

Energy Oil & Gas Services

Company Update Price Target Change Estimate Change

Rating: BUY
Price: \$50.06
Price Target: \$65.00
Previous: \$60.00
Bloomberg: NYSE: OIS

Market Data

52-Week Range: \$51.94-\$30.36
Total Entprs. Value (MM): \$3,023.3
Market Cap. (MM): \$2,548.1
Insider Ownership: 6.3%
Institutional Ownership: 100.0%
Shares Out. (MM): 50.9
Float (MM): 49.9
Avg. Daily Vol.: 753,601

Financial Summary

Book Value/Share: \$22.47
Net Debt (MM): \$475.2
Net Debt/Capital: 29.3%

USD	2006A	2007A	2008E	2009E
Rev. (MM)	1923.3	2088.2	2441.7	2654.6
Prev.	--	--	2410.2	2608.1
EV/Rev.	1.6x	1.4x	1.2x	1.1x
EBITDA (MM)	361.4	372.7	473.9	507.5
Prev.	--	--	458.5	494.9
EV/EBITDA	8.4x	8.1x	6.4x	6.0x
EPS				
Mar	0.92	1.05	1.31A	—
Prev.	--	--	1.16	--
Jun	0.88	0.86	0.94	—
Prev.	--	--	0.90	--
Sep	0.99	0.97	1.20	—
Prev.	--	--	1.17	--
Dec	0.98	0.95	1.26	—
Prev.	--	--	1.21	--
FY Dec	3.77	3.83	4.70	5.20
Prev. FY	--	--	4.45	5.00
FY P/E	13.3x	13.1x	10.7x	9.6x
Consensus	—	3.83	4.31	4.87

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Oil States Int'l (NYSE: OIS)

Improvement Across Product Lines Should Fuel Sharp EPS Growth

Investment Summary

We expect OIS to post rising EPS over the next few years driven by growth in the Oil Accommodations business, improving market conditions for rigs, rental tools and tubular distribution in North America and rising Offshore Products demand. Reiterate Buy and raising price target to \$65 from \$60.

Event

Posted first-quarter EPS of \$1.31, handily beating our estimate of \$1.16 (Consensus \$1.16) and well above the guidance of \$1.10-1.20.

Key Points

- **Exceptional 1Q Results** – First-quarter results handily beat expectations driven by strong performance by the oil sands accommodations business, as well as higher offshore products margins due to a favorable mix and solid execution.
- **Setting Up for Strong 2008** – Following limited growth in 2007, we believe earnings will follow an upward trajectory apart from the second-quarter seasonal weakness. We are raising our 2008 and 2009 EPS estimate to \$4.70 and \$5.20 from \$4.45 and \$5.00, respectively.
- **Good Visibility for Accommodations and Offshore Products** – A solid backlog and additional manufacturing capacity should drive another good year at Offshore Products, while continued expansion in oil sand accommodations remains a strong incremental contributor to earnings growth. The visibility from these two businesses gives us confidence in our higher 2008 estimates
- **Signs Point to Upside for Natural Gas Levered Businesses** – We expect rising North American drilling activity for the balance of 2008 and 2009, which should fuel growth for OIS' natural gas leveraged businesses, including drilling, rental tools and tubulars.
- **Raising Price Target to \$65** – We are raising our price target to \$65 from \$60 based on revised 2009 EBITDA estimates and our sum-of-parts valuation for each of the three segments.

Valuation/Risks

Our \$65 price target is based on sum-of-parts valuation. A material change in commodity prices of E&P spending could impact the demand of Oil States products and services and would likely affect pricing leverage, utilization rates and operating results.

INVESTMENT THESIS

The clouds seemed to have parted for Oil States as 2008-09 appear strong with the accommodations, offshore products and tubular services all set to benefit from healthy activity. Notwithstanding the seasonally weak second quarter, we would expect EPS to improve over the next few years as incremental contribution from the build out of the oil sands accommodations business, the new offshore products manufacturing facility and greater exposure to shale plays bear fruit. Furthermore, if the natural gas drilling activity pans out as we are expecting, the other businesses such as tubular services and rentals would be incrementally positive to late 2008/2009 results.

We are raising our price target to \$65 from \$60 based on revised 2009 EBITDA estimates and our sum-of-parts valuation for each of the three segments. Despite the recent bounce in the stock, the shares remain attractively valued with a 27% upside to our new price target.

FIRST-QUARTER RECAP

Oil States posted first-quarter EPS of \$1.31, handily beating our estimate of \$1.16 (Consensus \$1.16) and well above the guidance of \$1.10-1.20. The results compare to the fourth-quarter results of \$0.95 and \$1.05 in the year-ago quarter. Revenue of \$601.2 million beat our estimate by 1.9%, and rose 3.5% sequentially and 25.1% from a year ago. EBITDA of \$125.8 million yielded margins of 20.9%, 90 basis points above our estimate, 460 basis points higher than the fourth quarter and 50 basis points above the year-ago quarter. Not surprisingly, the oil sands accommodations business once again drove a significant portion of the sequential and year-over-year improvement as the capital investments made to expand capacity are already bearing fruit. It also appears that the cost overruns that hit the Offshore Products segment in the fourth quarter have been left behind, and smooth execution of a favorable product mix bolstered EBITDA margins to 19.0% in the quarter.

Well Site Services revenue rose 27.0% sequentially, 49.1% from a year ago to \$265.6 million, and beat our estimate by 6.7%. EBITDA of \$97.6 million yielded margins of 36.8%, 20 basis points shy of our estimate, 460 basis points above the fourth quarter, but 480 basis points below the year-ago quarter. The sequential improvement largely stemmed from the winter drilling activity in Canada, which benefited the traditional accommodations business, as well as strong utilization in the oil sands accommodations business. The rentals tools business was hit with some start-up costs from location expansion, project delays and mix following a lackluster fourth quarter. EBITDA declined on flat revenue, and results at drilling services were unfavorably impacted by lackluster utilization rates that have been flat with the prior quarter and year-ago quarter due to seasonal weakness in the Rockies offset by improvement in West Texas, and lower operating leverage.

Offshore Products revenue decreased 10.1% sequentially, but rose 6.6% from a year ago to \$126.9 million. EBITDA of \$24.1 million yielded margins of 19.0%, 200 basis points above our estimate, and 390 basis points and 180 basis points better than the prior quarter and year-ago quarter, respectively. While the sequential revenue decline was expected following fourth quarter's high level of shipments, margins surpassed expectations in the 16-18% range as the segment executed on higher margin bearing and connector products. Furthermore, the cost overruns from some drilling orders in the prior quarter were mere hiccups as margins on this quarter's drilling deliveries were back on track. Meanwhile, the 6% increase in backlog from the prior quarter to \$383.5 million continues to strengthen visibility in this business.

Tubular Services revenue slipped 9.5% sequentially, but rose 13.9% from a year ago to \$208.8 million. EBITDA of \$10.1 million yielded margins of 4.8%, in line with our estimate, 10 basis points ahead of the prior quarter and 30 basis points better than the year-ago quarter. The sequential decline was driven by a 7.2% decrease in shipments to 127,100 tons and a 2.4% drop in average revenue per ton of \$1,643 per ton. Inventory levels were down a slight 0.5% to \$190.4 million, but were 24.3% from the year-ago quarter.

Table 1: Oil States Int'l Segment Financials

	Revenue 1Q08	Pct Change from 4Q07	1Q07	EBITDA 1Q08	EBITDA Margin 1Q08	BPS Change from 4Q07	1Q07	Incremental EBITDA Margins	
								Sequential	Year-over-Year
Well Site Services	\$265.6	27.0%	49.1%	\$97.6	36.8%	462	(482)	41.8%	13.6%
Tubular Services	208.8	-9.5%	13.9%	10.1	4.8%	9	29	NM	NM
Offshore Products	126.9	-10.1%	6.6%	24.1	19.0%	390	184	NM	25.2%
Consolidated OIS	\$601.2	3.5%	25.1%	\$125.8	20.9%	463	53	32.0%	1.4%
Well Site Services									
Accommodations	146.3	59.8%	56.3%	60.9	41.6%	1,000	(13)	58.4%	NM
Rental Tools	82.5	0.2%	53.8%	25.5	30.9%	(331)	(1,056)	NM	11.2%
Drilling Services	36.8	4.4%	19.0%	11.2	30.5%	187	(1,075)	NM	NM

Source: Company Reports

EARNINGS OUTLOOK

We expect the usual second-quarter decline driven by the Canadian breakup season to negatively impact the accommodations and the portions of the rental tools businesses within the Well Site Services division, but solid rental activity in the United States coupled with better utilization rates in the drilling services business should partially offset some of the weakness. Meanwhile, 2008 should be another solid year for the Offshore Products segment with a \$384 million backlog as support, and the Tubular Services segment appears primed for a recovery as earlier (and expected) OCTG price hikes should pass easily to customers given low inventory levels and expectations for a pickup in drilling activity in the United States beginning in the back half of the year.

Management provided second-quarter EPS guidance of \$0.90-0.97 compared to our estimate of \$0.94. We are raising our 2008 and 2009 EPS estimate to \$4.70 and \$5.20 from \$4.45 and \$5.00, respectively.

Company Description

Oil States International provides specialty products and services to the worldwide oil and gas industry through three business segments-Well Site Services, Tubular Services, and Offshore Products. The company is a leading provider of remote site workforce accommodations, drilling, and tool rental; oil country tubular goods (OCTG) distribution, finishing, and logistics; and various offshore products, such as flexible bearings and connectors, subsea pipeline products, and marine winches and mooring systems. Oil States International was formed through the combination of four companies (HWC Energy Services, PTI Group, Sooner, and Oil States) and brought public in February 2001 with an initial offering of 10 million shares of common stock at \$9.00 per share.

Oil States International

Earnings Model

(dollars in millions, except per-share data)

	FY 2003	FY 2004	FY 2005	FY 2006	1Q07	2Q07	3Q07	4Q07	FY 2007	1Q08	2Q08E	3Q08E	4Q08E	FYE 2008	FYE 2009
Revenues:															
Well Site Services	\$256.1	\$336.9	\$548.8	\$657.6	\$178.1	\$149.5	\$179.7	\$209.1	\$716.4	\$265.6	\$209.2	\$231.2	\$242.2	\$948.1	\$1,001.6
Tubular Services	235.7	427.3	711.7	876.0	183.4	214.4	215.6	230.6	844.0	208.8	249.8	245.2	245.9	949.7	1,063.1
Offshore Products	231.9	206.8	271.2	389.7	119.0	135.4	132.1	141.2	527.8	126.9	137.0	135.0	145.0	543.9	590.0
Total Revenues	723.7	971.0	1,531.6	1,923.3	480.5	499.3	527.4	581.0	2,088.2	601.2	595.9	611.4	633.1	2,441.7	2,654.6
EBITDA															
Well Site Services	57.4	82.6	141.0	245.5	74.0	52.8	65.4	67.2	259.5	97.6	65.4	86.5	88.6	338.1	359.3
Tubular Services	6.6	41.8	76.7	68.6	8.4	11.3	10.2	11.0	40.8	10.1	16.2	15.9	16.0	58.3	63.8
Offshore Products	35.7	16.0	36.4	66.9	20.4	27.0	24.7	21.3	93.4	24.1	24.7	24.3	26.8	99.9	109.2
Corporate / Other	(5.8)	(8.4)	(11.5)	(19.7)	(4.9)	(5.5)	(5.7)	(4.9)	(20.9)	(6.1)	(5.5)	(5.5)	(5.5)	(22.4)	(24.8)
Total EBITDA	93.8	132.0	242.6	361.4	98.0	85.6	94.6	94.7	372.7	125.8	100.9	121.3	126.0	473.9	507.5
EBITDA Margins															
Well Site Services	22.4%	24.5%	25.7%	37.3%	41.6%	35.3%	36.4%	32.1%	36.2%	36.8%	31.3%	37.4%	36.6%	35.7%	35.9%
Tubular Services	2.8%	9.8%	10.8%	7.8%	4.6%	5.3%	4.7%	4.8%	4.8%	4.8%	6.5%	6.5%	6.5%	6.1%	6.0%
Offshore Products	15.4%	7.8%	13.4%	17.2%	17.2%	19.9%	18.7%	15.1%	17.7%	19.0%	18.0%	18.0%	18.5%	18.4%	18.5%
Total EBITDA Margin	13.0%	13.6%	15.8%	18.8%	20.4%	17.1%	17.9%	16.3%	17.8%	20.9%	16.9%	19.8%	19.9%	19.4%	19.1%
Depreciation and amortization	27.6	36.1	46.7	54.3	14.4	16.1	18.8	21.4	70.7	22.7	24.4	25.0	25.0	97.1	100.0
Interest & Other Income (Expense):															
Interest Expense	(6.6)	(7.6)	(13.9)	(19.4)	(4.8)	(3.7)	(4.2)	(5.2)	(18.0)	(5.2)	(4.9)	(4.9)	(4.9)	(19.9)	(19.0)
Interest Income	0.4	0.6	0.5	2.5	0.9	0.8	0.9	0.9	3.5	0.9	0.9	0.9	0.9	3.6	4.5
Total Interest & Other Income (Expense):	(6.2)	(7.0)	(13.4)	(16.9)	(3.9)	(3.0)	(3.3)	(4.3)	(14.5)	(4.3)	(4.0)	(4.0)	(4.0)	(16.3)	(14.5)
Pretax Income	60.0	88.9	182.5	290.1	79.6	66.5	72.4	69.0	287.6	98.7	72.5	92.3	97.0	360.5	393.0
Income Taxes	(14.4)	(29.4)	(65.3)	(98.6)	(27.2)	(22.9)	(22.0)	(20.8)	(92.8)	(32.3)	(24.6)	(31.4)	(33.0)	(121.3)	(133.6)
Tax Rate	-24.0%	-33.1%	-35.8%	-34.0%	-34.1%	-34.4%	-30.3%	-30.1%	-32.3%	-32.7%	-34.0%	-34.0%	-34.0%	-33.6%	-34.0%
Minority Interests, net of tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income From Continuing Operations	45.6	59.5	117.2	191.5	52.5	43.6	50.5	48.2	194.7	66.5	47.8	60.9	64.0	239.2	259.4
Discontinued/Extraordinary Items	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Income	45.6	59.5	117.2	191.5	52.5	43.6	50.5	48.2	194.7	66.5	47.8	60.9	64.0	239.2	259.4
Average Shares Outstanding (Basic)	48.6	49.3	49.3	49.5	49.3	49.3	49.7	49.7	49.5	49.4	49.4	49.4	49.4	49.4	48.4
Average Shares Outstanding (Diluted)	49.2	50.0	50.4	50.8	50.0	50.8	51.8	51.0	50.9	50.9	50.9	50.9	50.9	50.9	49.9
EPS - Basic	\$0.94	\$1.21	\$2.38	\$3.87	\$1.06	\$0.88	\$1.02	\$0.97	\$3.93	\$1.34	\$0.97	\$1.23	\$1.30	\$4.84	\$5.36
EPS - Diluted	\$0.93	\$1.19	\$2.32	\$3.77	\$1.05	\$0.86	\$0.97	\$0.95	\$3.83	\$1.31	\$0.94	\$1.20	\$1.26	\$4.70	\$5.20
Cash Flow	73.4	95.5	163.9	245.9	66.9	59.7	69.3	69.6	265.4	89.2	72.2	85.9	89.0	336.3	359.4
Cash Flow per Share (Diluted)	\$1.49	\$1.91	\$3.25	\$4.84	\$1.34	\$1.17	\$1.34	\$1.36	\$5.21	\$1.75	\$1.42	\$1.69	\$1.75	\$6.61	\$7.20
Capital Expenditures	42.4	60.0	83.5	154.1	36.9	64.1	71.0	68.0	240.0	61.0	70.0	70.0	70.0	271.0	125.0
Depreciation & Amortization *	27.8	36.0	46.7	54.3	14.4	16.1	18.8	21.4	70.7	22.7	24.4	25.0	25.0	97.1	100.0
Goodwill Amortization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total D&A plus Goodwill Amort.	27.8	36.0	46.7	54.3	14.4	16.1	18.8	21.4	70.7	22.7	24.4	25.0	25.0	97.1	100.0
EBITDA	93.8	132.0	242.6	361.4	98.0	85.6	94.6	94.7	372.7	125.8	100.9	121.3	126.0	473.9	507.5
EBITDA %	13.0%	13.6%	15.8%	18.8%	20.4%	17.1%	17.9%	16.3%	17.8%	20.9%	16.9%	19.8%	19.9%	19.4%	19.1%
Revenue Growth (Sequential)															
Well Site Services					12.4%	-16.1%	20.2%	16.4%		27.0%	-21.2%	10.5%	4.8%		
Tubular Services					-15.9%	16.9%	0.6%	7.0%		-9.5%	19.6%	-1.8%	0.3%		
Offshore Products					10.5%	13.8%	-2.4%	6.9%		-10.1%	7.9%	-1.5%	7.4%		
Total					-0.8%	3.9%	5.6%	10.1%		3.5%	-0.9%	2.6%	3.5%		
Revenue Growth (YOY)															
Well Site Services	22.0%	31.6%	62.9%	19.8%	-6.6%	-2.9%	16.4%	31.9%	8.9%	49.1%	40.0%	28.6%	15.8%	32.3%	5.6%
Tubular Services	8.9%	81.3%	66.5%	23.1%	-19.3%	-0.6%	0.3%	5.7%	-3.7%	13.9%	16.5%	13.7%	6.6%	12.5%	11.9%
Offshore Products	21.6%	-10.8%	31.1%	43.7%	52.1%	44.6%	20.1%	31.1%	35.4%	6.6%	1.2%	2.2%	2.7%	3.1%	8.5%
Total	17.3%	34.2%	57.7%	25.6%	-3.2%	7.8%	10.0%	20.0%	8.6%	25.1%	19.4%	15.9%	9.0%	16.9%	8.7%

Source: Company reports and Jefferies & Company, Inc.

Please see important disclosure information on pages 5 - 7 of this report.

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Page 4 of 7

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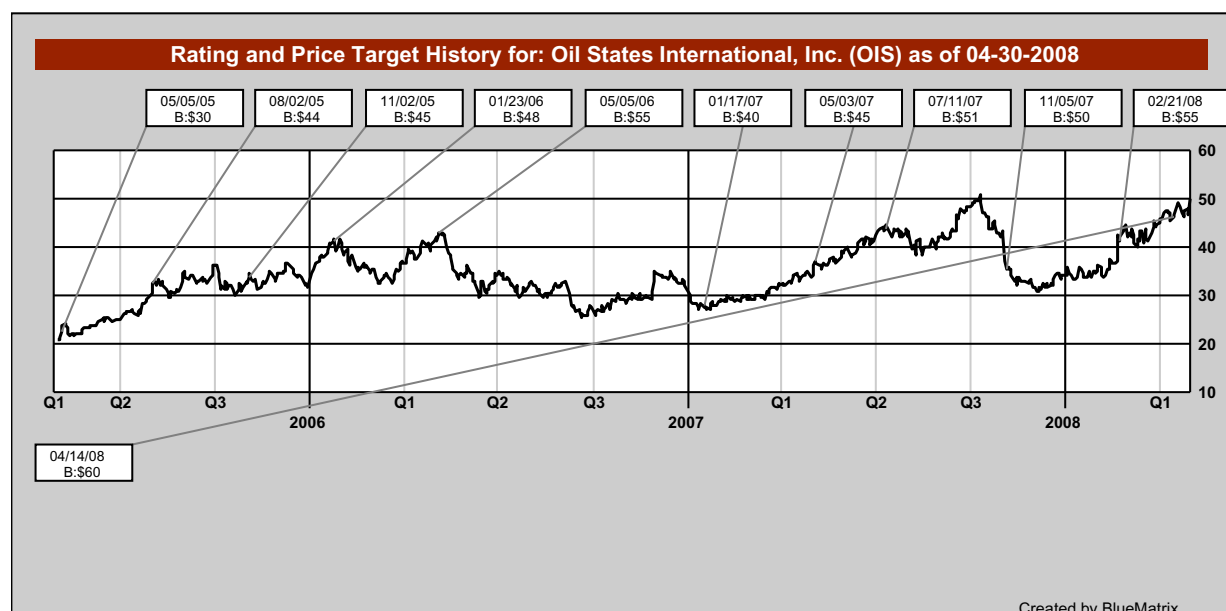
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Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY [BUY/ SB]	483	59.48	54	11.18
HOLD [HOLD]	305	37.56	27	8.85
SELL [SU/ UNPF]	24	2.96	5	20.83

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