OCEANEERING INTERNATIONAL INC
Form 10-Q
August 08, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2006

OR

o **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 1-10945

OCEANEERING INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	95-2628227
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
11911 FM 529 Houston, Texas	77041
(Address of principal executive offices)	(Zip Code)

(713) 329-4500
(Registrant s telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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 þ, No o.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

The number of shares of the registrant s common stock outstanding as of July 27, 2006 was 54,178,538.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

OCEANEERING INTERNATIONAL, INC. & SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(unaudited)
(in thousands)

	June 30, 2006	Dec. 31, 2005
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 24,957	$ 26,308
Accounts receivable, net of allowances for doubtful accounts of $110 and $112	308,928	269,497
Inventory and other	147,744	98,428
Total Current Assets	481,629	394,233
Property and Equipment, at cost	939,796	842,258
Less: Accumulated Depreciation	473,659	433,057
Net Property and Equipment	466,137	409,201
Goodwill	85,342	84,608
Investments in Unconsolidated Affiliates	64,469	61,598
Other	40,456	39,928
TOTAL ASSETS	$ 1,138,033	$ 989,568
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 78,691	$ 64,306
Accrued liabilities	164,768	142,168
Income taxes payable	27,766	16,193
Total Current Liabilities	271,225	222,667
Long-term Debt	195,000	174,000
Other Long-term Liabilities	60,778	56,783
Commitments and Contingencies		
Shareholders Equity	611,030	536,118
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 1,138,033	$ 989,568

The accompanying Notes are an integral part of these Consolidated Financial Statements.

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OCEANEERING INTERNATIONAL, INC. & SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(unaudited)
(in thousands, except per share amounts)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2006	2005	2006	2005
Revenue	$ 311,063	$ 235,970	$ 600,572	$ 446,707
Cost of Services and Products	239,106	195,403	468,298	372,937
Gross Margin	71,957	40,567	132,274	73,770
Selling, General and Administrative Expense	24,058	19,907	46,411	38,617
Income from Operations	47,899	20,660	85,863	35,153
Interest Income	62	93	130	154
Interest Expense, net of amounts capitalized	(3,131)	(2,221)	(5,922)	(4,415)
Equity Earnings of Unconsolidated Affiliates	3,879	3,956	8,233	8,048
Other Income (Expense), net	(1,192)	260	(1,187)	230
Income before Income Taxes	47,517	22,748	87,117	39,170
Provision for Income Taxes	16,916	8,075	31,014	13,905
Net Income	$ 30,601	$ 14,673	$ 56,103	$ 25,265
Basic Earnings per Share	$ 0.57	$ 0.28	$ 1.05	$ 0.49
Diluted Earnings per Share	$ 0.56	$ 0.28	$ 1.02	$ 0.48
Weighted Average Number of Common Shares	53,756	51,731	53,651	51,619
Incremental Shares from Stock Options and Restricted Stock	1,332	1,432	1,281	1,473

Weighted Average Number of Common Shares and Equivalents	55,088	53,163	54,932	53,092

The accompanying Notes are an integral part of these Consolidated Financial Statements.

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OCEANEERING INTERNATIONAL, INC. & SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(in thousands)

	For the Six Months Ended June 30, 2006	2005
Cash Flows from Operating Activities:		
Net income	$ 56,103	$ 25,265
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	38,345	36,190
Noncash compensation and other	5,844	820
Undistributed earnings of unconsolidated affiliates	(2,870)	(6,976)
Increase (decrease) in cash from:		
Accounts receivable	(39,431)	(2,768)
Inventory and other current assets	(49,316)	(19,544)
Other assets	(803)	(102)
Current liabilities	48,559	6,504
Other long-term liabilities	3,995	2,940
Total adjustments to net income	4,323	17,064
Net Cash Provided by Operating Activities	60,426	42,329
Cash Flows from Investing Activities:		
Business acquisitions, net of cash acquired		(42,634)
Purchases of property and equipment and other	(89,815)	(39,745)
Net Cash Used in Investing Activities	(89,815)	(82,379)
Cash Flows from Financing Activities:		
Net proceeds of revolving credit and other long-term debt	21,000	48,417
Proceeds from issuance of common stock	5,103	7,709
Excess tax benefits from stock option exercises	1,935	1,541
Net Cash Provided by Financing Activities	28,038	57,667
Net increase/(decrease) in Cash and Cash Equivalents	(1,351)	17,617
Cash and Cash Equivalents Beginning of Period	26,308	16,781

Cash and Cash Equivalents — End of Period	$ 24,957	$ 34,398

The accompanying Notes are an integral part of these Consolidated Financial Statements.

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OCEANEERING INTERNATIONAL, INC. & SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of Presentation and Significant Accounting Policies

We have prepared these unaudited consolidated financial statements pursuant to instructions for the quarterly report on Form 10-Q, which we are required to file with the Securities and Exchange Commission. These financial statements do not include all information and footnotes normally included in financial statements prepared in accordance with generally accepted accounting principles. These financial statements reflect all adjustments that we believe are necessary to present fairly our financial position at June 30, 2006 and our results of operations and cash flows for the periods presented. All such adjustments are of a normal and recurring nature. The financial statements should be read in conjunction with the consolidated financial statements and related notes included in our annual report on Form 10-K for the year ended December 31, 2005. The results for interim periods are not necessarily indicative of annual results.

On May 12, 2006, our Board of Directors declared a two-for-one stock split to be effected in the form of a stock dividend of our common stock to our shareholders of record at the close of business on May 25, 2006. The stock dividend was distributed on June 19, 2006. All historical share and per share data in this Form 10-Q reflects this stock split. The total number of authorized shares of common stock and par value were unchanged by this stock split. We have restated shareholders equity to give retroactive recognition of the stock split for all periods presented by reclassifying an amount equal to the par value of the additional shares issued through the stock dividend from additional paid-in capital to common stock.

The preparation of financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period. Actual results could differ from those estimates.

2. Investments in Unconsolidated Affiliates

Our investments in unconsolidated affiliates consisted of the following:

	June 30, 2006	Dec. 31, 2005
	(in thousands)	
Medusa Spar LLC	$ 63,132	$ 57,440
Smit-Oceaneering Cable Systems LLC		2,811
Other	1,337	1,347
Total	$ 64,469	$ 61,598

We own a 50% equity interest in Medusa Spar LLC. Medusa Spar LLC owns a 75% interest in a production spar platform, which is currently located at the site of the Medusa field in the Gulf of Mexico. Medusa Spar LLC s revenue is derived from processing oil and gas production for a fee based on the volumes processed through the platform (throughput). The majority working interest owner of the Medusa field has committed to deliver a minimum throughput, which we expect will generate sufficient revenue to repay Medusa Spar LLC s bank debt. Medusa Spar LLC financed its acquisition of its 75% interest in the production spar platform using approximately 50% debt and 50% equity from its equity holders. We believe our maximum exposure to loss from our investment in Medusa Spar LLC is our current carrying value of $63.1 million. Medusa Spar LLC is a variable interest entity.

As we are not the primary beneficiary under Financial Accounting Standards Board (FASB) Interpretation Number 46, *Consolidation of Variable Interest Entities,* we are accounting for our investment in Medusa Spar LLC under the equity method of accounting. Equity earnings from Medusa Spar LLC reflected in our financial statements are after amortization of our initial acquisition costs. The following are summarized 100% statements of operations of Medusa Spar LLC.

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	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2006	2005	2006	2005
	(in thousands)			
Medusa Spar LLC				
Condensed Statements of Operations				
Revenue	$ 9,693	$ 10,995	$ 20,726	$ 22,128
Depreciation	(2,370)	(2,370)	(4,739)	(4,739)
General and administrative	(60)	(35)	(76)	(51)
Interest	(506)	(609)	(997)	(1,261)
Net Income	$ 6,757	$ 7,981	$ 14,914	$ 16,077
Equity earnings reflected in our financial statements	$ 3,348	$ 3,840	$ 7,382	$ 7,849

We own a 50% interest in Smit-Oceaneering Cable Systems LLC, a cable-lay and maintenance venture. In March 2005, we purchased the cable-lay and maintenance equipment from the venture, and in June 2006, we purchased the vessel from the venture. The vessel purchase effectively ends the operations of the venture. It will be liquidated after collection of outstanding amounts receivable and payments of remaining amounts owed to creditors.

3. Inventory and Other Current Assets

Our inventory and other current assets consisted of the following:

	June 30, 2006	Dec. 31, 2005
	(in thousands)	
Inventory of spare parts for remotely operated vehicles	$ 56,757	$ 38,981
Other inventory, primarily raw materials	66,413	39,924
Deferred taxes	12,434	9,091
Other	12,140	10,432
Total	$ 147,744	$ 98,428

Inventory is stated at the lower of cost or market. We determine cost using the weighted-average method.

4. Debt

Our long-term debt consisted of the following:

	June 30, 2006	Dec. 31, 2005
	(in thousands)	
6.72% Senior Notes	$ 100,000	$ 100,000
Revolving credit facility	95,000	74,000

Total	$ 195,000	$ 174,000

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Scheduled maturities of our long-term debt as of June 30, 2006 were as follows:

	6.72% Notes	Revolving Credit	Total
		(in thousands)	
Remainder of 2006	$ 20,000	$	$ 20,000
2007	20,000		20,000
2008	20,000	95,000	115,000
2009	20,000		20,000
2010	20,000		20,000
Total	$ 100,000	$ 95,000	$ 195,000

Maturities through June 30, 2007 are not classified as current as of June 30, 2006, since we can extend the maturity by reborrowing under the revolving credit facility with a maturity date after one year. We capitalized interest charges of $47,000 in the first quarter of 2006 as part of construction-in-progress.

5. Shareholders Equity and Comprehensive Income

Our shareholders equity consisted of the following:

	June 30, 2006	Dec. 31, 2005
	(in thousands)	
Common Stock, par value $0.25; 90,000,000 shares authorized; 53,947,738 and 53,558,888 shares issued	$ 13,487	$ 13,390
Additional paid-in capital	181,088	172,437
Retained earnings	404,134	348,031
Other comprehensive income	12,321	2,260
Total	$ 611,030	$ 536,118

Comprehensive income is the total of net income and all nonowner changes in equity. The amounts of comprehensive income for the periods indicated are as follows:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2006	2005	2006	2005
		(in thousands)		
Net Income per Consolidated Statements of Income	$ 30,601	$ 14,673	$ 56,103	$ 25,265
Foreign Currency Translation Gains (Losses)	6,537	(5,194)	9,441	(9,317)
Change in Minimum Pension Liability Adjustment, net of tax		14	566	641
Change in Fair Value of Hedge, net of tax	8	(170)	54	361
Total	$ 37,146	$ 9,323	$ 66,164	$ 16,950

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Amounts comprising other elements of comprehensive income in Shareholders Equity are as follows:

	June 30, 2006	Dec. 31, 2005
	(in thousands)	
Accumulated Net Foreign Currency Translation Adjustments	$ 13,732	$ 4,291
Minimum Pension Liability Adjustment	(1,983)	(2,549)
Fair Value of Hedge	572	518
Total	$ 12,321	$ 2,260

6. Income Taxes

During interim periods, we provide for income taxes at our estimated annual effective tax rate, currently 35.6% for 2006, using assumptions as to (1) earnings and other factors that would affect the tax calculation for the remainder of the year and (2) the operations of foreign branches and subsidiaries that are subject to local income and withholding taxes.

We paid cash taxes of $18.8 million and $12.2 million for the six-month periods ended June 30, 2006 and 2005, respectively.

7. Business Segment Information

We supply a comprehensive range of technical services and specialty products to customers in a variety of industries. Our Oil and Gas business consists of five business segments: Remotely Operated Vehicles (ROVs); Subsea Products; Subsea Projects; Mobile Offshore Production Systems; and Inspection. Our Advanced Technologies business is a separate segment that provides project management, engineering services and equipment for applications outside the oil and gas industry. Unallocated expenses are those not associated with a specific business segment. These consist of expenses related to our incentive and deferred compensation plans, including restricted stock and bonuses, as well as other general expenses.

There are no differences in the basis of segmentation or in the basis of measurement of segment profit or loss from those used in our consolidated financial statements for the year ended December 31, 2005. The following summarizes certain financial data by business segment:

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	For the Three Months Ended			For the Six Months Ended	
	June 30, 2006	June 30, 2005	March 31, 2006	June 30, 2006	June 30, 2005
			(in thousands)		
Revenue					
Oil and Gas					
ROVs	$ 98,641	$ 75,607	$ 88,947	$ 187,588	$ 143,223
Subsea Products	81,815	49,038	84,518	166,333	89,716
Subsea Projects	42,989	23,464	41,120	84,109	47,942
Mobile Offshore Production Systems	12,355	12,747	13,332	25,687	24,110
Inspection	42,545	43,463	33,423	75,968	80,395
Total Oil and Gas	278,345	204,319	261,340	539,685	385,386
Advanced Technologies	32,718	31,651	28,169	60,887	61,321
Total	$ 311,063	$ 235,970	$ 289,509	$ 600,572	$ 446,707