

BARRON'S

MARKETS

Schlumberger: Coil, Sprung

By Ben Levisohn Jan. 20, 2017 3:18 pm ET

Shares of Schlumberger (SLB) have slipped today, despite meeting earnings forecasts and pointing to faster growth ahead. Maybe it's because Schlumberger has gained 42% during the past 12 months, and flat just isn't good enough. But Evercore ISI's James West and team believe investors are missing the point, as they note that the "international coil [is] set to spring." They explain:



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The International Coil Set To Spring? International visibility remains limited relative to North American shale as customer activity levels are more strictly governed by cash flow generation (as opposed to NAM where “the pursuit of shorter-term equity value takes precedence over full-cycle return on investment.”). Nonetheless, the international outlook has improved sequentially, with Schlumberger confirming that every regional market has bottomed including Sub-Saharan Africa and Asia, which were previously marred in uncertainty. The company conservatively steered away from quantifying the pace and timing of the recovery but noted that the international trajectory is equivocally aimed upward in every region (following the normal seasonal slowdown in 1Q). If NAM is a sprint, international is a marathon with 2017 marking the first leg of a multi-year upcycle. We are in firm accordance with SLB’s view that NAM unconventional production growth will inadequately counteract years of dramatic upstream underinvestment, with a third consecutive year of international underspend exacerbating the impact of a supply shock in the intermediate-term. SLB likened the international business to a “highly compressed coiled spring”, as the force of the recovery amasses concurrently with further underinvestment. Thus when NAM shale inevitably reaches critical mass, SLB will be strategically positioned to capitalize on diverging capex flows, with a boldly stated emphasis on outperforming peers on an earnings basis in every Geomarket (including NAM). While total NAM revenue has fallen 67% from 2014-2016, revenue in LatAm, Europe/CIS/West Africa, and Middle East & Asia has fallen by 61%, 52%, and 35%, respectively, and revenue from Mexico, Venezuela, Brazil, Sub-Saharan, Africa, China and Russia (land) has fallen by more 70% cumulatively over that same period. Thus while a NAM recovery presents the most enticing near-term upside, investors would be remiss to overlook the full-cycle recovery potential inherent to Big Blue. Schlumberger will be the most prolific beneficiary from capital rotation into longer-cycle plays as the upturn evolves, in our view.

Shares of Schlumberger have fallen 0.9% to \$86.44 at 3:17 p.m. today.

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