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SLB.N - Q1 2023 Schlumberger NV Earnings Call

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OVERVIEW:

SLB reported 1Q23 revenue of $7.7b and 1Q23 GAAP EPS of $0.65. Co. expects 2Q23 revenue to grow about mid-to-high single-digits.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the SLB Earnings Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

I would now like to turn the conference over to the Vice President of Investor Relations, ND Maduemezia. Please go ahead.

Ndubuisi Maduemezia - *Schlumberger Limited - VP of IR*

Thank you, Lea. Good morning, and welcome to the SLB First Quarter 2023 Earnings Conference Call. Today's call is being hosted from Rio, Brazil, following our Board meeting held earlier this week. Joining us on the call are Olivier Le Peuch, Chief Executive Officer; and Stephane Biguet, Chief Financial Officer.

Before we begin, I would like to remind all participants that some of the statements we'll be making today are forward-looking. These matters involve risks and uncertainties that could cause our results to differ materially from those projected in these statements. I therefore refer you to our latest 10-K filing and our other SEC filings.

Our comments today may also include non-GAAP financial measures. Additional details and reconciliation to the most directly comparable GAAP financial measures can be found in our first quarter press release, which is on our website.

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

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Thank you, ND. Ladies and gentlemen, thank you for joining us on the call today. In my prepared remarks, I will cover three topics. I will begin with an update on our first quarter results. Then I will share our latest view on the macro and our positioning for long-term success. And finally, I will close with our outlook for the second quarter and full year. Stephane will then provide more details on our financial results. And we'll open for your questions.

It has been a great start of the year as we have achieved results that set us on a solid footing for our full year financial ambitions. On a year-on-year basis, our financial and operational results were strong across all geographies and divisions. Following the remarks that I shared in our earnings release this morning, I would like to emphasize a few key highlights from the quarter.

First, we delivered very solid year-on-year growth at a magnitude lasting more than a decade ago. Geographically, year-on-year growth rates in North America and internationally were comparable. More importantly, the rate of change is tipping more in favor of the international market, where sequentially we experienced the smallest seasonal decline in recent times. Collectively, our Core divisions grew year-on-year by more than 30% and expanded operating margins by more than 300 basis points.

We continue to position the Core for long-term success with significant contract wins and technology innovations that improve efficiency and lower carbon emissions. A great example is EcoShield, a geopolymer-based, cement-free well integrity system and one of our latest Transition Technologies launched earlier this quarter. You will find many examples of these contract wins and the performance impact of our new technologies in today's press release.

In digital, we maintained strong growth momentum and also secured more contract wins. At the division level, the amount of year-on-year revenue growth in digital was somewhat masked by significantly lower EPS revenue due to production interruption in Ecuador and lower project revenue in the Palliser asset in Canada. Additionally, digital continues to help us elevate our efficiency and margin performance in the Core as we deploy this solution at scale in our global operations.

And in New Energy, we continue to make progress across our portfolio, notably with new carbon capture and sequestration activities that raise our involvement to around 30 projects globally. CCS is recognized as one of the fastest-growing opportunity to reduce carbon emissions. And with the tailwinds from the U.S. Inflation Reduction Act and other initiatives around the world, we expect more projects to move forward to final investment decisions in the next 2 years.

Finally, we are delivering on our commitment to increase returns to shareholders. During the quarter, we relaunched our share buyback program with repurchases totaling more than $200 million worth of shares. I would like to really thank the entire SLB team for their hard work and for delivering yet another successful quarter.

Moving to the macro. We maintain a constructive multiyear growth outlook. Through the first quarter, the resilience, breadth and durability of the upcycle has only become more evident. I would like to take a few minutes to describe these factors.

To begin, the underlying demand, investments and activity during this cycle are resilient despite short-term economic and demand uncertainties. The combination of energy security, the initiation of long-cycle projects and OPEC's policy sets the condition for a decoupling of the activity outlook for short-term demand uncertainties.

Indeed, energy security remains a top priority for most countries and is driving structural investments that are governed primarily by national interest. The extent of these investments is resulting into a broad-ranging growth outlook, comprised predominantly of resilient long-cycle projects in the Middle East, the international offshore basins and in gas projects. Collectively, we expect these market segments to reach or exceed more than 2/3 of the total global upstream spend and support a long tail of resilient activity over the next few years.

In parallel, the North America market, characterized by higher short-cycle exposure, is also set to benefit from positive demand outlook and supportive commodity pricing. However, this will be impacted by an anticipated activity plateau in the short term, which will subsequently be reflected in production volumes.

Moving to the dimensions of breadth and duration. These are also best emphasized by the latest activity outlook for the Middle East and offshore market segments. Fundamentally, the pivot to both segments as anchors of supply growth is a defining attribute of this cycle. This is providing an unprecedented level of investment visibility and a scale that is setting many records.

In the Middle East, the largest-ever investment cycle has now commenced. This will support ongoing capacity expansion projects over the next 4 years in both oil and gas. Consequently, this year, we expect to post our highest revenue ever in the Middle East, putting us on track to achieve our multiyear growth aspiration.

Simultaneously, we are witnessing further activity expansion in the offshore market. Offshore activity continues to surprise to the upside with breadth and a diversity of opportunities across all major basins. In addition, the latest FID projections and industry reports indicate that the offshore sector is set for its highest growth in a decade with more than $200 billion in new projects through the next 2 years.

This growth will be supported by three layers of activity. First, the resumption of infill and tieback activity in mature basins, which was very visible across Africa in 2022. This will continue to strengthen in multiple geographies from this year onward. Second, ongoing large development projects in both oil and gas that are ramping up and starting to scale. This is evident in Latin America, such as Guyana and Brazil, and in the Middle East, such as in Saudi Arabia, UAE and Qatar.

And third, the resurgence of exploration and appraisal activity, which is starting to gather strong momentum in the existing basins and new frontiers. From West and South Africa to the East Mediterranean, we are starting to see exploration and appraisal at a pace that was unforeseen just a few months ago. Additionally, the activity pipeline continues to elongate with new licensing rounds and new blocks awarded. As a result, we believe that we'll continue to witness durable offshore investment for many years to come.

Let me spend a couple of minutes highlighting what this means for SLB. As the cycle unfolds, the characteristics I have described continue to align with major strengths in our Core. This will support additional activity intensity for Well Construction; accelerated growth opportunity in Reservoir Performance through the return of exploration and appraisal activity; and further long-term growth potential for Production Systems.

One such example is the TPAO Sakarya project in the Southern Black Sea offshore Turkey. This project involved all our Core divisions, supporting the development of a challenging subsea gas asset and a simultaneous construction of a gas production facility, demonstrating SLB's unique ability to integrate at scale from pore-to-process.

Looking more in depth. Our Production Systems division is in a unique position as a long-cycle lever of growth for us with quarterly year-on-year results demonstrating our ability to fully harness its potential. We believe momentum is set to continue, benefiting from our strong market presence in the Middle East and in offshore basins.

In this division, we anticipate cumulative bookings in the range of $10 billion to $12 billion in 2023, up significantly from 2022. We have taken a strong step forward towards this ambition with more than $3 billion bookings in the first quarter. And the outlook supports continued strong bookings through at least 2025. Overall, this will provide durable revenue growth and a significant installed base for services in the years to come.

In this context, our exposure to the deepwater subsea market remains an essential component of our growth opportunity. And we continue to strengthen this part of our portfolio with much success. In subsea, we have grown 20% over the last 2 years and are already generating EBITDA margins in the high-teens, building on our technology, performance in execution and the depth of our processing portfolio. We expect strong momentum for this part of our business to be sustained through 2025 and beyond.

To conclude, we are in the midst of a unique cycle with qualities that enhance the long-term outlook for industry, resilience, breadth and durability, all reinforced by a pivot to the Middle East, offshore, gas and return of E&A. We could not ask for a better backdrop to execute our returns-focused strategy. During the early phase of this cycle, led by North America, our results have already demonstrated our ability to capture growth ahead of activity and expand margins visibly beyond pre-pandemic levels.

Looking forward, we are positioned to fully harness the international and offshore momentum that is now underway and to further our margins expansion journey. In the quarters ahead, we'll continue to demonstrate our returns focus, capital discipline and commitment to shareholders' returns. I'm truly excited about the outlook for SLB.

Next, I would like to comment on our progress over the shorter term. For the full year, our strong first quarter gives us renewed confidence in our financial ambitions for 2023. We are primed for revenue growth and margin expansion through the year, underpinned by a very solid international outlook.

In North America, we still expect tangible market growth but at a lower rate than originally anticipated at the start of the year, mainly as a result of ongoing weakness in gas prices. Taken together, we expect the strong international growth to offset any weakness in North America, keeping our full year ambitions intact with year-on-year growth in excess of 15%, which should support adjusted EBITDA growth in the mid-20s.

More specific to the second quarter. Directionally, we expect revenue to grow about mid- to high single digits with operating margins expanding by 50 to 100 basis points, driven by a seasonal rebound in the international markets. Growth will be led by Middle East and Asia area and continued momentum in the offshore markets.

Building on this, we expect our second quarter adjusted EBITDA to reach new highs in this cycle, further expanding the earnings growth journey we initiated 11 quarters ago and taking another positive step towards achieving our full year ambitions.

I will now turn the call over to Stephane.

Stephane Biguet - *Schlumberger Limited - Executive VP & CFO*

Thank you, Olivier, and good morning, ladies and gentlemen.

First quarter earnings per share excluding charges and credits was $0.63. This represents an increase of $0.29 or 85% when compared to the first quarter of last year. In addition, during the first quarter, we recorded a $0.02 gain relating to the sale of all of our remaining shares in Liberty, which brought our GAAP EPS to $0.65.

Overall, our first quarter revenue of $7.7 billion increased 30% year-on-year as the growth cycle continues to unfold. This represents the highest quarterly year-on-year increase in more than a decade. International revenue was up 29% year-on-year while North America increased 32%.

Company-wide adjusted EBITDA margin for the first quarter was 23.1%. In absolute dollars, adjusted EBITDA increased 43% year-on-year. As a reminder, our ambition is for adjusted EBITDA to grow in percentage terms in the mid-20s for the full year of 2023. The first quarter was certainly a strong start towards achieving this goal.

On a sequential basis, revenue decreased 2%, mostly driven by seasonally lower revenue in Asia and Russia as well as lower APS revenue in Ecuador. Russia represented approximately 5% of our consolidated Q1 revenue.

Sequentially, our pretax segment operating margins declined 178 basis points, largely due to seasonality and lower APS revenue. From a year-on-year perspective, margins expanded 298 basis points with significant margin growth in three of our four divisions.

Let me now go through the first quarter results for each division. First quarter Digital & Integration revenue of $894 million decreased 12% sequentially with margins declining 8 percentage points to 30%. These decreases were primarily due to lower APS project revenue and seasonally lower digital and exploration data licensing sales.

The APS revenue decline was mostly a result of a pipeline disruption in Ecuador that temporarily reduced production and lower commodity prices impacting our project in Canada. As a result of these issues, APS revenue declined year-on-year.

But this effect was more than offset by strong digital growth, including a more than 50% increase in our cloud and edge solutions. Margins for the Digital & Integration division are expected to improve in Q2 as the pipeline issue in Ecuador has been resolved and as digital sales will increase sequentially, in line with the usual seasonal trend.

Reservoir Performance revenue of $1.5 billion decreased 3% sequentially while margins declined 207 basis points to 16.1%. These decreases were primarily due to seasonal activity reductions in Europe and Asia and lower revenue in Russia. Year-on-year, revenue grew 24% and margins increased 291 basis points, driven by strong growth internationally, both on land and offshore.

Well Construction revenue of $3.3 billion increased 1% sequentially while margins of 20.6% decreased 44 basis points. However, year-on-year revenue grew 36% while margins expanded 444 basis points with very strong growth across all areas on higher activity, increased pricing and a favorable technology mix.

Finally, Production Systems revenue of $2.2 billion was essentially flat sequentially and margins declined 148 basis points to 9.3% due to seasonality and the activity mix in Europe and Asia.

Year-on-year, revenue increased 38% while margins expanded 217 basis points, driven by strong activity across all areas, led by Europe, Latin America and North America. Margins also improved compared to the first quarter of last year as supply chain and logistics constraints continued to ease.

Now turning to our liquidity. Our net debt increased approximately $1 billion sequentially to $10.3 billion. During the quarter, we generated $330 million of cash flow from operations and negative free cash flow of $265 million, reflecting the seasonal increase in working capital we typically experience in the first quarter.

This largely reflects the payout of our annual employee incentives and the buildup of working capital that will support our anticipated growth throughout the year. Our second quarter free cash flow is expected to be materially higher and to continue to increase into the third and fourth quarters.

Capital investments inclusive of CapEx and investments in APS projects and exploration data were $595 million in the first quarter. For the full year, we are still expecting capital investments to be approximately $2.5 billion to $2.6 billion.

During the quarter, we monetized our remaining investment in Liberty, which resulted in net proceeds of $137 million. We also spent $244 million, net of cash acquired, on acquisitions and investments in other businesses, the majority of which relates to the Gyrodata acquisition.

Finally, we resumed our stock repurchase program and repurchased 4.4 million shares during the quarter for a total purchase price of $230 million. We will continue to repurchase shares in the coming quarters. And as previously announced, we are targeting to return a total of $2 billion to our shareholders this year between dividends and stock buybacks.

I will now turn the conference call back to Olivier.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Thank you, Stephane. Ladies and gentlemen, I think we will open now the floor to your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We go to the line of James West with Evercore ISI.

James Carlyle West - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Olivier, you and Stephane, you outlined kind of an unprecedented, quite frankly, amount of contract awards, amount of visibility into the cycle. And curious, as you talk to your customers now, what you see as the durability of those awards, given the global volatility in economies and things of that nature.

How are you thinking about the next several years? How are you guys perceiving kind of the steadiness of these contract awards and their ability to continue to go forward, even if we were to have a recession or something like that, and how that would influence your revenue and results?

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

No, James, thank you. I think, indeed, I think we have highlighted, and I think in my prepared remarks, I shared the view that in the recent months and certainly in the last quarter, and I have been traveling in Asia, Middle East and South America, I have seen customers, I think, taking commitments and being ready to commit to the supply capacity and to the partnership they need to deploy and develop the assets going forward.

As we believe this cycle is unique through, as we said, element of resilience by the nature of investment and growth rate, including the long-term capacity expansion committed in Middle East, including the large long-cycle elements that are growing in proportion, led by offshore deepwater coming back.

The breadth, I think everywhere we go, every geo unit is seeing customer reaching out to mobilize resource, sometimes for short-cycle production enhancements, most of the time for development, commitment of assets and redevelopment expansion from infill to large-scale development. And durability is certainly improving. And duration of the cycle, I think, is improving as we see.

Because beyond the Middle East, '27 targets of capacity expansion from -- for (inaudible) in the country. Other countries are targeting this towards the end of the decade. And here, I'm in the city in Brazil, Brazil has a clear ambition for 4 million barrel by 2030. And I've already committed up to 20 FPSO contract that will continue to build the pipeline of offshore activity subsea in particular going forward.

So I'm very positive about the mix, if you like, of short cycle on production enhancements to address the anticipated supply risk and the commitment -- long commitment from Middle East, from deepwater and offshore operator to complement the long cycle. It's not to offset and not now take precedent over this short cycle and so turn -- as we indicated, a turn into the cycle towards international offshore and Middle East in particular. So that's where we are very confident.

James Carlyle West - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Okay. That's perfect, Olivier. And then a follow-up for me. In terms of pricing, international and offshore versus maybe North America, kind of what you're seeing there in terms of the level of concern, or maybe not concern but level of willingness to accept pricing increases. It seems to me like customers internationally and offshore are more looking at or concerned about availability of service capacity rather than what it actually costs.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Yes, I think the -- we are seeing pricing tailwinds. And we have seen pricing tailwinds in the global market for quite a few quarters and starting in North America. It has turned to international based on two things. First, indeed, securing capacity going forward, giving us -- giving -- considering the tight supply of equipment, unique technology, giving a level of sense of urgency to secure contract and elongating the contract. You have seen example of 9 years contract into the announcement we made today.

And at the same time, I think performance matters. Performance matters to offshore operator. Performance matters for first gas, first oil. And there's a sense of urgency to accelerate the cycle. This is one of the priority. And technology integration also makes a difference and is recognized and is driving a pricing premium. So the combination of supply capacity, the combination of, I would say, a sense of urgency for -- and quest for performance integration and technology deployment is driving pricing tailwinds that are serving us very well.

Operator

Next, we go to David Anderson with Barclays.

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

So question on kind of the duration of the cycle in your Core business. Well Construction is obviously a big part of that. I was hoping maybe you could talk about the pace of Well Construction that you see in front of you this year and where you should see the greatest uptick in activity and kind of the greatest shift in technology as well. I noticed that North America was up 9% sequentially, which is a bit of a surprise. But where does that Middle East ramp-up fit in here?

And kind of also a similar question to what James asked, a question of capacity. If I'm one of your customers, what am I most worried about today? Is it Well Construction? Is that kind of the -- I would have to think that has to be kind of towards the top of the list. But that -- if you can sort of help us understand that a little bit.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Yes. No, I think you are correct. I think the supply of high-performance equipment in the Well Construction domain is under stretch today. I think we are working very closely with our customers to prioritize equipment, prioritize technology application and use integration, use digital to help deliver the performance they expect. So there is a stretch indeed in this. But going forward, I think we are committing the resource when we see the returns to be accretive to our margins and align with our expectation and ambition to continue to expand margins.

So where we see the most activity, clearly, this year is an uptick. And this will be the case as sequentially next quarter is in Middle East and offshore, I think a combination of an integrated contract we have in offshore with relatively complex assets on occasion that demands a lot of technology deployments. And the intensity of activity in Middle East, that is a mix of short-cycle and long-cycle development project, this combination is unique and I think will be pulling more resource, more equipment, more technology and will drive revenue forward up.

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

And was the North America uptick, was that more offshore-driven than onshore this quarter?

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Yes, it was, indeed, absolutely. I think offshore is not only international, I think offshore is happening in North America. North America as Northeast Canada, Alaska offshore and Gulf of Mexico, the combination of which is set to grow and outpace this year, the -- I would say, the U.S. land and North America land activity. So we are also getting the benefit of our fit-for-basin success in North America that continues to hold and help us maintain, grow our share and come on a premium on pricing.

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

And then Olivier, in the D&I business, APS obviously impacted the performance this quarter. I was wondering maybe if you could kind of pull back a little bit and help us understand how the digital business is performing. I think the goal is to hit a $3 billion revenue target.

Wondering if you can kind of tell us where we are now in terms of that run rate. And in order to hit those targets, I'm just curious, is that about your existing customers using digital more? Is it adding more apps to DELFI? Is it adding more customers? Is it all of the above? Maybe help us understand a little bit more...

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

All of the above.

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

I had a feeling you would say that.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Indeed. But I think, indeed, Dave, I think first, in this quarter, obviously, the growth. And we have seen growth rate in digital that is aligned with our expectations, aligned with our ambition to double revenue from 2021 to 2025. We have seen, as Stephane mentioned during his prepared remarks, that the new technology edge and cloud is growing at more than 50%, continuing on the trajectory that we have set in the last couple of years. And we don't see any sign of this slowing down.

And indeed, expansion will come from multiple dimensions, obviously getting more consumption from the existing customer we have. And we are today deploying one of the largest contracts in Petrobras, where we were and we are meeting with the team here, very satisfied deployment and growing number of users. That's an axis, then growing number of applications. And that's where we want to deploy and go beyond geoscience and our petrotechnical suite, if you like, to digital operation, production and digital operation into the drilling domain, automating the full rig Well Construction process.

And again, in Brazil, we are very pleased to meet with Equinor and look after the Peregrino platform, where we're about to deploy for the first time in the world a full automated top side to bottom assembly, full automated autonomous digital journey that we'll realize this year. So we have both the geoscience application deployment, the digital operation. And we have new customers coming in. And you have seen some new contracts that we announced this quarter.

So we are growing to the pace we are expecting to be on our trajectory to double. And indeed, this quarter, this was unfortunately masked fully by the APS setback. But we expect this to resume and to be actually one of the leading growth sequential that you would see in the second quarter.

Operator

Next, we go to the line of Chase Mulvehill with Bank of America.

Chase Mulvehill - *BofA Securities, Research Division - Research Analyst*

So a quick question. I guess, coming back to international and just kind of focusing there, we get questions on this international ramp. And because the last 6 months, we've seen some oil price volatility. We've seen a couple of OPEC+ cuts. And so we kind of get a lot of investor questions if there's been any signs of OPEC slowing down, any kind of planned projects or CapEx plans. So let me just ask you if you've seen any indications of OPEC+ members slowing things down at all in the Middle East.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

No, we have not seen it. We have not seen any impact of businesses. And we don't believe there will be any. We believe that these companies and the national companies are really set and fully focused on mobilizing resource to execute their very ambitious capacity expansion plan. I think you are aware of all the commitments. And it's not only UAE and Saudi. This is across many countries in GCC. And I think this is to grow both oil capacity and also gas and commercial gas across the region.

So I think I had -- I've been recently in the Middle East, and I have not seen any sign of (inaudible) and challenging. And again, the multiplicity of contract awards that were tendered in the last 18 months and most of them multiyear, if not beyond 5 years, are really indicative of the commitment and the capacity expansion plan that have started. Inflection has happened, and you will see this growing for the rest of the year. So we don't foresee any impact.

Chase Mulvehill - *BofA Securities, Research Division - Research Analyst*

Okay, awesome, appreciate the color there. The follow-up is really kind of on CCUS. You had a lot of announcements in your press release, which really highlighted your experience on the sequestration side. But there are other parts obviously of the value chain. And are there other parts that you would actually think that would be a good fit for SLB, like possibly the capture technology side?

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

No, absolutely, I think we have indeed a unique right of play into the sequestration that have translated into significant number of studies and services and modeling in digital that we have provided to a lot of customers. And these customers have approached us to participate, some of them emitters that are non-oil and gas as you have seen some of the examples we gave in the press release earlier today.

And then we are using our technology and innovation capability to explore and to invest into capture technology or to partner as we are partnering with Linde into the application of CCS project across the domain of blue hydrogen and ammonia for decarbonizing the natural gas, ammonia and hydrogen production. So we are indeed either associating or investing into capture technology, hence broadening our scope beyond sequestration and using our right of play to expand and create a business that will stand on its own in the years to come.

Operator

Next, we go to the line of Arun Jayaram with JPMorgan.

Arun Jayaram - *JPMorgan Chase & Co, Research Division - Senior Equity Research Analyst*

Olivier, I wanted to get some insights on what you're seeing within the subsea segment of Production System. I think you highlighted broadly within Production Systems, $10 billion to $12 billion of backlog growth potential this year or bookings potential. I was wondering if you could maybe characterize SLB's technology offering and integration capabilities relative to your peers as well as provide any update on the strategic transaction that you announced last summer.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Yes. Let me take it at the level of Production System first and let me give a quick zoom. So the booking we are talking about is at the Production System level, which is the division encompassing Production System equipment capability from subsea, as you pointed out, from -- actually in well completion, in well actually, subsea surface system processing capabilities.

So when you put all of this together, you get an end-to-end from pore-to-process, from sandface-to-processing that is quite unique in integration and delivery capability. Hence, the opportunity we have to participate at scale and be a provider with our partner, Subsea 7, into the project of TPAO that you heard about, where the first gas to flare was realized yesterday and celebrated by the -- in country.

And this is quite unique. So that's differentiated. We have end-to-end integration capability. We can design and deploy and develop a gas facility. And we have done it in the past. And we can link it, too, with our partners to our subsea development and participate to the completion architecture. So this end-to-end is quite unique and give us opportunity to participate at a large scale into development.

Now very specific to subsea, I think we are also quite differentiated into the way that we can connect to the subsurface. And we have this integration capability from the subsea to the completion architecture. And one thing in particular I would like to highlight or two things, first is the electrical capability of transforming this subsea tree, this subsea control and this subsea well completion control into electric -- full electric capability.

This is a game-changer for the deepwater industry, game-changer for low carbon and control -- digital control of subsea equipment and control of zone equipment and completion. This is very much again the case in Brazil. We are very fortunate to have established here a unique center of excellence. And we have, under the sponsorship of ANP, working with multiple operators that have joined us into a joint development program, where we are deploying and we will soon deploy everything from subsea tree to safety valve to flow control valve fully electric that will change the game and creating a new step. So that's differentiated.

The other differentiated obviously is our processing, boosting and processing capability. You remember the award that we got last year into Shell for gas processing subsea equipment into a large installation in -- and you have seen two awards this quarter in Brazil, highlighting our boosting capabilities. So we are unique into that position. And again, ability we have to integrate processing equipment subsea with the rest of equipment, well or surface, is unique.

And that's something that is adding to our digital capability as well. So when it comes to the announced JV, I think we are seeing the process of going to the regulatory bodies in different parts of the world, so I cannot comment any further than what we commented earlier. This is an exciting outlook, exciting opportunity. But until close, we'll move forward.

Arun Jayaram - *JPMorgan Chase & Co, Research Division - Senior Equity Research Analyst*

Great. Olivier, my follow-up, you and the Board are in Rio this week. I was wondering if you could characterize on what you're seeing on the ground in terms of the upstream spending picture. And obviously, we've had a regime change recently with the new administration. Are you seeing any potential changes to the fiscal or regulatory regime that could impact spending over the next couple 2, 3 years?

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

If anything, this visit has been outstanding, outstanding for the Board, outstanding for engagement we have to customers and clearly highlighting the potential of Brazil to be fulfilling a significant supply growth. In the future, as I said, ANP and Brazil has ambition to reach or exceed 4 billion barrel from 3.3 billion today, I mean, on barrel per day. And they have already laid out the foundation of this of both production enhancement into the mature basin, the Campos Basin or the land basins and accelerating -- continue to accelerate the development of the subsalt deepwater with up to 20 FPSO already into the play.

So I think they also are pushing forward to the next frontier. They are about to explore Equinor margin. That give us another leg, if you like, of Brazil growth in the future beyond the already committed multiyear FPSO contract that are in place. So we don't see any change. If anything, we see an acceleration and extension of the duration of this Brazil outlook.

And if I had to highlight one noticeable change that I've seen, a commitment to decarbonize, a commitment to digitalize that I think is the new -- the leadership is recommitted to. And we have seen it. And you will see it in the future. Digital operation will accelerate in Brazil by the main operator here. And the country will accelerate this commitment to CCS.

We are very fortunate to be on the first and only bioenergy CCS project in Latin America with FS Bioenergia. And we met the team 2 days ago. And they are very pleased with the progress we are making on the CCS product in Brazil. So you will see more activity and no slowdown. But any upside -- only upside to the offshore environment and then a low-carbon and digital transition accelerating as well.

Operator

Next, we go to Neil Mehta with Goldman Sachs.

Neil Singhvi Mehta - *Goldman Sachs Group, Inc., Research Division - VP and Integrated Oil & Refining Analyst*

First question was around cash flow, and working capital specifically was a bigger outflow than we had modeled in the quarter. Does that all reverse over the course of the year and you could talk about some of the moving pieces around that?

Stephane Biguet - *Schlumberger Limited - Executive VP & CFO*

Sure, Neil. So yes, it does reverse. As you know, Q1 is always the lowest quarter of the year for free cash flow. As mentioned, we have the typical working cap buildup. Particularly, we have the payout of annual employee incentives. This is a one-off. It was about $500 million in the first quarter. And then we build inventory for anticipated growth, particularly in the Production System division, as we've mentioned.

So even though it was -- it remained negative, the free cash flow actually came slightly ahead of our own expectations. Our DSO was the lowest historically for a first quarter, so we were quite happy with that. So yes, it will increase in the second quarter. And it will accelerate in the second half on higher EBITDA, continuous capital discipline and working capital unwinding. Keeping in mind, we typically generate the majority of our annual cash flow in H2. But it will increase materially in Q2.

So when you put it all together, the 2023 full year free cash flow will be significantly higher than last year and clearly, on the trajectory to deliver the 10% free cash flow margin we committed for the 2021 to 2025 period. And just to close, this will allow us to, as Olivier mentioned and as I mentioned in my prepared remarks, to return $2 billion of -- to shareholders in the form of dividend and buybacks together.

Neil Singhvi Mehta - *Goldman Sachs Group, Inc., Research Division - VP and Integrated Oil & Refining Analyst*

That's really helpful. The follow-up is just the margins at digital. I think it's hard to isolate because of some of the volatility around APS. Can you give us a sense of how you're seeing the underlying margin trends at the core digital business? And in Q2, that segment margin progression, I would imagine, strengthens as you work through some of these Ecuador challenges.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

Yes. So as a reminder for everyone, I think our Digital & Integration division, I think, comprise and combines digital and exploration data with our Asset Performance Solutions. So at the onset of our digital journey, we have set clear ambition for digital margin to be highly accretive to SLB, at the same time, to accelerate our growth to double our revenue from '21 to '25. We are on that journey and clearly delivering a very accretive margin to SLB.

So now we have demonstrated in the last few quarters last year that we -- when we leverage best performance in APS and our differentiated digital offering, we deliver D&I margin visibly in excess of 30%. Now notwithstanding similar setback as we had natural setback in APS, ambition for D&I as a combination is to continue to deliver highly accretive margins, certainly in the 30s.

So going forward, we expect the margins of D&I to sequentially improve based on the very solid revenue growth from digital and very accretive margin for digital, combined with a return of growth for APS and returning a decent margin for APS. So as a whole, we're expecting to not only revenue increase but margin expand sequentially and to continue to be accretive -- highly accretive for the rest of the year.

Operator

Next, we go to the line of Scott Gruber with Citigroup.

Scott Andrew Gruber - *Citigroup Inc., Research Division - Director, Head of Americas Energy Sector & Senior Analyst*

Olivier, you mentioned the resurgence in exploration, which is great to hear for SLB. One concern out there though is the potentially limited number of experienced geologists across the customer base to prosecute the exploration programs just because G&G departments were definitely scaled down during the pandemic. Is this a legitimate constraint on the strength of the exploration cycle? Or is this capability being rebuilt across the industry? What are you seeing on that front?

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

No, I will not be overly concerned by this. I think there are two factors that are playing into this. The first at digital, I think, is having a significant productivity gain for processing, analyzing and generating prospects, as we call it, from modeling -- from structural modeling to prospect identification. The seismic dataset as well as the capability to process using digital capability has significantly improved. So the ability to create spotlight on the gas find or the oil pools, I think, is better than it's ever been and certainly much better than the last cycle.

And secondly, I think there is a significant service consulting capability that we participate into that can help complement and provide support to our customers. But I would say digital, productivity, technology, that has improved and give higher accuracy, better geology interpretation capability, better structural modeling from seismic to well line and to modeling or to sampling like (inaudible) technology, all combine to give a significant support to the G&G team of our customers and to not slow down but actually accelerate and improve the productivity and ability to generate prospects. So I'm not concerned. And I believe that you will see this prospect to be fast-tracked from exploration to appraisal to development going forward.

Scott Andrew Gruber - *Citigroup Inc., Research Division - Director, Head of Americas Energy Sector & Senior Analyst*

No, that's great. And just how would you compare the strength of this exploration cycle to those of the past? Is the trajectory trending us back towards that 2011 to 2014 period? Could we possibly get back to the mid- to late 2000s levels just as tieback opportunities are consumed? Just some color on the potential strength of this exploration cycle relative to history would be great.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

So I think I will contrast it more by saying the type of activity in exploration that is happening. And I think there are a lot of near-field exploration as it is called or backyard exploration that is being used by most operators that have gained access to critical asset, critical basin or advantaged assets. And they want to explore and do near-field exploration across and beyond and use tieback. So there is a lot of exploration happening across every basin, major basin, that characterize this and has been -- this trend has been going up.

And this trend is certainly different from the greenfield, frontier exploration that characterized maybe the last cycle. However, this cycle, I think, beyond the near-field exploration, we are seeing a return of frontier exploration, driven by energy security, driven by the desire to replace reserves and to secure new gas particularly. And we see it happening across many basins.

I mentioned before, the (inaudible) margin as one. You heard about obviously continuous exploration, which is almost becoming a near-field exploration across Guyana. But if you go across the Atlantic, you will find a lot of exploration happening in the south part of Africa, particularly some huge success for two or three operators into Namibia that are here on the onset of something that could be very significant for the industry in oil development.

And then gas in East Med, I think, has been developing. And you heard about the development that we helped fast-track on the Black Sea. That was also gas. So security is incentivizing people to invest and operators to invest into certain regions with access to the demand market. And near-field is continuing to grow very well. So in combination, it's different from the past, and I will not try to compare the scale. But I think the quality of this exploration and the diversity in terms of customers and in terms of basin is quite unique and is really accelerating this year.

Operator

Next, we go to the line of Roger Read with Wells Fargo.

Roger David Read - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Maybe just to come back to the exploration appraisal kind of question. You mentioned that earlier, slowdown in North America offset or more than offset by what's going on in E&A. So I was just curious, what -- and I think you also mentioned it had materially improved in the last couple of months.

What you think really has led to this increase in E&A? Because it's not as if commodity prices weren't good in '22, right? And there haven't been something exceptional thus far in '23. So is it a change in just how your customers are looking at their future inventories? Or is there something else that's helping to drive this improvement?

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

I think the energy security, the supporting commodity price outlook and the desire, indeed, to go and leverage the cycle, to explore and to tie back reserve to the existing advantaged basin or to fast-track gas or new oil pools as I described earlier. Now the timing of it, the acceleration, I think, is linked more to the availability of -- and the contracting of deepwater rigs or the contracting of rigs offshore or land on some occasion, when it is -- when this exploration is happening more than (inaudible).

But the cycle has started last year of E&A return, is accelerating in line to some extent with the offshore acceleration. And I think it will be part of the mix and will give an opportunity to extend and create a new leg of activity and a new leg of FID in 2 or 3 years from now, when those exploration will have been appraised and will be FID at that time.

So I think it's more -- it's an underlying trend that have started in the last few quarters and have accelerated. And I think that is a more long view that customers are taking and not looking at the short-term uncertainty or short-term commodity price variation and committing on one new basin or committing on expanding near-field exploration. So that's the way we have seen it.

Roger David Read - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Okay. So maybe just the natural evolution within a cycle, I mean, as things get some duration, you would expect the exploration to pick up. One other question for you, just APS, so obviously, kind of highlighted had some issues.

Looking back over the last couple of years, there's been talk of potentially disposing of these assets or at least not investing in them aggressively. I was just curious, it seems like M&A has picked up or at least talk of it within the E&P sector. So more likely, less likely, same to look for a way to exit these assets as you go forward?

Stephane Biguet - *Schlumberger Limited - Executive VP & CFO*

So look, Roger, on APS, we really have to distinguish Ecuador. These are service contracts, tariff-based. There's no intention to exit. And we do need to maintain a minimum level of investment. But rest assured, these projects are highly positive in terms of not only earnings but cash flow.

The Canada asset is a bit different. This is a pure equity position. And it's also very accretive in terms of cash flow even at current commodity prices. And as you know, we ran a process on that particular asset last year. We were not satisfied with the offers we received. So at the moment, we are happy with keeping that asset and the cash flow it generates. But if one day, there is an offer at the right price, we'll certainly consider it.

Olivier Le Peuch - *Schlumberger Limited - CEO & Director*

So ladies and gentlemen, I think I want to give a close to this call, it's almost to the hour. So to conclude today's call, I would like to leave you with the following takeaways. First, the quality of the unfolding upcycle in oil and gas is improving with unique attributes of resilience, breadth and duration. This is very much evidenced by the strengthening outlook in both Middle East and offshore markets and further reinforced by the tight supply balance as demand forecast approach new highs at year-end.

Second, our strong start of the year gives us further confidence in our full year financial ambition. Directionally, the dynamics in international markets will likely offset the moderation of activity growth in North America. In fact, we are witnessing a gradual shift from short- to long-cycle investment and a further transition to international with both effects closely aligned with our strengths and paving the way for an exciting outlook for years to come.

Third, our overall performance demonstrates the strength of our portfolio, focused on the most attractive and resilient market segments globally, both in oil and gas and low-carbon solutions. Our divisions continue to align with customer's utmost priorities on value delivered through performance and integration with digital transformation and decarbonization as industry mandates. Additionally, pricing continues to trend positively, enabling us to extract more value for our products and services.

As a result, we reaffirm our ambition to further expand margins as the cycle unfolds, to grow earnings to new levels in this cycle and to significantly increase returns to shareholders as further demonstrated this quarter. I remain very confident in the alignment of our strategy with the fundamental trends in the energy market and fully trust the SLB team to continue outperforming in this context.

Now before I close, I wanted to announce that ND Maduemezia will be moving to a new career opportunity in SLB after a remarkable stance in his position as Investor Relations VP for the past 3 years. Thank you, ND, for the support and positive engagement with our investors and market analysts. Replacing ND is James McDonald, who is transitioning from his previous role as Americas Land Basin President. Welcome, James.

With this, I wanted to close today's call and wish you all the best. Thank you. Good day, everyone.

Operator

Ladies and gentlemen, this does conclude your conference for today. Thank you for your participation. You may now disconnect.