Introduction
Good afternoon.

Marcon International provides consulting and brokerage services to the towing and offshore petroleum industries. While our primary focus is sale and purchase, we also arrange charters, perform appraisals and review project feasibility.

For the past twenty-four years Marcon has published a newsletter, mailed out to about 9,000 companies worldwide, listing a portion of the vessels we have for sale. We also produce quarterly market reports on the industry. The “printed word” expanded in 1994 to include an internet site updated daily.

Since the first supply boat sold by Marcon in 1983, we have brokered over 700 vessels and barges, including about 100 supply or tug supply vessels, plus have several sales pending.

I would like to provide a brief overview of the Gulf of Mexico offshore support vessel market, how vessel values are changed by that market, and the indicators that we, as brokers, follow.

Values
Values are affected by a number of factors; including vessel type, age, condition and trading restrictions. Independent of the vessel itself, values are equally dependent on the market at the time of the sale.

Vessel Types
Following is a breakdown of those types of vessels most likely to be financed or leased.
“Mini-suppliers” are a recent addition to the fleet with the first few being 110 – 120’ utility boats later stretched to 140’ in length. Like many vessel classes, purpose-built mini-suppliers are becoming larger with 200’ vessels now operating.

Straight supply or Platform Supply Vessels, like mini-suppliers, transport cargo and personnel to and from offshore platforms. These range from 150’ to over 300’ in length. The early standard was the 165’ straight supply boat with a capacity of about 700 – 850 tons, 2-3,000cft dry bulk and no bow thruster – at least at first. A natural progression was the 180’ hull with increased deadweight, about 4,000cft dry bulk plus liquid mud. Most were fitted with bow thrusters, but other than that there was no real increase in maneuverability over early 165 foot “plain jane” supply boats.

The first 220’ boats doubled capacities of the 180 footer, evolving in the late 90’s to the present designs for 220 – 280’ boats. In addition to hauling more cargo, many have increased maneuverability with joysticks, 360 degree azimuthing propulsion and/or dynamic positioning.

Anchor handling tug supply boats perform many of the same functions as supply vessels, but are fitted with double or triple drum winches and higher horsepower. Most of the U.S. fleet under 7,200HP was built between 1972 and 1984, but newer boats are now operating between 12,000 and 30,000HP.

Fast Supply Vessels are basically aluminum “crewboats” on steroids, designed to transport personnel and cargoes in smaller capacities than supply boats, but at higher speeds. Initially built between 65’ and 110’ in length, these have now expanded to “Fast Supply Vessels” up to 200’, carrying 92 passengers and 400 tons of deck cargo at speeds of 25kn.

Vessel values and the industry have gone through many ups and downs over the last twenty years. As we came out of previous depressions, many operators first rebuilt and stretched older hulls, before starting to build new. As we come out of this downturn though, it is unlikely that any effort will be put into rebuilding older hulls except in isolated cases. Costs are just too great to convert a 25 – 30 year old boat plus owners are taking a longer viewpoint, embracing new construction for fleet renewal.

**Vessel Age**

When appraising existing fleets, one factor Marcon uses is a 25-year lifespan, whereby vessels are depreciated an average of 4% per year. When Marcon started marketing OSV’s in the early 80’s, many operators declared vessels surplus at fifteen years of age. The average U.S. fleet age now is about 21 years. Vessel and market conditions though always have a greater effect on value than depreciation.
**Vessel Condition**

"Condition, Condition, Condition"\{12\} in vessel sales is like “Location, Location, Location” in real estate. Some items considered when determining values, in addition to physical condition, are class status; whether operating or laid-up and when last drydocked - as costs to drydock and renew certificates, even for an operating boat, can easily run over $300,000.

For years Marcon has tracked both asking and actual sales prices. This assists in establishing a base-line for a specific class of vessel. For example, Marcon has 67 supply vessels for sale worldwide between 180\{13\} and 190’ in length ranging from $525,000 to $1,750,000. Adjusting for age, size and horsepower differences, the average asking price for a “typical” 20-year old 180-footer would be just under a million dollars. There is a difference, however, between asking price and price achieved. During 2004, actual sales prices for all Marcon sales averaged about 86.5% of the asking price. Therefore, a concluded “base-line” price for our “typical” 180’, 20-year old supply boat, should be about $865,000.

Sale prices vary dramatically, above and below the average depending on condition.\{14\} In January, we sold a working, 200’, twenty-one year old, supply boat in Southeast Asia for just over $3,000,000. In December, another buyer inspected two twenty-four year old laid-up boats in the Gulf of Mexico priced at $950,000 each, rejected both due to condition, and is now \{15\} buying a forty-year old boat at a slightly higher price.

**The Market**

In addition to values being affected by vessel type, age, capacities and condition, the market plays a critical and equal part. For the last three years, the Gulf of Mexico supply boat market has been depressed. There just has not been sufficient drilling to keep even half \{16\} the OSV fleet employed. This lowered many vessel values. Good equipment, in class and actively working, is holding its value - but there is little interest in older laid-up boats.

**Day Rates & Utilization**\{17\} Vessel values are dependent on the revenues that a boat can earn. Day rates and utilization are important indicators of this earning capability, with the actual level strictly a “supply and demand” issue. “Supply” is determined by the number of vessels available for work, and “demand” controlled by the level of activity of drilling companies. In addition to being affected by the lack of, or availability of, work, corporate strategies sometimes also are involved.
In 1994, Tidewater’s domestic supply vessels were achieving 90% utilization - but at rates below $4,000 per day. At this time, operators were throwing boats into the market and bidding against each other to just get the work. Dayrates and utilization went through several more cycles, but after 2001, rates never approached earlier lows. This was due to a strategic decision, primarily made by Tidewater, to lay up surplus boats in order to support higher charter rates at the expense of dramatically lower utilization. The industry did avoid accelerating the downward spiral in day rates. However Tidewater, for example, ended up “cold-stacking” about 70% of their domestic supply and towing supply vessel fleet.

In March 2004 Tidewater declared 83 older domestic vessels “impaired”, taking a non-cash asset charge of $26.5 million. This was wise - due to the prolonged market weakness, vessels’ average age of 23.5 years, outdated specs, cost to return to service, and low customer demand. The voluntary withdrawal, not only by Tidewater, improved utilization statistics by reducing non-working boats in the count. More importantly though, this withdrawal tightened the supply side of the vessel equation. As demand improves, owners are now able to push for higher day rates.

Rig Counts

Rig counts are an important business barometer, as an average of one-and-a-half to two supply boats are required to service each active offshore rig. The rig count therefore acts as a leading indicator of demand for boat services – and as the graph shows the offshore rig count fell in 2001 - which is also when OSV utilization plummeted.

Over the last two years we have been asked why the Gulf of Mexico market has been depressed when everyone is reading about the high price of crude oil and paying top dollar at the gas pump. The Baker Hughes Rig Count followed the price of crude oil up until mid-2002, but afterwards the numbers diverge. Most drilling activity in the Gulf of Mexico is driven by natural gas instead of oil. While natural gas prices generally track oil prices, crude oil pricing has recently been influenced more by geo-political issues than the normal “supply and demand” factors affecting natural gas.

Energy Prices and E&P Budgets

Rig count trends are governed by oil company exploration and development spending, which in turn are normally influenced by energy prices. While we experienced record high crude oil prices in 2004 and oil companies saw record profits, this did not translate immediately into increased spending. Oil companies are not likely to base future drilling programs on relatively short-term “spikes”.

With energy prices driven by other factors than just “supply and demand”, it made more sense to spend windfalls on purchasing reserves, mergers, and stock buy-backs than drilling. When companies did drill, it was concentrated on land-based rigs in the United States which are less “service-intensive” than offshore.
What can we expect for 2005 onwards. Headlines in trade journals trumpet an increase in E&P spending worldwide in 2005 – but in reality there is not a lot of extra money for the Gulf of Mexico. Planned increases by oil and gas companies include both on-shore and off-shore drilling worldwide plus some of the funds will be absorbed by higher drilling and service costs, rather than providing for many new working rigs. Gulf of Mexico offshore spending will increase only slightly. Activity is still slow as we speak; with the Baker Hughes U.S. offshore rig count down three in January compared December 2004. The improvement in the OSV market will, at first, have to come mostly from control on the “supply side” rather than any substantial growth in demand – but there will be improvement.

Summary
Although there is a large fleet of laid-up vessels, good working boats are again becoming in short supply in the Gulf of Mexico. Not only does it seem like déjà vu, but it even like “déjà vu all over again” in the words of Yogi Berra. Most offshore support vessels that can work, are working. Operators are putting customers on notice that rates are rising and contract terms need to be longer.

Some domestic vessels relocated overseas will return and increase the supply, but we enter this upswing with a different dynamic than in the past. The key reason for the improvement in rates was the voluntary removal of many surplus vessels built during and just before the early 80’s construction boom. Marcon expects that this time the majority of these boats will stay out of active service permanently, partially due to owner’s discipline and more likely due to the substantial cost to re-activate.

Domestic new construction slowed over the last two years, but Marcon expects newbuilding activity to pick-up in 2006 and 2007 as operators look to renew fleets with larger, more efficient supply vessels and higher horsepower anchor handlers.

The present recovery is very fragile and the industry will always continue to have market swings. Marcon International though is optimistic for the longterm future health of the offshore support vessel industry, not only in the Gulf of Mexico, but worldwide through 2005 and beyond. The industry however needs to keep the “supply and demand” equation for OSV’s in balance.

Thank you.