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WFT - Q2 2017 Weatherford International PLC Earnings Call

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CORPORATE PARTICIPANTS

Karen David-Green *Weatherford International plc - VP of IR, Corporate Marketing and Communications*

Christoph Bausch *Weatherford International plc - CFO and EVP*

Mark McCollum *Weatherford International plc - President and CEO*

CONFERENCE CALL PARTICIPANTS

Jim Wicklund *Credit Suisse - Analyst*

David Anderson *Barclays Capital - Analyst*

Bill Herbert *Simmons & Company International - Analyst*

James West *Evercore ISI - Analyst*

Angie Sedita *UBS - Analyst*

Sean Meakim *JPMorgan - Analyst*

Kurt Hallead *RBC Capital Markets - Analyst*

PRESENTATION

Operator

Good morning. My name is Kimberly and I will be your conference operator today. At this time, I would like to welcome everyone to the Weatherford International second-quarter 2017 earnings conference call. (Operator Instructions) As a reminder, ladies and gentlemen, today's call is being recorded.

Thank you. I would now like to turn the conference over to Ms. Karen David-Green, Vice President, Investor Relations, Marketing, and Communications. You may begin your conference.

Karen David-Green - *Weatherford International plc - VP of IR, Corporate Marketing and Communications*

Thank you, Kimberly. Good morning and welcome to the Weatherford International second-quarter conference call. With me on today's call, we have Mark McCollum, President and Chief Executive Officer, and Christoph Bausch, Executive Vice President and Chief Financial Officer. Today's call is being recorded and a replay will be available on Weatherford's website for 10 days.

Before we begin with our prepared statements, I would like to remind our audience that some of today's comments may include forward-looking statements and non-GAAP financial measures. These matters may involve risks and uncertainties that could cause our actual results to differ materially from our forward-looking statements.

Please refer to our Form 10-K for the period ended December 31, 2016, and more recent reports on Form 8-K for risk factors and the customary caution on forward-looking statements. A reconciliation of GAAP to non-GAAP financial measures is included in our second-quarter press release, which can also be found on our website.

Christoph will now provide a financial update on the second quarter, followed by Mark's comments on the overall performance and our way forward. Following these prepared statements, we welcome your questions.

And now, I would like to turn the call over to Christoph.

Christoph Bausch - *Weatherford International plc - CFO and EVP*

Thank you, Karen. Second-quarter results included an adjustment for revenue in Venezuela amounting to $42 million. In order to better compare results with prior periods and estimates for the quarter, I have excluded this effect in the following comments unless specifically mentioned.

Second-quarter revenue increased by 1% sequentially. Segment operating income before R&D, corporate expenses, and charges and credits of $3 million improved by $55 million compared to last quarter, with sequential operating income margins improving by 400 basis points to 0.2%.

Excluding charges and credits, loss per share for the quarter was $0.28. And without the adjustment for Venezuela, loss per share for the quarter was $0.24.

Aside from the accounting change for Venezuela, we recorded $111 million of income and charges net of tax during the second quarter. This included a non-cash credit of $127 million related to the fair value adjustment of our outstanding warrants, $29 million of severance and restructuring charges, and $12 million in net credits, primarily related to the amortization of unrecognized net gains associated with our supplemental retirement plan.

North America operating income margins improved by 428 basis points and were positive for the first time since the fourth quarter 2014. All product lines operating in the lower 48 US land market showed sequential margin improvements.

North America revenue was down 3% sequentially, primarily due to the seasonal spring breakup in Canada. Offshore revenue in the Gulf of Mexico remained subdued and decreased by 22% compared to the first quarter.

Overall margins continued to improve, with operating income of $3 million, an improvement of $21 million or 428 basis points, including a loss of $8 million related to the US pressure pumping business.

Improved activity levels and pricing in our well construction, reservoir solutions, and artificial lift product lines combined with higher completions activity in the United States supported this sequential improvement.

We believe that in the third quarter, revenue in North America will continue to grow, despite the recent flattening of the rig count in the US, driven by the Canada rebound from the spring breakup and new contract commencements in the US. Sequential incrementals are expected to be in the low-single-digit percentage and are primarily impacted by increased employee compensation costs and other costs.

Adjusted second-quarter international revenue grew by 3%. And excluding the second-quarter revenue adjustment in Venezuela, our Latin America revenue was up 1% sequentially, with gains coming mainly from increased activity levels in Argentina as operations resumed after the temporary disruptions during the first quarter.

The corresponding second-quarter operating segment income was $7 million, a margin of 3%. The decrease in segment operating income of $2 million and the corresponding reduction in margins of 82 basis points is a result of higher compensation cost in Argentina following an agreement with local unions to retroactively increase salaries. Excluding the aforementioned adjustment in Venezuela, we expect third-quarter revenue in Latin America to decline due to lower activity levels and continued pricing pressure throughout the region.

In the Europe/Caspian/Russia/Sub-Saharan Africa region, revenue was flat sequentially, given that the first quarter benefited from high volume of low-margin product sales, which did not repeat in the second quarter. We witnessed seasonally higher activity in the Norwegian continental shelf and in Russia.

Operating income margins improved significantly by 608 basis points, given the favorable product mix and the seasonal rebound. Overall, we expect an increase in revenue during the third quarter, given higher activity levels in the North Sea. With a less favorable product mix and service mix, incrementals are expected in the low-double-digit range.

In the Middle East/North/Africa/Asia-Pacific region, revenue increased by 6% with strong incrementals, primarily driven by higher activity levels and the commencement of new projects in the United Arab Emirates, Kuwait, and Thailand as well as re-charges related to the Zubair contract with no margin. Operating income margins expanded by 384 basis points.

We expect revenue in the Middle East and Asia region to further increase in the third quarter as our market share continues to expand and new contracts continue to ramp up. We expect margins in the region to be relatively flat versus the second quarter, primarily as a result of increased startup costs for new projects and an expected change in geographical mix.

Revenue for our land rig business increased 13% sequentially, largely due to improved operational efficiency. Rigs in Algeria and Kuwait were fully operational during the quarter. And the structural improvements that we implemented in the first quarter were reflected in improved safety and service quality performance. These improvements were manifested in solid financial improvements in May and in June.

With potential opportunities to restart operations in other markets, we expect continued growth with positive incremental margins throughout the second half of 2017 and beyond.

We have completed our previously announced Project 300 cost reduction efforts, and as of the end of the quarter had reduced nearly 3,000 employees. This represents 100% of our previously planned reductions related to Project 300. We are confident that this reduced cost structure will support our capacity requirements while improving our efficiency in key manufacturing locations.

R&D and corporate expenses were slightly down compared to the prior quarter at $36 million and $33 million, respectively. We expect that the current run rate for R&D and corporate expenses will remain broadly flat for the remainder of 2017, but we are working on several initiatives to reduce our corporate costs, which will show in 2018 and beyond.

The tax expense of $20 million represents the expense associated with our method of recording a discrete tax charge based on actual quarterly results. The tax charge is reflective of profits in certain jurisdictions, deemed profit countries, and withholding taxes on intercompany charges. The cash tax paid in the quarter approximated the tax expense, partly offset by tax refunds related to prior years.

Our current estimate for quarterly tax charge in the second half of the year is approximately $30 million, which may be impacted by our actual geographical mix of revenue and earnings. Outside any significant discrete events and not considering timing differences, we continue to expect cash taxes to be in the same range as our tax expense.

Net cash used in operating activities was $62 million for the second quarter of 2017, including $107 million of debt interest payments, $40 million of cash severance and restructuring costs, and $30 million of SEC legal settlement costs. This was partially offset by the collection of other receivables, insurance proceeds, and favorable legal settlements totaling $93 million.

Capital expenditures of $42 million increased slightly by $2 million or 5% sequentially, and increased $11 million or 35% from the same quarter in the prior year. We expect capital expenditures for the second half of 2017 to range between $150 million and $170 million, which includes upgrades of 2 drilling rigs where we have recently won a contract in Kuwait. Total net debt of $7 billion increased by $113 million during the second quarter.

Including adjustments related to Venezuela, customer receivables decreased in the second quarter, and DSO decreased from 84 to 78 days. Inventory levels increased by $28 million sequentially, mainly as a result of a buildup of products destined for customer delivery in the Middle East/Asia region in the second half of 2017.

We have commenced a competitive land drilling rigs divestiture process and we have seen a high level of initial interest. This is a sizable opportunity for us, as Weatherford Drilling International is highly respected and one of the largest international land drilling contractors in the market. We have a fleet of 110 rigs with a premier customer base which is geographically diversified to take advantage of secular and cyclical trends.

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

Mark McCollum - *Weatherford International plc - President and CEO*

Thanks, Christoph, and good morning, everyone. I'm pleased to report a strong second-quarter performance. We generated significantly higher incrementals on increased revenue in the US, the Middle East, and Russia. And we improved our cash flow compared to the previous quarter.

Excluding the adjustment related to Venezuela, our operating margins improved by 400 basis points sequentially. Our service quality execution in the second quarter was exemplary, with consistent and reliable performance across all segments of our business and particularly noteworthy improvement in our land drilling rigs business, which achieved its lowest nonproductive time since 2012.

The Weatherford team has been doing particularly well in the Middle East. Rig activity has been going strong, and our tendering activity has correspondingly remained high with our market share steadily increasing.

During the second quarter, Middle East, North Africa and Asia Pacific revenue grew 6% sequentially. We've already signed several large contracts to date, with notable wins in the UAE, Oman, Kuwait, and Saudi Arabia. And we commenced work on our significant wireline and artificial lift contracts in Kuwait in June.

Weatherford has posted the best comparative service quality results in Saudi Arabia year to date. And as a result, we are invited to participate in large turnkey well construction projects, where we will have the opportunity to provide project management along with most of our products and services. During the quarter, we won a turnkey project related to rigless well testing operations, and we already mobilized assets and crews to commence operations.

The Middle East is a very important market for Weatherford, and I had the honor of joining fellow executives from across the industry at the Saudi US CEO forum in May. At this forum, we signed a memorandum of understanding as part of Saudi Arabia's in-kingdom total value-added program. We are strongly committed to the localization of content in Saudi Arabia as well as other countries in the region.

We've also had several successful field runs of our industry-leading technologies in this region. For example, Weatherford delivered record-setting directional drilling results in five different wells for an operator with our Revolution rotary steerable system, the hostile-environment-logging system, and logging-while-drilling-tools. In one well, Weatherford achieved a rate of penetration 80% higher than the field average.

In Kuwait, Weatherford provided a complete characterization of a challenging well in a prolific field. By deploying our Compact logging and formation testing tools on drill pipe, Weatherford saved the operator approximately 60 hours of rig time compared to conventional pipe-conveyed logging operations.

And in Australia, we deployed our WFX0 system, which is the industry's first fully integrated gravel pack system to achieve an API/ISO V0 rating, which has been tested to the industry's highest standard with zero gas leakage. While leveraging several V0-rated Weatherford technologies, including the TerraForm packer, the system enables gravel pack completions of multiple open-hole zones in a single trip and achieves cased-hole functionality in an open-hole environment.

Turning to Europe, we are seeing increased plug-and-abandonment activity in the North Sea and higher land activity across Europe, especially in geothermal wells. We expect these upward trends to continue in the second half of the year, contributing to improved results in that region.

I'm very pleased to share that Weatherford received the Eni Safety Award in the category of well services for the second year in a row in recognition of our team's achieving the best safety performance and maintaining a strong commitment to safety. In addition, after demonstrating high levels of service quality and efficiency on a one-well project in the North Sea, Weatherford replaced the incumbent on a five-year logging-while-drilling contract with options for extensions.

Rush activity levels were high, benefiting from a seasonal rebound. In addition, market share gains have allowed us to increase revenue and profitability. In June, we signed a technology cooperation agreement with Gazprom Neft intended to further develop our current business relationships and collaborations between the two companies.

In Latin America, our previously disclosed revenue accounting adjustment related to Venezuela negatively impacted our reported second-quarter results. Absent that adjustment, however, Latin America results improved sequentially on higher activity in Argentina, Colombia, and Mexico, where the first well drilled, as part of our recently awarded integrated services contract for a shallow water project in the Gulf of Mexico, set a new field record: drilling a horizontal well to total depth in 49 days, which is 7 days faster than the previous field record. The second well was drilled in 45 days, more than 17 days ahead of plan.

In addition, we are benefiting from several contract wins in Argentina and Chile. We've seen healthy activity levels in the US land market, especially in product lines such as drilling services, wireline, and well construction.

Pricing and utilization has improved in all product lines, as operators increasingly drill wells with complex profiles and longer laterals. As operators continue to move deeper into the well lifecycle, we expect further improvement in our production-related businesses. In addition, with the spring breakup behind us, the Canadian rig count has come back quickly and is above last year's levels.

During the quarter, we released the ForeSite production optimization platform, an integrated software solution that leverages the Internet of Things and advanced analytics to maximize equipment uptime and extend asset life. Trialed in North America, this software platform will help our global customers to reduce downtime of vital production assets and to optimize critical maintenance routines.

For the offshore market, we developed a premium version of RipTide, our RFID-controlled drilling reamer that incorporates advanced cutter technology, which was developed through collaborative efforts between Weatherford and US Synthetic, the leading provider of polycrystalline diamond cutters for the oil and gas industry.

During the quarter, we introduced a new wireline tool, the Raptor 2.0 cased-hole evaluation system. In its first deployment in Western Canada, the tool assessed the remaining production potential of three shut-in unconventional wells.

Data from the system identified untapped oil- and gas-producing zones in two of the three wells. Using this data, the operator has established initial production and is planning additional recompletion campaigns in the reservoir.

One of Weatherford's biggest asset is its strong customer relationships. I've experienced that first hand in my first few months, traveling to different regions throughout our organization to spend time with our customers.

It is clear to me that customers are encouraged to see Weatherford's consistent service quality and service delivery improvement over the past few quarters. This is resulting in increased confidence in Weatherford services, which is already resulting in a wider available market.

Customers told me that they are looking forward to seeing a more procedural, process-oriented, and disciplined company. And there is strong confidence in our ability to further improve performance.

Many customers have expressed their appreciation of Weatherford's support and our ability to deploy a skilled team to solve their challenges. The level of encouragement I received from our customers leave me confident that we have significant opportunities ahead of us.

Moving forward, we remain cautiously optimistic, despite the recent drop in oil price. Over the last few months, increasing US domestic production and resilient international non-OPEC production have placed pressure on oil prices. And the anticipated energy services recovery outside of completions activity in key US unconventional basins has been slow to develop.

We have seen a flattening of the North American rig count, which will make it more difficult, we believe, to obtain improved margins, in particular as certain input costs are likely to increase. On the other hand, with the spring breakup behind us, the Canadian rig count came back earlier than usual and is now above last year's levels. And internationally, numerous recent contract awards, coupled with the startup of new projects, should allow us to outpace rig count growth.

Over time, steady growth in demand, combined with natural decline rates in basins outside the US, should offset the US supply surplus and improve the global market outlook. But I'm anticipating that this is a couple years away.

It would be great to get some wind at our backs in the form of a market recovery. However, we cannot and are not holding out for a macro level change to strengthen our results. That doesn't mean, though, that there aren't plenty of things that we can do to improve our financial performance and position that are well within our control to execute.

My motivation coming into this role was based on the opportunities I can see available to Weatherford. And I'm committed to doing the heavy lifting to get things fixed. Obviously, our top priority is to strengthen our balance sheet. My goal is to cut our net debt in half by the end of 2019.

We have a number of initiatives underway designed to help achieve this goal, but let me bucket them into three categories. First, we intend to heighten our focus on operational and financial accountability with a more disciplined and streamlined management process.

We are currently carrying out a thorough and comprehensive evaluation of the way we operate, which today varies greatly between different product lines and geographies, with the goal of standardizing, simplifying, and in some cases automating key processes across the organization. Various teams have been working diligently across the Company for the last couple months, reviewing customer service delivery, supply chain, sales, and a host of back-office processes.

By improving these particular areas, we can better ensure flawless service quality, reliability, and consistency for our customers in the field. But the ultimate goal is to significantly reduce our support cost as a percentage of revenue by having a more efficient and lean organization.

Our businesses can execute well and be profitable, and we aren't that far away. We just need to do the right things with discipline to make that happen.

The second initiative underway is a complete portfolio review. We are working to thoroughly evaluate each product line and its position in Weatherford's portfolio. We are considering current business performance, available technologies and competitive positioning, future market outlook and growth opportunity, our technology pipeline, and future financial trajectory. If we're going to have it, it's got to have a future; it's got to make a return.

My early discussions with customers and review of operations suggest to me that there is significant untapped opportunity to improve Weatherford's market position and returns. We have an attractive and differentiated portfolio on which to build. We have great technologies, an extensive global presence, a set of outstanding collaborative customer relationships, and a high-caliber workforce.

These qualities make us an important partner for our customers in many basins around the world. There is a compelling strength to our fundamental qualities and underlying assets, which suggest an attractive revenue upside that we have the ability to secure. We just need a clearer strategic vision for our portfolio aligned with an organization designed to execute on that vision.

In that regard, these first two initiatives I've discussed are linked. My commitment is to get the composition and structure of this organization right.

Finally, in parallel with these other initiatives, we are continuing to move forward with the strategic transactions we disclosed earlier in the year. We are on track to close the OneStim joint venture transaction with Schlumberger in the second half of this year, which will allow us to better capitalize on the recovery in North America land unconventional activity.

We are also following through with marketing of our international land rigs business. The outlook for this business is improving and we have seen high levels of initial interest. We are working along a timeline to allow us to conclude this process before year end as well.

I know that you are all eager to hear more specifics about how we will harness these opportunities to create increased value for our stakeholders. We are moving expeditiously with these initiatives and will be reviewing results with the Board later this quarter. My goal is to be able to present a clear strategic direction to the market early in the fourth quarter. So stay tuned.

I joined Weatherford because I saw an incredible amount of opportunity in this Company. And in speaking with our customers, I see that they feel the same. They are supportive of Weatherford.

They just need us to be more aggressively focused on finding unique, internally collaborative solutions to the technical challenges they face and to up our game when it comes to consistent execution and service quality. I'm sure the same could be said for all of our competitors, too.

For our part, though, we as an organization have admittedly been a bit disjointed at times. That ends now. We are dedicating ourselves to moving forward a stronger, more unified company that is guided by our core values.

We intend to lead with ethics and integrity and we are committed to act with discipline in every aspect of our work. We are focusing on delivering reliable services and best-in-class technologies that provide maximum value to our customers, and in turn value to our shareholders.

We are going to strive for flawless execution, all while maintaining the highest levels of safety and service quality. And as we've shown in the second quarter, we can achieve that high level of execution.

And we will continue to foster collaboration and innovation, both within our organization, across product lines and functions, and with our customers and partners, sharing resources and capabilities to develop new solutions that continuously improve our product and service offerings and deliver exceptional results.

In closing, my key priority is to repair our balance sheet and to get the structure and operation of this organization right so that we can be successful regardless of the market that we find ourselves in. I look forward to further updating you about our next steps early in the fourth quarter. At that time, we will lay out a more specific strategic vision for the Company and present the more detailed path to sustainable value creation.

There's a lot of opportunities in front of us, both internally and externally. And make no mistake: we're going after them. I saw them from the outside when I chose to take the role and now that I've seen organization from a more granular level, I believe it to be truer than ever.

Weatherford will emerge a much stronger and better company with a clear purpose and vision for the future. It is my mission to ensure this happens for the greater good of all of our stakeholders.

With that, I will turn the call back to the operator for the question-and-answer session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Jim Wicklund, Credit Suisse.

Jim Wicklund - *Credit Suisse - Analyst*

Good morning, guys. And Mark, that was a nice speech and we look forward to the business plan. But I think you lay it out well. Just in general, you talk about when you were on the outside and now that you're on the inside, and people have looked at Weatherford as not being a technology leader.

And in your press release and in your comments this morning, you went through a list of technical wins. Can you talk about your view of Weatherford and technology after being in for three months versus being on the outside for years?

Mark McCollum - *Weatherford International plc - President and CEO*

Sure. No, I actually think that one of the things that's been underappreciated about Weatherford is the level of technology that they have. Obviously, when you are sitting in a competitor's shoes, your goal is to knock down everybody else's tools in favor of your own.

But I think admittedly, always had an appreciation for the technologies that Weatherford had. As I have gotten in and had a chance to spend more time and get a sense for it, Weatherford has great tools.

In some ways, it hasn't always been the guy who's in front on the technology development. But in a lot of the tools, what you find is that by being a fast follower, they've had the opportunity to work out bugs that other tools have.

So when the tools come forward, they are very, very strong. So like in the wireline space, the Compact series of tools are very well regarded. We are developing a new rotary steerable that I think is going to be extremely well accepted and probably will leapfrog some of the competition. And we are in field testing of that now. And you heard the list of some of the others.

In visiting with customers, I think customers have all expressed appreciation. They believe that the Weatherford tools perform exceptionally well. I think that the larger issue for the Weatherford organization has been possibly in inconsistent design of service, or at least the inconsistent deployment of design of service. So that when you are executing in the field, that execution of service quality has been somewhat inconsistent.

So we're driving hard on, first of all, making sure we are consistent. And as a part of some of these initiatives that we are working on -- I talked about service delivery -- part of that will be coming out with consistent design of service across all of our product lines and geographies so that we can ensure better execution of the tools and really get maximum advantage for the technologies that we have.

Jim Wicklund - *Credit Suisse - Analyst*

Okay, that's a helpful view. Because we don't always look at Weatherford as technology. My follow-up, if I could. You had made a comment, I guess at some conference or in some investors, but investors came away with the comment that Weatherford said they are willing to sell their crown jewels if necessary.

And I know you guys are going through a portfolio review process and that's not done yet. And I know the goal is to reduce debt, cut it in half by the middle of 2019. Land rigs are for sale. I understand cleaning up a portfolio, but can you talk about the likelihood that over the next couple years, you would be willing to or have to sell a crown jewel for Weatherford to survive?

Mark McCollum - *Weatherford International plc - President and CEO*

I think it's premature to reach the conclusion that that's the endgame for the portfolio review that we are doing. I think what I've tried to suggest is that coming in as a fresh face here, I am agnostic.

If you have been here for a long time, you probably have some emotional investment in some of the product lines, what might be a crown jewel or not. And my view is every product line is equal in the portfolio. It has an equal space, whether it is large or small, and they all have to perform. They have to perform on their own merits.

And so what we are trying to do is look at them very agnostically. We've got internal help and I've got external help helping me with this, too, to make an evaluation about not only what they are doing now, what they can do, what's their future, and to try to come up with a better strategy.

And then also for me to try to get a better sense of how we can synthesize this fairly disparate today group of product lines to bring them closer together. One of the issues that I see is all of our product lines run very independent from each other today.

And while that might have been okay for a long period of time, my discussion with customers, they are all -- they say we want solutions, we need solutions. And that begs the question of --

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Jim Wicklund - *Credit Suisse - Analyst*

So then [just product now].

Mark McCollum - *Weatherford International plc - President and CEO*

Exactly. How can we bring these to provide solutions. How can we get them to work together better. But I also think that in bringing them together, there are probably significant cost synergies to be had by leaning out the organization in how we run it, both at the top of the organization as well as down at the field interface.

Jim Wicklund - *Credit Suisse - Analyst*

Okay. Okay, that's very helpful and that corrects a misperception. So I appreciate it. Thanks, guys.

Operator

David Anderson, Barclays.

David Anderson - *Barclays Capital - Analyst*

Good to hear there's no sacred cows there, Mark. Question for you on the North American portfolio. It's quite a bit different than a lot of other companies now without the pressure pumping in there.

So I was wondering if you could help us out a little bit. You're later cycle now; so how do we think about your growth versus, say, a US land growth in terms of the rig count or well completions? I would think, particularly on the artificial lift, that there is a backlog of completions. There might arguably be even a bigger backlog of artificial lift. So does that come in later quarters? How should we be thinking about the progression?

Mark McCollum - *Weatherford International plc - President and CEO*

Yes, that's the way that we are seeing it. Artificial lift has done okay. One of the things that mask our performance is, of course, we don't have an ESP offering. So we are missing a little bit of that.

We've had a significant uptick in sales of jet pumps and gas lift. Gas lift has been going great, but it's a cheaper tool than traditional rod-lift systems by probably a 10 factor. And so while you are seeing increased volume, you don't see it necessarily show up in the sales percentages. But it has improved.

Of course, as these unconventional wells that are being drilled move later down the well lifecycle, at some point, they're going to go to rod lift. They just have to. ESPs and gas lift will work in the initial production phases, and customers are tending to stretch them out a bit. But at some point, they are going to shift that, so we should see an uptick.

In our well construction product lines, we are sold out of rotary steerables, like others. We've got every tool and we've brought in tools from other parts of the world to satisfy demand. And that's been going well. We've seen a big uptick in our wireline work.

Completions work has continued to do okay. The US piece probably has a larger percentage of Gulf of Mexico, which has been a bit weaker. But Canada has been ripping on completion sales. And so all of our other product lines have been doing fairly well.

The lift has probably been the one that's probably been later cycle, and with it some of the other well service product lines. And we do think that, particularly if the rig count levels out, that things will begin to mature and those product lines will see an uptick.

David Anderson - *Barclays Capital - Analyst*

Mark, you addressed the debt paydown. And obviously, your sense of urgency is obvious. The other issue for investors has been the cash burn. This has been the Achilles heel, I would say, probably the last 12, 18 months there with Weatherford.

Had another cash burn this quarter. There is a handful of one-offs in there. How should we be thinking about free cash flow, like second half of 2017 and then maybe kind of beyond there, if you wouldn't mind just touching on that.

Mark McCollum - *Weatherford International plc - President and CEO*

I will let Christoph handle the --.

Christoph Bausch - *Weatherford International plc - CFO and EVP*

I think, again, we drive very hard to get to breakeven cash flow. That's our commitment, and the whole Company works aligned on that. You have to understand, there are several costs which we still carry. We carry a lot of severance cost. We have our SEC settlements, which are negatively impacting the cash flow. So that's impacting our results.

Now, we had some favorable effects in Q2, to understand that. We had sold a note for a customer in Ecuador. And we had a couple of other positive ones, but we also had a couple of negative ones as well.

Going in the second half of the year, there is one difference on interest charges, which I think is very important to understand. Q2 interest is usually lower than Q3. And we also have a ramp-up on capital expenditure, as I'd outlined in my comments. But I would say as we get into Q4, we'll work and we will be at breakeven. That is our commitment from that. Q3 will not be there.

David Anderson - *Barclays Capital - Analyst*

Okay. Q4 will be breakeven. Okay, thank you very much. Appreciate it, Mark and Christoph.

Operator

Bill Herbert, Simmons.

Bill Herbert - *Simmons & Company International - Analyst*

Mark, with regard to the land rig sale timing, a targeted aspiration of resolution by year-end. Do you have any comments with regard to likely structure of the deal at this stage?

Is it open-ended in terms of any number of forms could take place? Is it a likely outright complete asset sale? Is it a JV? What are your thoughts on that front?

Mark McCollum - *Weatherford International plc - President and CEO*

It's a little early yet to know how that's going to go out. We have offered it as a complete package. We've also divided it in a way that if there was interest in smaller packages, such as like the Middle East, then that could also be a transaction that could come out of this. What we would want to try to do is maximize the value for the assets that we give up.

The Middle East business is doing really well, as we described in the calls. They've seen a significant uptick in not only rig deployment, but also their service quality. They moved profitable in June, and so -- as an entire group.

But that when you look at the Middle East business separately, it's a very nice business. So it could be that that's how it goes.

What I want to try to do is to maximize the amount of cash that we can get and reduce the complexity to execute that so that we can close as quickly as possible and get the cash in our pocket and reduce the debt.

So we are in the middle of the process now. We've got people in the data rooms. And expect to hopefully have something to present to our Board at the September meeting to see if we've got something that we can execute on. And then wrap that up before the end of the year.

Bill Herbert - *Simmons & Company International - Analyst*

Okay. And then secondly, kind of bigger picture here with regard to addressing the internal transformation of Weatherford. And you talked about your three objectives here, which are coherent and lucid.

I'm just curious as thus far, as you've examined Weatherford effectively from the outside in and now from the inside, but not for all that long, where is internal transformation unfolding at a targeted or better-than-a-targeted pace? You don't need to give all the examples, just a few. And where is -- and other than the balance sheet, where is the transformation looking harder and taking longer?

Mark McCollum - *Weatherford International plc - President and CEO*

That's a good question. The first initiative that I ascribe, where people are looking at various processes, I think that's going fairly rapidly. Some of those were already initiated, like some of the back-office processes.

Christoph had previously kicked off some work in the back-office to look at doing some business support centers and using extended enterprise to take a greater burden on some of our transactional work. So that is underway. It probably has a little bit of a head start across some other things. We are also working on sales, but trying to get that pushed harder.

To me, the end goal of it, of course, is working through and having revised and standardized processes. But with a goal of then saying, okay, now that we have that, we are going to reorganize the Company to better support those processes and lean out. I think that there's a big opportunity there as we look at a percentage of support cost to revenues.

So those things are moving along. And we have a fairly, I think, good view of where we need to go and to help that out. And we'll have something fairly quick.

The portfolio review -- we are going to have a view of what we need to do at the September Board meeting when we're presenting it to the Board. But it's hard to know at this point what the outcomes are going to be.

If some of those are going to making some transformational moves on those product lines, that may take a little bit longer to execute. It may go into 2018 to actually do. I just can't even say right now. But that is a little bit more.

The first initiative sort of designed it at taking a broad swipe at structural support cost and how we execute so that we can drive the Company to get it to profitability and cash flow generation sustainably very quickly. The second one has been looking at the portfolio and making sure we are moving it in the right direction.

I think that broadly, and I peppered this through my comments, but it really is true. When you look at the revenue opportunity, Weatherford's market position with its customers, and in my conversation with customers, most of them are like we really like Weatherford. We like what you're doing. We want more of you. You guys need to figure out how to get here.

It's actually on our side of the table to actually push harder to get a bigger share of the pie with a number of our key customers. And so that's a part of what -- but there's a lot of top-line opportunity that's going to take some time to get. But that's a big -- that's going to be a big push for us as well.

Bill Herbert - *Simmons & Company International - Analyst*

Okay, thanks, Mark.

Operator

James West, Evercore ISI.

James West - *Evercore ISI - Analyst*

Thanks for laying out your strategic priorities. My first question really is along the lines of the first one. It's both process and accountability, and I fully appreciate the processes are getting much better, especially given your background and your history.

But I have a question about accountability. That's one of the things that's always lagged at Weatherford. And what are you putting in place or what is the organization putting in place to drive that accountability throughout the organization in order to continue to help with operational excellence and all the things that go along with that, like cash generation?

Mark McCollum - *Weatherford International plc - President and CEO*

Well, it starts with me, right, and my engagement with the organization and being out there calling the question from the top. We're having, which is kind of a new thing for Weatherford, right, but even just something as simple as staff meetings at my level.

Of me being out -- I've been on the road for about four or five, six weeks in and out visiting operations and things. And people have told me that's the first time they'd ever seen the CEO. But getting out and communicating with people about what the expectations are.

And then one of the things to do here -- we've been working hard to improve forecasting. Christoph and the team and I are trying to also -- a lot of the financial -- there's a lot of information.

One of the things that's been a surprise for me is that it's really not that there's not a lot of information. There is a lot of information coming off the systems. The problem is that it's primarily historical.

But to turn that information and look forward so that people are spending more time thinking about the future, about the forecasting, and where we are going rather than where we've been. It seems -- sound simple, but sometimes that's hard to do, to get people's eyes focused on the horizon.

So by asking the right questions at my level and then pushing it down, making sure that we are working as a team and feeling accountable as a group rather than individuals running and doing their thing, is a key part of that. So it's interesting. It's been a big investment of time early, but that gets things started.

Now separate from that, and you heard the back end of my comments were really largely directed for our organization as a whole. We have redone the mission statement; we have redone our values. We are kicking off a lot of internal things to level set the organization about what the expectations are from a culture standpoint. What we are about; what we are going to be.

I think a lot of receptivity to that. I think employees like that, but ultimately the proof is in the pudding. It's not just saying the right things, but doing the right things.

And so for me long term, what I've got to do is not just encourage and cajole and to put values and all that out there, but also really hold people accountable. If you don't make your numbers, if you don't follow through, then there is a consequence to that as well, which is the hard part of leadership. But that's probably something that's been missing that we'll be introducing as well.

James West - *Evercore ISI - Analyst*

Okay, great. Great to hear. And then, Mark, with respect to the support costs in the organization and bringing those down further, given the unique portfolio that Weatherford has, is there any reason to think that you shouldn't be able to get support costs down to peer levels or even below that?

Mark McCollum - *Weatherford International plc - President and CEO*

Well, I would say that aspirationally, there's not a reason, okay. But I think that the question that we'll have to work through as we standardize all these processes and drive -- I'm going to drive pretty hard.

But there probably is a point where there's some level of cost can come out because of automation that comes with an expense. We don't have the luxury or the time to put in one instance of SAP worldwide.

So we have a good -- we have a very good system; JD Edwards is fine and we actually have one instance of it. The question is using it properly and doing everything we can around the seams to make sure that we get it out.

As I look at the opportunity, it feels like -- our support costs run 24%, 25% of revenues. Our peers are in the low teens. You can do the math and say, okay, from an opportunity set, it's a pretty significant opportunity.

And I'm going to try to push as hard as I can to get as much of that as we can, but it's going to take some work. At this point in time, the way that the organization has been built, from anything from real estate to the organization chart itself, this will be cutting into the Weatherford bone a bit. And I understand that, it's hard, but it's going to get done.

James West - *Evercore ISI - Analyst*

Got it, okay. Thanks, Mark.

Operator

Angie Sedita, UBS.

Angie Sedita - *UBS - Analyst*

Good morning, Mark. So appreciate the details on the game plan so far and your goals. And we'll look for more later in the year.

But on the complete portfolio review that's under way, certainly you have technology within Weatherford. And maybe a better ability to monetize and create revenue growth out of those product lines. And if you think through those product lines, either by either segment or region, where do you think the opportunities lie? Where are the products underperforming versus your technology capabilities?

Mark McCollum - *Weatherford International plc - President and CEO*

It's too early to really know. I have tried to step away from the early parts of this portfolio review. I'm going to have my first meetings on it next week. Christoph has been driving. Maybe he can tell you an answer that question, but I think it would be wrong of me to answer that question early.

What I would say, I think that I see opportunity across every single one of our product lines just from the early days. That's why I see in some of our very best customers around the world a huge opportunity to significantly expand our share. And we've got the tools.

It's interesting that there are some customers where we have a really large share of one product line, and then the next customer, a really large share of another product line. And those customers are doing the same thing. It's just inconsistency about how we've gone to market and how we've sold and built relationships or even demonstrated the prowess of the technology portfolio we have.

So I just look at that going, okay, you know what? There's opportunity everywhere and it's palpable. And that's actually exciting to me, quite frankly, that there's so much out there.

And customers, as I said, have been very supportive and they are cheerleading in the back. They want Weatherford to be a strong competitor in this market. And they are willing to help us do what we need to do, given the feedback and the direction to help us get this thing going in the right direction.

Angie Sedita - *UBS - Analyst*

All right, fair enough. And then if you could tap onto updated comments on working capital and how much -- now you've been in there more than a month and you've been there a little longer, how much cash do you think is still trapped on the balance sheet, specifically in inventory? And what product lines in that inventory is sitting on your balance sheet? And what do you think is easily monetizeable versus what would take time?

Christoph Bausch - *Weatherford International plc - CFO and EVP*

Angie, this is Christoph. So I will take that. We worked relatively well on the receivables this quarter, but there's more opportunity there. And it depends on the geography as well. As you go forward and revenue goes up, so you have a draw on receivables just naturally. But we are very, very focused actually on that part.

On the inventory, that's where the big opportunities are on our side. Simply, we haven't performed in Q2 as to what our expectations were. Now, there is reasons for that. We are preparing for some contracts, as I mentioned in my prepared remarks. So this will change going forward and we've put a very big effort in there.

So we will see some reductions in inventory going forward. But it's not an easy task because the geographical location and the exact fit of the right piece for the right opportunity. But you will see us pushing very, very hard on that. I don't want to give you a firm number, but you will see reductions going forward.

Mark McCollum - *Weatherford International plc - President and CEO*

The inventory number is a huge number. It's like $1.7 billion of inventory on the balance sheet today. My early visits, it's slower moving. That's partly a market overlay; the fact that the market is slow itself is causing some of that.

And from a process point of view, historically, manufacturing pushed product rather than it was a pull system. And that I think created part of this problem.

So I talked about these initiatives to review processes. Part of that, when I talk about supply chain, is reforming that so that as we do service delivery that we reframe this thing to be this pool system versus a push and stop that.

And so we've initiated processes so that there's high visibility around the world of what's on the shelf, where it is, and trying to give a pass to folks to move that stuff around as expeditiously as we can and start working it off.

But it would work off a lot faster and easier if we had a market to sell into. And that's the problem is as the market continues to be a bit slow, particularly in many of our international market, it's going to take a little while to work off.

Angie Sedita - *UBS - Analyst*

All right, fair enough. Thanks. I'll turn it over.

Operator

Sean Meakim, JPMorgan.

Sean Meakim - *JPMorgan - Analyst*

Thanks. Good morning. So on the portfolio review, you mentioned being agnostic coming in. And the OneStim deal seems like a real opportunity for you to generate some cash but also maintain some upside in what could be a better overall business once it's up and running.

So as you are doing a portfolio review, are you also looking at other value creation levers like that? More JVs? Or other types of more creative ways that could help you fix your balance sheet but also improve what your leverage looks like to a recovery eventually?

Mark McCollum - *Weatherford International plc - President and CEO*

Yes, the answer is yes. Not only JVs that would be product-line-oriented, but also there are some potential JVs that are regional-oriented that we might look at that are in the mix.

It would also be fair to say that as we evaluate product lines and understand what their future are to the extent that a fix might be an acquisition, that's something that we're going to factor in, too. And how do we acquire the technology that we need or whatever else. And sometimes that might be through a partnership or JV.

So we are just -- like I said, it's a pretty thorough and expansive review trying to really understand how the portfolio works today, how it will work in the future, and how it could work together. It's something that's not been done, so it's a clean sheet here. But we got to do it and we're moving fast on it.

Sean Meakim - *JPMorgan - Analyst*

Absolutely, yes. It seems like creativity could lead to a lot of good opportunities. So on the land rig fleet, for the land rig fleet, could you help us understand what can be done to improve profitability to a point where it can really help you to maximize value?

I guess I'm thinking about -- we don't have a lot of public comps for international land rigs, but where we do, we are still seeing generally pretty good EBITDA margins. Weatherford is closer to breakeven.

Is it just a function of fixed cost absorption in too many subscale markets? Is it day rates or legacy contracts, the makeup of the fleet? I guess it would be helpful to get a sense of the levers you have to improve that business, which I know it seems like the sales are fairly accelerated. But what are the levers you have to present that fleet in the best possible condition for sale?

Mark McCollum - *Weatherford International plc - President and CEO*

The biggest single factor right now is just utilization. Rigs are great when they are working, and when they are not, it can be punitive. And so a part of the issue has been just during this downturn, a number of these rigs are positioned in sections of the market that are not working.

Now, the Middle East has been a different situation there. The high percentage are working, and as they've moved, they have moved profitable. So that's probably the single-biggest factor here is continuing to get them to work.

Part of the issue has been that we have one and two rigs spread out all over the world, and that does make a difference.

The second factor: new leadership there has been working aggressively to lean out the organization to take out cost. Like other product lines within the Weatherford portfolio, it sits very separate from the other product lines. And so it's got its own locations and operations and functions in every single geography that it operates in.

Trying to make sure that the organization is as lean as it possibly can be has been part of the issue as well. So they have been working hard on that, and they made a lot of changes early, which you are seeing the results of now.

The third thing I would tell you is really around execution. One of the I think concerns have been inconsistent service and execution, which not only results sometimes in rigs being laid down. Customers will say, okay, we're not going to use that rig or whatever. Or just inability to get them working. You lose money by having to refund out of service quality issues.

They made a significant shift on that in the last quarter, had very, very good performance. And so as that continues, that should also improve, too. And again, that's management, that's leadership, and process discipline, just like we're trying to drive across the entire Weatherford organization.

Sean Meakim - *JPMorgan - Analyst*

Got it. That's very helpful feedback. Thank you, Mark.

Operator

Kurt Hallead, RBC.

Kurt Hallead - *RBC Capital Markets - Analyst*

Thank you, Mark, for letting me in on this last one. You laid out everything, and I know you got a game plan and a process. And you're going to provide us some more interesting stuff come the fourth quarter.

The $3 billion reduction or 50% reduction in debt, I should say, by the end of 2019. If you were to generally map that out, how much of that -- you don't have to give specifics, right? I'm just looking generality.

How would you consider that debt reduction in terms of free cash flow from operations, vis-a-vis asset sales, vis-a-vis improved marketing conditions in terms of generating higher net income? Just roughly, how do you think that might map out?

Mark McCollum - *Weatherford International plc - President and CEO*

Right now as the way I kind of view it, it's probably going to come one-third from cash generation from the Company and two-thirds from dispositions or transactional type work.

Kurt Hallead - *RBC Capital Markets - Analyst*

Okay, I appreciate that stab, Mark. So that would also not include the warrants and obviously not include the convert, right?

Mark McCollum - *Weatherford International plc - President and CEO*

That's right.

Kurt Hallead - *RBC Capital Markets - Analyst*

That's awesome, Mark. I will just keep it there. I appreciate it. Thanks.

Mark McCollum - *Weatherford International plc - President and CEO*

All right, thank you, everyone. We appreciate your participation on the call and we look forward to following up in the coming days.

Operator

Thank you, ladies and gentlemen. This concludes today's conference call and you may now disconnect.
