HORNBECK OFFSHORE SERVICES INC /LA
Form 10-Q
May 10, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2010

OR

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

For the transition period from ______ to ______

Commission file number 001-32108

Hornbeck Offshore Services, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**72-1375844**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

103 NORTHPARK BOULEVARD, SUITE 300

COVINGTON, LA 70433

(Address of Principal Executive Offices) (Zip Code)

(985) 727-2000

(Registrant s Telephone Number, Including Area Code)

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.:

Large accelerated filer x	Non-accelerated filer ¨
Accelerated filer ¨	Smaller reporting company ¨

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

The total number of shares of common stock, par value $.01 per share, outstanding as of March 31, 2010 was 26,386,818.

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

FORM 10-Q FOR THE QUARTER ENDED MARCH 31, 2010

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PART I FINANCIAL INFORMATION

Item 1 Financial Statements

HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	March 31, 2010 (Unaudited)	December 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 44,386	$ 51,019
Accounts receivable, net of allowance for doubtful accounts of $642 and $860, respectively	63,629	61,724
Other current assets	18,983	13,999
Total current assets	126,998	126,742
Property, plant and equipment, net	1,616,877	1,602,663
Deferred charges, net	42,618	41,195
Other assets	15,533	15,748
Total assets	$ 1,802,026	$ 1,786,348
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 18,753	$ 16,279
Accrued interest	9,626	9,787
Accrued payroll and benefits	6,204	6,878
Deferred revenue	1,508	1,876
Current taxes payable	1,082	1,615
Other accrued liabilities	12,870	4,571
Total current liabilities	50,043	41,006
Long-term debt, net of original issue discount of $50,513 and $53,326, respectively	749,487	746,674
Deferred tax liabilities, net	201,349	198,934
Other liabilities	1,962	2,671
Total liabilities	1,002,841	989,285
Stockholders equity:		
Preferred stock: $0.01 par value; 5,000 shares authorized; no shares issued and outstanding		
Common stock: $0.01 par value; 100,000 shares authorized; 26,387 and 26,161 shares issued and outstanding, respectively	264	262
Additional paid-in-capital	406,866	407,334
Retained earnings	391,770	389,218
Accumulated other comprehensive income	285	249
Total stockholders equity	799,185	797,063

Total liabilities and stockholders equity	$ 1,802,026	$ 1,786,348

The accompanying notes are an integral part of these consolidated statements.

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Three Months Ended March 31, 2010	2009
	(Unaudited)	
Revenues	$ 86,245	$ 109,647
Costs and expenses:		
Operating expenses	44,332	40,571
Depreciation	13,532	10,145
Amortization	4,311	5,003
General and administrative expenses	8,921	8,762
	71,096	64,481
Gain on sale of assets	524	245
Operating income	15,673	45,411
Other income (expense):		
Interest income	94	139
Interest expense	(11,657)	(2,731)
Other income (expense), net	(23)	(240)
	(11,586)	(2,832)
Income before income taxes	4,087	42,579
Income tax expense	1,535	15,478
Net income	$ 2,552	$ 27,101
Basic earnings per common share	$ 0.10	$ 1.04
Diluted earnings per common share	$ 0.09	$ 1.01
Weighted average basic shares outstanding	26,259	25,942
Weighted average diluted shares outstanding	27,119	26,803

The accompanying notes are an integral part of these consolidated statements.

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HORNBECK OFFSHORE SERVICES, INC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Three Months Ended March 31, 2010	2009
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 2,552	$ 27,101
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	13,532	10,145
Amortization	4,311	5,003
Stock-based compensation expense	2,358	2,657
Provision for bad debts	(218)	(90)
Deferred tax expense	1,163	8,506
Amortization of deferred financing costs	3,718	2,989
Gain on sale of assets	(524)	(245)
Equity in (income) loss from investment	6	225
Changes in operating assets and liabilities:		
Accounts receivable	(1,709)	16,965
Other receivables and current assets	3,187	(51)
Deferred drydocking charges	(6,424)	(4,953)
Accounts payable	1,393	(8,918)
Accrued liabilities and other liabilities	(3,557)	(5,312)
Accrued interest	(160)	5,596
Net cash provided by operating activities	19,628	59,618
CASH FLOWS FROM INVESTING ACTIVITIES:		
Costs incurred for MPSV program	(7,038)	(37,674)
Costs incurred for OSV newbuild program #4	(15,085)	(42,669)
Net proceeds from sale of assets	1,334	937
Vessel capital expenditures	(5,097)	(1,784)
Non-vessel capital expenditures	(400)	(2,774)
Net cash used in investing activities	(26,286)	(83,964)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings under revolving facility		25,000
Deferred financing costs	(55)	(6)
Net cash proceeds from other shares issued	45	83
Net cash provided by (used in) financing activities	(10)	25,077
Effects of exchange rate changes on cash	35	(38)
Net increase (decrease) in cash and cash equivalents	(6,633)	693
Cash and cash equivalents at beginning of period	51,019	20,216
Cash and cash equivalents at end of period	$ 44,386	$ 20,909
SUPPLEMENTAL DISCLOSURES OF CASH FLOW ACTIVITIES:		
Cash paid for interest	$ 11,027	$ 590

Cash paid for income taxes	$ 726	$ 12,365

The accompanying notes are an integral part of these consolidated statements.

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accompanying unaudited consolidated financial statements do not include certain information and footnote disclosures required by United States generally accepted accounting principles, or GAAP. The interim financial statements and notes are presented as permitted by instructions to the Quarterly Report on Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments necessary for a fair presentation of the interim financial statements have been included and consist only of normal recurring items. The unaudited quarterly financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Annual Report on Form 10-K of Hornbeck Offshore Services, Inc. (together with its subsidiaries, the Company) for the year ended December 31, 2009. The results of operations for the three month period ended March 31, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010.

The consolidated balance sheet at December 31, 2009 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements.

2. Earnings Per Share

Basic earnings per common share was calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per common share was calculated by dividing net income by the weighted average number of common shares outstanding during the year plus the effect of dilutive stock options and restricted stock unit awards, or restricted stock. Weighted average number of common shares outstanding was calculated by using the sum of the shares determined on a daily basis divided by the number of days in the period. The table below reconciles the Company s earnings per share (in thousands, except for per share data):

	Three Months Ended March 31,	
	2010	**2009**
Net income	$ 2,552	$ 27,101
Weighted average number of shares of common stock outstanding	26,259	25,942
Add: Net effect of dilutive stock options and unvested restricted stock (1)(2)	860	861
Adjusted weighted average number of shares of common stock outstanding (3)	27,119	26,803
Earnings per common share:		
Basic	$ 0.10	$ 1.04
Diluted	$ 0.09	$ 1.01

(1) Stock options representing rights to acquire 401 and 429 shares of common stock for the three months ended March 31, 2010 and 2009, respectively, were excluded from the calculation of diluted earnings per share, because the effect was anti-dilutive after considering the exercise price of the options in comparison to the average market price, proceeds from exercise, taxes, and related unamortized compensation.

(2) As of March 31, 2010 and 2009, the 1.625% convertible senior notes were not dilutive, as the average price of the Company s stock was less than the effective conversion price of such notes. See Note 3 for further information.

(3) Dilutive restricted stock is expected to fluctuate from quarter to quarter depending the Company s performance compared to a predetermined set of performance criteria. See Note 4 for further information regarding certain of the Company s restricted stock awards.

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Long-Term Debt

As of the dates indicated, the Company had the following outstanding long-term debt (in thousands):

	March 31, 2010	December 31, 2009
6.125% senior notes due 2014, net of original issue discount of $325 and $341	$ 299,675	$ 299,659
8.000% senior notes due 2017, net of original issue discount of $6,817 and $6,980	243,183	243,020
1.625% convertible senior notes due 2026, net of original issue discount of $43,371 and $46,005 (1)	206,629	203,995
Revolving credit facility due 2013		
	749,487	746,674
Less current maturities		
	$ 749,487	$ 746,674

(1) The notes initially bear interest at a fixed rate of 1.625% per year, declining to 1.375% beginning on November 15, 2013.

The Company s 6.125% senior notes due 2014, or 2014 senior notes, have semi-annual cash interest payments of $9.2 million due and payable each June 1 and December 1. The Company s 8.000% senior notes due 2017, or 2017 senior notes, have semi-annual cash interest payments of $10.0 million due and payable each March 1 and September 1. The Company s 1.625% convertible senior notes due 2026, or convertible senior notes, have semi-annual cash interest payments of $2.0 million due May 15 and November 15, declining to 1.375%, or $1.7 million semi-annually, beginning on November 15, 2013.

Under the Company s revolving credit facility, it has the option of borrowing at a variable rate of interest equal to either (i) LIBOR, plus an applicable margin, or (ii) the greatest of the Prime Rate, the Federal Funds Effective Rate plus $^{1}/2$ of 1% and the one-month LIBOR plus 1%, plus in each case an applicable margin. The applicable margin for each base rate is determined by a pricing grid, which is based on the Company s leverage ratio, as defined in the credit agreement governing the amended revolving credit facility. Unused commitment fees are payable quarterly at the annual rate of 50.0 basis points of the unused portion of the borrowing base of the amended facility. As of March 31, 2010 there were no amounts drawn under the Company s revolving credit facility and $0.9 million posted as a letter of credit. As of March 31, 2010, the Company is in compliance with all financial covenants contained in its revolving credit facility.

The Company estimates the fair value of its 2014 senior notes, its 2017 senior notes and its convertible senior notes by using quoted market prices. The fair value of the Company s revolving credit facility, when there are outstanding balances, approximates its carrying value. The face value, carrying value and fair value of the Company s total debt was $800.0 million, $749.5 million and $746.7 million, respectively, as of March 31, 2010.

Capitalized Interest

Interest expense excludes capitalized interest related to the construction or conversion of vessels in the approximate amounts of $2.6 million and $6.4 million for the three months ended March 31, 2010 and 2009, respectively.

HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Incentive Compensation

Stock-Based Incentive Compensation Plan

The Company has a stock-based incentive compensation plan covering a maximum of 3.5 million shares of common stock that allows the Company to grant restricted stock awards, restricted stock unit awards, or collectively restricted stock, stock options and stock appreciation rights to employees and directors.

During the three months ended March 31, 2010, the Company granted time-based and performance-based restricted stock. Time-based restricted stock was granted to directors, executive officers and certain shore-side employees of the Company. Performance-based restricted stock was granted to executive officers of the Company. The shares to be received under the performance-based restricted stock are calculated based on the Company s achievement of either of two pre-determined performance criteria over a three-year period, which under certain circumstances may be extended two additional years, as defined by the restricted stock agreement governing such awards. The actual number of shares that could be received by these award recipients can range from 0% to 100% of the Company s base share awards depending on the performance goals attained by the Company.

Compensation expense related to performance-based restricted stock is recognized over the period the restrictions lapse, from one to five years. The fair value of the Company s performance-based restricted stock, which is determined using a Monte Carlo simulation, is applied to the total shares that are expected to fully vest and is amortized over the vesting period based on the Company s internal performance measured against pre-determined criteria or relative performance compared to peers, as applicable. The compensation expense related to time-based restricted stock, which is amortized over a vesting period from one to four years, is determined based on the market price of the Company s stock on the date of grant applied to the total shares that are expected to fully vest.

In addition to the restricted stock granted in 2010, the Company granted performance-based and time-based restricted stock in 2007, 2008 and 2009. The performance-based restricted stock grants issued in 2007 were eligible for vesting in February 2010. Based on the Company s performance, a portion of such restricted stock vested and the remainder was cancelled. The related stock-based compensation expense charges from previously issued equity grants and the financial impact such grants have on the Company s operating results are reflected in the table below (in thousands, except for per share data):

	Three Months Ended March 31,	
	2010	2009
Income before taxes	$ 2,358	$ 2,657
Net income	$ 1,472	$ 1,689
Earnings per common share:		
Basic	$ 0.06	$ 0.07
Diluted	$ 0.05	$ 0.06

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In addition, the Company capitalized approximately $0.2 million and $0.3 million of stock-based compensation expense as part of its ongoing newbuild construction programs and general corporate projects for the three months ended March 31, 2010 and 2009, respectively.

5. Contingencies

In the normal course of its business, the Company becomes involved in various claims and legal proceedings in which monetary damages are sought. It is management s opinion that the Company s liability, if any, under such claims or proceedings would not materially affect its financial position or results of operations.

The Company insures against losses relating to its vessels, pollution and third party liabilities, including claims by employees under Section 33 of the Merchant Marine Act of 1920, or the Jones Act. Third party liabilities and pollution claims that relate to vessel operations are covered by the Company s entry in a mutual protection and indemnity association, or P&I Club, as well as by marine liability policies in excess of the P&I Club s coverage. In February 2010, the terms of entry with the P&I Club for both of the Company s segments contained an annual aggregate deductible (AAD) for which the Company remains responsible. The P&I Club is responsible for covered amounts that exceed the AAD, after payment by the Company of an additional individual claim deductible. The Company provides reserves for those portions of the AAD and any individual claim deductibles for which the Company remains responsible by using an estimation process that considers Company-specific and industry data, as well as management s experience, assumptions and consultation with outside counsel. As additional information becomes available, the Company will assess the potential liability related to its pending litigation and revise its estimates. Although historically revisions to such estimates have not been material, changes in estimates of the potential liability could materially impact the Company s results of operations, financial position or cash flows.

6. Segment Information

The Company provides marine transportation and logistics services through two business segments. The Company primarily operates new generation OSVs and MPSVs in the U.S. Gulf of Mexico, or GoM, other U.S. coastlines, Latin America and the Middle East and operates a shore-base facility in Port Fourchon, Louisiana through its Upstream segment. The OSVs, MPSVs and the shore-base facility principally support complex exploration and production projects by transporting cargo to offshore drilling rigs and production facilities and provide support for oilfield and non-oilfield specialty services, including military applications. The Downstream segment primarily operates ocean-going tugs and tank barges in the northeastern United States, the GoM, Great Lakes and Puerto Rico. The ocean-going tugs and tank barges provide coastwise transportation of refined and bunker grade petroleum products as well as non-traditional downstream services, such as support of deepwater well testing and other specialty applications for the Company s upstream customers.

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table shows reportable segment information for the three months ended March 31, 2010 and 2009, reconciled to consolidated totals and prepared on the same basis as the Company s consolidated financial statements (in thousands).

	Three Months Ended March 31,	
	2010	**2009**
Revenues:		
Upstream		
Domestic	$ 64,225	$ 71,064
Foreign (1)	12,372	19,512
	76,597	90,576
Downstream		
Domestic	9,285	18,833
Foreign (1)(2)	363	238
	9,648	19,071
Total	$ 86,245	$ 109,647
Operating Expenses:		
Upstream	$ 36,619	$ 29,001
Downstream	7,713	11,570
Total	$ 44,332	$ 40,571
Depreciation:		
Upstream	$ 11,394	$ 7,314
Downstream	2,138	2,831
Total	$ 13,532	$ 10,145
Amortization:		
Upstream	$ 3,685	$ 3,186
Downstream	626	1,817
Total	$ 4,311	$ 5,003
General and Administrative Expenses:		
Upstream	$ 8,231	$ 6,923
Downstream	690	1,839
Total	$ 8,921	$ 8,762
Gain on sale of assets:		
Upstream	$ 520	$
Downstream	4	245

Total	$ 524	$ 245
Operating Income:		
Upstream	$ 17,188	$ 44,152
Downstream	(1,515)	1,259
Total	$ 15,673	$ 45,411
Capital Expenditures:		
Upstream	$ 26,263	$ 84,134
Downstream	957	384
Corporate	400	383
Total	$ 27,620	$ 84,901

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	As of March 31, 2010	As of December 31, 2009
Identifiable Assets:		
Upstream	$ 1,569,270	$ 1,552,974
Downstream	204,678	204,850
Corporate	28,078	28,524
Total	$ 1,802,026	$ 1,786,348
Long-Lived Assets:		
Upstream		
Domestic	$ 1,270,669	$ 1,295,100
Foreign (1)	149,120	108,335
	1,419,789	1,403,435
Downstream		
Domestic	170,624	191,627
Foreign (1)(2)	19,166	
	189,790	191,627
Corporate	7,298	7,601
Total	$ 1,616,877	$ 1,602,663

(1) The Company s vessels conduct operations in international areas. Vessels will routinely move to and from international and domestic operating areas. As these assets are highly mobile, the long-lived assets reflected above represent the assets that were present in international areas as of March 31, 2010 and December 31, 2009, respectively.

(2) Included are amounts applicable to the Puerto Rico downstream operations, even though Puerto Rico is considered a possession of the United States and the Jones Act applies to vessels operating in Puerto Rican waters.

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Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations

The following Management s Discussion and Analysis of Financial Condition and Results of Operations should be read together with our unaudited consolidated financial statements and notes to unaudited consolidated financial statements in this Quarterly Report on Form 10-Q and our audited financial statements and notes thereto included in our Annual Report on Form 10-K as of and for the year ended December 31, 2009. This discussion contains forward-looking statements that reflect our current views with respect to future events and financial performance. Our actual results may differ materially from those anticipated in these forward-looking statements. See Forward Looking Statements for additional discussion regarding risks associated with forward-looking statements. In this Quarterly Report on Form 10-Q, company, we, us, our or like terms refer to Hornbeck Offshore Services, Inc. and its subsidiaries, except as otherwise indicated.

References in this Quarterly Report on Form 10-Q to OSVs mean offshore supply vessels; to TTB mean ocean-going tugs and tank barges; to MPSVs mean multi-purpose support vessels; to AHTS mean anchor-handling towing supply; to ROVs mean remotely operated vehicles; to DP-1 , DP-2 and DP-3 mean various classifications of dynamic positioning systems on new generation vessels to automatically maintain a vessel s position and heading; to flotel mean accommodations services, such as lodging, meals and office space; to deepwater mean offshore areas, generally 1,000 to 5,000 in depth; to ultra-deepwater mean offshore areas, generally more than 5,000 in depth; to deep well mean a well drilled to a true vertical depth of 15,000 or greater; to new generation, when referring to OSVs, mean modern, deepwater-capable vessels subject to the regulations promulgated under the International Convention on Tonnage Measurement of Ships, 1969, which was adopted by the United States and made effective for all U.S.-flagged vessels in 1992 and foreign-flagged equivalent vessels; and to conventional, when referring to OSVs, mean vessels that are at least 20 years old, are generally less than 200 in length or carry less than 1,500 dead weight tons of cargo when originally built and primarily operate on the Continental Shelf.

General

Outlook

Weakness in the overall economy continues to negatively impact both of our business segments, resulting in reduced dayrates and utilization. Notwithstanding these prevailing conditions, we have seen some indications that demand for services in our Upstream Segment is stabilizing, and perhaps showing signs of improvement. We have seen no improvement of market conditions prevailing in our Downstream Segment. The duration of current conditions affecting both of our segments is not predictable. In addition, we are currently unable to determine the nature, timing and extent of any potential impact on our business segments resulting from the recent oil spill disaster in the U.S. Gulf of Mexico, or GoM.

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Upstream Segment

As of March 31, 2010, our 41 active new generation OSVs, and four MPSVs were operating in domestic and international areas as noted in the following table:

Operating Areas	
Domestic	
GoM	27
Other U.S. coastlines	4
	31
Foreign (1)	
Latin America	12
Middle East	2
	14
Total Upstream Vessels (2)	45

(1) Our Upstream foreign areas of operation generally include the following countries: Mexico, Qatar and Brazil.
(2) Excluded from this table are eight of our new generation OSVs and two conventional OSVs that were stacked as of March 31, 2010.

Our average new generation OSV dayrates for the first quarter of 2010 were approximately $20,000 and our average OSV utilization was in the low-70% range. During the first quarter of 2010, our average OSV utilization was affected by approximately 282 days of aggregate downtime related to customer-required modifications and pre-positioning of eight vessels that have mobilized or are mobilizing to Latin America during the first half of 2010 for multi-year charters. This lower utilization also resulted from the continued soft OSV market conditions in the GoM, that began in early 2009. Our 200 class vessels have experienced a quarterly effective, or utilization-adjusted, dayrate decrease of over $9,000 from the first quarter of 2009 and spot dayrate decreases of $10,000, or roughly half of the spot dayrates experienced in early 2009. Effective dayrates for our 240 class and 265 class OSVs have decreased roughly $3,300 from the first quarter of 2009. An overall re-pricing of the OSV market has occurred over the last 6-12 months for long-term contracts that were negotiated from the 2005 to 2008 timeframe to current market fundamentals. Nearly all of our OSVs that were subject to re-pricing risk have rolled onto new contracts priced in the current dayrate environment. We only have two vessels that have contracts expiring before the end of 2010 and which have not already been re-priced in this down market. In addition, we have 21 other OSVs on long-term contracts with attractive pricing that have terms extending beyond the end of 2010, including some contracts that expire in 2014.

Vessels in the spot market will continue to be priced based on prevailing terms. We believe that the OSV demand outlook in the GoM will largely depend on various market indicators such as rig counts and oil and gas industry capital spending budgets for 2010. We also expect the overall supply of new generation OSVs in the GoM to increase over the balance of 2010 with the shipyard deliveries of an estimated 11 additional newbuild OSVs by year-end. Based on these supply/demand fundamentals, we had eight new generation OSVs stacked as of March 31, 2010. However, we expect two of these eight vessels to return to active service during the second quarter of 2010. The timing of any further vessel reactivations of our new generation OSVs will largely depend on the improvement of market drivers or a decrease in the overall supply of new generation OSVs in the GoM related to international deployments.

Fleetwide MPSV effective dayrates have trended about 28% lower than what we originally projected for first quarter 2010. We expect soft market conditions to have a continuing impact on dayrates and utilization of these vessels throughout 2010. Because these vessels, when operating, have worked at dayrates that are often considerably higher than OSV dayrates, their contribution can significantly increase volatility in our results of operations. The *HOS Achiever* is currently undergoing a crane upgrade, which will adversely affect its utilization on account of it being out-of-service for approximately 120 days during the first half of 2010, including 45 days of downtime that was incurred during the first quarter of 2010.

Downstream Segment

As of March 31, 2010, our Downstream fleet was comprised of a mix of nine double-hulled tank barges, four single-hulled tank barges and 16 ocean-going tugs. We also own two additional single-hulled tank barges that were retired from service in 2009 as required under OPA 90. In recognition of the soft market conditions for our single-hulled equipment that began early in the second quarter of 2008, we stacked all of our single-hulled tank barges and six lower horsepower tugs on various dates since the first quarter of 2008. The unfavorable revenue impact of stacking barges and tugs was partially offset by the reduced operating expenses associated with the lower cost of maintaining stacked equipment. Weak demand for Downstream equipment during the first quarter of 2010 has also impacted double-hulled tank barge utilization and dayrates, particularly for our black-oil equipment. Downstream results for the first quarter were adversely impacted by the continued decline in demand for petroleum products in the U.S. and an approximate 1.1 million-barrel increase in industry-wide newbuild double-hulled tank barge capacity during 2009. In addition, the seasonal heating oil market, which has historically driven demand for our vessels higher during the first quarter, was stunted this winter by the macro-economic conditions in the U.S that have existed over the last 12 to 18 months. We anticipate these weak market conditions will continue throughout 2010, and may result in our decision to stack one or more double-hulled tank barges in 2010. We do not expect to return to active service any of the currently stacked single-hulled barges in our Downstream fleet. With the protracted weak demand for tugs and tank barges coupled with the expansion of our Upstream fleet, we expect our Downstream segment to represent a much smaller portion of our consolidated operating results compared to historical trends.

Critical Accounting Policies

This Management s Discussion and Analysis of Financial Condition and Results of Operations discusses our unaudited consolidated financial statements included in this Quarterly Report on Form 10-Q. In many cases, the accounting treatment of a particular transaction is specifically dictated by generally accepted accounting principles. In other circumstances, we are required to make estimates, judgments and assumptions that we believe are reasonable based on available information. We base our estimates and judgments on historical experience and various other factors that we believe are reasonable based upon the information available. Actual results may differ from these estimates under different assumptions and conditions. Our significant accounting policies are discussed in Note 2 to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2009.

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Results of Operations

The tables below set forth, by segment, the average dayrates, utilization rates and effective dayrates for our vessels and the average number and size of vessels owned during the periods indicated. These new generation OSVs and tank barges generate the vast majority of our revenues and operating profit. Excluded from the OSV information below is the results of operations for our MPSVs, conventional vessels, our shore-base facility, and vessel management services.

	Three Months Ended March 31,	
	2010	**2009**
Offshore Supply Vessels:		
Average number of new generation OSVs (1)	48.5	40.6
Average new generation OSV fleet capacity (deadweight)	121,280	96,869
Average new generation vessel capacity (deadweight)	2,499	2,389
Average new generation OSV utilization rate (2)	72.9%	93.0%
Effective new generation OSV utilization rate (3)	87.3%	93.0%
Average new generation OSV dayrate (4)	$ 19,986	$ 23,085
Effective new generation OSV dayrate (5)	$ 14,570	$ 21,469
Tugs and Tank Barges:		
Double-hulled tank barges:		
Average number of double-hulled tank barges (6)	9.0	9.0
Average fleet capacity (barrels)	884,621	884,621
Average barge size (barrels)	98,291	98,291
Average utilization rate (2)	75.1%	80.0%
Average dayrate (7)	$ 15,816	$ 20,406
Effective dayrate (5)	$ 11,878	$ 16,325

(1) We owned 49 new generation OSVs as of March 31, 2010. For the quarter ended March 31, 2010, our average number of new generation OSVs above includes the *HOS Arrowhead* and the *HOS Pinnacle*, which are two newly constructed OSVs that were placed in service under our fourth OSV newbuild program in January 2010, and February 2010, respectively. As of March 31, 2010, eight new generation OSVs were stacked. Excluded from this data are ten conventional OSVs that were acquired in August 2007, eight of which were sold on various dates between 2008 and 2010. We consider our two remaining conventional OSVs to be non-core assets.

(2) Utilization rates are average rates based on a 365-day year. Vessels are considered utilized when they are generating revenues.

(3) Effective utilization rate is based on a denominator comprised only of vessel-days available for service by the active fleet, which excludes the impact of stacked vessel days.

(4) Average dayrates represent average revenue per day, which includes charter hire, crewing services and net brokerage revenues, based on the number of days during the period that the OSVs generated revenue.

(5) Effective dayrate represents the average dayrate multiplied by the average utilization rate.

(6) The operating data presented above reflects only the results from our double-hulled tank barges. Our six single-hulled tank barges, all of which have been stacked, have been excluded from our Downstream dayrate and utilization rate information. Our active Downstream fleet is comprised of nine double-hulled barges and ten ocean-going tugs.

(7) Average dayrates represent average revenue per day, including time charters, brokerage revenue, revenues generated on a per-barrel-transported basis, demurrage, shipdocking and fuel surcharge revenue, based on the number of days during the period that the tank barges generated revenue. For purposes of brokerage arrangements, this calculation excludes that portion of revenue that is equal to the cost paid by customers of in-chartering third-party equipment.

Non-GAAP Financial Measures

We disclose and discuss EBITDA as a non-GAAP financial measure in our public releases, including quarterly earnings releases, investor conference calls and other filings with the Commission. We define EBITDA as earnings (net income) before interest, income taxes, depreciation and amortization. Our measure of EBITDA may not be comparable to similarly titled measures presented by other companies. Other companies may calculate EBITDA differently than we do, which may limit its usefulness as comparative measure.

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We view EBITDA primarily as a liquidity measure and, as such, we believe that the GAAP financial measure most directly comparable to this measure is cash flows provided by operating activities. Because EBITDA is not a measure of financial performance calculated in accordance with GAAP, it should not be considered in isolation or as a substitute for operating income, net income or loss, cash flows provided by operating, investing and financing activities, or other income or cash flow statement data prepared in accordance with GAAP.

EBITDA is widely used by investors and other users of our financial statements as a supplemental financial measure that, when viewed with our GAAP results and the accompanying reconciliation, we believe provides additional information that is useful to gain an understanding of the factors and trends affecting our ability to service debt, pay deferred taxes and fund drydocking charges and other maintenance capital expenditures. We also believe the disclosure of EBITDA helps investors meaningfully evaluate and compare our cash flow generating capacity from quarter to quarter and year to year.

EBITDA is also a financial metric used by management (i) as a supplemental internal measure for planning and forecasting overall expectations and for evaluating actual results against such expectations; (ii) as a significant criteria for annual incentive cash compensation paid to our executive officers and bonuses paid to other shore-based employees; (iii) to compare to the EBITDA of other companies when evaluating potential acquisitions; and (iv) to assess our ability to service existing fixed charges and incur additional indebtedness.

The following table provides the detailed components of EBITDA as we define that term for the three months ended March 31, 2010 and 2009, respectively (in thousands).

	Three Months Ended March 31,	
	2010	**2009**
Components of EBITDA:		
Net income	$ 2,552	$ 27,101
Interest, net:		
Debt obligations	11,657	2,731
Interest income	(94)	(139)
Total interest, net	11,563	2,592
Income tax expense	1,535	15,478
Depreciation	13,532	10,145
Amortization	4,311	5,003
EBITDA	$ 33,493	$ 60,319

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The following table reconciles EBITDA to cash flows provided by operating activities for the three months ended March 31, 2010 and 2009, respectively (in thousands).

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
EBITDA Reconciliation to GAAP:		
EBITDA	$ 33,493	$ 60,319
Cash paid for deferred drydocking charges	(6,424)	(4,953)
Cash paid for interest	(11,027)	(590)
Cash paid for taxes	(726)	(12,365)
Changes in working capital	2,690	14,660
Stock-based compensation expense	2,358	2,657
Changes in other, net	(736)	(110)
Cash flows provided by operating activities	$ 19,628	$ 59,618

In addition, we also make certain adjustments to EBITDA for loss on early extinguishment of debt, stock-based compensation expense and interest income to compute ratios used in certain financial covenants of our revolving credit facility with various lenders. We believe that these ratios are a material component of certain financial covenants in such credit agreements and failure to comply with the financial covenants could result in the acceleration of indebtedness or the imposition of restrictions on our financial flexibility.

The following table provides certain detailed adjustments to EBITDA, as defined in our revolving credit facility, for the three months ended March 31, 2010 and 2009, respectively (in thousands).

Adjustments to EBITDA for Computation of Financial Ratios Used in Debt Covenants

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
Stock-based compensation expense	$ 2,358	$ 2,657
Interest income	94	139

Set forth below are the material limitations associated with using EBITDA as a non-GAAP financial measure compared to cash flows provided by operating activities.

- EBITDA does not reflect the future capital expenditure requirements that may be necessary to replace our existing vessels as a result of normal wear and tear,

- EBITDA does not reflect the interest, future principal payments and other financing-related charges necessary to service the debt that we have incurred in acquiring and constructing our vessels,

- EBITDA does not reflect the deferred income taxes that we will eventually have to pay once we are no longer in an overall tax net operating loss carryforward position, as applicable, and

- EBITDA does not reflect changes in our net working capital position.

Management compensates for the above-described limitations in using EBITDA as a non-GAAP financial measure by only using EBITDA to supplement our GAAP results.

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Summarized financial information concerning our reportable segments for the three months ended March 31, 2010 and 2009, respectively, is shown below in the following table (in thousands, except percentage changes):

	Three Months Ended March 31,		Increase (Decrease)	
	2010	2009	$ Change	% Change
Revenues:				
Upstream				
Domestic	$ 64,225	$ 71,064	$ (6,839)	(9.6)%
Foreign				

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3- Effect of Business Combination - Conciliation of Assets, Liabilities and Equity

	Telecom (acquired Company) (1)	Adjustments on Income of Previous FY s (2)	NIIF 3 Merger Effect (3)	Total indentifiable net assets, inc. as of 01.01.2018
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents	2,695	-	-	2,695
Trade receivables	8,467	184	(656)	7,995
Other current assets	6,371	-	32	6,403
Total current assets	**17,533**	**184**	**-624**	**17,093**
NON CURRENT ASSETS				
Deferred income tax assets	624	-	(624)	-
Investments	4,298	(21)	1,139	5,416
Goodwill	-	-	59,653	59,653
Property, plant and equipment (PP&E)	25,917	-	33,650	59,567
Intangible assets	6,888	(68)	31,464	38,284

Other non current assets	345	125	(125)	345
Total non currents assets	**38,072**	**36**	**125,157**	**163,265**
Total assets	**55,605**	**220**	**124,533**	**180,358**
LIABILITIES CURRENT LIABILITIES	-	-	-	-
Total current liabilities	**21,120**	**-**	**7**	**21,127**
NON CURRENT LIABILITIES				
Deferred income tax liabilities	-	92	16,023	16,115
Other non current liabilities	11,399	-	18	11,417
Total non current liabilities	**11,399**	**92**	**16,041**	**27,532**
Total Liabilities	**32,519**	**92**	**16,048**	**48,659**
EQUITY	-	-	-	-
Capital Stock - Outstanding Shares	969	-	(15)	954
Inflation Adjustment - Outstanding Shares	2,646	-	-	2,646
Capital Stock - Treasury Shares	15	-	-	15
Inflation Adjustment - Treasury Shares	42	-	-	42
Treasury shares acquisition cost	(461)	-	-	(461)
Merger Premium	-	-	109,469	109,469
Legal reserve	734	-	-	734
Special reserve for IFRS implementation	351	-	-	351
Voluntary reserve for investments in capital stock	461	-	-	461
Reserve for future cash dividend payments	9,730	-	-	9,730
Other comprehensive income	972	-	(972)	-
Cost of equity interest increase in controlled companies	(3)	-	3	-
Retained earnings	7,630	128	-	7,758
TOTAL EQUITY	**23,086**	**128**	**108,485**	**131,699**
TOTAL LIABILITIES	**55,605**	**220**	**124,533**	**180,358**

AND EQUITY

(1) According to the consolidated financial statements of Telecom as of December 31, 2017, approved by the Board of Directors of the Company on March 7, 2018.

(2) Adjustment to results of previous fiscal year s corresponding to Telecom Argentina for the application of IFRS 9 and IFRS 15 as of fiscal year 2018.

(3) Adjustments to the book value of Telecom in accordance with IFRS 3.

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4- Consolidated Income Statements - as reported in FFSS

	03/31/18	03/31/17
Revenues	**30,698**	**9,433**
Consolidated Operating Costs	(23,572)	(6,585)
Operating income	**7,126**	**2,848**
Net Financial results and results of equity in earnings from associates	(2,263)	29
Net income before income tax expense	**4,863**	**2,877**
Income tax expense	(1,382)	(985)
Net income	**3,481**	**1,892**
Attributable to:		
Controlling Company	3,460	1,874
Non-controlling interest	21	18
Operating income before D&A	**11,793**	**3,789**
As % of Revenues	38.4%	40.2%

Net Financial results	03/31/18	03/31/17
Financial expenses on debt		
Interest on debt	(534)	(159)
Exchange differences on debt	(2,008)	305
Financial discounts on debt	(25)	(2)
Other financial expenses on debt	37	9
Total financial expenses on debt	**(2,530)**	**153**
Other financial results, net		
Interest and gains on investments	290	55
Taxes and bank expenses	(354)	(116)
	411	(34)

Exchanges differences on cash and cash equivalents		
Exchanges differences from other items	(203)	(12)
Financial discounts on assets, debts and diverse	(6)	(7)
Results for operations with notes and bonds	192	(24)
Results from changes on fair value of financial instruments	-	(21)
Interest on provisions	(101)	(2)
Quinquennial financial costs	(15)	-
Others	10	(3)
Total other financial results, net	**224**	**(164)**
	(2,306)	**(18)**

5- **Breakdown of the Income Statements - as reported in FFSS**

	03/31/18	03/31/17
REVENUES FROM SERVICES	**28,503**	**9,317**
Mobile Services	**10,945**	**633**
Internet Services	**7,153**	**3,450**
Cable TV Services	**6,666**	**4,962**
Fixed Telephony and Data Services	**3,625**	**-**
Other revenues from services	**114**	**272**
REVENUES FROM EQUIPMENT SALES	**2,195**	**116**
REVENUES	**30,698**	**9,433**

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6- Consolidated Income Statements - Pro Forma

	03/31/18	03/31/17	Δ $	Δ %
Revenues	**30,698**	**24,124**	**6,574**	**27.3%**
Consolidated Operating Costs	(23,572)	(19,629)	(3,943)	20.1%
Operating income	**7,126**	**4,495**	**2,631**	**58.5%**
Net Financial results and results of equity in earnings from associates	(2,263)	22	-	-
Net income before income tax expense	**4,863**	**4,517**	**346**	**7.7%**
Income tax expense	(1,382)	(1,554)	172	-11.1%
Net income	**3,481**	**2,963**	**518**	**17.5%**
Attributable to:				
Controlling Company	3,460	2,946	514	17.4%
Non-controlling interest	21	17	4	23.5%
Operating income before D&A	**11,793**	**8,481**	**3,312**	**39.1%**
As % of Revenues	38.4%	35.2%		

Net Financial results	03/31/18	03/31/17	Δ $	Δ %
Financial expenses on debt				

Interest on debt	(534)	(407)	(127)	31.2%
Exchange differences on debt	(2,008)	548	(2,556)	-
Financial debt discounts on debt	(25)	(2)	(23)	-
Other financial expenses on debt	37	9	28	-
Total financial expenses on debt	**(2,530)**	**148**	**(2,678)**	-
Other financial results, net				
Interest and gains on investments	290	224	66	29.5%
Taxes and bank expenses	(354)	(256)	(98)	38.3%
Exchanges differences on cash and cash equivalents	411	(38)	449	-
Exchanges differences from other items	(203)	45	(248)	-
Financial discounts on assets, debts and diverse	(6)	(15)	9	-60.0%
Results for operations with notes and bonds	192	3	189	-
Results from changes on fair value of financial instruments	-	(21)	21	-100.0%
Interest on provisions	(101)	(72)	(29)	40.3%
Quinquennial financial costs	(15)	(12)	(3)	25.0%
Others	10	(24)	34	-141.7%
Total other financial results, net	**224**	**(166)**	**390**	**-**
	(2,306)	**(18)**	**(2,288)**	**-**

7- Breakdown of the Income Statements - Pro Forma

	03/31/18	03/31/17	Δ $	Δ %
REVENUES FROM SERVICES	**28,503**	**22,509**	**5,994**	**26.6%**
Mobile Services	**10,945**	**9,357**	**1,588**	**17.0%**
Internet Services	**7,153**	**5,045**	**2,108**	**41.8%**
	6,666	**4,962**	**1,704**	**34.3%**

Cable TV Services				
Fixed Telephony and Data Services	3,625	2,873	752	26.2%
Other revenues from services	114	272	-158	-58.1%
REVENUES FROM EQUIPMENT SALES	2,195	1,615	580	35.9%
REVENUES	30,698	24,124	6,574	27.3%

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8- Consolidated Income Statements - as reported in FFSS

	03/31/18	03/31/17
Revenues	**30,698**	**9,433**
Employee benefit expenses and severance payments	(5,217)	(1,551)
Interconnection and transmission costs	(931)	(172)
Fees for services, maintenance, materials and supplies	(2,881)	(1,020)
Taxes and fees with the regulatory authority	(2,469)	(691)
Commissions and advertising	(1,709)	(449)
Cost of equipments and handsets	(1,525)	(56)
Programming and content costs	(2,145)	(1,207)
Bad debt expenses	(613)	(134)
Other operating income and expenses	(1,415)	(364)
Subtotal Operating costs before D&A	**(18,905)**	**(5,644)**
Operating income before D&A	**11,793**	**3,789**
Depreciation, amortization (D&A) and impairment of PP&E	(4,667)	(941)
Operating income	**7,126**	**2,848**
Equity in earnings from associates	43	40
Financial expenses on debt	(2,530)	153
Other financial results, net	224	(164)
Net income before income tax expense	**4,863**	**2,877**

Income tax expense	(1,382)	(985)
Net Income	**3,481**	**1,892**
Attributable to:		
Controlling Company	3,460	1,874
Non-controlling interest	21	18

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9- Consolidated Income Statements - Pro Forma

	03/31/18	03/31/17	Δ $	Δ%
Revenues	**30,698**	**24,124**	**6,574**	**27.3%**
Employee benefit expenses and severance payments	(5,217)	(4,290)	(927)	21.6%
Interconnection and transmission costs	(931)	(933)	2	-0.2%
Fees for services, maintenance, materials and supplies	(2,881)	(2,438)	(443)	18.2%
Taxes and fees with the regulatory authority	(2,469)	(1,942)	(527)	27.1%
Commissions and advertising	(1,709)	(1,584)	(125)	7.9%
Cost of equipments and handsets	(1,525)	(1,237)	(288)	23.3%
Programming and content costs	(2,145)	(1,490)	(655)	44.0%
Bad debt expenses	(613)	(476)	(137)	28.8%
Other operating income and expenses	(1,415)	(1,253)	(162)	12.9%
	(18,905)	**(15,643)**	**(3,262)**	**20.9%**

Subtotal Operating costs before D&A				
Operating income before D&A	**11,793**	**8,481**	**3,312**	**39.1%**
Depreciation, amortization (D&A) and impairment of PP&E	(4,667)	(3,986)	(681)	17.1%
Operating income	**7,126**	**4,495**	**2,631**	**58.5%**
Equity in earnings from associates	43	40	3	7.5%
Financial expenses on debt	(2,530)	148	(2,678)	-
Other financial results, net	224	(166)	390	-
Net income before income tax expense	**4,863**	**4,517**	**346**	**7.7%**
Income tax expense	(1,382)	(1,554)	172	-11.1%
Net Income	**3,481**	**2,963**	**518**	**17.5%**
Attributable to:				
Controlling Company	3,460	2,946	514	17.4%
Non-controlling interest	21	17	4	-

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Telecom Argentina S.A.

Date:	May 11, 2018	By:	/s/ Gabriel P. Blasi
		Name:	Gabriel P. Blasi
		Title:	Responsible for Market Relations