

SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

Filing Date: **1994-05-13** | Period of Report: **1994-03-31**
SEC Accession No. **0000950129-94-000414**

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FILER

SMITH INTERNATIONAL INC

CIK: **721083** | IRS No.: **953822631** | State of Incorpor.: **DE** | Fiscal Year End: **1231**
Type: **10-Q** | Act: **34** | File No.: **001-08514** | Film No.: **94528339**
SIC: **3533** Oil & gas field machinery & equipment

Mailing Address
16740 HARDY ST
HOUSTON TX 77032

Business Address
16740 HARDY ST
HOUSTON TX 77032
7134433370

SECURITIES AND EXCHANGE
COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Under Section 13 or 15(d)
of the Securities Exchange Act of 1934

For the quarter ended March 31, 1994

Commission File Number 1-8514

SMITH INTERNATIONAL, INC.
(Exact name of registrant as specified in its charter)

DELAWARE
(State or other Jurisdiction of
incorporation or organization)

95-3822631
(I.R.S. Employer
Identification No.)

16740 Hardy Street, Houston, Texas
(Address of principal executive offices)

77032
Zip Code

Registrant's telephone number, including area code

(713) 443-3370

Indicate by check mark whether the registrant (1) has filed all reports 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 .
--- ---

On March 31, 1994, the registrant had 39,317,402 shares of common stock outstanding.

SMITH INTERNATIONAL, INC.

PART I. FINANCIAL INFORMATION

The condensed financial statements included herein have been prepared by the Company without audit pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of Management, all adjustments necessary for a fair statement of the results of operations for the three month periods ended March 31, 1994 and 1993 have been made. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information

presented not misleading. It is suggested that these condensed financial statements be read in conjunction with the financial statements and the notes thereto included in the Company's latest annual report on Form 10-K.

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SMITH INTERNATIONAL, INC.
 CONSOLIDATED STATEMENTS OF OPERATIONS
 For the three months ended March 31,

<TABLE>
 <CAPTION>

	1994	1993
	(Unaudited)	
	(In thousands,	
	except per share data)	
<S>	<C>	<C>
REVENUES.....	\$ 100,762	\$ 49,954
 COST AND EXPENSES:		
Cost of Revenues.....	65,181	32,780
Selling Expenses.....	17,950	8,805
General and Administrative Expenses.....	7,270	5,062
	90,401	46,647
 INCOME FROM CONTINUING OPERATIONS BEFORE INTEREST AND TAXES.....	10,361	3,307
 INTEREST EXPENSE, net.....	946	1,963
	---	---
 INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND MINORITY INTEREST.....	9,415	1,344
 INCOME TAX PROVISION.....	884	17
	---	---
 INCOME FROM CONTINUING OPERATIONS BEFORE MINORITY INTEREST.....	8,531	1,327
 MINORITY INTEREST.....	942	---
	7,589	1,327
 INCOME FROM CONTINUING OPERATIONS.....		
 INCOME FROM DISCONTINUED OPERATIONS (Note 4).	---	73,623
 CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE (Note 1).....	---	(1,300)
	7,589	73,650
 NET INCOME.....		
 PREFERRED STOCK DIVIDENDS.....	---	(434)
	\$ 7,589	\$ 73,216
 NET INCOME APPLICABLE TO COMMON STOCK.....	=====	=====
 PRIMARY EARNINGS PER COMMON SHARE (Note 2):		
Income from continuing operations.....	\$.20	\$.03
Income from discontinued operations.....	---	2.02
Cumulative effect of change in accounting principle.....	---	(.04)
	\$.20	\$ 2.01
 Net income.....	=====	=====

AVERAGE COMMON AND EQUIVALENT SHARES OUTSTANDING.....	38,791 =====	36,295 =====
--	-----------------	-----------------

</TABLE>

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

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SMITH INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS
ASSETS

<TABLE>
<CAPTION>

	March 31, 1994 ----- (Unaudited)	December 31, 1993 -----
	(in thousands)	
<S>	<C>	<C>
CURRENT ASSETS:		
Cash and cash equivalents.....	\$ 14,108	\$ 101,561
Receivables, less allowance of \$8,545 in 1994 and \$4,995 in 1993 for doubtful accounts.....	181,805	67,830
Inventories (Note 3).....	168,643	81,654
Prepaid expenses and other.....	12,420	4,802
	-----	-----
Total current assets.....	376,976	255,847
	-----	-----
RENTAL EQUIPMENT, net of accumulated depreciation of \$23,571 in 1994 and \$23,457 in 1993.....	21,740	20,510
	-----	-----
PLANT AND EQUIPMENT:		
Land.....	30,787	1,348
Buildings.....	63,925	18,007
Machinery and equipment.....	357,228	138,235
	-----	-----
	451,940	157,590
Less--accumulated depreciation.....	357,527	115,938
	-----	-----
Net plant and equipment.....	94,413	41,652
	-----	-----
OTHER ASSETS	47,291	27,423
GOODWILL (Note 4).....	50,463	2,954
	-----	-----
TOTAL ASSETS.....	\$ 590,883 =====	\$ 348,386 =====

</TABLE>

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

SMITH INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS
LIABILITIES AND SHAREHOLDERS' EQUITY

<TABLE>
<CAPTION>

	March 31, 1994 ----- (Unaudited)	December 31, 1993 -----
	(in thousands, except share data)	
<S>	<C>	<C>
CURRENT LIABILITIES:		
Short-term borrowings and current portion of long-term debt (Note 4).....	\$ 12,812	\$ 702
Accounts payable.....	50,478	24,763
Accrued payroll and severance related costs	18,963	10,923
Income taxes payable.....	15,100	9,484
Other.....	56,361	34,098
	-----	-----
Total current liabilities.....	153,714	79,970
	-----	-----
LONG-TERM DEBT (Note 4).....	119,500	46,000
	-----	-----
DEFERRED INCOME TAXES.....	4,514	4,563
	-----	-----
OTHER LONG-TERM LIABILITIES.....	16,772	3,387
	-----	-----
MINORITY INTERESTS (Note 4).....	74,700	---
	-----	-----
COMMITMENTS AND CONTINGENT LIABILITIES		
SHAREHOLDERS' EQUITY:		
Common stock:		
Authorized-60,000,000 shares, \$1 par value; issued and outstanding- 39,317,402 shares in 1994 and 39,311,447 in 1993.....	39,317	39,311
Common stock warrants		
Class A warrants: outstanding-225,520 in 1994 and 1993.....	---	---
Class B warrants: outstanding-1,872,205 in 1994 and 1993.....	---	---
Class C warrants: outstanding-451,357 in 1994 and 1993.....	7,278	7,278
Additional paid-in capital.....	271,613	271,582
Accumulated deficit.....	(75,844)	(83,433)
Cumulative translation adjustment.....	(6,767)	(6,358)
Less-treasury securities, at cost (628,583 common shares and 451,357 Class C warrants in 1994 and 1993).....	(13,914)	(13,914)
	-----	-----
Total shareholders' equity.....	221,683	214,466
	-----	-----
TOTAL LIABILITIES & SHAREHOLDERS' EQUITY.....	\$590,883	\$348,386
	=====	=====

</TABLE>

SMITH INTERNATIONAL, INC.
 CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THE THREE MONTHS ENDED MARCH 31,

<TABLE>
 <CAPTION>

	1994	1993
	(unaudited)	
	(in thousands)	
	<C>	<C>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income from continuing operations.....	\$ 7,589	\$ 27
Adjustments to reconcile net income to net cash provided by operating activities excluding the net effects of the acquisition of M-I Drilling Fluids Company:		
Depreciation and amortization.....	3,175	5,573
Provision for losses on accounts receivable.....	660	250
Gain on disposal of fixed assets.....	(311)	(737)
Foreign currency translation.....	625	29
Change in receivables.....	(5,189)	(1,774)
Change in inventories.....	1,144	748
Change in accounts payable.....	(10,660)	(2,527)
Changes in other current assets and liabilities..	(3,374)	10,507
Changes in other noncurrent assets and liabilities.....	(204)	(1,673)
Subtotal.....	(6,545)	10,423
Net results of discontinued operations.....	---	(6,483)
Net cash provided by (used in) operating activities..	(6,545)	3,940
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of M-I Drilling Fluids Company (Note 4)..	(160,000)	---
Proceeds from sale of DDS business (Note 4).....	---	247,703
Expenses paid related to DDS sale.....	---	(17,858)
Fixed asset additions.....	(5,784)	(5,103)
Proceeds from disposal of other fixed assets.....	978	2,941
Net cash provided by (used in) investing activities..	(164,806)	227,683
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt.....	83,500	---
Net increase (decrease) in short-term borrowing.....	428	(31,787)
Repayment of long-term debt.....	---	(57,182)
Proceeds from exercise of stock options and warrants.	37	2
Dividends on preferred stock.....	---	(434)
Net cash provided by (used in) financing activities..	83,965	(89,401)
Effect of exchange rate changes on cash.....	(67)	(96)

Increase (decrease) in cash and cash equivalents.....	(87,453)	142,126
Cash and cash equivalents at beginning of period.....	101,561	16,249
	-----	-----
Cash and cash equivalents at end of period.....	\$ 14,108	\$158,375
	=====	=====

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

Cash paid for interest.....	\$ 568	\$ 918
Cash paid for income taxes.....	663	284

</TABLE>

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

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SMITH INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

FOR THE THREE MONTHS ENDED MARCH 31, 1994

(UNAUDITED)

<TABLE>
<CAPTION>

	Common Stock		Common Stock Warrants	
	Number of shares	Amount	Number of shares	Amount
	-----	-----	-----	-----
	(In thousands, except share data)			
<S>	<C>	<C>	<C>	<C>
Balance, December 31, 1993.....	39,311,447	\$39,311	2,549,082	\$7,278
Exercise of employee stock options.....	5,955	6	---	---
Net income.....	---	---	---	---
Translation adjustment for the period.....	---	---	---	---
	-----	-----	-----	-----
Balance, March 31, 1994.....	39,317,402	\$39,317	2,549,082	\$7,278
	=====	=====	=====	=====

</TABLE>

<TABLE>
<CAPTION>

	Additional Paid-in Capital	Accum- ulated Deficit	Cumulative Translation Adjustment
	-----	-----	-----
	(In thousands, except share data)		
<S>	<C>	<C>	<C>
Balance, December 31, 1993.....	\$271,582	\$(83,433)	\$(6,358)
Exercise of employee stock options.....	31	---	---
Net income.....	---	7,589	---
Translation adjustment for the period.....	---	---	(409)
	-----	-----	-----
Balance, March 31, 1994.....	\$271,613	\$(75,844)	\$(6,767)
	=====	=====	=====

</TABLE>

<TABLE>
<CAPTION>

Treasury Securities

	Number of Common Shares -----	Amount -----	Number of Warrants -----	Amount -----
		(In thousands, except share data)		
<S>	<C>	<C>	<C>	<C>
Balance, December 31, 1993.....	(628,583)	\$(6,636)	(451,357)	\$(7,278)
Exercise of employee stock options.....	---	---	---	---
Net income.....	---	---	---	---
Translation adjustment for the period.....	---	---	---	---
	-----	-----	-----	-----
Balance, March 31, 1994.....	(628,583)	\$(6,636)	(451,357)	\$(7,278)
	=====	=====	=====	=====

</TABLE>

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

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SMITH INTERNATIONAL, INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(All data with respect to the three months ended March 31, 1994 and 1993 is unaudited.)

1) NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Reference is hereby made to the Notes to Consolidated Financial Statements contained in the financial statements filed on Form 10-K for the year ended December 31, 1993. There are no significant changes in the content of those notes except as discussed below.

During the first quarter of 1993, the Company adopted two new accounting pronouncements: Statement of Financial Accounting Standard (SFAS) No. 106 "Employees' Accounting for Postretirement Benefits other than Pensions" and SFAS No. 109 "Accounting for Income Taxes". As a result of adopting SFAS No. 106, the Company recorded the total outstanding liability related to such retiree benefits of \$1.3 million as the cumulative effect of a change in accounting principle. In connection with the adoption of SFAS No. 109, the Company elected not to restate prior years' consolidated financial statements and has determined that the cumulative effect of the change in accounting for income taxes was insignificant.

Certain reclassifications have been made to the 1993 consolidated financial statements and notes in order to be consistent with current year presentation.

2) EARNINGS PER SHARE

Earnings per common and equivalent share has been computed on the basis of the weighted average number of common and equivalent shares outstanding during the three month periods ended March 31, 1994 and 1993 after deducting preferred dividends for the three months ended March 31, 1993. Earnings per share assuming full dilution is substantially the same as primary earnings per share as presented for the three months ended March 31, 1994 and 1993 except that the income from discontinued operations and net income for the first quarter of 1993 are both \$1.89 per common share.

3) INVENTORIES

Inventories consisted of the following:

<TABLE>

<CAPTION>

	March 31, 1994	December 31, 1993
	-----	-----
	(\$000 omitted)	
<S>	<C>	<C>
Raw Materials.....	\$ 21,287	\$ 10,965
Work in Process.....	29,442	13,105
Finished Goods.....	129,062	68,732
	-----	-----
	179,791	92,802
Less: reserve to state certain domestic inventories (\$72,876 in 1994 and \$70,597 in 1993) on a LIFO basis.....	(11,148)	(11,148)
	-----	-----
	\$168,643	\$ 81,654
	=====	=====

</TABLE>

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4) DISPOSITIONS AND ACQUISITIONS

Sale of Directional Drilling Business

On March 29, 1993, the Company sold its directional drilling systems and services (DDS) business and certain of its subsidiaries and other affiliates to Halliburton Company (Halliburton) for 6,857,000 shares of Halliburton common stock. In April 1993, the Halliburton common stock was sold for approximately \$247.7 million. As a result, the Company recorded income from discontinued operations during the first quarter of 1993 of \$73.6 million including the gain from the sale of the DDS business of \$80.1 million. This gain includes provisions for various fees, expenses and taxes related to the DDS sale. The DDS business reported revenues of approximately \$36.3 million in the first quarter of 1993. The Company used a portion of the proceeds of the DDS sale to repay \$102.6 million of the Company's debt and acquire additional businesses as discussed below.

Acquisitions of A-Z/Grant and Lindsey

On December 22, 1993, the Company acquired the product line assets of A-Z International, Grant Oilfield Tools and Lindsey Completion Systems (A-Z/Grant and Lindsey) from Masex Energy Services Group, Inc. for \$19.0 million in cash. A-Z/Grant and Lindsey is a leading provider of downhole tools, remedial services and liner hangers to the oil and gas industry. This acquisition was accounted for as a purchase.

The historical balance sheets of the Company at March 31, 1994 and December 31, 1993 includes the historical accounts of A-Z/Grant and Lindsey and certain purchase accounting adjustments on an estimated basis. Management has not fully evaluated all of the consequences of the acquisition of A-Z/Grant and Lindsey including assessing the fair market value of the assets acquired and the total amount of costs that may be necessary to consolidate the operations of A-Z/Grant and Lindsey with the Company. Upon completion of these evaluations during 1994, any additional adjustments will be recorded and the excess purchase price over net assets acquired, if any, will be recorded as goodwill in accordance with purchase accounting rules and principles.

Acquisition of M-I Drilling Fluids Company

Effective February 28, 1994, the Company acquired a 64% interest in M-I Drilling Fluids Company (M-I) from Dresser Industries, Inc. (Dresser) for \$160 million. M-I was owned 64% by Dresser and 36% by Halliburton prior to the acquisition. M-I is a leading provider of drilling fluids and systems to the oil and gas drilling industry. The Company purchased the 64% interest in M-I using \$80 million of its cash and issuing a note payable to Dresser for \$80 million due on August 28, 1994. This acquisition is accounted for as a purchase.

The Company refinanced the Dresser note payable in March 1994 with a \$40 million term loan from two of its insurance company lenders and a \$65 million revolving line of credit from a bank group. The term loan bears interest at a rate of 6.02 percent and is payable over a four year period ending in January 1998. The revolving line of credit is due in March 1997 and bears interest at a rate ranging from LIBOR +3/4 percent to LIBOR +1-1/2 percent based upon the debt-to-total capitalization of the Company.

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The historical balance sheet of the Company at March 31, 1994 includes the historical accounts of M-I and certain purchase accounting adjustments on an estimated basis. Management has not fully evaluated all of the consequences of the acquisition of M-I including assessing the fair market value of the assets acquired and the total amount of costs that may be necessary to reorganize the operations of M-I. Upon completion of these evaluations during 1994, any additional adjustments will be recorded and the excess purchase price over net assets acquired, if any, will be recorded as goodwill in accordance with purchase accounting rules and principles.

The summarized unaudited pro forma results from continuing operations for the three months ended March 31, 1994 and 1993 assuming the acquisitions of A-Z/Grant and Lindsey and M-I had been made on January 1, 1994 and 1993 are as follows (dollars in millions except per share amounts):

<TABLE>
<CAPTION>

	1994	1993
	-----	-----
<S>	<C>	<C>
Unaudited pro forma revenues.....	\$176.1	\$149.0
	=====	=====
Unaudited pro forma income (loss) from continuing operations.....	\$ 6.2	\$ (1.1)
	=====	=====
Unaudited pro forma income (loss) from continuing operations per common share.	\$ 0.16	\$(0.04)
	=====	=====

</TABLE>

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

Smith International, Inc. manufactures and markets a wide range of

products and services used in the drilling of oil and gas wells. The Company historically has provided technologically advanced drill bits and drilling and completion products and services to the oil and gas industry.

The decline in worldwide oil and gas drilling activity which occurred in 1992 caused the Company to reassess its future strategy from both a business portfolio and financial flexibility standpoint. Management concluded that the sale of the Company's directional drilling systems and services (DDS) business was in the best long-term interest of the Company's shareholders. This conclusion resulted in the sale of the DDS business to Halliburton Company in March 1993 for \$247.7 million in cash.

The proceeds of the DDS sale have enabled the Company to pursue its strategic growth objective and reduce its debt burden. The Company used \$102.6 million of the cash proceeds to repay debt of the Company. In addition several key acquisitions have been accomplished as part of the Company's strategic program. The purchase of the product line assets of A-Z International, Grant Oil Tools, and Lindsey Completion Systems in December 1993 will enhance the Company's Smith Drilling and Completion Services division. On February 28, 1994, the Company acquired a 64% majority interest in M-I Drilling Fluids Company, an acknowledged world leader in drilling fluid systems, from Dresser Industries, Inc. These acquisitions complement the Company's existing core products in forming one of the more complete packages of expendable products to the oil and gas drilling and production industry.

FIRST QUARTER OF 1994 COMPARED TO FIRST QUARTER OF 1993

RESULTS OF OPERATIONS

REVENUES

The products manufactured and the services provided by the Company fall into three product and service groups that are marketed throughout the world. The following table sets forth the amounts and percentages of revenues by major product group and area, as well as average rig count data:

<TABLE>
<CAPTION>

	For the Three Months Ended March 31,			
	1994		1993	
	Amount	%	Amount	%
	(dollars in millions)			
<S>	<C>	<C>	<C>	<C>
Breakdown by Product Group:				
Drill Bits.....	\$ 42.8	43%	\$ 38.3	77%
Drilling Fluids.....	37.4	37	--	--
Drilling and Completion Services....	20.6	20	11.7	23
	-----	---	-----	---
Total.....	\$ 100.8	100%	\$ 50.0	100%
	=====	===	=====	===
Breakdown by Areas:				
Domestic.....	\$ 45.1	45%	\$ 21.1	42%
Export.....	10.5	10	5.7	11
International operations.....	45.2	45	23.2	47
	-----	---	-----	---
Total.....	\$ 100.8	100%	\$ 50.0	100%
	=====	===	=====	===

Average Active Rig Count:		
Domestic.....	759	757
Canada.....	298	183
International (excluding Canada)....	750	773
	-----	-----
Total.....	1,807	1,713
	=====	=====

</TABLE>

DRILL BITS

Drill bit revenues are generated from the sale of petroleum drill bits and mining bits. Petroleum drill bit revenues increased \$4.4 million or 12.9% from \$34.2 million in the first quarter of 1993 to \$38.6 million in the first quarter of 1994 due primarily to higher sales in Canada resulting from the increase in drilling activity, improved pricing in the United States and increased sales in the Middle East and Far East. These increases were partially offset by reduced sales in Europe/Africa due to lower drilling activity and reduced sales into the former Soviet Union. Mining bit revenues increased \$0.1 million or 2.4% from \$4.1 million in the first quarter of 1993 to \$4.2 million in the first quarter of 1994 due to higher sales in Australia.

DRILLING FLUIDS

Drilling Fluids revenues represents one month's operations related to the recently acquired M-I Drilling Fluids business.

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DRILLING AND COMPLETION SERVICES

Drilling and completion services revenues increased \$8.9 million or 76.1% from \$11.7 million in the first quarter of 1993 to \$20.6 million in the first quarter of 1994. The higher revenue levels were primarily due to the acquisition of the A-Z/Grant and Lindsey product lines and increased sales volumes in the United States and Colombia.

For the periods indicated, the following table summarizes certain operating results of the Company and presents results as a percentage of total revenues:

<TABLE>

<CAPTION>

	For the Three Months Ended March 31,			
	1994		1993	
	Amount	%	Amount	%
	-----	---	-----	---
	(dollars in millions)			
<S>	<C>	<C>	<C>	<C>
Revenues.....	\$100.8	100%	\$50.0	100%
	-----	---	-----	---
Costs and Expenses:				
Cost of revenues.....	65.2	65	32.8	66
Selling expenses.....	17.9	18	8.8	17
General and administrative expenses.....	7.3	7	5.1	10
	-----	---	-----	---
Total costs and expenses.....	90.4	90	46.7	93
	-----	---	-----	---
Income from continuing operations before interest and taxes.....	10.4	10	3.3	7

Interest expense, net.....	1.0	1	2.0	4
	-----	---	-----	---
Income from continuing operations before taxes and minority interest.....	9.4	9	1.3	3
Income tax provision.....	0.9	1	--	--
	-----	---	-----	---
Income from continuing operations before minority interest.....	8.5	8	1.3	3
Minority interest.....	0.9	1	--	--
	-----	---	-----	---
Income from continuing operations...	\$ 7.6	7%	\$ 1.3	3%
</TABLE>	=====	===	=====	===

Total revenues increased by \$50.8 million from \$50.0 million in the first quarter of 1993 to \$100.8 million in the first quarter of 1994. The increase primarily reflects the acquisitions of M-I and A-Z/Grant and Lindsey. In addition, revenues increased due to higher Canadian drilling activity, improved bit pricing in the United States and increased drilling and completion services volume in the United States and Colombia. These factors were partially offset by a decrease in revenues due to lower drilling activity in the Europe/Africa region.

Gross profit increased by \$18.4 million from \$17.2 million in 1993 to \$35.6 million in 1994. The increase was due primarily to the acquisitions of M-I and A-Z/Grant and Lindsey, higher volumes in Canada, improved bit pricing in the U.S., and lower operating costs in the United States.

Selling expenses and general and administrative expense increased from \$13.9 million in 1993 to \$25.2 million in 1994 due primarily to the additional costs associated with the acquired companies and higher variable costs related to the increased revenue levels partially offset by lower legal expenses. Operating expenses as a percentage of revenues decreased from 27.8% in 1993 to 25.0% in 1994.

Interest expense decreased \$1.0 million between periods due to reduced interest expense resulting from reduced debt levels and increased interest income from short-term investments.

The tax provision of \$0.9 million in 1994 consists primarily of foreign taxes on income.

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LIQUIDITY AND CAPITAL RESOURCES

The Company's cash position at March 31, 1994, totalled \$14.1 million or a decrease of \$87.5 million from the Company's cash position at December 31, 1993. The Company's current ratio also decreased to 2.45 to 1 at March 31, 1994 from 3.20 to 1 at December 31, 1993. The decrease in cash and the current ratio was due primarily to the acquisition of the 64% interest in M-I Drilling Fluids Company for \$160 million using \$80 million of its cash and issuing a note payable to Dresser for \$80 million.

The Company refinanced the Dresser note payable in March 1994 with a \$40 million term loan from two of its insurance company lenders and a \$65 million revolving line of credit from a bank group. The term loan bears interest at a rate of 6.02 percent and is payable over a period ending in January 1998. The revolving line of credit expires in March 1997 and bears interest at a rate ranging from LIBOR +3/4 percent to LIBOR +1-1/2 percent based upon the debt-to-total capitalization of the Company. The Company has borrowing capacity under its domestic line of credit at March 31, 1994 of

approximately \$21.5 million.

The Company also has various international borrowing facilities totalling approximately \$7.0 million. The Company has borrowing capacity under its international credit facilities at March 31, 1994 of approximately \$4.2 million. The Company expects to be able to meet its ongoing working capital and capital expenditure requirements from existing cash on hand, operating cash flows and existing credit facilities.

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SMITH INTERNATIONAL, INC.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 2. CHANGES IN SECURITIES

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

The following report on Form 8-K was filed during the first quarter of 1994:

Form 8-K dated March 2, 1994; Item 2.

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SIGNATURES

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

SMITH INTERNATIONAL, INC.
(Registrant)

By: /s/ DOUGLAS L. ROCK

DOUGLAS L. ROCK
Chairman of the Board and
Chief Executive Officer

By: /S/ LOREN K. CARROLL

LOREN K. CARROLL
Executive Vice President and
Chief Financial Officer

Dated: May 13, 1994