



Baker Hughes (BKR)

Updated October 19th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	\$25	5 Year CAGR Estimate:	10.8%	Market Cap:	\$25.2 B
Fair Value Price:	\$17	5 Year Growth Estimate:	18.0%	Ex-Dividend Date:	10/31/22 ¹
% Fair Value:	150%	5 Year Valuation Multiple Estimate:	-7.8%	Dividend Payment Date:	11/11/22 ¹
Dividend Yield:	2.9%	5 Year Price Target	\$38	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	F	Rating:	Hold

Overview & Current Events

Baker Hughes has operations in more than 120 countries, a market capitalization of \$25.2 billion and provides integrated oilfield products, services and digital solutions. On October 17th, 2019, Baker Hughes, a GE company with ticker BHGE, changed its name to Baker Hughes, which has BKR as a ticker. The change of the name followed the reduction of the stake of General Electric in the company below 50% (to 36.8%). On July 29th, 2020, General Electric announced that it will sell its whole stake in Baker Hughes over the next three years in order to reduce its debt load. In 2021, the oilfield services segment of Baker Hughes generated 47% of its total revenues while the segments of oilfield equipment, turbomachinery & process solutions, and digital solutions generated 12%, 31%, and 10% of total revenues, respectively. In mid-October, Baker Hughes reported (10/19/22) financial results for the third quarter of fiscal 2022. Its revenue of \$5.4 billion grew 6% sequentially and its orders of \$6.1 billion edged up 3%. Adjusted earnings-per-share grew from \$0.11 to \$0.26. However, given the exceptionally high prices of oil and gas this year amid the war in Ukraine, the results of Baker Hughes are disappointing, just like in the previous quarter. Baker Hughes blamed once again supply chain disruptions and high inflation. Due to the slower-than-expected recovery of Baker Hughes from the pandemic, we have lowered our earnings-per-share forecast for 2022 from \$1.20 to \$1.00.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$2.97	\$2.52	\$3.92	-\$4.49	-\$6.31	-\$0.17	\$0.65	\$0.85	\$0.03	\$0.63	\$1.00	\$2.29
DPS	\$0.60	\$0.60	\$0.64	\$0.68	\$0.68	\$0.69	\$0.72	\$0.72	\$0.72	\$0.72	\$0.72	\$0.72
Shares²	441.0	438.0	434.0	437.0	424.0	422.0	463.0	653.0	713.0	906.0	1010.0	1000.0

The recovery of Baker Hughes was lackluster before the pandemic. Major technological advances have made it possible to produce more oil with fewer operating rigs. In essence, providers of oilfield services and equipment have been victims of their own success. This helps explain the weak recovery of the results of Baker Hughes amid all-time high global and U.S. oil production in 2018-2019. However, the energy market is recovering strongly from the pandemic right now. The return of the U.S. and global oil production to their long-term growth trajectories will provide a tailwind to the business results of Baker Hughes in the upcoming years, particularly given that oil producers will have to make up for their depressed investment in new projects in the last three years. Moreover, a major growth driver could be the increasing demand from LNG projects. Overall, we expect Baker Hughes to grow its earnings-per-share at an 18.0% average annual rate until 2027. On the other hand, we note the extremely volatile and unreliable performance record of the company.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	15.0	19.3	16.3	---	---	---	47.4	28.1	---	36.8	25.0	16.7
Avg. Yld.	1.3%	1.2%	1.0%	1.2%	1.4%	2.0%	2.3%	3.0%	4.3%	3.1%	2.9%	1.9%

¹ Estimated date.

² In millions.

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Excluding the years in which depressed earnings resulted in abnormally high price-to-earnings ratios, Baker Hughes has traded at an average price-to-earnings ratio of 16.7 during the last decade. The stock is currently trading at 25.0 times its expected earnings this year. As its business recovers over the next five years, Baker Hughes could revert to its average valuation level during this period. If this occurs, the stock will incur a -7.8% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

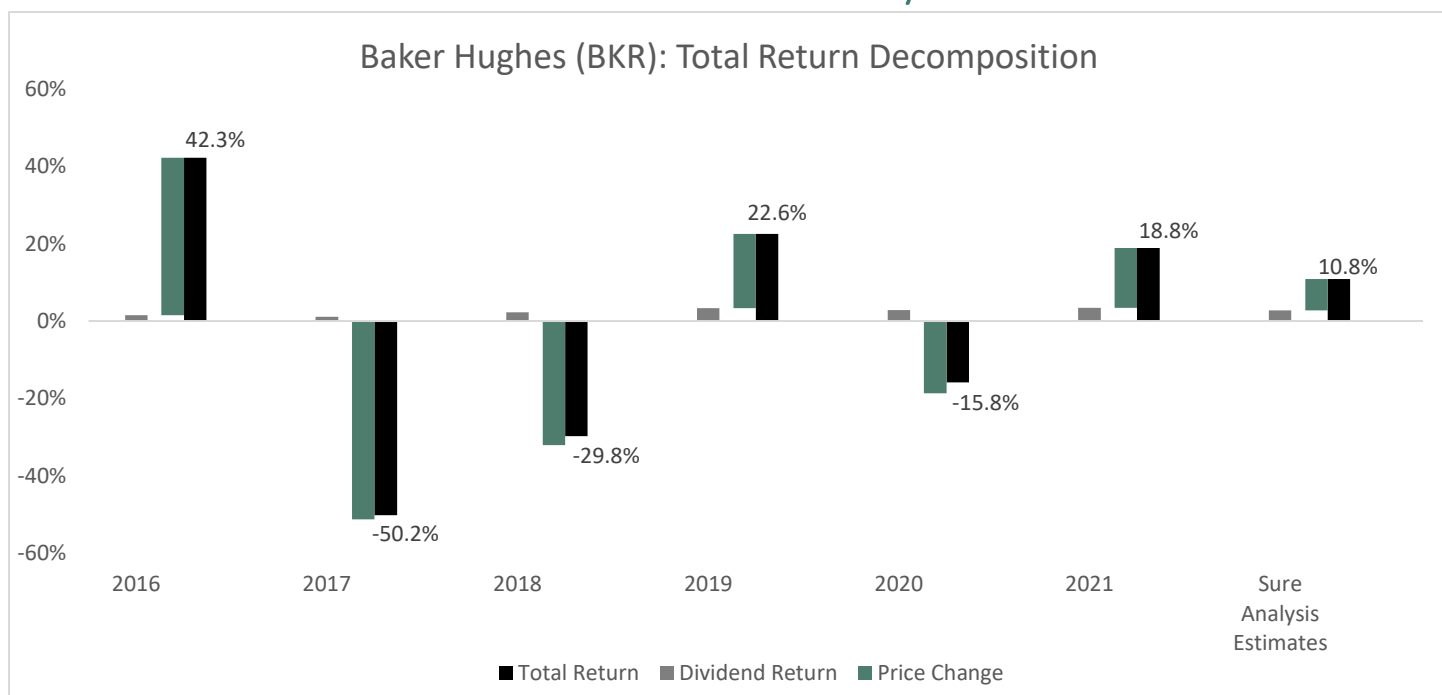
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	20.2%	23.8%	16.3%	---	---	---	111%	84.7%	---	114%	72.0%	31.5%

While Baker Hughes has great expertise in oilfield services, it lacks a durable competitive advantage. Just like its peers, Baker Hughes is highly cyclical and vulnerable to recessions and downturns in the oil market. The company saw its earnings-per-share plunge -74% in the Great Recession and incurred hefty losses for three consecutive years in the recent downturn of the energy sector (2015-2017). It was also severely hurt by the pandemic, though the worse seems to be behind the company in reference to this crisis. Moreover, the stock tends to underperform during broad market corrections or bear markets. Investors should be aware of these risks.

Final Thoughts & Recommendation

The energy market is recovering strongly from the pandemic and oil producers have begun to make up for their depressed investment in new projects in the last three years. Moreover, the stock of Baker Hughes has shed -32% off its peak in June, and thus it has become more attractive. We expect Baker Hughes to offer a 10.8% average annual return over the next five years thanks to 18.0% earnings growth and its 2.9% dividend, partly offset by a -7.8% valuation headwind. We need a higher expected return to rate the stock as a buy due to its poor business performance under the prevailing extremely favorable conditions. In addition, while the next downturn of the energy market may not show up anytime soon, investors should be aware of the high cyclical nature of the stock and its high sensitivity to the downturns of the energy market. Baker Hughes receives a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	---	---	---	16688	13269	17259	22877	23,838	20,705	20,502
Gross Profit	---	---	---	4495	3146	3213	3986	4,432	3,199	4,049
Gross Margin	---	---	---	26.9%	23.7%	18.6%	17.4%	18.6%	15.5%	19.7%
SG&A Exp.	---	---	---	2115	1938	2535	2699	2,832	2,404	2,470
D&A Exp.	---	---	---	530	550	1103	1486	1,418	1,317	1,105
Operating Profit	---	---	---	2380	1208	678	1287	1,600	795	1,579
Operating Margin	---	---	---	14.3%	9.1%	3.9%	5.6%	6.7%	3.8%	7.7%
Net Profit	---	---	---	-1262	668	-73	195	128	-9,940	(219)
Net Margin	---	---	---	-7.6%	5.0%	-0.4%	0.9%	0.5%	-48.0%	-1.1%
Free Cash Flow	---	---	---	670	-162	-1464	767	886	517	1,518
Income Tax	---	---	---	473	250	71	258	482	559	758

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	---	---	---	---	21,721	56,500	52,439	53,369	38,007	35,308
Cash & Equivalents	---	---	---	---	981	7,030	3,723	3,249	4,132	3,853
Accounts Receivable	---	---	---	---	1,699	4,700	4,974	5,448	4,676	4,724
Inventories	---	---	---	---	3,224	4,507	4,620	4,608	4,421	3,979
Goodwill & Int. Ass.	---	---	---	---	9,129	26,285	26,436	26,071	10,374	10,090
Total Liabilities	---	---	---	---	6,866	18,090	17,426	18,870	19,765	18,562
Accounts Payable	---	---	---	---	1,898	3,377	4,025	4,268	3,532	3,745
Long-Term Debt	---	---	---	---	276	8,262	7,227	6,622	7,633	6,727
Shareholder's Equity	---	---	---	---	14,688	14,277	17,465	21,929	12,893	14,830
LTD/E Ratio	---	---	---	---	0.02	0.58	0.41	0.30	0.59	0.45

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	---	---	---	---	---	-0.2%	0.4%	0.2%	-21.8%	-0.6%
Return on Equity	---	---	---	---	---	-0.4%	1.2%	0.6%	-57.1%	-1.6%
ROIC	---	---	---	---	---	-0.2%	0.4%	0.3%	-29.7%	-0.9%
Shares Out.	441.0	438.0	434.0	437.0	424.0	422.0	463.0	653.0	713.0	906.0
Revenue/Share	---	---	---	38.81	30.42	40.23	53.33	42.80	30.67	24.88
FCF/Share	---	---	---	1.56	(0.38)	(3.43)	1.79	1.59	0.49	1.84

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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