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FTI.N - Q3 2019 TechnipFMC PLC Earnings Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the TechnipFMC Third Quarter 2019 Earnings Conference Call. (Operator Instructions) Thank you.

I'll now turn the call over to Matt Seinsheimer. Please go ahead, sir.

Matt Seinsheimer - *TechnipFMC plc - VP of IR*

Good afternoon, and welcome to TechnipFMC's Third Quarter 2019 Earnings Conference Call. Our news release and financial statements issued yesterday can be found on our website.

I'd like to caution you with respect to any forward-looking statements made during this call. Although these forward-looking statements are based on our current expectations, beliefs and assumptions regarding future developments and business conditions, they are subject to certain risk and uncertainties that could cause actual results to differ materially from those expressed in or implied by these statements. Known material factors that could cause our actual results to differ from our projected results are described in our most recent 10-K, most recent 10-Q and other periodic filings with the U.S. Securities and Exchange Commission, the French AMF and the U.K. Financial Conduct Authority. We wish to caution you not to place undue reliance on any forward-looking statements, which speak only as of the date hereof. We undertake no obligation to publicly update or revise any of our forward-looking statements after the date they are made, whether as a result of new information, future events or otherwise.

I'll now turn the call over to Doug Pferdehirt, TechnipFMC's Chairman and Chief Executive Officer.



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Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

Thank you, Matt. Good morning, and good afternoon. Thank you all for participating in today's call. Joining me today are Maryann Mannen, Chief Financial Officer; and Catherine MacGregor, President of New Ventures and the CEO-elect for SpinCo.

In the third quarter, we announced the transaction that will create 2 diversified pure-play market leaders: RemainCo, which will retain the TechnipFMC name, will be a fully integrated technology and services provider that will continue to drive energy development; and SpinCo, a leading E&C player poised to capitalize on the global energy transition. The separation will enable both companies to benefit from distinct and compelling market opportunities across the energy value chain; dedicated focus on management, resources and capital; and unique value propositions with differentiated investment appeal.

Our balance sheet will support the creation of 2 financially strong companies. The capital structure of both companies will be tailored to their specific business needs, and we remain confident that both will have investment-grade metrics. We believe strongly that providing independence for these 2 world-class, high-performing businesses will unlock further opportunities and value creation for all stakeholders.

When thinking about the 2 companies, it's helpful to understand where the operational leverage resides. For RemainCo, 89% of the trailing 12-month revenue mix has been driven by Subsea projects and service technologies outside North America. We believe these international markets provide the best opportunities for growth. More specifically, we expect the Middle East will continue to lead our international growth in Surface Technologies, and we anticipate future Subsea activity will be driven in part by emerging markets such as Mozambique and Guyana, where, as an industry leader and first-mover focused on sustainability, we have created a strong footprint to help unlock the tremendous resource potential in both regions. We also expect activity to strengthen in Brazil as a result of the development of presold assets.

For SpinCo, we are providing additional insight into the significant backlog in hand today, which currently equates to nearly 3x the revenue projected for 2019. Looking at the backlog in greater detail, approximately 56% of the \$18 billion of total backlog is related to future work on LNG projects, including Yamal LNG, Prelude FLNG, Coral FLNG and Arctic LNG 2. Our recent announcement of the Rovuma LNG award, which the client has suggested will likely be sanctioned next year, is not included in these figures.

The announcement of our intention to create 2 distinct companies has also refocused the market's attention on the appropriate peer group for both entities. For RemainCo, we believe large-cap service companies and equipment manufacturers are the most relevant peers. This includes a select group of companies that have capabilities in subsea equipment, installation and services or capabilities in drilling and completion equipment and services, a global franchise across major upstream basins and a capital structure that provides the financial strength required by our customers. We consider the most relevant peers to be Baker Hughes, Halliburton, NOV and Schlumberger. In addition to these large-cap peers, there are a few companies with smaller market capitalizations that could also be considered, including Aker solutions, Oceaneering, Subsea 7 and The Weir Group.

For SpinCo, the company will be one of the largest global E&C pure-plays with leading positions notably in the LNG market. SpinCo's strong competitive position in the marketplace is driven by leading capabilities in LNG, a differentiated portfolio of process technologies, the ability to successfully execute the industry's most challenging projects, capabilities and services particularly around front end and project management consultancy and proprietary products and equipment.

Evaluation of the global peer group identifies only a handful of players with demonstrated LNG capabilities, including Fluor, JGC, KBR and Saipem. There are many other companies with whom we compete, but we firmly believe that this more limited set most appropriately reflects the key differentiating attributes and leadership positions of these 2 unique pure-play companies.

Turning to Subsea. Orders in the third quarter reflected continued strength driven by the integrated awards, services activity and the award of the industry's first 20K Subsea system. The momentum of the integrated commercial model continued as we inbounded several new iEPCI projects in the period. The value of integrated project awards in 2019 has increased by more than 90% from the levels we recorded through the first 9 months of 2018. Subsea services continue to benefit from the industry's largest and expanding installed base, with growth in the quarter reflecting increased installation, asset refurbishment and well intervention activities. Subsea services remains on track for double-digit growth for the full year.



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Also in the quarter, we received the industry's first award of a high-pressure, high-temperature system for LLOG's Shenandoah project in the Gulf of Mexico. This new technology was the result of a joint industry program led by TechnipFMC that included 5 major operators. This was the first time the industry collaborated to develop a new subsea system focused on the delivery of a single-part number and designed to handle hydrocarbons under the industry's most extreme pressure and temperature conditions to date.

Taken together, we reported inbound orders of \$1.5 billion in the quarter, which, again, exceeded revenues in the period. Inbound, through the first 9 months, totaled \$7 billion, reflecting a year-to-date book-to-bill of 1.7x.

We continue to believe that order growth for the full year will exceed 50%, significantly better than the total Subsea market growth, which we estimate closer to 20%. This high level of growth is coming in the third year of a market recovery and is the highest annual growth rate we have experienced in a decade. This year's order growth has been driven by increased adoption of the integrated model, and the successful introduction of iEPCI was only possible due to the creation of TechnipFMC. While 50% growth will be difficult to repeat, we do see potential for next year's inbound orders to match the absolute levels we anticipate for 2019.

Moving to the LNG outlook. The supply of new liquefaction capacity coming online today reflects investment decisions made as far back as 7 years ago. While we acknowledge near-term market sentiment, we continue to believe that natural gas is critical to the energy transition and that there is a need for significant new capacity to meet future gas demand. It is also important to remember that the decision to sanction projects today is based on gas -- first gas in 2023 and beyond. The demand scenario at that time will be very different than the one we currently face.

5 projects over the last 5 months have either been sanctioned or, as highlighted in public disclosures, moved closer to FID in 2020. 2 of these have progressed to the benefit of TechnipFMC. We announced the first project, Arctic LNG 2, back in July. And just 2 weeks ago, we announced the contract award for the Rovuma LNG project in Mozambique through a consortium including TechnipFMC, JGC and Fluor.

The Rovuma project includes the construction of two natural gas liquefaction trains, with total nameplate capacity of 15.2 million metric tons per annum as well as associated onshore facility. The award builds upon our expanding capabilities in the region where we are already present through our work on the Coral FLNG project and the Golfinho Integrated Subsea project. This serves as further confirmation of TechnipFMC's leadership in LNG and our strong capabilities in the delivery of remote projects. Selectivity of projects like Rovuma is paramount to our success. To emphasize this point, we have re-prioritized previously targeted projects where the commercial terms fell outside our acceptable limits.

We remain focused on securing the right projects where we can leverage our differentiation, those that have the right contractual terms for us and those with the best project economics for our customers.

I will now turn the call over to Maryann to discuss our financial results in the quarter.

Maryann T. Mannen - *TechnipFMC plc - Executive VP & CFO*

Thanks, Doug. Our third quarter highlights included solid orders in Subsea, strong execution in Onshore/Offshore and double-digit international revenue growth in Surface Technologies. We continue to build backlog for execution in 2020 and beyond, providing further confidence in our medium-term outlook and a solid foundation for our upcoming separation into 2 well-capitalized companies. We also generated positive operating cash flow in the quarter, which has now been positive for 5 consecutive quarters.

Moving to the results. Adjusted diluted earnings per share from continuing operations were \$0.12 in the quarter, when excluding after-tax charges and credits of \$0.07 per diluted share. Other pretax items impacting the quarter, for which we do not provide guidance, included: \$0.22 per diluted share related to an increase in the liability payable to joint venture partners that is included in interest expense and \$0.09 per diluted share of foreign exchange losses included in corporate expenses. Total company adjusted EBITDA was \$379 million, with cash flow from operations totaling \$92 million. We ended the quarter with net cash of \$596 million.

Turning to the segment results. Subsea delivered third quarter revenues of \$1.3 billion, an 11% increase versus the prior year quarter, driven by increased activity in Subsea projects and solid year-over-year growth in Subsea services. The increase in services revenue was driven by higher

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installation, well intervention and asset refurbishment activities, with notable strength in Asia Pacific and the North Sea. While we experienced solid revenue growth over the prior year period, this growth was impacted by the timing of key project milestones, shifting recognition of some anticipated revenue into the coming quarters. Revenue growth was also impacted by foreign exchange translation adjustments, which reduced the growth in revenue by \$44 million versus the prior year period. Adjusted EBITDA was \$139 million with a margin of 10.4%. We remain confident in our full year guidance for Subsea.

Onshore/Offshore reported third quarter revenue of \$1.6 billion, an increase of 4% from the prior year quarter. This was our second consecutive quarter of year-over-year revenue growth, benefiting from the significant expansion of our backlog. Adjusted EBITDA was \$304 million with a margin of 19.1%. The solid margin performance in the period reflects the Yamal LNG contribution and the continued strength in execution across the portfolio.

Following quarter end, we announced the award of an EPC contract for Mozambique's Rovuma LNG project. While we will perform some early work on the project in the near term, the impact on our backlog will not be material in the fourth quarter. The full contract value will be included in backlog when full notice to proceed is given. The client has indicated that the Final Investment Decision is anticipated in 2020.

Surface Technologies revenue of \$397 million was down modestly in the quarter versus the second quarter with continued strength in international markets, nearly offsetting the headwinds in North American activity. Adjusted EBITDA margin of 11.2% was largely unchanged sequentially, primarily due to lower volume and further pricing pressure in North America.

Turning to cash flow. We generated positive operating cash flow in the period of \$92 million, which would have been \$256 million, excluding settlement. This included a \$9 million contribution from Yamal LNG. This marked our fifth consecutive quarter of positive operating cash flow. Year-to-date, we generated operating cash flow of \$288 million, and we expect cash flow from operations to be positive again in the fourth quarter.

Beyond the operating line, capital expenditures were \$98 million in the period and included investments that will support for future growth. Please note that our full year guidance of approximately \$350 million excludes the \$80 million impact of the sale leaseback transaction we recorded in the first quarter for the dive support vessel.

And lastly, on the Q2 earnings call, I stated our intent to distribute the majority of the \$413 million liability to Yamal LNG joint venture partners before year end. In the third quarter, we made a cash distribution of \$223 million and expect to make an additional payment in the fourth quarter. Any further increase in the liability incurred in the second half of the year as a result of increased project profitability will likely be distributed beyond 2019.

Turning to our full year outlook. We have provided updates to our guidance for Surface Technologies and corporate expense. For Surface Technologies, lower North American activity continues to negatively impact both volume and price. Many of our international markets remain healthy, and we now expect our international revenues, which account for just over half of the segment total, to grow at a low double-digit rate for the full year. This trend supports our full year revenue guidance of \$1.6 billion to \$1.7 billion, although we are trending toward the low end of this range as a result of the weakness in North America. However, we are reducing our margin guidance to at least 10%, down from our previous guidance of at least 12%, due to the market challenges we are facing in North America. For corporate expense, we're increasing our full year guidance to a range of \$210 million to \$215 million versus our previous guidance of \$160 million to \$170 million, excluding the impact of FX. Our corporate cost have been impacted mainly by accelerated IT spending, where we elected to go forward with certain initiatives, including a global PC refresh, this incremental spend is materially complete.

The updated guidance reflects approximately \$40 million to \$45 million of corporate costs for the fourth quarter, which is in line with the underlying run rate of the first 9 months of the year. Given the discretionary nature of the incremental spend, we're confident in our ability to deliver this level of spend in the quarter.

Finally, we do not provide guidance for the impact of foreign exchange. I want to comment on the \$53 million expense we recorded in the quarter. The majority of the FX impact was driven by the devaluation of the Angolan Kwanza as the country's Central Bank took steps to more closely align



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its published rate with those offered in less traditional foreign exchange markets. We do not have the ability to hedge this exposure. Given continued devaluation in the month of October, we could see a further impact in our fourth quarter results.

Last quarter, we shared incremental disclosure on contract liabilities and project cash flows for Yamal LNG because of the importance of this project on our results. We also noted that the project had largely been funded given the project's physical progress is nearly complete. This funding has been included in our reported cash balance. As a reminder, contract liabilities reflect revenue that will be converted into cost or profit through project completion. In the third quarter, a contract liability was reduced by \$284 million. Given the strong financial results reported in Onshore/Offshore, it would be reasonable to assume that a meaningful portion of these revenues were recognized as profit as strong project closure mitigated additional costs and not as cash payments to vendors. And of that profit, our 50% share will remain with TechnipFMC.

We now have \$1.4 billion in contract liabilities remaining on Yamal LNG. Keep in mind that as the contract liability is reduced, the potential remains for us to convert more of this estimated liability into profit as we demonstrated in the third quarter. And this will shift a higher portion of a liability into profit and result in a reduction in the potential cash outflow needed to complete the project.

In closing, the quarterly highlights largely support our full year outlook with improved visibility for 2020 and beyond. Onshore/Offshore's strong profitability is sustained while the Rovuma LNG award is further confirmation of our LNG leadership position. Strength in iEPCI orders is sustaining market-leading book-to-bill trends in Subsea, where our full year order growth is expected to exceed 50%, the highest annual growth rate for our company in a decade. And we delivered positive operating cash flow for the fifth consecutive quarter, a trend we see continuing in the fourth quarter.

Looking ahead, we are making good progress on our plan to create 2 independent pure-play companies and remain on track to meet an accelerated time line for completion in the first half of 2020.

With that, operator, you may now open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Sean Meakim with JPMorgan.

Sean Meakim - JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst

So Doug, maybe we can start by addressing what I think is driving some of the weakness in the stock in Europe this morning, the Subsea margin in the quarter. I think you've indicated for some time that, given the lumpiness in the business, a 10% type of number was possible for a quarter, but '19 should still be the bottom with modest year-over-year improvement next year and a better step-up in '21 on the backlog that you booked in the first half. Could you maybe just give us some more context on the milestones that flipped in 3Q? Anything else that you would call out? And -- or otherwise, is there any change to your -- the broader strokes that laid out heading into next year?

Doug Pferdehirt - TechnipFMC plc - Chairman of the Board & CEO

Thank you for the question, Sean. Absolutely, the way you summarized it is what we had previously stated, and we remain committed to that statement. And nothing has changed in our outlook for the Subsea business or its ability to be able to continue to deliver improved results. As a matter of fact, the very strong inbound levels that we've enjoyed this year, year-to-date, a book-to-bill of 1.7 times only gives us greater confidence as it gives us a greater revenue coverage and allows us to improve and accelerate the utilization of underutilized assets in the company as we move forward. So you are absolutely right. Nothing has changed. The timing and the -- when we actually achieve certain milestones is not entirely within our control, and it's very difficult to predict on a quarter-to-quarter basis, which is why we give full year guidance. But we remain fully committed



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to the 2019 full year guidance, and our outlook has remained unchanged, if anything, strengthened by the quality and the quantity of the inbound we have received year-to-date.

Sean Meakim - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

That's very helpful. I appreciate that. And as we think about -- with Rovuma making its way into your project queue at some point here, how does capacity look for incremental projects for the On/Off business overall and specifically for LNG? You'll be working on several projects at once. Execution, of course, is critical. Maybe could we just talk about engineering capacity and how you think about managing some of the incremental projects that you still have on your board for LNG in particular?

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

This is a very critical question and one that we put a significant amount of focus on, and it's why selectivity is so important across our portfolio. But I'm going to ask Catherine MacGregor to talk a bit more about what is being done within Onshore/Offshore and how we track that utilization and make sure that we're matching capacity to our proven and demonstrated capability.

Catherine MacGregor - *TechnipFMC plc - President of New Ventures*

Yes. Sure, and good morning, Sean. So the way we look at our capacity in LNG is really not just in a number of projects but looking at different factors such as the type of projects within the project, what scope are we looking at and, of course, the timing. Because as you know, those projects tend to be very long. And depending on the phase they are in, the workload requirement is very, very different. We have demonstrated in the past, as you know, our capability to deliver and work simultaneously on 3 very, very large projects at the same time. And since then, in any -- since then, we really have increased in terms of our flexibility to our operating centers with a multi-country footprint, which we can leverage on.

So frankly, when I look at what we have today in our backlog and adding to that some of the opportunities that we are looking to integrate in the future, we're very comfortable that we can take and deliver and continue to execute on those project that we are involved in. This is really a topic that is central to the discussions that we're having internally. And systematically, every time we look at an opportunity, we ask for the projection of our workload, again, leveraging our multicenter footprint across the globe.

Operator

Your next question comes from the line of Angeline Sedita with Goldman Sachs.

Angie Sedita - *Goldman Sachs Group Inc., Research Division - Research Analyst*

Dough, so could you talk -- it's good to hear the confidence you have around Subsea orders remaining strong in 2020. So it's great to hear a little bit about the visibility you have just in general and specifically around IEPCI awards next year. A little bit of color will be helpful.

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

Certainly, Angie. We published our updated opportunity list for Subsea projects that we believe the market will likely move forward within the next 24 months. That's available in the materials that went out with the press release and on our website. And reflecting on that, we see a change in value, a positive change in value, taking out those awards, removing those awards that were -- those projects that were awarded in the quarter and those that will be replaced by incremental projects. So that is up almost 3/4 of \$1 billion in terms of the opportunity set. Many of which are moving forward quite into their advanced stages, where there could potentially be awards in the much shorter time frame than the long end of the 24 months. That's what gives us the confidence.



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On top of that, Angie, and I think it's really important to reflect on a quarter like Q3, the quarter that we're here talking about this morning, in terms of Subsea. There weren't many announced awards in the quarter, yet we delivered a book-to-bill of 1.1, and we delivered a very strong total inbound dollar value. That just shows the underlying strength of our Subsea services business, our unique alliances that we have with our clients, some of which that are over 2 decades old and exclusive to our company; our new integrated EPCI, or iEPCI, alliances of which we added yet another this quarter, which most of those will lead to direct awards to our company in terms of the continued activity in the brownfield and tieback area. So this just all points to the continued strength and resiliency of what we've been able to do with our business and how we've been able to transform the market.

In terms of iEPCI looking forward, quite frankly, it's becoming more -- well, it's more than 50% of our business today in terms of inbound level. So it's really becoming the norm. Someday we'll be talking about non-iEPCI projects, not iEPCI projects because the whole market is moving in that direction. We have several customers who have now publicly stated that this is the only model that they're going to use going forward because it just makes sense. It makes sense for us, and it makes sense for them and delivers a true win-win.

Angie Sedita - Goldman Sachs Group Inc., Research Division - Research Analyst

Great. That's very helpful. And then I appreciate the context around margins and the confidence that 2019 will be the trough. Maybe looking a little bit further, with 2020, is it fair to think that the gains in margins would be relatively modest, but in '21, as the installation process begins, that the margin gain could be even a little bit greater?

Doug Pferdehirt - TechnipFMC plc - Chairman of the Board & CEO

Yes, Angie. I would agree with your analysis. I think it's really important to remind people, when we announced an iEPCI project or an integrated project, that includes Subsea delivered, installed on the seabed, the only company that can do that as a single entity and why we've been so successful to date. But in order to be able to deliver that type of a business model, we made a decision to ensure that we would have the capabilities in terms of the installation capabilities available to be able to meet those commitments.

So reflecting on that, that means we are prioritizing our fleet towards those integrated projects. As a result of that, and when we announce large awards, a large volume of awards like we've already announced 90% improvement year-on-year, over 50% of our total inbound coming from iEPCI. We do have to design, engineer and manufacture the equipment before we can install the equipment. So therefore, it's realistic to think it takes in the neighborhood of 12 to 24 months depending upon the project to complete the first phase before you move into the installation phase, which is why I think your analysis is quite appropriate in terms of we'll really start to see the total impact once we're into that installation phase, which will be more into '20 -- '21, '22 time frame, as you point out.

Operator

Your next question comes from the line of James Evans with Exane BNP Paribas.

James Evans - Exane BNP Paribas, Research Division - Analyst of Oil and Gas

I just wondered on the spin-off in SpinCo, what the key steps on the road are now, the sort of key hurdles for you to get over in the near term?

Doug Pferdehirt - TechnipFMC plc - Chairman of the Board & CEO

Thank you, James. The -- because of the nature of the transaction, most of the critical steps are, let's say, within our control. Right now, the process that we are undertaking is the finalization of the drafting of the prospectus that will be delivered. And then we will work with the agencies in terms of answering any questions that might be generated until that is finally approved and made public.



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As a result of that, I would say that's the one thing really, James, the whole team is focused on. There's many aspects, and I'm really proud of the progress that we're making. I would say, in most cases, we've built a little float into the schedule, which is what project companies do. We've gotten some things, approvals and acknowledgments ahead of plan. But really, right now, it's around the prospectus, and that tends to be an iterative process, but we are in discussions and well advanced on the draft and looking forward to getting that process initiated very soon.

James Evans - *Exane BNP Paribas, Research Division - Analyst of Oil and Gas*

And then one for Maryann on Yamal LNG. I appreciate all the additional disclosure. Inevitably, yet another question. I just wondered roughly how much in 2020 we should think about the unwind of that contract liability given that if everything keeps on going well, it is quite a significant contributor to the margin?

Maryann T. Mannen - *TechnipFMC plc - Executive VP & CFO*

So you're welcome, James, and thanks for the comment on the disclosure. What we're anticipating right now, fairly consistent with what I think we shared last quarter, in a range of about \$400 million to \$500 million unwind in 2020. That's -- as we see it today, that's what we're expecting. Not much change from where we thought as we shared that last quarter.

Operator

Your next question comes from the line of David Anderson with Barclays.

David Anderson - *Barclays Bank PLC, Research Division - Director and Senior North America Oilfield Services & Equipment Analyst*

Doug, a question on your Surface business. You said recently that would disperse the E&C business. You can then focus your attention on the Surface. And now Surface becomes a, obviously, on a relative basis, a larger part of RemainCo. Could you elaborate a bit on those comments about what you mean by focusing on it? Are you specifically targeting on the U.S. side of the business? And if so, is this simply a question of your integrated strategy, whether how it's going to work? Or is there other self-help measures that you're looking to implement in there?

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

David, thank you very much for the question. So I'm going to build up to the answer, if you don't mind. Just to remind everybody that when we talk about our Surface Technologies business, 50% of that resides outside of the U.S., where we are very well positioned. It is a very resilient business for us, and we have a very high degree of vertical integration and technology differentiation in that part of the business. In that business, as we indicated in the earnings press release and prepared remarks, we are seeing an improvement in activity and the early stages of improvement in pricing as well. So that's really important to keep in the context of the discussion.

Certainly, we are doing things and we'll continue to do things. You may recall we made a small investment or acquisition in that space last year to help expand our capabilities in the international Surface Technologies market, and we'll continue to look to invest in that part of the business, which has the returns level that we feel is appropriate for our company and for our shareholders.

When we look at the North America market, look, we're all waking up to a new market reality. We certainly had a different expectation at this time last year for the North America market in 2019. Unfortunately, that did not transpire. That has led to us having to revise our margin guidance. When I think forward to the surface business, there's really 3 key activities that we're undertaking, surface North America business, let me be more specific. It's the high-grading of our contracts, which is most evident by the fact that you saw our announcement of our long-term agreement with Chevron to be their provider of our products and services that we provide to them in the North America market. That -- you'll see us do more of that. That's very important for us going forward as who we are associating with and the type of contracts that we have in place.



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Secondly is we are looking -- or we will be moving forward with further restructuring, simply to reflect the new market reality. And that is underway, and that will continue.

And then finally, the point that you made earlier, which is our strategy is to transform the business by really looking at it differentially and taking all the lessons learned we've had from Subsea, where we've been quite successful in changing that from a product sale business to now a fully integrated services business and doing the same thing in the production market in North America. When you do that, David, the point that maybe I had made previously about focus is it really takes a high-level of client engagement. Typically, when you -- to be able to change the commercial model with -- in an industry as we did in Subsea, it was not possible without very high-level endorsement from our clients. And I can't say how appreciative I am that they were able to see and understand and embrace the need for change and understood that we were bringing something unique into the market. And that led to the early success and continued success that we were having in transforming the subsea market. It will require that same amount of engagement, attention and focus to be able to transform the North America surface market.

That being said, when I -- when we talk about the transformation of the North America surface market, that will be where we will begin because of the share of magnitude and, let's say, the criticality to our company to address that. But it is also applicable to the global Surface Technologies market. We'll just start with a focus in North America.

David Anderson - *Barclays Bank PLC, Research Division - Director and Senior North America Oilfield Services & Equipment Analyst*

So Doug, on the same line, as you're talking about the high-grading of the contracts and the Chevron contract, how much does your work with, say, on Subsea side, translate over here onto the surface? Is there that same link? I would assume there's a familiarity that Chevron has with you having worked with them for, geez, probably decades here. Does that translate into that surface business? Is that how we should kind of think about that, that's sort of where you have that advantage against some of your smaller competitors on North America market?

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

Look, you have to compete against the peer group in any market in which you participate. So I think, first and foremost, we have to be the best in what we do. But certainly, having high-level client engagement and, in some cases, intimate and long-term relationships in one part of the business or the other allows us to be able to have some leverage as well. But in this particular instance and when we talk about this transformation, what we're most excited about is taking some proven Subsea Technologies and bringing those into the surface market. Look, you've heard me say this before, we have to fundamentally change the way that we operate in the North America market, and that means we have to focus on the reduction of greenhouse gas emissions. And we believe we're going to bring it to the market and it will be embraced by the market, an opportunity to reduce greenhouse gas emissions by over 50% during the production phase of these assets.

Operator

The next question comes from the line of Michael Alsford with Citigroup.

Michael Alsford - *Citigroup Inc, Research Division - Director*

I've just got a couple. So just firstly on the onshore and offshore E&C business, I was just wondering given the awards that you've seen, if you, Doug, could -- or maybe Catherine, could update us on your views as to what your sort of medium-term margins will be for the portfolio, if that's changed at all, if you've got more confidence on that outlook now those awards have come through? That'll be my first question.

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

So Michael, I just want to make sure that we're clear when we answer your question. You're talking about the offshore portion of Onshore/Offshore?



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Michael Alsford - *Citigroup Inc, Research Division - Director*

No. In the division as a whole, Doug.

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

The division as a whole. Okay. Catherine?

Catherine MacGregor - *TechnipFMC plc - President of New Ventures*

Yes. Thank you for the question. Obviously, we are very pleased with the recent inbound we've had, both on the Arctic LNG 2 as well as Rovuma even though it's not in our numbers yet, but very, very pleased with the way the portfolio is shaping up in the Onshore/Offshore GBU. Of course, Yamal has been and will continue to be a key contributor to our margin. It will wind down. Other projects will ramp up. The profile of margin of this project will be different. But when I look at the backlog, the mix we have, the LNG contribution, which we said is today at 56% of our backlog, we are very comfortable with the guidance we've given you in the past of 4% to 6% with a 200 bps improvement based on the LNG contribution. As we continue progressing through the transaction, we'll have further engagement with our investors community. And of course, we will look forward to giving you a little bit more color on what this margin will look like in the next few quarters and years.

Michael Alsford - *Citigroup Inc, Research Division - Director*

And sort of an unrelated follow-up, really, I guess is on the spin-off. I was wondering whether you can give any more color as to how you see the capital structures of both businesses, please.

Maryann T. Mannen - *TechnipFMC plc - Executive VP & CFO*

Sure. Thanks, Michael, for the question. We will be providing some good color here coming as you see the prospectus looking into the way that we are anticipating these structures for both SpinCo and RemainCo. As we've said before, our intent is to create 2 investment-grade companies, both SpinCo and RemainCo, and that continues to be our goal and objective as we go forward. So as you will see the prospectus, you'll have historical information, and you will also have a view of the way that we see the capital structure being outlined. And that will be coming very soon.

Operator

Your next question comes from the line of Dan Boyd with BMO Capital Markets.

Dan Boyd - *BMO Capital Markets Equity Research - Oilfield Services Analyst*

Two different questions. The first one, I just want to kind of go back to Subsea margins. And when you gave you guidance this year, I believe vessel utilization is running higher than you expected, and you're seeing a little better growth rates out of the service side of the business, which I also thought carries slightly higher margins. So is there an offsetting factor that maybe you didn't see coming into the year when you issued the guidance that's not providing upside to that margin target? Has pricing been a little bit more competitive than you thought? Or is there anything else that we should be thinking of?



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Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

Sure, Dan. And I don't disagree with the comments that you made, so I won't repeat those. Keeping in mind, when we look forward, there's really 2 things. One is you kind of got to predict the timing of when you're going to meet critical milestones, which, again, you can't do on a quarter-by-quarter basis, both in terms of as you're going to roll off a higher-quality backlog from the historical backlog, and then obviously, the new projects and the new inbound that's coming in. It is clear, and I have said this repeatedly, and I know it maybe hasn't been consistent across the sector, but we are not seeing a material improvement in competitive pricing when it is vessel-only contracts, or if you will, day-rate-type contracts. That's why we've tried to stay out of that market, unless we had a strategic reason or a true differentiation to be able to participate in those contracts. Instead, what we've done is we've decided to stay focused on keeping that capacity available for our integrated projects, again, many of which are targeting around a total project economic or total project return to where it's a true win-win for us and for our clients. And the ones that we've completed to date have all met or exceeded their project returns. So we're building a really incredible and strong case of references. That's why we're seeing so many repeat orders from our clients as this business model continues to be adopted and recognized going forward.

So -- but look, Dan, I'll repeat again, and I know it hasn't -- I know others are saying different things, but we are not seeing, as -- when it gets out there in just a, let's say, a commoditized tender where you're voting -- or you're -- excuse me, where you're tendering on just a vessel or just a vessel day rate that we're seeing a strong -- a change in the pricing behavior. We have a walk line. We will not go below that walk line, and we have lost awards. And you will see us lose awards in the future because we are just not going to go to that level. These contracts are locked in for anywhere from 2 to 3 years, and there's no reason to do that at this point in time, particularly given the strength of our integrated offering and the fact that over 50% of our orders are coming from that integrated offering.

Dan Boyd - *BMO Capital Markets Equity Research - Oilfield Services Analyst*

Okay. That's helpful. My follow-up question is just on the cash return profile. Just given the backlog that you see, how are you thinking about the dividend growth or kind of bringing back the buyback? What's the outlook over the next, maybe, into 2020?

Maryann T. Mannen - *TechnipFMC plc - Executive VP & CFO*

Thanks for the question. Obviously, as we continue to work through the separation of our 2 companies, we'll be refining the capital allocation strategies for both TechnipFMC and for SpinCo, and those policies will be clearly communicated to you. As Catherine said, she'll be looking forward to providing incremental color on SpinCo. And certainly, for RemainCo, we'll give you greater color on the way that we see the capital allocation policy unfolding going forward.

Operator

Your next question comes from the line of Jean-Luc Romain with CM-CIC Market Solutions.

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

Jean-Luc, perhaps you're on mute.

Operator

Jean-Luc, your line is open.

Your next question comes from the line of Kurt Hallead with RBC.



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Kurt Hallead - RBC Capital Markets, LLC, Research Division - Co-Head of Global Energy Research & Analyst

Doug and Maryann, thanks for the incremental color here this morning. It's always an interesting dynamic on how investors kind of react to certain information. But I want to come back around to some discussion points, Doug, and maybe give us some perspective as to your viewpoints on what is -- what you see happening and what your vision is for Subsea beyond 2.0. I think some investors out there might think that pretty much Subsea 2.0 and the benefit of that will have pretty much run its course in 2019 and kind of wondering out loud what the encore is to Subsea 2.0. So any perspectives on that, I think, would be helpful.

Doug Pferdehirt - TechnipFMC plc - Chairman of the Board & CEO

Thank you, Kurt. So I would reassure the community that Subsea 2.0 certainly will have not run its course in 2019. I think there's much more to be done. Obviously, we've talked before about the fact that the largest percentage of our FEED studies, or front-end engineering studies, now includes Subsea 2.0. We keep talking quarter after quarter about the deployment of additional Subsea 2.0 technology. I think there were at least 2 references to that in the press release this quarter. But the real beauty of it, Kurt, is as it runs through our organization because the Subsea 2.0 philosophy, it's more than just about the equipment. It's about a change in the operating model for the way that we run the company, and it gives us much greater leverage across our cost base that we will be able to recognize and benefit from that going forward. So I would say we're actually far from seeing -- or just I'd say in the early stages of seeing the impact from the Subsea 2.0 technology. And on -- beyond Subsea 2.0, it's easy to get me wound up, and I want to leave time for other questions. But look, we have a clear vision that goes far beyond Subsea 2.0. Subsea 2.0 was just the beginning. And I remind everyone that Subsea 2.0 was born a vision, and most of the engineering was born before the merger and creation of TechnipFMC. So now with the increased scope of Subsea activity, meaning including umbilical, risers, flowlines and installation, it is baffling how much we'll be able to do beyond Subsea 2.0. We have 14 discrete engineering programs underway right now supporting what will be and could be the building blocks for Subsea 3.0 and beyond.

So Kurt, I -- it's what gets me excited. It's what keeps me going, if you will. There's a whole lot left to be done, and we're just in the early stages of it. We're super proud of the creation of TechnipFMC. We're super proud of the iEPCI. We're super proud of 2.0, but it's really just the beginning.

Kurt Hallead - RBC Capital Markets, LLC, Research Division - Co-Head of Global Energy Research & Analyst

Great. And then maybe as a follow-up. I think in terms of the value proposition that Subsea 2.0 and maybe the next leg of what you just mentioned, right? And correct me if you think I've been mistaken on this, but it's -- part of it is accelerating the time to first cash flow for these projects for the oil companies. And the reason I bring that up is doesn't that kind of take you out of the realm of having to kind of do a pre-bid and a buy process? And don't you think you have maybe a little bit more upside on margins than what you would have historically seen in the Subsea business?

Doug Pferdehirt - TechnipFMC plc - Chairman of the Board & CEO

By nature, I'm very conservative, and I -- so I don't want to get ahead of ourselves here, but let me just be -- let me just stick to the facts. As you know, most of our awards in iEPCI have been direct awards, again, as a result of early engagement with the client, working in an open and collaborative way to redesign the Subsea architecture, removing waste that was nothing but cost to the project and changing our execution model to where, indeed, we can have a significant improvement in the time to first oil, which really drives the project returns. And that's why we have been able to be so successful. Impossible to do, unless you're a single company that controls all the levers. Very, very difficult to do otherwise. That's why we couldn't be more happy -- happier, and we're seeing the benefit, and the market is recognizing the benefit of the creation of TechnipFMC and the integrated Subsea solution. So more to come.

As I said, yes, there'll be more leverage from it, the greater the level of penetration into our backlog and into our business. We are demonstrating to our clients, again, on a repeat basis now the benefit of this type of methodology. And just if you think about the conversion rate, I mean, it's just -- it's astronomical to think that we could in such a short period of time have such a significant conversion rate. And in my prepared remarks, it may not have been picked up on, so I'll just repeat. When we talk about a 50% improvement in our inbound order rate in Subsea, the highest in over a



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decade, but the market in the same time frame or the 1-year time frame with the 50% improvement only improved by 20%, one can interpret what that means in terms of the way that the market is recognizing our success.

Operator

Your next question comes from the line of Bertrand Hodee with Kepler Cheuvreux.

Bertrand Hodee - *Kepler Cheuvreux, Research Division - Head of Oil and Gas Sector Research*

Yes. Two, if I may. When do you think you will provide the market with a Subsea margin for 2020? This will be my first question.

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

Bertrand, thank you for the question. We will report the -- we will be providing 2020 guidance when we have our Q4 and year-end earnings call.

Bertrand Hodee - *Kepler Cheuvreux, Research Division - Head of Oil and Gas Sector Research*

Okay. And one follow-up on Subsea services. You clearly pointed that Subsea services is gaining traction this year, if I recall the slide, plus 17%. When I look now at your backlog scheduling in Subsea for Q4, excluding Subsea services, it looks already very strong at above \$1.42 billion. So it looks like -- so it's implicit, I would say, Subsea revenues for Q4 looks around \$1.7 billion, so quite a step up compared to Q3. And then where do you see Subsea services going forward? Is it well established now at above \$1.2 billion per year and you see further growth to those numbers possibly?

Doug Pferdehirt - *TechnipFMC plc - Chairman of the Board & CEO*

Okay, Bertrand. I'll cover the first part, and then I'll pass it over to Maryann. I want to thank you for recognizing and emphasizing the fact that when we look at our backlog schedule, most of our Subsea Services businesses is not reflected in that backlog schedule because it's book-to-bill and it has to be added to it. So you're right. We're in a very strong position. Again, the benefit of having such a high level of inbound year-to-date and it being front-end loaded is actually a great benefit when you start to look for revenue coverage or the outlook for 2020. So you're right to point that out. I'll let Maryann add the additional color.

Maryann T. Mannen - *TechnipFMC plc - Executive VP & CFO*

Thanks, Bertrand. So just a few more items around your question for the fourth quarter. Our guidance on a full year basis is in a range of \$5.6 billion to \$5.8 billion, which likely, we could trend towards the lower end of that range versus the top end of that range. When you look at the backlog scheduled for the remaining 3 months or for the balance of 2019, you're sitting at about \$1.4 billion. But just keep in mind our Subsea Services is not backlog. So you would need to add the estimate for Subsea Services. And as we've kind of talked about numbers, that several hundred million of backlog that you wouldn't see in that number, this merely reflects the iEPCI or the project element. So services will be inbound in the quarter just like it is every other quarter. And that's how you would get to the full year range that you said in a range of \$1.5 billion to \$1.7 billion.

Operator

And our last question will come from the line of Marc Bianchi with Cowen.



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Marc Bianchi - *Cowen and Company, LLC, Research Division - MD*

First question has to do with the corporate expense. Maryann, you helpfully mentioned that fourth quarter would be \$40 million to \$45 million. And I appreciate that there was some IT spending previously, but even throughout the first 9 months of the year, it was materially above that level. Should we expect a \$40 million to \$45 million kind of run rate for the combined company beyond fourth quarter? Or could you talk to how you see that developing?

Maryann T. Mannen - *TechnipFMC plc - Executive VP & CFO*

Yes. Sure. No, appreciate the question and understand. Yes, you're right. From a run rate perspective kind of underlying, that's been our trend, and that's a trend for the combined company, TechnipFMC. I certainly don't want to try to give you color right now on what the combined corporate expense would look like for SpinCo and TechnipFMC. Obviously, we'll give you some guidance around that. But from a run rate perspective, it's been fairly consistent with the exception of that sort of unique spend of that discretionary spend this year.

Marc Bianchi - *Cowen and Company, LLC, Research Division - MD*

Okay. Is there anything in that \$40 million to \$45 million that is related to preparation for the separation?

Maryann T. Mannen - *TechnipFMC plc - Executive VP & CFO*

Look, it's hard to say unequivocally yes or no. Obviously, there's lots of people, right, in the organization who are working on the spin. But I think it's reasonable to say that there are certain activities that we are targeted to get the spin complete and meet our accelerated time line. I think that would be a fair assumption.

Operator

I will now turn the call back over to Mr. Seinsheimer for closing remarks.

Matt Seinsheimer - *TechnipFMC plc - VP of IR*

This concludes our third quarter conference call. A replay of our call will be available on our website beginning at approximately 8 p.m. British Summer Time today. If you have any further questions, please feel free to contact the Investor Relations team. Thank you so much for joining us. Operator, you may end the call.

Operator

Thank you. That concludes this conference call. You may now disconnect.



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