Second 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 Second Quarter 2022 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 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.

Our second quarter results were mixed as each product company navigated a different set of challenges ranging from component shortages and supply chain inflation to the suspension of our Russian operations. While OFS and TPS are managing through the current situation fairly well, OFE and DS have both experienced more difficulty.

As we look to the second half of 2022 and into 2023, the oil markets face an unusual set of circumstances and challenges. On one hand, the demand outlook for the next 12 to 18 months is deteriorating, as inflation erodes consumer purchasing power and central banks aggressively raise interest rates to combat inflation. On the other hand, due to years of underinvestment globally and the potential need to replace Russian barrels, broader supply constraints can realistically keep commodity prices at elevated levels, even in a scenario of moderate demand destruction.

As a result, we believe the outlook for oil prices remains volatile, but still supportive of relatively strong activity levels as higher spending is required to re-order the global energy map and likely offsets moderate demand destruction in most recessionary scenarios.

In the natural gas market, the re-drawing of the energy map is having an even greater impact, with sustained high prices, a frenzy of offtake contracting activity, and a growing pipeline of major LNG projects that seem likely to reach FID. There has been a significant increase in long-term LNG offtake agreements in the US, totaling over 35 MTPA during the first half of 2022. For comparison, year-to-date LNG contracting activity is three times greater than the average annual US contracting volume going back to 2015.

This sharp increase reflects the growing importance of natural gas and LNG as governments re-balance their priorities between sustainability, security, and affordability. We believe that solving this energy trilemma will be another long-term positive for natural gas. This theme will continue to grow in importance as countries around the world face acute energy shortages and are working to avoid industrial interruptions in certain sectors of their economies.

Overall, we remain very positive on the outlook for natural gas. We also believe that a significant increase in natural gas and LNG infrastructure investment is required over the next five to ten years in order to make natural gas a more affordable and reliable baseload fuel source that can be paired with intermittent renewable power sources.

Against this uncertain macro backdrop, Baker Hughes is preparing for all scenarios and will continue to execute on our long-term strategy. If commodity prices remain resilient as we expect, our portfolio is well positioned to benefit from a strong LNG cycle and a multi-year upstream spending cycle. We will also continue to invest in our energy transition and industrial initiatives, while also returning 60 to 80% of free cash flow to shareholders.

However, if the global economy experiences further turbulence and commodity price volatility, we believe our balanced portfolio of short and long cycle businesses will enable us to generate peer-leading free cash flow and allow us to maintain our policy of returning cash to shareholders. In addition to a strong backlog that affords cash flow visibility, we have a best-in-class balance sheet that allows us to invest opportunistically, either through share buybacks or tuck-in investment opportunities. In either scenario, Baker Hughes is well positioned to create value for shareholders.

From an operational and strategic perspective, we were active over the first half of the year, executing on a number of exciting tuck-in acquisitions and new energy investments such as Mosaic, Net Power, and HIF Global, which position us in key technologies for the future. We have also been focused on setting up internal commercial structures like CTS and IAM, which will help us to capitalize on opportunities in the energy transition and industrial areas.

In addition to these initiatives, our time is increasingly focused on optimizing and formalizing our operations around the two core business areas of OFSE and IET. As the energy markets continue to evolve, it is becoming clearer that aligning across these two core areas makes strategic sense. We are focusing on ways to simplify our process and systems, with a distinct focus on productivity and efficiency across our operations, as we look to drive additional synergies between both TPS and DS, and OFS and OFE. We believe that this will be a significant area of opportunity for Baker Hughes, as we look to further streamline our organization and position it for the future.

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

In **Oilfield Services**, activity levels continue to trend positively in both the international and North American markets and net pricing is being achieved across multiple product lines. We also see improving visibility for growth in some key areas into 2023 and beyond.

In international markets, broad diversified growth continues, with recent strength in Latin America, West Africa and the Middle East. We expect growth in most international markets to continue, with the strongest increases likely to come from the Middle East over the second half of the year and into 2023. Producers in the region are committed to an orderly increase in production and are beginning to execute drilling plans to improve both oil and natural gas production capacity in the region.

In North America, activity and pricing remains strong, with the rig count continuing to track above our expectations. We expect continued modest growth in rig count in the coming months, but the outlook for 2023 will be dependent on broader macro factors and oil prices.

Operationally, I am pleased overall with the progress made by the OFS team during the second quarter in navigating the challenges related to Russia, as well as supply chain constraints and inflation. During the second quarter, the suspension of our OFS operations in Russia accelerated quicker than anticipated as we moved closer to reaching an agreement to sell our OFS operations in the country.

Outside of the impacts from Russia, our OFS business executed well in the second quarter, with improvements in our production chemicals business. After being weighed down for several consecutive quarters by supply chain and inflationary impacts, chemicals saw a sequential increase in margins and has a line of sight to further increases in the coming quarters.

Going forward, we expect to continue to drive margin improvement despite the cost headwinds from the suspension of our operations in Russia.

Moving to **TPS**, the second quarter represented another solid performance in orders, where we remain on track to generate $8 to $9 billion in orders in 2022 with an optimistic view of 2023. Operationally, TPS performed well despite some revenue impacts from the suspension of operations in Russia, as well as some project shipment delays across both equipment and services.

We continue to believe that we are at the beginning of another constructive LNG cycle, particularly for US projects. Including the FID of VG's Plaquemines Phase 1 at the end of May and Cheniere's FID of Corpus Christi Stage 3 in June, we continue to expect 100 to 150 MTPA of LNG FIDs over the next two years with additional FIDs in 2024 and 2025.

During the second quarter, we were pleased to be awarded an order to provide seven mid-scale LNG trains to support the Stage 3 expansion project of Cheniere's Corpus Christi Liquefaction facility. Each train is comprised of two electric motor-driven compressors producing approximately 1.5 MTPA of LNG, totaling 10.5 MTPA of production capacity. This award builds on the strong relationship between Baker Hughes and Cheniere since 2012, as we currently provide all liquefaction equipment for Cheniere's Corpus Christi and Sabine Pass projects.

Outside of LNG, the TPS team booked an important gas processing award in Saudi Arabia to supply 14 electric motor-driven compressors for the Jafurah unconventional gas field project, the largest non-associated gas field in the country. Baker Hughes is leveraging its local compressor packaging facility in Modon to deliver the equipment and support the Kingdom's in-country total value add program.

Also, during the quarter, TPS booked an award from Tellurian to provide electric-powered Integrated Compressor Line technology and turbomachinery equipment for a natural gas transmission project in southwest Louisiana. The project is expected to supply upwards of 5.5 billion cubic feet of natural gas daily, with virtually no emissions.

ICL zero-emissions is landmark technology that lowers the carbon footprint of a key segment of the natural gas supply chain and is already reducing the climate footprint of pipeline projects in many regions that deliver vital gas supplies. This order marks the first time Baker Hughes will install its ICL decarbonization technology for pipeline compression in North America.

During the quarter, TPS' CTS organization continued to support the growth of the hydrogen economy. TPS secured a contract with Air Products to supply advanced syngas and ammonia compression technology for the production of green ammonia for the NEOM carbon-free hydrogen and ammonia facility in Saudi Arabia. This order builds on our hydrogen collaboration framework with Air Products and leverages Baker Hughes' broad experience and references in supplying syngas and ammonia compressors.

Next, on **Oilfield Equipment**, we are encouraged to see improving demand trends across the different business areas. However, we remain disappointed with the overall level of profitability of the business and are executing on further actions to drive additional cost out and improve operations across the portfolio.

At a macro level, trends in the subsea and offshore markets continue to improve and should have solid order momentum over the next couple of years. Despite recent commodity price volatility, we believe that a solid pipeline of deepwater opportunities will continue to develop across a few key markets.

Importantly, we continue to see OFE gain momentum outside of Brazil with its offshore flexible pipe technology, securing several large contracts with multiple customers across the Americas and the Middle East. OFE will provide flexible pipe systems and services, including risers, flowlines and jumpers, to improve oil recovery and help to extend field life and profitability. OFE booked their highest orders ever in flexibles in the second quarter, and over $600 million in flexibles orders for the first half of the year in 2022, also a record.

While activity and project awards are improving offshore, we recognize that we have work to do in OFE to drive operating margins back to an acceptable level. We are driving continued actions across the business to improve operations, while also ensuring we have the appropriate resources in place to take this business forward. We are also in the final stages of planning more integration between OFE and OFS, driving more efficient cost management across certain parts of the OFSE business area globally.

Finally, in **Digital Solutions**, while order activity was strong in the second quarter, the business continues to be hampered by supply chain challenges, mainly electronic shortages, as well as inflationary pressures.

During the quarter, DS saw continued interest for its condition monitoring systems and services in the industrial sector. Bently Nevada secured a contract to upgrade the machinery protection systems for critical machines at a steel plant in the Middle East. The contract includes Bently Nevada's latest Orbit 60 system, which will provide the customer reliable protection and will enable advanced condition monitoring without additional hardware spend.

DS also gained traction with its emissions management portfolio of technologies. Following an MOU signed in February, DS secured a contract with Petrosafe for the first deployment of flare.IQ technology for refining operations in Egypt. The deployment will be implemented at the APC Refinery in Alexandria, supporting Egypt's low-carbon strategy, and tackling emissions in the sector as the country prepares to host COP27 in November.

We also recently reached an agreement for the sale of our Nexus Controls product line to General Electric. GE will continue to provide Baker Hughes with GE's Mark control products currently in the Nexus Controls portfolio, and Baker Hughes will be the exclusive supplier and service provider of such GE products for its oil and gas customers' control needs. The transaction is expected to close in the second quarter of 2023.

As we have mentioned in the past, we continue to make strategic and operational changes across DS, including recent leadership changes in Bently Nevada during the quarter. We are also conducting a review of the broader DS portfolio, taking actions to ensure we have the right business composition to serve our customers and drive returns. As we move forward, there is clearly more work to do. We are committed to driving better performance, profitability and returns for the DS business.

Before I turn the call over to Brian, I would like to spend a few moments highlighting some of the achievements from our Corporate Responsibility Report that was published at the end of the second quarter. This report provides an expanded view of our environmental, social, and governance performance and outlines our corporate strategy and commitments for a sustainable energy future.

We again lowered our emissions footprint and expanded our emissions reporting. We achieved an 8% reduction in our Scope 1 and 2 carbon emissions in 2021 versus 2020, and a 23% reduction in 2021 compared to our 2019 baseline. We also expanded reporting of Scope 3 emissions across our value chain to include emissions from several new categories. I am also pleased to say that in 2021, we launched "Carbon Out," an internal company-wide initiative to take carbon out of our operations and meet our pledge to achieve a 50% reduction in emissions by 2030 and net-zero emissions by 2050.

We further expanded our programs and processes to embed Diversity, Equity, and Inclusion into our operating process. We launched a Global Council in 2021 to increase accountability on this strategic priority, and we updated our process to evaluate and reconcile pay equity across the company.

Overall, Baker Hughes is successfully executing on its vision as an energy technology company and to take energy forward – making it safer, cleaner, and more efficient for people and the planet. Our Corporate Responsibility Report demonstrates our progress in many of these areas.

Baker Hughes is well positioned to drive energy efficiency gains to meet global energy demand and support broader decarbonization objectives.

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 $5.9 billion, down 14% sequentially driven by TPS and OFE, partially offset by an increase in Digital Solutions and OFS.

Year-over-year, orders were up 15%, driven by increases across all four segments.

We are pleased with the orders performance in the quarter, following strong orders performance in the last two quarters.

Remaining Performance Obligation was $24.3 billion, down 6% sequentially. Equipment RPO ended at $8.8 billion, down 11% sequentially and services RPO ended at $15.5 billion, down 3% sequentially. The decrease in the RPO was driven by the suspension of our operations in Russia and foreign currency exchange movements.

Our total company book-to-bill ratio in the quarter was 1.2 and our equipment book-to-bill in the quarter was 1.2.

Revenue for the quarter was $5.0 billion, up 4% sequentially, driven by Digital Solutions, OFS, and OFE, partially offset by lower TPS volumes.

Year-over-year, revenue was down 2%, driven by decreases in OFE and TPS, partially offset by increases in OFS and Digital Solutions.

Operating loss for the quarter was $25 million.

Adjusted operating income was $376 million, which excludes $402 million of restructuring, impairment, separation, and other charges. Included in these charges was $365 million related to the suspension of our operations in Russia. As I will explain in a moment, our Russian activities were either prohibited under applicable sanctions or unsustainable in the current environment.

Adjusted operating income was up 8% sequentially and up 13% year-over-year. Our adjusted operating income rate for the quarter was 7.5%, up 20 basis points sequentially. Year-over-year, our adjusted operating income rate was up 100 basis points.

Adjusted EBITDA in the quarter was $651 million, up 4% sequentially and up 6% year-over-year. Adjusted EBITDA rate was 12.9%, up 100 basis points year-over-year.

Our adjusted operating income and adjusted EBITDA margins were largely impacted by the suspension of our Russia operations during the quarter and foreign currency exchange movements.

Corporate costs were $108 million in the quarter. For the third quarter, we expect corporate costs to decline and be more in line with first quarter levels.

Depreciation and amortization expense was $275 million in the quarter. For the third quarter, we expect D&A to decline roughly $5 million sequentially as a result of the impairments taken in the second quarter.

Net interest expense was $60 million.

Income tax expense in the quarter was $182 million.

GAAP diluted loss per share was $0.84 cents. Included in GAAP diluted loss per share are $426 million of losses related to our OFS business in Russia due to its classification as held for sale at the end of the second quarter. Also included was an $85 million loss from the net change in fair value of our investment in ADNOC Drilling, and a $38 million loss from the net change in fair value of our investment in C3 AI; all of which are recorded in other non-operating loss.

Adjusted earnings per share were $0.11 cents.

Turning to the cash flow statement, free cash flow in the quarter was $147 million.

Free cash flow in the quarter was impacted by lower collections, which are largely timing related, as well as a build in inventory as we get ready to execute on our large order backlog.

For the third quarter, we expect free cash flow to improve sequentially, primarily driven by higher earnings and seasonality. We now expect free cash flow conversion from adjusted EBITDA to be below 50% for the year, due to lower cash generation from Russia.

In the second quarter, we continued to execute on our share repurchase program, repurchasing 6.7 million Baker Hughes Class A shares for $226 million, at an average price of $34 per share.

Before I go into the segment results, I would like to give an update on our Russia operations, how these impacted our second quarter results, and how the current situation factors into our forward outlook.

As I mentioned earlier, our OFS business in Russia was classified as held for sale at the end of the second quarter. During the second quarter, we took the step to suspend our Russia OFS operations to ensure compliance with all sanctions. As a result, our OFS Russia revenue declined 51% sequentially to approximately $60 million in the second quarter, leading to meaningful cost under absorption as we maintained our full cost base.

Looking ahead, we are required to maintain our operating costs in the country until we reach a resolution for our Russian operations.

In TPS, we have suspended work on equipment and service contracts in Russia. As a result, these projects have been removed from RPO and second quarter revenue was impacted by roughly $160 million but with minimal impact to TPS operating margins. For the full year, we estimate that TPS revenue will be impacted by approximately $400 million but, again, with minimal impact to TPS margins in 2022.

In OFE, we have suspended all equipment and service contracts in Russia. OFE will be impacted by lower volume and cost under absorption over the next few quarters due to the removal of these projects from RPO.

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

Starting with **Oilfield Services**, revenue in the quarter was $2.7 billion, up 8% sequentially. International revenue was up 8% sequentially led by increases in Sub-Saharan Africa, Latin America, Europe, and the Middle East, partially offset by lower revenues in Russia Caspian. North America revenue increased 9% sequentially, with low double-digit growth in North America land.

Operating income in the quarter was $261 million, up 18% sequentially. Operating margin rate was 9.7%, with margins increasing 80 basis points sequentially driven by price improvements and productivity, partially offset by impacts from Russia and cost inflation. Year-over-year margins were up 240 basis points. Excluding Russia, OFS operating margin rate was 10.3% and OFS EBITDA rate was 18%.

As we look ahead to the third quarter, underlying energy fundamentals continue to improve, and we expect to see growth in both International and North American activity, as well as continued improvements in pricing.

For the third quarter, OFS revenue should increase sequentially in the mid-single digit range. With this revenue framework, we would expect our margin rate to increase by approximately 50 to 100 basis points sequentially, which assumes that we will continue to carry between $25 to $30 million of cost per quarter related to Russia.

For the full year 2022, we continue to see an improving outlook across most major markets.

In the international markets, we expect the continuation of a broad-based recovery with industry-wide activity growth in the mid-double digits.

In North America, we expect continued activity increases, with the broader market set to experience strong growth of 50% or greater.

Given this macro backdrop, we would expect OFS revenue to increase in the mid-double digits in 2022.

We expect EBITDA margin rates to increase over the next two quarters and to be between 19% and 20% in the fourth quarter, depending on timing of the resolution of our Russia business.

Moving to **Oilfield Equipment**, orders for the quarter were $723 million, up 6% year-over-year, driven by a strong increase in Flexibles and Services, partially offset by a decrease in SPS and the removal of Subsea Drilling Systems from consolidated results.

Revenue was $541 million, down 15% year-over-year, primarily driven by SPS, SPC, and the removal of SDS, partially offset by growth in Services and Flexibles.

Operating income was negative $12 million, down $40 million year-over-year, primarily driven by lower volume in the quarter. OFE's lower operating margin rate was primarily driven by lower volumes in SPS and some operational challenges on certain projects.

Although OFE has had to navigate some challenges this year, the current level of performance is unacceptable and, as Lorenzo mentioned, we are evaluating additional ways to drive cost-out and better operating performance, which includes more integration across OFS and OFE.

For the third quarter, we anticipate revenue to be approximately flat to down low-single digits sequentially, depending on the timing of backlog conversion. We expect operating income to be below breakeven due to cost under absorption following the suspension of contracts related to Russia.

For the full year 2022, we still expect a recovery in offshore activity and project awards, which should help drive a double-digit increase in orders. We expect OFE revenue to decline double digits, primarily driven by the de-consolidation of SDS, and OFE margins to be below breakeven.

Next, I will cover **Turbomachinery**. Orders in the quarter were $1.9 billion, up 23% year-over-year. Equipment orders were up 38% year-over-year, driven by a gas processing award in Saudi Arabia and an order for Cheniere's Corpus Christi Stage 3 expansion.

Service orders in the quarter were up 14% year-over-year, driven by installation orders and growth in contractual and transactional services, partially offset by a decrease in upgrades.

Revenue for the quarter was $1.3 billion, down 21% versus the prior year. Equipment revenue was down 30% driven by changes in project schedules, and foreign currency movements. Services revenue was down 11% year-over-year driven by a decrease in upgrades, transactional services, and Russia-related impacts during the quarter, offset by contractual services.

Operating income for TPS was $218 million, down 1% year-over-year. Operating margin rate was 16.8%, up 330 basis points year-over-year. Margin rates in the second quarter were favorably impacted by higher services mix.

Overall, the TPS team has navigated multiple headwinds as the year has unfolded, including Russia-related impacts, foreign currency movements, and a challenging supply chain environment. Despite these headwinds, we still feel confident in the full year operating income outlook relative to our expectations at the beginning of the year.

For the third quarter, we expect revenue to increase mid-single digits on a year-over-year basis, driven by higher equipment volume from planned backlog conversion.

With this revenue outlook, we expect TPS margin rates to be moderately lower on a year-over-year basis, depending on the ultimate mix between equipment and services.

For the full year, we still expect TPS orders to be between $8 and $9 billion, driven by increasing LNG awards.

We now expect revenue growth to be roughly flat to up low-single digits versus 2021. The lower revenue growth versus expectations earlier in the year is primarily driven by the suspension of operations in Russia, the depreciation of the Euro versus the dollar, and some modest changes in project execution schedules.

On the margin side, we now expect operating income margin rates to be slightly higher on a year-over-year basis, depending on the mix between services and equipment.

Finally, in **Digital Solutions**, orders for the quarter were $609 million, up 13% year-over-year. DS continues to see a strengthening market outlook and delivered growth in orders across Oil & Gas and Industrial end markets. Sequentially, orders were up 7% driven by higher Industrial and Power orders. As oil and gas end markets finally start to recover, DS orders are now at the highest level since the fourth quarter of 2019.

Revenue for the quarter was $524 million, up 1% year-over-year, driven by higher volumes in PPS and Waygate, partially offset by lower volume in Bently Nevada and Nexus Controls. Sequentially, revenue was up 11%, driven by higher volume in PPS, Bently Nevada, and Nexus Controls, partially offset by lower volume in PSI.

Operating income for the quarter was $18 million, down 28% year-over-year, largely driven by mix, inflation, and lower productivity. Sequentially, operating income was up 21%, driven by higher volume. Overall, DS continues to be affected by both chip and electronic component availability shortages, negatively impacting the convertibility of our backlog, and our ability to drive higher productivity.

As Lorenzo mentioned, we continue to make strategic and operational changes across DS designed to improve performance, as evidenced by recent leadership changes and the recently announced sale of Nexus Controls to GE.

For the third quarter, we expect to see low-single digit sequential revenue growth and a slight increase in operating margin rates.

For the full year, we expect DS revenue growth in the mid-single digit range and operating income margin rates to average in the mid-single digits for the full year.

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.