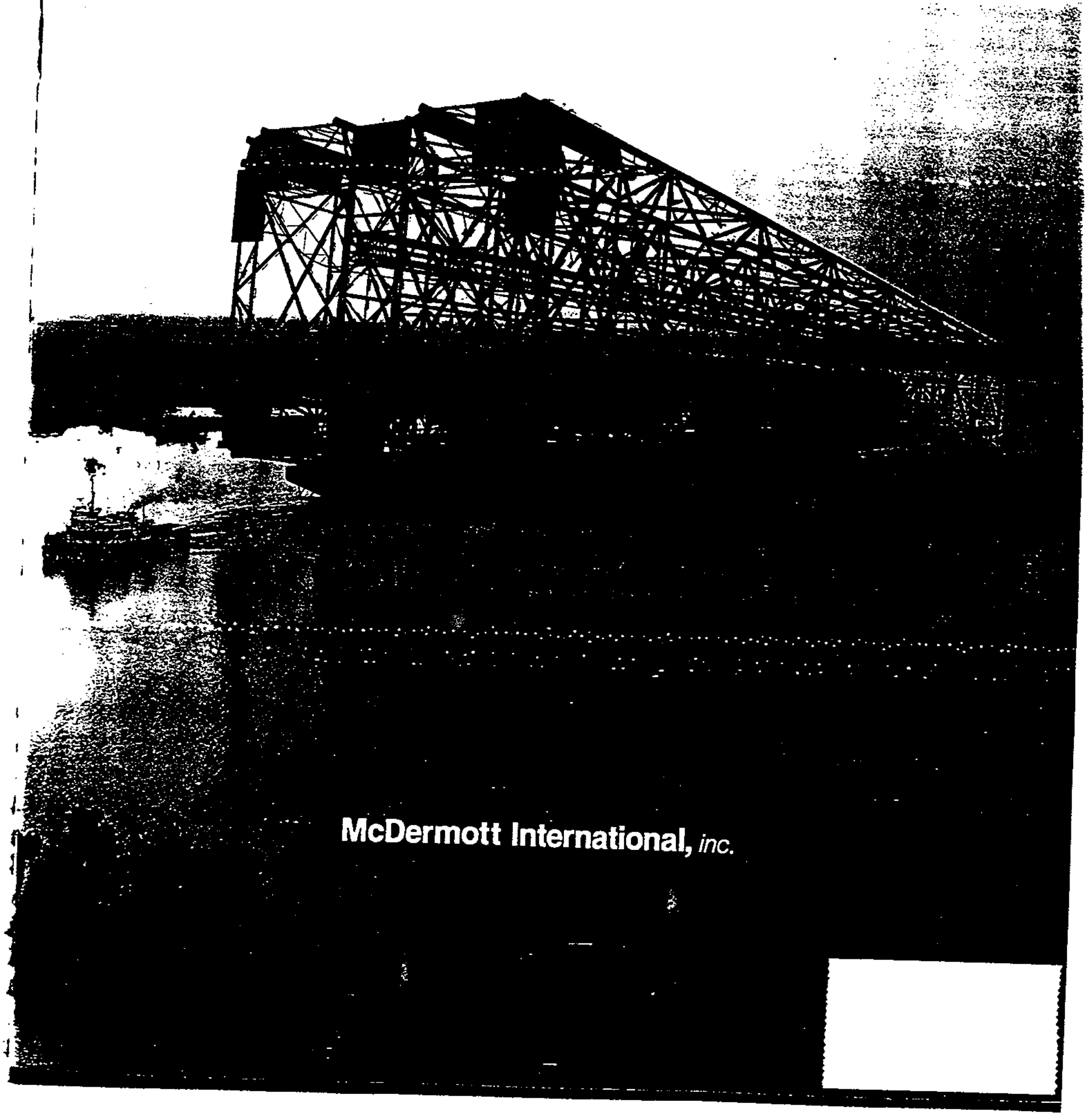
Annual Report for The Fiscal Year Ended March 31, 1987



McDermott International, *inc.*

Results at a Glance

McDermott International, Inc. for the Fiscal Years ended March 31, 1987 and 1986
In thousands of dollars except per share amounts and number of employees

	1987	1986
Revenues	**$ 3,289,322**	$ 3,109,239
Operating Loss	**(92,206)**	(46,093)
Income From Continuing Operations	**87,445**	82,693
Loss From Discontinued Operations	**(220,568)**	(26,393)
Net Income (Loss)	**(102,421)**	59,089
Earnings (Loss) Per Common and Common Equivalent Share:		
Continuing Operations	**2.36**	2.23
Discontinued Operations	**(5.96)**	(0.71)
Net Earnings (Loss)	**(2.77)**	1.60
Stockholders' Equity Per Common Share	**27.99**	32.54
Cash Dividends Per Common Share	**1.80**	1.80
Capital Expenditures	**133,315**	298,884
Backlog	**3,794,075**	4,063,460
Number Of Employees Including Subcontract Labor	**29,000**	33,000

The operations described in this publication include those of certain subsidiary and affiliated companies.

cover: *Standard Oil's 860-foot* Snapper *jacket being towed out for launch in the Gulf of Mexico. The 20,000-ton jacket was set about 100 miles south of Houston over a reservoir estimated to hold 40 million barrels of oil.*

To Our Stockholders

The conditions of our markets did not improve in fiscal 1987. Demand for our products and services was weak, and as a result, utilization of our assets remained at a low level. In addition, formidable competition confronted many of our operations as they attempted to generate new business.

The effects of this severe business climate, which has now persisted for five years, are again reflected in our financial results. Revenues for the fiscal year ended March 31, 1987 were $3.3 billion, compared with $3.1 billion a year earlier. We recorded a net loss for the year of $102.4 million, or $2.77 a share, compared with net income of $59.1 million, or $1.60 a share, in fiscal 1986.

The net loss reflects, primarily, the discontinued operations of the seamless tubular line of business of the Engineered Materials segment. In the fourth quarter of fiscal 1987, a provision of $223.7 million, net of deferred tax benefits of $121.5 million, was made for expenses related to the permanent closing of this business, and to reduce the carrying amount of associated assets to their net realizable values.

In addition, accelerated depreciation of certain assets, charges for consolidating and reorganizing certain operations, additional provisions and write-offs related to inactive and disposed plants and lines of business, and the write-down of permanently impaired goodwill contributed to this loss.

The operating loss was reduced by a pension settlement gain related to the purchase of a non-participating, single-premium annuity contract covering substantially all employees under the company's ERISA pension plans who retired before January 1, 1987. The operating loss and the net loss were further reduced by accounting changes related to depreciation and pension expense.

Other income and net income in fiscal 1987 benefited from substantially higher non-operating income, generated principally by the gain from the sale of Government Obligations.

Oil prices have stabilized over the course of the past several months, and we are beginning to see signs of improving market conditions. Nonetheless, the effects of the downturn in our business have been so severe that it will be some time before the ultimate results of a rebound are apparent. Accordingly, we will continue to reduce costs and increase productivity, and we will seize opportunities that are created as our markets slowly expand over the next few years.

James E. Cunningham
Chairman of the Board and Chief Executive Officer

Marine Construction Services

In fiscal 1987, Marine Construction Services revenues declined to $862.8 million from $908.2 million in fiscal 1986. While this decline reflects decreased utilization of our marine construction equipment, worldwide, and of our fabrication facilities in the United States, it was partially offset by revenues from our new heavy-lift vessels. Revenues also reflect the recognition in fiscal 1986 of the favorable settlement of marine claims in this segment's foreign marine operations.

The operating loss increased in fiscal 1987 to $81.5 million from $30.2 million last year as a result of the fiscal 1986 settlement, higher workers compensation insurance costs, reduced margins in our foreign operations, and the accelerated depreciation of facilities and equipment as they became less cost-effective and obsolete. Improved margins for U.S. operations, an accounting change for the depreciation of major marine vessels, reduced drydocking costs, and continued cost cutting benefited the operating results, as did the annuity contract.

The year was dedicated to increasing productivity and efficiency through automation, cutting costs through consolidation, and seeking and receiving new kinds of business.

At our Morgan City, Louisiana facilities, we began using a new automated panel line in our shipyard and initiated the automation of the girder, beam, and brace lines in our fabrication yard. At our Ardersier, Scotland facility, we completed the first phase of an integrated program which has already made the yard one of the most automated in the world. Computerized cranes move steel in the stockyards, while guided vehicles move plate and pipe inside the shops. Ultimately, complex process piping will also move automatically from station to station. The modernization of our pile handling facility allows us to move larger pieces than ever before without the use of cranes.

Automation in our fabrication yards has reduced manhours up to 25 percent for some tasks, and has improved our overall competitiveness.

To reduce costs elsewhere, Marine Construction consolidated administration and facilities. We moved our North Sea headquarters to London from Brussels, combining them with our London Engineering office. We also combined the administration of our Middle East, Southeast Asia and European operations into one office under the same executive, located in London.

In the Middle East, we completed the relocation of our Dubai facility to Dubai's new Industrial Zone at Jebel Ali, and in response to a weak market, we closed our Egypt yard. Major work for that area will now be bid from Dubai.

With the decline of many traditional markets, our strategy has been to develop new business by applying expertise developed for traditional work to non-traditional jobs, both in marine construction and other markets. Our fabrication yard in Morgan City, for instance, recently won an order for 9,000 tons of bridge girders to be built for the interstate highway system in Texas.

Our Morgan City shipyard signed a U.S. Navy contract, its first, to build the prototype SWATH (small waterplane-area, twin hull) ship. The contract for the prototype, which will tow sophisticated sonar equipment for subsea surveillance and submarine detection, is worth $25 million, and the Navy has options for three more SWATH ships.

Additionally, the shipyard completed work on a 4,000-ton dredge and six gantries for shipyard cranes. A 1,300-passenger ferry, which will operate from Woods Hole, Massachusetts, is now under construction.

In engineering and design, we began the first non-marine application of CADAD™, our Computer-Aided Design, Analysis and Drafting system. In conjunction with an architectural-engineering firm, we are using the system to analyze supports for the heating, ventilation, and air conditioning system at a nuclear power plant. The strict rules of the Nuclear Regulatory Commission, which oversees this project, will provide a major test for the CADAD system.

We also are actively marketing CADAD and some associated services, such as software we developed for our purchasing departments, to industries outside marine construction.

We have positioned ourselves in such non-traditional marine construction markets as subsea completions, tension-leg and floating production systems, extended reservoir test systems, and other concepts for incremental and marginal reservoir development.

An agreement between McDermott and Kvaerner Subsea Contracting of Norway has enhanced our subsea capabilities. Under the agreement, we will work together exclusively on projects on the Norwegian Continental Shelf and will pursue projects elsewhere on a case-by-case basis. An agency agreement with MCS International, an Irish company, gives us state-of-the-art capability for design and analysis of marine risers, mooring and offloading towers, and TLP tendons. The agreement makes MCS software, which is specialized for the offshore industry, available at all our engineering offices, and it allows sublicensing and time-sharing for the software through Power Computing Company, a Babcock & Wilcox division.

We believe this is only one of many ways to combine Marine Construction expertise with B&W capabilities. Several immediate prospects for the construction of floating production systems could offer B&W's Bailey Controls Company a market for integrated systems which will both control and monitor a floating platform, production equipment, and subsea wells. Similar opportunities exist for Marine Construction to work with B&W's Alliance Research Center and Nuclear Equipment Division.

In our traditional oil-related markets in fiscal 1987, we completed the fabrication and installation of Shell's 750-foot *Boxer* platform and Standard Oil's 860-foot *Snapper* platform, both for the Gulf of Mexico. We fabricated and installed Mobil Oil's Mary Ann facilities in Mobile Bay, Alabama, a project that reaffirms our commitment to total service. Our new 5,000-ton shear-leg crane lifted and set three decks in the the shallow waters of the environmentally sensitive bay after all equipment and facilities had been installed at our fabrication yard in Morgan City. Because the crane is mounted on a shallow draft barge, it was the only piece of equipment in the marine construction industry which could operate in the 15-foot depths of the bay and still set the large, integrated decks, weighing from 700 to 2,700 tons, in single lifts.

With the development of compliant tower technology, we extended our traditional engineering, installation, and fabrication markets to water depths over 2,500 feet. We are creating engineering systems and technical expertise, including random/compliant design procedures, to analyze and design this new class of deepwater structure. This technology not only will benefit compliant tower design, but also will make the design of traditional fixed platforms in deep waters more reliable and cost effective.

Power Generation Systems and Equipment

Revenues from this segment rose to $1.5 billion from $1.4 billion a year ago, primarily because of higher revenues from fossil steam system exports, nuclear services, Bailey Controls' micro-processor control systems, general construction, and Hudson Products' heat exchangers.

This segment's fiscal 1987 operating income was $72.3 million, compared with $36.8 million a year ago. Contributing to the increase were the higher revenues and better results from industrial boilers, increased nuclear services, better margins on fossil steam system repairs and alterations, and lower workers compensation costs. This segment also realized a gain from the annuity contract.

Costs for consolidating and restructuring operations, write-offs and provisions for plant closings, and higher sales and marketing costs reduced operating income.

The market for small boilers for industry and municipalities is stronger than our traditional market for large utility power generating boilers. Consequently, these small boilers have provided much of the activity in this segment.

Last year for the industrial and municipal market, we completed three power plants, two in Maine and one in California for Energy Factors. We also reached an agreement with Lauhoff Grain Company to design, build, operate, and maintain a $33-million coal-fired cogeneration facility at a Danville, Illinois, grain processing plant. The operating and maintenance contract is for more than 20 years and is valued at $78 million.

We continued to lead the market for refuse-burning boilers. We signed two major contracts with the Solid Waste Authority of Palm Beach County, Florida. The first, which was awarded to our joint venture with Bechtel Civil, Inc., is worth $174 million and covers building the plant, which will burn 2,000 tons of garbage a day. Under the second, B&W could receive up to $488 million over 21 years to operate the plant.

Rust International Corporation, as agent for Signal Environmental Systems, awarded B&W a contract valued at over $35 million for five refuse-burning Stirling Power boilers. These boilers will be installed for mass-burning refuse-to-energy facilities in Bridgeport, Connecticut, and Millbury, Massachusetts. In Texas, we signed a $20-million contract to supply a system, including two mass-burning refuse boilers, for the Waste-to-Energy Project of Austin.

We own 50 percent of the two Maine plants, which burn wood chips to produce electrical energy sold to Bangor Hydro-Electric, and we are developing several other projects which could give us equity in plants costing from $40 million to over $500 million. We believe the demand for small power plants will continue to grow as plants that burn non-traditional fuels, such as wood chips and refuse, and those that produce heat for manufacturing and electricity become an integral and widely accepted part of the U.S. utility system. As a result, we will continue to explore equity agreements such as we have in Maine.

While most of our new boiler business has been for small units, we are also working on large boiler projects. As part of our $187-million contract for work on the conversion of the William H. Zimmer generating station in Ohio from nuclear fuel to coal, we are building a 1,300-megawatt boiler. The plant is owned by American Electric Power, Cincinnati Gas & Electric, and Dayton Power and Light. On another large project, we have a $57-million contract to erect a 1,300-megawatt boiler, which we previously fabricated, at American Electric Power's plant in Rockport, Indiana.

The major market for large, new utility boilers is international, and our B&W Canada subsidiary has operated very successfully in that venue. The subsidiary is at work on several projects, including the $186-million second phase of the Suralaya plant in Indonesia and a $140 million, four-boiler contract with the People's Republic of China. In conjunction with these projects, the first B&W boiler manufacturing plants outside of North America went into production in Beijing, China, and Batam Island, Indonesia. The Beijing plant is a joint venture with Beijing Boiler Works, and the Batam plant is a joint venture with P.T. Santi Bakti. We expect further growth in the international market, and B&W Canada is poised to be an important element in that growth.

As utilities in the United States have turned away from investments in major new plants, they have begun aggressive life extension and maintenance programs for existing plants. Currently, service and maintenance account for approximately 30 percent of Power Generation Systems and Equipment revenues, and the percentage continues to grow. Healthy revenues from nuclear steam generator maintenance are the result of our robotic systems, which we use to inspect reactors and examine and repair steam generators, and our nuclear fuel sales to utilities such as Duke Power, which gave us a contract to refuel its Westinghouse-designed reactors.

Our TLT-Babcock joint venture assumed the Power Generation Group's ash handling business in fiscal 1987. About 50 percent of this business is generated by refuse burning facilities, and refuse projects account for about 25 percent of TLT's industrial fan revenues. TLT continued its success in the market for tunnel ventilation with the completion of the installation of fans in the Fort McHenry Tunnel near Baltimore, Maryland, and the award of a large contract for fans in the Mt. Baker Ridge and Mercer Island tunnels in Washington.

Another B&W joint venture was awarded a $48-million contract for work on the first pressurized fluid-bed combustion demonstration facility in the United States at the Ohio Power Company's Tidd Power Plant in Brilliant, Ohio.

The divisions within the Babcock & Wilcox Defense and Nuclear Power Group remain among the most stable in the company. The group contributes substantially to B&W's position as a leading supplier to the U.S. Navy's nuclear program and the rest of the nation's defense markets. In 1986, the group contributed to B&W's $250 million in Department of Energy contracts and its position as the DOE's number one contractor, a distinction B&W gained for the second consecutive year.

Near the end of the fiscal year, the group acquired the assets of a producer of high-precision mechanical components for the ordnance and missile industries. This acquisition gives us an entry into a new military market and strengthens our position as a defense contractor.

A new division, Electronic Information Systems, was formed in B&W to manage electronic information services, telecommunications, and data processing, corporation-wide. By the end of fiscal 1988, eight mainframe computers in McDermott International's North American operations will be consolidated under EIS at B&W's Power Computing Company.

Also included in Electronic Information Systems is Wisdom Systems, a developer and marketer of artificial intelligence and expert system services and software for engineering, design, and control.

B&W's Bailey Controls Company is the leading supplier of distributed digital control systems. Over 7,000 of Bailey's Network 90® microprocessor-based control systems have been installed—more than twice the number installed by Bailey's nearest competitors. Recently, systems have been installed in both onshore and offshore oil and gas production facilities, in refineries, and in pulp and paper mills, where Network 90® systems control processes millwide. There have been many shipboard applications, as well, including an installation on McDermott Marine Construction's *DB102*. Bailey has significantly increased its market share around the world and in the past year entered key process and utility markets in Europe and China.

Engineered Materials

The Engineered Materials segment's seamless tubing business was faced with continued worldwide overcapacity and a depressed market for its products in fiscal 1987. In light of these conditions, we decided prospects for this business were limited, and in June 1987, announced our intention to discontinue seamless tubing operations at our facilities in Beaver Falls, Ambridge, and Koppel, Pennsylvania, and in Bryan, Texas.

Revenues from continuing operations in the Engineered Materials segment were $130.4 million in fiscal 1987, a decline from the $148.1 million in the previous fiscal year. Operating income from continuing operations dropped to $11.3 million from $11.9 million.

The lower revenues were attributed to smaller shipments of and lower prices for welded tubing, a decline in volume from tubing used in nuclear propulsion plants for the U.S. Navy, and smaller shipments of insulating products. Lower volume in all product lines caused the decline in operating income.

At our welded tubular facility in Alliance, Ohio, major segments of a $28-million modernization program became operational during fiscal 1987, giving us a much stronger position in the welded tubing industry. New computer controlled components, which promise to revolutionize welded-tube making, include a large-diameter, heavy-wall electric-resistance welding mill; a 26-stand hot stretch reducing mill; a 500,000-pound drawbench; and a full periphery, high-speed ultrasonic testing unit, which is the first of its kind in North America. The stretch reducing mill will significantly lower the cost to manufacture welded mechanical and pressure tubing; it will also enable us to become more competitive in the market for automotive tubing and to offer an expanded line of boiler tube products.

The Insulating Products Division continued to perform well in fiscal 1987 under difficult market conditions, and it furthered its worldwide leadership in high temperature insulation. An aggressive program of new product and market development has resulted in joint ventures and licensee operations in Mexico, Taiwan, and Venezuela, the start-up of a state-of-the-art product facility at IPD's United Kingdom joint venture, and expanded capacity at Insulating Products' Brazilian subsidiary.

Trading

Revenues from MIT Trading and Coutinho, Caro & Co., the two groups that make up Trading, increased to $849.5 million in fiscal 1987, up from $655.1 million the year before. The operating loss, however, increased to $29.3 million from $536,000, primarily because of a $26 million write-down of goodwill.

The higher revenues came from MIT Trading's petrochemical and plastics unit, which completed its first full year of operation, and increased steel trading. Operating results benefited from higher margins in steel trading and a profit in the MIT Trading Group's petrochemical and plastics unit, which attained a substantial share of the worldwide market for its products in fiscal 1987.

In other MIT Trading activity, the countertrade unit completed a contract for Marine Construction in Brazil, is working towards the conclusion of an obligation for B&W's contract in China, and expanded its services to third party countertrade. The group also acquired Draco International, a Hong Kong-based general trading company which will help us as we enter the diverse markets of the Far East and especially the People's Republic of China.

While Coutinho, Caro & Co.'s international unit increased its trading volume of steel and steel related products in fiscal 1987, worldwide overcapacity and reduced margins lowered gross profits. Quota systems and geographical market restrictions further depressed CCC's steel trading, as did disappointing exports from the United States. In the coming year the international trading unit should benefit from its diversification into trading coal, paper, and paper related commodities.

CCC's international shipping company operated over 100 time-charters and opened a new office in Hong Kong in fiscal 1987. Half of the shipping volume was in-house and half was for third parties.

CCC's Construction and Engineering's Turnkey Projects Group completed jobs in Abu Dhabi, Kenya, and Nigeria, and concluded contracts for new projects in Abu Dhabi, Cameroon, West Africa, and Egypt. South and Central America, and Africa, the traditional markets for turnkey projects, were depressed, and as a result, we explored opportunities in other regions, including the People's Republic of China, where we signed a new brewery contract, the USSR, and certain Middle Eastern areas. We believe these are good markets for glass and food engineering projects, as well as environmentally related projects.

For the next several years, the Trading segment will concentrate on developing additional markets in China as well as new markets in the USSR, where we have commitments for the purchase of petrochemicals and plastics and are negotiating several turnkey projects and joint ventures.

Outlook

Fiscal 1988 will be another difficult year for McDermott International. Nonetheless, we believe that the next twelve months should be viewed as a transition that ultimately leads to a recovery from the very depressed market conditions we have experienced during the past few years.

Although our confidence in the future is strengthened by our ongoing efforts to reduce costs and increase productivity, we are further encouraged by two developments in the international marketplace. The value of the U.S. dollar continues to decline in the currency markets, and the price of oil has been stable at slightly less than $20 a barrel during the past several months.

We are all familiar with the declining value of the dollar. It has constantly been in the news for over two years. Although it has already fallen 45 percent against both the Japanese yen and German mark, further declines will more than likely occur during the next several months. Due to the inexpensive dollar, the prices of U.S. produced goods and services have decreased in the global marketplace, while the prices of the goods and services from other producers have increased. Accordingly, our competitive position in U.S. markets has strengthened, particularly against the Japanese and Europeans.

This exchange rate development in no way suggests that we can now relax our vigilance nor that we will soon return to the market conditions of the late 1970s. On the contrary, the Japanese and Europeans have ongoing programs to remain competitive, and they will both continue to battle us for market share. In addition, the exchange rate development has not affected Korea, Taiwan, or other newly industrializing nations. These third world economies continue to have significant labor cost advantages, and they will all strive to increase their market share in the manufacturing industries of the world economy.

The declining dollar has helped stabilize the international oil markets. These markets use the dollar as their pricing mechanism. As it has continued to fall in value over the past two and a half years, the price of oil in terms of the European and Japanese currencies has declined dramatically. As classical economics would predict, this reduction in price is beginning to lead to higher levels of oil consumption in many of the world's industrialized countries.

In addition to an increasing level of demand, international oil markets have experienced a supply-side response to the declining dollar. Revenues received by oil producers are purchasing fewer and fewer goods and services in the global marketplace. The $18 to $20 received for a barrel of oil today is equivalent in international purchasing power to less than $15 received in early 1985. In our opinion, this decline in the value of oil revenues has given OPEC a greater incentive to control its output and maintain prices at approximately $20 a barrel. Therefore, we believe that an increase in world oil consumption, accompanied by continued OPEC moderation, will stabilize oil prices at current or higher levels. As a consequence, our marine construction operations should benefit as offshore activity ultimately increases.

Let me again emphasize that neither of these developments—an inexpensive dollar nor stable oil prices—is going to generate any dramatic overnight changes. Rather, they will provide us with emerging opportunities in the global market, which will become apparent with the passage of time. We have every intention of responding to and benefiting from these opportunities.

J.E. Cunningham
Chairman of the Board and Chief Executive Officer

June, 1987

Marine Construction Services

For The Fiscal Year Ended March 31,	1987	1986
	In thousands	
Revenues	$ **862,785**	$ 908,186
Operating Loss	**(81,497)**	(30,196)
Backlog	**470,514**	735,765

Marine Construction Services is a diversified group, traditionally serving the oil and gas industry, but whose markets now extend to defense and non-marine engineering and fabrication. For our traditional markets, we specialize in designing and installing offshore drilling, production and processing platforms, underwater pipelines, and onshore processing plants. Our expertise extends from shallow marsh and shoreline areas to remote, deepwater locations, far offshore. In other markets, we provide engineering and analysis, fabrication for general construction, and shipbuilding.

We have three engineering offices and five active fabrication yards, worldwide. The activities of these locations, both engineering and fabrication, are complemented by highly automated systems. We use our Computer Aided Design, Analysis and Drafting system not only for the design and development of offshore structures, but also for the analysis of complex onshore facilites, unrelated to oil and gas production. At our fabrication yards, we use automated systems to assist in the fabrication of jackets, decks, and modules for installation offshore. These same systems, used in other applications, contribute to our diversification into new markets.

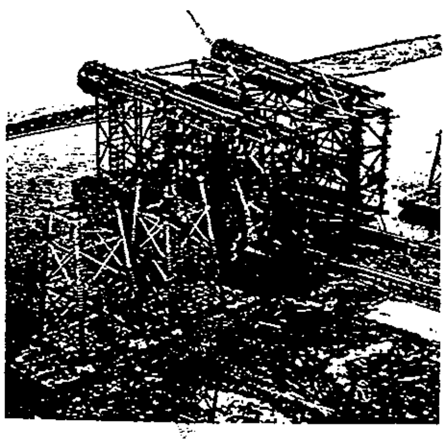
Our offshore operations are supported by the industry's largest and most modern fleet of marine construction vessels, which we use for the transportation, installation, hookup, commissioning and maintenance of offshore structures and pipelines. Included in our fleet are two of the world's largest heavy-lift vessels, the semi-submersible *Derrick Barge 102*, with a total lift capacity of 13,000 tons, and our barge mounted shear-leg crane, with a capacity of 5,000 tons.

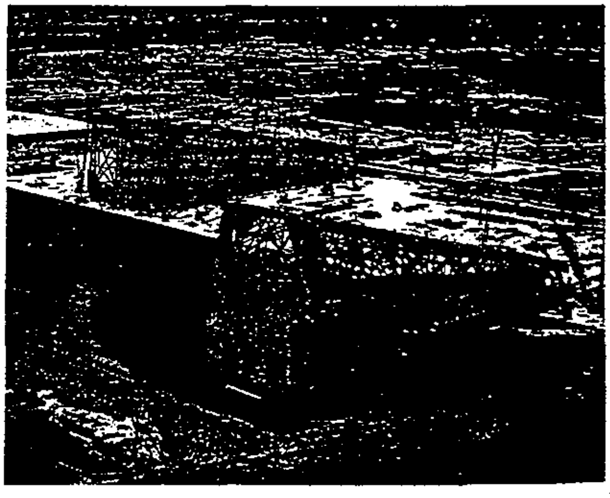
Our semi-submersible *Lay Barge 200* is one of several barges which support our offshore pipelaying operations. These operations have installed the world's deepest marine pipelines, including one in the Gulf of Mexico in water over 1,000 feet deep and two in the North Sea in water nearing 1,000 feet. We can install pipelines up to 72 inches in diameter and have simultaneously installed as many as five pipelines in various dimensions from a single barge.

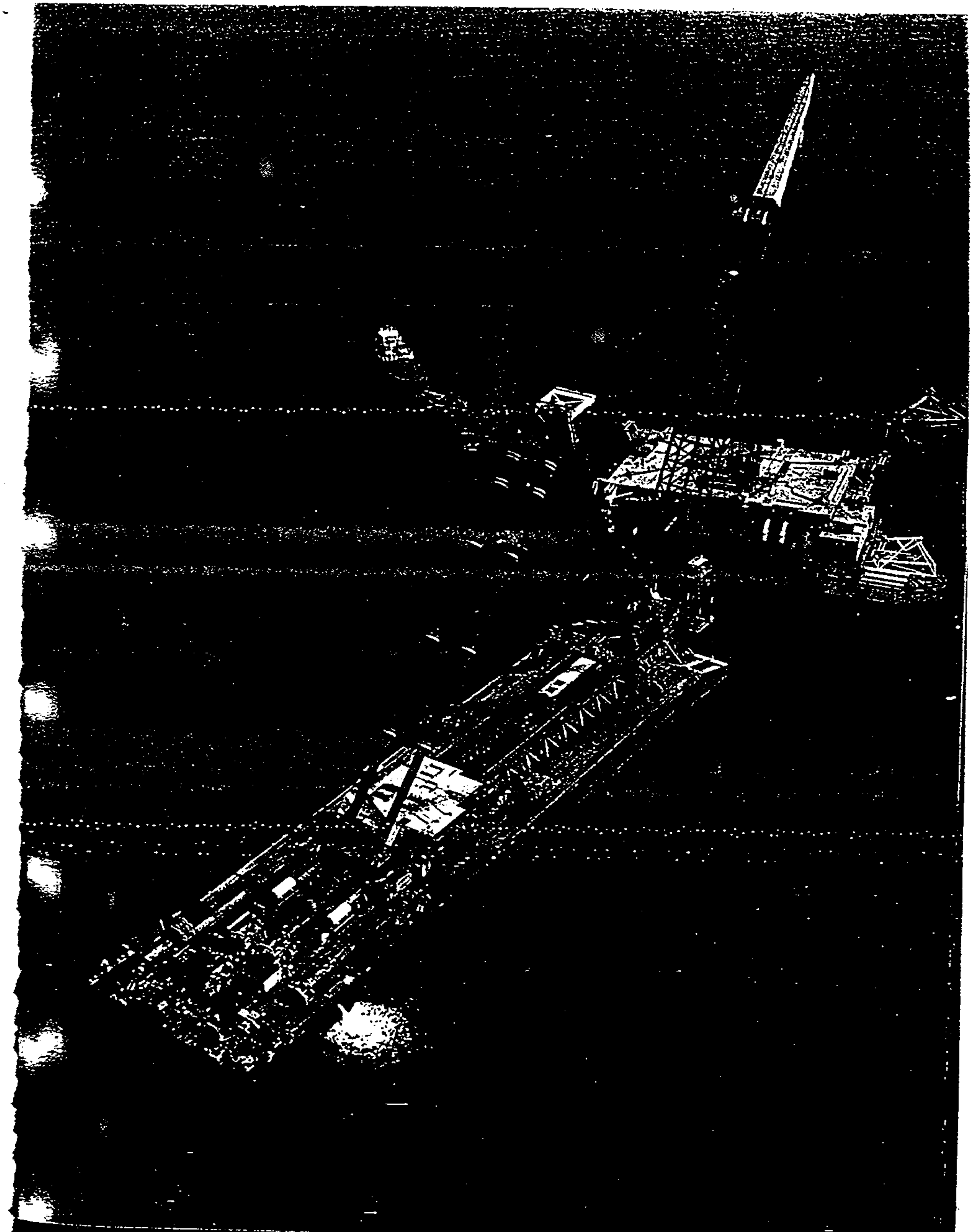
At our shipyard in Morgan City, Louisiana, we build and repair tugboats, supply boats, dredges, barges, ferries and other small vessels. In 1987, the yard began work on its first Navy vessel, the sophisticated SWATH (small water-plane, twin hull) ship.

Marine Construction Services' combination of skills in engineering, design, and fabrication, and its highly automated systems have given it an international reputation for quality and expertise, and for solving problems with efficiency and imagination.

below left: *Marathon's Brae B jacket being loaded out at McDermott Scotland. McDermott International's fabrication yard at Ardersier, Scotland has been building offshore structures for the North Sea since 1971. It is one of the most modern and efficient fabrication yards in the world.* **below right:** *In Morgan City, Louisiana, we build huge jackets to support oil and natural gas production in the Gulf of Mexico. Here, Shell's 750-foot* Boxer *platform (front) is being loaded-out for launch, and Standard Oil's 860-foot* Snapper *platform is in the last stages of construction.* **right:** *McDermott's newest piece of marine construction equipment is our shear-leg crane. The crane, which can lift 5,000 tons, is mounted on a shallow-draft barge allowing it to operate inland as well as offshore. The crane reclines to pass under overhead obstructions such as bridges.*







Power Generation Systems and Equipment

For The Fiscal Year Ended March 31,	1987	1986
	In thousands	
Revenues	**$ 1,525,952**	$ 1,447,394
Operating Income	**72,258**	36,771
Backlog	**2,998,268**	3,035,061

Our Power Generation Systems and Equipment segment provides innovative, high quality products and a full range of services to a variety of customers. Our operations serve utility, industrial, and municipal power generation industries, the defense industry, and a number of associated industries.

Our focus has been on engineering, manufacturing, and erecting fossil-fueled and nuclear steam systems. But our innovative, high quality products are complemented by a full range of services to the power generation market. In addition, we are actively involved in the new and growing market for systems that produce power through cogeneration and the burning of refuse and other non-traditional fuels. We have entered this market both as builders and suppliers of equipment, as operations and maintenance contractors, and as equity participants in build-own-operate projects.

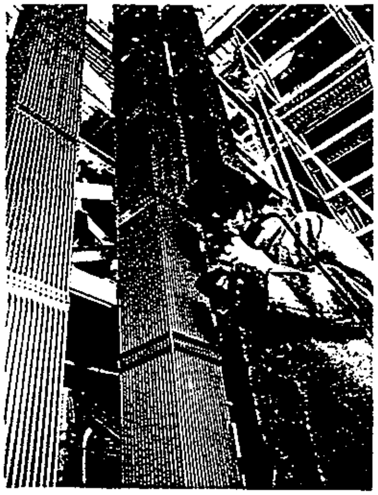
We have also been successful in the international market for power generation. Our operations include supplying equipment and systems to countries around the world, as well as establishing joint-ventures to help other nations build and supply their own equipment and systems.

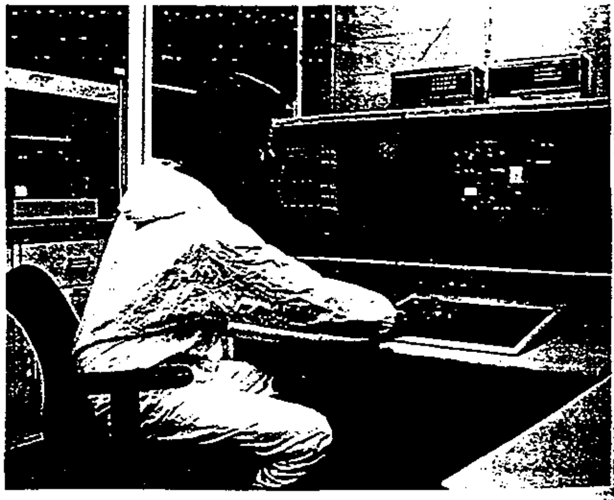
To support the power generation industry's needs, we provide such products and services as replacement parts, task and project management, testing and inspection, maintenance, computing systems, operator training, and engineered modifications to steam systems for electric utilities and industries. Our construction unit provides further service through its erection, repair, and alteration of power generation systems and equipment. This full range of services, from engineering to construction to operation, helps us improve our customers' equipment and facilities, and enhances their ability to operate at peak efficiency.

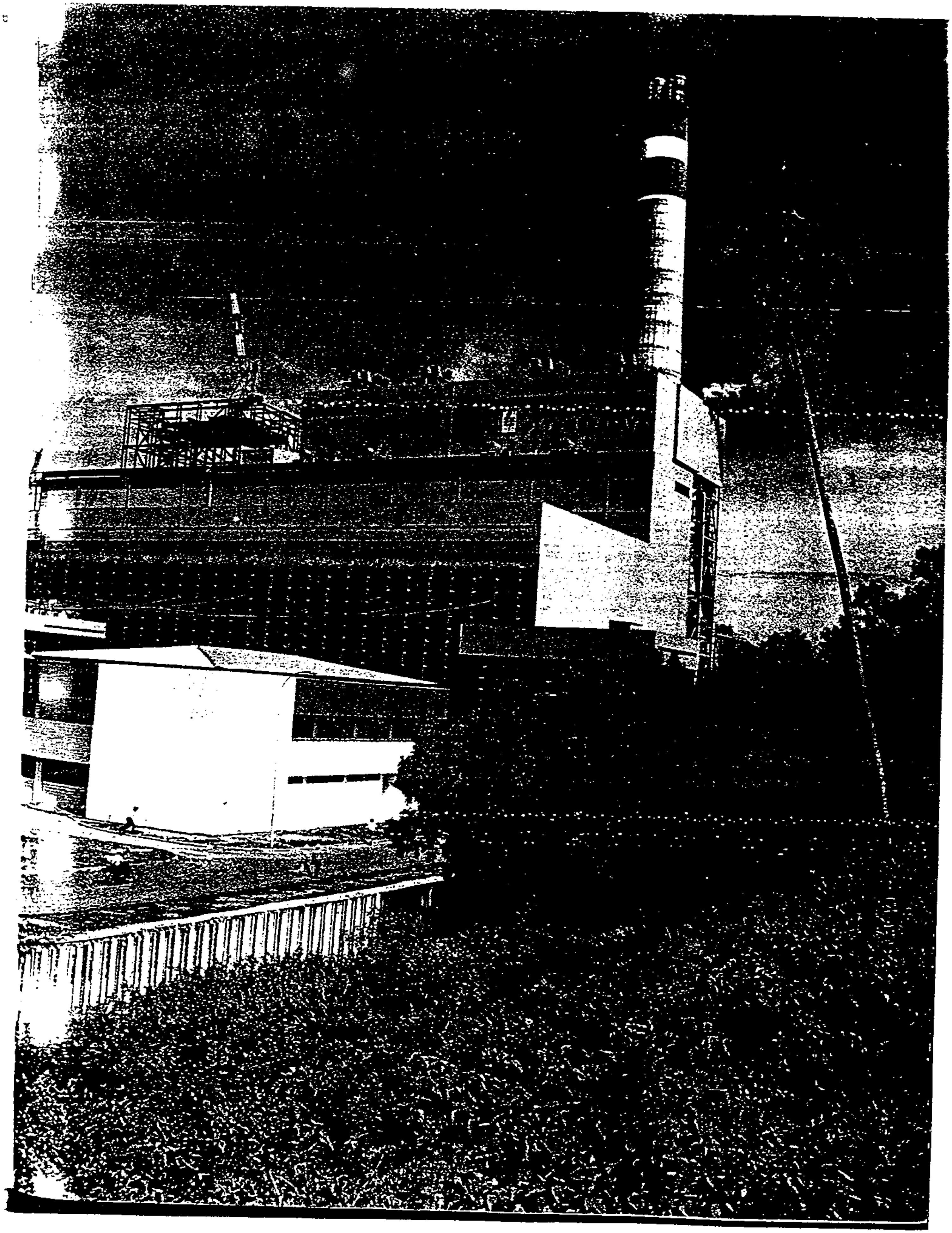
Power Generation Systems and Equipment also manufactures air heaters, fans, precipitators, heat transfer surface cleaning equipment, micro-processor based control systems, and air-cooled heat exchangers.

For defense markets, we produce precision components for a variety of applications. We are a leading producer of components for nuclear propulsion systems, and we are using our specialized manufacturing and welding capabilities to enter new defense markets. We have acquired a manufacturer of metallic components for ordnance and are developing an integrated ordnance business.

below left: *At our Lynchburg, Virginia, facility, we use precision equipment to build components such as nuclear fuel rods. Our Defense and Nuclear Power Group manufactures components for the U.S. Navy's nuclear program and for the nuclear power industry.* **below right:** *Network 90®, Bailey Controls' state-of-the-art microprocessor based controller, leads its field. Over 7,000 of the controllers—more than twice the number installed by our nearest competitors—are at work in a wide variety of industries.* **right:** *Babcock & Wilcox International builds power plants, like this one at Suralaya, Indonesia, around the world. BWI is completing work on the second phase of the Suralaya development and is working on projects in the People's Republic of China and Egypt.*







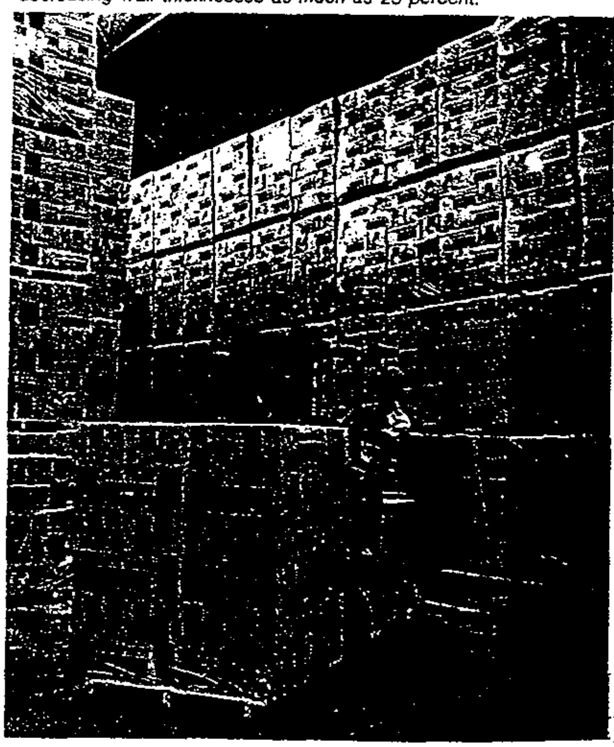
Engineered Materials

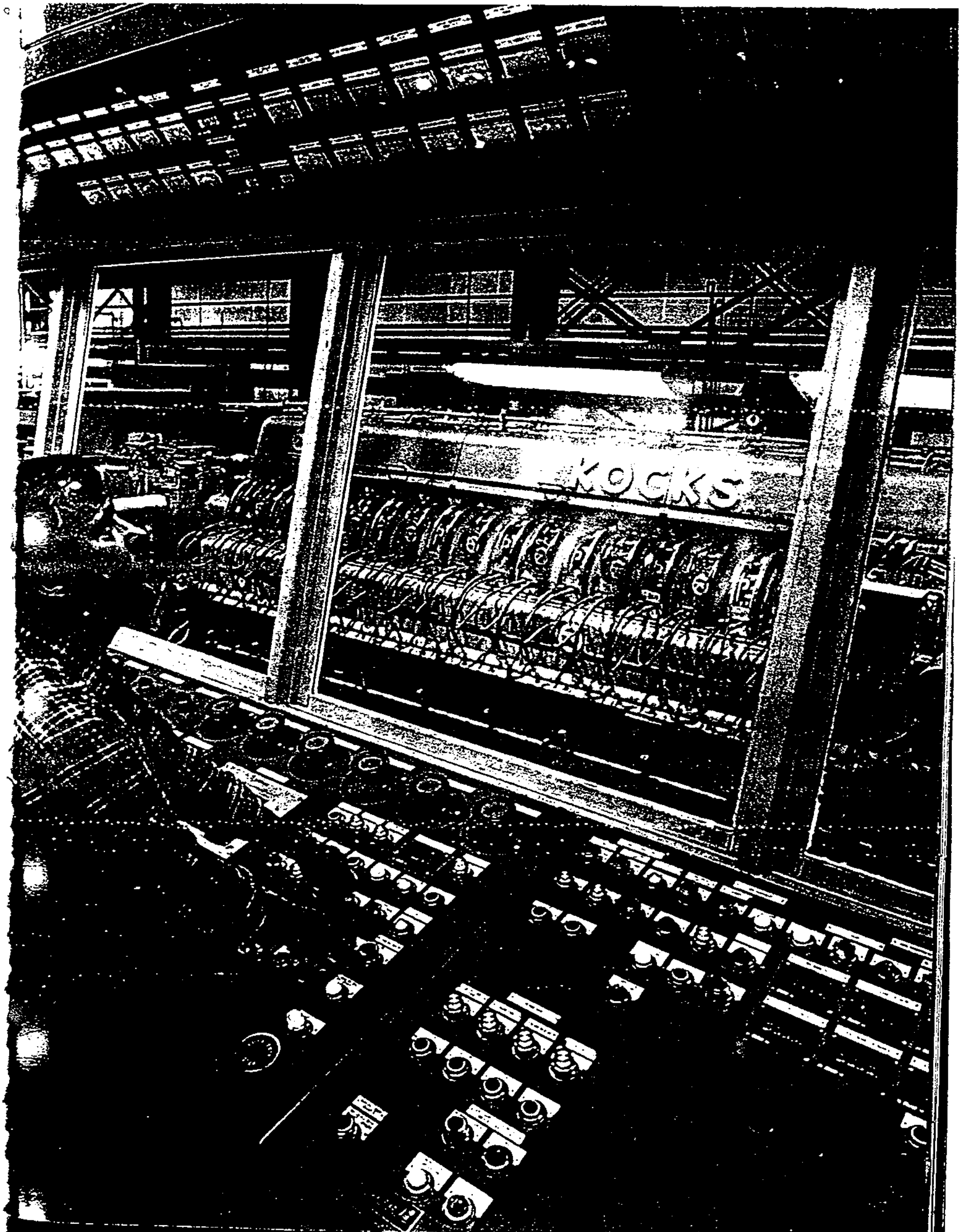
For The Fiscal Year Ended March 31,	1987	1986
	In thousands	
Revenues	$ **130,407**	$ 148,110
Operating Income	**11,349**	11,882
Backlog	**18,946**	15,849

Engineered Materials consists of insulating and tubular products. Our insulating products are designed to withstand high temperatures as well as other demanding circumstances. They insulate furnaces used for various heating and heat-treating purposes, and have applications where temperatures and unusual rates of combustion or chemical reaction are especially demanding. Products include specialty engineered and vacuum-formed ceramic fibers, and insulating and specialty firebrick, as well as plastics, mortars, castables, and special oxide refractories.

Engineered Materials also produces welded carbon and alloy tubing. These high quality products are engineered for special mechanical and pressure applications. Markets include the utility boiler, automotive, agricultural, and construction machinery industries. We also supply tubular products to the U.S. Navy's reactor program. Our welded tubing facility at Alliance, Ohio is highly automated and efficient, and has received large capital investments in recent years to make it more competitive.

below: *B&W K® Insulating Firebrick, manufactured at the Insulating Products Division in Augusta, Georgia, is used throughout the world to line the furnaces and kilns of heat processing industries.* **right:** *The heart of the Tubular Products Division's welded tubing facility in Alliance, Ohio is a 26-stand hot stretch mill, capable of increasing or decreasing wall thicknesses as much as 25 percent.*




KOCKS

Trading

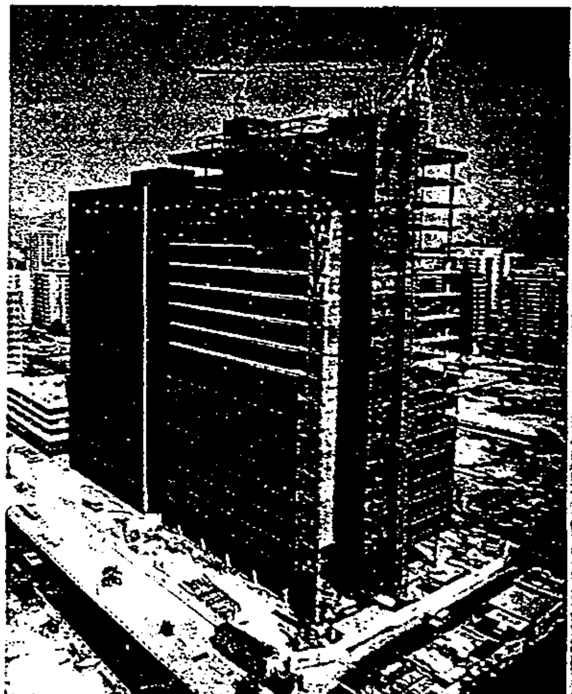
For The Fiscal Year Ended March 31,	1987	1986
	In thousands	
Revenues	**$ 849,496**	$ 655,145
Operating Loss	**(29,306)**	(536)
Backlog	**306,347**	276,785

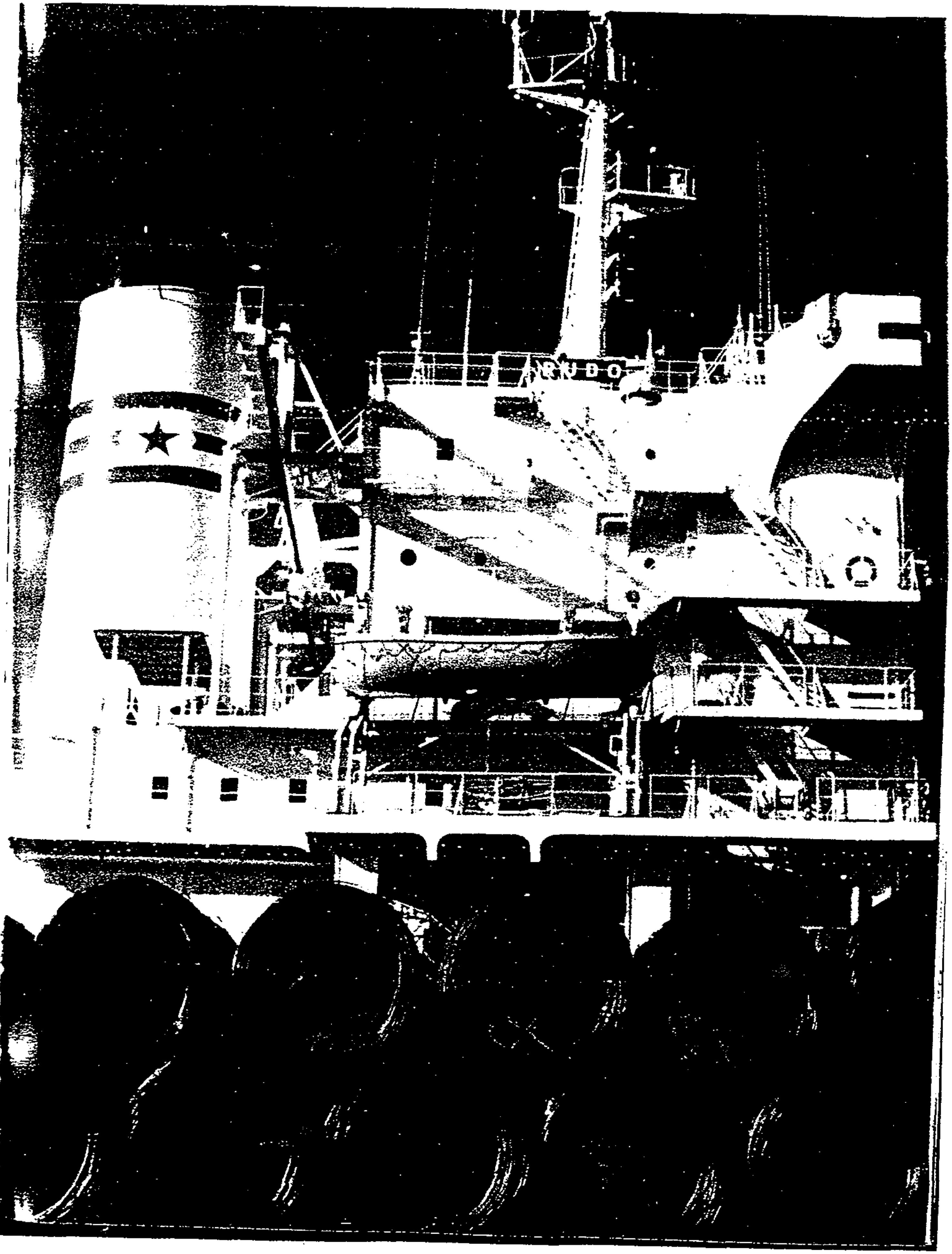
Trading is conducted through a worldwide network of offices managed by McDermott International Trading Co., Inc., and its operating groups, MIT Trading and Coutinho, Caro & Co. Trading activities involve steel and related products, non-ferrous materials, cables and equipment for electric power distribution, petrochemicals and plastics, and countertrade. We also charter ships for waterborne commerce, and assist our customers in arranging insurance and financing.

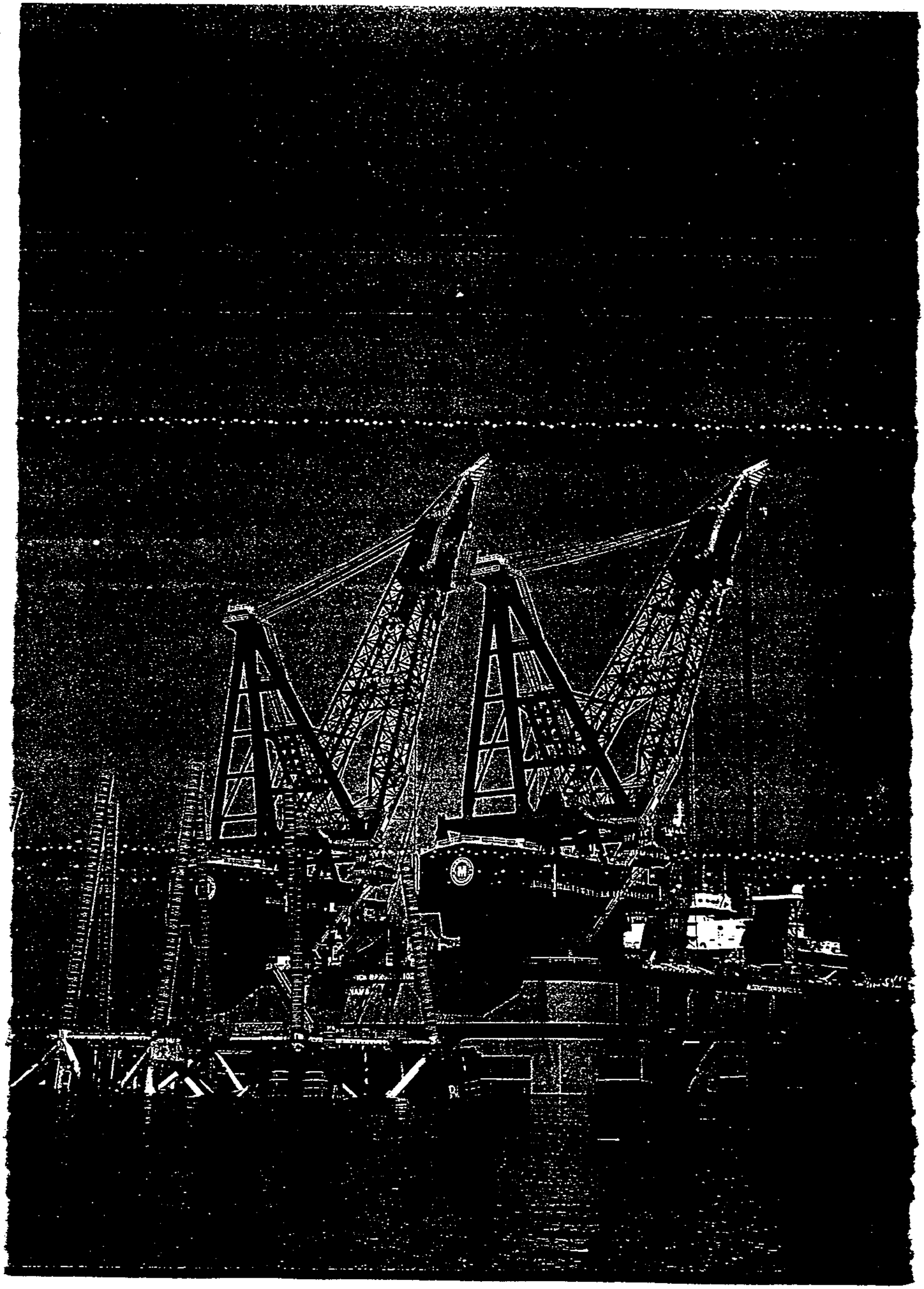
In addition, Coutinho, Caro & Co. also designs, constructs, and erects industrial plants, office buildings, business centers and other large complexes, broadening McDermott's role in engineering and construction. Trading's recent acquisition of Draco International gives the company expanded capabilities in general trading, particularly in the Far Fast.

Trading provides an integral service to other McDermott operating units because it maintains an extensive network of sources for the purchase and shipment of materials. This access, which is particularly advantageous in the procurement of steel, enables the company's other operations to compete more effectively in their respective markets.

below: *Coutinho, Caro & Co., a subsidiary of McDermott International Trading Company, has a construction and engineering unit which builds high-rise buildings like this one in Abu Dhabi. It also builds plants, primarily for the cement, glass, pulp and paper, and food industries.* **right:** *McDermott International Trading Company operates a network of offices around the world, dealing in goods such as steel, wire, chemicals, plastics, machinery, and electrical components. It also operates an international shipping company to assist in the movement of these goods.* **page fourteen:** *McDermott Marine Construction's* Derrick Barge 102 *is one of the industry's most versatile pieces of equipment. It can operate the largest pile-driving hammers available, has a total lift capacity of 13,000 tons, and can accommodate from 750 to 1,500 people, depending upon configuration.*







Directors and Management

Officer-Directors

James E. Cunningham[2]
Chairman of the Board and
Chief Executive Officer

Robert E. Howson
President and Chief Operating Officer,
McDermott Marine Construction and
Babcock & Wilcox
Chief Operating Officer,
McDermott International Trading Co., Inc.

John A. Lynott
Executive Vice President,
Chief Financial and Administrative Officer

Walter M. Vannoy
Vice Chairman of the Board

Directors

Thomas D. Barrow[3]
Retired Vice Chairman of the Board,
The Standard Oil Company -
integrated petroleum company

James L. Dutt[1]
Retired Chairman of the Board and
Chief Executive Officer,
Beatrice Foods, Co. -
producer of food, chemical, and
manufactured products

James A. Hunt[1,2,3,4]
Partner,
Kalb, Voorhis & Co -
securities brokers

J. Howard Macdonald[1]
Chairman of the Board and
Chief Executive Officer,
Dome Petroleum Limited -
oil and natural gas exploration and
production

John A. Morgan[1,2,3]
Partner,
Morgan, Lewis, Githens & Ahn -
investment bankers

John D. Ritchie[2,3]
Consultant and Director of various
corporations

William T. Seawell[2,3,4]
Retired Chairman of the Board and
Chief Executive Officer,
Pan American World Airways, Inc. -
commercial air transportation

Walter B. Shaw[1,4]
Retired Chairman of the Board and
Chief Executive Officer,
Turner Construction Company -
general construction contractors

Walter O. Spencer[3]
Former Dean,
The Graduate School of Business,
Tulane University

John B. Tweedy[1,4]
Attorney and
Former Executive Vice President and Director,
Tosco Corporation -
oil refining and marketing

Russell L. Wagner[1,2,3]
Retired Chairman of the Board and
Chief Executive Officer,
NLT Corporation -
insurance holding company

[1]Audit Committee
[2]Directors Nominating Committee
[3]Officers Salary and Supplemental Compensation Committees
[4]Career Executive Stock Plan Committee

Staff Organizaton

Frank C. Allen, Jr.
Vice President and General Counsel, and
Corporate Secretary

Charles F. Kraus
Vice President,
Tax Administration

Edward A. Robidoux
Vice President and Controller

Robert A. Jolliff
Treasurer

Nicholas E. Mezey
President,
McDermott International
Investments Co., Inc.

George A. Stoddart
Vice President,
Financial Relations

Richard E. Woolbert
Vice President,
Employee and Public Relations

Operating Organization

McDermott Marine Construction

William L. Higgins
Vice President and Group Executive, North and South America, and West Africa Operations

James E. Franklin
Vice President and General Manager, Fabrication and Shipyard Operations

Rene V. Joffrion
Vice President and General Manager, Offshore Operations

Robert D. Miller
Vice President, Marine Construction Services

Sidney P. Victory
Vice President, Houston, Lafayette, and New Orleans Engineering

Robert J. Machen
Vice President and Group Executive, Middle East, Southeast Asia, and Europe Operations

Edward S. Gaffney
Vice President and General Manager, United Kingdom, Egypt and India Operations, and London Engineering

Raymond E. Curtis
Vice President, London Engineering

Michael H. Lam
Vice President and General Manager, Europe Marine Operations

L. Edwards Walker
Vice President and General Manager, Middle East and Southeast Asia Operations

Babcock & Wilcox

Joseph J. Stewart
Vice President and Group Executive, Power Generation
Acting Vice President and General Manager, Domestic Fossil Operations

H. Kerner Smith
Vice President, Marketing, Domestic Fossil Operations

Robert E. Donovan
Vice President and General Manager, Babcock & Wilcox International

E.O. (Neal) Hooker
Vice President and General Manager, Americon, Inc.

E. Allen Womack, Jr.
Vice President, Research & Development and Contract Research Divisions

John P. Eckert
Vice President and Group Executive, Defense and Nuclear Power

George F. Ellis
Vice President, Government Operations

William F. Heer
Vice President and General Manager, Nuclear Equipment Division

Charles W. Pryor
Vice President and General Manager, Nuclear Power Division

Roger E. Tetrault
Vice President and General Manager, Naval Nuclear Fuel Division

M.A. (Bud) Keyes
Vice President and Group Executive, Industrial Products and Services

Douglas Cannon
President, Bailey Controls Company

John L. Finn
President, TLT-Babcock, Inc.

J. Brewster Given
Vice President and General Manager, Insulating Products Division

John A. Pittman
Vice President and General Manager, McDermott Heat Transfer Company

Stephen L. Seabury
Vice President and General Manager, Electronic Information Systems

Anton Salem
Vice President, Marketing

McDermott International Trading

Karel C.M. Thyssen
President, McDermott International Trading Co., Inc.
Chairman, Board of Management, Coutinho, Caro & Co. AG

Klaus F. Hummel
Board of Management, Coutinho, Caro & Co. AG

Helmut Mamsch
Board of Management, Coutinho, Caro & Co. AG

Jan J. Schütt
Board of Management, Coutinho, Caro & Co. AG

Friedrich C. Seifarth
Board of Management, Coutinho, Caro & Co. AG

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

Form 10-K

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

For the fiscal year ended March 31, 1987 — Commission file number 1-8430

McDermott International, *inc.*

(Exact name of Registrant as specified in its Charter)

Republic of Panama **(State or Other Jurisdiction of Incorporation or Organization)**	**72-0593134** **(I.R.S. Employer Identification No.)**
1010 Common Street, New Orleans, Louisiana **(Address of Principal Executive Offices)**	**70112** **(Zip Code)**

Registrant's Telephone Number, including area code (504) 587-5400

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock $1 Par Value	New York Stock Exchange
Warrants to Purchase Common Stock $1 Par Value	New York Stock Exchange
Rights to Purchase Common Stock (Currently Traded with Common Stock)	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act:

None

(Title of Class)

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, and (2) has been subject to such filing requirements for the past 90 days. Yes X No __

The aggregate market value of voting stock held by non-affiliates of the Registrant was $1,059,613,000 as of June 1, 1987.

The number of shares outstanding of the Company's Common Stock at June 1, 1987 was 37,166,157.

The Proxy Statement for the 1987 Annual Meeting of Shareholders is incorporated by reference into Part III of this report.

McDERMOTT INTERNATIONAL, INC.

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PAGE

PART I

PART I

Items 1. and 2. BUSINESS AND PROPERTIES

A. GENERAL

McDermott International, Inc. ("International") was incorporated under the laws of the Republic of Panama in 1959. Under a reorganization during the fiscal year ended March 31, 1983, International became the parent company of the McDermott group of companies which includes McDermott Incorporated (the "Delaware Company") which prior to the reorganization was the parent company. International's Common Stock and the Delaware Company's Series A $2.20 Cumulative Convertible Preferred Stock and Series B $2.60 Cumulative Preferred Stock are publicly held.

Unless the context otherwise requires, hereinafter "International" will be used to mean McDermott International, Inc., a Panama corporation, the "Delaware Company" will be used to mean McDermott Incorporated, a Delaware corporation, and "McDermott International" will be used to mean the consolidated enterprise.

During fiscal year 1985, International acquired the international trading business of Coutinho, Caro & Co. KGaA ("Coutinho"), which is headquartered in Hamburg, West Germany.

McDermott International operates in four business segments:

- Marine Construction Services performs activities for the oil and gas industry for offshore development drilling and for the production and transportation of oil and gas on a worldwide basis.
- Power Generation Systems and Equipment principally serves the electric utility industry and the U.S. Government.
- Engineered Materials produces metal tubular products for mechanical and pressure applications, and insulating products for a variety of industries.
- Trading comprises the worldwide trading, construction and engineering operations of Coutinho as well as other trading services of International.

The businesses of the Power Generation Systems and Equipment and Engineered Materials segments are conducted primarily through a subsidiary of the Delaware Company, The Babcock & Wilcox Company ("B&W"), which was acquired in 1978. In June 1987, McDermott International announced its intention to permanently close the seamless tubular line of business of the Engineered Materials segment. See Note 2 to the consolidated financial statements for additional information with respect to discontinued operations.

McDermott International has a continuing program of reviewing acquisition and disposition opportunities.

The following tables show revenues and operating income from continuing operations and their respective percentage contributions for the business segments of McDermott International for the three fiscal years ended March 31, 1987. See Note 11 of notes to consolidated financial statements for additional information with respect to McDermott International's business segments and operations in different geographic areas.

REVENUES AND PERCENT OF REVENUES

(Dollars in Millions)

	For Fiscal Years Ended March 31,					
	1987		1986		1985	
Marine Construction Services	$ 862.8	26%	$ 908.2	29%	$ 1,045.9	35%
Power Generation Systems and Equipment	1,526.0	46%	1,447.4	47%	1,413.5	47%
Engineered Materials	130.4	4%	148.1	5%	153.2	5%
Trading	849.4	26%	655.1	21%	435.9	14%
Intersegment Transfer Eliminations	(79.3)	(2%)	(49.6)	(2%)	(26.0)	(1%)
Total	$ 3,289.3	100%	$ 3,109.2	100%	$ 3,022.5	100%

OPERATING INCOME (LOSS)(1)

(Dollars in Millions)

	For Fiscal Years Ended March 31,		
	1987	1986	1985
Marine Construction Services	$ (81.5)	$ (30.2)	$ (8.3)
Power Generation Systems and Equipment	72.3	36.7	20.8
Engineered Materials	11.3	11.9	12.9
Trading	(29.3)	(0.5)	(4.1)
Total	$ (27.2)	$ 17.9	$ 21.3

(1) Reconciling items between Segment Operating Income (Loss) and Operating Income (Loss) in the Consolidated Statement of Income (Loss) and Retained Earnings are General Corporate Expenses.

B. MARINE CONSTRUCTION SERVICES

GENERAL

The Marine Construction Services segment consists of the design, construction and installation of specialized offshore fixed platforms and marine pipelines used for development drilling, production and transportation of oil and gas. Marine Construction Services also includes engineering and construction services for oil production in shoreline and marshland areas (principally in Louisiana and Texas); operation of a shipyard for the construction, repair and maintenance of tugboats, barges and other small vessels; and the engineering and construction of processing plants for the oil, gas and petrochemical and mineral industries, primarily for offshore installation.

Fixed platforms, which are fastened to the seafloor by pilings driven through their structural legs, have been installed by McDermott International in water depths of more than 1,000 feet. These platforms have been engineered to withstand increasingly greater weights and stresses as the search for oil and gas has expanded into deeper water and into areas subject to severe weather conditions.

McDermott International, a world leader (based upon industry standards) in the fabrication of offshore structures, has a principal fabrication yard located on approximately 1,300 acres of land, under lease, near Morgan City, Louisiana. This segment also operates fabrication yards on leased property in Indonesia at Batam Island; in the Middle East at Dubai and Ras Al Khaimah of the United Arab Emirates, and has fabrication capabilities on leased property in South East Asia at Singapore and in West Africa at Warri, Nigeria. McDermott International also operates a fabrication yard on company-owned property in Scotland, near Inverness. The equipment used at these yards, which is capable of fabricating a full range of offshore structures, consists principally of cranes, welding equipment, machine tools, robots and other automated equipment, in addition to other fabrication equipment, most of which is movable. This segment also operates a shipyard on approximately 58 acres of leased land in Morgan City, Louisiana.

Expiration dates, including renewal options of leases covering land for the shipyard and fabrication yards, follow:

Morgan City, Louisiana	Years 1988-2032
Batam Island, Indonesia	Year 2008
Dubai, U. A. E.	Year 2005
Ras Al Khaimah, U. A. E.	Year 1987
Singapore	Year 1999
Warri, Nigeria	Year 2065

This segment operates the largest fleet of marine equipment used in major offshore construction. The nucleus of a "construction spread" is a large derrick barge, pipelaying barge or combination derrick-pipelaying barge capable of offshore operations for an extended period of time in remote locations. The lifting capacities of McDermott International's derrick and combination derrick-pipelaying barges range from 700 tons to 13,000 tons. These barges, which range in length from 300 feet to 660 feet, are fully equipped with revolving cranes, auxiliary cranes, welding equipment, pile driving hammers, anchor winches and a variety of additional gear. The largest of the existing vessels provides quarters for approximately 750 workers. Included in the above is the DB102, the world's largest semi-submersible derrick barge in both size and lifting capacity.

This segment owns and operates 6 derrick barges, 3 pipelaying barges, 11 combination derrick-pipelaying barges and 2 pipeburying barges. These include 4 semi-submersible vessels presently assigned to the North Sea and the Gulf of Mexico, of which 3 are derrick barges capable of lifting 2,000 to 13,000 tons, 2 of which are self-propelled. The other semi-submersible vessel is a lay barge capable of laying 72 inch diameter pipe (including concrete coating) and is operable in water depths up to 2,000 feet. During fiscal 1987, this segment acquired a new shearleg crane capable of lifting up to 5,000 tons. The shear-leg crane has the capability of being installed on a number of vessels within the marine fleet. McDermott International also owns or leases a substantial number of other vessels such as tugs, utility boats and cargo barges to support the major marine vessels. Major spreads of equipment are in the Gulf of Mexico, the U.S. West Coast, the Middle East, South East Asia, the North Sea, and West Africa.

Underwater pipelaying operations conducted by this segment have required the development of new techniques and equipment as water depths have increased. McDermott International has the capability of installing pipelines with an outside diameter (including concrete coating) of up to 72 inches. This segment has installed several of the world's deepest marine pipelines including one from a platform in the Gulf of Mexico at depths greater than 1,000 feet and two which cross the Norwegian Trench in the North Sea at depths approaching 1,000 feet.

In connection with its construction and pipelaying activities, this segment conducts diving operations which, because of the water depths involved, require sophisticated equipment, including diving bells and an underwater habitat.

This segment has strengthened its competitive position through an aggressive program for automation and modernization of engineering, welding equipment, pipemill facilities and pipelaying operations and increased lifting capacity of its derricks.

McDermott International owns a 49% interest in a Mexican joint venture that operates 3 self-propelled combination barges and one pipelaying barge. Of these, 2 barges are capable of lifting 2,000 tons.

This segment's shipyard facility supplies complete maintenance and construction facilities and is a builder of a variety of marine vessels, including large tugs, packaged rigs, dredges, barges, ferries, oceanographic research and other ocean-going work vessels. During fiscal 1987, this facility was awarded its first contract to build a prototype ocean-going surveillance vessel for the U.S. Navy. The function of this vessel is to collect, process and transmit acoustic data.

Foreign Operations

The amounts of Marine Construction's revenues and operating income derived from operations outside of the United States, and the approximate percentages of those revenues and operating income to McDermott International's total revenues and operating income (loss) were as follows:

	REVENUES		OPERATING INCOME (LOSS)	
Fiscal Year	**Amount**	**Percent**	**Amount**	**Percent**
	(Dollars in Thousands)			
1987	$ 555,362	17	$ (47,506)	52
1986	603,532	19	18,657	-
1985	758,169	25	73,029	-

Raw Materials

The raw materials used by this segment, such as carbon and alloy steel in various forms, welding gases, concrete, fuel oil and gasoline, are available from many sources and this segment is not dependent upon any single supplier or source. Although shortages of certain of these raw materials and fuels have existed from time to time, no serious shortage exists at the present time.

Customers and Competition

This segment's principal customers are the larger oil and gas companies and the U.S. and other governments. Customers generally contract with this segment for the design, construction and installation of specific platforms, pumping stations, marine pipelines, production networks, and the construction of marine vessels. Contracts are usually awarded on a competitive bid basis.

There are a number of companies which compete effectively with McDermott International in each of the separate marine construction phases in various parts of the world, but none has the geographical distribution or the extent of capabilities of McDermott International.

Backlog

As of March 31, 1987 and 1986, the Marine Construction Services' backlog amounted to $470,514,000 and $735,765,000, respectively, a decrease of approximately 36%. The significant reduction in backlog is the result of lower levels of demand for Marine Construction Services discussed in more detail below. Of the March 31, 1987 backlog, $414,722,000 is expected to be recognized in fiscal 1988, and $55,792,000 in fiscal years 1989-1990.

Work is performed on a fixed price, cost plus or day rate basis or combination thereof. Almost all contracts call for progress payments and the segment attempts to cover increased costs of anticipated changes in general labor rates and material costs on long-term contracts, either through an estimation of such changes, which is reflected in the original fixed price, or through price escalation clauses. This segment's contracts for work in foreign areas generally provide for payment in U.S. Dollars, with exceptions for payments in foreign currencies in amounts approximately equal to expenses to be incurred by this segment in those currencies.

Factors Affecting Demand

Marine Construction Services' activity has traditionally been a cyclical industry depending mainly on the capital expenditure outlay of major oil and gas companies and foreign governments for developmental construction. These expenditures, which continue to be at low levels, are influenced by the price of oil, the sale and expiration dates of offshore leases in the United States and abroad, the discovery rates of new oil and gas reserves in offshore areas, local and international political and economic conditions, and the ability of the oil and gas industry to generate capital.

The price of oil and its uncertainty in the future has a strong effect on exploration and production which ultimately affects the demand for Marine Construction Services' activity. The oil surplus which the world has been experiencing has a depressing impact on oil prices, which will continue until consumption exceeds available production. The level of oil prices since 1986 has led the oil industry, including many of this segment's customers, to reduce capital expenditure budgets, resulting in lower levels of demand for Marine Construction Services. However, the strengthening of prices in recent months combined with oil and gas reserve depletions is expected to lead oil and gas companies to increase capital expenditures. Over the long-term, McDermott International expects an end to the current oil surplus and an improved level of demand for its Marine Construction Services.

C. POWER GENERATION SYSTEMS AND EQUIPMENT

General

The Power Generation Systems and Equipment segment, which business is primarily performed through B&W, is a supplier of individually engineered complete fossil fuel boilers, nuclear steam systems, nuclear fuel and nuclear fuel assemblies for the electric utility industry, as well as fossil fuel boilers for industrial processes and power generation. Power Generation Systems and Equipment also provides replacement parts, customer services and engineered modifications of existing fossil and nuclear steam systems, and specially engineered accessories and components, such as air heaters and precipitators, cleaning systems for heat transfer surfaces, nuclear reactor components, microprocessor-based control systems and nuclear control rod drives. It also supplies process recovery boilers and pollution control systems for the process and utility industries, heavy pressure vessels and air and water-cooled heat exchangers, fans and reflective metallic thermal insulation. This segment also provides nuclear reactor and fuel components and other components for the U.S. Department of Energy and the U.S. Department of Defense. It also is engaged in the erection of utility plants and industrial facilities and the repair and alteration of such existing equipment.

In addition, B&W is actively involved in the market for providing power through cogeneration, refuse and other small power units, primarily with non-traditional fuel burning capability. It is participating in this market as an equipment supplier, an equity participant, and as an operations and maintenance contractor. Fluid bed combustors are often the preferred boiler design for these projects and B&W offers both circulating and bubbling fluidized bed combustors to service this and the boiler retrofit market. B&W is also developing pressurized fluid bed combustors for commercial applications.

With regard to commercial nuclear power generation, utilities have delayed certain construction programs and in many cases have cancelled orders for nuclear steam generating systems. No contracts for domestic nuclear steam systems have been awarded in several years. As a consequence, engineering, computer services, other customer services, and fuel assemblies for refueling existing nuclear reactors have become the major part of this segment's commercial nuclear activity.

Business related to the supply of nuclear fuel assemblies and nuclear reactor components to the U.S. Navy has become an increasingly important part of this segment's results. Revenues from the U.S. Government related to this activity were approximately 12%, 13% and 14% of McDermott International's total revenues for fiscal years 1987, 1986 and 1985, respectively. This activity has contributed significant operating income to McDermott International in all three fiscal years and the Power Generation Systems and Equipment segment would have had an operating loss in fiscal years 1986 and 1985 without the contribution from this program. A decline in this business could have a significant impact on this segment's profitability.

To capitalize on its highly specialized manufacturing and welding capabilities, B&W is actively pursuing new opportunities in the defense market. In fiscal 1987, B&W acquired a precision manufacturer of ordnance metallic components, and established a systems organization for the development of an integrated military ordnance business.

The principal plants of B&W manufacturing power generation systems and equipment are situated at Barberton, Lancaster and Wickliffe, Ohio; Lynchburg, Virginia; Paris and Beasley, Texas; West Point, Mississippi; Williamsport, Pennsylvania; Indianapolis, Indiana; and Cambridge, Ontario. These plants and properties are owned by B&W and are well maintained, have suitable equipment, and are of adequate size. B&W has an ongoing program for automating and modernizing this segment's engineering and manufacturing facilities.

Raw Materials

The principal raw materials used by B&W to construct power generation systems and equipment consist of carbon and alloy steels in various forms, such as plate, structurals, bars, sheet, strip, heavy wall pipe and tubes. Significant amounts of components are also purchased for assembly into the equipment. These raw materials and components generally are purchased by B&W as needed for individual contracts. Requirements for very high alloy tubing for the naval nuclear reactor components program are supplied from within B&W.

The principal raw materials used by B&W in the manufacture of nuclear fuel components and assemblies consist of uranium (customer furnished), zircalloy and specialized stainless steel.

Although shortages of certain of these raw materials have existed from time to time, no serious shortage exists at the present time.

Customers and Competition

The principal customers of this business segment are the electric utility industry (including government-owned utilities), the U.S. Government (including its contractors), and the pulp and paper and other process industries. The electric utility industry (including government-owned utilities) accounted for approximately 19%, 20% and 22% of McDermott International's total revenues for fiscal years 1987, 1986 and 1985, respectively. U.S. Government business with this segment accounted for approximately 13%, 14% and 14% of McDermott International's total revenues for such periods.

Power Generation Systems and Equipment's orders are customarily awarded in response to competitive bids submitted pursuant to proposals based on the estimated cost of each job. Domestically, a relatively small number of companies specializing in large steam generating equipment compete with B&W in the utility fossil fuel steam system business. In international markets, these companies plus several foreign-based companies compete with B&W. In the sale of nuclear steam systems. B&W competes with a small number of companies. In the sale of nuclear fuel and nuclear fuel assemblies, B&W competes with the other manufacturers of nuclear steam systems. In the controls and instrumentation market, B&W competes with several broad-line suppliers and a great number of specialty suppliers. A number of companies are in competition with B&W in industrial boilers and the small power plant business. Other suppliers of fossil and nuclear fuel steam systems, as well as many other businesses in the case of fossil fuel systems, compete for repair and alterations and other services required to backfit and maintain existing systems. In the supply of nuclear fuel assemblies and nuclear components to the U.S. Navy, there are a small number of suppliers with B&W being the largest based upon revenues.

Backlog

Backlog as of March 31, 1987 was $2,998,268,000 or approximately 79% of McDermott International's backlog. Backlog at March 31, 1986 was $3,035,061,000. Of the March 31, 1987 backlog, it is expected that approximately $1,036,950,000 will be recorded in revenues in fiscal 1988, $1,407,260,000 in fiscal years 1989-1992, and $554,058,000 thereafter. If in management's judgment it becomes doubtful whether contracts will proceed, the backlog is adjusted accordingly.

Reduced electric demand growth, excess generating capacity, environmental restraints and financial pressures on the utility industry have resulted in continued delays, suspensions and cancellations of steam systems and environmental control systems. At March 31, 1987, delayed and suspended fossil fuel utility boiler and environmental control system contracts included in the backlog constituted approximately 7% of McDermott International's total backlog. B&W, at the present time, believes that these fossil fuel utility boiler and environmental control system contracts will proceed after the period of delay or suspension. If contracts are delayed, suspended or cancelled, B&W is usually entitled to a financial settlement related to the individual circumstances of the contract. This segment's backlog with the U.S. Government was approximately 25% of McDermott International's total backlog at March 31, 1987.

B&W attempts to cover increased costs of anticipated changes in labor, material and service costs of long-term contracts either through an estimation of such changes, which is reflected in the original price, or through price escalation clauses. Most long-term contracts have provisions for progress payments.

Factors Affecting Demand

New orders by the U.S. electric utility industry have been at depressed levels because of the low level of electrical demand growth, primarily due to cost induced conservation, and a decreased dependence on energy by U.S. industry. Fiscal 1984 saw the start of a moderate increase in electrical demand growth due, primarily, to the economic recovery, although existing capacity continues to be adequate to meet current demand. B&W continues its efforts to obtain orders outside the United States, expand its business in backfitting existing power plants, and increase its shares of the small power plant market. In fiscal 1987, B&W received two orders for the long-term operation of two of these small power plants.

D. ENGINEERED MATERIALS

General

The Engineered Materials segment consists of tubular and insulating products designed and manufactured by B&W. B&W has announced its intention to permanently close its manufacturing and steelmaking facilities in Beaver Falls, Ambridge and Koppel, Pennsylvania and in Bryan, Texas, which comprise the seamless tubular line of business of the Engineered Materials segment. Management believes that continued worldwide overcapacity and depressed market conditions in the product lines of the seamless tubular line of business have permanently impaired the prospects for this line of business. Accordingly, at March 31, 1987, the seamless tubular line of business has been accounted for as a discontinued operation in the consolidated financial statements, and the Consolidated Statements of Income (Loss) and Retained Earnings and Changes in Financial Position have been restated for all prior periods presented. The business and properties discussion of the Engineered Materials segment includes only welded tubular operations, tubing for naval nuclear reactor components and insulating products.

Tubular products include alloy and carbon welded tubes. These are products of high quality and are engineered for special mechanical and pressure tubing applications.

Insulating products include specially engineered and vacuum-formed ceramic fibers, insulating and specialty firebrick, fire protection insulation, plastics, mortars, castables and special oxide refractories. These insulating products are used in high temperature furnaces for various heating and heat-treating purposes and in other applications where the temperatures and rates of combustion or chemical reactions are unusually demanding.

B&W manufactures tubular products at Alliance, Ohio and insulating products are manufactured principally at Augusta, Georgia; Emporia, Kansas; and Burlington, Ontario. All of these plants and properties are owned by B&W, are well maintained, have suitable equipment, and are of adequate size. In fiscal 1985, B&W began an extensive two-year modernization of its welded-tube facility at Alliance, Ohio. The major portion of this project was placed in service in fiscal 1987.

Raw Materials

The principal raw materials used by B&W in the manufacture of welded tubular products consist of strip steel which it purchases in the open market. Tubing for naval nuclear reactor components is finished from very high alloy steel tubulars.

The principal raw material used to produce this segment's insulating products is kaolin clay which it obtains under a long-term supply contract. Also used are bauxite, alumina, silicon carbide, gypsum, plaster and wood chips, all of which are purchased in the open market.

Although shortages of certain of these raw materials have existed from time to time, no serious shortage exists at the present time.

Customers and Competition

The principal users of the tubular products portion of this business segment are the automotive, agricultural and construction machinery, fabricated metal and power generation industries. This segment services these users through both direct sales and sales to distributors. The sole user of tubing for naval nuclear reactor components is the U.S. Navy's naval reactor program.

The principal customers of the insulating products portion of this business segment are the iron and steel, chemical process, ceramic and foundry and furnace builders industries.

Many companies, both domestic and foreign, are in competition with B&W with respect to tubular and insulating products.

Backlog

As of March 31, 1987, the Engineered Materials' backlog was $18,946,000 compared with $15,849,000 as of March 31, 1986. Substantially all of this segment's backlog is expected to be recorded in revenues in fiscal 1988.

Factors Affecting Demand

Purchases of welded tubular products by nearly all industries served by this segment were at severely low levels throughout fiscal years 1987, 1986 and 1985. This segment supplies mechanical and pressure tubing for low stress and low corrosive applications and mechanical tubing where strict manufacturing tolerances are required or use of low carbon and alloy steels is acceptable. Demand for such tubing is closely tied to the capital spending of user industries or their ultimate customers, and such spending is at low levels. Demand for insulating products is dependent upon capital spending for modernization and expansion, production levels and energy conservation in user industries. Demand for tubing for naval nuclear reactor components is dependent on the U.S. Navy's nuclear shipbuilding program.

E. TRADING

General

The Trading segment operates through a network of offices located in the United States, Continental Europe, the United Kingdom, West Africa and South East Asia. The business is conducted through Coutinho, Caro & Co. KGaA headquartered in Hamburg, West Germany and through McDermott International Trading Co., AG headquartered in Zug, Switzerland.

This segment buys and sells primarily steel products, wire and wire products, non-ferrous materials, chemical products, cables and equipment for electric power distribution, electrical components, tools, machinery and utility vehicles, aromatics, olefins and plastics. The operations of this segment also include inland and ocean transport as well as assisting customers in arranging insurance and financing. While this segment ordinarily functions as a principal in its trading activities, it also acts as agent under certain circumstances. In addition, this segment regularly enters into substantial forward purchases and sales of all materials handled. These are not normally maintained over periods longer than three months.

This segment does not produce any of the materials in which it trades, but purchases them from others in the open market. No significant long-term contractual supply arrangements are in place. This segment has access to and purchases these materials on a worldwide basis.

The Trading segment also provides certain construction and engineering services which consist of the design, construction and erection of industrial plants, primarily for the cement, glass, pulp and paper and food industries.

Customers and Competition

The principal customers of this segment are warehousing and stockholding companies, steel producers and end-users of steel products such as construction companies, large chemical companies, and a number of other industrial consumers. These customers are mainly commercial organizations although some are partially or wholly government owned or controlled.

This segment's competitors in international trade include many large trading organizations and producers or end-users of the products in which this segment trades. No one competitor is dominant, although many have greater financial and other resources than McDermott International. Of the factors affecting competition in this business, the most significant are expertise, service and reliability.

This segment's customers for construction and engineering services include various process industries and development companies, some of which are owned or partly controlled by governments of the countries in which the contracts are performed. Customers generally contract with this segment for the design and construction of specific industrial plants or high-rise buildings. Contracts are normally awarded on a competitive bid basis and, particularly at the present time, are heavily dependent upon the conclusion of related project financing arrangements. Competition in the construction and engineering business is present on a worldwide basis, from companies based in all major developed countries, none of which is dominant.

Backlog

As of March 31, 1987, Trading segment backlog was $306,347,000 compared with $276,785,000 as of March 31, 1986. Of the March 31, 1987 backlog, $278,160,000 is expected to be recognized in fiscal 1988, and $28,187,000 in fiscal 1989.

The majority of trades are completed within three months. Payment is usually based on normal commercial terms and is normally settled using letters of credit arranged through various banks. Payment terms may be extended under certain circumstances. Credit insurance is purchased for the majority of trade accounts receivable.

Trades are primarily settled and major contracts normally call for payment in U.S. Dollars or Deutschemarks. This segment enters into substantial forward currency exchange contracts as a means of hedging its commitments in various currencies.

Construction and engineering work is principally performed on a turnkey fixed price or turnkey cost plus basis or a combination thereof. Almost all contracts call for progress payments and the segment attempts to cover increased costs on long-term contracts, either through an estimation of such charges, which is reflected in the original fixed price, or through price escalation clauses.

Factors Affecting Demand

Demand for this segment's services is influenced by the variety of changing market factors which affect supply and demand for the materials in which the segment trades. In addition, local and international political and economic conditions influence the capital and industrial development budgets of developing nations and their ability to obtain financing for projects or trading.

Due to the present uncertainty in the funding of industrial expansion programs of developing nations and delays in completing project financing arrangements, few contracts are being awarded at the present time. These factors are considered likely to affect the segment's construction and engineering activities until world demand and credit conditions become more favorable.

F. PATENTS AND LICENSES

Many U. S. and foreign patents have been issued to McDermott International and it has many pending patent applications. Patents and licenses have been acquired and licenses have been granted to others when advantageous to McDermott International. While McDermott International regards its patents and licenses to be of value, no single patent or license or group of related patents or licenses is believed to be material in relation to its business as a whole.

G. RESEARCH AND DEVELOPMENT ACTIVITIES

McDermott International conducts research and development activities at Alliance, Ohio; Lynchburg, Virginia; and Houston, Texas; and also conducts development activities at its various manufacturing plants and engineering and design offices. During the fiscal years ended March 31, 1987, 1986 and 1985, approximately $77,600,000, $86,000,000 and $79,800,000, respectively, was spent by McDermott International on research and development activities, of which approximately $42,100,000, $53,400,000 and $41,600,000, respectively, was paid for by customers of McDermott International. Research and development activities were related to development and improvement of new and existing products and equipment and conceptual and engineering evaluation for translation into practical applications. Approximately 407 employees were engaged full time in this activity.

H. INSURANCE

McDermott International maintains liability and property insurance that it considers normal in the industry. Certain risks are either not insurable or are available only at rates which McDermott International considers uneconomical. Among such risks are war and confiscation in certain areas of the world at certain times, and pollution liability in excess of relatively low limits. Depending on competitive conditions and other factors, McDermott International endeavors to obtain contractual protection against uninsured risks from its customers.

McDermott International has coverage under commercially available nuclear liability and property insurance for its five nuclear facilities. Two of these facilities are also subject to the indemnity and limitations of liability provisions of the Price-Anderson Act. This Act limits the public liability of manufacturers and operators of licensed nuclear facilities and other parties who may be liable, in respect of, and indemnifies them against all claims in excess of an amount which is determined by the sum of commercially available nuclear liability insurance plus certain retrospective premium assessments payable by operators of commercial nuclear reactors. One additional facility is covered by a contractual indemnity from the U.S. Government whereby the Government has assumed the risks of public liability claims.

McDermott International's insurance policies do not cover liability and property damage losses resulting from nuclear incidents at facilities of its utility customers. To protect against such losses McDermott International has obtained contractual indemnification from such customers and waivers of their insurers' rights of subrogation and generally has been named as an additional insured under its customers' nuclear property insurance policies. In addition, McDermott International's third-party nuclear liability is an insured risk under such customers' nuclear liability policies and the Price-Anderson Act indemnity discussed above.

McDermott International's offshore construction business is subject to the usual risks of operations at sea, with additional exposure due to the utilization of expensive construction equipment, sometimes under extreme weather conditions, often in remote areas of the world. In addition, McDermott International operates in many cases on or in proximity to existing offshore facilities which are subject to damage by McDermott International and such damage could result in the escape of oil and gas into the sea.

McDermott International has two wholly-owned insurance subsidiaries. To date, these subsidiaries have written policies concerning general liability, builders' risk within certain limits, marine hull, and workers compensation for McDermott International. No significant amounts of insurance have been written for unrelated parties.

I. EMPLOYEES

At March 31, 1987, McDermott International employed, under its direct supervision in continuing operations, approximately 29,000 persons compared with 33,000 at March 31, 1986. Approximately 6,000 employees were members of labor unions at March 31, 1987 compared with 7,000 employees at March 31, 1986. McDermott International considers its relations with its employees to be satisfactory.

J. GOVERNMENT REGULATIONS

McDermott International's compliance with U.S. federal, state and local environmental protection regulations necessitated capital expenditures of $418,000 in fiscal 1987, and it expects to spend another $5,474,000 over the next five years. However, McDermott International cannot predict all the environmental requirements or circumstances which will exist in the future. The recurring costs of complying with environmental regulations was a charge against income before taxes of approximately $874,000 in fiscal 1987.

McDermott International performs significant amounts of work for the U.S. Government under both prime contracts and subcontracts and operates certain nuclear facilities and thus is subject to continuing reviews by governmental agencies including the Environmental Protection Agency and the Nuclear Regulatory Commission.

Compliance with government regulations controlling the discharge of materials into the environment, or otherwise relating to the protection of the environment, does not have, nor is it expected to have a material effect upon the competitive position of McDermott International.

K. INTERCOMPANY AGREEMENT

In November 1982, International and the Delaware Company entered into a Stock Purchase and Sale Agreement (the "Intercompany Agreement"), pursuant to which the Delaware Company has the right to sell to International and International has the right to buy from the Delaware Company units of stock, each unit consisting of one share of International Common Stock and one share of International Series A Preferred Stock. If a unit is purchased by International upon the Delaware Company's exercise of its right to sell under the Intercompany Agreement, the purchase price of such unit will be 90% of the then current value of the unit, as defined in the agreement (the "unit value"). If a unit is purchased by International pursuant to an exercise of its right to purchase under the Intercompany Agreement, the purchase price of such unit will be 110% of the unit value. As of March 31, 1987, the unit value was $7,025 and the aggregate unit value of the Delaware Company's 100,000 units was $702,547,000.

L. DISCONTINUED OPERATIONS

In June 1987, McDermott International announced its intention to permanently close its manufacturing and steelmaking facilities in Beaver Falls, Ambridge and Koppel, Pennsylvania and in Bryan, Texas, which comprise the seamless tubular line of business of the Engineered Materials segment. Management believes that continued worldwide overcapacity and depressed market conditions in the product lines of the seamless tubular line of business have permanently impaired the prospects for this line of business.

Management anticipates that the permanent closure of the seamless tubular line of business, which principally includes seamless tubes and seamless rolled rings and employed approximately 700 persons at March 31, 1987 compared with approximately 1,900 at March 31, 1986, will be completed during fiscal 1988.

Item 3. LEGAL PROCEEDINGS AND PROPOSED TAX DEFICIENCY

The Internal Revenue Service (the "IRS") has examined the U.S. federal income tax returns of the Delaware Company for its fiscal years ended March 31, 1972 through March 31, 1983; and those of International for its fiscal years ended November 30, 1976 through March 31, 1983; and those of B&W for its fiscal years ended December 31, 1977 and March 31, 1978, the latter being the year ended on the day B&W was acquired by the Delaware Company. The IRS has issued notices which propose additions to the U.S. federal income tax liability of the Delaware Company and International in respect of each of these years. Such notices assert among other things that the Delaware Company is subject to U.S. federal income tax on unremitted earnings of International on the ground that the portion thereof which constituted "Subpart F" income under Sections 951 through 964 of the Internal Revenue Code substantially exceeded the portion so classified by the Delaware Company in its U. S. federal income tax returns. Additional U. S. federal income taxes asserted by the notices in question which are allocable to Subpart F income items from International are approximately $245,000,000.

In the notices issued by it for years through March 31, 1982, the IRS does not state specifically the grounds upon which additional taxes under Subpart F are asserted. Revenue Agents' reports delivered in connection with such notices assert that the income of International constituted Subpart F income because it was realized from the performance of services on behalf of the Delaware Company. These reports assert, in the alternative, that International was engaged in the business of manufacturing rather than in the construction business, with consequential effects on the calculation of Subpart F income. For the fiscal year ended March 31, 1983, the IRS has relied solely on the alternative ground. The Delaware Company is contesting the additional U.S. federal income taxes with respect to Subpart F income items proposed in the notices and believes it will succeed with respect thereto.

For the fiscal year ended March 31, 1983, the IRS has treated the reorganization in that fiscal year as a taxable event and has proposed deficiencies of approximately $300,000,000 in U.S. income taxes against the Delaware Company. This amount is duplicative to the extent of the $245,000,000 in income taxes asserted under Subpart F for years through March 31, 1983. The Delaware Company is contesting this proposed deficiency and believes it will succeed with respect thereto.

The notices to International essentially represent alternative grounds for asserting a deficiency with respect to a portion of the aforesaid Subpart F income. International believes it will succeed in contesting these deficiencies.

The notices also propose additional U.S. federal income taxes for the years in question on various other grounds, including additional taxes arising out of transactions done and contracts entered into by B&W before its acquisition by the Delaware Company and the consequential effects thereof on the Delaware Company for its fiscal years ending after the acquisition. The additional U.S. federal income taxes which the IRS has asserted on these grounds are substantial. The Delaware Company, however, believes that any U.S. federal income taxes ultimately assessed on the basis of such notices will not exceed reserves established with respect thereto.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matter was submitted during the fourth quarter of the fiscal year covered by this report to a vote of security holders, through the solicitation of proxies or otherwise.

PART II

Item 5. MARKET FOR THE REGISTRANT'S COMMON STOCK AND RELATED SECURITY HOLDER MATTERS

International's Common Stock is traded on the New York Stock Exchange. High and low stock prices and dividends declared for the years ended March 31, 1986 and 1987 follow:

	FISCAL 1986		
	SALES PRICE		CASH DIVIDENDS
QUARTER ENDED	HIGH	LOW	DECLARED
June 30, 1985	28 1/4	23 3/8	$0.45
September 30, 1985	26	16 5/8	$0.45
December 31, 1985	20 1/4	16 3/8	$0.45
March 31, 1986	19 1/8	13 5/8	$0.45

	FISCAL 1987		
	SALES PRICE		CASH DIVIDENDS
QUARTER ENDED	HIGH	LOW	DECLARED
June 30, 1986	21 3/4	15 3/8	$0.45
September 30, 1986	23 3/8	19 1/2	$0.45
December 31, 1986	23	19 3/4	$0.45
March 31, 1987	30 1/2	21 3/4	$0.45

As of March 31, 1987, the approximate number of record holders of Common Stock was 9,965.

Item 6. SELECTED FINANCIAL DATA

	For The Fiscal Years Ended March 31,				
	1987	1986	1985	1984	1983
	(In thousands except for per share amounts)				
Revenues	$ 3,289,322	$ 3,109,239	$ 3,022,512	$ 2,892,882	$ 3,443,882
Income From Continuing Operations	$ 87,445	$ 82,693	$ 48,336	$ 142,406	$ 50,958
Earnings (Loss) Per Common Share:					
Primary - From Continuing Operations	$ 2.36	$ 2.23	$ 1.31	$ 3.58	$ 1.38
Fully Diluted - From Continuing Operations	$ 2.31	$ 2.23	$ 1.31	$ 3.42	$ 1.38
Total Assets	$ 4,383,259	$ 4,350,942	$ 4,180,684	$ 3,981,114	$ 3,820,689
Long-Term Obligations	$ 781,124	$ 913,260	$ 732,248	$ 621,045	$ 525,086
Subsidiary's Redeemable Preferred Stocks	204,693	204,693	204,693	204,709	204,783
Total	$ 985,817	$ 1,117,953	$ 936,941	$ 825,754	$ 729,869
Cash Dividends per Common Share	$ 1.80	$ 1.80	$ 1.80	$ 1.80	$ 1.80

Revenues, income and earnings per share amounts have been restated for all prior periods reported to include only results from continuing operations (See Note 2 to the consolidated financial statements). See Note 3 regarding the change in method of depreciation, and Note 5 regarding the adoption of FASB Statement No. 87 and a plan settlement in accordance with FASB Statement No. 88 during fiscal year 1987, and changes in actuarial assumptions for domestic pension plans during fiscal year 1986.

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS

Results Of Operations

1987 VS 1986

Marine Construction Services' revenues decreased $45,401,000 to $862,785,000 and the operating loss increased $51,301,000 to $81,497,000. The decreased revenues resulted from lower utilization of marine construction equipment worldwide and fabrication facilities in the domestic operations, and the recognition in the prior fiscal year of the settlement of a $29,000,000 outstanding claim to McDermott International in this segment's foreign marine operations. These were offset in part by increased revenues from the marine operations due to the increased activities of greater lift-capacity vessels. The increase in the operating loss was partly due to the recognition of the settlement of the outstanding claim in foreign operations to McDermott International in the prior fiscal year, an increase in the provision for workers compensation insurance costs reflecting adverse actual and anticipated experience, significantly reduced operating margins in the foreign operations, and the accelerated depreciation of certain fabrication facilities and construction equipment due to diminished cost effectiveness and technical obsolescence. These increases in the operating loss were partially offset by improved margins in domestic operations. Marine Construction Services benefited from reduced depreciation charges of $15,593,000 resulting from a change in accounting method for the depreciation of major marine vessels, a reduction in the estimates of drydocking costs and the continuance of a cost reduction program. In addition, this segment benefited from a pension settlement gain of $24,710,000. While oil prices appear to be stabilizing, the demand for Marine Construction Services continues to be depressed, resulting in overcapacity in all of this segment's major activities.

Power Generation Systems and Equipment's revenues of $1,525,952,000 were $78,558,000 higher than last year. This was principally due to higher revenues from fossil systems exports, nuclear services activity, microprocessor-based control systems and heat exchangers. These higher revenues were partially offset by lower fossil services and replacement parts business, lower revenues from nuclear and other components for the U.S. Government, reduced volume from nuclear steam generators for foreign operations, lower fossil erection and lower repair and alterations activity. This segment reported operating income of $72,258,000 which was $35,487,000 higher than last year. The higher operating results were primarily due to a pension settlement gain of $81,834,000 and reduced pension expense of approximately $7,000,000 related to the adoption of FASB Statement No. 87 in fiscal 1987. In addition, fiscal 1987 income benefited from higher revenues and improved results from industrial boilers, increased nuclear services activity, improved margins on fossil repair and alterations, increased margins on fossil plant enhancement projects and lower workers compensation costs. These were offset by lower volume from nuclear and other components for the U.S. Government, lower fossil erection business, loss margins on the erection of prototype small power plants and a loss on the fabrication of a non-traditional project. Also, there were consolidation and restructuring charges for certain operations, net additional provisions and write-offs related to inactive and disposed plants and lines of business, and increased sales and marketing expenses covering several product lines.

Engineered Materials' revenues from continuing operations of $130,407,000 were $17,703,000 lower than last year due to lower shipments and prices on welded tubing, decreased volume from tubing used in nuclear propulsion plants for the U.S. Navy and lower shipments of insulating products. Operating income from continuing operations of $11,349,000 decreased $533,000 from last year due to the lower volume in all product lines.

The Trading segment had revenues of $849,496,000 and operating losses of $29,306,000 in fiscal 1987 compared with revenues of $655,145,000 and losses of $536,000 in fiscal 1986. Trading segment revenues increased $194,351,000 due to the new petrochemical business, which was only in operation from September 1985, as well as increased volume in the steel-trading business. The increased operating loss of $28,770,000 was due primarily to a $26,000,000 write-down of goodwill which in management's opinion had been permanently impaired, the favorable impact in the prior year of cost adjustments and settlement of outstanding claims on certain construction contracts. These were partially offset by higher margins in steel trading and a profit contribution from the petrochemical business.

Interest income for fiscal 1987 decreased $25,875,000 compared with fiscal 1986 and interest expense increased $1,376,000 during the same period. The decrease in interest income was consistent with changes in McDermott International's investment portfolio and interest rates prevailing thereon. The increase in interest expense was consistent with McDermott International's debt and the interest rates prevailing thereon in the respective periods except for cessation in the current fiscal year of interest capitalized on a construction loan and a decrease of $6,517,000 during fiscal 1987 in the provision for interest on estimated income taxes.

Equity in earnings of joint-venture companies in fiscal year 1987 decreased $8,105,000 over the prior fiscal year due primarily to losses in a Mexican joint-venture company.

Other-net income for fiscal 1987 was $224,361,000. Following the reclassification of provisions related to inactive and disposed plants of $4,374,000 to Discontinued Operations and $976,000 to Cost of Operations, other-net income was $81,002,000 for fiscal 1986. The increased income was primarily due to increased gains of $142,628,000 on the sale of government obligations and other asset disposals and reduced expense of $29,274,000 due to the settlement of certain antitrust litigation in fiscal 1986.

In fiscal 1987, the benefit from income taxes on income from continuing operations decreased $56,071,000 to a provision of $5,989,000. The decreased benefit arose primarily because International experienced lower pretax losses in jurisdictions where tax benefits exist.

Loss from Discontinued Operations, net of income taxes, increased $194,175,000 in fiscal 1987 compared with the prior year. This increase was principally due to a loss provision of $233,699,000, net of income taxes of $121,508,000, recorded in fiscal 1987.

1986 VS 1985

Marine Construction Services' revenues decreased $137,752,000 to $908,186,000 and operating loss increased $21,903,000 to $30,196,000. The decreased revenues resulted from lower utilization of marine construction equipment worldwide and fabrication facilities in the foreign operations offset to a significant extent by favorable settlements of outstanding claims in foreign operations and increased fabrication revenues from domestic operations. The increase in operating loss resulted from foreign operations and was primarily due to the decreased revenues and lower profit margins, offset primarily by approximately $29,000,000 relating to the settlement of an outstanding claim and the reversal of certain provisions no longer required. This decline was further offset by an increase in domestic operating income due primarily to improved profit margins, improved contract performance and favorable offshore working conditions. Marine Construction Services benefited from reduced operating costs due to implementation of a cost reduction program and reduced pension expense of approximately $12,200,000, resulting from a change in actuarial assumptions for domestic pension plans. A surplus of oil and natural gas and uncertainty regarding the future prices of these resources resulted in continued reduced demand for Marine Construction Services. Consequently, overcapacity continued in all major activities and asset utilization remained at low levels.

Power Generation Systems and Equipment's revenues of $1,447,394,000 were $33,913,000 higher than in fiscal year 1985. This was principally due to higher revenues from fossil plant enhancement and replacement parts, repair and alterations as well as higher revenues from microprocessor-based control systems and nuclear and other components for the U.S. Government. These higher revenues were partially offset by reduced activity on fossil steam and environmental control system fabrication and erection for electric utilities, lower revenues from nuclear fuel and services, heat exchangers and boiler-cleaning equipment. This segment reported operating income of $36,771,000 which was $15,974,000 higher than in fiscal 1985. The higher operating results were primarily due to a change in actuarial assumptions for domestic pension plans which reduced pension expense by approximately $27,500,000 (net of cost-sharing formulas on certain contracts with the U.S. Government). In addition, operating income in fiscal 1986 improved from the contribution to profits as a result of the increased revenues from the utility parts and plant enhancement business and from microprocessor-based controls. Also, there was lower spending on coal-water fuel development and improved operating results on heat exchangers despite their lower volume. These positive factors were partially offset by the lower volume with reduced operating margins on fossil steam and environmental control systems and erection, significant costs associated with prototype small power plants, and the lower revenues from boiler-cleaning equipment. Also, there were increased expenditures related to the development and marketing of cogeneration and refuse boilers, microprocessor-based control systems and construction services and an increase in insurance costs. In addition, in fiscal 1985 there were favorable contract adjustments to remaining nuclear steam systems as well as a favorable nuclear termination settlement.

Engineered Materials' revenues from continuing operations of $148,110,000 decreased $5,104,000 compared with the prior year due to lower shipments of welded mechanical and pressure tubing, partially offset by higher revenues from insulating products due to increased ceramic fiber sales. Operating income from continuing operations of $11,882,000 was $1,070,000 lower than the prior year, primarily due to lower operating margins from shipments of tubing used in nuclear propulsion plants for the U.S. Navy and lower profits in insulating products due to a strike in its Canadian operations and higher selling expense. These negative factors were partially offset by higher margins on welded tubular shipments.

The Trading segment had revenues of $655,145,000 and operating losses of $536,000 compared with revenues of $435,924,000 and losses of $4,137,000 in the prior year. The revenue and operating results of Coutinho for fiscal year 1986 included twelve months as opposed to only nine months in fiscal 1985, as Coutinho was not consolidated until the quarter ended September 30, 1984. After allowing for the above, Trading segment revenues increased over those in the prior year due primarily to the addition of the new petrochemical business in fiscal 1986 as well as an increase in steel and metal trading. These increased revenues were partially offset by reduced volume in the construction/ engineering business. The decrease in operating loss was due primarily to favorable cost adjustments and the settlement of outstanding claims on certain construction contracts, partially offset by lower margins in steel and metal trading and start-up costs associated with the new petrochemical trading operations.

Interest income reported for fiscal year 1986 decreased $18,964,000 from fiscal year 1985 and interest expense increased $20,602,000 over the same period. The primary reason for the decline in interest income was $10,160,000 of interest income that was received from a joint-venture company in fiscal 1985. The remainder of the decrease was consistent with changes in McDermott International's investment portfolio during fiscal 1986 and changes in the interest rates that prevailed during the two year period. The increase in interest expense in fiscal 1986 over fiscal 1985 was consistent with McDermott International's debt and the interest rates prevailing thereon in the respective periods, as well as being affected by an increase of $6,173,000 during fiscal 1986 in the provision for interest on estimated income taxes.

Other-net income for fiscal 1986 increased $84,358,000 over fiscal 1985. The primary reason for the increase was a $94,695,000 increase in the gain recognized from the sale of government obligations. In addition, the increase was affected by the payment in fiscal 1985 of $5,450,000 for fees relating to the termination of an agency agreement and a decrease in bad debt expense from fiscal 1985 to fiscal 1986 of $4,510,000. Expense for the settlement of certain antitrust civil litigation was $29,510,000 in fiscal 1986 compared with $31,299,000 in fiscal 1985. The increase was partially offset by a $21,078,000 decline in gains from the disposal of assets, a $8,715,000 decrease from fiscal 1985 to fiscal 1986 in the amount realized from receivables previously deemed restricted because of foreign exchange controls.

In fiscal 1986, the benefit from income taxes on income from continuing operations decreased $13,102,000 to $50,082,000. The decreased benefit arose primarily because of increased non-taxable earnings and reduced benefits in jurisdictions where losses were incurred.

Effect of Inflation and Changing Prices

McDermott International's financial statements are prepared in accordance with generally accepted accounting principles, using historical dollar accounting (historical cost). Statements based on historical cost, however, do not adequately reflect the cumulative effect of increasing costs and changes in the purchasing power of the dollar, especially during times of significant and continued inflation.

The management of McDermott International is cognizant of the effects of inflation and, in order to minimize the negative impact of inflation on its operations, attempts to cover the increased cost of anticipated changes in labor, material and service costs, either through an estimation of such changes, which is reflected in the original fixed price, or through price escalation clauses in its contracts.

Liquidity and Capital Resources

During the fiscal year ended March 31, 1987, McDermott International's working capital decreased by $374,367,000 from $1,258,000 at March 31, 1986. Changes in working capital included a net reclassification of $134,000,000 of long-term debt to notes payable and current maturities of long-term debt, a net increase of $140,750,000 in borrowings under short-term repurchase agreements and a net decrease of $96,685,000 attributable to the discontinued operations.

During fiscal 1987, the Delaware Company signed a credit agreement with various banks, dated June 20, 1986, establishing a $150,000,000 line of credit which is guaranteed by International. As of March 31, 1987, $130,000,000 was outstanding under this facility at an interest rate of 7.54%.

Also, during the same period, an amendment and guarantee agreement to the Delaware Company's credit agreement with various banks, dated June 15, 1981, was executed, whereby the credit facility is guaranteed by International. A term loan issued pursuant to this credit facility had an outstanding balance of $125,000,000 at March 31, 1987 at an interest rate of 7.18%.

In connection with the discontinuance of the seamless tubular line of business of the Engineered Materials segment (See Note 2), a provision for loss of $223,699,000, including $11,000,000 for anticipated losses during the phaseout period and net of deferred tax benefits of $121,508,000, has been made in the fourth quarter of fiscal 1987 to reduce the carrying amount of assets to their estimated net realizable values and provide for other costs and expenses related to the discontinued operations.

As a consequence of the discontinuance of the seamless tubular line of business of the Engineered Materials segment and the write-down of certain permanently impaired assets in the fourth quarter of fiscal 1987, compliance with certain of the Delaware Company's credit agreement covenants were waived by the Delaware Company's lenders. These waivers expire July 31, 1987, by which time the Delaware Company fully expects to have negotiated a long-term amendment to the credit agreements or have had the waivers extended. At March 31, 1987, the long-term debt portions of these credit agreements, $130,000,000 and $75,000,000, respectively, were classified as notes payable and current maturities of long-term debt.

Certain consolidated subsidiaries are restricted, principally as a result of credit agreement covenants, in their ability to transfer funds to International through intercompany loans, advances or cash dividends. At March 31, 1987, approximately $621,336,000 of the net assets of these subsidiaries were subject to such restrictions. It is not expected that these restrictions will have any significant practical effect on International's liquidity.

Certain debt agreements contain among other things, requirements as to maintenance of net worth and limitations on the incurrence of additional borrowings. Under the most restrictive of these agreements at March 31, 1987, additional borrowings were totally restricted. Subsequent to March 31, 1987, compliance with these requirements was waived by the Delaware Company's lenders as discussed above. Pursuant to the waiver, additional borrowings of McDermott International from April 1, 1987 through July 31, 1987, cannot exceed $200,000,000 and the Delaware Company must maintain a tangible net worth at least equal to $625,000,000 through July 31, 1987. Tangible net worth of the Delaware Company at March 31, 1987 was $680,000,000.

At March 31, 1987, International had entered into short-term repurchase agreements totaling $109,700,000, secured by $110,850,000 par value of its portfolio of government obligations, and the Delaware Company had entered into similar repurchase agreements for $92,484,000, secured by $91,750,000 par value of its portfolio of government obligations. International intends to continue utilizing short-term repurchase agreements in fiscal 1988.

International has available to it short-term lines of credit with various banks which were reduced from $85,000,000 to $10,000,000 during fiscal 1987. As of March 31, 1987, borrowings against these lines of credit were $2,300,000, an increase of $2,300,000 from March 31, 1986.

In addition, the Delaware Company has available to it from various banks short-term lines of credit which were increased by $4,000,000 to $64,000,000 during the period. At March 31, 1987, borrowings against these lines of credit totaled $7,500,000, an increase of $800,000 from March 31, 1986. Also, Coutinho has available short-term lines of credit from various banks totaling $60,000,000, an increase of $1,600,000 from March 31, 1986. Borrowings against these facilities at March 31, 1987 totaled $29,000,000, an increase of $10,000,000 from March 31, 1986.

During fiscal year 1987, the Delaware Company issued DM 100,000,000 6-1/2% bearer-bonds dated July 1, 1986 and due July 1, 1991. The net proceeds from the bond issue, which is guaranteed by International, were used to repay a portion of the outstanding balance of an existing short-term credit facility established by International in connection with the acquisition of Coutinho.

During fiscal year 1987, McDermott International Trading Company, GmbH negotiated a DM 40,000,000 Term Loan and a DM 25,000,000 Revolving Credit Facility with three foreign banks. The proceeds from the loans, which are guaranteed by International, were used to repay the remaining balance of a short-term credit facility established in connection with the acquisition of Coutinho. At March 31, 1987, DM 40,000,000 and DM 25,000,000 were outstanding against the Term Loan and the Revolving Credit Facility, respectively.

Pursuant to agreements between the Delaware Company and certain U.S. banks, a $50,000,000 floating-rate loan facility and a $35,000,000 floating-rate note were repaid by the Delaware Company during fiscal 1987.

In the third quarter of fiscal 1987, two partnerships formed by subsidiaries of the Delaware Company entered into two Loan Agreements with a governmental authority in connection with the financing, through the issuance of energy development revenue bonds, of the construction of two small power plants in Pennsylvania. The proceeds of the bonds plus accrued and unpaid interest are held under separate indentures by a trustee and offset the $123,250,000 principal plus accrued and unpaid interest outstanding under the Loan Agreements. Upon release of any of the proceeds by the trustee to either of the partnerships, after satisfaction of certain requirements, remaining funds held under the indentures and the outstanding balance of the Loan Agreements become separately reportable as assets and liabilities in McDermott International's Consolidated Balance Sheet.

During fiscal year 1987, McDermott International expended $133,315,000 for additions to property, plant and equipment, $66,586,000 for cash dividends on International's Common Stock, and approximately $73,000,000 for scheduled maturities of long-term debt. During the same period, working capital provided from continuing operations was $21,115,000. McDermott International has committed to make capital expenditures of approximately $22,047,000 during fiscal 1988. These proposed expenditures are principally to maintain McDermott International's existing facilities.

McDermott International expects to obtain funds for its capital expenditures and working capital requirements from its operations and from additional borrowings including short-term repurchase agreements.

McDermott International maintains an investment portfolio of primarily government obligations which is held for long-term investment purposes. During the year, McDermott International increased this portfolio $166,841,000 to an amortized cost at March 31, 1987 of $1,265,633,000 (market value of $1,221,586,000). These securities are carried at amortized cost, as in management's opinion there is no permanent loss in value of the portfolio, and there is no present intention to liquidate the securities at less than cost.

At March 31, 1987, the ratio of long-term debt to total common stock and other stockholder's equity was .75 as compared with .76 at March 31, 1986 and .61 at March 31, 1985. If long-term debt at March 31, 1987 had included the $205,000,000, which was reclassified to notes payable and current maturities of long-term debt, the ratio of long-term debt to total common stock and other stockholder's equity would have been .95.

The Tax Reform Act of 1986, enacted October 22, 1986, represents a major restructuring of U.S. income tax law. With respect to McDermott International, significant provisions of this Act include a reduction of income tax rates, the repeal of the investment tax credit, a change in allowable rates of depreciation of business assets, a revision in the method of accounting for long-term contracts and inventories and an alternative minimum tax. Except for the reduction in income tax rates, these provisions will either increase corporate income taxes or accelerate their payment. On September 2, 1986, the Financial Accounting Standards Board issued an Exposure Draft which proposes a new approach in accounting for income taxes in financial statements prepared in accordance with generally accepted accounting principles. Presently, accounting principles require that deferred taxes be provided based on the tax rates applicable during the current year without adjustment for subsequent changes in future tax rates. In contrast, the Exposure Draft uses a liability approach under which deferred taxes would be provided based on enacted tax rates applicable to the period(s) in which the taxes become payable. Because of the complexities of the Exposure Draft and the uncertainties regarding its final requirements, McDermott International cannot reliably predict the effects of the proposed statement.

Item 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Company Report on Consolidated Financial Statements

McDermott International has prepared the consolidated financial statements and related financial information included in this report. McDermott International has the primary responsibility for the financial statements and other financial information and for ascertaining that the data fairly reflect the financial position and results of operations of McDermott International. The financial statements were prepared in accordance with generally accepted accounting principles appropriate in the circumstances, and necessarily reflect estimates and judgments by appropriate officers of McDermott International with appropriate consideration given to materiality.

McDermott International believes that it maintains a system of internal accounting controls designed to provide reasonable assurance that assets are safeguarded against loss or unauthorized use and that the financial records are adequate and can be relied upon to produce financial statements in accordance with generally accepted accounting principles. The concept of reasonable assurance is based on the recognition that the cost of a system of internal control must not exceed the related benefits. Although accounting control procedures are designed to achieve these objectives, it must be recognized that errors or irregularities may nevertheless occur. McDermott International seeks to assure the objectivity and integrity of its accounts by its selection of qualified personnel, by organizational arrangements that provide an appropriate division of responsibility and by the establishment and communication of sound business policies and procedures throughout the organization. McDermott International believes that its accounting controls provide reasonable assurance that errors or irregularities that could be material to the financial statements are prevented or would be detected.

McDermott International's accompanying consolidated financial statements have been examined by its certified public accountants, who provide McDermott International with expert advice on the application of U.S. generally accepted accounting principles to McDermott International's business and also provide an objective assessment of the degree to which McDermott International meets its responsibility for the fairness of financial reporting. They regularly evaluate the system of internal accounting controls and perform such tests and other procedures as they deem necessary to reach and express an opinion on the fairness of the financial statements. The report of the certified public accountants appears elsewhere herein.

The Board of Directors pursues its responsibility for McDermott International's consolidated financial statements through its Audit Committee which is composed solely of directors who are not officers or employees of McDermott International. The Audit Committee meets periodically with the certified public accountants, management and the internal auditors to review matters relating to the quality of financial reporting and internal accounting control and the nature, extent and results of the audit effort. In addition, the Audit Committee is responsible for recommending to the Board of Directors the engagement of certified public accountants for McDermott International, who in turn submit the engagement to the stockholders for their approval. The certified public accountants, as well as the internal auditors, have free access to the Audit Committee.

June 16, 1987

Report of Certified Public Accountants

The Board of Directors and Stockholders
McDermott International, Inc.

We have examined the accompanying consolidated balance sheet of McDermott International, Inc. at March 31, 1987 and 1986, and the related consolidated statements of income (loss) and retained earnings and changes in financial position for each of the three years in the period ended March 31, 1987. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements mentioned above present fairly the consolidated financial position of McDermott International, Inc. at March 31, 1987 and 1986, and the consolidated results of operations and changes in financial position for each of the three years in the period ended March 31, 1987, in conformity with generally accepted accounting principles applied on a consistent basis during the period, except for the changes, with which we concur, in the method of computing depreciation as described in Note 3 and in the method of accounting for pension cost as described in Note 5 to the consolidated financial statements.

ARTHUR YOUNG & COMPANY

New Orleans, Louisiana
June 16, 1987

McDERMOTT INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEET
MARCH 31, 1987 AND 1986

ASSETS

	1987	1986
	(In thousands)	
Current Assets:		
Cash	$ 26,580	$ 21,272
Short-term investments, principally time deposits at cost which approximates market	70,190	85,127
Accounts and notes receivable	797,245	817,064
Income taxes refundable	—	8,753
Contracts in progress	288,021	296,811
Inventories	191,663	236,692
Prepaid expenses and other assets	84,618	33,883
Total Current Assets	1,458,317	1,499,602
Property, Plant and Equipment, at Cost:		
Land	21,565	30,101
Buildings	232,537	258,933
Machinery and equipment	1,912,130	2,036,901
Property under construction	72,533	90,358
	2,238,765	2,416,293
Less accumulated depreciation and amortization	1,112,263	1,110,361
Net Property, Plant and Equipment	1,126,502	1,305,932
Investments in Government Obligations, at Amortized Cost	1,265,633	1,098,792
Excess of Cost Over Fair Value of Net Assets of Purchased Businesses Less Accumulated Amortization of $61,006,000 at March 31, 1987 and $80,604,000 at March 31, 1986	221,776	345,257
Other Assets	311,031	101,359
TOTAL	$ 4,383,259	$ 4,350,942

See accompanying notes to consolidated financial statements.

LIABILITIES AND STOCKHOLDERS' EQUITY

	1987	1986
	(In thousands)	
Current Liabilities:		
Notes payable and current maturities of long-term debt	$ 536,385	$ 263,549
Accounts payable	254,607	282,806
Accrued employee benefits	112,472	118,266
Accrued interest payable	141,366	123,204
Accrued liabilities - other	396,028	307,554
Advance billings on contracts	162,788	176,305
Provision for warranty expense	72,047	69,513
U. S. and foreign income taxes	139,064	140,509
Dividends payable	16,669	16,638
Total Current Liabilities	1,831,426	1,498,344
Deferred and Non-Current Income Taxes	320,631	391,916
Long-Term Debt	781,124	913,260
Other Liabilities	205,499	133,949
Contingencies		
Minority Interest:		
Subsidiary's Redeemable Preferred Stocks:		
Series A $2.20 cumulative convertible, $1.00 par value; at redemption value	88,300	88,300
Series B $2.60 cumulative, $1.00 par value; at redemption value	116,393	116,393
Other minority interest	4,611	4,407
Total Minority Interest	209,304	209,100
Preferred Stock	—	—
Common Stock and Other Stockholders' Equity:		
Common stock, par value $1.00 per share, authorized 150,000,000 shares; outstanding 37,053,417 at March 31, 1987 and 36,973,724 at March 31, 1986	37,053	36,974
Capital in excess of par value	316,164	313,990
Retained earnings	716,429	885,436
Cumulative foreign exchange translation adjustments	(34,371)	(32,027)
Total Common Stock and Other Stockholders' Equity	1,035,275	1,204,373
TOTAL	$ 4,383,259	$ 4,350,942

McDERMOTT INTERNATIONAL, INC.
CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS
FOR THE THREE FISCAL YEARS ENDED MARCH 31, 1987

	1987	1986	1985
		(In thousands)	
Revenues	$ 3,289,322	$ 3,109,239	$ 3,022,512
Costs and Expenses:			
Cost of operations	2,922,643	2,714,421	2,649,971
Depreciation and amortization	168,520	138,358	129,899
Selling, general and administrative expenses	290,365	302,553	293,174
	3,381,528	3,155,332	3,073,044
Operating Income (Loss)	(92,206)	(46,093)	(50,532)
Other Income (Expense):			
Interest income	100,822	126,697	145,661
Interest expense	(117,747)	(116,371)	(95,769)
Equity in earnings of joint-venture companies	(5,979)	2,126	4,488
Minority interest	(15,817)	(14,750)	(15,340)
Other - net	224,361	81,002	(3,356)
	185,640	78,704	35,684
Income (Loss) From Continuing Operations Before Provision for Income Taxes, Extraordinary Items and Cumulative Effect of Accounting Change	93,434	32,611	(14,848)
Provision for (Benefit from) Income Taxes	5,989	(50,082)	(63,184)
Income From Continuing Operations Before Extraordinary Items and Cumulative Effect of Accounting Change	87,445	82,693	48,336
Loss from Discontinued Operations	(220,568)	(26,393)	(29,356)
Income (Loss) Before Extraordinary Items and Cumulative Effect of Accounting Change	(133,123)	56,300	18,980
Extraordinary Items	4,991	2,789	11,687
Cumulative Effect of Accounting Change	25,711	—	—
Net Income (Loss)	(102,421)	59,089	30,667
Retained Earnings — Beginning of Year	885,436	892,880	928,686
Deduct Cash Dividends — Common (per share, $1.80 in 1987, 1986 and 1985)	66,586	66,533	66,473
Retained Earnings — End of Year	$ 716,429	$ 885,436	$ 892,880
Earnings (Loss) Per Common and Common Equivalent Share:			
Continuing operations	$ 2.36	$ 2.23	$ 1.31
Discontinued operations	(5.96)	(0.71)	(0.79)
Extraordinary items	0.13	0.08	0.31
Accounting change	0.70	—	—
Net earnings (loss)	$ (2.77)	$ 1.60	$ 0.83
Cash Dividends Per Common Share	$ 1.80	$ 1.80	$ 1.80
Pro Forma Amounts Assuming the Effect of Accounting Change is Applied Retroactively:			
Income From Continuing Operations	$ 87,445	$ 91,684	$ 53,012
Earnings Per Share	$ 2.36	$ 2.48	$ 1.43
Net Income (Loss)	$ (128,132)	$ 68,080	$ 35,343
Earnings (Loss) Per Share	$ (3.46)	$ 1.84	$ 0.95

Earnings per share on a fully diluted basis for Income From Continuing Operations would be $2.31 and $2.23 in fiscal 1987 and 1986, respectively, and $2.31 and $2.46 per share pro forma in fiscal 1987 and 1986, respectively, assuming that the effect of the accounting change had been applied retroactively.

See accompanying notes to consolidated financial statements.

McDERMOTT INTERNATIONAL, INC.
CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE THREE FISCAL YEARS ENDED MARCH 31, 1987

	1987	1986	1985
		(In thousands)	
SOURCE OF FUNDS:			
Income from continuing operations	$ 87,445	$ 82,693	$ 48,336
Charges (credits) not affecting working capital:			
Depreciation and amortization	168,520	138,358	129,899
Write-down of non-current assets	44,755	—	—
Deferred income taxes	14,797	13,635	61,798
Gain on sales of government obligations	(237,340)	(94,712)	(17)
Gain on pension settlement	(121,339)	—	—
Other - net	64,277	(3,350)	(35,375)
Working capital provided from continuing operations	21,115	136,624	204,641
Loss from discontinued operations	(220,568)	(26,393)	(29,356)
Charges (credits) not affecting working capital:			
Depreciation and amortization and write-down of non-current assets	275,477	19,440	19,047
Gain on pension settlement and other	(67,592)	—	—
Deferred income taxes	(84,002)	(20,353)	9,025
Working capital used in discontinued operations	(96,685)	(27,306)	(1,284)
Total working capital provided from (used in) operations	(75,570)	109,318	203,357
Proceeds from sale and exchange of property, plant and equipment	11,075	11,965	39,428
Long-term borrowing (including fluctuations under the revolving credit agreement)	383,380	386,068	431,183
Sale of government obligations - net	70,499	—	—
Reduction in non-current assets and liabilities resulting from exchange rate changes	—	—	20,131
Foreign currency translation adjustments	—	8,103	—
Cumulative effect of accounting change	—	—	—
Other - net	—	6,390	20,359
	389,384	521,844	714,458
APPLICATION OF FUNDS:			
Purchase of government obligations - net	—	26,874	80,727
Additions to property, plant and equipment	133,315	298,884	172,349
Reduction and reclassification of long-term debt (including fluctuations under the revolving credit agreement)	402,639	205,879	343,585
Construction funds held by trustee	123,250	—	—
Reduction of non-current income taxes	10,183	15,618	23,327
Cash dividends	66,586	66,533	66,473
Increase in non-current assets and liabilities resulting from exchange rate changes	7,703	24,764	—
Acquisition of Coutinho:			
Non-current assets and liabilities - net	—	—	62,915
Foreign currency translation adjustments	2,344	—	14,409
Other - net	17,731	—	—
	763,751	638,552	763,785
NET DECREASE IN WORKING CAPITAL	$ (374,367)	$ (116,708)	$ (49,327)

McDERMOTT INTERNATIONAL, INC.
CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION (Continued)
FOR THE THREE FISCAL YEARS ENDED MARCH 31, 1987

CHANGES IN COMPONENTS OF WORKING CAPITAL:			
Increase (decrease) in current assets:			
Cash and short-term investments	$ (9,629)	$ (5,694)	$ (58,707)
Accounts, notes and income tax refund receivable	(28,572)	(121,199)	48,050
Contracts in progress	(8,790)	28,119	28,658
Inventories	(45,029)	(16,611)	19,143
Prepaid expenses and other assets	50,735	11,849	4,628
	(41,285)	(103,536)	41,772
Increase (decrease) in current liabilities:			
Notes and accounts payable and accrued liabilities	345,510	85,513	225,975
Advance billings on contracts	(13,517)	(13,309)	(35,308)
Provision for warranty expense	2,534	(8,514)	(22,892)
U.S. and foreign income taxes	(1,445)	(50,518)	(76,676)
	333,082	13,172	91,099
NET DECREASE IN WORKING CAPITAL	$ (374,367)	$ (116,708)	$ (49,327)

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements are presented in U.S. Dollars in accordance with accounting principles generally accepted in the United States and include the accounts of McDermott International, Inc. and all significant subsidiaries. In order to provide for a timely consolidation, the financial position and results of operations of Coutinho, Caro and Co. KGaA ("Coutinho") are included in McDermott International's consolidated financial statements as of Coutinho's December 31 closing date. Investments in joint-venture companies (20% to 50% owned) are accounted for on the equity method. All significant intercompany transactions and accounts have been eliminated.

Unless the context otherwise requires, hereinafter "International" will be used to mean McDermott International, Inc., a Panama corporation, the "Delaware Company" will be used to mean McDermott Incorporated, a Delaware corporation, which is a subsidiary of International, and "McDermott International" will be used to mean the consolidated enterprise.

The notes to consolidated financial statements are presented on the basis of continuing operations, unless otherwise stated, and in addition, certain amounts previously reported have been reclassified to conform with the presentation at March 31, 1987.

Contracts and Revenue Recognition

Contract revenues and related costs for Marine Construction Services, Power Generation Systems and Equipment, and the construction and engineering services of the Trading segment of McDermott International are principally recognized on a percentage of completion method for individual contracts or components thereof based upon work performed or the ratio of costs incurred to total estimated costs, as applicable to the product or activity involved. Revenues and related costs so recorded, plus accumulated contract cost that exceeds amounts invoiced to customers under the terms of the contract are included in contracts in progress. Billings that exceed accumulated contract costs and revenues and costs recognized under percentage of completion are included in advance billings. Most long-term contracts have provisions for progress payments. Contract price and cost estimates are reviewed periodically as the work progresses and adjustments proportionate to the percentage of completion are reflected in income in the period when such estimates are revised. There are no unbilled revenues which will not be billed. Provisions are made currently for all known or anticipated losses. Claims for extra work or changes in scope of work are included in contract revenues when collection is probable. International and certain of its subsidiaries keep books and file tax returns on the completed contract method of accounting.

	1987	1986
	(In thousands)	
Included in Contracts in Progress are:		
Costs incurred less cost of revenue recognized	$ 162,717	$ 188,907
Revenues recognized less billings to customers	125,304	107,904
Contracts in Progress	$ 288,021	$ 296,811
Included in Advance Billings on Contracts are:		
Billings to customers less revenues recognized	$ 162,844	$ 221,776
Cost of revenues recognized less costs incurred	(56)	(45,471)
Advance Billings on Contracts	$ 162,788	$ 176,305

McDermott International is usually entitled to financial settlements relative to the individual circumstances of deferrals or cancellations of Power Generation Systems and Equipment contracts. McDermott International does not recognize such settlements or claims for additional compensation until final settlement is reached.

Included in accounts and notes receivable are amounts representing retainages on contracts as follows:

	1987	1986
	(In thousands)	
Retainages	$ 175,443	$ 179,346
Retainages expected to be collected after one year	$ 79,091	$ 74,131

Revenues for Trading are recognized as individual trades are completed. For trades-in-progress, provisional billings to customers net of costs incurred are carried in the current liabilities section of the balance sheet as advance billings on contracts.

Depreciation, Maintenance and Repairs and Drydocking Expenses

Except for major marine vessels, McDermott International's property, plant and equipment is depreciated on the straight-line method, using estimated economic useful lives of 8 to 40 years for buildings and 2 to 28 years for machinery and equipment. Effective April 1, 1986, McDermott International changed the method of depreciation for major marine vessels (See Note 3) from the straight-line method to a units-of-production method based on the utilization of each vessel.

Maintenance, repairs and renewals which do not materially prolong the useful life of an asset are expensed as incurred except for drydocking costs for the marine fleet, which are estimated and accrued over the period of time between drydockings, and such accruals are charged to operations currently. In fiscal 1987, the estimated costs to drydock certain marine vessels were adjusted to reflect actual and anticipated experience.

Investments in Government Obligations

At March 31, 1987, McDermott International held $1,265,633,000 (amortized cost) of primarily government securities as a long-term investment, compared with $1,098,792,000 (amortized cost) at March 31, 1986. These securities are carried at amortized cost, as in management's opinion, there is no permanent loss in value of the portfolio, and there is no present intention to liquidate the securities at less than cost. The market value of these securities was $1,221,586,000 and $1,334,343,000 at March 31, 1987 and March 31, 1986, respectively. The face amount at March 31, 1987 was $1,256,701,000.

Amortization of Excess of Cost Over Fair Value of Net Assets of Purchased Businesses

The excess of the cost of McDermott International's investments in The Babcock & Wilcox Company ("B&W") and Coutinho over the fair value of net assets acquired is being amortized on a straight-line basis over forty years and twenty years, respectively. During the fourth quarter of fiscal 1987, $124,885,000 of Excess Cost Over Fair Value of Net Assets Purchased was written off primarily in connection with discontinued operations. Excess cost arising from business combinations prior to 1971, which amounts to $6,264,000, is not being amortized because, in the opinion of management, there has been no diminution in value.

Warranty Expense

McDermott International provides for estimated future warranty expense which may be required to satisfy contractual requirements, primarily of the Power Generation Systems and Equipment segment. Such provisions are accrued relative to revenue recognition on the respective contracts. In addition, specific provisions are made where the costs of warranty are expected to significantly exceed such accruals.

Research and Development

The cost of research and development which is not performed on specific contracts is charged to operations as incurred. Such expense was approximately $35,500,000, $32,600,000 and $38,200,000 in fiscal years 1987, 1986 and 1985, respectively. In addition, expenditures on research and development activities of approximately $42,100,000, $53,400,000 and $41,600,000 in fiscal years 1987, 1986 and 1985, respectively, were paid for by customers of McDermott International.

Capitalization of Interest Cost

In fiscal 1987, 1986 and 1985, total interest cost incurred including discontinued operations was $126,612,000, $130,258,000 and $100,036,000, respectively, of which $8,865,000, $13,887,000 and $4,267,000 was capitalized.

Foreign Currency Translation

McDermott International translates the financial statements of its foreign operations in accordance with FASB Statement No. 52, "Foreign Currency Translation." Under that Statement, all balance sheet accounts other than stockholders' equity are translated into U.S. Dollars at current exchange rates, and income statement items are translated at average exchange rates for the year; resulting translation adjustments are recorded in a separate component of stockholders' equity. An analysis of changes in the account which contains this cumulative translation component follows:

	(In thousands)
Balance March 31, 1984	$ (25,721)
Translation adjustments for fiscal 1985	(14,409)
Balance March 31, 1985	(40,130)
Translation adjustments for fiscal 1986	8,103
Balance March 31, 1986	(32,027)
Translation adjustments for fiscal 1987	(2,344)
Balance March 31, 1987	$ (34,371)

Foreign currency transaction adjustments are reported in income. Included in Other Income (Expense) are transaction gains (losses) of $653,000, $(9,028,000) and $(5,645,000) for fiscal years 1987, 1986 and 1985, respectively.

Earnings Per Share

Primary earnings per share are based on the weighted average number of common and common equivalent shares outstanding during the year. Fully diluted earnings per share include the dilutive effect of convertible preferred stock and warrants.

NOTE 2 - DISCONTINUED OPERATIONS

In June 1987, McDermott International announced its intention to permanently close its manufacturing and steelmaking facilities in Beaver Falls, Ambridge and Koppel, Pennsylvania and in Bryan, Texas, which comprise the seamless tubular line of business of the Engineered Materials segment. Management believes that continued worldwide overcapacity and depressed market conditions in the product lines of the seamless tubular line of business have permanently impaired the prospects for this line of business. Accordingly, the seamless tubular line of business has been accounted for as a discontinued operation in the consolidated financial statements, and the Consolidated Statements of Income (Loss) and Retained Earnings and Changes in Financial Position have been restated for all prior periods presented.

A provision for loss of $223,699,000, including $11,000,000 for anticipated losses during the phaseout period and net of deferred tax benefits of $121,508,000, has been made in the fourth quarter of fiscal 1987 to reduce the carrying amount of assets to their estimated net realizable values and provide for other costs and expenses related to the discontinuance of operations.

Loss from operations for fiscal year 1987 was $35,790,000, net of benefits from income taxes of $26,620,000, offset by a pension settlement gain of $38,921,000, net of income taxes of $31,134,000. In fiscal years 1986 and 1985, loss from operations was $26,393,000 and $29,356,000, net of benefits from income taxes of $21,152,000 and $26,429,000, respectively. Revenues applicable to discontinued operations were $70,320,000, $147,860,000 and $211,360,000 in fiscal 1987, 1986 and 1985, respectively.

Assets of discontinued operations included in McDermott International's Consolidated Balance Sheet at March 31, 1987 include current assets of $17,421,000, consisting primarily of inventories, and non-current assets of $6,840,000, consisting of property, plant and equipment, which have been reduced to their estimated net realizable values.

Management anticipates that the permanent closure of the seamless tubular line of business will be completed during fiscal 1988.

NOTE 3 - CHANGE IN DEPRECIATION METHOD

Effective April 1, 1986, McDermott International changed the method of depreciation for major marine vessels from the straight-line method to a units-of production method based on the utilization of each vessel. Depreciation expense calculated under the units-of-production method may be less than, equal to, or greater than depreciation expense calculated under the straight-line method in any period. McDermott International employs utilization factors as a key element in the management of marine construction operations and believes the units-of-production method, which recognizes both time and utilization factors, accomplishes a better matching of costs and revenues than the straight-line method. The cumulative effect of the change on prior years at March 31, 1986 of $25,711,000, net of income taxes of $17,362,000 ($0.70 per share), is included in the accompanying Consolidated Statement of Income (Loss) and Retained Earnings for the fiscal year ended March 31, 1987. The effect of the change on the fiscal year ended March 31, 1987 was to increase Income From Continuing Operations Before Extraordinary Items and Cumulative Effect of Accounting Change and decrease Net Loss $6,556,000 ($0.18 per share). Pro forma amounts showing the effect of applying the units-of-production method of depreciation retroactively, net of related income taxes, are presented in the Consolidated Statement of Income (Loss) and Retained Earnings.

NOTE 4 - INVENTORIES

Inventories are carried at the lower of cost or market. Cost is determined on an average cost basis except for certain materials inventories, for which the last-in first-out (LIFO) method is used. The cost of approximately 15% and 35% of total inventories was determined using the LIFO method at March 31, 1987 and March 31, 1986, respectively. Consolidated inventories at March 31, 1987 and 1986 are summarized below:

	1987	1986
	(In thousands)	
Raw Materials and Supplies	$ 58,220	$ 64,686
Work in Progress	45,911	97,414
Finished Goods	87,532	74,592
	$ 191,663	$ 236,692

NOTE 5 - PENSION PLANS AND POSTRETIREMENT BENEFITS

Pension Plans - McDermott International provides retirement benefits, primarily through non-contributory pension plans, for substantially all of its regular full-time employees, except certain non-resident alien employees of foreign subsidiaries who are not citizens of a European Common Market country or who do not earn income in the United States, Canada, or the United Kingdom.

Salaried plan benefits are based on final average compensation and years of service, while hourly plan benefits are based on a flat benefit rate and years of service. McDermott International's funding policy is to fund applicable pension plans to meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974 (ERISA) and, generally, to fund other pension plans as recommended by the respective plan actuary and in accordance with applicable law.

Effective April 1, 1986, McDermott International adopted FASB Statement No. 87, "Employers' Accounting for Pensions," for its domestic pension plans and certain of its foreign pension plans. The Statement requires a standardized method for measuring net periodic pension cost (pension expense), immediate recognition of a pension liability under certain conditions, and expanded pension plan disclosures. The effect of the above change, including discontinued operations, was to reduce net periodic pension cost by $27,128,000 and increase income from continuing operations by $9,199,000 ($0.25 per share primary and $0.23 per share fully diluted) and decrease net loss by $15,859,000 ($0.43 per share primary and fully diluted) for the fiscal year ended March 31, 1987.

Net periodic pension cost for fiscal year 1987 included the following components:

	(In thousands)
Service cost - benefits earned during the period	$ 24,056
Interest cost on projected benefit obligation	61,586
Actual return on plan assets	(192,858)
Net amortization and deferral	98,123
Net periodic pension cost	$ (9,093)

At January 1, 1987, the weighted-average discount rate for active employees and for retired employees, and the rate of increase in future compensation levels used in determining the actuarial present value of the projected benefit obligations were 8-1/2% and 4-1/2%, respectively. The expected long-term rate of return on assets was 8-1/2%.

Total pension expense of $4,031,000 and $54,981,000 in fiscal 1986 and 1985, respectively, was accounted for on the basis of APB 8, "Accounting for the Cost of Pension Plans," and is therefore not comparable to the net periodic pension cost reported above for fiscal year 1987.

On February 6, 1987, McDermott International accepted a life insurance company's bid to issue a non-participating single premium annuity contract covering substantially all pre-January 1, 1987 retirees under McDermott International's ERISA pension plans. This agreement constitutes a settlement in accordance with FASB Statement No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits." Consequently, McDermott International recognized a pre-tax gain in fiscal 1987 of $191,394,000 including $70,055,000 related to discontinued operations.

As a consequence of the discontinuance of the seamless tubular line of business of the Engineered Materials segment (See Note 2), the curtailment and intended termination of a related pension plan has been accounted for as a settlement. Consequently, the loss on disposal measured in accordance with APB 30, "Reporting the Results of Operations", includes a net after-tax loss on curtailment and termination of $598,000.

The following table sets forth the plans' funded status and amounts recognized in McDermott International's consolidated financial statements at March 31, 1987 for its domestic pension plans and certain of its foreign pension plans after recognition of the above referenced settlement gains and the effects of the discontinued operations:

	Plans For Which	
	Assets Exceed Accumulated Benefits	**Accumulated Benefits Exceed Assets**
	(In thousands)	
Actuarial present value of benefit obligations:		
Vested benefit obligation	$ 258,408	$ 42,218
Accumulated benefit obligation	$ 309,283	$ 48,687
Projected benefit obligation	$ 410,987	$ 51,500
Plan assets at fair value	731,613	26,761
Projected benefit obligation (in excess of) or less than plan assets	320,626	(24,739)
Unrecognized net (gain) or loss	(67,739)	(2,936)
Prior service cost not yet recognized in net periodic pension cost	491	267
Unrecognized net obligation at April 1, 1986	(147,404)	(576)
Prepaid pension cost (pension liability) recognized in the consolidated financial statements	$ 105,974	$ (27,984)

Based upon a comprehensive study of actuarial assumptions, effective January 1, 1985 (the beginning of each ERISA plan's fiscal year), the actuarial investment rate of return assumptions and the actuarial salary increase assumptions were changed to reflect more closely the past and expected experience of such ERISA plans. The effect of the above changes on both continuing and discontinued operations was to reduce fiscal 1986 pension expense by approximately $56,300,000, which includes $15,895,000 accrued in fiscal year 1985, and to increase income from continuing operations by approximately $24,600,000 or $0.66 per share primary and $0.62 per share fully diluted and net income by approximately $29,300,000 or $0.79 per share primary and fully diluted.

In December 1985, the two principal ERISA pension plans were amended to provide that, subject to certain limitations, any excess assets in such plans would be used to increase pension benefits if certain events occurred within a 60 month period following a change in control of International.

Multiemployer Plans - One of McDermott International's subsidiaries contributes to various multiemployer plans. The plans generally provide defined benefits to substantially all unionized workers in this subsidiary. Amounts charged to pension cost and contributed to the plans were $7,499,000, $7,984,000 and $6,485,000 in fiscal years 1987, 1986 and 1985, respectively.

Postretirement Health Care and Life Insurance Benefits - McDermott International offers postretirement health care and life insurance benefits to substantially all of its retired regular full-time employees, including those associated with discontinued operations, except certain non-resident alien retired employees who are not citizens of a European Common Market country or who, while employed, did not earn income in the United States, Canada or the United Kingdom. McDermott International shares the cost of providing these benefits with all affected retirees. McDermott International's cost of providing such benefits is recognized by expensing the insurance programs' premiums and the self-insured program's claims as paid. The aggregate amount so expensed, including discontinued operations, totaled $11,752,000, $10,755,000 and $8,503,000 in fiscal years 1987, 1986 and 1985, respectively. McDermott International has made no provision for recognizing the cost of postretirement benefits which may eventually be paid to employees who have not yet retired.

NOTE 6 - INCOME TAXES

Income taxes have been provided based upon the tax laws and rates in the countries in which operations are conducted. All income has been earned outside of Panama and McDermott International is not subject to income tax in Panama on income earned outside of Panama. Therefore, there is no expected relationship between the provision for, or benefit from, income taxes and income, or loss, before income taxes. The major reason for the variations in such relationships is that income is earned within and subject to the taxation laws of various countries, each of which has a regime of taxation which varies from that of any other country (not only with respect to nominal rate but also with respect to the allowability of deductions, credits and other benefits) and because the proportional extent to which income is earned in, and subject to tax by, any particular country or countries varies from year to year.

The provision for (benefit from) income taxes consists of:

	1987		1986		1985	
	Current	Deferred	Current	Deferred	Current	Deferred
			(In thousands)			
U.S. - Federal	$ (12,089)	$ (87,078)	$ (49,610)	$ (31,232)	$ (100,365)	$ 9,133
U.S. - State & Local	1,300	(5,015)	(4,510)	4,042	2,239	(3,926)
Other than U.S.	10,013	(5,765)	3,478	4,198	24,515	(14,448)
	$ (776)	$ (97,858)	$ (50,642)	$ (22,992)	$ (73,611)	$ (9,241)

The provision for (benefit from) income taxes is included in the financial statements as follows:

	1987	1986	1985
		(In thousands)	
Continuing operations	$ 5,989	$ (50,082)	$ (63,184)
Discontinued operations	(116,994)	(21,152)	(26,429)
Extraordinary items	(4,991)	(2,400)	6,761
Cumulative effect of accounting change	17,362	—	—
	$ (98,634)	$ (73,634)	$ (82,852)

The provision for (benefit from) income taxes is based upon income (loss) before income taxes which are included in the financial statements as follows:

	1987	1986	1985
		(In thousands)	
Continuing operations	$ 93,434	$ (32,611)	$ (14,848)
Discontinued operations	(337,562)	(47,545)	(55,785)
Extraordinary items	—	389	18,448
Cumulative effect of accounting change	43,073	—	—
	$ (201,055)	$ (14,545)	$ (52,185)

Income (loss) before provision for (benefit from) income taxes is derived as follows:

	1987	1986	1985
		(In thousands)	
U.S.	$ (351,519)	$ (209,769)	$ (222,561)
Other than U.S.	150,464	195,224	170,376
	$ (201,055)	$ (14,545)	$ (52,185)

U.S. Federal tax credits, principally investment tax credits, are accounted for on the flow-through method. Amounts utilized in fiscal 1987, 1986 and 1985 were $8,614,000, $9,916,000 and $6,445,000, respectively. For U.S. Federal income tax purposes, a net operating loss of $35,120,000 and tax credits, principally investment tax credits, of $66,904,000 at March 31, 1987 are available to reduce taxes payable through 2002.

Extraordinary items in 1987, 1986 and 1985 include tax benefits of $4,991,000, $2,579,000 and $1,725,000, respectively, arising from the utilization of operating loss carryforwards. See Note 7 regarding income taxes provided on extraordinary gains arising from the extinguishment of debt.

Deterred income taxes are provided in the financial statements due to timing differences between financial and taxable income. The principal timing differences in recognizing certain revenues, expenses and tax credits for tax return and financial statement purposes and their effect on the provision for deferred income taxes were:

	1987	1986	1985
		(In thousands)	
Excess tax over financial depreciation	$ 17,609	$ 35,495	$ 33,612
Long-term contracts, primarily on the completed contract method for tax purposes	(29,597)	(11,421)	(22,061)
Warranty expense	10,746	2,107	8,903
Provision for cost of certain facility closings, relocations and dispositions	(6,409)	4,258	5,600
Loss on disposal of discontinued operations	(121,508)	—	—
Interest on proposed tax deficiences	(7,054)	(11,659)	(6,990)
Self insurance	(1,236)	(3,936)	(9,295)
Supplemental compensation	(3,046)	(4,203)	552
Pension expense	8,482	8,848	(25,574)
Purchased tax benefits	(19,731)	4,284	6,520
Gain on settlement of retiree pension obligation	84,638	—	—
Tax loss carryforwards	(22,848)	(1,326)	(3,207)
Tax credits	(3,815)	(50,047)	—
Other	(4,089)	4,608	2,699
	$ (97,858)	$ (22,992)	$ (9,241)

The Internal Revenue Service has issued notices for years prior to March 31, 1984 which propose substantial additional taxes. McDermott International believes that the outcome of any income taxes ultimately assessed will not have a material adverse effect on its consolidated financial statements.

NOTE 7 - LONG-TERM DEBT AND NOTES PAYABLE

Long-term debt consists of:

	1987	1986
	(In thousands)	
Unsecured Debt:		
8.27% Note due 1991 with annual sinking fund installments of $15,000,000 beginning 1989	$ 45,000	$ 45,000
10.20% Sinking fund debentures due 1999 with annual sinking fund installments of $2,500,000	35,000	37,450
10% Subordinated debentures ($149,921,000 face amount in 1987) due 2003 with annual sinking fund installments of $15,000,000 beginning 1994	127,180	126,247
$9^5/_8$% Debentures due 2004	6,718	6,718
6.80% Pollution control revenue bonds due 2009 with annual sinking fund installments of $4,250,000 beginning 2006	17,000	17,000
$8^1/_2$% Note payable $3,960,000 annually to 1997	40,200	44,160
9% Note payable $3,300,000 annually to 1991	17,000	20,300
9% Note payable $1,650,000 annually to 1996	16,750	18,400
DM 100,000,000 $6^1/_2$% Bearer-bonds due 1991	55,281	—
Pennsylvania Energy Development Authority Bonds payable 1991-2011 (net of $123,250,000 construction funds held by trustee)	—	—
Floating rate note, due four hundred calendar days after demand, interest at daily federal funds rate plus 1.10%	—	35,000
Floating rate notes ($150,000,000 face value), interest at LIBOR plus 0.125% (6.69% inclusive at March 31, 1987) due 1992	149,602	149,522
Floating rate note, due four hundred calendar days after demand, interest at daily federal funds rate plus 0.75%	—	50,000
Floating rate note, interest at LIBOR plus 0.75% (7.125% inclusive at March 31,1987) due 1989	26,500	26,500
Floating rate note, interest at LIBOR plus 0.5% (6.8125% inclusive at March 31, 1987) due 1989	25,250	25,250
Bank term loan	125,000	175,000
Revolving credit agreement	130,000	—
DM 40,000,000 Term loan 6.75% due 1991	22,159	—
DM 25,000,000 Revolving credit agreement due 1991	13,850	—
Other notes payable through 2009	14,487	21,568
Secured Debt:		
10.375% Note payable	157,000	157,000
Capitalized lease obligations	19,225	17,514
Other notes payable through 1996	12,458	13,387
	1,055,660	986,016
Less:		
Non-current obligation classified as current	205,000	—
Other amounts due within one year	69,536	72,756
	$ 781,124	$ 913,260

During fiscal 1987, the Delaware Company signed a credit agreement with various banks establishing a $150,000,000 line of credit which is guaranteed by International. The Delaware Company may elect to borrow at interest rates equal to $^1/_2$ of 1% plus the prime rate, 1% plus the London Interbank Offered Rate (LIBOR) or 1% plus the certificate of deposit rate. As of March 31, 1987, $130,000,000 was outstanding under this facility at an interest rate of 7.54%. On October 1, 1988, all outstanding borrowings will convert to a term loan payable in eighteen equal quarterly installments and bearing interest at the applicable rate of $^3/_4$ of 1% plus the prime rate, $1^1/_4$% plus LIBOR, or $1^1/_4$% plus the certificate of deposit rate, to maturity at March 31, 1993.

Also, during fiscal 1987, an amendment and guarantee agreement to the Delaware Company's credit agreement with various banks was executed, whereby the credit facility is guaranteed by International. A term loan issued pursuant to this credit facility is payable in equal quarterly installments of $12,500,000 on June 30, September 30, December 31 and March 31 and bears interest at the applicable rate of $^1/_4$ of 1% plus the prime rate, $^3/_4$ of 1% plus LIBOR or $^3/_4$ of 1% plus the certificate of deposit rate, as elected by the Delaware Company. As of March 31, 1987, $125,000,000 was outstanding under this facility at an interest rate of 7.18%.

As a consequence of the discontinuance of the seamless tubular line of business of the Engineered Materials segment and the write-down of certain permanently impaired assets in the fourth quarter of fiscal 1987, compliance with certain of the Delaware Company's credit agreement covenants were waived by the Delaware Company's lenders. These waivers expire July 31, 1987, by which time the Delaware Company fully expects to have negotiated a long-term amendment to the credit agreements or have had the waivers extended. At March 31, 1987, the long-term debt portions of these credit agreements, $130,000,000 and $75,000,000, respectively, were classified as notes payable and current maturities of long-term debt.

McDermott International's $157,000,000 long-term loan at an interest rate of 10.375% is secured by a portion of McDermott International's portfolio of government obligations which must amount to a fair market value of at least $108,645,000. The principal is repayable in twenty ascending payments commencing in fiscal 1989 and the final installment is due June 25, 1998.

During fiscal year 1987, the Delaware Company issued DM 100,000,000 $6^1/_2$% bearer-bonds dated July 1, 1986 and due July 1, 1991. The net proceeds from the bond issue, which is guaranteed by International, were used to repay a portion of the outstanding balance of an existing short-term credit facility established by International in connection with the acquisition of Coutinho.

During fiscal year 1987, McDermott International Trading Company, GmbH negotiated a DM 40,000,000 Term Loan and a DM 25,000,000 Revolving Credit Facility with three foreign banks. The Term Loan bears interest, which is payable quarterly, at $6^3/_4$% per annum and requires mandatory sinking fund payments of 25%, 25% and 50% on June 30, 1989, 1990 and 1991, respectively. The Revolving Credit Facility's original commitment of DM 25,000,000 is subject to mandatory reductions of 25%, 25% and 50% on June 30, 1989, 1990 and 1991, respectively, and bears interest at the London Interbank Offered Rate plus $^1/_2$ of 1% (5.4375% at March 31, 1987) on drawdown options of 3, 6, 9, or 12 months. The proceeds from the loans, which are guaranteed by International, were used to repay the remaining balance of a short-term credit facility established in connection with the acquisition of Coutinho. At March 31, 1987, DM 40,000,000 and DM 25,000,000 were outstanding against the Term Loan and the Revolving Credit Facility, respectively.

Maturities of long-term debt during the five fiscal years subsequent to March 31, 1987 are as follows: 1988 - $274,536,000, including the non-current obligation of $205,000,000 classified as current; 1989 - $64,491,000; 1990 - $77,288,000; 1991 - $51,705,000; 1992 - $251,782,000.

Certain consolidated subsidiaries are restricted principally as a result of credit agreement covenants, in their ability to transfer funds to International through intercompany loans, advances or cash dividends. At March 31, 1987, approximately $621,336,000 of the net assets of these subsidiaries were subject to such restrictions. It is not expected that these restrictions will have any significant practical effect on International's liquidity.

Certain debt agreements contain among other things, requirements as to maintenance of net worth and limitations on the incurrence of additional borrowings. Under the most restrictive of these agreements at March 31, 1987, additional borrowings were totally restricted. Subsequent to March 31, 1987, compliance with these requirements was waived by the Delaware Company's lenders as discussed above. Pursuant to the waiver, additional borrowings of McDermott International from April 1, 1987 through July 31, 1987, cannot exceed $200,000,000 and the Delaware Company must maintain a tangible net worth at least equal to $625,000,000 through July 31, 1987. Tangible net worth of the Delaware Company at March 31, 1987 was $680,000,000.

International and certain of its subsidiaries at March 31, 1987 had available unused short-term lines of credit from various banks totaling approximately $134,000,000.

Current notes payable to banks at March 31, 1987 and 1986 were $59,665,000 and $129,359,000, respectively. At March 31, 1987, other current notes payable of $202,184,000 were secured by $202,600,000 par value of government obligations as compared with $61,434,000 and $52,750,000, respectively, at March 31, 1986.

The Delaware Company recognized extraordinary gains of $210,000, net of income taxes of $179,000 and $9,962,000, net of income taxes of $8,486,000, during fiscal 1986 and 1985, respectively, resulting from the extinguishment of certain debt.

NOTE 8 - CONTINGENCIES AND COMMITMENTS

Litigation - International and certain of its officers, directors and subsidiaries are defendants in numerous legal proceedings. Management and general counsel believe that the outcome of these proceedings will not have a material adverse effect upon the consolidated financial statements.

Operating Leases - Future minimum payments required under operating leases that have initial or remaining noncancellable lease terms in excess of one year at March 31, 1987 are as follows: 1988 - $25,875,000; 1989 - $18,904,000; 1990 - $12,935,000; 1991 - $7,567,000; 1992 - $6,906,000 and thereafter - $45,815,000. Future minimum lease payments and leased property under capital leases are not material. Total rental expense for fiscal 1987, 1986 and 1985 was $80,852,000, $74,633,000 and $112,227,000, respectively. These expense figures include contingent rentals and are net of sublease income, both of which are not material.

Other - McDermott International performs significant amounts of work for the U.S. Government under both prime contracts and subcontracts and thus is subject to continuing reviews by governmental agencies.

Firm and contemplated commitments for capital expenditures amounted to approximately $22,047,000 at March 31, 1987.

McDermott International is contingently liable under standby letters of credit totaling $371,556,000 at March 31, 1987, issued in the normal course of business.

NOTE 9 - SUBSIDIARY'S REDEEMABLE PREFERRED STOCKS

At March 31, 1987 and 1986, 13,000,000 shares of Delaware Company Preferred Stock, with a par value of $1 per share, were authorized. Of the authorized shares, 2,825,554 and 3,724,629 shares of Series A and Series B Preferred Stock, respectively, were outstanding at March 31, 1987 and 1986. The outstanding shares are entitled to $31.25 per share in liquidation. Preferred dividends of approximately $15,900,000 are classified as minority interest in Other Income (Expense) in each of the fiscal years 1987, 1986 and 1985.

The outstanding shares were issued in connection with the acquisition of B&W and are stated at the mandatory redemption value which approximated market value at the time the shares were issued. Both series of Preferred Stock are entitled to general voting rights of one-half vote for each share. The Board of Directors of the Delaware Company may authorize additional series of Preferred Stock, and may set terms of each new series except that the Delaware Company cannot create any series of stock senior to the existing Series A and Series B Preferred Stock without the consent of the holders of at least 50% of the shares of such Preferred Stock.

Each share of the outstanding Series A Preferred Stock is convertible into one share of Common Stock of International plus $0.10 cash. The shares are redeemable at the option of the Delaware Company on or after March 31 of each of the following years, at the following prices, plus accrued dividends: 1987 - $31.97; 1988 - $31.62; and 1989 through 2008 - $31.25. On March 31, 1989 and each subsequent year through March 31, 2008, the Delaware Company is obligated to redeem, at a redemption price of $31.25 plus accrued dividends, 5% of the number of shares which are issued at December 31, 1988. Based on the number of shares issued at March 31, 1987 the obligation to redeem Series A Preferred Stock is $9,809,000 for each of the fiscal years 1989 through 1992.

Series B Preferred Stock is redeemable at the option of the Delaware Company at $31.25 per share plus accrued dividends. On March 31 of each of the fiscal years 1988 through 1995, March 31 of each of the fiscal years 1996 through 2006, and March 31 of each of the fiscal years 2007 and 2008, the Delaware Company is obligated to redeem 315,877, 252,702 and 189,526 shares of Series B Preferred Stock, respectively. The obligation to redeem Series B Preferred Stock is $9,871,000 for each of the fiscal years 1988 through 1992. The Delaware Company applied 315,877 shares of Series B Preferred Stock that it owned to satisfy the March 31, 1987 mandatory sinking fund obligation.

Additional shares of Series A or Series B Preferred Stock, equal to the number of shares the Delaware Company is obligated to redeem, may be redeemed on each mandatory redemption date by the Delaware Company, on a non-cumulative basis. The Delaware Company may apply to the mandatory sinking fund obligations any Series A or B Preferred Stock owned, previously redeemed or surrendered for conversion which have not been previously credited against the mandatory sinking fund obligations. At March 31, 1987, 42,863 shares of Series A Preferred Stock have been converted to date and the Delaware Company owned 3,451,999 and 1,961,162 shares of Series A and Series B Preferred Stock, respectively.

NOTE 10 - CAPITAL STOCK

Common Stock - Changes in Common Stock during the three years ended March 31, 1987 are summarized as below:

	Shares	Par Value	Capital in Excess of Par Value
		(In thousands except for share data)	
Balance, March 31, 1984	36,903,571	$ 36,903	$ 311,875
Shares issued upon conversion of Series A $2.20 cumulative convertible preferred stock	609	1	18
Shares issued upon exercise of stock options	31,284	31	739
Shares issued upon exercise of warrants	2,600	2	53
Deferred career executive stock plan expense (net of forfeitures)	(1,540)	(1)	538
Balance, March 31, 1985	36,936,524	$ 36,936	$ 313,223
Shares issued upon conversion of Series A $2.20 cumulative convertible preferred stock	2	—	—
Shares issued upon exercise of stock options	37,118	38	542
Shares issued upon exercise of warrants	80	—	2
Deferred career executive stock plan expense	—	—	223
Balance, March 31, 1986	36,973,724	$ 36,974	$ 313,990
Shares issued upon exercise of stock options	79,693	79	2,011
Deferred career executive stock plan expense	—	—	163
Balance, March 31, 1987	37,053,417	$ 37,053	$ 316,164

The Panamanian regulations relating to acquisitions of securities of companies, such as International, registered with the National Securities Commission require, among other matters, that detailed disclosure concerning the offeror, which is subject to review by either the Panamanian National Securities Commission or the Board of Directors of the subject company, be finalized prior to the beneficial acquisition of more than 5 percent of the outstanding shares of any class of stock. Transfers of securities in violation of these regulations are invalid and cannot be registered for transfer.

At March 31, 1987 and 1986, 58,250,257 and 58,535,582 shares of Common Stock, respectively, were reserved for issuance in connection with exercise of warrants, exercise of rights, the 1974 Career Executive Stock Plan, exercise of stock options, the 1983 Long-Term Performance Incentive Compensation Program and conversion of Series A Preferred Stock.

International Rights - On December 30, 1985, each holder of Common Stock received a dividend distribution of one Right for each outstanding share of Common Stock. The Rights currently trade with the Common Stock and at March 31, 1987 and 1986, International had outstanding Rights to purchase 37,153,417 and 37,073,724 shares, respectively, of its Common Stock at a price of $50 per share subject to anti-dilution adjustments. The Rights will become exercisable and will detach from the Common Stock 10 days after a person or a group either becomes the beneficial owner of 20 percent or more of the outstanding Common Stock, or commences or announces an intention to commence a tender or exchange offer for 30 percent or more of the outstanding Common Stock. If thereafter the acquiring person or group engages in certain self-dealing transactions, holders of Rights may purchase at the exercise price that number of shares of Common Stock having a market value equal to twice the exercise price. In the event International merges with or transfers 50 percent or more of its assets or earnings to any person after the Rights become exercisable, holders of Rights may purchase at the exercise price that number of shares of Common Stock of the acquiring entity having a market value equal to twice the exercise price. The Rights are redeemable by International and expire on December 30, 1995.

International Warrants - At March 31, 1987 and 1986, International had outstanding warrants to purchase 5,995,990 shares of its Common Stock exercisable by the payment per share of $25 cash or $25 principal amount of the Delaware Company's 10% Subordinated debentures due 2003. The International warrants expire on April 1, 1990 or as early as April 1, 1988 if the International Common Stock trades at not less than 125% of the warrant exercise price for a specified period of time.

Long-Term Performance Incentive Compensation Programs - Under the program which was adopted February 8, 1983, the Career Executive Stock Plan Committee (the "Committee") may grant to the officers and key employees options to purchase in the aggregate up to 2,000,000 shares of Common Stock at 100% of the fair market value on the date of grant. Options are exercisable not less than one year and not more than ten years after the date of grant. The Committee may grant stock appreciation rights in connection with the granting of options under the program. Such stock appreciation rights permit the holders thereof to surrender exercisable options in exchange for shares of Common Stock having a fair market value on the date of such surrender equal to the excess (up to, but not greater than, the fair market value of the underlying shares on the date of grant) of the fair market value on such date of the shares to which such surrendered option relates over the aggregate option price under the related options. The Committee may, at its discretion, grant holders of stock appreciation rights the right to receive up to 50% of such excess in cash in lieu of shares of Common Stock. The program also authorizes the Committee to grant performance unit awards which are earned by the achievement of performance standards established by the Committee. Performance units are paid in cash or shares of Common Stock or both at the discretion of the Committee. At March 31, 1987, 1986 and 1985, stock option and stock appreciation rights awards of 733,185, 1,031,560 and 309,590, respectively, were awarded and outstanding at an average price of $18.3512 per share. At March 31, 1987, 1986 and 1985, 889,665, 876,615 and 1,606,180 shares were available for award under the program and 285,325, 7,595 and 50,545 options were excercised or surrendered for appreciation rights during the year ended on each such date. During fiscal 1987 and 1985, no stock options or stock appreciation rights were awarded. During fiscal 1986, 733,320 stock options and stock appreciation rights were awarded. Awards relating to 13,050, 3,755 and 2,030 shares were forfeited during fiscal 1987, 1986 and 1985, respectively. Charges (credits) to income with respect to stock appreciation rights and performance units were $(9,484,000), $(2,257,000) and $(1,891,000) during fiscal 1987, 1986 and 1985, respectively.

Career Executive Stock Plan - This plan, which was adopted as a plan of International effective March 15, 1983, originally authorized 600,000 shares of Common Stock to be issued to eligible employees in consideration of their services. Employees granted stock under the plan pay $1.00 per share as the option purchase price. Restrictions with respect to issued shares lapse in approximately equal amounts on the second through tenth anniversary dates of the date of issuance. The cost of the plan, based on fair market value on the date of issuance of Common Stock, is amortized over a ten year period following the date of issuance. Upon forfeiture of stock to employees, previous expense attributable to unvested stock is credited to income. During fiscal 1987 and 1986 no shares were forfeited under the plan. During fiscal 1985, 1,540 shares were forfeited under the plan. As of June 30, 1984, no further awards could be made under the plan. Charges to income under the plan were $163,000, $223,000 and $538,000 during fiscal 1987, 1986 and 1985, respectively.

International Preferred Stock - At March 31, 1987 and 1986, 25,000,000 shares of Preferred Stock were authorized and International has issued 100,000 shares of Series A Participating Preferred Stock (the "Participating Preferred Stock") and 100,000 shares of Series B Non-Voting Preferred Stock (the "Non-Voting Preferred Stock"), all of which are owned by the Delaware Company. The annual per share dividend rates for the Participating Preferred Stock and the Non-Voting Preferred Stock are $10 (but no more than ten times the amount of the per share dividend on International Common Shares) and $20, respectively, payable quarterly, and dividends on such shares are cumulative to the extent not paid. In addition, shares of Participating Preferred Stock are entitled to receive additional dividends whenever dividends in excess of $3.00 per International Share are declared (or deemed to have been declared) in any fiscal year. At the time of issuance, the Participating Preferred Stock, as a class, was entitled to an aggregate number of votes equal to 10% of the total number of votes entitled to be cast on any matter by the stockholders of International. On February 10, 1987, the Board of Directors of International, with the consent of the Delaware Company (as holder of all issued and outstanding Participating Preferred Stock), repealed and eliminated the voting rights of the Participating Preferred Stock.

The issuance of additional International Preferred Stock in the future and the specific terms thereof, such as the dividend rights, conversion rights, voting rights, redemption prices and similar matters, may be authorized by the Board of Directors of International without stockholder approval, except to the extent such approval may be required by applicable rules of the New York Stock Exchange or applicable law. If additional Preferred Stock is issued, such additional shares will rank senior to International Common Stock as to dividends and upon liquidation.

NOTE 11 - SEGMENT REPORTING

McDermott International operates primarily in four industry segments—Marine Construction Services; Power Generation Systems and Equipment; Engineered Materials; and Trading.

Marine Construction Services principally involves the construction of specialized offshore platforms and marine pipelines used for development drilling, production and transportation of oil and gas.

Power Generation Systems and Equipment includes individually engineered complete fossil fuel boilers, nuclear steam systems, nuclear fuel and nuclear fuel assemblies, specially engineered accessories and components, microprocessor-based control systems, replacement parts and customer services and associated equipment for electric utility applications as well as fossil fuel boilers for industrial processes and power generation.

Engineered Materials consists of tubular and insulating products designed and manufactured from basic and raw materials. Tubular products include alloy and carbon welded tubes. Insulating products include specially engineered and vacuum-formed ceramic fibers, insulating and specialty firebrick, fire protection insulation, plastics, mortars, castables and special oxide refractories.

Trading consists primarily of buying and selling iron and steel products, nonferrous materials, chemical products, cables and equipment for electric power distribution, tools, machinery and utility vehicles, aromatics, olefins, plastics and fine chemicals, as well as the construction and engineering operations of Coutinho.

Identifiable assets by industry segment are those assets that are used in McDermott International's operations in each segment. Corporate assets are principally cash, short-term investments and marketable securities.

Intersegment sales are accounted for at prices which are generally established by reference to similar transactions with unaffiliated customers.

Revenues attributable to transactions with unconsolidated joint-venture companies were $31,788,000, $53,403,000 and $22,327,000 in fiscal years 1987, 1986 and 1985, respectively. In addition, interest income of $10,160,000 on a note from a joint-venture company and a gain of approximately $5,100,000 on the sale of certain fixed assets to joint-venture companies were recognized in fiscal year 1985.

In the fiscal years 1987, 1986 and 1985, the U.S. Government accounted for approximately 12%, 13% and 14%, respectively, of total revenues. These revenues are included in the Power Generation Systems and Equipment segment.

Operating Income (Loss) in fiscal 1987 includes $19,626,000 in Marine Construction Services and $6,902,000 in Power Generation Systems and Equipment for accelerated depreciation on equipment and facilities which were considered to be obsolete and have diminished cost effectiveness. Operating Income (Loss) in fiscal 1987 also includes $26,000,000 in Trading, $11,747,000 in Power Generation Systems and Equipment and $7,008,000 in Engineered Materials for the write-off of goodwill.

Operating Income (Loss) reflects a provision of $976,000 made by McDermott International in fiscal year 1986 to cover the closing of certain of the Power Generation Systems and Equipment's facilities. In addition, fiscal year 1985 includes a gain of $5,452,000 related to the sale of certain other Power Generation Systems and Equipment's facilities closed in prior years. Such amounts were previously included in the Other Income (Expense) section of the Consolidated Statement of Income (Loss) and Retained Earnings as Other-Net.

Segment Information For the Three Fiscal Years Ended March 31, 1987.

1. Information about McDermott International's Operations in Different Industry Segments.

	1987	1986	1985
		(In thousands)	
Revenues(1)			
Marine Construction Services	$ 862,785	$ 908,186	$ 1,045,938
Power Generation Systems & Equipment	1,525,952	1,447,394	1,413,481
Engineered Materials	130,407	148,110	153,214
Trading	849,496	655,145	435,924
Intersegment Transfer Eliminations	(79,318)	(49,596)	(26,045)
Total Revenues	$ 3,289,322	$ 3,109,239	$ 3,022,512
Operating Income (Loss)(2)			
Marine Construction Services	$ (81,497)	$ (30,196)	$ (8,293)
Power Generation Systems & Equipment	72,258	36,771	20,797
Engineered Materials	11,349	11,882	12,952
Trading	(29,306)	(536)	(4,137)
Total Operating Income (Loss)	$ (27,196)	$ 17,921	$ 21,319

(1) Segment revenues include intersegment transfers as follows:

	1987	1986	1985
Marine Construction Services	$ 962	$ 12,028	$ —
Power Generation Systems & Equipment	2,093	2,809	607
Engineered Materials	13,611	19,188	20,942
Trading	62,652	15,571	4,496
Total	$ 79,318	$ 49,596	$ 26,045

(2) Reconciling items between Segment Operating Income (Loss) and Operating Income (Loss) on the Consolidated Statement of Income (Loss) and Retained Earnings are General Corporate Expenses.

	1987	1986	1985
		(In thousands)	
Capital Expenditures			
Marine Construction Services	$ 69,323	$ 231,408	$ 107,514
Power Generation Systems & Equipment	49,092	36,102	39,212
Engineered Materials	8,387	19,483	10,447
Trading	4,746	2,376	550
Corporate	608	7,207	3,380
Discontinued Operations	1,159	2,308	11,246
Total Capital Expenditures	$ 133,315	$ 298,884	$ 172,349
Depreciation and Amortization (1)			
Marine Construction Services	$ 104,925	$ 90,008	$ 83,154
Power Generation Systems & Equipment	48,917	35,119	32,678
Engineered Materials	5,623	4,031	3,881
Trading	4,800	4,123	2,656
Corporate	4,255	5,077	7,500
	168,520	138,358	129,899
Discontinued Operations	20,816	19,440	19,047
Total Depreciation and Amortization	$ 189,336	$ 157,798	$ 148,946
Identifiable Assets			
Marine Construction Services	$ 1,131,277	$ 1,166,129	$ 1,039,835
Power Generation Systems & Equipment	1,290,349	1,179,135	1,177,221
Engineered Materials	232,316	175,765	139,961
Trading	296,553	285,683	229,780
Corporate	1,408,503	1,215,474	1,208,166
Discontinued Operations	24,261	328,756	385,721
Total Identifiable Assets	$ 4,383,259	$ 4,350,942	$ 4,180,684

(1) Depreciation and amortization excludes the write-down of property, plant and equipment in connection with discontinued operations and the write-off of goodwill.

2. Information about McDermott International's Operations in Different Geographic Areas.

		1987	1986 (In thousands)	1985
Revenues (1)	- Unites States	$ 1,936,701	$ 1,808,986	$ 1,756,507
	- Europe and West Africa	798,867	812,446	697,709
	- Other Foreign	553,754	487,807	568,296
	- Total	$ 3,289,322	$ 3,109,239	$ 3,022,512
Operating Income (Loss) by Geographic Area (2)	- United States	$ 43,772	$ (11,315)	$ (51,067)
	- Europe and West Africa	(21,775)	32,611	30,455
	- Other Foreign	(49,193)	(3,375)	41,931
	- Total	$ (27,196)	$ 17,921	$ 21,319
Identifiable Assets	- United States	$ 1,707,475	$ 1,570,232	$ 1,508,474
	- Europe and West Africa	885,696	857,293	653,344
	- Other Foreign	357,324	379,187	424,979
	- Corporate	1,408,503	1,215,474	1,208,166
	- Discontinued Operations	24,261	328,756	385,721
	- Total	$ 4,383,259	$ 4,350,942	$ 4,180,684

(1) Transfers between geographic areas and export sales are immaterial and not separately presented.

(2) Reconciling items between Segment Operating Income (Loss) by Geographic Area and Income (Loss) in the Consolidated Statement of Income (Loss) and Retained Earnings are General Corporate Expenses.

NOTE 12 - QUARTERLY FINANCIAL DATA

The following tables set forth selected unaudited quarterly financial information for the fiscal years ended March 31, 1987 and 1986:

	1987 Quarter Ended			
	June 30, 1986	Sept. 30, 1986	Dec. 31, 1986	March 31, 1987
	(In thousands except for per share amounts)			
Revenues	$ 757,054	$ 822,726	$ 811,990	$ 897,552
Operating income (loss)	(18,653)	(12,633)	(18,105)	(42,815)
Income (loss) from continuing operations	201,379	(23,741)	(21,112)	(69,081)
Net income (loss)	221,335	(32,257)	(31,472)	(260,027)
Earnings (loss) per share:				
Primary				
From continuing operations	5.45	(0.64)	(0.57)	(1.87)
Net earnings (loss)	5.99	(0.87)	(0.85)	(7.03)
Fully Diluted				
From continuing operations	5.08	(0.64)	(0.57)	(1.87)
Net earnings (loss)	5.58	(0.87)	(0.85)	(7.03)

For the quarter ended March 31, 1987, loss from continuing operations includes expenses of $62,481,000 related to the write-off of goodwill and accelerated depreciation, provisions of $33,112,000 for certain additional contract losses and certain restructuring and consolidation expenses and a pension settlement gain of $68,803,000. In addition, net loss includes a provision for loss of $223,699,000 and a pension settlement gain of $38,921,000 both attributable to discontinued operations.

	1986 Quarter Ended			
	June 30, 1985	Sept. 30, 1985	Dec. 31, 1985	March 31, 1986
	(In thousands except for per share amounts)			
Revenues	$ 726,772	$ 771,689	$ 798,567	$ 812,211
Operating income (loss)	(39,612)	(5,591)	6,192	(7,082)
Income (loss) from continuing operations	3,879	9,569	44,762	24,483
Net income (loss)	(1,077)	357	38,750	21,059
Earnings (loss) per share:				
Primary				
From continuing operations	0.10	0.26	1.21	0.66
Net earnings (loss)	(0.03)	0.01	1.05	0.57
Fully Diluted				
From continuing operations	0.10	0.26	1.16	0.65
Net earnings (loss)	(0.03)	0.01	1.01	0.57

For the quarter March 31, 1986, income from continuing operations and net income include charges of $15,886,000 related to the settlement of certain antitrust civil litigation and gains of $24,340,000 for the sale of government obligations.

Item 9. DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

PART III

Item 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

There are no family relationships between any of the executive officers, directors or persons nominated to be such, and no executive officer was elected to his position pursuant to any arrangement or understanding between himself and any other person.

Information required by this item with respect to directors and executive officers is incorporated by reference to the material appearing under the headings "Election of Directors" in the Proxy Statement for the 1987 Annual Meeting of Shareholders.

Item 11. EXECUTIVE COMPENSATION

Information required by this item is incorporated by reference to the material appearing under the heading "Cash Compensation of Executive Officers and Certain Relationships and Related Transactions" in the Proxy Statement for the 1987 Annual Meeting of Shareholders.

Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Information required by this item is incorporated by reference to the material appearing under the heading "Election of Directors" in the Proxy Statement for the 1987 Annual Meeting of Shareholders.

Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information required by this item is incorporated by reference to the material appearing under the heading "Cash Compensation of Executive Officers and Certain Relationships and Related Transactions" in the Proxy Statement for the 1987 Annual Meeting of Shareholders.

PART IV

Item 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

Consolidated Financial Schedules

All required schedules will be filed by amendment to this Form 10-K on Form 8.

Exhibit Index

3	Articles of Incorporation and By-Laws (Items 3(a) and 3(b) are incorporated by reference to Exhibit 3 to the Company's annual report on Form 10-K, as amended, for the fiscal year ended March 31, 1983). (a) The Company's Restated Articles of Incorporation (b) The Company's By-Laws	
4(a)	Warrant Agreement (incorporated by reference to Exhibit 4 to the Company's annual report on Form 10-K, as amended, for the fiscal year ended March 31, 1983).	
4(b)	Rights Agreement (incorporated by reference to Exhibit 1 to the Company's registration statement on Form 8-A, dated December 27, 1985).	
10	Material Contracts (Exhibits 10(a) through 10(b) and 10(d) through 10(f) are incorporated by reference to Exhibit 10 to the Company's annual report on Form 10-K, as amended, for the fiscal year ended March 31, 1983, Exhibit 10(c) is incorporated by reference to Exhibit 10 to the Company's annual report on Form 10-K, as amended, for the fiscal year ended March 31, 1984 and Exhibit 10(g) is incorporated by reference to Exhibit 10 to the Company's annual report on Form 10-K, as amended, for the fiscal year ended March 31, 1986). (a) Supplemental Executive Retirement Plan (b) 1983 Long-Term Performance Incentive Compensation Program (c) Supplemental Compensation Plan (d) Restoration of Retirement Income Plan for Certain Participants in the Retirement Plan for Employees of McDermott International, Inc. (e) Career Executive Stock Plan—1974 (f) Intercompany Agreement (g) Trust for Supplemental Executive Retirement Plan (including employment agreement with J. E. Cunningham) (h) Variable Supplemental Compensation will be filed by amendment to this Form 10-K on Form 8	
11	Statement Re Computation of Per Share Earnings (Loss)	47
22	Significant Subsidiaries of the Registrant	49
24	Consent of Certified Public Accountants	50

FORM 8-K REPORTS

Report on Form 8-K, Item 5 was reported, but no financial statements were filed in connection with International's current report on Form 8-K dated May 18, 1987.

EXHIBIT 11

McDERMOTT INTERNATIONAL, INC.
STATEMENT RE COMPUTATION OF PER SHARE EARNINGS (LOSS)
FOR THE THREE FISCAL YEARS ENDED MARCH 31, 1987

(In thousands, except shares and per share amounts)

Primary

	1987	1986	1985
Income from continuing operations	$ 87,445	$ 82,693	$ 48,336
Loss on discontinued operations	(220,568)	(26,393)	(29,356)
Extraordinary items	4,991	2,789	11,687
Cumulative effect of accounting change	25,711	—	—
Net income (loss) for primary computation	$ (102,421)	$ 59,089	$ 30,667
Weighted average number of common shares outstanding during the year	36,984,044	36,958,187	36,926,242
Common stock equivalents of stock options, stock appreciation rights and performance units based on "treasury stock" method	379	53,798	106,731
Weighted average number of common and common equivalent shares outstanding during the year	36,984,423	37,011,985	37,032,973
Earnings (loss) per common and common equivalent share:			
Continuing operations	$ 2.36	$ 2.23	$ 1.31
Discontinued operations	(5.96)	(0.71)	(0.79)
Extraordinary items	0.13	0.08	0.31
Accounting change	0.70	—	—
Net income (loss)	$ (2.77)	$ 1.60	$ 0.83

Fully Diluted

Earnings (loss) per common equivalent share assuming full dilution are the same except for fiscal 1987 and 1986 Income From Continuing Operations which are calculated as follows:

	1987	1986
Net income from continuing operations	$ 87,445	$ 82,693
Dividends on Subsidiary's Series A $2.20 Cumulative Convertible Preferred Stock assuming conversion to Common Stock	6,216	6,216
Net income for fully diluted computation	$ 93,661	$ 88,909
Weighted average number of common shares outstanding during the year	36,984,044	36,958,187
Common stock equivalents of stock options, stock appreciation rights and performance units based on "treasury stock" method	35,153	53,818
Shares applicable to warrants based on "treasury stock" method	714,110	—
Shares applicable to Subsidiary's Series A $2.20 Cumulative Convertible Preferred Stock	2,825,554	2,825,554
Weighted average number of common and common equivalent shares outstanding during the year, assuming full dilution	40,558,861	39,837,559
Earnings (loss) per common and common equivalent share assuming full dilution:		
Continuing operations	$ 2.31	$ 2.23

Fully diluted earnings (loss) per share includes only computations which cause dilution.

EXHIBIT 22

McDERMOTT INTERNATIONAL, INC.
SIGNIFICANT SUBSIDIARIES OF THE REGISTRANT
FISCAL YEAR ENDED MARCH 31, 1987

Name of Company	Organized Under the Laws of	Percentage of Voting Shares Owned
McDermott International Investments Co., Inc.	Panama	100
McDermott International Trading (Germany) GMBH	West Germany	100
McDermott Incorporated	Delaware	92
The Babcock & Wilcox Company	Delaware	100

The subsidiaries omitted from the foregoing list do not, considered in the aggregate, constitute a significant subsidiary.

CONSENT OF CERTIFIED PUBLIC ACCOUNTANTS

We consent to the incorporation by reference in the Registration Statement (Form S-3 No. 33-4631 and 22-15078) of McDermott Incorporated and in the related Prospectus and in the Registration Statement (Form S-8 No. 2-83692) of McDermott International, Inc. and in the related Prospectus of our report dated June 16, 1987 with respect to the consolidated financial statements of McDermott International, Inc. included in this Annual Report (Form 10-K) for the year ended March 31, 1987.

ARTHUR YOUNG & COMPANY

New Orleans, Louisiana
June 16, 1987

SIGNATURES OF THE REGISTRANT

Pursuant to the requirements of Sections 13 or 15(d) 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 on June 16, 1987.

McDERMOTT INTERNATIONAL, INC.
(Registrant)

By: s/J. E. Cunningham
J. E. Cunningham
Chairman of the Board and
Chief Executive Officer

By: s/John A. Lynott
John A. Lynott
Executive Vice President,
Chief Financial and
Administrative Officer

By: s/E. A. Robidoux
E. A. Robidoux
Vice President and Controller

SIGNATURES OF DIRECTORS

Pursuant to the requirements of the Securities Exchange Act of 1934, this report is signed below by the following persons on behalf of the registrant and in the capacities indicated on June 16, 1987.

s/T. D. Barrow
T. D. Barrow
Director

s/J. E. Cunningham
Chairman of the Board and
Chief Executive Officer,
and Director

s/James L. Dutt
James L. Dutt
Director

s/R. E. Howson
R. E. Howson
President and Chief Operating
Officer, McDermott Marine
Construction and Babcock &
Wilcox, and Director

s/James A. Hunt
James A. Hunt
Director

s/John A. Lynott
John A. Lynott
Executive Vice President,
Chief Financial and
Administrative Officer,
and Director

s/J. H. Macdonald
J. H. Macdonald
Director

s/John A. Morgan
John A. Morgan
Director

s/John D. Ritchie
John D. Ritchie
Director

s/William T. Seawell
William T. Seawell
Director

s/Walter B. Shaw
Walter B. Shaw
Director

s/Walter O. Spencer
Walter O. Spencer
Director

s/John B. Tweedy
John B. Tweedy
Director

s/Walter M. Vannoy
Walter M. Vannoy
Vice-Chairman of the Board,
and Director

s/Russell L. Wagner
Russell L. Wagner
Director

Common Stock Transfer Agents and Registrars

Morgan Shareholder Services Trust Company
30 West Broadway
New York, New York 10007-2192

Banco General, S.A.
Apartado Postal 4592
Panama 5, Panama
(Appointment Pending)

- Common Stock of McDermott International, Inc.

Preferred Stock Transfer Agent and Registrar

Morgan Shareholder Services Trust Company
30 West Broadway
New York, New York 10007-2192

- Series A $2.20 Cumulative Convertible Preferred Stock of McDermott Incorporated
- Series B $2.60 Cumulative Preferred Stock of McDermott Incorporated

Rights Agent, Trustees, and Paying Agents

Morgan Guaranty Trust Company of New York
30 West Broadway
New York, New York 10015

- Rights to purchase Common Stock of McDermott International, Inc.
- $9^5/_8$% Debentures Due March 15, 2004
- 10.20% Sinking Fund Debentures Due December 1, 1999
- Floating Rate Notes Due March 1992

Pittsburgh National Bank
Post Office Box 340747
Pittsburgh, Pennsylvania 15230

- 6.80% Pollution Control Revenue Bonds, Series A Due February 1, 2009

Deutsche Bank Aktiengesellschaft
Taunusanlage 12
D-6000 Frankfurt am Main 1
Federal Republic of Germany

- $6^1/_2$% Deutsche Mark Bearer Bonds Due July 1, 1991

Trustee, Paying Agent, Warrant Agent, and Exchange Agent

Bankers Trust Company
Post Office Box 318
Church Street Station
New York, New York 10015

- 10% Subordinated Debentures Due April 1, 2003
- Warrants to purchase Common Stock of McDermott International, Inc.

Certified Public Accountants

Arthur Young & Company
1340 Poydras Street
New Orleans, Louisiana 70112
(504) 581-3131

Annual Meeting

The Annual Meeting of the Stockholders of McDermott International, Inc. for the fiscal year ended March 31, 1987 will be held at the Marriott Hotel, Panama City, Republic of Panama on Tuesday, August 11, 1987 at 9:30 a.m. local time.

Information

Additional information about the Company, including financial statement schedules and exhibits to the Annual Report to shareholders on Form 10-K for the fiscal year ended March 31, 1987 may be obtained, without charge by writing:
Corporate Secretary
McDermott International, Inc.
1010 Common Street
New Orleans, Louisiana 70112
(504) 587-5400

Inquiries regarding stockholder account matters should be addressed to:
Morgan Shareholder Services Trust Company
30 West Broadway
New York, New York 10007-2192
(212) 587-6515

McDermott International, *inc.*
1010 Common Street
New Orleans, LA 70112
(504) 587-5400