INTRODUCTION

Smedvig asa (the "Company") is a corporation incorporated in the Kingdom of Norway. The principal executive offices of the Company are located at Finnestadveien 28, P.O. Box 110, N-4001 Stavanger, Norway.

Except as otherwise specified, all amounts in this Annual Report are expressed in Norwegian kroner ("kroner", "NOK" or "krone"). For the convenience of the reader, unless otherwise stated, translations of kroner amounts into U.S. dollars ("U.S. dollars", "$" or "U.S.$") in this Annual Report have been made at the rate of NOK 7.5800 = U.S.$1.00 (U.S.$0.1319 = NOK 1), the noon buying rate in New York City for cable transfers payable in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York (the "Noon Buying Rate") on December 31, 1998. On June 9, 1999, such rate was NOK 7.87 = U.S.$1.00 (U.S.$0.1270 = NOK 1). The Noon Buying Rate on December 31, 1998 differs from the actual rates used in the preparation of the Company's Financial Statements, and U.S. dollar amounts used in this Annual Report may differ from the actual U.S. dollar amounts that were translated into Norwegian kroner in the preparation of such Financial Statements. Translations of kroner amounts into U.S. dollars in this Annual Report should not be construed as a representation that the kroner amounts have been or could be converted into U.S. dollars at the above rates or at any other rates. See "Item 8. Selected Financial Data — Exchange Rates".

As used in this Annual Report, the following customer names refer to the companies indicated:

"Amerada Hess" — Amerada Hess Limited (a subsidiary of Amerada Hess Corp.); "Amoco" — Amoco (UK) Exploration Company (a subsidiary of Amoco Corp.); "ARCO" — Atlantic Richfield Company; "British Petroleum" — BP Norge UA or BP Exploration Operating Company Limited (subsidiaries of The British Petroleum Company plc); "CMS NOMECO" — Walter International Congo Inc. (a subsidiary of CMS NOMECO Oil & Gas Co.); "Elf" — Elf Aquitaine SA; "ENSCO" — ENSCO International Incorporated; "Esso" — Esso Exploration and Production Norway AS or Esso Production Malaysia Inc. (subsidiaries of Exxon Corp.); "Mobil" — Mobil Exploration Norway Inc. (an affiliate of Mobil Corporation); "Navion" — Navion ASA, (a subsidiary of Statoil); "Norsk Hydro" — Norsk Hydro Produksjon a. s. (a subsidiary of Norsk Hydro ASA); "Petronas" — Petronas Carigali Sdn. Bhd. (a subsidiary of Petroliam Nasional Bhd.); "Phillips Petroleum" — Phillips Petroleum Company Norway (a subsidiary of Phillips Petroleum Co.); "Schlumberger" — Schlumberger Norge AS; "Shell" — Brunei Shell Petroleum Company Sdn Bhd or Shell Deepwater Development Inc. or Sarawak Shell Berhad or Sabah Shell Petroleum Company Limited (subsidiaries of Royal Dutch Petroleum Co.); "Statoil" — Den norske stats oljeselskap a.s or Statoil (Thailand) Limited; "Thaipo" — Thaipo Ltd. (a subsidiary of Pogo Producing Company); "TOTAL" — TOTAL Exploration and Production Thailand (a subsidiary of TOTAL S.A.); and "Unocal" — Unocal Thailand, Ltd. (a subsidiary of Unocal Corp.).

PART I

ITEM 1. DESCRIPTION OF BUSINESS.

General

The Company is an offshore drilling contractor headquartered in Stavanger, Norway. The Company owns and operates a fleet of high specification drilling rigs for offshore oil and gas exploration and development, which are equipped for operations in harsh environments. The Company's primary activities are located in the Norwegian Sector of the North Sea and Southeast Asia (principally offshore Thailand, Brunei and Malaysia). Smedvig's fleet of mobile drilling units consists of one fourth-generation and two third-generation semi-submersible drilling rigs and one ultra-large jack-up rig, all of which are equipped for operations in harsh environments. The Company operates its fleet under long-term contracts in the Norwegian shelf of the North Sea. One fifth-generation semi-submersible drilling rig and one drillship are under construction. These units are being constructed as deepwater drilling units and are expected to be among the most advanced units ever developed. The Company also provides platform drilling services, well services and well maintenance services on fixed platforms in the Norwegian Sector of the North Sea. The Company operates the world's largest fleet of self-erecting tender rigs, primarily in Southeast Asia. The fleet consists of eleven units (ten of which are wholly or partially owned by the Company), including two semi-submersible tender drilling rigs. One of the semi-submersible tender rigs, which was under construction in 1998, was delivered in March 1999. The Company also provides innovative and technologically advanced well construction services and reservoir and well technology products and services to the offshore oil and gas industry worldwide through its Reservoir and Well Technology Division, which is being merged with Multi-Fluid ASA, a company listed on the Oslo Stock Exchange ("Multi-Fluid"), during 1999. See "—Recent Developments".

Historical Developments

The history of the Smedvig group dates back to 1915, when the Peder Smedvig Shipping Company was established. The Smedvig group entered the offshore oil and gas market by investing in an exploration company in 1965, at the start of offshore exploration and production activities in the North Sea. In 1973, further investment in the offshore market was made through the design, development and construction of the first Norwegian-flagged semi-submersible drilling unit, West Venture. The Smedvig group expanded its drilling business with the construction of the West Vanguard in 1982 and the West Vision in 1986 and by purchasing one of the largest operators of mobile drilling units in Norway in 1988. In 1989, the Company was organized to hold all of the Smedvig family's offshore drilling and oil services businesses. In a private placement followed by a listing on the Oslo Stock Exchange in 1990, the Smedvig family's interest in the Company was reduced to approximately 49 percent. In November 1996, the Company increased its equity capital through a U.S.$143 million stock offering to U.S., Norwegian and international investors, and by a listing of the Company's shares on the New York Stock Exchange. The Smedvig family sold one million shares in connection with the equity offering. In 1998, the Smedvig family purchased 425,300 Class A shares and currently owns approximately 39.7 percent of the outstanding voting shares and 30.2 percent of the equity capital of the Company. See "Item 4. Control of Registrant". Today, the Company operates independently from the other Smedvig family businesses.

In 1990, the Company increased its international presence by acquiring Robray Offshore Drilling Company Ltd. (the predecessor to Smedvig Asia Ltd.), a tender rig company headquartered in Singapore. The Company sold three of its tender rigs in 1991 and one additional tender rig in 1994 to Varia Perdana Sdn. Bhd. ("Varia Perdana"), a Malaysian company established under a joint venture between the Company, which owns a 49 percent interest, and an entity controlled by the Renong Group, a Malaysian industrial group. In February 1997, the Company enhanced its presence in the developing Southeast Asian market through the acquisition of Petrodril Holdings, Inc. ("Petrodril"), the owner of one tender rig and one semi-submersible tender drilling rig. In January 1998, the Company signed an agreement to build an advanced semi-submersible tender rig against a five-year operating contract in Southeast Asia. The unit was delivered in March 1999.

In mid-1994, the Company, in response to perceived changes in the market for mobile drilling units, made a strategic decision to concentrate on the upper-end of the worldwide offshore drilling market. As a result, the

Company restructured its semi-submersible and jack-up rig fleet and focused on those assets that are equipped for harsh environments, which require more advanced equipment and technological solutions. As a part of this restructuring, the Company sold four of its smaller jack-up rigs and one older semi-submersible rig and acquired a 50 percent (now 52.4 percent) interest in West Alpha, its fourth-generation semi-submersible drilling rig, and the remaining 50 percent interest in West Delta, a third-generation semi-submersible drilling rig. In 1997, the Company ordered a fifth-generation semi-submersible drilling rig and two deepwater drillships, all contracted against five year or longer operating contracts with major oil companies. In August 1998, the Company terminated the construction project for one of these drillships with the consent of the operator. See "—Recent Developments". The remaining drilling units under construction are expected to be among the most technologically advanced drilling units developed to date.

In 1994, the Company decided also to broaden its range of technology products and services both to complement its well construction services and to become a significant supplier of reservoir and well engineering technology. In pursuit of this strategy, between 1995 and 1997, the Company acquired six reservoir software and management companies and a drilling engineering company, which it combined under the name Smedvig Technologies to offer reservoir technology products and services.

In 1991, due in part to its belief that mobile production solutions represented a growing new business opportunity, the Company acquired an interest in a mobile production unit. Mobile production solutions capitalize on advances in floating production technology which have reduced the capital requirements for, and lead time in, developing certain offshore oil and gas projects, such as those in remote locations or in deep water. The Company increased its involvement in this developing market in 1994 by committing to design, build and market the Balder FPU, which was subsequently sold to Esso. Lately, this market has experienced increasing competition with the entry of new market participants, resulting in reduced profit margins. In 1997, the Company decided to refrain from further investments in mobile production solutions. In April 1998, the Company decided to discontinue its mobile production activities in response to deteriorating market conditions, low profitability and Esso's termination of the Balder contracts. See "—Activities To Be Discontinued".

The Company performs drilling and maintenance services on fixed platforms in the North Sea. In November 1998, pursuant to the Company's decision to concentrate on geographic markets in which it has a large business volume, the Company sold its platform drilling operations on the British Continental shelf, where the Company only offered platform drilling services. The Company intends to maintain its leading position in the Norwegian sector of the North Sea.

Recent Developments

Since 1997, the Company has experienced significant cost increases and delays for its newbuilding project, the West Navion, a deepwater drillship (formerly known as West Navion I), and significant delays for its newbuilding project, the West Venture (formerly known as West Future II), a fifth-generation semi-submersible drilling rig.

In May 1999, the Company announced further increases in the total capital expenditure and further delivery delay for West Navion. Revised total cost estimate is in the range of U.S.$560-600 million, depending on the final completion date. Under the revised project schedule, the delivery of West Navion is expected during the fourth quarter of 1999. However, there are still uncertainties related to delivery and commissioning of certain critical components. This includes the blow-out preventer and final commissioning of the Ramrig drilling package.

In June 1999, after negotiations with Statoil, the five-year drilling contract for the West Navion was replaced by a one-year contract. Terms and conditions for the new contract are substantially the same as for the original contract. The reason for the reduction in contract duration was the delayed delivery schedule for the drillship. At the same time, the Company's partner Navion ASA, a subsidiary of Statoil formerly known as Statoil Shipping & Maritime Technology ("Navion"), which owns 50 percent of the West Navion, notified the Company that they reserve their right to seek compensation from the Company for Navion's portion of the cost overruns related to the construction and outfitting of the drillship. The Company believes that such claim would be groundless.

In April 1999, the Company, following a comprehensive and detailed review of the project, announced that the delivery of West Venture, which was ordered in 1997, will be further delayed because the shipyard responsible for the completion and delivery of the rig has experienced delay in the execution of the project. The Company also announced that the delay will result in a further 5 percent cost increase due to time-related project management and financing costs.

In March 1999, the Company agreed to merge Smedvig Technologies (Holding) AS ("Smedvig Technologies"), the Company's subsidiary holding the assets, rights and liabilities of the Company's Reservoir and Well Technology Division, with Multi-Fluid, a Norwegian company listed on the Oslo Stock Exchange. The primary business of Multi-Fluid is the production of multiphase flow-meters for the oil industry. Multi-Fluid will be the surviving entity and will be renamed ROXAR ASA. The merger agreement provided for an exchange ratio whereby the Company would own 57 percent of the merged company and Multi-Fluid shareholders would own 43 percent. Prior to completion of the merger, the Company has proposed to distribute approximately 30 percent of the shares of Smedvig Technologies through a dividend distribution to the Company's shareholders. Thus, the Company will have less than 50 percent ownership interest in the merged company, which will not be consolidated as a subsidiary of the Company but will be reported as an associated company in the Company's financial statements as of May 11, 1999. Shareholders of the Company will vote on the distribution at the extraordinary general meeting to be held on August 17, 1999. The merger was approved by the general meetings of Multi-Fluid and Smedvig Technologies in May 1999. The merger is expected to be completed in August 1999 and will be accounted for as a pooling of interests.

The Company believes that the strategic initiatives over the past year (exit from mobile production, termination of the West Navion II drillship, sale of the UK platform drilling activities and spin-off of the reservoir and well technology activities) will allow the Company to focus on its core business competencies, including mobile drilling units, tender rigs and platform drilling in the Norwegian and Southeast Asian niche markets.

In March 1999, Christian Bull Eriksson was appointed new Chief Executive Officer of the Company. Mr. Bull Eriksson joined the Company on June 7, 1999.

Business Strategy

The Company's goal is to strengthen its position in the technologically advanced segment of the offshore drilling industry by building on its solid market position in the Norwegian sector of the North Sea and Southeast Asia.

The Company's activities are focused on well construction, well services and reservoir technology.

The Company pursues a strong earnings-driven growth strategy by offering innovative and cost-efficient solutions to the oil and gas industry.

The Company seeks to achieve its profit and growth targets through organic growth and selected investments and acquisitions.

The Company is committed to serving its customers with a strong market presence, a sound technology base and understanding of client needs.

The Company prefers long-term contracts and business relationships with its customers.

The Company aims at delivering products and services with a consistently high level of quality, efficiency and safety in all its operations.

Industry Overview

The market for offshore drilling and oil services is fundamentally driven by the exploration, development and production expenditures of oil and gas companies and the availability of offshore drilling units. Industry exploration, development and production expenditures depend on the cash flow of oil and gas producers, which is primarily determined by oil and gas prices and production volumes. Oil and gas prices are influenced by a variety of political and economic factors beyond the control of oil and gas companies, including worldwide demand for oil and gas, production levels, governmental policies regarding exploration and development of reserves, political factors in producing countries and weather conditions.

During the last decade, the offshore drilling and oil services industry has seen a number of restructurings, consolidations and mergers which were driven in part by overcapacity, low margins and the need for greater cost efficiencies.

Increasing focus by the oil and gas companies on reducing their costs has had important implications for the offshore drilling and oil services business. Some of the oil and gas producers have been redefining the core areas of their businesses and have downsized their organizations in order to concentrate their resources, maximize returns from existing assets and focus on finding and developing new reserves. As a result, oil and gas producers are increasingly outsourcing responsibility for certain field exploration, development and production activities, including responsibility for the commercial and technical aspects of development and operation. This has created new opportunities for the offshore drilling and oil services sector.

In 1995, 1996 and early 1997, the economic fundamentals of the offshore drilling and oil services industry improved considerably, due in part to favorable oil and gas prices. Exploration, production and development expenditures increased, and the search for reserves in deep water and harsh environments, combined with the development of marginal fields, has increased demand for and utilization of high quality semi-submersible and jack-up drilling rigs. This resulted in higher dayrates for rigs. Other trends having a positive impact on the offshore drilling and oil services sector include technological innovation and the opening of new areas for exploration. Since October 1997, oil prices have been declining and in late 1998, oil prices were at their lowest in this century in real terms. This led oil companies to defer their exploration programs and cut back on planned investments. So far these reductions have mainly affected lower specification drilling units under short-term contracts. However, a sustained low oil price is expected to have a negative impact on drilling services in general. This could also lead to pressure from oil companies to modify or amend existing contractual terms. The Company's near term prospects are not expected to be significantly affected by the current market pessimism. This comes as a result of the Company's strategy of entering into long-term contracts when the market is strong. As of December 31, 1998, the Company had an average remaining contract length of approximately three years for its mobile drilling units and approximately two years for its tender rigs. This is expected to provide a strong and stable cash flow in the years ahead and will limit to some extent the Company's exposure to changes in oil industry activity levels.

Technological Innovations

Technological innovations in the offshore drilling and oil services sector have improved oil and gas exploration success rates, lowered the cost of exploration and production and increased demand for services in many phases of an oil and gas field's development. Specifically, advances such as three-dimensional (3-D) seismic surveying techniques, complex reservoir modeling and simulation techniques and advanced reservoir monitoring techniques have reduced exploration and reservoir-related risks and improved well design and operating efficiency. Extended-reach directional and multilateral drilling techniques and improved secondary and tertiary recovery techniques have greatly increased recovery from existing fields. Technologies such as ultra deepwater wellheads, umbilicals and flowlines and subsea well completions have allowed operators to access deepwater fields that were technically unfeasible a few years ago. Advances in mobile production technologies and subsea developments have reduced the capital requirements for developing certain offshore oil and gas projects, such as those in remote locations or in deep water and can significantly reduce the time from discovery to first production from such fields.

These technological innovations have been driven, in part, by the need to facilitate exploration for and development of new reserves and large fields in remote deepwater and harsh-environment offshore regions and by the need to permit development and production of commercially marginal fields and extend production from existing fields. The Company believes that the development and improvement of these various enabling technologies (i) have positively affected long-term demand for offshore drilling and related services such as those provided by the Company, particularly in remote locations, deepwater or harsh-environment geographies, and (ii) have contributed to the trend towards allocating more spending for development drilling. Development drilling is less sensitive to industry cycles than exploration drilling since the oil companies which develop a field have already made an initial investment in the exploration of such field and they are granted permits or concessions of limited duration. At the same time, technological advances have reduced the capital investment required for finding and developing reserves on a per barrel basis.

Additionally, technological developments have reduced the cost of developing offshore oil and gas fields, and smaller fields that previously would have been too costly to develop have become viable. Consequently, oil and gas producers have increased their offshore development and production activities, particularly for projects within reach of existing infrastructure, in order to exploit fully known resources.

Rig Dayrates

As expenditures by the oil and gas industry for exploration, development and production increased, the demand for drilling rigs and worldwide utilization of the available rigs rose, leading to significant increases in dayrates from 1995 to early 1998. Since early 1998, however, dayrates for new contracts have declined as a result of lower oil prices that adversely affected the oil companies' capital expenditures. Over the past two years, the number of rigs under construction or conversion has increased somewhat as a result of increased demand.

In line with its strategy, the Company entered into long-term contracts for its drilling units during the period of increasing dayrates and the Company is benefiting from this strategy in the current market where rates have decreased.

After a decline in dayrates for tender rigs in Southeast Asia during 1995 and 1996, dayrates improved in 1997 and first quarter of 1998. Since the first quarter of 1998, however, dayrates in this region have declined as a result of the effect of lower oil prices on oil companies' expenditures as well as competition from small jack-up rigs.

Outlook

The Company believes that the long-term outlook for offshore drilling remains good, particularly in the deepwater market. In order to maintain their reserves, the oil and gas companies need to increase their spending on exploration drilling from mobile units in deeper waters and outside existing infrastructure, which, if successful, will further increase the demand for mobile units to perform developments drilling. The Company's short-term prospects are not expected to be significantly affected by the current market pessimism due to the Company's strategy of entering into long-term contracts when the market is strong. At December 31, 1998, the Company had an average contract length of approximately three years for its mobile drilling units and approximately two years for its tender rigs. The Company believes this should provide a strong and stable cash flow during the next two to three years and should limit the Company's exposure to changes in oil industry activity levels. The drilling units under construction West Navion and West Venture, have a one-year contract and a long-term contract, respectively.

The Platform Drilling Division is engaged in production drilling and maintenance operations from existing installations, and it is therefore less sensitive to changes in oil prices.

The Company believes that it is well positioned despite the current cyclical downturn in the market. Upon completion of its newbuilding program, the Company will have a large fleet of high specification drilling units, all of which are under contracts.

The Company's key priorities are to complete and deliver its newbuildings, in accordance with delivery schedules and cost estimates, and commence drilling under the contracts. The Company aims at maintaining profitability, safety and efficiency in ongoing operations.

For the Company's cautionary statement relating to the forward looking statements contained in this document, see "—Industry and Operating Risks".

The Company's Business Divisions

At December 31, 1998, the Company had five business divisions. The business divisions were Mobile Units, Platform Drilling, Tender Rigs, Reservoir and Well Technology and Activities To Be Discontinued. In March 1999, the Company agreed to merge Smedvig Technologies (that constitutes its Reservoir and Well Technology Division) with Multi-Fluid, a Norwegian public company. The Company will have less than 50 percent ownership interest in the merged company, which will not be consolidated as a subsidiary of the Company but will be reported as an associated company in the Company's financial statements as of May 11, 1999. See "—Recent Developments". During 1996, 1997 and 1998, operations in the North Sea provided approximately 84 percent, 81 percent and 80 percent, respectively, of the Company's revenues and accounted for approximately 79 percent, 89 percent and 75 percent, respectively, of the Company's operating profit before gains on sale of assets. The rest of the world, principally Southeast Asia, provided approximately 16 percent, 19 percent and 20 percent of such revenues in 1996, 1997 and 1998, respectively. Excluding gains on sale of assets, approximately 82 percent, 82 percent and 78 percent of the Company's North Sea revenues and almost all of its North Sea operating profit were attributable to Norway in 1996, 1997 and 1998, respectively.

Mobile Units Division

The Company's strategy for its Mobile Units Division is to offer innovative and cost-effective services encompassing drilling, completion and maintenance of offshore wells in deep waters and harsh environments. The Company intends to maintain high utilization of its drilling units through long-term contracts, thereby ensuring a stable cash flow. The Company is thus less exposed to market fluctuations and has laid the basis for long-term investment and growth. In line with this strategy, the fleet is concentrated on high specification drilling rigs, all of which are employed under long-term contracts, mainly in production drilling. The Company emphasizes high quality operations, stressing safety, health, efficiency and environmental considerations. The Company's drilling capacity is being expanded by the construction of advanced drilling units for efficient exploration and production drilling in deep waters and harsh environments.

As of December 31, 1998, the Company's mobile drilling rig fleet consisted of the three semi-submersible drilling rigs, West Alpha, West Delta and West Vanguard, and the jack-up rig, West Epsilon. All the rigs are employed in the Norwegian sector of the North Sea, and are engaged mainly in production drilling.

The fourth-generation rig West Alpha continued drilling production wells under a contract with Esso Norge on the Balder field throughout the year. This assignment was completed in December 1998. The rig then started on a three-year drilling contract with Amoco, and was sublet to Statoil for drilling of two wells on the Statfjord field. The rig is currently being classified and upgraded during a yard-stay in Norway, expected to be completed before the end of June 1999.

The third-generation rigs West Delta and West Vanguard continued exploration and production drilling for Norsk Hydro throughout the year. The West Delta drilled production wells on the Visund field until a three-week yard- stay in the third quarter for upgrades and modifications. Thereafter, the rig drilled two exploration wells on the Oseberg field before being moved to Oseberg Syd to start a production drilling program expected to last 15 months.

The West Vanguard operated on the Troll and Oseberg fields. In the second quarter, this rig completed the drilling of a record-long 3,200 meter horizontal section of a well on the Troll field. Following a three-week yard-stay in the third quarter for upgrades and modifications, the rig was engaged in drilling and well maintenance operations on the Oseberg field. The rig returned to the Troll field at the end of the year, where the operator's plans call for its use in production drilling for two-to-three years in connection with Troll Phase II.

The West Epsilon drilled production wells for Statoil on Sleipner Vest during the year. This activity will continue until summer 1999. The drilling program for the remaining contract period until December 2002, has not yet been decided.

Operation of the Company's mobile units has proceeded satisfactorily during the year, yielding record operating profits. The quality of these operations has improved over the year as a result of systematic planning with an emphasis on safety, quality and efficiency, and a continuous modernization and improvement of the rigs.

In 1997 and 1998, the Mobile Units Division accounted for approximately 32 percent and 31 percent of the Company's revenues (excluding gains on sale of assets), respectively.

The newbuilding program for mobile units consists of a deepwater drillship, the West Navion, and a fifth-generation semi-submersible rig, the West Venture (formerly known as West Future II). These drilling units will be among the most advanced ever built.

Semi-submersible rigs consist of an upper working and living quarters deck resting on vertical columns connected to lower hull members. Such rigs operate in a "semi-submerged" position, remaining afloat, off bottom, in a position in which the lower hull is below the water line and the upper deck protrudes high above the surface. The rig is typically anchored or dynamically positioned and remains stable for drilling in the semi-submerged floating position, due in part to its wave transparency characteristics at the water line.

In 1996, the Company, in close cooperation with Norsk Hydro, developed a new fifth-generation semi-submersible drilling rig concept intended for efficient development drilling in deep water and harsh environments. In February 1997, the Company ordered West Venture, a semi-submersible drilling rig designed for operations in deep water and harsh environments, on the basis of a long-term contract with Norsk Hydro. The rig will be one of the world's first fifth-generation rigs, and is to be provided with dual drilling derrick, full dynamic positioning system and a deep water capability of 1,500 meters. Its drilling efficiency is expected to surpass that of existing drilling rigs. The rig is under construction at the Hitachi yard in Japan, and is approximately 86 percent completed. The shipyard has indicated that there will be delays, and the Company estimates delivery to take place in the fourth quarter of 1999. As a result, the contract has been shortened by approximately nine months. Estimated financial and project management costs have increased due to the delayed delivery schedule, and total project costs for the Company are estimated to be approximately U.S.$315 million, up from an original estimate of U.S.$280 million.

Drillships are ships equipped for drilling and are typically self-propelled and move from one location to another under their own power. Drillships are positioned over the well through use of either an anchoring system or computer controlled thruster system similar to those used on semi-submersible rigs. Certain drillships are capable of drilling in water depths of more than 6,000 feet.

In 1997, the Company entered into agreements with Navion for the construction of two deepwater drillships against long-term contracts. The Company currently has one drillship under construction, the West Navion (formerly known as West Navion I). In February 1998, the hull of the deepwater drillship West Navion was delivered from the Korean shipyard Samsung. West Navion is owned by Navion and the Company, each with a 50 percent ownership interest. The Company will also be responsible for operating the drillship. The vessel is being equipped with drilling equipment at the Offshore & Marine yard in Norway, and will have a dual drilling derrick, full dynamic positioning, a high deck load capacity and a deepwater drilling capability of initially 1,500 meters, which may be increased to 2,500 meters. After delivery, the vessel will be employed under a one-year operating contract with Statoil. From the outset, the complexity and time frame of the project have been considerably underestimated. The project costs have significantly increased and the delivery schedule has been delayed. The increase in estimated costs is due to various factors, including design modifications, weight increases, delayed delivery of equipment, higher water depth capacity than originally planned for, as well as tight time schedules. All the modules have now been installed, and the vessel is approximately 88 percent completed. The current developments indicate further increases in total man-hours required to complete the vessel as well as delayed delivery. In spring 1999, a review was undertaken and the review revealed additional cost increases and delayed delivery of the vessel. The revised total cost estimate is in the range of U.S.$560-600 million, depending on the final completion date. The revised project schedule implies delivery during the fourth quarter. However, there are still uncertainties related to delivery and commissioning of certain components. This includes the blow-out preventer and final commissioning of the Ramrig drilling package. The original cost estimate was approximately U.S.$250 million. The revised total project costs estimate includes all construction costs, interest expenses, project management, contingencies and operational preparations. See "—Recent Developments".

In May 1998, the Company completed a comprehensive review of the costs, delivery schedules and project management of all of its newbuilding projects. The review resulted in increased cost estimates and delayed delivery schedules for the drillship newbuildings. As a result, the Company implemented corrective actions to improve performance and reduce its risk exposure. See "—Industry and Operating Risks".

In August 1998, Navion and the Company decided to terminate their jointly owned construction project for the drillship West Navion II, due to major uncertainties regarding the total construction costs and anticipated delivery date. This decision was made with the consent of the operator, Shell. The Company's share of the costs associated with the termination amounted to NOK 535 million. Navion, which owned 50 per cent of the vessel, bore the remaining portion of such costs.

Jack-up rigs are mobile, self-elevating drilling platforms equipped with legs that are lowered to the ocean floor. A jack-up rig is towed by tugboats to the drillsite with its hull riding in the sea as a vessel and its legs raised. Once over a drillsite, the legs are lowered until they rest on the seabed, and jacking continues until the hull is elevated above the surface of the water. After completion of drilling operations, the hull is lowered until it rests in the water, and the legs are then raised for the rig to be relocated to another drillsite. The Company has one jack-up rig, West Epsilon, which is one of the world's largest and most advanced jack-ups, is capable of drilling at water depths of up to 380 feet and is outfitted for operations in harsh environments.

The following table sets forth certain information concerning the Company's mobile drilling units, including units currently under construction:

Mobile Drilling Units

Type and Name	Ownership Percent	Maximum Water Depth Capability(ft)	Variable Deck Load (MT)	Attributes	Year Built/ Latest Enhancement	Current Location/ Customer	Estimated Contract Expiration
Semi-submersibles							
West Venture (fifth-generation)	100.0%	5,000	5,500	DP, DD, TDS, 4M 15K	1999	Under construction/Norsk Hydro	1st quarter 2004 (1)/Options for further seven years
West Alpha (fourth-generation)	52.4	2,300	3,000	SP, TDS	1986/96	Norway/Amoco	February 2002 (2)
West Vanguard (third-generation)	100.0	1,480	2,000	SP, TDS	1982/85	Norway/Norsk Hydro	April 2001/Option until March 2006
West Delta (third-generation)	100.0	1,480	2,000	SP, TDS, 3M, 15K	1981/97	Norway/Norsk Hydro	March 2000/Option until December 2000
Drillships							
West Navion	50.0	8,200	7,500	DP, DD, 3M, TDS, 15K	1999	Under construction/ Statoil	December 2000 (3)
Ultra-large Jack-up							
West Epsilon	90.1	380	3,700	IC, SO, TDS, 3M, 15K	1992/95	Norway/Statoil	December 2002/ Options to June 2006

Attributes

DP = Dynamic Positioning	IC = Independent-Leg Cantilevered Rig	SP = Self-Propelled	4M = Four Mud Pumps
DD = Dual Derrick	SO = Skid-Off Capability	TDS = Top-Drive Drilling System	3M = Three Mud Pumps
			15K = 15,000 psi Blow-Out Preventer

(1) Estimated start-up is the fourth quarter of 1999.

(2) A two month yard stay is being undertaken in the second quarter of 1999, resulting in the contract with Amoco being extended by two months to February 2002.

(3) Estimated contract start-up is December 1999.

The Company generally seeks to secure long-term contracts for its mobile drilling units under favorable market conditions that allow for attractive fixed and incentive type dayrates structures. The Company's contracts for mobile drilling units provide for a basic drilling dayrate, and some provide for a lower or zero dayrate during periods of mobilization or when drilling operations are interrupted or restricted by equipment breakdowns, adverse environmental conditions or other conditions beyond the control of the Company. The contracts also contain clauses pursuant to which the customer assumes responsibility for all or a substantial part of any changes in personnel, insurance or other costs, subject to certain limitations.

The initial terms of the Company's current mobile drilling contracts generally expire on the expiration date specified in the table above, which may be extended by the customer through the exercise of options provided in the contracts. Actual contract durations may vary depending on the number of wells involved and the time required for the particular drilling project. The contracts may be terminated by the customer in the event the drilling unit is destroyed or lost, or if drilling operations are suspended for a specified period of time as a result of a major equipment breakdown resulting from events beyond the control of either party. Under some contracts, the customer can also terminate at any time without cause, subject to the payment of certain termination fees which are generally intended to minimize the financial impact of such termination on the Company. Under certain of the operating contracts for the units under construction, the customer has the right to terminate the operating contracts if the Company fails to satisfy its contractual obligations, including its obligation to deliver such unit at a specified time.

Upon the expiration of existing contracts, there can be no assurance that such contracts will be renewed or extended, that new contracts will be available or, if contracts are available, that they will provide revenues adequate to cover all fixed and variable costs associated with the rigs.

The following table sets forth certain information comparing the Company's rig utilization to that of the offshore drilling industry as a whole during the past five years:

Mobile Drilling Fleet Utilization (1)

	Averages for Year Ended December 31,									
	1994		1995		1996		1997		1998	
	Company	Industry	Company	Industry	Company	Industry	Company	Industry	Company (2)	Industry
Fourth-Generation Semi-submersibles (3)										
Supply	1.0	13.7	1.0	14.2	1.0	17.1	1.0	17.9	1.0	23.9
Utilization	0%	91%	84%	99%	61%	98%	100%	100%	100%	94%
Other Semi-submersibles (3)										
Supply	2.0	106.8	2.0	101.0	2.0	104.0	2.0	107.9	2.0	107.1%
Utilization	67%	80%	87%	88%	79%	95%	92%	98%	100%	95%
Total Semi-submersibles (3)										
Supply	3.0	120.5	3.0	115.2	3.0	121.1	3.0	125.8	3.0	131.0%
Utilization	45%	81%	86%	89%	73%	95%	94%	98%	100%	95%
Jack-ups (4)										
Supply	6.0	299.8	2.9	294.1	2.0	284.2	2.0	289.8	2.0	294.8%
Utilization	65%	83%	96%	86%	100%	94%	100%	97%	100%	92%

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(1) Company data for each period is based on all rigs operated during such period. Industry statistics of rig utilization are from Offshore Data Services. Company and industry statistics have been determined under the "working method," which is the ratio of the number of rig days in operation to the total number of rig days available. Total supply for each period includes only actively marketed rigs, i.e., excludes national oil company-owned and mothballed rigs, among others. Industry data is based upon competitive rigs (as defined by Offshore Data Services) of the types indicated and includes many rigs that may be dissimilar to the Company's rigs in many significant respects, including performance capabilities, age, operational criteria and environmental capabilities.

(2) Under the "revenue method," which is the ratio of the contractual revenue actually generated to the maximum potential revenue obtainable pursuant to the operating contract, in 1998, the utilization rates for the Company's fourth-generation semi-submersible, other semi-submersibles, total semi-submersibles and jack-ups were 97 percent, 96 percent, 96 percent and 98 percent, respectively.

(3) The Company's fourth generation rig, West Alpha, was not employed during 1994 and was being mobilized and upgraded in connection with the Esso contract during the majority of the first half of 1996. West Delta was mobilized and upgraded in the second half of 1996 and the first two months of 1997 in connection with a new contract.

(4) Includes both shallow (less than 350 feet maximum depth capability) and deepwater (over 350 feet) jack-up rigs. Company data includes ENSCO 100, which has been operated as a water injection platform by the former Mobile Production Division since April 1994 and Activities To Be Discontinued since January 1, 1998.

Platform Drilling Division

Oil and gas fields in the North Sea have traditionally been developed through the use of permanently installed drilling and production platforms, with the drilling operations being performed by a drilling contractor such as the Company. However, the current trend favors floating production techniques and subsea production systems that require mobile drilling rigs for well construction. Thus, demand for traditional platform drilling services is expected to decrease gradually in the future. In order to maintain and expand its activities in this market, the Company's strategy is to broaden its traditional offering of drilling and maintenance services. Other offered services include wireline operations (described below) and services related to the shut-down of production wells, markets in which the Company sees a growth potential.

In connection with the discontinuation of the Mobile Production Division in the spring of 1998, the remaining operations, including the Janice Alpha, three production operations contracts and certain consulting services, were included under the Platform Drilling Division as of January 1, 1998.

In the fourth quarter of 1998, the Company sold its platform drilling operation in the British continental shelf, the operating contract for the Janice Alpha and the company Altra Consultants Limited to Deutag AG, a German company ("Deutag"). The sales price was NOK 340 million with a sales gain of NOK 165 million. The sale was motivated by a strategic decision to concentrate operations in those geographic regions where the Company conducts a major volume of its business. This provides a basis for offering a broad spectrum of products and services to the oil companies, resulting in cost-effectiveness, synergies and profitability. The sale was also a consequence of the Company's decision in early 1998 to discontinue its involvement in mobile production through the Mobile Production Division, which was headquartered in Aberdeen, Scotland. As a result of the foregoing decision, the Company considered the high costs associated with maintaining the headquarters in Aberdeen to be disproportionate to the low margins provided by the Company's platform drilling operations in the British continental shelf.

The Company will maintain its strong position in platform drilling in the Norwegian sector of the North Sea and this remains an essential factor in the Company's strategy.

During 1998, the Company performed drilling and maintenance operations on nine platforms in the Norwegian sector of the North Sea and, until mid-November 1998, on five installations in the British sector of the North Sea. The Company also provided well services from a number of mobile drilling rigs and fixed installations. These operations proceeded satisfactorily during the year, and the level of activity increased compared to the previous year.

The Company is developing more cost efficient drilling and maintenance techniques for use on fixed platforms. The Company expects that the market for such services will grow as the North Sea fields are gradually depleted and as the drilling equipment on these platforms no longer satisfies applicable regulatory requirements. The Company has also noted a possible growing market for plugging wells on platforms that are to be shut down and removed.

The Statfjord field saw a high level of drilling and maintenance activity throughout the year, as well as upgrades of the drilling facilities. In one period during the latter half of the year, the Company was drilling on three platforms, rather than the customary two. The Company was engaged in drilling operations on the Veslefrikk field through-out the year. The level of activity is expected to diminish in 1999 in connection with a drilling halt for classification and maintenance of the Veslefrikk B platform. In 1996, Phillips Petroleum awarded the Company a five-year well plugging and maintenance contract for the Ekofisk field. During 1997, Phillips Petroleum exercised its option to purchase the rig, which is being built in Canada by Hitec and Dreco. In 1998, the Company assisted Phillips Petroleum in the construction, onshore completion and testing of the modularized rig, named Rig 66. Under the Agreement, this rig will carry out a two and a half-year drilling program on the Eldfisk field, with start-up scheduled for the end of the second quarter 1999. The Company will operate the unit.

The Company's maintenance contract for Norsk Hydro's Oseberg C field expired in the first half of 1998. Over the year, the Company drilled an 8,750 meter well on the Gyda field at a distance of 7,000 meters from the platform. This is the first ultra high-deviation well on the field, and the world's third longest well. The contract for the Ula and Gyda fields expired in March 1999.

The Company also offers sales of equipment and services to the oil industry through Camco Services Norway A/S ("Camco Services Norway") and wireline operations. Wireline operations are an efficient and economical way of performing well interventions. The wire makes it possible to manipulate service tools several thousand meters below the surface. 1999 was a positive year for the Company's wireline operations.

On May 11, 1999, the Company signed an agreement with Schlumberger Norge Holdings AS ("Schlumberger") to sell its 50 per cent ownership in Camco Services Norway. The agreed sale price was U.S.$4 million. The integration of accounts will be effective from March 31, 1999, and a final approval from the Norwegian Ministry of Industry and Trade is required. The Company and Schlumberger also signed a four year agreement concerning wireline services in the Norwegian sector of the North Sea. This represents a continuation of the existing cooperation in this business. Camco Services Norway's activities consist of the sale and rental of Camco products and related services.

The following table sets forth the status of the Company's contracts for fixed platform drilling projects:

Fixed Installations

Field	Customer	Contract Awarded	Estimated Contract Duration
Norway			
Statfjord A, B and C	Statoil	July 1982	September 2002
Veslefrikk A and B	Statoil	July 1987	Field lifetime
Ekofisk	Phillips Petroleum	November 1992	November 2002
Ekofisk, P&A	Phillips Petroleum	December 1996	June 1999 until December 2001 (1)

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(1) Contract start-up is estimated to be the second quarter of 1999. Since the fourth quarter of 1998, the Company has operated a snubbing unit for Phillips Petroleum on the Ekofisk field.

Tender Rigs Division

Smedvig is one of the world's leading operators of self-erecting tender rigs. Through its wholly-owned subsidiary, Smedvig Asia Ltd., the Company has 26 years of offshore operating experience in Southeast Asia. The Company currently operates the world's largest fleet of self-erecting tender rigs. The company aims at further increasing its involvement in production drilling in Southeast Asia. This strategy entails an expansion of the tender rig fleet to further strengthen its market position and profitability. The Company anticipates that the market in Southeast Asia will demand more advanced units in the longer term. In order to meet this challenge, in 1998, the Company had one advanced semi-tender under construction.

As of June 6, 1999, the Company operates a fleet of eleven self-erecting tender drilling rigs (ten of which are wholly or partially owned by the Company). The fleet, which includes two semi-submersible tender drilling rigs, provides development drilling and well maintenance services in Southeast Asia and West Africa. The West Menang, a semi-submersible tender drilling rig that was under construction in 1998, was delivered on budget and on schedule in March 1999. The West Menang started performing its operating contract on April 30, 1999.

The Company's tender rigs are engaged in production drilling and well maintenance in Southeast Asia and West Africa. The self-erecting tender rigs are purpose-built barges designed with the capability of lifting the drilling equipment packages from the tender to a fixed platform. Semi-submersible tender rigs have semi-submersible hulls and are equipped with equipment similar to that of the self-erecting tender rigs. The tender, which contains living quarters, power machinery for running the drilling equipment, other drilling and well completion equipment and storage for drilling supplies, is moored next to the fixed platform during drilling operations. Historically, the use of self-erecting tender rigs has been important in Southeast Asia because it allows development and workover operations to be done on small fixed platforms, without the need for permanently installed drilling packages.

The table below sets forth certain information concerning the Company's tender rig fleet:

Tender Rig Fleet

Rig Designation	Ownership Percent	Year Built/Latest Enhancement	Current Location/Customer	Estimated Contract Expiration (1)
T-1 (2)	49%	1974/97	Thailand/PTTEP (3)	October 1999
T-2 (2)	49	1975/97	Malaysia/EPMI	December 2000/Options to
T-3 (2)(4)	49	1980/97	Brunei/Shell	December 2001
T-4	100	1981/98	Thailand/Thaipo	January 2000
T-5 (5)	100	1981/95	Congo/CMS Nomeco	July 1999
T-6 (2)	49	1983/98	Singapore/Shipyard Malaysia/Petronas	October 2004
T-7	100	1983/90	Thailand/Unocal	November 2000
T-8	100	1982/98	Thaipo	February 2001
West Pelaut	100	1994	Brunei/Shell	April 2000/Options to April 2009
West Menang	100	1999	Brunei/Shell	April 2004
Teknik Berkat (6)	0	1991/98	Malaysia/Petronas	September 2000

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(1) The duration of the contracts depends on the oil companies' drilling program. The above mentioned dates are therefore estimated ending dates.

(2) T-1, T-2, T-3 and T-6 are owned by Varia Perdana, a Malaysian joint-venture company in which the Company owns a 49 percent interest.

(3) PTT Exploration and Production Company Ltd.

(4) Began operations under a new contract in January 1999.

(5) T-5 is contracted to CMS Nomeco in Congo until August 1999.

(6) Teknik Berkat is operated by the Company.

In 1991, the Company sold three of its tender rigs to Varia Perdana, a Malaysian company established under a joint-venture between the Company, which owns a 49 percent interest, and an entity controlled by the Renong Group, a Malaysian industrial group. In 1994, the Company sold an additional tender rig to Varia Perdana. Through its 49 percent interest in and agreement with the entity that manages the Varia Perdana fleet, the Company continues to operate these tender rigs and receives a fee for such services. The Company believes this arrangement has enhanced its local presence in the developing Southeast Asian market. In February 1997, the Company expanded the scope of its operations in Southeast Asia through the acquisition of the assets of Petrodril for U.S.$69 million. Petrodril owned a large tender rig and a modern semi-submersible drilling tender.

In 1998, the Company signed with Shell a five-year drilling contract in connection with the construction of a semi-submersible rig for platform drilling assistance in Brunei. The rig, which is named the West Menang, was delivered as scheduled in March 1999. The total construction costs were U.S.$100 million, which is below the estimate of U.S.$105 million. The rig began operations under its contract at the end of April 1999.

In 1998, some of the Company's tender rigs were reclassified and/or upgraded in order to start the performance of contracts entered into in 1997 and early 1998. These contracts were entered into at favorable terms due to the good market conditions. All of the Company's tender rigs are under contract throughout 1999, with the exception of the T-1, T-2 and T-5, which are scheduled to complete their assignments in the latter half of 1999. The tender rig T-3 completed the contract with Sarawak Shell in June 1998 and underwent significant modifications and a scheduled classification in connection with the contract with Brunei Shell, which commenced in January 1999. In February 1998, the T-4 began employment under a two-year drilling contract with Thaipo in Thailand. The T-6 started its drilling contract with Petronas in July 1998. In June 1999, the contract was extended by approximately four years until October 2004. The contract includes a three-month yard-stay for upgrading and classification which is covered by Petronas. The T-8 began employment under a three-year contract with Thaipo in April 1998. Dayrates for new contracts have declined since the market peaked in February 1998, due to lower oil prices resulting in lower activity and increased competition from small jack-up rigs.

The demand for production drilling in Southeast Asia has been steady despite relatively low oil and gas prices. This is due primarily to requirements from the Thai and Malaysian governments to produce set minimum quotas. Secondly, the local governments prioritize oil production to meet their needs for hard currency in response to the Asian economic set-back. Some multi-national oil companies that are involved in production-sharing agreements with national oil companies in the region are less inclined to continue field expansions given the current market conditions. However, considerations of national interest and pressure from the national oil companies have resulted in the continuation of such an expansion, and production contracts have therefore been extended. Thirdly, this region has a need to be as self-sufficient as possible from an energy standpoint. However, given the reserves that have already been discovered in Southeast Asia, the Company believes that the need for drilling involving tender rigs is likely to continue.

The following table sets forth certain information comparing the Company's tender rig utilization to that of the tender rig industry as a whole for the past five years:

Tender Rig Utilization (1)

	Averages for Year Ended December 31,									
	1994		1995		1996		1997		1998	
	Company	Industry	Company	Industry	Company	Industry	Company	Industry	Company (2)	Industry
Supply	8.0	26.8	8.0	28.0	8.0	26.6	10.0	26.6	10.0	26.3
Utilization ...	89%	82%	75%	78%	88%	76%	70%	85%	88%	90%

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(1) Company data for each period is based on all rigs owned and operated during such period. Industry statistics of rig utilization are from Offshore Data Services. Company and industry statistics have been determined under the "working method", which is the ratio of the number of rig days in operation to the total number of rig days available. Total supply for each period includes only actively marketed rigs, i.e., excludes national oil company-owned and mothballed rigs, among others. Industry data is based upon competitive rigs (as defined by Offshore Data Services) of the types indicated and includes many rigs that may be dissimilar to the Company's rigs in many significant respects, including performance capabilities, age, operational criteria and environmental capabilities.

(2) Under the "revenue method", which is the ratio of the full contractual revenue actually generated to the maximum potential revenue obtainable pursuant to the operating contracts, the tender rig utilization rate was 86 percent in 1998.

Reservoir and Well Technology Division

The Company's Reservoir and Well Technology Division is involved in three business areas: reservoir monitoring, reservoir modeling and reservoir services.

In 1997 and 1998, the Reservoir and Well Technology Division contributed approximately 13 percent and 12 percent of the Company's revenues excluding gains on sale of assets, respectively. In 1996, the Reservoir and Well Technology Division consisted of three corporate entities: Smedvig Technology; Geomatic; and Prodrill. The Company also acquired Reservoir Simulation Research Corporation (RSRC) in Oklahoma, USA. These four companies were consolidated to form Smedvig Technologies as of February 1997. The Company made further investments to be able to offer its products and services in selected international markets. In May 1997, the Company acquired Petresim Integrated Technologies Inc. in Houston to strengthen its presence in North and South America. The division has also expanded through organic growth. The strategy of establishing an international network of sales offices has been successfully pursued and the division now has its own offices in the United States, the United Kingdom, Norway, the United Arab Emirates, Malaysia, Australia and China. In 1998, all the division's activities were organized under the legal entity Smedvig Technologies (Holding) AS. At the beginning of 1999, Smedvig Technologies had approximately 245 employees and consultants.

In March 1999, the Company agreed to merge Smedvig Technologies with Multi-Fluid. The primary business of Multi-Fluid is the provision of multiphase flow-meters for the oil industry. Multi-Fluid will be the surviving entity and will be renamed ROXAR ASA. See "—Recent Developments".

Smedvig Technologies' strategy is to deliver integrated products, software and services that enable increased recovery of oil and gas reservoirs. It is an international niche supplier in two fields of technology: computer software for reservoir modeling and permanently installed measuring equipment for monitoring production in the reservoir. The reservoir models estimate future production, while the measuring systems monitor the actual production conditions in each individual well. The long-term goal is to link these technologies in order to generate more precise estimates and a better basis for production planning. This will make it possible to increase oil and gas recovery and, at the same time, cut associated technology costs. Smedvig Technologies also offers technology to enable selective production management of different reservoir zones.

By combining modeling, measuring and down-hole management solutions, Smedvig Technology intends to offer an integrated system for reservoir management, the IRMS (Intelligent Reservoir Management System). The Company's strategy is to tailor new technologies to the oil companies' needs, and to commercialize these technologies in standardized products for sale through an international network of sales offices. In its product development efforts, Smedvig Technology sometimes works in cooperation with outside research experts and other technology companies.

Reservoir Monitoring. Smedvig Technologies' sales of reservoir monitoring systems increased by 52 percent during 1998. Smedvig Technologies is a dominant supplier in the Norwegian reservoir monitoring market. In 1998, Smedvig Technologies increased its sales of reservoir monitoring equipment in Southeast Asia, and has formed a joint venture in Malaysia to further promote sales to national and international oil companies in the region. As of December 31, 1998, Smedvig Technologies had an order back-log of 17 installations in Southeast Asia, which represents a significant market share in that region of the world.

Smedvig Technologies developed a number of reservoir monitoring technologies. Hybrid electronics have now been used in high temperature measuring sensors to increase their operational reliability. Smedvig Technologies is developing a downhole "radar" to track the movements of the water/oil interface in the reservoir. Working together with Multi-Fluid, Smedvig Technologies has begun developing a downhole device to measure the water content of the oil. These technologies will enable improved reservoir management and increased recovery. PROMAC, Smedvig Technologies' new technology for the selective guidance of oil flows from different production zones into the well, completed a successful test program and its trademark was registered in 1998. The water/oil sensor being developed in cooperation with Multi-Fluid is PROMAC-compatible, and allows the operator to ascertain the water content produced by each zone.

Reservoir Modeling. Smedvig Technologies primary 3-D geological modeling products have been improved, and can now be linked to the industrial databases used by the oil companies to coordinate different software. New versions of the software products were launched in 1998. The integration of these various software products is almost complete. Smedvig Technologies has also developed a new and improved simulation model that makes it possible to plan reservoir production more quickly and comprehensively than earlier.

Software sales increased by 50 percent during the first half of the year, but decreased in the second half. This is due to lower exploration expenditures by the oil companies as a result of low oil prices. New versions of the software and further improvements of the sales organization are expected to boost sales over the longer term.

Reservoir Services. In 1998, Smedvig Technologies carried out a number of projects associated with field development and optimal reservoir exploitation in Venezuela, Thailand, Oman, Great Britain and Norway. Smedvig Technologies was responsible for well planning and follow-up of a number of drilling operations in Malaysia and Brunei. Smedvig Technologies has established its own service teams, offering expertise in optimizing the use of its software. Such services are offered in the form of special studies and/or direct user support within the customer's own organization.

In November 1998, the division's well-engineering services in Great Britain and the Middle East were sold to Deutag AG, a German company. The remaining services relate to the division's core reservoir technology focus. In 1999, revenues from the division will decline as a result of the sale.

Activities To Be Discontinued

In April 1998, the Company made a strategic decision to discontinue its mobile production activities due to deteriorating market conditions, low profitability and Esso's termination of the Balder contracts. As a result, the Company terminated its projects within the former Mobile Production Division. This entailed the cancellation of the construction contract for the production vessel SPU 550, the sale of the former storage vessel SPU 4, the sale of Altra Consultants Limited, three production contracts and the operating contract for the Janice Alpha. In the wake of these sales, the division is involved in the operation of the ENSCO 100 water-injection platform, and in preparations for legal proceedings in connection with Esso's termination of the Balder contracts.

In 1998, the Company's operating contracts for the ENSCO 100, Balder FPU, SPU 4 and SPU 550 were reported under "Activities To Be Discontinued". The remaining production operations were reported under the Platform Drilling Division. In November 1998, these activities were sold to Deutag. See "—Platform Drilling Division". The Mobile Production Division/Activities To Be Discontinued accounted for approximately 13 percent and 6 percent of the Company's revenues excluding gains on sale of assets in 1997 and 1998, respectively.

Set forth below is certain information concerning the Company's Activities To Be Discontinued:

ENSCO 100. The Company operates the jack-up rig ENSCO 100 (formerly West Omikron), which is one of the world's largest jack-up rigs. ENSCO 100 is performing water injection for Phillips Petroleum in the Ekofisk field and has a water injection capacity of up to 350,000 barrels per day. In November 1997, the Company sold the rig to ENSCO in order to improve the Company's financial position and reallocate capital to finance its extensive newbuilding program. The gain from the sale totaled NOK 355 million (100 percent basis). The Company continues to operate the rig for Phillips Petroleum in the Ekofisk field under a bareboat charter with ENSCO. The bareboat charter with ENSCO runs until the end of the operating contract with Phillips Petroleum, which expires in January 2000, with options for Phillips Petroleum to extend the contract for up to two additional years.

SPU 550. In 1996, the Company acquired a 50 percent ownership interest in the SPU 550, a production vessel hull that was under construction in Japan, from the Norwegian Rasmussen Group. In April 1997, the Rasmussen Group sold its 50 percent ownership interest in the SPU 550 to Navion. In April 1998, the Company and Navion canceled the construction contract for the hull of the production vessel as a result of the Japanese yard's failure to deliver the vessel hull within the scheduled time frame. The delivery of the vessel hull, originally scheduled for the third quarter of 1997, was subsequently delayed. The yard accepted the cancellation and refunded all installments.

SPU 4. In December 1996, through a joint venture, the Company and Navion purchased a 50 percent interest each in a former storage vessel for conversion into a storage and/or production unit intended for use in areas with benign weather, such as Southeast Asia and West Africa. In April 1998, the Company and Navion sold the former storage vessel at a loss of NOK 8 million for the Company's 50 percent interest.

Balder FPU. The production unit Balder FPU was designed by a company jointly owned by the Company and Keppel FELS Limited (formerly Far East Levingston Shipbuilding Ltd.) ("KFELS") for continuous oil production in harsh environmental conditions. The Balder FPU was built by KFELS in Singapore and the Offshore & Marine AS yard in Norway, at a price of approximately U.S.$250 million, and was sold to Esso at a price of U.S.$295 million. In March 1997, the Company delivered the production vessel Balder FPU to Esso. In January 1997, it became evident that the total cost for completing the vessel would be higher than first estimated, and the capital gain previously booked on the vessel was therefore reversed effective in the fourth quarter of 1996. Some of the additional costs are related to guarantee works which the Company had advanced in order to secure completion of the vessel and which the Company will seek to reclaim from its subcontractors. The Company and Esso have disagreed on the allocation of these and other costs related to the project.

In September 1997, the Company initiated limited arbitration proceedings against KFELS in London in order to determine a procedure for enforcing the contractual warranty provisions. However, it was determined that the Company was not entitled to establish such procedures. Consequently, the issue of the warranty provisions remains unsettled. The Company intends to continue negotiations to settle the dispute.

In October 1997, Esso terminated the contract to operate the production vessel, along with the remaining portion of the sales contract. The termination does not mean that the vessel will be returned to the Company. Following the termination, Esso itself will perform the installation and operate the vessel on the Balder field. According to the sales contract, termination may be demanded only on grounds of substantial breach and, in the Company's view, only prior to formal delivery. Following review of the Company's contractual obligations in comparison with the condition of the ship at the time of its delivery to Esso in March 1997, it is the Company's view that it has satisfied its contractual obligations. The Company denies all allegations of a substantial breach of contract.

In April 1998, the Company brought a formal claim against Esso before the Stavanger City Court in Norway for unlawful termination and willful breach of the sales contract as well as the operating contract for the production vessel Balder FPU. In September 1998, Esso rejected the Company's claim and brought counterclaims against the Company totaling approximately NOK 4 billion. See "Item 3. Legal Proceedings".

Business Development and Contracting

The Company markets its services to integrated oil and gas companies and selected exploration and production companies. The Mobile Units Division, Platform Drilling Division and Tender Rigs Division have approximately 18 existing customers, many of which have independently functioning divisions that contract separately with the Company. As a result, most of these customers have more than one contract for the Company's services. The Reservoir and Well Technology Division services this same client base as well as other clients.

In the last five years, the Company has engaged in offshore drilling and other services for many leading international oil and gas companies, including Statoil, Norsk Hydro, Phillips Petroleum, Esso, Elf, British Petroleum, Amerada Hess, Amoco, Unocal, Shell, ARCO, Petronas, TOTAL, Exxon, ENSCO, Thaipo and Mobil. The Company's three largest customers during 1998 were Statoil, Norsk Hydro and Phillips Petroleum, which accounted for 26 percent, 21 percent and 8 percent, respectively, of the Company's consolidated revenues excluding gains on sale of assets in 1998, as compared with 28 percent, 21 percent and 12 percent in 1997. The loss of any significant customer, which could occur over time, could have a material adverse effect on the Company's results of operations.

The Company's marketing staff and the senior executives of the Company and each division are in regular contact with its existing and potential customers. In addition to responding to requests for tenders and proposals, through informal discussions and formal presentations, the Company actively seeks opportunities to promote the use of its assets and services.

The Company's preference is to employ its assets through long-term contractual arrangements. In a market where dayrates are profitable and rising, the Company seeks long-term contracts only, while in weaker markets it generally accepts only short-term contracts. Long-term contracts require less mobilization/de-mobilization costs, decrease volatility of return on assets, require less management time and, in the opinion of management, enhance its customer relationships. Although this strategy affords some protection against the negative effects of cyclicality and/or volatility in the industry, this preference for long-term asset utilization also limits the ability of the Company to participate fully in short-term upswings in the market. Management believes these advantages offset the possible foregone revenues from dayrates that in some periods may be lower than short-term market peaks.

Contracts for services of the Company's Mobile Units Division, Platform Drilling Division and Tender Rigs Division are typically multi-year. Actual contract durations generally vary depending on the number of wells involved and the time required for the particular project. Contracts generally provide an established dayrate structure, payable monthly, and some provide for lower dayrates during periods of immobilization or under certain circumstances when operations are interrupted or restricted. Under some contracts, the Company is entitled to additional payments for exceeding performance goals. The contracts also provide for the assumption by the customer of responsibility for changes in certain costs. Many contracts are extendable at the option of the other party. Such options may involve re-setting the dayrate based on current market rates. The contracts may be terminated by the customer upon the occurrence of certain events, including force majeure, and some contracts permit termination by the customer at any time without cause, subject to the payment of termination fees. In addition, some of the operating contracts for the units under construction may be terminated and provide for liquidated damages if the Company fails to deliver the units within the time frames specified in the contract.

Governmental Regulation and Environmental Matters

Many aspects of the Company's operations are affected by domestic and foreign political developments and are subject to numerous domestic and foreign laws and regulations that may relate directly or indirectly to the offshore drilling and oil services industry, including, without limitation, laws and regulations controlling the discharge of materials into the environment, requiring removal and cleanup or otherwise relating to environmental protection, and certification, licensing, safety and training and other requirements imposed by treaties, laws, regulations and conventions in the jurisdictions in which the Company operates. The offshore drilling and oil services industry is dependent on demand for services from the oil and gas exploration industry and, accordingly, is affected by changing taxes, regulations and other laws relating to the oil and gas industry generally.

In recent years, increased concern has been raised over protection of the environment. Offshore drilling in certain areas has been opposed by environmental groups and, in certain areas, has been restricted. To date, the Company has not had material operations in any areas where offshore drilling has been subject to such opposition or restriction. Accordingly, such opposition and restriction has not had a material impact on the Company's operations. However, to the extent new laws are enacted or other governmental actions are taken that prohibit or restrict offshore drilling or impose additional environmental protection requirements that result in increased costs to the oil and gas industry in general and the offshore drilling industry in particular, the business and prospects of the Company could be adversely affected.

The Company's operations may involve the use or handling of materials that may be classified as environmentally hazardous substances. Environmental laws and regulations applicable in the countries in which the Company conducts operations have generally become more stringent. Such laws and regulations may expose the Company to liability for the conduct of or conditions caused by others, or for acts of the Company which were in compliance with all applicable laws at the time such acts were taken. While the Company does not believe that environmental regulations have had any material adverse effect on its capital expenditures, results of operations or competitive position, the Company has invested and will continue to invest in capital expenditures necessary for the protection of life, health and the environment. However, the modification of existing laws or regulations or the adoption of new laws or regulations curtailing or further regulating exploratory or development drilling and production for oil and gas for political, economic, environmental or other reasons could have a material adverse effect on the Company's operations. The Company cannot predict the extent to which future earnings may be affected by compliance with such new legislation or regulations. In addition, the Company may become subject to additional laws and regulations as a result of future rig relocations.

Whenever possible, the Company generally seeks to obtain indemnity agreements from the Company's customers requiring such customers to hold the Company harmless in the event of liability for pollution that originates below the water surface, and maintains marine liability insurance and additional expense coverage which affords limited protection to the Company. There can be no assurance that such contractual indemnification or insurance coverage will be sufficient or effective to protect the Company from liability or exposure to additional expense.

With effect from 1996, a new tax scheme for shipowning and offshore companies was introduced in 1997 in Norway. According to the principles of the new tax scheme, no income tax is assessed on the income of those companies that qualify and elect to participate in the scheme. Taxation will occur when dividends are paid by companies within the scheme or when a company elects to withdraw from the scheme. The Company joined the new tax scheme with effect from 1996 for the majority of its fleet. For companies entering the scheme deferred tax on temporary differences are reversed. Since the Company deems it preferable to stay within the new scheme for a long time no provision for taxes has been provided for those companies within the scheme.

Competition

The Company is faced with competition that varies in nature in each of its business divisions. While consolidation in the offshore drilling and oil services industry has decreased the number of competitors over the past few years, some of the Company's competitors may have significantly greater financial, marketing, personnel and other resources than the Company. As a result, such competitors may be better able to withstand cyclical fluctuations in demand for offshore drilling and oil services or to compete for existing demand for such services.

The Company's Mobile Units Division, Platform Drilling Division and Tender Rigs Division operate in the offshore drilling industry, which historically has been highly cyclical, with periods of high demand, short rig supply and high dayrates followed by periods of low demand, excess rig supply and low dayrates. The mobile drilling and tender rigs market is characterized by high capital costs, long lead times for construction of new rigs and significant competition for relatively few customers. The offshore drilling business is influenced by many factors, including the current and anticipated prices of oil and gas (which affect the expenditures by oil and gas companies for exploration and production) and the availability of drilling units. Drilling contracts are traditionally awarded on a competitive bid basis. While an operator selecting a rig may consider, among other things, the quality of service and equipment, price competition is often the primary factor in determining which among qualified contractors is awarded a job. However, it is not unusual for contracts for technically-advanced drilling units to be awarded on a negotiated basis rather than through competitive bidding.

Competition in the Reservoir Technology Division comes from a variety of sources, including a few large integrated oil services companies, as well as independent consulting companies.

Order Backlog

The Company's total order backlog (based on the value of firm contracts and excluding any options) was NOK 6.5 billion, NOK 14.1 billion and NOK 11.0 billion, as of December 31, 1996, 1997 and 1998, respectively. The decrease in order backlog from December 31, 1997, to December 31, 1998, primarily related to the decrease in the number of new contracts that were entered into during 1998. The decrease in new contracts was due to the Company's obligations under existing contracts. In 1996 and 1997, the Company experienced an increase in operating contracts primarily due to the five-year operating contracts concerning the Company's new vessels. Most of the Company's units are now committed to perform such contracts and it would not be available to be used in the performance of new contracts for the next few years, thus reducing the Company's ability to enter into new contracts. Moreover, new contracts are not negotiated until six to twelve months prior to the expiration of existing contracts and most of the Company's existing contracts will expire within more than twelve months. The options of the Company's clients to extend such contracts would amount to approximately NOK 9.0 billion of additional order backlog at the end of 1998, but are subject to repricing in certain cases.

Industry and Operating Risks

In order to utilize the "Safe Harbor" provisions of the United States Private Securities Litigation Reform Act of 1995, the Company is providing the following cautionary statement. This document contains certain forward-looking statements with respect to the financial condition, results of operations and business of the

Company and certain of the plans and objectives of the Company with respect to these items. In particular, among other statements, certain statements in "Item 1. Description of Business" and "Item 9. Management's Discussion and Analysis of Financial Condition and Results of Operations" with regard to management aims and objectives, planned investments and projects, expected or targeted utilization or dayrates, the date or period in which a project or action is scheduled or expected to be completed, cost estimates for newbuilding projects, industry outlook and the statements in "Item 9. Management's Discussion and Analysis of Financial Condition and Results of Operations" with regard to trends in results of operations, margins, overall market trends, risk management and exchange rates are forward-looking in nature. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. There are a number of factors that could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements. In addition to factors set forth elsewhere in this Annual Report, the following are important factors, although not exhaustive, that may cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements.

The Company's business and operations depend principally upon conditions prevailing in the oil and gas industry and, in particular, the exploration, development and production expenditures of oil and gas companies and the availability of offshore drilling units. The offshore drilling and oil services industry is influenced by many factors, including the current and anticipated prices and demand for oil and gas, which in turn affect the expenditures by oil and gas companies for exploration, development and production. Low oil prices typically mean that exploration drilling is curtailed as a result of limited oil and gas company capital expenditure budgets. The Company cannot predict the future level of demand for its services or future conditions of the oil and gas industry. While the Company believes that its long-term contracts reduce its exposure in the near term to fluctuations in oil and gas prices and changes in oil companies' spending, decreases in exploration, development and production expenditures could have a material adverse effect on the Company's business and results of operations.

Approximately 88 percent, 87 percent and 88 percent of the Company's revenues excluding gains on sale of assets for the three years ended December 31, 1996, 1997 and 1998, respectively, were derived from offshore exploration and production activities, which are characterized by high capital costs, long lead times for construction of new rigs and significant competition. Historically, the offshore drilling industry has been highly competitive and cyclical, with periods of high demand, short rig supply and high dayrates followed by periods of low demand, excess rig supply and low dayrates.

Demand for the Company's offshore drilling and oil services has historically been volatile. Market conditions will remain dependent on a variety of political and economic factors beyond the Company's control, including worldwide demand for oil and gas, the ability of OPEC to set and maintain production levels, the level of production of non-OPEC countries, the prices of oil and gas and the policies of the various governments regarding exploration and development of their oil and gas reserves. See "—Industry Overview".

The Company's international operations are also subject to political, economic and other uncertainties, including, among others, risks of war, expropriation, nationalization, renegotiation or nullification of existing licenses or treaties, taxation and resource development policies, foreign exchange restrictions, changing political conditions, international monetary fluctuations and other risks relating to foreign governmental sovereignty over certain areas in which the Company conducts operations.

As a result of extensive review of the costs, delivery schedule and project management of all of its newbuilding projects, the Company has revised its total project cost estimates and delivery schedules for the drillship West Navion and the semi-submersible West Venture. While the Company believes that such revised estimates now represent total project costs, including interest expense, project management, contingencies and operation preparations, no assurance can be given, however, that further cost increases will not result. In view of the current project construction status, combined with the risks associated with final hook-up and commissioning, there still remains uncertainties concerning the final completion, delivery and costs of the two units under construction. No assurance can be given that further cost increases or delays will not have a material effect on the Company's business and results of operations.

The Company has planned capital expenditures of approximately U.S.$280 million in 1999. In order to finance these expenditures, the Company has raised additional funds through bank borrowing and asset sales in 1998. The Company is of the opinion that the current revolving credit facility and cash-flow from operations are sufficient to finance the newbuilding program. See "Item 9. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources".

Several of the Company's contracts contain cancellation clauses that permit the customers to terminate the contract upon the occurrence of specified events. Significantly, the West Venture operating contract provides Norsk Hydro a right to terminate in the event that the commencement date is delayed more than a specified number of days. There can be no assurance that such clauses will not become effective and if it becomes effective such party will not exercise its cancellation right. In addition, cancellation of any of these contracts could have a material adverse effect on the Company's business and results of operations.

Employees

At June 1, 1999, the Company had approximately 3,351 employees, consisting of approximately 1,724 employees in Norway and approximately 1,627 outside Norway. Approximately 1,101 of the Company's employees in Norway are represented by unions pursuant to industry-wide collective bargaining arrangements. The Company considers its employee relations to be good.

ITEM 2. DESCRIPTION OF PROPERTY

The Company's principal executive offices are located in Stavanger, Norway, and are under a lease with A/S Veni which will expire in June 2000 and is for approximately 1,800 square meters of space at the same location. Smedvig Offshore has entered into separate leases with A/S Veni for the base at Dusavik and for the offices, expiring in October 1998 and January 2008, respectively. A/S Veni is a real estate company wholly owned by Peter T. Smedvig and other members of the Smedvig family. See "Item 13. Interest of Management in Certain Transactions". Other leased facilities of the Company are located in Stavanger, Bergen, Oslo, London, Houston, Singapore, Kuala Lumpur and Bangkok. The Company believes that all of its owned and leased properties are well maintained and are suitable and adequate for the present activities of the Company.

ITEM 3. LEGAL PROCEEDINGS

In late 1995, the Company sold the production vessel Balder FPU to Esso. In March 1997, the vessel was delivered to Esso for final completion by Esso in Scotland. In October 1997, Esso notified Smedvig that the company was terminating the contract to operate the production vessel, along with the remaining portion of the contract to sell the ship. Pursuant to the review of the Company's contractual obligations in comparison with the condition of the ship at the time of her delivery to Esso in March 1997, Smedvig believes that the Company has fulfilled its contractual obligations. In April 1998, the Company brought a formal claim against Esso before the Stavanger City Court in Norway for unlawful termination and willful breach of the sales contract as well as the operating contract for the production vessel Balder FPU. In the claim, the Company claims payment of the final settlement under the sales contract plus compensation for unlawful termination and willful breach of contracts up to a total of approximately NOK 2.6 billion. In its reply, filed in September 1998, Esso rejected the Company's claim and brought counterclaims totaling some NOK 4 billion against the Company, based mainly on Esso's claim that the Company substantially breached the sales and purchase contract and was grossly negligent in its handling of the Balder project. The Company rejects this claim as unfounded, and a formal response was filed at the end of March 1999. The Company maintains that Esso undertook comprehensive modifications and upgrades of the vessel above and beyond those specified in the construction contract, and that the oil company is liable for the costs thereof. The Stavanger City Court requested Esso and the Company to initiate negotiations in October 1999 with the aim of narrowing the scope of the dispute. The Stavanger City Court scheduled to hear the case between March and October 2000. The Company believes that provisions for loss are not necessary.

The Company initiated arbitration proceedings against KFELS in London in September 1997 in order to determine a procedure for enforcing the warranty provisions independent of other conditions about which the parties are in disagreement. In November 1997, the arbitration proceedings ended and the Company's claim was denied. As a result, the issue of enforcing the warranty provisions remains unsettled. The arbitration process is currently dormant pending the outcome of the lawsuit between Esso and Smedvig.

ITEM 4. CONTROL OF REGISTRANT

The following table sets forth certain information regarding the beneficial ownership of the class A ordinary shares (the "Class A Shares") and class B ordinary shares (the "Class B Shares") as of May 3, 1999, by all persons known by the Company to own, directly or indirectly, more than 10 percent of the Company's outstanding voting securities and all officers and directors of the Company as a group.

Owner	Number of Class A Shares Owned	Percent of Class	Number of Class B Shares Owned	Percent of Class
Peder Smedvig Capital as (1)(2)	8,795,817	32.2%	1,092,629	7.9%
Smedvigs Rederi A/S (2)	425,344	1.6%	106,336	0.8%
A/S Veni (2)	306,230	1.1%	76,558	0.6%
DS AS Isbjrn (2)	206,888	0.8%	51,722	0.4%
Mr. Peter T. Smedvig (3)	10,279,163	37.6%	1,463,466	10.6%
Mrs. Nora Smedvig	413,624	1.5%	103,316	0.8%
Ms. Nora Smedvig, Jr	110,000	0.4%	27,500	0.2%
Ms. Hjrdis Smedvig	52,000	0.2%	13,000	0.1%
Officers and directors as a group (4)	10,383,746	37.97%	1,514,671	10.9%

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(1) Previously Summa AS.

(2) Peder Smedvig Capital as, Smedvigs Rederi A/S, A/S Veni and DS AS Isbjrn are each owned by Mr. Peter T. Smedvig, Chairman of the Board of Directors of the Company, Ms. Nora Smedvig, Jr. and Ms. Hjrdis Smedvig, who are the sisters of Mr. Smedvig. Mr. Smedvig owns a majority of the voting shares of each company.

(3) Includes 8,795,817 Class A Shares and 1,092,629 Class B Shares owned by Peder Smedvig Capital as, 425,344 Class A Shares and 106,336 Class B Shares owned by Smedvigs Rederi A/S, 306,230 Class A Shares and 76,558 Class B Shares owned by A/S Veni and 206,888 Class A Shares and 51,722 Class B Shares owned by DS AS Isbjrn. Each such company disclaims beneficial ownership of shares owned by the others.

(4) Includes an aggregate of 9,734,279 Class A Shares and 956,408 Class B Shares owned by Peder Smedvig Capital as, Smedvigs Rederi A/S, A/S Veni and DS AS Isbjrn.

The Smedvig family members identified in the above table as of May 21, 1999, owned an aggregate of 10,854,427 Class A Shares (39.7 percent) and 1,607,282 Class B Shares (11.6 percent) directly and through Peder Smedvig Capital as, Smedvigs Rederi A/S, A/S Veni and DS AS Isbjrn. Pursuant to a shareholder agreement among the Smedvig family members identified above, Peder Smedvig Capital as, Smedvigs Rederi A/S, A/S Veni and DS AS Isbjrn, such shareholders vote their shares as a group on all matters at general meetings of shareholders of the Company. In the summer of 1998, Peder Smedvig Capital as, purchased a total of 425,300 Class A Shares.

ITEM 5. NATURE OF TRADING MARKET

The principal trading market for the Company's ordinary shares is the Oslo Stock Exchange, where the Class A Shares have been listed since September 1990. The Class B Shares have been listed on the Oslo Stock Exchange since August 30, 1996. Prior to the registered public offering of Class B Shares in November 1996, the Class A and Class B Shares, in the form of American Depositary Shares ("Class A ADSs" and "Class B ADSs", respectively), were traded in the over-the-counter market in the United States, although trading had been relatively inactive. The Class A and Class B ADSs have been listed on The New York Stock Exchange since November 8, 1996, under the symbols SMVA (for the Class A shares) and SMVB (for the Class B shares), respectively.

The following tables below set forth, for the periods indicated, the high and low closing prices on the Oslo Stock Exchange for the Class A and Class B Shares and the highest and lowest closing sales prices of ADSs as reported on the New York Stock Exchange composite tape.

	Class A Shares			
	Oslo Stock Exchange		New York Stock Exchange	
	Price per Class A Share		Price per Class A ADS (2)	
	High	Low	High	Low
	NOK	NOK	U.S.$	U.S.$
1997				
First Quarter	178.50	139.00	27.00	20.88
Second Quarter	193.00	156.00	25.75	22.13
Third Quarter	223.00	183.00	29.75	24.13
Fourth Quarter	243.00	155.00	34.00	19.63
1998				
First Quarter	181.00	133.00	24.88	16.63
Second Quarter	176.00	91.00	23.63	12.63
Third Quarter	102.00	58.00	13.65	7.75
Fourth Quarter	83.50	55.00	11.12	7.13
1999				
First Quarter	87.00	75.00	11.24	7.50
Second Quarter (through June 9, 1999)	105.00	79.00	12.87	10.06

	Class B Shares			
	Oslo Stock Exchange		New York Stock Exchange	
	Price per Class B Share		Price per Class B ADS (2)	
	High	Low	High	Low
	NOK	NOK	U.S.$	U.S.$
1997				
First Quarter	176.00	131.00	26.25	20.00
Second Quarter	190.00	152.00	26.25	21.88
Third Quarter	226.00	180.00	29.63	24.75
Fourth Quarter	239.00	155.00	33.94	20.88
1998				
First Quarter	175.00	130.00	23.25	15.88
Second Quarter	164.00	95.00	21.63	11.63
Third Quarter	94.00	82.00	12.92	6.45
Fourth Quarter	73 00	50.00	10.62	6.13
1999				
First Quarter	75.00	47.50	9.37	6.31
Second Quarter (through June 9, 1999)	93.00	66.50	11.75	8.50

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(1) Each Class A ADS represents one Class A share.

(2) Each Class B ADS represents one Class B Share.

The Company has entered into two deposit agreements with Citibank, N.A., as depositary (the "Depositary"), and the holders from time to time of American Depositary Receipts issued thereunder pursuant to which a separate sponsored American Depositary Receipt facility was made available with respect to each of the Class A Shares and the Class B Shares.

Based upon information available from the Norwegian share registry, Verdipapirsentralen ("VPS"), as of May 12, 1999, the Company had 2,119 holders of record of Class A Shares, of which 20 had registered addresses in the United States and held a total of 2,962,620 Class A Shares, and 1,565 holders of record of Class B Shares, of which 16 had registered addresses in the United States and held a total of 1,056,665 Class B Shares. Citibank, N.A., as Custodian, is the registered holder for holders of Class A ADSs representing 503,200 Class A Shares and the holders of Class B ADSs representing 1,994,960 Class B Shares. According to Citibank's registry, there were three registered holders of Class A ADSs and there were six registered holders of Class B ADSs. Holders of record of Class A Shares and Class B Shares having registered addresses in the United States, together with the registered holders of Class A ADSs and Class B ADSs in Citibank's registry, held an aggregate of approximately 12.7 percent and 22.0 percent of the total number of Class A Shares and Class B Shares, outstanding on such date, respectively. The above numbers may not be representative of the actual number of U.S. beneficial holders or the number of Class A Shares and Class B Shares beneficially held by U.S. persons.

ITEM 6. EXCHANGE CONTROLS AND OTHER LIMITATIONS AFFECTING SECURITY HOLDERS

Under Norwegian foreign exchange controls, transfers of capital to and from Norway are not subject to prior government approval, except for the physical transfer of payments in currency, which is restricted to licensed banks. Consequently, a non-Norwegian resident may only receive dividend payments without a Norwegian exchange control consent if such payment is made through a licensed bank.

Under the articles of association of the Company (the "Articles of Association"), the holders of Class B Shares are not entitled to vote at general meetings of shareholders. However, under Norwegian law, the holders of Class B Shares are entitled to vote under certain limited circumstances. In November 1997, the shareholders approved an Amendment to the Articles of Association, and as a result, in order to participate in and vote at the general meetings, shareholders must notify the Company in advance of their intent to do so. Pursuant to the Articles of Association, ownership of shares is subject to approval by the Board of Directors of the Company. Such approval requirement applies to all prospective shareholders. There are no limitations, under either Norwegian law or the constituent documents of the Company, on the right of non-resident or foreign owners to hold or vote the Class A Shares or Class B Shares.

ITEM 7. TAXATION

The following is a summary of certain United States federal income and Norwegian tax consequences of ownership of Class A Shares or Class B Shares ("Class A or B Shares") or Class A ADSs or Class B ADSs ("Class A or B ADSs") by an investor that is not a resident of Norway for tax purposes and holds such Class A or B Shares or Class A or B ADSs as capital assets. This summary does not purport to address all material tax consequences of the ownership of Class A or B Shares or Class A or B ADSs, and does not take into account the specific circumstances of any particular investors (such as tax-exempt entities, certain insurance companies, broker-dealers, investors liable for alternative minimum tax, investors that actually or constructively own 10 percent or more of the voting shares of the Company, investors that hold Class A or B Shares or Class A or B ADSs as part of a straddle or a hedging or conversion transaction or investors whose functional currency is not the U.S. dollar), some of which may be subject to special rules. This summary is based on the tax laws of the United States (including the Internal Revenue Code of 1986, as amended, its legislative history, existing and proposed regulations thereunder, published rulings and court decisions) and Norway as in effect on the date hereof, as well as on the Convention Between the United States of America and the Kingdom of Norway for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and Property (the "Treaty"), all of which are subject to change (or changes in interpretation). In addition, the summary is based in part upon the representations of the Depositary and the assumption that each obligation in the Deposit Agreement and any related agreement will be performed in accordance with its terms.

For purposes of this discussion, a "U.S. Holder" is any beneficial owner of Class A or B Shares or Class A or B ADSs that is (i) a citizen or resident of the United States, (ii) a corporation organized under the laws of the United States or any State or (iii) otherwise subject to United States federal income taxation on a net income basis in respect of a Class A or B Share or Class A or B ADS.

The discussion does not address any aspects of United States taxation other than federal income taxation or any aspects of Norwegian taxation other than income taxation, transfer taxation, property taxation, gift and inheritance taxation and capital taxation. Investors are urged to consult their tax advisors regarding the United States federal, state and local and the Norwegian and other tax consequences of their ownership of Class A or B Shares and Class A or B ADSs.

In general, and taking into account the earlier assumptions, for United States federal income and Norwegian tax purposes, holders of Class A or B ADRs evidencing Class A or B ADSs will be treated as the owners of the Class A or B Shares represented by those Class A or B ADSs, and exchanges of Class A or B Shares for Class A or B ADSs, respectively, and Class A or B ADSs for Class A or B Shares, respectively, will not be subject to United States federal income or to Norwegian tax.

Taxation of Dividends

Norwegian Taxation

Under Norwegian tax law, dividends paid to foreign shareholders of Norwegian corporations are, unless otherwise provided for in an applicable tax treaty, subject to a withholding tax in Norway of 25 percent. Pursuant to the Treaty, the maximum rate of withholding tax is 15 percent on dividends paid by a Norwegian corporation to a person resident (for purposes of the Treaty) in the United States, provided that such person does not have a permanent establishment in Norway with which the dividends are effectively connected. The 15 percent withholding rate will apply to dividends paid on Class A or B Shares held directly by U.S. Holders who properly demonstrate to the Company and to the Norwegian tax authorities that they are entitled to the benefits of the Treaty. In particular it should be noted that certain entities only qualify to the extent such entities are subject to tax on their income. Additionally, according to recently established Norwegian tax practice, the 15 percent withholding tax rate will also apply on dividends paid to the Depositary, but only if the Depositary has obtained a consent in advance (upon fulfillment of certain conditions) from the Norwegian Tax Directorate. If such consent is not obtained in advance, dividends paid to the Depositary will be subject to withholding at the 25 percent rate. U.S. Holders of Class A or B ADSs who believe they are entitled to the benefits of the Treaty may apply to the Norwegian tax authorities for a refund of amounts withheld in excess of 15 percent. The application has to be filed with the Norwegian Tax Directorate.

The Company intends to file any reports with the Norwegian authorities or agencies necessary to obtain the benefits of the Treaty for those U.S. Holders who are entitled to them. The Company will exercise its right under the Deposit Agreement to reasonably request from the Depositary such information from its records to enable the Company to file such reports.

If, however, the recipient of a dividend is a U.S. Holder who is determined to be engaged in a business activity taxable in Norway and the Class A or B Shares or Class A or B ADSs with respect to which the dividend is paid are effectively connected with such activity, then the amount distributed to such U.S. Holder will be treated as taxable domestic dividend income in Norway, subject to the provisions of the Treaty, where applicable.

United States Federal Income Taxation

Under the United States federal income tax laws, and subject to the passive foreign investment company ("PFIC") and foreign personal holding company rules discussed below, U.S. Holders will include in gross income the gross amount of any dividend paid (before reduction for Norwegian withholding taxes) by the Company out of its current or accumulated earnings and profits (as determined for United States federal income tax purposes) as ordinary income when the dividend is actually or constructively received by the U.S. Holder, in the case of Class A or B Shares, or by the Depositary, in the case of Class A or B ADSs. The dividend will not be eligible for the dividends-received deduction generally allowed to United States corporations in respect of dividends received from other United States corporations. The amount of the dividend distribution includible in income of a U.S. Holder will be the U.S. dollar value of the Norwegian krone payments made, determined at the spot Norwegian krone/U.S. dollar rate on the date such dividend distribution is includible in the income of the U.S. Holder, regardless of whether the payment is in fact converted into U.S. dollars. Generally, any gain or loss resulting from currency exchange fluctuations during the period from the date the dividend payment is includible in income to the date such payment is converted into U.S. dollars will be treated as ordinary income or loss. Such gain or loss will generally be income from sources within the United States for foreign tax credit limitation purposes.

Subject to certain limitations, the Norwegian tax withheld in accordance with the Treaty and paid over to Norway will be creditable against the U.S. Holder's United States federal income tax liability. To the extent a refund of the tax withheld is available to a U.S. Holder under the laws of Norway or under the Treaty, the amount of tax withheld that is refundable will not be eligible for credit against the U.S. Holder's United States federal income tax liability.

For foreign tax credit limitation purposes, the dividend will be income from sources without the United States, but generally will be treated separately, together with other items of "passive income" (or, in the case of certain holders, "financial services income").

Distributions of additional Class A or B Shares to U.S. Holders with respect to their Class A or B Shares or Class A or B ADSs that are made as part of a pro rata distribution to all shareholders of the Company generally will not be subject to United States federal income tax.

Taxation of Capital Gains

Norwegian Taxation

A U.S. Holder normally is not taxed in Norway on gains from the sale or other disposal of Class A or B Shares or Class A or B ADSs. Such U.S. Holder may, however, be subject to taxation if the shareholding is effectively connected with a business carried out by the U.S. Holder through a permanent establishment in Norway. In addition, a U.S. Holder may be subject to taxation on gains if the U.S. Holder is an individual who is or has been a resident of Norway for income tax purposes and the disposal takes place within five years after the calendar year in which such U.S. Holder ceased to be a resident of Norway. Under the Treaty, gains realized by a resident of the United States from the sale or other disposal of Class A or B Shares or Class A or B ADSs generally are not subject to Norwegian taxation unless the shareholding is effectively connected with a permanent establishment in Norway or the U.S. Holder is an individual who (i) maintains for at least 183 days during the taxable year a fixed base in Norway with which such gains are effectively connected or (ii) is physically present in Norway for at least 183 days during the taxable year. The same rules apply to gains realized upon complete liquidation of the Company or upon redemption of Class A or B Shares. Repayment in connection with a reduction of the share capital by reducing the nominal value of the A or B Shares is, however, subject to withholding tax as dividend distribution, if exceeding paid-in capital.

Deposits and withdrawals of Class A or B Shares in exchange for Class A or B ADSs will not result in taxable gain or loss for Norwegian tax purposes.

United States Federal Income Taxation

Subject to the PFIC rules discussed below, upon a sale or other disposition of Class A or B Shares or Class A or B ADSs, a U.S. Holder will recognize gain or loss for United States federal income tax purposes in an amount equal to the difference between the U.S. dollar value of the amount realized and the U.S. Holder's tax basis (determined in U.S. dollars) in such A or B Shares or Class A or B ADSs. Generally, such gain or loss will be capital gain or loss, will be long-term capital gain or loss if the U.S. Holder's holding period for such Class A or B Shares or Class A or B ADSs exceeds one year and such gain will be income from sources within the United States for foreign tax credit limitation purposes.

Additional United States Federal Income Tax Considerations

PFIC Rules

The Company believes that Class A or B Shares and Class A or B ADSs should not be treated as stock of a passive foreign investment company (a "PFIC") for United States federal income tax purposes, but this conclusion is a factual determination made annually and thus may be subject to change.

In general, the Company will be a PFIC with respect to a U.S. Holder if, for any taxable year in which the U.S. Holder held the Company's Class A or B ADSs or A or B Shares, either (i) at least 75 percent of the gross income of the Company for the taxable year is passive income or (ii) at least 50 percent of the value (determined on the basis of a quarterly average) of the Company's assets is attributable to assets that produce or are held for the production of passive income. For this purpose, passive income generally includes dividends, interest, royalties, rents (other than certain rents and royalties derived in the active conduct of a trade or business), annuities and gains from assets that produce passive income. If a foreign corporation owns at least 25 percent by value of the stock of another corporation, the foreign corporation is treated for purposes of the PFIC tests as owning its proportionate share of the assets of the other corporation, and as receiving directly its proportionate share of the other corporation's income.

If the Company is treated as a PFIC, a U.S. Holder would be subject to special rules with respect to (a) any gain realized on the sale or other disposition of Class A or B Shares or Class A or B ADSs and (b) any "excess distribution" by the Company to the U.S. Holder (generally, any distributions to the U.S. Holder in respect of the Class A or B Shares or Class A or B ADSs during a single taxable year that are greater than 125 percent of the average annual distributions received by the U.S. Holder in respect of the Class A or B Shares or Class A or B ADSs during the three preceding taxable years or, if shorter, the U.S. Holder's holding period for the Class A or B Shares or Class A or B ADSs). Under these rules, (i) the gain or excess distribution would be allocated ratably over the U.S. Holder's holding period for the Class A or B Shares or Class A or B ADSs, (ii) the amount allocated to the taxable year in which the gain or excess distribution was realized would be taxable as ordinary income, (iii) the amount allocated to each prior year, with certain exceptions, would be subject to tax at the highest tax rate in effect for that year, and (iv) the interest charge generally applicable to underpayments of tax would be imposed in respect of the tax attributable to each such year.

Special rules apply with respect to the calculation of the amount of the foreign tax credit with respect to excess distributions by a PFIC.

A U.S. Holder who owns Class A or B Shares or Class A or B ADSs during any year that the Company is a PFIC must file Internal Revenue Service Form 8621.

Foreign Personal Holding Company Rules

The Company believes that it is not and is not likely to become a foreign personal holding company for United States tax purposes, but this conclusion is a factual determination made annually and thus subject to change. In general, if the Company were a foreign personal holding company, U.S. Holders of Class A or B Shares or Class A or B ADSs would be taxed currently on certain categories of undistributed passive income of the Company and a U.S. person who acquires shares from a decedent would not have a stepped-up basis in the Class A or B Shares or Class A or B ADSs but would have a tax basis equal to the lower of the fair market value of the Class A or B Shares or Class A or B ADSs or the decedent's basis in the Class A or B Shares or Class A or B ADSs.

Additional Norwegian Tax Considerations

Transfer Tax

There is currently no Norwegian share transfer tax on the transfer of shares.

Inheritance Tax

When Class A or B Shares or Class A or B ADSs are transferred, either through inheritance or as a gift, such transfer may give rise to inheritance tax in Norway if the deceased, at the time of death, or the donor, at the time the gift is made, is a resident or citizen of Norway. However, if the deceased, at the time of death, is not a resident of Norway but rather a citizen of Norway, Norwegian inheritance tax will not be levied if inheritance tax, or a similar tax, is levied in the country of residence. Irrespective of residency or citizenship, Norwegian inheritance tax may be levied if the Class A or B Shares or Class A or B ADSs are effectively connected to a permanent establishment in Norway.

Wealth Tax

Norway does not levy any property tax or similar tax on the Class A or B Shares. A holder of Class A or B Shares or Class A or B ADSs who is not a resident or citizen of Norway is not subject to Norwegian wealth tax with respect to such Class A or B Shares or Class A or B ADSs unless such holder is an individual or entity other than a corporation and his shareholding is effectively connected with a business carried out by the holder through a permanent establishment in Norway.

ITEM 8. SELECTED FINANCIAL DATA

The following selected financial data should be read in conjunction with, and is qualified in its entirety by reference to, the Consolidated Financial Statements and the Notes thereto and the other financial information included herein. The selected consolidated financial data for each of the years in the five year period ended December 31, 1998, has been derived from the audited Consolidated Financial Statements of the Company as restated to conform with the accounting presentation adopted in this Annual Report. See Note 1 to the audited Consolidated Financial Statements—Basis of Consolidation. The Company's audited Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles in Norway, which differ in certain respects from generally accepted accounting principles in the United States. See Note 30 to the audited Consolidated Financial Statements.

The selected financial data should be read in conjunction with, and are qualified in their entirety by reference to, the financial statements and notes included elsewhere herein.

	Year Ended December 31,					
	1994	1995	1996 (1)	1997	1998	1998 (2)
INCOME STATEMENT DATA:						
Amounts in Accordance with Norwegian GAAP						
Revenues	NOK 1,953	NOK 2,116	NOK 2,451	NOK 3,084	NOK 3,679	U.S.$485
Operating expenses	1,607	1,701	1,911	2,377	2,818	371
Depreciation	345	340	332	354	288	38
Operating profit	1	75	208	353	573	76
Financial income (expense)	(65)	2	(23)	(51)	7	1
Other items (3)	101	195	—	390	(372)	(49)
Income taxes	(4)	(80)	35	(58)	16	2
Minority interests	20	13	(10)	(48)	(11)	(2)
Net income	53	205	210	586	213	28
Earnings per share (4)	1.76	6.12	6.06	14.30	5.17	0.68
Dividends per share (4)(5)	.60	1.60	2.00	2.25	1.75	0.23
Amounts in Accordance with U.S. GAAP						
Net income	142	204	98	233	189	25
Basic earnings per share (4)	4.67	6.09	2.83	5.68	4.59	0.61
Diluted earnings per share (6)	4.67	6.06	2.81	5.66	4.59	0.61
OTHER FINANCIAL DATA:						
Amounts in Accordance with Norwegian GAAP						
Capital expenditures	537	1,220	871	1,830	2,631	347
Adjusted EBITDA (7)	346	415	540	707	861	114
Net cash flow provided by operating activities	175	416	350	475	742	98
Net cash provided by (used in) investing activities	(280)	(1,315)	807	(998)	(2,529)	(334)
Net cash provided by (used in) financing activities	347	632	(1,216)	970	1,568	207

	Year Ended December 31,					
	1994	**1995**	**1996 (1)**	**1997**	**1998**	**1998 (2)**
BALANCE SHEET DATA						
Amounts in Accordance with Norwegian GAAP						
Cash, cash equivalents and short-term investments	NOK 711	NOK 954	NOK 534	NOK 1,074	NOK 882	U.S.$116
Working capital	660	1,079	788	1,442	1,281	169
Fixed assets	2,425	2,554	2,777	2,674	2,733	361
New building contract	1,166	1,463	422	3,525	4,228	558
Total assets	4,977	5,640	5,236	8,668	9,239	1,219
Long-term debt	1,712	1,568	862	1,913	3,853	508
Shareholders' equity	1,650	1,804	2,899	3,417	3,597	475
Amounts in Accordance with U.S. GAAP						
Shareholders' equity	1,722	1,913	2,948	3,123	3,254	429

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(1) In 1996, a new interpretation of Norwegian accounting rules permitted the use of a proportionate method when consolidating participation in jointly owned limited companies. The financial result of Varia Perdana Sdn. Bhd. have been proportionately consolidated in accordance with this new interpretation. Smedvig's financial statements have been restated accordingly for prior years.

(2) Translations of amounts from Norwegian kroner into U.S. dollars and from U.S. dollars into Norwegian kroner have been made solely for the convenience of the reader at an exchange rate of U.S.$1.00 = NOK 7.5800, the Noon Buying Rate on December 31, 1998.

(3) The Company terminated the newbuilding project West Navion II and expensed the full amount of costs incurred, (NOK 535 million), in 1998. In 1998, projects related to the previous Mobile Production Division, SPU 550 and SPU 4, were also terminated. As a result, a gain of NOK 6 million was realized on the SPU 550, whereas the sale of SPU 4 resulted in a loss of NOK 8 million.

In November 1998, the Company sold its platform drilling operation in the United Kingdom and realized a gain of NOK 165 million. Some activities related to the Reservoir and Well Technology Division were included in the sale.

In the third quarter of 1997, the Company sold the rig West Royal. The sale resulted in a capital gain of NOK 33 million. In the fourth quarter of 1997, the jack-up rig West Omikron was sold. This sale resulted in a capital gain of NOK 357 million.

(4) Earnings and dividends per share in accordance with Norwegian accounting rules have been calculated using the average number of shares outstanding, retroactively adjusted for (i) a two-for-one share split effected in April 1994 and (ii) the one-for-four bonus issue of B Shares to holders of A Shares effected in August 1996. The average numbers of shares outstanding for the years ended December 31, 1994 through 1998, as so adjusted, were 30,390,080, 33,495,108, 34,645,529, 41,023,375 and 41,179,115 respectively. Basic earnings per share in accordance with U.S. GAAP have been calculated using the average number of shares outstanding adjusted as above.

(5) Dividends in respect of a fiscal year are paid during the following fiscal year. The payment dates were May 16, 1995, May 21, 1996, May 21, 1997, May 19, 1998, and May 19, 1999, for the dividends relating to fiscal years 1994, 1995, 1996, 1997 and 1998, respectively. The Norwegian kroner/U.S. dollar exchange rate (Noon Buying Rate) on each of the respective payment dates was 6.3830, 6.6130, 7.0260, 7.5130 and 7,7425. The dividends per share, expressed in U.S. dollars based on the exchange rate at each respective payment date, were U.S.$0.09, U.S.$0.24, U.S.$0.28 U.S.$0.30 and U.S.$0.23.

(6) Diluted earnings per share in accordance with U.S. GAAP have been calculated using the average number of shares outstanding, retroactively adjusted for (1) a two-for-one share split effected in April 1994 and (ii) then one-for-four bonus issue of Class B Shares to holders of Class A Shares effected in August 1996 and adjusted to include the dilutive effect of all outstanding share options under the treasury stock method. The number of shares used in calculating diluted earnings per share in accordance with U.S. GAAP for the years ended December 31, 1994, 1995, 1996, 1997 and 1998 were 30,390,080, 33,678,870, 34,895,739, 41,154,810 and 41,193,778 respectively.

(7) Adjusted EBITDA (net income (loss) before income taxes, depreciation, financial income (expenses) and termination expenses and gains on sale of assets) is a supplemental financial measure commonly used by investors in the oil services industry and is being presented to provide supplemental information about the Company's ability to meet its future requirements for debt service, capital expenditures and working capital. Adjusted EBITDA should be read in conjunction with all of the financial data in the Selected Consolidated Financial Data, as well as the Consolidated Financial Statements and the Notes thereto prepared in accordance with generally accepted accounting principles. Adjusted EBITDA should not be considered as an alternative to net income (loss) or net cash flow provided by operating activities, or as a measure of the Company's liquidity.

Exchange Rates

The following table sets forth, for the periods indicated, certain information concerning the exchange rate for Norwegian kroner into United States dollars based on the Noon Buying Rate, expressed in Norwegian kroner per U.S. dollar.

	1994	1995	1996	1997	1998
High	7.5700	6.8110	6.6160	7.7564	8.3200
Low	6.4930	6.1155	6.3000	6.3420	7.3130
Average*	7.0074	6.3121	6.4492	7.0953	7.5549
Year-end	6.7640	6.3210	6.3750	7.3740	7.5800

* The average of the Noon Buying Rates on the last day of each month during the year.

On December 31,1998, the Noon Buying Rate was NOK 7.5800 = U.S.$1.00 (U.S.$0.1319 = NOK 1).

ITEM 9. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the Company's audited Consolidated Financial Statements, the Notes thereto and the other financial information included elsewhere herein. The Consolidated Financial Statements have been prepared in accordance with Norwegian GAAP, which differ in certain significant respects from U.S. GAAP. For a discussion of the principal differences between Norwegian GAAP and U.S. GAAP and a reconciliation of net income for each of the years in the three year period ended December 31, 1998, and shareholders' equity as of December 31, 1997 and 1998 from Norwegian GAAP to U.S. GAAP, see Note 30 to the Consolidated Financial Statements.

In 1996, a new interpretation of Norwegian accounting rules permitted the use of a proportionate method when consolidating participation in jointly owned limited companies. The financial results of Varia Perdana Sdn. Bhd. have been proportionately consolidated and results for prior years have been restated in accordance with this new interpretation.

Overview

The Company's business is dependent on exploration, development and production spending by its customer base of integrated oil and gas companies and independent exploration and production companies. Industry exploration, development and production spending depends on the earnings and cash flow of oil and gas producers, which are determined primarily by oil and gas prices and production volumes. Oil and gas prices are influenced by a variety of political and economic factors beyond the control of oil and gas companies, including worldwide demand for oil and gas, production levels, governmental policies regarding exploration and development of reserves, political conditions in producing countries and weather conditions. As a result of oil price fluctuations, oil wells may become economically unfeasible to operate, which may have an adverse effect on the Company's results of operations. Further, there can be no assurance that any customer would not terminate its contractual arrangements with the Company upon the occurrence of such event.

The Company's business is capital intensive and requires significant capital outlays for equipment, such as vessels, mobile drilling units, tender rigs and other fixed assets. As a result, the Company incurs high fixed costs in its operations. Any inability of the Company to secure contracts and maintain high utilization rates for its fixed assets and crews will have an adverse impact on the Company's operating results. There can be no assurance that the Company's existing and future contracts will provide revenues adequate to cover all fixed and variable costs associated with its rigs, or that such contracts will be renewed, extended or replaced upon expiration. In addition, capital expenditures for newbuilding projects are variable and initial estimates have increased as a result of many factors, including delayed delivery, project complexity and project management. Further increased costs and delivery delays may also have an adverse effect on the Company's results of operations and liquidity. No assurance can be given that the Company will not incur further capital expenditures or delays associated with its newbuilding projects. See "Item 1. Description of Business — Recent Developments". Several of the Company's contracts contain cancellation clauses that permit the customers to terminate the contract on the occurrence of specified events. The Company can give no assurance that any such party will not exercise its cancellation right in the event that such clause becomes effective.

The Company owns and operates a fleet of high specification drilling rigs for offshore oil and gas exploration, provides tender rig drilling services and provides reservoir and well technology products and services to the offshore oil and gas industry worldwide. Most of the Company's revenues and operating profits are currently attributable to operations in the North Sea (principally offshore Norway and the United Kingdom) and Southeast Asia (principally offshore Thailand and Brunei), although a substantial portion of the Company's assets are mobile. Approximately 84 percent, 81 percent and 80 percent of the Company's revenues excluding gains on sale of assets for the years ended December 31, 1996, 1997 and 1998, respectively, were attributable to the North Sea. Approximately 82 percent, 82 percent and 78 percent, respectively, of such North Sea revenues were attributable to Norway. The Company also has significant operations in Southeast Asia, principally offshore Thailand. Excluding gains on sale of assets, revenues attributable to Thailand represented approximately 7 percent, 5 percent and 6 percent of the Company's revenues (excluding such gains) for the years ended December 31, 1996, 1997 and 1998, respectively. See Note 2 to the Consolidated Financial Statements.

As of December 31, 1997, and effective as of January 1997, the Company divided its operations into five business divisions, three of which (Mobile Units Division, Platform Drilling Division and Tender Rigs Division) were the former subdivisions of the former Well Construction Division. The five divisions reported by the Company as of December 31, 1997, were: Mobile Units Division; Platform Drilling Division; Tender Rigs Division; Reservoir and Well Technology Division; and Mobile Production Division. On April 27, 1998, the Company's Board of Directors decided to discontinue a substantial portion of the operations of its Mobile Production Division, effective as of January 1, 1998. The operations that were discontinued included ENSCO 100, Balder FPU, SPU 4 and SPU 550. The Board also decided to report these businesses as Activities to be Discontinued and the Company's internal reporting was changed to comply with the Board's decision. The remaining operations, which consisted of the Company's businesses in the UK (mainly Altra and SRM) from that time were transferred from the Mobile Production Division to the Platform Drilling Division. In November 1998, after some months of negotiations, these remaining operations were sold to Deutag. See "Item 1. Description of Business—Recent Developments" and "Item 1. Description of Business—Activities To Be Discontinued".

Revenues. Excluding gains on sale of assets, approximately 30 percent, 32 percent and 31 percent of the Company's revenues for the years ended December 31, 1996, 1997 and 1998, respectively, were derived from the Mobile Units Division.

Substantially all of the Company's revenues excluding gains on sale of assets are derived from drilling contracts, production contracts or other service contracts, with additional revenues being generated from the sale of software and other technology products. Revenues from contracts are recognized during the period in which the services are rendered at the rate structures stipulated in the contracts. Revenues are primarily a function of dayrates and utilization, which can vary considerably over time depending on market demand. Contracts for services of the Company's Mobile Units, Platform Drilling and Tender Rigs divisions are typically multi-year. Actual contract duration generally varies depending on the number of wells involved and the time required for the particular project. Contracts generally provide an established dayrate structure, payable monthly, and some provide for lower dayrates during periods of mobilization or under certain circumstances when operations are interrupted or restricted. Under some contracts, the Company is entitled to additional payments for exceeding performance goals. The contracts also provide for the assumption by the customer of responsibility for changes in certain costs. Many contracts are extendable at the option of the other party. Such options may involve re-setting the dayrate based on current market rates. The contracts may be terminated by the customer upon the occurrence of certain force majeure events, and some contracts permit termination by the customer at any time without cause, subject to the payment of termination fees.

All of the Company's semi-submersible and jack-up rigs are currently employed offshore Norway under long-term contracts (generally two to four years), the earliest of which expires in 2000. During the periods presented, the Company also had a semi-submersible rig employed offshore Vietnam. The Company believes that the employment of its mobile drilling assets under long-term contracts will reduce the Company's exposure to market variations and fluctuations in oil prices over the next several years. Revenues are also affected by rig mobilizations, demobilizations and time out of service. The termination of certain contracts, or expiration if not renewed or replaced, can also adversely affect the Company's results of operations and liquidity. See the table captioned Mobile Drilling Units under "Item 1. Description of Business—Mobile Units Division".

The Company has a portfolio of high quality long-term contracts for platform drilling operations in the North Sea. The market for platform drilling is relatively mature. However, the Company believes that the current level of activity on fixed installations can be maintained by expanding its traditional line of drilling and maintenance services to include well workovers from existing platforms and new methods to increase the recovery rate of existing fields or to access untapped areas in the reservoirs. See the table captioned Fixed Installations under "Item 1. Description of Business—Platform Drilling Division".

Substantially all of the Company's revenues from tender rig operations are attributable to Thailand, Brunei and Malaysia. The Company also currently employs one tender rig offshore Congo. Tender rig contracts provided approximately NOK 414 million and NOK 662 million in revenues and approximately NOK 46 million and NOK 169 million in operating profit for the years ended December 31, 1997 and 1998, respectively. The Company believes that the contracts entered into in 1998 will increase revenues and operating profit for the next couple of years. See the table captioned Tender Rig Fleet under "Item 1. Description of Business—Tender Rigs Division". The Company believes the market outlook for tender rigs in the region should improve over the longer term due in part to rising energy consumption and an anticipated increase in new field developments in Southeast Asia. However, future developments in this market are difficult to predict. The Company owns a 49 percent interest in Varia Perdana, which owns four tender rigs. The Company believes this arrangement has enhanced its local presence in the developing Southeast Asian market. In 1997, the Company expanded its operation in this region with the acquisition of Petrodril, which owned one tender rig and one semi-submersible tender rig. In 1998, the Company signed an agreement to build another semi-submersible tender rig, further increasing its fleet of self-erecting tender units. This unit was delivered in March 1999.

Revenues from Reservoir and Well Technology are generated primarily through sales of software and service contracts for reservoir monitoring, reservoir engineering services and other related technology. A significant percentage of the revenues generated from sales of these products and services are attributable to the North Sea, primarily Norway. However, the share of sales abroad is increasing.

In 1997, revenues from Activities To Be Discontinued were generated primarily through the operation of West Omikron, now renamed ENSCO 100, and, until its cancellation in October 1997, the Balder FPU pre-operation contract. In 1998, revenues from Activities To Be Discontinued were generated primarily through the operation of ENSCO 100.

As part of its strategy, the Company acquires and disposes of assets from time to time. Gains on sale of assets have historically had a significant impact on the Company's net income, particularly in recent years during which the Company actively restructured its fleet. Capital gains in 1997 were NOK 390 million and resulted from the sale of two units from the Mobile Production Division. Excluding gains on sale of assets, the Company estimates that net income for the year ended December 31, 1997, would have been approximately NOK 266 million, compared to NOK 586 million, including such gains. In 1998, there was a loss of NOK 372 million. See "—Results of Operations—Year Ended December 31, 1998 Compared to Year Ended December 31, 1997—Termination Expenses and Gains on Sales of Assets".

During the period from 1991 to 1995, the Company's drilling units have been depreciated over an assumed economic life of 20 years. Similarly, costs for upgrading rigs have been capitalized and depreciated over the remaining economic life of the unit. Because the actual lives of the Company's drilling units have generally been longer than their estimated useful lives for depreciation purposes, this depreciation policy proved to be conservative, resulting in significant gains on sale of such assets. As a result, effective January 1, 1996, the Company's fourth generation semi-submersible and ultra-large jack-up rigs are being depreciated over an assumed economic life of 25 years. Commencing January 1, 1996 and 1997, respectively, the third generation rigs, West Delta and West Vanguard, are being depreciated over 25 years. See Note 1 to the Consolidated Financial Statements.

Operating Expenses. The Company's operating expenses are relatively constant in nature, although expenses vary from region to region. Operating expenses are generally higher in Norway and the United Kingdom than in Southeast Asia, due to the harsh environment in the North Sea and to higher personnel costs resulting from higher North Sea wages and other worker benefits in the United Kingdom and Norway. In general, operating expenses are not normally affected by changes in dayrates or significantly impacted by fluctuations in utilization, but tend to be higher during periods when rigs are operated under shorter term contracts. The largest expense items are personnel costs and depreciation. Other operating expenses include repair and maintenance, insurance and administrative costs. Personnel costs vary depending on headcount, geographic region and complexity of operations. The Company is generally able to offset in part the impact of pay increases for crews employed in platform drilling and mobile drilling operations, since most of its contracts for such services contain clauses that compensate the Company by an increase in dayrates for a portion of any such increases. Depreciation costs are affected by acquisitions, upgradings and disposals of assets. Goodwill arising from acquisitions is typically amortized over an assumed economic life of four to ten years. Costs for periodic rig overhauls, which are generally conducted every fourth or fifth operating year for semi-submersibles and jack-up rigs, are accrued and expensed annually based upon the estimated annual portion of such costs. Such costs may vary in accordance with the schedule for rig overhauls and actual disbursements. Effective January 1, 1998, the Company increased the annual provision for periodic overhauls to approximately NOK 82 million, compared to approximately NOK 40 million in 1997 and NOK 36 million in 1996. The increase in the provision is primarily the result of more stringent safety regulations for the mobile units to which the Company is subject and a change in the Company's policy with respect to periodic overhauls of tender rigs (including the tender rigs owned by Varia Perdana), which are now performed at regularly scheduled intervals rather than in connection with mobilizations under new contracts. As a result, operating expenses for subsequent periods will reflect higher provisions for repair and maintenance. Overall, insurance costs are relatively constant although premiums as a percentage of insured asset values have declined since 1991.

Operating Profit. Operating profit is a function of revenues and operating expenses. Fluctuations in operating profit are primarily caused by changes in revenues, since normal operating expenses tend to be relatively constant.

Minority Interest. At December 31, 1998, third parties owned minority interests in one of the Company's mobile units and KS Smedvig Production Contracting, which was responsible for the completion and delivery of the Balder FPU to Esso. In addition, at December 31, 1997, and prior to October 1996, there were minority interests in KS West Omikron and in the Company's subsidiary, Geomatic.

The following table sets forth certain income and expense items as a percentage of total revenues for the periods indicated:

	Year ended December 31,		
	1996	1997	1998
Revenues	100%	100%	100%
Personnel costs	49	51	40
Other operating expenses	29	27	36
Depreciation	14	11	8
Total operating expenses	92	89	84
Operating profit	8	11	16
Interest income	3	3	1
Foreign exchange gains (losses)	1	0	1
Interest expense	(4)	(4)	(2)
Net financial items	0	(1)	0
Income before other items	8	10	16
Termination expenses and gains on sale of assets	—	12	(10)
Income before income taxes	8	22	6
Income taxes	1	(2)	0
Minority interests	0	(1)	0
Net income	9%	19%	6%

Results of Operations

The following table sets forth the revenues, operating profit (loss) and adjusted cash flow by division for the periods indicated:

	Year ended December 31,		
	1996	1997	1998
		(in millions)	
Revenues			
Mobile Units	NOK 723	NOK 992	NOK 1,157
Platform Drilling	848	974	1,216
Tender Rigs	344	414	662
Reservoir and Well Technology	298	413	441
Activities to be Discontinued	238	291	203
Total revenues	2,451	3,084	3,679
Operating Profit (Loss)			
Mobile Units	122	246	316
Platform Drilling	56	74	113
Tender Rigs	28	46	169
Reservoir and well Technology	(22)	(15)	(14)
Activities to be Discontinued	24	2	(11)
Total operating profit	208	353	573
Cash Flow			
Net cash flow provided by operating activities	350	475	742
Net cash provided by (used in) investing activities	807	(998)	(2,529)
Net cash provided by (used in) financing activities	(1,216)	970	1,568
Adjusted cash flow (2) Mobile Units	266	397	470
Platform Drilling	85	106	146
Tender Rigs	67	112	235
Reservoir and Well Technology	(1)	12	20
Activities to be Discontinued	134	108	(10)
Total adjusted cash flow	551	735	861

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(1) Adjusted cash flow is defined as pre-tax operating profit (excluding gains on sale of assets) plus depreciation, adjusted for the non-cash portion of the provision for periodic rig overhauls. Adjusted cash flow, as so defined, should not be considered as an alternative to net income (loss) as an indicator of financial performance, or as an alternative to net cash flows from operating, investing and financing activities as a measure of the Company's liquidity.

Year Ended December 31, 1998 Compared to Year Ended December 31, 1997

Revenues

In 1998, the Company's consolidated revenues increased by NOK 595 million, or 19.3 percent, to NOK 3,679 million from NOK 3,084 million in 1997. Revenues increased from all divisions except for Activities to be Discontinued, most significantly from the Tender Rigs Division. The increase in revenues from the Tender Rigs Division primarily related to increased dayrates and utilization of tender rigs as well as an additional unit, the T-8, which commenced operations in February 1998. In addition, revenues from the Mobile Units Division increased from the Norwegian sector due to higher dayrates and higher utilization rates for the mobile drilling units. United Kingdom revenues, reported under the Platform Drilling Division increased significantly until the operation was sold in November.

Mobile Units. In 1998, revenues from the Mobile Units Division increased by NOK 165 million, or 16.6 percent, to NOK 1,157 million from NOK 992 million in 1997. This increase primarily was due to higher dayrates for all mobile drilling units as well as an increased NOK/U.S.$ exchange rate. The increase was strongest for West Delta and West Vanguard, but also West Alpha and West Epsilon achieved higher revenues in 1998.

Platform Drilling. In 1998, revenues from the Platform Drilling Division increased by NOK 242 million, or 24.9 percent, to NOK 1,216 million from NOK 974 million in 1997. The increase primarily was due to increased activities on the Ekofisk field, and was partially offset by decreased activity on the Oseberg and Veslefrikk fields. Revenues from operations on the British sector increased significantly until the operations were sold in November.

Tender Rigs. In 1998, revenues from the Tender Rigs Division increased by NOK 248 million, or 59.9 percent, to NOK 662 million from NOK 414 million in 1997. All the rigs except T-3 achieved higher revenues than in 1997 due to higher dayrates and increased utilization. The T-8, which started on a new contract in February following a major upgrading, had the largest increase, but also T-1, T-4 and T-6 experienced significant increases.

Reservoir and Well Technology. In 1998, revenues from the Reservoir and Well Technology Division increased by NOK 28 million, or 6.8 percent, to NOK 441 million from NOK 413 million in 1997, primarily due to growth in sales internationally of reservoir monitoring systems. Software sales also increased whereas the sale of services decreased due to the disposal of parts of the well engineering activities in November.

Activities to be Discontinued. In 1998, revenues from the Activities to be Discontinued Division decreased by NOK 88 million, or 30.2 percent, to NOK 203 million from NOK 291 million in 1997, due to the cancellation by Esso of the Balder contracts in October 1997.

Operating Expenses

In 1998, the Company's total operating expenses increased by NOK 375 million, or 13.7 percent, to NOK 3,106 million from NOK 2,731 million in 1997, primarily as a result of greater business volume. Depreciation expenses decreased by NOK 66 million, or 18.6 percent, to NOK 288 million from NOK 354 million in 1997. The decrease relates to the sale of West Omikron in 1997, partly offset by increases due to additional investments in 1998.

Mobile Units. In 1998, operating expenses excluding depreciation for units in the Mobile Units Division increased by NOK 78 million, or 12.8 percent, to NOK 687 million from NOK 609 million in 1997. A substantial part of the increase is attributable to increased personnel costs partly compensated for by higher dayrates. Operating expenses for West Delta increased compared to last year due to higher maintenance costs and miscellaneous equipment repairs in connection with the yard-stay in September. The Company's other mobile drilling units experienced only modest increases in operating expenses. Depreciation expenses increased by NOK 17 million, or 12.4 percent, to NOK 154 million from NOK 137 million in 1997. The increase is due to additional investments in 1998.

Platform Drilling. In 1998, operating expenses excluding depreciation for units in the Platform Drilling Division increased by NOK 202 million, or 23.3 percent, to NOK 1,070 million from NOK 868 million in 1997. The increase reflects a greater business volume. Depreciation expenses for Platform Drilling increased by NOK 1 million, or 3 percent, to NOK 33 million from NOK 32 million in 1997.

Tender Rigs. In 1998, operating expenses, excluding depreciation for tender rigs in the Tender Rigs Division, increased by NOK 115 million, or 36.9 percent, to NOK 427 million from NOK 312 million in 1997. After giving effect to the increase in utilization rate, operating expenses remained stable. Depreciation expenses increased by NOK 10 million, or 17.9 percent, to NOK 66 million from NOK 56 million in 1997, primarily due to the upgrade of T-8.

Reservoir and Well Technology. In 1998, operating expenses excluding depreciation for equipment and Goodwill in the Reservoir and Well Technology Division increased by NOK 20 million, or 5.0 percent, to

NOK 421 million from NOK 401 million in 1997. The increase primarily was due to increased business volume, but the increase was lower than the increase in revenues due to reduced overhead costs. Depreciation expenses increased by NOK 7 million, or 25.9 percent, to NOK 34 million from NOK 27 million in 1997, primarily due to increased amortization of goodwill.

Activities to be Discontinued. In 1998, operating expenses excluding depreciation for units in the Activities to be Discontinued Division increased by NOK 26 million, or 13.9 percent, to NOK 213 million from NOK 187 million in 1997. Ordinary operating expenses decreased in line with the reduction of business volume. The increase is, however, a consequence of the sale of West Omikron in December 1997. In 1998, the Company operated the rig under a Bareboat agreement and the capital expenses were recorded as operating expenses whereas the corresponding cost in 1997 was depreciation expenses. Consequently, depreciation expenses decreased by NOK 101 million, or 99.0 percent, to NOK 1 million from NOK 102 million in 1997.

Operating Profit

In 1998, the Company's operating profit increased by NOK 220 million, or 62.3 percent, to NOK 573 million from NOK 353 million in 1997. This increase primarily was due to the increased revenues from Tender Rigs Division generated by increased dayrates and higher utilization as well as one more unit in operation, while operating costs remained relatively stable. In addition, to a lesser extent, the increase in revenues from the Mobile Units Division and Platform Drilling Division also contributed to the increase in operating profit.

Interest Income

In 1998, interest income decreased by NOK 45 million, or 48.9 percent, to NOK 47 million from NOK 92 million in 1997. The decrease was due primarily to a lower average cash and cash equivalent balance in 1998.

Foreign Exchange

In 1998, net foreign exchange gain amounted to NOK 20 million compared to a net foreign exchange loss of NOK 1 million in 1997. The improvement was due to a strengthening of NOK compared to U.S.$ during 1998.

Interest Expense

In 1998, interest expense decreased by NOK 82 million, or 57.8 percent, to NOK 60 million from NOK 142 million in 1997. Long-term debt increased during the year, but interest expenses decreased as a larger portion of interest was capitalized on the newbuilding projects.

Termination Expenses and Gains on Sale of Assets

In 1998, Other Items amounted to a loss of NOK 372 million compared to a gain of NOK 390 million in 1997. In 1998, the Company terminated the newbuilding project West Navion II and expensed in this connection NOK 535 million. In addition, the projects SPU 550 and SPU 4 were terminated at a gain of NOK 6 million and a loss of NOK 8 million, respectively. In November 1998, the Company sold its platform drilling operation in the UK and realized a gain of NOK 165 million. In 1997, the Company had gains on sale of assets of NOK 390 million from the sales of West Omikron and West Royal.

Income Taxes

In 1998, income taxes were positive by NOK 16 million, which represented an improvement of NOK 74 million from 1997. The decrease is due primarily to the West Navion II termination expenses which are tax deductible; in addition, several of the mobile units and tender rigs are organized under the Norwegian zero taxation scheme, thus producing a positive net tax for the year.

Minority Interest

In 1998, minority interests accounted for a decrease in net income of NOK 11 million, primarily due to the allocation to the minority holders of net income from KS Smedvig Production Contracting and West Epsilon AS.

Net Income

The Company reported consolidated net income of NOK 213 million in 1998, a NOK 373 million decrease compared to 1997. The decrease was due to net expenses of NOK 372 million associated with the termination of the construction contract for a drillship, which was in part offset by the gain from the sale of the UK platform drilling division.

Year Ended December 31, 1997, Compared to Year Ended December 31, 1996

Revenues

Management discussion and analysis for 1997 have been restated to reflect that the Company as of January 1, 1998, changed accounting principles for the accounting of "Termination Expenses and Gains on Sale of Assets" as well as the discontinuation of the Mobile Production Division and the establishment of a new division, Activities to be Discontinued. This change has also had an impact on the numbers and analysis for the Platform Drilling Division.

In 1997, the Company's consolidated revenues increased by NOK 633 million, or 25.8 percent, to NOK 3,084 million from NOK 2,451 million in 1996. Revenues increased from all divisions, most significantly from the Mobile Units Division. The increase in revenues from the Mobile Units Division primarily related to increases in revenues in the Norwegian sector due to higher dayrates and higher utilization rates for the mobile drilling units. In addition, Southeast Asia and Congo revenues increased due to increased rates and utilization of tender rigs, while Thailand revenues decreased due to lower utilization of tender rigs. United Kingdom revenues increased primarily due to increased sales of consultancy services.

Mobile Units. In 1997, revenues from the Mobile Units Division increased by NOK 269 million, or 37.2 percent, to NOK 992 million from NOK 723 million in 1996. This increase primarily was due to higher dayrates and improved utilization rates of all mobile drilling units. In particular, West Delta's revenues increased by 295.6 percent as a result of being utilized for 10 months in 1997, compared to six months in 1996. Revenues from West Epsilon also increased significantly.

Platform Drilling. In 1997, revenues from the Platform Drilling Division increased by NOK 126 million, or 14.9 percent, to NOK 974 million from NOK 848 million in 1996. The increase primarily was due to increased activities on the Statfjord and Veslefrikk fields, and was partially offset by decreased activity on the Oseberg field. Revenues from operations on the British sector increased also due to the full year consolidation of Altra Consultants and increased activities on the platform operations.

Tender Rigs. In 1997, revenues from the Tender Rigs Division increased by NOK 70 million, or 20.4 percent, to NOK 414 million from NOK 344 million in 1996. This increase primarily relates to the acquisition of Petrodril as well as improved utilization rates for T-3, which were partially offset by reductions in utilization rates for T-1 and T-4.

Reservoir and Well Technology. In 1997, revenues from the Reservoir and Well Technology Division increased by NOK 115 million, or 38.6 percent, to NOK 413 million from NOK 298 million in 1996, primarily due to growth in sales and services and, to a lesser extent, the sales of software and reservoir monitoring systems from 1996.

Activities to be Discontinued. In 1997, revenues from the Activities to be Discontinued Division increased by NOK 53 million, or 22.3 percent, to NOK 291 million from NOK 238 million in 1996, primarily due to increased revenues from the Balder contract.

Operating Expenses

In 1997, the Company's operating expenses increased by NOK 488 million, or 21.8 percent, to NOK 2,731 million from NOK 2,243 million in 1996, primarily as a result of greater business volume by each division. Depreciation expenses increased by NOK 22 million, or 6.6 percent, to NOK 354 million from NOK 332 million in 1996. The increase relates primarily to increased depreciation for tender rigs due to the acquisition of Petrodril.

Mobile Units. In 1997, operating expenses excluding depreciation for units in the Mobile Units Division increased by NOK 148 million, or 32.1 percent, to NOK 609 million from NOK 461 million in 1996. The increase primarily was due to the operation of West Delta in Norway in 1997, which generally has higher operating expenses than other geographical areas. The Company's other mobile drilling units experienced only modest increases in operating expenses, primarily due to increased personnel expenses. However, in the case of West Alpha, which was upgraded in 1996, this increase was partially offset by reduced operating costs.

Platform Drilling. In 1997, operating expenses excluding depreciation for units in the Platform Drilling Division increased by NOK 108 million, or 14.2 percent, to NOK 868 million from NOK 760 million in 1996. The increase primarily was due to increased sales and platform drilling services on Statfjord and Veslefrikk as well as increased business volume in the British sector. Depreciation expenses for Platform Drilling of NOK 32 million remained unchanged.

Tender Rigs. In 1997, operating expenses, excluding depreciation for tender rigs in the Tender Rigs Division, increased by NOK 32 million, or 11.4 percent, to NOK 312 million from NOK 280 million in 1996. Depreciation expenses increased by NOK 20 million, or 55.6 percent, to NOK 56 million from NOK 36 million in 1996, primarily due to the acquisition of West Pelaut and T-8, which increased depreciation expenses by NOK 17 million. After giving effect to the acquisition and the change in utilization rate, operating expenses remained stable.

Reservoir and Well Technology. In 1997, operating expenses excluding depreciation for equipment in the Reservoir and Well Technology Division increased by NOK 102 million, or 34.1 percent, to NOK 401 million from NOK 299 million in 1996. The increase primarily was due to increased sales volume to higher expenses related to product development and establishment of an international sales network. Depreciation expenses increased by NOK 6 million or 28.6 percent to NOK 27 million from NOK 21 million in 1996, primarily due to the amortization of goodwill related to the acquisition of Petresim Integrated.

Activities to be Discontinued. In 1997, operating expenses excluding depreciation for the Activities to be Discontinued Division increased by NOK 76 million or, 68.5 percent, to NOK 187 million from NOK 111 million in 1996. This increase was due primarily to increased costs related to the Balder contract as a consequence of the cancellation of this contract in October 1997.

Operating Profit

In 1997, the Company's operating profit increased by NOK 145 million, or 69.7 percent, to NOK 353 million from NOK 208 million in 1996. This increase in operating profits primarily was due to the increased revenues from Mobile Units generated by increased dayrates, while operating costs remained relatively stable. In addition, to a lesser extent, the increase in revenues from the Platform Drilling Division and the Tender Rigs Division also contributed to the increase in operating profit.

Interest Income

Interest income in 1997 increased by NOK 23 million, or 33.3 percent, to NOK 92 million from NOK 69 million in 1996. The increase was due primarily to a higher average cash and cash equivalent balance in 1997 as well as marginally higher interest rates.

Foreign Exchange

In 1997, net foreign exchange loss amounted to NOK 1 million compared to a net foreign exchange gain of NOK 16 million in 1996.

Interest Expense

Interest expense in 1997 increased by NOK 34 million, or 31.5 percent, to NOK 142 million from NOK 108 million in 1996, primarily due to an increase in long-term debt incurred in connection with the acquisition of Petrodril and, to a lesser extent, cash payments on new buildings and a slight increase in interest rates.

Termination Expenses and Gains on Sale of Assets

The Company had gains on sale of assets of NOK 390 million in 1997, compared to no gains in 1996. The gains related to the sale of West Omikron and the sale of West Royal.

Income Taxes

Income tax expense in 1997 was NOK 58 million, which represented an increase of NOK 93 million from 1996. Norway introduced a new tax scheme for shipping and offshore companies which came into effect in 1996 for parts of the Company's activities. This entailed adjustments to the provisions for deferred taxes made previously consisting of a write-back of deferred taxes in the amount of NOK 84 million. As a result, the total income tax expense for 1996 resulted in a benefit of NOK 35 million including the deferred income tax benefit. The current income tax expense amounted to NOK 37 million and NOK 24 million in 1997 and 1996, respectively. The increase reflects higher taxable income from the tender rig operations.

Minority Interest

In 1997, minority interests accounted for a decrease in net income of NOK 48 million, primarily due to the allocation to the minority holders of net income from KS Smedvig Production Contracting, West Omikron and West Epsilon.

Net Income

The Company reported consolidated net income of NOK 586 million in 1997, a NOK 376 million increase compared to 1996. The increase was due to a NOK 145 million increase in operating profits from 1996, which was only in part offset by the NOK 28 million increase in net financial expenses.

Liquidity and Capital Resources

The Company's principal sources of funds are cash generated from operations as well as proceeds from borrowings and, from time to time, the sale of assets. The Company's principal requirements for funds are for capital expenditures. Net cash provided by operating activities increased to NOK 742 million in 1998 from NOK 475 million in 1997, primarily as a result of increased cash flow from ordinary operations.

Net cash used in investing activities in 1998 was NOK 2,529 million, compared to NOK 998 million in 1997. Capital expenditures in 1998 increased to NOK 2,631 million, from NOK 1,830 million in 1997. The increase in capital expenditures is primarily related to progress payments relating to the newbuilding projects, West Venture (NOK 897 million), West Navion (NOK 865 million) and West Menang (NOK 512 million). In addition, the Company has upgraded mobile units for NOK 139 million and Tender Rigs for NOK 110 million.

Net cash provided by financing activities amounted to NOK 1,568 million in 1998, compared to NOK 970 million in 1997. In 1998, primarily to finance capital expenditures, the Company borrowed NOK 2,320 million in long-term debt and repaid NOK 634 million of long-term debt, compared to NOK 1,484 and NOK 431 million in 1997, respectively. Proceeds from the sale of fixed assets relates to the proceeds from the disposal of the British platform drilling operations and well engineering services for approximately U.S.$45 million in November 1998. At December 31, 1998, the Company had cash, cash equivalents and short-term investments of NOK 882 million, with long-term debt of NOK 3,853 million. At December 31, 1997, cash, cash equivalents and short-term investments were NOK 1,074 million, with long-term debt of NOK 1,913 million.

At December 31, 1998, the Company had planned capital expenditures of approximately U.S.$200 million in 1999. In April and May 1999, the Company revised its plan of capital expenditures for 1999. The Company now plans to spend approximately U.S.$280 million in 1999. The increase is due to higher cost projections for West Navion and West Venture. The main part of the payments is progress payments for the newbuilding projects West Navion, West Venture and West Menang which are due in 1999.

The Company expects to fund capital expenditures, required debt and interest payments and working capital requirements through 2000 out of cash flow from operations, amounts remaining under the U.S.$650 million revolving credit facility (as defined below), sale of assets, additional funds raised in the capital markets or a combination of thereof.

The Company from time to time also reviews possible acquisitions of or investments in businesses, drilling units and other assets, and may in the future make capital commitments for such purposes. Any such acquisition could involve the payment by the Company of a substantial amount of cash financed by cash flows from operations, the issuance of additional equity or the incurrence of additional indebtedness.

On September 4, 1998, the Company entered into a secured U.S.$650 million reducing and revolving credit loan and guarantee facility (the U.S.$650 million Revolving Credit Facility) with a group of banks, for whom Skandinaviska Enskilda Banken AB (Publ.), Christiania Bank og Kreditkasse ASA, Citibank N.A., and Den norske Bank ASA acted as co-arrangers, which replaced most of the Company's existing loan facilities. This facility replaced the existing U.S.$250 million and U.S.$400 million unsecured revolving credit facilities. The new terms provide an amortization arrangement better targeted to the Company's financial needs. At the same time, the loan was secured and repriced at a somewhat higher interest rate margin. The U.S.$650 million Revolving Credit Facility has a final maturity date five years after the date of the agreement and provides for repayments or facility reductions, beginning 18 months after the date of the agreement, in six equal semi-annual installments or reductions of U.S.$60 million each, followed by a balloon repayment or reduction of the balance on the final maturity date. The U.S.$650 million Revolving Credit Facility bears interest at LIBOR plus 1.00 percent per annum until completion and charterer's acceptance of the drillship West Navion currently under construction and delivery and charterer's acceptance of the fifth generation semi-submersible drilling rig West Venture currently under construction, following which the rate will decrease by 0.125 percent per annum with effect from July 15, 2000. The U.S.$650 million Revolving Credit Facility contains certain financial and other covenants, including covenants requiring it to maintain (i) a minimum value adjusted net worth equal to the greater of U.S.$250 million, and 37.5 percent of its total value adjusted assets until October 10, 1999, increasing to U.S.$300 million and 40 percent, respectively, thereafter, (ii) a minimum liquidity balance (cash and cash equivalents) of U.S.$50 million and (iii) certain minimum current assets to current liabilities and interest coverage ratios. The Company is not permitted to declare or pay dividends in respect of any year in excess of 50 percent of average income before income taxes for such year and the two preceding years, nor to enter into any merger unless the Company will be the surviving entity and remain bound by the terms of the U.S.$650 million Revolving Credit Facility, and such merger would not reasonably be expected to adversely affect the Company's ability to comply with the financial covenants under the U.S.$650 million Revolving Credit Facility. At April 20, 1999, the Company had drawn down U.S.$530 million under the U.S.$650 million Revolving Credit Facility. The remaining portion under the U.S.$650 million Revolving Credit Facility will be used to finance capital expenditures for its construction projects.

Exposure to Currency Fluctuations

The Company is exposed to the risk of fluctuations in foreign currency exchange rates due to the international nature and scope of its operations. A substantial portion of the Company's revenues and expenses are denominated in U.S. dollars. The Company also incurs certain expenses in local currencies of the other countries in which it operates, although such expenses, except for those in Norwegian Kroner, do not constitute a material portion of the Company's expenses. The Company's foreign currency risks arise from; (i) fluctuations in exchange rates on the value of the Company's sales and purchases in foreign currencies (transaction exposure) and certain financial assets and liabilities (translation exposure) and (ii) the Company's investment in certain subsidiaries' net assets (translation exposure). The Company primarily uses U.S. dollar-denominated forward exchange contracts and foreign currency options to manage its foreign currency exposure. The Company's policy is to try to hedge most of its transaction risk primarily on its net exposure. The Company hedges part of the transaction risk of future cash flows from firm commitments such as contracts for mobile units. All realized and unrealized gains and losses on hedges of firm commitments are deferred and recognized in the period in which the hedged cash flows are received. It is the policy of the Company to hedge part of the translation risk of the net investment in the assets of certain subsidiaries, most of which are valued in U.S. dollars, through the designation of certain long-term borrowings in the same currency. See Note 20 to the Consolidated Financial Statements.

In general, a weakening of the Norwegian krone against other currencies in which the Company conducts operations tends to affect operating income positively, while a strengthening of the Norwegian krone against such other currencies tends to affect operating income negatively.

Interest Rate Risk Management

The Company uses certain financial instruments, including interest rate swaps and interest rate caps, to manage its exposure to changes in interest rates. The amount and nature of interest rate swaps and interest rate caps utilized by the Company is determined by management based upon an analysis of relevant factors, such as future cash flow forecasts, the amount and nature of the Company's financing activities and prevailing market conditions. See Note 20 to Consolidated Financial Statements.

Net Operating Loss Tax Carry Forwards

At December 31, 1998, the Company had net tax loss carry forwards of NOK 386 million. The loss carry forwards expire in varying amounts between 2004 and 2008. Norway introduced a new tax scheme for shipping and offshore companies which came into effect in 1996 for parts of the Company's activities, these activities are taxed at a zero rate.

Inflation

Inflation has not had a significant impact on the Company's operations and results during the periods presented. The inflation rates in Norway, according to the Norwegian Central Bureau of Statistics, were 1.3 percent, 2.6 percent and 2.3 percent in 1996, 1997 and 1998, respectively,

Year 2000

The so-called Year 2000 issue concerns computer applications that include only the last two digits in the number of the year. Without proper adjustments, such applications could mistake the year 2000 for the year 1900, thus creating serious operational problems.

The Company has recognized that Year 2000 could potentially cause problems to electronic, electro-mechanical and data processing systems, and has instructed its corporate departments and business divisions to take action in order to identify critical areas, map consequences of potential problems and implement corrective actions. Because the Year 2000 problem is a challenge faced by most companies, the Company is working with other organizations, suppliers, and competitors, to help resolve the problem on a cost effective basis for all the parties concerned.

The corporate departments and Business Divisions of the Company have established special Year 2000 projects (the "Millennium Projects") which consist of mapping, planning and following up activities related to Year 2000 issues with the objective to resolve potential problems and reduce the risk of system malfunctions.

The costs associated with the reprogramming are estimated to be NOK 19 million and will be expensed as they accrue. NOK 2 million were expensed in 1998.

Smedvig Offshore. Smedvig Offshore, together with its business partners, is currently mapping and dealing with the implications for its business activities in the event of potential problems with its electronic and electro-mechanical equipment as a result of computer data processing, in general, and the Year 2000, in particular. In March 1998, Smedvig Offshore set up a special Millennium Project Group, whose responsibility is to plan the activities of the Millennium (Year 2000) Project, and to work with its suppliers to bring this issue to a timely and successful conclusion. The focus is on Smedvig Offshore's major systems that have been identified as critical. The Project will also demand status reports from Smedvig Offshore's suppliers and its customers.

Smedvig Offshore's Millennium Project covers two main areas. One concerns the rig systems and includes such systems on the rig as drilling equipment and marine, positioning and communications systems. The other concerns the IT systems and includes such administrative systems as standard software and LAN/WAN.

The Millennium Project is also divided into two phases. Phase 1, which started on March 2, 1998, and was completed on September 21, 1998, included the registration and verification of equipment and components, risk evaluation, contacts with suppliers and tests. Phase 2, which started on July 13, 1998, and is expected to be completed on August 31, 1999, includes the implementation of problem testing and solutions.

Smedvig Asia. Smedvig Asia has been actively pursuing a program to identify and rectify possible problems with equipment on its rigs that may be adversely affected by a failure to recognize the millennium date change. The program has been implemented since April 1998.

Smedvig Asia recognizes that any piece of equipment containing process control chips incorporating date sensitive functions, even if those functions are dormant, may be vulnerable to failure. Smedvig Asia's program is built on a systematic approach aiming at ensuring that all such equipment onboard the rig, that is essential for the safe and proper operation of the rig, will function without fault in relation to the millennium date change. Its approach is to ensure that: (a) the manufacturers of any such vulnerable equipment give Smedvig Asia a written confirmation that the equipment will function properly in relation to the millennium date change; and (b) the equipment, to the extent that the manufacturers cannot or will not give such confirmation, is tested in order to determine whether it, separately or in combination with other equipment, will function properly in relation to the millennium date change. If the foregoing confirmation and/or tests show that the equipment might not function properly, then necessary steps will be taken to solve the problem.

Each rig manager working in conjunction with toolpushers, senior maintenance personnel and Smedvig Asia's technical manager, has produced rig specific lists of equipment that is essential for the safe and normal operations of the rig and that could be affected by the millennium date change. The manufacturers of the listed equipment have been asked to provide written confirmation that the specific piece of equipment will function properly in relation to the millennium date change. Each rig manager is responsible for following up on the confirmation process and setting up the testing of equipment if a written confirmation may not be obtained from the manufacturer. Each rig manager is also responsible for taking action to correct any problem so identified and keeping the client informed on the status of the relevant rig's compliance program.

Similarly, Smedvig Asia has carried out controls on office equipment in area offices such as its Kuala Belait office as well as its logistics office in Loyang and its main office in Singapore to ensure that its computer and communications equipment is year 2000 compliant.

Smedvig Technologies. Smedvig Technologies is currently running a Year 2000 compliance project assisted by Allianse IT, a consultancy firm, focusing on computing hardware, operating systems and software. The first phase of the project has involved detailed mapping of the foregoing systems and testing of Year 2000 compliance in close cooperation with the vendors. Non-compliant items have been identified and remedial action has been prescribed. This test in Norway will serve as the model for other geographical divisions in Smedvig Technologies. The plan is to complete the full project for Smedvig Technologies during the third quarter of 1999. Smedvig Technologies has sent a standard Year 2000 reply to clients and a standard request letter to suppliers.

In order to certify that all Smedvig Technologies' software products are year 2000 compliant, Smedvig Technologies has undertaken, in close cooperation with Cap Gemini, a systems evolutions phase, a systems modifications phase and a systems validations phase.

All Smedvig Technologies' software products rely on a variable number of third party software products. Therefore, any year 2000 problem related to the use of Smedvig Technologies software products may be caused by such third party products as well as by the Smedvig Technologies products themselves. However, to assist its customers in avoiding any year 2000 problems when using Smedvig Technologies software products, Smedvig Technologies has enclosed statements received from its major third party software vendors.

Based on the foregoing Year 2000 compliance projects, the Company believes that once the correcting and testing of computer systems is complete, internal systems and equipment will not give rise to significant operational problems as a result of the Year 2000 issue.

However, due to the general uncertainty inherent in the Year 2000 problem and about the readiness of the Company's external business partners, the Company is unable at this time to determine whether Year 2000 failures will have a material impact on its operations, liquidity or financial condition. Scenarios under consideration include: corruption of data in internal information systems; hardware failures; the failure of infrastructure services provided by governmental agencies, public utilities and other third party suppliers including energy and telecommunications; and health, safety and environmental issues relating to company facilities. If any of these were to occur, operations within the Company could be interrupted, in some cases for a prolonged period of time. If the Company's operations on rigs and platforms should come to a halt due to the operators not having adopted their systems, the Company's contracts include force majeure clauses which could result in reduced revenues for the Company. The global nature of the Company's operations adds to the risks currently being assessed. Extensive work is therefore in progress to help reduce the level of uncertainty and to establish most likely risk scenarios from which the Company will develop contingency plans. The Company offers services which to a limited extent are dependent on complex IT systems which could cause systematic or long-term problems for the Company's business operations as a whole. Therefore, the most reasonable likely worst case scenario consists of disruptions of the foregoing systems that could affect specific business processes, facilities or suppliers for a short time. The Company's operations are to a very limited extent dependent on external suppliers, except for the supply of spare parts and the Company believes that any disruptions caused by the key suppliers due to lack of Year 2000 compliance, will be insignificant.

In 1998 and 1999, the Company has implemented a new financial management system for the Group which is fully Year 2000 compliant. The Company does therefore not foresee any significant disruptions in its financial management processes. The Year 2000 compliance project has not delayed any other IT projects.

Companies within the drilling industry have to operate very strict contingency plans as failures of their operations can cause series damages to personnel, environment and equipment. The Company's contingency plans have been updated to take into account Year 2000 risks. The Company has tested and replaced critical components onboard its units to minimise risks. In addition, the Company and its suppliers have a large number of spares on stock as most of the components are standardized. In addition, plans are at present being drawn up to evaluate the necessity of bringing onboard additional personnel as well as additional spare parts.

The Company has made forward-looking statements regarding its Year 2000 program. Those statements include: the Company's expectations about the timetable for completion of each phase of its program and contingency plans; the estimated costs associated with the Year 2000 program; the Company's belief that its internal system and equipment will not give rise to significant operational problems as a result of the Year 2000 issue. The Company has described many of the risks associated with those forward-looking statements above. However, the Company wishes to caution the reader that there are many factors that could cause its actual results to differ materially from those stated in the forward-looking statements. This is especially the case because many aspects of its Year 2000 program are outside its control such as the performance of its third party suppliers, partners and customers. As a global company it operates in many different countries, some of which may not be addressing the Year 2000 problem to the same extent as in the United States. As a result, there may be unforeseen problems in different parts of the world. All of these factors make it impossible for the Company to ensure that it will be able to resolve all year 2000 problems in a timely manner to avoid materially adversely affecting its operations or business or exposing the group to third party liability.

Reconciliation of Norwegian GAAP to U.S. GAAP

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133 ("SFAS 133"), "Accounting for Derivative Instruments and Hedging Activities." This statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as "derivatives"), and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. This statement is effective for all fiscal quarters of fiscal years beginning after June 15, 1999. Management has not determined the effect of the adoption of SFAS 133.

During January 1998, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position 98-1 *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use* ("SOP 98-1") which becomes effective for all fiscal years beginning after December 15, 1998. Under SOP 91-1, computer software costs that are incurred in the preliminary project stage are expensed as incurred. Once specific capitalization criteria have been met, external direct costs of materials and service consumed in developing or obtaining internal-use computer software, certain personnel costs, and interest costs incurred when developing computer software for internal use are capitalized. Training costs and data conversion costs are generally expensed as incurred. Such capitalized costs are amortized over the estimated useful life of the software. The Company is evaluating the effect of the pronouncement.

The AICPA issued Statement of Positions 98-5, *Reporting on the Costs of Start-Up Activities* ("SOP 98-5") in April 1998 and is effective for fiscal periods beginning after December 15, 1998 SOP 98-5 provides guidance on the financial reporting of start-up costs and organization costs. It requires costs of start-up activities and organization costs to be expenses as incurred. The Company is evaluating the effect of the pronouncement.

ITEM 9A. QUALITATIVE AND QUANTITATIVE DISCLOSURE OF MARKET RISK

Financial Instruments and Risk Management

The Company has operations and assets in a number of countries world-wide. Consequently, the Company's results from operations are affected, when measured in NOK, by fluctuations in currency exchange rates, primarily relative to the U.S. dollar. When the NOK appreciates against other currencies, the Company's profits from operations in foreign currencies reported in NOK may decrease. Likewise, when the NOK depreciates against other currencies, the Company's profits from operations in foreign currencies reporting in NOK may increase. The Company is also exposed to changes in interest rates. Different financial instruments are used by the Company to manage these foreign currency and interest rate risks as summarised below:

Foreign Currency Risk Management

The Company's contract portfolio, forward contracts on currencies and foreign currency options are used to hedge the future value of income and expenses denominated in foreign currencies and the foreign exchange risk of Smedvig's assets and liabilities. The Company's foreign currency risks arise from: (i) fluctuations in exchange rates on the value of the Company's sales and purchases in foreign currencies (transaction exposure) and certain financial assets and liabilities (translation exposure) and (ii) the Company's investment in certain foreign subsidiaries' net asset (translation exposure).

The Company is hedging most of its transaction risk by way of its net exposure. At the end of 1998, the Company's long-term interest bearing debt was hedged against foreign currency fluctuations by operating contracts in the same currency which ensures sufficient cash flow to settle operating expenses, interest and installment payments. Foreign currency exposure related to long-term debt was eliminated by having operating income and expenses, interest expenses, installment payments and interest bearing debt being recorded at fixed exchange rates. Of the revolving credit facility with a limit of U.S.$650 million, U.S.$505 million was drawn at December 31, 1998.

Interest Rate Risk Management

The extent of the utilization of financial instruments for interest rate risk management is determined by reference to the Company's net debt exposure and the Company's views regarding future interest rates. At the end of 1998, approximately 70 percent of the Company's U.S. dollar interest bearing debt was hedged with interest rate swap agreements. This implies that the Company for this part of the debt has a fixed interest rate. Most of these contracts have a term of three to five years. If an interest rate swap agreement is terminated, the Company will continue to account for the gain or loss in accordance with the swap agreement for as long as the underlying loan still exists. In the case the Company terminates the underlying loan, the effect of the financial instrument is booked to the income statement. The Company's loans are denominated in U.S. dollars.

Sensitivity Analysis

The analysis below presents the sensitivity of the market or fair value of the Company's financial instruments to selected changes in market rates and prices. The range of changes chosen reflects the Company's view of changes that are reasonably possible over a one year period.

Interest Rates Sensitivity

The Company's interest bearing debt totalled NOK 3,749 million at year-end (corresponding to approximately U.S.$518 million), all of which is denominated in U.S.$. All loans have floating rates. However, at the end of the year, the Company had entered into interest swap arrangements for U.S.$359 million. A change of one percentage point (100 basis points) in the interest rate would result in a change of approximately NOK 2.9 million the Company's annual interest expenses. The effect is somewhat moderated by corresponding changes in interest income from the Company's cash and short-term investments.

Exchange Rates Sensitivity

A significant portion of the Company's revenues is generated in U.S.$. Similarly, its fixed assets are financed mainly in U.S.$. The Company's operating cash flow in U.S.$ exceeds annual installments and interest payments on the Company's debt. A strong U.S.$ therefore has a positive effect on the Company's financials, business statements and operations. This effect is somewhat moderated as a consequence of the Company's foreign exchange accounting policy (see Note 1 to the Consolidated Financial Statements). A 10% change in the NOK/U.S.$ exchange rate would alter the operating profit for the year by approximately NOK 60 million.

ITEM 10. DIRECTORS AND OFFICERS OF REGISTRANT

The principal executive officers and the directors of the Company at June 1, 1999, were:

Name	Age	Position	Date First Elected or Appointed Director or Executive Officer
Peter T. Smedvig	52	Chairman of Board of Directors	1989
Raymond De Smedt	60	Director	1994
Odd Martinsen	63	Director	1989
J. Larry Nichols	55	Director	1996
Andrew C. Salvesen	52	Director	1990
Christian Bull Eriksson	42	Chief Executive Officer	1999
Stale Rd	49	Executive Vice President	1989
Ketil Lenning	48	Executive Vice President Projects	1989
Ole Gladhaug	44	Chief Financial Officer	1995
Einar Bryne	51	Human Resource Director	1989
Torkell Gjerstad	44	Managing Director, Smedvig Technologies (Holding) AS	1995
Kjell E. Jacobsen	42	Managing Director, Smedvig Offshore AS	1991
Larry Robbins	51	Acting Managing Director, Smedvig Asia Ltd	1998
Petter Aalvik	33	Company Secretary	1997

Peter T. Smedvig has served as Chairman of the Board of the Company since 1989, and as Chairman of the Board in the private Smedvig companies since 1977. In 1987, on behalf of the private Smedvig companies, Mr. Smedvig acquired and merged ScanArmatur and ScanPaint to form Scana Industrier asa and listed the company on the Oslo Stock Exchange in 1995. The private Smedvig companies retain a 50.7 percent interest in Scana Industrier asa, and Mr. Smedvig has served as Chairman of the Board since 1991. Further, in connection with the private Smedvig companies' venture capital activity, Mr. Smedvig serves inter alia as Non-Executive Director of Shield Diagnostics Group plc, a company listed on the London Stock Exchange and as Non-Executive Director of Apax Partners Corporate Finance Limited, the corporate finance arm of Apax Partners & Co. Ventures Limited, a leading London-based venture capital organization.

Mr. Smedvig was President of the Norwegian Shipowners Association for the years 1986 and 1987. He was introduced to the oil and gas industry through his internships with Petrofina in 1971 and Elf Aquitaine in 1972 to 1973. Mr. Smedvig earned a Bachelor of Arts degree from the University of Newcastle upon Tyne in 1970 and a Master of Business Administration degree from the Wharton School of Finance and Commerce, University of Pennsylvania in 1972.

Raymond De Smedt joined the Company's Board of Directors in 1994. He is a Director and Executive Vice Chairman of Bitech Corporation, a public Canadian company. Mr. De Smedt is the Chairman of the Board of Norbay Oil Limited, a privately held company involved in oil and gas exploration and production with interests primarily in South America. He has over 35 years experience in the oil service industry, having held senior executive positions in various global regions with the Schlumberger group. Mr. De Smedt is a Civil Engineer who graduated from the (I.R.A.M.) University of Mons in Belgium in 1962.

Odd Martinsen has been a Director of the Company since 1989. After joining the Smedvig group in 1968, Mr. Martinsen has served as Executive Finance Officer and Chief Executive Officer of various Smedvig family companies. Until 1998, Mr. Martinsen was Chief Executive Officer of the Smedvig family companies: Smedvigs Rederi A/S, A/S Veni and Peder Smedvig Capital as. He is still employed as consultant to these companies. He is also a Director of the Board of Scana Industrier asa. Mr. Martinsen graduated from the Norwegian School of Economics and Business Administration in 1962.

J. Larry Nichols became a Director of the Company in 1996. He co-founded Devon Energy Corporation, a public U.S. oil and gas exploration and production company. He has been a Director of such entity since 1971 and President and Chief Executive Officer since 1980. He serves as a director of the Independent Petroleum Association of America. Mr. Nichols is the President of the Domestic Petroleum Council, and is also a Director of the National Petroleum Council and the National Association of Manufacturers. Mr. Nichols holds a geology degree from Princeton University and a law degree from the University of Michigan. He served as a law clerk to Mr. Chief Justice Earl Warren of the U.S. Supreme Court.

Andrew C. Salvesen has been a Director of Smedvig since 1990. Following three and a half years in the merchant navy, Mr. Salvesen joined Christian Salvesen plc, a large diversified Scottish company in 1970 and was responsible for the development of that company's oil field service interests headquartered in Aberdeen over a 17 year period. He was a director from 1989 until 1997 and joined the Board of Aggreko plc following the spinoff of this company from Christian Salvesen plc in September 1997. Mr. Salvesen is Chairman of Canvas Holidays and Roberston Research Holdings. He is also a director of Stirling Shipping, a leading North Sea supply ship operation. Mr. Salvesen was born in Edinburgh and educated in Scotland.

Christian Bull Eriksson joined the Company as new Chief Executive Officer on June 7, 1999. He has 16 years of experience in the oil and gas industry. From 1995 until he joined the Company, he served as Project Manager (1996-1998) and Country Director Norway (1998-1999) in Rockwater A/S Brown and Root Energy Services (Halliburton). From 1992 until 1995, he was Managing Director of RC Subsea A/S. He held several positions in Cameron, Saga Petroleum and Elf Aquitaine. Mr. Eriksson graduated from the Norwegian Technical Institute in Chemical Engineering/Petroleum Engineering in 1982.

Stale Rd acted as the Chief Executive Officer of the Company from the end of March 1998 until June 7, 1999. Mr. Rd is at present the Executive Vice President. Mr. Rd will return to his previous position as Managing Director of Smedvig Asia. Mr. Rd joined the Company in 1981 and served as Manager of Drilling from 1987 to 1990. From 1990 to 1996, Mr. Rd served first as the Company's Chief Financial Officer and then as the Company's Chief Operating Officer. From 1996 to 1998, he served as the Managing Director of Smedvig Asia Ltd., the Company's principal operating subsidiary for the Tender Rigs Division. Mr. Rd earned a degree in engineering and a degree in economics from the Norwegian School of Business Administration. He also received a Master of Business Administration degree from the University of Wisconsin in 1980.

Ketil Lenning is the Executive Vice President Projects. He joined the Company in 1989 and has served in various senior positions, including as Chief Operating Officer of the Company and Managing Director of Smedvig Production Contracting AS. He has 24 years of experience in the oil and gas industry, including 13 years with Norsk Hydro. He received a Bachelor of Science degree from Texas A&M University.

Ole Gladhaug is the Chief Financial Officer. He joined the Company in 1995. Mr. Gladhaug has 13 years experience from senior positions in banking, the securities industry, and the fund management industry. He serves as a non-Executive Director of the Board of the bank Sparebanken Rogaland. Mr. Gladhaug graduated from the Norwegian School of Economics and Business Administration in 1981, and also holds a degree in Political Science from the University of Bergen.

Einar Bryne is the Human Resource Director. He joined the Company in 1985. Previously, he served as Personnel and Administration Manager with Aker Norsco from 1978 to 1985. He earned a Bachelor of Arts degree in 1974.

Torkell Gjerstad serves as the Managing Director of Smedvig Technologies, the Company's principal operating subsidiary for the Reservoir and Well Technology Division. Prior to joining the Company in 1995, he managed Technica Ltd., a U.K. based consulting company with a worldwide presence within industrial risk management and associated software development. Mr. Gjerstad's previous experience includes petroleum research in Norway and employment with the French oil company Elf. He received a Master of Science degree from the Norwegian Institute of Technology in 1977.

Kjell E. Jacobsen is the Managing Director of Smedvig Offshore AS, the Company's principal operating subsidiary for the Norwegian operations of the Mobile Units Division and Platform Drilling Division. He joined the Company in 1991. Previously, he was employed by Statoil from 1981 to 1986 and in the corporate finance department of Citicorp in both Oslo and London from 1986 to 1991. Mr. Jacobsen graduated from the

Norwegian Naval Academy in 1976 and from the Norwegian School of Economics and Business Administration in 1981.

Larry Robbins is the Acting Managing Director of Smedvig Asia Ltd., the Company's principal operating subsidiary for the Tender Rigs Division. He joined Smedvig Asia Ltd. (formerly Robray Drilling Company) in 1981 and served as Area Manager in Kuala Lumpur, Malaysia from 1981 to 1993. From 1993 until 1998, he served as Operations Manager in Singapore. He earned a Bachelor of Science degree in Engineering from the University of Texas in 1972 and has been involved in offshore drilling operations since then.

Petter Aalvik joined the Company in 1997 and serves as the Company Secretary. Previous experience includes management consulting with the Boston Consulting Group in Stockholm and Oslo and a position as Vessel Manager for Stolt Comex Seaway S.A. in Haugesund. Mr. Aalvik graduated from the Norwegian Naval Academy in 1986 and received a Bachelor of Engineering degree from Glasgow University in 1990. He received a Master of Business Administration degree from INSEAD in 1994.

ITEM 11. COMPENSATION OF DIRECTORS AND OFFICERS

The aggregate amount of compensation paid by the Company and its subsidiaries for the year ended December 31, 1998, to all directors and officers of the Company as a group (13 persons) was approximately NOK 16 million, of which NOK 14 million consisted of salaries and NOK 2 million consisted of benefits in relation to exercised stock options in 1998. For the year ended December 31, 1998, the Chief Executive Officer received NOK 1.9 million in remuneration.

ITEM 12. OPTIONS TO PURCHASE SECURITIES FROM REGISTRANT OR SUBSIDIARIES

The Company currently has four share option plans. As of December 31, 1998, a total of 434,250 options, which are exercisable for an aggregate of 137,500 A Shares and 276,750 B Shares, were outstanding under such plans. Share options held by directors and officers of the Company as of December 31, 1998, are as follows: Peter T. Smedvig, 0; Raymond De Smedt, 0; Odd Martinsen, 0; Andrew C. Salvesen, 0; J. Larry Nichols, 0; Stale Rd, 101,500; Ketil Lenning, 57,750; Ole Gladhaug, 14,000; Einar Bryne, 17,125; Torkell Gjerstad, 1,500; Kjell E. Jacobsen, 39,000; Larry Robbins, 2,625; and Petter Aalvik, 1,125. As of December 31, 1998, the Board of Directors of the Company was authorized to grant a further 100,000 options, which are exercisable for an aggregate of 0 A Shares and 100,000 B Shares, from such plans. All share options are exercisable. See Note 19 to the Consolidated Financial Statements.

ITEM 13. INTEREST OF MANAGEMENT IN CERTAIN TRANSACTIONS

The Company and certain of its subsidiaries lease certain properties, including the Company's principal executive offices, from A/S Veni, which is a real estate company wholly owned, directly or indirectly, by Peter T. Smedvig and members of the Smedvig family and of which Odd Martinsen, a director of the Company, is a consultant. The aggregate amounts of rent paid in respect of such properties were NOK 13.9 million, NOK 16.0 million and NOK 11.0 million for 1996, 1997 and 1998, respectively.

The Smedvig family members identified in the above table own an aggregate of 10,854,427 Class A Shares (39.7 percent) and 1,607,282 Class B Shares (11.6 percent) directly and through Peder Smedvig Capital as, Smedvigs Rederi A/S, A/S Veni and DS AS Isbjrn. Pursuant to a shareholder agreement among the Smedvig family members identified above, Peder Smedvig Capital as, Smedvigs Rederi A/S, A/S Veni and DS AS Isbjørn, such shareholders vote their shares as a group on all matters at general meetings of shareholders of the Company.

PART III

ITEM 15. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 16. CHANGES IN SECURITIES AND CHANGES IN SECURITIES FOR REGISTERED SECURITIES

None.

PART IV

ITEM 18. FINANCIAL STATEMENTS

See pages F-1 through F-32 incorporated herein by reference.

ITEM 19. FINANCIAL STATEMENTS AND EXHIBITS

(a) Financial Statements.

The following financial statements and the notes thereto, together with the report of KPMG a/s, independent public accountants, thereon, are included herein:

(b) Exhibits.

1. English translation of Certificate of Registration, dated May 22, 1999.
2. Amendment No. 2 to Contract No. NH10604420, dated November 13, 1998, between Norsk Hydro Produksjon a.s. and Smedvig Offshore AS.*
3. U.S.$650 million Reducing and Revolving Credit Loan and Guarantee Facility Agreement, dated September 4, 1998, between the Company and a group of banks for whom Christiania Bank og Kreditkasse ASA, Citibank N.A., Den norske Bank ASA and Skandinaviska Enskilda Banken AB (Publ.) acted as Co-Arrangers.*

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* Certain portions of these documents have been omitted pursuant to a request for confidential treatment.

SIGNATURES

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, the Registrant certifies that it meets all of the requirements for filing this Annual Report on Form 20-F and has duly caused this Annual Report to be signed on its behalf by the undersigned, thereunto duly authorized.

SMEDVIG asa
(Registrant)

By: /s/ OLE GLADHAUG
Name: Ole Gladhaug
Title: Chief Financial Officer

Dated: June 22, 1999

REPORT OF INDEPENDENT ACCOUNTANTS

THE BOARD OF DIRECTORS
Smedvig asa

We have audited the consolidated balance sheets of Smedvig asa and subsidiaries as at December 31, 1997, and 1998, and the related consolidated statements of income and cash flows for each of the years in the three-year period ended December 31, 1998. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Norway, which are substantially the same as those generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Smedvig asa and subsidiaries as at December 31, 1997 and 1998, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1998, in conformity with generally accepted accounting principles in Norway.

Generally accepted accounting principles in Norway vary in certain significant respects from generally accepted accounting principles in the United States. Application of generally accepted accounting principles in the United States would have affected results of operations for each of the years in the three-year period ended December 31, 1998 and shareholders' equity as at December 31, 1997 and 1998 to the extent summarized in Note 30 to the Consolidated Financial Statements.

Stavanger, Norway
March 26, 1999

KPMG as

Aage K. Seldal
State Authorized Public Accountant

SMEDVIG asa AND SUBSIDIARIES

CONSOLIDATED INCOME STATEMENTS

	Notes	1996	1997	1998	1998
		(NOK)	(NOK)	(NOK)	(U.S.$ Note 1) (unaudited)
		(millions, except per share data)			
Revenues	(2)	2,451	3,084	3,679	485
Revenues					
Total revenues		2,451	3,084	3,679	485
Operating expenses		(1,199)	(1,560)	(1,480)	(195)
Personnel expenses					
Other operating expenses	(3)	(712)	(817)	(1,338)	(177)
Depreciation	(11)	(332)	(354)	(288)	(38)
Total operating expenses		(2,243)	(2,731)	(3,106)	(410)
Operating profit		208	353	573	75
Financial income and expenses		69	92	47	6
Interest income					
Foreign exchange gains (losses)		16	(1)	20	3
Interest expense		(108)	(142)	(60)	(8)
Net financial items		(23)	(51)	7	1
Income before other items		185	302	580	76
Other items	(4)	—	390	(372)	(49)
Termination expenses and gains on sale of assets					
Total other items		—	390	(372)	(49)
Income before income taxes		185	692	208	27
Income taxes	(5)	35	(58)	16	2
Minority interests		(10)	(48)	(11)	(1)
Net income		210	586	213	28
Earnings per share		6.06	14.30	5.17	.68
Diluted earnings per share		6.01	14.25	5.17	.68

The accompanying notes form an integral part of these Consolidated Financial Statements.

SMEDVIG asa AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	Notes	1997 (NOK)	1998 (NOK)	1998 (U.S.$ Note 1) (Unaudited)
		As at December 31, (in millions)		
ASSETS				
Current assets				
Cash and cash equivalents	(6)	767	579	76
Short-term investments	(7)	307	303	40
Accounts receivable	(8)	1,042	1,028	136
Spare parts		105	141	19
Total current assets		2,221	2,051	271
Long-term assets				
Shares, investments in and receivables from associated companies and long-term investments	(9)	158	177	23
Goodwill	(10)	90	50	7
Mobile units and tender rigs	(11)	2,509	2,550	336
Other tangible assets	(11)	165	183	24
Newbuilding contracts	(12)	3,525	4,228	558
Total long-term assets		6,447	7,188	948
Total assets		8,668	9,239	1,219
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current liabilities				
Short-term interest bearing debt	(13)	1	—	—
Income taxes payable	(5)	25	26	3
Dividends payable		93	72	10
Accounts payable		151	130	17
Other current liabilities	(14)	509	542	72
Total current liabilities		779	770	102
Long-term liabilities				
Long-term debt	(15)	1,913	3,853	508
Newbuilding contracts	(12)	2,019	800	106
Deferred income tax	(5)	59	7	1
Other long-term liabilities	(16)	378	130	17
Total long-term liabilities		4,369	4,790	632
Minority interests		103	82	11
Shareholders' equity				
Share capital (27,349,502 class A shares at NOK 3.00 and 13,864,125 class B shares at NOK 3.00)		123	124	16
Other equity		3,294	3,473	458
Total shareholders' equity	(18)	3,417	3,597	474
Total liabilities and shareholders' equity		8,668	9,239	1,219
Mortgages	(28)	—	3,853	508
Limited partnerships capital not paid	(28)	613	479	63
Guarantees	(28)	390	412	54
Off balance sheet items	(29)			

The accompanying notes form an integral part of these Consolidated Financial Statements.

SMEDVIG asa AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,			
	1996 (NOK)	1997 (NOK)	1998 (NOK)	1998 (U.S.$ Note 1) (Unaudited)
	(in millions)			
Cash flows from operating activities				
Net income	210	586	213	28
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	332	354	288	38
Gains on sale of assets	—	(390)	(167)	(22)
Gains on sale of securities	(7)	(1)	—	—
Loss on termination of newbuilding projects	—	—	537	71
Provision for periodic overhauls	11	28	6	1
Deferred income taxes	(59)	21	(52)	(7)
Minority interests	16	21	(21)	(3)
Change in assets and liabilities, net of effect of acquisitions:				
Accounts receivable	(631)	163	(116)	(15)
Spare parts	(15)	(29)	(44)	(6)
Income taxes payable	(36)	25	19	3
Accounts payable	(51)	81	(9)	(1)
Other current liabilities	580	(384)	88	12
Net cash provided by operating activities	350	475	742	99
Cash flows from investing activities				
Capital expenditures long-term investments	(155)	(1)	(19)	(3)
Capital expenditures on fixed assets and newbuilding contracts	(871)	(1,830)	(2,631)	(347)
Proceeds from sale of subsidiary, net of cash	—	—	269	35
Proceeds from sale of fixed assets	1,469	1,066	4	1
Paid upon termination of newbuilding projects	—	—	(156)	(21)
Proceeds from sale and maturity of securities	1,003	255	123	16
Purchase of securities	(617)	(270)	(119)	(16)
Purchase of subsidiary, net of cash acquired	(22)	(218)	—	—
Net cash provided by (used in) investing activities	807	(998)	(2,529)	(335)
Cash flows from financing activities				
Long-term debt borrowings	1,871	1,484	2,320	306
Payments of long-term debt	(3,913)	(431)	(634)	(84)
Equity issue	937	27	6	1
Minority's share of cash paid (cash received) in limited partnership	(57)	(28)	(31)	(4)
Dividends	(54)	(82)	(93)	(12)
Net cash provided by (used in) financing activities	(1,216)	970	1,568	207
Effect of exchange rate changes	18	77	31	4
Net increase (decrease) in cash and cash equivalents	(41)	524	(188)	(25)
Cash and cash equivalents at beginning of year	284	243	767	101
Cash and cash equivalents at end of year	243	767	579	76

The accompanying notes form an integral part of these Consolidated Financial Statements.

SMEDVIG asa AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying consolidated financial statements present the financial position of Smedvig asa and consolidated subsidiaries (the "Company" or "Smedvig"). The accounts have been prepared in accordance with generally accepted accounting principles in Norway ("Norwegian GAAP"). These accounting principles vary in certain significant respects from accounting principles generally accepted in the United States ("U.S. GAAP"). See Note 30 for a discussion of the principal differences between Norwegian GAAP and U.S. GAAP that affect the Company's consolidated net income and shareholders' equity.

Solely for the convenience of the reader, the consolidated financial statements as at and for the year ended December 31, 1998 have been translated from Norwegian kroner ("NOK") into United States dollars ("U.S.$") using the December 31, 1998 Noon Buying Rate of the Federal Reserve Bank of New York of U.S.$1.00 = NOK 7.580.

Nature of Operation

Smedvig is an offshore drilling contractor that has been a supplier to the oil and gas industry since 1965. It provides well construction and reservoir technology services to the oil and gas industry.

In addition to owning and operating mobile drilling rigs, Smedvig has contracts for production drilling and maintenance on fixed installations on the Norwegian shelf of the North Sea. The Company also pursues substantial drilling operations in Southeast Asia. In the technological field, the Company is involved with reservoir modeling and monitoring as well as related services.

Due to the international nature of the Company's operations, exchange rate movements give rise to foreign currency transaction risk and translation risk when revenues, costs and net assets of foreign subsidiaries are converted into Norwegian kroner. The Company seeks to hedge certain parts of its exposures to adverse movements in foreign exchange rates, see Note 20.

Use of Estimates

The preparation of financial statements is in conformity with generally accepted accounting principles requires the Company to make estimates and assumptions that effect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Basis of Consolidation

Subsidiaries in which the Company's holding exceeds 50 percent are consolidated in the financial statements.

The Company also consolidates certain limited partnerships and subsidiaries, in which the Company's holding is less than 50 percent, in accordance with the proportionate consolidation method.

The equity method of accounting is used for investments in associated companies in which the investment provides the Company with the ability to exercise significant influence over operating and financial policies of the investee company. Such influence is presumed to exist for investments in companies in which the Company's direct or indirect ownership is between 20 and 50 percent. Under the equity method, the Company's share of profits and losses of associated companies is included in the consolidated income statement under financial items.

As a result of changes in Norwegian GAAP, the Company in 1996 changed the reporting of its ownership interest in Varia Perdana Sdn. Bhd. Smedvig considers its participation in this company to be an integral part of its operations. The Company has therefore changed the accounting for this investment from using the equity method to using the proportionate consolidation method.

The cost method of accounting is used for investments in associated companies during which the Company's ownership is less than 20 percent.

All material intercompany transactions and internal sales have been eliminated during consolidation.

Revenue Recognition

The substantial majority of the Company's revenues are derived from dayrate-based drilling contracts or other service contracts. Revenues are recognized in the period that services are rendered at the rates established in the contracts.

Other items

Sale of material assets or parts of a business division is classified as "Other items" in the Income Statements, and presented in the Income Statements between Financial items and Income before income taxes.

Foreign Currencies

Bank deposits, short-term receivables and short-term liabilities denominated in foreign currency are translated at year-end exchange rates. Long-term liabilities which are not hedged are translated at the higher of either the foreign exchange rate at the date the liability was accrued or the year-end exchange rate. Smedvig does not record unrealized foreign exchange loss/gain on long-term debt where the rig securing the debt has an employment contract that provides a net cash flow in the same currency sufficient to retire the debt.

Foreign Subsidiaries

In the consolidated financial statements, the balance sheets of foreign subsidiaries are translated into Norwegian kroner at the foreign exchange rate at the balance sheet date, and the income statements are translated at the average exchange rate prevailing during the year. Exchange rate differences arising on the translation of financial statements of foreign subsidiaries are recorded as a separate component of shareholders' equity.

Cash and Bank Deposits

Cash and cash equivalents include other highly liquid investments with an original maturity of ninety days or less.

Short-term Investments

Short-term investments are recorded at the lower of cost or market value determined on a portfolio basis. A charge against income is recorded in the period in which the market value of the investment portfolio is less than cost. Single investments with material and permanent decline in value are written down separately.

Accounts Receivable

Accounts receivable are recorded net of an allowance for doubtful accounts, if any.

Spare Parts

Spare parts are generally recorded at the lower of cost or market value. Spare parts are shown net of a reserve for obsolete parts and parts with low turnover rate.

Fixed Assets and Depreciation

Fixed assets are recorded at historical cost less accumulated depreciation. Fixed assets are depreciated on a straight line basis over the economic life of the assets. The Company's mobile units and semi-tenders are depreciated over 25 years while the rest of the tender rigs are depreciated over 20 years. Drilling equipment and fixtures are estimated to have useful lives ranging from three to ten years, depending upon their use.

Towards the end of a rig's operating life the Company may in certain situations decide to upgrade a rig in order to extend the lifetime of the unit or find alternative employment for the rig. If the Company deems it financially justifiable to undertake the upgrading, the associated cost will be capitalized and depreciated over the remaining life of the unit.

Newbuilding Contracts

Newbuilding contracts are included in fixed assets at their full contractual value and the corresponding liability is entered as newbuilding contract under long-term liabilities. Other expenditures and interest expenses related to the construction of the vessel during the construction period are capitalized. Installments to the yard are recorded at the exchange rate at the date of payment, whereas outstanding contract liabilities are recorded at the year-end exchange rate.

Capitalized Interests

Interest expenses relating to upgradings and newbuildings are capitalized based on the amount of accumulated expenditures for the applicable project during the construction period using the Company's current available rate of borrowing.

Pensions

The Company has several defined benefit plans with retirement, death and termination benefits. The retirement benefits are generally a function of years of employment and amount of compensation. The plans are primarily funded through payments to insurance companies.

The Company records its pension costs in the period during which the services are rendered by employees and amounts are based on actuarial calculations.

Long-term Maintenance

Provision for periodic overhauls on mobile units and tender rigs is accrued evenly over the anticipated period between repairs, generally five years. On disposal of a mobile unit or tender rig, the related provision for major repairs is included in the calculation of the gain or loss on disposal.

All other maintenance and repair costs are expensed when incurred.

Derivative Financial Instruments

Forward exchange contracts

Unrealized gains on forward exchange contracts and currency options are deferred and recognized only when realized while net unrealized losses on forward exchange contracts and currency options are expensed as they occur. The Company's forward exchange contracts do not qualify for hedge accounting treatment, as they are not designated as hedges of specific assets, liabilities or firm commitments.

The Company's criteria to qualify for hedge accounting are:

— The instrument must be related to a foreign currency asset, liability or firm commitment whose characteristics have been identified;

— The nominal amount of the instrument cannot exceed the amount of the hedged item;

— It must involve the same currency as the hedged item; and

— It must reduce the risk of foreign currency exchange movements on the Company's operations.

Interest rate swap and forward rate agreements

Interest rate swap agreements and forward rate agreements that are designated as a hedge of a debt obligation are accounted for on an accrual basis. That is, the interest payable and interest receivable under the agreements are accrued and recorded as an adjustment to the interest expense of the designated liability.

Amounts due from or payable to the counterparties of interest rate swaps and forward rate agreements are recorded on an accrual basis at each reporting date based on amounts computed by reference to the respective agreement.

It is the policy of the Company that the terms and the contractual maturities of the interest rate swap agreements must correspond to the underlying debt obligation to which the swap relates in order to qualify for hedge accounting.

The Company's criteria to qualify for hedge accounting are:

— The instrument must be related to an asset or a liability;

— The nominal amount of the instrument cannot exceed the amount of the hedged item;

— The terms and the contractual maturities of the instrument must correlate to the underlying hedged item; and

— It must change the character of the interest rate by converting a variable rate to a fixed rate or vice versa.

Income Taxes

Income tax expense consists of taxes currently payable and changes in deferred tax assets and liabilities. Deferred tax assets and liabilities are based on temporary differences that arise between the book basis and tax basis of assets and liabilities and the future tax benefit of tax loss carry forwards.

Deferred tax assets in a specific tax jurisdiction can only be recognized if it is probable that the future benefit will be realized. Such assets cannot exceed the amount of deferred tax liabilities in that tax jurisdiction.

With effect from 1996 a tax scheme for shipowning and offshore companies was introduced in Norway. According to the principles of the scheme no income tax is assessed on the income of those companies that qualify and elect to participate in the scheme. Under the scheme taxation will occur when dividends are paid by companies within the scheme or when a company decides to withdraw from the scheme.

Smedvig has joined the tax scheme for the majority of its fleet. For companies entering the scheme deferred tax on temporary differences was reversed. Since Smedvig deems it preferable to stay within the new scheme for a long time, no provision for taxes has been provided for on the subsidiaries within the scheme.

The Company aims to distribute a dividend every year. The dividend for each year will depend on the Company's earnings and financial situation. The dividend will primarily be taken from earnings which have been subject to ordinary taxation, from distributable reserves and finally from earnings under the Norwegian zero taxation scheme.

Earnings per Share

Earnings per share are calculated as net income divided by the weighted average number of shares outstanding. The average number of shares has been adjusted for the bonus issue in August 1996 and the issue of B-shares in November 1996. The average number of shares for the years 1996, 1997 and 1998 is consequently: 34,645,529, 41,023,375 and 41,179,115 respectively.

Diluted Earnings per Share

Diluted earnings per share takes into account all potential outstanding shares in the period which have a dilutive effect. The calculation does not take into account 214,875 share options which at December 31, 1998 are accretive to earnings per share. At December 31, 1997 31,500 share options were accretive to earnings per share.

Goodwill

Acquisitions are accounted for using the purchase method. The excess of the purchase price over the fair value of the net assets acquired is recorded as goodwill and amortized on a straight-line basis, generally over periods of four to ten years.

Note 2 — SEGMENT INFORMATION

The Company provides well construction services and reservoir and well technology products and services to the offshore oil and gas industry. There has not been any intersegment sales. The accounting principles for the segments are the same as for consolidated accounts.

Geographic segment data

The following presents the Company's revenues, earnings and assets by geographic area:

Revenues from unaffiliated customers

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Norway	1,685	2,049	2,288
Brunei	—	102	122
United Kingdom	363	440	644
Thailand	178	160	224
Other (principally Southeast Asia)	225	333	401
Total	2,451	3,084	3,679

Earnings before income taxes

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Norway (1)	164	711	(122)
Brunei	—	12	35
United Kingdom (2)	1	(6)	186
Thailand	15	12	63
Other (principally Southeast Asia) (3)	28	14	39
Operating profit	208	743	201
Other income (expense)	(23)	(51)	7
Earnings before income taxes	185	692	208

Tangible assets (4)

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Norway (5)	2,946	5,419	5,371
Brunei (6)	—	350	1,130
United Kingdom	24	29	—
Thailand	129	86	96
Other (principally Southeast Asia)	100	315	364
Total	3,199	6,199	6,961

(1) Included in these amounts are termination expenses of NOK 529 million in 1998 and gains on sale of assets of NOK 390 million for the year ended December 31, 1997.

(2) Included in these amounts are gains on sale of the platform drilling operation in UK of NOK 165 million for the year ended December 31, 1998.

(3) Included in these amounts are termination expenses of NOK 8 million for the year ended December 31, 1998.

(4) A substantial portion of the Company's assets are mobile. Asset locations at the end of a period are not necessarily indicative of the geographic distribution of the revenues or operating profits generated by such assets during such period.

(5) Included in these amounts are newbuilding contract amounts of NOK 3,453 million, NOK 3,525 million and NOK 422 million for the years ended December 31, 1998, 1997 and 1996, respectively.

(6) Included in these amounts is a newbuilding contract of NOK 775 million for the year ended December 31, 1998.

Industry segment data

Information regarding the Company's industry segments is as follows:

Revenues from unaffiliated customers

	Year ended December 31,		
	1996	**1997**	**1998**
	(NOK in millions)		
Mobile Units	723	992	1,157
Platform Drilling	848	974	1,216
Tender Rigs	344	414	662
Reservoir and Well Technology	298	413	441
Activities to be Discontinued (1)	238	291	203
Total	2,451	3,084	3,679

Depreciation and amortization

	Year ended December 31,		
	1996	**1997**	**1998**
	(NOK in millions)		
Mobile Units	140	137	154
Platform Drilling	32	32	33
Tender Rigs	36	56	66
Reservoir and Well Technology	21	27	34
Activities to be Discontinued (1)	103	102	1
Total	332	354	288

Earnings before income taxes

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Mobile Units	122	246	316
Platform Drilling	56	74	113
Tender Rigs	28	46	169
Reservoir and Well Technology	(22)	(15)	(14)
Activities to be Discontinued (1)	24	2	(11)
Operating profit	208	353	573
Net financial items	(23)	(51)	7
Other items (2) and (3)	—	390	(372)
Total	185	692	208

Total assets

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Mobile Units (4)	2,881	5,423	6,530
Platform Drilling	255	305	148
Tender Rigs (5)	420	1,414	2,059
Reservoir and Well Technology	194	257	275
Activities to be Discontinued (1) and (6)	1,486	1,269	227
Total	5,236	8,668	9,239

Capital expenditures

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Mobile Units	451	1,587	1,943
Platform Drilling	16	33	46
Tender Rigs	3	126	625
Reservoir and Well Technology	56	21	17
Activities to be Discontinued (1)	345	63	0
Total	871	1,830	2,631

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(1) On April 27, 1998, the Board of Directors decided to discontinue a substantial portion of the operations in its Mobile Productions segment. The businesses that were discontinued included ENSCO 100, Balder FPU, SPU 4 and SPU 550. The Board also decided to report these businesses as Activities To Be Discontinued and the Company's internal reporting was changed to comply with the Board's decision. The remaining operations which consisted of the Company's businesses in the UK (mainly Altra and SRM) from that time were transferred from Mobile Production to Platform Drilling. In November 1998, after some months with negotiations, these remaining operations were sold to Deutag.

(2) Included in these amounts are gains on sale of the platform drilling operation in UK of NOK 165 million for the year ended December 31, 1998.

(3) Included in these amounts are termination expenses related to a newbuilding project of NOK 537 million for the year ended December 31, 1998. For 1997, a gain on sale of assets of NOK 390 million is included.

(4) Included in these amounts are newbuilding contract amounts of NOK 3,453 million and NOK 3,041 million for the years ended December 31, 1998 and 1997, respectively.

(5) Included in these amounts are newbuilding contract amounts of NOK 775 million for the year ended December 31, 1998.

(6) Included in these amounts are newbuilding contract amounts of NOK 484 million and NOK 422 million for the years ended December 31, 1997 and 1996, respectively.

Note 3 — PROVISION FOR PERIODIC OVERHAUL

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Changes in the provision for periodic overhaul:			
Balance at the beginning of the year	24	35	69
Provided from acquisitions	—	6	—
Provisions	36	40	82
Costs incurred	(25)	(12)	(76)
Balance at the end of the year	35	69	75

Note 4 — TERMINATION EXPENSES AND GAINS ON SALE OF ASSETS

The Company terminated the newbuilding project West Navion II and expensed in this connection the full amount, NOK 535 million, in 1998. During the year projects also related to the previous Mobile Production Division, SPU 550 and SPU 4, were terminated. As a result a gain of NOK 6 million was realized on the SPU 550, whereas the sale of SPU 4 resulted in a loss of NOK 8 million.

Mid-November, the Company sold its platform drilling operation in the United Kingdom and realized a gain of NOK 165 million. Some activities related to the Reservoir and Well Technology Division were included in the sale.

In the third quarter of 1997, the Company sold the rig West Royal. The sale resulted in a capital gain of NOK 33 million. In the fourth quarter of 1997, the jack-up rig West Omikron was sold. This sale resulted in a capital gain of NOK 357 million.

Reconciliation of remaining — and discontinuing operations:

	Year ended December 31,					
	Remaining operations			Discontinuing operations		
	1996	1997	1998	1996	1997	1998
	(NOK in millions)					
Revenues						
Revenues	2,111	2,558	3,092	340	526	587
Operating expenses						
Personnel costs	(1,025)	(1,273)	(1,134)	(174)	(287)	(346)
Other operating expenses	(671)	(699)	(1,139)	(41)	(118)	(199)
Depreciation	(215)	(233)	(266)	(117)	(121)	(22)
Total operating expenses	(1,911)	(2,205)	(2,539)	(332)	(526)	(567)
Operating profit	200	353	553	8	0	20
Financial income and expenses						
Interest income	66	90	44	3	2	3
Foreign exchange gains	18	—	22	(2)	(1)	(2)
Interest expense	(103)	(135)	(56)	(5)	(7)	(4)
Net financial items	(19)	(45)	10	(4)	(6)	(3)
Other items						
Termination expenses and gains on sale of assets	—	—	—	—	390	(372)
Total other items	—	—	—	—	390	(372)
Income before income taxes	181	308	563	4	384	(355)
Income taxes	36	(53)	(89)	(1)	(5)	105
Minority interests	(10)	(48)	(11)	—	—	—
Net income	207	207	463	3	379	(250)

Note 5 — INCOME TAXES

Allocation of income before income taxes:

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Norway	177	773	28
Outside Norway	8	(81)	180
Total	185	692	208

Income tax expense (benefit) consists of the following:

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Payable tax:			
Norway	—	12	1
Outside Norway	24	25	35
Total payable tax	24	37	36
Total deferred income tax expense (benefit) Norway	(59)	21	(52)
Total	(35)	58	(16)

The principal differences between the expected tax expense computed by applying the Norwegian statutory tax rate of 28 percent to income before income taxes and the actual tax expense are as follows:

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
"Expected" income taxes	52	194	58
Foreign tax rate differential	27	44	(1)
Shipowners' taxation in Norway	(84)	(196)	(130)
Tax deductible expenses	(30)	—	—
Other	—	16	11
Total	(35)	58	(62)
Valuation allowances (1)	—	—	46
Income taxes	(35)	58	(16)

Deferred income taxes reflect the impact of temporary differences between the amount of assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes. The net deferred tax liability consists of the following:

	Year ended December 31,	
	1997	1998
	(NOK in millions)	
Deferred tax assets:		
Tax loss carry forward	81	108
Provisions	23	30
Other	1	—
Gross deferred tax assets	105	138
Valuation allowance (1)	—	(46)
Net deferred tax assets	105	92
Deferred tax liabilities:		
Fixed assets	68	37
Other	96	62
Gross deferred tax liabilities	164	99
Net deferred tax liabilities	59	7

(1) Norwegian GAAP do not allow deferred income tax assets. NOK 46 million is therefore recorded as a valuation allowance.

At December 31, 1998, the Company's deferred tax asset of NOK 108 million consists of NOK 386 million in tax loss carry forward, which expire in varying amounts between 2004 to 2008. The Company is of the opinion that the remaining balance of deferred tax assets is expected to be realized through future profits and the reversal of taxable temporary differences.

Note 6 — CASH AND CASH EQUIVALENTS

	Year ended December 31,	
	1997	1998
	(NOK in millions)	
Cash	49	378
Certificates of deposit	718	201
Total	767	579

The Company has NOK 42 million and NOK 37 million deposited in banks as of December 31, 1998 and 1997, respectively, related to withholding taxes.

Note 7 — SHORT-TERM INVESTMENTS

	As at December 31,							
	1997				1998			
	Book value	Unrealized gains	Unrealized losses	Fair value	Book value	Unrealized Gains	Unrealized losses	Fair value
	(NOK in millions)							
Debt securities (bonds)	307	2	—	309	303	—	—	303

The maturity dates of the Company's short-term investments in debt securities with an original maturity of greater than ninety days as of December 31, 1998, were:

	(NOK in millions)
Less than one year	40
1 — 5 years	188
5 — 10 years	75
Total	303

Other information regarding the short-term investments:

	As at December 31,		
	1996	1997	1998
	(NOK in millions)		
Purchases	617	270	119
Proceeds from sales	993	255	123
Proceeds from maturities	10	—	—
Realized gains	8	1	—
Realized losses	—	(1)	—

Realized gains and losses on the sale of securities are determined by reference to the carrying value at the time when the specific security is sold.

Note 8 — ACCOUNTS RECEIVABLE

	As at December 31, 1997	1998
	(NOK in millions)	
Trade receivables	767	608
Other receivables	275	420
Total	1,042	1,028

The trade receivables are primarily from major international oil and gas companies. The Company continually evaluates the credit risk associated with each customer and, when considered necessary, requires certain guarantees. At December 31, 1998 and 1997 no "Provision for doubtful accounts" was considered necessary. Of other receivables, approximately net NOK 175 million are from Esso Norge/Keppel-Fels. See Note 29 for further details regarding this issue.

The following table summarizes revenues from major customers as a percentage of total revenues (revenues in excess of 10 percent for the period):

	Year ended December 31, 1996	1997	1998
Statoil	30%	28%	26%
Norsk Hydro	7%	20%	21%
Phillips Petroleum	10%	12%	8%

Note 9 — SHARES, INVESTMENTS IN AND RECEIVABLES FROM ASSOCIATED COMPANIES AND LONG-TERM INVESTMENTS

	As at December 31, 1997	1998
	(NOK in millions)	
Shares North Norway Drilling Co. AS	2	2
Shares Offshore & Marine ASA	20	23
Receivables KS West Alpha	126	112
Other	10	40
Total	158	177

The company has financed KS West Alpha. The rig is in operation, and the debt is being repaid in accordance with the loan agreement.

Note 10 — GOODWILL

	As at December 31, 1997	1998
	(NOK in millions)	
Cost	183	204
Goodwill from acquisitions during the year	21	6
Reduction due to sale of companies	—	(39)
Accumulated amortization	(114)	(121)
Net book value	90	50
Amortization	27	28

Note 11 — MOBILE UNITS, TENDER RIGS AND OTHER TANGIBLE ASSETS

	Mobile units and tender rigs	Drilling equipment inventory and fixtures	Buildings	Total
Original cost January 1, 1998	4,365	320	30	4,715
Additions	249	104	5	358
Disposals	—	(155)	(18)	(173)
Cost December 31, 1998	4,614	269	17	4,900
Accumulated depreciation December 31, 1998	(2,064)	(102)	(1)	(2,167)
Net value at December 31, 1998	2,550	167	16	2,733
Depreciation for the year 1998	197	62	1	260
Percentage depreciation	4-13%	10-30%	4%	

Investments and sales of fixed assets:

	1997		1998	
	Investment	Sales	Investment	Sales
Mobile units and tender rigs	864	1,060	249	—
Drilling equipment, inventory, and fixtures	109	6	104	214
Buildings	—	—	5	12
Total	973	1,066	358	226

Note 12 — NEWBUILDING CONTRACTS

At December 31, 1998, the company had the following newbuilding contracts:

Unit	Yard	Newbuilding contract assets	Newbuilding contract liabilities
West Venture	Hitachi, Japan	2,028	537
West Navion (1)	Samsung, South Korea/Offshore & Marine, Norway	1,425	—
West Menang	Keppel Shipyard, Singapore	775	263
Total		4,228	800

(1) Navion ASA has an option to purchase the Company's 50 percent share of West Navion. This option can be exercised at the earliest four years and at the latest six years subsequent to the start of the drilling contract with Statoil.

Note 13 — SHORT-TERM INTEREST BEARING DEBT

At December 31, 1998, the Company had an undrawn amount of NOK 100 million on an overdraft facility.

Note 14 — OTHER CURRENT LIABILITIES

	As at December 31,	
	1997	1998
	(NOK in millions)	
Withheld taxes, social security and holiday pay	142	131
Accrued interest expenses	37	72
Other current liabilities	330	339
Total	509	542

Note 15 — LONG-TERM DEBT AND INTEREST EXPENSES

The Company has a revolving credit facility with a limit of U.S.$650 million of which U.S.$505 million was drawn at year-end. The Revolving Credit Facility bears interest at LIBOR plus 1.00 percent per annum until completion and charterer's acceptance of the drillship West Navion currently under construction and delivery and charterer's acceptance of the fifth generation semi-submersible drilling rig West Venture currently under construction, following which the rate will decrease by 0.125 percent per annum with effect from July 15, 2000. The U.S.$650 million Revolving Credit Facility contains certain financial and other covenants, including covenants requiring it to maintain (i) a minimum value adjusted net worth equal to the greater of U.S.$250 million, and 37.5 percent of its total value adjusted assets until October 10, 1999, increasing to U.S.$300 million and 40 percent, respectively, thereafter, (ii) a minimum liquidity balance (cash and cash equivalents) of U.S.$50 million and (iii) certain minimum current assets to current liabilities and interest coverage ratios. The Company is not permitted to declare or pay dividends in respect of any year in excess of 50 percent of average income before income taxes for such year and the two preceding years, nor to enter into any merger unless the Company will be the surviving entity and remain bound by the terms of the U.S.$650 million Revolving Credit Facility, and such merger would not reasonably be expected to adversely affect the Company's ability to comply with the financial covenants under the U.S.$650 million Revolving Credit Facility.

Long-term interest bearing debt totaling NOK 3,853 million and NOK 1,913 million at December 31, 1998 and 1997, respectively, consisted primarily of bank loans used to finance the acquisition of drilling rigs and newbuilding projects. Actual interest rates ranged from 6.0 percent to 6.5 percent in 1998 and 6.3 percent to 6.7 percent in 1997. Approximately all of the long-term debt is denominated in U.S. dollars.

Long-term interest bearing debt at December 31, 1998, will be payable as follows:

Year	(NOK in millions)
1999	25
2000	74
2001	253
2002	867
2003	2,634
Total	3,853

The Company has various covenants in its loan agreements. As at December 31, 1998, the Company was not in default under any of these agreements.

For the years ended December 31, 1998, 1997 and 1996, interest costs incurred were NOK 229 million, NOK 142 million and NOK 117 million, respectively. Interest cost of NOK 169 million was capitalized in 1998 as part of the financing cost for assets under construction and upgrading of drilling rigs. In 1997 and 1996, the corresponding amounts were NOK 35 million and NOK 9 million, respectively.

Note 16 — OTHER LONG-TERM DEBT

	As at December 31,	
	1997	1998
	(NOK in millions)	
Long-term debt to Navion ASA	301	—
Accrual for long-term maintenance	69	75
Other long-term debt	8	55
Total	378	130

Note 17 — PENSION PLANS

The Company has a pension plan that covers approximately 1,000 employees. The funded status of the plan is as follows:

Disclosure about pensions and other postretirement benefit according to Statement of Financial Accounting Standards (SFAS) no. 132.

Change in Projected Benefit Obligation	As at December 31, 1997	1998
	(NOK in millions)	
PBO at the start of the year	54	82
Service cost	19	22
Interest cost	3	7
Plan amendments*	0	49
Actuarial loss/(gain)	6	(9)
PBO at the end of the year	82	151

* The plan amendment of NOK 49 million is in respect of an early retirement plan implemented on January 1, 1998, for the employees of AS Smedvig Prodrill.

Change in plan assets	As at December 31, 1997	1998
	(NOK in millions)	
Fair value of the assets at the start of the year	44	61
Accrual return on plan assets	4	0
Employer contributions	13	27
Fair value of the assets at the end of the year	61	88

	As at December 31, 1997	1998
	(NOK in millions)	
Funded status	21	63
Unrecognised Net Loss/(Gain)	12	9
Unrecognised Prior Service Cost	0	41
Unrecognised Transition Obligation/(Asset)	6	4
Net amount recognised	3	9
Amounts recognised in the statement of financial position consist of:		
Accrued benefit liability	(3)	(27)
Intangible asset	0	18
Net amount recognised	(3)	(9)

Assumptions:

	1996	1997	1998
Discount rate at end of the year	6.00%	5.50%	5.50%
Expected return on plan assets for the year	6.50%	7.00%	7.00%
Rate of compensation increase at end of the year	3.50%	3.50%	3.50%

Components of net periodic benefit cost	Year ended December 31, 1996	1997	1998
	(NOK in millions)		
Service cost	7	19	22
Interest cost	3	3	7
Expected return on plan assets	(3)	(4)	(5)
Amortisation of transition obligation (asset)	0	1	1
Amortisation of prior service cost	0	0	8
Total net periodic benefit cost	7	19	33

Note 18 — SHAREHOLDERS' EQUITY

The company has two classes of common stock, Class A Shares and Class B Shares. The Class B Shares do not carry a right to vote at the general meetings. Otherwise, holders of Class B Shares have the same rights and privileges as the holders of Class A Shares.

Changes in the number of Class A Shares (par value NOK 3 per share), Class B Shares (par value NOK 3 per share) and share capital are as follows:

	Number of Class A Shares	Number of Class B Shares	Share Capital
			(NOK in millions)
Balance at January 1, 1993 and December 31, 1993	20,838,912	5,209,728	78
Public rights issue in 1994	5,953,974	1,488,494	22
Balance at December 31, 1994 and 1995	26,792,886	6,698,222	100
New share issuance in 1996	241,116	7,060,278	22
Balance at December 31, 1996	27,034,002	13,758,500	122
New share issuance in 1997	248,500	88,875	1
Balance at December 31, 1997	27,282,502	13,847,375	123
New share issuance in 1998	67,000	16,750	1
Balance at December 31, 1998	27,349,502	13,864,125	124

Changes in additional paid-in capital, retained earnings and accumulated other comprehensive income:

	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (1)	Other equity
Balance at January 1, 1996	1,513	227	(16)	1,724
Comprehensive income				
Net income	—	210	—	210
Foreign exchange translation	—	—	29	29
Comprehensive income				239
Dividend	—	(81)	—	(81)
Bonus issue	(20)	—	—	(20)
Equity issue	915	—	—	915
Balance at December 31, 1996	2,408	356	13	2,777
Comprehensive income				
Net income	—	586	—	586
Foreign exchange translation	—	—	(2)	(2)
Comprehensive income				584
Dividend	—	(93)	—	(93)
Equity issue	26	—	—	26
Balance at December 31, 1997	2,434	849	11	3,294
Comprehensive income				
Net income	—	213	—	213
Foreign exchange translation	—	—	32	32
Comprehensive income				245
Dividend	—	(72)	—	(72)
Equity issue	6	—	—	6
Balance at December 31, 1998	2,440	990	43	3,473

(1) Accumulated other comprehensive income consists solely of the Company's cumulative foreign currency adjustments.

Note 19 — STOCK OPTION PLANS AND STOCK SAVINGS SCHEME

Based on a resolution by the General Meeting on June 14, 1990, Smedvig established a Board and Management Share Option Plan for senior management and board members (the "1990 Program"). The exercise price of the options issued under the 1990 Program was NOK 94.50. Options issued under the 1990 Program were to be exercised up to June 30, 1998. The remaining outstanding options under the 1990 Program were exercised in 1998.

Based on a resolution by the Annual General Meeting on April 26, 1995 Smedvig introduced a second Management Share Option Plan for senior management (the "1995 Program"). Options issued under the 1995 Program may be exercised over a five year period ending April 26, 2000. The exercise price is NOK 111 up to June 30, 1999 and NOK 115 up to the date of expiry. Options issued under the 1995 Program are not transferable. Options may be withdrawn upon termination of employment at Smedvig. Grantees who exercise options are obliged to maintain ownership for at least two calendar years to at least 10 percent of the shares acquired.

On August 13, 1996, the Company issued 140,000 share options under the 1995 Program to management. All options granted were exercised by August 14, 1996.

As a result of the bonus issue and the introduction of two share classes, each option issued under the 1990 Program and the 1995 Program, and each unallocated option issuable under the 1995 Program, are exercisable for one Class A Share and one-fourth of one Class B Share, without adjustment of the exercise price.

Based on a resolution by the General Meeting on November 4, 1997, a new option program was introduced for managers employed in the company's foreign operations (the "1997 Program"). Options issued under the 1997 Program are exercisable for one Class B Share and may be exercised over a five year period ending November 3, 2002. The exercise price of the options allotted under this plan in 1997 is NOK 193.00. The options issued under the 1997 Program are not transferable. Options may be withdrawn upon termination of employment at Smedvig. Grantees who exercise options are obliged to maintain an ownership for at least three calendar years to at least 25 percent of the shares acquired by exercising the option.

Based on the authorization by the General Meeting on November 4, 1997, it was resolved to offer management in Norway Class B Shares as part of a stock savings scheme. The price per share was NOK 75 and on December 6, 1997, 26,750 Class B Shares were subscribed for. The employees are obliged to maintain ownership for at least three calender years to at least 25 percent of the shares acquired.

Based on the resolution by the General Meeting on November 4, 1997, two new option programs were introduced in 1998, one for the Chief Executive Officer of 50,000 options (the "1998 (I)-Program") and one for senior management of 69,375 options (the "1998 (II)-Program"). The options issued under the 1998 Programs offer the right to buy one Class B Share per option. The options are not transferable. Options may be withdrawn upon termitation of employment at Smedvig. Grantees who exercise options are obliged to maintain ownership for at least three calendar years to at least 25 percent of the shares acquired by exercising the options.

Options issued under the 1998 (I)-Program may be exercised up to October 5, 2001. The share price on the date of issue was NOK 56 per share. The exercise price increases by one percent per month.

Options issued under the 1998 (II)-Program may be exercised up to November 3, 2002. The share price on the date of issue was NOK 50 per share. The exercise price increases by one percent per month.

	Exercise price range per option	Number of Class A Shares	Number of Class B Shares
Outstanding at January 1, 1996	94.50 — 98.00	574,000	143,500
Options granted 1996	102.00	140,000	35,000
Options exercised 1996	94.50 — 120.00	241,000	60,250
Outstanding at December 31, 1996	94.50 — 120.00	473,000	118,250
Options granted 1997	193.00		31,500
Options exercised 1997	94.50 — 107.00	248,500	62,125
Outstanding at December 31, 1997	94.50 — 193.00	224,500	87,625
Options granted 1998	50.50 — 57.68		119,375
Options exercised 1998	94.50	67,000	16,750
Withdrawn			13,500
Outstanding at December 31, 1998	50.50 — 193.00	157,500	176,750

As of December 31, 1998, the Board could grant a further 135,875 options or shares under the 1997 authorization and 5,000 options under the 1995 authorization.

All issued share options are exercisable.

The Company does not record as compensation expenses benefits arising from granting or exercising of options. However, national insurance contribution arising from options and shares subscribed for is treated as compensation expenses.

FAS 123 Disclosure

In October 1995, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123), which encouraged the use of a fair value based method of accounting for compensation expense associated with stock options and similar plans. However, SFAS No. 123 permits the continued use of the intrinsic value based method prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," but requires additional disclosures, including pro forma calculations of net earnings and earnings per share as if the fair value method of accounting prescribed by SFAS No. 123 had been applied in 1995, 1996 and 1997. The pro forma data presented below is not representative of the effects on reported amounts for future years, since SFAS No. 123 does not apply to awards prior to 1995 and additional awards are expected in the future.

	As Reported			Pro Forma		
	1996	1997	1998	1996	1997	1998
Net income (in millions)	210	586	213	206	584	210
Earnings per share	6.06	14.30	5.17	5.96	14.24	5.11
Average shares outstanding	34,645,529	41,023,375	41,179,115	34,645,529	41,023,375	41,179,115
Average fair value of grants during the year	—	—	—	NOK 22	NOK 52	NOK 22
Black sholes option pricing model assumptions:						
Risk free interest rate				3.5	4.5	6.5
Expected life (years)				1 - 4	5	3
Volatility				30%	33%	55%

Note 20 — FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company has operations and assets in a number of countries worldwide. Consequently, the Company's results from operations are affected, when measured in NOK, by fluctuations in currency exchange rates, primarily relative to the U.S. dollar. When the NOK appreciates against other currencies, the Company's profit from operations in foreign currencies reported in NOK may decrease. Likewise, when the NOK depreciates against other currencies, the Company's profit from operations in foreign currencies reported in NOK may increase. The Company is also exposed to changes in interest rates. Different financial instruments are used by the Company to manage these foreign currency and interest rate risks as summarized below:

Notional amounts and credit exposure

The notional amounts of off balance sheet financial instruments presented in this Note represent the face or contractual amounts and thus are not a measure of the exposure of the Company through its use of such financial instruments. The actual amounts exchanged are calculated on the basis of the notional amounts and the other terms of the financial instruments, which relate to interest rates and exchange rates.

The Company is exposed to credit related losses in the event that counterparties to the off balance sheet financial instrument contracts do not perform according to the terms of the contract.

In the opinion of the management, the counterparties to the financial instrument contracts are creditworthy financial institutions, and the Company does not expect any significant loss to result from non-performance by such counterparties. The Company, in the normal course of business, does not demand collateral. The credit exposure of interest rate swaps and foreign currency contracts is represented by the fair value of contracts with a positive fair value at the end of each period, reduced by the effects of master netting agreements. It is the Company's policy to enter into master netting agreements with the counterparties to financial instrument contracts. These master netting agreements give the Company the legal right to discharge all or a portion of the amounts owed to a counterparty by offsetting it against amounts that the counterparty owes to the Company.

Foreign currency risk management

Smedvig's contract portfolio, forward contracts on currencies, and foreign currency options are used to hedge the future value of income and expenses denominated in foreign currencies and the foreign exchange risk of Smedvig's assets and liabilities. The Company's foreign currency risk arises from:

— fluctuations in exchange rates on the value of the Company's sales and purchases in foreign currencies (transaction exposure) and certain financial assets and liabilities (translation exposure); and

— the Company's investment in certain foreign subsidiaries' net asset (translation exposure).

The Company is hedging most of its transaction risk by way of its net exposure. At the end of 1998, the Company's long-term interest bearing debt is hedged against foreign currency fluctuations by operating contracts in the same currency which ensures sufficient cash flow to settle operating expenses, interest and installment payments. Foreign currency exposure related to long-term debt has been eliminated by having operating income and expenses, interest expenses, installment payments and interest bearing debt being recorded at fixed exchange rates. Of the revolving credit facility with a limit of U.S.$650 million, U.S.$505 million was drawn at December 31, 1998.

Realized gains and losses on forward exchange contracts and foreign currency options are recognized in the income statement in the period such items are closed or settled. Unrealized gains that are considered hedges of net currency exposures are deferred while unrealized losses are expensed in the income statement.

Premiums paid or received for the purchase or sale of options are deferred and charged or credited to the income statement at the expiration of the options.

The following table presents information regarding the contract amount in NOK equivalent amounts and the estimated fair value of all of the Company's foreign currency options with a positive fair value (assets) and a negative fair value (liabilities) as at December 31, 1998 and 1997.

	As at December 31,			
	1997		1998	
	Notional amount	Fair value	Notional amount	Fair value
	(NOK in millions)			
Foreign currency options				
Liabilities	825	(23)	0	0

The major currency of the Company's option contracts is U.S. dollar.

Interest rate risk management

The following is a summary of interest rate swaps and interest rate caps of the Company. Swaps and caps that have a positive fair value are listed as assets while swaps and caps with a negative fair value are listed as liabilities.

	As at December 31,			
	1997		1998	
	Notional amount	Fair value	Notional amount	Fair value
	(NOK in millions)			
Interest rate swaps				
Liabilities	1,359	(27)	2,695	(85)

The extent of the utilization of financial instruments is determined by reference to the Company's net debt exposure and the Company's views regarding future interest rates. At the end of 1998, approximately 70 percent of the Company's U.S. Dollar interest bearing debt was hedged with interest rate swap agreements. This implies that the Company for this part of the debt has a fixed interest rate. Most of these contracts have a term of three to five years. If an interest rate swap agreement is terminated, the Company will continue to account for the gain or loss in accordance with the swap agreement for as long as the underlying loan still exists. In the case the Company terminates the underlying loan the effect of the financial instrument is booked to the income statement. The Company's loans are denominated in U.S. dollars.

The Company had the following interest rate swap agreements as of December 31, 1998:

Notional amount (NOK in millions)	Receive rate	Pay rate	Length of contract
190	6 month LIBOR	5.96%	January 10, 1996 - January 10, 2001
238	6 month LIBOR	7.86%	February 15, 1996 - August 15,2000
124	6 month LIBOR	5.65%	May 3, 1996 - November 3, 2000
238	3 month LIBOR	7.45%	July 15, 1994 - July 15, 2004
381	6 month LIBOR	5.64%	February 18, 1998 - February 18, 2003
381	3 month LIBOR	5.42%	February 18, 1998 - February 18, 2003
381	3 month LIBOR	5.97%	August 18, 1998 - August 18, 2003
381	3 month LIBOR	5.88%	June 2, 1998 - June 2, 2003
381	3 month LIBOR	5.87%	June 2, 1998 - June 2, 2003

The primary loan is obtained by the parent company and not the rig owning companies. The interest rate swap agreements are therefore not any longer linked to individual rigs or ships.

Concentration of credit risk

As at December 31, 1998, the Company had approximately 50 percent of its receivables from two customers. Nevertheless, the Company perceives the concentration of credit risk as low due to the solidity of the two companies, whose majority shareholder is the Norwegian Government.

Note 21 — FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company has used a variety of methods and assumptions, which are based on market conditions and risks existing at the time, to estimate the fair value of the Company's financial instruments as at December 31, 1998 and December 31, 1997. For certain instruments, including cash and cash equivalents, accounts payable and accruals, it was assumed that the carrying amount approximated fair value due to the short-term maturity of those instruments. The difference between carrying value and fair value for cash and cash equivalents and long-term debt is due to the hedged NOK/U.S. Dollar exchange rate for the book value of the long-term debt.

Quoted market prices or dealer quotes for the same or similar financial instruments were used to estimate the fair value of the marketable securities, long-term investments, and long-term debt. The estimated value of the Company's off balance sheet financial instruments are primarily based on settlement values. These values represent the estimated amount that would be received or paid in the event of termination of the contract, taking into consideration current interest rates, the creditworthiness of the counterparties and current foreign currency exchange rates.

	As at December 31,			
	1997		1998	
	Carrying value	Fair value	Carrying value	Fair value
	(NOK in millions)			
Assets:				
Cash and cash equivalents	767	928	579	579
Short-term investments	307	309	303	303
Receivables	1,042	1,042	1,028	1,028
Liabilities:				
Accounts payable	151	151	130	130
Long-term debt	1,913	2,149	3,853	3,944
Off balance sheet financial instruments				
Interest rate risk management	—	(27)	—	—
Foreign currency risk management	(8)	(23)	—	(85)

See Note 20 for further details regarding fair values of off balance sheet financial instruments.

Note 22 — LEASES

The Company has signed operating leases for certain premises. The majority of the premises are leased from the Smedvig family's real estate company, A/S Veni. See Note 26 related party transactions. Smedvig Offshore AS has a lease with A/S Veni lasting until 2007 for the offices at Dusavik, Stavanger.

Rental expenses amounts to NOK 27 million for 1998, which is an increase of NOK 4 million from 1997, and an increase of NOK 6 million from 1996.

Note 23 — PROPORTIONATE CONSOLIDATION

The Company consolidates certain joint-stock companies and limited partnerships in accordance with proportionate consolidation principles. The Company's ownership interest in such companies and partnerships is approximately 50 percent. The table below presents the Company's pro rata share of the condensed financial information of the companies that have been proportionally consolidated.

	As at December 31,	
	1997	1998
	(NOK in millions)	
Balance		
Current assets	85	166
Non-current assets	2,102	1,796
Current liabilities	39	62
Non-current liabilities	1,314	167

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Income statement			
Revenues	274	242	332
Operating profit (loss)	28	23	58
Income (loss) before income taxes	9	(8)	7

Note 24 — REMUNERATION TO THE BOARD OF DIRECTORS AND CHIEF EXECUTIVE OFFICER

	1998
	(NOK)
Remuneration expensed in 1998:	
Board of Directors	600,000
Chief Executive Officer	1,925,621

The Chairman of the Board, Peter T. Smedvig, has not received any remuneration in 1998.

Note 25 — AUDITOR'S REMUNERATION

	1998
	(NOK)
Audit of parent company	380,000
Advisory services in connection with reporting to the Securities and Exchange Commission	242,500
Audit of subsidiaries	1,707,500
Other advisory services	2,856,000

Note 26 — RELATED PARTY TRANSACTIONS

The Company has signed miscellaneous lease agreements with A/S Veni. A/S Veni is a real estate company wholly owned by the Smedvig family which is the largest shareholder in Smedvig asa. The lease agreements primarily relate to office premises and expire at various dates through 2007. The lease payments to A/S Veni for the year ended December 31, 1998 were NOK 11 million. Corresponding figures for each of the years ended December 31, 1997 and 1996 were NOK 16 million and NOK 14 million, respectively.

Note 27 — SUPPLEMENTAL CASH FLOW INFORMATION

The following is a summary of investing activities related to the acquisition of certain subsidiaries in 1998 and 1997:

	As of December 31,	
	1997	1998
	(NOK in millions)	
Assets acquired (sold)	538	(347)
Liabilities assumed	(320)	78
Cash paid, net of cash acquired	218	(269)

Cash paid for interest and taxes are as follows:

	Year ended December 31,		
	1996	1997	1998
	(NOK in millions)		
Interest paid	134	101	188
Taxes paid	58	12	25

Note 28 — MORTGAGE, GUARANTEES AND CAPITAL NOT CALLED IN FROM LIMITED PARTNERSHIPS

Mortgages

	As of December 31, 1998
	(NOK in millions)
Mortgages	3,853
Pledged mobile units and tender rigs	2,550
Pledged newbuilding projects	3,428
Book value pledged assets	5,978

Guarantees

The Company has issued guarantees in favor of third parties amounting to NOK 412 million. The majority of the guarantees are limited performance guarantees issued to the Company's customers. In addition to the limited guarantees, the Company has issued a performance guarantee in favor of Phillips Petroleum Company Norway for the fulfillment of the water injection contract for ENSCO 100 (ex West Omikron). The parent company has issued a performance guarantee in favor of Statoil in connection with a contract entered into by its subsidiary Smedvig Technologies AS for the installation of permanent pressure gauge systems.

Capital not called in from limited partnerships

The Company's committed, but not called in, capital in limited partnerships amounts to NOK 479 million as at December 31, 1998.

Note 29 — OFF BALANCE SHEET ITEMS

Balder FPU

The production vessel Balder FPU was constructed by Keppel Fels in Singapore. The vessel was sold to Esso Norge AS. The costs related to the completion of the vessel were considerably higher than expected. Some of the additional costs are related to works which the Company had advanced in order to secure completion of the vessel and which the Company will seek to reclaim from Esso/Keppel Fels. The Company has withheld payment of the final installment to Keppel Fels, which amount has been offset against the Company's claim regarding the said work.

Balder FPU was delivered to Esso in March 1997 with required certificates. Esso moved the vessel to a shipyard in Scotland to complete their modification program in connection with adaptation to certain new Balder-specific requirements, and to carry out other remaining work. At the shipyard in Scotland, Esso claims to have discovered a number of defects in the vessel. On October 17, 1997, Esso notified the Company that it terminated the operating contract for the Balder FPU, as well as the remaining part of the sales contract, which can only be terminated in the event of substantial breach. The termination will not result in the vessel being redelivered to the Company. As of December 31, 1998, amounts owed to the Company by Esso under the sales contract totalled U.S.$46.5 million (NOK 340 million).

Smedvig and Esso are in agreement that certain work was incomplete when the vessel was delivered to Esso, and that this work should be performed by Esso for Smedvig's account. However, the parties disagree as to the amount of the outstanding work and the costs required for completion.

In April 1998, Smedvig filed a complaint against Esso in Stavanger City Court for unlawful termination and willful breach of the sales contract and operating contract for the Balder FPU. In the complaint, Smedvig claims payment of the final settlement under the sales contracts plus compensation for unlawful termination and willful breach of contract up to a total of approximately NOK 2.6 billion. In its reply, filed in September 1998, Esso rejected Smedvig's claim and brought counterclaims totaling some NOK 4 billion against Smedvig, based mainly on Esso's assertion that Smedvig substantially breached the sales and purchase agreement and exhibited gross negligence in its handling of the Balder project. Smedvig rejects this claim as unjustified, and a formal response was filed at the end of March 1999. Smedvig maintains that Esso undertook comprehensive modifications and upgrades of the vessel above and beyond those specified in the construction contract, and that the oil company is liable for the associated costs.

The dispute between Esso and Smedvig is expected to be tried at Stavanger City Court during year 2000.

Other receivables include a net claim of approximately NOK 175 million against Esso and Keppel Fels.

Based on the Company's review of its contractual obligations and consideration of the state of the vessel at delivery to Esso, the Company believes that it has complied with its material obligations under these contracts. Although the ultimate outcome of this dispute may result in a material charge to results of operations in a particular year, the Company does not believe that the ultimate outcome of this dispute will have a material adverse effect on the financial position of the Company.

Note 30 — THE APPROXIMATE EFFECT ON NET INCOME OF SIGNIFICANT DIFFERENCES BETWEEN NORWEGIAN AND U.S. ACCOUNTING PRINCIPLES

Norwegian GAAP differs in certain respects from U.S. GAAP. Differences which have significant effect on the Company's consolidated net income and shareholder's equity are set out below:

	Reference to note below	1996	1997	1998
Net income in accordance with Norwegian GAAP		210	586	213
Adjustment for U.S. GAAP:				
Foreign currency	(a)	(20)	(87)	23
Bonds and shares	(b)	—	—	2
Financial instruments	(c)	(15)	—	—
Provision for periodic overhauls	(e)	20	25	(15)
Compensation expenses	(f)	(7)	(3)	—
Disposal of vessel	(g)	—	(151)	76
Other		(1)	(1)	(2)
Deferred taxes	(h)	(93)	(196)	(84)
The tax effect of U.S. GAAP adjustments	(h)	4	60	(24)
Approximate net income in accordance with U.S. GAAP		98	233	189
Approximate basic earnings per share in accordance with U.S. GAAP		2.83	5.68	4.59
Approximate diluted earnings per share in accordance with U.S. GAAP		2.81	5.66	4.59

The approximate effect on shareholders' equity of significant differences between Norwegian GAAP and U.S. GAAP is as follows:

	Reference to note below	1997	1998
Shareholder equity in accordance with Norwegian GAAP		3,417	3,597
Adjustment for U.S. GAAP:			
Foreign currency	(a)	(114)	(91)
Equity and debt securities	(b)	2	0
Dividends	(d)	93	72
Provision for periodic overhauls	(e)	100	85
Disposal of vessel	(g)	(151)	(75)
Other		6	4
Deferred taxes	(h)	(230)	(338)
Approximate shareholders' equity in accordance with U.S. GAAP		3,123	3,254

Principal differences between Norwegian GAAP and U.S. GAAP

a) *Foreign exchange*

In accordance with Norwegian GAAP long-term debt denominated in foreign currencies is reported at the higher of either the foreign exchange rate at the date the debt was incurred or the exchange rate at year-end. Under U.S. GAAP, in accordance with Statement of Financial Accounting Standards (SFAS), No. 52, "Foreign Currency Translation," assets and liabilities denominated in a foreign currency are recorded at period-end rates with any resulting unrealized gain or loss recognized in the income statement.

In accordance with Norwegian GAAP certain long-term debt denominated in foreign currencies is recorded at the exchange rate that existed at the origination of the debt, as drilling contracts denominated in the same currency existed that effectively hedged the foreign exchange risk. These transactions do not comply with the hedge criteria under the U.S. GAAP, therefore the long-term debt denominated in foreign currency would be recorded at year-end exchange rates with any resulting unrealized gain or loss recognized in the income statement under U.S. GAAP.

Under Norwegian GAAP unrealized gains on forward exchange contracts and foreign currency options are deferred and recognized only when realized. Under U.S. GAAP unrealized gains on forward exchange contracts and foreign currency options which do not qualify for hedge accounting treatment would be recognized as income when they occur. The amounts of unrealized gains were immaterial.

b) *Equity and debt securities*

Under Norwegian GAAP, short-term investments are recorded at the lower of cost or market value determined on a portfolio basis. For U.S. GAAP purposes, all investments in debt and equity securities with a readily determinable market value are classified as "available for sale" and are recorded at fair value with changes in unrealized appreciation or depreciation recorded directly to shareholders' equity, net of applicable deferred income tax.

c) *Interest rate swaps*

Under Norwegian GAAP when debt is refinanced the related interest rate swap agreement can be designated as a hedge of the new debt without any impact to the income statement. Under U.S. GAAP, when debt is refinanced the related interest rate swap agreement should be marked-to-market with the resulting unrealized gain or loss being credited or charged to the income statement.

d) *Dividends*

Under Norwegian law, dividends are payable out of annual earnings. The dividend is subject to approval by the Annual General Meeting following the fiscal year to which the dividend relates. Under Norwegian GAAP, dividends are recorded when declared. Accordingly, under U.S. GAAP, dividends are recorded in the year following the year they are recorded under Norwegian GAAP.

e) *Provision for periodic overhauls*

Under Norwegian GAAP, a provision for periodic overhauls on mobile units and tender rigs is accrued evenly over the anticipated period between overhauls, generally five years. Under U.S. GAAP, the costs of such overhauls would be capitalized when incurred and depreciated over the estimated future period benefited by such costs, generally five years.

f) *Compensation expenses*

If stock options are granted at a point in time where the prevailing market price exceeds the exercise price, or if shares are offered at a purchase price below prevailing market price, Smedvig does not charge to income the employee benefits in accordance with this difference. Under U.S. GAAP, however, such benefits must be charged to income in accordance with this difference. The associated social security costs, however, are expensed as personnel costs both under Norwegian GAAP and U.S. GAAP.

g) *Disposal of vessel*

In December 1997, the Company sold the West Omikron to ENSCO for approximately NOK 750 million. At the time the vessel was sold it was under contract to a customer. The Company has leased the vessel back from ENSCO in order to fulfill its obligations under the contract. Under Norwegian GAAP, the entire amount of the gain was recognized at the time of the sale. Under U.S. GAAP, only a portion of the gain would be recognized at the time of the sale and the remainder would be amortized into income ratably over the period of the lease.

h) *Deferred taxes*

The income tax effects of other U.S. GAAP adjustments are recorded as deferred tax expense, where appropriate.

In 1996, Norway introduced new rates for taxation of shipping and offshore companies. According to the new tax rules, taxation will be based upon funds distributed to shareholders. Thus, under Norwegian GAAP such income is not taxable. However, under U.S. GAAP, a deferred tax liability and tax charge should be recognized on such income.

In 1998, Smedvig has a net tax asset related to the operation in Norway. In 1996 there was a similar situation in the United Kingdom. Under Norwegian GAAP the benefit of deferred tax assets is not recognized because there is no corresponding deferred tax liability within the same tax jurisdiction against which the assets can be offset. Under U.S. GAAP the benefit of the deferred tax asset may be recognized if it is more likely than not that the asset will be realized. The Company has determined that it is more likely than not that it will realize the benefit of this deferred tax asset through future taxable earnings. At year end 1998 net tax asset is calculated at NOK 46 million.

i) *First year's installment on long-term debt*

Under Norwegian GAAP, the first year's installment on long-term debt is included in long-term debt. The installments due in 1999 of NOK 25 million would be classified as short-term debt, under U.S. GAAP.

j) *Newbuilding contracts*

According to Norwegian GAAP, the entire construction contract value is included in the balance sheet from the start of the construction. The contractual obligation is also recorded as a liability. Other cost, including interest under construction, are capitalized when they occur. Under U.S. GAAP, only accrued expenses at the period-end would be capitalized.

Newbuilding contracts at December 31, 1998, of NOK 4,228 million are specified in Note 12. According to U.S. GAAP the amount in the accounts would have been approximately NOK 3,400 million without any corresponding liability.

k) *Proportionate consolidation method*

Under Norwegian GAAP the Company consolidates certain joint stock companies and limited partnerships, in which the Company's holdings are 50 percent or less, in accordance with the proportionate consolidation method. Condensed financial information for the companies and partnerships that have been proportionally consolidated is included in Note 23.

Under U.S. GAAP the Company's ownership interest in these companies and partnerships would be accounted for under the equity method. The effect on total assets, shareholders' equity and net income of using the proportionate consolidation method versus the equity method would not be material as of and for the years ended December 31, 1998, 1997 and 1996.

l) *Other items*

Other items in the 1998 income statement include termination expenses and a gain from the sale of the UK platform drilling operation. Gains on sale of assets in previous years have been reclassified correspondingly. In accordance with U.S. GAAP such amounts should be classified as operating expenses, respectively income.

m) *Accounting standards issued but not yet adopted*

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133 ("SFAS 133"), "Accounting for Derivative Instruments and Hedging Activities." This statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives), and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. This statement is effective for all fiscal quarters of fiscal years beginning after June 15, 1999. Management has not determined the effect of the adoption of SFAS 133.

During January 1998, the American Institute of Certified Public Accountants (AICPA) issued Statement of Position 98-1 *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use* ("SOP 98-1") which becomes effective for all fiscal years beginning after December 15, 1998. Under SOP 98-1, computer software costs that are incurred in the preliminary project stage are expensed as incurred. Once specific capitalization criteria have been met, external direct costs of materials and service consumed in developing or obtaining internal-use computer software, certain personnel costs, and interest costs incurred when developing computer software for internal use are capitalized. Training costs and data conversion costs are generally expensed as incurred. Such capitalized costs are amortized over the estimated useful life of the software. The Company is evaluating the effect of the pronouncement.

The AICPA issued Statement of Positions 98-5, *Reporting on the Costs of Start-Up Activities* ("SOP 98-5) in April 1998 and is effective for fiscal periods beginning after December 15, 1998 SOP 98-5 provides guidance on the financial reporting of start-up costs and organization costs. It requires costs of start-up activities and organization costs to be expensed as incurred. The Company is evaluating the effect of the pronouncement.

Note 31 — SUBSEQUENT EVENT (UNAUDITED)

In June 1999, after negotiations with Statoil, the five-year drilling contract for the West Navion was replaced by a one-year contract. Terms and conditions for the new contract are substantially the same as for the original contract. The reason for the reduction in contract duration was the delayed delivery schedule for the drillship. At the same time, the Company's partner Navion, which owns 50 percent of the West Navion, notified the Company that they reserve their right to seek compensation from the Company for Navion's portion of the cost overruns related to the construction and outfitting of the drillship. The Company believes that such claim would be groundless.

Smedvig

1998 Annual Report on Form 20-F

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Omitted items are not applicable.

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

(Mark One)

[ ] REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

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

For the fiscal year ended December 31, 1998

OR

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

For the transition period from to

Commission file number: 1-14532

SMEDVIG asa

(Exact name of Registrant as specified in its charter)

Kingdom of Norway

(Jurisdiction of incorporation or organization)

Finnestadveien 28, P.O. Box 110, N-4001, Stavanger, Norway

(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Class A Ordinary Shares, par value NOK 3.00 per share	New York Stock Exchange, Inc.*
Class A American Depositary Shares, each representing one Class A Ordinary Share	New York Stock Exchange, Inc.
Class B Ordinary Shares, par value NOK 3.00 per share	New York Stock Exchange, Inc.*
Class B American Depositary Shares, each representing one Class B Ordinary Share	New York Stock Exchange, Inc.

* Not for trading, but only in connection with registration of American Depositary Shares representing such Class A and Class B Shares, pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report:

27,349,502 Class A Ordinary Shares, with nominal value of NOK 3.00 per share
13,864,125 Class B Ordinary Shares, with nominal value of NOK 3.00 per share

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No ____

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 ____ Item 18 X