

# **Baker Hughes Company (BKR) Barclays 38th Annual CEO Energy-Power Conference (Transcript)**

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**Body**

Baker Hughes Company (BKR)

Barclays 38th Annual CEO Energy-Power Conference Call

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Company Participants

Lorenzo Simonelli - Chief Executive Officer

Conference Call Participants

Dave Anderson - Barclays

Presentation

Dave Anderson

Since the merger of the GE Oil & Gas and Baker Hughes, we've been fortunate with our front-row seat to the company's transformation as they've used our conference to roll out its annual presentation and evolving strategy each year. So, it's been an impressive journey for the company, and I believe a lot of credit for Baker's execution strategy and culture belongs to Lorenzo Simonelli, CEO of Baker Hughes. Since the merger of 2017, Baker has really carved out a unique position in the energy service sector.

And it's always great to see Lorenzo at our conference. Lorenzo, thank you very much for joining us today.

Lorenzo Simonelli

Dave, thank you very much.

Question-and-Answer Session

Q - Dave Anderson

So, maybe just to start off kind of a little bit bigger picture here, since you've been CEO, Baker has gone through a tremendous transformation in terms of portfolio strategy and key members of management. Really so I think the company has hit its stride over the last few years. There was a time when execution was the Achilles' heel, it's now turned into an asset with the strong results each quarter after quarter. So, what's been the secret behind this improved execution? Was it a cultural shift? Was it an organizational change? I think, people who have been in this room, remember 10 years ago, that was kind of such an issue, but now it's -- like I said, it's a strength now. So, what was the change?

Lorenzo Simonelli

Well, first of all, thank you for recognizing that Baker Hughes has come a long way. And I think it really is an aspect of consistent strategy and focus. And for those of you that know the history that we've been through even from the merger, it's been tumultuous. We've been through events from a roller-coaster perspective of a merger with General Electric, a separation from General Electric, we've been through the pandemic like others, and the exit of Russia. And I really look at our strategy of developing a differentiated energy technology company always being at the forefront.

And you look at where we are this year, you look at the midpoint of our guidance, our margin rates are at EBITDA of 16%, above where they've been historically. When you look at what we're going to do from an EBITDA perspective, again, looking at about $4.5 billion and again, that above 50% from 2019. So, it's been a focus of the strategic execution that we put into place. And I'd lay it down into really three areas.

The first has been transform the core, which is focused on operational execution, focused on consistency of delivery to the customer, and making sure that we take out the costs and simplify the company.

The second has been invest in profitable growth. We have a differentiated portfolio between our equipment side of gas turbines, compression, and also with digital capabilities, and with the production and chemicals, and for mature asset solutions. So, invest in those areas, where we've got differentiation.

And thirdly, new frontiers. We were at the forefront of saying energy transition is about lowering emissions. How do we start to move into areas of CCUS, hydrogen, clean integrated power solutions, geothermal?

And these three pillars, with the hard work of the team and the continued focus on execution, have been really the driving force of the improvement, which will continue because we're just at the beginning.

Dave Anderson

So, culture is something that, I guess, when I was younger -- earlier in my career, I didn't really think much of. Now, I've been doing this for a little while. I think it's one of the -- arguably the most important things for a lot of companies. It's probably the hardest thing to define and even harder to create. So, how did you, broadly speaking, change this culture at Baker Hughes from what it was before to what it is now? Is there a kind of a magic formula here, or did you -- is there just kind of constant working with your organization? Like is it -- how does somebody create a culture essentially from scratch, or with two very disparate companies coming together?

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Lorenzo Simonelli

It starts with making sure that you have a purpose statement that can rally the company together. And we clearly came from a background of tainted history and bringing the two companies together was all-around how do we create one purpose of helping the world, providing clean efficient energy to the people and the planet, and then, leveraging those skills, making management changes, and having the right people around you.

It started out for us with knowing commercial intimacy, knowing the customers, the relationships with customers. And that's something from a geographic perspective, we've had a great presence, but we needed to rekindle that aspect of being in front of the customer. Then came, now that the customer is there, we got to make sure that we're executing for the customer and the focus on the operational side. And throughout, being consistent in the investments in technology. And as you start to deliver execution quarter-on-quarter, the culture builds on itself.

Now, I think everybody knows that culture eats strategy for breakfast. So, we've got a very clear strategy and really the secret sauce is mobilizing close to 58,000 people around the world in creating the differentiated energy technology company. And I'm very proud of what the team has done. It's been heavy lifting. As you mentioned, we have made significant management changes. We continue to look at areas where we can improve, develop from within, and continue to also improve ourselves for our customers.

Dave Anderson

So, you just made a management change. I think it was announced yesterday, Maria Claudia, who has been critical in essentially kind of overhauling OFSE for the last five, six years. She's moving on to a new role, a strategic role, Chief Growth and Experience Officer. You have a new guy coming in, former SLB player, I believe, Amerino Gatti.

Lorenzo Simonelli

Yes.

Dave Anderson

Can you talk about the change that was made? Why did you make this change? And looking forward, Mr. Gatti, what's he going to bring to the table?

Lorenzo Simonelli

Yeah. One of the important aspects as a leader charting the course of the company is also being able to anticipate what are the changes that are needed. So, let's take the move of Maria Claudia Borras from Oilfield Services and Equipment, where she's been very successful over the course of the last six years, delivering on the strategy that we laid out to get OFSE to a 20% EBITDA. A lot of restructuring, a lot of core heavy lifting. And she knows the company well. She knows both sides of the company well from the Industrial and Energy Technology, as well as the Oilfield Services and Equipment.

And as we move forward, it's going to be very important to offer that portfolio of capabilities to our large customers, because the energy ecosystem is also changing, and it's not just about a drilling service contract or a well construction, it's about a CCUS project. It's about the complexity of gas infrastructure. And as Chief Growth and Experience Officer, she's going to be very focused on that next horizon of growth, as we look at the capabilities that we can offer, not just our existing customers, but the new customers as well, because everybody realizes that they've got to do more in reducing their emissions and also that energy demand is continuing to increase. So, very much looking forward to her in her new role, and again, compliments to what she's achieved and she did what we asked her to.

Bringing in Amerino Gatti, bringing in a seasoned individual who knows oilfield services and equipment, and also knows the industrial side. He was actually CEO of TEAM, Inc., a diversified industrial services company. He's also been on the board of Helix. And he comes with a background of production solutions. Our view is that mature assets are going to become much more important as we go forward. And as we think about today's production, 70% of the world's production comes from mature assets. And the mature asset well has been in existence for 25 years or 50% of the reserves have been depleted. As we continue to see demand increase, brownfield extensions, more recovery from the actual existing mature assets is where the CapEx and the OpEx is being spent. And with the experience that he brings from his past, as you mentioned, also 25 years in the oilfield services space, he led many of the production solutions internationally as well as in North America, and I'm looking forward to him really helping us as we continue to chart that growth going forward.

Dave Anderson

So, part of Maria Claudia's new role is looking at that next horizon for growth. Can you just maybe just touch on where you think that horizon is? I think you just touched on it a bit with CCUS, but what are some of the other things that you think are in that second horizon -- on the next horizon?

Lorenzo Simonelli

Well, as we look at the next horizon, you can see, as I mentioned, CCUS, you can also see the complexity of power generation towards data centers. And if you think about new customer base, you know that everybody is talking about artificial intelligence, generative AI, electrical consumption by data centers is predicted to double by 2026, going from 2% to 4% consumption. If you think about that from a scale perspective, 4% is the same amount of energy that Japan uses in a year. And we don't have grid stability. So, there's an interconnectivity that's going to be required around where the gas is available and also where the power generation takes place. That's one area where there's an opportunity to grow.

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Likewise, as you think of geothermal, and you think about understanding the subsurface and the top side and the way in which you can actually generate power. We, as an energy technology company, have the product breadth that actually enables that capability for the end customer. And it's going into new sectors such as mining. Mining is very energy-intensive. They're also trying to reduce their emissions. How do we continue to provide them with the capabilities and the solutions?

And look, I'll give you a good example. Everybody used to think of Baker Hughes just as LNG on the industrial side. Well, I think we've demonstrated this year, we do a lot more than just LNG. And if you think about our rotating equipment, it goes into multiple end-user applications that are beyond just the oil and gas space. And this is the further frontier of growth that we as a company have.

Dave Anderson

So, speaking of which, your orders guide for the year is like $12 billion. Maybe just help people understand how much of that were you expected to be out of LNG this year?

Lorenzo Simonelli

Well, given that the moratorium came in at the beginning of the year, we didn't change our guidance because we were confident on the gas infrastructure developments. We were confident in the non-LNG growth. And as you look at this year, non-LNG orders will be up 50%, and we see that as a continuing theme. And also, as we go forward, we think the LNG FIDs will come back. So, I think the consistency and also the durability of that tailwind for continued industrial orders growth is there for the future.

Dave Anderson

[It is] (ph) gas infrastructure. But more broadly speaking, just sticking with the LNG side, you've often talked about 800 million tons per annum as being kind of ultimately where we're going to end up in this part of the LNG cycle. I think you're still thinking about 100 million coming over the next couple of years as...

Lorenzo Simonelli

Correct.

Dave Anderson

...we get through. So, what then? What next? What are you seeing on kind of the horizon? Do you think there'll be another wave? Do we have to kind of go through a market process of absorbing this gas first? Or how do you see that playing out?

Lorenzo Simonelli

So, I think I'm in my fourth cycle of LNG, and this isn't the last cycle. There is going to be more LNG required, and it's actually interesting to see it play out time over time. And we're going through, obviously, a build cycle right now. We've said many times, and I think we stated it the first time back in 2019 that we were going to need 800 MTPA by 2030 of installed capacity. That is very much the case.

What we're seeing now is that there is an understanding and an appreciation that energy demand continues to increase in the developing world and where the population is increasing. And natural gas, LNG, is one of the best ways to provide that. And the energy transition itself is going to take time as we anticipated. It takes a huge amount of effort to change the energy mix.

So, we're already hearing from customers and partners about projects that extend beyond 2030. And you just have to look at the areas where there's a lot of gas available. You can see that Argentina is talking about LNG. You can see locations in Africa that are talking about LNG. So, beyond what's always been talked about with regards to Qatar, Australia, and the US, you've got new emerging areas that are going to be LNG feedstock for the world where gas is prevalent.

Dave Anderson

Shifting back to the US of the permitting kind of been on moratorium for the last, what, eight, nine months now. Any signs of progress there? Or is this just straight up politics here?

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Lorenzo Simonelli

So, I think recently, there was one approval that was given on one project, which we compliment the administration on. We think -- again, we've said this publicly that we don't agree with the moratorium. We think we should be going forward with taking advantage of the gas exports and LNG exports. I just go by what we heard this year from the secretary that come March next year, this should be in the rearview mirror. That's what was stated. And we think that, again, going forward, it's a good thing for the US to be able to export LNG.

I'll also say, as a company that provides equipment and liquefaction trains to LNG projects around the world, those projects internationally are going to go forward. And it's a decision the US needs to make, does it want to participate, and hopefully, and we think they'll make the right decision.

Dave Anderson

Hopefully, they get that environmental study done soon. Very much needed. So...

Lorenzo Simonelli

I hear it's done.

Dave Anderson

On a separate subject, you alluded to it before, LNG is just one part of this IET order book. Can you talk about some of the other end markets that kind of make up the majority of that? And what are you really excited about in terms of growth over the next few years?

Lorenzo Simonelli

So, putting aside LNG, if you think about the breadth of the products and capability we have, it goes from a wide range of compressors, it goes to a wide range of gas turbines that are also hydrogen-driven gas turbines from various aspects of megawatt, it goes to valves that control valves, safety valves, and it goes to pumps. So, you can look at it across the spectrum, inclusive of electric motors.

Now, you look at the end markets, onshore/offshore production. We look at that continuing to be a solid marketplace when you think of FPSOs. And we see seven to nine FPSOs on a yearly basis as we go forward.

Then, you move on to the power generation side. Again, many of these sites onshore need power generation. And so, we see that as a growing marketplace for distributed power source and off the grid.

Next, gas infrastructure. If you think about all of the LNG or you think about the increase in gas, take the discussion before on the Jafurah field, a huge gas field. Yes, you have to drill. You have to have the well. But you actually need the gas infrastructure around it and you need the compression capability and you need to be able to have the pipeline. If you think of Saudi Arabia earlier this year, Master Gas System 3, which we announced. Again, there's likely a Master Gas System 4. You look at Algeria, the gas infrastructure that's required there for supplying Europe. So, that whole aspect of gas infrastructure.

Then, you go into the petrochemicals, the refineries, and you look at the elements of the components and products that go into that end market from the pumps, the valves, the electric motors.

So, these are all areas that we serve. And the good thing about our equipment is, it is molecule-agnostic. And you need it when you're moving molecules around, and we're very good at that.

Dave Anderson

So, the Master Gas System 3 in Saudi, essentially, Saudi is transforming a big chunk of their power towards natural gas, and we're going to see this kind of continue to go in this direction. Probably the more success they have with [indiscernible] and other, you'll see more of this. You mentioned Algeria. What other countries -- I would imagine other countries are going to start moving this direction. Where do you -- what other areas do you see opportunities for Baker Hughes' equipment in terms of power generation or basically gas infrastructure changes?

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Lorenzo Simonelli

Again, as you look at Argentina, clearly, a lot of gas there and a lot of gas infrastructure that's going to be required. Continuing growth here in the United States, even from a domestic standpoint of the continued usage of gas. As you look at Indonesia, and again, some of the gas that's been found there, Southeast Asia. You've got also upgrade. And I think it's important to note the whole aspect of upgrades that are needed on existing new infrastructure and old infrastructure. And then, as you look at the new energy areas of hydrogen as well that are appearing, they're going to require the same equipment. So, it's by basin in different geography, but it's actually a very large significant area of growth.

Dave Anderson

You touched on it before, data centers. Obviously, a huge theme that's been going on in the last several months, a lot of power needed to all the AI, the whole new trend here. Where does Baker fit in there? I know you have certain turbines that might fit. Can you just talk about your opportunity within the kind of the broader scheme. I know there's a lot of different plans out there. There's a lot of debates about the power required. So, where does Baker fit in that?

Lorenzo Simonelli

And this is an evolving space. And I think it's going to play out over the course of the next few years. And if you look at the different predictions, you can go from 500 megawatts to 1.5 gigawatts that we've got an opportunity for. And we play in the industrial gas turbine size of 16, 32, and these are modular sizes that can be placed next to where gas is available. And the other area where we play is also in the ability to have hydrogen-ready. So, as you're thinking about being able to reduce your emissions, we're one of the companies that already has a hydrogen-ready turbine.

So, these are the ecosystems in which we're playing with different partners, some of the hyperscalers, some of the developers, and looking at that opportunity and speaking, obviously, to the big companies, Microsoft, AWS, and exploring how they're going to meet their needs. And it's not only in the United States. I think as you look at also other areas around the globe, in the Middle East, in particular, there's going to be a buildout of data centers as well.

Dave Anderson

Finishing up on the IET side, you have a margin target of 20% margins by 2026. How much of that is already known? In other words, you already know the backlog, you already know the pricing. So, what other elements do you need to get to that 20%? What do you need to do internally, or what do you need to see market-wise to get to there? And is that -- I mean, I would assume pricing is already part of that you already know.

Lorenzo Simonelli

So, the industrial energy technology benefits from being a longer cycle business and also benefiting from being a razor/razor blade. So, as we install equipment, then we've got an annuity of service stream that takes place for many, many years, up to 25, 30 years. As you look at the pathway from where we are today to 20% EBITDA by 2026, we came out with this target in 2022, and we were very clear on the areas in which we were going to execute to get that. And today, I'm very confident that we will get there.

The first is the backlog. As you look at what we've put into backlog, and we have a record backlog, we've gone in at higher margin rates. Pricing has been beneficial during the last few years. And so, as we convert that backlog, it comes through at a higher margin rate.

Secondly, the volume that we're putting through the factories and the efficiency that we can drive from the volume leverage, that gives us, again, a margin accretion on what we're doing today and it's already visible to us.

Next, there is our Industrial Products and Solutions businesses. During the pandemic, we said that they were struggling from supply chain shortages, but their gross margins were still good. As we've improved on the supply chain side, we're now back to the normal margin rates. And again, that's accretive.

You look at new offerings and services, upgrades that are taking place. And as the -- all the service contracts come into place.

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And finally, the simplification and the cost restructuring that we put in place in IET. Now that we've separated really from GE, we're able to get on with the actual restructuring and simplification, and our R&D spend will smooth out over time.

So, those five levers give us the capability to say 20% EBITDA in 2026, and the team is very confident.

Dave Anderson

Great. I spent most of my time talking about IET, so maybe shift over to the OFSE side. A sluggish year for spending. Obviously, spending slowed a bit more than we were expecting this year. So, your internal assumptions as you're thinking out the next couple of years, what are you factoring in, in terms of maybe global upstream spending, I don't know, international, US, but how are you thinking about that? And maybe what are some of the puts and takes and some of the strengths that you see in the market that Baker is better aligned for?

Lorenzo Simonelli

So, I think maybe to start off, we haven't changed our outlook from the beginning of the year. And I think when we came into the year, maybe we differed slightly from others. We said we saw North America being weak and actually being negative. We saw international at the high-single-digit, not the double-digit. We're seeing that play out. And we anticipate that next year, again, international will continue to be robust, and it will continue to grow, but at a decelerated rate, and North America will flatten out, and some people say it maybe up. Our focus though is really on the production and the chemical side and more of the downstream, and that's an area of strength, as well as the international exposure we have. So, we feel good about the outlook as we go into 2025 with those assumptions.

Dave Anderson

So, your OFSE portfolio has changed quite a bit over the last few years. Are you happy where it is now? Do you see other things that -- other kind of parts of the portfolio you want to add in there, or is this sort of the theme you're going with?

Lorenzo Simonelli

We like our portfolio. Clearly, we'll always look at areas that we can prune or areas that we can add from a technology standpoint. A few years back, we made the Altus acquisition, which was very beneficial and helped us from a technology standpoint. Technology is important, and we'll continue to look at tuck-ins. I'd say from a portfolio standpoint, though, again, the area of focus is around that mature asset solution and really getting more from the wells that exist today, and that's where our strength lies.

Dave Anderson

So, mature asset production, you're basically sort of -- OFSE is a bit later cycle business...

Lorenzo Simonelli

Correct.

Dave Anderson

...than your peers. So, how do you see? Is that more of a maintenance CapEx? Is that more of a maintenance spend? Is it OpEx that you're more aligned towards? Is that...

Lorenzo Simonelli

We're more on the OpEx side. Clearly, we do have the exploration, and we do have also some of the CapEx, but from a peer perspective, we are more on the OpEx and the consistency of the production side.

Dave Anderson

One final question on OFSE. So, I've been to your -- I've seen up close in Saudi over the years. It seems to me that you had taken a different strategy, a different approach. And IKTVA was a big focus of Saudi over the years. Was that intentional? You're doing a lot of manufacturing in the country. Is that part of the strategy to gain more work by being local -- essentially being a local manufacturer in there? And is that paying off for you?

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Lorenzo Simonelli

We developed a "in-Kingdom for-Kingdom" strategy, and that was back in 2019, and we deployed it, and it's proven very successful. And it's not about just Aramco, it's about the Kingdom and also where the Kingdom is going, because we play across infrastructure that's broader than just an oilfield services element. So, being able to produce in-country, being able to benefit from the local talent that they have there, and then also export from the Kingdom into other GCC locations as well as across the world. And most recently, we started up a chemical facility there. We've got an expansion on our compressor facility, and those are aspects that are very beneficial within the Kingdom.

Dave Anderson

Do you foresee exporting from Saudi to other markets? Is that sort of one of the goals of Saudi, or do they want to keep that all in Kingdom?

Lorenzo Simonelli

No, we'll look to export as well and where it makes sense. Again, you are always strategic in what you localize with the intent to be able to then export in neighboring locations. So, the chemical facility will be providing also chemicals to the GCC. Our wellhead business provides wellheads to not only the GCC, but other locations around the world. And we find it a competitive location to manufacture.

Dave Anderson

And drill bits as well, right?

Lorenzo Simonelli

And drill bits. And in fact, we also export drill bits back into the United States.

Dave Anderson

All right. One final question. IET backlog is converting over the next few years. Free cash flow is poised to increase quite a bit over the next few years. Should investors expect most of that to come back to them? I know you just touched on the M&A side, but can -- is that going to be the priority? Or do you think you have other uses for the cash?

Lorenzo Simonelli

Our policy hasn't changed. And again, we look to return 60% to 80% to shareholders. We've done that consistently, and we think it's important to retain the dividend, keep a focus on the dividend, and then also use buybacks as appropriate.

Dave Anderson

Great. Lorenzo, thank you very much.

Lorenzo Simonelli

Thank you very much.

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