

DRIL-QUIP INC
Form 10-K
February 27, 2019

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

FORM 10-K

(MARK ONE)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2018

or

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

For the transition period from _____ to _____
Commission file number 001-13439

DRIL-QUIP, INC.
(Exact name of registrant as specified in its charter)

Delaware	74-2162088
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

6401 N. Eldridge Parkway
Houston, Texas 77041
(Address of principal executive offices) (Zip code)
Registrant's telephone number, including area code: (713) 939-7711

Securities registered pursuant to Section 12(b) of the Act:
Title of Each Class Name of Each Exchange On Which Registered
Common Stock, \$.01 par value per share New York Stock Exchange
Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined by Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements

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incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 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 Accelerated filer
Non-Accelerated filer Smaller reporting company
Emerging growth company

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 Rule 12b-2 of the Exchange Act). Yes No

At June 29, 2018, the aggregate market value of the registrant's Common Stock held by non-affiliates of the registrant was approximately \$1,909,500,000 based on the closing price of such stock on such date of \$51.40.

At February 25, 2019, the number of shares outstanding of registrant's Common Stock was 36,387,703.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Proxy Statement for its 2019 Annual Meeting of Stockholders to be filed pursuant to Regulation 14A are incorporated by reference in Part III of this Form 10-K.

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FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K 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:

- future operating results and cash flow;
- scheduled, budgeted and other future capital expenditures;
- 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; and
- future operations, financial results, business plans and cash needs.

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 this report and the following:

- the volatility of oil and natural gas prices;
- the cyclical nature of the oil and gas industry;
- uncertainties associated with the United States and worldwide economies;
- uncertainties regarding political tensions in the Middle East, South America, Africa and elsewhere;
- current and potential governmental regulatory actions in the United States and regulatory actions and political unrest in other countries;
- uncertainties regarding future oil and gas exploration and production activities, including new regulations, customs requirements and product testing requirements;
- operating interruptions (including explosions, fires, weather-related incidents, mechanical failure, unscheduled downtime, labor difficulties, transportation interruptions, spills and releases and other environmental risks);
- project terminations, suspensions or scope adjustments to contracts reflected in the Company’s backlog;
- the Company’s reliance on product development;
- technological developments;

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the Company's reliance on third-party technologies;
acquisition and merger activities involving the Company or its competitors;
the Company's dependence on key employees and technical personnel;
increases in price or decreases in availability of raw materials;
impact of environmental matters, including future environmental regulations;
competitive products and pricing pressures;
fluctuations in foreign currency, including those attributable to the Brexit;
the ability of the Organization of Petroleum Exporting Countries (OPEC) to set and maintain production levels and pricing;
the Company's reliance on significant customers;
creditworthiness of the Company's customers;
fixed-price contracts;
changes in general economic, market or business conditions;
access to capital markets;
negative outcome of litigation, threatened litigation or government proceedings;
terrorist threats or acts, war and civil disturbances; and
changes to, and differing interpretations of, tax laws with respect to our operations and subsidiaries.

Many of such factors are beyond the Company's ability to control or predict. Any of the factors, or a combination of these factors, could materially affect the Company's future results of operations and the ultimate accuracy of the forward-looking statements. Management cautions against putting undue reliance on forward-looking statements or projecting any future results based on such statements or present or prior earnings levels. Every forward-looking statement speaks only as of the date of the particular statement, and the Company undertakes no obligation to publicly update or revise any forward-looking statement.

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PART I

Item 1. Business

General

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. Dril-Quip’s products are used by major integrated, large independent and foreign national oil and gas companies and drilling contractors throughout the world. The Company’s principal products consist of subsea and surface wellheads, subsea and surface production trees, subsea control systems and manifolds, mudline hanger systems, specialty connectors and associated pipe, drilling and production riser systems, liner hangers, wellhead connectors, diverters and safety valves. 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.

Dril-Quip has developed its broad line of subsea equipment, surface equipment and offshore rig equipment primarily through its internal product research and development efforts. The Company believes that it has achieved significant market share and brand name recognition with respect to its established products due to the technological capabilities, reliability, cost effectiveness and operational timesaving features of these 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 major manufacturing facilities in all three of its regional headquarter locations as well as in Macae, Brazil. The Company maintains additional facilities for fabrication and/or reconditioning and rework in Australia, Norway, Denmark, Nigeria, Indonesia, China, Ecuador, Egypt, Ghana, Hungary, Mexico, Qatar and Venezuela. The Company’s major operating subsidiaries are Dril-Quip (Europe) Limited, located in Aberdeen with branches in 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 (Nigeria) Ltd., located in Port Harcourt, Nigeria; Dril-Quip Egypt for Petroleum Services S.A.E., located in Alexandria, Egypt; 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.A. de C.V., located in Villahermosa, Mexico; TIW de Venezuela S.A., located in Anaco, Venezuela and with a registered branch located in Shushufindi, Ecuador; TIW (UK) Limited, located in Aberdeen, Scotland; TIW Hungary LLC, located in Szolnok, Hungary; and TIW International LLC, with a registered branch located in Singapore.

Dril-Quip markets its products through its offices and sales representatives located in the major international energy markets throughout the world. In 2018, the Company generated approximately 61% of its revenues from foreign sales compared to 55% and 66% in 2017 and 2016, respectively.

The Company makes available, free of charge on its website, its Annual Report on Form 10-K and quarterly reports on Form 10-Q (in both HTML and XBRL formats), current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practical after it electronically files such reports with, or furnishes them to, the Securities and Exchange Commission (SEC). The Company’s website address is www.dril-quip.com. Documents and information on the Company’s website, or on any other website, are not incorporated by reference into this Form 10-K. The SEC maintains a website (www.sec.gov) that contains reports the Company has filed with the SEC.

The Company also makes available free of charge on its website (www.dril-quip.com/govern.html) its:

• Corporate Governance Guidelines,

• Code of Business Conduct and Ethical Practices,

Audit Committee Charter,
Nominating and Governance Committee Charter, and
Compensation Committee Charter.

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Any stockholder, who so requests, may obtain a printed copy of any of these documents from the Company. Changes in or waivers to the Company's Code of Business Conduct and Ethical Practices involving directors and executive officers of the Company will be posted on its website.

Overview and Industry Outlook

Both 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. The level of capital expenditures has generally been dependent upon the prevailing view of future oil and gas prices, which are influenced by numerous factors affecting the supply and demand for oil and gas, including worldwide economic activity, interest rates and the cost of capital, environmental regulation, tax policies and the ability and/or desire of OPEC and other producing nations to set and maintain production levels and prices. The Brent crude oil price reached a high of \$115.19 per barrel in June 2014 and then began to drop sharply during 2015, and continued to drop in 2016, reaching a low of \$26.01 per barrel in the first quarter of 2016, before rebounding to end the year at \$54.96 per barrel. Oil prices began a slow recovery in 2017, with an average price of \$54.15 compared to an average price of \$43.67 in 2016. During 2018, crude oil prices fluctuated significantly, with a high of \$86.07 per barrel and ending the year at a low of \$50.57 per barrel. According to the December 2018 release of the Short-Term Energy Outlook published by the Energy Information Administration (EIA) of the U.S. Department of Energy, Brent Crude oil prices averaged approximately \$71.34 per barrel in 2018 and the price is forecasted to average \$61.00 per barrel in 2019 and \$65.00 per barrel in 2020.

On November 30, 2016, OPEC met and decided to cut production by approximately 1.2 million barrels per day. The reduced production helped to increase the average price per barrel between 2016 and 2017. Capital expenditures are also dependent on the cost of exploring for and producing oil and gas, the availability, expiration date and price of leases, the discovery rate of new oil and gas reserves, technological advances and alternative opportunities to invest in onshore exploration and production operations. Oil and gas prices and the level of drilling and production activity have historically been characterized by significant volatility. Future declines in oil and gas prices may further adversely affect the willingness of some oil and gas companies to make capital expenditures on exploration, drilling and production operations, which could have an adverse impact on the Company's results of operations, financial position and cash flows. In its December 2018 Short-Term Energy Outlook, the EIA projected United States crude oil production averaged an estimated 10.9 million barrels per day in 2018, with an average of 11.5 million barrels per day in the month of November, and is forecasted to average 12.1 million barrels per day in 2019.

Brent crude oil prices per barrel for the three-year period ended December 31, 2018 are summarized below:

	Brent Crude Oil Prices		
	2018	2017	2016
High	\$86.07	\$66.80	\$54.96
Low	50.57	43.98	26.01
Average	71.34	54.15	43.67
Closing, December 31,	\$50.57	\$66.73	\$54.96

The volatility in Brent crude oil prices over the past three years continues to have a significant effect on major integrated, large independent and foreign national oil and gas companies' capital expenditure budgets. The Company expects continued pressure in both crude oil and natural gas prices, as well as in the level of drilling and production related activities, particularly as they relate to offshore activities. Even during periods of high prices for oil and natural gas, companies exploring for oil and gas may cancel or curtail programs, seek to renegotiate contract terms, including the price of products and services, or reduce their levels of capital expenditures for exploration and production for a variety of reasons. Lower drilling and production activity had a negative impact on the Company's results for the year ended December 31, 2018 and is expected to improve slightly in 2019. A prolonged delay in the recovery of commodity prices could also lead to further material impairment charges to tangible or intangible assets or otherwise result in a material adverse effect on the Company's results of operations. See "Item 1A. Risk Factors—A material or

extended decline in expenditures by the oil and gas industry could significantly reduce our revenue and income.”

Recent Developments

As a result of continued unfavorable offshore market conditions and low commodity prices, the Company engaged in a strategic review with a third-party firm in 2018. In conjunction with the strategic review, the Company adjusted its forecast for recovery to reflect a more delayed recovery in the offshore industry, with pre-downturn demand not returning until after 2025.

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Additionally, the Company pursued a global transformation, which includes a reduction in workforce, realignment of facilities and restructuring of operations. We expect this transformation to allow us to maintain our global footprint in key markets, while supporting an integrated supply chain model that we expect to create more flexibility and allow us to continue serving our customers. The Company expects to complete the strategic restructuring by the end of 2019.

Products and Services

Dril-Quip's revenues are generated from two sources: products and services. Product revenues are derived from the sale of drilling and production equipment. Service revenues are earned when the Company provides technical advisory assistance and rental tools during installation and retrieval of the Company's products. Additionally, the Company earns service revenues when rework and reconditioning services are provided. In 2018, the Company derived 69% of its revenues from the sale of its products, 19% of its revenues from services and 12% of its revenues from leasing rental tools, compared to 77%, 14% and 9% for products, services and leasing rental tools in 2017, respectively, and 80%, 12% and 8% for products, services and leasing rental tools in 2016, respectively. Service and leasing revenues generally correlate to revenues from product sales because increased product sales typically generate increased demand for technical advisory assistance services during installation and rental of running tools. However, existing customer equipment can be used in certain circumstances, which creates demand for services with no correlating product sales. The Company has substantial international operations, with approximately 61% of its revenues derived from foreign sales in 2018, 55% in 2017 and 66% in 2016. Substantially all of the Company's domestic revenue relates to operations in the U. S. Gulf of Mexico. Domestic revenue approximated 39% of the Company's total revenues in 2018, 45% in 2017 and 34% in 2016.

Product contracts are typically 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 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 as a result of 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, maintenance of market share, the introduction of new products and general market conditions.

Products

Dril-Quip designs, manufactures, fabricates, inspects, assembles, tests and markets subsea equipment, surface equipment and offshore rig equipment. The Company's products are used primarily to explore for oil and gas from offshore drilling rigs, such as floating rigs and jack-up rigs, and for drilling and production of oil and gas wells on offshore platforms, tension leg platforms (TLPs), Spars and moored vessels such as FPSOs. TLPs are floating production platforms that are connected to the ocean floor via vertical mooring tethers. A Spar is a floating cylindrical structure approximately six or seven times longer than its diameter and is anchored in place. FPSOs are floating production, storage and offloading monohull moored vessels. The TIW products are used in the drilling and production for oil and gas both onshore and offshore.

Subsea Equipment. Subsea equipment is used in the drilling and production of offshore oil and gas wells around the world. Included in the subsea equipment product line are subsea wellheads, mudline hanger systems, specialty connectors and associated pipe, production riser systems, subsea production trees, liner hangers, safety valves, subsea control systems and subsea manifolds.

Subsea wellheads are pressure-containing vessels that are sometimes referred to as a "wellhead housing" and are made from forged and machined steel. A casing hanger, also made of steel, lands inside the wellhead housing and suspends casing (pipe) downhole. As drilling depth increases, successively smaller diameter casing strings are installed, each suspended by an independent casing hanger. Subsea wellheads are utilized when drilling from floating drilling rigs, either semi-submersible or drillship types, or TLPs and Spars. The Company's flagship subsea wellhead, called the

SS-15® Subsea Wellhead System, is rated for 15,000 psi internal pressure and is offered to the industry in a variety of configurations. The Company's newest wellhead product, the SS-20™ BigBore™ II-e Subsea Wellhead System, is designed to contain higher pressures (20,000 pounds per square inch (psi)) and provides the ability to reduce the number of casing strings in the well design by increasing load carrying and pressure capacities of casing hangers and associated installation tools.

Mudline hanger systems are used in jack-up drilling operations to support the weight of the various casing strings at the ocean floor while drilling a well. They also provide a method to disconnect the casing strings in an orderly manner at the ocean floor after the well has been drilled, and subsequently reconnect to enable production of the well by either tying it back vertically to a subsequently installed platform or by installing a shallow water subsea tree.

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Large diameter weld-on specialty connectors (threaded or stab type) are used primarily in offshore wells drilled from floating drilling rigs, jack-up rigs, fixed platforms, TLPs and Spars. Specialty connectors join lengths of conductor or large diameter (16-inch or greater) casing. Specialty connectors provide a more rapid connection than other methods of connecting lengths of pipe. Connectors may be sold individually or as an assembly after being welded to sections of Company or customer supplied pipe. Dril-Quip's weld-on specialty connectors are designed to prevent cross threading and provide a quick, convenient method of joining casing joints with structural integrity compatible with casing strength.

Production riser systems are generally designed and manufactured to customer specifications. Production risers provide a vertical conduit from the subsea wellhead up to a TLP, Spar or FPSO floating at the surface.

A subsea production tree is an assembly composed of valves, a wellhead connector, control equipment and various other components installed on a subsea wellhead or a mudline hanger system and used to control the flow of oil and gas from a producing well. Subsea trees may be used as stand alone satellite wells or multiple well template mounted and cluster arrangements. These types typically produce via a subsea gathering system of manifolds and flowlines to a central control point located on a platform, TLP, Spar or FPSO. The use of subsea production trees has become an increasingly important method for producing wells located in hard-to-reach deepwater areas or economically marginal fields located in shallower waters. The Company is an established manufacturer of complicated dual-bore production trees. In addition, Dril-Quip manufactures a patented single bore (SingleBore™) subsea completion system which features a hydraulic valve mechanism instead of a wireline-installed mechanism that allows the operator to plug the tubing hanger annulus remotely from the surface via a hydraulic control line and subsequently unplug it when the well is put on production. This mechanism eliminates the need for an expensive multibore installation and workover riser, thereby saving both cost and installation time. The patented horizontal bore (HorizontalBore™) subsea production component accommodates numerous completion configuration possibilities and features large vertical access drill-through for passage of drill-bits, submersible pumps, coil tubing strings and Dril-Quip's slimline casing hanger system. Dril-Quip's subsea production trees are used in ultra-deepwater applications. These trees feature remote flowline and control connections, utilizing remotely operated intervention tools. The Company's subsea production trees are generally custom designed and manufactured to customer specifications.

A subsea control system provides control of subsea trees, manifolds, ocean floor process equipment and pipeline protection equipment. Dril-Quip has developed a variety of subsea control systems, including fiber optic based multiplex control systems that provide real time access to tree functions and tree equipment status. The control system can be packaged for shallow water or deepwater applications. Dril-Quip also manufactures control systems used in the installation, retrieval and workover of production equipment.

A subsea manifold is a structure located on the ocean floor consisting of valves, flowline connections and a control module used to collect and control the flow of oil and gas from subsea wells for delivery to a floating production unit or terminal.

Downhole Tools. Downhole tools are primarily comprised of liner hangers, production packers, safety valves and specialty downhole tools. A liner hanger is used to hang-off and seal casing into a previously installed casing string in the well bore, and can provide a means of tying back the liner for production to surface. Dril-Quip has developed a state-of-the-art liner hanger system and has installed its liner hangers in a number of difficult well applications, resulting in improved industry recognition and market opportunities. In addition to liner hanger systems that are well suited for onshore use, TIW offers expandable liner hanger systems that are typically utilized in challenging environments such as deepwater or High Pressure, High Temperature (HPHT) applications.

A safety valve is used to provide a quick, sure shutoff in the drill string at the drill floor and prevent flow up the drill pipe. The TIW Kelly Valve is located in the drill string below the kelly, the uppermost component of the drill string, and is designed to be closed under pressure to remove the kelly.

Surface Equipment. Surface equipment is principally used for flow control on offshore production platforms, TLPs and Spars. Included in the Company's surface equipment product line are platform wellheads, platform production trees and riser tensioners. Dril-Quip's development of platform wellheads and platform production trees was facilitated by adaptation of its existing subsea wellhead and tree technology to surface wellheads and trees.

Platform wellheads are pressure-containing forged and machined metal housings in which casing hangers are landed and sealed at the platform deck to suspend casings. The Company emphasizes the use of metal-to-metal sealing wellhead systems with operational time-saving features which can be used in high pressure, high temperature and corrosive drilling and production applications.

After installation of a wellhead, a platform production tree, consisting of gate valves, a surface wellhead connector, controls, tree cap and associated equipment, is installed on the wellhead to control and regulate oil or gas production. Platform production trees are similar to subsea production trees but utilize less complex equipment and more manual, rather than

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hydraulically actuated, valves and connectors. Platform wellheads and platform production trees and associated equipment are designed and manufactured in accordance with customer specifications.

Riser tensioners are used on a floating drilling/production vessel to provide a continuous and reliable upward force on a riser string that is independent of the movement of the floating vessel.

Offshore Rig Equipment. Offshore rig equipment includes drilling riser systems, wellhead connectors and diverters. The drilling riser system consists of (i) lengths of riser pipe and associated riser connectors that secure one to another; (ii) the telescopic joint, which connects the entire drilling riser system to the diverter at top of the riser at the rig and provides a means to compensate for vertical motion of the rig relative to the ocean floor; and (iii) the wellhead connector, which provides a means for remote connection and disconnection of the blowout preventer stack to or from the wellhead. Diverters are used to provide protection from shallow gas blowouts and to divert gases off of the rig during the drilling operation.

Wellhead connectors are used on production riser systems and drilling riser systems. They are also used on both TLPs and Spars, which are installed in deepwater applications. The principal markets for offshore rig equipment are new rigs, rig upgrades, TLPs and Spars. Drilling risers, wellhead connectors and diverters are generally designed and manufactured to customer specifications.

Certain of the Company's products are used in potentially hazardous drilling, completion and production applications that can cause personal injury, product liability and environmental claims. See "Item 1A. Risk Factors—Our business involves numerous operating hazards that may not be covered by insurance. The occurrence of an event not fully covered by insurance could have a material adverse effect on our results of operations, financial position and cash flows."

Services

The Company provides services to customers, including technical advisory assistance as well as rework and reconditioning services on its customer-owned products. These services are provided from the Company's worldwide locations and represented approximately 19% of revenues in 2018 compared to 14% in 2017 and 12% in 2016.

Technical Advisory Assistance. Dril-Quip generally does not install products for its customers, but it does provide technical advisory assistance to the customer, if requested, in the installation of its products. The customer is not obligated to utilize these services and may use its own personnel or a third party to perform these services. Technical advisory assistance services performed by the Company are negotiated and sold separately from the Company's products. These services are not a prerequisite to the sale of the Company's products as its products are fully functional on a stand alone basis. The Company's technicians provide assistance in the onsite installation of the Company's products and are available on a 24-hour call out from the Company's facilities located in Houston, Texas; Midland, Texas; Oklahoma City, Oklahoma; Youngsville, Louisiana; Villahermosa, Mexico; Anaco, Venezuela; Shushufindi, Ecuador; Macae, Brazil; Aberdeen, Scotland; Szolnok, Hungary; Stavanger, Norway; Esbjerg, Denmark; Port Harcourt, Nigeria; Alexandria, Egypt; Takoradi, Ghana; Tianjin, China; Doha, Qatar; Singapore; and Perth, Australia. Reconditioning. The Company provides reconditioning of its customer-owned products at its facilities in Houston, Texas; Macae, Brazil; Aberdeen, Scotland; Stavanger, Norway; Esbjerg, Denmark; Port Harcourt, Nigeria; Alexandria, Egypt; Takoradi, Ghana; Balikpapan, Indonesia; Tianjin, China; Doha, Qatar; Singapore; and Perth, Australia. The Company does not typically service, repair or recondition its competitors' products.

Leasing

The Company rents running and installation tools for use in installing its products. These tools are required to install and retrieve the Company's products that are purchased by customers. Rental or purchase of running tools is not a condition of the sale of the Company's products and is contracted for separately from product sales and other services offered by the Company. Running tools are available from Dril-Quip's locations in Houston, Texas; Midland, Texas; Oklahoma City, Oklahoma; Youngsville, Louisiana; Villahermosa, Mexico; Anaco, Venezuela; Shushufindi, Ecuador; Macae, Brazil; Aberdeen, Scotland; Szolnok, Hungary; Stavanger, Norway; Esbjerg, Denmark; Beverwijk, Holland; Singapore; and Perth, Australia. These rentals are provided from the Company's worldwide locations and represented approximately 12% of revenues in 2018 compared to 9% in 2017 and 8% in 2016.

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Manufacturing

Dril-Quip has major manufacturing facilities in Houston, Texas; Aberdeen, Scotland; Singapore; and Macae, Brazil. See “Item 2. Properties—Manufacturing Facilities.” Dril-Quip maintains its high standards of product quality through the implementation of Advanced Product Quality Planning (APQP) methodologies, as well as through the use of quality control specialists.

The Company’s Houston, Aberdeen, Singapore and Macae manufacturing plants are ISO 14001, OHSAS 18001 and ISO 9001 certified. The Houston, Aberdeen, Singapore and Macae plants are also licensed to applicable American Petroleum Institute (API) product specifications and are API Q1, 9th edition and APIQ2 compliant. The Metallurgical Laboratory at the Houston operations is ISO 17025 certified for Crack Tip Opening Displacement, Hardness, Tensile and Charpy V-Notch testing. Dril-Quip works to maintain its high standards of product quality through the use of precision measuring equipment such as Gage Masters, Faro Arms, Coordinate Measuring Machine and the application of APQP. APQP entails concurrent engineering principles to identify and address potential quality concerns early in the product development process. The Company has the capability to manufacture its products globally and continues to have local capability in key critical markets.

The Company’s primary raw material is cast steel ingots, from which it produces steel shaped forgings at its forging and heat treatment facility in Houston, Texas. The Company routinely purchases steel ingots from multiple suppliers on a purchase order basis and does not have any long-term supply contracts. The Company’s Houston facility has the capability to provide forgings and heat treatment for its Houston, Aberdeen, Singapore and Macae facilities.

Prolonged periods of low demand in the market for drilling and production equipment could have a greater effect on the Company than on certain of its competitors that have not made such large capital investments in their facilities.

Dril-Quip’s manufacturing facilities utilize state-of-the-art computer numerically controlled (CNC) machine tools and equipment, which contribute to the Company’s product quality and timely delivery. The Company has also developed a cost effective, in-house machine tool rebuild and refurbishment capability, which produces machine upgrades with customized features to enhance the economic manufacturing of its specialized products. This strategy provides the added advantage of in-house expertise for repairs and maintenance of these machines.

Customers

The Company’s principal customers are major integrated, large independent and foreign national oil and gas companies. Drilling contractors and engineering and construction companies also represent a portion of the Company’s customer base. The Company’s customers are generally oil and gas companies that are well-known participants in exploration and production.

The Company is not dependent on any one customer or group of customers. In 2018, the Company’s top 15 customers represented approximately 56% of total revenues, and BP and its affiliated companies accounted for approximately 13% of total revenues. In 2017 and 2016, the Company’s top 15 customers represented approximately 49% and 75% of total revenues, respectively, and Chevron and its affiliated companies accounted for approximately 14% and 16% of total revenues, respectively. No other customer accounted for more than 10% of total revenues in 2018, 2017 or 2016.

The number and variety of the Company’s products required in a given year by any one customer depends upon the amount of that customer’s capital expenditure budget devoted to exploration and production and on the results of competitive bids for major projects. Consequently, a customer that accounts for a significant portion of revenues in one fiscal year may represent an immaterial portion of revenues in subsequent years. While the Company is not dependent on any one customer or group of customers, the loss of one or more of its significant customers could, at least on a short-term basis, have an adverse effect on the Company’s results of operations.

Backlog

Backlog consists of firm customer orders of Dril-Quip products for which a purchase order, signed contract or letter of award has been received, satisfactory credit or financing arrangements exist and delivery is scheduled. Historically, the Company’s revenues for a specific period have not been directly related to its backlog as stated at a particular point in time. The Company’s product backlog was approximately \$270.0 million and \$207.3 million at December 31, 2018 and 2017, respectively. The backlog at the end of 2018 represents an increase of approximately \$62.7 million, or 30%, from the end of 2017. The Company’s backlog balance during 2018 was negatively impacted by translation

adjustments of approximately \$3.1 million, due primarily to the weakening of the Brazilian Real against the U.S. dollar, and approximately \$11.7 million in cancellations.

During the first quarter of 2018, Dril-Quip Asia-Pacific Pte Ltd. was awarded a contract to supply top-tensioned riser (TTR) systems and related services for the development of the Ca Rong Do Project (CRD Project) located offshore Vietnam operated by Repsol with the participation of Mubadala, PVEP and PetroVietnam. The CRD Project is included within the backlog balance presented in the accompanying consolidated financial statements; however, due to ongoing territorial discussions between China and Vietnam, the CRD Project may experience continued delays or cancellation.

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The Company expects to fill approximately 70% to 80% of the December 31, 2018 product backlog by December 31, 2019. The remaining backlog at December 31, 2018 consists of longer-term projects which are being designed and manufactured to customer specifications requiring longer lead times. In August 2012, the Company's Brazilian subsidiary, Dril-Quip do Brasil LTDA, was awarded a four-year contract by Petrobras, Brazil's national oil company. The contract was valued at \$650.0 million, net of Brazilian taxes, at exchange rates in effect at that time (approximately \$342.2 million based on the December 31, 2018 exchange rate of 3.8748 Brazilian real to 1.00 U.S. dollar) if all the equipment under the contract was ordered. Amounts are included in the Company's backlog as purchase orders or letters of award are received. As of December 31, 2018, the Company's backlog included \$9.3 million of purchase orders under this Petrobras contract. As part of an amendment to extend the term of the contract, Petrobras agreed to issue purchase orders totaling a minimum of approximately \$25.3 million (based on current exchange rates) before 2019. As of December 31, 2018, Petrobras has issued a total of three purchase orders (one during each year of 2016, 2017 and 2018) totaling the committed amount. The Company cannot provide assurance that Petrobras will order all of the equipment under the contract. See "Item 1A. Risk Factors—Our backlog is subject to unexpected adjustments and cancellations and is, therefore, an uncertain indicator of our future revenues and earnings."

Marketing and Sales

Dril-Quip markets its products and services throughout the world directly through its sales personnel in multiple domestic and international locations. In addition, in certain foreign markets the Company utilizes independent sales agents or representatives to enhance its marketing and sales efforts.

Some of the locations in which Dril-Quip has sales agents or representatives are Trinidad, Indonesia, Malaysia, Saudi Arabia and United Arab Emirates. Although they do not have authority to contractually bind the Company, these representatives market the Company's products in their respective territories in return for sales commissions. The Company advertises its products and services in trade and technical publications targeted to its customer base. The Company also participates in industry conferences and trade shows to enhance industry awareness of its products. The Company's customers generally order products on a purchase order basis. Orders, other than those considered to be long-term projects, are typically filled within twelve months after receipt, depending on the type of product and whether it is sold out of inventory or requires some customization. Contracts for certain of the Company's larger, more complex products, such as subsea production trees, drilling risers and equipment for TLPs and Spars, can take a year or more to complete.

The primary factors influencing a customer's decision to purchase the Company's products are the quality, reliability and reputation of the product, price, technology, service and timely delivery. For large drilling and production system orders, project management teams coordinate customer needs with the Company's engineering, manufacturing and service organizations, as well as with subcontractors and vendors.

A portion of the Company's business consists of designing, manufacturing and selling equipment, as well as offering technical advisory assistance during installation of the equipment, for major projects pursuant to competitive bids. The number of such projects in any year may fluctuate. The Company's profitability on such projects is critically dependent on making accurate and cost effective bids and performing efficiently in accordance with bid specifications. Various factors, including availability of raw materials, changes in customer requirements and governmental regulations, can adversely affect the Company's performance on individual projects, with potential material adverse effects on project profitability.

Product Development and Engineering

The technological demands of the oil and gas industry continue to increase as exploration and drilling expand into more hostile environments. Conditions encountered in these environments include water depths in excess of 10,000 feet, well pressures exceeding 15,000 psi, well flowing temperatures beyond 350°F (Fahrenheit) and mixed flows of oil, gas and water that may also be highly corrosive and impact material properties.

Since its founding in 1981, Dril-Quip has actively engaged in continuing development efforts to generate new products and improve existing products. When developing new products, the Company typically seeks to design the most technologically advanced version for a particular application to establish its reputation and qualification in that product. Thereafter, the Company leverages its expertise in the more technologically advanced product to produce less

costly and complex versions of the product for less demanding applications. The Company also focuses its activities on reducing the overall cost to the customer, which includes not only the initial capital cost but also operating, installation and maintenance costs associated with its products.

In the 1980s, the Company introduced its first product, specialty connectors, as well as mudline suspension systems, template systems and subsea wellheads. In the 1990s, the Company introduced a series of new products, including diverters, wellhead connectors, SingleBore™ subsea trees, improved severe service dual bore subsea trees, subsea and platform valves, platform wellheads, platform trees, subsea tree workover riser systems, drilling riser systems and TLP and Spar production riser systems. Since 2000, Dril-Quip has introduced multiple new products, including liner hangers, subsea control systems, subsea

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manifolds, riser tensioners, and enhanced versions of subsea wellhead connectors and Dril-Quip's industry leading subsea wellhead system(s).

Historically, Dril-Quip's product development work is primarily conducted at its facilities in Houston, Texas; however, such activities have gradually increased in other regions, such as Aberdeen, Scotland, Singapore and Brazil. In addition to the work of its product development staff, the Company's application engineering staff provides technical services to customers in connection with the design and sales of its products. The Company's ability to develop new products and maintain technological advantages is important to its future success. See "Item 1A. Risk Factors-Our business could be adversely affected if we do not develop new products and secure and retain patents related to our products."

The Company believes that the success of its business depends more on the technical competence, creativity and marketing abilities of its employees than on any individual patent, trademark or copyright. Nevertheless, as part of its ongoing product development and manufacturing activities, Dril-Quip's policy has been to seek patents when appropriate on inventions concerning new products and product improvements. All patent rights for products developed by employees are assigned to the Company and almost all of the Company's products have components that are covered by patents.

In 2018, major production milestones were met for several key global projects. In the North Sea, the last of an initial 18 subsea completion trees for a subsea field development project was successfully installed. Following the success of the aforementioned project, Dril-Quip was awarded a front-end engineering and design contract for a subsea production system project located off the coast of South America. Additionally, subsea trees were delivered and installed for a field development project off the coast of Gabon. Also, off the coast of Trinidad, multiple deepwater subsea wellhead systems were installed with the support of a service facility in Trinidad, continuing Dril-Quip's aftermarket support presence in the region established the previous year. With the completion of engineering, manufacturing, assembly and testing of dry tree equipment, Dril-Quip was able to support the tieback of multiple wells for projects in the Gulf of Mexico. Engineering, manufacturing, assembly and test work continued on additional dry tree projects in the Company's backlog. The requirements of the equipment in these projects represent significant technological challenges, the development of which is serving to enhance the Company's overall engineering capabilities.

Dril-Quip's continued efforts in developing technologically advanced products enable Dril-Quip to offer products for the harshest environments. The latest subsea wellhead system has been accepted by a major oil company for its high pressure, high temperature applications, further strengthening Dril-Quip's position in the subsea market.

In an ongoing test program, the Company continued the utilization of its recently constructed high-load horizontal test machine and fatigue test machine for rigorous validation testing of its existing specialty connector product line. Active engineering programs have been initiated in-house to continue development in specialty connector product enhancements as well as new product development. This high-load horizontal test machine has been instrumental in the development and qualification of our latest 20,000 psi wellhead system and riser connector that utilize Dril-Quip proprietary locking and sealing profiles. Engineering development efforts are on-going in subsea production systems. In early 2016, the Company announced that it is establishing a research and development facility in Singapore that focuses on materials and products suitable for HPHT applications. The new facility serves as an additional hub for research and development activities for the Company.

Dril-Quip has numerous U.S. registered trademarks, including Dril-Quip®, Quik-Thread®, Quik-Stab®, Multi-Thread®, MS-15®, SS-15®, SS-10®, SU-90®, DX® and TIW®. The Company has registered its trademarks in the countries where such registration is deemed material.

Although in the aggregate, the Company's patents and trademarks are of considerable importance to the manufacturing and marketing of many of its products, the Company does not consider any single patent or trademark or group of patents or trademarks to be material to its business as a whole, except the Dril-Quip® trademark. The Company also relies on trade secret protection for its confidential and proprietary information. The Company routinely enters into confidentiality agreements with its employees and suppliers. There can be no assurance, however, that others will not independently obtain similar information or otherwise gain access to the Company's trade secrets.

Competition

Dril-Quip faces significant competition from other manufacturers and suppliers of exploration and production equipment. Several of its primary competitors are diversified multinational companies with substantially larger operating staffs and greater capital resources than those of the Company and which, in many instances, have been engaged in the manufacturing business for a much longer period of time than the Company. The Company competes principally with the petroleum production equipment segments of Baker Hughes, a GE Company; Schlumberger, Ltd.; TechnipFMC plc; and Aker Solutions.

Because of their relative size and diversity of products, several of the Company's competitors have the ability to provide "turnkey" services for drilling and production applications, which enables them to use their own products to the exclusion of

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Dril-Quip's products. See "Item 1A. Risk Factors—We may be unable to successfully compete with other manufacturers of drilling and production equipment." The Company also competes to a lesser extent with a number of other companies in various products. The principal competitive factors in the petroleum drilling and production equipment markets are quality, reliability and reputation of the product, price, technology, service and timely delivery.

Employees

The total number of the Company's employees as of December 31, 2017 was 2,019. Of those 2,019 employees, 1,095 were located in the United States. As a result of worldwide reductions in workforce and natural attrition, the total number of the Company's employees as of December 31, 2018 was 1,926, a 5% reduction from December 31, 2017. Of those 1,926 employees, 946 were located in the United States. As a result of the Company's ongoing efforts to control costs, we expect to reduce approximately 15% of our workforce in 2019, resulting in \$7.3 million in severance costs being recognized in the year ended December 31, 2018. Substantially all of the Company's employees are not covered by collective bargaining agreements, and the Company considers its employee relations to be good.

The Company's operations depend in part on its ability to attract quality employees. While the Company believes that its wage and salary rates are competitive and that its relationship with its labor force is good, a significant increase in the wages and salaries paid by competing employers could result in a reduction of the Company's labor force, increases in the wage and salary rates paid by the Company or both. If either of these events were to occur, in the near-term, the profits realized by the Company from work in progress would be reduced and, in the long-term, the production capacity and profitability of the Company could be diminished and the growth potential of the Company could be impaired. See "Item 1A. Risk Factors—Loss of our key management or other personnel could adversely impact our business."

Governmental Regulations

Many aspects of the Company's operations are affected by political developments and are subject to both domestic and foreign governmental regulations, including those relating to oilfield operations, the discharge of materials into the environment from our manufacturing or other facilities, health and worker safety aspects of our operations, or otherwise relating to human health and environmental protection. In addition, the Company depends on the demand for its services from the oil and gas industry and, therefore, is affected by changing taxes, price controls and other laws and regulations relating to the oil and gas industry in general, including those specifically directed to onshore and offshore operations. The adoption of laws and regulations curtailing 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 the Company's products. See "Item 1A. Risk Factors—Our operations and our customers' operations are subject to a variety of governmental laws and regulations that may increase our costs, limit the demand for our products and services or restrict our operations."

In recent years, increased concern has been raised over the protection of the environment. Legislation to regulate emissions of greenhouse gases has been introduced, but not enacted, in the U.S. Congress, and there has been a wide-ranging policy debate, both nationally and internationally, regarding the impact of these gases and possible means for their regulation. In addition, efforts have been made and continue to be made in the international community toward the adoption of international treaties or protocols that would address global climate change issues, such as the annual United Nations Climate Change Conferences. In November 2015, the United Nations Climate Change Conference (COP21) was held in Paris with the objective to achieve a legally binding and universal agreement on climate, with the aim of keeping global warming below 20 C (Celsius), from all nations, regardless of size. The Paris Agreement, signed by the U.S. on April 22, 2016, requires countries to review and "represent a progression" in their nationally determined contributions, which set greenhouse gas emission reduction goals, every five years. However, in August 2017, the United States informed the United Nations of its intent to withdraw from the Paris Agreement. The earliest possible effective withdrawal date from the Paris Agreement is November 2020. Also, the U.S. Environmental Protection Agency (EPA) has undertaken efforts to collect information regarding greenhouse gas emissions and their effects. Following a finding by the EPA that certain greenhouse gases represent a danger to human health, the EPA expanded its regulations relating to those emissions and adopted rules imposing permitting and reporting obligations. The results of the permitting and reporting requirements could lead to further regulation of these

greenhouse gases by the EPA. Moreover, specific design and operational standards apply to U.S. outer continental shelf vessels, rigs, platforms, vehicles, structures and equipment.

The U.S. Bureau of Safety and Environmental Enforcement (BSEE) regulates the design and operation of well control and other equipment at offshore production sites, among other requirements. BSEE has adopted stricter requirements for subsea drilling production equipment. In April 2016, BSEE published a final blowout preventer systems and well control rule, which focuses on blowout preventer requirements and includes reforms in well design, well control, casing, cementing, real-time monitoring and subsea containment, among other things. BSEE also finalized a rule in September 2016 concerning production safety systems for oil and natural gas operations on the Outer Continental Shelf. However, in December 2017, BSEE published a proposed rule that would revise a number of the requirements in the September 2016 rule. The final rule implementing these revisions was published in September 2018. In addition, in May 2018, BSEE published a proposed rule that would revise

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several requirements of the blowout preventer systems and well control rule. A final rule has not yet been issued. In addition, drilling in certain areas has been opposed by environmental groups and, in certain areas, has been restricted. For example, in December 2016, the Obama administration banned offshore drilling in portions of the Arctic and Atlantic oceans. Although the Trump administration announced a proposal in January 2018 to open most U.S. coastal waters to offshore drilling, several coastal states have taken steps to prohibit offshore drilling. For example, California passed laws in September 2018 barring the construction of new oil drilling-related infrastructure in state waters. Similarly, in November 2018, voters in Florida approved an amendment to the state constitution that would ban oil and gas drilling in offshore state waters. Further, in December 2018, environmental groups challenged incidental harassment authorizations issued by the National Marine Fisheries Service that allow companies to conduct air gun seismic surveys for oil and gas exploration off the Atlantic coast. The attorneys general for nine coastal states also sought to intervene as plaintiffs. To the extent that new laws or other governmental actions prohibit or restrict drilling or impose additional environmental protection requirements that result in increased costs to the oil and gas industry in general and the drilling industry in particular, the business of the Company could be adversely affected. Similarly, restrictions on authorizations needed to conduct seismic surveys could impact our customers' ability to identify oil and gas reserves, thereby reducing demand for our products. The Company cannot determine to what extent its future operations and earnings may be affected by new legislation, new regulations or changes in existing regulations. See "Item 1A. Risk Factors—Our business and our customers' businesses are subject to environmental laws and regulations that may increase our costs, limit the demand for our products and services or restrict our operations."

Our operations are also governed by laws and regulations related to workplace safety and worker health, such as the Occupational Safety and Health Act and regulations promulgated thereunder.

Based on the Company's experience to date, the Company does not currently anticipate any material adverse effect on its business or consolidated financial position as a result of future compliance with existing environmental, health and safety laws. However, future events, such as changes in existing laws and regulations or their interpretation, more vigorous enforcement policies of or by regulatory agencies, or stricter or different interpretations of existing laws and regulations, may require additional expenditures by the Company, which may be material.

Executive Officers of the Registrant

Pursuant to Instruction 3 to Item 401(b) of Regulation S-K and General Instruction G(3) to Form 10-K, the following information is included in Part I of this Form 10-K:

The following table sets forth the names, ages (as of February 20, 2019) and positions of the Company's executive officers:

Name	Age	Position
		President, Chief
Blake T. DeBerry	59	Executive Officer and Director Senior Vice
James A. Garipey	61	President and Chief Operating Officer Vice
Jeffrey J. Bird	52	President and Chief Financial Officer

James C. Webster 49 Vice
President,
General
Counsel
and
Secretary

Blake T. DeBerry has been President and Chief Executive Officer and a member of the Board of Directors of the Company since October 2011. Mr. DeBerry was Senior Vice President—Sales and Engineering from July 2011 until October 2011, and was Vice President—Dril-Quip Asia Pacific (which covers the Pacific Rim, Asia, Australia, India and the Middle East) from March 2007 to July 2011. He has been an employee of the Company since 1988 and has held a number of management and engineering positions in the Company's domestic and international offices. Mr. DeBerry holds a Bachelor of Science degree in mechanical engineering from Texas Tech University.

James A. Gariepy is Senior Vice President and Chief Operating Officer, positions he has held since October 2011. Mr. Gariepy was Senior Vice President—Manufacturing, Project Management and Service from July 2011 until October 2011, and was Vice President—Dril-Quip Europe (which covers Europe, Africa and Northern Eurasia) from March 2007 to July 2011. He has held domestic and international management positions since joining the Company in 2004. Mr. Gariepy holds a Bachelor of Science degree in mechanical engineering from the Lawrence Technological University and an MBA from the University of St. Thomas.

Jeffrey J. Bird is Vice President and Chief Financial Officer, positions he has held since he joined the Company in March 2017. From December 2014 through February 2017, he was Executive Vice President and Chief Financial Officer of Frank's International, a provider of engineered tubular services to the oil and gas industry. Prior to joining Frank's International, Mr. Bird was the Vice President of Finance and Chief Financial Officer of Ascend Performance Materials, a provider of chemicals, fibers and plastics in Houston, Texas, from September 2010. Prior to joining Ascend, Mr. Bird served in a variety of

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accounting and finance roles, primarily in the industrial manufacturing sector including serving as a division Chief Financial Officer at Danaher Corporation. Mr. Bird holds a BA in Accounting from Cedarville University in Ohio. James C. Webster is Vice President, General Counsel and Secretary. He joined the Company in February 2011 as Vice President and General Counsel and was elected to the additional position of Secretary in May 2011. From September 2005 until September 2010, he was Vice President, General Counsel and Secretary of M-I SWACO, at the time, a joint venture between Smith International, Inc. and Schlumberger Ltd., and then was an area general counsel for Schlumberger from September 2010 to February 2011 following Schlumberger's acquisition of Smith International. From 1999 to September 2005, he was an associate with, and later a partner in, the law firm of Gardere Wynne Sewell LLP (now part of Foley & Lardner LLP) in Houston. Mr. Webster holds an economics degree from the University of Arizona and a joint Law/MBA from Loyola University.

Item 1A. Risk Factors

In this Item 1A., the terms "we," "our," "us" and "Dril-Quip" used herein refer to Dril-Quip, Inc. and its subsidiaries unless otherwise indicated or as the context so requires.

A material or extended decline in expenditures by the oil and gas industry could significantly reduce our revenue and income.

Our business depends upon 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. The level of capital expenditures is generally dependent on the prevailing view of future oil and gas prices, which are influenced by numerous factors affecting the supply and demand for oil and gas, including:

- worldwide economic activity;
- the level of exploration and production activity;
- interest rates and the cost of capital;
- environmental regulation;
- federal, state and foreign policies regarding exploration and development of oil and gas;
- the ability and/or desire of OPEC and other major producers to set and maintain production levels and pricing;
- governmental regulations regarding future oil and gas exploration and production;
- the cost of exploring and producing oil and gas;
- the cost of developing alternative energy sources;
- the availability, expiration date and price of onshore and offshore leases;
- the discovery rate of new oil and gas reserves in onshore and offshore areas;
- the success of drilling for oil and gas in unconventional resource plays such as shale formations;
- alternative opportunities to invest in onshore exploration and production opportunities;
- technological advances and new techniques that render drilling more efficient or reduce demand for, and production of, fossil fuels; and
- weather conditions and natural disasters.

Oil and gas prices and the level of drilling and production activity have been characterized by significant volatility in recent years. Worldwide military, political and economic events have contributed to crude oil and natural gas price volatility and are likely to continue to do so in the future.

We expect continued pressure in both crude oil and natural gas prices, as well as in the level of drilling and production related activities, particularly as they relate to offshore activities. Even during periods of high prices for oil and natural gas, companies exploring for oil and gas may cancel or curtail programs, seek to renegotiate contract terms, including the price of our products and services, or reduce their levels of capital expenditures for exploration and production for a variety of reasons. These risks are greater during periods of low or declining commodity prices. The sustained lower crude oil and natural gas prices, along with lower drilling and production activity, have had a negative impact on our results of operations.

We may not be able to satisfy technical requirements, testing requirements or other specifications under contracts and contract tenders.

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Our products are used primarily in deepwater, harsh environment and severe service applications. Our contracts with customers and customer requests for bids typically set forth detailed specifications or technical requirements for our products and services, which may also include extensive testing requirements. We anticipate that such testing requirements will become more common in our contracts. In addition, recent scrutiny of the drilling industry has resulted in more stringent technical specifications for our products and more comprehensive testing requirements for our products to ensure compliance with such specifications. We cannot assure you that our products will be able to satisfy the specifications or that we will be able to perform the full-scale testing necessary to prove that the product specifications are satisfied in future contract bids or under existing contracts, or that the costs of modifications to our products to satisfy the specifications and testing will not adversely affect our results of operations. If our products are unable to satisfy such requirements, or we are unable to perform any required full-scale testing, our customers may cancel their contracts and/or seek new suppliers, and our business, results of operations, cash flows or financial position may be adversely affected.

We rely on technology provided by third parties and our business may be materially adversely affected if we are unable to renew our licensing arrangements with them.

We have existing contracts and may enter into new contracts with customers that require us to use technology or to purchase components from third parties, including some of our competitors. In the ordinary course of our business, we have entered into licensing agreements with some of these third parties for the use of such technology, including a license from a competitor of a technology important to our subsea wellheads. We may not be able to renew our existing licenses or to purchase these components on terms acceptable to us, or at all. If we are unable to use a technology or purchase a component, we may not be able to meet existing contractual commitments without increased costs or modifications or at all. In addition, we may need to stop selling products incorporating that technology or component or to redesign our products, either of which could result in a material adverse effect on our business and operations.

We may be unable to successfully compete with other manufacturers of drilling and production equipment.

Several of our primary competitors are diversified multinational companies with substantially larger operating staffs and greater capital resources than ours and which have been engaged in the manufacturing business for a much longer time than us. If these competitors substantially increase the resources they devote to developing and marketing competitive products and services, we may not be able to compete effectively. Similarly, consolidation among our competitors could enhance their product and service offerings and financial resources, further intensifying competition.

The loss of a significant customer could have an adverse impact on our financial results.

Our principal customers are major integrated oil and gas companies, large independent and foreign national oil and gas companies throughout the world. Drilling contractors and engineering and construction companies also represent a portion of our customer base. In 2018, our top 15 customers represented approximately 56% of total revenues, and BP and its affiliated companies accounted for approximately 13% of total revenues. In 2017 and 2016, our top 15 customers represented approximately 49% and 75% of total revenues, respectively, and Chevron and its affiliated companies accounted for approximately 14% and 16% of total revenues, respectively. The loss of one or more of our significant customers could have an adverse effect on our results of operations, financial position and cash flows.

Our customers' industries are undergoing continuing consolidation that may impact our results of operations.

The oil and gas industry is rapidly consolidating and, as a result, some of our largest customers have consolidated and are using their size and purchasing power to seek economies of scale and pricing concessions. This consolidation may result in reduced capital spending by some of our customers or the acquisition of one or more of our primary customers, which may lead to decreased demand for our products and services. We cannot assure you that we will be able to maintain our level of sales to a customer that has consolidated or replace that revenue with increased business activity with other customers. As a result, the acquisition of one or more of our primary customers may have a significant negative impact on our results of operations, financial position or cash flows. We are unable to predict what effect consolidations in the industry may have on price, capital spending by our customers, our selling strategies, our competitive position, our ability to retain customers or our ability to negotiate favorable agreements with our

customers.

Increases in the cost of raw materials and energy used in our manufacturing processes could negatively impact our profitability.

Any increases in commodity prices for items such as nickel, molybdenum and heavy metal scrap that are used to make the steel alloys required for our products would result in an increase in our raw material costs. Similarly, any increase in energy costs would increase our product costs. If we are not successful in raising our prices on products to compensate for any increased raw material or energy costs, our margins will be negatively impacted.

We depend on third-party suppliers for timely deliveries of raw materials, and our results of operations could be adversely affected if we are unable to obtain adequate supplies in a timely manner.

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Our manufacturing operations depend upon obtaining adequate supplies of raw materials from third parties. The ability of these third parties to deliver raw materials may be affected by events beyond our control. Any interruption in the supply of raw materials needed to manufacture our products could adversely affect our business, results of operations and reputation with our customers.

Conditions in the global financial system may have impacts on our business and financial position that we currently cannot predict.

Uncertainty in the credit markets may negatively impact the ability of our customers to finance purchases of our products and services and could result in a decrease in, or cancellation of, orders included in our backlog or adversely affect the collectability of our receivables. If the availability of credit to our customers is reduced, they may reduce their drilling and production expenditures, thereby decreasing demand for our products and services, which could have a negative impact on our financial position. Additionally, unsettled conditions could have an impact on our suppliers, causing them to be unable to meet their obligations to us. A prolonged constriction on future lending by banks or investors could result in higher interest rates on future debt obligations or could restrict our ability to obtain sufficient financing to meet our long-term operational and capital needs.

We are exposed to the credit risks of our customers, and a general increase in the nonpayment and nonperformance by customers could have an adverse impact on our cash flows, results of operations and financial condition.

Our business is subject to risks of loss resulting from nonpayment or nonperformance by our customers. Certain of our customers finance their activities through cash flow from operations, the incurrence of debt or the issuance of equity. In an economic downturn, commodity prices typically decline, and the credit markets and availability of credit can be expected to be constrained. Additionally, certain of our customers' equity values could decline. The combination of lower cash flow due to commodity prices, a reduction in borrowing bases under reserve-based credit facilities and the lack of available debt or equity financing may result in a significant reduction in our customers' liquidity and ability to pay or otherwise perform on their obligations to us. Furthermore, some of our customers may be highly leveraged and subject to their own operating and regulatory risks, which increases the risk that they may default on their obligations to us. Any increase in the nonpayment and nonperformance by our customers could have an adverse impact on our operating results and could adversely affect our liquidity.

Our backlog is subject to unexpected adjustments and cancellations and is, therefore, an uncertain indicator of our future revenues and earnings.

The revenues projected in our backlog may not be realized or, if realized, may not result in profits. All of the projects currently included in our backlog are subject to change and/or termination at the option of the customer. In case of a change or termination, the customer is generally required to pay us for work performed and other costs necessarily incurred as a result of the change or termination.

We can give no assurance that our backlog will remain at current levels. Sales of our products are affected by prices for oil and natural gas, which have fluctuated significantly and may continue to do so in the future. Contracts denominated in foreign currency are also affected by changes in exchange rates, which may have a negative impact on our backlog. When drilling and production levels are depressed, a customer may no longer need the equipment or services currently under contract or may be able to obtain comparable equipment or services at lower prices. As a result, customers may delay projects, exercise their termination rights or attempt to renegotiate contract terms.

For example, during the first quarter of 2018, Dril-Quip Asia-Pacific Pte Ltd. was awarded a contract to supply TTR systems and related services for the development of the CRD Project located offshore Vietnam operated by Repsol with the participation of Mubadala, PVEP and PetroVietnam. The CRD Project is included within the backlog balance presented in the accompanying consolidated financial statements; however, due to ongoing territorial discussions between China and Vietnam, the CRD Project may experience continued delays or cancellation.

Continued declines in, or sustained low levels of, oil and natural gas prices could also reduce new customer orders, possibly causing a decline in our future backlog. If we experience significant project terminations, suspensions or scope adjustments to contracts reflected in our backlog, our financial condition, results of operations and cash flows may be adversely impacted.

Impairment in the carrying value of long-lived assets, inventory, intangible assets and goodwill could negatively affect our operating results.

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.

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As a result of continued unfavorable offshore market conditions and low commodity prices, the Company engaged in a strategic review with a third-party firm in 2018. In conjunction with the strategic review, the Company adjusted its forecast for recovery to reflect a more delayed recovery in the offshore industry, with pre-downturn demand not returning until after 2025. Additionally, the Company pursued a global transformation, which includes a reduction in workforce, realignment of facilities and restructuring of operations. We expect this transformation to allow us to maintain our global footprint in key markets, while supporting an integrated supply chain model that we expect to create more flexibility and allow us to continue serving our customers. The Company expects to complete the strategic restructuring by the end of 2019.

During the fourth quarter of 2018, we incurred inventory and long-lived asset write-downs of approximately \$32.1 million and \$14.9 million, respectively, as a result of changes in our business structure and where specific products are manufactured. These charges are reflected as Impairment, restructuring and other charges in our consolidated statement of operations.

In connection with our preparation and review of financial statements for the year ended December 31, 2017, after considering current Brent crude (Brent) consensus forecasts and expected rig counts for the foreseeable future, we determined the carrying amount of certain of our long-lived assets in the Western Hemisphere exceeded the fair values of such assets due to projected declines in asset utilization, and that the cost of some of our worldwide inventory exceeded its market value. As a result, we recorded corresponding impairments and other charges. Primarily as a result of the factors described above, we recorded charges of approximately \$33.6 million related to inventory and \$27.4 million related to fixed assets. No additional impairments were recorded during the three months ended December 31, 2017. Additionally, no impairments were recorded for the year ended December 31, 2016.

For goodwill, an assessment for impairment is performed annually or when there is an indication an impairment may have occurred. We typically complete our annual impairment test for goodwill and other indefinite-lived intangibles using an assessment date of October 1. Goodwill is reviewed for impairment by comparing the carrying value of each of our three reporting units' net assets, including allocated goodwill, to the estimated fair value of the reporting unit. We determine the fair value of our reporting units using a discounted cash flow approach. We selected this valuation approach because we believe it, combined with our best judgment regarding underlying assumptions and estimates, provides the best estimate of fair value for each of our reporting units. Determining the fair value of a reporting unit requires the use of estimates and assumptions. Such estimates and assumptions include revenue growth rates, future operating margins, the weighted average cost of capital, a terminal growth value and future market conditions, among others. We believe that the estimates and assumptions used in our impairment assessments are reasonable. If the reporting unit's carrying value is greater than its calculated fair value, we recognize a goodwill impairment charge for the amount by which the carrying value of goodwill exceeds its calculated fair value.

At October 1, 2018, the Company performed its annual impairment test on each of its reporting units and concluded that there had been no impairment because the estimated fair values of each of those reporting units exceeded its carrying value. Relevant events and circumstances that could have a negative impact on goodwill include: macroeconomic conditions; industry and market conditions, such as commodity prices; operating cost factors; overall financial performance; the impact of dispositions and acquisitions; and other entity-specific events. Further declines in commodity prices or sustained lower valuation for the Company's common stock could indicate a reduction in the estimate of reporting unit fair value which, in turn, could lead to an impairment of reporting unit goodwill.

In December 2018, the overall offshore market conditions declined. This decline was evidenced by lower commodity prices, decline in expected offshore rig counts, decrease in our customers' capital budgets and potential delays associated with certain of our long term projects. Further, in December 2018 due to the decline in our stock price, our market capitalization dropped below the carrying value of our assets. As a result, an interim goodwill impairment analysis was performed in connection with our preparation and review of financial statements for the year ended December 31, 2018. Based on this analysis, we recorded an impairment loss of \$38.6 million for our Western Hemisphere reporting unit for the year ended December 31, 2018. Following this impairment charge, the Western Hemisphere reporting unit has no remaining goodwill balance. The remaining goodwill balance is associated with our Eastern Hemisphere reporting unit. Based on our interim goodwill impairment analysis the fair value of the Eastern

Hemisphere reporting unit exceeds its carry value by 71%. Further declines in the overall offshore market, commodity prices, or sustained lower valuation for the Company's common stock could indicate a reduction in the estimate of the Eastern Hemisphere's reporting unit fair value which, in turn, could lead to additional impairment charges associated with goodwill. No goodwill impairment losses were recorded for the years ended December 31, 2017 and 2016. During 2018, Brent crude oil prices fluctuated significantly, with a high of \$86.07 per barrel, a low of \$50.57 per barrel, and an average of \$71.34 per barrel. Although the prices have experienced some recovery in 2017 and 2018, continued weakness or volatility in market conditions may further deteriorate the financial performance or future prospects of our

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operating segments from current levels, which may result in an impairment of long-lived assets, inventory or goodwill and negatively impact our financial results in the period of impairment.

Our international operations expose us to instability and changes in economic and political conditions and other risks inherent to international business, which could have a material adverse effect on our results of operations, financial position or cash flows.

We have substantial international operations, with approximately 61% of our revenues derived from foreign sales in 2018, 55% in 2017 and 66% in 2016. We operate our business and market our products and services in many of the significant oil and gas producing areas in the world and are, therefore, subject to the risks customarily attendant to international operations and investments in foreign countries. Risks associated with our international operations include:

- volatility in general economic, social and political conditions;
- terrorist threats or acts, war and civil disturbances;
- expropriation or nationalization of assets;
- renegotiation or nullification of existing contracts;
- foreign taxation, including changes in laws or differing interpretations of existing laws;
- assaults on property or personnel;
- restrictive action by local governments;
- foreign and domestic monetary policies;
- limitations on repatriation of earnings;
- the occurrence of a trade war or other governmental action related to tariffs or trade agreements or policies;
- travel limitations or operational problems caused by public health threats; and
- changes in currency exchange rates.

Any of these risks could have an adverse effect on our ability to manufacture products abroad or the demand for our products and services in some locations. To date, we have not experienced any significant problems in foreign countries arising from local government actions or political instability, but there is no assurance that such problems will not arise in the future. Interruption of our international operations could have a material adverse effect on our overall operations.

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.

Doing business on a worldwide basis exposes us and our subsidiaries to risks inherent in complying with the laws and regulations of a number of different nations, including various anti-bribery laws. We do business and have operations in a number of developing countries that have relatively underdeveloped legal and regulatory systems compared to more developed countries. Several of these countries are generally perceived as presenting a higher than normal risk of corruption, or as having a culture in which requests for improper payments are not discouraged. As a result, we may be subject to risks under the U.S. Foreign Corrupt Practices Act, the United Kingdom's Bribery Act of 2010 and similar laws in other countries that generally prohibit companies and their representatives from making, offering or authorizing improper payments to government officials for the purpose of obtaining or retaining business. We have adopted policies and procedures, including our Code of Business Conduct and Ethical Practices, which are designed to promote compliance with such laws. However, maintaining and administering an effective compliance program under applicable anti-bribery laws in developing countries presents greater challenges than is the case in more developed countries.

In addition, the movement of goods, services and technology subjects us to complex legal regimes governing international trade. Our import activities are governed by unique tariff and customs laws and regulations in each of the countries where we operate. Further, many of the countries in which we do business maintain controls on the export or reexport of certain goods, services and technology, as well as economic sanctions that prohibit or restrict business activities in, with or involving certain persons, entities or countries. These laws and regulations concerning import and export activity, including their recordkeeping and reporting requirements, are complex and frequently changing. Moreover, they may be adopted, enacted, amended, enforced or interpreted in a manner that could materially impact

our operations.

The precautions we take to prevent and detect misconduct, fraud or non-compliance with applicable laws and regulations governing international trade, including anti-bribery laws, may not be able to prevent such occurrences, and we could face unknown risks or losses. Our failure to comply with applicable laws or regulations or acts of misconduct could subject us to criminal or civil penalties, such as fines, imprisonment, sanctions, debarment from government contracts, seizure of shipments

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and loss of import and export privileges. In addition, actual or alleged violations of such laws and regulations could be expensive and consume significant time and attention of senior management to investigate and resolve, as well as damage our reputation and ability to do business, any of which could have a material adverse effect on our business and our results of operations, financial position and cash flows. We are also subject to the risks that our employees, agents and other representatives may act or fail to act in violation of such laws or regulations or our compliance policies and procedures.

The results of the United Kingdom's referendum on withdrawal from the European Union, including the subsequent exchange rate fluctuations and political and economic uncertainties, may have a negative effect on global economic conditions, financial markets and our business.

In a referendum held on June 23, 2016, voters in the United Kingdom (U.K.) approved the exit (Brexit) of the U.K. from the European Union (E.U.). On March 29, 2017, the U.K. government commenced the exit process under Article 50 of the Treaty of the European Union by notifying the European Council of the U.K.'s intention to leave the E.U. This notification started a two-year time period ending on March 29, 2019 for the U.K. and the remaining E.U. Member States to negotiate a withdrawal agreement. Negotiations remain ongoing to determine the future terms of the U.K.'s relationship with the E.U. The impact on the Company's business as a result of Brexit will depend, in part, on the outcome of tariff, trade, regulatory and other negotiations.

The consequences of Brexit, together with the protracted negotiations around the terms of Brexit, could introduce significant uncertainties into global financial markets and adversely impact the regions in which we and our clients operate. For example, importing and exporting activity from our Aberdeen manufacturing facility could be subject to higher costs and delays, which could cause disruptions in our delivery schedules to our customers. In the long term, Brexit could also create uncertainty with respect to the legal and regulatory requirements to which we and our customers in the U.K. are subject and lead to divergent national laws and regulations as the U.K. government determines which E.U. laws to modify or replace.

The referendum adversely impacted global markets, including currencies, and resulted in a decline in the value of the British pound sterling, as compared to the U.S. dollar and other currencies. Volatility in exchange rates could be expected to continue in the short term as the U.K. negotiates its exit from the E.U. A weaker British pound sterling compared to the U.S. dollar during a reporting period would cause local currency results of the Company's U.K. operations to be translated into fewer U.S. dollars.

Continued adverse consequences, such as deterioration in economic conditions and volatility in currency exchange rates, and the uncertainty surrounding Brexit could have a negative impact on the Company's financial position and results of operations.

Tax reform in the United States may have adverse effects on our financial position.

On December 22, 2017, the Tax Cuts and Jobs Act was enacted (US Tax Reform). US Tax Reform includes a number of changes that impacted our business. These changes include a reduction in the corporate tax rate from 35% to 21% starting in 2018, the elimination or reduction of certain domestic deductions and credits and limitations on the deductibility of interest expense and executive compensation. US Tax Reform also transitions U.S. international taxation from a worldwide tax system to a modified territorial system, which includes base erosion prevention measures on non-U.S. earnings, which have the effect of subjecting certain earnings of our foreign subsidiaries to U.S. taxation stemming from guidelines such as Global Low Tax Intangible Income (GILTI). The US Tax Reform also includes a one-time transition tax on the mandatory deemed repatriation of cumulative foreign earnings as of December 31, 2017.

US Tax Reform also provides for the acceleration of depreciation for certain assets placed into service after September 27, 2017 as well as prospective changes beginning in 2018, including repeal of the domestic manufacturing deduction. Changes in corporate tax rates, the taxation of foreign earnings and the deductibility of expenses had a material impact on the recoverability of our deferred tax assets, and resulted in an increase of the Company's effective tax rate in 2017. The provisions of US Tax Reform reduced the Company's effective tax rate in 2018, but it is important to note that the ultimate impact on the Company's effective tax rate will largely depend on the percentage of pre-tax earnings that is generated in the United States as compared to the rest of the world.

We are subject to taxation in many jurisdictions and there are inherent uncertainties in the final determination of our tax liabilities.

As a result of our international operations, we are subject to taxation in many jurisdictions. Accordingly, our effective income tax rate and other tax obligations in the future could be adversely affected by a number of factors, including changes in the mix of earnings in countries with differing statutory tax rates, the mix of business executed in deemed profit regimes compared to book income regimes, changes in the valuation of deferred tax assets and liabilities, disagreements with taxing authorities with respect to the interpretation of tax laws and regulations and changes in tax laws. In particular, foreign income tax returns of foreign subsidiaries and related entities are routinely examined by foreign tax authorities, and these tax

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examinations may result in assessments of additional taxes, interest or penalties. Refer to "Item 3. Legal Proceedings" regarding tax assessments in Brazil. We regularly assess all of these matters to determine the adequacy of our tax provision, which is subject to discretion. If our assessments are incorrect, it could have an adverse effect on our business and financial condition.

Moreover, the United States Congress, the Organization for Economic Co-operation and Development and other government agencies in the other jurisdictions where we and our subsidiaries do business have had an extended focus on issues related to the taxation of multinational corporations. One example is in the area of "base erosion and profit shifting," where payments are made between affiliates from a jurisdiction with high tax rates to a jurisdiction with lower tax rates. As a result, the tax laws in the United States and other countries in which we and our subsidiaries do business could change on a prospective or retroactive basis, and such changes could adversely affect us.

Our excess cash is invested in various financial instruments which may subject us to potential losses.

We invest excess cash in various financial instruments including interest bearing accounts, money market mutual funds and funds which invest in U.S. Treasury obligations and repurchase agreements backed by U.S. Treasury obligations. However, changes in the financial markets, including interest rates, as well as the performance of the issuers, can affect the market value of our short-term investments.

We may suffer losses as a result of foreign currency fluctuations and limitations on the ability to repatriate income or capital to the United States.

We conduct a portion of our business in currencies other than the U. S. dollar, and our operations are subject to fluctuations in foreign currency exchange rates. We cannot assure you that we will be able to protect the Company against such fluctuations in the future. Further, we cannot assure you that the countries in which we currently operate will not adopt policies limiting repatriation of earnings in the future.

Our foreign subsidiaries also hold significant amounts of cash that may be subject to both U.S. income taxes (subject to adjustment for foreign tax credits) and withholding taxes of the applicable foreign country if we repatriate that cash to the United States.

Our business involves numerous operating hazards that may not be covered by insurance. The occurrence of an event not fully covered by insurance could have a material adverse effect on our results of operations, financial position and cash flows.

Our products are used in potentially hazardous drilling, completion and production applications that can cause personal injury, product liability and environmental claims. In addition, certain areas where our products are used, including in and near the U.S. Gulf of Mexico, are close to high population areas and subject to hurricanes and other extreme weather conditions on a relatively frequent basis. A catastrophic occurrence at a location where our equipment and/or services are used may expose us to substantial liability for personal injury, wrongful death, product liability, environmental damage or commercial claims. Our general liability insurance program includes an aggregate coverage limit of \$200 million for claims with respect to property damage, injury or death and pollution. However, our insurance policies may not cover fines, penalties or costs and expenses related to government-mandated cleanup of pollution. In addition, our insurance does not provide coverage for all liabilities, and we cannot assure you that our insurance coverage will be adequate to cover claims that may arise or that we will be able to maintain adequate insurance at rates we consider reasonable. The occurrence of an event not fully covered by insurance could have a material adverse effect on our results of operations, financial position and cash flows.

We attempt to further limit our liability through contractual indemnification provisions with our customers. We generally seek to enter into contracts for the provision of our products and services that provide for (1) the responsibility of each party to the contract for personal injuries to, or the death of, its employees and damages to its property, (2) cross-indemnification with other contractors providing products and/or services to the other party to the contract with respect to personal injury, death and property damage and (3) the operator being responsible for claims brought by third parties for personal injury, death, property loss or damage relating to pollution or other well control events. Due to competitive market pressures, we may not be able to successfully obtain favorable contractual provisions, and a failure to do so may increase our risks and costs, which could materially impact our results of operations. In addition, we cannot assure you that any party that is contractually obligated to indemnify us will be

financially able to do so or that a court will enforce all such indemnities.

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We may lose money on fixed-price contracts.

A portion of our business consists of the designing, manufacturing and selling of our equipment for major projects pursuant to competitive bids, and is performed on a fixed-price basis. Under these contracts, we are typically responsible for all cost overruns, other than the amount of any cost overruns resulting from requested changes in order specifications. Our actual costs and any gross profit realized on these fixed-price contracts may vary from the estimated amounts on which these contracts were originally based. This may occur for various reasons, including:

- errors in estimates or bidding;
- changes in availability and cost of labor and materials;
- variations in productivity from our original estimates; and
- material changes in foreign currency exchange rates.

These variations and the risks inherent in our projects may result in reduced profitability or losses on projects.

Depending on the size of a project, variations from estimated contract performance could have a material adverse impact on our operating results.

Our business could be adversely affected if we do not develop new products and secure and retain patents related to our products.

Technology is an important component of our business and growth strategy, and our success as a company depends to a significant extent on the development and implementation of new product designs and improvements. Whether we can continue to develop systems and services and related technologies to meet evolving industry requirements and, if so, at prices acceptable to our customers will be significant factors in determining our ability to compete in the industry in which we operate. Many of our competitors are large multinational companies that may have significantly greater financial resources than we have, and they may be able to devote greater resources to research and development of new systems, services and technologies than we are able to do.

Our ability to compete effectively will also depend on our ability to continue to obtain patents on our proprietary technology and products. Although we do not consider any single patent to be material to our business as a whole, the inability to protect our future innovations through patents could have a material adverse effect.

We may be required to recognize a charge against current earnings because of over time method of accounting.

Revenues and profits on long-term project contracts are recognized on an over time basis. We calculate the percent complete and apply the percentage to determine revenues earned and the appropriate portion of total estimated costs. Accordingly, purchase order 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. To the extent that these adjustments result in a reduction or elimination of previously reported profits, we would have to recognize a charge against current earnings, which could be significant depending on the size of the project or the adjustment.

Loss of our key management or other personnel could adversely impact our business.

We depend on the continued services of our executive officers and other key members of management, particularly our President and Chief Executive Officer. From time to time, there may be changes in our executive management team resulting from the hiring or departure of executives. Such changes in our executive management team may be disruptive to our business. The loss of one or more of our key employees or groups could have a material adverse effect on our results of operations, financial position and cash flows.

Acquisitions, dispositions and investments may not result in anticipated benefits and may present risks not originally contemplated, which could have a material adverse effect on our financial condition, results of operations and cash flows.

From time to time, we evaluate purchases and sales of assets, businesses or other investments. These transactions may not result in the anticipated realization of savings, creation of efficiencies, offering of new products or services, generation of cash or income or reduction of risk. In addition, acquisitions may be financed by borrowings, requiring us to incur debt, or by the issuance of our common stock. These transactions involve numerous risks, and we cannot ensure that:

- any acquisition would be successfully integrated into our operations and internal controls;

the due diligence conducted prior to an acquisition would uncover situations that could result in financial or legal exposure;
the use of cash for acquisitions would not adversely affect our cash available for capital expenditures and other uses;

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any disposition, investment, acquisition or integration would not divert management resources from the operation of our business; or

any disposition, investment, acquisition or integration would not have a material adverse effect on our financial condition, results of operations or cash flows.

Restrictions in the agreement governing the Asset Backed Loan (ABL) Credit Facility could adversely affect our business, financial condition and results of operations.

The operating and financial restrictions in the ABL Credit Facility and any future financing agreements could restrict our ability to finance future operations, capital needs or to access to capital at a reasonable cost or otherwise pursue our business activities. For example, ABL Credit Facility limits our and our subsidiaries' ability to, among other things:

incur additional debt or issue guarantees;

incur or permit certain liens to exist;

make certain investments, acquisitions or other restricted payments, including payments for the purchase of equity interests in the Company;

dispose of assets;

engage in certain types of transactions with affiliates;

merge, consolidate or transfer all or substantially all of our assets; and

prepay certain indebtedness.

Furthermore, the ABL Credit Facility contains a covenant requiring us to maintain a fixed charge coverage ratio of 1.0 to 1.0 based on the ratio of consolidated EBITDA to fixed charges when availability under the ABL Credit Facility falls below the greater of \$10 million and 15% of the lesser of the borrowing base and aggregate commitments.

In addition, any borrowings under the ABL Credit Facility may be at variable rates of interest that expose us to interest rate risk. If interest rates increase, our debt service obligations on the variable rate indebtedness will increase even though the amount borrowed will remain the same, and our net income and cash flows will correspondingly decrease.

A failure to comply with the covenants in the agreement governing the ABL Credit Facility could result in an event of default, which, if not cured or waived, would permit the exercise of remedies against us that could have a material adverse effect on our business, results of operations and financial position. Remedies under the ABL Credit Facility include foreclosure on the collateral securing the indebtedness and termination of the commitments under the ABL Credit Facility, and any outstanding borrowings under the ABL Credit Facility may be declared immediately due and payable.

Our operations and our customers' operations are subject to a variety of governmental laws and regulations that may increase our costs, limit the demand for our products and services or restrict our operations.

Our business and our customers' businesses may be significantly affected by:

federal, state, local and foreign laws and other regulations relating to the oilfield operations, worker safety and the protection of the environment;

changes in these laws and regulations;

levels of enforcement of these laws and regulations; and

interpretation of existing laws and regulations.

In addition, we depend on the demand for our products and services from the oil and gas industry. This demand is affected by changing taxes, price controls and other laws and regulations relating to the oil and gas industry in general, including those specifically directed to offshore operations. For example, the adoption of laws and regulations curtailing exploration and development drilling for oil and gas for economic or other policy reasons could adversely affect our operations by limiting demand for our products. We cannot determine the extent to which our future operations and earnings may be affected by new legislation, new regulations or changes in existing regulations and enforcement thereof.

Various new regulations intended to improve particularly offshore safety systems and environmental protection have been issued since 2010 that have increased the complexity of the drilling permit process and may limit the opportunity

for some operators to continue deepwater drilling in the U.S. Gulf of Mexico, which could adversely affect the Company's financial operations. Third-party challenges to industry operations in the U.S. Gulf of Mexico may also serve to further delay or restrict activities. If the new regulations, policies, operating procedures and possibility of increased legal liability are viewed by our

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current or future customers as a significant impairment to expected profitability on projects, they could discontinue or curtail their operations, thereby adversely affecting our financial operations by decreasing demand for our products. Because of our foreign operations and sales, we are also subject to changes in foreign laws and regulations that may encourage or require hiring of local contractors or require foreign contractors to employ citizens of, or purchase supplies from, a particular jurisdiction. If we fail to comply with any applicable law or regulation, our business, results of operations, financial position and cash flows may be adversely affected.

Our businesses and our customers' businesses are subject to environmental laws and regulations that may increase our costs, limit the demand for our products and services or restrict our operations.

Our operations and the operations of our customers are also subject to federal, state, local and foreign laws and regulations relating to the protection of human health and the environment. These environmental laws and regulations affect the products and services we design, market and sell, as well as the facilities where we manufacture our products. For example, our operations are subject to numerous and complex laws and regulations that, among other things, may regulate the management and disposal of hazardous and non-hazardous wastes; require acquisition of environmental permits related to our operations; restrict the types, quantities and concentrations of various materials that can be released into the environment; limit or prohibit operation activities in certain ecologically sensitive and other protected areas; regulate specific health and safety criteria addressing worker protection; require compliance with operational and equipment standards; impose testing, reporting and record-keeping requirements; and require remedial measures to mitigate pollution from former and ongoing operations. We are required to invest financial and managerial resources to comply with such environmental, health and safety laws and regulations and anticipate that we will continue to be required to do so in the future. In addition, environmental laws and regulations could limit our customers' exploration and production activities. These laws and regulations change frequently, which makes it impossible for us to predict their cost or impact on our future operations. For example, legislation to regulate emissions of greenhouse gases has been introduced, but not enacted, in the U.S. Congress, and there has been a wide-ranging policy debate, both nationally and internationally, regarding the impact of these gases and possible means for their regulation. In addition, efforts have been made and continue to be made in the international community toward the adoption of international treaties or protocols that would address global climate change issues, such as the annual United Nations Climate Change Conferences, including the United Nations Climate Change Conference in Paris (COP 21) in November 2015, which resulted in the creation of the Paris Agreement. The Paris Agreement, signed by the U.S. on April 22, 2016, requires countries to review and "represent a progression" in their nationally determined contributions, which set greenhouse gas emission reduction goals, every five years. However, in August 2017, the United States informed the United Nations of its intent to withdraw from the Paris Agreement. The earliest possible effective withdrawal date from the Paris Agreement is November 2020. Also, the EPA has undertaken efforts to collect information regarding greenhouse gas emissions and their effects. Following a finding by the EPA that certain greenhouse gases represent a danger to human health, the EPA expanded its regulations relating to those emissions and adopted rules imposing permitting and reporting obligations. The results of the permitting and reporting requirements could lead to further regulation of these greenhouse gases by the EPA. Subsequent to the Paris Agreement, there has been no significant legislative progress in cap and trade proposals or greenhouse gas emission reductions. The adoption of legislation or regulatory programs to reduce greenhouse gas emissions could also increase the cost of consuming, and thereby reduce demand for, the hydrocarbons that our customers produce. Consequently, such legislation or regulatory programs could have an adverse effect on our financial condition and results of operations. It is too early to determine whether, or in what form, further regulatory action regarding greenhouse gas emissions will be adopted or what specific impact a new regulatory action might have on us or our customers. Generally, the anticipated regulatory actions do not appear to affect us in any material respect that is different, or to any materially greater or lesser extent, than other companies that are our competitors. However, our business and prospects could be adversely affected to the extent laws are enacted or modified or other governmental action is taken that prohibits or restricts our customers' exploration and production activities or imposes environmental protection requirements that result in increased costs to us or our customers.

Environmental laws may provide for “strict liability” for damages to natural resources or threats to public health and safety, rendering a party liable for environmental damage without regard to negligence or fault on the part of such party. Sanctions for noncompliance may include revocation of permits, corrective action orders, administrative or civil penalties and criminal prosecution. Some environmental laws and regulations provide for joint and several strict liability for remediation of spills and releases of hazardous substances. In addition, we may be subject to claims alleging personal injury or property damage as a result of alleged exposure to hazardous substances, as well as damage to natural resources. These laws and regulations also may expose us to liability for the conduct of or conditions caused by others, or for our acts that were in compliance with all applicable laws and regulations at the time such acts were performed. Any of these laws and regulations could result in claims, fines or expenditures that could be material to results of operations, financial position and cash flows.

Our business could be adversely affected by a failure or breach of our information technology systems.

Our business operations depend on our information technology (IT) systems. Despite our security and back-up measures, our IT systems are vulnerable to cyber incidents or attacks, natural disasters and other disruptions or failures. Due to the nature

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of cyber-attacks, breaches to our IT systems could go unnoticed for a prolonged period of time. The failure of our IT systems to perform as anticipated for any reason or any significant breach of security could disrupt our business and result in numerous adverse consequences, including reduced effectiveness and efficiency of our operations and those of our customers, the loss, theft, corruption or inappropriate disclosure of confidential information or critical data, increased overhead costs, loss of revenue, loss of intellectual property and damage to our reputation, which could have a material adverse effect on our business and results of operations. In addition, we may be required to incur significant costs to prevent or respond to damage caused by these disruptions or security breaches in the future.

Our business is subject to complex and evolving U.S. and foreign laws and regulations regarding privacy and data protection.

The regulatory environment surrounding data privacy and protection is constantly evolving and can be subject to significant change. New laws and regulations governing data privacy and the unauthorized disclosure of confidential information, including the European Union General Data Protection Regulation and recent California legislation, pose increasingly complex compliance challenges and potentially elevate our costs. Any failure, or perceived failure, by us to comply with applicable data protection laws could result in proceedings or actions against us by governmental entities or others, subject us to significant fines, penalties, judgments and negative publicity, require us to change our business practices, increase the costs and complexity of compliance, and adversely affect our business. As noted above, we are also subject to the possibility of cyber incidents or attacks, which themselves may result in a violation of these laws. Additionally, if we acquire a company that has violated or is not in compliance with applicable data protection laws, we may incur significant liabilities and penalties as a result.

The market price of our common stock may be volatile.

The trading price of our common stock and the price at which we may sell common stock in the future are subject to large fluctuations in response to any of the following:

- limited trading volume in our common stock;
- quarterly variations in operating results;
- general financial market conditions;
- the prices of natural gas and oil;
- announcements by us and our competitors;
- our liquidity;
- changes in government regulations;
- our ability to raise additional funds;
- our involvement in litigation; and
- other events.

We do not anticipate paying dividends on our common stock in the near future.

We have not paid any dividends in the past and do not intend to pay cash dividends on our common stock in the foreseeable future. Our Board of Directors reviews this policy on a regular basis in light of our earnings, financial position and market opportunities. We currently intend to retain any earnings for the future operation and development of our business as well as potential stock repurchases or acquisition opportunities.

Provisions in our corporate documents and Delaware law could delay or prevent a change in control of the Company, even if that change would be beneficial to our stockholders.

The existence of some provisions in our corporate documents and Delaware law could delay or prevent a change in control of our company, even if that change would be beneficial to our stockholders. Our certificate of incorporation and bylaws contain provisions that may make acquiring control of our company difficult, including:

- provisions relating to the classification, nomination and removal of our directors;
- provisions regulating the ability of our stockholders to bring matters for action at annual meetings of our stockholders;
- provisions requiring the approval of the holders of at least 80% of our voting stock for a broad range of business combination transactions with related persons; and
- the authorization given to our Board of Directors to issue and set the terms of preferred stock.

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In addition, the Delaware General Corporation Law imposes restrictions on mergers and other business combinations between us and any holder of 15% or more of our outstanding common stock.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

Manufacturing Facilities

Location	Building Size (Approximate Square Feet)	Land (Approximate Acreage)	Owned or Leased
Houston, Texas			
—Hempstead Highway	175,000	12.9	Owned
—N. Eldridge Parkway	1,731,000	218	Owned
—S. Main Street	127,000	2.9	Owned
Youngsville, Louisiana	36,100	0.8	Owned
Aberdeen, Scotland	222,800	24.1	Owned
Singapore	293,200	14.4	Leased
Macaé, Brazil	169,600	10.6	Owned

The Company's forging and heat treatment activities are performed at the Houston Eldridge Parkway facility. For additional information on our manufacturing facilities, see "Item 1. Business - General" and "Manufacturing".

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Sales, Service and Reconditioning Facilities

Location*	Building Size (Approximate Square Feet)	Land (Approximate Acreage)	Activity
Midland, Texas	10,000	0.2	Sales/Service/Warehouse
Oklahoma City, Oklahoma*	6,000	0.1	Sales/Warehouse
Villahermosa, Mexico*	12,400	0.3	Sales/Service/Warehouse
Anaco, Venezuela*	3,000	0.1	Sales/Service/Warehouse
Quito, Ecuador	2,600	0.1	Sales
Shushufindi, Ecuador	135,800	3.1	Sales/Service/Warehouse
Szolnok, Hungary	4,300	0.1	Sales/Service/Warehouse
Beverwijk, Holland	32,000	0.7	Sales/Warehouse
Stavanger, Norway*	42,000	6.1	Sales/Service/Reconditioning/Warehouse/Fabrication
Esbjerg, Denmark	19,100	2.6	Sales/Service/Reconditioning/Warehouse
Takoradi, Ghana	2,500	0.8	Service/Reconditioning/Warehouse
Port Harcourt, Nigeria	6,600	0.1	Service/Reconditioning/Warehouse
Cairo, Egypt	2,200	—	Sales
Alexandria, Egypt	5,200	0.6	Service/Reconditioning/Warehouse
Balikpapan, Indonesia	2,000	—	Reconditioning
Doha, Qatar	8,900	—	Service/Reconditioning/Warehouse
Shekou, China	11,100	—	Sales/Service/Warehouse
Perth and Welshpool, Australia	28,000	2.9	Sales/Service/Reconditioning/Warehouse
Mumbai, India	130	—	Sales
Jakarta, Indonesia	150	—	Sales
Kuala Lumpur, Malaysia	400	—	Sales
Beijing, China	120	—	Sales

*These facilities are owned; all other facilities are leased.

The Company also performs sales, service and reconditioning activities at its facilities in Houston, Youngsville, Alberta, Aberdeen, Singapore and Macae. For additional information on our manufacturing facilities, see "Item 1. Business - General".

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Item 3. Legal Proceedings

Brazilian Tax Issue

From 2002 to 2007, the Company's Brazilian subsidiary imported goods through the State of Espirito Santo in Brazil and subsequently transferred them to its facility in the State of Rio de Janeiro. During that period, the Company's Brazilian subsidiary paid taxes to the State of Espirito Santo on its imports. 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 (Santo Credits) on the importation of goods from July 2005 to October 2007. The Company has objected to these assessments on the grounds that they would represent double taxation on the importation of the same goods and that the Company is entitled to the credits under applicable Brazilian law. The Company's Brazilian subsidiary filed appeals with a State of Rio de Janeiro judicial court to annul both of these tax assessments following rulings against the Company by the tax administration's highest council. In connection with those appeals, the Company deposited with the court a total amount of approximately \$8.8 million in December 2014 and December 2016 as the full amount of the assessments with penalties and interest. The Company believes that these credits are valid and that success in the judicial court process is probable. Based upon this analysis, the Company has not accrued any liability in conjunction with this matter.

Since 2007, the Company's Brazilian subsidiary has paid taxes on the importation of goods directly to the State of Rio de Janeiro and the Company does not expect any similar issues to exist for periods subsequent to 2007.

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 dependency on the condition of the oil and gas industry. Additionally, products of the Company are used in potentially hazardous drilling, completion, and production applications that can cause personal injury, property damage and environmental claims. Although exposure to such risk has not resulted in any significant problems in the past, there can be no assurance that ongoing and future developments will not adversely impact the Company.

For a further description of the Company's legal proceedings, see "Commitments and Contingencies," Note 15 of Notes to Consolidated Financial Statements. The Company also is 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 4. Mine Safety Disclosure

Not applicable.

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PART II

Item 5. Market for Registrant's Common Stock, Related Stockholder Matters and Issuer Purchases of Equity Securities
The Company's common stock is publicly traded on the New York Stock Exchange under the symbol "DRQ".

There were approximately 170 stockholders of record of the Company's common stock as of December 31, 2018. This number includes the Company's employees and directors that hold shares, but does not include the number of security holders for whom shares are held in a "nominee" or "street" name.

The Company has not paid any dividends in the past and does not currently anticipate paying any dividends in the foreseeable future. The Company intends to reinvest any retained earnings for the future operation and development of its business, or to use for potential stock repurchases or acquisition opportunities. The Board of Directors will review this policy on a regular basis in light of the Company's earnings, financial position, market opportunities and restrictions under the ABL Credit Facility.

Information concerning securities authorized for issuance under equity compensation plans is included in "Stock-Based Compensation and Stock Awards", Note 18 of Notes to Consolidated Financial Statements.

Repurchase of Equity Securities

The following table summarizes the repurchase and cancellation of our common stock during the year ended December 31, 2018:

		Twelve months ended December 31, 2018	
	Total Average Number of Shares Purchased	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Dollar Value (in millions) of Shares that May Yet be Purchased Under the Plans or Programs
April 1-30, 2018	—	—	—