

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

UNIVERSAL COMPRESSION HOLDINGS INC

Form 10-Q

August 10, 2001

1

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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

For the Quarterly Period Ended June 30, 2001

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 Numbers: 001-15843
333-48279

UNIVERSAL COMPRESSION HOLDINGS, INC.
UNIVERSAL COMPRESSION, INC.
(Exact name of registrants as specified in their charters)

DELAWARE	13-3989167
TEXAS	74-1282680
(States or other jurisdictions of incorporation of organization)	(I.R.S. Employer Identification Nos.)

4440 BRITTMOORE ROAD	
HOUSTON, TEXAS	77041-8004
(Address of principal executive offices)	(Zip Code)

(713) 335-7000
(Registrants' telephone number, including area code)

Indicate by check mark whether the registrants (1) have 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 registrants were required to file such reports), and (2) have been subject to such filing requirements for the past 90 days.

Yes ☒ [X] No ☐ []

UNIVERSAL COMPRESSION, INC. MEETS THE CONDITIONS SET FORTH IN GENERAL INSTRUCTION H(1)(a) AND (b) OF FORM 10-Q AND IS THEREFORE FILING THIS FORM 10-Q WITH THE REDUCED DISCLOSURE FORMAT.

As of July 31, 2001, there were 30,517,343 shares of Universal Compression Holdings, Inc.'s common stock, \$0.01 par value, outstanding and 4,910 shares of Universal Compression, Inc.'s common stock, \$10.00 par value, outstanding.

2

PART I. FINANCIAL INFORMATION

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

ITEM 1. FINANCIAL STATEMENTS

UNIVERSAL COMPRESSION HOLDINGS, INC. CONSOLIDATED BALANCE SHEETS (IN THOUSANDS)

	June 30, 2001 ----- (unaudited)	March -----
ASSETS		
Current Assets:		
Cash	\$ 10,589	\$
Accounts receivable, net	95,256	
Inventories	109,213	
Other current assets	24,720	
	-----	-----
Total current assets	239,778	
Property, plant and equipment		
Rental equipment	615,512	
Other	52,898	
Accumulated depreciation	(63,716)	
	-----	-----
Net property, plant, and equipment	604,694	
Goodwill	304,689	
Other assets, net	49,237	
	-----	-----
Total assets	\$ 1,198,398	\$
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 130,719	\$
Current portion of long term debt and capital lease obligation	10,146	
	-----	-----
Total current liabilities	140,865	
Long-term debt	208,125	
Non-current deferred tax liability	90,110	
Deferred gain	88,700	
Capital lease obligations	5,557	
Other liabilities	704	
	-----	-----
Total liabilities	534,061	
Common stock	285	
Treasury Stock	(134)	
Paid in capital	664,253	
Currency translation adjustment	1,692	
Retained deficit	(1,759)	
	-----	-----
Total stockholders' equity	664,337	
	-----	-----
Total liabilities and stockholders' equity	\$ 1,198,398	\$
	=====	=====

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

See accompanying notes to unaudited consolidated financial statements

2

3

UNIVERSAL COMPRESSION HOLDINGS, INC. UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS (IN THOUSANDS, EXCEPT SHARE AND PER SHARE AMOUNTS)

	Three Months 2001
Revenues:	
Rentals	\$ 75,950
Sales	64,411
Other	(47)
Total revenues	140,314
Costs and expenses:	
Rentals, exclusive of depreciation and amortization	27,565
Cost of sales, exclusive of depreciation and amortization	53,275
Depreciation and amortization	11,380
Selling, general and administrative	12,676
Operating lease	12,593
Interest expense	5,532
Non-recurring charges	--
Total costs and expenses	123,021
Income (loss) before income taxes and extraordinary items	17,293
Income taxes (benefit)	6,748
Income (loss) before extraordinary items	\$ 10,545
Extraordinary loss, net of \$3,759 income tax benefit	--
Net income (loss)	\$ 10,545
Weighted average common and common equivalent shares outstanding:	
Basic	28,481
Diluted	28,811
Earnings per share - basic:	
Income (loss) before extraordinary items	\$ 0.37
Extraordinary loss	--
Net income (loss)	\$ 0.37
Earnings per share - diluted:	
Income (loss) before extraordinary items	\$ 0.37
Extraordinary loss	--
Net income (loss)	\$ 0.37

See accompanying notes to unaudited consolidated financial statements.

3

4

UNIVERSAL COMPRESSION HOLDINGS, INC.
UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	Three Months 2001 -----
Cash flows from operating activities:	
Net income (loss)	\$ 10,545
Adjustments to reconcile net loss to cash provided by operating activities, net of effect of acquisitions:	
Depreciation and amortization	11,380
Gain (loss) on asset sales	137
Amortization of debt issuance costs	653
Accretion of discount notes	4,896
Deferred income taxes	(16)
Other	(9,566)

Net cash provided by operating activities	18,029
Cash flows from investing activities:	
Additions to property, plant and equipment, net	(40,325)
Acquisitions	(25,029)
Proceeds from sale of fixed assets	973

Net cash used in investing activities	(64,381)
Cash flows from financing activities:	
Principal repayments of long-term debt	(1,467)
Net borrowings (repayment) under revolving line of credit	6,000
Net repayment on sale-leaseback of vehicles	(394)
Net borrowings (repayment) on financing lease	40,000
Common stock issuance	371
Debt issuance costs	(695)
Treasury stock	--

Net cash provided by financing activities	43,815
Effect of exchange rate	847
Net increase (decrease) in cash and cash equivalents	(1,690)
Cash and cash equivalents at beginning of period	12,279

Cash and cash equivalents at end of period	\$ 10,589 =====

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

See accompanying notes to unaudited consolidated financial statements.

4

5

UNIVERSAL COMPRESSION HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2001

1. BASIS OF PRESENTATION

Organization

Universal Compression Holdings, Inc. (the "Company") was formed on December 12, 1997 for the purpose of acquiring Tidewater Compression Service, Inc. ("TCS") from Tidewater Inc. ("Tidewater"). Upon completion of the acquisition on February 20, 1998 (the "Tidewater Acquisition"), TCS became the Company's wholly owned subsidiary and changed its name to Universal Compression, Inc. ("Universal"). Through this subsidiary, the Company's gas compression service operations date back to 1954. The Company is a holding company which conducts its operations through its wholly owned subsidiary, Universal. Accordingly, the Company is dependent upon the distribution of earnings from Universal, whether in the form of dividends, advances or payments on account of intercompany obligations, to service its debt obligations.

Effective May 30, 2000, the Company completed an initial public offering of 7,275,000 shares of its common stock (which includes 275,000 shares of common stock issued pursuant to an over allotment option granted to the underwriters), which provided the Company with net proceeds (after deducting underwriting discounts and commissions) of approximately \$149.2 million. Concurrently with the initial public offering, the Company implemented a recapitalization pursuant to which all existing classes of the Company's stock were converted into common stock. Also concurrently with the initial public offering, the Company entered into a \$50 million revolving credit facility and \$200 million operating lease facility. The proceeds of the offering and the \$62.6 million in initial proceeds from the new operating lease facility were used to repay \$192.7 million of indebtedness, and the remaining proceeds were used for working capital and to pay expenses associated with the offering and concurrent financing transactions.

On July 3, 2001, the Company completed the public offering (the "Offering") of 1,333,333 shares of its common stock, par value \$0.01 per share, together with 2,666,667 shares of the Company's common stock sold by certain selling stockholders, including Castle Harlan Partners III, L.P. and its affiliates. The shares were sold in the Offering at a price of \$28.50 per share, and the Offering provided the Company with net proceeds (after deducting underwriting discounts and commissions) of approximately \$36.1 million. The Company used the proceeds to fund the cash portion of the purchase price in its acquisition of KCI, Inc., to repay a portion of KCI's indebtedness concurrently with the acquisition, as described below and to partially fund the purchase price in its acquisition of Louisiana Compressor Maintenance, Inc., as described below. Following the Offering, Castle Harlan owned or had voting control over approximately 6% of the Company's outstanding common stock.

The Company completed the acquisition of Gas Compression Services, Inc. ("GCSI") on September 15, 2000, of Weatherford Global Compression Services, L.P. ("Weatherford Global") on February 9, 2001, of ISS Compression, Inc. and its

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

operating subsidiary, IEW Compression, Inc. (collectively "IEW") on February 28, 2001, of the international operations of Compressor Systems, Inc. ("CSII") on April 23, 2001, of KCI, Inc. ("KCI") on July 11, 2001 and of Louisiana Compressor Maintenance, Inc. ("LCM") on July 13, 2001.

These consolidated financial statements should be read in conjunction with the consolidated financial statements presented in the Company's Annual Report on Form 10-K for the year ended March 31, 2001. That report contains a more comprehensive summary of the Company's major accounting policies. In the opinion of management, the accompanying unaudited consolidated financial statements contain all appropriate adjustments, all of which are normally recurring adjustments unless otherwise noted, considered necessary to present fairly the financial position of the Company and its consolidated subsidiaries and the results of operations and cash flows for the respective periods. Operating results for the three-month period ended June 30, 2001 are not necessarily indicative of the results that may be expected for the fiscal year ending March 31, 2002.

5

6

EARNINGS PER SHARE (UNAUDITED)

Basic and diluted net income (loss) per share is calculated in accordance with Statement of Financial Accounting Standards No. 128 ("SFAS 128"), "Earnings per Share".

The following table sets forth the computation of basic and diluted net income (loss) per share (in thousands, except per share amounts):

BASIC EARNINGS PER SHARE

	Three Months Ended June 30,	
	2001	2000
	-----	-----
Income (loss) before extraordinary loss	\$ 10,545	\$ (4,664)
Extraordinary loss, net of income tax	--	(6,264)
	-----	-----
Net income (loss)	\$ 10,545	\$ (10,928)
	=====	=====
Weighted average common stock outstanding	28,481	8,817
Basic net income (loss) per share:		
Before extraordinary loss	\$ 0.37	\$ (0.53)
Extraordinary loss, net of income tax	--	(0.71)
	-----	-----
Basic net income (loss) per share	\$ 0.37	\$ (1.24)
	=====	=====

DILUTED EARNINGS PER SHARE

Income (loss) before extraordinary loss	\$ 10,545	\$ (4,664)
Extraordinary loss, net of income tax	--	(6,264)

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

Net income (loss)	\$ 10,545	\$ (10,928)
Weighted average common stock outstanding	28,481	8,817
Dilutive effect of stock options outstanding	330	--
Weighted average diluted shares of common stock outstanding	28,811	8,817
Diluted income (loss) per share:		
Before extraordinary loss	\$ 0.37	\$ (0.53)
Extraordinary loss, net of income tax	--	(0.71)
Diluted net income (loss) per share	\$ 0.37	\$ (1.24)

RECLASSIFICATIONS

Certain reclassifications have been made to the prior year amounts to conform to the current year classification.

2. RECENT ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") 133, "Accounting for Derivative Instruments and Hedging Activities." In June 2000, the FASB issued SFAS 138, which amends certain provisions of SFAS 133 to clarify four areas causing difficulties in implementation. The amendment included expanding the normal purchase and sale exemption for supply contracts, permitting the offsetting of certain intercompany foreign currency derivatives and thus reducing the number of third party derivatives, permitting hedge accounting for foreign-currency denominated assets and liabilities, and redefining interest rate risk to reduce sources of

ineffectiveness. SFAS 133 requires that an entity recognize all derivative instruments as either assets or liabilities in the balance sheet and measure those instruments at fair value. If certain conditions are met, a derivative may be specifically designated as (1) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, (2) a hedge of the exposure to variable cash flows of a forecasted transaction, or (3) a hedge of the foreign currency exposure of a net investment in a foreign operation, an unrecognized firm commitment, an available-for-sale security, or a foreign-currency-denominated forecasted transaction. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. We adopted SFAS 133 and the corresponding amendments under SFAS 138 on April 1, 2001. This statement had no impact on our consolidated results of operations, financial positions or cash flows.

In December 1999, the SEC issued Staff Accounting Bulletin ("SAB") 101, "Revenue Recognition in Financial Statements." SAB 101 summarizes certain of the SEC's views in applying generally accepted accounting principles to revenue recognition in financial statements. On June 26, 2000, the SEC issued an amendment to SAB 101, effectively delaying its implementation until the fourth

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

quarter of fiscal years beginning after December 15, 1999. After reviewing SAB 101 and its amendment, we believe that our revenue recognition policy is appropriate and that the effects of SAB 101 and its amendment were immaterial to our results of operations.

In July 2001, the FASB issued SFAS 141, "Business Combinations," effective for all business combinations initiated after June 30, 2001 and SFAS 142, "Goodwill and Other Intangible Assets". The Company elected to adopt SFAS 142 effective April 1, 2001 as the first interim period financial statements had not previously been issued. Statement 141 addresses financial accounting and reporting for goodwill and other intangible assets acquired in a business combination at acquisition. Statement 142 addresses financial accounting and reporting for intangible assets acquired individually or with a group of other assets (but not those acquired in a business combination) at acquisition. It also addresses financial accounting and reporting for goodwill and other intangible assets subsequent to their acquisition. We adopted SFAS 142 effective April 1, 2001. Had the Standard been effective April 1, 2000, we would have adopted it in the first quarter of fiscal 2001 and our loss before taxes and extraordinary items would have been \$6,788 as a result of the elimination of \$0.7 million of amortization expense related to goodwill, net loss would have been \$10,506 as a result of the elimination of \$0.7 million of amortization expense related to goodwill and a decrease in the recorded income tax benefit of \$0.3 million and loss per basic share and diluted share would have been \$1.19 and \$1.19, respectively.

3. ACQUISITIONS

On April 23, 2001, the Company acquired the international operations of Compressor Systems, Inc. based in Midland, Texas for approximately \$30 million in cash. The acquisition resulted in the recording of \$13 million of goodwill, which is not subject to amortization.

This acquisition was accounted for as a purchase and accordingly, the results of operations of the acquired business are included in the accompanying financial statements from the date of acquisition.

4. INVENTORIES

Inventories consisted of the following (in thousands):

	June 30, 2001	March 31, 2001
	-----	-----
	(unaudited)	
Raw materials	\$ 64,252	\$ 63,473
Finished goods	30,479	38,705
Work-in-progress	14,482	18,761
	-----	-----
Total	\$ 109,213	\$ 120,939
	=====	=====

5. OPERATING LEASE FACILITIES

In May 2000, the Company and Universal entered into a \$200 million operating lease facility pursuant to which the Company sold and leased back certain compression equipment from a Delaware business trust for a five-year term. The rental payments under the lease facility included an amount based on

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

LIBOR plus a variable amount depending on the Company's operating and financial results, applied to the funded amount of the lease. Under the lease facility, the Company received an aggregate of approximately \$155 million in proceeds from the sale of compression equipment in May, November and December 2000 and in connection with the GCSI acquisition, in September 2000. The equipment was sold and leased back by the Company for a five-year period from May 2000 and deployed by the Company under its normal operating procedures. The equipment sold had a book value of approximately \$106 million and the equipment sale resulted in deferred gain of approximately \$49 million that was transferred to new operating lease facilities.

The Company had residual value guarantees on the equipment under the operating lease facility of approximately 85% of the funded amount that were due upon termination of the lease and which could be satisfied by a cash payment or the exercise of the purchase option. The facility contained certain covenants restricting the Company's operations, including its ability to enter into acquisition and sales transactions, incur additional indebtedness, permit additional liens on its assets and pay dividends. The Company's obligations under this facility were collateralized by liens on its compression equipment subject to the lease and certain related rights. Under the operating lease facility, Universal was the lessee and the Company guaranteed certain of Universal's obligations thereunder. The Company has replaced this facility with new operating lease facilities with similar terms.

7

8

In connection with the Weatherford Global acquisition, on February 9, 2001, the Company raised \$427 million under a new seven-year term senior secured notes operating lease facility (the "SSN Operating Lease Facility") funded primarily through an offering of \$350 million 8 7/8% senior secured notes due 2008 by an unaffiliated entity that is the lessor under the operating lease. The Company also entered into a new \$125 million secured revolving credit facility and a new \$200 million asset-backed securitization operating lease facility (the "ABS Operating Lease Facility"), which facility consists of a series of six leases with terms ranging from three to eight years. At the closing of the Weatherford Global acquisition, the Company funded approximately \$80 million under the ABS Operating Lease Facility and had no amounts outstanding under the new revolving credit facility. The proceeds from the two new operating lease facilities were used to restructure existing operating lease obligations and refinance certain existing indebtedness of the Company (including the previous operating lease facility described above in the first paragraph) and Weatherford Global.

During the quarter, the Company funded \$40 million under the ABS Operating Lease Facility. The funds were used for acquisitions as well as for general working capital purposes. At June 30, 2001, the Company had outstanding lease balances totaling \$567.5 million and the equipment sold to the two new operating lease facilities had a book value of approximately \$478.8 million and the equipment sale resulted in a deferred gain of approximately \$88.7 million.

Under the operating lease facilities, the Company, as lessee, makes rental payments to the lessor for the leased equipment. Under the SSN Operating Lease Facility, the rental payments include amounts based on the interest accrued on the 8 7/8% senior secured notes and an amount based on LIBOR or a variable base rate equal to the sum of the interest accrued on the lessor's term loan, the yield on the equity investment in the lessor and other fees. The equipment leased by the Company under the SSN Operating Lease Facility had an initial appraised value of \$427 million. The Company has residual value

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

guarantees on the equipment under the SSN Operating Lease Facility of approximately 82% of the funded amount that are due upon termination of the lease in the event the purchase option or renewal options are not selected by the lessee.

Under the ABS Operating Lease Facility, the rental payments are based on a variable rate plus the yield on the equity investment in the facility. The ABS Operating Lease Facility is collateralized by a first priority security interest in all of the assets under the facility. At the end of each lease term under the ABS Operating Lease Facility, the Company has residual value guarantees on the equipment under the facility of approximately 85% of the funded amount.

The Company annually assesses whether it is probable that the value of the property at the end of the lease terms will be less than the residual value guarantee for each operating lease. On the date the deficiency becomes probable the expected deficiency (up to the maximum for which the Company is responsible) would be accrued by the Company using the straight-line method over the remaining term of the leases.

6. EXTRAORDINARY LOSSES

During the quarter ended June 30, 2000, the Company incurred extraordinary losses of \$6.3 million (net of \$3.8 million income tax benefit) related to its debt restructuring that occurred concurrently with the Company's initial public offering of its common stock.

7. NON-RECURRING CHARGES

During the quarter ended June 30, 2000, the Company incurred non-recurring charges of \$7.1 million, related to the early termination of a management agreement and a consulting agreement and other related fees in connection with the Company's initial public offering and concurrent financing transactions.

8. RELATED PARTY TRANSACTIONS

Management Agreement

Castle Harlan Inc., an affiliate of a significant stockholder of the Company, entered into an agreement whereby, in exchange for certain management services rendered, the Company agreed to pay a fee to Castle Harlan Inc. totaling \$3 million per year. The amount was paid in advance for the first year and quarterly in advance thereafter. The agreement was for a term of five years, renewable automatically from year to year thereafter unless Castle Harlan Inc. or its affiliates beneficially own less than 20% of the then outstanding stock of the Company.

In connection with the initial public offering in the quarter ended June 30, 2000, the Company terminated its Management Agreement with Castle Harlan, Inc. In exchange for such termination, the Company paid \$3 million in cash and issued 136,364 shares of its common stock to Castle Harlan.

Transitional Services Agreement

Concurrently with the closing of the Weatherford Global acquisition, Weatherford and Weatherford Global, as the Company's subsidiary, entered into a transitional services agreement under which Weatherford provided certain administrative and support services, such as shared corporate office space and general communication and information services, to Weatherford Global until June 9, 2001. Weatherford Global paid Weatherford \$125,000 for thirty days of these services.

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

9. INDUSTRY SEGMENTS

Prior to the Weatherford Global merger, the Company had three principal industry segments: Domestic Rental and Maintenance, International Rental and Maintenance and Engineered Products. Due to the Weatherford Global merger, the changing nature of the markets the Company serves and in order to align ourselves with those markets, the Company changed its internal business organization during fiscal 2001. The Company is now organized into four principal businesses or operating segments: Domestic Rental and Maintenance, International Rental and Maintenance, Fabrication and Parts Sales and Service. The two Rental and Maintenance Segments provide natural gas compression rental and maintenance services to meet specific customer requirements. The Fabrication Segment involves the design, fabrication and sale of natural gas and air compression packages to meet

8

9

customer specifications. The International Rental and Maintenance Segment represents all of the Company's international rental and maintenance operations. The Parts Sales and Service Segment involves the sale of parts to and the service of compressor units owned by oilfield companies.

The Company's reportable segments are strategic business units that offer different products and services. They are managed separately since each business requires different marketing strategies due to customer specifications. Each of these business groups has one or more general managers who report directly to the Chief Executive Officer ("CEO"). The CEO has been identified as the Chief Operating Decision Maker as defined by SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." We have restated segment results for prior periods as a result of our fiscal 2001 realignment.

In addition to these four operating segments, accounting, administration, facilities, finance, human resources, legal, marketing, procurement and sales groups also report to the CEO. The CEO does not evaluate the operating segments based upon fully allocated profit and loss statements, and the segments' reportable operating profit excludes allocated expenses. Operating segments do not have material sales to other segments, and accordingly, there are no inter-segment revenues to be reported. The Company also does not allocate our restructuring charges, interest and other income, interest expense or income taxes to operating segments.

The following table presents sales and other financial information by industry segment for the three-month period ended June 30, 2001 (in thousands):

	DOMESTIC RENTAL AND MAINTENANCE	INTERNATIONAL RENTAL AND MAINTENANCE	FABRICATION	PARTS SALES AND SERVICE	
Revenues	\$ 61,920	\$ 14,030	\$ 32,234	\$ 32,177	\$
Gross margin	38,755	9,281	4,193	7,295	
Operating income	24,591	5,555	1,098	4,224	

The following table presents sales and other financial information by industry segment for the three-month period ended June 30, 2000 (in thousands):

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

	DOMESTIC RENTAL AND MAINTENANCE	INTERNATIONAL RENTAL AND MAINTENANCE	FABRICATION	PARTS SALES AND SERVICE	
Revenues	\$ 22,175	\$ 4,099	\$ 7,661	\$ 609	\$
Gross margin	14,245	3,059	1,522	201	
Operating income	5,703	1,308	921	121	

No one customer accounted for more than 10% of revenues for either of the periods presented.

10. COMMITMENTS AND CONTINGENCIES

In the ordinary course of business, the Company is involved in various pending or threatened legal actions. In the opinion of management, the amount of ultimate liability, if any, with respect to these actions will not have a materially adverse effect on the Company's financial position, operating results or cash flows.

The Company has no other commitments or contingent liabilities, which in the judgment of management, would result in losses that would materially affect the Company's consolidated financial position or operating results.

On May 24, 2001, the Company entered into an agreement with Tidewater to settle acquisition-related claims, which included costs for remediation pursuant to an environmental assessment, in exchange for payment to the Company of \$1 million and termination of the purchase price adjustment agreement, which eliminated any payment obligation by the Company under that agreement.

11. SUBSEQUENT EVENTS

On July 3, 2001, the Company completed the Offering of 1,333,333 shares of its common stock, par value \$0.01 per share, together with 2,666,667 shares of the Company's common stock sold by certain selling stockholders, including Castle Harlan Partners III, L.P. and its affiliates. The underwriters did not purchase additional shares to cover over allotments. The shares were sold in the Offering at a price of \$28.50 per share, and the Offering provided the Company with net proceeds (after deducting underwriting discounts and commissions) of approximately \$36.1 million. The Company used the proceeds to fund the cash portion of the purchase price in its acquisition of KCI, Inc., to repay a portion of KCI's indebtedness concurrently with the acquisition, as described below, and to partially fund the cash portion of the purchase price in its acquisition of Louisiana Compressor Maintenance, Inc., as described below. Following the Offering, Castle Harlan owned or had voting control over approximately 6% of the Company's outstanding common stock.

Pursuant to the indenture governing the 9 7/8% senior discount notes due 2008 of Universal, the holders of the notes have the right to require UCI to repurchase the notes through August 23, 2001 at a price equal to 101% of the accreted value, plus accrued and unpaid interest to date as a result of the consummation of the Offering as Castle Harlan's ownership of less than 20% of the Company's common stock constituted a change of control under the indenture. As of June 30, 2001, UCI had approximately \$205.7 million aggregate principal amount outstanding under its 9 7/8% senior

discount notes. The Company expects to finance any repurchases of the 9 7/8% senior discount notes through its revolving credit facility or its operating lease facilities.

Immediately following the Offering, an affiliate of Weatherford International, Inc. ("Weatherford") beneficially owned approximately 46% of the Company's outstanding common stock. Pursuant to a voting agreement entered into concurrently with the Company's acquisition of Weatherford Global and certain related entities, Weatherford agreed to limit its voting power to 33 1/3% of the Company's outstanding common stock, until the earlier of two years from the closing of the acquisition or the date that Castle Harlan and its affiliates own less than 5% of the Company's outstanding stock. The sale of shares by Castle Harlan in the Offering did not result in a termination of the voting agreement giving Weatherford voting control over the full 46% of the Company's shares that it owned following the Offering.

In addition to its voting control, Weatherford and its affiliates are entitled to designate, which it has done, three persons to serve on our board of directors for so long as they own at least 20% of our outstanding common stock. If Weatherford's ownership falls below 20%, Weatherford may designate only two directors. If Weatherford's ownership falls below 10%, it will no longer have the right to designate directors to our board. Castle Harlan was also entitled to designate a total of three persons to our board of directors. Although it lost this right following the Offering, its two current designees, John K. Castle and William M. Pruellage, are serving terms that do not expire until our 2003 annual meeting of stockholders.

On July 11, 2001, the Company completed its acquisition of KCI, a Tulsa, Oklahoma-based fabricator of large horsepower compressors. Under the terms of the purchase agreement, the Company acquired KCI for approximately \$26.3 million in cash and 694,927 shares of the Company's common stock. In addition, the Company incurred costs and assumed other liabilities related to the transaction of approximately \$6 million. Concurrently with the acquisition, the Company repaid substantially all of KCI's approximately \$51 million of indebtedness. In order to fund the acquisition the Company used approximately \$50 million of the availability under its revolver and \$27.3 million of the funds received from the public Offering of its stock.

In connection with the acquisition and the issuance of shares of common stock in the acquisition, the Company entered into registration rights agreements, which provide certain demand and piggyback registration rights to the former holders of the common stock of KCI and the partnership interests of KCI Compression Company, L.P. Under the terms of the agreements, the Company has agreed to prepare and file a registration statement to register the resale of the shares of common stock issued in the acquisition. In addition, the former KCI holders may request to have the sale of their shares included in certain registration statements with respect to any proposed public offering by the Company or other holders of the Company's common stock. The former KCI shareholders have agreed, with exceptions, not to sell or transfer any shares of the Company's common stock until after October 9, 2001, 90 days after the closing of the acquisition.

On July 13, 2001, the Company completed its acquisition of LCM, a Houma, Louisiana based supplier of maintenance, repair, overhaul and upgrade services to the natural gas pipeline and related markets. Under the terms of the purchase agreement, the Company acquired LCM for approximately \$26.3 million in cash. In order to fund the acquisition the Company used approximately \$25 million of the availability under its revolving credit facility and \$1.3 million

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

of the funds received from the public offering of its stock.

10

11

UNIVERSAL COMPRESSION, INC. CONSOLIDATED BALANCE SHEETS (IN THOUSANDS)

	June 30, 2001	March 31, 2001
	(unaudited)	
ASSETS		
Current Assets:		
Cash	\$ 10,589	\$
Accounts receivable, net	95,256	
Inventories	109,213	
Other current assets	24,567	
Total current assets	239,625	
Property, plant and equipment		
Rental equipment	615,512	
Other	52,898	
Accumulated depreciation	(63,716)	
Net property, plant, and equipment	604,694	
Goodwill	304,458	
Other assets, net	44,899	
Total assets	\$ 1,193,676	\$
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 130,945	\$
Current portion of long term debt and capital lease obligation	10,146	
Total current liabilities	141,091	
Long-term debt	208,125	
Non-current deferred tax liability	90,110	
Deferred gain	88,700	
Capital lease obligations	5,557	
Other liabilities	704	
Total liabilities	534,287	
Common stock	49	
Paid in capital	651,978	
Currency translation adjustment	1,692	
Retained deficit	5,670	

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

Total stockholders' equity	659,389
----------------------------	---------

Total liabilities and stockholder's equity	\$ 1,193,676	\$
--	--------------	----

See accompanying notes to unaudited consolidated financial statements.

11

12

UNIVERSAL COMPRESSION, INC. UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS (IN THOUSANDS)

	Three Months 2001
Revenues:	
Rentals	\$ 75,950
Sales	64,411
Other	(47)
Total revenues	140,314
Costs and expenses:	
Rentals, exclusive of depreciation and amortization	27,565
Cost of sales, exclusive of depreciation and amortization	53,275
Depreciation and amortization	11,380
Selling, general and administrative	12,676
Operating lease	12,593
Interest expense	5,532
Non-recurring charges	--
Total costs and expenses	123,021
Income (loss) before income taxes and extraordinary items	17,293
Income taxes (benefit)	6,748
Income (loss) before extraordinary items	\$ 10,545
Extraordinary loss, net of \$2,037 income tax benefit	--

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

Net income (loss)

\$ 10,545

See accompanying notes to unaudited consolidated financial statements.

12

13

UNIVERSAL COMPRESSION, INC. UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS (IN THOUSANDS)

	Three Months Ended J 2001	
Cash flows from operating activities:		
Net loss	\$ 10,545	\$
Adjustments to reconcile net loss to cash provided by operating activities, net of effect of acquisitions:		
Depreciation and amortization	11,380	
Gain (loss) on asset sales	137	
Amortization of debt issuance costs	653	
Increase in payable to parent	--	
Accretion of discount notes	4,896	
Deferred income taxes	(16)	
Other	(9,566)	
Net cash provided by operating activities	18,029	
Cash flows from investing activities:		
Additions to property, plant and equipment, net	(40,325)	
Acquisitions	(25,029)	
Proceeds from sale of fixed assets	973	
Net cash used in investing activities	(64,381)	
Cash flows from financing activities:		
Principal repayments of long-term debt	(1,467)	
Net borrowings (repayment) under revolving line of credit	6,000	
Net repayment on sale-leaseback of vehicles	(394)	
Net proceeds (repayment) of financing lease	40,000	
Investment in subsidiary by parent	371	
Debt issuance costs	(695)	
Net cash provided by financing activities	43,815	
Effect of exchange rate	847	
Net increase (decrease) in cash and cash equivalents	(1,690)	
Cash and cash equivalents at beginning of period	12,279	

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

Cash and cash equivalents at end of period	\$	10,589	\$
	=====		=====

See accompanying notes to unaudited consolidated financial statements.

13

14

UNIVERSAL COMPRESSION, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2001

1. BASIS OF PRESENTATION

Organization

Universal Compression, Inc. was formed on December 12, 1997 for the purpose of acquiring Tidewater Compression Service, Inc. ("TCS") from Tidewater Inc. ("Tidewater"). Upon completion of the acquisition on February 20, 1998 (the "Tidewater Acquisition"), Acquisition Corp. was merged with and into TCS, which changed its name to Universal Compression, Inc. (the "Company"). The Company is a wholly owned subsidiary of Universal Compression Holdings, Inc. ("Holdings").

Effective May 30, 2000, Holdings completed an initial public offering of 7,275,000 shares of its common stock (which includes 275,000 shares of common stock issued pursuant to an over allotment option granted to the underwriters), which provided Holdings with net proceeds (after deducting underwriting discounts and commissions) of approximately \$149.2 million. Concurrently with the initial public offering, Holdings implemented a recapitalization pursuant to which all existing classes of Holdings' stock were converted into common stock. Also concurrently with the initial public offering, the Company entered into a \$50 million revolving credit facility and \$200 million operating lease facility. The proceeds of the offering and the \$62.6 million in initial proceeds from the new operating lease facility were used to repay \$192.7 million of indebtedness, and the remaining proceeds were used for working capital and to pay expenses associated with the offering and concurrent financing transactions.

On July 3, 2001, Holdings completed the public offering (the "Offering") of 1,333,333 shares of its common stock, par value \$0.01 per share, together with 2,666,667 shares of Holdings' common stock sold by certain selling stockholders, including Castle Harlan Partners III, L.P. and its affiliates. The shares were sold in the Offering at a price of \$28.50 per share, and the Offering provided Holdings with net proceeds (after deducting underwriting discounts and commissions) of approximately \$36.1 million.

The Company completed its acquisition of Gas Compression Services, Inc. ("GCSI") on September 15, 2000, of Weatherford Global Compression Services, L.P. and certain related entities ("Weatherford Global") on February 9, 2001, of ISS Compression, Inc. and its operating subsidiary, IEW Compression, Inc. (collectively "IEW") on February 28, 2001, of the international operations of Compressor Systems, Inc. ("CSII") on April 23, 2001, of KCI, Inc. ("KCI") on July 11, 2001 and of Louisiana Compressor Maintenance, Inc. ("LCM") on July 13, 2001.

These consolidated financial statements should be read in conjunction

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

with the consolidated financial statements presented in the Company's Annual Report on Form 10-K for the year ended March 31, 2001. That report contains a more comprehensive summary of the Company's major accounting policies. In the opinion of management, the accompanying unaudited consolidated financial statements contain all appropriate adjustments, all of which are normally recurring adjustments unless otherwise noted, considered necessary to present fairly the financial position of the Company and its consolidated subsidiaries and the results of operations and cash flows for the respective periods. Operating results for the three-month period ended June 30, 2001 are not necessarily indicative of the results that may be expected for the fiscal year ending March 31, 2002.

RECLASSIFICATIONS

Certain re classifications have been made to the prior year amounts to conform to the current year classification.

2. RECENT ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") 133, "Accounting for Derivative Instruments and Hedging Activities." In June 2000, the FASB issued SFAS 138, which amends certain provisions of SFAS 133 to clarify four areas causing difficulties in implementation. The amendment included expanding the normal purchase and sale exemption for supply contracts, permitting the offsetting of certain intercompany foreign currency derivatives and thus reducing the number of third party derivatives, permitting hedge accounting for foreign-currency denominated assets and liabilities, and redefining interest rate risk to reduce sources of ineffectiveness. SFAS 133 requires that an entity recognize all derivative instruments as either assets or liabilities in the balance sheet and measure those instruments at fair value. If certain conditions are met, a derivative may be specifically designated as (1) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, (2) a hedge of the exposure to variable cash flows of a forecasted transaction, or (3) a hedge of the foreign currency exposure of a net investment in a foreign operation, an unrecognized firm commitment, an available-for-sale security, or a foreign-currency-denominated forecasted transaction. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. The Company adopted SFAS 133 and the corresponding amendments under SFAS 138 on April 1, 2001. This statement had no impact on our consolidated results of operations, financial positions or cash flows.

In December 1999, the SEC issued Staff Accounting Bulletin ("SAB") 101, "Revenue Recognition in Financial Statements." SAB 101 summarizes certain of the SEC's views in applying generally accepted accounting principles to revenue recognition in financial statements. On June 26, 2000, the SEC issued an amendment to SAB 101, effectively delaying its implementation until the fourth quarter of fiscal years beginning after December 15, 1999. After reviewing SAB 101 and its amendment, the Company believes that our revenue recognition policy is appropriate and that the effects of SAB 101 and its amendment were immaterial to our results of operations.

In July 2001, the FASB issued SFAS 141, "Business Combinations," effective for all business combinations initiated after June 30, 2001 and SFAS 142, "Goodwill and Other Intangible Assets". The Company elected to adopt SFAS 142 effective April 1, 2001 as the first interim period financial statements had not previously been issued. Statement 141 addresses financial accounting and reporting for goodwill and other intangible assets acquired in a business combination at acquisition. Statement 142 addresses financial accounting and reporting for intangible assets acquired individually or with a group of other assets (but not those acquired in a business combination) at acquisition. It

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

also addresses financial accounting and

14

15

reporting for goodwill and other intangible assets subsequent to their acquisition. We adopted SFAS 142 effective April 1, 2001. Had the Standard been effective April 1, 2000, we would have adopted it in the first quarter of fiscal 2001 and our loss before taxes and extraordinary items would have been \$6,188 as a result of the elimination of \$0.7 million of amortization expense related to goodwill and net loss would have been \$7,260 as a result of the elimination of \$0.7 million of amortization expense related to goodwill and a decrease in the recorded income tax benefit of \$0.3 million.

3. ACQUISITIONS

On April 23, 2001, the Company acquired the international operations of Compressor Systems, Inc. based in Midland, Texas for approximately \$30 million in cash. The acquisition resulted in the recording of \$13 million of goodwill, which is not subject to amortization.

This acquisition was accounted for as a purchase and accordingly, the results of operations of the acquired business are included in the accompanying financial statements from the date of acquisition.

4. INVENTORIES

Inventories consisted of the following (in thousands):

	June 30, 2001 ----- (unaudited)	March 31, 2001 -----
Raw materials	\$ 64,252	\$ 63,473
Finished goods	30,479	38,705
Work-in-progress	14,482	18,761
	-----	-----
Total	\$ 109,213	\$ 120,939
	=====	=====

5. OPERATING LEASE FACILITIES

In May 2000, the Company and Holdings entered into a \$200 million operating lease facility pursuant to which the Company sold and leased back certain compression equipment from a Delaware business trust for a five-year term. The rental payments under the lease facility included an amount based on LIBOR plus a variable amount depending on the Company's operating and financial results, applied to the funded amount of the lease. Under the lease facility, the Company received an aggregate of approximately \$155 million in proceeds from the sale of compression equipment in May, November and December 2000 and in connection with the GCSI acquisition, in September 2000. The equipment was sold and leased back by the Company for a five-year period from May 2000 and deployed by the Company under its normal operating procedures. The equipment sold had a book value of approximately \$106 million and the equipment sale resulted in deferred gain of approximately \$49 million that was transferred to new operating

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

lease facilities.

The Company had residual value guarantees on the equipment under the operating lease facility of approximately 85% of the funded amount that were due upon termination of the lease and which could be satisfied by a cash payment or the exercise of the purchase option. The facility contained certain covenants restricting the Company's operations, including its ability to enter into acquisition and sales transactions, incur additional indebtedness, permit additional liens on its assets and pay dividends. The Company's obligations under this facility were collateralized by liens on its compression equipment subject to the lease and certain related rights. Under the operating lease facility, Universal was the lessee and the Company guaranteed certain of Universal's obligations thereunder. The Company has replaced this facility with new operating lease facilities with similar terms.

In connection with the Weatherford Global acquisition, on February 9, 2001, the Company raised \$427 million under a new seven-year term senior secured notes operating lease facility (the "SSN Operating Lease Facility") funded primarily through an offering of \$350 million 8 7/8% senior secured notes due 2008 by an unaffiliated entity. The Company also entered into a new \$125 million secured revolving credit facility and a new \$200 million asset-backed securitization operating lease facility (the "ABS Operating Lease Facility"), which facility consists of a series of six leases with terms ranging from three to eight years. At the closing of the Weatherford Global acquisition, the Company funded approximately \$80 million under the ABS Operating Lease Facility and had no amounts outstanding under the new revolving credit facility. The proceeds from the two new operating lease facilities were used to restructure existing operating lease obligations and refinance certain existing indebtedness of the Company (including the previous operating lease facility described above in the first paragraph) and Weatherford Global.

During the quarter, the Company funded \$40 million under the ABS Operating Lease Facility. The funds were used for acquisitions as well as for general working capital purposes. At June 30, 2001, the Company had outstanding lease balances totaling \$567.5 million and the equipment sold to the two new operating lease facilities had a book value of approximately \$478.8 million and the equipment sale resulted in a deferred gain of approximately \$88.7 million.

Under the operating lease facilities, the Company, as lessee, makes rental payments to the lessor for the leased equipment. Under the SSN Operating Lease Facility, the rental payments include amounts based on the interest accrued on the 8 7/8% senior secured notes and an amount based on LIBOR or a variable base rate equal to the sum of the interest accrued on the lessor's term loan, the yield on the equity investment in the lessor and other fees. The equipment leased by the Company under the SSN Operating Lease Facility had an initial appraised value of \$427 million. The Company

has residual value guarantees on the equipment under the SSN Operating Lease Facility of approximately 82% of the funded amount that are due upon termination of the lease in the event the purchase option or renewal options are not selected by the lessee.

Under the ABS Operating Lease Facility, the rental payments are based on a variable rate plus the yield on the equity investment in the facility. The ABS Operating Lease Facility is collateralized by a first priority security interest in all of the assets under the facility. At the end of each lease term under the ABS Operating Lease Facility, the Company has residual value

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

guarantees on the equipment under the facility of approximately 85% of the funded amount.

The Company annually assesses whether it is probable that the value of the property at the end of the lease terms will be less than the residual value guarantee for each operating lease. On the date the deficiency becomes probable the expected deficiency (up to the maximum for which the Company is responsible) would be accrued by the Company using the straight-line method over the remaining term of the leases.

6. EXTRAORDINARY LOSSES

During the quarter ended June 30, 2000, the Company incurred extraordinary losses of \$3.4 million (net of \$2.0 million income tax benefit) related to its debt restructuring that occurred concurrently with Holdings' initial public offering of its common stock.

7. NON-RECURRING CHARGES

During the quarter ended June 30, 2000, the Company incurred non-recurring charges of \$7.1 million, related to the early termination of a management agreement and a consulting agreement and other related fees in connection with Holdings' initial public offering and concurrent financing transactions.

8. RELATED PARTY TRANSACTIONS

Management Agreement

Castle Harlan Inc., an affiliate of a significant stockholder of Holdings, entered into an agreement whereby, in exchange for certain management services rendered, Holdings agreed to pay a fee to Castle Harlan Inc. totaling \$3 million per year. The amount was paid in advance for the first year and quarterly in advance thereafter. The agreement was for a term of five years, renewable automatically from year to year thereafter unless Castle Harlan Inc. or its affiliates beneficially own less than 20% of the then outstanding stock of Holdings.

In connection with the initial public offering in the quarter ended June 30, 2000, Holdings terminated its Management Agreement with Castle Harlan, Inc. In exchange for such termination, Holdings paid \$3 million in cash and issued 136,364 shares of its common stock to Castle Harlan.

Transitional Services Agreement

Concurrently with the closing of the Weatherford Global acquisition, Weatherford and Weatherford Global, as the Company's subsidiary, entered into a transitional services agreement under which Weatherford provided certain administrative and support services, such as shared corporate office space and general communication and information services, to Weatherford Global until June 9, 2001. Weatherford Global paid Weatherford \$125,000 for thirty days of these services.

9. INDUSTRY SEGMENTS

Prior to the Weatherford Global merger, the Company had three principal industry segments: Domestic Rental and Maintenance, International Rental and Maintenance and Engineered Products. Due to the Weatherford Global merger, the changing nature of the markets the Company serves and in order to align ourselves with those markets, the Company changed its internal business organization during fiscal 2001. The Company is now organized into four principal businesses or operating segments: Domestic Rental and Maintenance,

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

International Rental and Maintenance, Fabrication and Parts Sales and Service. The two Rental and Maintenance Segments provide natural gas compression rental and maintenance services to meet specific customer requirements. The Fabrication Segment involves the design, fabrication and sale of natural gas and air compression packages to meet customer specifications. The International Rental and Maintenance Segment represents all of the Company's international rental and maintenance operations. The Parts Sales and Service Segment involves the sale of parts to and the service of compressor units owned by oilfield companies.

The Company's reportable segments are strategic business units that offer different products and services. They are managed separately since each business requires different marketing strategies due to customer specifications. Each of these business groups has one or more general managers who report directly to the Chief Executive Officer ("CEO"). The CEO has been identified as the Chief Operating Decision Maker as defined by SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." The Company has restated segment results for prior periods as a result of our fiscal 2001 realignment.

In addition to these four operating segments, accounting, administration, facilities, finance, human resources, legal, marketing, procurement and sales groups also report to the CEO. The CEO does not evaluate the operating segments based upon fully allocated profit and loss statements, and the segments' reportable operating profit excludes allocated expenses. Operating segments do not have material sales to other segments, and accordingly, there are no inter-segment revenues to be reported. The Company also does not allocate our restructuring charges, interest and other income, interest expense or income taxes to operating segments.

The following table presents sales and other financial information by industry segment for the three-month period ended June 30, 2001 (in thousands):

17

	DOMESTIC RENTAL AND MAINTENANCE	INTERNATIONAL RENTAL AND MAINTENANCE	FABRICATION	PARTS SALES AND SERVICE	CORPORATE AND OTHER
Revenues	\$ 61,920	\$ 14,030	\$ 32,234	\$ 32,177	\$
Gross margin	38,755	9,281	4,193	7,295	
Operating income	24,591	5,555	1,098	4,224	

The following table presents sales and other financial information by industry segment for the three-month period ended June 30, 2000 (in thousands):

	DOMESTIC RENTAL AND MAINTENANCE	INTERNATIONAL RENTAL AND MAINTENANCE	FABRICATION	PARTS SALES AND SERVICE	CORPORATE AND OTHER
Revenues	\$ 22,175	\$ 4,099	\$ 7,661	\$ 609	\$
Gross margin	14,245	3,059	1,522	201	
Operating income	5,703	1,308	921	121	

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

No one customer accounted for more than 10% of revenues for either of the periods presented.

10. COMMITMENTS AND CONTINGENCIES

In the ordinary course of business, the Company is involved in various pending or threatened legal actions. In the opinion of management, the amount of ultimate liability, if any, with respect to these actions will not have a materially adverse effect on the Company's financial position, operating results or cash flows.

The Company has no other commitments or contingent liabilities, which in the judgment of management, would result in losses that would materially affect the Company's consolidated financial position or operating results.

On May 24, 2001, the Company entered into an agreement with Tidewater to settle acquisition-related claims, which included costs for remediation pursuant to an environmental assessment, in exchange for payment to the Company of \$1 million and termination of the purchase price adjustment agreement, which eliminated any payment obligation by the Company under that agreement.

11. SUBSEQUENT EVENTS

On July 3, 2001, Holdings, completed the public offering (the "Offering") of 1,333,333 shares of its common stock, par value \$0.01 per share, together with 2,666,667 shares of Holdings' common stock sold by certain selling stockholders, including Castle Harlan Partners III, L.P. and its affiliates. The underwriters did not purchase additional shares to cover over allotments. The shares were sold in the Offering at a price of \$28.50 per share, and the Offering provided Holdings with net proceeds (after deducting underwriting discounts and commissions) of approximately \$36.1 million.

Pursuant to the indenture, consummation of the Offering gave the holders of the Company's 9 7/8% senior discount notes the right to require the Company to repurchase those notes at a price equal to 101% of the accreted value, plus accrued and unpaid interest to date. As of June 30, 2001, UCI had approximately \$205.7 million aggregate principal amount outstanding under its 9% senior discount notes. The Company expects to finance any repurchases of the 9% senior discount notes through its revolving credit facility or its operating lease facilities.

On July 11, 2001, the Company completed its acquisition of KCI, a Tulsa, Oklahoma-based fabricator of large horsepower compressors. Under the terms of the purchase agreement, the Company acquired KCI for approximately \$26.3 million in cash and 694,927 shares of the Company's common stock. In addition, the Company incurred costs and assumed other liabilities related to the transaction of approximately \$6 million. Concurrently with the acquisition, the Company repaid substantially all of KCI's approximately \$51 million of indebtedness. In order to fund the acquisition the Company used approximately \$50 million of the availability under its revolver and \$27.3 million of the funds received from the public offering of its stock.

In connection with the acquisition and the issuance of Holdings' shares of common stock in the acquisition, Holdings entered into registration rights agreements, which provide certain demand and piggyback registration rights to the former holders of the common stock of KCI and the partnership interests of KCI Compression Company, L.P. Under the terms of the agreements, Holdings has agreed to prepare and file a registration statement to register the resale of the shares of common stock issued in the acquisition. In addition, the former

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

KCI holders may request to have the sale of their shares included in certain registration statements with respect to any proposed public offering by Holdings or other holders of Holdings' common stock. The former KCI shareholders have agreed, with exceptions, not to sell or transfer any shares of Holdings' common stock until after October 9, 2001, 90 days after the closing of the acquisition.

On July 13, 2001, the Company completed its acquisition of LCM, a Houma, Louisiana-based supplier of maintenance, repair, overhaul and upgrade services to the natural gas pipeline and related markets. Under the terms of the purchase agreement, the Company acquired LCM for approximately \$26.3 million in cash. In order to fund the acquisition the Company used approximately \$25 million of the availability under its revolving credit facility and \$1.3 million of the funds received from the public offering of its stock.

17

18

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

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains "forward-looking statements" intended to qualify for the safe harbors from liability established by the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact contained in this report are forward-looking statements, including, without limitation, statements regarding future financial position, business strategy, proposed acquisitions, budgets, litigation, projected costs and plans and objectives of management for future operations. You can identify many of these statements by looking for words such as "believes," "expects," "will," "intends," "projects," "anticipates," "estimates," "continues" or similar words or the negative thereof.

Forward-looking statements in this report include, without limitation:

anticipated cost savings and other synergies resulting from our acquisition of Weatherford Global and other businesses;

the sufficiency of our available cash flows to fund our continuing operations;

anticipated synergies, future revenues and EBITDA, as adjusted, resulting from our acquisitions of Weatherford Global, Gas Compression Services, Inc., IEW Compression, Inc., KCI, Inc., Louisiana Compressor Maintenance, Inc. and other businesses;

capital improvements;

the expected amount of capital expenditures;

our future financial position;

the future value of our equipment;

our growth strategy and projected costs; and

plans and objectives of our management for our future operations.

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

These forward-looking statements are subject to various risks and uncertainties that could cause our actual results to differ materially from those anticipated as of the date of this report. The risks related to our business described in our Annual Report on Form 10-K for the year ended March 31, 2001 under "Risk Factors" and in this report could cause our actual results to differ from those described in, or otherwise projected or implied by, the forward-looking statements. Although the Company believes that the expectations reflected in these forward-looking statements are based on reasonable assumptions, no assurance can be given that these expectations will prove to be correct. Important factors that could cause our actual results to differ materially from the expectations reflected in these forward-looking statements include, among other things:

our inability to successfully integrate the business of Weatherford Global Gas Compression Services, Inc., IEW Compression, Inc., KCI, Inc., Louisiana Compressor Maintenance, Inc. and other businesses;

conditions in the oil and gas industry, including the demand for natural gas and the impact of the price of natural gas;

competition among the various providers of contract compression services;

changes in safety and environmental regulations pertaining to the production and transportation of natural gas;

changes in economic or political conditions in operating markets;

introduction of competing technologies by other companies;

our ability to retain and grow our customer base;

employment workforce factors, including loss of key employees; and

liability claims related to the use of our products and services.

All subsequent written and oral forward-looking statements made by us or on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. The forward-looking statements included in this report are only made as of the date of this report and the Company undertake no obligation to publicly update such forward-looking statements to reflect new information, subsequent events or otherwise.

The terms "our," "Company," "we," and "us" when used in this report refer to Universal Compression Holdings, Inc. and its subsidiaries, including Universal Compression, Inc. ("Universal"), as a combined entity, except where it is made clear that such term means only the parent company, and includes its predecessors.

We were formed in December 1997 to acquire all of the outstanding stock of Tidewater Compression Service, Inc. Upon completion of the acquisition in February 1998, Tidewater Compression became our wholly-owned operating subsidiary and changed its name to Universal Compression, Inc. Through this subsidiary, our gas compression service operations date back to 1954.

During the quarter ended June 30, 2000, we completed an initial public

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

offering of 7,275,000 shares of our common stock (including 275,000 shares of common stock issued pursuant to an over allotment option granted to the underwriters), which provided us with net proceeds (after deducting underwriting discounts and commissions) of approximately \$149.2 million. Concurrently with our initial public offering, we implemented a recapitalization pursuant to which all then existing classes of our stock were converted into common stock. We used the proceeds of the offering and the \$62.6 million in initial proceeds from an operating lease facility to repay \$192.7 million of indebtedness, and the remaining proceeds for working capital and to pay expenses associated with the offering and concurrent financing transactions.

On July 3, 2001, the Company completed the public offering (the "Offering") of 1,333,333 shares of its common stock, par value \$0.01 per share, together with 2,666,667 shares of the Company's common stock sold by certain selling stockholders, including Castle Harlan Partners III, L.P. and its affiliates. The underwriters did not purchase additional shares to cover over allotments. The shares were sold in the Offering at a price of \$28.50 per share, and the Offering provided the Company with net proceeds (after deducting underwriting discounts and commissions) of approximately \$36.1 million. The Company used the proceeds to fund the cash portion of the purchase price in its acquisition of KCI, Inc., to repay a portion of KCI's indebtedness concurrently with the acquisition, as described below and to partially fund the purchase price in its acquisition of Louisiana Compressor Maintenance, Inc., as described below. Following the Offering, Castle Harlan owned or had voting control over approximately 6% of the Company's outstanding common stock.

Consummation of the Offering gave the holders of Universal's 9 7/8% senior discount notes the right to require Universal to repurchase those notes at a price equal to 101% of the accreted value, plus accrued and unpaid interest to date. The Company expects to finance any repurchases of the 9 7/8% senior discount notes through the Credit Agreement or the operating lease facilities.

Since our initial public offering, we have completed six acquisitions. Our completed acquisitions include Gas Compression Services, Inc. ("GCSI") in September 2000, Weatherford Global and IEW Compression in February 2001, Compressor Systems International, Inc., the international operations of Compressor Systems, Inc. ("CSII"), in April 2001, KCI, Inc. on July 11, 2001 and Louisiana Compressor Maintenance, Inc. on July 13, 2001. GCSI added approximately 138,000 horsepower to our fleet and provided us with an increased customer base, additional market segments and additional fabrication capabilities. IEW added approximately 26,000 horsepower to our fleet, as well as important offshore service capabilities. CSII added approximately 34,000 horsepower to our fleet in Mexico and Argentina. KCI added approximately 125,000 horsepower to our domestic fleet as well as significant fabrication expertise and capabilities, a 100,000 square foot fabrication facility in Tulsa, Oklahoma and expertise in the pipeline and related natural gas markets. LCM added to our ability to be a supplier of maintenance, repair, overhaul and upgrade services to natural gas pipeline and related markets.

Our Weatherford Global acquisition in February 2001 more than doubled our size. We acquired Weatherford Global, which was the second largest natural gas compression services company in the world in terms of horsepower, for 13,750,000 shares of our common stock (approximately 46% of total outstanding shares following the Offering) and the restructuring of approximately \$323 million in debt and operating lease obligations. This acquisition added over 950,000 horsepower to our fleet and provided us with a number of important strategic and operational benefits, including expanded international operations, an increased parts sales and service business and cost savings and synergies. Pursuant to a voting agreement, Weatherford agreed to limit its voting power to 33 1/3% of the Company's outstanding common stock, subject to certain limitations.

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

We are the second largest provider of natural gas compressor rental, sales, operations, maintenance and fabrication services to the natural gas industry in terms of horsepower, with one of the largest gas compressor fleets in the U.S. and a strong presence in key international markets.

UNIVERSAL COMPRESSION HOLDINGS, INC.

Three months ended June 30, 2001 compared to three months ended June 30, 2000

Revenues. Our total revenues for the three months ended June 30, 2001 increased \$105.5 million, or 303.2%, to \$140.3 million, compared to \$34.8 million for the three months ended June 30, 2000. Our rental revenues increased by \$49.7 million, or 189.0%, to \$76.0 million during the three months ended June 30, 2001 from \$26.3 million during the three months ended June 30, 2000. Domestic rental revenues increased by \$39.7 million, or 178.8%, to \$61.9 million during the three months ended June 30, 2001 from \$22.2 million during the three months ended June 30, 2000. Our international rental revenues increased by \$9.9 million, or 241.5%, to \$14.0 million during the three months ended June 30, 2001 from \$4.1 million during the three months ended June 30, 2000. The increase in domestic rental revenues primarily resulted from continued expansion of our existing rental fleet and through the acquisition of GCSI, Weatherford Global and IEW. The increase in international rental revenues resulted from expansion of our international rental fleet primarily through the addition of horsepower from our acquisitions, particularly our Weatherford Global acquisition, continued expansion of our existing rental fleet and continued high utilization rates.

Domestic average rented horsepower for the three months ended June 30, 2001 increased by 197.8% to approximately 1,465,000 horsepower from approximately 492,000 horsepower for the three months ended June 30, 2000. In addition, international average rented horsepower for the three months ended June 30, 2001 increased by 447.2% to approximately 290,000 horsepower from approximately 53,000 horsepower for the three months ended June 30, 2000, primarily through expansion of our international rental fleet, continued high utilization rates and additional service. Our average horsepower utilization rate for the three months ended June 30, 2001 was approximately 89.4%, up from 84.3% in the three months ended June 30, 2000. At the end of the quarter, we had approximately 2.0 million available horsepower. These horsepower and utilization amounts include Weatherford Global and IEW for the full first quarter and CSII for the 68 days from the date of the acquisition.

Our revenue from fabrication increased to \$32.2 million from \$7.7 million, an increase of 318.2%. The increase in fabrication revenue, consisting mostly of equipment fabrication, was due primarily to our acquisition of Weatherford Global. Revenues from fabrication vary quarter to quarter

due to the time of completion of the equipment being sold. Our backlog of fabrication projects at the end of June 2001 was approximately \$46.9 million, compared with a backlog of \$18.4 million at the same time a year earlier. From March 31 to June 30, 2001, our backlog increased \$6.5 million.

Our revenues from parts sales and service increased to \$32.2 million during the three months ended June 30, 2001 from \$609 thousand during the three months ended June 30, 2000, an increase of 5,187.4%. The increase was due primarily to our acquisitions of Weatherford Global and IEW which have made the parts sales and service segment a more significant part of our business.

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

Gross Margin. Our gross margin (defined as total revenue less rental expense, cost of sales (exclusive of depreciation and amortization), gain on asset sales and interest income) for the three months ended June 30, 2001 increased \$40.4 million, or 211.5%, to \$59.5 million from \$19.1 million for the three months ended June 30, 2000. Our rental gross margin for the three months ended June 30, 2001 increased \$30.7 million, or 177.5%, to \$48.0 million compared to gross margin of \$17.3 million for the three months ended June 30, 2000. Rental gross margin increased primarily as the result of our rental revenue growth discussed above and operating cost improvements realized by rental operations. Our fabrication gross margin for the three months ended June 30, 2001 increased \$2.7 million, or 180.0%, to \$4.2 million compared to a gross margin of \$1.5 million for the three months ended June 30, 2000. Fabrication gross margin increased primarily due to increased sales resulting from our acquisitions of GCSI and Weatherford Global as well as strong customer demand, cost reductions and their resulting gross margin effects.

Our parts sales and service gross margin for the three months ended June 30, 2001 increased \$7.1 million or 3,532.3%, to \$7.3 million compared to a gross margin of \$201 thousand for the three months ended June 30, 2000. Parts sales and service gross margin increased primarily due to our acquisition of Weatherford Global and operating cost improvements.

Selling, General and Administrative Expenses. Our selling, general and administrative expenses for the three months ended June 30, 2001 increased \$9.2 million compared to the three months ended June 30, 2000. Selling, general and administrative expenses represented 9.0% of revenue for the three months ended June 30, 2001 compared to 9.9% of revenue for the three months ended June 30, 2000. The percentage decrease was primarily due to the elimination of management fees in connection with our initial public offering in May 2000 in addition to synergies achieved in our acquisitions of GCSI and Weatherford Global. These reductions have been offset partially by increases in certain expenses related to our operating as a publicly traded company.

EBITDA, As Adjusted. Our EBITDA, as adjusted, for the three months ended June 30, 2001 increased 196.2% to \$46.8 million from \$15.8 million for the three months ended June 30, 2000, primarily due to increases in horsepower from acquisitions and continued expansion of our existing rental fleet and utilization of the compression rental fleet, gross margin contribution from fabrication, operating cost improvements realized by rental operations, and a decreased percentage of selling, general and administrative expenses, as discussed above. EBITDA, as adjusted, is defined as net income plus income taxes, interest expense, leasing expense, management fees, depreciation and amortization, excluding non-recurring items and extraordinary gains or losses. EBITDA, as adjusted, is not a measure of financial performance under generally accepted accounting principles and should not be considered an alternative to operating income or net income as an indicator of our operating performance or to net cash provided by operating activities as a measure of its liquidity. Additionally, the EBITDA, as adjusted, computation used herein may not be comparable to other similarly titled measures of other companies. EBITDA, as adjusted, represents a measure upon which management assesses financial performance, and certain covenants in our borrowing arrangements are tied to similar measures. We believe that EBITDA, as adjusted, is a standard measure of financial performance used for valuing companies in the compression industry. EBITDA, as adjusted, is a useful yardstick as it measures the capacity of companies to generate cash without reference to how they are capitalized, how they account for significant non-cash charges for depreciation and amortization associated with assets used in the business (the majority of which are long-lived assets in the compression industry), or what their tax attributes may be.

Non-recurring Charges. During the three months ended June 30, 2000, we incurred non-recurring charges of \$7.1 million related to the early termination

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

of a management agreement and a consulting agreement and other related fees in connection with our initial public offering and concurrent financing transactions.

Depreciation and Amortization. Depreciation and amortization increased by \$3.9 million to \$11.4 million during the three months ended June 30, 2001, compared to \$7.5 million during the three months ended June 30, 2000. The increase resulted primarily from the expansion of our rental fleet offset partially by the compression equipment sold and leased back under our operating lease facilities. Included in depreciation and amortization for the three months ended June 30, 2000 is \$675 thousand of amortization expense. As of April 1, 2001, the Company has adopted SFAS 142 which, among other things, eliminated amortization of goodwill.

Operating Lease. Operating lease expense increased by \$11.9 million to \$12.6 million during the three months ended June 30, 2001 from \$689 thousand during the three months ended June 30, 2000. The increase is due to the expense associated with increased balance on the operating lease facilities entered into concurrently with the Weatherford Global merger. The outstanding balance under the operating lease facilities at June 30, 2001 was \$567.5 million, consisting of \$427.0 million under our new operating lease facility and \$140.5 million under our asset-backed securitization operating lease facility.

Interest Expense. Interest expense decreased \$2.5 million to \$5.5 million for the three months ended June 30, 2001 from \$8.0 million for the three months ended June 30, 2000 primarily as a result of the reduction of debt resulting from our initial public offering and financing restructurings. The decrease in interest expense was offset partially by increased accretion of our 9 7/8% senior discount notes and the assumption and refinancing of debt related to our GCSI acquisition.

Extraordinary Loss. During the three months ended June 30, 2000, we incurred extraordinary losses of \$10.0 million (\$6.3 million net of income tax) related to debt restructurings that occurred concurrently with our initial public offering.

Net Income (Loss). We had net income of \$10.5 million for the three months ended June 30, 2001 compared to a net loss of \$10.9 million for the three months ended June 30, 2000. The change was primarily due to extraordinary and non-recurring charges incurred during the three months ended June 30, 2000 as well as increase in our gross margins and decrease in interest expense, offset partially by increased depreciation and amortization related to the continued expansion of our fleet, increased leasing expense resulting from our operating lease facilities, increased selling, general and administrative expense resulting from our increased headcount due to growth and increased income tax expense resulting from our positive operating income.

Liquidity and Capital Resources

In May 2000, concurrently with our initial public offering, we entered into a \$200 million, five-year operating lease facility, which involved a sale and leaseback of compression equipment to a trust. Under this operating lease facility, certain of our compression equipment was sold to the trust for approximately \$155 million and leased back by us for a five-year period. At the same time, we repaid and terminated a term loan and revolving credit facility and entered into a \$50 million secured revolving credit facility which had a

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

five-year term. This revolver and our previous operating lease facility were repaid and terminated in February 2001 in connection with our Weatherford Global acquisition, as described below.

Our cash and cash equivalents balance at June 30, 2001 was \$10.6 million, compared to \$12.3 million at March 31, 2001. For the three months ended June 30, 2001, we provided cash flow from operations of \$18.0 million, used \$64.4 million of cash for investing activities and provided another \$43.8 million of cash in financing activities and had a \$0.8 million positive effect of exchange rate change.

During the three months ended June 30, 2001, \$40.0 million was received for compression equipment under our asset-backed securitization operating lease facility, \$10.5 million was generated from net income, and \$6.0 million was received from borrowings under our revolving credit facility. We used this cash as follows: \$40.3 million for capital expenditures, \$25.0 million for acquisitions, \$9.6 million on working capital changes and \$1.5 million to make net principal payments on outstanding indebtedness.

On July 3, 2001, the Company, completed the offering of 1,333,333 shares of its common stock, par value \$0.01 per share, together with 2,666,667 shares of the Company's common stock sold by certain selling stockholders, including Castle Harlan Partners III, L.P. and its affiliates. The shares were sold in the Offering at a price of \$28.50 per share, and the Offering provided the Company with net proceeds (after deducting underwriting discounts and commissions) of approximately \$36.1 million. The Company used the proceeds to fund the cash portion of the purchase price in its acquisition of KCI, Inc., to repay a portion of KCI's indebtedness concurrently with the acquisition, as described below, and to partially fund the cash portion of the purchase price in its acquisition of Louisiana Compressor Maintenance, Inc. as described below. Following the Offering, Castle Harlan owned or had voting control over approximately 6% of the Company's outstanding common stock.

Pursuant to the indenture governing the 9 7/8% senior discount notes due 2008 of Universal, the holders of the notes have the right to require Universal to repurchase the notes through August 23, 2001 as a result of the consummation of the Offering as Castle Harlan's ownership of less than 20% of the Company's common stock constitutes a change of control under the indenture. As of June 30, 2001, Universal had approximately \$205.7 million aggregate principal amount outstanding under the 9 7/8% senior discount notes. The Company expects to finance any repurchases of the 9 7/8% senior discount notes through its revolving credit facility or its operating lease facilities.

As of July 31, 2001, we had unused availability of approximately \$109.5 million (approximately \$59.5 million under our asset-backed securitization facility and \$50.0 million under our revolving credit facility). Under the revolving credit facility, \$110 million is currently committed and \$15 million is obtainable upon payment of additional fees. Subject to certain covenant restrictions, we also have up to an additional \$366 million available under our new operating lease facility until one year from February 9, 2001. Additional amounts under this facility would be funded through an additional issuance of senior secured notes by BRL, an unaffiliated entity which is the lessor under that facility, and a corresponding increase in the related BRL term loan and equity investment. The proceeds, if any, from the additional notes, term loan and equity investment would then be used to purchase additional equipment to lease to Universal under the operating lease.

On July 11, 2001, the Company completed its acquisition of KCI, a Tulsa, Oklahoma-based fabricator of large horsepower compressors. Under the terms of the purchase agreement, the Company acquired KCI for approximately \$26.3 million in cash and 694,927 shares of the Company's common stock. In addition, the Company incurred costs and assumed other liabilities related to

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

the transaction of approximately \$6 million. Concurrently with the acquisition, the Company repaid substantially all of KCI's approximately \$51 million of indebtedness. In order to fund the acquisition the Company used approximately \$50 million of the availability under its revolver and \$27.3 million of the funds received from the Offering. This acquisition provides us with significant fabrication expertise and capabilities and added approximately 125,000 horsepower to our rental fleet with an average horsepower utilization rate of 85%. As of July 31, 2001, we estimate that KCI's fabrication backlog was approximately \$70 million.

In connection with the acquisition and the issuance of shares of common stock in the acquisition, the Company entered into registration rights agreements, which provide certain demand and piggyback registration rights to the former holders of the common stock of KCI and the partnership interests of KCI Compression Company, L.P. Under the terms of the agreements, the Company has agreed to file a registration statement to register the resale of the shares of common stock issued in the acquisition. In addition, the former KCI holders may request to have the sale of their shares included in certain registration statements with respect to any proposed public offering by the Company or other holders of the Company's common stock. The former KCI holders have agreed, with exceptions, not to sell or transfer any shares of the Company's common stock until after October 9, 2001, 90 days after the closing of the acquisition.

On July 13, 2001, the Company completed its acquisition of LCM, a Houma, Louisiana-based supplier of maintenance, repair, overhaul and upgrade services to the natural gas pipeline and related markets. Under the terms of the purchase agreement, the Company acquired LCM for approximately \$26.3 million in cash. In order to fund the acquisition the Company used approximately \$25 million of the availability under its revolver and \$1.3 million of the funds received from the Offering. Under current operating conditions, we expect LCM to add approximately \$18 million in revenue and approximately \$4.5 million in EBITDA, as adjusted, in the first full year of combined operations.

As of June 30, 2001, we have realized approximately \$20 million of cost savings on an annualized basis from our Weatherford Global acquisition. The key drivers for the savings were the elimination of overlapping areas of various domestic operations, including fabrication facilities, as well as duplicate selling, general and administrative activities.

For fiscal 2002, the Company is expecting revenues to be approximately \$650 to \$660 million, with EBITDA, as adjusted, of approximately \$210 to \$213 million. These results are expected based on slight quarterly gross margin improvements in both the domestic and international rental segments and the parts, sales and service segment, as well as, continued revenue growth in all business segments.

21

22

Operating lease and net interest expense are expected to be approximately \$77 to \$80 million with depreciation being approximately \$48 to \$50 million for the fiscal year.

These projections are expected to result in approximately \$1.70 earnings per diluted share for the fiscal year.

Capital expenditures, excluding our acquisitions of CSII, KCI and LCM, are expected to be approximately \$180 to \$200 million for the year, with international expenditures between \$30 and \$40 million and only \$25 million

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

being used for maintenance, capital and other corporate needs.

We believe that funds generated from our operations, together with our existing cash, the net proceeds to us from the Offering, and the additional capacity available under our revolving credit facility and operating lease facilities will be sufficient to finance our current operations, planned capital expenditures and internal growth for fiscal year 2002. If we were to make significant additional acquisitions for cash, we may need to obtain additional debt, equity or operating lease financing.

UNIVERSAL COMPRESSION, INC.

Three months ended June 30, 2001 compared to three months ended June 30, 2000

Revenues. Universal's total revenues for the three months ended June 30, 2001 increased \$105.5 million, or 303.2%, to \$140.3 million, compared to \$34.8 million for the three months ended June 30, 2000. Universal's rental revenues increased by \$49.7 million, or 189.0%, to \$76.0 million during the three months ended June 30, 2001 from \$26.3 million during the three months ended June 30, 2000. Domestic rental revenues increased by \$39.7 million, or 178.8%, to \$61.9 million during the three months ended June 30, 2001 from \$22.2 million during the three months ended June 30, 2000. Universal's international rental revenues increased by \$9.9 million, or 241.5%, to \$14.0 million during the three months ended June 30, 2001 from \$4.1 million during the three months ended June 30, 2000. The increase in domestic rental revenues primarily resulted from continued expansion of our existing rental fleet as well as through the acquisition of GCSI, Weatherford Global and IEW. The increase in international rental revenues resulted from expansion of Universal's international rental fleet primarily through the addition of horsepower from Universal's acquisitions, particularly our Weatherford Global acquisition, continued expansion of our existing rental fleet and continued high utilization rates.

Domestic average rented horsepower for the three months ended June 30, 2001 increased by 197.8% to approximately 1,465,000 horsepower from approximately 492,000 horsepower for the three months ended June 30, 2000. In addition, international average rented horsepower for the three months ended June 30, 2001 increased by 447.2% to approximately 290,000 horsepower from approximately 53,000 horsepower for the three months ended June 30, 2000, primarily through expansion of our international rental fleet and continued high utilization rates. Our average horsepower utilization rate for the three months ended June 30, 2001 was approximately 89.4%, up from 84.3% in the three months ended June 30, 2000. At the end of the quarter, we had approximately 2.0 million available horsepower. These horsepower and utilization amounts include Weatherford Global and IEW for the full first quarter and CSII for the 68 days from the date of their acquisition.

Universal's revenue from fabrication increased to \$32.2 million from \$7.7 million, an increase of 318.2%. The increase in fabrication revenue, consisting mostly of equipment fabrication was due primarily to Universal's acquisition Weatherford Global. Revenues from fabrication vary quarter to quarter due to the time of completion of the equipment being sold. Universal's backlog of fabrication projects at the end of June 2001 was approximately \$46.9 million, compared with a backlog of \$18.4 million at the same time a year earlier. From March 31 to June 30, 2001, Universal's backlog increased \$6.5 million.

Universal's revenues from parts sales and service increased to \$32.2 million during the three months ended June 30, 2001 from \$609 thousand during the three months ended June 30, 2000, an increase of 5,187.4%. The increase was due primarily to Universal's acquisitions of Weatherford Global and IEW which have made the parts sales and service segment a more significant part of Universal's business.

Gross Margin. Universal's gross margin (defined as total revenue less rental expense, cost of sales (exclusive of depreciation and amortization), gain on asset sales and interest income) for the three months ended June 30, 2001 increased \$40.4 million, or 211.5%, to \$59.5 million from \$19.1 million for the three months ended June 30, 2000. Universal's rental gross margin for the three months ended June 30, 2001 increased \$30.7 million, or 177.5%, to \$48.0 million compared to gross margin of \$17.3 million for the three months ended June 30, 2000. Rental gross margin increased primarily as the result of Universal's rental revenue growth discussed above and operating cost improvements realized by rental operations. Universal's fabrication gross margin for the three months ended June 30, 2001 increased \$2.7 million, or 180.0%, to \$4.2 million compared to a gross margin of \$1.5 million for the three months ended June 30, 2000. Fabrication gross margin increased primarily due to increased sales resulting from Universal's acquisitions of GCSI and Weatherford Global as well as strong customer demand, cost reductions and their resulting gross margin effects.

Universal's parts sales and service gross margin for the three months ended June 30, 2001 increased \$7.1 million or 3,532.3%, to \$7.3 million compared to a gross margin of \$201 thousand for the three months ended June 30, 2000. Parts sales and service gross margin increased primarily due to Universal's acquisition of Weatherford Global and operating cost improvements.

Selling, General and Administrative Expenses. Universal's selling, general and administrative expenses for the three months ended June 30, 2001 increased \$9.2 million compared to the three months ended June 30, 2000. Selling, general and administrative expenses represented 9.0% of revenue for the three months ended June 30, 2001 compared to 9.9% of revenue for the three months ended June 30, 2000. The percentage decrease was primarily due to the elimination of management fees in connection with Universal's initial public offering in May 2000 in addition to synergies achieved in Universal's acquisitions of GCSI and Weatherford Global. These reductions have been offset partially by increases in certain expenses related to Universal's operating as a publicly traded company.

EBITDA, As Adjusted, Our EBITDA, as adjusted, for the three months ended June 30, 2001 increased 196.2% to \$46.8 million from \$15.8 million for the three months ended June 30, 2000, primarily due to increases in horsepower and utilization of the compression rental fleet, gross margin contribution from fabrication, operating cost improvements realized by rental operations, and a decreased percentage of selling, general and administrative expenses, as discussed above. EBITDA, as adjusted, is defined as net income plus income taxes, interest expense, leasing expense, management fees, depreciation and amortization, excluding non-recurring items and extraordinary gains or losses. EBITDA, as adjusted, is not a measure of financial performance under generally accepted accounting principles and should not be considered an alternative to operating income or

net income as an indicator of Universal's operating performance or to net cash provided by operating activities as a measure of its liquidity. Additionally, the EBITDA, as adjusted, computation used herein may not be comparable to other similarly titled measures of other companies. EBITDA, as adjusted, represents a measure upon which management assesses financial performance, and certain covenants in Universal's borrowing arrangements will be tied to similar measures. We believe that EBITDA, as adjusted, is a standard measure of financial performance used for valuing companies in the compression industry. EBITDA, as adjusted, is a useful yardstick as it measures the capacity of

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

companies to generate cash without reference to how they are capitalized, how they account for significant non-cash charges for depreciation and amortization associated with assets used in the business (the majority of which are long-lived assets in the compression industry), or what their tax attributes may be.

Non-recurring Charges. During the three months ended June 30, 2000, we incurred non-recurring charges of \$7.1 million related to the early termination of a management agreement and a consulting agreement and other related fees in connection with Holdings' initial public offering and concurrent financing transactions.

Depreciation and Amortization. Depreciation and amortization increased by \$3.9 million to \$11.4 million during the three months ended June 30, 2001, compared to \$7.5 million during the three months ended June 30, 2000. The increase resulted primarily from the expansion of Universal's rental fleet offset partially by the compressor equipment sold and leased back under Universal's operating lease facility. Included in depreciation and amortization for the three months ended June 30, 2000 is \$675 thousand of amortization expense. As of April 1, 2001, the Company has adopted SFAS 142 which, among other things, eliminated amortization of goodwill.

Operating Lease. Operating lease expense increased by \$11.9 million to \$12.6 million during the three months ended June 30, 2001 from \$689 thousand during the three months ended June 30, 2000. The increase is due to the expense associated with an increased balance on the operating lease facilities entered into concurrently with the Weatherford Global merger. The outstanding balance under the operating lease facilities at June 30, 2001 was \$567.5 million, consisting of \$427.0 million under Universal's new operating lease facility and \$140.5 million under Universal's asset-backed securitization operating lease facility.

Interest Expense. Interest expense decreased \$1.9 million to \$5.5 million for the three months ended June 30, 2001 from \$7.4 million for the three months ended June 30, 2000 primarily as a result of the reduction of debt resulting from Universal's initial public offering and financing restructurings. The decrease in interest expense was offset partially by increased accretion of Universal's 9 7/8% senior discount notes and the assumption and refinancing of debt related to Universal's GCSI acquisition.

Extraordinary Loss. During the three months ended June 30, 2000, we incurred extraordinary losses of \$5.4 million (\$3.4 million net of income tax) related to debt restructurings that occurred concurrently with Holdings' initial public offering.

Net Income (Loss). We had net income of \$10.5 million for the three months ended June 30, 2001 compared to a net loss of \$7.7 million for the three months ended June 30, 2000. The change was primarily related to extraordinary and non-recurring charges incurred during the three months ended June 30, 2000 as well as increase in Universal's gross margins and decrease in interest expense, offset partially by increased depreciation and amortization related to the continued expansion of Universal's fleet, leasing expense resulting from Universal's operating lease facilities, selling, general and administrative expense resulting from Universal's increased headcount due to growth and income tax expense resulting from Universal's positive operating income.

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to some market risk due to the floating or variable interest rates under our financing arrangements. A portion of the interest and lease payments under our financing arrangements are based on a floating rate (a base rate or LIBOR, at our option, in the case of our revolving credit facility, and LIBOR, in the case of our operating lease facilities) plus a variable amount based on our operating results. The one-month LIBOR rate at June 30, 2001 was 3.835%. A 1.0% increase in interest rates would result in a \$0.8 million annual increase in our interest and operating lease expense. As of June 30, 2001, approximately \$83 million of our indebtedness and other obligations outstanding bear interest at floating rates.

In order to minimize any significant foreign currency credit risk, we generally contractually require that payment by our customers be made in U.S. dollars. If payment is not made in U.S. dollars, we generally utilize the exchange rate into U.S. dollars on the payment date or balance payments in local currency against local expenses.

PART II. OTHER INFORMATION

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits.

The following documents have been included as Exhibits to this report:

Exhibit -----	Description -----
10.1	Registration Rights Agreement dated July 11, 2001 by and among Universal Compression Holdings, Inc. and the former shareholders of KCI, Inc., (incorporated by reference to Exhibit 10.1 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K dated July 23, 2001).
10.2	Registration Rights Agreement dated July 11, 2001 by and among Universal Compression Holdings, Inc., MCNIC Compression GP, Inc. and MCNIC Compression LP, Inc. (incorporated by reference to Exhibit 10.2 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K dated July 23, 2001).

* Filed herewith

(b) Reports on Form 8-K.

Two reports were filed on Form 8-K during the first quarter of fiscal 2002:

- The Company and Universal filed a Current Report on Form 8-K on May 21, 2001 to report under Item 5 among other things, the filing of a Registration Statement on Form S-4 with respect to the exchange offer of \$350,000,000 principal amount of registered 8% senior secured notes of BRL Universal Equipment 2001 A, L.P., the lessor under our senior secured notes operating lease facility, and its subsidiary, for like principal amount of outstanding unregistered 8% senior secured notes that were issued in a private placement transaction pursuant to Rule

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

144A under the Securities Act of 1933, as amended.

- The Company and Universal filed a Current Report on Form 8-K on June 5, 2001 to report under Item 5 among other things, (i) the settlement of the Company's claims against Tidewater, Inc. relating to the Company's 1998 acquisition of Tidewater Compression Service Inc. in exchange for payment to the Company of \$1 million and termination of the Purchase Price Adjustment Agreement dated as of February 20, 1998, (ii) the Company's entering into an agreement to acquire KCI, Inc. and (iii) the filing of a Registration Statement on Form S-3 with respect to the Offering.

In addition, the Company and Universal filed a Current Report on Form 8-K on July 23, 2001 to report under Item 5 among other things, (i) the completion of the Offering, (ii) the right of holders of Universal's 9% senior discount notes to require Universal to repurchase those notes as a result of Castle Harlan's reduced ownership of the Company's common stock following the Offering, (iii) completion of the acquisition of KCI and (iv) completion of the acquisition of LCM.

24

25

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrants have duly caused this report to be signed on their behalf by the undersigned, thereunto duly authorized.

UNIVERSAL COMPRESSION HOLDINGS, INC.

Date: August 10, 2001

By: /s/ RICHARD W. FITZGERALD

Richard W. FitzGerald,
Senior Vice President and
Chief Financial Officer

UNIVERSAL COMPRESSION, INC.

By: /s/ RICHARD W. FITZGERALD

Richard W. FitzGerald,
Senior Vice President and
Chief Financial Officer

25

26

INDEX TO EXHIBITS

Exhibit	Description
-----	-----

10.1	Registration Rights Agreement dated July 11, 2001 by and among Universal
------	--

Edgar Filing: UNIVERSAL COMPRESSION HOLDINGS INC - Form 10-Q

Compression Holdings, Inc. and the former shareholders of KCI, Inc., (incorporated by reference to Exhibit 10.1 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K dated July 23, 2001).

- 10.2 Registration Rights Agreement dated July 11, 2001 by and among Universal Compression Holdings, Inc., MCNIC Compression GP, Inc. and MCNIC Compression LP, Inc. (incorporated by reference to Exhibit 10.2 of Universal Compression Holdings Inc.'s Current Report on Form 8-K dated July 23, 2001).

* Filed herewith