National Oilwell Varco, Inc.
Second Quarter 2015 Earnings
Conference Call Remarks

LOREN SINGLETARY
VP – Investor and Industry Relations

Thank you, Kevin, and welcome, everyone, to the National Oilwell Varco Second Quarter 2015 Earnings Conference Call. With me today is Clay Williams, President, CEO and Chairman of National Oilwell Varco.

Before we begin this discussion of National Oilwell Varco's financial results for its second quarter ended June 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 on limited information as of today, which is subject to change. They are subject to risks 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
President, Chairman, and Chief Executive Officer

Thank you, Loren, and welcome, everyone. This morning we announced that National Oilwell Varco earned $0.74 per fully diluted share in its second quarter ended June 30, 2015 on US GAAP basis. Excluding $17MM in pre-tax charges or 3 cents/share after tax related to severance and facilities closures, earnings were $0.77 per fully diluted share, down 32% sequentially from first quarter 2015 earnings and down 48% from the second quarter of 2014, excluding other items from all periods.

Revenues were $3.9B in the second quarter of 2015, down 19% sequentially and down 26% YOY. Consolidated operating profit excluding other items was $455MM or 11.6% of sales in the second quarter. Decremental operating leverage was 26% sequentially and 36% YOY.

EBITDA excluding charges in the second quarter was $627 million or 16.0% of sales, down 25% sequentially and down 45% YOY.

Almost all of our business units posted lower sequential sales due to low oil prices and lower activity around the globe, with only a few areas like Argentina and the Middle East bucking the trend. We also felt a full-quarter effect of customer discounts implemented during the first quarter, along with cost absorption challenges in manufacturing facilities. Generally, we still see some price pressures in certain products, mostly in international markets, but most NAM business units are reporting that pricing is stabilizing at new, lower levels, as the rig count flattens. Consolidated revenues for the US declined 29% sequentially, Canada down 37% sequentially and international revenues fell 14% sequentially.

Orders improved 33% sequentially for Rig Systems, but they still remained low, at $313M. Q2 included a jackup package and a production platform rig. The Rig Systems backlog declined 13% sequentially to $9.0B. At this point we are expecting orders to remain roughly flat in Q3 but to start to pick up in Q4, driven by higher demand for land rigs, and rising inquiries around capital components. Offshore order recovery is still many quarters away, and we expect NOC-driven jackup demand to recover before floaters.

Within Completion & Production Solutions, orders fell 19% to $264MM, leading backlog 18% lower sequentially. We expect orders to remain low in Q3, although we may get some incremental help from flexible pipe orders.

The oilfield services industry we sell to is very good at stopping expenditures when oilfield activity turns down, which they are demonstrating right now. We believe these spending levels are not sustainable, because they support ongoing operations by depleting their inventories of consumables and equipment they have on the shelf, or by raiding idled rigs for parts, components and drillpipe.

As oilfield service companies gradually destock they will eventually run out of opportunities to cannibalize their existing fleets, and we expect orders to begin to flow again to NOV, given that oil & gas remains a highly capital-intensive undertaking, and that NOV is one of its largest capital manufactures and suppliers of technology. Our visibility into the how long they can live destocking and cannibalizing varies by product- we know drillpipe, for instance, is cannibalized from idled land rigs by some, but not all, drilling contractors, and DP is probably a year away from meaningful recovery. On the other hand, some products feel much closer to the turn. We are beginning to see some inquiries come in for drilling motor parts and relines. Last week we began to see some new orders for fiberglass pipe. Our XL Systems conductor pipe unit, which sells mostly into the offshore, had a record quarter for inquiries in Q2. Demand for wireline units is holding up pretty well, with a bright outlook for the second half. After declining every single month since last October, spares orders within our Rig Aftermarket group ticked up for the first time in July. A few weeks of improved order inquiries does not necessarily signal the turn around, and we are hesitant to call bottom just yet. But we know from past downturns that once the rig count stabilizes the end of destocking and cannibalization is just a matter of time.

I would add, too, that I don't believe that fastidious equipment maintenance, for the long run, is at the top of our customer's priority list right now. Equipment is run hard in the field and just parked next to the fence and hosed down. Customers living hand-to-mouth aren't sure if it will ever get another job and sure don't want to put cash into equipment without a firm job on the board.

Just about everything on land can be cannibalized, but offshore typically only top drives, racker arms and iron roughnecks will be cannibalized. This time around we will be helped by the fact that a lot of new generation equipment has flowed into the fleet, so the large overhang of mechanical and SCR equipment will be less usable on the newer tier 1 AC rigs that the industry is migrating to.

We also believe that the level of drilling we are stabilizing at is not sufficient to grow production, which will one day be required to meet rising demand. Unfortunately, NAM shale production is not yet rolling over, like we had hoped, as operators are apparently high-grading their drilling into the core areas of the shale plays, and as completions slowly catch up with drilled wells. And now we are dealing with slowing economic growth in China and the potential return of 700,000 BOPD from Iran, meaning that our outlook for recovery gets pushed at least a couple of more quarters into the future.

So, in the meantime we have three areas of focus, one of which is to manage what we can- we are cutting costs.

In the second quarter we reduced SG&A 14% sequentially and 21% since the end of 2014. Within our Cost-of-Sales structure we are insourcing much more of our work from outside suppliers, seeking to preserve our core NOV employee base and utilize NOV machine shops and fabrication capabilities, as much as possible. Our downhole tools business decreased outsourced manufacturing spend 58% sequentially. YTD we've insourced 36,000 hours into one of our large Rig Systems manufacturing plants. By reducing overtime, winning discounts from our suppliers and high-grading our supply chain across the organization, we were able to increase the margins we achieved on existing project work in Rig Systems- the segment posted a 120 basis point margin improvement sequentially despite a 24% sequential decline in revenues. Our drillpipe business is pacing production to match orders at about half of capacity, to preserve our core team.

These reductions are difficult but necessary and effective. We will emerge more efficient when the inevitable recovery does finally arrive.

Second, we continue to invest in our long-term strategic plans, which will shape our opportunity set when we ultimately emerge from the current downturn. We are striking a balance between prudent cost reductions in the shortrun, and investments in a future which will see the oil and gas industry continue to rely on sophisticated technologies to supply an energy-hungry world. We intend to emerge a better company in that world.

These initiatives include, for instance within our Completion & Production Solutions segment, constructing a more comprehensive package of equipment for floating production systems, by acquisition, investing in R&D and working with industry partners. Over the past few years we have quietly added promising new technologies to our Process & Flow Technologies group that separate oil from produced waters, separate sand from production streams, and inject seawater into deepwater reservoirs. These have been added to our offering of pumps, valves, manifolds and other product, and they complement offloading systems, cranes, deck machinery, composite pipe systems, turret mooring systems and flexible pipe, and a patented design for a FPSO hull that can reduce steel costs by as much as 20%, and mooring costs by as much as 25%.

By offering a more complete package of components, and by developing standard modular packages for floating production units, we are simplifying the supply chain for these complex vessels, reducing both the cost and the construction risk. This is precisely what our deepwater E&P customers are looking for. We continue to work a handful of potential large FPSO projects as the sponsors rework and reduce costs. Our engineering activity has risen YOY, and generally we are seeing larger vessels, buoys and turrets within these projects.

Elsewhere in the deepwater arena we see demand for gas-tight conductor connections we developed within our XL Systems product line, which helped fuel higher sequential sales in the second quarter, at strong incrementals. We have been steadily investing in technology, and adding capacity in this product in West Africa and the Gulf Coast. Likewise, our flexible pipe capacity additions in Brazil led to slightly higher sequential results for this group in the second quarter, although pricing pressure on this product remains high.

Our Completion & Production Solutions segment has also assembled the global leading supplier of coiled tubing and CT units, pressure pumping, blending, mixing and other fracture stimulation equipment, along with wireline units and composite piping systems, including quick-installation reeled composite pipe that are impervious to corrosion- technologies which are enabling the shale revolution, and for which we see further growth internationally in the long run. Our large installed base of equipment offers opportunities for NOV to invest in aftermarket support and periodic recertification of high-pressure frac fleets and wireline equipment through the next few years.

Our Wellbore Technologies segment is pressing new developments in Big Data, software answer products, closed-loop drilling automation systems, and managed pressure drilling within the Dynamic Drilling Solutions business unit, to continue to drive safer, faster drilling operations to drive higher returns for our customers. Lately we've seen large directional drillers bring new technology to lower tier marketplaces to win business; we believe this will create new opportunities for our downhole tools unit to also sell new technologies into these areas as well. We began operating our new test rig in Navasota, Texas earlier this year, which provides us with a great new laboratory to pioneer new technologies like these, and we expect to undertake a half-dozen or so drilling automation jobs through the remainder of 2015.

Within the segment these new, transformative technologies build on several trusted, global franchises like Grant Prideco, which pioneered premium drillpipe designs that are able to execute the challenging horizontal drilling wellpaths that are fueling the shale revolution. Earlier this year Grant Prideco launched a new intervention riser product, and has sold three strings already, including the industry's first 7-5/8" string. Our Tuboscope franchise works closely with Grant Prideco to inspect, coat, hardband, and repair drillpipe, along with providing critical coating, threading and quality assurance services for tubing, casing and line pipe globally. Shale programs are highly consumptive of both drillpipe as well as production tubulars, which has helped drive good growth within Tuboscope through the past several years.

Likewise, our Wellsite Services business foresees longer-term growth prospects in solids control to improve drilling speeds, drilling fluids technologies, waste management around drill cuttings, and water handling and management- some of the largest and most costly challenges faced by operators both onshore and offshore. NOV is, for instance, the leading provider of thermal desorption cuttings treatment units globally, and we are seeing new markets emerge in places like North Dakota, West Africa, and China, which is implementing zero-discharge rules.

Our Rig Aftermarket segment declined more than we expected through the first half of 2015, due to the cannibalization I mentioned earlier. Spare part purchases, in particular, continued to slip, which rising SPS work failed to fully offset. We expect to see the SPS project count increase once again in Q3, but at a lower rate than we would otherwise expect as customers are scrapping some rigs scheduled for SPS, and postponing others until they get a contract. Customers are also trimming the scope of the SPS's moving forward to be bare bones, rather than seeking to upgrade and differentiate their rigs.

We expect Rig Aftermarket segment revenues to be roughly flat from Q2 to Q3 and Q4, but to again resume growth in 2016 due to its large and growing installed base of sophisticated equipment requiring close OEM support. We have invested in training and support facilities closer to our customer's operations around the globe, and in condition monitoring technologies that will further differentiate NOV's level of support. The extraordinary installed base of NOV equipment in the oilfield following a decade of intensive retooling, and the nature of this equipment and the high level of sophistication it embodies, creates a remarkable aftermarket support opportunity unique to NOV, which we will continue to vigorously prosecute.

Turning to Rig Systems, we also see potential for future opportunities despite a very weak order environment today. Our Rig Systems segment continues to invest in rig designs for tomorrow- configurable rig floors, low-cost vessels, more highly-automated land rigs, NOVOS control systems that enable third party-developed apps, and retrievable subsea BOP pods.

While offshore rig newbuild demand is expected to remain low for an extended period, we believe demand for land rigs- specifically AC, tier 1, walking, electronic controlled, 7500 psi mud system capable, land rigs, could resume in earnest as early as late 2015, driven by several conversations we have underway in the Middle East, Latin America, and NAM. We see the new rig technology strategy- AC powered, electronic controls, high levels of automation- prevailing strategically in all rig categories, land and offshore.

So to summarize our second current initiative is to recognize that the industry will recover, and to make sure that we have continued to invest in technology that will maximize our position in that recovery. NOV is unique in its ability to pioneer new technologies, business models and capabilities to serve the industry, and we will not let this downturn distract us from our long term vision.

Our third initiative is to deploy capital into acquisition opportunities which will emerge in this downturn. The strategies I outlined earlier can be enhanced and accelerated by combining businesses. We are actively seeking M&A opportunities, but, to be clear, we will be disciplined in our approach. We have closed three bolt-on acquisitions so far this year and have letters of intent with several more, but thus far we find making the bids and asks converge continues to be a challenge. As most of you know we have a long history of building NOV through acquisitions, and we have a lot of experience in this area. That experience teaches us to be patient…until it is time to be otherwise. In preparation for potential opportunities we expanded our revolving line of credit to $4.5B during the second quarter.

So, to summarize- we are reducing costs, we are continuing to invest in our long term plans, and we are pursuing M&A opportunities to accelerate and enhance those long-term growth opportunities. All to position NOV for future growth and profitability.

This couldn't happen without the terrific employees that make up NOV, and I want to thank them for their hard work and leadership through this difficult time. In a challenging market our customers need us more than ever to provide great service and technology and crisp execution and I'm proud to be a part of the team that does that better than anybody.

Let me touch on a couple of more subjects before I turn it over to Loren to review detailed financial results.

Unfortunately, in Brazil, we don't have a lot more clarity on the resolution of Sete's rig building financing than we did last quarter. While there have been press reports of reductions in rig building, we have not received any cancellations from our customers on the 22 floater packages for which we have binding contracts, in hand, to provide. Consequently we continue to report these contracts in our backlog, and at June 30, 2015 they totaled $3.1B, and during the second quarter we recognized $80MM in revenue related to the shipyard where we continue to be paid. We have suspended activity in the other three.

Next, the liquidation of our working capital is proceeding more slowly than we would like, for a couple of reasons. We had extraordinarily large cash tax payments in the quarter related to a foreign tax matter we reported in Q1. The unwind of our Rig Systems backlog and associated customer financing will naturally soak up calculated working capital as we earn revenue against projects for which we have already been paid. Second, the negotiated delay of several rigs in the shipyard means we will hold inventory for these projects longer than we originally planned, but, as we noted on the last call, we expect the margins we earn on these to benefit. Finally, our customers have been slower to pick up their equipment given market conditions, resulting in inventory remaining on our books a little longer than normal. We remain focused on improving cash conversion and expect to make better progress over the next few quarters.

We are also aggressively pursuing more repatriation of cash from overseas, after good progress last year on this front. We believe the second half of 2015 will see further improvement in this area.

At this point let me turn it over to Loren to discuss our second quarter performance and outlook in more detail. Loren?

LOREN SINGLETARY
VP – Investor and Industry Relations

Thanks, Clay. I will now discuss our segment operating results for the second quarter of 2015.

NOV Rig Systems generated revenues of $1.9B, down 24% sequentially and 19% compared to the second quarter of 2014. Revenue out of backlog was down 24% sequentially to $1.7B. We completed 8 offshore drilling equipment packages during the quarter. Improved project execution and the impact of several cost reduction measures including renegotiating vendor pricing, improved logistics, and supply chain optimization allowed for an increase to segment margins. Operating profit for the segment was $395MM, yielding operating margins of 20.5%, up 120 basis points from the first quarter of 2015 on improved margins on projects. Decremental leverage was 16% sequentially and 24% YOY, well below normal leverage for the business in the 30-40% range, due to cost reductions. EBITDA was $419MM or 21.7% of sales, and EBITDA margins increased 140 basis points as a result of these cost savings measures. Q1 to Q2, offshore revenues declined 18%, and land revenues declined 35%.

Now, let's discuss capital equipment orders and the resulting backlog for NOV Rig Systems. In the second quarter, we received $313MM in new orders resulting in a book-to-bill of 18%, a moderate increase from Q1. We ended the quarter with a backlog of $9.0B, down 13% sequentially. Of the total $9.0B backlog, approximately 91% is offshore and 92% is destined for international markets.

As we move into the third quarter of 2015, we expect total NOV Rig Systems revenues to decline approximately 20%, into the range of $1.5 to $1.6B. We expect to see revenue out of backlog slowing to the range of $1.3B, as we will ship fewer land rigs and continue to work through deliveries of offshore rigs which have been rescheduled for delivery later than originally planned. We are continuing our cost reduction initiatives to reduce overtime, and decrease supply chain costs, which is helped by easing congestion in the shipyards, but lower volumes are expected to lead segment OP margins to decline into the mid-to-high teens for Q3. Right-sizing and efficiency savings will likely be more than offset by under-absorption resulting from the revenue decline.

We expect orders for offshore newbuilds to remain low, but we do see a few opportunities for specialized equipment like 20,000psi and arctic offshore rigs, and jackup rigs for drilling contractors to go into national oil company programs through the next 18 months or so. On land, we are seeing rising inquiries for international bright spots in Latin America, and, in the Middle East, as there is a growing appetite for the higher-horsepower desert rigs especially suited for that region. We also have NAM customers committed to their long-term strategies of high-grading the technology of their rig fleets to Tier 1 AC rigs with high pressure mud systems, and believe we will begin to see meaningfully higher land rig orders late this year. We also expect capital component orders to slowly recover later in the year and into 2016, to support the ongoing rigs continuing to work. Nevertheless, we expect the book-to-bill for the segment to remain below one for at least the next few quarters.

Our NOV Rig Aftermarket segment sales declined more than we expected in the second quarter. It generated revenues of $657MM, down 9% sequentially and down 16% compared to the second quarter of 2014. As Clay noted, the sharp decline in both offshore and onshore drilling activity led to sharp reductions in cash expenditures by drilling contractors, most notably in spare parts sales as customers continue to consume existing inventories and cannibalize equipment off stacked rigs before making any new purchases. Customers are doing the absolute bare minimum in terms of maintenance and repair- only what's necessary to keep their fleets running. Operating profit for the segment was $145MM, resulting in operating margins of 22.1%. Margins were down 560 basis points sequentially and 550 basis points year-over-year, and sequential decremental leverage was extraordinarily high at 87%, due to lower revenues, pricing pressure and inventory charges related to older equipment. Excluding the charges sequential decremental leverage would have been in the mid-50% range. EBITDA was $152MM, or 23.1% of sales. Land sales were approximately 25% of total segment revenues, consistent with Q1.

As we move into the third quarter, we believe NOV Rig Aftermarket revenues will be roughly flat with Q2, with slight increases across most spare parts product lines and additional repair work, offset by less demand for field service and fewer manifold and expendable sales from our Mission product line.

Operating margins are expected to increase slightly from Q2 on a higher mix of spare parts sales and on reduced charges. Long term our outlook for this segment remains very bright, as the industry is high-grading its fleet of equipment with much more NOV technology within the installed base. When worldwide drilling activity recovers, drilling contractors - who are currently delaying purchases - will need this segment to respond quickly. An increase in demand, accompanied with efficiencies and cost reductions currently being implemented, will position the segment for sharp improvement.

For the second quarter of 2015, NOV Wellbore Technologies generated revenues of $956MM, down 18% sequentially and down 34% compared to the second quarter of 2014, on lower global drilling activity. Operating profit for the segment was $47MM, resulting in operating margins of 4.9%, down 570 basis points sequentially and 1,370 basis points from the second quarter of 2014. Segment-wide cost reduction efforts, in the face of falling rig counts, helped mitigate some of the intense price pressure felt across the group, which helped hold sequential decrementals to 36%. Pricing appears to be stabilizing across most NAM markets as the rig count has more-or-less stabilized, and has ranged from low single digits on up. Some international markets are continuing to receive invitations to discount as international activity has slowly declined. EBITDA in the second quarter was $146M, or 15.3% of revenue. As we've noted in the past, drilling activity tends to drive results for the segment overall, but portions of this business are more related to production and well servicing, so areas like tubing reclamation and line pipe coating within Tuboscope are helping offset drilling-related declines.

Looking into the third quarter of 2015, we believe that Wellbore Technologies revenues will be down in mid-single-digit percentage terms, as backlogs for drillpipe and other manufactured products from the group have declined through the second quarter. As Clay noted earlier, our customers are destocking inventories, and some of our products within Wellbore Technologies are closer to a resumption of orders than others. We expect margins to decline slightly from the second quarter on mix and continued discounting in certain areas. Nevertheless, we are also continuing to implement strategies to reduce costs while also increasing operational efficiencies around the world, and we are defending our strong market positions within Wellbore Technology by investing in R&D and innovating new technologies, to position ourselves for the inevitable upturn.

NOV Completion & Production Solutions generated revenues of $873MM for the second quarter of 2015, down 8% sequentially and 23% compared to the second quarter of 2014. Operating profit for the segment was $81MM, resulting in operating margins of 9.3%, down 210 basis points sequentially and 470 basis points year-over-year. Sequential decrementals were 36%, and second quarter EBITDA for the segment was $141MM, or 16.2% of sales. Sequential sales changes across this segment varied widely, with XL Systems and NOV Flexibles both posting improvements, while sales of coiled tubing and pressure pumping equipment declined sharply, on lower backlogs and on customers delaying pickup of equipment they ordered in prior periods.

Turning to our capital equipment orders and resulting backlog for NOV Completion & Production Solutions, the second quarter saw an order intake of $264MM and recognized $538MM of revenue out of backlog resulting in a book-to-bill of 49% and a quarter-ending backlog of $1.2B, down 19% sequentially. Orders were down 19% from the $327MM won in Q1, and of the total $1.2B backlog, approximately 71% is offshore and 82% is international.

As we move into the third quarter 2015, we believe revenues will be roughly flat with Q2 results, and expect revenue out of backlog to be in the range of $450MM+. Lower revenues and continuing pricing pressures across the segment should offset cost reduction efforts, which will result in a slight margin decline in the third quarter. We expect the next few quarters to be challenging in the FPSO space, but we expect to continue to help NOC's and IOC's develop cost-effective solutions to improve the economics of offshore projects. Low oil prices have prompted these customers to reevaluate project scoping and seek ways to reduce costs. The Completions & Production Solutions segment is well positioned to help.

Now, let's discuss our financial statements.

Working down the Consolidated Statement of Income for the second quarter of 2015, you will see that gross margin declined to 22.3%, generally reflecting pricing pressure partially offset by cost reductions. SG&A decreased 14%, or $69MM sequentially due to cost reductions, and was 10.7% of revenue. Other items were $17MM in the quarter due primarily to severance and facility closure costs. Equity income decreased to $7MM, and we believe that it will continue to fall through the remainder of the year due to sliding demand for OCTG. Other expense for the quarter was $30MM, which represents a $26MM delta sequentially primarily due to fewer foreign exchange losses and asset write-offs during the second quarter of 2015. The effective tax rate for the second quarter was 26.9%, down from the 37.6% rate that we posted in the first quarter of 2015. The first quarter's rate included a discrete foreign exposure which did not recur. The low second quarter rate reflects a much higher mix of income for low-rate foreign jurisdictions, which we expect to have a smaller effect later in the year. Looking forward to Q3, we expect the tax rate to be a little higher in comparison to the second quarter.

EBITDA for the second quarter, excluding other items, was $627MM, or 16.0% of sales.

Turning to the balance sheet, our June 30, 2015 balance sheet employed working capital, excluding cash and debt, of $6.1B, up $343MM or 6% sequentially. The increase was driven entirely by accrued taxes, which declined $408MM in the quarter on large cash tax payments. Other movements within working capital saw accrued liabilities and accounts payable decline, which were offset by a decrease in accounts receivable, down $548MM sequentially. Net customer financing- the net of prepayments, progress billings, and costs-in-excess-of-billings, was a use of cash of $124MM in the quarter, due to our declining backlog in Rig Systems. Inventory ticked up slightly due to delays in customers picking up frac equipment, and the negotiated delays in offshore rig deliveries, partly offset by inventory reductions in almost all other business units.

For the quarter, the Company generated $194MM in cash flow from operations, and capital spending was $104MM, down 20% sequentially and 41% YOY. In the quarter, we also made dividend payments of $178MM; and, we spent $447MM to repurchase 8.6MM shares of NOV stock for a total of $2.6B in share repurchases under our $3B authorization. Debt increased $60MM to $4.3B and our net-debt-to-capitalization was 9.3%. As a result, we ended the second quarter of 2015 with a cash balance of $2.5B, down $480MM sequentially. Of the $2.5B in cash, 3% of the balance was in the U.S. at June 30, 2015.

With that we would like to open it up for questions.