

Rig manufacturers roar back to life

The boom in drilling activities has shaken the rig-building industry out of a 2-decade slumber.

And the dramatic jump in demand for both new and refurbished rigs is leaving many companies with maxed-out capacity and component shortages.

By Linda Hsieh, associate editor

IT'S EASY TO sum up the rig manufacturing market for the past year: "We're selling them as fast as we can make them," one manufacturer said. For oilfield equipment manufacturers, full capacity and production hikes have been the norm.

Schramm, a Pennsylvania-based company that makes all-hydraulic drilling rigs, has nearly 100 rigs on order right now, according

to CEO **Ed Breiner**. The company increased its capacity this year by about 40% over 2005 and hopes to produce 90 rigs. For 2007, it's targeting an additional 33% increase to 120 rigs.

While these appear to be significant increases over a 2-year period, they don't seem to be covering demand.

"We're still flat-out, meaning we're booked through mid-2007," Mr Breiner said. "But I think that's fairly typical of anyone serving the energy market right now. I don't think this kind of backlog is unique to us."

Houston-based **IDM Equipment**, which specializes in AC rigs, has no manufacturing slots available until the second quarter 2007, according to sales manager **Barry Olsen**.

And in Odessa, Texas, **MD Cowan** is making "super-single" rigs that are smaller than conventional rigs and require only 2 workers to operate. President **Mike Cowan** said his company is also booked through mid-2007. It put out 7 rigs in 2005, doubled production to 14 rigs this year, and plans to push capacity to 24 in 2007. That's nearly a 250% growth over 2 years.

"We're increasing our capacity as much as we can and as fast as we can," Mr Cowan said. "We also do rig refurbishments, but the newbuilds are taking over the refurbs. There's nothing left to refurbish anymore. The used inventory is exhausted. They're gone."

LOOKING ELSEWHERE

In mid-2005, Houston-based **Nicklos Drilling** was looking to buy a new rig and found China's **Baoji Oilfield Machinery Company (BOMCO)**. Its headquartered just south of Xi'an – best known in the West for its terra-cotta warrior figures – and is a subsidiary of the state-owned **China National Petroleum Corp.** The Nicklos Drilling rig – Rig 5 – may be BOMCO's first complete rig sold to an American company and operating in the United States, but the company makes 70% of rigs used in China and has exported products to countries such as Azerbaijan, Turkmenistan, Cuba, Oman and Iran.

"I have seen very strong interest in Chinese-manufactured rigs," said **James Hayes**, senior vice president of **BOMA Drilltech**, the US contractor for BOMCO.

BOMCO produced more than 70 rigs in 2005 and plans to produce 90 rigs in

Q&A with National Oilwell Varco's Pete Miller

Pete Miller, chairman, president and CEO of National Oilwell Varco, spoke with Drilling Contractor on the industry's new building cycle, challenges, the future and more.

Q: How would you describe the demand for new rigs so far in 2006?

A: Clearly it's been outstanding. NOV's backlog was \$3.2 billion at the end of Q1 (which rose to \$4.1 billion as of 30 June). That's pretty sizable. It's been a very good market.

Q: How does that compare with the demand from 2005?

A: It's sharply up. In 2005, NOV announced backlogs that were less than \$1 billion a few times, so it's been increasing dramatically, and it's really pushed by the international offshore market.

For us, the spike in demand is always relative to what goes on offshore. For instance, if someone wants to build a land rig, NOV revenue potential is about \$10 million, and that's very good. But if someone wants to build an offshore floater, NOV revenue potential is \$200 million. So a floater vs. a land rig, NOV will take the floater every time.

I love land rigs too, but clearly over



Pete Miller

the last few months, the floating segment of the market has been hotter, so our backlog has built much more dramatically.

Q: How does this current building boom compare with the boom that went on when you first came into the industry in 1979?

A: 1979-82 was one of the biggest building cycles the industry had ever seen, but there were a lot more players then. To give you an example, in 1981, National Supply – no Oilwell, no Varco – delivered 3 drilling rigs a day. In 1981 alone, National Supply delivered 1,100 rigs and the entire industry delivered over 1,500 land rigs. You can't do that anymore. The capacity and companies to do it just aren't there.

In 1983, the industry delivered 100 jackups. This year, the industry will probably deliver about 15 jackups. The industry just doesn't have the capability that it had back in the late '70s and early '80s. National Supply built 20 years worth of rigs in 2 years. You can't do that now.

Q: So you don't think drilling contractors are overbuilding?

A: I think they're building more replacement rigs than people want to admit to. If there are 1,600 rigs out there and 300 new ones are coming out, they say we're going to have 1,900 rigs. Fact of the matter

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2006 and 95 in 2007. About 20 of this year's 90 are headed for the US, going to companies such as **Nabors**, **Parker Drilling** and **Lariat Services**.

"BOMCO will increase its production very steadily every year, and more and more of that production will go outside of China," Mr Hayes said.

Nicklos' 1,500-hp Rig 5 was ordered in June 2005, took approximately 3 months to construct and 2 months to ship to

Houston. The drilling contractor then spent another 2 months putting in US-manufactured engines, blowout preventers and mud system.

But rig construction as short as 3 months was back then. Nicklos Drilling placed its order ahead of other US contractors, according to its operations manager **Bill Brannan**, so "their delivery time probably would've stretched out somewhat."

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is, there's probably 200-300 rigs that need to be retired. The vast majority of these rigs were built in 1979 to 1982, and these rigs can't run forever.

And the rigs being built today are totally different from rigs built 25 years ago. People want better technology and safer rigs. Every industry has to upgrade at some point.

So while I believe that NOV is adding to capacity, NOV is also replacing capacity, and I don't think anybody has really defined that well enough yet.

Q: Is National Oilwell Varco working to increase its capacity?

A: Capacity is a dynamic around here. NOV is increasing capacity everyday by changing processes. Are we building new plants? Not necessarily. Are we increasing capacity? NOV does it on a daily basis.

Q: Some rig manufacturers and drilling contractors have turned to outside the US to bring in new rigs or components because of long lead times in the US. What do you think of that?

A: I don't know of anybody that can build them any faster in any other parts of the world.

You've got to make a determination what it is you want. If delivery time is the only thing that matters to you, then I would probably say you're making a mistake. NOV views competition all over the world, but NOV is all over the world too. So if someone's buying a rig from China, chances are pretty good they might be buying it from NOV because we manufacture in China as well as in the United States.

Q: What are the biggest challenges for a company like National Oilwell Varco in this kind of industry boom?

A: I think the biggest challenge is probably expectations. We've been in an industry where people haven't had to plan a lot, and now all of a sudden things are moving a little bit more rapidly, and instead of just picking up the phone and getting whatever they want, we have to plan a little bit more. I think the challenges are working together and ensuring that you have a realistic expectation on when you can receive something and getting it into the field.

Q: What is your outlook for the industry?

A: It's very positive. NOV is not overly worried about what goes on here in the lower 48. NOV is more in tune with what goes on internationally, and there are markets like Russia, the Middle East and North Africa that are much more vibrant than just what goes on domestically.

I think the future of the oil and gas business is very bright for international players. If you're just looking at the lower 48, while your outlook is still very positive, it could be much choppier. That's one of the reasons NOV has built a global footprint. NOV has 25,000 employees around the world, and NOV has done that so we can take advantage of the business wherever it is.

It's a great business, I enjoy it. You're up and you're down. There's challenges everyday, and that's just the way it is. We relish the opportunity to compete. We like what we're doing today, and we're excited about the business well into the future. ♠

BOMCO's delivery time estimate is now a year, Mr Hayes said.

"We can't keep up with the demand," he said. "Lead time has doubled."

Looking within the US, although most

regions are reporting full capacity, one manufacturer says his market has been overlooked: Arkansas.

Fabrication Specialities of Arkansas is quickly expanding and has clients in Texas, Oklahoma, Utah, Louisiana,

Tennessee and its home state of Arkansas. Owner **Gerald Graham** said his company is operating at about 60% of capacity and estimates delivery time to be 6-8 weeks.

"Our backlog has gone up at least 50% over last year, but we're still kind of an unknown market in Arkansas. Not that many people know about us. Many companies are talking about being booked a year out. So every time we find a new client, they jump right on it because we can get things done quicker."

THE EQUIPMENT HEADACHE

While operators are finding rigs hard – or impossible – to secure on short notice nowadays, rig manufacturers are finding their own equipment suppliers stretched as well. Lead times for components such as drawworks, mud pumps, bearings and drill pipe have been getting significantly longer than before.

Equipment suppliers "are absolutely the slowest part of the whole process," Mr Graham said.

Oklahoma-based manufacturer **GEFCO**, which makes the Speedstar line of portable drilling rigs, has close to 40 rigs on order and is booked into the second quarter of 2007.

"All of our suppliers were caught off guard by this boom because nobody was expecting it," said GEFCO representative **Jimmy Davis**. "Some of our bearing companies have told us they couldn't supply us anymore, and we bought last year. We bought a whole year's production, and we ran out in the first quarter of this year. So we're having to pay higher prices from distributors who might have the same items."

Yes, prices have been going up. Estimates given by different contractors and manufacturers range from 5% to double. But these increases are inevitable in this industry climate.

"My vendors are just passing on their net increase, and naturally I'm doing the same thing," Mr Cowan of MD Cowan said.

UNIQUE CHALLENGE

While capacity and component lead times are big headaches for most US manufacturers, for China's **BOMCO**, its biggest challenge has been fighting skepticism over the quality of its rigs.

"People always ask, 'Is the quality good?'" Mr Hayes said. "And I tell them, we have an engineering staff of more than 300 and hold 8 API certificates – more than anyone else. We also often invite drilling contractors to tour our plant in China so they can see how we work and compare the products themselves."

Mr Hayes also pointed out that **BOMCO** and **BOMA Drilltech** are teaming up with Houston-based **M&I Electric Industries** to make SCR and VFD drilling drives. The joint venture aims to take advantage of Chinese capacity and US technologies.

THE FUTURE

If there is one consensus among rig manufacturers, it's on their strong outlook for next year. With many companies already through half of next year and with orders still coming in, it looks like business will remain for the near term.

"I haven't seen any sign of saturation," Mr Hayes said. "I expect we'll get better year by year." ♦