NOV, Inc.
Third Quarter 2023 Earnings Conference Call Remarks

BLAKE MCCARTHY
Vice President, Corporate Development & Investor Relations

Welcome everyone to NOV's third quarter 2023 earnings conference call. With me today are Clay Williams, our Chairman, President, and CEO, and Jose Bayardo, our Senior Vice President and CFO.

Before we begin, I would like to remind you that some of today's comments are forward-looking statements, within the meaning of the federal securities laws. They involve risks and uncertainty, and actual results may differ materially. No one should assume these forward-looking statements remain valid later in the quarter, or later in the year. For a more detailed discussion of the major risk factors affecting our business, please refer to our latest Forms 10-K and 10-Q filed with the Securities and Exchange Commission. Our comments also include non-GAAP measures. Reconciliations to the nearest corresponding GAAP measures are in our earnings release available on our website.

On a U.S. GAAP basis for the third quarter of 2023, NOV reported revenues of $2.19 billion and net income of $114 million or $0.29 per fully diluted share. Our use of the term EBITDA throughout this morning's call corresponds with the term "Adjusted EBITDA" as defined in our earnings release. Later in the call, we will host a question and answer session. Please limit yourself to one question and one follow-up to permit more participation. Now, let me turn the call over to Clay.

CLAY WILLIAMS
Chairman, President, and Chief Executive Officer

Thank you, Blake.

NOV's third quarter revenues of $2.185 billion were up 4% sequentially and up 16% compared to the third quarter of 2022. The Company posted fully diluted earnings of $0.29 per share for the third quarter, up $0.21 YOY, and EBITDA was $267MM. Both sequential and YOY EBITDA leverage was 24%, driving consolidated margins up 50 bps sequentially and 190 bps YOY to 12.2% in the third quarter.

NOV's extensive offshore business drove results. Consolidated sales destined for offshore markets increased 10% sequentially and roughly 40% YOY, lifting our offshore mix to 46%. All three segments posted higher offshore revenues sequentially, with Completion & Production Solutions and Rig Technologies both posting solid double-digit growth. Our strong franchises in oil & gas as well as offshore wind carried the day.

Following a decade of underinvestment, which saw North American shale crowd out spending in offshore and international land drilling, we are pleased to see growing momentum in several offshore basins around the world, in addition to international land. Underpinned by LNG and constructive commodity prices, global offshore FIDs look to be in the range of $140B in 2023, up 60% from the average of the preceding 8 years. And 2024 looks to be even stronger. Offshore service capacity continues to tighten broadly, driving improved economics for us and our customers. Leading-edge dayrates for high-spec drillships are barreling towards $500 thousand a day, and jack-up rates are rising as well. Importantly, we are hearing of operators looking to lock up rigs for longer terms, which we hope will give our customers greater confidence to pull the trigger on capital projects that will drive future NOV orders. Although we are a long way from offshore rig newbuilds, we are intrigued by inquiries we've received related to three Eastern Hemisphere national oil companies considering potential newbuild jackups and a newbuild floater. In the meantime, our Rig Technologies segment is benefitting from strong demand for aftermarket spares and reactivations, as offshore rigs continue to mobilize. Rig Technologies aftermarket increased 10% sequentially and 46% YOY.

Completion & Production Solutions saw bookings rise 18% and posted a book-to-bill of 114%, led by our Subsea, XL Systems, and Process & Flow Technologies business units selling kit into offshore developments. Rig Technologies capital equipment bookings for the offshore were up 14% sequentially, but overall bookings fell $44MM following Q2's strong demand for land equipment.

Our consolidated revenues into international land drilling programs increased 3%, with Wellbore Technologies leading the way, posting double-digit sequential gains coming from Africa, Asia-Pacific, and the Middle East. Consolidated international and offshore sales gains were partially offset by sequentially lower revenues in North American land markets, down about 2% sequentially. Low gas prices and lower levels of U.S. drilling softened demand for drilling equipment orders, but CAPS benefitted from some large e-frac equipment orders in the third quarter for the U.S.

It's been an interesting time. We've navigated a decade of significant global underinvestment in oil and gas everywhere — except North American shale, which was responsible for 80% of global oil supply growth over the past 10 years. And during the last few years of this journey, we have been pommeled by inflationary gales and a supply chain tsunami. In response, we've cut costs everywhere - except new technology development. We've pushed prices to try to keep up with inflation, which has been challenging. Nevertheless, I am very, very pleased with the reception our new products are getting. As the oilfield goes back to work, our customers are benefitting from NOV's new solutions that are driving better performance, better safety, and lower emissions. They like what they are seeing, and demand is building, notwithstanding their pledges of capital austerity and lack of animal spirits.

Let me take a few minutes to address revenues, margins, and cashflow. First, with respect to revenue, NOV's performance has been strong. Specifically, NOV's top line growth rate since our low point in the first quarter of 2021 has been at a rate of about ~25% annual growth, ~6% higher than the Big 3 average through the same period. This has been driven by new bits and new drilling motors; new composite pipe designs; new digital products, including new wired drillpipe high-speed connections to the bottom of the hole, new edge computing products and new control systems; and new automation tools - all of which drive performance for our customers.

Thus far, NOV's sales outperformance has been accomplished without a meaningful capital equipment recovery. It has been achieved through re-setting our activity-driven product and service portfolio to offer what we knew all along our customers would eventually need.

Oilfield downcycles all end in, well, upcycles. At the end of every downcycle and the beginning of the next upcycle, scarred by their near-death experiences, oilfield service survivors generally suffer from chronic PTSD. They all swear never to spend a dollar of capital they don't have to ever again, and never, ever to stretch or wreck their balance sheets ever again. 1992, 1999, today. In a lot of ways, following periods of underinvestment, solemn pledges of capital discipline kind of mark the opening ceremony for an upcycle.

As an upcycle gains momentum and activity rises, the challenge oilfield service companies face is less financial fidelity and more related to the laws of physics. The oil and gas industry consumes highly specialized, fit-for-purpose equipment voraciously. Putting a bit five miles into the earth to hit a precise target devours expensive pipe and rigs. As demand rises and equipment is consumed, prices rise to ration its availability, leading to outsized margins and returns for oilfield service participants who own scarce equipment. When E&P companies face these equipment shortages, they actively sponsor additions to fleets through profitable, longer-term contracts to both incumbents and start-ups. And as the upcycle progresses…well, you know the rest of the story. Now, perhaps this time will be different…but we shall see.

The second thing I'd like to talk about are margins. While our margins continue to improve, they still remain below levels we need to generate adequate returns. Thus, we are focused on pulling the levers we can control, namely price and cost structure. We announced that we intend to further streamline our overhead by going from three segments to two segments, Energy Equipment and Energy Products and Services, starting January 1st. This is part of the $75MM cost reduction program we disclosed last quarter and is designed to make our business more efficient, while capitalizing on the new technologies we are bringing to the marketplace. We will be providing historical pro forma financials for your models next quarter.

As we continue to reduce costs, we are also intent on putting better quality and higher-margin orders into our backlog. We have been very intentional about price, risk, and commercial terms on large tenders, particularly in the offshore and international markets. Predictably, this has led to missing some project awards on price and terms, but, having been stung by inflation, we are sticking with our disciplined approach of price leadership, and, quarter-by-quarter, we see our competitive positioning improving as end customers come to appreciate execution, reliability, and technology more and more. We are confident in our strategy because we have good visibility on a growing pipeline of tenders, plus we are carrying solid and stable backlogs: $3.0B for Rig, which has had a book-to-bill of 102% through the last year; and $1.6B for Completion & Production Solutions, which has posted a book-to-bill of 106% through the past year. And, as I mentioned earlier, we've been able to post significant revenue growth since 2021, up 75%, on the strength of the rest of our portfolio, our non-capital equipment products. Our expectation is that, as the upcycle emerges, these new businesses, together with blossoming capital equipment demand at higher margins, will translate to overall higher margins and returns for NOV on a consolidated basis. Said another way, our quick-turn transactional businesses have enabled NOV to post strong revenue growth, while our later cycle equipment businesses represent additional optionality to a future upcycle.

Finally, free cash flow during the quarter improved $114MM sequentially but remains negative at $34MM. As we discussed on last quarter's call, the healing of the global supply chain has led to an acceleration of raw material and component deliveries for our businesses, and net working capital remained at an elevated 33% of annualized revenue during the quarter as a result. This trend is expected to begin reversing during the fourth quarter as our product shipments continue to catch up to the supply chain, which will improve our cash flows sequentially. Looking ahead to next year, the normalization of supply chains and working capital intensity should enable NOV to generate meaningfully positive cash flow and position us to begin returning more capital to our shareholders.

So, to summarize: 1.) NOV's new products and technology are amazing and are fueling strong revenue gains for the company without much assistance from our later cycle capital equipment businesses; 2.) if history is a guide, these capital equipment businesses will begin to grow, and then grow sharply, as an upcycle matures, but for now remain mostly optionality; 3.) margins have been pressured by extraordinary supply chain disruptions and inflation, but progress in these areas has lifted margins steadily from breakeven to 12.2% in 2-1/2 years; and 4.) after cresting in the third quarter, we expect working capital to decline in the fourth quarter to begin to drive strong positive free cash flow through 2024 and beyond.

Years of underinvestment in the oilfield, combined with operator demands for better reliability in the field and improving cash flow for our customer base, should drive our oilfield service customers to more normalized levels of maintenance spending and re-investment in their asset bases. More efficient manufacturing operations and a fully healed supply chain, together with a higher-margin backlog converting into revenue, will drive better incremental margins. All of these things will contribute to improving financial results for NOV as we work to provide the global energy industry with the technologies and customer service for which NOV is so well known.

Before I turn it over to Jose for more detail, I want to thank the NOV employees listening today for all your hard work and diligence to take such great care of our customers as well as each other. Two of the best examples that I can think of are Kirk Shelton and Isaac Joseph, whom I have enjoyed working with for many, many years. Many thanks to both you guys, and I wish you all the best.

Jose?

JOSE BAYARDO
Senior Vice President and Chief Financial Officer

Thank you, Clay. NOV's consolidated revenue totaled $2.185 billion in the third quarter, an increase of 4 percent sequentially, and 16 percent compared to the third quarter of 2022. Revenue from international markets grew 11 percent sequentially, offsetting a six percent decline in revenue from North America. EBITDA for the third quarter totaled $267 million, or 12.2 percent of sales, representing an incremental flowthrough of 24 percent sequentially.

We are in the early phases of our $75 million cost savings plan and realized modest savings during the third quarter. As we noted last quarter, we expect the majority will be captured in 2024, helped by the additional restructuring efforts Clay discussed.

We generated $40 million in cash flow from operations with working capital continuing to be a use of cash. As anticipated, receivable days increased slightly with the shift in our business toward international markets. Inventory also increased, as vendors have continued to debottleneck their operations and make deliveries earlier than originally planned. However, we believe our inventory build crested in August. The timing of these deliveries also contributed toward the $82 million sequential drop in accounts payables, which further impacted cash flow in the third quarter. We expect working capital metrics to improve from here, leading to healthy free cash flow in the fourth quarter and setting up a very strong free cash flow year in 2024.

Wellbore Technologies

Our Wellbore Technologies segment generated $799 million of revenue during the third quarter, a decrease of $5 million or less than 1% compared to the second quarter and an increase of 8% compared to the third quarter of 2022. Improving international activity and market share gains have offset lower drilling activity in the U.S. Despite the slight sequential decline in revenue, EBITDA grew slightly to $166 million, or 20.8% of revenue.

Our ReedHycalog drill bit business posted sequential revenue growth in the mid-single digits, driven by continued growth in the Middle East, a strong recovery from the spring break-up in Canada, and continued market share gains in the U.S. Despite U.S. drilling activity levels that have declined 16% since the fourth quarter of 2022, ReedHycalog has increased its revenues in the U.S. for three straight quarters. Our new cutter technologies continue to deliver better drilling performance and record bit runs, driving market share gains while commanding premium pricing.

Our Downhole tools business reported revenue growth in the low single digits with strong incremental margins. The strong seasonal recovery in Canada and continued gains in the Middle East and Latin America more than offset bottoming activity in the U.S. Despite the unit posting a slight sequential decline in overall U.S. results, revenue from our drilling motors business in the U.S. grew 3% sequentially against a 10% decline in drilling activity. Record runs and strong performance from new products is fueling demand for our drilling motors, which has continued to exceed supply – with operators increasingly preferring our Series 55 motors along with premium power sections, a combination that delivers stronger drilling performance in some of the most challenging drilling environments.

Our Wellsite Services business reported low single-digit revenue growth with strong incremental margins. The improved results were driven by growing demand for solids control and managed pressure drilling services and equipment in the

Middle East and offshore markets, which more than offset softer demand in the U.S. and Latin America. New product offerings like our iNOVaTHERM solids waste control units and our growing suite of new MPD technology have positioned this business particularly well in light of climbing international and offshore activity.

Our Grant Prideco drill pipe business posted a double-digit drop in revenue with outsized EBITDA decrementals after a very strong recovery in the second quarter. Over the course of the year, we have seen our mix shift from North America to international land and offshore markets. We expect this internationally-oriented revenue mix to continue into the fourth quarter. However, based on customer inquiries, the outlook for orders in the U.S. may improve sooner than we'd normally expect, likely reflecting expectations for higher levels of drilling activity in 2024.

Our Tuboscope business unit posted a slight sequential increase in revenue, achieving its 12th straight quarter with topline growth. Strong demand in the Eastern Hemisphere offset softer activity in the U.S. and Latin America. The unit realized stronger demand for pipe coating services and our TK Liner products across the Eastern Hemisphere, where activity remains strong, while lower drilling activity in the U.S. and higher industry inventory levels of OCTG reduced demand for inspection services at steel mills and outside processors.

Our MD Totco™ business' results in the third quarter were flat with its record results in the second quarter. Revenues from Drilling Surface Data decreased sequentially due to lower drilling activity in the U.S. and strong Q2 sales of capital equipment in the Far East that did not repeat, partially offset by higher activity in the Middle East and Canada. Lower revenue from Drilling Surface Data were offset by another strong increase in revenue from our eVolve wired drill pipe drilling optimization services. During the quarter, we helped a major operator in the North Sea shave more than 30 days from its drilling plan for a well on the Norwegian Continental Shelf by utilizing our wired drill pipe optimization and visualization tools, which are starting to see significant interest in the Middle East. We estimate this significant improvement in drilling efficiencies saved our North Sea customer more than $15 million, substantially improving its well's economics.

For the fourth quarter, we expect continued strength in international and offshore markets will more than offset bottoming U.S. land activity, resulting in revenue for our Wellbore Technologies segment increasing 4-6% accompanied by incremental margins in the low to mid 20% range.

Completion & Production Solutions

Our Completion and Production Solutions segment generated revenues of $760 million in the third quarter of 2023, an increase of 1 percent compared to the second quarter and an increase of 12 percent compared to the third quarter of 2022. EBITDA for the third quarter was $67 million or 8.8 percent of sales, down $2 million from the second quarter and up $11 million from the third quarter of 2022.

While our CAPS segment's results were essentially flat sequentially and drilling and completion activities remain subdued in North America, positive momentum in international and offshore markets helped us drive an 18 percent increase in orders to $530 million, resulting in a book-to-bill of 114 percent. Backlog at the end of the third quarter totaled $1.626 billion. We've remained disciplined on what projects we take and continue to insist on driving pricing higher, resulting in the addition of margin-accretive projects into our backlog, which will result in higher margins for the segment as we move into 2024.

Our Process & Flow Technologies business unit posted a low-teens sequential increase in revenue with solid EBITDA flow through, led by accelerating progress on new, higher-margin projects in our Wellstream Processing operations. We continue to pursue a large pipeline of potential offshore projects for our Wellstream and APL businesses. While some operators remain cautious, others are moving projects forward. We are seeing a sufficient number of quality opportunities advance that are allowing us to remain extremely disciplined with our pricing, to drive better margins in our backlog, while still posting a book to bill near 100% in the third quarter.

Our Subsea flexible pipe business posted results that were effectively in-line with the second quarter, but orders more than doubled sequentially, achieving the unit's highest order intake since 2015. While it has taken some time for customers to recalibrate their expectations and the unit is still working through lower-margin backlog, our disciplined approach related to which projects we are willing to take, and at what price, is beginning to pay off. Our efforts along with growing demand from Brazil, West Africa, Australia, and the North Sea are allowing us to book projects that have much healthier margins and more favorable milestone payment terms than those booked over the last several years.

Our XL Systems conductor pipe connections business posted a low single-digit sequential decrease in the third quarter after a robust increase in revenue during the second quarter. Orders remained strong, and book to bill was over 100% for the fifth straight quarter, led by demand from West Africa and the North Sea. In addition to the unit's success in its core offshore market, the business continues to see growing opportunities in geothermal markets and recently completed the first sale of its new XCalibur gas-tight threaded connector to a geothermal customer in California.

Our Fiberglass Systems business posted a low-single digit increase in revenues during the third quarter. Solid growth in oil and gas markets, led by the Middle East, more than offset slightly softer demand from industrial and fuel handling markets. The outlook for this unit remains bright with growing demand for our new corrosion proof composite pipe products from international oil and gas markets. We also continue to see meaningful opportunities to supply our new flame-and-smoke resistant composite ducts for semiconductor manufacturing plants and to support the lithium mining and processing space.

Our Intervention and Stimulation Equipment business realized a double-digit sequential decrease in revenue largely due to lower deliveries of pressure pumping equipment, partially offset by higher shipments of process and wireline equipment. While drilling and completion related activity in the U.S. continued to soften during the quarter, order intake remained solid with the business unit posting a greater than 100% book-to-bill underpinned by demand for our new eFrac products. Demand from international and offshore markets remains solid, and customers in North America remain focused on replacing and upgrading their asset base with more operationally and energy efficient equipment. During the quarter, we booked orders for 25,000 hydraulic horsepower of eFrac equipment and 3 of our power pod systems that enable hybrid fleets, where eFrac equipment works alongside conventional assets, making it easy for customers to begin capitalizing on the efficiencies of our eFrac technology as they replace their conventional pumping units over time. Despite the perception that there is much excess completion equipment in North America, demand remains steady from technology driven customers, as evidenced by the eFrac order. Demand from technology-forward customers is not limited to pressure pumping but also applies to wireline and coiled tubing equipment. In the third quarter, we sold four of our i-Maxx wireline units and two high-spec coiled tubing spreads that are fully equipped with our latest controls and utilize our new digital Max Completions platform to deliver process, machine, and control data to provide superior service at the wellhead. NOV's technology leadership is second to none, which is also reflected in our team being selected by a major IOC to engineer the industry's first 20,000 psi pressure control equipment for use in completion and intervention services in the Gulf of Mexico.

For our Completions & Production Solutions segment, we expect continued improvements in offshore markets will more than offset bottoming activity in North America, resulting in sequential revenue growth of between 2 to 4 percent in the fourth quarter. Additionally, a better mix of higher margin business and cost savings should result in a 100 to 300 basis point improvement in EBITDA margin, which should reach into the double digits for the first time in three years.

Rig Technologies

Our Rig Technologies segment generated revenues of $686 million in the third quarter, an increase of $80 million or 13% sequentially. The strong growth was driven primarily by an increase in deliveries of capital equipment packages, greater progress on projects, and an increase in sales of aftermarket parts and services. Adjusted EBITDA increased $29 million to $100 million, or 14.6% of revenue. The strong incremental leverage of 36% was driven by a more favorable sales mix with improved output from our aftermarket operations, as well as progress on cost reductions.

New orders totaled $178 million, and we also received a $145 million inflationary price adjustment related to the new rigs for Saudi Arabia, resulting in a total of $323 million added to our backlog. When netted against Q3 shipments of $248 million, the segment's backlog increased by $75 million sequentially to $2.968 billion.

The bulk of the segment's capital equipment orders were to upgrade or replace various rig components for offshore and land rigs. We also saw increasing demand for our new automation and robotics technology due to its ability to enhance wellsite safety and improve drill-floor efficiencies. While orders for rig capital equipment remained muted, we are growing increasingly optimistic that dynamics in the offshore drilling markets will continue to improve, driving additional demand for capital equipment sales.

Our Aftermarket business delivered strong results in the third quarter, up 10 percent sequentially, and up 46% year-over-year. The sequential growth was driven by a 12% increase in spare part sales. Accelerated deliveries from our vendors allowed us to ramp our throughput and begin chipping away at our backlog of orders. While total inventory increased, we were able to ship a large amount of spare part packages and assemblies that were awaiting missing components, which was reflected in a 25% sequential reduction in the segment's work in process inventory. We expect our shipments will continue to grow during the fourth quarter, and combined with lower deliveries from our vendors, should drive both improved profitability and cash flow. Beyond the fourth quarter, the outlook for our aftermarket business, which now comprises 56 percent of Rig Technology's mix, is strong. Customers are digging deeper into their stacks for rig reactivations and the active rig fleet is aging, driving larger opportunities for our aftermarket operations. We are seeing this playout in our backlog of reactivation, upgrade and recertification projects. Excluding projects with a scope of less than $2 million, in the first quarter, we had $199 million in active projects with an average cost of $9 million. In the second quarter the total value of projects in execution increased to $316 million with an average price of $11 million, and in the third quarter the total increased to $404 million with an average price of $14 million. We expect the combination of a growing number of actively working offshore rigs and continued reactivations will continue to support a healthy environment for our aftermarket business.

I next want to take a moment to highlight the importance of the duration of contracts between our offshore drilling contractor customers and their E&P operating company customers. Over the recent past, we've seen our offshore drilling contractor customers reset and repair their balance sheets, supported by rapidly improving day rates. To date, any rig reactivation or upgrade has been supported by operator contracts that provide mobilization fees, higher day rates, and a duration sufficient to reach a payback on the meaningful investments required to get stacked rigs back to work. However, despite all the contracts that have been announced over the past two years, most of the fleet remained on short, well-to-well contracts, and it wasn't until recently that the average duration of contracts for the active drillship fleet exceeded one year in length. In fact, the average duration of high-spec drillship contracts signed from 2015 to 2022 was about 8 months. Today it is pushing well beyond a year. Similarly, semis and jackups are also seeing meaningful expansions of average term. This is important because it drives drilling contractors' investment decisions on capital expenditures. We believe that with extending visibility of healthy cash flow, backed by contracts across the offshore drilling fleet, contractors will become more willing to buy upgraded equipment and reactivate rigs without contracts in order to improve their competitive positioning for upcoming tenders in which they can secure work over longer time horizons. We are already beginning to see signs of this taking place. In the jack-up market, the supply-demand dynamic within the high-spec asset class continues to tighten, with leading-edge, high-spec, day rates now eclipsing $170 thousand, a level above which newbuilds become possible. While we don't anticipate any of the established drilling contractors to place orders anytime soon, as Clay referenced, three NOCs have made serious inquiries into current newbuild pricing, shipyard availability, and construction timing.

In the offshore wind market, the impact of higher interest rates and cost inflation is challenging the economics of certain high-profile projects. Therefore, it was not surprising that wind installation vessel contractors deferred tenders during the quarter. Despite the recent challenges, there is still a projected shortfall in vessel capacity needed for projects that have been sanctioned, which is driving constructive conversations with multiple contractors. While we did not book a new wind installation vessel during the quarter, we did receive an order for an offshore cable lay vessel equipment package from a European contractor, who will use their new vessel to install critical infrastructure for offshore wind development. We believe this award supports the view that the buildout of offshore wind will continue to advance once expectations on project economics are reset.

Looking forward for our Rig Technologies segment, we believe steadily improving market conditions and manufacturing throughput will drive improved financial results for the segment. In the fourth quarter, we expect revenue to increase between 1 to 3 percent with EBITDA flow through in the low-to-mid thirty percent range.

For consolidated company results, we believe building momentum in numerous offshore markets, including rising exploration activity, along with continued growth in the Middle East, will more than offset soft North American land activity, enabling EBITDA to reach the $300 million range, with much improved cash flow in the fourth quarter.

With that, we will open the call to questions.