Fourth Quarter 2022 – Earnings Conference Call Prepared Remarks

Jud Bailey *Baker Hughes – VP of Investor Relations*

Thank you.

Good morning everyone, and welcome to the Baker Hughes Fourth Quarter 2022 Earnings Conference Call. Here with me are our Chairman and CEO, Lorenzo Simonelli; and our CFO, Nancy Buese. The earnings release we issued earlier today can be found on our website at bakerhughes.com.

As a reminder, during the course of this conference call, we will provide forward-looking statements. These statements are not guarantees of future performance and involve a number of risks and assumptions. Please review our SEC filings and website for a discussion of the factors that could cause actual results to differ materially.

As you know, reconciliations of operating income and other GAAP to non-GAAP measures can be found in our earnings release.

With that I will turn the call over to Lorenzo.

Lorenzo Simonelli *Baker Hughes – Chairman & CEO*

Thank you, Jud. Good morning everyone and thanks for joining us.

I would like to start off by highlighting a couple of changes for this earnings call. For the first time, we are hosting our earnings call from Florence, Italy, where we will host our Board meeting later this week and welcome over 2,000 customers and industry experts next week at our Annual Meeting. We will also be using a presentation during this webcast, which has also been published on our investor website, that we will reference over the course of our prepared remarks.

As you can see on slide 4, we were very pleased to end 2022 with solid momentum across our two business segments. In the fourth quarter, we saw continued margin improvement in our OFSE segment and an extremely strong level of orders for IET, which was driven by multiple awards across different end markets.

2022 was an important year for Baker Hughes on a number of fronts. Strategically, we took a large step forward in re-shaping the company as we announced a formal restructuring and re-segmentation of Baker Hughes into two business segments. This kicked off a major transformation effort across the organization, including key executive management changes, which will fundamentally improve the way the company operates.

Operationally, our performance for the year was mixed. During the first half of the year, we experienced multiple headwinds across our organization, as well as a number of operational challenges. While our performance improved over the second half, we still have more work to do and are focused on various initiatives to improve shorter-term execution and meet the longer-term financial objectives we laid out at an investor conference last September.

Commercially, orders performance in LNG and New Energy hit new highs and are poised to remain strong into 2023. In 2022, we booked almost $3.5 billion in LNG equipment orders, our highest ever, and booked over $400 million in New Energy orders, showing over 50% growth versus 2021.

Although not yet back to previous historical levels, orders for our offshore-exposed businesses also accelerated. Within OFSE, SSPS booked over $3 billion in orders in 2022, representing 36% growth versus 2021. In IET, Onshore/Offshore Production recorded equipment orders of almost $1.9 billion in 2022.

We are also seeing improvements in our industrial segments with Industrial Technology orders of $3.3 billion in 2022, up 6% year-over-year.

As we look ahead to 2023, we expect order momentum to continue across both OFSE and IET despite what is likely to be a mixed macro environment.

Turning to slide 5, in 2023, the global economy is expected to experience some challenges under the weight of inflationary pressures and tightening monetary conditions. Despite recessionary pressures in some of the world's largest economies, we maintain a positive outlook for the energy sector. With years of under investment now being amplified by recent geopolitical factors, global spare capacity for oil and gas has deteriorated and will likely require years of investment growth to meet forecasted future demand.

For this reason, we continue to believe that we are in the early stages of a multi-year upturn in global activity and are poised to see a second consecutive year of solid double-digit increases in global upstream spending in 2023. In addition to strong growth in traditional oil and gas spending, we also believe that the Inflation Reduction Act in the US and potential new legislation in Europe will support significant growth opportunities in New Energy in 2023 and beyond.

We also remain positive on the near term and long-term prospects for the natural gas and LNG investment cycle. Near term, we believe that the likely reopening of China, combined with Europe's need to refill gas storage supplies, will play a critical role in keeping global gas and LNG markets tight. Longer-term, we remain optimistic on the structural growth outlook for natural gas and LNG as the world looks to lower emissions and displace the consumption of coal.

While cost inflation and higher interest rates slowed the pace of new LNG FIDs in 2022, we are seeing progress on a number of fronts. We continue to expect significant growth in new project sanctions in 2023, with elevated activity levels likely continuing into 2024. Following 36 MTPA of LNG FIDs in 2022, we continue to expect to see an additional 65 to 115 MTPA of LNG projects reach FID in 2023.

Just as important as the near-term outlook for LNG orders, we are now gaining visibility into new project opportunities that are developing towards the middle of the decade. Most notably, we are seeing progress on a number of brownfield initiatives and advancements in new modular concepts that is likely to extend the current wave of activity several more years.

Turning to slide 6, given this macro backdrop, Baker Hughes is intensely focused on four key areas in 2023 in order to drive future value for shareholders.

First, we are well positioned to capitalize on the significant growth opportunities that are building across both business segments. These opportunities reach across the entire OFSE portfolio, as well as in IET, most notably in LNG, Onshore/Offshore Production, and New Energy.

Second, we remain focused on optimizing our corporate structure and transforming the Baker Hughes organization to drive improvements in our margin and returns profile. While we are still in the early stages of this process, we are increasingly confident in driving at least $150 million of cost-out by the end of 2023 as well as structural changes that will simplify the organization and enhance our operational efficiency.

The cost-out and integration initiatives we are undertaking over the next 12 to 18 months will play a key role in hitting our EBITDA margin targets of 20% in OFSE and IET over the next two to three years, and delivering Return on Invested Capital of 15% and 20%, for OFSE and IET respectively.

Third, we continue to develop our portfolio of new energy technologies. We have been particularly active over the last few years acquiring and investing in multiple new technologies around hydrogen, carbon capture, clean power, and geothermal. We are now transitioning more towards the incubation of the existing portfolio. This will enable our new energy portfolio to achieve its full commercial potential, with a particular focus on high impact technologies like NET Power and Mosaic.

Finally, we will continue to focus on all these initiatives and while also generating strong free cash flow and returning 60% to 80% of this to shareholders through a combination of share buybacks and dividends.

In 2022, we increased our dividend for the first time since 2017. Going forward, our goal is to continue to increase shareholder returns with an emphasis on continuing to grow the dividend as the IET business experiences broader structural growth in revenue and earnings.

Turning to slide 7, I will provide an update on each of our segments.

In **Oilfield Services and Equipment**, the outlook remains promising with growth trends shifting more in favor of international and offshore markets, while North America activity levels off. Importantly, the team continues to execute well as supply chain pressures moderate and the pricing environment remains favorable.

Geographically, the Middle East retains the most promising outlook with activity scheduled to increase in multiple countries this year and likely next year. In Latin America and West Africa, offshore activity is driving growth in several countries and creating opportunities across our diverse portfolio. In North America, visibility remains limited given the current oil and gas price environment, and generally expect range bound activity from current levels over the course of 2023.

Within our OFSE product lines, we have seen strong growth for Well Construction, driven by opportunities across our drilling portfolio, and for CIM, where our completions portfolio continues to see solid improvement.

In Production Solutions, we saw strong volume growth and margin improvement in our chemicals business throughout the year as supply chain constraints continue to ease and profitability normalizes. For 2023, we expect further improvement in our chemicals business as margin levels normalize back to historical levels and our Singapore plant becomes fully operational.

Our legacy OFS segment executed well in the fourth quarter, and we were pleased to see them achieve 19.6% EBITDA margins, and 20% when normalizing for the impact of Russia.

In SSPS, order activity remains strong as offshore activity continues to pick up. Importantly, we saw good order traction in both subsea trees and Flexibles in the fourth quarter. After a record year in 2022 in Flexibles orders, we expect another strong year in 2023 as well as a significant increase in subsea trees awards.

We also continue to make progress on integrating SSPS into our OFSE segment, as well as restructuring the business to drive better profitability and returns. After a thorough review of the SSPS business, Maria Claudia and her team are finalizing plans to rationalize approximately 40% to 50% of the manufacturing capacity in Subsea Production Systems. These steps will be in addition to the cost savings gained from removing management layers and will largely come into effect in 2024.

For 2023, we expect OFSE to deliver double-digit revenue growth and solid improvement in margins as activity increases in multiple regions, inflationary pressures subside, we execute our cost-out program, and pricing remains favorable in most key markets.

Moving to **IET**, the fourth quarter generated record orders driven by multiple awards in LNG and multiple awards in Onshore/Offshore Production. Operationally, IET continues to navigate challenges in Gas Tech Services, as well as challenges in different parts of the supply chain, ranging from chips and circuit boards to gas engines, castings, and forgings.

Orders during the fourth quarter for Gas Technology illustrate the breadth and depth of its portfolio.

In LNG, we saw continued progress across our world-class franchise. During the quarter, we were pleased to be awarded another major order to provide an LNG system for the second phase of Venture Global's Plaquemines project. This order builds on an award in the third quarter of 2022 for another power island system.

Furthermore, this follows an award in the first quarter of 2022 for the first phase of Plaquemines and a similar contract for VG's Calcasieu Pass terminal in 2019, which are all part of a 70 MTPA master supply agreement.

In Onshore/Offshore Production, IET booked contracts for five different projects in Latin America and Sub-Saharan Africa worth almost $900 million on a combined basis. With these awards, IET maintains its leadership in the FPSO market by providing power generation systems, compression trains and pumps that totals more than 30 aeroderivative gas turbines, two steam turbines and 20 compressors of various sizes.

On the New Energy front, we were pleased to book an order from Malaysia Marine and Heavy Engineering to supply CO_2 compression equipment to PETRONAS' Kasawari offshore carbon capture and sequestration project in Sarawak, Malaysia. The project is expected to be the world's largest offshore CCS facility, with capacity to reduce CO_2 emissions by 3.3 MTPA.

Baker Hughes will deliver two trains of low-pressure booster compressors to enable CO_2 removal through membrane separation technology, as well as two trains for reinjecting the separated CO_2 into a dedicated storage site.

Orders in our Industrial Technology business continue to perform well with strong traction this quarter across Inspection and Pumps, Valves and Gears. In our Inspection business, we achieved significant commercial wins in the recovering aviation industry, including a record deal for visual inspection services in the Latin America region, as well as a number of orders for advanced ultrasonic testing systems with different customers in Asia Pacific.

In addition to solid growth in orders, we were pleased to see some signs of operational improvement in our Industrial Tech businesses, led by volume and margin increases in Condition Monitoring and Inspection. We expect this positive momentum to continue into 2023 as the chip shortage and supply chain issues start to abate and backlog convertibility recovers.

As we enter 2023, IET has a record backlog of $25 billion and a robust pipeline of new order opportunities in LNG, Onshore/Offshore, and New Energy, and we now expect IET orders in 2023 between $10.5 to $11.5 billion. Despite the supply chain challenges we are closely monitoring for both Gas Tech and Industrial Tech, we are well positioned to execute on this backlog to help drive significant revenue growth in 2023 and 2024.

While 2022 presented some unique challenges to Baker Hughes, it was also a pivotal year for us strategically and accelerated a number of changes in the organization. As we look at 2023 and beyond, I feel confident in the structural changes we are executing and our positioning to capitalize on the multi-year upstream spending cycle, the unfolding wave of LNG investment, and the acceleration in New Energy opportunities.

Across our entire enterprise, Baker Hughes is focused on significantly improving our margins and financial returns and meeting our customers' needs in a quickly changing energy landscape. Achieving these goals will require acute focus across the entire organization, as well as the depth and scale of global resources and engineering talent.

The culture of this company is unique in its diversity, its inclusiveness, and its principles, as well as its ability to adapt to change. Our team is focused on taking energy forward, transforming the way we operate, and achieving the margin and return targets we have laid out to help drive best-in-class shareholder value and returns.

With that, I will turn the call over to Nancy.

Nancy Buese *Baker Hughes – CFO*

Thanks, Lorenzo. I will begin on slide 9 with an overview of total company results and then discuss our balance sheet, free cash flow, and capital allocation before then moving into the business segment details and our forward outlook.

Total company orders for the quarter were $8.0 billion, up 32% sequentially driven by Industrial & Energy Technology, up 82% versus the prior quarter. Oilfield Services and Equipment orders were flat sequentially.

Year-over-year, orders were up 20%, driven by an increase in both segments.

We are extremely pleased with the orders performance at IET during the quarter following strong orders throughout 2022. Total company orders for the full year were $26.8 billion, an increase of 24% versus 2021.

Remaining Performance Obligation was $27.8 billion, up 13% sequentially. OFSE RPO ended at $2.6 billion, up 8% sequentially, while IET RPO ended at $25.3 billion, up 13% sequentially.

Our total company book-to-bill ratio in the quarter was 1.4 and IET was 1.8. Total company book-to-bill for the year was 1.3 and IET was 1.6.

Revenue for the quarter was $5.9 billion, up 10% sequentially and up 8% year-over-year, driven by increases in both segments.

Operating income for the quarter was $663 million.

Adjusted operating income was $692 million, which excludes $29 million of restructuring, impairment, and other charges.

Adjusted operating income was up 38% sequentially and up 21% year-over-year. Our adjusted operating income rate for the quarter was 11.7%, up 240 basis points sequentially. Year-over-year, our adjusted operating income rate was up 130 basis points.

Adjusted EBITDA in the quarter was $947 million, up 25% sequentially and up 12% year-over-year. Adjusted EBITDA rate was 16.0%, up 190 basis points sequentially and up 70 basis points year-over-year.

Corporate costs were $100 million in the quarter, driven by the realization of some of our corporate optimization efforts. For the first quarter, we expect corporate costs to be roughly flat compared to fourth quarter levels.

Depreciation and amortization expense was $255 million in the quarter. For the first quarter, we expect D&A to remain flat with fourth quarter levels.

Net interest expense was $64 million.

Income tax expense in the quarter was $157 million.

GAAP earnings per share was $0.18 cents. Included in GAAP earnings per share were unrealized mark-to-market net losses in fair value for our investments in ADNOC Drilling and C3 AI of $89 million and $11 million, respectively. Also included were $81 million of charges related to the termination of the Tax Matters Agreement with General Electric. These are all recorded in other non-operating loss.

Adjusted earnings per share were $0.38 cents.

Turning to slide 10, we maintain a strong balance sheet with total debt of $6.7 billion and net debt of $4.2 billion, which is 1.4 times our trailing 12 months adjusted EBITDA.

We generated free cash flow in the quarter of $657 million, up $239 million sequentially, driven by higher adjusted EBITDA and strong cash collections.

For the first quarter, we expect free cash flow to decline sequentially, primarily driven by seasonality. We will continue to target 50% free cash flow conversion from adjusted EBITDA on a through-cycle basis but expect 2023 to be in the low to mid 40% range.

Turning to slide 11 and capital allocation. We increased our quarterly dividend by one cent to $0.19 per share during the fourth quarter and also repurchased 4.2 million Class A shares for $101 million at an average price of $24 per share. For the full year 2022, we returned a total of $1.6 billion to shareholders.

During the quarter, we closed the recently announced acquisitions of BRUSH Power Generation, Quest Integrity, and AccessESP. The total net cash paid for these three transactions was approximately $650 million. To fund these transactions, we took advantage of our strong balance sheet and used cash on hand.

Baker Hughes remains committed to a flexible capital allocation policy that balances returning cash to shareholders and investing in growth opportunities. Our capital allocation philosophy starts with a priority of maintaining a strong balance sheet and targeting free cash flow conversion from adjusted EBITDA in excess of 50% on a through-cycle basis.

This framework will enable Baker Hughes to return 60% to 80% of our free cash flow back to shareholders. This will also allow us to invest in bolt-on M&A opportunities that can complement the current IET and OFSE portfolios as well as our efforts in New Energy.

As we look to return cash to shareholders, we will prioritize growing our regular dividend given the secular growth opportunities for IET and complementing this with opportunistic share repurchases.

Now I will walk you through the business segment results in more detail and give you our thoughts on the outlook going forward.

Starting with **Oilfield Services and Equipment** on slide 12, orders in the quarter were $3.7 billion, flat sequentially.

Subsea & Surface Pressure System orders were $738 million, up 45% year-over-year driven by an increase in subsea tree awards across multiple regions.

OFSE revenue in the quarter was $3.6 billion, up 5% sequentially, driven by increases across all product lines.

International revenue was up 5% sequentially driven by Latin America up 10% and Middle East/Asia up 7%, offset by Europe/CIS/SSA down 2%. North America revenue increased 5% sequentially. Excluding SSPS, both International and North America revenue were up 5%.

OFSE Operating Income in the quarter was $416 million, up 28% sequentially. Operating income rate was 11.6%, with margin rates increasing 210 basis points sequentially.

OFSE EBITDA in the quarter was $614 million, up 16% sequentially. EBITDA margin rate was 17.1%, with margins increasing 160 basis point sequentially, driven by increased volume and price improvements, partially offset by cost inflation. Year-over-year EBITDA margins were up 160 basis points.

We are really pleased with the margin performance in OFSE, particularly in the legacy OFS segment, which achieved a 19.6% EBITDA margin in the fourth quarter. Legacy OFS EBITDA margins were 20% excluding under-absorbed costs incurred prior to the completion of the sale of OFS Russia to local management in November.

Turning to slide 13, **IET** orders were $4.3 billion, up 20% year-over-year and a record orders quarter for IET. The strong fourth quarter orders performance closed out a great 2022 for IET with $12.7 billion of orders, up 28% year-over-year.

Gas Technology Equipment orders in the quarter were up 36% year-over-year. Gas Tech Equipment orders were supported by the LNG award for the second phase of Venture Global's Plaquemines project, a number of Onshore/Offshore Production awards, and the award for CO2 compression equipment for the Kasawari CCS project.

Gas Tech Services orders in the quarter were down 4% year-over-year, driven by lower contractual services orders, partially offset by an increase in upgrades.

RPO for IET ended at $25.3 billion, up 13% sequentially. Within IET RPO, Gas Tech Equipment RPO was $9.5 billion and Gas Tech Services RPO was $13.6 billion.

Industrial Technology orders were up 6% year-over-year. Pumps, Valves & Gears, Inspection, and PSI & Controls orders were up year-over-year, offset by Condition Monitoring orders, which were down year-over-year.

Turning to slide 14, revenue for the quarter was $2.3 billion, up 1% versus the prior year. Gas Tech Equipment revenue was up 24% year-over-year driven by the execution of project backlog.

Gas Tech Services revenue was down 17% year-over-year driven by lower contractual services and upgrades. This was primarily related to the loss of service revenue from the discontinuation of our Russia operations, foreign exchange movements, supply chain delays and outage pushouts. As we have noted previously, the strength in commodity prices continues to shift maintenance schedules for some of our customers, a dynamic that we believe should normalize over time.

Gas Tech Services also continues to see supply chain delays, largely stemming from delivery delays in aeroderivative gas turbines and associated components. This is an area that we will continue to monitor and manage going forward.

Industrial Technology revenue was flat year-over-year. Condition Monitoring, Inspection and PSI & Controls revenue was up year-over-year, while PVG was down year-over-year.

Operating income for IET was $377 million, down 5% year-over-year. Operating margin was 16.2%, down 110 basis points year-over-year.

IET EBITDA was $429 million, down 4% year-over-year. EBITDA margin rate was 18.4%, down 110 basis points year-over-year, with higher equipment mix, cost inflation, and higher R&D spend partially offset by higher pricing and slightly higher volume. As we increasingly execute on our record Gas Tech equipment backlog, we are seeing a meaningful shift in the mix of our revenue profile, with equipment revenue representing 55% of total revenue in the quarter versus 45% a year ago.

Turning to slide 15, I would like to update you on our outlook for the two business segments and our cost-out program.

With new reporting segments, we are providing a formal outlook in order to give another level of transparency for each business segment, as well as further details around our forward-looking expectations. As we transition to this new framework, we are providing a range of expectations and also highlight the variables that drive the different potential outcomes.

Overall, we feel optimistic on the outlook for both OFSE and IET with solid growth tailwinds across our business, as well as continued operational enhancements to help drive margin improvement. In addition to executing on the growing pipeline of commercial opportunities, a key focus for Baker Hughes in 2023 is transforming our organization through at least $150 million of annualized cost-out by the end of this year. All necessary actions to achieve this target should be completed by the end of the second quarter and the full impact will be realized by the end of the fourth quarter.

For Baker Hughes, we expect first quarter revenue between $5.3 and $5.7 billion and Adjusted EBITDA between $700 and $760 million. For the full year, we expect revenue between $24 and $26 billion and Adjusted EBITDA between $3.6 and $3.8 billion.

For OFSE, we expect first quarter results to reflect usual seasonal declines in International activity, as well as typical seasonality in North America. We therefore expect first quarter revenue for OFSE between $3.3 and $3.5 billion and EBITDA between $515 and $585 million.

Factors driving this range include the magnitude of seasonality in some international markets, timing of budget deployments in the US, backlog conversion in SSPS, and the pace of our cost-out initiatives.

For the full year 2023, we expect another strong year of market growth internationally, spread across virtually all geographic regions led by the Middle East, Latin America, and West Africa. Overall, we expect international D&C spending to likely increase in the middle-double digits on a year-over-year basis.

In North America, we expect activity levels to likely remain range-bound for the balance of the year depending on oil and natural gas prices and activity levels among private operators. However, we believe that this level of activity, as well as cost inflation, will still translate into North America D&C spending growth in the mid to high double-digits in 2023.

Given this macro backdrop, we would expect OFSE revenue between $14.5 and $15.5 billion and EBITDA between $2.4 and $2.8 billion in 2023. Factors driving this range include the pace of growth in various international markets, a range of potential outcomes in North America activity, continued improvement in Chemicals, the pace of backlog conversion and cost-out initiatives in the SSPS segment, and our broader cost-out initiatives.

For IET, we expect strong revenue growth on a year-over-year basis supported by backlog conversion at Gas Tech Equipment and modest growth in Industrial Technology. We therefore expect first quarter IET revenue between $1.9 and $2.4 billion and EBITDA between $250 and $300 million.

The major factors driving this revenue range will be the pace of backlog conversion for Gas Tech Equipment, growth in Industrial Tech driven by improving supply chain dynamics, and the impact of any continued deferrals in maintenance activity or supply chain delays at Gas Tech Services.

For the full year, as Lorenzo mentioned, we now expect IET orders to be between $10.5 and $11.5 billion, driven by LNG and Onshore/Offshore production.

We forecast full year IET revenue between $9.5 and $10.5 billion and EBITDA between $1.35 and $1.65 billion. The largest factor driving this range will be the pace of backlog conversion for Gas Tech Equipment and any impacts associated with supply chain delays.

Other factors that drive this range include foreign currency movements, the pace of improvement in supply chain impacts at Industrial Tech, the level of R&D spend related to our new energy investments, and the timing of maintenance activity in Gas Tech Services.

With that, I will turn the call back over to Lorenzo.

Lorenzo Simonelli *Baker Hughes – Chairman & CEO*

Thank you, Nancy. Turning to slide 16, Baker Hughes is committed to delivering for our customers and our shareholders. We remain focused on capitalizing on the growth opportunities across OFSE and IET, including LNG and New Energy, where we are increasing R&D to develop our technology portfolio in hydrogen, carbon capture and clean power.

We also remain committed to optimizing our corporate structure to enhance
our margin and return profile, where we are targeting EBITDA margins of 20% in OFSE & IET and increasing ROIC in both businesses to 15% and 20% respectively.

And finally, we will continue to focus on generating strong free cash flow and returning 60 to 80% of this free cash flow to shareholders, while also investing for growth across our world class business.

With that, I will turn it back over to Jud.

Jud Bailey *Baker Hughes – VP of Investor Relations*

Thanks, Lorenzo.

Operator, let's open the call for questions.