

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended September 30, 2021

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 001-13439

**DRIL-QUIP, INC.**

(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

74-2162088  
(I.R.S. Employer  
Identification No.)

6401 N. ELDRIDGE PARKWAY  
HOUSTON, TEXAS  
77041

(Address of principal executive offices) (Zip Code)

(713) 939-7711

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class                      | Trading symbol(s) | Name of each exchange on which registered |
|--|-------------------|---|
| Common Stock, \$0.01 par value per share | DRQ               | New York Stock Exchange                   |

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

|                         |                                     |                           |                          |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer         | <input type="checkbox"/> |
| Non-accelerated filer   | <input type="checkbox"/>            | Smaller reporting company | <input type="checkbox"/> |
|                         |                                     | Emerging growth company   | <input type="checkbox"/> |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2). Yes  No

As of October 25, 2021, the number of shares outstanding of the registrant's common stock, par value \$0.01 per share, was 35,385,885.

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## PART I—FINANCIAL INFORMATION

## Item 1. Financial Statements

**DRIL-QUIP, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(UNAUDITED)**

|  | September 30,<br>2021 | December 31,<br>2020 |
|--|-----------------------|----------------------|
| (In thousands, except per share data)  |                       |                      |
| <b>ASSETS</b>  |                       |                      |
| Current assets:  |                       |                      |
| Cash and cash equivalents  | \$ 375,172            | \$ 345,955           |
| Trade receivables, net   | 102,715               | 116,202              |
| Unbilled receivables   | 114,357               | 140,318              |
| Inventories, net   | 194,720               | 212,536              |
| Prepays and other current assets   | 40,307                | 48,182               |
| Total current assets   | 827,271               | 863,193              |
| Operating lease right of use assets  | 5,284                 | 6,962                |
| Property, plant and equipment, net   | 224,676               | 234,823              |
| Deferred income taxes  | 5,965                 | 5,768                |
| Intangible assets  | 27,137                | 29,434               |
| Other assets   | 3,404                 | 10,992               |
| Total assets   | \$ 1,093,737          | \$ 1,151,172         |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                       |                      |
| Current liabilities:   |                       |                      |
| Accounts payable   | \$ 40,007             | \$ 37,424            |
| Accrued income taxes   | 1,687                 | 4,343                |
| Contract liabilities   | 5,585                 | 11,339               |
| Accrued compensation   | 7,414                 | 5,015                |
| Operating lease liabilities  | 881                   | 1,110                |
| Other accrued liabilities  | 36,252                | 26,281               |
| Total current liabilities  | 91,826                | 85,512               |
| Deferred income taxes  | 6,194                 | 6,779                |
| Income tax payable   | 9,525                 | 9,383                |
| Operating lease liabilities, long-term   | 4,414                 | 5,845                |
| Other long-term liabilities  | 2,001                 | 2,125                |
| Total liabilities  | 113,960               | 109,644              |
| Contingencies (Note 12)  |                       |                      |
| Stockholders' equity:  |                       |                      |
| Preferred stock: 10,000,000 shares authorized at \$0.01 par value (none issued)  | -                     | -                    |
| Common stock:  |                       |                      |
| 100,000,000 shares authorized at \$0.01 par value, 35,385,885 and 35,417,712 shares issued and outstanding at September 30, 2021 and December 31, 2020 | 363                   | 363                  |
| Additional paid-in capital   | 75,154                | 65,613               |
| Retained earnings  | 1,059,563             | 1,125,263            |
| Accumulated other comprehensive losses   | (155,303)             | (149,711)            |
| Total stockholders' equity   | 979,777               | 1,041,528            |
| Total liabilities and stockholders' equity   | \$ 1,093,737          | \$ 1,151,172         |

The accompanying notes are an integral part of these condensed consolidated financial statements.

**DRIL-QUIP, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)**  
**(UNAUDITED)**

|  | Three months ended                    |                  | Nine months ended  |                    |
|--|---------------------------------------|------------------|--------------------|--------------------|
|  | September 30,                         |                  | September 30,      |                    |
|  | 2021                                  | 2020             | 2021               | 2020               |
|  | (In thousands, except per share data) |                  |                    |                    |
| <b>Revenues:</b>                                   |                                       |                  |                    |                    |
| Products   | \$ 53,622                             | \$ 66,451        | \$ 165,066         | \$ 197,142         |
| Services   | 19,560                                | 17,778           | 54,763             | 57,342             |
| Leasing  | 9,815                                 | 7,066            | 25,204             | 23,255             |
| <b>Total revenues</b>                              | <b>82,997</b>                         | <b>91,295</b>    | <b>245,033</b>     | <b>277,739</b>     |
| <b>Cost and expenses:</b>                          |                                       |                  |                    |                    |
| <b>Cost of sales:</b>                              |                                       |                  |                    |                    |
| Products   | 48,120                                | 50,550           | 133,243            | 153,926            |
| Services   | 7,020                                 | 9,125            | 24,687             | 28,035             |
| Leasing  | 7,694                                 | 7,536            | 23,229             | 23,591             |
| <b>Total cost of sales</b>                         | <b>62,834</b>                         | <b>67,211</b>    | <b>181,159</b>     | <b>205,552</b>     |
| Selling, general and administrative                | 25,265                                | 20,843           | 84,416             | 68,832             |
| Engineering and product development                | 3,510                                 | 3,983            | 11,270             | 14,882             |
| Impairments  | -                                     | -                | -                  | 7,719              |
| Restructuring and other charges                    | -                                     | 602              | 26,020             | 34,902             |
| (Gain) loss on sale of assets                      | (13)                                  | 14               | (3,886)            | (538)              |
| Foreign currency transaction (gains) and losses    | (1,663)                               | 746              | (764)              | (1,679)            |
| <b>Total costs and expenses</b>                    | <b>89,933</b>                         | <b>93,399</b>    | <b>298,215</b>     | <b>329,670</b>     |
| <b>Operating loss</b>                              | <b>(6,936)</b>                        | <b>(2,104)</b>   | <b>(53,182)</b>    | <b>(51,931)</b>    |
| Interest income                                    | 188                                   | 188              | 300                | 2,047              |
| Interest expense                                   | (94)                                  | (138)            | (592)              | (538)              |
| Loss before income taxes                           | (6,842)                               | (2,054)          | (53,474)           | (50,422)           |
| Income tax provision (benefit)                     | 4,301                                 | (16,380)         | 11,094             | (30,908)           |
| <b>Net income (loss)</b>                           | <b>\$ (11,143)</b>                    | <b>\$ 14,326</b> | <b>\$ (64,568)</b> | <b>\$ (19,514)</b> |
| <b>Income (loss) per common share:</b>             |                                       |                  |                    |                    |
| Basic  | \$ (0.31)                             | \$ 0.41          | \$ (1.82)          | \$ (0.55)          |
| Diluted  | \$ (0.31)                             | \$ 0.41          | \$ (1.82)          | \$ (0.55)          |
| <b>Weighted average common shares outstanding:</b> |                                       |                  |                    |                    |
| Basic  | 35,387                                | 35,049           | 35,386             | 35,255             |
| Diluted  | 35,387                                | 35,249           | 35,386             | 35,255             |

The accompanying notes are an integral part of these condensed consolidated financial statements.

**DRIL-QUIP, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
**(UNAUDITED)**

|  | <u>Three months ended</u> |                  | <u>Nine months ended</u> |                    |
|--|---------------------------|------------------|--------------------------|--------------------|
|  | <u>September 30,</u>      |                  | <u>September 30,</u>     |                    |
|  | <u>2021</u>               | <u>2020</u>      | <u>2021</u>              | <u>2020</u>        |
|  | (In thousands)            |                  |                          |                    |
| Net income (loss)                              | \$ (11,143)               | \$ 14,326        | \$ (64,568)              | \$ (19,514)        |
| Other comprehensive income (loss), net of tax: |                           |                  |                          |                    |
| Foreign currency translation adjustments       | (6,548)                   | 4,845            | (5,592)                  | (18,086)           |
| Total comprehensive income (loss)              | <u>\$ (17,691)</u>        | <u>\$ 19,171</u> | <u>\$ (70,160)</u>       | <u>\$ (37,600)</u> |

The accompanying notes are an integral part of these condensed consolidated financial statements.

**DRIL-QUIP, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**

|   | Nine months ended<br>September 30, |             |
|---|------------------------------------|-------------|
|   | 2021                               | 2020        |
| (In thousands)  |                                    |             |
| <b>Operating activities</b>   |                                    |             |
| Net loss  | \$ (64,568)                        | \$ (19,514) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: |                                    |             |
| Depreciation and amortization   | 22,658                             | 24,721      |
| Stock-based compensation expense  | 9,541                              | 9,461       |
| Impairments   | -                                  | 7,719       |
| Restructuring and other charges   | 22,465                             | 34,902      |
| Gain on sale of assets  | (3,886)                            | (538)       |
| Deferred income taxes   | (993)                              | (2,116)     |
| Changes in operating assets and liabilities:  |                                    |             |
| Trade receivables, net  | 11,632                             | 8,705       |
| Unbilled receivables  | 25,961                             | (4,815)     |
| Inventories, net  | (6,680)                            | (38,475)    |
| Prepays and other assets  | 14,706                             | (23,185)    |
| Accounts payable and accrued expenses   | 2,902                              | (1,169)     |
| Other, net  | -                                  | 2           |
| Net cash provided by (used in) operating activities                                       | 33,738                             | (4,302)     |
| <b>Investing activities</b>   |                                    |             |
| Purchase of property, plant and equipment   | (7,928)                            | (10,243)    |
| Proceeds from sale of equipment   | 5,967                              | 3,646       |
| Net cash used in investing activities   | (1,961)                            | (6,597)     |
| <b>Financing activities</b>   |                                    |             |
| Repurchase of common shares   | (1,132)                            | (25,000)    |
| Other   | (113)                              | (176)       |
| Net cash used in financing activities   | (1,245)                            | (25,176)    |
| Effect of exchange rate changes on cash activities  | (1,315)                            | (3,700)     |
| Increase (decrease) in cash and cash equivalents  | 29,217                             | (39,775)    |
| Cash and cash equivalents at beginning of period  | 345,955                            | 398,946     |
| Cash and cash equivalents at end of period  | \$ 375,172                         | \$ 359,171  |

The accompanying notes are an integral part of these condensed consolidated financial statements.

**DRIL-QUIP, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
**(UNAUDITED)**

|   | Common Stock                  | Additional Paid-In<br>Capital | Retained<br>Earnings | Accumulated Other<br>Comprehensive<br>Losses | Total               |
|---|-------------------------------|-------------------------------|----------------------|--|---------------------|
|   | (In thousands, except shares) |                               |                      |  |                     |
| <b>Balance at July 1, 2021</b>              | \$ 363                        | \$ 71,878                     | \$ 1,071,838         | \$ (148,755)                                 | \$ 995,324          |
| Foreign currency translation adjustment     | -                             | -                             | -                    | (6,548)                                      | (6,548)             |
| Net loss                                    | -                             | -                             | (11,143)             | -  | (11,143)            |
| Comprehensive loss                          |                               |                               |                      |  | (17,691)            |
| Repurchase of common stock (45,225 shares)  | -                             | -                             | (1,132)              | -  | (1,132)             |
| Stock option expense                        | -                             | 3,276                         | -                    | -  | 3,276               |
| <b>Balance at September 30, 2021</b>        | <u>\$ 363</u>                 | <u>\$ 75,154</u>              | <u>\$ 1,059,563</u>  | <u>\$ (155,303)</u>                          | <u>\$ 979,777</u>   |
| <b>Balance at January 1, 2021</b>           | \$ 363                        | \$ 65,613                     | \$ 1,125,263         | \$ (149,711)                                 | \$ 1,041,528        |
| Foreign currency translation adjustment     | -                             | -                             | -                    | (5,592)                                      | (5,592)             |
| Net loss                                    | -                             | -                             | (64,568)             | -  | (64,568)            |
| Comprehensive loss                          |                               |                               |                      |  | (70,160)            |
| Repurchase of common stock (45,225 shares)  | -                             | -                             | (1,132)              | -  | (1,132)             |
| Stock option expense                        | -                             | 9,541                         | -                    | -  | 9,541               |
| <b>Balance at September 30, 2021</b>        | <u>\$ 363</u>                 | <u>\$ 75,154</u>              | <u>\$ 1,059,563</u>  | <u>\$ (155,303)</u>                          | <u>\$ 979,777</u>   |
|   | Common Stock                  | Additional Paid-In<br>Capital | Retained<br>Earnings | Accumulated Other<br>Comprehensive<br>Losses | Total               |
|   | (In thousands, except shares) |                               |                      |  |                     |
| <b>Balance at July 1, 2020</b>              | \$ 363                        | \$ 59,327                     | \$ 1,122,191         | \$ (166,494)                                 | \$ 1,015,387        |
| Foreign currency translation adjustment     | -                             | -                             | -                    | 4,845  | 4,845               |
| Net income                                  | -                             | -                             | 14,326               | -  | 14,326              |
| Comprehensive income                        |                               |                               |                      |  | 19,171              |
| Stock option expense                        | -                             | 3,004                         | -                    | -  | 3,004               |
| <b>Balance at September 30, 2020</b>        | <u>\$ 363</u>                 | <u>\$ 62,331</u>              | <u>\$ 1,136,517</u>  | <u>\$ (161,649)</u>                          | <u>\$ 1,037,562</u> |
| <b>Balance at January 1, 2020</b>           | \$ 371                        | \$ 52,870                     | \$ 1,181,023         | \$ (143,563)                                 | \$ 1,090,701        |
| Foreign currency translation adjustment     | -                             | -                             | -                    | (18,086)                                     | (18,086)            |
| Net loss                                    | -                             | -                             | (19,514)             | -  | (19,514)            |
| Comprehensive loss                          |                               |                               |                      |  | (37,600)            |
| Repurchase of common stock (808,389 shares) | (8)                           | -                             | (24,992)             | -  | (25,000)            |
| Stock option expense                        | -                             | 9,461                         | -                    | -  | 9,461               |
| <b>Balance at September 30, 2020</b>        | <u>\$ 363</u>                 | <u>\$ 62,331</u>              | <u>\$ 1,136,517</u>  | <u>\$ (161,649)</u>                          | <u>\$ 1,037,562</u> |

The accompanying notes are an integral part of these condensed consolidated financial statements.

**DRIL-QUIP, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(UNAUDITED)****1. Organization and Basis of Presentation**

Dril-Quip, Inc., a Delaware corporation (the “Company” or “Dril-Quip”), designs, manufactures, sells and services highly engineered drilling and production equipment that is well suited primarily for use in deepwater, harsh environment and severe service applications. The Company’s principal products consist of subsea and surface wellheads, subsea and surface production trees, mudline hanger systems, specialty connectors and associated pipe, drilling and production riser systems, liner hangers, wellhead connectors, diverters and safety valves. Dril-Quip’s products are used by major integrated, large independent and foreign national oil and gas companies and drilling contractors throughout the world. Dril-Quip also provides technical advisory assistance on an as-requested basis during installation of its products, as well as rework and reconditioning services for customer-owned Dril-Quip products. In addition, Dril-Quip’s customers may rent or purchase running tools from the Company for use in the installation and retrieval of the Company’s products.

The Company’s operations are organized into three geographic segments — Western Hemisphere (including North and South America; headquartered in Houston, Texas), Eastern Hemisphere (including Europe and Africa; headquartered in Aberdeen, Scotland) and Asia-Pacific (including the Pacific Rim, Southeast Asia, Australia, India and the Middle East; headquartered in Singapore). Each of these segments sells similar products and services, and the Company has manufacturing facilities in all three of its regional headquarter locations, as well as in Macae, Brazil. The Company’s major subsidiaries are Dril-Quip (Europe) Limited, located in Aberdeen with branches in Azerbaijan, Denmark, Norway and Holland; Dril-Quip Asia-Pacific PTE Ltd., located in Singapore; and Dril-Quip do Brasil LTDA, located in Macae, Brazil. Other operating subsidiaries include TIW Corporation (TIW) and Honing, Inc., both located in Houston, Texas; DQ Holdings Pty. Ltd., located in Perth, Australia; Dril-Quip Cross (Ghana) Ltd., located in Takoradi, Ghana; PT DQ Oilfield Services Indonesia, located in Jakarta, Indonesia; Dril-Quip Egypt for Petroleum Services S.A.E., located in Alexandria, Egypt; Dril-Quip TIW Saudi Arabia Limited, located in Dammam, Kingdom of Saudi Arabia; Dril-Quip Oilfield Services (Tianjin) Co. Ltd., located in Tianjin, China, with branches in Shenzhen and Beijing, China; Dril-Quip Qatar LLC, located in Doha, Qatar; Dril-Quip TIW Mexico S. de R.L.C.V., located in Villahermosa, Mexico; Dril-Quip Venezuela S.C.A., located in Anaco, Venezuela and with a registered branch located in Ecuador; TIW (UK) Limited, located in Aberdeen, Scotland; and TIW International LLC, with a registered branch located in Singapore.

The condensed consolidated financial statements included herein are unaudited. The balance sheet at December 31, 2020 has been derived from the audited consolidated financial statements as of that date. In the opinion of management, the unaudited condensed consolidated interim financial statements include all normal recurring adjustments necessary for a fair statement of the financial position as of September 30, 2021 and the results of operations and comprehensive income (loss) for the three and nine months ended September 30, 2021 and 2020 and cash flows for the nine months ended September 30, 2021 and 2020. Certain information and footnote disclosures normally included in annual audited consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission. The results of operations and comprehensive income (loss) for the three and nine months ended September 30, 2021 and cash flows for the nine months ended September 30, 2021 are not necessarily indicative of the results to be expected for the full year. The condensed consolidated financial statements included herein should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2020.

We are continuing to experience effects resulting from the COVID-19 pandemic, albeit to a lesser degree as compared to 2020. Increased availability of the COVID-19 vaccine to the general population has resulted in a lower rate of new infections, hospitalizations and deaths in the current quarter, as compared to 2020. Although the downward trend is encouraging, the potential emergence and spread of new COVID-19 variants adds uncertainty for an economic recovery. The effect of the pandemic and the actions and changes in consumer behavior resulting from the pandemic continue to impact our business and have significantly reduced global economic activity and global demand for oil and gas, despite marginal improvements in the current quarter. Effects of the pandemic are also seen in our supply chain as a result of logistics bottlenecks which are resulting in increased transportation costs. We continue to experience delayed recovery in 2021 as the market continues to be volatile and challenging. The extent of the impact of the pandemic, including economic impacts that may persist following the widespread global deployment of vaccines and the fluctuations in demand for oil on our operational and financial performance will depend on future developments, which are uncertain and cannot be predicted. An extended period of economic disruption could have a material adverse impact on our business, results of operations, access to sources of liquidity and overall financial condition.



## 2. Significant Accounting Policies

### *Principles of Consolidation*

The condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All material intercompany accounts and transactions have been eliminated.

### *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect reported amounts of assets and liabilities as of the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates. Some of the Company's more significant estimates are those affected by critical accounting policies for revenue recognition and asset recoverability tests and inventories.

### *Revenue Recognition*

The Company generates revenues through the sale of products, the sale of services and the leasing of running tools. The Company normally negotiates contracts for products, including those accounted for under the over-time method, rental tools and services separately. Modifications to the scope and price of sales contracts may occur in the form of variations and change orders. For all product sales, it is the customer's decision as to the timing of the product installation, as well as whether Dril-Quip running tools will be purchased or rented. Furthermore, the customer is under no obligation to utilize the Company's technical advisory assistance services. The customer may instead choose to use a third party or its own personnel.

### *Leasing revenues*

The Company earns leasing revenues from the rental of running tools. Revenues from rental of running tools are recognized on a day rate basis over the lease term, which is generally between one to three months.

On April 30, 2021, as a result of lower activity stemming from the COVID-19 pandemic, AFGlobal Corporation provided a 90-day written notice of termination of the lease agreement between the Company and AFGlobal in relation to the Company's forge facility and equipment at its Houston Eldridge campus.

Based on the initial 5-year term of the lease agreement, the Company had straight-lined the total anticipated lease revenue for that initial term into equal monthly lease revenue. As a result of the lease termination, the Company has approximately \$2.3 million in unbilled revenue that was expensed in second quarter of 2021. Leasing revenue from renting this facility that was not recognized due to the termination of the lease agreement was approximately \$0.5 million and \$1.0 million for the three and nine months ended September 30, 2021, respectively. The Company has numerous other forging suppliers and does not expect any disruptions in forging supply as a result of the lease termination.

### *Fair Value of Financial Instruments*

The Company's financial instruments consist primarily of cash and cash equivalents, receivables and payables. The carrying values of these financial instruments approximate their respective fair values as they are short-term in nature.

### *Impairment of Long-Lived Assets*

Long-lived assets, including property, plant and equipment and definite-lived intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. We evaluate our property and equipment and definite-lived intangible assets for impairment whenever changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. Should the review indicate that the carrying value is not fully recoverable, the amount of the impairment loss is determined by comparing the carrying value to the estimated fair value. We assess recoverability based on undiscounted future net cash flows. Estimating future net cash flows requires us to make judgements regarding long-term forecasts of future revenues and costs related to the assets subject to review. These forecasts are uncertain in that they require assumptions about our revenue growth, operating margins, capital expenditures, future market conditions and technological developments. If changes in these assumptions occur, our expectations regarding future net cash flows may change such that a material impairment could result.

### Restructuring and Other Charges

During the first half of 2021, the Company incurred additional costs under our existing 2018 global strategic plan to realign manufacturing facilities globally. These charges were primarily related to the restructuring of our downhole tools business where we exited certain underperforming countries and markets and shifted from manufacturing in-house to a vendor sourcing model. The Company has concluded its 2018 global strategic plan and did not incur any additional costs in the third quarter of 2021. During the first half of 2020, the overall offshore market conditions declined as a result of the COVID-19 pandemic and developments in global oil markets. As such, we incurred additional costs under our existing 2018 global strategic plan to realign our manufacturing facilities globally. These charges are reflected as "Restructuring and other charges" in our condensed consolidated statements of income (loss).

### Repurchase of Equity Securities

On February 26, 2019, the Board of Directors authorized a share repurchase plan under which the Company can repurchase up to \$100 million of its common stock. The repurchase plan has no set expiration date and any repurchased shares are expected to be cancelled. The manner, timing and amount of any purchase will be determined by management based on an evaluation of market conditions, stock price, liquidity and other factors. The program does not obligate the Company to acquire any amount of common stock and may be modified or superseded at any time at the Company's discretion.

For the three and nine months ended September 30, 2021, the Company purchased 45,225 shares under the share repurchase plan at an average price of approximately \$25.02 per share totaling approximately \$1.1 million and has retired such shares.

For the nine months ended September 30, 2020, the Company purchased 808,389 shares under the share repurchase plan at an average price of approximately \$30.91 per share totaling approximately \$25.0 million and has retired such shares. For the three months ended September 30, 2020, the Company purchased no shares under the share repurchase plan.

### Earnings Per Share

Basic earnings per common share is computed by dividing net income (loss) by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per common share is computed considering the dilutive effect of stock awards using the treasury stock method.

In each relevant period, the net income used in the basic and dilutive earnings per share calculations is the same. The following table reconciles the weighted average basic number of common shares outstanding and the weighted average diluted number of common shares outstanding for the purpose of calculating basic and diluted earnings per share:

|  | Three months ended<br>September 30, |        | Nine months ended<br>September 30, |        |
|--|-------------------------------------|--------|------------------------------------|--------|
|  | 2021                                | 2020   | 2021                               | 2020   |
|  | (In thousands)                      |        |                                    |        |
| Weighted average common shares outstanding – basic   | 35,387                              | 35,049 | 35,386                             | 35,255 |
| Dilutive effect of common stock awards               | -                                   | 200    | -                                  | -      |
| Weighted average common shares outstanding – diluted | 35,387                              | 35,249 | 35,386                             | 35,255 |

For the three and nine months ended September 30, 2021 and 2020, the Company has excluded the following common stock options and awards because their impact on the income/(loss) per share is anti-dilutive (in thousands on a weighted average basis):

|                         | Three months ended<br>September 30, |      | Nine months ended<br>September 30, |      |
|-------------------------|-------------------------------------|------|------------------------------------|------|
|                         | 2021                                | 2020 | 2021                               | 2020 |
|                         | (In thousands)                      |      |                                    |      |
| Director stock awards   | 63                                  | -    | 60                                 | 45   |
| Stock options           | 54                                  | -    | 56                                 | 122  |
| Performance share units | 323                                 | 9    | 328                                | 276  |
| Restricted stock awards | 477                                 | 7    | 479                                | 326  |

### 3. New Accounting Standards

In December 2019, the FASB issued ASU 2019-12 “Income Taxes (Topic 740).” Topic 740 is effective for fiscal years and interim periods beginning after December 15, 2020. This update simplifies the accounting for income taxes by removing certain exceptions such as the exception to the incremental approach for intraperiod tax allocation, the exception to the requirement to recognize a deferred tax liability for equity method investments, the exception to the ability not to recognize a deferred tax liability for a foreign subsidiary and the exception to the general methodology for calculating income taxes in an interim period. The adoption of ASU 2019-12 did not have a material impact on our financial position, results of operations or cash flows.

### 4. Revenue Recognition

Revenues from contracts with customers (excludes leasing) consisted of the following:

|                  | Three months ended September 30, |                  |                    |                  |                  |                  |                  |                  |
|------------------|----------------------------------|------------------|--------------------|------------------|------------------|------------------|------------------|------------------|
|                  | Western Hemisphere               |                  | Eastern Hemisphere |                  | Asia-Pacific     |                  | Total            |                  |
|                  | 2021                             | 2020             | 2021               | 2020             | 2021             | 2020             | 2021             | 2020             |
|                  | (In thousands)                   |                  |                    |                  |                  |                  |                  |                  |
| Product Revenues | \$ 37,612                        | \$ 36,095        | \$ 10,217          | \$ 13,377        | \$ 5,793         | \$ 16,979        | \$ 53,622        | \$ 66,451        |
| Service Revenues | 12,872                           | 10,974           | 2,458              | 3,689            | 4,230            | 3,115            | 19,560           | 17,778           |
| <b>Total</b>     | <b>\$ 50,484</b>                 | <b>\$ 47,069</b> | <b>\$ 12,675</b>   | <b>\$ 17,066</b> | <b>\$ 10,023</b> | <b>\$ 20,094</b> | <b>\$ 73,182</b> | <b>\$ 84,229</b> |

  

|                  | Nine months ended September 30, |                   |                    |                  |                  |                  |                   |                   |
|------------------|---------------------------------|-------------------|--------------------|------------------|------------------|------------------|-------------------|-------------------|
|                  | Western Hemisphere              |                   | Eastern Hemisphere |                  | Asia-Pacific     |                  | Total             |                   |
|                  | 2021                            | 2020              | 2021               | 2020             | 2021             | 2020             | 2021              | 2020              |
|                  | (In thousands)                  |                   |                    |                  |                  |                  |                   |                   |
| Product Revenues | \$ 112,787                      | \$ 114,364        | \$ 25,505          | \$ 45,772        | \$ 26,774        | \$ 37,006        | \$ 165,066        | \$ 197,142        |
| Service Revenues | 33,813                          | 35,094            | 7,748              | 11,620           | 13,202           | 10,628           | 54,763            | 57,342            |
| <b>Total</b>     | <b>\$ 146,600</b>               | <b>\$ 149,458</b> | <b>\$ 33,253</b>   | <b>\$ 57,392</b> | <b>\$ 39,976</b> | <b>\$ 47,634</b> | <b>\$ 219,829</b> | <b>\$ 254,484</b> |

#### Contract Balances

Balances related to contracts with customers consisted of the following:

#### Contract Assets (amounts shown in thousands)

|                                       |                   |
|---------------------------------------|-------------------|
| Contract Assets at December 31, 2020  | \$ 135,973        |
| Additions                             | 72,185            |
| Transfers to Trade Receivables, Net   | (97,722)          |
| Contract Assets at September 30, 2021 | <u>\$ 110,436</u> |

#### Contract Liabilities (amounts shown in thousands)

|  |                 |
|--|-----------------|
| Contract Liabilities at December 31, 2020  | \$ 10,815       |
| Additions                                  | 21,160          |
| Revenue Recognized                         | (26,627)        |
| Contract Liabilities at September 30, 2021 | <u>\$ 5,348</u> |

Contract assets include unbilled accounts receivable associated with contracts accounted for under the over-time accounting method which were approximately \$65.0 million and \$98.2 million at September 30, 2021 and December 31, 2020, respectively. Unbilled contract assets are transferred to trade receivables, net, when the rights become unconditional. The contract liabilities primarily relate to advance payments from customers.

Obligations for returns and refunds were considered immaterial as of September 30, 2021.

### Remaining Performance Obligations

The aggregate amount of the transaction price allocated to remaining performance obligations from our over-time product lines was \$39.5 million as of September 30, 2021. The Company expects to recognize revenue on approximately 89.9% of the remaining performance obligations over the next 12 months and the remaining 10.1% thereafter.

The Company applies the practical expedient available under the revenue standard and does not disclose information about remaining performance obligations that have original expected durations of one year or less.

### 5. Stock-Based Compensation and Stock Awards

During the three and nine months ended September 30, 2021, the Company recognized approximately \$3.3 million and \$9.5 million, respectively, of stock-based compensation expense. Stock-based compensation is included in "Selling, general and administrative" in our accompanying condensed consolidated statements of income (loss) and "Additional paid-in capital" in our accompanying condensed consolidated balance sheets. During the three and nine months ended September 30, 2020, the Company recognized approximately \$3.0 million and \$9.5 million, respectively of stock-based compensation expense.

### 6. Inventories, net

Inventories consist of the following:

|  | September 30,<br>2021 | December 31,<br>2020 |
|--|-----------------------|----------------------|
|  | (In thousands)        |                      |
| Raw materials and supplies                           | \$ 28,612             | \$ 32,833            |
| Work in progress                                     | 42,278                | 44,924               |
| Finished goods                                       | 215,640               | 216,928              |
|  | 286,530               | 294,685              |
| Less: allowance for slow moving and excess inventory | (91,810)              | (82,149)             |
| Total inventory                                      | <u>\$ 194,720</u>     | <u>\$ 212,536</u>    |

### 7. Impairment, Restructuring and Other Charges

#### Restructuring and Other Charges

During the nine months ended September 30, 2021, the Company incurred additional costs under our existing 2018 global strategic plan to realign manufacturing facilities globally. These charges were primarily related to the restructuring of our downhole tools business where we exited certain underperforming countries and markets and shifted from manufacturing in-house to a vendor sourcing model. The Company has concluded its 2018 global strategic plan and did not incur any additional costs during the three months ended September 30, 2021.

As a result of unfavorable market conditions primarily due to the COVID-19 pandemic and developments in global oil markets, which triggered historically low crude oil prices and decreases in our customers' capital budgets, we incurred additional costs under our 2018 global strategic plan primarily focused on workforce reductions and the reorganization of certain facilities during the three and nine months ended September 30, 2020.

The following table summarizes the components of charges included in "Restructuring and other charges" in our condensed consolidated statements of income (loss) for the three and nine months ended September 30, 2021 and 2020 (in thousands):

|                             | Three months ended September 30, |               | Nine months ended September 30, |                  |
|-----------------------------|----------------------------------|---------------|---------------------------------|------------------|
|                             | 2021                             | 2020          | 2021                            | 2020             |
| Inventory write-down        | \$ -                             | \$ -          | \$ 19,251                       | \$ 17,272        |
| Severance                   | -                                | -             | 2,745                           | 8,399            |
| Long-lived asset write-down | -                                | -             | -                               | 7,854            |
| Other                       | -                                | 602           | 4,024                           | 1,377            |
|                             | <u>\$ -</u>                      | <u>\$ 602</u> | <u>\$ 26,020</u>                | <u>\$ 34,902</u> |

The following table summarizes the changes to our accrued liability balance related to restructuring and other charges as of September 30, 2021 (in thousands):

|                                      | <b>Total</b>    |
|--------------------------------------|-----------------|
| Beginning balance at January 1, 2021 | \$ 1,146        |
| Additions for costs expensed         | 5,768           |
| Reductions for payments              | (2,554)         |
| Other                                | (2)             |
| Ending balance at September 30, 2021 | <u>\$ 4,358</u> |

#### *Goodwill Impairment*

For the three months ended March 31, 2020, as a result of our updated assessment of market conditions and restructuring efforts, impairment losses consisted of a full impairment of our Goodwill balance of \$7.7 million, all of which was in the Eastern Hemisphere reporting unit. These charges are reflected as "Impairments" in our condensed consolidated statements of income (loss).

### **8. Intangible Assets**

Intangible assets, the majority of which were acquired in the acquisition of TIW and OPT, consist of the following:

|                        | Estimated Useful Lives | <b>September 30, 2021</b> |                          |                              | Net Book Value   |
|------------------------|------------------------|---------------------------|--------------------------|------------------------------|------------------|
|                        |                        | Gross Book Value          | Accumulated Amortization | Foreign Currency Translation |                  |
| (In thousands)         |                        |                           |                          |                              |                  |
| Trademarks             | 15 years               | \$ 8,257                  | \$ (1,442)               | \$ (28)                      | \$ 6,787         |
| Patents                | 15 - 30 years          | 6,058                     | (3,179)                  | (1)                          | 2,878            |
| Customer relationships | 5 - 15 years           | 26,078                    | (8,678)                  | (49)                         | 17,351           |
| Organizational costs   | 3 years                | 185                       | (61)                     | (3)                          | 121              |
|                        |                        | <u>\$ 40,578</u>          | <u>\$ (13,360)</u>       | <u>\$ (81)</u>               | <u>\$ 27,137</u> |

|                        | Estimated Useful Lives | <b>December 31, 2020</b> |                          |                              | Net Book Value   |
|------------------------|------------------------|--------------------------|--------------------------|------------------------------|------------------|
|                        |                        | Gross Book Value         | Accumulated Amortization | Foreign Currency Translation |                  |
| (In thousands)         |                        |                          |                          |                              |                  |
| Trademarks             | 15 years               | \$ 8,238                 | \$ (1,033)               | \$ (5)                       | \$ 7,200         |
| Patents                | 15 - 30 years          | 6,054                    | (2,715)                  | (2)                          | 3,337            |
| Customer relationships | 5 - 15 years           | 25,966                   | (7,304)                  | 65                           | 18,727           |
| Organizational costs   | 3 years                | 179                      | (15)                     | 6                            | 170              |
|                        |                        | <u>\$ 40,437</u>         | <u>\$ (11,067)</u>       | <u>\$ 64</u>                 | <u>\$ 29,434</u> |

### **9. Asset Backed Loan (ABL) Credit Facility**

On February 23, 2018, the Company, as borrower, and the Company's subsidiaries TIW and Honing, Inc., as guarantors, entered into a five-year senior secured revolving credit facility (the "ABL Credit Facility") with JPMorgan Chase Bank, N.A., as administrative agent, and other financial institutions, as lenders with total commitments of \$100.0 million, including up to \$10.0 million available for letters of credit. The maximum amount that the Company may borrow under the ABL Credit Facility is subject to the borrowing base, which is based on a percentage of eligible accounts receivable and eligible inventory, subject to reserves and other adjustments.

All obligations under the ABL Credit Facility are fully and unconditionally guaranteed jointly and severally by the Company, TIW, Honing, Inc., and future significant domestic subsidiaries, subject to customary exceptions. Borrowings under the ABL Credit Facility are secured by liens on substantially all of the Company's personal property, and bear interest at the Company's option at either (i) the CB Floating Rate (as defined therein), calculated as the rate of interest publicly announced by JPMorgan Chase Bank, N.A., as its "prime rate," subject to each increase or decrease in such prime rate effective as of the date such change occurs, with such CB Floating Rate not being less than Adjusted One Month LIBOR (as defined therein) or (ii) the Adjusted LIBOR (as defined therein), plus, in each case, an applicable margin. The applicable margin ranges from 1.00% to 1.50% per annum for CBFR loans and 2.00% to 2.50% per annum for Eurodollar loans and, in each case, is based on the Company's leverage ratio. The unused portion of the ABL Credit Facility is subject to a commitment fee that varies from 0.250% to 0.375% per annum, according to the average unused commitments under the ABL Credit Facility. Interest on Eurodollar loans is payable at the end of the selected interest period, but no less frequently than quarterly. Interest on CB Floating Rate loans is payable monthly in arrears.

The ABL Credit Facility contains various covenants and restrictive provisions that limit the Company's ability to, among other things, (1) enter into asset sales; (2) incur additional indebtedness; (3) make investments or loans and create liens; (4) pay certain dividends or make other distributions; and (5) engage in transactions with affiliates. The ABL Credit Facility also requires the Company to maintain a fixed charge coverage ratio of 1.1 to 1.0, based on the ratio of EBITDA (as defined therein) to Fixed Charges (as defined therein) during certain periods, including when availability under the ABL Credit Facility is under certain levels. If the Company fails to perform its obligations under the agreement that results in an event of default, the commitments under the ABL Credit Facility could be terminated and any outstanding borrowings under the ABL Credit Facility may be declared immediately due and payable. The ABL Credit Facility also contains cross default provisions that apply to the Company's other indebtedness. The Company is in compliance with the related covenants as of September 30, 2021.

As of September 30, 2021, the availability under the ABL Credit Facility was \$31.1 million, after taking into account the outstanding letters of credit of approximately \$7.2 million issued under the facility.

## 10. Geographic Areas

The Company's operations are organized into three geographic segments - Western Hemisphere (including North and South America; headquartered in Houston, Texas), Eastern Hemisphere (including Europe and Africa; headquartered in Aberdeen, Scotland) and Asia-Pacific (including the Pacific Rim, Southeast Asia, Australia, India and the Middle East; headquartered in Singapore). Each of these segments sells similar products and services and the Company has manufacturing facilities in all three of its regional headquarter locations as well as in Macae, Brazil.

Eliminations of operating profits are related to intercompany inventory transfers that are deferred until shipment is made to third party customers.

|  | Three months ended September 30, |           |                    |           |              |           |              |             |            |            |
|--|----------------------------------|-----------|--------------------|-----------|--------------|-----------|--------------|-------------|------------|------------|
|  | Western Hemisphere               |           | Eastern Hemisphere |           | Asia-Pacific |           | DQ Corporate |             | Total      |            |
|  | 2021                             | 2020      | 2021               | 2020      | 2021         | 2020      | 2021         | 2020        | 2021       | 2020       |
|  | (In thousands)                   |           |                    |           |              |           |              |             |            |            |
| Revenues                                   |                                  |           |                    |           |              |           |              |             |            |            |
| Products                                   |                                  |           |                    |           |              |           |              |             |            |            |
| Point in Time                              | \$ 22,692                        | \$ 16,937 | \$ 6,276           | \$ 8,033  | \$ 3,953     | \$ 7,776  | \$ -         | \$ -        | \$ 32,921  | \$ 32,746  |
| Over-Time                                  | 14,920                           | 19,158    | 3,941              | 5,344     | 1,840        | 9,203     | -            | -           | 20,701     | 33,705     |
| Total Products                             | 37,612                           | 36,095    | 10,217             | 13,377    | 5,793        | 16,979    | -            | -           | 53,622     | 66,451     |
| Services                                   |                                  |           |                    |           |              |           |              |             |            |            |
| Technical Advisory                         | 10,814                           | 8,317     | 2,038              | 2,285     | 3,629        | 2,402     | -            | -           | 16,481     | 13,004     |
| Reconditioning                             | 2,058                            | 2,657     | 420                | 1,404     | 601          | 713       | -            | -           | 3,079      | 4,774      |
| Total Services<br>(excluding rental tools) | 12,872                           | 10,974    | 2,458              | 3,689     | 4,230        | 3,115     | -            | -           | 19,560     | 17,778     |
| Leasing                                    | 6,627                            | 5,384     | 1,564              | 1,970     | 1,624        | (288)     | -            | -           | 9,815      | 7,066      |
| Total Services<br>(including rental tools) | 19,499                           | 16,358    | 4,022              | 5,659     | 5,854        | 2,827     | -            | -           | 29,375     | 24,844     |
| Intercompany                               | 4,029                            | 3,060     | 920                | 1,006     | 576          | 4,329     | -            | -           | 5,525      | 8,395      |
| Eliminations                               | -                                | -         | -                  | -         | -            | -         | (5,525)      | (8,395)     | (5,525)    | (8,395)    |
| Total Revenues                             | \$ 61,140                        | \$ 55,513 | \$ 15,159          | \$ 20,042 | \$ 12,223    | \$ 24,135 | \$ (5,525)   | \$ (8,395)  | \$ 82,997  | \$ 91,295  |
| Depreciation and amortization              | \$ 4,736                         | \$ 4,831  | \$ 1,044           | \$ 882    | \$ 1,194     | \$ 1,265  | \$ 925       | \$ 930      | \$ 7,899   | \$ 7,908   |
| Income (loss) before income taxes          | \$ 8,417                         | \$ 3,339  | \$ (1,273)         | \$ 3,255  | \$ 2,002     | \$ 5,396  | \$ (15,988)  | \$ (14,044) | \$ (6,842) | \$ (2,054) |

During the three months ended September 30, 2021, the Company did not incur any additional restructuring and other charges. During the three months ended September 30, 2020, we recorded restructuring and other charges of \$0.6 million, consisting primarily of consulting fees in DQ Corporate.

|  | Nine months ended September 30, |            |                    |             |              |           |              |             |             |             |
|--|---------------------------------|------------|--------------------|-------------|--------------|-----------|--------------|-------------|-------------|-------------|
|  | Western Hemisphere              |            | Eastern Hemisphere |             | Asia-Pacific |           | DQ Corporate |             | Total       |             |
|  | 2021                            | 2020       | 2021               | 2020        | 2021         | 2020      | 2021         | 2020        | 2021        | 2020        |
| (In thousands)                             |                                 |            |                    |             |              |           |              |             |             |             |
| <b>Revenues</b>                            |                                 |            |                    |             |              |           |              |             |             |             |
| <b>Products</b>                            |                                 |            |                    |             |              |           |              |             |             |             |
| Point in Time                              | \$ 76,927                       | \$ 54,774  | \$ 17,086          | \$ 23,834   | \$ 19,420    | \$ 20,516 | \$ -         | \$ -        | \$ 113,433  | \$ 99,124   |
| Over-Time                                  | 35,860                          | 59,590     | 8,419              | 21,938      | 7,354        | 16,490    | -            | -           | 51,633      | 98,018      |
| Total Products                             | 112,787                         | 114,364    | 25,505             | 45,772      | 26,774       | 37,006    | -            | -           | 165,066     | 197,142     |
| <b>Services</b>                            |                                 |            |                    |             |              |           |              |             |             |             |
| Technical Advisory                         | 26,916                          | 26,169     | 6,058              | 7,718       | 11,603       | 8,629     | -            | -           | 44,577      | 42,516      |
| Reconditioning                             | 6,897                           | 8,925      | 1,690              | 3,902       | 1,599        | 1,999     | -            | -           | 10,186      | 14,826      |
| Total Services<br>(excluding rental tools) | 33,813                          | 35,094     | 7,748              | 11,620      | 13,202       | 10,628    | -            | -           | 54,763      | 57,342      |
| Leasing                                    | 15,297                          | 13,819     | 4,635              | 6,544       | 5,272        | 2,892     | -            | -           | 25,204      | 23,255      |
| Total Services<br>(including rental tools) | 49,110                          | 48,913     | 12,383             | 18,164      | 18,474       | 13,520    | -            | -           | 79,967      | 80,597      |
| Intercompany                               | 8,807                           | 8,691      | 1,558              | 2,026       | 8,875        | 9,998     | -            | -           | 19,240      | 20,715      |
| Eliminations                               | -                               | -          | -                  | -           | -            | -         | (19,240)     | (20,715)    | (19,240)    | (20,715)    |
| Total                                      | \$ 170,704                      | \$ 171,968 | \$ 39,446          | \$ 65,962   | \$ 54,123    | \$ 60,524 | \$ (19,240)  | \$ (20,715) | \$ 245,033  | \$ 277,739  |
| Depreciation and amortization              | \$ 13,291                       | \$ 15,254  | \$ 3,021           | \$ 2,808    | \$ 3,576     | \$ 3,859  | \$ 2,770     | \$ 2,800    | \$ 22,658   | \$ 24,721   |
| Income (loss) before income taxes          | \$ (13,136)                     | \$ 16,516  | \$ (583)           | \$ (27,415) | \$ 17,540    | \$ 12,580 | \$ (57,295)  | \$ (52,103) | \$ (53,474) | \$ (50,422) |

During the nine months ended September 30, 2021, we recorded \$26.0 million of restructuring and other charges. These charges were related to non-cash inventory write downs, severance charges and other charges, primarily consisting of facilities restructuring exit costs and consulting fees. Of these charges, \$21.0 million was recorded in the Western Hemisphere, \$1.6 million in the Eastern Hemisphere and \$3.4 million in DQ Corporate. During the nine months ended September 30, 2020, we recorded impairments, restructuring and other charges of \$42.6 million. Of these charges, \$32.1 million was recorded in the Eastern Hemisphere, \$3.2 million in the Western Hemisphere, \$7.1 million in DQ Corporate and \$0.2 million in Asia-Pacific.

|                                 | September 30,<br>2021 |           | December 31,<br>2020 |           |
|---------------------------------|-----------------------|-----------|----------------------|-----------|
| (In thousands)                  |                       |           |                      |           |
| <b>Total long-lived assets:</b> |                       |           |                      |           |
| Western Hemisphere              | \$                    | 335,900   | \$                   | 350,577   |
| Eastern Hemisphere              |                       | 222,057   |                      | 222,741   |
| Asia-Pacific                    |                       | 62,448    |                      | 68,600    |
| Eliminations                    |                       | (353,939) |                      | (353,939) |
| Total                           | \$                    | 266,466   | \$                   | 287,979   |
| <b>Total assets:</b>            |                       |           |                      |           |
| Western Hemisphere              | \$                    | 720,191   | \$                   | 769,649   |
| Eastern Hemisphere              |                       | 793,426   |                      | 779,147   |
| Asia-Pacific                    |                       | 195,085   |                      | 186,808   |
| Eliminations                    |                       | (614,965) |                      | (584,432) |
| Total                           | \$                    | 1,093,737 | \$                   | 1,151,172 |

As of September 30, 2021, we had \$19.1 million of non-cash inventory write-downs in the Western Hemisphere and \$0.2 million in the Eastern Hemisphere as we shifted from the manufacturing of our downhole tools products business to a vendor outsourcing model. During 2020, we wrote down \$25.5 million related to inventory and long-lived assets balances, with \$22.3 million recorded in the Eastern Hemisphere and \$3.2 million in the Western Hemisphere. We also recorded a full impairment of our goodwill balance of \$7.7 million during the first quarter of 2020, all of which was in the Eastern Hemisphere.

## 11. Income Tax

The effective tax rate for the three and nine months ended September 30, 2021 was (62.9)% and (20.7)%, respectively, compared to 797.5% and 61.3%, respectively, for the same period in 2020. The change in the effective tax rate between the periods resulted primarily from discretely recognized tax benefits of Net Operating Losses (“NOLs”) in 2020 due to the Coronavirus, Aid, Relief and Economic Security Act (“CARES Act”), changes in income or loss earned in foreign jurisdictions, changes in valuation allowances in the United States, changes in nondeductible compensation and the mix of earnings in jurisdictions with differing tax rates.

We have historically considered the majority of undistributed earnings of our foreign subsidiaries and equity investees to be indefinitely reinvested, and, accordingly, no deferred taxes had been provided on the indefinitely reinvested earnings. As of June 30, 2020, the Company reversed its indefinite reinvestment assertion. As a result, we recorded a deferred foreign tax liability, which had a balance of \$3.3 million as of September 30, 2021, and is primarily related to estimated foreign withholding tax associated with repatriating all non-U.S. earnings back to the United States.

The Company is subject to ongoing tax authority examinations in various jurisdictions in which it operates. The Company reviews its accrual for uncertain tax positions at each reporting period and updates positions based on available information.

## 12. Contingencies

### *Brazilian Tax Issue*

From 2002 to 2007, the Company's Brazilian subsidiary imported goods through, and paid taxes on such imports to, the State of Espirito Santo in Brazil. Upon the final sale of these goods, the Company's Brazilian subsidiary collected taxes from customers and remitted them to the State of Rio de Janeiro net of the taxes paid on importation of those goods to the State of Espirito Santo in accordance with the Company's understanding of Brazilian tax laws. In December 2010 and January 2011, the Company's Brazilian subsidiary was served with two assessments totaling approximately \$13.0 million from the State of Rio de Janeiro to cancel the credits associated with the tax payments to the State of Espirito Santo on the importation of goods from July 2005 to October 2007. The Company's Brazilian subsidiary objected to these assessments and filed appeals with a State of Rio de Janeiro judicial court to annul both of these tax assessments.

In the first quarter of 2021, the relevant governmental agencies of the State of Rio de Janeiro authorized an amnesty program with interest discounts and reduced fines. The Company's Brazilian subsidiary elected to participate in this amnesty program and recorded the settlement amount of approximately \$2.1 million as of March 31, 2021. As a result of settling these tax assessments with the relevant governmental agencies pursuant to the amnesty program, the security amounts previously deposited with the court totaling approximately \$6 million at current exchange rates were returned to our Brazilian subsidiary during the second and third quarter of 2021.

### *FMC Technologies Lawsuit*

On October 5, 2020, FMC Technologies, Inc. ("FMC") sued the Company alleging misappropriation of trade secrets and sought money damages and injunctive relief in the 127th District Court of Harris County in an action styled *FMC Technologies, Inc. v. Richard Murphy and Dril-Quip, Inc.*, Cause No. 2020-63081. FMC alleged that its former employee communicated FMC trade secrets to the Company and the Company used those trade secrets in its VXTe subsea tree systems. On April 29, 2021, the jury returned a verdict in favor of the Company. FMC filed a notice of appeal on August 20, 2021. The Company intends to continue its vigorous defense of this matter on appeal.

### *General*

The Company operates its business and markets its products and services in most of the significant oil and gas producing areas in the world and is, therefore, subject to the risks customarily attendant to international operations and is dependent on the condition of the oil and gas industry. Additionally, certain of the Company's products are used in potentially hazardous drilling, completion, and production applications that can cause personal injury, property damage and environmental claims. Although exposure to such risks have not resulted in any significant problems for the Company in the past, ongoing exposure to these risks and future developments could adversely impact the Company in the future.

The Company is also involved in a number of legal actions arising in the ordinary course of business. Although no assurance can be given with respect to the ultimate outcome of such legal action, in the opinion of management, the ultimate liability with respect thereto will not have a material adverse effect on the Company's results of operations, financial position or cash flows.



## Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

### Forward-Looking Statements

This Quarterly Report on Form 10-Q includes certain statements that may be deemed to be “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Statements contained in all parts of this document that are not historical facts are forward-looking statements that involve risks and uncertainties that are beyond the control of Dril-Quip, Inc. (the “Company” or “Dril-Quip”). You can identify the Company’s forward-looking statements by the words “anticipate,” “estimate,” “expect,” “may,” “project,” “believe” and similar expressions, or by the Company’s discussion of strategies or trends. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, no assurance can be given that these expectations will prove to be correct. These forward-looking statements include the following types of information and statements as they relate to the Company:

- the impact of the ongoing COVID-19 pandemic and the effects thereof;
- the impact of actions taken by OPEC and non-OPEC nations in response to their dispute over production levels and the effects thereof;
- future operating results and cash flow;
- scheduled, budgeted and other future capital expenditures;
- planned or estimated cost savings;
- working capital requirements;
- the need for and the availability of expected sources of liquidity;
- the introduction into the market of the Company’s future products;
- the Company’s ability to deliver its backlog in a timely fashion;
- the market for the Company’s existing and future products;
- the Company’s ability to develop new applications for its technologies;
- the exploration, development and production activities of the Company’s customers;
- compliance with present and future environmental regulations and costs associated with environmentally related penalties, capital expenditures, remedial actions and proceedings;
- effects of pending legal proceedings;
- changes in customers’ future product and service requirements that may not be cost effective or within the Company’s capabilities;
- future operations, financial results, business plans and cash needs; and
- the overall timing and level of transition of the global energy sector from fossil-based systems of energy production and consumption to more renewable energy sources.

These statements are based on assumptions and analysis in light of the Company’s experience and perception of historical trends, current conditions, expected future developments and other factors the Company believes were appropriate in the circumstances when the statements were made. Forward-looking statements by their nature involve substantial risks and uncertainties that could significantly impact expected results, and actual future results could differ materially from those described in such statements. While it is not possible to identify all factors, the Company continues to face many risks and uncertainties. Among the factors that could cause actual future results to differ materially are the risks and uncertainties discussed under “Item 1A. Risk Factors” in Part II of this report, “Item 1A. Risk Factors” in Part I of the Company’s Annual Report on Form 10-K for the year ended December 31, 2020.

Investors should note that Dril-Quip announces financial information in SEC filings, press releases and public conference calls. Dril-Quip may use the Investors section of its website ([www.dril-quip.com](http://www.dril-quip.com)) to communicate with investors. It is possible that the financial and other information posted there could be deemed to be material information. The information on Dril-Quip’s website is not part of this Form 10-Q.

The following is management’s discussion and analysis of certain significant factors that have affected aspects of the Company’s financial position, results of operations, comprehensive income (loss) and cash flows during the periods included in the accompanying unaudited condensed consolidated financial statements. This discussion should be read in conjunction with the Company’s unaudited condensed consolidated financial statements and notes thereto presented elsewhere herein as well as the discussion under Part II – Item 1A, “Risk Factors,” included herein and “Risk Factors,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2020.

## Overview

Dril-Quip, Inc., a Delaware corporation (the “Company” or “Dril-Quip”), designs, manufactures, sells and services highly engineered drilling and production equipment that is well suited primarily for use in deepwater, harsh environment and severe service applications. The Company’s principal products consist of subsea and surface wellheads, subsea and surface production trees, mudline hanger systems, specialty connectors and associated pipe, drilling and production riser systems, liner hangers, wellhead connectors, diverters and safety valves. Dril-Quip’s products are used by major integrated, large independent and foreign national oil and gas companies and drilling contractors throughout the world. Dril-Quip also provides technical advisory assistance on an as-requested basis during installation of its products, as well as rework and reconditioning services for customer-owned Dril-Quip products. In addition, Dril-Quip’s customers may rent or purchase running tools from the Company for use in the installation and retrieval of the Company’s products.

### *Business Environment*

During the second quarter of 2021, Dril-Quip entered into a collaboration and supply agreement in which the Company will serve as a supplier of subsea wellheads, tubular goods, liner hangers and other related tools and services to a peer provider of subsea equipment and services. The arrangement provides a framework for bundling several of our products and services into an integrated engineering, procurement and construction offering by our peer for the subsea production system market. We believe this collaboration and supply agreement will lead to opportunities to participate in more subsea projects and bids as a subcontractor for this industry peer that we previously may not have had access to independently.

The COVID-19 pandemic continues to have a global impact. Increased availability of the COVID-19 vaccine to the general population has resulted in a downward trend in the rate of new infections, hospitalizations and deaths. Although the downward trend is encouraging, emergence and spread of the new COVID-19 variants adds uncertainty to a potential economic recovery. The effect of the pandemic and the actions and changes in consumer behavior continue to impact our business and have significantly reduced global economic activity and demand for oil and gas. The pandemic has also affected our supply chain as a result of logistics bottlenecks and increased transportation costs. We continue to experience delayed recovery in 2021 as the market continues to be volatile and challenging. We actively review our global production plans with our supply chain and manufacturing groups have adopted contingency plans where possible to minimize the impact of these COVID-19 related disruptions. However, the potential emergence and spread of new COVID-19 variants adds uncertainty to future economic recovery.

Although oil prices have started to stabilize during 2021, the extent of the impact of the pandemic, including economic impacts that may persist following the widespread deployment of vaccines and the uncertainty in the sustainability of current oil prices on our operational and financial performance will depend on future developments. An extended period of economic disruption and uncertain conditions in the oil and gas industry could have a material adverse impact on our business, results of operations, access to sources of liquidity and overall financial condition.

As a larger proportion of the population gets vaccinated from increased availability of the COVID-19 vaccines, some jurisdictions in which the Company operates have eased safety protocols such as face mask and social distancing requirements. The Company will continue to implement safety measures as recommended by government health agencies until we have determined that the COVID-19 pandemic has been adequately contained. We continue to enact safety measures, including implementing social distancing protocols, requiring remote work arrangements where possible, staggering shifts, suspending travel, and extensively and frequently disinfecting our workspaces. Additionally, as COVID-19 vaccines became available in the first quarter of 2021, the Company organized administration of the vaccines on site to our employees and their families in the US. Furthermore, we have also utilized government employee support packages where available, in an effort to retain employees during this uncertain period.

The Company took advantage of the Payroll Tax Deferral provided by the CARES Act in 2020. The Payroll Tax Deferral allows the Company to defer the payment of the Company’s share of FICA taxes of 6.2%. As such, the Company was able to defer its share of FICA taxes for the period beginning March 27, 2020 and ending December 31, 2020. This resulted in approximately \$2.9 million in FICA cash tax payments being deferred to 2021 and 2022. The CARES Act provided for the five-year carryback of Net Operating Losses (“NOLs”) generated in the 2018, 2019 and 2020 taxable years. The Company filed returns to carryback its NOLs to generate a refund of \$31.0 million.

During 2020 and 2021, the Company also took advantage of job support schemes as they became available in Singapore, Australia, the U.K. and Denmark under which the governments introduced a plan to help businesses co-fund wages of workers to encourage employers to retain their workers. The Company has recorded an estimated benefit of \$1.0 million through September 30, 2021.

All our facilities currently remain operational with staggered shifts which has impacted production output. We expect the constraints and limits imposed on our operations to slow or diminish our research and development activities and qualification activities with our customers. We do not believe that remote work arrangements have adversely affected our ability to maintain financial reporting systems, internal controls over financial reporting and disclosure controls and procedures. The Company has taken steps and adjusted its workforce to be in line with the current situation as we continue to monitor ongoing market conditions. The extent to which our future results are affected by these externalities will depend on various factors and circumstances beyond our control, such as the duration and scope of the pandemic, additional actions by businesses and governments in response to the pandemic, the speed and effectiveness of containing the virus and developments in the global oil markets. We believe the COVID-19 pandemic will continue to negatively impact oilfield activity for the majority of 2021 and possibly linger into 2022. Similarly, we expect that the uncertainty in the sustainability of current oil prices will continue to have a negative impact on oil and gas activities. In addition to this, COVID-19 and the associated depressed global economic conditions could also aggravate the risk factors identified in our Annual Report on Form 10-K for the fiscal year ended December 31, 2020, including leading to further material impairment charges.

#### *Oil and Gas Prices*

The market for drilling and production equipment and services and the Company's business are substantially dependent on the condition of the oil and gas industry and, in particular, the willingness of oil and gas companies to make capital expenditures on exploration, drilling and production operations. Oil and gas prices and the level of drilling and production activity have historically been characterized by significant volatility.

According to the Energy Information Administration (EIA) of the U.S. Department of Energy, Brent Crude oil prices per barrel are listed below for the periods covered by this report:

| Brent Crude Oil Price per Barrel | Three months ended |          | Nine months ended |         |
|----------------------------------|--------------------|----------|-------------------|---------|
|                                  | September 30,      |          | September 30,     |         |
|                                  | 2021               | 2020     | 2021              | 2020    |
| Low                              | \$ 65.51           | \$ 38.53 | \$ 50.37          | \$ 9.12 |
| High                             | 78.85              | 46.01    | 78.85             | 70.25   |
| Average                          | 73.51              | 42.91    | 67.89             | 41.15   |
| Closing                          | 77.81              | 40.30    | 77.81             | 40.30   |

According to the October 2021 release of the Short-Term Energy Outlook published by the EIA, Brent Crude oil prices are projected to average approximately \$71 per barrel in 2021 and \$72 per barrel in 2022, compared with an average of \$41.69 per barrel in 2020. In its October 2021 Oil Market Report, the International Energy Agency projected global oil demand to grow by 5.5 million barrels per day in 2021 and 3.3 million barrels per day in 2022, after contracting by 8.7 million barrels per day in 2020.

Although crude oil prices have started to recover in 2021, we have yet to see an increase in activity from our customers as any recovery in the subsea market generally lags relative to the overall recovery in crude oil prices. If the Company experiences significant contract terminations, suspensions or scope adjustments to its contracts, then its financial condition, results of operations and cash flows may be adversely impacted.

#### *Offshore Rig Count*

Detailed below is the average contracted offshore rig count (rigs currently drilling as well as rigs committed, but not yet drilling) for the Company's geographic regions for the nine months ended September 30, 2021 and 2020. The rig count data includes floating rigs (semi-submersibles and drillships) and jack-up rigs. The Company has included only these types of rigs as they are the primary assets used to deploy the Company's products.

|                    | Nine months ended September 30, |              |               |              |
|--------------------|---------------------------------|--------------|---------------|--------------|
|                    | 2021                            |              | 2020          |              |
|                    | Floating Rigs                   | Jack-up Rigs | Floating Rigs | Jack-up Rigs |
| Western Hemisphere | 56                              | 40           | 56            | 46           |
| Eastern Hemisphere | 45                              | 58           | 50            | 63           |
| Asia-Pacific       | 30                              | 252          | 36            | 261          |
| Total              | 131                             | 350          | 142           | 370          |

Source: IHS—Petrodata RigBase – September 30, 2021 and 2020

According to IHS-Petrodata RigBase, as of September 30, 2021, there were 480 contracted rigs for the Company’s geographic regions (133 floating rigs and 347 jack-up rigs), largely unchanged from the rig count of 479 rigs (132 floating rigs and 347 jack-up rigs) as of September 30, 2020.

#### Regulation

The demand for the Company’s products and services is also affected by laws and regulations relating to the oil and gas industry in general, including those specifically directed to offshore operations. The adoption of new laws and regulations, or changes to existing laws or regulations that curtail exploration and development drilling for oil and gas for economic or other policy reasons, could adversely affect the Company’s operations by limiting demand for its products.

In March 2018, the President of the United States issued a proclamation imposing a 25 percent global tariff on imports of certain steel products, effective March 23, 2018. The President subsequently proposed an additional 25 percent tariff on approximately \$50 billion worth of imports from China, and the government of China responded with a proposal of an additional 25 percent tariff on U.S. goods with a value of \$50 billion. The initial U.S. tariffs were implemented on July 6, 2018, covering \$34 billion worth of Chinese goods, with another \$16 billion of goods facing tariffs beginning on August 23, 2018.

In September 2018, the President directed the U.S. Trade Representative (USTR) to place additional tariffs on approximately \$200 billion worth of additional imports from China. These tariffs, which took effect on September 24, 2018, were initially set at a level of 10 percent until the end of the year, at which point the tariffs were to rise to 25 percent. However, on December 19, 2018, USTR postponed the date on which the rate of the additional duties would increase to 25 percent until March 2, 2019. On May 9, 2019, USTR announced that the United States increased the level of tariffs from 10 percent to 25 percent on approximately \$200 billion worth of Chinese imports. The President also ordered USTR to begin the process of raising tariffs on essentially all remaining imports from China, which are valued at approximately \$300 billion. On August 13, 2019 and August 23, 2019, USTR announced the imposition of an additional tariff of 15 percent on approximately \$300 billion worth of Chinese imports, effective September 1, 2019 (or December 15, 2019 for certain articles). Following the conclusion of a phase one trade deal with China, USTR suspended the implementation of the 15 percent additional duty on approximately \$160 billion worth of Chinese imports and reduced the applicable duty from 15 percent to 7.5 percent for \$120 billion worth of Chinese imports. Negotiations for a phase two trade deal with China had begun prior to the outbreak of the global COVID-19 pandemic and if continued could lead to additional changes to the tariff rates described above. However, President Biden has indicated that these tariffs will likely remain in place while the new administration assesses the United States’ current posture, including a review of the phase one trade deal with China.

In November 2018, the United States, Mexico and Canada signed the United States-Mexico-Canada Agreement (USMCA), the successor agreement to the North American Free Trade Agreement. The three countries have all ratified the new agreement, and on July 1, 2020, the USMCA became effective.

The imposition of any additional tariffs or initiation of trade restrictions by or against the United States could cause our cost of raw materials to increase or affect the markets for our products. However, given the uncertainty regarding the scope and duration of these trade actions by the United States and other countries, their ultimate impact on our business and operations remains uncertain.

On June 23, 2016 the United Kingdom (U.K.) held a referendum in which a majority of British voters voted to exit the E.U., commonly known as “Brexit”, with the U.K. officially withdrawing from the E.U. on January 31, 2020. A transition period (during which the trading relationship between the E.U. and the U.K. remained substantially the same as prior to Brexit) followed, and this transition period expired on December 31, 2020. Shortly prior to expiration of the transition period, in December 2020, the U.K. and the E.U. reached an accord on a trade and cooperation agreement (TCA). Brexit and the terms of the TCA brought to an end the U.K.’s automatic access to the E.U. single market, resulting in the U.K. no longer benefitting from the free movement of goods and services between the E.U. and the U.K. The rights of people to freely move between the E.U. and the U.K. have also been restricted. The TCA entered into force on January 1, 2021 and, following formal ratification by the E.U. on April 28, 2021, entered fully into force on May 1, 2021. For more information on the risks associated with Brexit and the TCA, see “Our international operations require us to comply with a number of U.S. and foreign regulations governing the international trade of goods, services and technology, which expose us to compliance risks” under “Item 1A. Risk Factors” in Part II of this report and “Item 1A. Risk Factors” in Part I of the Company’s Annual Report on Form 10-K for the year ended December 31, 2020.

The U.K.’s Financial Conduct Authority (FCA), which regulates LIBOR, intends to phase out LIBOR as a benchmark in new contracts by the end of 2021. The FCA has announced that 30 LIBOR settings (all non-US dollar tenors plus one-week and two-month US dollar LIBOR) will either cease or become non-representative after December 31, 2021. The remaining five US dollar LIBOR settings (overnight, one-month, three-month, six-month and 12-month US dollar LIBOR) will continue to be published on a representative basis until June 30, 2023. At the present time, the ABL Credit Facility has a term that does not extend beyond 2023, and borrowings under the ABL Credit Facility (as defined herein) bear interest at the Company’s option at either (i) the CB Floating Rate (as defined therein), calculated as the rate of interest publicly announced by JPMorgan Chase Bank, N.A., as its “prime rate,” subject to each increase or decrease in such prime rate effective as of the date such change occurs, with such CB Floating Rate not being less than Adjusted One Month LIBOR (as defined therein) or (ii) the Adjusted LIBOR (as defined therein), plus, in each case, an applicable margin. We have not yet pursued any technical amendment or other contractual alternative to address this matter. We are currently evaluating the potential impact of the eventual replacement of the LIBOR interest rate.

The Company believes that its backlog should help mitigate the impact of negative market conditions; however, slow recovery in commodity prices or an extended downturn in the global economy or future restrictions on, or declines in, oil and gas exploration and production could have a negative impact on the Company and its backlog. The Company’s product backlog at September 30, 2021 was approximately \$179.0 million, compared to approximately \$191.2 million at June 30, 2021, \$196.7 million at March 30, 2021, and \$195.7 million at December 31, 2020.

The following table represents the change in backlog for the three months ended September 30, 2021, June 30, 2021, March 31, 2021 and December 31, 2020:

|                                   | <b>Three months ended</b>     |                          |                           |                              |
|-----------------------------------|-------------------------------|--------------------------|---------------------------|------------------------------|
|                                   | <b>September 30,<br/>2021</b> | <b>June 30,<br/>2021</b> | <b>March 30,<br/>2021</b> | <b>December 31,<br/>2020</b> |
|                                   | (In thousands)                |                          |                           |                              |
| Beginning Backlog                 | \$ 191,190                    | \$ 196,661               | \$ 195,650                | \$ 221,566                   |
| Bookings:                         |                               |                          |                           |                              |
| Product (1)                       | 45,501                        | 52,788                   | 58,639                    | 37,259                       |
| Service                           | 19,560                        | 17,536                   | 17,667                    | 18,235                       |
| Leasing                           | 9,815                         | 7,401                    | 7,989                     | 7,307                        |
| Cancellation/Revision adjustments | (3,783)                       | (3,427)                  | (1,048)                   | (2,014)                      |
| Translation adjustments           | (274)                         | 1,028                    | (997)                     | 531                          |
| Total Bookings                    | <u>70,819</u>                 | <u>75,326</u>            | <u>82,250</u>             | <u>61,318</u>                |
| Revenues:                         |                               |                          |                           |                              |
| Product                           | 53,622                        | 55,860                   | 55,583                    | 61,692                       |
| Service                           | 19,560                        | 17,536                   | 17,667                    | 18,235                       |
| Leasing                           | 9,815                         | 7,401                    | 7,989                     | 7,307                        |
| Total Revenue                     | <u>82,997</u>                 | <u>80,797</u>            | <u>81,239</u>             | <u>87,234</u>                |
| Ending Backlog                    | <u>\$ 179,012</u>             | <u>\$ 191,190</u>        | <u>\$ 196,661</u>         | <u>\$ 195,650</u>            |

- (1) The backlog data shown above includes all bookings as of September 30, 2021, including contract awards and signed purchase orders for which the contracts would not be considered enforceable or qualify for the practical expedient under ASC 606. As a result, this table will not agree to the disclosed performance obligations of \$39.5 million as of September 30, 2021 within “Revenue Recognition”, Note 4 to the Notes to Condensed Consolidated Financial Statements.

### *Employees*

As a result of worldwide reductions in workforce and natural attrition, the total number of employees as of September 30, 2021 were reduced to 1,347, of which 671 were located in the United States. The total number of the Company's employees as of December 31, 2020 were 1,424, of which 729 were located in the United States. As of September 30, 2020, the total number of the Company's employees were 1,444, of which 748 were located in the United States.

*Revenues.* Dril-Quip's revenues are generated from three sources: products, services and leasing. Product revenues are derived from the sale of drilling and production equipment. Service revenues are earned when the Company provides technical advisory assistance and rework and reconditioning services. Leasing revenues are derived from rental tools used during installation and retrieval of the Company's products. For the three months ended September 30, 2021 and 2020, the Company derived 64.6% and 72.8%, respectively, of its revenues from the sale of its products, 23.6% and 19.5%, respectively, of its revenue from services, and 11.8% and 7.7%, respectively, of its revenues from leasing. For the nine months ended September 30, 2021 and 2020, the Company derived 67.4% and 71.0%, respectively, of its revenues from the sale of its products, 22.3% and 20.6%, respectively, of its revenue from services, and 10.3% and 8.4%, respectively, of its revenues from leasing. Service and leasing revenues generally correlate to revenues from product sales because increased product sales typically generate increased demand for technical advisory assistance services and rental of running tools during installation. The Company has substantial international operations, with approximately 64.5% and 66.7% of its revenues derived from foreign sales for the nine months ended September 30, 2021 and 2020, respectively. The majority of the Company's domestic revenue relates to operations in the U.S. Gulf of Mexico. Domestic revenue approximated 35.5% and 33.3% of the Company's total revenues for the nine months ended September 30, 2021 and 2020, respectively.

Product contracts are generally negotiated and sold separately from service contracts. In addition, service contracts are not typically included in the product contracts or related sales orders and are not offered to the customer as a condition of the sale of the Company's products. The demand for products and services is generally based on worldwide economic conditions in the oil and gas industry and is not based on a specific relationship between the two types of contracts. Substantially all of the Company's sales are made on a purchase order basis. Purchase orders are subject to change and/or termination at the option of the customer. In case of a change or termination, the customer is required to pay the Company for work performed and other costs necessarily incurred due to the change or termination.

Generally, the Company attempts to raise its prices as its costs increase. However, the actual pricing of the Company's products and services is impacted by a number of factors, including global oil prices, competitive pricing pressure, the level of utilized capacity in the oil service sector, preservation of market share, the introduction of new products and overall market conditions.

The Company accounts for more complex, customer specific projects that have relatively longer manufacturing time frames on an over-time basis. For the three months ended September 30, 2021, there were 29 projects representing approximately 24.9% of the Company's total revenues and approximately 38.6% of its product revenues that were accounted for using over-time accounting, compared to 50 projects for the three months ended September 30, 2020, which represented approximately 36.9% of the Company's total revenues and approximately 50.7% of its product revenues. For the nine months ended September 30, 2021, there were 45 projects representing approximately 21.1% of the Company's total revenues and approximately 31.3% of its product revenues that were accounted for using over-time accounting, compared to 55 projects for the nine months ended September 30, 2020, which represented approximately 35.3% of the Company's total revenues and approximately 49.7% of its product revenues. These percentages may fluctuate in the future. Revenues accounted for in this manner are generally recognized based upon a calculation of the percentage complete, which is used to determine the revenue earned and the appropriate portion of total estimated cost of sales to be recognized. Accordingly, price and cost estimates are reviewed periodically as the work progresses, and adjustments proportionate to the percentage complete are reflected in the period when such estimates are revised. Losses, if any, are recorded in full in the period they become known. Amounts received from customers in excess of revenues recognized are classified as a current liability.

*Cost of Sales.* The principal elements of cost of sales are labor, raw materials, manufacturing overhead, and application engineering expenses related to customized products. Cost of sales as a percentage of revenues is influenced by the product mix sold in any particular period, costs from projects accounted for under the over-time method, over/under manufacturing overhead absorption, pricing and market conditions. The Company's costs related to its foreign operations do not significantly differ from its domestic costs.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses include the costs associated with sales and marketing, general corporate overhead, business development expenses, compensation expense, stock-based compensation expense, legal expenses and other related administrative functions.

*Engineering and Product Development Expenses.* Engineering and product development expenses consist of new product development and testing.

*Impairments.* We evaluate our property and equipment for impairment whenever changes in circumstances indicate that the carrying amount of an asset may not be recoverable, and we could incur additional impairment charges related to the carrying value of our long-lived assets. There were no impairment charges recorded for the three months ended September 30, 2021.

*Restructuring and Other Charges.* Restructuring and other charges consist of costs associated with our global strategic plan that was initiated in 2018 to better align our operations with market conditions. This plan continued in 2020 as a result of the COVID-19 pandemic and the developments in global oil markets. During 2021, we continued to incur restructuring charges under the global strategic plan as we exited from certain underperforming countries and markets and shifted from manufacturing in-house to a vendor outsourcing model. The Company concluded its 2018 global strategic plan and did not incur any additional costs during the three months ended September 30, 2021.

*(Gain) Loss on Sale of Assets.* Gain or loss on sale of assets consists of sales of certain property, plant and equipment.

*Foreign Currency Transaction (Gains) and Losses.* Foreign currency transaction (gains) and losses result from a change in exchange rates between the functional currency and the currency in which a foreign currency transaction is denominated.

*Income Tax Provision (Benefit).* The Company's effective income tax rate fluctuates from the U.S. statutory tax rate based on, among other factors, changes in pretax income in jurisdictions with varying statutory tax rates, impact of valuation allowances, changes in tax legislation, and other permanent differences related to the recognition of income and expense between U.S. GAAP and applicable tax rules.

## Results of Operations

The following table sets forth, for the periods indicated, certain condensed consolidated statements of income (loss) data expressed as a percentage of revenues:

|   | Three months ended |        | Nine months ended |        |
|---|--------------------|--------|-------------------|--------|
|   | September 30,      |        | September 30,     |        |
|   | 2021               | 2020   | 2021              | 2020   |
| Revenues:                                       |                    |        |                   |        |
| Products  | 64.6%              | 72.8%  | 67.4%             | 71.0%  |
| Services  | 23.6               | 19.5   | 22.3              | 20.6   |
| Leasing   | 11.8               | 7.7    | 10.3              | 8.4    |
| Total revenues                                  | 100.0              | 100.0  | 100.0             | 100.0  |
| Cost of sales:                                  |                    |        |                   |        |
| Products  | 58.0               | 55.4   | 54.4              | 55.4   |
| Services  | 8.5                | 10.0   | 10.1              | 10.1   |
| Leasing   | 9.3                | 8.3    | 9.5               | 8.5    |
| Total cost of sales                             | 75.8               | 73.7   | 74.0              | 74.0   |
| Selling, general and administrative             | 30.4               | 22.8   | 34.5              | 24.8   |
| Engineering and product development             | 4.2                | 4.4    | 4.6               | 5.4    |
| Impairments                                     | -                  | -      | -                 | 2.8    |
| Restructuring and other charges                 | -                  | 0.7    | 10.6              | 12.6   |
| (Gain) loss on sale of assets                   | -                  | -      | (1.6)             | (0.2)  |
| Foreign currency transaction (gains) and losses | (2.0)              | 0.8    | (0.3)             | (0.6)  |
| Operating loss                                  | (8.4)              | (2.4)  | (21.8)            | (18.8) |
| Interest income                                 | 0.2                | 0.2    | 0.1               | 0.7    |
| Interest expense                                | (0.1)              | (0.2)  | (0.2)             | (0.2)  |
| Loss before income taxes                        | (8.3)              | (2.4)  | (21.9)            | (18.3) |
| Income tax provision (benefit)                  | 5.2                | (17.9) | 4.5               | (11.1) |
| Net income (loss)                               | (13.5)%            | 15.5%  | (26.4)%           | (7.2)% |

The following table sets forth, for the periods indicated, a breakdown of our products and service revenues:

|                        | Three months ended |         | Nine months ended |          |
|------------------------|--------------------|---------|-------------------|----------|
|                        | September 30,      |         | September 30,     |          |
|                        | 2021               | 2020    | 2021              | 2020     |
|                        | (In millions)      |         |                   |          |
| Revenues:              |                    |         |                   |          |
| Products:              |                    |         |                   |          |
| Subsea equipment       | \$ 37.2            | \$ 54.6 | \$ 115.3          | \$ 154.0 |
| Surface equipment      | 4.1                | 4.5     | 10.0              | 12.2     |
| Downhole tools         | 11.6               | 5.7     | 33.3              | 22.8     |
| Offshore rig equipment | 0.7                | 1.6     | 6.5               | 8.1      |
| Total products         | 53.6               | 66.4    | 165.1             | 197.1    |
| Services               | 19.6               | 17.8    | 54.7              | 57.3     |
| Leasing                | 9.8                | 7.1     | 25.2              | 23.3     |
| Total revenues         | \$ 83.0            | \$ 91.3 | \$ 245.0          | \$ 277.7 |

*Three Months Ended September 30, 2021 Compared to Three Months Ended September 30, 2020*

**Revenues.** Revenues decreased by \$8.3 million, or approximately 9.1%, to \$83.0 million for the three months ended September 30, 2021 from \$91.3 million for the three months ended September 30, 2020. Product revenues decreased by approximately \$12.8 million for the three months ended September 30, 2021 as compared to the same period in 2020 as a result of \$17.4 million in decreased revenues in subsea equipment, \$0.9 million in offshore rig equipment and \$0.4 million in surface equipment, partially offset by increased downhole tools revenue of \$5.9 million. Product revenues in the Asia-Pacific region and the Eastern Hemisphere decreased by \$11.2 million and \$3.1 million, respectively, partially offset by increased product revenues of \$1.5 million in the Western Hemisphere. Although oil prices have started to stabilize during 2021, there is generally a delay in recovery of drilling activity in the offshore market. As such, our revenues continue to be negatively impacted by reduced global demand and customer drilling schedule delays. These negative impacts were attributable to both the COVID-19 pandemic and developments in the global oil markets. In any given time period, the revenues recognized between the various product lines and geographic areas will vary depending upon the timing of shipments to customers, completion status of the projects accounted for under the over-time accounting method, market conditions and customer demand.

Service revenues increased by approximately \$1.8 million resulting mainly from increase in service revenues in the Western Hemisphere of \$1.9 million, in the Asia-Pacific region of \$1.1 million, partially offset by decrease in service revenues of \$1.2 million in the Eastern Hemisphere. Increase in service revenues in the Western Hemisphere and the Asia-Pacific region is mainly due to customer specific increases in technical advisory services and maintenance requests tied to drilling schedules. Lower service revenues in the Eastern Hemisphere resulted primarily from developments in the global oil markets. Global travel restrictions resulting from the COVID-19 pandemic also impacted service revenue, especially in the Eastern Hemisphere.

Leasing revenues increased by approximately \$2.7 million resulting mainly from increased leasing revenues in the Asia-Pacific region of \$1.9 million, in the Western Hemisphere of \$1.2 million, partially offset by a decrease in leasing revenues of \$0.4 million in the Eastern Hemisphere. The majority of the increases in the Asia-Pacific region and the Western Hemisphere are related to increased subsea rental tool utilization due to timing of customer drilling activity. The decrease in the Eastern Hemisphere is related to decreased subsea rental tool utilization due to timing of customer drilling activity and the COVID-19 related restrictions.

**Cost of Sales.** Cost of sales decreased by \$4.4 million, or approximately 6.5%, to \$62.8 million for the three months ended September 30, 2021 from \$67.2 million for the same period in 2020. The decrease in costs of sales were mainly in line with the decrease in revenue for the three months ended September 30, 2021. Cost of sales as a percentage of revenue increased to 75.8% from 73.7% for the three months ended September 30, 2021 and 2020, respectively, primarily as a result of increases in manufacturing and freight costs.

**Selling, General and Administrative Expenses.** For the three months ended September 30, 2021, selling, general and administrative expenses increased by \$4.4 million, or 21.2% to \$25.3 million from \$20.8 million for the same period in 2020. This increase was attributable mainly to higher legal expenses in the current period related to costs incurred in connection with the FMC Technologies, Inc. lawsuit, reinstatement of employee short-term incentive plan for the current year, consulting fees associated with our ongoing global strategic plan and administrative costs associated with the importation tax settlement under the Brazilian tax amnesty program.

**Engineering and Product Development Expenses.** For the three months ended September 30, 2021, engineering and product development expenses decreased by approximately \$0.5 million, or 11.9%, to \$3.5 million from \$4.0 million for the same period in 2020. This decrease was attributable mainly to lower spend on research and development activities as we completed certain strategic projects.



*Restructuring and Other Charges.* For the three months ended September 30, 2021, the Company did not incur any additional costs as we concluded the 2018 global strategic plan. We recorded restructuring and other charges of \$0.6 million primarily related to consulting fees for the three months ended September 30, 2020.

*(Gain) Loss on Sale of Assets.* For the three months ended September 30, 2021, and 2020, the gain or loss on sale of assets was deemed immaterial.

*Foreign Currency Transaction (Gains) and Losses.* Foreign exchange gain for the three months ended September 30, 2021, was \$1.7 million as compared to a loss of \$0.7 million for the same period in 2020.

*Income Tax Provision (Benefit).* Income tax provision for the three months ended September 30, 2021 was \$4.3 million on a loss before taxes of \$6.8 million, resulting in an effective tax rate of (62.9)%. Income tax expense was different than the U.S federal statutory income tax rate of 21% primarily due to changes in pre-tax income or loss in foreign jurisdictions, nondeductible compensation and the change in valuation allowances in the United States and in various foreign countries. Income tax benefit for the three months ended September 30, 2020 was \$16.4 million on a loss before taxes of \$2.1 million, resulting in an effective income tax rate of approximately 797.5%. Income tax expense was different than the U.S federal statutory income tax rate of 21% primarily due to tax benefits of the CARES Act, changes in the valuation allowances in the United States and in various foreign countries. The change in the effective tax rate between the periods was primarily a result of discretely recognized benefits of the CARES Act in 2020, changes in valuation allowances, and a mix of earnings in jurisdictions with differing tax rates.

*Net Income (Loss).* Net loss was approximately \$11.1 million for the three months ended September 30, 2021 as compared to a net income of \$14.3 million for the same period in 2020 for the reasons set forth above.

#### *Nine Months Ended September 30, 2021 Compared to Nine Months Ended September 30, 2020*

*Revenues.* Revenues decreased by \$32.7 million, or approximately 11.8%, to \$245.0 million for the nine months ended September 30, 2021 from \$277.7 million for the nine months ended September 30, 2020. Product revenues decreased by approximately \$32.0 million for the nine months ended September 30, 2021 as compared to the same period in 2020 as a result of decreased revenues in subsea equipment of \$38.7 million, in surface equipment of \$2.2 million and in offshore rig equipment of \$1.6 million, partially offset by increased downhole tools revenue of \$10.5 million. Product revenues in the Eastern Hemisphere, the Asia-Pacific region and the Western Hemisphere decreased by \$20.2 million, \$10.2 million and \$1.6 million, respectively. Although oil prices have started to stabilize during 2021, there is generally a delay in recovery of drilling activity in the offshore market. As such, our revenues continue to be negatively impacted by reduced global demand and customer drilling schedule delays. These negative impacts were attributable to both the COVID-19 pandemic and developments in the global oil markets. In any given time period, the revenues recognized between the various product lines and geographic areas will vary depending upon the timing of shipments to customers, completion status of the projects accounted for under the over-time accounting method, market conditions and customer demand.

Service revenues decreased by approximately \$2.6 million resulting mainly from decreased service revenues in the Eastern Hemisphere of \$3.9 million and in the Western Hemisphere of \$1.3 million, partially offset by an increase in the Asia-Pacific region of \$2.6 million. Lower service revenues in the Eastern Hemisphere and Western Hemisphere resulted primarily from COVID-19 disruptions and developments in the global oil markets. Global travel restrictions also impacted service revenue, especially in the Eastern Hemisphere. Increase in service revenues in Asia-Pacific is mainly due to customer specific increases in technical advisory services and maintenance requests.

Leasing revenues increased by approximately \$1.9 million resulting mainly from increased leasing revenues in the Asia-Pacific region of \$2.4 million and in the Western Hemisphere of \$1.4 million, partially offset by decreased leasing revenues in the Eastern Hemisphere of \$1.9 million. Increase in leasing revenues in the Western Hemisphere and the Asia-Pacific region were due to customer specific increases in rental tool utilization. The majority of the decrease in the Eastern Hemisphere is related to decreased subsea rental tool utilization due to timing of customer drilling activity and COVID-19 related travel restrictions.

*Cost of Sales.* Cost of sales decreased by \$24.4 million, or approximately 11.9%, to \$181.2 million for the nine months ended September 30, 2021 from \$205.6 million for the same period in 2020. The decrease in cost of sales were mainly in line with the decrease in revenue for the nine months ended September 30, 2021. Cost of sales as a percentage of revenue was largely unchanged at 74.0% and excluding a one-time expense related to the termination of our forge facility lease agreement with AFGlobal, decreased to 73.0% from 74.0% for the nine months ended September 30, 2021 and 2020, respectively, as a result of savings from our business transformation activities.

*Selling, General and Administrative Expenses.* For the nine months ended September 30, 2021, selling, general and administrative expenses increased by \$15.6 million, or approximately 22.6% to \$84.4 million from \$68.8 million for the same period in 2020. This increase was attributable mainly to higher legal expenses in the current period related to costs incurred in connection with the FMC Technologies, Inc. lawsuit, reinstatement of employee short-term incentive plan for the current year, an importation tax settlement under a Brazilian tax amnesty program introduced in the first quarter of 2021 and consulting fees associated with our ongoing global strategic plan.

*Engineering and Product Development Expenses.* For the nine months ended September 30, 2021, engineering and product development expenses decreased by approximately \$3.6 million, or 24.3%, to \$11.3 million from \$14.9 million for the same period in 2020. This decrease was attributable mainly to lower spend on research and development activities as we completed certain strategic projects.

*Restructuring and Other Charges.* For the nine months ended September 30, 2021, the Company incurred additional costs under our existing 2018 global strategic plan to realign manufacturing facilities globally. These charges were primarily related to the restructuring of our downhole tools business where we exited certain underperforming countries and markets and shifted from manufacturing in-house to a vendor sourcing model which resulted in non-cash inventory write downs of \$19.3 million, severance charges of \$2.7 million and other charges of \$4.0 million, consisting of facilities-related market exit costs and consulting fees. The Company concluded its 2018 global strategic plan and did not incur any additional charges in the third quarter of 2021. As a result of unfavorable market conditions primarily due to the COVID-19 pandemic and developments in the global oil markets, we recorded inventory write-downs, severance charges, long-lived asset write-downs and other charges of \$34.9 million during the nine months ended September 30, 2020.

*Gain on Sale of Assets.* For the nine months ended September 30, 2021, gain on sale of assets was approximately \$3.9 million, primarily related to the sale of two of our buildings in Singapore. For the nine months ended September 30, 2020, gain on sale of assets was \$0.5 million, which consisted primarily of the sale of our TIW Oklahoma facility.

*Foreign Currency Transaction Gains.* Foreign exchange gain for the nine months ended September 30, 2021, was \$0.8 million as compared to a gain of \$1.7 million for the same period in 2020.

*Income Tax Provision (Benefit).* Income tax provision for the nine months ended September 30, 2021 was \$11.1 million on a loss before taxes of \$53.5 million, resulting in an effective tax rate of (20.7)%. Income tax expense was different than the U.S federal statutory income tax rate of 21% primarily due to changes in pre-tax income or loss in foreign jurisdictions, nondeductible compensation and the change in valuation allowances in the United States and in various foreign countries. Income tax benefit for the nine months ended September 30, 2020 was \$30.9 million on a loss before taxes of \$50.4 million, resulting in an effective income tax rate of approximately 61.3%. Income tax expense was different than the U.S federal statutory income tax rate of 21% primarily due to tax benefits of the CARES Act, changes in the valuation allowances in the United States and in various foreign countries. The change in the effective tax rate between the periods was primarily a result of discretely recognized benefits of the CARES Act in 2020, changes in valuation allowances and a mix of earnings in jurisdictions with differing tax rates.

*Net Loss.* Net loss was approximately \$64.6 million for the nine months ended September 30, 2021 as compared to a net loss of \$19.5 million for the same period in 2020 for the reasons set forth above.

## **Non-GAAP Financial Measures**

We have performed a detailed analysis of the non-GAAP measures that are relevant to our business and its operations and determined that the appropriate unit of measure to analyze our performance is Adjusted EBITDA (earnings before interest, taxes, depreciation and amortization, as well as other significant non-cash items and other adjustments for certain charges and credits). The Company believes that the exclusion of these charges and credits from these financial measures enables it to evaluate more effectively the Company's operations period over period and to identify operating trends that could otherwise be masked by excluded items. It is our determination that Adjusted EBITDA is a more relevant measure of how the Company reviews its ability to meet commitments and pursue capital projects.

### *Adjusted EBITDA*

We calculate Adjusted EBITDA as one of the indicators to evaluate and compare the results of our operations from period to period by removing the effect of our capital structure from our operating structure. This measurement is used in concert with net income and cash flows from operations, which measures actual cash generated in the period. In addition, we believe that Adjusted EBITDA is a supplemental measurement tool used by analysts and investors to help evaluate overall operating performance, ability to pursue and service possible debt opportunities and analyze possible future capital expenditures. Adjusted EBITDA does not represent funds available for our discretionary use and is not intended to represent or to be used as a substitute for net income, as measured under U.S. generally accepted accounting principles. The items excluded from Adjusted EBITDA, but included in the calculation of reported net income, are significant components of the condensed consolidated statements of income (loss) and must be considered in performing a comprehensive assessment of overall financial performance. Our calculation of Adjusted EBITDA may not be consistent with calculations of Adjusted EBITDA used by other companies.

The following table reconciles our reported net income to Adjusted EBITDA for each of the respective periods:

|   | Three months ended September 30, |           | Nine months ended September 30, |             |
|---|----------------------------------|-----------|---------------------------------|-------------|
|   | 2021                             | 2020      | 2021                            | 2020        |
|   | (In thousands)                   |           |                                 |             |
| Net income (loss)                               | \$ (11,143)                      | \$ 14,326 | \$ (64,568)                     | \$ (19,514) |
| Add:  |                                  |           |                                 |             |
| Interest (income) expense, net                  | (94)                             | (50)      | 292                             | (1,509)     |
| Income tax provision (benefit)                  | 4,301                            | (16,380)  | 11,094                          | (30,908)    |
| Depreciation and amortization expense           | 7,899                            | 7,908     | 22,658                          | 24,721      |
| Impairments                                     | -                                | -         | -                               | 7,719       |
| Restructuring and other charges <sup>(2)</sup>  | 1,400                            | 602       | 38,470                          | 34,902      |
| (Gain) loss on sale of assets                   | (13)                             | 14        | (3,886)                         | (538)       |
| Foreign currency transaction (gains) and losses | (1,663)                          | 746       | (764)                           | (1,679)     |
| Stock compensation expense                      | 3,276                            | 3,003     | 9,541                           | 9,461       |
| Brazilian amnesty settlement                    | -                                | -         | 1,787                           | -           |
| Adjusted EBITDA <sup>(1)</sup>                  | \$ 3,963                         | \$ 10,169 | \$ 14,624                       | \$ 22,655   |

<sup>(1)</sup> Adjusted EBITDA does not measure financial performance under GAAP and, accordingly, should not be considered as an alternative to net income as an indicator of operating performance.

<sup>(2)</sup> Restructuring and other charges include legal expenses related to the FMC Technologies, Inc. lawsuit. These legal expenses are included in "Selling, general and administrative" in our condensed consolidated statements of income (loss) for the three and nine months ended September 30, 2021 and 2020 (in thousands).

## Liquidity and Capital Resources

### Cash Flows

Cash flows provided by (used in) type of activity were as follows:

|  | Nine months ended September 30, |             |
|--|---------------------------------|-------------|
|  | 2021                            | 2020        |
|  | (In thousands)                  |             |
| Operating activities                               | \$ 33,738                       | \$ (4,302)  |
| Investing activities                               | (1,961)                         | (6,597)     |
| Financing activities                               | (1,245)                         | (25,176)    |
|  | 30,532                          | (36,075)    |
| Effect of exchange rate changes on cash activities | (1,315)                         | (3,700)     |
| Increase (decrease) in cash and cash equivalents   | \$ 29,217                       | \$ (39,775) |

Statements of cash flows for entities with international operations that are local currency functional exclude the effects of the changes in foreign currency exchange rates that occur during any given period, as these are non-cash changes. As a result, changes reflected in certain accounts on the condensed consolidated statements of cash flows may not reflect the changes in corresponding accounts on the condensed consolidated balance sheets.

The primary liquidity needs of the Company are (i) to fund capital expenditures to improve and expand facilities and manufacture additional running tools and (ii) to fund working capital. The Company's principal source of funds is cash flows from operations. As of September 30, 2021, the Company had approximately \$375.2 million of cash and cash equivalents on hand and an availability of \$31.1 million under the ABL Credit Facility.

Although there still remains uncertainty related to the impact of the COVID-19 pandemic on our future results, we continue to monitor our spend and reduce non-essential spending. Further, the Company adjusted the workforce to be in line with the current situation as we continue to monitor the ongoing market conditions.

We believe our business model, our current cash reserves and the recent downhole tools business restructuring and facility realignment will strengthen our balance sheet and leave us well-positioned to manage our business through this crisis as it continues to unfold. We continue to review potential scenarios in connection with the impact of COVID-19 on the global economy and the oil and gas industry. Based on our analysis, we believe our existing balances of cash and cash equivalents and our currently anticipated operating cash flows will be sufficient to meet our cash needs arising in the ordinary course of business for the next twelve months.

Net cash provided by operating activities for the nine months ended September 30, 2021 was \$33.7 million as compared to net cash used in operating activities of \$4.3 million for the nine months ended September 30, 2020. The \$38.0 million net change is primarily due to increased cash flow resulting from changes in operating assets and liabilities of \$107.5 million. This was partially offset by \$24.4 million of non-cash movements which included decreases in items such as impairments, restructuring and other charges, and an increase in net loss of \$45.1 million.

The change in operating assets and liabilities for the nine months ended September 30, 2021 resulted in a \$107.5 million increase in cash as compared to the change in operating assets and liabilities for the nine months ended September 30, 2020. The \$37.9 million decrease in prepaids and other assets was primarily due to receipt of tax receivables and the reimbursement of the security amounts deposited with the Brazilian courts related to the tax amnesty program. The decrease in inventory of \$31.8 million was mainly related to our continued focus on inventory management and consumption during the year. The decrease in unbilled receivables by \$30.8 million mainly due to progress and completion of some of our major projects that are accounted for on an over-time basis. The increase in accounts payable and accrued expenses of \$4.1 million was mainly related to the reinstatement of our short-term incentive plan in 2021. Trade receivables decreased by \$2.9 million primarily due to our continued focus on global cash collections by improving our invoicing cycle time and increasing collection efforts across all business units.

The change in investing cash flows for the nine months ended September 30, 2021 resulted in a \$2.0 million decrease in cash primarily due to capital expenditure spend by the Company, partially offset by the sale of two of our buildings in Singapore for \$5.9 million. Capital expenditures by the Company were \$7.9 million and \$10.2 million for the nine months ended September 30, 2021 and 2020, respectively. Capital expenditures for the nine months ended September 30, 2021 were \$3.7 million for machinery and equipment related to our global strategic program which includes consolidation of our manufacturing facilities from the Eastern Hemisphere to the Western Hemisphere, \$2.8 million for rental tools to support our current and recently developed products and \$1.4 million for other capital expenditures. Capital expenditures for the nine months ended September 30, 2020 were \$4.4 million for rental tools, \$3.5 million for machinery and equipment and \$2.3 million for other capital expenditures. We constantly review capital expenditure needs to ensure these are justified expenditures.

#### *Repurchase of Equity Securities*

On February 26, 2019, the Board of Directors authorized a share repurchase plan under which the Company can repurchase up to \$100 million of its common stock. The repurchase plan has no set expiration date and any repurchased shares are expected to be cancelled. The manner, timing and amount of any purchase will be determined by management based on an evaluation of market conditions, stock price, liquidity and other factors. The program does not obligate the Company to acquire any amount of common stock and may be modified or superseded at any time at the Company's discretion.

For the three and nine months ended September 30, 2021, the Company purchased 45,225 shares under the share repurchase plan at an average price of approximately \$25.02 per share totaling approximately \$1.1 million and has retired such shares.

For the nine months ended September 30, 2020, the Company purchased 808,389 shares under the share repurchase plan at an average price of approximately \$30.91 per share totaling approximately \$25.0 million and has retired such shares.

#### *Asset Backed Loan (ABL) Credit Facility*

As of September 30, 2021, the availability under the ABL Credit Facility was \$31.1 million, after taking into account the outstanding letters of credit of approximately \$7.2 million issued under the facility. For additional information on the ABL Credit Facility, see "Asset Backed Loan (ABL) Credit Facility", Note 9 to the Notes to Condensed Consolidated Financial Statements.

#### **Off-Balance Sheet Arrangements**

The Company currently has no derivative instruments and no off-balance sheet hedging or financing arrangements, contracts or operations.

#### **Other Matters**

From time to time, the Company enters into discussions or negotiations to acquire other businesses or enter into joint ventures. The timing, size or success of any such efforts and the associated potential capital commitments are unpredictable and dependent on market conditions and opportunities existing at the time. The Company may seek to fund all or part of any such efforts with proceeds from debt or equity issuances. Debt or equity financing may not, however, be available at that time due to a variety of circumstances, including, among others, the Company's credit ratings, industry conditions, general economic conditions and market conditions.

#### **Critical Accounting Policies**

Refer to our Annual Report on Form 10-K for the year ended December 31, 2020 for a discussion of our critical accounting policies. During the nine months ended September 30, 2021, there were no material changes in our judgments and assumptions associated with the development of our critical accounting policies.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

The Company is currently exposed to certain market risks related to interest rate changes on its short-term investments and fluctuations in foreign exchange rates. The Company does not engage in any material hedging transactions, forward contracts or currency trading which could mitigate the market risks inherent in such transactions. There have been no material changes in market risks for the Company since December 31, 2020.

**Foreign Exchange Rate Risk**

The Company has operations in various countries around the world and conducts business in a number of different currencies. Our significant foreign subsidiaries may also have monetary assets and liabilities not denominated in their functional currency. These monetary assets and liabilities are exposed to changes in currency exchange rates which may result in non-cash gains and losses primarily due to fluctuations between the U.S. dollar and each subsidiary's functional currency.

The Company experienced a foreign currency pre-tax gain of approximately \$1.7 million and \$0.8 million, respectively, during the three and nine months ended September 30, 2021. During the three and nine months ended September 30, 2020, the Company experienced a foreign currency pre-tax loss of approximately \$0.7 million and a pre-tax gain of approximately \$1.7 million, respectively.

The Company does not engage in any material hedging transactions, forward contracts or currency trading which could mitigate the effects and risks inherent in such transactions. Additionally, there is no assurance that the Company will be able to protect itself against currency fluctuations in the future.

**Item 4. Controls and Procedures**

In accordance with Exchange Act Rules 13a-15 and 15d-15, the Company carried out an evaluation, under the supervision and with the participation of management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2021 to provide reasonable assurance that information required to be disclosed in the Company's reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and such information is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding disclosure.

There has been no change in the Company's internal control over financial reporting that occurred during the three months ended September 30, 2021 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II—OTHER INFORMATION****Item 1. Legal Proceedings**

For a description of the Company's legal proceedings, see "Contingencies," Note 12 to the Notes to Condensed Consolidated Financial Statements.

**Item 1A. Risk Factors**

There have been no material changes from the risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2020 and updated in our Quarterly Report on Form 10-Q for the period ending June 30, 2021.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table summarizes the repurchase and cancellation of our common stock during the three and nine months ended September 30, 2021.

|                        | <b>Three months ended<br/>September 30, 2021</b>    |   |   |   |
|------------------------|---|---|---|---|
|                        | <b>Total<br/>Number of<br/>Shares<br/>Purchased</b> | <b>Average<br/>Price<br/>paid per<br/>Share</b> | <b>Total Number<br/>of Shares<br/>Purchased<br/>as Part of<br/>Publicly<br/>Announced<br/>Plans or<br/>Programs (1)</b> | <b>Maximum<br/>Dollar Value<br/>(in millions)<br/>of Shares that<br/>May Yet be<br/>Purchased<br/>Under the Plans<br/>or Programs</b> |
| July 1 - 31, 2021      | -   | \$ -  | -   | \$ 48.5   |
| August 1 - 31, 2021    | -   | -   | -   | 48.5  |
| September 1 - 30, 2021 | 45,225  | 25.02   | 45,225  | 47.3  |
|                        | <u>45,225</u>                                       | <u>\$ 25.02</u>                                 | <u>45,225</u>   | <u>\$ 47.3</u>  |

|                        | <b>Nine months ended<br/>September 30, 2021</b>     |   |   |   |
|------------------------|---|---|---|---|
|                        | <b>Total<br/>Number of<br/>Shares<br/>Purchased</b> | <b>Average<br/>Price<br/>paid per<br/>Share</b> | <b>Total Number<br/>of Shares<br/>Purchased<br/>as Part of<br/>Publicly<br/>Announced<br/>Plans or<br/>Programs (1)</b> | <b>Maximum<br/>Dollar Value<br/>(in millions)<br/>of Shares that<br/>May Yet be<br/>Purchased<br/>Under the Plans or<br/>Programs</b> |
| January 1 - 31, 2021   | -   | \$ -  | -   | \$ 48.5   |
| February 1 - 28, 2021  | -   | -   | -   | 48.5  |
| March 1 - 31, 2021     | -   | -   | -   | 48.5  |
| April 1 - 30, 2021     | -   | -   | -   | 48.5  |
| May 1 - 31, 2021       | -   | -   | -   | 48.5  |
| June 1 - 30, 2021      | -   | -   | -   | 48.5  |
| July 1 - 31, 2021      | -   | -   | -   | 48.5  |
| August 1 - 31, 2021    | -   | -   | -   | 48.5  |
| September 1 - 30, 2021 | 45,225  | 25.02   | 45,225  | 47.3  |
|                        | <u>45,225</u>                                       | <u>\$ 25.02</u>                                 | <u>45,225</u>   | <u>\$ 47.3</u>  |

**Item 6.**

(a) Exhibits

The following Exhibits are filed herewith:

| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| *3.1               | — <a href="#">Restated Certificate of Incorporation of the Company (incorporated herein by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2017).</a>                                     |
| *3.2               | — <a href="#">Amended and Restated Bylaws of the Company (incorporated herein by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K filed on May 20, 2014).</a>  |
| *4.1               | — <a href="#">Form of Certificate representing Common Stock (incorporated herein by reference to Exhibit 4.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2018, File No. 001-13439).</a>                      |
| *10.1              | — <a href="#">Separation and Release Agreement by and between the Company and Blake T. DeBerry dated September 1, 2021 (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on September 1, 2021).</a> |
| 31.1               | — <a href="#">Rule 13a-14(a)/15d-14(a) Certification of Blake T. DeBerry.</a>  |
| 31.2               | — <a href="#">Rule 13a-14(a)/15d-14(a) Certification of Raj Kumar.</a>   |
| 32.1               | — <a href="#">Section 1350 Certification of Blake T. DeBerry.</a>  |
| 32.2               | — <a href="#">Section 1350 Certification of Raj Kumar.</a>   |
| 101.INS            | — Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.   |
| 101.SCH            | — Inline XBRL Taxonomy Extension Schema Document.  |
| 101.CAL            | — Inline XBRL Taxonomy Extension Calculation Linkbase Document.  |
| 101.DEF            | — Inline XBRL Taxonomy Extension Definition Linkbase Document.   |
| 101.LAB            | — Inline XBRL Taxonomy Extension Label Linkbase Document.  |
| 101.PRE            | — Inline XBRL Taxonomy Extension Presentation Linkbase Document  |
| 104                | — Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101).  |

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\* Incorporated herein by reference as indicated.

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**DRIL-QUIP, INC.**

Date: October 28, 2021

BY: \_\_\_\_\_ /s/ Raj Kumar

**Raj Kumar,  
Vice President – Chief Financial Officer  
(Principal Financial Officer and  
Duly Authorized Signatory)**



## RULE 13a-14(a)/15d-14(a) CERTIFICATION

I, Blake T. DeBerry, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Dril-Quip, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 28, 2021

/s/ Blake T. DeBerry

Blake T. DeBerry

*Chief Executive Officer and Director (Principal Executive Officer)*

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## RULE 13a-14(a)/15d-14(a) CERTIFICATION

I, Raj Kumar, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Dril-Quip, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 28, 2021

/s/ Raj Kumar

Raj Kumar

*Vice President – Chief Financial Officer  
(Principal Financial Officer and Duly Authorized Signatory)*

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906  
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Dril-Quip, Inc. (the “Company”) on Form 10-Q for the period ended September 30, 2021 (the “Report”), as filed with the Securities and Exchange Commission on the date hereof, I, Blake T. DeBerry, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: October 28, 2021

/s/ Blake T. DeBerry

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Blake T. DeBerry

*Chief Executive Officer and Director (Principal Executive Officer)*

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906  
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Dril-Quip, Inc. (the "Company") on Form 10-Q for the period ended September 30, 2021 (the "Report"), as filed with the Securities and Exchange Commission on the date hereof, I, Raj Kumar, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: October 28, 2021

/s/ Raj Kumar

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Raj Kumar

*Vice President - Chief Financial Officer  
(Principal Financial Officer and Duly Authorized Signatory)*

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