $472 million of revenue out of backlog, resulting in a book to bill of 99%. Of the $1.2 billion backlog at quarter end, approximately 76% is offshore and 86% is international.

As we move into the fourth quarter, we anticipate demand for new pressure pumping and coiled tubing units, especially in North America, will remain low. And while customer interest remains elevated for NOV’s more cost effective solutions in the FPSO space, near-term we anticipate a general slowing in prospect development, due to the current commodity price environment.

We believe revenues will decrease by a mid-single digit percentage, and expect revenue out of backlog to remain in the $450 million to $470 million range. Margins should move down slightly on lower volumes.

Now let's discuss some additional detail regarding our consolidated financial statements. Working down the consolidated statement of income for the third quarter, gross margin declined 110 basis points to 21.2%. SG&A decreased 15% or $63 million sequentially due to cost reductions, and was 10.7% of revenue.

Other items of $112 million for the quarter resulted primarily from a $55 million pretax intangible asset impairment, as well as a $57 million pretax charges associated with severance, facility closures, and other costs.
Equity income fell to breakeven as demand for OCTGs or green tube associated with our Voest Alpine joint venture remains muted, given the low demand for new drill pipe.

Other expense for the quarter decreased $10 million sequentially to $20 million, due primarily to a reduction in foreign exchange related losses relative to the second quarter of 2015.

The effective tax rate for the third quarter was 18.8%, down from the 26.9% rate posted in the second quarter of 2015. Excluding the impact of $112 million in other items, the effective tax rate would have been approximately 24%, reflective of the continuing high mix of income from low rate foreign jurisdictions.

EBITDA for the third quarter excluding other items was $511 million or 15.5% of sales.

Turning to the balance sheet, working capital excluding cash and debt totaled $5.9 billion at September 30, 2015, down $206 million or 3% sequentially. The decrease in working capital was primarily the result of a $222 million reduction in inventory levels, a $151 million reduction in accounts receivable, an $88 million increase in accrued taxes, and a $10 million decrease in customer financings, which is the net of prepayments and billings in excess of costs against costs in excess of billings.

The reductions in working capital were partially offset by decreases in accrued liabilities and accounts payable. While we are pleased to see total working capital decrease and we anticipate the pace of cash flow generation from working capital will increase as we move forward, we continue to manage several items impacting our efforts to reduce the capital employed in our business, including insourcing of machining hours which increases our inventory by bringing in raw materials which otherwise would have been held by third-party vendors; customers looking to delay equipment deliveries and extend payment terms; and our Rig Systems backlog and its associated customer financings.

Regarding the financings as projects approach their completion, we do anticipate the spread between prepayments and costs in excess of billings to narrow, further contributing to a future reduction in working capital.

For the quarter the Company generated $410 million in cash flow from operations. Offsetting this cash flow were share repurchases of $444 million, dividend payments of $174 million, investments in our business of $124 million, and FX impact on our cash balances and other items totaling $44 million.

The net impact of our cash flow for the quarter was a $376 million increase in net debt. However, total debt decreased $322 million as we successfully repatriated $1.1 billion to the US. We ended the quarter with a cash balance of $1.8 billion, $4 billion in debt, and our net to debt capitalization was 11.8%.

While we remain focused on managing costs and improving efficiencies, we believe the strength of our enterprise uniquely positions NOV to capitalize on compelling acquisition opportunities that will emerge in this downturn, and to continue investing in the development of technologies that will help our customers improve their economics.

With that, we’d like to turn it open to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) David Anderson, Barclays.
David Anderson - Barclays - Analyst

So, Clay, I was struck by the commentary; you said extraordinary opportunities arising from this downturn. Can you help me understand a little bit of kind of how you are thinking about this? You have a lot of product lines out there. Are you talking about adding new product lines, or do they expand out the current ones?

And I guess I’m also kind of wondering, are you willing to look outside the traditional upstream oil and gas market, or do you see other opportunities potentially emerging, say maybe midstream, downstream, maybe even industrials?

Clay Williams - National Oilwell Varco - CEO

David, I’m going to stay away from getting too specific, but I will tell you we take a pretty broad view and look both at enhancing our existing product lines. You know we report four reporting segments, and those are comprised really of 15 business units that make this up. And I would say in all 15, we continually look for opportunities to enhance and expand.

And then beyond that, the great thing about oilfield services is it’s composed of dozens and dozens and dozens of interesting subsectors. So we are continually looking across those for opportunities to deploy capital and develop our business.

We also have some great industrial product lines in businesses and markets that we serve. Usually those are characterized by some sort of overlapping competence that we have in the oilfield. We make a product, for instance, that the oilfield needs that also goes into other industrial segments. So usually there is some sort of overlap or synergy that’s embedded in those sort of opportunities.

But yes, we are taking a very expansive view. The reason for the comments obviously is a lot of parts of — well, really all parts of oilfield services and manufacturing under stress in the current environment and the landscape shifting. So at the low points in the cycles where we frequently see the best opportunities.

And as you know, we have a long history of executing acquisitions, and both National Oilwell and Varco came out of private equity roots. And through the years between our two organizations — we came together about 10 years ago — we’ve done probably in excess of 300 transactions. So this is becoming a buyers’ market, and we are pretty excited about that.

David Anderson - Barclays - Analyst

Now, Clay, you mentioned three smaller acquisitions during the quarter. Can you just help us understand a little bit kind of where those fit in? Obviously, you didn’t announce any numbers here behind it, but just maybe kind of more qualitatively of what these businesses are?

Clay Williams - National Oilwell Varco - CEO

Yes, actually it was four, David, and they are between our Wellbore Technologies and our Completion and Production Solutions; both those segments picked up smaller deals. And these are the sort of bolt-on things that we do continuously here. I think in the last quarter, I mentioned we had a half dozen or so letters of intent out there, and this one is the completion of four of those. And we still have a number of smaller things that we are looking at. But as we kind of move into this kind of market, we are looking at some larger things and really looking across the board.

David Anderson - Barclays - Analyst

Great. And I guess a follow-up would be on your costs initiatives and some of the internal stuff that you are doing there. You’ve talked in the past about pulling in-house some of — I think even Jose mentioned this — about pulling some of your outsource manufacturing. I think you have said something like 52% was outsourced before.
Can you tell me where you stand on that front? And I guess also secondarily, we are hearing from some of the subsea guys that forging costs aren’t really coming down because of strengths in other markets. Are you faced with that same issue that maybe you can’t squeeze as much out of your suppliers as you were hoping to?

**Clay Williams - National Oilwell Varco - CEO**

Yes, we do have sort of an outsourcing model. Basically, we recognize all of the things that we manufacture serve cyclical industries, so demand rises and falls. So we try to avoid scaling up to internally manage peak demand. And as -- I would say over the past few years, a number of our business units have done more outsourcing.

So as you go the other way as things sort of cycle down, we really try to bring more in-house, keep our core teams busy. And we are doing that, moving machining hours to our plants. As Jose mentioned, it takes a little more inventory to accomplish.

On the steel cost front, it varies by product line. We've seen dramatic deflation in pipe prices, for instance. On castings and forgings, yes, I think we are seeing the same thing others are, which is a little deflation. But really across the entire supplier network, we are pressing for lower pricing and continually trying to become more efficient.

**David Anderson - Barclays - Analyst**

Thanks, Clay.

**Operator**

Jim Crandell, Cowen.

**Jim Crandell - Cowen Securities - Analyst**

Good morning and congratulations, Jose, on joining NOV.

**Jose Bayardo - National Oilwell Varco - CFO and SVP**

Thank you. It’s great to be here.

**Jim Crandell - Cowen Securities - Analyst**

Clay, how do you see your non-Rig Systems business trending in the first half of the year if oil prices remain where they are today?

**Clay Williams - National Oilwell Varco - CEO**

Yes. Jim, we are, like a lot of companies, moving into the fourth quarter we are doing more detailed planning around what 2016 is going to look like. And we always reach out to our customers to kind of get their guidance. And what we are finding is they don’t know what they are going to spend. So generally, though, I think the first part of 2016 is going to continue to be really challenging.

And as I said in my prepared remarks, our expectation is activity is going to trend lower. I think like everybody in this industry, though, we remain hopeful we will get a little bit of commodity price help and relief. And then maybe in the second half of the year, we start to see maybe some activity pick up a little bit. But I don’t have a lot of data to point to as to why that would happen.
Jose and I were chatting earlier and, Jose, you mentioned the fact that producers come under a lot of pressure when they start facing production declines. So I think there will be an impetus at least across North America to get back to drilling as soon as they can.

Of course, that will take a while. A lot of the equipment that’s out there has been depleted of spare parts and cannibalized, and so a little bit of uptick in activity is going to take a lot of work from NOV. So we are looking forward to that time.

**Jim Crandell - Cowen Securities - Analyst**

Okay. Follow-up, Clay, is in your Wellbore Technologies group, is Grant Prideco falling off meaningfully more steeply than your other businesses there? And is that a business with just because of the nature and its exposure to new rigs a business that’s going to continue to or will fall off at a greater than average rate?

**Clay Williams - National Oilwell Varco - CEO**

Yes, that business is certainly under a lot of pressure, and the management team there has done a great job scaling back to match the market and holding as best they can. But yes, that’s our business that makes drill pipe for the rest of you. And what we see is particularly onshore operators moving drill pipe off of idled rigs and moving that onto the rigs that remain working.

It’s a little more challenging offshore. It’s expensive to demobilize a string of pipe off of an offshore rig, so a little less impacted from cannibalization there. But certainly onshore, that’s impacted them.

Good news is, is that their mix has improved. We are the market leader in terms of providing premium connections of high tensile strength pipe; set new records in places like Sakhalin Island in terms of extended reach drilling out 7, 8 miles. And really, broadly speaking, you step back and view the demand for drill pipe, a lot of technology in drill pipe. And drill pipe is consumed at a much faster rate when it’s used to drill these horizontal wells, these long laterals that are really making the shale plays go.

So, yes, we are in this period when demand is down. The team has done a great job there managing through it. But once we recover, I think the shale phenomenon is going to continue to consume more and more drill pipe that we make.

**Jim Crandell - Cowen Securities - Analyst**

Great, okay. Thanks, Clay.

**Operator**

Bill Herbert, Simmons & Company.

**Bill Herbert - Simmons & Company - Analyst**

Clay, to clarify, did you prophesy or guide for Rig Systems revenue out of backlog in 2016 at $2.4 billion?

**Clay Williams - National Oilwell Varco - CEO**

Yes, that is -- out of the $8 billion that we currently have in our backlog, that’s things that are scheduled to flow out in 2016, without benefit of orders that we will continue to win in the fourth quarter and into the first part of 2016, Bill.
Bill Herbert - Simmons & Company - Analyst

Got that. Thank you. And then back to your use of the term extraordinary -- and I will kind of asked the question a little bit differently. I understand that that encompasses the prospect of enhancing existing product lines. But really what I am most interested in is you're extolling the sort of attractive economic propositions given the adjustment in price. But I'm also curious as to what's the subset of opportunities that you are looking at which are really kind of transformational to NOV? And whether or not they, at least potentially, fundamentally redefine National Oilwell Varco, if your aspirations are consummated?

And adding to that, does this entail significantly increased service content? Does it entail possibly significantly increased non-energy exposure? I'm just curious as to how expansive your review is.

Clay Williams - National Oilwell Varco - CEO

Yes, you want stock symbols alphabetically?

Bill Herbert - Simmons & Company - Analyst

Yes, please, thank you. And also price, too.

Clay Williams - National Oilwell Varco - CEO

Well, Bill, I know you'll appreciate if I don't precisely give a roadmap in terms of what we are thinking over here. And I tried to touch on this in my opening remarks. The principles that we apply -- since I've been with the Company, we've grown from two business units to 15. And I will reiterate, we take a broad view across oilfield services and look for opportunities to deploy capital and develop strategies around things.

I will go back a couple of years and give you a real world example. We launched an FPSO initiative about four or five years ago, and I will point out this is long before anybody was talking about standardization, about industrial efficient supply chain, when we were sort of a lone voice on this subject.

But we recognized NOV has built and installed and commissioned 300 complicated offshore rigs. We've worked with every major shipyard out there. We've got great project management expertise, great relationships with every major shipyard around the globe, and these same shipyards were -- customers are very challenged when it comes to building FPSO vessels on-time, on budget.

Plus when we looked at our portfolio of product offerings between hose reel systems, offloading systems, cranes, composite piping, production chokes and valves and manifolds and other things, we had a lot of content on FPSO. So we've cultivated an FPSO strategy and said we have specific -- we are uniquely positioned in terms of our shipyard expertise to execute a strategy of improving FPSO construction; bringing more industrially elegant solutions to the supply chain, again simplifying the things that you are hearing a lot more of lately to reduce cost and risk around FPSO construction.

And NOV is uniquely positioned with regards to a vessel strategy in the deepwater. And then we supplemented that with acquisitions along the way, including APL turret mooring systems, one of the three global providers of turret mooring systems and swivel stack technologies; with NKT Flexibles, which is now NOV Flexibles, one of three global providers of flexible pipe, a big component of SURF packages that sort of fit this strategy.

So that's an example of where we are deploying capital to execute a strategy that I think has positioned us to be transformative in a significant sector in oilfield services, and thereby reduce costs for our customers. So that's an example of the kind of things that we are looking at. And suffice to say in a cyclical downturn, we are continuing to look for other opportunities to deploy capital and develop businesses.
Bill Herbert - Simmons & Company - Analyst

All right. Thank you.

Clay Williams - National Oilwell Varco - CEO

You bet. Thank you, Bill.

Operator

Jeff Tillery, Tudor, Pickering, Holt.

Jeff Tillery - Tudor, Pickering, Holt - Analyst

Clay, it's a relatively broad question, but as you look at the relatively short cycle businesses that you have and obviously the customers are consuming what they have. But could you just kind of walk us through what you perceive to be the customer inventories in terms of when we ultimately do see an uptick in activity, whether it be spare parts for rigs or some of the consumables in the other product lines? How much of a lag before you think your business starts to improve?

Clay Williams - National Oilwell Varco - CEO

Yes, it's a great question, Jeff. And unfortunately, it's driven by rig count and really the inverse of rig count which are stacked rigs. Because the stacked rigs, as activity goes down, then it frees up a string of drill pipe. It frees up the downhole tools that would otherwise be working on that working rig.

So it's very fluid and very difficult to tell, frankly, until we hit bottom on activity and we see a little time pass beyond that. Very difficult to tell kind of where that's going to lie. We are seeing customers be far more aggressive, I think, in this downturn with regards to cannibalizing their equipment, about repositioning it.

They are getting -- if they have a particular piece of equipment in a different region, there's a cost to repositioning that. There's freight, there's -- they have to invest in that just to move it and maybe to get it back to working order. And we are seeing customers go to more extraordinary lengths, I think, in this downturn than we have in the preceding couple of downturns with regards to cannibalization.

So there's a very, very Darwinian, very Draconian move to preserve cash and use what's on hand, and so we are seeing that. We do know it will turn around and when it does, one day the phones will light up and people will all of a sudden need it yesterday. So that's the other side of this, but we just -- at this point we don't know when that's going to occur.

Jeff Tillery - Tudor, Pickering, Holt - Analyst

That's helpful context. As I think about the Rig Systems business as we progress through the next year, so there will continue to be some volumetric pressure. Some of the offsetting factors are your ability to do more in-house.

How do you think about the floor in margins; not looking for single quarter, but at the trough of the cycle is that a business that can sustain low teens operating margins, do you think?
Clay Williams - National Oilwell Varco - CEO

Yes. First, I have a lot of confidence in our management team there to manage through this. They have done a great job along the way. Second, as I mentioned, we have sort of an outsourcing model in good times. And they are doing a great job sort of scaling back our outside suppliers about insourcing more and managing to the volume that's out there.

Third, as backlog moves down, there is more flexibility that opens up with regards to steps that they can take. Absorption does become harder, I think, from here on out. And then fourth, I think the wild card out there sort of remains pricing to some degree, kind of where that lands.

So I think – it's very difficult, I think -- I'd be reluctant to throw a margin number or range out there right now, other than we are, as I said many times before, we are going to manage what we can and manage to the market.

It may be helpful, too, to point out that our global network within Rig Systems of plants and facilities really serve both Rig Systems and Rig Aftermarket. The same plants that make components for rigs also make spare parts, and these components are used both offshore and on land. And between Rig Aftermarket continuing demand and ongoing work, and ongoing demand for components to replace things that are worn out, replace things that are burned up; to upgrade rigs even in the downturn, you are going to see rigs that need to upgrade certain components in order to qualify for certain work.

I think we could keep a decent load on our plants and our core team through that. So that's what we are kind of shifting to as newbuilds slow down a little bit.

The other part that I'm probably more optimistic about in terms of demand in Rig is we know a number of drilling contractors in North America and around the globe who are completely bought into the idea and the need to upgrade their fleets to AC technology. This is clearly where the market is going. So I think in terms of recovery, that's where we see it next.

Jeff Tillery - Tudor, Pickering, Holt - Analyst

All right. Thank you very much.

Operator

Jud Bailey, Wells Fargo.

Jud Bailey - Wells Fargo - Analyst

I wanted to follow up on the comment on revenue out of backlog and try to dig a little deeper into that if I could. Could you tell us, does that number include any revenues from Brazil related projects, or does that exclude anything from Sete?

Clay Williams - National Oilwell Varco - CEO

Minimal revenue out of Brazil.

Jud Bailey - Wells Fargo - Analyst

Okay. And helping us think about book and turn for the year, what was that number a year ago to help us calibrate how to think about your revenue out of backlog as we go through next year?
Clay Williams - National Oilwell Varco - CEO

I don’t have that at my fingertips, Jud. But yes, right now based on what we have on the books, that’s what we foresee.

Jud Bailey - Wells Fargo - Analyst

Okay, all right. That’s fair. And then my follow-up question is on Rig Aftermarket. I wanted to just follow up; you said Rig Aftermarket would be up slightly in the fourth quarter. And I may have missed, what exactly is driving the uptick in the fourth quarter for aftermarket?

Clay Williams - National Oilwell Varco - CEO

There is usually some seasonality in Aftermarket, a little bit in Q4, one. Two, we are seeing rising inquiries around stacking service and equipment things, and then some specific SPS things that are happening out there that we are working on. So that’s what gives rise to our outlook for Rig Aftermarket.

Jud Bailey - Wells Fargo - Analyst

Okay.

Operator

Marshall Adkins, Raymond James.

Marshall Adkins - Raymond James - Analyst

I want to come back to the margin thing. I think we were all surprised at how good a job you all did at holding up margins. In the commentary you’ve given so far today, it sounds like at least on Rig Systems and Aftermarket, you think that the margins will be fairly resilient. Is that -- am I reading that correctly?

Clay Williams - National Oilwell Varco - CEO

Yes. And again, we pulled up from quantifying that, but the high level of outsourcing, the flexibility, kind of open it up there. And we’ve got a great team there working on that question.

Marshall Adkins - Raymond James - Analyst

Subject to a few things, one of those you included was pricing. I assume pricing is holding up fairly well?

Clay Williams - National Oilwell Varco - CEO

I would say everything we do is under pricing pressure now, Marshall.
Marshall Adkins - Raymond James - Analyst

Okay. Last one for me; your orders in Rig Systems are a little higher than I thought they would be, given the current commodity environment. What are people ordering right now?

Clay Williams - National Oilwell Varco - CEO

We are still seeing interest out there, mostly around -- mostly from international markets, mostly from drilling contractors that are working closely with national oil companies. And I think this quarter it was around half land, half offshore. But there is, even in the worst of times, there is an ongoing level of demand for components for rigs. Things burn up, they break, they have to be replaced, they have to be upgraded.

So that kind of hits a pause when you first hit a downturn and people -- our customers will look at pulling off of other rigs, and we are certainly seeing that. But rigs are working and, as I said in my comments, when they work they consume mechanical components. So that’s kind of what we are seeing out there.

Marshall Adkins - Raymond James - Analyst

Good stuff. Thanks, guys.

Clay Williams - National Oilwell Varco - CEO

You bet. Thank you, Marshall.

Bill Sanchez - Howard Weil - Analyst

I know you all dedicated some time in terms of just the revenue out of backlog number, Clay, for next year, $2.4 billion. I was just curious if you could help us; could you maybe talk about given the deliveries you’ve seen push to the right, maybe just how much revenue maybe you’ve had slide here that you thought you would have booked in 2016 on the backlog; that has now moved into 2017. And I guess given that, is it too early for you guys to have a 2017 number in terms of revenue from backlog?

Clay Williams - National Oilwell Varco - CEO

Well, yes. I mean, what that encompasses is, as we’ve said over the last couple of calls, we’ve worked with our customers to push certain deliveries out and you’ve seen some announcements. So this is kind of the latest estimate including all of those shifts and, as I just said, includes pushing out a lot of Brazilian revenue as well. So it’s kind of the latest and greatest. We are continuing to work this. It remains a little bit fluid, but this is kind of what we are looking at right now.

Bill Sanchez - Howard Weil - Analyst

Got you. And it doesn’t sound like anything in terms of the terms of what you’ve agreed to with these customers. Nothing has really changed on these delayed deliveries; is that fair?
Clay Williams - National Oilwell Varco - CEO

Well, no, no, no. And I would add there's a little bit upside -- I don't want to overstate this -- picking up incremental maintenance work around this equipment. If it's going to be in a shipyard for an extra 12 months, then it needs some OEM maintenance and care, extension of warranty, those sorts of things. So we are being compensated for this.

And then operationally, the added benefit is that we are able to execute these projects at lower cost and better margins. And specifically, if we kind of slow down the pace of work on some of these, then we are able to avoid overtime, for instance. We are able to execute these with the best part of our supply chain, kind of our top-tier suppliers and the like. So that's the benefit for NOV.

Bill Sanchez - Howard Weil - Analyst

Great. One more, Clay, if I could ask for you. As far as the buyback is concerned, you finished that up. You've talked about clearly a focus on M&A, but that really being more of a 2016 event it sounds like, just given the bid/ask spreads out there right now.

Was there any thought or is the Board going to re-examine a new authorization here and possibly seeing some repurchases take place in 4Q, or is the buyback for now just shelved?

Clay Williams - National Oilwell Varco - CEO

A recommendation for management -- we'll be talking about this with our Board here through the fourth quarter, but I really want to really get focused on M&A. We are fortunate to have both, I think, as attractive applications of capital, and we can always put a buyback back in. But I think kind of given the emerging things that we are seeing in the M&A space, that's probably -- as we said in our opening comments, that's probably a better use of our capital right now.

So if that starts to diminish a little bit, if we feel like we're not going to get bids and asks to converge, then we can go back to buying back shares. But I would say here I think we are going to see more attractive opportunities emerge in the M&A space.

Bill Sanchez - Howard Weil - Analyst

I appreciate the time.

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.

Clay Williams - National Oilwell Varco - CEO

Again, we really appreciate you joining us this morning, and I look forward to speaking to you in February 2016. Thank you very much.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. Thank you for your participation. You may now disconnect.
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