



# Deep Expertise in Shallow Water

## HERCULES Offshore

### World Energy interviews Randall Stilley, CEO, Hercules Offshore

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**World Energy:** What is your vision for Hercules, and how is that translated into the company's mission?

**Stilley:** Our vision has always been to become a leader in offshore services, and our mission is to provide safe, efficient and cost-effective services to the offshore E&P industry, primarily through our liftboat and contract drilling services segments.

**World Energy:** What do you see as your company's advantages?

**Stilley:** We are entrepreneurial and opportunistic, and our advantages lie in our ability to move quickly, close transactions and integrate the acquired assets into our existing businesses. Furthermore, we have the managerial talent and experience necessary to operate the assets very effectively.

**World Energy:** What is Hercules' overall strategy today? Has it changed since the inception?

**Stilley:** Our strategy is to grow the company primarily through acquisitions, diversifying our asset base and geographic footprint, while maintaining financial discipline. We continue to see opportunities for additional acquisitions in our core markets and in other markets around the world where we can utilize our shallow-water expertise. For each acquisition we deem a good strategic fit for our company, we analyze a number of financial metrics, including return on capital, internal rate of return, earnings-per-share accretion and net asset value. If a potential acquisition does not meet our internal hurdles, we will not follow through with it.

**World Energy:** What are your company's most notable accomplishments since we last talked with you?

**Stilley:** Since our initial public offering (IPO) in late 2005, we have grown revenue and profits by over 100 percent, generated industry-leading returns on capital employed and reduced debt/capital ratios.

Our international expansion is another notable highlight. While 100 percent of our revenue at the time of our IPO was generated in the Gulf of Mexico, approximately one-third of our revenue will be generated in international markets during 2007 before the TODCO acquisition.

**World Energy:** Speaking of TODCO, that acquisition gives Hercules the fourth-largest jackup rig fleet and opens up business to 10 countries on five continents. Do you see any change in your corporate culture in light of your new strength in the marketplace?

**Stilley:** We intend to continue doing the things that we have been doing, which is providing safe, efficient, reliable services to our customers, pursuing growth through acquisition and diversifying our asset and geographic base. The TODCO acquisition will allow us to pursue some new opportunities, particularly in building up our overseas locations, and it positions us for further growth.



## ***We remain focused on providing efficient services to our customers, employee development and safety, and providing good returns for our shareholders.***

Throughout all our acquisitions, our corporate culture has remained strong. We are focused on providing efficient services to our customers, employee development and safety, and good returns for our shareholders. No acquisition will change who we are.

**World Energy:** During the past 18 months, what changes have occurred in the locations you serve?

**Stilley:** While business in most international locations is robust, we have seen some volatility in the Gulf of Mexico. We followed the devastating hurricane season of 2005 with almost no storms during 2006, coupled with a mild winter and high natural gas storage leading to lower natural gas prices. This resulted in weaker Gulf of Mexico drilling business conditions in late 2006 and early 2007.

**World Energy:** How have you adjusted your strategy in view of these changes?

**Stilley:** Before the 2006 hurricane season, we had already started expanding internationally to diversify our business and we plan to continue with this strategy. We also strengthened our Gulf of Mexico-related businesses and will continue to look for opportunities to consolidate both the liftboat and drilling segments.

**World Energy:** Hercules clearly drives growth through acquisition. Why acquisition over building new assets?

**Stilley:** We believe that acquiring existing assets often offers superior returns for our shareholders in today's environment, and that such acquisitions typically provide immediate earnings and cash flow. Building new assets can be more expensive and take a long time to complete, while the markets we serve can be extremely volatile.

**World Energy:** How in particular do you deal with volatile markets or regions?

**Stilley:** Our drilling business is volatile and I don't see that changing. However, we try to spread the risk over different regions and different types of assets to reduce volatility. We now derive over a third of our

revenue outside of the U.S. Gulf of Mexico, and this percentage will likely continue to grow in the future. Our liftboat business, which is much less volatile than drilling, comprised 44 percent of our 2006 revenue. Diversification of our asset portfolio in an attempt to reduce volatility is one aspect of our acquisition strategy.

**World Energy:** What criteria do you use to determine the merits of a potential acquisition?

**Stilley:** We primarily look at strategic fit and expected financial returns when evaluating a potential acquisition. We check to see if it matches our asset and geographic profile, and we ask if the transaction will be accretive to earnings and produce an acceptable return on our investment.

**World Energy:** There seems to be a lot of money-chasing opportunity in various sectors of the energy industry today. Are you able to take advantage of this to finance further growth?

**Stilley:** One of the reasons we became a public company was to have access to capital at a lower cost. We have been very successful in financing our growth in a prudent fashion.

**World Energy:** What are your company's current growth opportunities?

**Stilley:** We continue to identify growth opportunities in three key areas: jackups and liftboats in the Gulf of Mexico, international acquisitions of jackups, and international redeployment for our domestic jackups and liftboats.

**World Energy:** How do you view the drilling environment in 2007 and into 2008?

**Stilley:** Since we are focused offshore, I'll address that environment. The global offshore drilling market is extremely robust. Most oil and gas drilling locations, with the exception of the U.S. Gulf of Mexico, are underserved at present, and it appears demand growth will be more than sufficient to absorb all the new capacity entering the market through 2007 and early 2008.



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**World Energy:** What's the impact of commodity price fluctuations on your business?

**Stilley:** In the short run, there is very little impact internationally due to long-term contracts and longer-term customer planning. In the Gulf of Mexico, it's a different story. Many of our customers are smaller independent E&P companies, and current cash flow is critical for them. Also, reservoir decline rates are high and targets are getting smaller in the Gulf of Mexico, so commodity prices ultimately drive drilling activity on the shelf.

**World Energy:** What is the size of the shallow-water drilling business in the Gulf? What's the total base of opportunity?

**Stilley:** Currently there are about 60 jackups working in the U.S. Gulf of Mexico. However, this is the lowest level of activity in a number of years, and demand should improve over the next one to two years.

**World Energy:** What share of this does Hercules capture?

**Stilley:** We currently have six rigs working the Gulf of Mexico, so our ability to capture more presence in this area will depend on acquiring existing shallow-water rigs, as with our recent acquisition of TODCO. However,

it is important to understand that the market for offshore rigs is a global one, and if one region generates excess returns, rigs are mobile by their nature and will move from weaker to stronger markets, bringing supply and demand back into balance.

**World Energy:** How do you define the shallow-water drilling business? What kinds of opportunities does Hercules particularly target?

**Stilley:** We consider shallow-water activity to be anywhere a jackup or barge drilling rig can operate – typically up to a water depth of 350-400 feet. Our target opportunities include almost any shallow-water drilling rig or liftboat that might be available for acquisition.

**World Energy:** How does the current Hercules fleet position you in the marketplace?

**Stilley:** Our fleet is a mix of mat-supported jackup rigs, independent-leg jackup rigs, and the world's largest liftboat fleet. A third of our rigs operate internationally, and we are the leaders in the Gulf of Mexico and West Africa liftboat markets (the two largest liftboat markets globally).

**World Energy:** With your fleet, are you able to undertake the very deep wells in older formations that some operators are drilling in shallow-water areas?

**Stilley:** No, we have decided to target the large majority of conventional offshore wells with the belief that while the ultra-deep continental shelf holds promise from an exploration standpoint, we can achieve better utilization of our assets working on traditional projects.

**World Energy:** Is your company investing in high-temperature/high-pressure (HTHP) wells?

**Stilley:** Again, rather than focus on niche opportunities, we believe we can provide better returns for our shareholders working on conventional drilling projects at this time. This has been our primary strategy since the company was formed.

**World Energy:** Rigs have been leaving the Gulf of Mexico for higher day rates and longer contracts in international waters. Does this affect your strategy?



## ***We built a great team of people, and I believe we are providing value for our customers in the shallow-water markets of the world.***

**Stilley:** It fits our strategy perfectly. Growing our asset base through acquisitions will expand our opportunities to mobilize rigs to international locations. These strategic mobilizations will help to balance supply and demand both domestically and internationally, and will help to diversify our business.

**World Energy:** What are the main drivers in the liftboat market? Are there differences between the Gulf of Mexico and international locations?

**Stilley:** The drivers of the liftboat business are similar whether in the Gulf or internationally. Existing production infrastructure drives this business for the most part, although storm damage can create additional short-term spikes in activity in the Gulf. Our normal business is primarily a mix of platform inspection and maintenance, construction, well intervention and platform decommissioning.

**World Energy:** What competitive factors other than price are important in the liftboat market?

**Stilley:** Availability of the appropriate class of liftboat for each project, safety, operational reliability and level of service are key factors in the liftboat market. Hercules is the leader in all of these areas.

**World Energy:** We often hear about shortages of qualified workers in the drilling and offshore businesses. Has this been an issue for Hercules?

**Stilley:** It has been a significant issue in recent years, particularly after the 2005 hurricane season. Many workers were displaced by storm damage on land, opportunities on reconstruction projects pulled many people from our industry, and the tremendous amount

of repair work offshore created a huge need for workers. The situation is better now, because overall activity offshore and along the Gulf Coast is less frantic, and with additional drilling rigs leaving the region there is less demand for skilled personnel.

**World Energy:** How do you recruit and retain the people you need?

**Stilley:** We recruit people from all over the United States and provide an attractive compensation and benefits package, coupled with training and personal growth opportunities to retain them. Our focus on providing a safe working environment is also a key factor in retaining qualified employees.

**World Energy:** Any final thoughts?

**Stilley:** There are a number of exciting opportunities on the horizon for Hercules Offshore. We built a great team of people, and I believe we are providing value for our customers in the shallow-water markets of the world. Our growth in the future will continue to build on what we've accomplished so far.

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**Hercules Offshore, Inc. ([www.herculesoffshore.com](http://www.herculesoffshore.com)) provides offshore drilling and liftboat services to help oil and gas operators search for and develop reserves in shallow-water depths in the U.S. Gulf of Mexico and international markets. Their jackup drilling fleet ranks as the fourth largest in the U.S. Gulf. Hercules also operates the Gulf's largest liftboat fleet with leg lengths greater than 100 feet. In fact, Hercules is the only company that offers both drilling and liftboat services in the Gulf of Mexico operating in water depths of 250 feet and less.**

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**NASDAQ Global Market  
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