Q1 2024 Financial Results Conference Call

Tuesday, 14th May 2024

Welcome

Christophe Barnini

Senior Vice President, Group Communications and Investor Relations, CGG

Good morning and good afternoon, ladies and gentlemen. Welcome to this presentation of CGG's First Quarter 2024 Results. The call today is hosted from Paris, where Mrs Sophie Zurquiyah, Chief Executive Officer, and from Los Angeles, where Mr Jérôme Serve, our Group CFO, will provide an overview of the quarter results as well as provide comments on our outlook.

Let me remind you that some of the information contains forward-looking statements, and, therefore, that may change at any time. Following the overview of the quarter, we will be pleased to take your questions.

And now I will turn the call over to Sophie.

Q1 2024 Financial Results

Sophie Zurquiyah

Chief Executive Officer, CGG

Thank you, Christophe. Good morning and good afternoon ladies and gentlemen. And thank you for participating in this Q1 2024 conference call.

I would like to start by first recognising Christophe's numerous contributions to CGG. After 28 years in the company and holding various key finance, business and commercial leadership positions, he will be retiring in a few weeks. All the best into your future endeavours, Christophe, and thank you for the great work.

Q1 2024 key segment financial highlights

We are now moving on to slide two. We are off to a good start in 2024. Overall, activity was strong in Q1 across all our three business lines and across all geographic locations. Exploration activities continued to progressively pick up globally with interest from all client profiles in all geographies, including in an increasing number of frontier areas. To respond to projected supply-demand balance, our clients are also continuing to accelerate their field development programmes, where Ocean Bottom Node technology, which requires advanced imaging, is establishing itself as the reference in mature basins across the globe.

The Gulf of Mexico and Norway remain very active, sustained by demand for incremental barrels, which is driving increased high-end imaging and OBN activity. The Middle East and North Africa are active while Asia Pacific is picking up nicely with increasing IOC presence.

Net cash flow

Looking at CGG in Q1, I am very pleased to report our best first quarter since 2018. Overall, the quarter was strong with excellent performance and $30 million in net cash flow generation, despite $20 million paid for our vessel contractual commitments, which highlights the benefits of our decision to become an asset-light company.

Revenue

Q1 revenue reached $273 million, up 30% year-on-year. Geoscience was up 11% year-on-year at $88 million. Global activity remained strong, supported by demand for high-end large projects and NOCs' increasing activity. Earth Data was up 50% year-on-year at $97 million, driven mainly by broader geographical demand. Sensing and Monitoring was up 35% year-on-year at $89 million, with high deliveries of land equipment this quarter.

EBITDA

Segment EBITDA was up 58% year-on-year at $106 million, including $16 million of penalty fees from vessel commitments at 39% margin.

Q1 2024 post-closing events

Now on slide three, there were two positive post-closing events in April that I would like to highlight. First, the S&P Global Ratings upgraded our long-term debt, recognising our commitment to deleverage our balance sheet. And second, the settlement of our long-lasting dispute in India for a net amount of around $30 million. These are positive events for our financial roadmap.

DDE segment: Key business indicators

Going on to slide four, DDE segment revenue was solid this quarter at $185 million, up 28% year-on-year, with growth in both Geoscience and Earth Data. Profitability improved year-on-year to 56% EBITDA margin while still being impacted by penalty fees from vessel commitments.

Geoscience: Key business indicators

Let us go on to the business line now on slide five. Geoscience's external revenue was $88 million in Q1, up 11% year-on-year. Geoscience had very solid activity led by high-end work in all regions. The market continues to strengthen, driven mainly by increased activity in infrastructure-led exploration and field development. Backlog at $227 million is up 23% since the end of last year thanks to catch-up in order intake.

Geoscience: Q1 operational highlights

Geoscience

Slide six, following 18% external revenue growth in 2023, Geoscience grew 11% in Q1 year-on-year. Increasing demand for our high-end technologies, along with the increasing size of projects, drove the solid start of the year for Geoscience. Use of our unique elastic full waveform inversion is expanding geographically, increasingly providing value in all basins globally across all geologic settings, including those that are less [inaudible] definition and fidelity, we can also apply the latest artificial intelligence and machine-learning techniques with our expert modifications to extract insights that accelerate the speed and accuracy of structural and stratigraphic interpretation.

The picture on this slide is a very nice example of the added value of AI to detect sand injectites, and they are in green on the picture in the Norwegian North Sea, which are expected to be oil-bearing. Combining the best geoscience technology with the best data science technology is a powerful combination and fits CGG's strength very well.

New businesses

Looking at our low-carbon businesses in CCUS, we see increasing demand in reservoir screening along with monitoring design. And in Minerals and Mining, we used our high-end imaging technology to successfully map an ore body of interest deep below the surface in Australia to identify new extraction opportunities.

Advanced 4D FWI for better reservoir time-lapse monitoring

Slide seven, we continue to advance the value of seismic for reservoir management. Reservoir engineers are interested in understanding small reservoir changes in time, which has historically been a challenge. Full waveform inversion is increasingly being applied successfully in the space. And this example is offshore Brazil, and it shows our advanced 4D full waveform inversion technology clearly distinguished the producing and water injection layers in the 4D response, helping reservoir engineers adjust their reservoir models and optimise production.

Earth Data: Key business indicators

Now going on to Earth Data, slide eight. In general, we see our clients starting to expand the breadth of their focus areas, especially IOCs, international oil companies, who are regaining interest and becoming more active in frontier areas.

Q1 Earth Data cash CAPEX was $50 million, up 79% year-on-year, driven by a larger portfolio of well-funded ongoing projects. Pre-funding revenue was very strong at $58 million, driving our pre-funding rate to 116%. After-sales were $39 million this quarter, up 32% year-on-year, mainly driven by active projects and interest in South America, North Sea and Africa.

Earth Data: Q1 operational highlights

Slide nine, with a strong level of pre-funding, our portfolio of ongoing multi-client projects is growing larger and geographically broader in scope. This quarter, we completed our second Gulf of Mexico node project ahead of schedule, despite initial weather delays. In Asia, we completed our 2D survey in Malaysia and started a new survey in Australia. We continued the expansion of our CCUS subsurface data packages in the Gulf of Mexico and in the UK, mainly for screening application and the recent CCUS lease round in Norway fits very well our data library.

SMO segment: Key business indicators

Now on Sensing and Monitoring, slide ten. Our Sensing and Monitoring segment revenue at $89 million was stronger year-over-year this quarter, up 35%. The growth was mainly supported by land equipment sales at $39 million while marine equipment sales remained stable year-on-year at $34 million, driven by demand for OBN equipment. Sales from our new businesses were stable at $11 million, and at this level of revenue, the EBITDA margin of the Sensing and Monitoring business line was 11%.

SMO: Q1 operational highlights

Now with highlights on slide 11. During the quarter, SMO sold its first 528 Land Acquisition System together with the new VE564 Vibrator Electronics System. The 528 Land Acquisition System includes several new features designed to improve recording capacity, reliability, productivity and data fidelity [inaudible] this challenging survey requirements. We had significant deliveries of our GPR300 node this quarter in Europe as clients appreciate the quality of our unique sensor, which enables better imaging.

In our new businesses, we deployed a commercial railway monitoring solution during the first quarter, and it is worth noting that we see a progressively increasing portion of our equipment, standard equipment, going to a new group of clients for application outside the oil and gas industry.

Let me now give the floor to Jérôme for more comments on our financials.

Q1 2024 Financial Results

Jérôme Serve

Chief Financial Officer, CGG

A high 59% EBITDAs Y-O-Y improvement

Thank you, Sophie. Good morning and good afternoon, ladies and gentlemen. I will comment the Q1 2024 financial results starting with the P&L on slide 13. Our segment revenue was up 30% year-on-year at $273 million, which was our best first quarter since our decision to become an asset-light company in 2018. As mentioned by Sophie, all Group businesses were up this quarter with Geoscience growing in line with the E&P[?] CAPEX, EDA driven by both higher pre-funding and after-sales, and SMO benefiting from strong land system deliveries.

The respective contributions from the Group businesses were 32% from Geo, 35% from EDA and 33% from the SMO segment.

Adjusted segment EBITDA was $106 million despite $16 million fees related to vessel underutilisation. Segment EBITDA was up 59% year-on-year at a margin of 39%. The segment EBITDA was at $103 million, or 56% margin, and our SMO segment EBITDA was at $10 million, or 11% margin.

Adjusted segment operating income was $29 million, or 11% margin. With an IFRS 15 adjustment of negative $8 million, this led to an IFRS operating income of $20 million for the quarter.

Net income was close to breakeven at minus $3 million.

A solid $30m net cash flow generation despite $(20)m vessel contractual fees

Q1 2024 segment operating cash flow

Moving on to slide 14, Q1 2024 segment operating cash flow, which is EBITDA minus tax, but before change in working capital, was at $102 million. This quarter, we had no change in working capital with the negative impact of our revenue growth offset by the tight management of the sales and inventory, showing the first benefits of the transformation plan that we initiated in [inaudible] at the end of last year.

Q1 2024 CAPEX

Q1 2024 CAPEX was $58 million, up 11% year-on-year. Industrial CAPEX was $4 million down, back to a more normal level, while 2023 included $18 million related to the construction of the new HPC data centre in UK. Research and development CAPEX was $4 million, quite stable, and our multi-client cash CAPEX was $50 million, up $22 million versus last year, driven by our first node project in the Gulf of Mexico. Pre-funding ratio remained very high at 116% this quarter.

Cash cost of debt & other financial items

After \$2 million of other financial items, \$12 million lease repayments, \$3 million discontinued operations, the net cash flow ended up for the quarter at \$30 million. As a reminder, the \$30 million net cash flow does not include circa \$30 million settlements from ONGC, the Indian litigation that Sophie referred to initially, that we received early May.

Net debt / adjusted EBITDA ratio down to 2.2x

Moving on to slide 15, on the group balance sheet. The group liquidity at the end of March amounted to \$350 million, excluding \$90 million of undrawn RCF. Before IFRS 16, gross debt was close to \$1.2 billion and group net debt was at \$858 million. After IFRS 16, group gross debt was close to \$1.3 billion, and net debt was \$966 million. Segment leverage ratio of net debt to segment EBITDA improved to 2.2 multiples at the end of March 2024.

I now hand the floor back to Sophie for the conclusion.

Conclusion

Sophie Zurquiyah

Chief Executive Officer, CGG

Thank you, Jérôme. As a summary, I am very pleased with our first quarter performance. We continue to see gradual improvements in our core markets with continued volatility quarter-to-quarter, especially in SMO and EDA after-sales.

Overall, we see a positive dynamic in our backlog and a higher level of client interactions, which increases our confidence in delivering our 2024 objectives. And in our new businesses, while they are still in the early stages of development, increasing market interest and early feedback from our new clients is building confidence in our unique value proposition and our ability to develop meaningful businesses in the low carbon markets of CCUS and Minerals and Mining, as well as outside of energy in the HPC and Cloud Solutions and infrastructure monitoring market.

Thank you for your interest and we are now ready to take your questions.

Q&A

Daniel Thomson (BNP Paribas): Hi, good evening. Thanks for taking my questions, and congrats to Christophe on the retirement. Firstly, Sophie, if I could just touch on the point around the IOC demand and that coming back, and I think you said previously that that has been the one missing ingredient in this upcycle for the seismic companies. So I wondered, when did you first start seeing the demand from IOCs coming back? How does it compare to previous years? And is it one or two of them or all of them? And lastly, when can we start to see the benefits flowing to CGG?

And then the second question is just on the cash flow. You have left guidance unchanged, but, obviously, we have had a very good Q1. And then combined with the ONGC settlement, I was just wondering on what your expectations are for the rest of the year in terms of cash flow and particularly working capital as you have left that guidance unchanged. Thank you.

Sophie Zurquiyah: Yes, thank you, and good evening, Daniel. Thanks for the great question, as usual. So the first comment on the more the macro environment, IOCs actually have never really left. They have always kept portfolios in frontier areas, but some of them had put them more in the dormant mode and had made comments like they would not go into new countries and things like that. So we are starting to see them this year break those paradigms.

And so we are seeing some IOC who said, 'We will not go into any new countries,' starting to enter new countries. So I would say really this year marks a bit of a broader interest from pretty much across the board. So obviously, as you would know, the American IOCs were, as of last year, already looking more broadly. And initially, when you look at broadly, it does not cost you a lot of money because it is more acquiring, sometimes just 3D seismic data, all the data, looking, evaluating. So you could start doing those things a bit cheaply under the radar, and I think a lot of that happened last year, and this is becoming more visible.

So I would still add a caveat to that, is that they still remain very disciplined. So you will see them focusing on, say, Suriname, you will see them focusing on Namibia, Egypt but more and more, we are seeing, say, Malaysia emerge. We are seeing countries like Uruguay, which is an equivalent to Namibia, on the other side, starting to emerge. Brazil, definitely you saw the last bid run, good interest in the Pelotas area. So I think last year maybe undercover, more work was happening that was not visible externally, but it is becoming more visible this year.

And on the cash flow side, I will let Jérôme answer the question.

Jérôme Serve: Thank you, Daniel. So, honestly, it is a bit early to upgrade the cash guidance at this stage. To be fully transparent, we are actually contemplating a potential strategic, but non-budgeted investment in our library. And the good news on ONGC could help partly fund this investment. So, again, a bit too early and I think we will provide more details in July for future results.

Daniel Thomson: Okay. Thanks. Understood. I will turn it back.

Baptiste Lebacq (Oddo-BHF): Yes, good afternoon. Thanks for taking my question. A special word for Christophe, when I started, he was already there, and I wish for him a good new life. A question from my side, you already answered part of this question, but regarding the cash coming from the ONGC settlement. If I understand quite well your answer, this cash will be used as CAPEX and not to reimburse part of your debt. Please correct me if I am wrong.

And second question, regarding your target in terms of petaflops, what is the target that you have in mind for the end of the year and for the next three or four years? Because we clearly see that there is an acceleration of appetite from AI and so on. What do you have in mind in terms of target of petaflops from your side? Thank you.

Sophie Zurquiyah: So thank you and good evening, Baptiste. I might actually make a comment still on the cash side. I think really what you need to take away from our response is that it is a little early to really define exactly where we will land. So we have a few moving parts, and we just want to be cautious at this point in time and not change the guidance. And Jérôme can add later on.

On the petaflops, this year, we are not going to do a huge increase. Last year, if you remember, we increased our petaflops by 50% from 350 to 500. And the reason we did that is, as we invested into a new centre, we decided to upgrade and change a lot of the material and the computing that was in the old centre into the new centres. There was a big step up. So therefore, this year, we do not expect that number of petaflops to increase significantly. Still around the same number, maybe 5% increase to 530, somewhere along these lines.

But I think that as of next year, we will continue the ramp up, and we have defined a five-year roadmap. And you should see us definitely going into the 600 and 700 petaflops in the next few years. And there is always a balance investing by what do we need for our computing. We are looking, of course, at our CAPEX and our profitability. So we are putting all these elements into the equation. And keep in mind, as well, we work on our efficiency gains. So we constantly work at optimising our workflows so that we could do more with the same amount of petaflops.

So all these things are happening in parallel, and every year we re-evaluate what we need for the following year. But we did a big step-up in 2023, and therefore, this year, we do not need to do such a big step.

So Jérôme, did you want to add on the cash?

Jérôme Serve: So Baptiste, no much further. What I said, obviously, if this investment does not materialise, the additional cash will be used for paying down more debt, either through debt buybacks or, at the time of the refinancing, as per the financial roadmap that we outlined in May. So both options are on the table at the moment and a bit of moving pieces. So that is why we do not want to commit at this stage.

Baptiste Lebacq: Thank you, Jérôme.

Kevin Roger (Kepler Cheuvreaux): Yes, good evening. Thanks for taking the time. And again on my side, congrats to Christophe for all the work that you have done. Those years at CGG has been always very helpful. So thanks for all the things that you have done, Christophe.

If I may come back on the guidance, and maybe on a more broadly side, in terms of top line, EBITDA, because basically, you confirm the full guidance, but you have a Q1 that is probably better than expected. You just mentioned, Sophie, that the international oil companies are, in a way, coming back a bit. So why do you not increase the full guidance on top line and EBITDA, if you have seen those moves recently on the industry?

And the second question is also on the industry. Two of your direct peers, PGS and TGS, are now very close to complete[?] their merger. Have you seen any change in the industry behaviour, even on their side, on the client side? As we are moving close to their merger, is there any change in the industry behaviour? Thanks a lot.

Sophie Zurquiyah: Yes. Thank you, Kevin, and good evening. So why not change the guidance? I think we are in Q1. It is a little early, and, as you know, Geoscience has backlog, and we have decent visibility. So we are confident that Geoscience will continue that gradual increase through the year. We do have continued volatility, both in Earth Data and in SMO, because in Earth Data, again, the sequencing of the after-sale is not linear, unfortunately.

So we had really a good Q1, maybe Q2 is not as good, but we still feel we are on our trajectory. And Sensing and Monitoring has that element too, because it is made of the recurring business, if you want, which is the spare parts for the install base. But then you always have these larger deals that could be in a quarter and not in the next quarter.

So we do expect that quarterly volatility. So I would not draw a straight line again, that okay, we are increasing 30%, we are not going to increase 30% full year. So yes, things all fell in place, many good things fell in place in Q1, but it is early to draw a line for the full year. We are still confident about the full year. And then in Q2, it will be a good time to refine that trajectory for the year. So that is the first question.

On the PGS, TGS merger, we certainly see a change in behaviour of TGS, which is a logical change. As they have become asset-heavy, the natural thing for them to do is to utilise the assets on their multi-client. So there has been a definite trend as of them acquiring Magseis to utilising their own OBN acquisition on their projects. And we do expect to see the same happening once they embrace PGS, that they start wanting to use PGS vessels on their multi-client survey. So that is one change of TGS behaviours, which is totally fair and logical.

The second change, we do see clients are a bit concerned because it creates a larger company. And as a result of that, some clients would tend to favour perhaps a CGG, which is, again, in a setting like that where you have two companies merging, that clients get concerned and want to make sure there is competition out there. So you will see the procurement organisation of the clients start trying to spread the work a little differently.

Kevin Roger: Okay. Thanks a lot for that.

Sophie Zurquiyah: Sure.

Thank you very much. Thank you for attending.

Jérôme Serve: Daniel has one question.

Sophie Zurquiyah: Daniel has one more question.

Daniel Thomson: Hi, sorry. Thanks for letting me jump back in. I did have two further questions if I could. Yes, Sophie, I just wanted to give you the opportunity to maybe talk a bit about the two very recent announcements. Firstly, the CCS alliance with Baker Hughes, any more colour on what you are targeting there and timelines and the firmness of that agreement. And then, of course, the launch of the AI Cloud Solution, yes, just how that feeds in to be on the core growth story.

And then secondly, just on the SMO optimisation plan that was outlined the last quarter, has there been a bit of progress there in delineating the cost savings that we can expect? And would any of that hit in 2024, or is that more a 2025-plus story for the margins in SMO? Thank you.

Sophie Zurquiyah Thank you, Daniel. So, on the first question pertaining to our new businesses, so the Baker Hughes-CGG announcement is very exciting. It actually has been driven by both companies seeing the value of one plus one being more than two. So we each have our strength, and the idea was to be able to provide a larger part of the workflow.

So Baker Hughes, of course, as you know, is all in the subsurface. They actually have quite a number of elements around the surface transportation of CCUS, compressors and things like that. And we are, of course, best-in-class when it comes to reservoir characterisation. And so we believe the alliance of the two is very powerful.

So just to remind you what CGG is focusing on right now, we are focusing on that imaging, characterisation of the reservoirs, and we are focusing as well on the monitoring. So the modelling of the monitoring, what will you need to put in place to monitor that reservoir in the long-term. And so there is a lot of modelling associated to that, and then possibly installing the sensors and CGG sensors to be able to do that in the long-run, which complements really nicely what Baker has.

So our plan is to start targeting clients where we are very recognised and strong, the two of us, and see if we get take up for those combined offers. So it is early days, we are very excited by what this entails, and our game plan is to be very targeted with the number of clients where we feel we can make a difference.

The launch of the AI Cloud is just a step forward into our strategy to be able to provide outcome as a service, in terms of cloud services. So we are trying to target a niche market where we think it is a combination of need of super intense, high performance computing is required, but also where we can add value by helping the client optimise their workflow or optimise their algorithms, a bit of a combination of helping them optimise the outcome. And we have chosen a number of verticals, and one of them is the AI. Not AI broadly, but the inference. And the inference is once you have a trained model, that you actually run instances of that trained model.

So we believe that requires computing and that we can make a difference there. So that is that step forward. We have a few clients in the, actually, bio-sense life science space and then in the AI space that we are pursuing. So that is for beyond the core.

Now going on to the Sensing and Monitoring optimisation plan, as you would imagine, we are looking at pretty much everything. And some are going to be quick wins, and others are going to take longer. So some of the quick wins is around inventory management. So just take one thing, which is safety stocks. Perhaps we were too cautious on the level of safety stock we were keeping or the level of inventory we were keeping. So we revisited that. So there will be immediate benefits that Jérôme commented already on Q1. But also there are things that are a bit longer, like some of the costs that are in the structure that we are carefully identifying, and then perhaps those will take a little bit longer to realise, but certainly expect a chunk. And this has been sized, and I think we did comment on that last quarter. And we think part of it, say, call it half, or part of it will be this year and the other half will be next year.

Jérôme, you want to comment on which number we gave last quarter?

Jérôme Serve: Yes. So we said between $20 million and $30 million benefits to the P&L, to the EBITDA, and we could add another $20 million on the cash by tighter management of our working capital, and then maybe a bit of CAPEX as well that we can play with. So it is the full benefit. And I would say in $25 million of $50 million, that is what we believe we can achieve for the [inaudible] transformation.

Daniel Thomson Perfect. Thanks for the colour and good evening.

Sophie Zurquiyah: Thank you.

Thank you very much. Thank you for the great questions and thank you for attending. And I look forward to future interactions in the coming weeks. Good evening, everyone.

Jérôme Serve: Good evening, everybody.

[END OF TRANSCRIPT]