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OVERVIEW:

Co. reported 1Q21 revenue of $5.2b and EPS of $0.21.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Schlumberger 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 D. Maduemezia - *Schlumberger Limited - VP of IR*

Thank you, Lea. Good morning, and welcome to the Schlumberger Limited First Quarter 2021 Earnings Conference Call. Today's call is being hosted from Houston, following the Schlumberger Limited 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 will 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, and good morning, ladies and gentlemen. Thank you for joining us on the call. In my prepared remarks today, I will cover 3 topics: our first quarter results, our progress on our performance strategy, and finally, our outlook for the second quarter and second half of the year. Stephane will then give more details on our financial results, and we will open the floor for questions.

The first quarter of 2021 was a strong step forward. The quarter unfolded as we anticipated, with acceleration in North America activity and momentum continuing to build in the international markets, aside from the usual seasonal effects. We executed very well within that context. We expanded our global operating margins for the third consecutive quarter, and free cash flow was once again solidly positive.

Here are some highlights in support of this performance. Well Construction sustained growth sequentially, and in North America, outpaced U.S. land rig count, demonstrating enhanced market participation in the recovery. Reservoir Performance grew, when adjusted for the OneStim® divestiture. Digital & Integration delivered another strong quarter with resilient margins on track for our full year target. In North America, execution of our returns-focused strategy drove strong margin expansion, fully aligned with our double-digit margin targets. And in international markets, despite severe seasonality and relative exposure in Russia and China, we continued growth across geographies.

In this environment, as the industry prepares for an upcycle, performance matters, and decision on contract awards and capacity allocation are increasingly driven by technology and execution. We are very pleased with the outcome of several international multiyear contract awards, specifically in Middle East and in offshore, building a pipeline that will support growth in 2022 and beyond.

We are determined to drive performance differentiation, leveraging our fit-for-basin technology and digital capabilities. This combination benefited our integration performance, with our largest LSTK operations achieving a 6% improvement in drilling efficiency during the quarter. This strong start of the year, characterized by resilient revenue, sequential margin expansion and positive free cash flow position us very well to meet our full year financial ambitions and to deleverage our balance sheet. I want to congratulate the entire Schlumberger team, who delivered strong execution for our customers, having positioned us for the growth that is now underway.

Next, I would like to comment on 3 elements of our performance strategy that present further opportunity for growth in this upcoming cycle and beyond: digital, sustainability and Schlumberger New Energy. Starting with digital. 18 months ago, we stated our ambition to lead the digital transformation in our industry and to significantly grow new digital revenue streams. I want today to update you with our progress.

Our digital strategy is a platform strategy, leveraging unique and open platforms, DELFI*, OSDU(TM), and Agora*. Since launching our core DELFI platform, we have significantly expanded its market reach from Google(TM) Cloud to Microsoft® Azure, and more recently, using IBM-Red Hat® technology to enable hybrid cloud and offer fit-for-basin cloud solutions, as highlighted this morning in our collaboration with Yandex.

We'll continue to execute on this platform journey to expand the choice for our customers and to support our 3 digital business streams: workflow, data and operations.

First, we offer our customers the opportunity to transition their technical workflows, from the desktop to the cloud, to realize productivity gains from DELFI workflow integration, collaboration and access to scalable cloud computing.

Our market leadership on the desktop position us very well to capture this market. In the last 18 months, our customers have increasingly transitioned to the cloud, resulting in 50% growth of our contract backlog and a tenfold increase in full-time DELFI users. As we expand our cloud-native applications and enable additional workflow within DELFI, we expect increased adoption across our customer base, resulting in steady growth of our digital workflow revenue.

Second, recognizing that data is the key to unlock the industry digital transformation, we worked with the industry OSDU Forum to open source and contribute the underlying DELFI data ecosystem, helping to establish OSDU as the industry standard, an essential step to liberate data at scale for AI applications and to enable multivendor interoperable workflows. In this context, we recently partnered with Microsoft to offer Azure customers access to our OSDU enterprise data management solution. We will augment this offering with additional AI capabilities and will also expand our geographical reach. The market potential for this data business stream is very significant as it underpins every customer digital transformation, as exemplified by our recent announcement with Equinor.

Third, our customer operations represent a unique opportunity to realize the promise of asset and field digital solution. We designed an open IoT platform, Agora, to enable edge applications, complementing our DELFI platform operational workflows and integrating with our partner, Sensia. Using Agora and DELFI, we are deploying digital operation solutions for drilling and production, both with our customers and as part of our integrated projects. This digital offering can significantly impact our own operations, as was demonstrated this quarter in the Ecuador project and in our main LSTK operations, and also greatly benefit our customers. Our ambition is to establish critical market share in this white space and accelerate collaboration with industry partners to further its adoption.

These 3 digital business streams, workflow, data and operation, built on open platform are supporting our digital growth ambition. We are very pleased with the progress on our platform foundation with the adoption by a broad set of customers and are confident in the success of each business stream as we execute our road maps.

Moving now to sustainability. We are strengthening our commitment to action, particularly as the industry face a decarbonization mandate and world leaders have reaffirmed commitments or advanced stronger goals in recent days. As it relates to climate action, this goes beyond reducing our own greenhouse gas emissions, as we believe there is a significant opportunity for our technology and operating practice to decisively impact and accelerate the industry's decarbonization effort, as well as contribute towards emission reduction goals around the world.

Our technology portfolio includes solutions that help our customers eliminate flaring, reduce fugitive methane emissions and leverage automation and digital surveillance to reduce environmental impact. This technology focus on low-carbon impact will be an increasing element of differentiation for Schlumberger in the future.

An example that resonates with our customer is the complete electrification of offshore production systems, as outlined in our earnings release with the BP project for subsea electrification. This is the next offshore frontier, and it will also pave the way to full digital enablement.

Beyond our industry, our CCS partnership with LafargeHolcim and the bioenergy CCS project in Mendota, California are examples of cross-sectors initiatives aligned with climate actions.

Specifically, in Schlumberger New Energy, we reached milestones in the sectors where we are participating across the energy transition: hydrogen, lithium, CCS, geothermal and geo-energy. During the quarter, we established and accelerated new ventures, formed strategic partnerships and gained market exposure and are progressing in derisking technology for upscaling.

We'll continue to build out the New Energy portfolio throughout the year, and we will keep you updated on our progress. We are extremely proud of the tangible results we have realized in only a short time as it clearly outlines the power of the Schlumberger brand and the potential of this new chapter for the future of the company.

Turning to the outlook—upward revisions in global economic forecast-- growth forecast by the IMF and positive demand forecast adjustment by both IEA and OPEC reinforce the transition into a demand-led recovery, which will strengthen through the second half of 2021, absent new setbacks in vaccination rollouts or easing of lockdowns.

Against this backdrop, we are increasingly confident in our full year activity outlook.

In North America, in the second quarter, we see sustained activity growth in U.S. land and the seasonal rebound of North America offshore being partially offset by the Canada breakup. As our first quarter results have shown, particularly in Well Construction, our new mix and sizable exposure in the North America market will increasingly contribute to our results.

Moving to international markets. Activity growth will broaden in the second quarter with the seasonal recovery in Russia and China, augmenting continued growth in Africa and the Middle East, while Latin America should remain resilient. In addition, the offshore recovery will continue in the second quarter, including the gradual return of exploration and appraisal in key international markets.

The depth and diversity of our international franchise give us a great exposure to this market expansion, especially in Well Construction and Reservoir Performance, which will lead in the second quarter.

More broadly, we anticipate all Divisions to grow sequentially at different pace and margin expansion to be led again by Reservoir Performance and Well Construction.

In light of this, directionally, we expect total second quarter revenue to grow in mid-single digits and our operating margins to further expand by 50 to 100 basis points.

Looking farther into the second half of 2021. In North America, the pace of growth is expected to moderate on budget exhaustion and seasonal effect but could surprise to the upside, resulting in full year growth when excluding the impact of divestitures.

In the international markets, our confidence in the second half outlook has been strengthening based on the latest international rig count trends, CapEx signal and customer engagements. International activity will broaden and accelerate in the second half, impacting short to long cycle, both on land and offshore, including deepwater activity in the most advantaged offshore basins.

The magnitude of these leading indicators, combined with upward revisions to global economic growth and demand recovery, present the potential from -- for an even stronger inflection than initially anticipated for the second half of the year. Therefore, we have greater confidence in the previous guidance of a double-digit increase in international revenue in the second half when compared to the same period last year. And absent of a setback in a post-economic -- post-pandemic recovery, we foresee an upside for full year growth internationally, resulting in a stronger footing as we enter 2022.

In the context of this top line growth and the steps we took to reset the earnings power, we are confident that we will fully realize our operating leverage to deliver our full year ambition of 250 to 300 bps margin expansion year-over-year. We expect to continue expanding during -- margins during the recovery to support increasing cash flow throughout the year, which should provide subsequent deleveraging opportunities.

Now I would like to pass the call to Stephane.

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

Thank you, Olivier, and good morning, ladies and gentlemen. First quarter earnings per share was $0.21. There were no charges or credits recorded during the first quarter of 2021. Excluding the charges and credits recorded in the previous periods, this represents a decrease of $0.01 sequentially and $0.04 when compared to the first quarter of last year.

Overall, our first quarter revenue of $5.2 billion decreased approximately 6% sequentially. However, if we adjust for the OneStim and artificial lift low-flow divestitures, which were completed during the fourth quarter of last year, revenue was essentially flat sequentially despite the first quarter seasonality.

Excluding the impact of divestitures, North America revenue increased 10% sequentially, reflecting a significant activity increase on land, partially offset by lower product sales offshore.

International revenue declined only 3% sequentially despite the effects of the extended winter period we experienced in Russia and the usual seasonality in the Far East.

Pretax operating margins were 12.7% and have now increased for 3 quarters in a row. In addition, pretax operating margins were 230 basis points higher compared to the same quarter of last year. This represents the highest margin since the third quarter of 2019. This strong margin performance reflects the significant operating leverage we have created through the combination of the high-grading of our portfolio and our cost-out program, which is now essentially complete.

Company-wide adjusted EBITDA margins of 20.1% for the first quarter were flat sequentially as the positive impact of the OneStim divestiture was offset by the seasonal effects we typically experience in the first quarter. EBITDA margins were 203 basis points higher compared to the same quarter of last year.

Let me now go through the first quarter results for each Division. First quarter Digital & Integration revenue of $773 million decreased 7% sequentially, driven by seasonally lower sales of digital solutions and multiclient licenses. Margins only decreased by 37 basis points to 32% as the effects of the digital solutions and multiclient revenue declines were largely offset by improved profitability from APS projects.

Reservoir Performance revenue of $1 billion decreased 20% sequentially. However, excluding the impact of the divested OneStim business, revenue increased 3%, despite seasonally lower revenue in Russia and China. The revenue growth was driven primarily by higher activity in Latin America and the Middle East.

Margins increased 260 (sic) [261] basis points to 10.2%, largely due to the divestiture of the OneStim business that was dilutive to the Division's fourth quarter margins.

Well Construction revenue of $1.9 billion increased 4% sequentially, and margins increased 103 basis points to 10.8% due to increased activity in North America land and Latin America. This growth was partially offset by the seasonal slowdown in drilling activity in Russia and China.

Production Systems revenue of $1.6 billion decreased 4% sequentially. International revenue declined 4%, while North America was down 3%.

Despite the revenue decline, margins only decreased 71 basis points to 8.7% as a result of cost measures as well as improved profitability in midstream production systems due to higher activity.

Now turning to our liquidity. During the quarter, we generated $429 million of cash flow from operations and positive free cash flow of $159 million, despite severance payments of $112 million and the increase in working capital requirements we always experienced in the first quarter due to the annual payout of employee incentives. Our cash flow will improve throughout the rest of the year, consistent with our historical quarterly trends.

Our net debt at the end of the first quarter was $13.7 billion, a decrease of $207 million when compared to the end of the previous quarter. During the quarter, we made capital investments of $270 million. This amount includes CapEx, investments in APS projects and multiclient. For the full year 2021, we are still expecting to spend between $1.5 billion to $1.7 billion on capital investments.

On that note, let me take the opportunity to provide you with a quick update on our capital stewardship program. Optimizing the allocation of our capital investments will be critical to maximize the benefits of the ongoing activity recovery, which is poised to accelerate in the next few quarters. As part of the company's reorganization, we implemented a new capital allocation framework that governs all types of investments. The underlying principle behind the framework is that investment opportunities are prioritized based on returns and cash flow before any other metric.

At the corporate level, this framework allows us to critically assess our technology portfolio and rationalize our offering to reduce capital intensity and maximize returns. At the Division level, we have strengthened our processes to ensure that new assets, as well as existing assets, are deployed where they will generate the highest returns. We are also leveraging this capital discipline to drive commercial behaviors and improve the quality of our revenue.

With this in place, we remain confident in our ability to achieve double-digit cash flow margin -- free cash flow margin for the full year of 2021 and beyond. This will allow us to deleverage the balance sheet, which remains a top priority for us.

It is worth noting that during the quarter, the 2 major credit rating agencies confirmed our long-term credit ratings of A2 and A, respectively. And both cited our expected strong cash flow profile and our commitment to deleveraging.

I will now turn the conference call back to Olivier.

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

Thank you, Stephane. So I believe that we are ready to open the floor for the Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question is from James West with Evercore ISI.

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

So Olivier, great to hear your increased conviction about international top line growth in the second half of this year. I'd love to hear or understand how you're thinking about the slope or shape of that recovery and then, really, as it relates more so to '22 and '23, which I think will be very important years.

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

No. Thank you, James. I think, first, I think -- I believe it's clear that we are about to enter demand-led recovery. And I think the macro factor, both economic growth and what we are seeing indicates that the oil demand recovery will reach 2019 level by or before the end of 2022. In this context, I believe that we are ready and starting at, and during the second half of this year, facing the beginning of a demand-led recovery that will trigger a multiyear recovery cycle and industry upcycle.

In this context, if you look at the recent period of underinvestment, look at the structural constraints in North America due to capital discipline, I believe that this will create the condition to create a significant pull on international supply. So this will support international supply activity buildup, not only at the end of this year, but well into '22 and '23.

In addition to this, I believe that the offshore, being a unique market, a privileged market for IOCs, some NOCs and focused independents will also see a gradual but very strong recovery over the long term. It is -- the offshore advantaged basins represents extremely good oil production plateau for some basins at low carbon footprint, so this will support also the long-term international recovery.

So we believe really that we are very well positioned to outperform in this macro because we believe that this macro outlook that would include a growing international mix, including offshore, will play very well to our strength. In addition, we have accelerated our strategy transformation, both the organizational transformation and key strategic elements that will place very well from efficiency performance focus from our capital stewardship, our fit-for-basin that is resonating very well for our customer, and finally, for our digital and decarbonization strategic focus we are putting.

So I believe that we are seeing the beginning of this multiyear growth. We are also seeing that our performance strategy is resonating very well for customers, and we have been awarded several multiyear contract that is -- that are creating the backlog we need to support this growth going forward. So yes, I'm optimistic not only on the second half of this year but on an accelerated path in 2022 and the long cycle strength, including offshore, in '22, '23 and beyond.

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

No. It's very clear, Olivier. Maybe the second follow-up for me is on the margins. You've had good margin progression in the last 2 or 3 quarters. How do you think about sustainable margin progression and expansion as the recovery takes hold?

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

I think going forward, James, as we enter this industry upcycle, I believe there are 3 elements that will favorably impact our margin expansion. First, I think is the -- as I described, is the very favorable macro outlook that combined the pace of international growth, the offshore element and also, as we are starting to see this quarter, the return of exploration and appraisal activity that is still needed to replenish the reserve and also that is becoming more near fleet exploration close to the offshore hubs in particular. So these factors are very favorable.

Secondly, I believe that we have created quality revenue initiatives as part of our initiatives. First, fit-for-basin. Fit-for-basin technology is creating the premium that differentiate us in some critical basin, in some critical assets and give us the premium for revenue quality improvement. Similarly, I think our technology access, as we have seen in North America, has played a great role in helping us to expand market but also to command premium with our technology partner. And finally, the success of digital will be accretive over the period to this.

So the third element, I think, beyond this strategy, I think, is the step change we expect to materialize into our integration contracts. From a performance efficiency using digital, as we have demonstrated already, using fit technology and using practice that are becoming best-in-class. So we believe that these 3 elements, the backdrop, the key element of our strategy for revenue quality and the enhanced margin on our integrated contract will all combine to create a condition for further margin expansion and acceleration of our margin expansion going forward.

Operator

And our next question is from David Anderson with Barclays Capital.

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

Just want to follow up on the discussion around the Middle East. You talked about robust growth in Saudi and Qatar this quarter. It really seems to be kind of the first tangible size of international inflection. I was just wondering if you could talk a little bit about that performance during the quarter and whether or not those were new contracts starting up or existing contracts starting-- coming back on.

But more importantly, I was wondering if you could just talk about the types of tenders that are being discussed in the Middle East. And do you see projects that would be expanding capacity in the region? And also, do you think this will be more project management work? I think you talked about LSTK kind of doing a little bit better this quarter. Do you think that's going to be a bigger part of the mix going forward?

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

I think, first, to comment on our growth in Middle East, indeed, we had sequential growth in Middle East during the quarter. And I think this was led by indeed, Saudi and Qatar, to a large extent. And this was due to 2 factors. Qatar, I think, is our market position, combined with the activity growth, have resulted into activity. In Saudi, I think it's more related to performance and activity share awards that resulted from our performance in execution in the quarter.

And I think we see this factor of a strong market position we have, of performance differentiation to help us go forward. So that's to maybe support and substantiate what we see going forward. In addition to this, as you have seen from last quarter to this quarter, we did announce some critical awards that are securing or expanding this market position in Middle East.

Now there is a lot of LSTK and some of our peers have talked about large and very large contract tenders underway, so I cannot and will not comment on these as these tenders are underway. But what I can say is that the activity is rebounding, the activity outlook, both land and offshore in Middle East, is and will be strengthening. So our customers are indeed securing capacity and looking for best performer and looking for, in a sense, the condition that will make them successful in their ambition to augment their capacity and augment their production going forward. So it will be performance that will matter most in the future for Middle East, in our opinion.

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

Makes sense. My other question is on the digital side. You made a lot of progress over the last year establishing your footprint with the platform with DELFI. Across a lot of IOCs and NOCs, I believe Chevron is actually even implementing across the Permian. So it feels like you're kind of where you want to be in terms of your footprint. It was interesting to hear you talk about the 3 elements of the workflow, data and operations. So I'm just wondering if you could just maybe expand a bit on how you see each the pace of growth in each of those and what is that dependent upon.

Partly I'm wondering, is the customers just getting more comfortable in using digital and day-to-day operations? But do you also need to build out new software applications or maybe it's just something else?

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

No. First, I think it's clear that we need to recognize an industry as it has gone out of this crisis and turn into a new landscape has realized that digital is a tenet of the future, and digital is here to impact efficiency performance and to make this industry more resilient for the long term. So first, there has been a catalyst in the last 18 months that accelerated adoption of digital. That's the first.

We believe that our platform strategy is being recognized, accepted and across different customer type from national company to independent to the IOCs. As you have seen, there is a large adoption of this because we have kept this platform open. Now when it comes to the pace and growth factor that differentiates workflow, data, and operation, I believe that workflow is the one that is the most mature because it builds on our existing desktop market leadership we have. And here, we are transitioning the existing customer base we have towards the cloud.

And each of them is realizing the power of the cloud from productivity, from collaboration, from access to scalable cloud computing, we simply need to reassure them that our platform is open and that they can make the choice, their choice on the cloud infrastructure, which we are doing.

The second data, I think, is renaissance of the data market that used to be a major market in digital 20 years ago. Everybody realized that without the data, we cannot unlock the power of digital transformation. So thankfully, the industry has come together and has created this OSDU platform, Open Subsurface Data Universe, driven by the Open Forum, and we have been fortunate to technically contribute our DELFI ecosystem to this. So on that foundation, every company will have to roll out and will certainly use the opportunity to roll out OSDU as a platform so that it unlocks the data access, liberate the data and then data provider and then service provider, a consulting company and the customer themselves will tap into this data using AI application, and this is where we want to participate, both the data transition to this new platform and the AI opportunity upon this.

Finally, operation. Operation is the biggest prize long term but also the most difficult to realize because every asset, every infrastructure on the field, every infrastructure at the edge is different. So while we believe that there is an immense opportunity to use digital in operation, and we are doing it very successfully internally, the complexity, the system integration needs and the fit-for-purpose digital deployment will slow down on the adoption of this. Yet we'll make progress and we'll continue to partner with other companies to make sure that we offer integrated offering to the industry.

When you combine these 3 at the different pace of growth, you create the condition for multiplicity of revenue stream that will support our double digital ambition that we'll realize within the decade.

Operator

Our next question is from Chase Mulvehill with Bank of America Merrill Lynch.

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

I guess first thing I wanted to hit on was kind of New Energy. So I don't know if maybe at a high level, could you take a minute and talk to how Schlumberger is viewing the New Energy environment? And what are the key highlights of your New Energy transition strategy? And it actually would be great if you could lay out a prospective road map as Schlumberger embarks on this New Energy transition journey.

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

Yes. Great question, Chase. I think as you have seen, we've decided to enter a new chapter for the company. And the way we decided to go after this is to first identify and selectively the domain in which we believe we can leverage our strength. The subsurface can leverage our strengths, our technology and global footprint to create and forge partnership, technology, acquisition, or organically grow the domain.

So first, we have decided to explore and establish market position and diversify our market entrants into this domain. So you have seen that we have, in parallel, from lithium to CCS, from hydrogen to geo-energy and geothermal created ventures, each of them with potentially a different partner for addressing a different industry sector, so that we diversify not only our approach but diversify and expand our market reach. So that has been the first, is to make sure that we diversify our investments, diversify our market approach and our type of partnership. So that has been our first, I would say, framework that we have used to develop this.

Now what is our ambition there? Ambition is to create the future of the company in the long run. So within the decade and within the next 2 or 3 years, specifically, we will derisk at scale this technology investment, these venture investments, working with our partners, working internally to develop those technology as we are for green hydrogen, as we will with our CCS Mendota bioenergy plant or with LafargeHolcim for CCS and cement plant. We will work, develop, embark into venture where we will derisk, enhance, and then when it is derisked at scale, will then make bigger investments, large investments that will then support the long-term growth.

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

Perfect. As a quick follow-up to James' first question around international. You mentioned that 2019 -- so next year, we could kind of get back to 2019 levels. So I guess my question would be, 2019 was pretty tight and you're starting to see some pricing. So if we get back to 2019 levels next year, like what could this mean for pricing? And when we think about the full international cycle, could we actually see a real pricing cycle unfold internationally as the recovery gains momentum?

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

First, I think our approach to this is, first and foremost, performance. We believe that performance creates the revenue opportunity, the revenue quality and the margin expansion, we believe, that are the foundation of our strategy. So now whether the market capacity in some basin for some specific business line will create the condition for pricing, I believe it will. But again, it will depend on how do we differentiate for performance, how do we make sure that our technology is unique and is in high demand and create conditions for the customer to accept to a premium on this technology. And that's our approach.

Now whether the capacity -- global capacity will create, in a short term, global pricing, I don't think it will but I think it will, certainly in the coming quarters, create pricing inflection on some business lines in some basins. We are already seeing it today in North America for very specific Well Construction technology that is in high demand and demand a premium.

Operator

And 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*

So the D&I margin of 32%, super impressive. How should we think about incrementals for that segment over the course of the year? By definition, they obviously need to be healthy, given the starting point. But what's a reasonable range? And relatedly, as you get deeper into these digital management contracts with customers, obviously, profitability improves over time, will that be a material driver during the rest of the year? Or is that incremental margin benefit more in '22 and beyond?

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

No. I think, first, I think we are -- we provided a guidance for full year margin at 30%. And I think you have seen that the way we started the year is putting us in an excellent footing to realize that margin outlook. And this margin comes from 2 major factors: one is the performance of our integration contracts; and secondly, the strength and margin of our digital business.

Now going forward and rolling into the later part of the year, obviously, the digital will gradually start to improve its size and will create and generate the fall through that we believe will support this 30% ambition and could, as we exit 2021, clearly outperform and put us on a better opportunity for margin expansion into 2022. So over time, long term, the digital will indeed grow, and we shared our ambition there and will clearly help continue to support these impressive margins and possibly expand it further in the long term.

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

Got you. And just shifting gears a little bit and maybe somewhat premature to ask, but just given that the international recovery outlook is strengthening, and obviously, the capital intensity of your portfolio is now in a decline, how do you think about the use of free cash flow? Is the focus purely on building cash and deleveraging? What conditions would you look for to start enhancing the cash return? And as we move deeper into the recovery, is there a preference for dividend enhancement versus buybacks when the time is right to return cash?

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

So I'll answer that question, Scott. Yes, you said that our immediate priority is indeed to deleverage the balance sheet. At the same time, we want to make sure that we can sustain growth in our core business, of course, even though our CapEx intensity has reduced quite a bit compared to the past. But we also need to leave enough capacity to execute our strategy, particularly as it relates to new horizons of growth.

So in any case, whether it relates to our core business or white spaces, as I mentioned during the prepared remarks, any new investment will be looked at under the strict lens of our return-based capital allocation framework. And beyond that, yes, once we have filtered all this project, we will return any excess cash to our shareholders through either dividend or stock repurchases. We do not have a prescribed split between the 2. It will depend on the conditions at that time, the time we have to make that decision, and in particular, the sustainability of cash flows.

Operator

And our next question is from Sean Meakim with JPMorgan.

Sean Christopher Meakim - *JPMorgan Chase & Co, Research Division - Senior Equity Research Analyst*

So I appreciate the commentary on the outlook for the Middle East. Maybe just a follow-up. Can we talk about the legacy margin-dilutive LSTK contracts? Just to what extent have you been able to mitigate some of the challenges there? They're now a few years old. I was just curious, to what extent does the contract roll create an opportunity for resetting the margin impact for those contracts maybe in the medium term?

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

Yes. I think, as you know, for the last 2 years, I think we have been increasing our focus management and operational focus on resolving or improving this highly dilutive contract that they were 2 or 3 years ago. And I think we have made great progress. I think whether they are exactly where I would like them to be and accretive to the overall margin, maybe not.

But I think we have made progress in 3 directions: first, in engaging our customers and making them realize the complexity and providing the support to execute this contract with better support and eliminating or mitigating some risk; secondly, by adopting and accelerating adoption within this contract of fit-for-basin technology that are unique and that will create, for the long run, an opportunity to set benchmark on those contracts, hence to keep our market position and enhance our future execution; and finally, we have, in the last few quarters, last few months, actually, to roll out our digital operation capability to extract further automation, further efficiency on this.

So we have improved, enhanced customer collaboration on those contracts. We have created the technology portfolio that is starting to mitigate and enhance the operational execution, and we have rolled out unique digital features that are creating. So those conditions are unique. Customers recognize it and I think as we'll get opportunity to renew this contract and expand would obviously look for making sure the commercial terms and the revenue quality we'll exploit in the future will be more accretive than they are today.

Sean Christopher Meakim - *JPMorgan Chase & Co, Research Division - Senior Equity Research Analyst*

That's very helpful. It's encouraging as well. So just to come back maybe to cash flow. North of $2 billion for free cash looks to be the bar here for full year, just given the 10% margin target. Could you just maybe highlight any major levers that would materially deviate from that goal? And then I'm also just thinking beyond cash flow. Are there plans for potential further pruning of the portfolio to optimize fit-for-basin, maybe help accelerate delevering of the balance sheet?

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

So look, Sean, I don't think there's anything that's going to deviate from us achieving double digit, i.e., possibly more than 10% free cash flow this year. There is a typical seasonality in the working cap and free cash flow throughout the year. So free cash flow will improve quarter after quarter like it has in the past and we will deliver that ambition.

It can be enhanced by exceptional proceeds. We are continuously looking at our portfolio, as I mentioned earlier. We are particularly working on 2 key divestitures: one is I mentioned in the previous quarter in regards to our APS portfolio. We are looking at launching very soon in the next few days, actually, a formal process for the APS asset in Canada. There's a lot of interest still and the economics have improved quite a bit. So we are quite hopeful there to close a good transaction.

And the second one is the rigs we have in the Middle East. We are actually even more advanced there. We are in a formal process. We have shortlisted a few interested buyers and they are just concluding the due diligence. So we should be closing or at least signing, sorry, this transaction in the next few months. So this will enhance the cash flow profile and the potential reduction of our net debt and the flexibility it will give on liquidity basically.

Operator

Next, we go to Connor Lynagh with Morgan Stanley.

Connor Joseph Lynagh - *Morgan Stanley, Research Division - Equity Analyst*

I think we had noticed that you guys were a bit more upbeat on the offshore side of things. And basically, I'm wondering if you could frame how you think that market is going to trend relative to last cycle. And in particular, how do you think customers are thinking about exploration activity?

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

That's a great question. I think, first, it's worth saying that offshore basins and the most advantaged offshore basins are still very much very critical resource and core resource for some of our customers, IOCs, some unique NOCs and a few independents that are pure-play offshore independents from relative medium to large size. So first, this resource are precious. This resource typically have a good geology. And as I said, both from the production plateau, they provide and/or the low-carbon opportunity they have in terms of mix of API grade, I think this excellent resource.

The second thing I believe is that the economics for offshore due to integration success, feed technology, and digital practice have improved from the last cycle. And I think opportunity exists for the industry to leverage this and accelerate some FID going forward.

So another factor that is very critical as you touch the exploration appraisal is that most of the major and large NOC on this -- in this context are recognizing the impact of exploiting hubs, offshore hubs. And the offshore hubs, the opportunity is to exploit those hubs to improve the return on asset, improve return on infrastructure and focus on near-field or backyard exploration so that they maximize the return on existing infrastructure, existing FPSO, existing platform, so that it is also something that plays very well in our portfolio for infield drilling or for subsea tieback as we are expanding in this domain.

So I believe that the exploration appraisal will not necessarily accelerate in frontier exploration but will accelerate in near-field exploration offshore, and we're starting to see this, this quarter and will accelerate during the second half of the year. So I'm optimistic indeed on offshore. And if you read some of the Rystad or IHS reports or some of the report highlighting the FID pipeline, you see that the FID pipeline that are pre-committed towards '22, '23 have the potential over '22, '23 and beyond to eclipse the last 2017, 2019 in terms of number of projects but also in terms of total CapEx invested in deepwater.

Connor Joseph Lynagh - *Morgan Stanley, Research Division - Equity Analyst*

Got it, that's helpful. And maybe just sticking with the offshore theme, could you help us think through on the Production Systems, I think you called out you expected all Divisions to grow sequentially. But how should we think through the long-cycle portion of that business, particularly the subsea business?

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

Yes. I think first, the Production System, I think, is not only subsea system as both short- and long-cycle as exposure in short cycle in North America to the ESP, which is coming back strongly, and the Cameron surface equipment also servicing the frac and our partner, Liberty. And also -- and internationally, it's indeed a mix of short for ESP and some completion equipment and long cycle for midstream as well as for subsea and surface equipment.

So it's a mix of long and short with very tangible exposure in North America, benefiting in short term and long term international long cycle, both recovery and production new projects. In that context and back to the point on offshore, I believe that the subsea market is very alive. And I think last year, the number of subsea trees were short of 200 compared to higher than 50 in 2019. The prediction this year is to be above 200. 220 is our prediction and is aligned with the market prediction. And this will be more or less increasing going forward gradually to be within between 250 to 300 over the midterm period to support this offshore project.

Operator

And our next question is from Marc Bianchi with Cowen and Company.

Marc Gregory Bianchi - *Cowen and Company, LLC, Research Division - MD & Lead Analyst*

The guidance for second quarter for the mid-single-digit revenue and 50 to 100 of margin improvement seems to suggest a little bit maybe weaker margin progression than I would have otherwise expected. And certainly, if I look at the operating leverage that the business has had over the past few quarters, it would seem that there's a little bit less operating leverage implied in second quarter. So I'm curious, are there some unusual costs that you're realizing? Perhaps there's start-up costs for some of these contracts you mentioned? Any color around that and how maybe that could progress beyond second quarter would be helpful.

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

Yes, Marc, thank you for the question. So indeed, our guidance though for operating margin expansion between 50 and 100 bps into the mid-single digits will still imply on the high end of that -- on that range, 30-plus incremental [margin] (added by company after the call). So I believe that this is the first remark.

The second is that we are still on track, okay, and very confident on our 250 to 300 full year --300 bps full year margin expansion. So in the second quarter, indeed, there are 2 factors: one is the fact that you are mobilizing for what the offshore return and some of the activity that are prepping and mobilizing for the second half already in the later part of the quarter. But also there are some persistent but temporary COVID-related constraints and cost that as the lockdown are still in place in many countries, that adding cost upfront into those mobilization and making this mobilization cost maybe a little bit more than they would have been in other cycle the past. So these are the factors that are shaping up, but we are very confident that the margin expansion is in place and will continue going forward.

Marc Gregory Bianchi - *Cowen and Company, LLC, Research Division - MD & Lead Analyst*

Wonderful. And then you mentioned in your prepared remarks and then in -- also in the press release about the kind of double-digit growth for the second half in international setting up for kind of upside to already robust growth anticipated for 2022. I'm curious what the baseline is for that comment. Are you referring to a market forecast that's out there? Or are you referring to sell-side consensus? Just curious what the benchmark we should be thinking about is.

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

No, it's a combination of facts. As I said, I think there are some market indicators on the CapEx of some of the NOC, national oil company. There is the rig count projection that we are making based on our engagement with customer and with rig contractor. And there are some market position or market enhancements and contract award that we have been benefiting in the last few quarters. So the mix of our market position, favorable mix, the market expansion on international for that has an element of seasonal effect as well as reinvestment. And the national oil company increasing their investment in second half all combine to make us more confident on where 3 months ago on the shape and inflection of this recovery in the second half.

Operator

Ladies and gentlemen, I will now turn you back to Schlumberger for closing remarks.

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

Okay. Thank you very much. So thank you, and to conclude, I would like to offer 3 takeaways: first, the macroeconomic and activity outlook are increasingly supporting an attractive industry upcycle, characterized with an inflection in international activity, a consolidation of short-cycle activity and a return of advantaged offshore plays, all playing to our core strength.

In particular, we are increasingly optimistic about the international growth trajectory during the second half of the year, which absent of a setback in pandemic recovery, will result in full year international growth. As a consequence, we have reinforced our confidence in our 2021 financial targets on margin expansion and free cash flow generation.

Second, we are convinced that our performance strategy is aligned with the new industry landscape and is increasingly resonating with our customers as performance matters critically in this environment. This is translating into market wins, partly in Middle East and offshore basins, and we support our ambition to outperform through the cycle. In addition, the steady progress in our digital strategy will translate over time in expanding new revenue streams and accretive margins.

Third, the margin expansion realized this quarter, both sequentially and year-on-year, is reflecting the impact of both our capital stewardship and the restructuring program and will translate into substantial operating leverage as the year progress and activity strengthened in all basins. We anticipate the upcoming quarters to further this margin expansion, with broad contribution from our Basins and Divisions.

Finally, our commitment towards both sustainability and New Energy is materializing in a growing portfolio of technology and ventures that will contribute to the global climate actions and to the future of the company.

Ladies and gentlemen, this year represents a unique opportunity for the new Schlumberger to execute on its new performance journey and outperform the market within an increasingly attractive outlook. Thank you very much.

Operator

Ladies and gentlemen, that does conclude your conference for today. Thank you for your participation and for using AT&T Teleconference Service. You may now disconnect.
