First Quarter 2021 – Earnings Conference Call Prepared Remarks

Jud Bailey *Baker Hughes – VP of Investor Relations*

Thank you.

Good morning everyone, and welcome to the Baker Hughes First Quarter 2021 Earnings Conference Call. Here with me are our Chairman and CEO, Lorenzo Simonelli; and our CFO, Brian Worrell. 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 some 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.

We are pleased with our first quarter results as we generated strong free cash flow, continued to drive forward our cost-out efforts, and took further meaningful steps in the execution of our strategy to lead the energy transition. During the quarter, TPS delivered solid orders and operating income while OFS continued to execute our cost-out program to help drive another strong quarter of margin performance.

As we look ahead to the rest of 2021, we remain cautiously optimistic that the global economy and oil demand will recover from the impact of the global pandemic. As vaccine rollouts ramp up around the world, we expect rising oil and gas demand combined with continued discipline from OPEC plus and publicly-traded operators to re-balance inventories. This should be supportive of higher oil prices and solid free cash flow across the industry.

Following a resilient 2020, the natural gas and LNG markets' longer-term demand outlook appears increasingly positive. We anticipate future demand improving as governments around the world accelerate the transition towards cleaner sources of energy.

Accordingly, we see potential upside to our 2030 LNG demand view, which previously called for 550 to 600 MTPA of demand by the end of the decade. Based on recent third-party analysis, and directionally supported by discussions with some of our customers, we now see the potential for 600 to 650 MTPA of global LNG demand by 2030.

Outside of oil and gas, the focus on cleaner energy sources and technology to decarbonize resource-intensive industries continues to accelerate. The US is more closely aligning with Europe and other developed nations in steering government policy to incentivize clean energy sources as well as carbon capture technologies. We believe that these policy shifts will be crucial to supporting new industry-wide investment in areas like renewables, green hydrogen, and CCUS.

With this overall macro view in mind, we continue to believe that we are taking the right steps with our strategic priorities to position Baker Hughes as the leader in the energy transition.
We have had a busy start to 2021, making solid progress on all three pillars of our strategy.

On the first pillar to transform the core of the business, we continue to identify and remove structural costs from our operations, as evidenced by the improvement in our OFS margins despite lower revenue. Our goal is to continue to optimize our processes and infrastructure in order to deliver further cost reductions and footprint consolidation in 2021.

In addition to cost-out actions, we continue to focus on portfolio optimization to narrow our focus, streamline operations, and improve overall operating efficiency.

As an example, during the first quarter we announced an agreement with Akastor to create a joint venture company in which we will contribute our Subsea Drilling Systems product line with Akastor's MHWirth business. This transaction helps align our portfolio with our long-term strategic objectives. Additionally, we completed the sale of pressure pumping assets in Argentina, which includes a hydraulic fracturing fleet, coiled tubing unit, and related equipment.

On the second pillar of investing for growth, we continue to identify opportunities to expand in the industrial sector and increase our condition monitoring and asset management offerings. To that end, in the first quarter we announced the acquisition of ARMS Reliability, an asset reliability services and software company with a strong presence across a broad range of industrial sectors, including metals and mining, power, manufacturing, and utilities. The acquisition enables our Bently Nevada business to expand further into asset performance management, and to scale the ARMS Reliability technology utilizing our global footprint. This transaction further reinforces our commitment to accelerate the digital transformation of industrial assets across an ever-increasing range of end-markets.

On the third pillar of positioning for new frontiers, we took steps to build out our energy transition offerings. We announced an exclusive license for SRI International's mixed salt process for carbon capture. The mixed salt technology enables significant cost reductions through a more energy efficient and environmentally friendly carbon capture process. This provides total cost of ownership savings for energy and industrial operators to decarbonize their operations. The mixed salt process adds to our portfolio of capture technology development, which also includes the commercially available chilled ammonia process and an amines-based process through our Compact Carbon Capture acquisition last year.

Additionally, we recently announced our intention to invest in the FiveT hydrogen fund alongside other cornerstone investors, Plug Power and Chart Industries. This fund, which is targeting an ultimate size of approximately €1 billion, is designed to accelerate the infrastructure and technology investment necessary to develop the hydrogen value chain.

We have also made progress commercially on our energy transition efforts, building a diverse portfolio of offerings, supported by scale and technology development.

In the first quarter we signed an MOU with Horisont Energi for the Polaris carbon storage project off the northern coast of Norway. Under the agreement, we will explore the development and integration of technologies to minimize the carbon footprint, cost, and delivery time of the project. This is a great example of what the unique Baker Hughes portfolio can bring to customers. OFS will bring technology and services to drill and complete the injection wells; OFE will supply subsea trees, controls systems and injection risers; TPS will supply compression equipment for CO2 injection; and DS will provide monitoring solutions.

As we continue to execute on these three strategic pillars and our evolution as an energy technology company, we will maintain our discipline and prioritize free cash flow and returns above our cost of capital.

Now, I will give you an update on each of our segments.

In **Oilfield Services**, activity has increased solidly in select areas so far this year. The strong commodity price performance has resulted in positive signs for further improvement across multiple regions over the course of 2021.

In the international markets, we have greater confidence in our outlook for the second half as customer conversations and project opportunities are firming up in key markets such as the Middle East, Latin America, and Russia. Based on discussions with our customers, we still expect a recovery in international activity to be second half weighted, which should provide strong momentum for growth in 2022.

In North America, stronger than expected activity in the first quarter helped us to mitigate some of the impacts from the Texas winter storms and also provides some upside potential for the full year versus our prior expectations. Although the rig count is moving higher, we believe that the commitment towards capital discipline and maintenance-mode spending remains intact among the public E&Ps.

While we are pleased to see the outlook for OFS is improving somewhat faster than we anticipated, our primary focus remains on increasing the margin and return profile of this business through improved efficiency and portfolio actions. We continue to execute on our plan to reduce our rooftops by approximately 100 facilities in 2021 and size our product lines appropriately for the current environment.

Overall, we believe that OFS remains on track to achieve double digit operating income margins given the significant structural cost reductions we have made, improved operating processes, and the increasing use of remote operations.

Moving to **TPS**, we continue to balance our focus between new energy initiatives and current core operations like LNG, high technology compression applications, pumps and valves, and aftermarket services.

As I mentioned earlier, our long-term outlook for demand growth in the LNG market is improving. The resilience of demand during the pandemic combined with the acceleration of climate commitments has resulted in improving optimism over the demand outlook. This has also been reflected in our conversations with customers. As more nations, such as China, make net zero commitments, it is becoming increasingly clear that a phase out of coal in favor of natural gas is necessary to reach their goals, as well as broader global carbon targets.

Based on this outlook, we feel increasingly confident in our expectation of 3 to 4 projects reaching FID in 2021, followed by a strong pipeline of opportunities in 2022 and beyond.

For the non-LNG segments of our TPS portfolio, order activity remains solid with a positive outlook. During the first quarter, we booked awards for power generation and compression equipment for multiple FPSOs in Latin America and for a fixed platform in Asia.

For TPS Services, we are optimistic about the outlook for recovery in 2021 and 2022 as customers resume spending to maintain and, in some cases, upgrade their equipment. We expect growth to be led by a recovery in transactional services and upgrades, areas that were particularly impacted in 2020.

In our contractual services business, we were pleased to receive a ten-year contract extension to the existing global service contract with the PETRONAS Malaysia LNG project, one of the largest LNG facilities in the world. This contract is an extension of the 40-year partnership between the TPS team and PETRONAS Malaysia LNG. The relationship has included key technology injections that have helped the customer increase production capacity by reducing machine downtime and saving cost with extended mean-time between maintenance.

On a longer-term basis, we are optimistic on the outlook for upgrade opportunities as customers seek to reduce carbon emissions and improve the efficiency of their equipment. As an example, in the first quarter we announced a cooperation agreement with PAO NOVATEK to upgrade existing liquefaction trains at Yamal LNG to run on hydrogen blends, supporting their emissions reduction efforts. Together with NOVATEK, we are introducing the first solution for decarbonizing the core of LNG production, an area we expect to grow meaningfully in the future.

Next, on **Oilfield Equipment**, we continue to focus on right-sizing the business and optimizing the portfolio in the face of a challenging offshore market environment.

With Brent prices moving into the $60s and a more optimistic view for oil demand over the next few years, we continue to see the outlook for industry subsea tree awards improving modestly in 2021, though still well below 2019 levels. Longer term, we believe that deepwater activity will be increasingly dominated by low cost basins and that it will be difficult to sustain 2019 industry order levels for the foreseeable future.

As I mentioned, in the first quarter we announced an agreement with Akastor to create a 50-50 joint venture company to deliver global offshore drilling solutions, through the combination of our SDS business with Akastor's MHWirth business. This transaction will result in a leading equipment and services provider with integrated delivery capabilities, financial strength, a focused and experienced management team, and the flexibility to address a full range of customer priorities.

Finally, in **Digital Solutions**, although our operating results were below our initial expectations, we experienced a strong recovery in orders in the first quarter. This was primarily led by industrial end-markets as the global economy began to recover.

In the first quarter, we were awarded several projects that demonstrate our capabilities in emissions reduction solutions, as well as our growing industrial presence.

The Panametrics product line secured several orders for the Flare.IQ advanced flare gas monitoring and optimization system, with contracts for oil and gas operators in North America, China and the U.A.E. We signed a new agreement with a customer in the U.A.E. to pilot our Flare.IQ technology, marking the first deployment of Flare.IQ in the Gulf region. Our technology will enable the customer to reduce methane emissions from flare operations and reduce its operational costs at the pilot sites by delivering high-efficiency flare combustion.

We were also pleased to secure an important award with a major aircraft engine OEM to utilize our Druck technology to improve fuel efficiency performance, displacing a competitor. Druck's Dual Channel Pressure Sensors technology will enable the customer to deliver improved fuel efficiency and reliability performance.

In our Waygate Technologies business, we were awarded several orders from LG Energy Solution to support electric vehicle battery cell inspection across facilities in Asia and Europe.

Overall, we executed well in the first quarter, delivering strong free cash flow and making significant progress on our strategic priorities.

With a broad portfolio and a strategic focus on the rapidly changing energy market, Baker Hughes is well positioned to take advantage of a recovery in the global economy and the oil and gas markets near-term. Longer-term, we are well positioned for growth as we develop decarbonization solutions across multiple industries. We remain focused on driving better outcomes for customers, executing on our strategy, and delivering for our shareholders.

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

Brian Worrell *Baker Hughes – CFO*

Thanks, Lorenzo. I will begin with the total company results and then move into the segment details.

Orders for the quarter were $4.5 billion, down 12% sequentially driven by OFE and TPS, partially offset by an increase in Digital Solutions. Year-over-year, orders were down 18%, driven by declines in OFS and OFE, partially offset by increases in Digital Solutions and TPS.

Remaining Performance Obligation was $23.2 billion, down 1% sequentially. Equipment RPO ended at $7.5 billion, down 6% sequentially and services RPO ended at $15.7 billion, up 2% sequentially. Our total company book-to-bill ratio in the quarter was 0.9 and our equipment book-to-bill in the quarter was 0.8.

Revenue for the quarter was $4.8 billion, down 13% sequentially, with declines in all four segments. Year-over-year, revenue was down 12%, driven by declines in OFS, OFE, and Digital Solutions, partially offset by an increase in TPS.

Operating income for the quarter was $164 million. Adjusted operating income was $270 million, which excludes $106 million of restructuring, separation, and other charges. The restructuring charges in the first quarter relate to projects previously announced in 2020. Adjusted operating income was down 42% sequentially and up 13% year-over-year. Our adjusted operating income rate for the quarter was 5.6%, down 280 basis points sequentially. Year-over-year, our adjusted operating income rate was up 120 basis points. We are pleased with the operating margin improvement on a year-over-year basis, which was largely driven by strong execution on our restructuring actions and continued improvements in operating productivity.

Adjusted EBITDA in the quarter was $562 million, which excludes $106 million of restructuring, separation, and other charges. Adjusted EBITDA was down 27% sequentially and down 5% year-over-year. This quarter we began disclosing total company adjusted EBITDA in our earnings release as well as EBITDA by reporting segment. In conjunction with this new disclosure, we filed an 8-K this morning that provides three years of history by quarter for both total company and reporting segment EBITDA.

Corporate costs were $109 million in the quarter. For the second quarter, we expect corporate costs to be flat to slightly down compared to first quarter levels from continued cost-out efforts. Depreciation and amortization expense was $292 million in the quarter. For the second quarter, we expect D&A to be roughly flat sequentially and to gradually decline in the second half of the year.

Net interest expense was $74 million. Income tax expense in the quarter was $69 million.

GAAP loss per share was $0.61 cents. Included in GAAP loss per share is a $788 million loss from the change in fair value of our investment in C3.ai, partially offset by the reversal of current accruals of $121 million due to the settlement of certain legal matters. Adjusted earnings per share were $0.12 cents.

Turning to the cash flow statement, free cash flow in the quarter was $498 million. Free cash flow for the first quarter includes $108 million of cash payments related to restructuring and separation activities. We are particularly pleased with our free cash flow performance in the quarter. The sequential improvement was largely driven by working capital and a lower level of cash restructuring and separation payments.

For the second quarter, we expect free cash flow to decline sequentially primarily due to less favorable working capital trends. For the total year, we still expect free cash flow to improve significantly versus 2020 and to be in-line with or better than historical levels. The drivers for free cash flow versus 2020 will be higher operating income, modestly lower capex, and significantly lower restructuring and separation cash payments.

Lastly, as Lorenzo mentioned, in the first quarter we reached an agreement with Akastor to create a joint venture company that will bring together our Subsea Drilling Systems product line and Akastor's wholly owned subsidiary, MHWirth. We expect the transaction to close in the second half of the year, subject to customary closing conditions. This transaction reflects our continued focus on optimizing our portfolio.

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

In **Oilfield Services**, the team delivered a strong quarter in a mixed market environment.
OFS revenue in the quarter was $2.2 billion, down 4% sequentially. International revenue was down 5% sequentially led by declines in Russia and the Middle East. North America revenue increased 1% sequentially with solid growth in our North America land well construction businesses, offset by declines in the Gulf of Mexico and chemicals. For the first quarter, our production-related businesses accounted for over 60% of our total North America revenue.

Despite the 4% decline in revenue, operating income of $143 million grew 1% sequentially while margin rate expanded 30 basis points to 6.5%. The improvement in margin rate was driven by our restructuring and cost-out initiatives.

The OFS team executed very well on robust cost-out programs over the last year under difficult market conditions. Despite a 30% decline in OFS revenue versus the first quarter of 2020, EBITDA margin rate for OFS was up 110 basis points year-over-year to 15.6%.

As we look ahead to the second quarter, we expect to see a seasonal increase in international activity, which should be followed by a stronger cyclical recovery over the second half of the year. As a result, we expect our second quarter international revenue to increase in the mid-single digit range on a sequential basis.

In North America, we expect the recent momentum in drilling and completion activity in the US land segment to continue. As a result, we expect growth in North American OFS revenues to be in the mid- to high-single digit range.

We expect solid and steady margin rate improvement through the year as volumes improve and our cost reduction efforts yield further results.

For the full year 2021, our industry outlook has modestly improved from what we shared on our fourth quarter earnings call.

Internationally, we still expect a second half recovery in activity with positive signs developing from multiple customers. However, without clear visibility on some of these incremental opportunities, we expect our international revenue to be down in the mid-single-digit range on a year-over-year basis.

In North America, the recent increase in commodity prices and strong recovery from private E&Ps have improved the near-term outlook. As activity recovers, we believe that drilling and completion activity is likely to be modestly higher on a year-over-year basis. We expect our North American revenue to lag overall industry spending and rig count trends given our portfolio mix and the exit of several commoditized businesses last year.

Although commodity prices have increased and signals around customer spending and rig count are moving in a positive direction, I want to reiterate that we will not be chasing revenue. We remain focused on pursuing projects that are accretive to margins and returns. Given these dynamics, OFS revenue may be down modestly for the full year, but we expect our cost-out actions to translate to a strong improvement in OFS margins in 2021.

Moving to **Oilfield Equipment**, orders in the quarter were $345 million, down 30% year-over-year, and down 39% sequentially.

Revenue was $628 million, down 12% year-over-year, primarily driven by declines in Subsea Services, Subsea Drilling Systems, and the disposition of SPC Flow, partially offset by growth in SPS and Flexibles.

Operating income was $4 million, which is up $12 million year-over-year. This was driven by higher volume in SPS and Flexibles along with help from our cost-out program, partially offset by softness in services activity and Subsea Drilling Systems.

For the second quarter, we expect revenue to decrease sequentially driven by lower SPS and Flexibles backlog conversion. We expect operating income to remain close to first quarter levels.

For the full year 2021, we expect the offshore markets to remain challenged as operators re-assess their portfolios and project selection. We expect OFE revenue to be down double digits on a year-over-year basis due to the lower order intake in 2020 and a likely continuation of a difficult offshore environment in 2021.

Although revenue will be down in 2021, our goal remains to generate positive operating income as our cost out efforts should offset the decline in volumes.

Next, I will cover **Turbomachinery**. The team delivered another strong quarter with solid execution.

Orders in the quarter were $1.4 billion, up 4% year-over-year. Equipment orders were up 28% year-over-year. Orders this quarter were supported by awards for power generation and compression equipment for multiple FPSOs in Latin America and for a fixed platform in Asia.
Service orders in the quarter were down 9% year-over-year, primarily driven by declines in transactional services and contractual services.

Revenue for the quarter was $1.5 billion, up 37% versus the prior year. Equipment revenue was up over 100% as we continue to execute on our LNG and Onshore / Offshore production backlog. Services revenue was up 6% versus the prior year.

Operating income for TPS was $207 million, up 55% year-over-year, driven by higher volume and strong execution on cost productivity, partially offset by a higher equipment mix. Operating margin was 13.9%, up 160 basis points year-over-year. We were very pleased with the margin rate improvement year-over-year, particularly given the change in equipment revenue mix from 32% to 47%.

For the second quarter, we expect revenue to be roughly flat sequentially based on expected equipment backlog conversion. With this revenue outlook, we expect TPS margin rates to be roughly flat versus the second quarter of 2020 due to a higher mix of equipment revenue and an increase in technology spending.

For the full year 2021, we expect TPS to generate double-digit year-over-year revenue growth, driven by equipment backlog conversion and modest growth in TPS Services. We expect the higher mix of equipment revenue to result in roughly flat margin rates year-over-year. However, we still anticipate solid growth in operating income based on higher volumes and improved cost productivity.

Finally, in **Digital Solutions**, orders for the quarter were $549 million, up 10% year-over-year. We saw growth in orders across oil & gas and most industrial end-markets, while aviation remains a challenge. Sequentially, orders were up 4% driven by the improving global economic environment.

Revenue for the quarter was $470 million, down 4% year-over-year primarily driven by lower volumes in Nexus Controls, Process & Pipeline Services, and Waygate Technologies. Sequentially, revenue was down 15% due to a lower opening backlog driven by reduced order intake in 2020, as well as typical seasonality.

Operating income for the quarter was $24 million, down 17% year-over-year driven by lower volume, partially offset by cost productivity. Sequentially, operating income was down 68% driven by lower volume.

For the second quarter, we expect to see strong sequential revenue growth and operating margin rates back into the high single digits.

For the full year 2021, we expect modest growth in revenue on a year-over-year basis, primarily driven by a recovery in industrial end-markets. With higher volumes and a continued focus on cost, we believe DS margin rates can get back to low double digits for the full year.

Overall, we delivered a strong quarter in TPS and OFS, along with exceptionally strong free cash flow. While we faced volume challenges in our OFE and DS businesses, we are confident in our ability to execute as the rest of the year unfolds.

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

Jud Bailey *Baker Hughes – VP of Investor Relations*

Thanks, Brian. Operator, let's open the call for questions.