National Energy Services Reunited
Q1 2021 conference call
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<u>**Presenters**</u>
Sherif Foda -- Chairman of the Board and Chief Executive Officer
Chris Boone -- Chief Financial Officer

<u>**Q&A Participants**</u>
David Anderson -- Barclays
George O'Leary -- TPH & Co.
Igor Levi -- BTIG
Blake Gendron -- Wolfe Research

Operator
Good day and welcome to the National Energy Services Reunited Q1 2020 Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance or technical support, please press star zero on your telephone keypad. As a reminder, this conference is being recorded. It is now my pleasure to turn the floor over to Mr. Chris Boone, Chief Financial Officer, please go ahead, sir.

Chris Boone
Good day, and welcome to NESR’s first quarter 2021 earnings call. With me today is Sherif Foda, Chairman and Chief Executive Officer of NESR. On today's call, we will comment on our first quarter results and overall performance. After our prepared remarks, we will open up the call to questions. Before we begin, I'd like to remind our participants that some of the statements we'll be making today are forward-looking. These matters involve risks and uncertainties that could cause our results to differ materially from those projected in these statements. I therefore refer you to our latest earnings released, filed earlier today and other SEC filings. Our comments today may also include non-GAAP financial measures, additional details on reconciliations to the most directly comparable GAP financial measures can be found in our press release, which is on our website.

Also, as noted in our press release, the company is still reviewing the potential impact of the recent SEC guidance on accounting for warrants issued by SPACs. Certain GAP financial information that could be subject to adjustment will not be discussed on the call today. This information will be provided upon the filing of our quarterly report with the SEC. Finally, feel free to contact us after the call with any additional questions you may have. Our Investor Relations contact information is available on our website. Now I’ll hand the call over to Sherif.

Sherif Foda

Thanks, Chris. Ladies and gentlemen, thank you for participating in this conference call. I'm very pleased with our sustained momentum and solid start of the year. We continue to solidify our position organically and inorganically, in line with our strategy. We grew 7% year-on-year, while the market contracted by around 25% and maintained flat sequentially despite the usual slow start, that was evident by our peer average drop Q on Q of 5 to 6%. We have the solid free cashflow of $37 million dollar on the back of good collection this quarter, which gives me a very positive indication of the year, as expected. I would like to thank our team in the field for their dedication, perseverance, and effort to achieve those outstanding results, despite the evolving COVID situation. Middle East is now seeing the effect of the wave two and continued to be in a semi-lockdown mode, watching carefully what is happening in neighboring countries like India. We have maintained our 100% capacity of operations, despite several countries in the region within specific quarantine requirement, which have certainly made the logistics a very complex exercise.

Our crisis management team continued to be running the show on a day-to-day basis, and we don't foresee it changing until we have a solid vaccination and ease of movement. Some countries are progressing very well with clear mandated vaccine to people ending the premises and operations. Abu Dhabi is a very good example, where our client provided the vaccine for everyone. On the macro side, on the long-term, Middle East continues to cement its place as the pivotal figure in the oil and gas landscape. No one can compete with the lowest cost producers. In addition to the global pressure and speed to move out of fossil fuel, and the acceleration of the renewables for power infrastructure, the region has an unmatched reserve and the biggest demand market next door in Asia.

The growth market in Asia, largely insulated from the dynamics you see here in the Western Hemisphere and will depend on hydrocarbons for many years to come, especially as gas continue to replace coal as the cleaner fuel. The drive for the region is to concentrate on diversifying and growing their renewables and massive increase in gas production to meet the local demand, while investing in oil production to meet the global demand. Hence, from our point of view, our existing core business has an inbuilt recession proof baseline growth, which I don't believe the larger market agree appreciate its magnitude. This will continue for decades, and our aim has always been to turbocharge the growth with accretive strategies as the partner of choice to all our customers.

On the short term, we have been saying now for over a year, that the oil markets will tighten on the account of U.S. shale effect, not enough discoveries, and lack of investment in exploration to offset the natural declines of existing field globally. The pandemic delayed the onset of this demand tightening, and yes, it also may have structurally changed the demand longer term, but this has only delayed the inevitable. As yet we don't see alternatives covering for the declines we see in the oil and gas supply. As an immediate effect, we already see our activity now

starting to increase, and I see double digit activity growth in the second half of the year. I believe all our peers are also saying the same.
Although demand from key markets like India may get affected by the second with that (PH), I believe we are now firmly in an early stage of an upcycled which is here to stay, for a while. Also, with a lot of major advocating reduced investment in oil and gas project or actively talking about exiting markets or even the space altogether, it gives more responsibility on the NOCs to remain the reliable supplier to the world. And hence, all roads lead to the Middle East. Again, if you want security of supplies, and long-term stability, therefore, the Middle East gaining back that position as the swing producer.

Our customers are very wise and are already making the right moves to ensure they are able to meet this demand. We at NESR have seen this coming and have planned accordingly, by front loading our capital needs, actually started planning since the second half of last year. We also have worked with our strategic suppliers to get first in line on some of the long lead time hardware, including pre-ordering some items with manufacturers to hold them in inventory, which go in the equipment to accelerate our deliveries to catch this growth in H2. We have been evaluating our needs this quarter, and deciding to order more equipment and products for the second half and early 2022. We need to maintain a buffer of resources and be first to act when our customers need us, again, as the most reliable partner.

To focus now specifically on some of our operations. I wanted to talk about Libya. Libya is all of you know has gone through a lot of turmoil over the last 10 years, and lately has achieved a breakthrough, an amicable political situation that no one had ever dreamt off, which in turn gives the country a good steppingstone for growth. Libya has a lot of potential and production has dropped to almost 20% of its existing capabilities. As a start, the first million barrel is what I call the easier task. Then to get back to its full potential, you need a lot of rigs and massive Regulus and workover activities. We have been investing heavily since the beginning, and now we have the solid base in both the east and the west, enabling us to service all the clients. We are adding product line and enhancing our facilities to ensure we can reliably answer all our customer needs.

In addition, we have an almost 100% national talented team, with many years of experience under their belt. They know their customers and the NOC and continue to be very close to them as we were since the beginning in the most difficult times. We need to provide technology and answer product to swiftly increase the production. Now let me move and talk about the technologies and segments. Here, I have to specifically mention our progress in D&E (PH) this quarter. We have done very well by growing both Wireline and Slickline operations. And I'm very happy to say that we did the same amount of revenue for both this quarter as we did in the whole year prior to the merger.

We have deployed new tools to target markets, have several--managed to acquire several operating and Wireline Slick units at a fraction of the price during the severe downturn last year in the U. S. It is a continuation of our drive efficiently use our CapEx dollar and leverage opportunistic purchases as and when they come along. On drilling, we are making great progress operationally. In Kuwait, we have introduced new agitators as part of our downhole tools offering achieving record performance improvement, resulting in significant market share gains in our fishing (PH) services. This quarter, we announced our partnership with Phoenix Technology, for MWD, and motors. And I'm glad to report that we have already run these motors in jobs designed and planned by us, and these jobs have significantly outperformed existing established players and broke ROP records for those sections. Actually, we broke existing records on 60% of the run, which is an impressive achievement. To give you an example, we drilled this section and 30 hours, instead of the field average of almost 60 hours, which means we saved the client more than a day, in such a small section of the well. We continue to work on identifying key markets and get assigned rigs where we can demonstrate clear differentiation.

In addition, we recently announced our partnership with Beyond and we formed a new JV to operate and implement the market leading managed pressure drilling technology, not only in our core miner operation, but also in other countries in Asia and Africa. With contracts awarded already in both Malaysia and Ivory Coast, we will be able to demonstrate better reliability, better drilling performance, better cost of ownership. Beyond has patented technologies that offer customers a more compact and practical full MPD package that takes less time to rig up rig down, and is easier to operate, saving time and money for customers. As a result, it has become the leader in MPD market in the U. S. and Canada.

Unlike many players in the MBT specific spectrum, Beyond owns the technologies included in their MPD packages from API monogrammed RCDs that outperform the competition by margins, up to three times to specialize state of the art MPD control and design software. Another technology we're very proud of being an early investor, and we believe is a game changer is Kinetic Pressure Control, who were recently featured on the cover of GPT. You may recall Kinetic, or K-BOS has invented the device, which merges next generation materials used in the space programs with military technology to address blowout prevention. Essentially, it acts as an airbag for the drilling operation.

They have just completed the test on the drilling and coil BOTs, which have significant consequence on how our customer can safely conduct their operations. As you know, blow outs like Deepwater Horizon have significant negative environmental impact, and this device pretty much eliminates that possibility. And we are taking the lead in implementing it in the region. We are now set on the ground, which is shortly going to be qualified and tested, so a great success in the making. As you know, our performance has been achieved by continuing to focus on our execution capabilities. determination for the region, being the flagship the MENA (SP) national champion, and our customer centricity.

We are working relentlessly to provide a strong platform of technologies to enable our industry to produce efficiently and sustainably. Part of our ESG impact effort is our early investment in ICE Thermal harvesting, which we believe is a very forward-looking idea on how to harness the thermal capabilities of the blade (PH) or produce gas to provide electricity. We hold a pilot of this technology within a year and implement it in the region. We have also made considerable progress on firming up on our water specific opportunities on our brand to run a pilot and technology demonstrator with one of our main customers. We are also in the final stage towards an offering in the (INAUDIBLE) detection space and should be announcing an investment and partnership to that effect, shortly. This is something which will hit the ground running and we hope to run these technologies immediately. Lastly, I want to convey that subsequent to our recent announcement on our acquisition in Kuwait, we have successfully closed the transaction and are effectively running the operation as we speak.

I want to take this opportunity to thank Sheikh Mubarak and his team working round the clock with us to help grow this business. These are accretive contracts from day one, and given our strength and cement and poised businesses, we can ramp up this operation significantly in a very short period of time. Secondly, the drilling fluids product line, which was a very small offering for us, now graduates to a sizable part of the business in Kuwait and forms a baseline for our growth in the region. Kuwait is a big story for us, as an anchor country that had significant reserves with a savvy NOC. We grew organically securing several contracts in drilling, cementing, testing, and now with this force multiplier acquisition, we will have a substantial role to play and be part of their vision to transform the oil and gas sector.

Overall, As you have noticed, and as promised, we have announced and closed on two major transactions in approximately one year, in the midst of the pandemic. We have largely handled these internal resources to keep the costs in check. More important, we demonstrated our ability to agree on terms and execute the deals with our own cash generated from operations. That ability will even enhance going forward, as we will generate more cash and will have the capacity for more technology in any accretive deal. On that note, I'd like to pass the call back to Chris to talk about the financials in detail.

Chris Boone
Thank you, Sherif. Turning to our preliminary results, we've reported quarterly revenue of $212 million. This represents an increase of 7% over the prior year quarter, and flat over the fourth quarter. The year over year quarterly increase was primarily driven from the growth of the unconventional product line, and new contracts in Kuwait and the UAE. These offset lower activity in other markets and other service lines related to the impact of COVID, which had a little effect on our operations in the first quarter of last year. Adjusted EBITDA the first quarter was $50 million or 24% of revenue. This represents a decrease from 26% in the prior year quarter and the prior quarter.

EBITDA adjustments of $2 million for the quarter are mainly for integration costs associated with last year's acquisition, transaction costs associated with our recent acquisition, and other restructuring activities. As we highlighted on our last call, we continue to incur significant COVID related labor and supply chain inefficiencies and costs. We are carrying incremental labor costs in anticipation of the expected market recovery. However, NESR will be positioned to react immediately to new customer requests, while our competitors are delaying ramping up their operations. As is our practice, we did not reflect any of these COVID related or other items in EBITDA or EPS add back. Moving to our segments, our productions segment revenue for the first quarter was $137 million dollars, growing 3% over the same period last year and 1% over the prior quarter. Adjusted EBITDA margins for the production group were 27% in the first quarter, down 2% sequentially due to the increased proportion of pass-through revenue from hydraulic fracturing operations. Separately, our drilling and evaluation segment revenue of $76 million dollars in the first quarter was up 15% compared to the same quarter last year, but down 2% sequentially. The increase over the prior year quarter is primarily related to higher drilling revenue in Saudi Arabia.

Adjusted EBITDA margins of 24% in the first quarter were up from 22% in the prior quarter, but down from 25% last quarter, due to varying activity levels and product line mix. Depreciation and amortization increased to $31.8 million in the first quarter compared to $31 million in the fourth quarter of last year. The prior quarter had a benefit from a fixed asset valuation adjustment for the final purchase accounting of last year's acquisition. We expect D&E to continue in the $32 million range next quarter before the impact of the recent acquisition. Interest expense in the first quarter was $3.2 million down slightly from $3.4 million in the prior quarter.

Our adjusted tax rate this quarter, which includes the impact of the noted EBITDA adjustments, and any potential impact of a change in warrant accounting was 12.1%. Excluding the benefit of the release of a reserve on prior year taxes, the adjusted tax rate would have been approximately 20%, which we expect to continue to improve upon going forward. Adjusted net income and EPS, which includes the impact of the noted EBITDA adjustments and any potential impact of a change in warrant accounting was $13.6 million and $0.15 per diluted share.

Switching to free cashflow, we're extremely pleased with the record free cashflow generated this quarter of $36.7 million up from $32.8 million last quarter, and negative $13.6 million in the prior year quarter. The sequential free cashflow improvement was accomplished mainly due to another quarter of strong collections and lower capital spending. We continue to improve in our days to invoice while most customers have returned to normal payment practices. In addition, we were able to collect retention payments earlier than expected and that boosted overall collections. Overall, DSO improved by 16 days over the prior quarter level a strong accomplishment by the whole NESR organization. Additional actions are in process to lower DSO even further during the year.

Capital expenditures in the first quarter were $11 million, down from $14 million in the fourth quarter. This reduction was due to the lower new CapEx orders placed in 2020 and improved utilization. In 2021, we continue to expect capital expenditures to be flat with 2020 levels to support planned growth and pay for existing commitments. Free cashflow in 2021 should significantly increase over 2020 due to flat, planned CapEx, continuous improvement on fleet

utilization and improved DSO. Also, another positive, net debt decreased to $302 million at the end of the first quarter, compared to $323 million at the end of the fourth quarter.
The sequential decline is primarily from higher cash balances from improved free cashflow and net debt payments. As of March 31st, 2021 our net debt to adjusted EBITDA ratio was 1.6, flat from 1.6 last quarter, and should reduce to our target level of approximately 1.5 or lower in future quarters. Also, we remained in full compliance with our primary credit facility financial covenants in the first quarter. In conclusion, in Q1, we put the company on an even stronger financial footing with our strong free cashflow generation and are better prepared for the expected upcoming market growth and additional inorganic opportunities. With this, I'd like to pass back to Sherif for his final comments.

Sherif Foda
Thanks, Chris. In conclusion, I would like to leave you with key takeaways. We are focused to be the trusted and reliable partner for our customers and have the capacity and resources to tackle their needs while managing the pandemic and restrictions. Two, we are already seeing activity starting to pick up, and I'm confident that we'll have very strong second half. Three ESG impact segment is progressing well with our water flaring and methane detection efforts. Four, we will continue to produce free cashflow and will invest in new partnerships, and accretive M&A. And on that note, I'd like to pass back to the call to the operator for your question, Christy (SP)?

Operator
Thank you. The floor is now open for questions. If you would like to ask a question, please press star one on your telephone keypad. And if you're using a speakerphone, please pick up your handset to provide the best sound quality. Again, ladies and gentlemen, if you do have a question or comment, please press star one on your telephone keypad. And our first question comes from David Anderson with Barclays. Please go ahead.

David Anderson
Thanks, good morning Sherif, how are you?

Sherif Foda
Good morning, David. Thanks.

David Anderson
So maybe I'll just start from kind of a bigger picture question to start with. So operations in the Middle East are heavily dependent upon a lot of labor from Southeast Asian countries, including India. And as you noted at the top, there is a lot of COVID issues still in those areas. I'm just wondering, as we look out into the back part of the year and we're all kind of seeing this this ramp up, is there any concern that this situation could delay anything? Is that a concern for you at all in terms of the labor situation, and how that could play out to the Middle East?

Sherif Foda

So, as an industry, you're absolutely right. Some of the players will get affected, especially the ones that are dependent, or they have a very small percentage of localization. They will get affected, especially with the restriction being put today on travel. I think for us, being again very national and have a very high percentage of nationalization workforce, we will not see any of the issues that the others will. I would say in some specific countries, where you still have a high percentage, the industry overall will get affected, and we might get affected accordingly because of some of the delays, for example of rig readiness. So in some countries, yes, you might not have a rig crew, for example, if the current crew are being there now already for seven to eight months, and they will not be able to get a crew change. Definitely, there is a lot of things going on to replace some of those people. But yes, you're absolutely right. If the situation gets aggravated, you might get some delays of those rigs.

David Anderson
Now Sherif, you were talking about sort of the balance between natural gas and crude oil in the region. And I think kind of last 10 years, I guess you could say that Saudi and some of the neighbors have really shifted spending and activity towards natural gas. And if I'm not mistaken, I think around 60% of the onshore recount in Saudi is actually directed towards natural gas, not sure what is today. But just wondering kind of bigger picture--you know, the oil markets are tightening OPEC, clearly looking at recapture share, do you expect this mix to shift back to more the oil side? Do you expect the majority of tenders now to focus on the oil side? Or does that not actually change because of their capacity situation?

Sherif Foda
I think you're absolutely right, in the second half of your question. It's not going to change, I think, definitely, they have the capacity again, to put oil to the market. Let's say if the market gets even tighter, and they need to put more than 6 million barrels, yes, they will--you will have some short-term shifts of some of the rigs going to the oil to get some of this production. But overall, I mean, their vision is to really get the gas in the different countries to be the main fuel for their internal demand. And always remember that most of this in the countries are done for internal consumption, the only one that has huge capacity to export is Qatar. But the majority of the rest is really using it for internal consumption. So this is not going to change. And you saw, for example, the Saudi leadership is very clear on moving to renewable and to gas for all internal consumption, and really sparing the production, the oil production, import/export.

David Anderson
And then my last question, if I can just squeeze one more in, you talked about kind of pre-ordering equipment in front of kind of what you're seeing as a ramp up and want to make sure that you've got the capacity while others don't. You know, we've seen in the last couple of years, it seems like you've been growing, everybody else has been sort of treading water. Just wondering if you just kind of give us an overall sense of the capacity situation over there, I guess, if you're pre-ordering equipment, you must be thinking that the capacity situation is pretty tight. I know everybody's got to kind of looking a little bit different in terms of capacity. But just from your standpoint, in your product lines--you know, could this market really tighten

really quickly in the back part of the year, it just seems like you're the only one who has really been spending any money over there.

Sherif Foda
I would say there's still excess capacity, overall, right? That what will happen is the readiness of this capacity. So if I want to be a bit more specific, today, I know that the market is going to get tight on some of the product line, for example, readiness of (INAUDIBLE) fleet, when you have all this Regulus activity that is going to sharply increase and people are not planning for it, some people as well have issues with spare parts or equipment they did not prepare. They did not sorry--repair during the pandemic, and these equipment despite the fact they are physically there, but they are not ready to answer some of the jobs.

The jobs as well are getting a bit complicated where the client needs higher specs, longer reach bigger pipe and some of this activity these equipment are not ready in each country. And that's where I'm saying we front loaded our CapEx, we looked at this last year, we have obviously--I explained it in the prepared remarks, we looked at the opportunity to buy some of the equipment, so we bought actually several of those equipment at a fraction of its price $0.20 cents to the dollar and bought Slickline equipment Wireline equipment, some of the high pressure equipment and we shipped all this to the Middle East. And we have that ready green tagged as I call it, ready to be deployed. So, it is very important that I think some of the smaller companies will not get will not be ready at all for this increase.

Already I see them turning down jobs and we will be able to capture some of the work. And some of the others as well, some of the other like I would say, competitors, they have issue with cash, right? So either they have a restructuring or something like that, so they are not capable of putting CapEx as we can, right? So, and I think this is where the client looks at who has a buffer, when they make a call and ask for this. So today, you don't see that visibility, but I am quite confident that this is going to happen in H2. And that's why we are preparing for specific market to have specific equipment, for what I think they will need. And then I will be able to capture that before the others.

David Anderson
That's a nice opportunity. Thank you, Sherif.

Sherif Foda
Thank you, sir.

Operator
And our next question comes from George O'Leary with TPH and Company, please go ahead.

George O'Leary
Good morning Sherif, good morning Chris.

Sherif Foda
Good morning George.
George O'Leary
Just curious for a little more color on the shape of revenue throughout the year, Q1 ’21 panned out much more resilient than all your competitors in our expectations, which was great to see. But I wondered if you could bifurcate a little bit between production and the D&E segments. And talk about the progression of revenue, Q2, Q3 Q4, just if it's heavier in the back half, or if we see a nice ramp in the second quarter. And just curious on the bifurcation between the segments, given the some of the idiosyncratic factors that play in like the M&A you guys have executed on the partnership with Phoenix that can provide a boost to the directional drilling side and already seems to be doing so. Any color there would be super helpful.

Sherif Foda
Okay, great. So let me start with first the split, I would say that, given, again, the size of the unconventional and the frac operation, with all the growth that we are seeing on the D&E, I would say the split will not change that much, until year end, I would say it's going to start to change maybe from next year. But until year end, I would say you would see more or less than two thirds/one third in our business, between production and D&E. In addition to that, as I said, the H2 is going to be very strong, and obviously some of the countries will want to see some of their regulates and production activity increasing, I would say the demand of some of the production segments will increase.

And even with the growth of the D&E, you're still going to get growth or higher growth, even in the production segment, because of that. On your second part of the question, I would say H2 over H1 is going to be significant. And as I mentioned, you're going to get a little increase in Q2, but really, you will see the real increase in H2. And one of the reasons that people have to remember that during Q2, you have the month of Ramadan, which we are in now, and then you have the holidays. So you know, this usually comes a bit of a slower activity due to that. So I would say, you're going to see real ramp up in G2, where it's obviously, as well, the client wants to see clarity of the demand and clarity of the situation of the pandemic and the European opening, and the board that I mean, you see most of the countries now are talking about first of July, complete opening, the tourism is back.

You see there is a still lock down, there are still restriction, some countries that did not open at all, and then you cannot even enter them, like for example, you know. So what I would say you're gonna see a significant H2 over H1, and that's why I call it always a double-digit growth for ourselves, in my opinion, H2 over H1 revenue. I don't know if I answered all your question, you have something?

George O'Leary
No, that was great Sherif. And then just drilling into the partnership with Phoenix a bit and pun fully intended there, can you--it seems like now you're in a good position to compete with the largest players there, and I think back to a conversation you and I had a few years ago when we

first met in person in Houston. And that was kind of one of the areas you guys were really looking to press forward into and get more exposure to within the Middle East. So does this--do all you guys need to do to compete against the big boys so to speak in that Middle East market on the high end of the directional drilling market?

Sherif Foda
No, the honest answer is absolutely not. This is basically as a call a steppingstone on the drilling portfolio. So you have to differentiate the drilling portfolio today is you have the motors, high spec motors, MWD business and then the real rotary steerable market, that is the large part of the business. And today that part is with LWT (PH) high spec or high end, right? So what we have been doing all along, is we are very credible with our customer, and we want to only bring partners that are reliable, and they make a difference. So what we looked at Phoenix and I was very impressed with what they achieved here in the Permian and replacing everyone on their on their high spec Atlas Motors, and the velocity with the MWD.

So what we said, we looked at the market in the Middle East, we segregated, and we said, "Why nobody is doing that, in that market, why those sections are being drilled with Norman (PH) motors." And we had a very good agreement with John Hooks with Phoenix, and we agreed, "Let's put those. But let's make sure when we go there and replace some of the competitors on that--on those sections, we have to outperform them, otherwise, what's the point?" Right? So we did that, and they did an outstanding job. And almost every single one, we outperformed the existing field average, as they call ROP. So I was actually quite impressed yesterday when I looked at the numbers, and actually we had an 83 to 84 foot per hour versus the average of 42.

Right. So basically, they doubled the ROP of that section, which is basically, you can drill that section in 50% of the time. So if that section takes you today, two days or for example, the example I put there is 60 hours we do it in 30 hours, that day, day and a half. If the rig count, the spread rate in the Middle East costs you around $45,000 to $55,000 a day, day and a half is significant, right? So you're talking about $70, 000-$80,000. And if the price is the same or equivalent, then we already saved this client. And that's where we see how can we grow we go this point. We have a full-blown technology roadmap on the drilling to ensure that we have all those factors. So we have high spec motors working on (INAUDIBLE) working on MWD, LWD, etc. And this is when I would say, I have a solid portfolio, and now I can tell you, "Yes, I can compete with the big boys for the entire drilling portfolio." But today, no, we are only specifically targeting that part of the market.

George O'Leary
Right, I appreciate the honesty and the color that was very helpful context. Sneak in one more, if I can, that the acquisition you guys announced during the quarter was nice to see and good to see you guys press into Kuwait further, just wanted to get your thoughts on pull through opportunities that might emerge from that? Or is this more a Kuwait focused acquisition, you have opportunities to pull those revenues in other geo markets?

Sherif Foda
No, I would say--yeah, this Kuwait basically make us as I call it an “Anchor country.” Like the big countries that we have. And this will make sure that we have that present, and ready where we can have fantastic infrastructure, they have an amazing facility, three facilities, they have the solid--obviously, relationship and contracts for five years. The only part that I would say will make a big difference for us to go outside of Kuwait on this is the drilling fluids. So today, the drilling fluids they have is a state of the art, they just started that contract, they have a very strong base.

And we will be able to demonstrate that ability to show some technology partnership that we have added to that contract and take that business, the way we perform and showcase this to the other countries. You know, it's exactly like, for example, what we did in the frack business in Saudi Arabia. Today, as we are the leader in that business, we can demonstrate this to all the neighboring countries, they see what we are doing in Saudi and Saudi with their leadership in how they perform this, as a client, how did they make this unconventional a huge success for them? How can--and we were part of it as one of their provider. Now if you do the same thing on the drilling fluids and then show it to the neighboring countries, then you start to gain share on that--you know, one and a half billion-dollar market that today we don't even touch right. So this drilling fluids is very good business that we just started now.

George O'Leary
Thanks, Sherif. I'll turn it back over.

Operator
And as a reminder, ladies and gentlemen, if you would like to ask a question, please press star one on your telephone keypad. Our next question comes from Igor Levi with BTIG. Please go ahead.

Igor Levi
Good morning.

Sherif Foda
Morning, Igor.

Igor Levi
On the ESG front last quarter, you talked about plans to convert the infield water into drinkable water as well as remove sulfate from water, so you can use lower quality water for drilling freeing up higher quality water for drinking. I remember you were you mentioned, I think you were in conversations with three customers and thought--you know, they may pull the trigger on a project before the end of the year. I wanted to see if you could provide some color on how

many customers you're speaking with, is that still the plan is--you know, in terms of timeline and such.

Sherif Foda

Thanks, Igor. Yes, absolutely. Very exciting about the water, especially the freshwater part. And we are in the final stage of designing the pilot and sending it, and we will have the pilot in four to six weeks, I would say in the country. And we will be able to see the benefit and the results of that facility in--with one of our major customers. And then definitely this will be a showcase. If it works exactly as we said it will work, being able to remove the solids, being able to--and I would say test it at extreme conditions. So what we are working on is actually taking that technology to a different level. So there is H2S, there is some oil content, there's very high salt, and very high solids content. And we see--we want to see how can we design that pilot to be able to remove all this and get fresh water on the other side, right?

So yes, I would say as promised, we will have that definitely before year end. And we are at the same time in parallel negotiation with two other customers to make the same thing and making sure that we have this type of facility or a pilot as well before year end. So we're very excited about the water, and I would say that, we should see that, and then obviously, as we explained, we should see then after that big project, making able to convert those pilot to a big facility, because that's our aim, right and the client as well. Most of our clients in the Middle East have huge, huge targets for their ESG and their circular economy. So you can see that they announced a lot of like--you know, the 5 billion trees, and there is a lot of activity going on today for this, and this definitely will be a huge differentiation.

Igor Levi

Thank you and as a follow up, could you comment on how your partnership with ICE on the geothermal side will contribute to your ESG goals? Is that something we're gonna actually see as well before the end of the year on that front?

Sherif Foda

No, this is now early investment right. So, this is basically you know, if I give more even color on that, so, the partnership we do it's very important to differentiate. So, we do some of established companies, have the proven technology and we have that partnership like for example, we have with next year like now we have with Phoenix, we just announced Beyond which is actually with Beyond to a joint venture as well to operate with that joint venture into the international market, which is something that we just we announced and now we have two contracts awarded.

So this JV will operate those contracts, and then you have the early stage what I call the "Innovative people" that have something that is not proven, right. So it is--today ICE an amazing ideas, they are working on some patents, they're working on some new technology and here we become an investor. So we put money to like venture capital, so we put money and with other investors and they are going to work on the idea, they work on the technology, they are

going to test the technology and then they have an ESB then they have an EMP and then we commercialize it.
So as a small company, usually this cycle can take up to two to three years. As a small company and a small and very talented people like we have with ICE, we are targeting one year, so 12 months for that EXP. So basically, we put the investment that will be called for, an additional investment and then the product will come in a year time for us to be able to take it and pilot test it. Whether we're going to pilot test this directly in Middle East, or we're going to pilot test it first in the U. S., then transfer it to the Middle East, that's yet to be seen. But, you know, today, Igor, we have around four or five of those that we are working on. And then it's--again, that's our R&D. And that's what I always explain, that's our philosophy of open platform. So we target with very innovative people, and we give them money to try to start a new project or a new tool, or a new idea. And that's how we see how it will work, and then take that outside. We have some--we have one of them that we've been investing now more than a year. And but it because it's heavy in electronics, I don't see this, for example, until next year. That's why we don't announce about it right. But we are working on that, that's our R&D arm. And that's how we do it.

Igor Levi
Great, I appreciate the color I'll turn it back.

Sherif Foda
Thank you.

Operator
Our next question comes from Blake Gendron with Wolfe Research. Please go ahead.

Blake Gendron
Thanks. Good morning wanted to follow up on the unconventional opportunity. And really just frack broadly, I think before, where there was more focus, when this was ramping up, there was one unconventional fleet in Saudi, there may be another--you know, quasi conventional plus conventional fleet in Qatar and maybe rotating between a few countries. What do operations look like now, and now that we're,--you know, getting through the pandemic, somewhat here, slowly, but surely, what's the ambition to grow that part of the business for Nasser?

Sherif Foda
Thanks, Blake, so, let me just emphasize, we have today two fleets in Saudi Arabia. So we have--and they are working actively between Jafurah basin and the (INAUDIBLE). And again, Saudi has been really a pioneer in developing those fields and state of the art, what they have done. So we are working with them, we are in discussion, as I explained earlier, with three other customers and other countries to start the frack business in those countries. The discussion is very active, we are--our ambition is to land two of those before year end. So as I

explained before, what our aim is to have four fleets in the country, in those countries before year end, and my expectation is we're going to have one in H1 and one in H2, right?
So that's exactly--and then obviously, you're got to see real revenue. And I would say, in the second half of the year. The client majority, they have a lot of clients that are working around the clock around those activities. You have to again, differentiate in the Middle East, between unconventional and conventional, do they do frack in the Middle East, but they do not frack what you know, in the U. S., whatever you have. That style of multipads (PH) 50-60 stage per well, it's only done today, in Jafurah bason. The rest is really much smaller footprint, but you have a lot of fracks, you have fracks in Ajman, since very long time, they have type formation. You saw the announcement of UAE, with His Excellency with (INAUDBLE). And they exported--they said they exported the first unconventional gas from the Deeb (SP). It was announced definitely they have a huge program in UAE for the unconventional.

You have unconventional everywhere. But I think the main activity, or the matured activity is always going to be in Saudi because of the size. And then you will see more and more coming. So we are we are in very, very, I would say good shape, to announce hopefully the awards of those fracks, before year end.

Blake Gendron
That's very helpful. Moving to the back half and the double-digit activity increase that you anticipate, it was helpful to hear about the equipment readiness, it was helpful to hear about the split between PS and DE. Just wondering in terms of your market share assumptions, it sounds like you're still going to be able to outmaneuver some of the smaller competitors that are maybe cash strapped. It was our understanding though that through the pandemic, you were able to also maybe outmaneuver some of the larger competitors, just because of travel restrictions. Do you anticipate those larger competitors perhaps reestablishing some share in the back half of this year, or is it still very much NESR's for the taking just given--you know your ability and equipment readiness?

Sherif Foda
We're obviously very careful about everybody. And we, I would say, we have a lot of respect to every competitor we have, I would say that we have a path of our growth and our market share. I don't see this hampering or slowing down in the near future. Part of it is what we explained that we understand the customer extremely well, we have kind of, I would say, visible activity, what's coming in the second half, we prepared those equipment, we prepared the people.

Honestly, speaking, I don't think anybody else is. So there is a lot of constraints on the smaller guys for cash strapped or profitability, etc. And some of it, you have to really, I would call it "Bite the bullet" and--you know, again, be socially responsible, especially with the pandemic, not to release the people, to make sure that you have your crew ready, you have to make sure as well--you know, you take care of them and their family, etc. and this will pay out, right. So we have readiness, in a lot of the countries where I see our small competitors not ready. I see,

again, the cash strapped people are some of the competitors, or even the international ones, some of them have some issues with the CapEx deployment.
I don't see--I'm not saying that the big guys are not ready, they are obviously, but I don't see them being able to take part of the growth that we that we are forecasting, I see that we are going to have the market share gain that we are planning. And I see that we are very confident that we're going to have the second half with double digit on the first half. The path is clear. And I would say that we will make our numbers.

Blake Gendron
That's totally fair. One more housekeeping if I can maybe get in here, for Chris, it looks like very few charges and credits this quarter, obviously versus last quarter, and it was largely due to the transaction costs, it looks like in this quarter. I know we'd previously talked about--you know, logistics costs associated with pandemic and how you included those in numbers and not wanting to adjust those out. But Chris, you know, are those charges and costs still very much there? And do you anticipate those to moderate through the year, and do you have any visibility into sort of the pace at which those heightened costs moderate for you?

Sherif Foda
The costs are there that gets reset. The real key is having the revenue growth that will absorb them--you know and improve the employee utilization. That's really the key. So, it's just getting the leverage back on those employee costs, the costs will stay, the costs are not going away, they just need to be utilized.

Blake Gendron
Okay, thanks I appreciate the time.

Sherif Foda
Yeah, I mean, if I may just compliment what Chris just said I mean, if you look at our--the way we structured the whole thing of the CMT and crisis management team, etc., is we just said that this is part of the business and you just have to live with it, you see what I mean? So, your PCR test, your extra people, your restriction on travel, your airport issues today, for example, I just give you an example, that if you want to go to one of the countries, they are requiring you, if you come from a certain you have to stay in another country for 14 days. All these people go to that other countries, stay there for 14 days, and then after that they--what they call the are from the green country, then they will be able to travel to the other one. And all this is part of our business.

If I look at our transaction and costs which we take out, we call out, that's all due to the nature of acquisition, M&A, lawyer fees--you know, some of the exit of some people, for example, if we do some restructuring, and then all the stuff that we call out like the--you know, the preparation for Sox (SP) and etc., etc. That's the only cost we call out because that's basically it should stop and going forward, you should not have that, right. So, I mean, I would say you might see it for a while because we are very active in M&A. So you will see that. But definitely as Chris explained the pandemic and all the stuff, I cannot call this out because this might stay for, I don't know how long. But definitely, as we said, the CMT and the way we operate, we keep it the same way because we don't know how this will will last, when it's going to stop, how it's going to work out. We are obviously working very hard with the vaccinating of our people. But we do this with the government and with the clients, and with the customers in the different jurisdiction right. So trying to elaborate more on that.

Blake Gendron
--(INAUDIBLE) I didn't know it was a source of upside, potentially for you--you know, as we move through here. I know you don't call it out and appreciate that you don't call it out. But you understand that there is a pandemic related cost that's in there. And, I just didn't know if it was going to be a source of upside, potentially, from the woodlands (PH) moving forward.

Sherif Foda
Yeah, I mean, honestly, I--there isn't--I wouldn't call it an upsell. I mean, yeah, it might be, but I have to as well be quite frank, that you have as well--we save some costs because nobody's travelling, except a couple of people, right. So there is as well, some cost avoidance we're working on--you know, and a lot of people especially on the management side, on Zooms, etc. Right, but yeah, might be.

Blake Gendron
Thank you.

Operator
And I'm showing no further questions from the phone lines at this time. So I'll turn it back to management for any closing remarks.

CONCLUSION

Sherif Foda
Thanks, Chris, thanks. Thanks, everybody. Very excited again on a solid quarter and I would say very bright future. Quite optimistic actually about the next second half and next year. Thank you very much. Thanks for your time.

Operator
And that concludes today's conference call. Thank you for attending. You may disconnect your lines at this time and have a great day.