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## ESV - Q2 2009 Ensco International Earnings Conference Call

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**Brian Uhlmar**

## PRESENTATION

**Operator**

Good day everyone and welcome to the Ensco International second quarter of 2009 earnings conference call. As a reminder, this call is being recorded and your participation constitutes consent to its taping.

I will now turn this conference over to Mr. Sean O'Neill, VP of Investor Relations, who will moderate the call. Please go ahead, sir.

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**Sean O'Neill** - *Ensco International - VP of IR*

Good morning and welcome to Ensco's second quarter of 2009 conference call. With me in Dallas are Dan Rabun, Chairman and CEO, Bill Chadwick our COO and Jay Swent, Chief Financial Officer, as well as other members of our executive management team. This morning we issued our earnings release which is available on our website at enscointernational.com. Later today we plan to file our SEC Form 10(Q). As usual, we will keep our call to one hour. Any comments we make about expectations are forward-looking statements and are subject to risks and uncertainties. Many factors could cause actual results to differ materially. Please refer to our earnings release and SEC filings on our website that define forward-looking statements and list risk factors and other events that could impact future results. Also, please note that the Company undertakes no duty to update forward-looking statements. As a reminder, our monthly rig status report was last issued on July 15. Now let me turn it over to Dan Rabun, Chairman and CEO.

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**Dan Rabun** - *Ensco International - CEO, President*

Thanks, Sean, and good morning everyone. First, let me introduce Sean O'Neill to those of you who have not had the opportunity to meet him. Sean joined us in May as Vice President of Investor Relations and he brings many years of investor relations experience. We are pleased to have him with us.

Before we get into the numbers, I'm going to take a few minutes to provide you a mid-year update on some important milestones that we achieved so far this year and also comment on our overall competitive position. Let me start with our deepwater business.

As many of you know, in 2005 we strategically embarked on our deepwater expansion plan to build the first of the ENSCO 8500 Series rigs. On June 6, it was extremely gratifying to announce that the first of the ENSCO 8500 Series rigs has commenced drilling operations and is now on the payroll. This is a major milestone in the history of our Company and the startup and operation of the rig has gone extremely well. Also in June we announced that ENSCO 8501, the second in the series, was delivered in Singapore and is now in transit to the Gulf of Mexico. We expect ENSCO 8501 will arrive in the Gulf of Mexico on August 2, 2009.

Together with ENSCO 7500 working in Australia, we now have three ultra-deepwater semisubmersible drilling rigs. Our success with ENSCO 7500, which has been in our fleet since 2000, gave us the confidence to launch the ENSCO 8500 series program. In total, we are now investing more than $3 billion over eight years to build seven new ultra-deepwater rigs. Next year we expect to add two more 8500 series rigs to our fleet, both of which are already under contract. During 2011 and 2012, we plan to take delivery of three more ultra-deepwater semis bringing our total fleet to eight rigs.

With five of the eight rigs under contract, we already have locked-in a sizeable stream of revenues and we expect the final three rigs in the series will be delivered as scheduled. Although we have had some minor delays in our initial deliveries, overall I'm very pleased with our performance in terms of meeting our timetables for the newbuild program, especially relative to others



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who have had long delays. I feel very comfortable about customer demand for our three remaining uncontracted rigs and I'll discuss the deepwater markets in a moment.

As some of you may recall, we are using a proprietary design for the ENSCO 8500 Series rigs that was developed through extensive discussions with our customers. All seven newbuild rigs have the same design and are being built in the same shipyard, giving us enormous efficiencies in terms of construction, daily operations, repairs and maintenance, spare parts and training. It's also worth noting that the first four 8500 Series rigs will all be working in the Gulf of Mexico which gives us additional economies of scale.

Another major milestone that we achieved is passing the halfway mark for the funding of our $3 billion plus investment in the 8500 Series program. Remaining commitments for the ENSCO 8500 Series program are now less than $1.4 billion. I should add that we have not financed these newbuilds through debt but rather through operating cash flows. Our cash position has continued to improve since the end of the quarter and now stands at approximately $1 billion, and our long-term debt is just 5% of total capital.

So in a nutshell, our deepwater expansion strategy is beginning to pay off in a major way. We are in a great position in terms of our balance sheet strength, and I mention these milestones because it is important to note that they will not only buffer us from some of the current challenges in the jackup market, but also provide us long-term growth opportunities.

In hindsight, bolstering our balance sheet was clearly the right defensive move, given the decline in the global economy. As we look ahead, we believe our strong balance sheet also gives us an offensive capability as we consider new investment alternatives. Our commitment to disciplined investing hasn't changed and we remain committed to meeting our strict return criteria.

Finally, before I provide a market overview, we were very pleased to receive accreditation from the International Association of Drilling Contractors for our offshore competency assurance programs. Our investment in employee development is just that, an investment. Training our workforce leads to improved safety, more efficient operations and greater reliability for our customers. And I should add that our safety record has been exceptional again this year.

Now let's talk about the markets.

During the second quarter challenges in the jackup market continued as we indicated they were during our last earnings call. Jackup utilization declined further as customers continue to be cautious about new programs in the face of unfavorable credit markets and unstable oil and gas prices that were driven in part by lower demand and rising inventories. As more jackups roll off existing contracts and more newbuilds enter the market, we expect the supply demand and balance will become more acute, although, cold stacking of rigs will provide some relief. For Ensco, jackup utilization in the second quarter was 72% down from 79% in the first quarter and 95% a year ago. Average jackup day rates were also down sequentially from $168,000 in the first quarter to $159,000 in the second quarter. Year-over-year day rates were up $10,000 from $149,000 in last year's second quarter.

Given the challenges of the current environment, we will continue to market heavily and pursue opportunities in all the major markets around the world. When we do not see prospects for work, we will cold stack rigs to sharply lower cost as we did with two rigs in the second quarter.

We believe we continue to have a cost advantage versus most of our peers and will continue to actively manage our cost stand wherever possible. Now let me turn to specific regions.

The Middle East and Southeast Asia/Pacific Rim remain very competitive markets, although we have recently seen a very noticeable increase in discussion levels and bidding activity for work starting late this year or in 2010. The most active areas are the United Arab Emirates, Indonesia, India and China with several other areas having one or two jackup requirements. Saudi



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Aramco has not tendered for rigs yet, but reportedly will start developing two newly discovered offshore gas fields and is targeting a 50% increase in non-associated natural gas production by 2015 to help meet rising domestic demand. In the North Sea with ongoing shortage of funding from financial institutions and low natural gas prices, operators continue to defer programs and there are only a few short-term opportunities for work in 2009. However, there has also been a recent increase of short and longer term programs surfacing for work starting in 2010 and beyond.

Turning to the US Gulf of Mexico, the jackup market continues to shrink. The impact of lower natural gas prices is being exacerbated by unfavorable credit markets and the onset of hurricane season. More drillers, including Ensco, are cold stacking rigs and we are being even more selective on drilling locations during hurricane season. We expect only a few new drilling opportunities until we emerge from the hurricane season and day rates will remain under pressure during this period.

The good news is that we've been successful in moving rigs to Mexico. We now have four jackups working for Pemex and we will move one more to Mexico from the Gulf in the third quarter.

Also on a positive note, we expect Pemex will tender soon for three incremental 300 foot independent cantilever jackups for work in Mexico starting in 2010.

To give you some perspective on the longer term shift in our business, in 2005 when we made this strategic decision to expand our deepwater business, the Gulf of Mexico was our largest market and jackup revenues accounted for one-third of our total company-wide revenues. With the expansion of our deepwater fleet and mobilizations of jackups for international markets, we anticipate that third quarter revenues for our jackup fleet in the Gulf of Mexico to be only 6% of revenue.

In Venezuela we have kept everyone informed about the status of ENSCO 69 through our news releases during the quarter and more information will be contained in our Form 10-Q to be filed later today. Jay will address the accounting more fully, but we won't be commenting beyond our prepared remarks since we are in the process of pursuing claims as we have disclosed. More broadly in South America, new jackup programs are emerging in Brazil, Columbia, Trinidad, Suriname, and Guyana and we are pursuing all of these opportunities.

Now let's turn to deepwater. Brazil remains by far the strongest market. Operators in the region are continuing to report successes in their exploration programs and these discoveries are expected to lead to development work possibly starting by late 2011. Petrobras has announced that they will tender for an additional seven or eight rigs during the third quarter with a requirement that the rigs be built in Brazil. It's still unclear how all this will unfold.

There are several outstanding bids for work elsewhere in 2010 and onward and new discoveries are being announced that are expected to require development work. West Africa continues to be an area of high activity with several multiyear existing tenders for programs -- for projects in Angola and Nigeria. Also, there are additional inquiries in tenders for work in India, China, Indonesia and Australia.

In the Mediterranean a significant gas discovery was found offshore Israel and is on the fast track for development. Work continues offshore Italy and Libya is worth watching as well.The US Gulf of Mexico is relatively quite now as far as new deepwater programs but continued exploration successes in the lower tertiary trend is expected to create additional demand for development rigs in the future. We are actively marketing and are engaged in discussions with several operators regarding perspective work programs for our three uncommitted deepwater rigs. With deliveries not scheduled until the second half of 2011 and in 2012 we fully expect that the rigs will be contracted before delivery.

During the quarter we announced that Jeff Saile would be retiring from the company and we wish him the very best. Jeff is one of our founding employees and has served in multiple management positions around the world. His dedication has been instrumental in growing our company and his commitment to the safety of our employees will long be remembered. Bill Chadwick, our Chief Operating Officer, will now add direct responsibility for North and South America business and Carey Lowe has taken over responsibility for our deepwater business. Now with those comments, let me turn it over to Jay.



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**Jay Swent** - *Ensco International - CFO*

Thanks, Dan, and good morning everyone. My comments this morning will cover details of second quarter results, our outlook for the third quarter and full year 2009 and a review of our financial position.

Before we get started, I'd like to remind everybody that ENSCO 69 financial results for current and all prior periods are now reflected in discontinued operations. The loss from discontinued operations in the second quarter was $0.18 per share. This amount is less than the $0.26 per share estimate provided in our July 15 news release because we subsequently received an $11.5 million payment from PDVSA on July 17.

Second quarter earnings from continuing operations were $1.59 per share compared to $1.98 a year ago. Earnings per share, including the loss from discontinued operations, was $1.41, down from $2.05 last year. Total revenue for the second quarter was $512 million, a 16% decline from last year. Jackup segment revenues declined $133 million or 23%. This was partially offset by a $35 million increase in deepwater revenue as ENSCO 7500 went back to work in Australia in early April at a day rate of $550,000 and ENSCO 8500 commenced drilling operations in the Gulf of Mexico in early June.

As Dan mentioned, our average jackup day rate was higher this quarter than in the second quarter last year but this was more than offset by a significant decline in utilization which dropped to 72%. Currently, we have 11 jackups warm stacked and two are cold stacked. We reduced total contract drilling expense for all jackup segments by 20% versus last year. Offsetting this, deepwater segment costs increased 144% due to the addition of ENSCO 8500 and ENSCO 7500 operating in Australia where expenses are higher. Overall, this nets to a 12% reduction in total contract drilling expense.

We took the following actions to reduce drilling costs during the second quarter. First, we closely managed all elements of our cost structure to reduce year-over-year costs. Specifically, we cold stacked two jackup rigs and reduced personnel on idle rigs to reduce expenses where we did not see near-term prospects for additional work; and we continue to press vendors and service providers for cost reductions. Now let's discuss quarterly trends by comparing second quarter 2009 sequentially to the first quarter 2009.

Please remember that the income statement for first and second quarter reflects ENSCO 69 results in discontinued operations as I mentioned earlier. Second quarter revenue of $512 million increased slightly from first quarter levels. This increase is attributable to a $68 million increase in deepwater revenue for the reasons previously mentioned which was largely offset by a decline in jackup revenues in Asia Pacific, Europe and Africa.

Contract drilling expense was up 9% sequentially from the first quarter versus our 15% estimate last quarter.

This breaks down as follows. We had an $18.9 million increase for the deepwater segment primarily due to ENSCO 7500 and ENSCO 8500 commencing drilling operations during the second quarter and jackup expenses decreased by $4.8 million due to lower utilization and cost containment actions offset in part by higher costs associated with operating rigs in Mexico and Venezuela as well as higher repair and maintenance on rigs that were not contracted. As we've done historically, we are taking advantage of rig downtime to complete surveys and repair and maintenance work so that our fleet is ready for when the market turns.

Looking at other expenses, as expected depreciation increased by $2 million due mainly to ENSCO 8500 coming online during the quarter. G&A expense was up $4 million more than we had predicted last quarter due to an early retirement of the senior executive and higher professional fees. Our cash generation remains strong during the first half of 2009 with cash from operations totaling $586 million. Cash on hand at quarter end was $882 million even after $472 million of capital investments during the first six months, $329 million of which related to our deepwater fleet expansion.



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Let's now look at the outlook and our expectations for third quarter 2009. Revenue is expected to decrease by about 12% from second quarter levels. More jackup rigs are likely to become idle and day rates will remain under pressure. We expect to see a 12% decline in average number of days our jackups are utilized in the third quarter when compared to second quarter.

Higher revenue from the deepwater segment should partially offset these factors. However, I should point out that we anticipate ENSCO 7500 will have non-routine downtime to replace recently installed equipment that failed prematurely. This will impact third quarter revenues by approximately $12 million. We expect third quarter contract drilling expense will increase by approximately 4%. Deepwater expenses will increase 46% because ENSCO 7500 and ENSCO 8500 combined will have 43% more operating days in the third quarter. This will be partially offset by a 2% decline in the jackup segments.

Depreciation expense will increase by approximately $5 million in the third quarter mostly due to adding ENSCO 8500 to the fleet. Finally, we anticipate G&A expense will be approximately $14 million during the third quarter.

Now a few comments about our 2009 full year outlook. The revenue contribution from our deepwater fleet is projected to more than triple in 2009 to approximately $280 million. In addition, we expect 2010 deepwater revenues to more than double again to approximately $600 million. Contract drilling expense is estimated to decrease by 5% from last year's level of $752 million. I'd point out here for everyone that this is the number after adjusting for discontinued operations treatment of ENSCO 69. Deepwater segment expenses will increase by approximately 236% reflecting higher activity levels, but this will be more than offset by our cost containment actions that we are taking, including stacking of jackup rigs which will reduce jackup segment expenses by approximately 15%.

In July we completed our insurance renewals and, as expected, insurance premiums have increased significantly. We have elected to purchase windstorm coverage for ENSCO 8500 but given the prohibitively expensive premiums that were quoted by underwriters, we have not purchased windstorm coverage for our Gulf of Mexico jackups. Since last year, we have reduced our Gulf of Mexico jackup rig exposure significantly to just five rigs now marketed in the US Gulf. To further mitigate risk, we are being very selective about the drilling locations we will accept during hurricane season.

We expect 2009 depreciation to increase approximately 12% to $210 million due to the addition of our two new ultra-deepwater rigs. G&A expense will approximate last year's level of $54 million. Our effective tax rate is projected to be approximately 19% for the year as we indicated last quarter. 2009 capital spending projections are unchanged from last quarter but please remember that enhancements and sustaining budgets may be adjusted over the balance of the year. At this point, we expect 2009 capital spending to be approximately $790 million with $530 million committed to our 8500 Series rigs, $160 million for rig enhancement projects and $100 million for sustaining projects.

Let's now turn to the balance sheet. We have steadily strengthened our financial position despite turbulent market conditions and the significant cash investments that we have made to expand our ultra-deepwater fleet. Our strong balance sheet has a distinct advantage given the challenges of the current market environment and provides us the financial flexibility to consider future investment opportunities that meet our strict return criteria.

During the second quarter, Standard & Poor's reissued its rating on Ensco and assigned us a BBB+ corporate credit rating. In its report, S&P noted that Ensco's credit measures are currently strong for the BBB+ rating and compare favorably to the investment grade peer group. In particular, S&P cited our strong cash position, our $350 million revolving credit facility that is fully available, our low debt levels with no significant near-term maturities, a growing ultra-deepwater fleet, global diversification and our ability to maintain strong operating margins and returns on capital. I think S&P summed up our position quite well. Moody's also has a similar credit rating for Ensco of BAA1.

In summary I'd like to note the following, our growing deepwater fleet is ramping up nicely and we project its contribution to earnings will grow significantly. This should help offset some of the weakness that we are currently experiencing in our jackup markets. On the expense side, we are aggressively managing cost during the current slow down and we will continue to stack jackup rigs as we did in the second quarter to reduce costs where we do not have reasonable prospects for work. We have a



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very strong balance sheet and I think we are very well-positioned to not only weather the difficulties of the current market but also take advantage of potential opportunities as they arise.

The level of customer inquiries has improved for programs starting in 2010 and if oil prices can stabilize around current levels, we believe this will be very positive for demand for contract drilling services next year, especially since customers have curtailed drilling during 2009. Now, with that, I'll turn the call back over to Sean.

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**Sean O'Neill** - *Ensco International - VP of IR*

Operator, if you could please open it up for questions.

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) We will go to our first question from Pierre Conner.

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**Pierre Conner** - *Capital One Southcoast - Analyst*

Dan, my first one is macro. You started out with a commentary of supply/demand imbalance getting worse, noted several potential opportunities coming. I wanted to get a little more perspective from you on, that's just kind of making it less of a problem than it was 90 days ago, is that the point or do you feel we can absorb -- how many of the newbuilds coming on?

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**Dan Rabun** - *Ensco International - CEO, President*

You are talking about the jackups?

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**Pierre Conner** - *Capital One Southcoast - Analyst*

Yes, sir.

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**Dan Rabun** - *Ensco International - CEO, President*

Yes. Pierre, the activity level and dialogue with customers has picked up appreciably. It is hard to get a handle on the magnitude of all these opportunities because they are fairly recent in being developed and how that will affect the supply of jackups. I tend to believe what we will see is a fairly slow ramp-up in activity and I think utilization and rate increases will be under pressure for a little bit because of supply. It's a little early to see how it's all going to unfold. We have a lot of moving parts with rigs being cold stacked, and new rigs coming on board. I would say it's net positive but the effect of the newbuilds is still a question mark in my mind.

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**Pierre Conner** - *Capital One Southcoast - Analyst*

Okay. Understand. On speaking of newbuilds, we get asked it all the time, but with the backlog coming out, the potential for some of those becoming available, in your discussions do you see the bid/ask spread for any potential purchases widening? There was a recent acquisition that was a bit high from my perspective but wondered if you thought there was opportunity for some of those to be sold.



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**Dan Rabun** - *Ensco International - CEO, President*

Pierre, strangely enough it's fairly quiet on that front. So I wouldn't characterize the bid/ask spread getting any closer. There just hasn't been a lot of dialogue since the last earnings call on that front.

**Pierre Conner** - *Capital One Southcoast - Analyst*

Okay.

**Jay Swent** - *Ensco International - CFO*

I think, Pierre, just to add what we've seen over the last several months is a number of those, the operators or owners of those rigs sort of solving their financial situations for the short term in terms of getting extensions or waivers on their financing commitments. I think most people are sitting tight trying to kind of wait out the market to see if things are going to improve and I think they are hopeful they will get higher prices for those rigs in the next year or two.

**Dan Rabun** - *Ensco International - CEO, President*

One thing we do continue to see, Pierre, and it has been this way for a while, with the newbuilds. Ensco with our outstanding operational excellence and commitment to the safety of our employees, we see opportunities that newbuild companies don't see and that will continue to be the case. So notwithstanding the challenge of the supply side of the equation, Ensco will continue to get jobs and opportunities that newbuild guys won't.

**Pierre Conner** - *Capital One Southcoast - Analyst*

One last one specific for Jay or Sean, when those rigs go into accommodation mode, can you give us a rate of what that OpEx changes to, the jackups I'm talking about?

**Jay Swent** - *Ensco International - CFO*

I would say Pierre this is a rough number, it's probably $10,000 to $15,000 per day maximum. The reduction, that is.

**Pierre Conner** - *Capital One Southcoast - Analyst*

The reduction is $10,000 to $15,000.

**Jay Swent** - *Ensco International - CFO*

Yes.

**Pierre Conner** - *Capital One Southcoast - Analyst*

Thank you. The last thing, it didn't sound like Jeff was actually there.



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**Dan Rabun** - *Ensco International - CEO, President*

No, Jeff is here. So we can speak about him.

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**Pierre Conner** - *Capital One Southcoast - Analyst*

I might not say the things I was going to say then. But very personally, Jeff, congratulations, many thanks for everything, congratulations for what you've done for Ensco. We wish you all the best.

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**Jeff Saile** - *Ensco International - SVP Business Development*

Thanks, Pierre, I appreciate that.

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**Pierre Conner** - *Capital One Southcoast - Analyst*

Thank you, gentlemen.

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**Operator**

We will take our next question from Mike Drickamer with Morgan Keegan.

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**Mike Drickamer** - *Morgan Keegan - Analyst*

Good morning, guys. Real quickly about a month ago one of your competitors was talking about offering some incentives to keep the rigs working during hurricane season, offering contracts that had no day rate during evacuation. Are you guys offering any comparable incentives or asked by customers to accept comparable terms?

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**Bill Chadwick** - *Ensco International - COO*

This is Bill. No, we have not been requested to do that and we haven't considered it.

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**Mike Drickamer** - *Morgan Keegan - Analyst*

Okay. Jay, looking at the Gulf of Mexico fleet, it's interesting that you guys decided not to re-up the windstorm coverage. I can definitely understand the increase in cost. Can you update us perhaps what's the total book value of Gulf of Mexico jackup fleet or what's your exposure here?

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**Jay Swent** - *Ensco International - CFO*

I don't have the number right off the top of my head. It's pretty low. We are going to end up with seven to eight rigs in the Gulf, five that are marketed and many of which are fully depreciated on a book basis. It would be a pretty low number.

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**Mike Drickamer** - *Morgan Keegan - Analyst*

That's all for me, guys. Thank you.



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**Operator**

We will take our next question from Tom Curran with Wells Fargo.

**Tom Curran** - *Wells Fargo - Analyst*

Good morning, guys. First I'd just like to echo Pierre's sentiments, Jeff, want to wish you the best of luck and thanks for everything you've done for Ensco. Dan, curious. As you look across each of the jackup geo-markets, longer term which market do you think has the most potential for demand to surprise the upside because of the nature of the demand? In other words, there are certain markets we are all focused on because it's very clear that there is going to be incremental demands driven by long-term expansion of, say, new fields, but are there other markets where due to maybe brown field revitalization or other types of work you think the potential for demand is being underappreciated?

**Dan Rabun** - *Ensco International - CEO, President*

I am going to go out on a limb on this one. I think the market that has the potential for the most near term surprise is probably going to be the US Gulf of Mexico because the supply of rigs has dropped so dramatically and any return, any improvement in natural gas prices is going to result in an uptick in drilling activity. Plus, there's just been very little work out in the Gulf of Mexico in terms of work, overwork. It's a very large and developed area and people are not going to not drill forever. Whenever drilling activity picks up there, it's going to go up fast and sharp and I don't have any prediction of when that might occur. That's the one that historically has provided the most short-term surprises positively and negatively so I don't think that it's going to be any different in the future. I think the North Sea, quite frankly, is going to have some potential for good opportunities in the future. Again, that's a very protected market in terms of rig supply. So I think those two markets probably are going to show some surprises.

**Jeff Saile** - *Ensco International - SVP Business Development*

I will go out on a limb with you since it's not quite as dangerous for me, this is Jeff. I think he's absolutely correct about the Gulf of Mexico. One thing, there's some pent up demand manifesting itself now and there's a lot of demand out there from restoration work that needs to be done from going as far back as Rita and that has not been addressed and I think the MMS is probably going to start forcing that hand. In the short term, that should provide a little bit of activity and, as Dan was mentioning, the supply is certainly decreased out there. So I think there may be a little pleasant surprise in the short term there and then consequently the long-term will probably be affected basically the same way.

**Tom Curran** - *Wells Fargo - Analyst*

Thanks, guys, that's very helpful. One market I've been curious about is West Africa as Nigeria continues to struggle with the militant men group disruption of its onshore capacity, could we see them look to offset that with a level of investment in jackup related activity that they otherwise wouldn't have pursued or could it perhaps, could Angola seek to exploit Nigeria's troubles by ramping up its shallow water activity?

**Jay Swent** - *Ensco International - CFO*

The only thing I would say, Tom, is most of those guys have really fast boats. The notion that a jackup is exempt from those problems is probably not realistic in Nigeria. Certainly going further offshore for deepwater drilling in some of those places might help a bit, but even there those guys have really fast boats now.



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**Dan Rabun** - *Ensco International - CEO, President*

There is a very noticeable uptick in deepwater activity both in Nigeria and Angola. There are existing tender from multi-year programs from several operators outstanding in those markets currently.

**Tom Curran** - *Wells Fargo - Analyst*

So fast boats and [inaudible] are generally a good deterrent I take it. Thanks, guys. I'll turn it back.

**Operator**

Moving next we will go to Dan Boyd with Goldman Sachs.

**Dan Boyd** - *Goldman Sachs - Analyst*

Thanks. Dan I thought I heard you earlier say that you expect utilization to potentially increase in the jackup market. I wanted to make sure I heard you correctly and see if that was due at a pick up in demand or just more of you were talking about effective utilization due to stacking?

**Dan Rabun** - *Ensco International - CEO, President*

No. We indicated actually that we would see in the jackup market certainly that utilization would be going down in the third quarter.

**Dan Boyd** - *Goldman Sachs - Analyst*

When would you expect that to bottom, more talking to the tenders and activity that you see picking up, do you see a bottom at any point?

**Dan Rabun** - *Ensco International - CEO, President*

Dan, based on what we are seeing, there is a very noticeable uptick in activity for work later this year and into 2010. So we have some momentum of rigs coming off contract so when that balance is I'm not really sure but it feels like we are getting close to the bottom.

**Dan Boyd** - *Goldman Sachs - Analyst*

Okay. Helpful. And also in past conversations you've expressed an interest in if you could buy two deepwater rigs that were very similar such as remaining PetroMena rigs you would be interest there had as opposed to just one-off assets. Can you give us an update on any potential sale pros sets there and are there other opportunities that you seek to acquire multiple similarly designed rigs?

**Dan Rabun** - *Ensco International - CEO, President*

I mean there are some opportunities out there, Dan. There's not a whole lot of them. We did look at the PetroMena rigs and decide to pass on that opportunity. Our competitive advantage within ENSCO 8500 which we repeated many times is our





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operating efficiencies and that gives our -- Ensco has been pretty good about having good margins in this business and the way you do that is through efficiencies. So one-off operations just is contrary to our philosophy. So, yes, if we could fine a collection of assets that we could get efficiencies from and get them at the right price, very important, we would clearly, we are looking at opportunities, we just haven't found the right one just yet.

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**Dan Boyd** - *Goldman Sachs - Analyst*

Along the same lines, you are in a very good net cash position. You have $1 billion in cash and according to our model you still generate quiet a bit of of free cash flow even after paying for the new bill Capex you have coming up. Are you starting to think about if those opportunities don't come up returning cash to shareholders or building additional 8500 series rigs?

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**Dan Rabun** - *Ensco International - CEO, President*

We are not currently contemplating building any more 8500 Series rigs at this time. We have our hands full right now with our current program. Dan, yes, we look at that, we've said on every call we look at that every quarter with our Board very carefully. Obviously, today we feel a lot more comfortable than we did last quarter and we feel a lot more comfortable than we did six months ago about the stability of the credit markets. So, yes, we do look at that and we can't find the good use for our cash, it will get returned to shareholders.

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**Dan Boyd** - *Goldman Sachs - Analyst*

I guess the way I think about the timing of that is once you would expect that the jackup mark to be bottoming out we would start to see an uptick in utilization you would be more comfortable returning cash to shareholders as opposed to when things continue to decline. Is that fair?

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**Dan Rabun** - *Ensco International - CEO, President*

That's a fair statement. I think we said on the last few earnings calls, especially six months ago when credit markets were nonexistent, we just didn't feel real comfortable. The debt markets have opened up very nicely and most of our competitors have accessed the debt markets. We haven't felt it necessary to do that. I will say for committed lines of credit and things of that nature those markets still haven't opened up except at exceptionally high cost. So there's still some unstability out there that causes us, make us feel good about having cash on hand.

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**Dan Boyd** - *Goldman Sachs - Analyst*

Then looking forward you do pay a small dividend but historically you've preferred to buy back shares. Is that still what would you do if you did decide to return cash to shareholders through share repurchases?

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**Dan Rabun** - *Ensco International - CEO, President*

No, not necessarily, Dan, we've considered both. We have had a lot lively debate about both, so.

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**Dan Boyd** - *Goldman Sachs - Analyst*

Thank, I'll turn it back over.

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**Operator**

We will go to our next question from [Scott Gruber] with Bernstein.

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**Scott Gruber** - *Bernstein - Analyst*

Yes, good morning, gentlemen.

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**Dan Rabun** - *Ensco International - CEO, President*

Good morning.

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**Scott Gruber** - *Bernstein - Analyst*

I just have one macro question. What oil price, oil price range, do you think is needed to do drive the jackup utilization back up toward the 90% level or above?

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**Dan Rabun** - *Ensco International - CEO, President*

Quite frankly, I think we are there. I mean if you could get stability in the commodity price for a long time I think quite frankly this is extremely healthy price.

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**Unidentified Corporate Representative** - *Ensco International*

Lack of confidence right now.

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**Scott Gruber** - *Bernstein - Analyst*

So if oil prices stay in the mid 60s around 70, how long do you think it would take to reach back up to 90% given the newbuilds coming out?

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**Dan Rabun** - *Ensco International - CEO, President*

I can't give you any prediction of timing. One thing I've learned about in this business and the period I've been here the words you never say, it's different this time. I don't think it's any different this time if you look at historic charts of commodity prices and utilization and day rates, there's a pretty good historic trend there and quite frankly I think if you look at historic trends at this price you would see fairly high utilization and fairly good day rates and we don't expect it will be any different this time. We do have a little bit different factor because of the supply side of the equation and natural gas prices are not particularly robust, so it's not exactly a parity with oil and gas prices anymore. So there are a few factors that are a little bit different. But clearly if commodity prices stay at this level I would fully expect the day rates and utilization would go up.

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**Scott Gruber** - *Bernstein - Analyst*

Okay. Great. That's all I had. I'll turn it back.

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**Operator**

We will take our next question from Arun Jayaram with Credit Suisse.

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**Arun Jayaram** - *Credit Suisse - Analyst*

Good morning, guys.

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**Dan Rabun** - *Ensco International - CEO, President*

Good morning.

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**Arun Jayaram** - *Credit Suisse - Analyst*

Jay, I want to drill a little bit on the operating costs just broadly how we should think about the cost for stacked equipment versus rigs that you list as available or idle in your fleet status report on the jackup front. And also given the costs associated with getting the 7500 over to Australia, what is the cost per day including the amortization of the (inaudible)?

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**Jay Swent** - *Ensco International - CFO*

Let me try to take your first question, Arun. I think in terms of rigs that are cold stacked, probably safe to think in terms of $5,000 a day would be the cost of that. Although I'd caution you, as we said, we are looking at this as an opportunity in the shipyards are a little slower than they were before, costs are a little better now than they have been before, so we are looking at this as an opportunity where it makes sense to do some repair and maintenance work. Obviously we are not going to go overboard on that. Some of these rigs will get stacked, either warm or cold stacked, but there will be some level of work probably done on them. I think relative to a warm stacked rig, we've said you are probably going to take $10,000 to, $15,000 per day off of the normal operating cost just to be in warm stack mode. I think we've tried to be, as I said in my comments, I think we tried to be pretty careful about that and get as many people off the rigs as we can when they go into warm stack status, certainly make sure we keep all the senior people on board but where we can get the headcount down just as low as we possibly can. On the 7500 -- if you wouldn't mind, let me have Sean get back to you with the specific numbers on that. They are large.

---

**Arun Jayaram** - *Credit Suisse - Analyst*

I just want to make sure we get that right because they are large. Last question in terms of your guidance, Jay, in the back half of the year you have 11 jackups which roll off their current contract. There are options associated with those but what do you think in terms of your ability to keep those rigs operating? What are you assuming for the third quarter in terms of the ability to get new contracts and rigs that roll off?

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**Jay Swent** - *Ensco International - CFO*

Well, I think I was pretty specific about what we think is going to happen to revenue.

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**Sean O'Neill** - *Ensco International - VP of IR*

Yes, and also on the jackup side specifically in Jay's prepared remarks. We said there would be about a 12% decline in average number of days that our jackups are utilized in the third quarter.



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**Jay Swent** - *Ensco International - CFO*

I think the only thing we didn't cover there is there is probably going to be a little bit of day rate movement as well, obviously in the downward mode. I think the point Dan was talking about, we are seeing more activity, it gives us a little more confidence but really hard to tell when that turns back into the rigs being back on payroll and I think most of the discussions we are having right now probably center more around early 2010 and very late 2009. So I don't think we are going to see any real improvement in the third quarter from the discussions that we are currently having.

**Arun Jayaram** - *Credit Suisse - Analyst*

Okay. Fair enough. Last question. Dan, any sense of the timing of the tenders coming out of the Pemex?

**Dan Rabun** - *Ensco International - CEO, President*

They were rumored to be coming out end of July, first part of August. They've indicated that for a couple of months, but I think now our information is next week or first part of August, that's the last I heard. Bill, you have any update?

**Bill Chadwick** - *Ensco International - COO*

That's the most current information we have.

**Arun Jayaram** - *Credit Suisse - Analyst*

Okay. Thanks a lot guys. I really appreciate it.

**Operator**

We'll take our next question from Ian MacPherson with Simmons & Company.

**Ian Macpherson** - *Simmons & Company - Analyst*

Hey, good morning, congratulations on the quarter. I'm sorry to ask you to repeat, I just caught your AP, the jackup days utilized is expected to be down 12% sequentially. What did you say about revenues?

**Jay Swent** - *Ensco International - CFO*

Well, we said that we are going to have a movement in revenues. We are going to be up on deepwater and down on jackups.

**Sean O'Neill** - *Ensco International - VP of IR*

So it nets out to a total sequentially quarter over quarter about a 12% decline.



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**Ian Macpherson** - *Simmons & Company - Analyst*

Okay. With respect to the full year cost guidance that you provided, are there assumptions about further cold stackings embedded within that or not?

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**Jay Swent** - *Ensco International - CFO*

There are some but it's pretty limited in the number that I gave you.

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**Ian Macpherson** - *Simmons & Company - Analyst*

Okay. Lastly, it sounds like the outlook is that, I'm talking industry-wide here for jackups, activity levels may be close to bottoming and you have reason to believe that they stabilize them to move higher next year possibly. Looking at the North Sea, what do you think specifically is kind of the I don't know the six-month outlook there, you've got a couple of rigs rolling off and one or two rigs available, I believe. So how do you bridge the now and the then in that market?

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**Mark Burns** - *Ensco International - President Ensco Offshore International Company*

Ian, this is Mark Burns, in the North Sea currently we've got eight jackups. The majority of our units are located in the southern North Sea which, as you know, is more driven by gas well production. The price of natural gas in the UK, as it is here in the US Gulf of Mexico, is very depressed. We've seen independents deferr programs. We don't see a lot of activity between now, and the end of 2009. However, we do see, as Jay mentioned and Dan mentioned in their earlier remarks, we have seen the number of inquires increase. There's a lot of interest in availability starting in late fourth quarter and first and second quarter of 2010. So certainly we are expecting to see some improvement there. In the central North Sea that's more oil and condensate drilling, that's more your heavier duty jackups. Most of those units are, again, there are lots of interest in contract discussions in the future so we don't see a great impact on activity levels for those bigger rigs.

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**Dan Rabun** - *Ensco International - CEO, President*

One thing that is encouraging, what we are seeing is a noticeable uptick in activity by the majors to take advantage of low service cost or trying to lock in multi year program. So a lot of the inquires we are seeing as opposed to three and six-month programs you are seeing multi year programs out in the marketplace now that we wouldn't have seen last year?

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**Ian Macpherson** - *Simmons & Company - Analyst*

Okay. That's helpful. Thank you.

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**Dan Rabun** - *Ensco International - CEO, President*

Thanks, Ian.

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**Operator**

Moving next to Mike Urban with Deutsche Bank.

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**Mike Urban** - *Deutsche Bank - Analyst*

Thanks, good morning. Wanted to follow up on a couple of other issues on the jackup market. You guys have spent a lot of time going through this. I think I have got what you're saying, but want to be clear. It sounds like the supply side is really kind of muddling things giving the newbuild situation. If we just look at international jackup demand you said you are seeing inquiries and some interest in activity and rigs going back to work. Would you say that that just the demand side is at or close to a bottom here in the second half 2009.

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**Dan Rabun** - *Ensco International - CEO, President*

I don't think there's any question about that.

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**Mike Urban** - *Deutsche Bank - Analyst*

Okay. That's what I suspected. And then on the balance sheet, again, you've been keeping the powder dry and clearly one of the indicators you would be looking up is the jackup market bottoming for going back to the buy back. Would another factor be contracting one or more of the uncontracted 8500 series rigs?

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**Dan Rabun** - *Ensco International - CEO, President*

I mean all those would be positive indications, yes.

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**Mike Urban** - *Deutsche Bank - Analyst*

Okay. That was it. The rest of my questions were answered. Thank you.

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**Dan Rabun** - *Ensco International - CEO, President*

Thanks, Mike.

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**Operator**

Moving next to David Smith with SMH Capital.

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**David Smith** - *SMH Capital - Analyst*

Hey, good morning. I think about 60% of the international jackup demand to date, I'm sorry, the global jackup demands to date has been with the national oil companies and that's grown steadily from 25% in 2001. We know how the independent EMPs and jow the majors respond to oil and good color on the North Sea, I wonder if you can give color on how you've seen the NOCs respond to oil prices historically with jackup demand?

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**Mark Burns** - *Ensco International - President Ensco Offshore International Company*

I think, Dave, if you look at each area independently obviously you look at the Middle East you think of Saudi Aramco. They have been very vocal in their efforts to maintain activity based on the commodity price of oil and gas. They have recently announced that they would like to increase their natural gas production over the next few years so I think we will see activity from Saudi Aramco additional jackups potentially there. If you go around and look at the other -- go in to Southeast Asia and



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look at Petrobras in Malaysia and other areas. I think these companies are watching the price of oil and gas very closely and they are going to adopt and mold their programs accordingly. The same with regards to Pemex in Mexico. You will see them also adjust their drilling schedule accordingly. So, anyway, we -- the national oil company that we work for very important part of our portfolio and we watch these guys very closely and they are very adept at understanding and following the market.

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**David Smith** - *SMH Capital - Analyst*

Okay. Thank you of the real quick wonder if I could get some color on the cost savings this year versus last year by going self-insured in the US Gulf for hurricane season?

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**Jay Swent** - *Ensco International - CFO*

It isn't really so much a cost savings as a cost avoidance. Our windstorm coverage last year in the Gulf of Mexico was not that expensive. This year it was quoted at a rate it was exorbitantly high and it just made no sense at all.

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**David Smith** - *SMH Capital - Analyst*

Appreciate it. Thank you.

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**Jay Swent** - *Ensco International - CFO*

Sure.

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**Operator**

Going next to Jeff Spittel with Natixis Bleichroeder.

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**Jeff Spittel** - *Natixis Bleichroeder - Analyst*

Good morning, guys. I guess first question with regard to cost containment. Your stacking rigs. You talked a little bit about R and M expense in the shipyards coming off a little bit. To what extent at this point have you started to see some success in terms of pressuring equipment vendors on either replacement or new equipment and getting some cost relief there as well?

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**Dan Rabun** - *Ensco International - CEO, President*

As I've said, we've had a lot of interaction with vendors and service providers. We've been pushing really hard on this issue and the range is everywhere from 0% to probably 50% reductions. And you can imagine who the people are that are close to the 0% range. We've had a very disciplined approach to our cost containment efforts and every vendor down to the by we by coffee from we pressured for cost concessions but it's paid very large dividends. It's an ongoing effort and, yes, as Jay said, you can imagine there is -- haven't had a lot of movement but we've got some good concessions from others and we are going to keep pushing.

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**Jeff Spittel** - *Natixis Bleichroeder - Analyst*

Good. I guess following up on your comments to Ian about the North Sea, you talked about your starting to see a pick up in bidding inquiries for jackups I guess globally. Is the phenomenon of starting to see NOC's looking to lock up jack-ups longer term specific to the North Sea or are you starting to see that in other areas as well?

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**Dan Rabun** - *Ensco International - CEO, President*

We didn't say national oil companies, we said majors. Yes, I think you are going to see that trends quite frankly all over the place. I think with the drilling rig costs coming down you will see the majors and NOCs that had multiyear programs try to lock up jackups for longer term.

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**Jeff Spittel** - *Natixis Bleichroeder - Analyst*

Okay. That's it for me, guys.

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**Operator**

Moving next to Brian Uhlmar with Pritchard Capital.

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**Brian Uhlmar**

Good morning. I have two quick questions for you. First, I thought I heard you say that you expect all of your deepwater rigs to come out of the yard. By the time they come out of yard to have contracts. I was curious, could you give a little bit more color on that, if you are talking about some of the tenders that we already see out there if you are working on negotiated agreements with folks on those, and what regions you are looking at right now.

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**Dan Rabun** - *Ensco International - CEO, President*

Yes, we pretty consistently said the market in these rigs you need to be within two years of the delivery date to really get lively discussions with the customers. We are getting close to getting inside two years on ENSCO 8504. I would characterize the dialogue with customers as pretty substantial. So we really don't view that as a substantial risk to our business.

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**Brian Uhlmar**

Okay. Good deal. And, second, on the Gulf of Mexico jackups, as you look out, I mean would your outlook kind of make you stop you from bidding on some of the rigs that you have in the Gulf of Mexico down into Mexico or other regions? Do you want to keep some critical mass in the Gulf of Mexico and about where do you see that number?

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**Dan Rabun** - *Ensco International - CEO, President*

We don't feel any different about the market than we always had. I mean, what we said is we are going to pursue the markets that have the longest term and the highest rates and Gulf of Mexico offers term and rate, we will certainly keep them there but until that market does that we are going to look at other markets that have longer term and higher rates. But I do feel comfortable about that market rebounding, but even in a rebound situation we are still going to look for longer term.

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**Brian Uhlmar**

And not chase kind of leverage to the spot market?

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**Dan Rabun** - *Ensco International - CEO, President*

Yes, I mean you have another factor going on in the Gulf of Mexico that I don't think we've ever had before. This insurance situation is a very difficult situation for us and other drilling rig contractors. So it's an important issue for the industry that somehow is going to have to rationalize itself. Also, hurricane criteria for accepting drilling locations is substantially different than it was in the past. So there's a lot of moving parts in that market that it's not just an Ensco issue. It's a very critical issue for the entire industry.

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**Brian Uhlmar**

All right. Thank you, gentlemen.

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**Operator**

We will take our next question from Joe Hill with Tudor, Pickering Holt.

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**Joe Hill** - *Tudor, Pickering, Holt - Analyst*

Good morning. Would you all talk about what you think your ability or what you think your ability is to place an 8500 series with Petrobras given the local content requirements that seem to be strengthening and whether or not you would consider something creative or unusual like a joint venture structure to work down there?

---

**Dan Rabun** - *Ensco International - CEO, President*

Yes. We view that there's great opportunities for our rigs down there so, and the local content requirements, I assume you are referring to the new rigs they want to see built down in Brazil. There is still a lot of opportunities even with those rigs for work down there. So we view that as a very good opportunity for us.

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**Joe Hill** - *Tudor, Pickering, Holt - Analyst*

Okay. So above and beyond the 28 that they need -- that they've said are going to be owned locally.

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**Dan Rabun** - *Ensco International - CEO, President*

I mean, yes, first of all that has a lot of complexity to it to be worked out. So during the interim there's a lot of drilling opportunities down there before those rigs will ever get built and delivered.

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**Joe Hill** - *Tudor, Pickering, Holt - Analyst*

Okay. Thanks.

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**Dan Rabun** - *Ensco International - CEO, President*

And we are not looking at any joint ventures or anything like that.

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**Joe Hill** - *Tudor, Pickering, Holt - Analyst*

I appreciate it.

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**Operator**

Going next to Lucas Daul with SEB Enskilda.

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**Lucas Daul** - *SEB Enskilda - Analyst*

Thank you, good morning. I was wondering giving the latest fixtures in deepwater, the Cajun Express, where do you see the day rate level in 2010 as we approach the time where many more deepwater newbuilds in 2011 will be coming to the market?

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**Dan Rabun** - *Ensco International - CEO, President*

I'm sorry, what was your question?

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**Lucas Daul** - *SEB Enskilda - Analyst*

My question was, we saw a very good fixture recently on Cajun Express. As we approach the time, as we approach 2011 where there will be about 20 rigs becoming available in the deepwater market, what do you think, what are your thoughts on the day rate level with that kind of supply increase?

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**Dan Rabun** - *Ensco International - CEO, President*

We still see a very large number of opportunities for deepwater drilling and you have to remember all the deepwater drilling, or a vast majority of it today, is in exploration and the development work that will result from all this exploration activity there is going to be plenty of work. We view that market is going to continue to be pretty healthy, and yes that was a very good fixture with the Cajun Express.

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**Lucas Daul** - *SEB Enskilda - Analyst*

Okay. One more question on the jackup side as well. There was another transaction in which a premium jackup rig was sold at $175. Do you think that was a one-off or is that the level that we could expect going forward on similar transactions?

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**Dan Rabun** - *Ensco International - CEO, President*

I'm not that familiar. I know which rig you're referring to and I don't really don't know the background to it so I really couldn't comment on it.

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**Lucas Daul** - *SEB Enskilda - Analyst*

Okay. Fair enough. Thanks.

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**Sean O'Neill** - *Ensco International - VP of IR*

Andrea, we will take one more call.

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**Operator**

We will take out last question from Geoff Kieburtz with Weeden.

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**Geoff Kieburtz** - *Weeden - Analyst*

Thanks very much. Just one quick one. You mentioned a couple of times that you are seeing more interest in term contracts as the rates come down. I haven't heard you say what your response is going to be. Could you just kind of describe that?

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**Dan Rabun** - *Ensco International - CEO, President*

We will take term contracts.

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**Geoff Kieburtz** - *Weeden - Analyst*

I guess what I'm saying is prices have come down, are you ready to basically if you could put all of your rigs to work for term contracts would you do it at today's rates?

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**Dan Rabun** - *Ensco International - CEO, President*

Yes, yes.

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**Geoff Kieburtz** - *Weeden - Analyst*

There are no strategy to kind of building of laddered portfolio or anything like that?

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**Dan Rabun** - *Ensco International - CEO, President*

[Laughing] We are not that smart.

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**Geoff Kieburtz** - *Weeden - Analyst*

Okay. That was the last question I had.

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**Sean O'Neill** - *Ensco International - VP of IR*

In that case thanks everyone for joining us today. We greatly appreciate your questions and we very much look forward to speaking with you again on our third quarter earnings call. Thanks very much.



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**Operator**

And once again this does conclude today's call. We thank you for your participation.

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