Rule 424(b)(5)
Reg. No. 333-2680

PROSPECTUS SUPPLEMENT
(TO PROSPECTUS DATED APRIL 12, 1996)

7,523,140 SHARES
[DIAMOND OFFSHORE LOGO] DIAMOND OFFSHORE DRILLING, INC.
COMMON STOCK

All of the shares of common stock, par value $0.01 per share ("Diamond Offshore Common Stock"), of Diamond Offshore Drilling, Inc., a Delaware corporation ("Diamond Offshore"), offered hereby (the "Offered Shares") will be sold by Alphee S.A., a Luxembourg corporation ("Alphee"), and Forvaltnings AB Ratos, a Swedish corporation ("Ratos" and, together with Alphee, the "Selling Stockholders"). See "Selling Stockholders." Diamond Offshore will not receive any of the proceeds from the sale of the Offered Shares.

Of the 7,523,140 Offered Shares, 6,018,140 Offered Shares are being offered initially in the United States and Canada (the "U.S. Offering") by the U.S. Underwriters (as defined herein) and 1,505,000 Offered Shares are being offered outside the United States and Canada (the "International Offering" and, together with the U.S. Offering, the "Offerings") by the International Managers (as defined herein). The public offering price and the aggregate underwriting discount per share will be identical for both Offerings. See "Underwriting."

Pursuant to the Plan of Acquisition dated as of February 9, 1996, as amended (as so amended, the "Plan of Acquisition"), among Diamond Offshore, Diamond Offshore (USA) Inc., a Delaware corporation ("Diamond Offshore (USA)"), AO Acquisition Limited, a Bermuda company ("Acquisition Sub"), and Arethusa (Off-Shore) Limited, a Bermuda company ("Arethusa"), and the Amalgamation Agreement dated as of February 9, 1996 (the "Amalgamation Agreement") between Arethusa and Acquisition Sub, Diamond Offshore acquired Arethusa (the "Acquisition") on the terms set forth in the Plan of Acquisition and Amalgamation Agreement. The Acquisition was consummated on April 29, 1996 (the "Effective Time"). Arethusa shareholders received 17,893,344 shares of Diamond Offshore Common Stock, representing approximately 26.4% of the total Diamond Offshore Common Stock currently outstanding, of which the Selling Stockholders received an aggregate of 8,375,455 shares.

Diamond Offshore Common Stock is listed on the New York Stock Exchange (the "NYSE") under the symbol "DO." On May 20, 1996, the closing price of the Diamond Offshore Common Stock on the NYSE was $49 3/8 per share.

FOR A DISCUSSION OF CERTAIN FACTORS THAT SHOULD BE CONSIDERED IN CONNECTION WITH AN INVESTMENT IN THE OFFERED SHARES, SEE "RISK FACTORS" BEGINNING ON PAGE 6 OF THE ACCOMPANYING PROSPECTUS.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS SUPPLEMENT OR THE ACCOMPANYING PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

	PRICE TO PUBLIC	UNDERWRITING DISCOUNT(1)	PROCEEDS TO SELLING STOCKHOLDERS(2)
Per Share..................................	$49.25	$1.48	$47.77
Total(3)....................................	$370,514,645	$11,134,247	$359,380,398

(1) Diamond Offshore, Loews Corporation and the Selling Stockholders have agreed to indemnify the several Underwriters (as defined herein) against certain liabilities, including certain liabilities under the Securities Act of 1933, as amended. See "Underwriting."

(2) Diamond Offshore has agreed to pay certain expenses of the Offerings estimated at $500,000. The Selling Stockholders have agreed to pay certain other expenses of the Offerings estimated at $167,500. The Underwriters have agreed to pay certain expenses of the Selling Stockholders estimated at $100,000.

(3) The Selling Stockholders have granted the U.S. Underwriters and the International Managers options, exercisable within 30 days after the date of this Prospectus Supplement, to purchase up to 601,814 and 150,501 additional shares of Diamond Offshore Common Stock, respectively, solely to cover over-allotments, if any. If such options are exercised in full, the total Price to Public, Underwriting Discount and Proceeds to Selling Stockholders will be $407,566,159, $12,247,674 and $395,318,485, respectively. See "Underwriting."

The Offered Shares are offered by the several Underwriters, subject to prior sale, when, as and if issued and accepted by them, subject to approval of certain legal matters by counsel for the Underwriters and certain other conditions. The Underwriters reserve the right to withdraw, cancel or modify such offer and to reject orders in whole or in part. It is expected that delivery of the Offered Shares will be made in New York, New York on or about May 24, 1996.

MERRILL LYNCH & CO.

CS FIRST BOSTON

SALOMON BROTHERS INC

The date of this Prospectus Supplement is May 20, 1996.

IN CONNECTION WITH THESE OFFERINGS, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF DIAMOND OFFSHORE COMMON STOCK AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH TRANSACTIONS MAY BE EFFECTED ON THE NYSE OR OTHERWISE. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

DURING THESE OFFERINGS, CERTAIN PERSONS AFFILIATED WITH PERSONS PARTICIPATING IN THE DISTRIBUTION MAY ENGAGE IN TRANSACTIONS FOR THEIR OWN ACCOUNTS OR FOR THE ACCOUNTS OF OTHERS IN THE DIAMOND OFFSHORE COMMON STOCK PURSUANT TO EXEMPTIONS FROM RULES 10B-6, 10B-7, AND 10B-8 UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

DIAMOND OFFSHORE DRILLING, INC.

Diamond Offshore engages principally in the contract drilling of offshore oil and gas wells. Diamond Offshore's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Asia and, including those rigs acquired as a result of the Acquisition, consists of 30 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 19 jack-up rigs owned and/or operated by Diamond Offshore and one drillship. Diamond Offshore also operates 10 land rigs deployed in South Texas. Except for two jack-up rigs operated pursuant to bareboat charter contracts, all of Diamond Offshore's offshore and land rigs are wholly owned.

On April 29, 1996, Diamond Offshore consummated the Acquisition, thereby adding to its fleet Arethusa's 13 owned and/or operated mobile offshore drilling rigs. Arethusa provided drilling services worldwide to international and government-controlled oil and gas companies. Arethusa's eight semisubmersible rigs now owned by Diamond Offshore are located in the Gulf of Mexico and offshore Brazil and Arethusa's five jack-up rigs now owned by Diamond Offshore are located offshore India, Indonesia and Egypt, in the Gulf of Mexico and in the Dutch sector of the North Sea.

Diamond Offshore Common Stock is listed on the NYSE under the symbol "DO." For the period from April 12 through May 20, 1996, the high and low closing prices of Diamond Offshore Common Stock as reported by the NYSE were $52 5/8 and $44 1/4 per share, respectively. For the high and low closing prices for earlier periods, see "Management -- Price Range of Diamond Offshore Common Stock" in the accompanying Prospectus.

USE OF PROCEEDS

Diamond Offshore will not receive any of the proceeds from the sale of the Offered Shares by the Selling Stockholders.

SELLING STOCKHOLDERS

All of the Offered Shares being offered hereby are being offered by Alphee and Ratos. The following table sets forth information, as of the date of this Prospectus Supplement, relating to beneficial ownership (as defined in Rule 13d-3 of the Securities Exchange Act of 1934, as amended) of Diamond Offshore Common Stock by each Selling Stockholder.

NAME OF SELLING STOCKHOLDER	BENEFICIAL OWNERSHIP OF DIAMOND OFFSHORE COMMON STOCK PRIOR TO THE OFFERINGS		NUMBER OF SHARES OF DIAMOND OFFSHORE COMMON STOCK TO BE SOLD(1)	BENEFICIAL OWNERSHIP OF DIAMOND OFFSHORE COMMON STOCK AFTER THE OFFERINGS(1)	
	NUMBER	PERCENT	NUMBER	NUMBER	PERCENT
Alphee S.A......................... 11, Avenue de la Gare 1611 Luxembourg	4,708,248	6.9%	4,234,771	473,477	0.7%
Forvaltnings AB Ratos............. Drottninggatan 2 Stockholm, Sweden	3,667,207	5.4%	3,288,369	378,838	0.6%

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(1) In addition to the shares of Diamond Offshore Common Stock indicated, the Selling Stockholders have granted the U.S. Underwriters and the International Managers options, exercisable within 30 days after the date of this Prospectus Supplement, to purchase up to 601,814 and 150,501 additional shares of Diamond Offshore Common Stock, respectively, solely to cover over-allotments, if any. If such options are exercised in full, (a) the number of shares of Diamond Offshore Common Stock to be sold by Alphee and Ratos will be 4,658,248 and 3,617,207, respectively, and (b) beneficial ownership of Diamond Offshore Common Stock after the Offerings by Alphee and Ratos will be 50,000 (.07%) and 50,000 (.07%), respectively.

See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and the Selling Stockholders," "-- Registration Rights of Selling Stockholders" and "Plan of Distribution" in the accompanying Prospectus for additional information with respect to the Selling Stockholders.

CAPITALIZATION

The following table sets forth the capitalization of Diamond Offshore as of March 31, 1996 and as adjusted as of such date after giving effect to the Acquisition. This table should be read in conjunction with the Consolidated Financial Statements (including the Notes thereto) and the Unaudited Pro Forma Consolidated Condensed Financial Statements included elsewhere in this Prospectus Supplement.

	MARCH 31, 1996 (UNAUDITED)	
	HISTORICAL	AS ADJUSTED
	(IN THOUSANDS)	
Total debt	$ 15,000	$ 82,477
Stockholders' equity:		
Common stock, $.01 par value	500	679
Additional paid-in capital	665,107	1,215,605
Accumulated deficit	(152,712)	(152,712)
Cumulative translation adjustment	(1,263)	(1,263)
Total stockholders' equity	511,632	1,062,309
Total capitalization	$ 526,632	$ 1,144,786

SELECTED CONSOLIDATED FINANCIAL DATA

The following tables set forth selected consolidated historical and pro forma financial data for Diamond Offshore. The selected consolidated financial data were derived from the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore included in this Prospectus Supplement and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore included in this Prospectus Supplement. The results of operations for the three months ended March 31, 1996 are not necessarily indicative of results to be anticipated for the entire year.

	PRO FORMA THREE MONTHS ENDED MARCH 31, 1996	THREE MONTHS ENDED MARCH 31, 1996	THREE MONTHS ENDED MARCH 31, 1995
	(IN THOUSANDS, EXCEPT PER SHARE DATA)		
INCOME STATEMENT DATA:			
Total revenues	$147,662	$106,868	$ 70,760
Operating expenses:			
Contract drilling	86,454	66,157	61,751
General and administrative	5,552	3,103	3,140
Depreciation(1)	20,018	12,069	14,988
Gain on sale of assets	(157)	(157)	(389)
Operating income (loss)	35,795	25,696	(8,730)
Interest expense	(1,291)	--	(8,486)
Other income (expense), net	484	434	355
Income tax benefit (expense)	(7,861)	(7,398)	5,289
Net income (loss)	27,127	18,732	(11,572)
Net income per share	.40	0.37	--

	PRO FORMA MARCH 31, 1996	MARCH 31, 1996
	(IN THOUSANDS)	
BALANCE SHEET DATA:		
Working capital	$ 109,185	$ 70,480
Drilling and other property and equipment, net	1,083,485	533,645
Goodwill and other assets	28,956	3,984
Total assets	1,295,738	658,185
Long-term debt	71,874	15,000
Stockholders' equity	1,062,309	511,632

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(1) Effective January 1, 1996, Diamond Offshore revised the estimated useful lives for certain classes of its offshore drilling rigs. The estimated useful lives of Diamond Offshore's offshore drilling rigs, after the change in estimate, range from 10 to 25 years. The effect of such change reduced depreciation expense and increased net income for the three months ended March 31, 1996 by approximately $2.1 million and $1.5 million ($0.03 per share), respectively.

UNAUDITED PRO FORMA CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

The unaudited pro forma consolidated condensed financial statements as of and for the three months ended March 31, 1996 have been prepared based on the historical financial statements of Diamond Offshore and Arethusa as of and for the three months ended March 31, 1996. Such historical financial statements are unaudited but, in the opinion of management, include all adjustments necessary, consisting only of normal recurring accruals. The unaudited pro forma consolidated condensed income statement for the year ended December 31, 1995 has been prepared based on the historical financial statements of Diamond Offshore as of and for the year ended December 31, 1995 and based on pro forma income statement data for Arethusa that reflect adjustments to Arethusa's historical consolidated income statement for the year ended September 30, 1995 in connection with (i) the acquisition of the Arethusa Yatzy, (ii) the sale of the Treasure Stawinner and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of common stock, par value $0.10 per share, of Arethusa ("Arethusa Common Stock")) as if each had occurred at the beginning of fiscal year 1995. The pro forma income statement for the three months ended March 31, 1996 gives effect to the Acquisition. The pro forma income statement for the year ended December 31, 1995 gives effect to (i) the Acquisition, (ii) the initial public offering of Diamond Offshore Common Stock in October 1995 (the "Diamond Offshore Initial Public Offering") and, in connection therewith, the use of the proceeds to repay all of Diamond Offshore's then outstanding indebtedness to Loews Corporation, a Delaware corporation ("Loews"), and to fund the payment of a special dividend to Loews and (iii) interest expense for working capital borrowings, and commitment and other fees, under Diamond Offshore's $150.0 million credit facility with a group of banks (the "Diamond Offshore Bank Credit Facility"). The Acquisition was accounted for under the purchase method of accounting using a purchase price of $560.7 million, which was calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced. The pro forma consolidated condensed balance sheet was prepared assuming such transactions were consummated on March 31, 1996 and give effect to events directly attributable to the transactions, including those that are nonrecurring. The pro forma consolidated condensed income statement was prepared assuming the transactions were consummated as of the beginning of the period presented and give effect to events directly attributable to the transactions which are expected to have a continuing impact on the combined entity. These pro forma consolidated condensed financial statements should be read in conjunction with the other financial information of Diamond Offshore and Arethusa presented elsewhere in this Prospectus Supplement and the accompanying Prospectus. The pro forma consolidated condensed financial statements are presented for illustrative purposes only and are not necessarily indicative of actual results that would have been achieved had the transactions been consummated on such dates, and are not necessarily indicative of future results. The allocation of the purchase price is preliminary, as valuation and other studies have not been finalized. It is not expected that the final allocation of the purchase price will produce materially different results from those presented herein.

PRO FORMA CONSOLIDATED CONDENSED BALANCE SHEET
MARCH 31, 1996

	HISTORICAL(A)			
	DIAMOND OFFSHORE	ARETHUSA	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS)			
Cash and other current assets	$ 32,932	$ 49,722	$ (16,549)(b)	$ 66,105
Accounts receivable	87,624	29,568	--	117,192
Drilling and other property and equipment, net	533,645	230,853	318,987(c)	1,083,485
Goodwill and other assets	3,984	2,071	22,901(d)	28,956
Total assets	$ 658,185	$ 312,214	$ 325,339	$1,295,738
Current liabilities	$ 50,076	$ 20,536	$ 3,500(e)	$ 74,112
Long-term debt	15,000	56,874	--	71,874
Deferred credits and other liabilities	81,477	1,884	4,082(f)	87,443
Common stock	500	2,033	(1,854)(g)	679
Additional paid-in capital	665,107	218,800	331,698(g)	1,215,605
Accumulated earnings (deficit)	(152,712)	12,087	(12,087)	(152,712)
Cumulative translation adjustment	(1,263)	--	--	(1,263)
Total liabilities and stockholders' equity	$ 658,185	$ 312,214	$ 325,339	$1,295,738

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(a) There are no significant adjustments required to the historical financial statements of Diamond Offshore or Arethusa to conform accounting policies of the two companies.

(b) Adjustment for fair values of identifiable current assets acquired and for certain events directly attributable to the transaction. Such items include:

Severance, consulting, and salary continuation plans	$ (5,526)(1)
Financial advisory services	(7,500)(2)
Legal, accounting, and other	(2,500)(3)
Office lease cancellation	(1,023)(4)
	$(16,549)

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(1) Under the Plan of Acquisition, from and after the Effective Time, Diamond Offshore and Arethusa and their respective subsidiaries will honor in accordance with their terms certain Arethusa employment, severance, consulting and salary continuation plans.

(2) Arethusa has agreed to pay Merrill Lynch, Pierce, Fenner & Smith Incorporated a fee of $7.5 million for financial advisory services in connection with the Acquisition upon the closing of the Acquisition.

(3) Adjustment for legal, accounting, printing and other nonrecurring charges expected to be incurred in connection with the Acquisition.

(4) Arethusa is committed under a lease agreement for office space that continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1.0 million. Such payment has no future economic benefit to the combined company and is incremental to other costs incurred by either Arethusa or Diamond Offshore in the conduct of activities prior to the Effective Time.

(c) Adjustment for fair values, based on current appraisals, of the eight semisubmersible drilling rigs, three jack-up drilling rigs, and other property and equipment owned by Arethusa.

(d) Adjustment for fair values of identifiable assets and for the excess of the cost of Arethusa over the sum of the amounts assigned to identifiable assets acquired less liabilities assumed.

(e) Adjustment for the estimated unfunded termination liability related to the Arethusa defined benefit plan.

(f) Adjustment for fair values of liabilities assumed and for the deferred tax liability for estimated future tax effects of differences between the tax bases and the fair value amounts assigned to identifiable assets and liabilities of Arethusa, offset by net operating loss carryforwards of Arethusa of approximately $30.0 million. As a result of the Acquisition, Diamond Offshore will have available to it certain Arethusa net operating loss carryforwards to reduce future U.S. federal income taxes payable. Due to the change in ownership of Arethusa resulting from the Acquisition, there will be annual limitations on the amount of Arethusa tax carryforwards available to be utilized by Diamond Offshore.

(g) The pro forma financial statements reflect the purchase of 100% of the outstanding shares of Arethusa Common Stock for a total consideration of $560.7 million which is comprised of the following:

Diamond Offshore Common Stock to be issued	$539,296(1)
Options assumed	11,381(2)
Total equity consideration	550,677
Transaction costs	10,000(3)
Total consideration	$560,677

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(1) The value of the Diamond Offshore Common Stock to be issued in the Acquisition is calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995) of $30.14.

(2) Amount represents the fair value of the Arethusa Options assumed by Diamond Offshore pursuant to the Amalgamation Agreement. The fair value is based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995), the Amalgamation Ratio (as defined herein) and the option exercise price including the $3.00 reduction, which was approved by Arethusa shareholders at Arethusa's annual general meeting of shareholders on April 29, 1996.

(3) Amounts represent transaction costs directly associated with the Acquisition. See (b) above.

PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT
THREE MONTHS ENDED MARCH 31, 1996

	HISTORICAL			
	DIAMOND OFFSHORE	ARETHUSA	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)			
Revenues	$106,868	$ 40,794	$ --	$ 147,662
Operating expenses:				
Contract drilling	66,157	20,297	--	86,454
General and administrative	3,103	2,449	--	5,552
Depreciation and amortization	12,069	8,277	(328) (a)	20,018
Gain on sale of assets	(157)	--	--	(157)
Total operating expenses	81,172	31,023	(328)	111,867
Operating income (loss)	25,696	9,771	328	35,795
Other income (expense):				
Interest expense	--	(1,291)	--	(1,291)
Other, net	434	50	--	484
Income (loss) before income tax (expense) benefit	26,130	8,530	328	34,988
Income tax (expense) benefit	(7,398)	(348)	(115) (b)	(7,861)
Net income	$ 18,732	$ 8,182	$ 213	$ 27,127
Net income per common share	$ 0.37	$ 0.40		$ 0.40
Weighted average common shares outstanding	50,000	20,333		67,893(c)

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(a) To record the adjustment to depreciation expense and amortization of goodwill resulting from the allocation of the purchase price. The pro forma adjustment assumes an 18-year average estimated useful life for depreciation and a 20-year amortization period for goodwill.

(b) To record income tax expense on the effect of the pro forma adjustments to depreciation and amortization.

(c) Weighted average shares outstanding as if the issuance of 17.9 million shares to be issued by Diamond Offshore in consideration of the Arethusa Common Stock had taken place on January 1, 1996.

PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT
YEAR ENDED DECEMBER 31, 1995

	HISTORICAL DIAMOND OFFSHORE	PRO FORMA ARETHUSA(A)	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
Revenues	$336,584	$ 120,166	$ --	$ 456,750
Operating expenses:				
Contract drilling	259,560	86,532	--	346,092
General and administrative	13,857	9,033	--	22,890
Depreciation and amortization	52,865	29,008	3,897(b)	85,770
Gain on sale of assets	(1,349)	--	--	(1,349)
Total operating expenses	324,933	124,573	3,897	453,403
Operating income (loss)	11,651	(4,407)	(3,897)	3,347
Other income (expense):				
Interest expense	(27,052)	(6,697)	26,296(c)	(7,453)
Other, net	1,598	4,048	--	5,646
Income (loss) before income tax benefit (expense)	(13,803)	(7,056)	22,399	1,540
Income tax benefit (expense)	6,777	(1,440)	(7,840)(d)	(2,503)
Net income (loss)	$ (7,026)	$ (8,496)	$ 14,559	$ (963)
Net income per common share	$ 0.20(f)	$ (0.42)		$ (0.01)
Weighted average common shares outstanding	50,000(f)	20,333		67,893(e)

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(a) Pro forma income statement data for Arethusa reflect (i) the acquisition of the Arethusa Yatzy, which occurred on May 3, 1995, (ii) the sale of the Treasure Stawinner, which occurred June 30, 1995, and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of Arethusa Common Stock) as if each had occurred at the beginning of fiscal year 1995. Set forth below in this footnote (a) are the historical amounts, and the adjustments thereto, upon which the pro forma Arethusa amounts are based.

ARETHUSA PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT
YEAR ENDED SEPTEMBER 30, 1995

	HISTORICAL		ADJUSTMENTS			
	ARETHUSA	YATZY(1)	YATZY ACQUISITION	STAWINNER SALE	DIVIDEND/ CAPITAL DISTRIBUTION	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)					
Contract drilling revenue	$122,147	$12,315	$ --	$(14,296)(6)	$ --	$120,166
Operating expenses:						
Direct costs	87,953	8,060	(623)(5) (375)(2)	(8,483)(6)	--	86,532
General and administrative	8,658	--	375(2)	--	--	9,033
Depreciation	29,547	--	1,352(3)	(1,891)(6)	--	29,008
Total operating expenses	126,158	8,060	729	(10,374)	--	124,573
Operating income (loss)	(4,011)	4,255	(729)	(3,922)	--	(4,407)
Other income (expense):						
Interest expense	(6,311)	--	(1,168)(4)	782(6)	--	(6,697)
Interest income	5,692	--	--		(1,453)(7)	4,239
Gain (loss) on sale of assets	27,820	--	--	(27,885)(6)	--	(65)
Other, net	(126)	--	--	--	--	(126)
Income (loss) before income taxes	23,064	4,255	(1,897)	(31,025)	(1,453)	(7,056)
Tax provision	(1,440)	--	--	--	--	(1,440)
Net income (loss)	$ 21,624	$ 4,255	$(1,897)	$(31,025)	$(1,453)	$ (8,496)
Net income (loss) per common share	$ 1.06					$ (0.42)
Weighted average common shares outstanding	20,333					20,333

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(1) The historical financial information of the Yatzy operations for the period from October 1, 1994, through May 2, 1995 is based upon Arethusa records, as manager of the rig. The previous owner of the rig prepared financial information only on a semi-annual, calendar year basis; and was unable to provide the complete financial information for the twelve months ended September 30, 1995. Financial statement captions for which Yatzy historical information is not presented (historical depreciation and interest expense) would have been adjusted to reflect Arethusa's cost basis in the Arethusa Yatzy and Arethusa's financing of the rig. Pro forma Yatzy acquisition adjustments (3) and (4) discussed below provide fully for depreciation using Arethusa's cost basis in the Arethusa Yatzy and interest based on Arethusa's financing of the rig. Additionally, it is management's understanding that there are no other significant transactions or activities related to the historical operations of Yatzy which would have a material impact on the as-adjusted pro forma income statement. Therefore, management believes the resulting pro forma income statement is in compliance with Article 11 of Regulation S-X.

(2) To reclassify and eliminate the management fee paid to Arethusa from direct costs to general and administrative expenses.

(3) To reflect depreciation expense calculated based upon Arethusa's cost and estimated useful life of 25 years, which is consistent with Arethusa's previously established depreciation policy.

(4) To adjust for additional interest expense associated with Arethusa's $30.0 million note entered into in connection with the acquisition of the Arethusa Yatzy.

(5) To adjust for a reduction in insurance expense resulting from Arethusa's lower insured value for the Arethusa Yatzy.

(6) To reflect the elimination of historical operations, interest expense and gain on sale of assets for the Treasure Stawinner.

(7) To reflect the reduction in interest income resulting from the dividend and capital distribution made to shareholders in fiscal 1995.

(b) To record the additional depreciation expense and amortization of goodwill resulting from the allocation of the purchase price. The pro forma adjustment assumes an 18-year average estimated useful life for depreciation and a 20-year amortization period for goodwill.

(c) To adjust interest expense, assuming that the Diamond Offshore Initial Public Offering and repayment of indebtedness occurred on January 1, 1995.

(d) To record income tax expense on the effect of the pro forma adjustments to depreciation and amortization and interest expense.

(e) Weighted average shares outstanding as if both the October 1995 issuance of 15.0 million shares by Diamond Offshore through the Diamond Offshore Initial Public Offering and the 17.9 million shares to be issued by Diamond Offshore in consideration of the Arethusa Common Stock had taken place on January 1, 1995.

(f) After the Diamond Offshore Initial Public Offering, Diamond Offshore had 50.0 million shares of Diamond Offshore Common Stock outstanding. Assuming the Diamond Offshore Initial Public Offering had occurred at January 1, 1995, Diamond Offshore would have recognized net income of $10.0 million, or $0.20 per share of Diamond Offshore Common Stock, after adjusting for the after-tax effects of a reduction in interest expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with Diamond Offshore's Consolidated Financial Statements (including the Notes thereto) included elsewhere in this Prospectus Supplement.

RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 1996 AND 1995

Comparative data relating to Diamond Offshore's revenues and operating expenses by equipment type are listed below (eliminations offset dayrate revenues earned when Diamond Offshore's rigs are utilized in its turnkey operations). Diamond Offshore's drillship, Ocean Clipper I, is included in Other Semisubmersibles for discussion purposes.

	THREE MONTHS ENDED MARCH 31, 1996	THREE MONTHS ENDED MARCH 31, 1995	INCREASE/ (DECREASE)
	(IN THOUSANDS)		
REVENUES			
Fourth-Generation Semisubmersibles	$ 21,465	$ 11,703	$ 9,762
Other Semisubmersibles	52,995	35,511	17,484
Jack-ups	20,136	16,926	3,210
Turnkey	13,626	3,143	10,483
Land	5,102	5,475	(373)
Other	--	--	--
Eliminations	(6,456)	(1,998)	(4,458)
Total Revenues	$106,868	$ 70,760	$ 36,108
CONTRACT DRILLING EXPENSE			
Fourth-Generation Semisubmersibles	$ 7,898	$ 8,294	$ (396)
Other Semisubmersibles	31,490	30,774	716
Jack-ups	14,927	15,506	(579)
Turnkey	14,128	4,598	9,530
Land	4,772	4,709	63
Other	(602)	(132)	(470)
Eliminations	(6,456)	(1,998)	(4,458)
Total Contract Drilling Expense	$ 66,157	$ 61,751	$ 4,406
OPERATING INCOME (LOSS)			
Fourth-Generation Semisubmersibles	$ 13,567	$ 3,409	$ 10,158
Other Semisubmersibles	21,505	4,737	16,768
Jack-ups	5,209	1,420	3,789
Turnkey	(502)	(1,455)	953
Land	330	766	(436)
Other	602	132	470
General and Administrative Expense	(3,103)	(3,140)	37
Depreciation Expense	(12,069)	(14,988)	2,919
Gain on Sale of Assets	157	389	(232)
Total Operating Income (Loss)	$ 25,696	$ (8,730)	$ 34,426

REVENUES. The $9.8 million increase in revenues from fourth-generation semisubmersibles resulted from improvements in dayrates ($6.3 million) and increases in utilization ($3.5 million). The improvement in utilization for 1996 was partially attributable to the relocation between markets of two fourth-generation rigs during the comparable period of the prior year, reducing the days worked for these rigs during that period. The $17.5 million increase in revenues from other semisubmersibles was primarily attributable to increases in dayrates in both the North Sea and the Gulf of Mexico. These increases were partially offset by a reduction in revenues of approximately $4.8 million due to the Ocean Princess and the Ocean Baroness being out of service while modifications were being performed prior to these rigs beginning term contracts in the North Sea and South America, respectively. The $3.2 million increase in revenues from jack-ups resulted from increased utilization and dayrates in the Gulf of Mexico. The $10.5 million increase in turnkey revenues resulted from projects of greater magnitude completed during the first quarter of 1996 as compared to those completed during the same period of the prior year. In addition, Diamond Offshore performed overall project management services for two customers during the current year, generating approximately $2.7 million which is included in turnkey revenue for the first quarter of 1996.

CONTRACT DRILLING EXPENSE. Contract drilling expense for fourth-generation semisubmersibles, other semisubmersibles, and jack-ups was relatively unchanged from the first quarter of the prior year. The $9.5 million increase in turnkey expense resulted from more extensive turnkey wells drilled, project management services provided and cost overruns on one turnkey well during the current year.

GENERAL AND ADMINISTRATIVE EXPENSE. General and administrative expense of $3.1 million for the quarter ended March 31, 1996 was unchanged from the comparable period of the prior year.

DEPRECIATION EXPENSE. Depreciation expense of $12.1 million for the quarter ended March 31, 1996 included a change in accounting estimate to increase the estimated useful lives for certain classes of rigs which reduced depreciation expense by approximately $2.1 million, as compared to the quarter ended March 31, 1995. Partially offsetting this decrease were increases in depreciation for three rig upgrades performed in 1995 and capital expenditures associated with Diamond Offshore's continuing rig enhancement program. In addition, depreciation expense for the comparable period of the prior year included a $2.1 million write-down in the carrying value of a semisubmersible.

INTEREST EXPENSE. Diamond Offshore incurred $0.2 million of interest expense for the quarter ended March 31, 1996 as compared to $8.5 million for the same period of the prior year. This decrease was attributable to a reduction in the outstanding indebtedness resulting from the repayment of Diamond Offshore's loan from Loews in connection with the Diamond Offshore Initial Public Offering in October 1995. The $0.2 million of interest expense for 1996 has been capitalized to the cost of construction on the Ocean Quest and Ocean Star. See Notes 3 and 5 to Diamond Offshore's Consolidated Financial Statements included in this Prospectus Supplement.

INCOME TAX (EXPENSE) BENEFIT. The income tax (expense) benefit for the quarter ended March 31, 1996 was $(7.4) million as compared to $5.3 million for the comparable period of the prior year. This change resulted primarily from the increase of $43.0 million in Diamond Offshore's income before income tax (expense) benefit.

NET INCOME (LOSS). Net income for the quarter ended March 31, 1996 increased $30.3 million to $18.7 million, as compared to a net loss of $(11.6) million for the comparable period of the prior year. The increase resulted primarily from an increase in operating income of $34.4 million and a decrease in interest expense of $8.5 million, partially offset by an increase in income tax expense of $12.7 million.

OUTLOOK

The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances, including 3-D seismic, horizontal drilling, and subsea completion procedures. Both the Gulf of Mexico and the North Sea semisubmersible markets have experienced increased utilization and significantly higher dayrates through the first quarter of 1996. Customers are continuing to contract rigs serving those markets under term contracts (as opposed to contracts let on a single well or well-to-well basis). In the Gulf of Mexico, the Ocean Valiant's contract has been extended through 1996 at an increased dayrate. Contracts for Diamond Offshore's other semisubmersibles in the Gulf of Mexico continue to be primarily on a well-to-well or multi-well basis. However, term contract opportunities are becoming more prevalent. Diamond Offshore's drillship, the Ocean Clipper I, is scheduled to be upgraded during 1996 and 1997 to operate in the ultra-deep water market of the Gulf of Mexico with dynamic positioning capabilities, in connection with a four-year term contract with a major oil company that has been agreed to in principle. The oil company has an option to terminate the contract prior to its scheduled termination date upon payment to Diamond Offshore of a termination fee. See " -- Capital Resources" in this Prospectus Supplement.

In the North Sea, the Ocean Alliance is contracted for work through late 1996 and has received an increase in its dayrate. Diamond Offshore's three other marketed semisubmersibles in the North Sea are all committed under term contracts. The Ocean Nomad, which was relocated from South America, began its two-year contract in late November 1995. The Ocean Princess has completed the modifications necessary for its two-year contract which commenced in late March 1996. The Ocean Guardian is currently drilling pursuant to a one-year term contract expiring during the third quarter of 1996. Of the remaining semisubmersibles in Diamond Offshore's fleet, the Ocean Baroness completed modifications and began, in early April 1996, a three-year term contract for drilling offshore Brazil. In addition, the Ocean Zephyr, also operating offshore Brazil, is contracted to July 1997.

The market for jack-up rigs in the Gulf of Mexico appears to have stabilized and has shown some signs of strengthening in recent months. Dayrates have improved from those earned in early 1995; however, volatile natural gas prices and an oversupply of rigs prevented significant improvements through early 1996.

Historically, the offshore contract drilling market has been highly competitive and cyclical, and Diamond Offshore cannot predict the extent to which current conditions will continue.

LIQUIDITY

Net cash provided by operating activities for the three months ended March 31, 1996 increased by $13.0 million to $23.7 million, as compared to $10.7 million for the comparable period of the prior year. This increase was attributable to a $30.3 million increase in net income for the first quarter of 1996, partially offset by an increase of $13.1 million in accounts receivable, as compared to a decrease in accounts receivable of $4.6 million for the same period of the prior year. Cash used in investing activities increased $36.8 million primarily due to capital expenditures for major upgrades of $32.7 million and $8.2 million for the purchase during the first quarter of 1996 of the land and eight-story building in which Diamond Offshore has its corporate headquarters. Cash provided by financing activities for the three months ended March 31, 1996 increased $19.2 million primarily due to net borrowings of $15.0 million on the Diamond Offshore Bank Credit Facility as compared to $6.0 million net repayments on Diamond Offshore's indebtedness during the same period of the prior year.

Diamond Offshore uses funds available under the Diamond Offshore Bank Credit Facility, together with cash flow from operations, to fund its capital expenditure and working capital requirements. The Diamond Offshore Bank Credit Facility is a revolving line of credit for a five-year term providing a maximum credit commitment of $150.0 million until the second anniversary, at which time and at the end of each six-month period thereafter, the commitment will decrease by $12.5 million to a final maximum credit commitment of $75.0 million during the last six months. Borrowings under the Diamond Offshore Bank Credit Facility bear interest, at Diamond Offshore's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. Diamond Offshore is required to pay a commitment fee of .375% on the unused available portion of the maximum credit commitment. Borrowings are secured by security interests in certain of Diamond Offshore's assets. The Diamond Offshore Bank Credit Facility also contains covenants that limit the amount of total consolidated debt, require the maintenance of certain consolidated financial ratios and limit dividends and similar payments. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity" in the accompanying Prospectus. As of March 31, 1996, Diamond Offshore was in compliance with each of these covenants.

It is anticipated that the Diamond Offshore Bank Credit Facility will be used primarily to fund rig upgrades and similar capital expenditure requirements. In management's opinion, Diamond Offshore's cash generated from operations and borrowings available under the Diamond Offshore Bank Credit Facility are sufficient to meet its anticipated short- and long-term liquidity needs, including its capital expenditure requirements.

CAPITAL RESOURCES

Cash requirements for capital commitments result from rig upgrades to meet specific customer requirements and from Diamond Offshore's continuing rig enhancement program, including top-drive drilling system installations and water depth and drilling capability upgrades. Diamond Offshore expects to spend approximately $198.1 million, including interest expense to be capitalized, during 1996 for rig upgrades in connection with contract requirements. Included in this amount is approximately $55.8 million for 1996 expenditures in conjunction with the planned upgrade of the Ocean Clipper I to operate in deep water with dynamic positioning capabilities. In addition, approximately $124.7 million is included for the upgrades relating to a letter of intent and a contract for the Ocean Star and Ocean Quest, respectively. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Outlook" in the accompanying Prospectus. Because these projects are expected to be accompanied by term contracts at favorable dayrates, the expenditures are, in Diamond Offshore's opinion, financially justified. During the first quarter of 1996, $32.7 million was expended on these projects. Diamond Offshore expects to evaluate other projects as opportunities arise. In addition, Diamond Offshore has budgeted $40.4 million for 1996 capital expenditures associated with its continuing rig enhancement program. During the first quarter of 1996, $2.9 million was expended on this program. It is management's opinion that significant improvements in operating cash flow resulting from current conditions of improved dayrates and the increasing number of term contracts for rigs in certain markets, in conjunction with borrowings under the Diamond Offshore Bank Credit Facility, will be sufficient to meet these capital requirements.

Diamond Offshore is analyzing financing alternatives that may be available to it in the public or private capital markets. Proceeds of any such financing transactions may be used for repayment of higher cost debt, to fund rig upgrades, acquisitions or for other corporate purposes. Diamond Offshore's ability to effect any such financings will be dependent on its historical results of operations and its current financial condition and prospects at the time it seeks access to the capital markets, and to other factors beyond Diamond Offshore's control, including the prevailing interest rate environment and, with respect to offerings of common or preferred stock or debt obligations convertible into such common stock, other financial market conditions, and the investment community's perception of Diamond Offshore and the offshore contract drilling industry generally. Any such offering would be subject to the restrictions imposed by the Shareholders Agreement, dated as of February 9, 1996, as amended (as so amended, the "Shareholders Agreement"), among Diamond Offshore, Diamond Offshore (USA), Acquisition Sub, Alphee and Ratos, on public sales or distributions of Diamond Offshore Common Stock, or securities convertible into common stock, and until October 10, 1996, to obtaining the prior written consent of CS First Boston Corporation ("CS First Boston") as required by the underwriting agreement entered into in connection with the Diamond Offshore Initial Public Offering. See "Underwriting" in this Prospectus Supplement and "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity," "-- Capital Resources" and "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders" in the accompanying Prospectus.

Also, from time to time Diamond Offshore reviews acquisition opportunities, although Diamond Offshore has no current plans to purchase or otherwise acquire additional rigs, other than with respect to the Acquisition. See "-- Other" in this Prospectus Supplement.

OTHER

ACQUISITION OF ARETHUSA. Diamond Offshore consummated the Acquisition on April 29, 1996. Under the Plan of Acquisition and the Amalgamation Agreement, holders of Arethusa Common Stock will receive approximately 17.9 million shares of Diamond Offshore Common Stock to be issued by Diamond Offshore based on a ratio of .88 shares of Diamond Offshore Common Stock for each share of Arethusa common stock (the "Amalgamation Ratio").

SALE OF ASSET. Subsequent to March 31, 1996, Diamond Offshore entered into an agreement to sell its jack-up drilling rig, the Ocean Magallanes, to Cliffs Drilling Company for $4.5 million. The rig is currently stacked in Punta Arenas, Chile. The sale, expected to close during the second quarter of 1996, will generate an after-tax gain of approximately $2.0 million for Diamond Offshore.

CURRENCY RISK. Certain of Diamond Offshore's subsidiaries use the local currency in the country where they conduct operations as their functional currency. Currency environments in which Diamond Offshore has material business operations include the U.K., Australia and Brazil. Diamond Offshore generally attempts to minimize its currency exchange risk by seeking international contracts payable in local currency in amounts equal to Diamond Offshore's estimated operating costs payable in local currency and in U.S. dollars for the balance of the contract. Because of this strategy, Diamond Offshore has minimized its unhedged net asset or liability positions denominated in local currencies and has not experienced significant gains or losses associated with changes in currency exchange rates. However, contracts presently covering three of Diamond Offshore's four rigs operating in the U.K. sector of the North Sea are payable in U.S. dollars. Diamond Offshore has not hedged its exposure to changes in the exchange rate between U.S. dollars and pounds sterling for operating costs payable in pounds sterling, although it may seek to do so in the future.

Currency translation adjustments are accumulated in a separate section of stockholders' equity. However, when Diamond Offshore ceases its operations in a currency environment, the accumulated adjustments are recognized currently in results of operations. Translation gains and losses for Diamond Offshore's operations in Brazil have been recognized currently due to the hyperinflationary status of this environment. The effect on results of operations has not been material and is not expected to have a significant effect in the future due to the recent stabilization of currency rates in Brazil.

ACTIVE MOBILE OFFSHORE DRILLING RIGS

Information as of April 24, 1996 concerning the Diamond Offshore fleet of active mobile offshore drilling rigs is set forth in the table below.

TYPE AND NAME(A)	WATER DEPTH CAPABILITY (FT)	ATTRIBUTES(B)	YEAR BUILT/LATEST ENHANCEMENT(C)	CURRENT LOCATION	CUSTOMER(D)
FOURTH-GENERATION SEMISUBMERSIBLES(3):					
Ocean Alliance........	5,000	TDS; DP; 15K; 3M	1988/1995	North Sea	BP
Ocean America.........	5,000	TDS; SP; 15K; 3M	1988/1992	Gulf of Mexico	BP
Ocean Valiant.........	5,000	TDS; SP; 15K; 3M	1988/1995	Gulf of Mexico	Exxon
OTHER SEMISUBMERSIBLES(27):					
Arethusa Worker.......	3,300	TDS	1982/1992	Gulf of Mexico	Texaco
Ocean Voyager.........	3,200	TDS; VC	1973/1995	Gulf of Mexico	Enserch
Arethusa Yatzy(e).....	3,000	TDS; DP	1989	Brazil	Petrobras
Arethusa Lexington....	2,500	TDS; 3M	1976/1995	Gulf of Mexico	Marathon
Arethusa Neptune......	2,500	TDS; 3M	1977/1995	Gulf of Mexico	Kerr-McGee
Arethusa Concord......	2,200	TDS	1975/1995	Gulf of Mexico	Shell
Arethusa Saratoga.....	2,200	TDS; 3M	1976/1995	Gulf of Mexico	Shell
Arethusa Yorktown.....	2,200	TDS	1976/1989	Brazil	Petrobras
Ocean Endeavor........	2,000	TDS; VC	1975/1994	Gulf of Mexico	Oryx
Ocean Rover...........	2,000	TDS; VC; 15K	1973/1992	Gulf of Mexico	Amerada Hess
Ocean Prospector......	1,700	VC	1971/1981	Gulf of Mexico	Newfield(f)
Arethusa Whittington.........	1,500	TDS; 3M	1974/1995	Gulf of Mexico	Mobil
Ocean Bounty..........	1,500	TDS; VC; 3M	1977/1992	Australia/ Indonesia	BHPP
Ocean Guardian........	1,500	TDS; SP; 3M	1985	North Sea	BP
Ocean New Era.........	1,500	TDS	1974/1990	Gulf of Mexico	Hardy Oil & Gas(g)
Ocean Princess........	1,500	TDS; 15K	1977/1995	North Sea	Marathon
Ocean Epoch...........	1,200	TDS	1977/1990	Australia	BHPP
Ocean General.........	1,200	TDS	1976/1990	Vietnam	Pedco
Ocean Nomad...........	1,200	TDS	1975/1995	North Sea	Shell
Ocean Ambassador(h)...	1,100	TDS	1975/1995	Gulf of Mexico	Committed
Ocean Baroness........	1,100	TDS; VC	1973/1995	Brazil	Petrobras
Ocean Star(i)(j)......	850	VC	1974/1992	Gulf of Mexico	Committed
Ocean Century.........	800		1973	Gulf of Mexico	Stacked
Ocean Quest(k)........	800	VC	1973	Gulf of Mexico	Committed
Ocean Liberator.......	600		1974	Nigeria	Ashland
Ocean Victory.........	600	VC	1972	North Sea	Stacked
Ocean Zephyr..........	600		1972	Brazil	Petrobras
JACK-UPS(19):					
Ocean Titan...........	350	TDS; IS; 15K; 3M	1974/1989	Gulf of Mexico	LL&E
Ocean Tower...........	350	IS; 3M	1972	Gulf of Mexico	Sonat Exploration(l)
Bonito II(m)..........	300	TDS; IC	1983/1995	Gulf of Mexico	Unocal
Miss Kitty(n).........	300	IC	1982	Enroute	ONGC
Ocean King............	300	TDS; IC	1973/1989	Gulf of Mexico	Conoco
Ocean Nugget..........	300	TDS; IC	1976/1995	Gulf of Mexico	Amoco
Ocean Summit..........	300	SDS; IC	1972/1991	Gulf of Mexico	Forcenergy
Ocean Warwick.........	300	TDS; IS; SO	1971/1984	Gulf of Mexico	Stacked
Arethusa Heritage.....	250	TDS; IC	1981/1995	Egypt	EDC
Arethusa Sovereign....	250	TDS; IC	1981/1994	Indonesia	Maxus
Ocean Champion........	250	MS	1975/1985	Gulf of Mexico	Chevron
Ocean Columbia........	250	TDS; IC	1978/1990	Gulf of Mexico	Coastal Oil & Gas
Ocean Spartan.........	250	TDS; IC	1980/1994	Gulf of Mexico	Meridian
Ocean Spur............	250	TDS; IC	1981/1994	Gulf of Mexico	Houston Exploration(o)
Ocean Conquest........	200	MS	1978	Gulf of Mexico	Stacked
Ocean Crusader........	200	TDS; MC	1982/1992	Gulf of Mexico	Chevron
Ocean Drake...........	200	TDS; MC	1983/1986	Gulf of Mexico	Murphy
Arethusa Scotian......	180	TDS; IC; 15K	1981/1988	North Sea (Dutch sector)	Elf
Ocean Magallanes(p)...	150	IC	1980	Chile	Stacked
DRILLSHIP(1):					
Ocean Clipper I.......	1,200	SP	1976	Enroute	Committed(q)

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(a) Does not include one other semisubmersible rig held for disposition that is also not included in the discussion of Diamond Offshore's fleet.

(b) Attributes legend:

DP	--	Dynamically Positioned/Self-Propelled
MS	--	Mat-Supported Slot Rig
TDS	--	Top-Drive Drilling System
IC	--	Independent-Leg Cantilevered Rig
SDS	--	Side-Drive Drilling System
VC	--	Victory-Class
IS	--	Independent-Leg Slot Rig
SO	--	Skid-Off Capability
3M	--	Three Mud Pumps
MC	--	Mat-Supported Cantilevered Rig
SP	--	Self-Propelled
15K	--	15,000 psi Blowout Preventer

(c) Such enhancements include the installation of top-drive drilling systems, water depth upgrades, mud pump additions and increases in deck load capacity.

(d) For ease of presentation in this table, customer names have been shortened or abbreviated.

(e) Arethusa acquired the Arethusa Yatzy on May 3, 1995. Prior to this date the rig was operated by Arethusa under a management agreement.

(f) Turnkey operator is ADTI.

(g) Project manager is DOTS.

(h) Committed for two-well contract after completion of rig enhancements.

(i) Formerly named Ocean Countess.

(j) Committed under a letter of intent for a three-year term contract with Texaco in the Gulf of Mexico.

(k) Committed under a three-year term contract with Chevron in the Gulf of Mexico.

(l) Turnkey operator is Triton.

(m) Diamond Offshore charters the rig pursuant to a bareboat charter agreement which expires in August 1996. The rig is under contract for sale, upon closing of which such charter will terminate.

(n) Diamond Offshore operates the rig pursuant to a bareboat charter agreement which expires in July 1997. Diamond Offshore has the option to extend the charter agreement for one additional year. The rig is enroute to India following completion of leg repairs.

(o) Turnkey operator is Brown/R&B.

(p) Under contract for sale.

(q) Committed under an agreement in principle for a four-year term contract in the Gulf of Mexico following completion of rig enhancement.

UNDERWRITING

Subject to the terms and conditions set forth in the U.S. purchase agreement (the "U.S. Purchase Agreement") among Diamond Offshore, the Selling Stockholders and each of the underwriters named below (the "U.S. Underwriters"), and concurrently with the sale of 1,505,000 shares of Diamond Offshore Common Stock to the International Managers (as defined below), the Selling Stockholders have agreed to sell to the U.S. Underwriters, and each of the U.S. Underwriters severally has agreed to purchase from the Selling Stockholders, the number of shares of Diamond Offshore Common Stock set forth opposite its name below.

U.S. UNDERWRITER	NUMBER OF SHARES
Merrill Lynch, Pierce, Fenner & Smith Incorporated	2,006,048
CS First Boston Corporation	2,006,046
Salomon Brothers Inc	2,006,046
Total	6,018,140

Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch"), CS First Boston and Salomon Brothers Inc are acting as representatives (the "U.S. Representatives") of the U.S. Underwriters.

Diamond Offshore and the Selling Stockholders have also entered into the international purchase agreement (the "International Purchase Agreement") with certain underwriters outside the United States and Canada (the "International Managers" and, together with the U.S. Underwriters, the "Underwriters") for whom Merrill Lynch International, CS First Boston Limited and Salomon Brothers International Limited are acting as representatives (the "International Representatives"). Subject to the terms and conditions set forth in the International Purchase Agreement, and concurrently with the sale of 6,018,140 shares of Diamond Offshore Common Stock to the U.S. Underwriters pursuant to the U.S. Purchase Agreement, the Selling Stockholders have agreed to sell to the International Managers, and the International Managers severally have agreed to purchase from the Selling Stockholders, an aggregate of 1,505,000 shares of Diamond Offshore Common Stock. The public offering price per share of the Diamond Offshore Common Stock and the total underwriting discount per share are identical under the U.S. Purchase Agreement and the International Purchase Agreement.

In the U.S. Purchase Agreement and the International Purchase Agreement, the several U.S. Underwriters and the several International Managers, respectively, have agreed, subject to the terms and conditions set forth therein, to purchase all of the shares of Diamond Offshore Common Stock being sold pursuant to each such Purchase Agreement if any of such shares of Diamond Offshore Common Stock being sold pursuant to each such Purchase Agreement are purchased. Under certain circumstances, the commitments of non-defaulting U.S. Underwriters or International Managers (as the case may be) may be increased. The closings with respect to the sale of shares of Diamond Offshore Common Stock to be purchased by the International Managers and the U.S. Underwriters are conditioned upon one another.

The U.S. Underwriters and the International Managers have entered into an intersyndicate agreement (the "Intersyndicate Agreement") providing for the coordination of their activities. Under the terms of the Intersyndicate Agreement, the U.S. Underwriters and the International Managers are permitted to sell shares of Diamond Offshore Common Stock to each other for purposes of resale at the public offering price, less an amount not greater than the selling concession. Under the terms of the Intersyndicate Agreement, the U.S. Underwriters and any dealer to whom they sell shares of Diamond Offshore Common Stock will not offer to sell or sell shares of Diamond Offshore Common Stock to persons who are non-United States persons or non-Canadian persons or to persons they believe intend to resell to persons who are non-United States persons or non-Canadian persons, and the International Managers and any dealer to whom they sell shares of Diamond Offshore Common Stock will not offer to sell or sell shares of Diamond Offshore Common Stock to persons who are United States or Canadian persons or to persons they believe intend to resell to United States or Canadian persons, except, in each case, for transactions pursuant to the Intersyndicate Agreement.

The U.S. Representatives have advised Diamond Offshore and the Selling Stockholders that the U.S. Underwriters propose to offer the shares of Diamond Offshore Common Stock offered hereby to the public at the public offering price set forth on the cover page of this Prospectus Supplement, and to certain dealers at such price less a concession not in excess of $.90 per share of Diamond Offshore Common Stock. The U.S. Underwriters may allow, and such dealers may reallow, a discount not in excess of $.10 per share of Diamond Offshore Common Stock on sales to certain other dealers. After the public offering, the public offering price, concession and discount may be changed.

The Selling Stockholders have granted an option to the U.S. Underwriters, exercisable during the 30-day period after the date of this Prospectus Supplement, to purchase up to an aggregate of 601,814 additional shares of Diamond Offshore Common Stock at the public offering price, less the underwriting discount. The U.S. Underwriters may exercise this option only to cover over-allotments, if any, made on the sale of Diamond Offshore Common Stock offered hereby. To the extent that the U.S. Underwriters exercise this option, each U.S. Underwriter shall be obligated, subject to certain conditions, to purchase the number of additional shares of Diamond Offshore Common Stock proportionate to such U.S. Underwriter's initial amount reflected in the foregoing table. The Selling Stockholders also have granted an option to the International Managers, exercisable during the 30-day period after the date of this Prospectus Supplement, to purchase up to an aggregate of 150,501 additional shares of Diamond Offshore Common Stock to cover over-allotments, if any, on terms similar to those granted to the U.S. Underwriters.

The Selling Stockholders have agreed not to directly or indirectly sell, offer to sell, grant any option for sale of, contract or otherwise transfer any shares of Diamond Offshore Common Stock (except for the shares offered hereby) or any securities convertible into or exchangeable or exercisable for Diamond Offshore Common Stock for a period of 90 days after the date of this Prospectus Supplement (the "Underwriters' Restricted Period") without the prior written consent of Merrill Lynch. In addition, the Selling Stockholders have agreed that, during the Underwriters' Restricted Period, without the prior written consent of Merrill Lynch, the Selling Stockholders will not release Diamond Offshore from Diamond Offshore's obligation under the Shareholders Agreement not to effect, and to cause Loews to agree not to effect, any public sale or distribution of any securities the same as or similar to the Diamond Offshore Common Stock, or any securities convertible into or exchangeable into securities the same as or similar to the Diamond Offshore Common Stock (except pursuant to registrations on Form S-4 or any successor form, or Form S-8 or any successor form relating solely to securities offered pursuant to any benefit plan). See "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders" in the accompanying Prospectus.

Pursuant to the terms of an engagement letter dated September 1, 1995 (as amended), Arethusa has agreed to pay Merrill Lynch $7.5 million for financial advisory services in connection with the Acquisition. Arethusa has also agreed to reimburse Merrill Lynch for its reasonable out-of-pocket expenses, including all reasonable fees and disbursements of counsel, and to indemnify Merrill Lynch and certain related persons against certain liabilities relating to or arising out of its engagement, including certain liabilities under the federal securities laws. In addition, during the past two years Merrill Lynch has performed investment banking services for Loews, an affiliate of Diamond Offshore, from time to time and has been compensated therefor. Such services have included, among other things, acting as manager of, or participating as a syndicate member in, various securities transactions of Loews and its subsidiaries and providing financial advisory services to Loews.

In consideration of financial advisory services rendered in connection with the Acquisition, Diamond Offshore has agreed to pay CS First Boston a $500,000 fee. In addition, Diamond Offshore has agreed to reimburse CS First Boston for all reasonable out-of-pocket expenses, including the fees and expenses of its legal counsel and any other advisor retained by CS First Boston resulting from or arising out of Diamond Offshore's engagement of CS First Boston with respect to the Acquisition, and has agreed to indemnify CS First Boston (and its directors, officers, employees, and persons controlling CS First Boston) against certain liabilities and expenses in connection with the Acquisition, including certain liabilities under federal securities laws. The Underwriters have agreed to pay certain expenses of the Selling Stockholders incurred in connection with the sale of the Offered Shares estimated at $100,000.

The Underwriters do not intend to confirm sales of the shares of Diamond Offshore Common Stock offered hereby to any accounts over which they exercise discretionary authority.

Diamond Offshore, Loews and the Selling Stockholders have agreed to indemnify the Underwriters against certain liabilities, including certain liabilities under the Securities Act of 1933, as amended, or to contribute to payments the Underwriters may be required to make in respect thereof.

LEGAL MATTERS

The validity of the shares of Diamond Offshore Common Stock offered hereby will be passed on for Diamond Offshore by Weil, Gotshal & Manges LLP, Houston, Texas. Certain legal matters will be passed on for the Underwriters by Skadden, Arps, Slate, Meagher & Flom, New York, New York.

INDEX TO PROSPECTUS SUPPLEMENT FINANCIAL STATEMENTS

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	MARCH 31, 1996	DECEMBER 31, 1995
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 3,867	$ 10,306
Short-term investments	5,110	5,041
Accounts receivable	87,624	74,496
Rig inventory and supplies	15,746	15,330
Prepaid expenses and other	8,209	10,601
Total current assets	120,556	115,774
DRILLING AND OTHER PROPERTY AND EQUIPMENT, LESS ACCUMULATED DEPRECIATION	533,645	502,278
OTHER ASSETS	3,984	--
Total assets	$ 658,185	$ 618,052
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 14,171	$ 18,322
Accrued liabilities	35,905	33,929
Total current liabilities	50,076	52,251
LONG-TERM DEBT	15,000	--
DEFERRED TAX LIABILITY	79,737	72,907
OTHER LIABILITIES	1,740	--
Total liabilities	146,553	125,158
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Preferred stock (par value $.01, 25,000,000 shares authorized, none issued and outstanding)	--	--
Common stock (par value $.01, 200,000,000 shares authorized, 50,000,000 shares issued and outstanding)	500	500
Additional paid-in capital	665,107	665,107
Accumulated deficit	(152,712)	(171,444)
Cumulative translation adjustment	(1,263)	(1,269)
Total stockholders' equity	511,632	492,894
Total liabilities and stockholders' equity	$ 658,185	$ 618,052

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	THREE MONTHS ENDED MARCH 31, 1996	1995
REVENUES	$106,868	$ 70,760
OPERATING EXPENSES:		
Contract drilling	66,157	61,751
General and administrative	3,103	3,140
Depreciation	12,069	14,988
Gain on sale of assets	(157)	(389)
Total operating expenses	81,172	79,490
OPERATING INCOME (LOSS)	25,696	(8,730)
OTHER INCOME (EXPENSE):		
Interest expense	--	(8,486)
Currency transaction gains (losses)	86	(34)
Other, net	348	389
INCOME (LOSS) BEFORE INCOME TAX (EXPENSE) BENEFIT	26,130	(16,861)
INCOME TAX (EXPENSE) BENEFIT	(7,398)	5,289
NET INCOME (LOSS)	$ 18,732	$(11,572)
NET INCOME PER SHARE	$ 0.37	
WEIGHTED AVERAGE SHARES OUTSTANDING	50,000	

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	THREE MONTHS ENDED MARCH 31, 1996	1995
OPERATING ACTIVITIES:		
Net income (loss)	$ 18,732	$(11,572)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	12,069	12,918
Gain on sale of assets	(157)	(389)
Write-down of asset	--	2,070
Accrued interest converted to notes payable to Loews	--	8,484
Deferred tax provision (benefit)	7,124	(5,489)
Changes in operating assets and liabilities:		
Accounts receivable	(13,128)	4,611
Rig inventory and supplies and other current assets	2,339	(9)
Other assets, non-current	(2,583)	--
Accounts payable and accrued liabilities	(2,175)	48
Other liabilities, non-current	1,740	--
Other, net	(288)	20
Net cash provided by operating activities	23,673	10,692
INVESTING ACTIVITIES:		
Capital expenditures	(43,757)	(6,981)
Proceeds from sales of assets	478	439
Change in short-term investments	(69)	--
Net cash used in investing activities	(43,348)	(6,542)
FINANCING ACTIVITIES:		
Borrowings on revolving line of credit	37,000	--
Repayments on revolving line of credit	(22,000)	--
Deferred financing costs	(1,764)	--
Net repayments to Loews	--	(6,000)
Net cash provided by (used in) financing activities	13,236	(6,000)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(6,439)	(1,850)
Cash and cash equivalents, beginning of period	10,306	17,770
Cash and cash equivalents, end of period	$ 3,867	$ 15,920

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL

The consolidated financial statements of Diamond Offshore Drilling, Inc. and subsidiaries (the "Company") should be read in conjunction with the Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 1-13926).

Interim Financial Information

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all disclosures required by generally accepted accounting principles for complete financial statements. The consolidated financial information has not been audited but, in the opinion of management, includes all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation of the consolidated balance sheets, statements of operations, and statements of cash flows at the dates and for the periods indicated. Results of operations for interim periods are not necessarily indicative of results of operations for the respective full years.

Cash and Cash Equivalents

All short-term, highly liquid investments that have an original maturity of three months or less are considered cash equivalents.

Supplementary Cash Flow Information

Non-cash financing activities for the three months ended March 31, 1995 included $8.5 million of interest expense accrued and included in notes payable to Loews Corporation ("Loews"). There were no non-cash financing activities for the three months ended March 31, 1996. Cash payments made for interest on long-term debt for the three months ended March 31, 1996 totaled $37,000.

Drilling and Other Property and Equipment

For financial reporting purposes, depreciation is provided on the straight-line method over the remaining estimated useful lives from the date the asset is placed into service. The Company believes that certain offshore drilling rigs, due to their upgrade and design capabilities and maintenance history, have an operating life in excess of their depreciable life as originally assigned. For this reason, a change in accounting estimate, effective January 1, 1996, increased the estimated useful lives for certain classes of offshore drilling rigs. As compared to the original estimate of useful lives, the effect of such change reduced depreciation expense and increased net income for the three months ended March 31, 1996 by approximately $2.1 million and $1.5 million ($0.03 per share), respectively. The estimated useful lives of the Company's offshore drilling rigs, after the change in estimate, range from 10 to 25 years.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimated.

Reclassifications

Certain amounts applicable to the prior periods have been reclassified to conform to the classifications currently followed. Such reclassifications do not affect earnings.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

2. PENDING MERGER OF THE COMPANY AND ARETHUSA (OFF-SHORE) LIMITED

The Company and Arethusa (Off-Shore) Limited ("Arethusa"), a Bermuda corporation, have entered into an agreement to merge the two companies. The agreement provides that, upon consummation of the merger, holders of Arethusa stock will receive 17.9 million shares of common stock to be issued by the Company based on 20.3 million shares of Arethusa's common stock issued and outstanding and on a ratio of .88 shares for each share of issued and outstanding Arethusa common stock. The merger is subject to requisite shareholder approval at the April 29, 1996 annual meeting of both companies. The merger will be accounted for as a purchase for financial reporting purposes, and accordingly, the costs of the merger will be allocated to assets acquired and liabilities assumed based on their estimated fair market values.

Arethusa owns a fleet of 11 mobile offshore drilling rigs, operates two additional mobile offshore drilling rigs, and provides drilling services worldwide to international and government-controlled oil and gas companies. For the year ended September 30, 1995, Arethusa reported revenues of $122.1 million, net income of $21.6 million, and net income per share of $1.06.

3. DRILLING AND OTHER PROPERTY AND EQUIPMENT

Cost and accumulated depreciation of drilling and other property and equipment are summarized as follows:

	MARCH 31, 1996	DECEMBER 31, 1995
	(IN THOUSANDS)	
Drilling rigs and equipment	$ 705,957	$ 689,438
Construction work in progress	37,271	19,016
Land and buildings	11,845	3,655
Office equipment and other	6,761	6,300
	761,834	718,409
Less accumulated depreciation	(228,189)	(216,131)
Total	$ 533,645	$ 502,278

For the three months ended March 31, 1996, the Company capitalized total interest cost incurred of $.2 million in construction work in progress with respect to qualifying construction projects.

4. ACCRUED LIABILITIES

Accrued liabilities consist of the following:

	MARCH 31, 1996	DECEMBER 31, 1995
	(IN THOUSANDS)	
Compensation and benefits	$16,517	$ 17,402
Other	19,388	16,527
Total	$35,905	$ 33,929

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

5. LONG-TERM DEBT

In the first quarter of 1996, the Company executed a definitive credit agreement governing a $150.0 million credit facility with a group of banks (the "Credit Facility"). Borrowings under the Credit Facility bear interest, at the Company's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. The Company is required to pay a commitment fee of .375% on the unused available portion of the maximum credit commitment. Debt financing costs are deferred and amortized over the term of the debt. The weighted average interest rate on the Credit Facility, including commitment and arrangement fees, was 14.5% at March 31, 1996. Borrowings are secured by security interests in certain of the Company's assets. The Credit Facility also contains covenants that limit the amount of total consolidated debt, require the maintenance of certain consolidated financial ratios and limit dividends and similar payments.

8,375,455 SHARES

[DIAMOND OFFSHORE LOGO]

DIAMOND OFFSHORE DRILLING, INC.

COMMON STOCK

($.01 PAR VALUE)

PROSPECTUS

This Prospectus relates to 8,375,455 shares (the "Offered Shares") of common stock, par value $0.01 per share ("Diamond Offshore Common Stock"), of Diamond Offshore Drilling, Inc., a Delaware corporation ("Diamond Offshore"), which Offered Shares may be offered from time to time by and for the account of Alphee S.A., a Luxembourg corporation ("Alphee"), and/or Forvaltnings AB Ratos, a Swedish corporation ("Ratos" and, together with Alphee, the "Selling Stockholders"). Diamond Offshore will not receive any of the proceeds from the sale of the Offered Shares. Diamond Offshore will bear certain costs relating to the registration of the Offered Shares.

Pursuant to the Plan of Acquisition dated as of February 9, 1996, as amended (as so amended, the "Plan of Acquisition"), among Diamond Offshore, Diamond Offshore (USA) Inc., a Delaware corporation ("Diamond Offshore (USA)"), AO Acquisition Limited, a Bermuda company ("Acquisition Sub"), and Arethusa (Off-Shore) Limited, a Bermuda company ("Arethusa"), and the Amalgamation Agreement dated as of February 9, 1996 (the "Amalgamation Agreement") between Arethusa and Acquisition Sub, Diamond Offshore acquired Arethusa (the "Acquisition"), on the terms set forth in the Plan of Acquisition and Amalgamation Agreement. All of the information presented herein assumes consummation of the Acquisition on April 29, 1996. Arethusa shareholders received 17,893,344 shares of Diamond Offshore Common Stock, representing approximately 26.4% of the total Diamond Offshore Common Stock currently outstanding, of which the Selling Stockholders received an aggregate of 8,375,455 shares.

The Offered Shares may be offered for sale from time to time by the Selling Stockholders to or through underwriters or directly to other purchasers or through agents in one or more transactions on the New York Stock Exchange, Inc. (the "NYSE"), in the over-the-counter market, in one or more private transactions, or in a combination of such methods of sale, at prices and on terms then prevailing, at prices related to such prices, or at negotiated prices. The Selling Stockholders and any brokers and dealers through whom sales of the Offered Shares are made may be deemed to be "underwriters" within the meaning of the Securities Act of 1933, as amended, and the commissions or discounts and other compensation paid to such persons may be regarded as underwriters' compensation.

Diamond Offshore Common Stock is listed on the NYSE under the symbol "DO."

FOR A DISCUSSION OF CERTAIN FACTORS THAT SHOULD BE CONSIDERED IN CONNECTION WITH AN INVESTMENT IN THE OFFERED SHARES, SEE "RISK FACTORS" BEGINNING ON PAGE 6.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THIS PROSPECTUS MAY NOT BE USED PRIOR TO CONSUMMATION OF THE ACQUISITION.

The date of this Prospectus is April 12, 1996.

NO DEALER, SALESPERSON OR OTHER INDIVIDUAL HAS BEEN AUTHORIZED TO GIVE ANY INFORMATION OR MAKE ANY REPRESENTATION NOT CONTAINED IN THIS PROSPECTUS IN CONNECTION WITH THE OFFERING COVERED BY THIS PROSPECTUS. IF GIVEN OR MADE, SUCH INFORMATION OR REPRESENTATIONS MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY DIAMOND OFFSHORE, THE SELLING STOCKHOLDERS OR THE UNDERWRITERS. THIS PROSPECTUS DOES NOT CONSTITUTE AN OFFER TO SELL, OR A SOLICITATION OF AN OFFER TO BUY, THE OFFERED SHARES IN ANY JURISDICTION WHERE, OR TO ANY PERSON TO WHOM, IT IS UNLAWFUL TO MAKE SUCH OFFER OR SOLICITATION. NEITHER THE DELIVERY OF THIS PROSPECTUS NOR ANY SALE MADE HEREUNDER SHALL, UNDER ANY CIRCUMSTANCES, CREATE AN IMPLICATION THAT THERE HAS NOT BEEN ANY CHANGE IN THE FACTS SET FORTH IN THIS PROSPECTUS OR IN THE AFFAIRS OF DIAMOND OFFSHORE SINCE THE DATE HEREOF.

AVAILABLE INFORMATION

Diamond Offshore is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and, in accordance therewith, files reports and other information with the Securities and Exchange Commission (the "Commission"). Reports, proxy and information statements filed pursuant to Sections 14(a) and 14(c) of the Exchange Act and other information filed with the Commission can be inspected and copied at the public reference facilities maintained by the Commission at Room 1024, 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549, and at the following Regional Offices of the Commission: Chicago Regional Office, Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661 and New York Regional Office, 7 World Trade Center, Suite 1300, New York, New York 10048. Copies of such material can also be obtained at prescribed rates from the Public Reference Section of the Commission at its principal office at 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549. In addition, Diamond Offshore's reports, proxy and information statements filed pursuant to Sections 14(a) and 14(c) of the Exchange Act and other information concerning Diamond Offshore can be inspected at the offices of the NYSE, 20 Broad Street, New York, New York 10005, on which exchange Diamond Offshore securities are listed.

Diamond Offshore has filed with the Commission a Registration Statement (the "Registration Statement") under the Securities Act of 1933, as amended (the "Securities Act"), on Forms S-4/S-1 with respect to the securities offered hereby. This Prospectus also constitutes the prospectus of Diamond Offshore filed as part of the Registration Statement and does not contain all of the information set forth in the Registration Statement and the exhibits thereto, certain parts of which are omitted in accordance with the rules and regulations of the Commission. Statements made in this Prospectus as to the contents of any contract, agreement or other document referred to are not necessarily complete (but are accurate statements of those matters considered by Diamond Offshore to be material to a prospective investor in the Offered Shares); with respect to each such contract, agreement or other document filed as an exhibit to the Registration Statement, reference is made to the exhibit for a more complete description of the matter involved, and each such statement shall be deemed qualified in its entirety by such reference. The Registration Statement and any amendments thereto, including exhibits filed as a part thereof, are available for inspection and copying at the Commission's offices as described above.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF DIAMOND OFFSHORE COMMON STOCK AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH TRANSACTIONS MAY BE EFFECTED ON THE NYSE OR OTHERWISE. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

DURING THIS OFFERING, CERTAIN PERSONS AFFILIATED WITH PERSONS PARTICIPATING IN THE DISTRIBUTION MAY ENGAGE IN TRANSACTIONS FOR THEIR OWN ACCOUNTS OR FOR THE ACCOUNTS OF OTHERS IN THE DIAMOND OFFSHORE COMMON STOCK PURSUANT TO EXEMPTIONS FROM RULES 10B-6, 10B-7, AND 10B-8 UNDER THE EXCHANGE ACT.

PROSPECTUS SUMMARY

The following summary is qualified in its entirety by, and should be read in conjunction with, the more detailed information and the Consolidated Financial Statements (including the Notes thereto) included elsewhere in this Prospectus. Unless the context otherwise requires, references in this Prospectus to "Diamond Offshore" shall mean Diamond Offshore Drilling, Inc. and its consolidated subsidiaries including, from and after the consummation of the Acquisition on April 29, 1996 (the "Effective Time"), Arethusa and its consolidated subsidiaries. In this Prospectus, references to "dollars" and "$" are to United States dollars.

DIAMOND OFFSHORE

Diamond Offshore engages principally in the contract drilling of offshore oil and gas wells. Diamond Offshore's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Asia and consists of 30 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 19 jack-up rigs owned and/or operated by Diamond Offshore and one drillship. Diamond Offshore also operates 10 land rigs deployed in South Texas. Except for two jack-up rigs operated pursuant to bareboat charter contracts, all of Diamond Offshore's offshore and land rigs are wholly owned.

Market Overview. The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances (including 3-D seismic, horizontal drilling and subsea completion procedures) that have broadened opportunities for offshore exploration and development. Both the Gulf of Mexico and the North Sea semisubmersible markets have experienced increased utilization and significantly higher dayrates in 1995 and 1996, and customers increasingly are seeking to contract for rigs serving these markets under term contracts (as opposed to contracts let on a single well or well-to-well basis). As part of this trend, Diamond Offshore recently received a commitment from a major oil company for a four-year term contract for its drillship Ocean Clipper I, which will support an upgrade of the rig to operate in deep water with dynamic positioning capabilities. In addition, Diamond Offshore has entered into a contract and a letter of intent with two major oil companies for two Victory-class semisubmersibles to conduct deep water drilling operations in the Gulf of Mexico under three-year term contracts, in connection with which Diamond Offshore will significantly enhance these rigs. The market for jack-up rigs in the Gulf of Mexico, which weakened during 1994, appears to have stabilized during 1995 and has shown some signs of strengthening in recent months. Historically, however, the offshore contract drilling market has been highly competitive and cyclical, and Diamond Offshore cannot predict the extent to which current conditions will continue.

Business Strategy. Diamond Offshore seeks to maximize dayrates and rig utilization by continuously adapting to changes in its markets, improving the capabilities of its drilling rigs and increasing the quality of its service. The key elements of its strategy are to:

- Market worldwide its large, diverse fleet, which is capable of satisfying customer requirements in a variety of applications;

- Continue to enhance its fleet to meet customer demand for diverse drilling capabilities, including those required for deep water and harsh environment operations;

- Exploit the potential of Diamond Offshore's nine Victory-class semisubmersible rigs by pursuing projects that take advantage of this rig type's unique design to yield significantly enhanced rigs; and

- Maintain a program of continuous improvement of quality and safety through Diamond Offshore's Global Excellence Management System and further capitalize on customer recognition of Diamond Offshore's quality and safety achievements.

The Acquisition. On April 29, 1996 Diamond Offshore completed the Acquisition, thereby augmenting its fleet with Arethusa's 13 owned and/or operated mobile offshore drilling rigs. Arethusa provided drilling services worldwide to international and government-controlled oil and gas companies. The eight semisubmersible rigs owned by Arethusa are located in the Gulf of Mexico and offshore Brazil and the five jack-up rigs in its fleet are located offshore India, Indonesia and Egypt, in the Gulf of Mexico and in the Dutch sector of the North Sea.

Pursuant to the Acquisition, Diamond Offshore issued and sold to its wholly owned subsidiary Diamond Offshore (USA) 17,893,344 shares of Diamond Offshore Common Stock, representing approximately 26.4% of the total Diamond Offshore Common Stock currently outstanding, which were contributed by Diamond Offshore (USA) to the capital of Acquisition Sub and delivered by Acquisition Sub to Arethusa shareholders in consideration of all of the issued and outstanding shares of Arethusa common stock, par value $0.10 per share ("Arethusa Common Stock"). The Acquisition was accomplished pursuant to an amalgamation (the "Amalgamation") of Arethusa with Acquisition Sub, a wholly owned subsidiary of Diamond Offshore (USA). The surviving company in the Amalgamation, Diamond Offshore Exploration (Bermuda) Limited ("Diamond Offshore Exploration (Bermuda)"), succeeded to the assets and liabilities of Arethusa and Acquisition Sub and is continuing the business of Arethusa and Acquisition Sub as a wholly owned subsidiary of Diamond Offshore (USA). See "Business -- The Acquisition."

Fleet Size and Diversity. Diamond Offshore's large, diverse fleet, which includes some of the most technologically advanced rigs in the world, enables it to offer a broad range of services worldwide in various markets, including the deep water market, the harsh environment market (such as the North Sea), the conventional semisubmersible market and the jack-up market. Diamond Offshore believes that it is well positioned to compete in the most complex deep water and harsh environment markets with its three fourth-generation semisubmersibles, each of which is capable of drilling in water depths of up to 5,000 feet and operating in harsh environments. Diamond Offshore's 27 remaining semisubmersible rigs, including 16 that are capable of drilling in waters of 1,500 feet or more and three that are currently marketed for drilling in the North Sea, give Diamond Offshore a significant presence worldwide in the expanding semisubmersible market. In addition, Diamond Offshore owns and/or operates 19 jack-up rigs with diverse capabilities that operate in water depths of up to 350 feet, including 14 capable of drilling in water depths of 250 feet or more.

Diamond Offshore believes that its presence in multiple markets provides a competitive advantage. For example, Diamond Offshore believes that its experience with safety and other regulatory matters in the United Kingdom has been beneficial in Australia and in the Gulf of Mexico and that production experience gained through Brazilian and North Sea operations has application worldwide. Additionally, Diamond Offshore believes that its performance for a customer in one market segment or area enables Diamond Offshore to better understand that customer's needs and serve that customer in different market segments or other geographic locations.

Fleet Enhancements. Diamond Offshore has continued to enhance its fleet both to increase overall technical capabilities and to meet specific drilling requirements. Diamond Offshore plans to continue its program of selectively enhancing its rigs to meet customer demand for advanced features or capabilities, including those required for operation in the deep water or harsh environment markets. For example, Diamond Offshore upgraded the semisubmersible Ocean Voyager to operate in maximum water depths of 3,200 feet and has modified the semisubmersible Ocean Nomad to allow it to be certified for service in the U.K. sector of the North Sea, where it is operating under a two-year contract at improved dayrates. Diamond Offshore converted three of its 300-foot cantilever jack-up rigs from slot rigs, which Diamond Offshore believes has resulted in these rigs achieving higher dayrates and utilization. In addition, Diamond Offshore has added top-drive drilling systems to many rigs, so that 36 rigs in Diamond Offshore's fleet are now so equipped. From time to time Diamond Offshore is able to negotiate lump-sum payments or increased dayrates from a customer to offset a portion of the costs of specific upgrades undertaken to enhance a rig to meet such customer's requirements for a particular drilling project.

Victory-Class Enhancements. The design of the Victory-class semisubmersible rigs, including their cruciform hull configurations, long fatigue-life and advantageous stress characteristics, makes this class of rig particularly well-suited for significant upgrading projects. Currently, Diamond Offshore's Victory-class rigs are outfitted for service in maximum water depths of 600 to 3,200 feet. Five of Diamond Offshore's nine Victory-class rigs are equipped with top-drive drilling systems, two are modified for increased efficiency in the handling of subsea completion equipment and one has stability enhancements that allow increased variable deck load. In management's opinion, it is unlikely that new semisubmersibles will be built unless there is a substantial and sustained improvement in the market; therefore, Diamond Offshore believes that the relative ease and efficiency with which it can significantly enhance its Victory-class rigs is a competitive advantage in a market requiring increasing capability from offshore drilling rigs.

The Ocean Quest, one of Diamond Offshore's Victory-class rigs, is currently undergoing an upgrade pursuant to contract with a major oil company for a three-year commitment. The rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 3,500 feet. This project includes enhancements to provide additional hull buoyancy, which will allow a variable deck load exceeding 5,000 tons, the addition of a new self-contained chain/wire mooring system, and drilling system upgrades, including the installation of a top-drive drilling system, a 15,000 psi blowout prevention system, a third mud pump and 2,900 barrel liquid mud capacity. The Ocean Quest is scheduled to be placed in service in the fourth quarter of 1996. In addition, during the third quarter of 1995 Diamond Offshore entered into a letter of intent with another major oil company for a three-year commitment for a second Victory-class rig, the Ocean Star (formerly named Ocean Countess), pursuant to which the rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 4,500 feet. The upgrade project for the Ocean Star also includes stability enhancements, the installation of a new mooring system and drilling system upgrades similar to those planned for the Ocean Quest. The Ocean Star is scheduled to be placed in service late in the fourth quarter of 1996. Following the upgrades, Diamond Offshore believes that these rigs will be able to compete effectively in the fourth-generation deep water market. Diamond Offshore is currently pursuing other such upgrade opportunities for its seven remaining Victory-class rigs. However, there can be no assurance that the upgrades for the Ocean Quest and the Ocean Star will be completed as planned, or within Diamond Offshore's budget for these projects, or that the definitive drilling contract contemplated by the letter of intent relating to the Ocean Star will be executed. In addition, there can be no assurance as to if, when or to what extent upgrades will be made to other Victory-class rigs in Diamond Offshore's fleet.

Additional Victory-class upgrade potential exists, including conceptual plans Diamond Offshore is developing for the possible construction of an ultra-large semisubmersible, the Ocean Legend. The Ocean Legend is intended to take advantage of the cruciform design of the Victory-class semisubmersibles to "square off" the rig by adding large corner columns and other new equipment to yield a rig with capabilities beyond a traditional fourth-generation unit at a significantly reduced cost as compared to new construction. Diamond Offshore has completed its feasibility studies and has begun preliminary design engineering in connection with the upgrade. See Note 1 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein. Although Diamond Offshore is proposing the design to several major oil companies, there can be no assurance that the Ocean Legend can be built in a cost-effective manner, that if a Victory-class rig is so upgraded, there will be adequate demand for its services, or that competitors will not achieve capability beyond that of fourth-generation semisubmersibles through other means attractive to customers.

Quality. Diamond Offshore maintains a program to continuously improve quality and safety through its Global Excellence Management System ("GEMS"), which was instituted in 1993 to increase Diamond Offshore's commitment to quality of service, safety and the environment. Diamond Offshore also seeks to capitalize on customer recognition of Diamond Offshore's quality and safety achievements. Diamond Offshore is the only drilling contractor to have won more than once (in April 1994 and April 1995) the annually awarded U.S. Minerals Management Service National Safety Award for Excellence.

RISK FACTORS

In addition to the other information contained in this Prospectus and incorporated herein by reference, prospective investors should carefully consider the matters set forth below before purchasing any of the Offered Shares.

DEPENDENCE ON OIL AND NATURAL GAS INDUSTRY; INDUSTRY CONDITIONS

Diamond Offshore's business and operations depend principally upon the condition of the oil and gas industry and, specifically, the exploration and production expenditures of oil and gas companies. Historically, the offshore contract drilling industry has been highly competitive and cyclical, with periods of high demand, short rig supply and high dayrates followed by periods of low demand, excess rig supply and low dayrates. The offshore contract drilling business is influenced by a number of factors, including the current and anticipated prices of oil and natural gas, the expenditures by oil and gas companies for exploration and production and the availability of drilling rigs. For a number of years, depressed oil and natural gas prices and an oversupply of rigs have adversely affected the offshore drilling market, particularly in the Gulf of Mexico, where the prolonged weakness and uncertainty in the demand for and price of natural gas resulted in a significant decline in exploration and production activities. Demand for drilling services outside the United States, excluding the North Sea, has been less volatile in recent years, but remains dependent on a variety of political and economic factors beyond Diamond Offshore's control, including worldwide demand for oil and natural gas, the ability of the Organization of Petroleum Exporting Countries ("OPEC") to set and maintain production levels and pricing, the level of production of non-OPEC countries and the policies of the various governments regarding exploration and development of their oil and natural gas reserves.

COMPETITION

The contract drilling industry is highly competitive. Customers often award contracts on a competitive bid basis, and although a customer selecting a rig may consider, among other things, a contractor's safety record, crew quality and quality of service and equipment, the oversupply of rigs has created an intensely competitive market in which price is the primary factor in determining the selection of a drilling contractor. Diamond Offshore believes that competition for drilling contracts will continue to be intense for the foreseeable future because of the worldwide oversupply of drilling rigs and the ability of contractors to move rigs from areas of low utilization and dayrates to areas of greater activity and relatively higher dayrates. In addition, there are inactive non-marketed rigs or rigs being operated in non-drilling activities that could be reactivated to meet an increase in demand for drilling rigs in any given market. Such movement or reactivation or a decrease in drilling activity in any major market could depress dayrates and could adversely affect utilization of Diamond Offshore's rigs. See "Business -- Offshore Contract Drilling Services."

HISTORY OF OPERATING LOSSES

Diamond Offshore reported operating income of $11.7 million for the year ended December 31, 1995, operating loss of $14.6 million for the year ended December 31, 1994, operating income of $4.5 million for the year ended December 31, 1993, operating loss of $49.2 million for the year ended December 31, 1992 and operating loss of $15.4 million for the year ended December 31, 1991. Additionally, Diamond Offshore reported net loss of $7.0 million, $34.8 million, $16.6 million, $53.4 million and $26.6 million for the years ended December 31, 1995, 1994, 1993, 1992 and 1991, respectively. Diamond Offshore had total stockholders' equity of $492.9 million as of December 31, 1995, net of an accumulated deficit of $171.4 million. Diamond Offshore's financial results in the future will depend primarily on the utilization and dayrates of the rigs operated by Diamond Offshore and the cost of such operations. Although demand for drilling services has improved recently, an oversupply of rigs has existed since the early 1980's and has led to intense price competition among drilling contractors. There can be no assurance that Diamond Offshore's operating results will improve in future periods. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Results of Operations."

AVERAGE AGE OF FLEET

The average age of the Diamond Offshore fleet of offshore drilling rigs (calculated as of December 31, 1995 and measured from year built) is 17.7 years. Many of Diamond Offshore's rigs have been upgraded during the last five years with enhancements such as top-drive drilling systems, increases to water depth capability, mud pump additions or increases in deck load capacity, and Diamond Offshore believes that it will be feasible to continue to upgrade its fleet, particularly its Victory-class semisubmersible rigs, notwithstanding the average age of its fleet. However, there can be no assurance as to if, when or to what extent upgrades will be made to rigs in Diamond Offshore's fleet. In addition, to the extent Diamond Offshore is not able to enhance its fleet with upgrade projects, Diamond Offshore will have fewer rigs available to meet customer demand for harsh environment and deep water operations than if such projects had been successfully implemented.

CONTROL BY MAJOR STOCKHOLDER AND POTENTIAL CONFLICTS OF INTEREST

Loews Corporation, a Delaware corporation ("Loews"), beneficially owns approximately 51.6% of the outstanding shares of Diamond Offshore Common Stock and is in a position to control actions that require the consent of stockholders, including the election of directors, amendment of Diamond Offshore's Restated Certificate of Incorporation and any mergers or any sale of substantially all the assets of Diamond Offshore. In connection with the initial public offering, in 1995, of Diamond Offshore Common Stock (the "Diamond Offshore Initial Public Offering"), Loews and Diamond Offshore entered into certain agreements providing for certain rights and obligations of each of them. See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and Loews."

Diamond Offshore's Board of Directors includes, and is expected to continue to include, persons who are also directors or officers of, or otherwise represent, Loews. Diamond Offshore's Board of Directors presently consists of five directors, one of whom (James S. Tisch) is also a director and the President and Chief Operating Officer of Loews, and another of whom (Herbert C. Hofmann) is a Senior Vice President of Loews. See "Management -- Security Ownership of Management and Directors." Loews (other than through Diamond Offshore) and Diamond Offshore are generally engaged in businesses sufficiently different from each other as to make conflicts as to possible corporate opportunities unlikely. It is possible, however, that Loews may in some circumstances be in direct or indirect competition with Diamond Offshore, including competition with respect to certain business strategies and transactions that Diamond Offshore may propose to undertake. In addition, potential conflicts of interest exist or could arise in the future for such directors with respect to a number of areas relating to the past and ongoing relationships of Loews and Diamond Offshore, including tax and insurance matters, financial commitments, and sales of Diamond Offshore Common Stock pursuant to registration rights or otherwise. Although the affected directors may abstain from voting on matters in which the interests of Diamond Offshore and Loews are in conflict so as to avoid potential violations of their respective fiduciary duties to stockholders of the respective corporations, the presence of potential or actual conflicts could affect the process or outcome of Board deliberations, and no policies, procedures or practices have been adopted by Diamond Offshore to reduce or avoid such conflicts. There can be no assurance that such conflicts of interest will not materially adversely affect Diamond Offshore. See "Management -- Certain Relationships and Related Transactions."

ENVIRONMENTAL MATTERS

Diamond Offshore's operations are subject to numerous federal, state and local environmental laws and regulations that relate directly or indirectly to its operations, including certain regulations controlling the discharge of materials into the environment, requiring removal and clean-up under certain circumstances, or otherwise relating to the protection of the environment. For example, Diamond Offshore may be liable for damages and costs incurred in connection with oil spills for which it is held responsible. Laws and regulations protecting the environment have become increasingly stringent in recent years and may in certain circumstances impose "strict liability" and render a company liable for environmental damage without regard to negligence or fault on the part of such company. Such laws and regulations may expose Diamond Offshore to liability for the conduct of or conditions caused by others, or for acts of Diamond Offshore that were in compliance with all applicable laws at the time such acts were performed. The application of these requirements or the adoption of new requirements could have a material adverse effect on Diamond Offshore. See "Business -- Governmental Regulation."

The United States Oil Pollution Act of 1990 ("OPA '90") and similar legislation enacted in Texas, Louisiana and other coastal states address oil spill prevention and control and significantly expand liability exposure across all segments of the oil and gas industry. OPA '90, such similar legislation and related regulations impose a variety of obligations on Diamond Offshore related to the prevention of oil spills and liability for damages resulting from such spills. OPA '90 imposes strict and with limited exceptions joint and several liability upon each responsible party for oil removal costs and a variety of public and private damages. OPA '90 also imposes ongoing financial responsibility requirements on a responsible party. A failure to comply with ongoing requirements or inadequate cooperation in a spill may subject a responsible party, including in some cases Diamond Offshore, to civil or criminal enforcement action. Also, the U.S. Minerals Management Service is required to promulgate regulations to implement the financial responsibility requirements for offshore facilities. If implemented as written, the financial responsibility requirements of OPA '90 could have the effect of significantly increasing the amount of financial responsibility that oil and gas operators must demonstrate to comply with OPA '90. While industry groups and marine insurance carriers are seeking modification of these requirements, implementation of these requirements in their current form could adversely affect the ability of some of Diamond Offshore's customers to operate in U.S. waters, which could have a material adverse effect on Diamond Offshore. See "Business -- Governmental Regulation."

OPERATIONAL HAZARDS

Diamond Offshore's operations are subject to hazards inherent in the drilling of oil and gas wells such as blowouts, reservoir damage, loss of production, loss of well control, cratering or fires, the occurrence of which could result in the suspension of drilling operations, injury to or death of rig and other personnel and damage to or destruction of Diamond Offshore's, Diamond Offshore's customer's or a third party's property or equipment. Damage to the environment could also result from Diamond Offshore's operations, particularly through oil spillage or uncontrolled fires. In addition, offshore drilling operations are subject to perils peculiar to marine operations, including capsizing, grounding, collision and loss or damage from severe weather. Diamond Offshore has insurance coverage and contractual indemnification for certain risks but there can be no assurance that such coverage or indemnification will adequately cover Diamond Offshore's loss or liability in many circumstances or that Diamond Offshore will continue to carry such insurance or receive such indemnification. See "Business -- Indemnification and Insurance."

GOVERNMENTAL REGULATION AND TAX POLICY

Diamond Offshore's operations are subject to numerous governmental laws and regulations. In addition, demand for services in the drilling industry is dependent on the oil and gas exploration industry and accordingly is affected by changes in tax and other laws relating to the energy business generally.

Significant capital expenditures may be required to comply with governmental laws and regulations applicable to Diamond Offshore and such compliance could materially adversely affect the results of operations or competitive position of Diamond Offshore. It is possible that such regulations may in the future add significantly to the cost of operating offshore drilling equipment or may significantly limit drilling activity. See "Business -- Governmental Regulation."

OPERATIONS OUTSIDE THE UNITED STATES

Operations outside the United States accounted for approximately 36.4%, 34.0% and 44.8% of Diamond Offshore's total consolidated revenues for fiscal years 1995, 1994 and 1993, respectively. Operations outside the United States accounted for approximately 47.5%, 52.3% and 63.9% of Arethusa's total consolidated revenues for fiscal years 1995, 1994 and 1993, respectively. Diamond Offshore's non-U.S. operations are subject to certain political, economic and other uncertainties not encountered in U.S. operations, including risks of war and civil disturbances (or other risks that may limit or disrupt markets), expropriation and the general hazards associated with the assertion of national sovereignty over certain areas in which operations are conducted. Diamond Offshore's operations outside the United States may face the additional risk of fluctuating currency values, hard currency shortages, controls of currency exchange and repatriation of income or capital. No prediction can be made as to what governmental regulations may be enacted in the future that could adversely affect the international drilling industry.

TURNKEY CONTRACTS

Diamond Offshore, through Diamond Offshore Turnkey Services, Inc. ("DOTS"), a Delaware corporation and a direct, wholly owned subsidiary of Diamond Offshore, selectively engages in drilling services pursuant to turnkey drilling contracts under which DOTS agrees to drill a well to a specified depth for a fixed price. Generally, DOTS is not entitled to payment unless the well is drilled to the specified depth and profitability of the contract depends upon its ability to keep expenses within the estimates used by DOTS in determining the contract price. Drilling a well under a turnkey contract therefore typically requires a cash commitment by Diamond Offshore in excess of those drilled under conventional dayrate contracts and exposes DOTS to risks of potential financial losses that generally are substantially greater than those that would ordinarily exist when drilling under a conventional dayrate contract. The financial results of a turnkey contract depend upon the performance of the drilling unit, drilling conditions and other factors, some of which are beyond the control of DOTS. See "Business -- Offshore Contract Drilling Services."

SHARES AVAILABLE FOR FUTURE SALE

Subject to the restrictions described in "Management -- Certain Relationships and Related Transactions -- Controlling Stockholder" and "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders" and applicable law, Loews is free to sell any and all of the shares of Diamond Offshore Common Stock it owns. In addition, as described in "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders," each of Alphee and Ratos is free to sell, without restriction, at its election, all or part of the shares of Diamond Offshore Common Stock received by such person in connection with the Acquisition. No prediction can be made as to the effect, if any, that future sales of Diamond Offshore Common Stock, or the availability of Diamond Offshore Common Stock for future sale, may have on the market price of the Diamond Offshore Common Stock prevailing from time to time. Sales of substantial amounts of Diamond Offshore Common Stock or the perception that such sales might occur could adversely affect prevailing market prices for the Diamond Offshore Common Stock. In connection with the Diamond Offshore Initial Public Offering, Diamond Offshore agreed that it will not offer, sell, contract to sell, pledge or otherwise dispose of, directly or indirectly, or file with the Commission a registration statement under the Securities Act relating to any additional shares of Diamond Offshore Common Stock or securities convertible into or exchangeable or exercisable for any shares of Diamond Offshore Common Stock until October 10, 1996 without the prior written consent of CS First Boston Corporation ("CS First Boston"), except grants of employee stock options pursuant to any subsequently adopted plan or issuances upon any exercise thereof. Loews agreed to similar restrictions on behalf of itself and its affiliates (other than Diamond Offshore) with respect to shares of the Diamond Offshore Common Stock. Also in connection with the Diamond Offshore Initial Public Offering, Diamond Offshore and Loews entered into an agreement that provides Loews with certain rights to have the shares of Diamond Offshore Common Stock owned by Loews registered by Diamond Offshore under the Securities Act in order to permit the public sale of such shares. See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and Loews -- Registration Rights Agreement."

USE OF PROCEEDS

Diamond Offshore will not receive any proceeds from the sale of the Offered Shares by the Selling Stockholders.

SELLING STOCKHOLDERS

All the Offered Shares being offered hereby are being offered by Alphee and/or Ratos who hold 4,708,248 shares (or approximately 6.9%) and 3,667,207 shares (or approximately 5.4%) of the Diamond Offshore Common Stock, respectively, and who, in the aggregate, hold all 8,375,455 Offered Shares, representing approximately 12.3% of the outstanding shares of Diamond Offshore Common Stock. All of the Offered Shares are being offered hereby.

Diamond Offshore, Diamond Offshore (USA), Acquisition Sub, Alphee and Ratos entered into a Shareholders Agreement, dated as of February 9, 1996, as amended (as so amended, the "Shareholders Agreement"), and therein agreed to certain provisions concerning the Fee Agreement, dated as of February 9, 1996, as amended, between Diamond Offshore and Arethusa (as so amended, the "Fee Agreement"). See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and the Selling Stockholders" and "-- Registration Rights of Selling Stockholders."

DIVIDEND POLICY

There were no cash dividends declared by Diamond Offshore for 1995 or 1994, except for a $2.1 million special dividend paid to Loews in connection with the Diamond Offshore Initial Public Offering. See Note 2 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein. Diamond Offshore does not anticipate that it will declare or pay any dividends on the Diamond Offshore Common Stock in the foreseeable future. Diamond Offshore expects that it will retain all earnings for the development and growth of its business. Any future determination as to payment of dividends will be made at the discretion of the Board of Directors of Diamond Offshore and will depend upon Diamond Offshore's operating results, financial condition, capital requirements, general business conditions and such other factors that the Board of Directors deems relevant. In addition, the payment of cash dividends is limited by the terms of Diamond Offshore's $150.0 million credit facility with a group of banks (the "Diamond Offshore Bank Credit Facility"). Generally, the Diamond Offshore Bank Credit Facility limits cash dividends to the then "Available Amount," as therein defined, not to exceed in the aggregate $20.0 million plus at the date of determination an amount equal to (i) 25% of cumulative consolidated net income for fiscal quarters ending after January 1, 1996 and prior to such date minus (ii) 100% of cumulative consolidated net loss for fiscal quarters ending after January 1, 1996 and prior to such date. The "Available Amount," for any date of determination, means $70.0 million plus (i) a percentage of cumulative consolidated EBITDA (as defined in the Diamond Offshore Bank Credit Facility) for fiscal quarters ending after January 1, 1996 and prior to such date, less adjustments for interest expense, provisions for taxes and certain drilling contract revenues, plus (ii) amounts attributable to certain asset sales and issuances of equity, minus (iii) amounts attributable to certain capital expenditures and investments made prior to such date, and to cash dividends theretofore paid. At February 8, 1996 (the effective date of the Diamond Offshore Bank Credit Facility), the "Available Amount" equalled $70.0 million, and Diamond Offshore would have been permitted to pay cash dividends aggregating $20.0 million at such date within the limits imposed by the Diamond Offshore Bank Credit Facility. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity" and Note 12 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

CAPITALIZATION

The following table sets forth the capitalization of Diamond Offshore as of December 31, 1995 and as adjusted as of such date after giving effect to the Acquisition. This table should be read in conjunction with the Consolidated Financial Statements (including the Notes thereto) and the Unaudited Pro Forma Consolidated Condensed Financial Statements included elsewhere in this Prospectus.

	DECEMBER 31, 1995 (UNAUDITED)	
	HISTORICAL	AS ADJUSTED
	(IN THOUSANDS)	
Total debt	$ --	$ 72,778
Stockholders' equity:		
Common stock, $.01 par value	500	679
Additional paid-in capital	665,107	1,215,605
Accumulated deficit	(171,444)	(171,444)
Cumulative translation adjustment	(1,269)	(1,269)
Total stockholders' equity	492,894	1,043,571
Total capitalization	$ 492,894	$ 1,116,349

SELECTED CONSOLIDATED FINANCIAL DATA

The following tables set forth selected consolidated historical and pro forma financial data for Diamond Offshore. The selected consolidated financial data were derived from the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore included elsewhere herein. The pro forma financial data reflect certain adjustments that give effect to the Acquisition, accounted for under the purchase method of accounting, and assuming that the Diamond Offshore Initial Public Offering had occurred at January 1, 1995. Such tables should be read in conjunction with the "Unaudited Pro Forma Consolidated Condensed Financial Statements" included elsewhere herein.

	YEAR ENDED DECEMBER 31,					
	1995 PRO FORMA	1995	1994	1993	1992(1)	1991
	(IN THOUSANDS, EXCEPT PER SHARE DATA)					
INCOME STATEMENT DATA:						
Total revenues....................	$ 456,750	$336,584	$307,918	$288,069	$214,885	$64,056
Operating expenses:						
Contract drilling..............	346,092	259,560	256,919	228,211	199,201	61,928
General and administrative......	22,890	13,857	11,993	11,785	15,401	3,416
Depreciation(2).................	85,770	52,865	55,366	46,819	49,667	14,545
Gain on sale of assets..........	(1,349)	(1,349)	(1,736)	(3,201)	(231)	(414)
Operating income (loss)...........	3,347	11,651	(14,624)	4,455	(49,153)	(15,419)
Interest expense..................	(7,453)	(27,052)	(31,346)	(25,906)	(28,591)	(7,296)
Other income (expense), net.......	5,646	1,598	(455)	(219)	(207)	106
Income tax benefit (expense)(3)...	(2,503)	6,777	11,621	5,041	24,575	(4,000)
Net loss..........................	(963)	(7,026)	(34,804)	(16,629)	(53,376)	(26,609)
Pro forma net income (loss) per share...........................	(0.01)	0.20(4)	--	--	--	--

	DECEMBER 31,					
	1995 PRO FORMA	1995	1994	1993	1992(1)	1991
	(IN THOUSANDS)					
BALANCE SHEET DATA:						
Working capital(5).................	$ 85,335	$ 63,523	$ 57,521	$ 52,904	$ 35,391	$ 8,960
Drilling and other property and equipment, net..................	1,052,118	502,278	488,664	498,740	478,454	94,574
Goodwill..........................	47,167	--	--	--	--	--
Total assets......................	1,268,930	618,052	588,158	592,162	582,418	117,414
Long-term debt(6)..................	62,175	--	394,777	353,483	233,216	88,254
Stockholders' equity(7)...........	1,043,571	492,894	124,066	158,361	275,300	5,550

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(1) Diamond Offshore acquired all of the common stock of Odeco Drilling Inc., a Delaware corporation ("Odeco"), for approximately $376.6 million in cash effective January 1, 1992.

(2) Effective January 1, 1993, Diamond Offshore revised the estimated useful lives for certain classes of its offshore drilling rigs. The estimated useful lives of Diamond Offshore's offshore drilling rigs, after the change in estimate, range from 10 to 25 years. As compared to the original estimate of useful lives, this change resulted in a reduction of approximately $6.3 million in depreciation expense during 1993 and a corresponding increase in operating income.

(3) Prior to the Diamond Offshore Initial Public Offering, Diamond Offshore was included in the consolidated U.S. federal income tax return of Loews. Effective January 1, 1992, Diamond Offshore adopted Statement of Financial Accounting Standards ("SFAS") No. 109 "Accounting for Income Taxes" which utilizes the liability method of accounting for income taxes. For all preceding periods,

Accounting Principles Board Opinion No. 11, the deferral method, was utilized. The cumulative effect of adoption of SFAS No. 109 on Diamond Offshore's results of operations for the year ended December 31, 1992 was not material. Prior to 1992, Diamond Offshore's profitable subsidiaries were allocated a share of the Loews consolidated tax expense and no benefit was given to any of Diamond Offshore's subsidiaries generating taxable losses. Effective January 1, 1992, a tax sharing agreement with Loews was adopted to allow for the recognition of expenses and benefits related to taxable income and losses as if Diamond Offshore filed a separate consolidated return. In conjunction with the Diamond Offshore Initial Public Offering, the tax sharing agreement was terminated and all assets and liabilities were settled by offsetting these amounts against notes payable to Loews. For taxable periods subsequent to the Diamond Offshore Initial Public Offering, Diamond Offshore will file a consolidated U.S. federal income tax return on a stand-alone basis.

(4) Pro forma net income per share gives effect to the Diamond Offshore Initial Public Offering and the after-tax effects of a reduction in interest expense. Assuming the Diamond Offshore Initial Public Offering had occurred at January 1, 1995, Diamond Offshore would have recognized net income of $10.0 million, or $0.20 per share of Diamond Offshore Common Stock, after adjusting for the after-tax effects of a reduction in interest expense. See Note 1 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

(5) Pro forma working capital includes fair values of identifiable current assets acquired and liabilities assumed, including liabilities for certain costs directly associated with the Acquisition and current maturities of long-term debt of Arethusa assumed by Diamond Offshore.

(6) Long-term debt consisted solely of notes payable to Loews for the historical periods presented.

(7) In connection with the Diamond Offshore Initial Public Offering, Diamond Offshore paid a special dividend of $2.1 million to Loews with a portion of the proceeds. No other cash dividends were paid during the historical periods presented.

UNAUDITED PRO FORMA CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

The following unaudited pro forma consolidated balance sheet has been prepared based on the historical financial statements of Diamond Offshore as of and for the year ended December 31, 1995 and of Arethusa as of and for the year ended September 30, 1995. The following unaudited pro forma consolidated condensed income statement has been prepared based on the historical financial statements of Diamond Offshore as of and for the year ended December 31, 1995 and based on pro forma income statement data for Arethusa that reflect adjustments to Arethusa's historical consolidated income statement for the year ended September 30, 1995 in connection with (i) the acquisition of the Arethusa Yatzy, (iii) the sale of the Treasure Stawinner and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of Arethusa Common Stock) as if each had occurred at the beginning of fiscal year 1995. The pro forma financial statements give effect to (i) the Acquisition, (ii) the Diamond Offshore Initial Public Offering and, in connection therewith, the use of the proceeds to repay all of Diamond Offshore's then outstanding indebtedness to Loews and to fund the payment of a special dividend to Loews and (iii) interest expense for working capital borrowings, and commitment and other fees, under the Diamond Offshore Bank Credit Facility. The Acquisition was accounted for under the purchase method of accounting using a purchase price of $560.7 million, which was calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced. The pro forma consolidated condensed balance sheet was prepared assuming such transactions were consummated on December 31, 1995 and give effect to events directly attributable to the transactions, including those that are nonrecurring. The pro forma consolidated condensed income statement was prepared assuming the transactions were consummated as of the beginning of the period presented and give effect to events directly attributable to the transactions which are expected to have a continuing impact on the combined entity. These pro forma consolidated condensed financial statements should be read in conjunction with the other financial information of Diamond Offshore and Arethusa presented elsewhere in this Prospectus. The pro forma consolidated condensed financial statements are presented for illustrative purposes only and are not necessarily indicative of actual results that would have been achieved had the transactions been consummated on such dates, and are not necessarily indicative of future results. The allocation of the purchase price is preliminary, as valuation and other studies have not been finalized. It is not expected that the final allocation of the purchase price will produce materially different results from those presented herein.

PRO FORMA CONSOLIDATED CONDENSED BALANCE SHEET

	HISTORICAL(A)			
	DIAMOND OFFSHORE	ARETHUSA	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS)			
Cash and other current assets	$ 41,278	$ 46,878	$ (21,632)(b)	$ 66,524
Accounts receivable	74,496	28,625	--	103,121
Drilling and other property and equipment, net	502,278	237,324	312,516(c)	1,052,118
Goodwill and other assets	--	2,505	44,662(d)	47,167
Total assets	$ 618,052	$ 315,332	$ 335,546	$1,268,930
Current liabilities	$ 52,251	$ 28,559	$ 3,500(e)	$ 84,310
Long-term debt	--	62,175	--	62,175
Deferred credits and other liabilities	72,907	2,019	3,948(f)	78,874
Common stock	500	2,033	(1,854)(g)	679
Additional paid-in capital	665,107	218,800	331,698(g)	1,215,605
Accumulated earnings (deficit)	(171,444)	132	(132)	(171,444)
Unrealized gain on equity securities	--	1,614	(1,614)	--
Cumulative translation adjustment	(1,269)	--	--	(1,269)
Total liabilities and stockholders' equity	$ 618,052	$ 315,332	$ 335,546	$1,268,930

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(a) There are no significant adjustments required to the historical financial statements of Diamond Offshore or Arethusa to conform accounting policies of the two companies.

(b) Adjustment for fair values of identifiable current assets acquired and for certain events directly attributable to the transaction. Such items include:

Severance, consulting, and salary continuation plans	$ (5,526)(1)
Arethusa dividend	(5,083)(2)
Financial advisory services	(7,500)(3)
Legal, accounting, and other	(2,500)(4)
Office lease cancellation	(1,023)(5)
	$(21,632)

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(1) Under the Plan of Acquisition, from and after the Effective Time, Diamond Offshore and Arethusa and their respective subsidiaries will honor in accordance with their terms certain Arethusa employment, severance, consulting and salary continuation plans. See "Business -- The Acquisition -- Continuing Arethusa Severance, Consulting and Salary Continuation Plans."

(2) On March 15, 1996, in anticipation of the Acquisition, and as expressly permitted by the Plan of Acquisition, Arethusa paid a dividend of $0.25 per share of Arethusa Common Stock.

(3) Arethusa has agreed to pay Merrill Lynch a fee of $7.5 million for financial advisory services in connection with the Acquisition upon the closing of the Acquisition.

(4) Adjustment for legal, accounting, printing and other nonrecurring charges expected to be incurred in connection with the Acquisition.

(5) Arethusa is committed under a lease agreement for office space that continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1.0 million. Such payment has no future economic benefit to the combined company and is incremental to other costs incurred by either Arethusa or Diamond Offshore in the conduct of activities prior to the Effective Time.

(c) Adjustment for fair values, based on current appraisals, of the eight semisubmersible drilling rigs, three jack-up drilling rigs, and other property and equipment owned by Arethusa.

(d) Adjustment for fair values of identifiable assets and for the excess of the cost of Arethusa over the sum of the amounts assigned to identifiable assets acquired less liabilities assumed.

(e) Adjustment for the estimated unfunded termination liability related to the Arethusa defined benefit plan.

(f) Adjustment for fair values of liabilities assumed and for the deferred tax liability for estimated future tax effects of differences between the tax bases and the fair value amounts assigned to identifiable assets and liabilities of Arethusa, offset by net operating loss carryforwards of Arethusa of approximately $30.0 million. As a result of the Acquisition, Diamond Offshore will have available to it certain Arethusa net operating loss carryforwards to reduce future U.S. federal income taxes payable. Due to the change in ownership of Arethusa resulting from the Acquisition, there will be annual limitations on the amount of Arethusa tax carryforwards available to be utilized by Diamond Offshore.

(g) The pro forma financial statements reflect the purchase of 100% of the outstanding shares of Arethusa Common Stock for a total consideration of $560.7 million which is comprised of the following:

Diamond Offshore Common Stock to be issued	$539,296(1)
Options assumed	11,381(2)
Total equity consideration	550,677
Transaction costs	10,000(3)
Total consideration	$560,677

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(1) The value of the Diamond Offshore Common Stock to be issued in the Acquisition is calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995) of $30.14.

(2) Amount represents the fair value of the Arethusa Options to be assumed by Diamond Offshore pursuant to the Amalgamation Agreement. The fair value is based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995), the Amalgamation Ratio and the option exercise price including the $3.00 reduction, which is subject to shareholder approval at the Arethusa Annual Meeting. See "Other Arethusa Annual Meeting Matters -- Decrease of Option Exercise Price."

(3) Amounts represent transaction costs directly associated with the Acquisition. See (b) above.

PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT

	HISTORICAL DIAMOND OFFSHORE	PRO FORMA ARETHUSA(A)	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
Revenues	$336,584	$ 120,166	$ --	$ 456,750
Operating expenses:				
Contract drilling	259,560	86,532	--	346,092
General and administrative	13,857	9,033	--	22,890
Depreciation and amortization	52,865	29,008	3,897(b)	85,770
Gain on sale of assets	(1,349)	--	--	(1,349)
Total operating expenses	324,933	124,573	3,897	453,403
Operating income (loss)	11,651	(4,407)	(3,897)	3,347
Other income (expense):				
Interest expense	(27,052)	(6,697)	26,296(c)	(7,453)
Other, net	1,598	4,048	--	5,646
Income (loss) before income tax benefit (expense)	(13,803)	(7,056)	22,399	1,540
Income tax benefit (expense)	6,777	(1,440)	(7,840)(d)	(2,503)
Net income (loss)	$ (7,026)	$ (8,496)	$ 14,559	$ (963)
Net income per common share	$ 0.20(f)	$ (0.42)		$ (0.01)
Weighted average common shares outstanding	50,000(f)	20,333		67,893(e)

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(a) Pro forma income statement data for Arethusa reflect (i) the acquisition of the Arethusa Yatzy, which occurred on May 3, 1995, (ii) the sale of the Treasure Stawinner, which occurred June 30, 1995, and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of Arethusa Common Stock) as if each had occurred at the beginning of fiscal year 1995. Set forth below in this footnote (a) are the historical amounts, and the adjustments thereto, upon which the pro forma Arethusa amounts are based.

ARETHUSA PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT

	HISTORICAL		ADJUSTMENTS			
	ARETHUSA	YATZY(1)	YATZY ACQUISITION	STAWINNER SALE	DIVIDEND/ CAPITAL DISTRIBUTION	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)					
Contract drilling revenue.........	$122,147	$12,315	$ --	$(14,296)(6)	$ --	$120,166
Operating expenses:						
Direct costs....................	87,953	8,060	(623)(5) (375)(2)	(8,483)(6)	--	86,532
General and administrative......	8,658	--	375(2)	--	--	9,033
Depreciation....................	29,547	--	1,352(3)	(1,891)(6)	--	29,008
Total operating expenses..............	126,158	8,060	729	(10,374)	--	124,573
Operating income (loss)...........	(4,011)	4,255	(729)	(3,922)	--	(4,407)
Other income (expense):						
Interest expense................	(6,311)	--	(1,168)(4)	782(6)	--	(6,697)
Interest income.................	5,692	--	--		(1,453)(7)	4,239
Gain (loss) on sale of assets...	27,820	--	--	(27,885)(6)	--	(65)
Other, net......................	(126)	--	--	--	--	(126)
Income (loss) before income taxes...........................	23,064	4,255	(1,897)	(31,025)	(1,453)	(7,056)
Tax provision.....................	(1,440)	--	--	--	--	(1,440)
Net income (loss).................	$ 21,624	$ 4,255	$(1,897)	$(31,025)	$(1,453)	$ (8,496)
Net income (loss) per common share...........................	$ 1.06					$ (0.42)
Weighted average common shares outstanding.....................	20,333					20,333

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(1) The historical financial information of the Yatzy operations for the period from October 1, 1994, through May 2, 1995 is based upon Arethusa records, as manager of the rig. The previous owner of the rig prepared financial information only on a semi-annual, calendar year basis; and was unable to provide the complete financial information for the twelve months ended September 30, 1995. Financial statement captions for which Yatzy historical information is not presented (historical depreciation and interest expense) would have been adjusted to reflect Arethusa's cost basis in the Arethusa Yatzy and Arethusa's financing of the rig. Pro forma Yatzy acquisition adjustments (3) and (4) discussed below provide fully for depreciation using Arethusa's cost basis in the Arethusa Yatzy and interest based on Arethusa's financing of the rig. Additionally, it is management's understanding that there are no other significant transactions or activities related to the historical operations of Yatzy which would have a material impact on the as-adjusted pro forma income statement. Therefore, management believes the resulting pro forma income statement is in compliance with Article 11 of Regulation S-X.

(2) To reclassify and eliminate the management fee paid to Arethusa from direct costs to general and administrative expenses.

(3) To reflect depreciation expense calculated based upon Arethusa's cost and estimated useful life of 25 years, which is consistent with Arethusa's previously established depreciation policy.

(4) To adjust for additional interest expense associated with Arethusa's $30.0 million note entered into in connection with the acquisition of the Arethusa Yatzy.

(5) To adjust for a reduction in insurance expense resulting from Arethusa's lower insured value for the Arethusa Yatzy.

(6) To reflect the elimination of historical operations, interest expense and gain on sale of assets for the Treasure Stawinner.

(7) To reflect the reduction in interest income resulting from the dividend and capital distribution made to shareholders in fiscal 1995.

(b) To record the additional depreciation expense and amortization of goodwill resulting from the allocation of the purchase price. The pro forma adjustment assumes an 18-year average estimated useful life for depreciation and a 20-year amortization period for goodwill.

(c) To adjust interest expense, assuming that the Diamond Offshore Initial Public Offering and repayment of indebtedness occurred on January 1, 1995.

(d) To record income tax expense on the effect of the pro forma adjustments to depreciation and amortization and interest expense.

(e) Weighted average shares outstanding as if both the October 1995 issuance of 15.0 million shares by Diamond Offshore through the Diamond Offshore Initial Public Offering and the 17.9 million shares to be issued by Diamond Offshore in consideration of the Arethusa Common Stock had taken place on January 1, 1995.

(f) After the Diamond Offshore Initial Public Offering, Diamond Offshore had 50.0 million shares of Diamond Offshore Common Stock outstanding. Assuming the Diamond Offshore Initial Public Offering had occurred at January 1, 1995, Diamond Offshore would have recognized net income of $10.0 million, or $0.20 per share of Diamond Offshore Common Stock, after adjusting for the after-tax effects of a reduction in interest expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with Diamond Offshore's Consolidated Financial Statements (including the notes thereto) included elsewhere herein.

RESULTS OF OPERATIONS

GENERAL

REVENUES. Diamond Offshore's revenues vary based upon demand, which affects the number of days the fleet is utilized and the dayrates received. Revenues can also increase or decrease as a result of the acquisition or disposal of rigs. In order to improve utilization or realize higher dayrates, Diamond Offshore may mobilize its rigs from one market to another. During periods of mobilization, however, revenues are generally adversely affected. As a response to changes in demand, Diamond Offshore may withdraw a rig from the market by stacking it or may reactivate a rig which was previously stacked, which may decrease or increase revenues, respectively.

Revenues from dayrate drilling contracts are recognized currently. When mobilization or enhancement is required for a contract, Diamond Offshore may receive a lump-sum payment to offset a portion of the cost of such requirements. Mobilization revenues less costs incurred to mobilize an offshore rig from one market to another are usually recognized over the term of the related drilling contract. In addition, payments received for rig enhancements are recognized as revenues over the term of the related drilling contract. Revenues from offshore turnkey contracts are recognized on the completed contract method, with revenues accrued to the extent of turnkey costs until the specified turnkey depth and other contract requirements are met.

OPERATING INCOME (LOSS). Operating income (loss) is primarily affected by revenue factors, but is also a function of varying levels of operating expenses. Operating expenses are not affected by changes in dayrates, nor are they necessarily significantly affected by fluctuations in utilization. For instance, if a rig is to be idle for a short period of time, Diamond Offshore realizes few decreases in operating expenses since the rig is typically maintained in a prepared state with a full crew. However, if the rig is to be idle for an extended period of time, Diamond Offshore may reduce the size of a rig's crew and take steps to "cold stack" the rig, which lowers expenses and partially offsets the impact on operating income associated with loss of revenues. Diamond Offshore recognizes as an operating expense maintenance activities such as painting, inspections and routine overhauls that maintain rather than upgrade its rigs. These expenses vary from period to period. Costs of rig enhancements are capitalized and depreciated over the expected useful lives of the enhancements. Depreciation expense decreases operating income in periods subsequent to capital upgrades. From time to time, Diamond Offshore sells assets in the ordinary course of its business and gains or losses associated with such sales are included in operating income (loss).

YEARS ENDED DECEMBER 31, 1995 AND 1994

Comparative data relating to Diamond Offshore's revenues and operating expenses by equipment type are listed below (eliminations offset dayrate revenues earned when Diamond Offshore's rigs are utilized in its turnkey operations). Diamond Offshore's drillship, Ocean Clipper I, is included in Other Semisubmersibles for discussion purposes.

	YEAR ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, 1994	INCREASE/ (DECREASE)
	(IN THOUSANDS)		
REVENUES			
Fourth-Generation Semisubmersibles	$ 67,393	$ 46,862	$ 20,531
Other Semisubmersibles	168,582	134,302	34,280
Jack-ups	68,829	89,883	(21,054)
Turnkey	27,121	25,296	1,825
Land	19,926	21,443	(1,517)
Other	4	11	(7)
Eliminations	(15,271)	(9,879)	(5,392)
Total Revenues	$336,584	$307,918	$ 28,666
CONTRACT DRILLING EXPENSE			
Fourth-Generation Semisubmersibles	$ 34,717	$ 30,207	$ 4,510
Other Semisubmersibles	129,795	124,090	5,705
Jack-ups	60,798	66,723	(5,925)
Turnkey	30,297	25,957	4,340
Land	17,899	18,240	(341)
Other	1,325	1,581	(256)
Eliminations	(15,271)	(9,879)	(5,392)
Total Contract Drilling Expense	$259,560	$256,919	$ 2,641
OPERATING INCOME (LOSS)			
Fourth-Generation Semisubmersibles	$ 32,676	$ 16,655	$ 16,021
Other Semisubmersibles	38,787	10,212	28,575
Jack-ups	8,031	23,160	(15,129)
Turnkey	(3,176)	(661)	(2,515)
Land	2,027	3,203	(1,176)
Other	(1,321)	(1,570)	249
General and Administrative Expense	(13,857)	(11,993)	(1,864)
Depreciation Expense	(52,865)	(55,366)	2,501
Gain on Sale of Assets	1,349	1,736	(387)
Total Operating Income (Loss)	$ 11,651	$(14,624)	$ 26,275

REVENUES. The $20.5 million increase in revenues from fourth-generation semisubmersibles resulted primarily from increases in dayrates in the North Sea and the Gulf of Mexico. In addition, $3.9 million in revenue for rig enhancements and mobilization fees in excess of mobilization costs was recognized during 1995. These increases were partially offset by a reduction of revenues resulting from the mobilization between markets of two fourth-generation rigs during the first quarter of 1995. The $34.3 million increase in revenues from other semisubmersibles is primarily attributable to increases in dayrates and utilization in both the North Sea and the Gulf of Mexico. In the North Sea, increases in utilization resulted in approximately $13.5 million of additional revenues and increases in dayrates resulted in approximately $4.2 million of additional revenues. In the Gulf of Mexico, increases in utilization resulted in approximately $12.6 million of additional revenues and increases in dayrates resulted in approximately $6.6 million of additional revenues. In addition, the operations of two of three rigs acquired during the second and third quarters of 1994 contributed a $6.0 million increase in other semisubmersible revenue. Also, revenues for rig enhancements of $2.5 million were recognized during 1995. These increases were partially offset by a reduction of revenues resulting from the mobilization between markets of three other semisubmersibles: the Ocean Nomad from South America to the North Sea, the Ocean Princess from Southeast Asia to the North Sea, and the Ocean Baroness from Trinidad to Brazil. The $21.1 million decrease in revenues from jack-ups resulted primarily from lower dayrates as compared to 1994 and a decline in utilization. The decline in utilization in the Gulf of Mexico caused a $5.8 million reduction in revenues, primarily from cold stacking two rigs located in the Gulf of Mexico in mid-1995, both of which were utilized during the prior year. Partially offsetting these decreases was an increase in utilization for two jack-ups which were moved from Venezuela to the Gulf of Mexico during the first half of 1994. Decreases in dayrates in the Gulf of Mexico caused a $14.0 million reduction in revenues for jack-ups. The $1.8 million increase in turnkey revenues resulted from an increase in the number of turnkey wells drilled. Eleven turnkey wells were drilled during the year ended December 31, 1995 as compared to nine wells drilled during the prior year. The $1.5 million decrease in land revenues resulted primarily from a decline in utilization as compared to 1994.

CONTRACT DRILLING EXPENSE. The $4.5 million increase in contract drilling expense for fourth-generation semisubmersibles resulted from improved utilization of the two rigs located in the Gulf of Mexico and increased expenses for the mobilization of two rigs during the first quarter of 1995 to relocate the rigs between the Gulf of Mexico and the North Sea. The $5.7 million increase in contract drilling expense for other semisubmersibles resulted primarily from additional operating costs of $9.4 million associated with the three rigs acquired in 1994, including mobilization costs of $4.0 million. In addition, improved utilization for a rig operating in the North Sea resulted in a $2.3 million increase in operating costs. These increases were partially offset by cost reductions of $5.7 million from the cold stacking of two rigs located in the Gulf of Mexico. One of these semisubmersibles, the Ocean Prospector, was cold stacked in the first quarter and reactivated during the fourth quarter of 1995. The other rig, the Ocean Quest, was cold stacked in the third quarter of 1994 and is currently undergoing significant rig enhancements in preparation for a three-year term contract anticipated to begin in the fourth quarter of 1996. The $5.9 million decrease in contract drilling expense for jack-ups resulted primarily from cost reductions associated with the cold stacking of two rigs in the Gulf of Mexico. The $4.3 million increase in turnkey expense resulted primarily from the increase in the number of turnkey wells drilled and cost overruns on one turnkey well in progress at December 31, 1995, for which an estimated loss of $3.6 million has been recorded.

GENERAL AND ADMINISTRATIVE EXPENSE. General and administrative expense increased $1.9 million in 1995 due to increases in staff and other administrative expenses and the commencement in 1995 of the Diamond Offshore Management Bonus Program, an incentive plan for cash bonuses to selected officers and key employees of Diamond Offshore.

DEPRECIATION EXPENSE. Depreciation expense of $52.9 million for 1995 included a $2.1 million write-down in the carrying value of a semisubmersible, as compared to a $5.5 million write-down on another semisubmersible included in depreciation expense for 1994. Partially offsetting this decrease was an additional $1.2 million of depreciation expense associated with the three rigs acquired during the second and third quarters of 1994.

GAIN ON SALE OF ASSETS. Gain on sale of assets for the year ended December 31, 1995 of $1.3 million resulted from the sale of a semisubmersible which was held for disposition and from sales of miscellaneous assets. Gain on sale of assets for the year ended December 31, 1994 of $1.7 million primarily resulted from the sale of eight land drilling rigs.

INTEREST EXPENSE. Interest expense for the year ended December 31, 1995 decreased $4.2 million to $27.1 million as compared to $31.3 million for the prior year. This decrease resulted from the payment of all of Diamond Offshore's outstanding indebtedness to Loews in connection with the Diamond Offshore Initial Public Offering.

FOREIGN CURRENCY TRANSACTION LOSSES. Foreign currency transaction losses of $.2 million for 1995 decreased $1.1 million from $1.3 million for 1994. This decrease is primarily due to a loss of $.7 million recognized in 1994 for the accumulated translation adjustment upon discontinuance of operations in Venezuela. See "-- Other."

OTHER INCOME (EXPENSE). Other income increased $.9 million to $1.8 million as compared to $.9 million for 1994. This increase is primarily attributable to additional interest income resulting from an increase in average cash balances during 1995.

INCOME TAX BENEFIT. The income tax benefit for the year ended December 31, 1995 decreased $4.8 million to $6.8 million, as compared to $11.6 million for 1994. This decrease resulted primarily from a decrease in Diamond Offshore's net loss before taxes of $32.6 million, as compared to 1994. See Note 8 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

NET LOSS. Net loss for 1995 decreased $27.8 million to $7.0 million, as compared to $34.8 million for 1994. The decrease resulted primarily from an increase in operating income of $26.3 million.

YEARS ENDED DECEMBER 31, 1994 AND 1993

Comparative data relating to Diamond Offshore's revenues and operating expenses by equipment type are listed below (eliminations offset dayrate revenues earned when Diamond Offshore's rigs are utilized in its turnkey operations). Diamond Offshore's drillship, Ocean Clipper I, is included in Other Semisubmersibles for discussion purposes.

	YEAR ENDED DECEMBER 31,		INCREASE/
	1994	1993	(DECREASE)
	(IN THOUSANDS)		
REVENUES			
Fourth-Generation Semisubmersibles	$ 46,862	$ 36,791	$ 10,071
Other Semisubmersibles	134,302	125,979	8,323
Jack-ups	89,883	94,137	(4,254)
Turnkey	25,296	18,038	7,258
Land	21,443	17,770	3,673
Other	11	934	(923)
Eliminations	(9,879)	(5,580)	(4,299)
Total Revenues	$307,918	$288,069	$ 19,849
CONTRACT DRILLING EXPENSE			
Fourth-Generation Semisubmersibles	$ 30,207	$ 25,090	$ 5,117
Other Semisubmersibles	124,090	114,434	9,656
Jack-ups	66,723	61,530	5,193
Turnkey	25,957	16,416	9,541
Land	18,240	15,503	2,737
Other	1,581	818	763
Eliminations	(9,879)	(5,580)	(4,299)
Total Contract Drilling Expense	$256,919	$228,211	$ 28,708
OPERATING INCOME (LOSS)			
Fourth-Generation Semisubmersibles	$ 16,655	$ 11,701	$ 4,954
Other Semisubmersibles	10,212	11,545	(1,333)
Jack-ups	23,160	32,607	(9,447)
Turnkey	(661)	1,622	(2,283)
Land	3,203	2,267	936
Other	(1,570)	116	(1,686)
General and Administrative Expense	(11,993)	(11,785)	(208)
Depreciation Expense	(55,366)	(46,819)	(8,547)
Gain on Sale of Assets	1,736	3,201	(1,465)
Total Operating Income (Loss)	$(14,624)	$ 4,455	$(19,079)

REVENUES. The $10.1 million increase in revenues from fourth-generation semisubmersibles resulted primarily from a $17.8 million increase in revenues from the two rigs located in the Gulf of Mexico during the year ended December 31, 1994, offset by a $7.7 million decrease in revenues from reduced utilization of the rig in the North Sea. The $8.3 million increase in revenues from other semisubmersibles resulted primarily from the operations of two of the three rigs acquired during the second and third quarters of 1994. The $4.3 million decrease in revenues from jack-ups resulted primarily from two rigs that were idle during the first half of 1994. During this period, the rigs were mobilized from Venezuela and refitted for operation in the Gulf of Mexico. The $7.3 million increase in turnkey revenues resulted from an increase in the number of turnkey wells drilled. Nine turnkey wells were drilled during the year ended December 31, 1994 as compared to four wells drilled during the prior year.

CONTRACT DRILLING EXPENSE. The $5.1 million increase in contract drilling expense for fourth-generation semisubmersibles resulted from improved utilization of the two rigs located in the Gulf of Mexico which was partially offset by reduced utilization for the rig located in the North Sea. The $9.7 million increase in contract drilling expense for other semisubmersibles resulted primarily from operating costs of $8.3 million associated with the three rigs acquired during the second and third quarters of 1994 and from an increase in mobilization costs of $2.2 million. These increases were partially offset by cost reductions of $3.7 million from the cold stacking, upon expiration of a term contract, of a rig in South America during the fourth quarter of 1994. The $5.2 million increase in contract drilling expense for jack-ups resulted primarily from increased costs incurred for the mobilization and shipyard maintenance of two rigs moved from Venezuela to the Gulf of Mexico during the first half of 1994. The $9.5 million increase in turnkey expense resulted from the additional number of wells drilled. In addition, cost overruns on one turnkey well resulted in additional expense, beyond that anticipated, of $2.3 million during the year ended December 31, 1994. The $2.7 million increase in contract drilling expense for land drilling operations resulted primarily from an increase in the number of land turnkey wells drilled during the year ended December 31, 1994 as compared to the prior year.

GENERAL AND ADMINISTRATIVE EXPENSE. General and administrative expense of $12.0 million for the year ended December 31, 1994 was relatively unchanged from the $11.8 million incurred during the prior year.

DEPRECIATION EXPENSE. Depreciation expense increased $8.5 million over the prior year, primarily as a result of Diamond Offshore's decision to decrease the carrying value of one of its other semisubmersible rigs by $5.5 million. In addition, depreciation expense increased $1.2 million associated with the acquisition of three rigs in the second and third quarters of 1994 and $1.1 million from the full year recognition of depreciation expense in 1994 associated with the acquisition of the remaining interest in a fourth-generation semisubmersible in March 1993.

GAIN ON SALE OF ASSETS. Gain on sale of assets for the year ended December 31, 1994 of $1.7 million primarily resulted from the sale of eight land drilling rigs. Gain on sale of assets for the year ended December 31, 1993 of $3.2 million primarily resulted from the sale of Diamond Offshore's three platform rigs.

INTEREST EXPENSE. Interest expense for the year ended December 31, 1994 increased $5.4 million to $31.3 million as compared to $25.9 million for the prior year. Interest expense consisted only of interest on notes payable to Loews. During 1994, notes payable to Loews increased $41.3 million due to $25.0 million of additional borrowings to finance the acquisition of three semisubmersibles purchased during the second and third quarters of 1994 and due to $31.3 million for interest accrued on notes payable to Loews.

FOREIGN CURRENCY TRANSACTION LOSSES. Foreign currency transaction losses of $1.3 million for the year ended December 31, 1994 were relatively unchanged from $1.5 million for the prior year.

OTHER INCOME (EXPENSE). Other income of $.9 million for the year ended December 31, 1994 was relatively unchanged from $1.3 million for the prior year.

INCOME TAX BENEFIT. The income tax benefit for the year ended December 31, 1994 increased $6.6 million to $11.6 million, as compared to $5.0 million for the prior year. This increase resulted primarily from the increase in Diamond Offshore's net loss before taxes from $21.7 million for the year ended December 31, 1993 to $46.4 million for the year ended December 31, 1994.

NET LOSS. Net loss for the year ended December 31, 1994 increased $18.2 million to $34.8 million, as compared to $16.6 million for the prior year. The increase resulted primarily from a decrease of $19.1 million in operating income and an increase of $5.4 million in interest expense. The increase in net loss was partially offset by an increase of $6.6 million in income tax benefit, as compared to the prior year.

OUTLOOK

The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances, including 3-D seismic, horizontal drilling, and subsea completion procedures. Both the Gulf of Mexico and the North Sea semisubmersible markets have experienced increased utilization and significantly higher dayrates in 1995 and 1996, and customers increasingly are seeking to contract rigs serving those markets under term contracts (as opposed to contracts let on a single well or well-to-well basis). In the Gulf of Mexico, the Ocean Valiant's contract has been extended through 1996 at an increased dayrate. Contracts for Diamond Offshore's other semisubmersibles in the Gulf of Mexico continue to be primarily on a well-to-well or multi-well basis. However, one rig has received a contract extension on a long-term basis through January 1998. Diamond Offshore's drillship, the Ocean Clipper I, is scheduled to be upgraded during 1996 and 1997 to operate in the ultra-deep water market of the Gulf of Mexico with dynamic positioning capabilities and other features, in connection with a four-year term contract with a major oil company that has been agreed to in principle. Also, as part of this trend, Diamond Offshore entered into a contract and a letter of intent with two major oil companies for the Ocean Quest and Ocean Star (formerly named Ocean Countess), respectively, to conduct deep water drilling operations in the Gulf of Mexico under three-year term contracts, in connection with which Diamond Offshore will significantly enhance these rigs. See "-- Capital Resources."

In the North Sea, the Ocean Alliance is contracted for work through late 1996 and has received an increase in its dayrate. Diamond Offshore's three other marketed semisubmersibles in the North Sea are all committed under long-term contracts. The Ocean Nomad, which was relocated from South America, began its two-year contract in late November 1995. The Ocean Princess has completed the modifications necessary for its two-year contract which commenced in late March 1996. The Ocean Guardian is currently drilling pursuant to a one-year term contract expiring during the third quarter of 1996. Of the remaining semisubmersibles in Diamond Offshore's fleet, the Ocean Baroness has a three-year term contract for drilling offshore Brazil through the first quarter of 1999. In addition, the Arethusa Yatzy and Ocean Zephyr, also operating offshore Brazil, are contracted to November 1998 and July 1997, respectively.

The market for jack-up rigs in the Gulf of Mexico, which weakened during 1994, appears to have stabilized and has shown some signs of strengthening in recent months. Dayrates have improved from those earned in early 1995; however, volatile natural gas prices and an oversupply of rigs prevented significant improvements through the end of 1995. Two of Diamond Offshore's jack-up rigs are committed through the first quarter of 1997, one drilling offshore Indonesia and the other in the Dutch sector of the North Sea.

Historically, the offshore contract drilling market has been highly competitive and cyclical, and Diamond Offshore cannot predict the extent to which current conditions will continue.

LIQUIDITY

Net cash provided by operating activities for the year ended December 31, 1995 increased by $10.2 million to $52.8 million, as compared to $42.6 million for the prior year. This increase was attributable to a $27.8 million decrease in net loss from 1994, partially offset by an increase of $16.7 million in accounts receivable in 1995, as compared to a decrease in accounts receivable of $4.5 million for the prior year. Cash used in investing activities increased $21.7 million primarily due to construction work in progress of $19.0 million for rig upgrades in 1995. Cash provided by financing activities for 1995 decreased due to repayment of Diamond Offshore's notes payable to Loews in conjunction with the Diamond Offshore Initial Public Offering.

Diamond Offshore's principal sources of funds have been cash flow from operations and borrowings on notes payable to Loews. Upon completion of the Diamond Offshore Initial Public Offering, Diamond Offshore used a portion of the net proceeds to repay such notes in full. The remainder of the proceeds was used to pay Loews a special dividend of $2.1 million. See Note 2 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

Diamond Offshore uses funds available under the Diamond Offshore Bank Credit Facility, together with cash flow from operations, to fund its capital expenditure and working capital requirements. The Diamond Offshore Bank Credit Facility is a revolving line of credit for a five-year term providing a maximum credit commitment of $150.0 million until the second anniversary, at which time and at the end of each six-month period thereafter, the commitment will decrease by $12.5 million to a final maximum credit commitment of $75.0 million during the last six months. Borrowings will bear interest, at Diamond Offshore's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. Diamond Offshore is required to pay a commitment fee of .375% on the unused available portion of the maximum credit commitment. Borrowings are secured by a first priority security interest in five semisubmersible drilling rigs, including Diamond Offshore's three fourth-generation rigs, a pledge of 65% of the capital stock of Diamond Offshore Limited, which owns the Ocean Alliance, and certain subsidiary guarantees. Under the Diamond Offshore Bank Credit Facility, Diamond Offshore is required to maintain a ratio of consolidated EBITDA (as defined) to consolidated interest expense of at least 2.50:1.00 and a ratio of consolidated indebtedness (including borrowings under such facility) to total capitalization (equal to the sum of such indebtedness plus consolidated net worth) of no more than 0.40:1.00. Diamond Offshore is also required to maintain a positive working capital balance. In addition, the agreement has covenants that limit aggregate capital expenditures, dividends and similar payments. See "Dividend Policy."

It is anticipated that the Diamond Offshore Bank Credit Facility will be used primarily to fund rig upgrades and similar capital expenditure requirements. In management's opinion, Diamond Offshore's cash generated from operations and borrowings available under the Diamond Offshore Bank Credit Facility are sufficient to meet its anticipated short and long-term liquidity needs, including its capital expenditure and debt service requirements.

CAPITAL RESOURCES

Cash requirements for capital commitments result from rig upgrades to meet specific customer requirements and from Diamond Offshore's continuing rig enhancement program, including top-drive drilling system installations and water depth and drilling capability upgrades. Diamond Offshore expects to spend approximately $208.1 million, including interest expense to be capitalized, during 1996 for significant rig upgrades in connection with contract requirements. Included in this amount is approximately $55.8 million for 1996 expenditures in conjunction with the scheduled upgrade of the Ocean Clipper I to operate in ultra-deep water with dynamic positioning capabilities and other features. In addition, approximately $124.7 million is included for the upgrades relating to the letter of intent and the contract for the Ocean Star (formerly named Ocean Countess) and Ocean Quest, respectively. Also included in this amount is approximately $10.0 million to upgrade the Arethusa Neptune to work in 3,000 feet of water. Because these projects are expected to be accompanied by term contracts at favorable dayrates, the expenditures are, in Diamond Offshore's opinion, financially justified. Diamond Offshore expects to evaluate other projects as opportunities arise. In addition, Diamond Offshore has budgeted $47.4 million for 1996 capital expenditures associated with its continuing rig enhancement program. It is management's opinion that significant improvements in operating cash flow resulting from current conditions of improved dayrates and the increasing number of term contracts for rigs in certain markets, in conjunction with borrowings under the Diamond Offshore Bank Credit Facility, will be sufficient to meet these capital requirements.

In connection with the Acquisition, Diamond Offshore assumed Arethusa's obligations with respect to approximately $69.2 million of secured indebtedness at December 31, 1995, which was outstanding under two separate facilities. In December 1994 Arethusa refinanced its then existing secured debt of $66.1 million with a new $80.0 million loan facility. See Note 6 to Arethusa's Consolidated Financial Statements included elsewhere herein. This loan facility was subsequently paid down by $38.9 million to $41.1 million at December 31, 1995. Currently, quarterly payments on this facility total $6.8 million per annum with a

December 1999 balloon payment of $15.4 million. Additionally, in connection with the acquisition of the Arethusa Yatzy (see Notes 4 and 6 to Arethusa's Consolidated Financial Statements included elsewhere herein), Arethusa drew upon a $30.0 million loan facility. Semi-annual payments totaling $3.8 million per annum are due under this facility, which brings total current maturities under these facilities to $10.6 million as of December 31, 1995. In management's view, cash generated from operations and borrowings available under the Diamond Offshore Bank Credit Facility will be sufficient to meet Diamond Offshore's debt service obligations under these facilities.

Diamond Offshore is analyzing financing alternatives that may be available to it in the public or private capital markets. Proceeds of any such financing transactions may be used for repayment of higher cost debt, to fund rig upgrades or acquisitions or for other corporate purposes. Diamond Offshore's ability to effect any such financings will be dependent on its historical results of operations and its current financial condition and prospects at the time it seeks access to the capital markets, and to other factors beyond Diamond Offshore's control, including the prevailing interest rate environment and, with respect to offerings of common or preferred stock or debt obligations convertible into such common stock, other financial market conditions, and the investment community's perception of Diamond Offshore and the offshore contract drilling industry generally. Any such offering would be subject to the restrictions imposed by the Shareholders Agreement on public sales or distributions of Diamond Offshore Common Stock, or securities convertible into common stock, and until October 10, 1996, to obtaining the prior written consent of CS First Boston as required by the underwriting agreement entered into in connection with the Diamond Offshore Initial Public Offering.

Also, from time to time Diamond Offshore reviews acquisition opportunities such as that presented by Arethusa, although Diamond Offshore has no current plans to purchase or otherwise acquire additional rigs.

OTHER

Certain of Diamond Offshore's subsidiaries use the local currency in the country where they conduct operations as their functional currency. Currency environments in which Diamond Offshore has material business operations include the United Kingdom, Australia and Brazil. Diamond Offshore generally attempts to minimize its currency exchange risk by seeking international contracts payable in local currency in amounts equal to Diamond Offshore's estimated operating costs payable in local currency and in U.S. dollars for the balance of the contract. Because of this strategy, Diamond Offshore in the past has minimized its unhedged net asset or liability positions denominated in local currencies and has not experienced significant gains or losses associated with changes in currency exchange rates. However, at present contracts covering three of Diamond Offshore's four rigs operating in the United Kingdom sector of the North Sea are payable in U.S. dollars. Diamond Offshore has not hedged its exposure to changes in the exchange rate between U.S. dollars and pounds sterling for operating costs payable in pounds sterling, although it may seek to do so in the future.

Currency translation adjustments are accumulated in a separate section of stockholders' equity. However, when Diamond Offshore ceases its operations in a currency environment, the accumulated adjustments are recognized currently in results of operations. During 1994, Diamond Offshore recognized a loss of $.7 million for the accumulated translation adjustment upon discontinuance of operations in Venezuela. Additionally, translation gains and losses for Diamond Offshore's operations in Brazil have been recognized currently due to the hyperinflationary status of this environment. The effect on results of operations has not been material and is not expected to have a significant effect in the future due to the recent stabilization of currency rates in Brazil.

In February 1996, Diamond Offshore purchased for approximately $8.2 million the eight-story building containing approximately 182,000 net rentable square feet on approximately 6.2 acres in which it had leased office space for its corporate headquarters. A portion of the building is currently occupied by other tenants under leases which expire through 2005. This purchase will reduce general and administrative expenses in the future by eliminating rent expense and will provide rental income from the leases, offset by depreciation and related interest expense. Diamond Offshore does not expect this purchase to have a material effect on its results of operations.

BUSINESS

GENERAL

Diamond Offshore engages principally in the contract drilling of offshore oil and gas wells. Diamond Offshore's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Asia and consists of 30 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 19 jack-up rigs and one drillship. Diamond Offshore also operates 10 land rigs deployed in South Texas. All of Diamond Offshore's offshore and land rigs are wholly owned except for two jack-up rigs operated pursuant to bareboat charters.

Diamond Offshore is a Delaware corporation with its principal executive offices located at 15415 Katy Freeway, Suite 400, Houston, Texas 77094, where its telephone number is (713) 492-5300.

BUSINESS STRATEGY

Diamond Offshore seeks to maximize dayrates and rig utilization by continuously adapting to changes in its markets, improving the capabilities of its drilling rigs and increasing the quality of its service. The key elements of its strategy are to:

- Market worldwide its large, diverse fleet, which is capable of satisfying customer requirements in a variety of applications;

- Continue to enhance its fleet to meet customer demand for diverse drilling capabilities, including those required for deep water and harsh environment operations;

- Exploit the potential of Diamond Offshore's nine Victory-class semisubmersible rigs by pursuing projects that take advantage of this rig type's unique design to yield significantly enhanced rigs; and

- Maintain a program of continuous improvement of quality and safety through Diamond Offshore's Global Excellence Management System and further capitalize on customer recognition of Diamond Offshore's quality and safety achievements.

INDUSTRY CONDITIONS

Diamond Offshore's business and operations depend principally upon the condition of the oil and gas industry and, specifically, the exploration and production expenditures of oil and gas companies. Historically, the offshore contract drilling industry has been highly competitive and cyclical, with periods of high demand, short rig supply and high dayrates followed by periods of low demand, excess rig supply and low dayrates. The offshore contract drilling business is influenced by a number of factors, including the current and anticipated prices of oil and natural gas, the expenditures by oil and gas companies for exploration and production and the availability of drilling rigs. For a number of years, depressed oil and natural gas prices and an oversupply of rigs have adversely affected the offshore drilling market, particularly in the Gulf of Mexico, where the prolonged weakness and uncertainty in the demand for and price of natural gas resulted in a significant decline in exploration and production activities. Demand for drilling services outside the United States, excluding the North Sea, has been less volatile in recent years, but remains dependent on a variety of political and economic factors beyond Diamond Offshore's control, including worldwide demand for oil and natural gas, the ability of OPEC to set and maintain production levels and pricing, the level of production of non-OPEC countries and the policies of the various governments regarding exploration and development of their oil and natural gas reserves.

The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances that have broadened opportunities for offshore exploration and development. Both the Gulf of Mexico and the North Sea semisubmersible markets experienced increased utilization and significantly higher dayrates in 1995 and 1996, and customers increasingly are seeking to contract for rigs serving these markets for a stated term (as opposed to contracts for the drilling of a single well or a group of wells). The market for jack-up rigs in the Gulf of Mexico, which weakened during 1994, appears to have stabilized during 1995 and has shown some signs of strengthening in recent months. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Outlook."

COMPETITION

The contract drilling industry is highly competitive. Customers often award contracts on a competitive bid basis, and although a customer selecting a rig may consider, among other things, a contractor's safety record, crew quality and quality of service and equipment, the oversupply of rigs has created an intensely competitive market in which price is the primary factor in determining the selection of a drilling contractor. Diamond Offshore believes that competition for drilling contracts will continue to be intense for the foreseeable future because of the worldwide oversupply of drilling rigs and the ability of contractors to move rigs from areas of low utilization and dayrates to areas of greater activity and relatively higher dayrates. In addition, there are inactive non-marketed rigs or rigs being operated in non-drilling activities that could be reactivated to meet an increase in demand for drilling rigs in any given market. Such movement or reactivation or a decrease in drilling activity in any major market could depress dayrates and could adversely affect utilization of Diamond Offshore's rigs. See "-- Offshore Contract Drilling Services."

THE ACQUISITION

BACKGROUND. In September 1995 Arethusa publicly announced that it was exploring strategic alternatives to maximize shareholder value, including a possible sale of Arethusa. Following completion of the Diamond Offshore Initial Public Offering, Diamond Offshore commenced an investigation of Arethusa and in November 1995 submitted a formal indication of interest in acquiring Arethusa, which was rejected. However, further discussions transpired that led to execution of a letter of intent on December 7, 1995 pursuant to which Diamond Offshore and Arethusa agreed to work together on an exclusive basis in an effort to agree on the terms of the definitive documentation for the Acquisition. Subsequent negotiations among representatives of Arethusa, Alphee, Ratos, Diamond Offshore and Loews took place in numerous meetings, telephone conversations and correspondence, following which the definitive documentation for the Acquisition was executed on February 9, 1996.

Diamond Offshore elected to proceed with the Acquisition principally because it viewed the Acquisition as a means of expanding its geographic areas of operation and the size of its semisubmersible fleet, including the addition of some units that may be suitable for upgrading. In addition, Diamond Offshore expects that the increase in the number of publicly traded shares of Diamond Offshore Common Stock resulting from the Acquisition, and the anticipated consequential increase in Diamond Offshore's market capitalization, will heighten trading volume and institutional interest in Diamond Offshore's securities, which should ultimately benefit all Diamond Offshore stockholders.

THE AMALGAMATION. Pursuant to the Plan of Acquisition and the Amalgamation Agreement, at the Effective Time, (1) Arethusa and Acquisition Sub have amalgamated and will continue their businesses as one amalgamated company under the name "Diamond Offshore Exploration (Bermuda) Limited," a wholly owned subsidiary of Diamond Offshore (USA), (2) each issued and outstanding share of Arethusa Common Stock (other than any such shares held by Diamond Offshore, Diamond Offshore (USA) or Acquisition Sub) was canceled and ceased to exist and each holder thereof became entitled to receive in consideration of each share so canceled 0.88 shares of Diamond Offshore Common Stock (the "Amalgamation Ratio") and (3) each share of Arethusa Common Stock held by Diamond Offshore, Diamond Offshore (USA) or Acquisition Sub (other than any such shares held in a fiduciary capacity or in satisfaction of a debt previously contracted) was canceled, retired and ceased to exist, and no payment of Diamond Offshore Common Stock was or will be made in respect thereof. Each certificate that immediately prior to the Effective Time represented a share or shares of Arethusa Common Stock now represents the right to receive, upon surrender of such certificate as provided in the Amalgamation Agreement and subject to the provisions set forth therein governing fractional shares, that number of shares of Diamond Offshore Common Stock determined by multiplying the number of shares of Arethusa Common Stock formerly represented by such certificate by the Amalgamation Ratio. From and after the Effective Time, the holders of certificates previously representing shares of Arethusa Common Stock ceased to have any other rights except as otherwise provided in the Amalgamation Agreement or by law.

MEMORANDUM OF ASSOCIATION; BYE-LAWS; DIRECTORS; OFFICERS. Under the Amalgamation Agreement, (1) at the Effective Time, the Memorandum of Association of Arethusa, as in effect immediately prior to the Effective Time, became the Memorandum of Association of Diamond Offshore Exploration (Bermuda), (2) the Bye-laws of Arethusa, as in effect immediately prior to the Effective Time, became the Bye-laws of Diamond Offshore Exploration (Bermuda), (3) the directors of Acquisition Sub immediately prior to the Effective Time became the directors of Diamond Offshore Exploration (Bermuda), each to hold office in accordance with the Memorandum of Association and Bye-laws of Diamond Offshore Exploration (Bermuda) until their respective successors are duly elected or appointed and qualified, and (4) the officers of Acquisition Sub immediately prior to the Effective Time became the officers of Diamond Offshore Exploration (Bermuda), each to hold office in accordance with the Bye-laws of Diamond Offshore Exploration (Bermuda) until their respective successors are duly elected or appointed and qualified.

CONTINUING ARETHUSA SEVERANCE, CONSULTING AND SALARY CONTINUATION PLANS. Under the Plan of Acquisition, from and after the Effective Time, Diamond Offshore will honor in accordance with their terms the following Arethusa employment, severance, consulting and salary continuation plans: (1) the Employment Agreement between Arethusa and Jan Rask, as amended (the "Rask Employment Agreement"), (2) the Severance Agreement between Arethusa Off-Shore Company, Arethusa's principal operating subsidiary ("AOC"), and O. Peter Blom, (3) the Severance Agreement between AOC and Vincent G. Bounds, (4) the Severance Agreement between AOC and Harris I. Knecht, (5) the Severance Agreement between AOC and Danny R. Richardson, (6) the Severance Agreement between AOC and James E. Traber, Jr., (7) the Severance Agreement between AOC and Charles R. Richter, (8) the AOC Severance Policy for all AOC shore-based employees, (9) the Arethusa 1993 Employee Stock Option Plan and (10) the Arethusa 1994 Nonqualified Stock Option Plan for Non-Employee Directors. To the extent permitted or required under applicable law, each employee of Arethusa or its subsidiaries will be given credit for all service with Arethusa or its subsidiaries (or service credited by Arethusa or its subsidiaries) under all employee benefit plans maintained by Arethusa, Diamond Offshore, Diamond Offshore (USA) or Acquisition Sub in which they participate or in which they become participants for purposes of eligibility and vesting.

In October 1994, Arethusa entered into the Rask Employment Agreement with Jan Rask. The Rask Employment Agreement provides for a current annual salary of $325,000. In addition, the Rask Employment Agreement provides that Arethusa will pay Mr. Rask bonus compensation as may from time to time be awarded by the Board of Directors of Arethusa and that Mr. Rask is entitled to participate in all employee benefit plans and other compensatory arrangements sponsored by Arethusa. The Rask Employment Agreement may be terminated by either party upon 180 days' prior written notice and by Arethusa at any time for "cause" (as therein defined). The Rask Employment Agreement provides that until December 31, 1996, Mr. Rask will agree to assist in the pursuit of certain types of business combinations and that Mr. Rask will receive a payment upon completion of any such transaction. As a result of the consummation of the Acquisition, Mr. Rask became entitled to a payment of $487,500 pursuant to the Rask Employment Agreement, $81,250 of which was previously paid.

In October 1995, AOC entered into Executive Severance Agreements (the "Arethusa Severance Agreements") with Messrs. Blom, Bounds, Knecht, Traber, Richardson and Richter. The Arethusa Severance Agreements provide that these executive officers will assist with activities arising in connection with proposed business combinations and provide for certain benefits if any of these executive officers are terminated or their employment is materially changed within 2.5 years following a merger, sale or change of control, where the change of control is to a competing drilling contractor, and the termination or change is either (a) by the ongoing company for reasons other than for cause or as a consequence of the executive's death, permanent disability or retirement, or (b) by the executive if the executive is not offered continued employment in an equivalent officer-level position in the Houston area, a compensation program at least equal to such executive's compensation (excluding bonus) immediately prior to such merger, sale or change of control and a comparable fringe benefit program. In such event, such executive officers will receive a lump sum cash payment equal to 30 times such executive's monthly base salary, outplacement consulting assistance and earned and accrued vacation. The consummation of the Acquisition results in such payments becoming due to each of such executive officers.

Under the Plan of Acquisition, following the Effective Time, except with respect to any collective bargaining agreements, Diamond Offshore or its subsidiaries will cause the employees of Arethusa and its subsidiaries to receive compensation, benefits, fringe benefits, plans, programs and arrangements that are no less favorable in the aggregate than the lesser of such compensation, benefits, fringe benefits, plans, programs and arrangements to which (1) such employees are entitled immediately prior the Effective Time or (2) similarly situated employees of Diamond Offshore are entitled. With respect to any welfare plan maintained by Arethusa or its subsidiaries or Diamond Offshore in which employees or former employees of Arethusa or its subsidiaries (or their dependents) participate after the Effective Time, Diamond Offshore will waive or cause to be waived any preexisting condition provision (except for preexisting conditions of any employee or former employee (or dependent) that are currently excluded under existing Arethusa welfare plans in which such employee or former employee (or dependent) currently participates) and each employee or former employee and his dependents will be given credit for any claims incurred prior to the Effective Time toward any applicable deductible under any such welfare plan.

All members of Arethusa's Board of Directors resigned at the Effective Time.

ARETHUSA STOCK OPTION PLANS. Pursuant to the Amalgamation Agreement, at the Effective Time, each outstanding option to purchase shares of Arethusa Common Stock under Arethusa's 1993 Employee Stock Option Plan (the "Arethusa Employee Plan") and Arethusa's 1994 Nonqualified Stock Option Plan for Non-Employee Directors (the "Arethusa Director Plan" and, together with the Arethusa Employee Plan, the "Arethusa Stock Option Plans"), whether or not then vested or exercisable (the "Arethusa Options") was assumed by Diamond Offshore. See "Management -- Stock Option Plans."

INDEMNIFICATION. Diamond Offshore, Diamond Offshore (USA) and Acquisition Sub agreed in the Plan of Acquisition that all rights to indemnification existing in favor of the present or former directors, officers and employees (as such) of Arethusa or any of its subsidiaries, as provided in Arethusa's Memorandum of Association or Bye-laws or similar documents of any of such subsidiaries, or any agreement to which Arethusa or any such subsidiary is a party as in effect at February 9, 1996 with respect to matters occurring prior to the Effective Time would survive the Amalgamation, and Diamond Offshore agreed to cause Diamond Offshore Exploration (Bermuda) to comply fully with Arethusa's obligations thereunder. In addition, from and after the Effective Time, in the Plan of Acquisition Diamond Offshore agreed to, and agreed to cause Diamond Offshore Exploration (Bermuda) to, indemnify, defend and hold harmless the present directors and officers of Arethusa against any costs and expenses (including reasonable attorneys' fees), judgments, fines, losses, claims, damages and liabilities, and amounts paid in settlement thereof with Diamond Offshore's consent, in connection with any claim, action, suit, proceeding or investigation relating to any of the transactions contemplated by the Plan of Acquisition, the Amalgamation Agreement or the Fee Agreement.

RIGHTS OF DISSENTING SHAREHOLDERS. After the Effective Time, shares of Arethusa Common Stock that were issued and outstanding immediately prior to the Effective Time held by Arethusa shareholders who did not vote in favor of the adoption and approval of the Amalgamation Agreement and who comply with Section 106(6), (6A), (6B) and (6C) of The Companies Act 1981 of Bermuda, as amended ("The Companies Act") will, at the election of Diamond Offshore (USA), either (1) be canceled and shares of Diamond Offshore Common Stock delivered in consideration thereof, subject to the rights of such shareholders under Section 106(6), (6A), (6B) and (6C) of The Companies Act, or (2) not be canceled and the holders thereof not be entitled to receive shares of Diamond Offshore Common Stock unless and until such holders have failed to perfect or have effectively withdrawn or lost their rights to appraisal under The Companies Act, whereupon such shares will be canceled and shares of Diamond Offshore Common Stock delivered in consideration thereof. Diamond Offshore has not elected whether to proceed with respect to any such shares under (1) or (2) as described in the preceding sentence above.

ACCOUNTING TREATMENT. The Acquisition will be accounted for using the purchase method of accounting pursuant to Opinion No. 16 of the Accounting Principles Board. The purchase method accounts for a business combination as the acquisition of one company by another. The acquiring corporation, Diamond Offshore, records assets less liabilities assumed. A difference between the cost of the acquired corporation, Arethusa, and the sum of the fair values of tangible and identifiable intangible assets less liabilities is recorded as goodwill. The reported income of Diamond Offshore after the Effective Time will include the operations of Arethusa after consummation of the Acquisition.

THE FLEET

Diamond Offshore's large, diverse fleet, which includes some of the most technologically advanced rigs in the world, enables it to offer a broad range of services worldwide in various markets, including the deep water market, the harsh environment market (such as the North Sea), the conventional semisubmersible market and the jack-up market.

SEMISUBMERSIBLES. Diamond Offshore owns and operates 30 semisubmersibles. Semisubmersible rigs consist of an upper working and living deck resting on vertical columns connected to lower hull members. Such rigs operate in a "semi-submerged" position, remaining afloat, off bottom, in a position in which the lower hull is from about 55 to 90 feet below the water line and the upper deck protrudes well above the surface. The rig is typically anchored in position and remains stable for drilling in the semi-submerged floating position due in part to its wave transparency characteristics at the water line.

Diamond Offshore owns and operates three of the world's 13 fourth-generation semisubmersibles. Fourth-generation semisubmersibles are larger than other semisubmersibles, are capable of working in harsh environments and have other advanced features. Diamond Offshore's existing fleet of three fourth-generation semisubmersibles are all capable of operating in water depths of up to 5,000 feet. Currently the Ocean Valiant and the Ocean America are located in deep water areas of the Gulf of Mexico and the Ocean Alliance is located in the harsh environment of the North Sea market west of the Shetland Islands. At present, nine of the world's fourth-generation semisubmersibles are contracted for service in the harsh environment North Sea market and four are operating in the deep water Gulf of Mexico market.

In addition to its fourth-generation semisubmersibles, Diamond Offshore owns and operates 27 other semisubmersibles (including nine Victory-class rigs), 18 of which operate in maximum water depths of between 1,000 to 2,500 feet, and three of which are capable of drilling in 3,000 feet or more of water. The diverse capabilities of most of these semisubmersibles enable them to work in both shallow and deep water environments in the United States and most markets outside the United States. Currently, 15 of these semisubmersibles are located in the Gulf of Mexico; four are located in the North Sea; four are located offshore Brazil; two are located offshore Australia; one is located offshore Nigeria; and one is located offshore Vietnam. In addition to these 27 semisubmersibles, Diamond Offshore owns one other semisubmersible held for disposition.

JACK-UPS. Diamond Offshore owns and/or operates a total of 19 jack-up rigs. Jack-up rigs are mobile, self-elevating drilling platforms equipped with legs that are lowered to the ocean floor until a foundation is established to support the drilling platform. The rig hull includes the drilling rig, jacking system, crew quarters, loading and unloading facilities, storage areas for bulk and liquid materials, heliport and other related equipment. Jack-ups are used extensively for drilling in water depths from 20 feet to 350 feet. The water depth limit of a particular rig is principally determined by the length of the rig's legs. A jack-up rig is towed by tugboats to the drillsite with its hull riding in the sea as a vessel with its legs retracted. Once over a drillsite, the legs are lowered until they rest on the seabed and jacking continues until the hull is elevated above the surface of the water. After completion of drilling operations, the hull is lowered until it rests in the water and then the legs are retracted for relocation to another drillsite.

The principal market for Diamond Offshore's jack-up rigs is currently the Gulf of Mexico, where 14 of Diamond Offshore's jack-up rigs are located. Of Diamond Offshore's jack-up rigs in the Gulf of Mexico, seven are independent-leg cantilevered rigs, two are mat-supported cantilevered rigs, two are independent-leg slot rigs, two are mat-supported slot rigs and one is an independent-leg slot rig that has been modified with skid-off capability. One of Diamond Offshore's jack-up rigs in the Gulf of Mexico is operated pursuant to a bareboat charter and the other 13 are wholly owned by Diamond Offshore. Diamond Offshore also owns and operates one jack-up rig offshore each of Indonesia, Egypt and The Netherlands, and Diamond Offshore operates one jack-up rig offshore India pursuant to a bareboat charter. One of Diamond Offshore's jack-ups is cold stacked in Chile. The jack-up located in the Gulf of Mexico that Diamond Offshore bareboat charters is also under contract for sale, upon closing of which such charter will terminate.

DRILLSHIP. Drillships, which are typically self-propelled, are positioned over a drillsite through the use of either an anchoring system or a computer controlled thruster (dynamic positioning) system similar to those used on certain semisubmersible rigs. Drillships normally require water depth of at least 200 feet in order to conduct operations. Diamond Offshore's drillship, the Ocean Clipper I, which uses a conventional anchoring system, is currently located offshore Africa. The Ocean Clipper I currently has water depth capability of 1,200 feet and variable deck load capacity in excess of 11,000 tons. However, the Ocean Clipper I is scheduled to be upgraded during the year 1996 through the first half of 1997 to operate in the ultra-deep water market of the Gulf of Mexico with dynamic positioning capabilities, 15,000 psi blowout preventers, three mud pumps and other refurbishments and upgrades. The drillship is anticipated to commence operation in the Gulf of Mexico following completion of the upgrade in the second quarter of 1997 pursuant to a four-year term contract with a major oil company that has been agreed to in principle. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Capital Resources."

FLEET ENHANCEMENTS. Diamond Offshore's strategy is to maximize dayrates and utilization by adapting to trends in its markets, including enhancing its fleet to meet customer demand for diverse drilling capabilities. Many of Diamond Offshore's rigs have been upgraded during the last five years with enhancements such as top-drive drilling systems, increases in water depth capability, mud pump additions or increases in deck load capacity. For example, Diamond Offshore upgraded the semisubmersible Ocean Voyager to operate in maximum water depths of 3,200 feet and has modified the semisubmersible Ocean Nomad to allow it to be certified for service in the United Kingdom sector of the North Sea, where it is operating under a two-year contract at improved dayrates. Diamond Offshore converted three of its 300-foot cantilever jack-up rigs from slot rigs, which Diamond Offshore believes has resulted in these rigs achieving higher dayrates and utilization. Also, Diamond Offshore has added top-drive drilling systems to many rigs, so that 36 rigs in Diamond Offshore's fleet are now so equipped.

Notwithstanding the average age of the Diamond Offshore fleet of 17.7 years (calculated as of December 31, 1995 and measured from year built), Diamond Offshore believes that it will be feasible to continue to upgrade its fleet, particularly its Victory-class semisubmersible rigs. The design of the Victory-class semisubmersible rigs, including their cruciform hull configurations, long fatigue-life and advantageous stress characteristics, makes this class of rig particularly well-suited for significant upgrading projects. Currently, Diamond Offshore's Victory-class rigs are outfitted for service in maximum water depths of 600 to 3,200 feet. Five of Diamond Offshore's nine Victory-class rigs are equipped with top-drive drilling systems, two are modified for increased efficiency in the handling of subsea completion equipment and one has stability enhancements that allow increased variable deck load. In management's opinion, it is unlikely that new semisubmersibles will be built unless there is a substantial and sustained improvement in the market; therefore, Diamond Offshore believes that the relative ease and efficiency with which it can significantly enhance its Victory-class rigs is a competitive advantage in a market requiring increasing capability from offshore drilling rigs.

The Ocean Quest, one of Diamond Offshore's Victory-class rigs, is currently undergoing an upgrade pursuant to a contract with a major oil company for a three-year commitment. The rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 3,500 feet. This project includes enhancements to provide additional hull buoyancy, which will allow a variable deck load exceeding 5,000 tons, the addition of a new self-contained chain/wire mooring system, and drilling system upgrades, including the installation of a top-drive drilling system, a 15,000 psi blowout prevention system, a third mud pump and 2,900 barrel liquid mud capacity. The Ocean Quest is scheduled to be placed in service in the fourth quarter of 1996. In addition, during the third quarter of 1995 Diamond Offshore entered into a letter of intent with another major oil company for a three-year commitment for a second Victory-class rig, the Ocean Star (formerly named Ocean Countess), pursuant to which the rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 4,500 feet. The upgrade project for the Ocean Star also includes stability enhancements, the installation of a new mooring system and drilling system upgrades similar to those planned for the Ocean Quest. The Ocean Star is scheduled to be placed in service late in the fourth quarter of 1996. Following the upgrades, Diamond Offshore believes that these rigs will be able to compete effectively in the fourth-generation deep water market.

Additional Victory-class upgrade potential exists, including conceptual plans Diamond Offshore is developing for the possible construction of an ultra-large semisubmersible, the Ocean Legend. The Ocean Legend is intended to take advantage of the cruciform design of the Victory-class semisubmersibles to "square off" the rig by adding large corner columns and other new equipment to yield a rig with capabilities beyond a traditional fourth-generation unit at a significantly reduced cost as compared to new construction. Diamond Offshore has completed its feasibility studies and has begun preliminary design engineering in connection with the upgrade. See Note 1 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein. Although Diamond Offshore is proposing the design to several major oil companies, there can be no assurance that the Ocean Legend can be built in a cost-effective manner, that if a Victory-class rig is so upgraded, there will be adequate demand for its services, or that competitors will not achieve capability beyond that of fourth-generation semisubmersibles through other means attractive to customers.

For the year ended December 31, 1995, Diamond Offshore spent approximately $.6 million on conceptual design studies and related costs associated with the Ocean Legend project. Diamond Offshore expects to evaluate other projects as opportunities arise. Once a capital project is undertaken by Diamond Offshore, Diamond Offshore may later determine that completion of such project is infeasible based on its analysis of factors such as design criteria, anticipated costs of construction, market demand and availability of financing, and Diamond Offshore may be unable to recoup the expenditures made before such project is abandoned. In addition, to the extent Diamond Offshore determines that its fleet cannot be upgraded as it currently anticipates, Diamond Offshore will have fewer rigs available to compete in the harsh environment and deep water markets than if such upgrades had been successfully implemented.

More detailed information as of March 28, 1996 concerning the Diamond Offshore fleet of active mobile offshore drilling rigs is set forth in the table below.

TYPE AND NAME(A)	WATER DEPTH CAPABILITY (FT)	ATTRIBUTES(B)	YEAR BUILT/LATEST ENHANCEMENT(C)	CURRENT LOCATION	CUSTOMER(D)
FOURTH-GENERATION SEMISUBMERSIBLES(3):					
Ocean Alliance........	5,000	TDS; DP; 15K; 3M	1988/1995	North Sea	BP
Ocean America.........	5,000	TDS; SP; 15K; 3M	1988/1992	Gulf of Mexico	BP
Ocean Valiant.........	5,000	TDS; SP; 15K; 3M	1988/1995	Gulf of Mexico	Exxon
OTHER SEMISUBMERSIBLES(27):					
Arethusa Worker.......	3,300	TDS	1982/1992	Gulf of Mexico	Texaco
Ocean Voyager.........	3,200	TDS; VC	1973/1995	Gulf of Mexico	Enserch
Arethusa Yatzy(e).....	3,000	TDS; DP	1989	Brazil	Petrobras
Arethusa Lexington....	2,500	TDS; 3M	1976/1995	Gulf of Mexico	Marathon
Arethusa Neptune......	2,500	TDS; 3M	1977/1995	Gulf of Mexico	Kerr-McGee
Arethusa Concord......	2,200	TDS	1975/1995	Gulf of Mexico	Shell
Arethusa Saratoga.....	2,200	TDS; 3M	1976/1995	Gulf of Mexico	Shell
Arethusa Yorktown.....	2,200	TDS	1976/1989	Brazil	Petrobras
Ocean Endeavor........	2,000	TDS; VC	1975/1994	Gulf of Mexico	Oryx
Ocean Rover...........	2,000	TDS; VC; 15K	1973/1992	Gulf of Mexico	Amerada Hess
Ocean Prospector......	1,700	VC	1971/1981	Gulf of Mexico	Newfield(f)
Arethusa Whittington.........	1,500	TDS; 3M	1974/1995	Gulf of Mexico	Mobil
Ocean Bounty..........	1,500	TDS; VC; 3M	1977/1992	Australia/ Indonesia	Phillips
Ocean Guardian........	1,500	TDS; SP; 3M	1985	North Sea	BP
Ocean New Era.........	1,500	TDS	1974/1990	Gulf of Mexico	Hardy Oil & Gas(g)
Ocean Princess(h).....	1,500	TDS; 15K	1977/1995	North Sea	Committed
Ocean Epoch...........	1,200	TDS	1977/1990	Australia/ Indonesia	Enterprise
Ocean General.........	1,200	TDS	1976/1990	Vietnam	Fina
Ocean Nomad...........	1,200	TDS	1975/1995	North Sea	Shell
Ocean Ambassador......	1,100	TDS	1975/1995	Gulf of Mexico	LL&E
Ocean Baroness........	1,100	TDS; VC	1973/1995	Brazil	Committed
Ocean Star(i)(j)......	850	VC	1974/1992	Gulf of Mexico	Committed
Ocean Century.........	800		1973	Gulf of Mexico	Stacked
Ocean Quest(k)........	800	VC	1973	Gulf of Mexico	Committed
Ocean Liberator.......	600		1974	Nigeria	Ashland
Ocean Victory.........	600	VC	1972	North Sea	Stacked
Ocean Zephyr..........	600		1972	Brazil	Petrobras
JACK-UPS(19):					
Ocean Titan...........	350	TDS; IS; 15K; 3M	1974/1989	Gulf of Mexico	LL&E
Ocean Tower...........	350	IS; 3M	1972	Gulf of Mexico	Sonat Exploration(l)
Bonito II(m)..........	300	TDS; IC	1983/1995	Gulf of Mexico	Unocal
Miss Kitty(n).........	300	IC	1982	India	ONGC
Ocean King............	300	TDS; IC	1973/1989	Gulf of Mexico	Conoco
Ocean Nugget..........	300	TDS; IC	1976/1995	Gulf of Mexico	Amoco
Ocean Summit..........	300	SDS; IC	1972/1991	Gulf of Mexico	Forcenergy
Ocean Warwick.........	300	TDS; IS; SO	1971/1984	Gulf of Mexico	Stacked
Arethusa Heritage.....	250	TDS; IC	1981/1995	Egypt	EDC
Arethusa Sovereign....	250	TDS; IC	1981/1994	Indonesia	Maxus
Ocean Champion........	250	MS	1975/1985	Gulf of Mexico	Chevron
Ocean Columbia........	250	TDS; IC	1978/1990	Gulf of Mexico	Coastal Oil & Gas
Ocean Spartan.........	250	TDS; IC	1980/1994	Gulf of Mexico	Meridian
Ocean Spur............	250	TDS; IC	1981/1994	Gulf of Mexico	Houston Exploration(o)
Ocean Conquest........	200	MS	1978	Gulf of Mexico	Stacked
Ocean Crusader........	200	TDS; MC	1982/1992	Gulf of Mexico	Chevron
Ocean Drake...........	200	TDS; MC	1983/1986	Gulf of Mexico	Murphy
Arethusa Scotian......	180	TDS; IC; 15K	1981/1988	North Sea (Dutch sector)	Elf
Ocean Magallanes......	150	IC	1980	Chile	Stacked
DRILLSHIP(1):					
Ocean Clipper I.......	1,200	SP	1976	Africa	Committed(p)

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(a) Does not include one other semisubmersible rig held for disposition that is also not included in the discussion of Diamond Offshore's fleet.

(b) Attributes legend:

DP	--	Dynamically Positioned/Self-Propelled
MS	--	Mat-Supported Slot Rig
TDS	--	Top-Drive Drilling System
IC	--	Independent-Leg Cantilevered Rig
SDS	--	Side-Drive Drilling System
VC	--	Victory-Class
IS	--	Independent-Leg Slot Rig
SO	--	Skid-Off Capability
3M	--	Three Mud Pumps
MC	--	Mat-Supported Cantilevered Rig
SP	--	Self-Propelled
15K	--	15,000 psi Blowout Preventer

(c) Such enhancements include the installation of top-drive drilling systems, water depth upgrades, mud pump additions and increases in deck load capacity.

(d) For ease of presentation in this table, customer names have been shortened or abbreviated.

(e) Arethusa acquired the Arethusa Yatzy on May 3, 1995. Prior to this date the rig was operated by Arethusa under a management agreement.

(f) Turnkey operator is ADTI.

(g) Turnkey operator is DOTS.

(h) Preparing for a two-year term contract that commenced late March 1996.

(i) Formerly named Ocean Countess.

(j) Committed under a letter of intent for a three-year term contract with Texaco in the Gulf of Mexico.

(k) Committed under a three-year term contract with Chevron in the Gulf of Mexico.

(l) Turnkey operator is Triton.

(m) Diamond Offshore charters the rig pursuant to a bareboat charter agreement which expires in August 1996. The rig is under contract for sale, upon closing of which such charter will terminate.

(n) Diamond Offshore operates the rig pursuant to a bareboat charter agreement which expires in July 1997. Diamond Offshore has the option to extend the charter agreement for one additional year.

(o) Turnkey operator is Brown/R&B.

(p) Committed under an agreement in principle for a four-year term contract in the Gulf of Mexico following completion of rig enhancement.

OFFSHORE FLEET UTILIZATION

The following table sets forth certain information comparing the rig utilization of the respective fleets of Diamond Offshore and Arethusa relative to that of the offshore drilling industry as a whole during the year ended December 31, 1995 and during the three months ended March 31, 1996. Industry statistics and statistics for each of the companies were compiled by Offshore Data Services. Diamond Offshore's one drillship had an average utilization of 59.4% and 95.6% for the year ended December 31, 1995 and the three months ended March 31, 1996, respectively.

	AVERAGES FOR THREE MONTHS ENDED MARCH 31,			AVERAGES FOR THE YEAR ENDED DECEMBER 31,		
	1996			1995		
	DIAMOND OFFSHORE	ARETHUSA	INDUSTRY	DIAMOND OFFSHORE	ARETHUSA	INDUSTRY
FOURTH-GENERATION SEMISUBMERSIBLES:						
Total Rigs.......................	3.0	--	13.0	3.0	--	13.0
Under Contract...................	3.0	--	13.0	3.0	--	13.0
Utilization Rate.................	100.0%	--	100.0%	100.0%	--	100.0%
OTHER SEMISUBMERSIBLES:						
Total Rigs.......................	19.0	8.0	112.0	19.0	8.0	110.1
Under Contract...................	16.3	8.0	97.3	14.5	7.8	89.3
Utilization Rate.................	86.0%	100.0%	86.9%	76.3%	96.9%	81.2%
JACK-UPS:						
Total Rigs.......................	14.0	5.0	302.3	14.0	5.0	306.8
Under Contract...................	11.0	5.0	254.3	10.6	4.8	249.1
Utilization Rate.................	78.6%	100.0%	84.1%	75.6%	95.0%	81.2%

MARKETS

Diamond Offshore's principal markets for its offshore contract drilling services are the Gulf of Mexico, Europe, including principally the United Kingdom sector of the North Sea, South America and Australia/Southeast Asia. Diamond Offshore actively markets its rigs worldwide. In the past, rigs in Diamond Offshore's fleet have also operated in the Mediterranean Sea, the Black Sea and other markets. See Note 11 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

Diamond Offshore believes that its presence in multiple markets provides a competitive advantage. For example, Diamond Offshore believes that its experience with safety and other regulatory matters in the United Kingdom has been beneficial in Australia and in the Gulf of Mexico and that production experience gained through Brazilian and North Sea operations has potential application worldwide. Additionally, Diamond Offshore believes that its performance for a customer in one market segment or area enables Diamond Offshore to better understand that customer's needs and serve that customer in different market segments or other geographic locations.

OFFSHORE CONTRACT DRILLING SERVICES

Diamond Offshore's contracts to provide offshore drilling services vary in their terms and provisions. Diamond Offshore often obtains its contracts through competitive bidding, although it is not unusual for Diamond Offshore to be awarded drilling contracts without competitive bidding. Drilling contracts generally provide for a basic drilling rate on a fixed dayrate basis regardless of whether such drilling results in a successful well. Drilling contracts may also provide for lower rates during periods when the rig is being moved or when drilling operations are interrupted or restricted by equipment breakdowns, adverse weather or water conditions or other conditions beyond the control of Diamond Offshore. Under dayrate contracts, Diamond Offshore generally pays the operating expenses of the rig, including wages and the cost of incidental supplies. Revenues from dayrate contracts have historically accounted for a substantial portion of Diamond Offshore's revenues. In addition, Diamond Offshore has worked some of its rigs under dayrate contracts pursuant to which the customer also agrees to pay Diamond Offshore an incentive bonus based upon performance.

A dayrate drilling contract generally extends over a period of time covering either the drilling of a single well, a group of wells (a "well-to-well contract") or a stated term (a "term contract") and may be terminated by the customer in the event the drilling unit is destroyed or lost or if drilling operations are suspended for a specified period of time as a result of a breakdown of major equipment or in some cases due to other events beyond the control of either party. In addition, certain of Diamond Offshore's contracts permit the customer to terminate the contract early by giving notice and in some circumstances may require the payment of an early termination fee by the customer. The contract term in many instances may be extended by the customer exercising options for the drilling of additional wells at fixed or mutually agreed terms, including dayrates.

The duration of offshore drilling contracts is generally determined by market demand and the respective management strategy of the offshore drilling contractor and its customers. In periods of rising demand for offshore rigs, contractors typically prefer well-to-well contracts that give contractors the flexibility to profit from increasing dayrates. In contrast, during these periods customers with reasonably definite drilling programs typically prefer longer term contracts to maintain drilling prices at the lowest level possible. Conversely, in periods of decreasing demand for offshore rigs, contractors generally prefer longer term contracts to preserve dayrates at existing levels and ensure utilization, while the customers prefer well-to-well contracts that allow them to obtain the benefit of lower dayrates. In general, Diamond Offshore seeks to have a reasonable balance of single well, well-to-well and term contracts to minimize the downside impact of a decline in the market while still participating in the benefit of increasing dayrates in a rising market. Although many of Diamond Offshore's semisubmersible rigs are contracted on a term basis, Diamond Offshore's jack-up fleet is primarily committed for short-term single-well or well-to-well arrangements.

Diamond Offshore believes that more of its customers are seeking to establish continuing relationships with a small number of preferred drilling contractors rather than seeking bids for each drilling contract from a large number of contractors. Diamond Offshore also believes that those contractors who provide the highest quality and the greatest range of services will achieve preferred contractor status. In response to this change in customer attitude, in May 1993 DOTS began offering a portfolio of drilling and production services to complement Diamond Offshore's offshore contract drilling business. These services include overall project management and drilling and production operations on a turnkey or modified-turnkey basis. Under a turnkey contract, the drilling contractor agrees to perform a specified drilling service, such as drilling a well to a specified depth for a fixed price. The ability of the contractor to make a profit on this type of contract depends on the contractor's ability to complete the specified project while keeping expenses within the estimates used to determine the contract price. Under a turnkey contract, the drilling contractor bears the financial risk of delays in completion of the project. Since May 1993, DOTS has engaged in 22 turnkey drilling projects in the Gulf of Mexico and, in conjunction with a tanker owner, has completed an extended well test on a modified-turnkey basis for an operator in the North Sea. Diamond Offshore also intends to seek alternative uses for the rigs in its fleet that are no longer competitive in the drilling market and do not meet Diamond Offshore's criteria for modification. Such alternative uses may include employment of these rigs as mobile offshore production units or as a part of floating production systems. These operations have not been a significant part of Diamond Offshore's business. See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

BAREBOAT CHARTER CONTRACTS

Diamond Offshore operates two of its rigs pursuant to bareboat charter contracts. Under a bareboat charter, Diamond Offshore charters the use of a rig for a specified period and operates the rig as if it were owned.

BONITO II CONTRACT. Diamond Offshore operates the Bonito II under a bareboat charter agreement expiring in August 1996. Under the agreement, Diamond Offshore makes periodic payments to the rig owner consisting of (i) monthly basic charter hire payments and (ii) quarterly additional hire payments based on certain revenue/cost criteria. Diamond Offshore recognizes all revenues and costs, including the charter fee, in its financial statements. The rig is under contract for sale, upon closing of which such charter will terminate.

MISS KITTY CONTRACT. Diamond Offshore operates the Miss Kitty under a bareboat charter agreement initially expiring in July 1996, and recently extended to July 1997. Under the agreement, Diamond Offshore makes periodic payments to the rig owner consisting of (i) monthly basic charter hire payments and (ii) quarterly additional hire payments based on certain revenue/cost criteria. Diamond Offshore recognizes all revenues and costs, including the charter fee, in its financial statements.

LAND DRILLING OPERATIONS

In addition to its offshore drilling fleet, Diamond Offshore owns and operates 10 land rigs, all of which are currently located in South Texas, and a fleet of heavy-duty trucks designed to transport these rigs to drilling locations. Seven of Diamond Offshore's 10 land rigs are Cabot-design trailer-mounted rigs that are highly mobile and relatively sophisticated, making them more desirable to drilling contractors than non-trailer-mounted land rigs of similar capability. Diamond Offshore believes that these trailer-mounted rigs have achieved higher utilization rates than non-trailer-mounted rigs would have achieved. Diamond Offshore's land rigs typically operate under dayrate, footage or turnkey contracts (compensation under footage contracts is based on the number of feet drilled and involves more risk for a contractor than dayrate contracts and the potential for greater financial gains or losses), although most of its contracts are dayrate contracts.

More detailed information concerning Diamond Offshore's land drilling rigs, as of March 28, 1996, is set forth in the table below.

RIG NUMBER	TYPE OF RIG	DRILLING DEPTH CAPABILITY (FT)	CUSTOMER(1)
840...............	Oilwell 840-E	18,000	UPRC
851...............	National 80-B	15,000	Parker & Parsley
859...............	Brewster N-75	15,000	Quisto Exploration
865...............	Cabot 1200	14,000	Cox & Perkins
866...............	Cabot 1200	14,000	Enron Oil & Gas
863...............	Cabot 1000	13,000	Enron Oil & Gas
864...............	Cabot 1000	13,000	Coastal Oil & Gas
861...............	Cabot 900	11,000	Swift Energy
862...............	Cabot 900	11,000	Conoco
860...............	Cabot 750	9,500	Sanchez-O'Brien

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(1) For ease of presentation in this table, customer names have been shortened or abbreviated.

CUSTOMERS

Diamond Offshore provides offshore drilling services to a customer base that includes independent and major integrated oil companies and state-owned oil companies. Occasionally, several customers have accounted for 10.0% or more of Diamond Offshore's annual consolidated revenues, although the identity of such customers may vary from year to year. During 1995, Diamond Offshore performed services for approximately 90 different customers and British Petroleum Co., PLC ("BP"), accounted for 16.5% of Diamond Offshore's annual total consolidated revenues. During 1994, Diamond Offshore performed services for approximately 90 different customers and no single customer accounted for more than 8.2% of Diamond Offshore's annual total consolidated revenues. During 1993, Diamond Offshore performed services for approximately 85 different customers and BP accounted for 10.5% of Diamond Offshore's annual total consolidated revenues. Management believes that at current levels of activity Diamond Offshore has alternative customers for its services such that the loss of a single customer would not have a material adverse effect on Diamond Offshore on a long-term basis.

Diamond Offshore's services are marketed principally through its Houston office, with support from its regional offices in New Orleans, Louisiana; Aberdeen, Scotland; and Perth, Australia. Technical and administrative support for Diamond Offshore's operations is provided by its Houston office.

QUALITY

Diamond Offshore maintains a program to continuously improve quality and safety through GEMS, which was instituted in 1993 to increase Diamond Offshore's commitment to quality of service, safety and the environment. GEMS is a quality system that provides for formal procedures to assist in continuous improvement in Diamond Offshore's efforts to exceed customer expectations in safety, environmental concerns, equipment maintenance, rig enhancements, material handling and personnel training and performance. The key to GEMS is Diamond Offshore's end-of-well report, which is intended to ensure feedback for improvement and communication of Diamond Offshore's concern for customer satisfaction. Diamond Offshore also seeks to capitalize on customer recognition of Diamond Offshore's quality and safety achievements. Diamond Offshore is the only drilling contractor to have won more than once (in April 1994 and April 1995) the annually awarded U.S. Minerals Management Service National Safety Award for Excellence.

GOVERNMENTAL REGULATION

Diamond Offshore's operations are subject to numerous federal, state and local environmental laws and regulations that relate directly or indirectly to its operations, including certain regulations controlling the discharge of materials into the environment, requiring removal and clean-up under certain circumstances, or otherwise relating to the protection of the environment. For example, Diamond Offshore may be liable for damages and costs incurred in connection with oil spills for which it is held responsible. Laws and regulations protecting the environment have become increasingly stringent in recent years and may in certain circumstances impose "strict liability" and render a company liable for environmental damage without regard to negligence or fault on the part of such company. Such laws and regulations may expose Diamond Offshore to liability for the conduct of or conditions caused by others, or for acts of Diamond Offshore that were in compliance with all applicable laws at the time such acts were performed. The application of these requirements or the adoption of new requirements could have a material adverse effect on Diamond Offshore.

OPA '90 and similar legislation enacted in Texas, Louisiana and other coastal states address oil spill prevention and control and significantly expand liability exposure across all segments of the oil and gas industry. OPA '90, such similar legislation and related regulations impose a variety of obligations on Diamond Offshore related to the prevention of oil spills and liability for damages resulting from such spills. OPA '90 imposes strict and with limited exceptions joint and several liability upon each responsible party for oil removal costs and a variety of public and private damages. OPA '90 also imposes ongoing financial responsibility requirements on a responsible party. A failure to comply with such ongoing requirements or inadequate cooperation in a spill may subject a responsible party, including in some cases Diamond Offshore, to civil or criminal enforcement action. OPA '90 also requires the U.S. Minerals Management Service to promulgate regulations to implement the financial responsibility requirements for offshore facilities. If implemented as written, the financial responsibility requirements of OPA '90 could have the effect of significantly increasing the amount of financial responsibility that oil and gas operators must demonstrate to comply with OPA '90. While industry groups and marine insurance carriers are seeking modification of these requirements, implementation of these requirements in their current form could adversely affect the ability of some of Diamond Offshore's customers to operate in U.S. waters, which could have a material adverse effect on Diamond Offshore.

The Federal Water Pollution Control Act of 1972, commonly referred to as the Clean Water Act ("CWA"), prohibits the discharge of certain substances into the navigable waters of the U.S. without a permit. The regulations implementing the CWA require permits to be obtained by an operator before certain exploration or drilling activities occur. Violations of monitoring, reporting and permitting requirements can result in the imposition of civil and criminal penalties. The provisions of the CWA can also be enforced by citizens' groups. Many states have similar laws and regulations.

The Outer Continental Shelf Lands Act authorizes regulations relating to safety and environmental protection applicable to lessees and permittees operating on the Outer Continental Shelf. Specific design and operational standards may apply to Outer Continental Shelf vessels, rigs, platforms, vehicles and structures.

Violation of lease terms relating to environmental matters or regulations issued pursuant to the Outer Continental Shelf Lands Act can result in substantial civil and criminal penalties as well as potential court injunctions curtailing operations and the cancellation of leases. Such enforcement liabilities can result from either governmental or citizen prosecution.

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended ("CERCLA"), currently exempts crude oil, and the Resource Conservation and Recovery Act, as amended ("RCRA"), currently exempts certain drilling materials, such as drilling fluids and production waters, from the definitions of hazardous substances and hazardous wastes. However, Diamond Offshore's operations may involve the use or handling of other materials, such as fracturing fluids or acids, that may be classified as environmentally hazardous substances or wastes. There can be no assurance that such exemption will be preserved in future amendments of such acts, if any, or that more stringent laws and regulations protecting the environment will not be adopted. CERCLA assigns strict liability to each responsible party, as defined, for all response and remediation costs, as well as natural resource damages. Few defenses exist to the liability imposed by CERCLA.

Diamond Offshore's operations may involve the generation, use or handling of materials, such as unused fracturing fluids or acids, that may be classified as hazardous waste, and that are subject to RCRA and comparable state statutes. The Environmental Protection Agency ("EPA") and various state agencies have limited the disposal options for certain hazardous and nonhazardous wastes and are considering the adoption of stricter handling and disposal standards for nonhazardous wastes. RCRA currently exempts certain drilling materials, such as drilling fluids and production waters, from the definitions of hazardous wastes. There can be no assurance that such exemption will be preserved in future amendments of such acts, if any, or that more stringent laws and regulations protecting the environment will not be adopted.

The operations of Diamond Offshore are subject to the Clean Air Act, as amended, and comparable state statutes. Traditional air quality programs relating to the prevention of significant deterioration of air quality in areas with unacceptable pollution levels ("nonattainment areas") restrict drilling in affected areas. Amendments to the Clean Air Act were adopted in 1990 and contain provisions that may result in the imposition over the next decade of certain requirements with respect to air emissions, which requirements may require capital expenditures by Diamond Offshore. The EPA is currently developing regulations to implement these requirements. Pursuant to a mandate of the Clean Air Act, the EPA together with other agencies of the federal government is conducting a study of the effects of emissions from drilling activities in nonattainment areas on the Outer Continental Shelf. Upon completion of the study, these agencies will determine whether additional regulatory requirements are necessary for these nonattainment areas. Any greater degree of regulation in nonattainment areas would increase the cost associated with operation in those areas.

LIMITATION ON OWNERSHIP BY NON-U.S. CITIZENS

Diamond Offshore, as the owner of United States flag vessels, is subject to the Shipping Act, 1916, as amended ("Shipping Act"), which provides that a controlling interest in Diamond Offshore may not be acquired by a non-U.S. citizen without the consent of the U.S. Secretary of Transportation, acting through the United States Maritime Administration ("MARAD"). Current MARAD regulations authorize the transfer of a controlling interest in a company as long as the United States is not at war, the transferee is not a national of a country to which the transfer would be contrary to the foreign policy of the United States and the company's U.S. flag vessels remain documented under the U.S. flag after the transfer. In the absence of MARAD consent (either by the current regulations or otherwise) the transfer of a controlling interest in Diamond Offshore to non-U.S. citizens would enable MARAD to exercise various remedies under the Shipping Act including seizure of vessels, civil penalties and, in certain cases, criminal penalties.

INDEMNIFICATION AND INSURANCE

Diamond Offshore has generally been able to obtain contractual indemnification pursuant to which Diamond Offshore's customers agree to protect and indemnify Diamond Offshore to some degree from liability for reservoir, pollution and environmental damages, but there can be no assurance that Diamond

Offshore can obtain such indemnities in all of its contracts, that the level of indemnification that can be obtained will be meaningful, that such indemnification agreements will be enforceable or that the customer will be financially able to comply with its indemnity obligations. In addition, Diamond Offshore maintains insurance coverage against certain property damage, war risk (in the case of certain operations outside the U.S.), general liability and environmental liabilities, including pollution caused by sudden and accidental oil spills, but there can be no assurance that such insurance will continue to be available or carried by Diamond Offshore or if available and carried will be adequate to cover Diamond Offshore's loss or liability in many circumstances. Except with respect to its fourth-generation semisubmersibles, Diamond Offshore does not maintain business interruption insurance and may elect to discontinue this coverage for its fourth-generation semisubmersibles at any time.

EMPLOYEES

As of December 31, 1995, Diamond Offshore and Arethusa had approximately 2,500 and 1,101 employees, respectively (including international crews furnished through labor contractors), approximately 260 of which Diamond Offshore employees were union members. Diamond Offshore has experienced satisfactory labor relations and provides comprehensive benefit plans for its hourly paid employees. Diamond Offshore does not consider the possibility of a shortage of qualified personnel to be a material factor in its business. If demand for oil field services were to increase rapidly, retention of qualified people might become more difficult without significant increases in compensation.

PROPERTIES

Diamond Offshore owns an 18,000 square foot building and 20 acres of land in New Iberia, Louisiana used for its offshore drilling warehouse and storage facility, a 13,000 square foot building and five acres of land in Aberdeen, Scotland used in connection with its North Sea operations, a 15,000 square foot building and 10 acres of land in Alice, Texas for its land drilling office, warehouse and storage facility, six acres of land near Houston, Texas used as a warehouse facility and an eight-story office building located at 15415 Katy Freeway, Houston, Texas, where Diamond Offshore currently has its corporate headquarters in approximately 60,000 square feet of such building. Diamond Offshore leases approximately 29,000 square feet of office space in downtown Houston and various office, warehouse and storage facilities and lots in Louisiana, The Netherlands, the United Kingdom, Australia, India, Indonesia, Singapore and Brazil to support its offshore drilling operations.

In February 1996, Diamond Offshore purchased for approximately $8.2 million the eight-story building containing approximately 182,000 net rentable square feet on approximately 6.2 acres in which it had leased office space for its corporate headquarters. A portion of the building is currently occupied by other tenants under leases which expire through 2005. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Other."

LEGAL PROCEEDINGS

Various claims have been filed against Diamond Offshore in the ordinary course of business, particularly claims alleging personal injuries. Management believes that Diamond Offshore has established adequate reserves on its books for any liabilities that may reasonably be expected to result from these claims. In the opinion of management, no pending or threatened claims, actions or proceedings against Diamond Offshore are expected to have a material adverse effect on Diamond Offshore's financial position or results of operations.

MANAGEMENT

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

The table below sets forth certain information with respect to each person or entity known by Diamond Offshore to be the beneficial owner of more than 5% of Diamond Offshore Common Stock as of the Effective Time (based upon beneficial ownership of Diamond Offshore Common Stock, with respect to Loews, as of March 28, 1996 and Arethusa Common Stock, with respect to Alphee and Ratos, as of April 2, 1996).

TITLE OF CLASS	NAME AND ADDRESS OF BENEFICIAL OWNER	AMOUNT AND NATURE OF BENEFICIAL OWNERSHIP	PERCENT OF CLASS
Common Stock	Loews Corporation 667 Madison Avenue New York, N.Y. 10021-8087	35,050,000	51.6%
Common Stock	Alphee S.A. 11, Avenue de la Gare P.O. Box 2255 L-1022 Luxembourg	4,708,248	6.9%
Common Stock	Forvaltnings AB Ratos Drottninggatan 2 P.O. Box 1661, S-111 96 Stockholm, Sweden	3,667,207	5.4%

SECURITY OWNERSHIP OF MANAGEMENT AND DIRECTORS

The following table shows the amount and nature of beneficial ownership of Diamond Offshore Common Stock and Loews common stock beneficially owned by each director of Diamond Offshore, each Named Executive Officer of Diamond Offshore and all directors and officers of Diamond Offshore as a group, as of March 28, 1996. Directors and executive officers of Diamond Offshore individually and as a group own less than 1% of equity securities of Diamond Offshore, Loews or any subsidiary of Diamond Offshore. Except as otherwise noted, the named beneficial owner has sole voting power and sole investment power with respect to the number(s) of shares shown below.

NAME OF BENEFICIAL OWNER	DIAMOND OFFSHORE COMMON STOCK	LOEWS COMMON STOCK
James S. Tisch	0	80,000(1)
Herbert C. Hofmann	1,000(2)	400(2)
David M. Ifshin	0	0
Robert E. Rose	2,100(3)	0
Raymond S. Troubh	2,500	5,000
Lawrence R. Dickerson	500(3)	200
Ronald C. Johnson(4)	0	0
Thomas P. Richards	6,000(5)	0
David W. Williams	100	0
Richard L. Lionberger	0	0
All Directors and Executive Officers as a Group	12,300	85,950

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(1) In addition, 58,000 shares of Loews common stock are held by a charitable foundation as to which Mr. Tisch has shared voting and investment power.

(2) In addition, 350 shares of Loews common stock and 300 shares of Diamond Offshore Common Stock are owned by Mr. Hofmann's son, as to which shares Mr. Hofmann disclaims any beneficial ownership.

(3) Voting power and investment power with respect to shares listed with Mr. Rose and Mr. Dickerson are shared with each such individual's spouse.

(4) Mr. Johnson ceased to be an executive officer of Diamond Offshore in March 1996.

(5) The number of shares shown includes 4,000 shares owned by Richards Brothers Company, a Texas corporation, of which all non-voting common stock is owned by the children of Mr. Richards, and as to which Mr. Richards disclaims any beneficial ownership.

DIRECTORS

Diamond Offshore's Board of Directors presently consists of five directors. The directors are James S. Tisch, Herbert C. Hofmann, David M. Ifshin, Robert E. Rose and Raymond S. Troubh. Two of such directors, Mr. Troubh and Mr. Ifshin, are not directors, officers or employees of Loews or officers or employees of Diamond Offshore. All directors are elected annually to serve until the next annual meeting of stockholders and until their successors are duly elected and qualified. Each of the five directors is serving a term of one year to expire at the 1997 annual meeting of stockholders and until his successor is elected and qualifies or until his earlier death, resignation, disqualification or removal from office. Information with respect to the current directors of Diamond Offshore is set forth below.

NAME	POSITION	AGE AS OF JANUARY 31, 1996	DIRECTOR SINCE
James S. Tisch(1)........	Chairman of the Board	43	1989
Herbert C. Hofmann(1)....	Director	53	1992
David M. Ifshin(2).......	Director	47	1995
Robert E. Rose(1)........	Director, President and Chief Executive Officer	57	1989
Raymond S. Troubh(2).....	Director	69	1995

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(1) Member, Executive Committee of the Board of Directors.

(2) Member, Audit Committee of the Board of Directors.

James S. Tisch has served as the Chairman of the Board since 1995 and as a director of Diamond Offshore since June 1989. Mr. Tisch has served as President and Chief Operating Officer of Loews, a diversified holding company, since 1994 and prior thereto served as Executive Vice President of Loews for more than five years. Mr. Tisch, a director of Loews since 1986, also serves as a director of CNA Financial Corporation, an 84% owned subsidiary of Loews, and Gillett Holdings, Inc.

Herbert C. Hofmann has served as a director of Diamond Offshore since January 1992. Mr. Hofmann has served as Senior Vice President of Loews since January 1992, and prior thereto served as Vice President -- Operations Planning of Loews for more than five years. He has served as President and Chief Executive Officer of Bulova Corporation, a 97% owned subsidiary of Loews since August 1989, and as Chief Operating Officer of Bulova Corporation prior thereto. Bulova Corporation distributes and sells watches and clocks.

David M. Ifshin has served as a director of Diamond Offshore since November 1995. Mr. Ifshin currently holds several professional positions. Since 1993, he has served as a Senior Advisor of Galway Partners, Senior Vice President of Cassidy Associates, and as partner in the law firm Ifshin & Friedman. Between 1983 and 1993, Mr. Ifshin served as a Managing Director of Prudential Securities, Inc., Senior Vice President and Managing Director of Kemper Securities (Prescott, Ball & Turben), Director, Washington, Capital Markets Office of E.F. Hutton & Company, Inc. and a partner with the law firm of Manatt, Phelps, Rothenberg & Phillips.

Robert E. Rose has served as President and Chief Executive Officer of Diamond Offshore and as a director since June 1989.

Raymond S. Troubh has served as a director of Diamond Offshore since November 1995. Mr. Troubh is a financial consultant in New York City and a former Governor of the American Stock Exchange. For the past five years, Mr. Troubh has been the principal of Raymond Troubh & Company. Mr. Troubh also serves as a director of ADT Limited, America West Airlines, Inc., Applied Power Inc., ARIAD Pharmaceuticals, Inc., Becton, Dickinson and Company, Benson Eyecare Corporation, Foundation Health Corporation, General

American Investors Company, Manville Corporation, Olsten Corporation, Petrie Stores Corporation, Riverwood International Corporation, Time Warner Inc., Triarc Companies, Inc., and WHX Corporation.

DIRECTOR COMPENSATION. Directors who are employees of Diamond Offshore are not paid any fees or additional compensation for service as members of the Board of Directors or any committee thereof. The annual retainer payable to directors of Diamond Offshore who are not employees of Diamond Offshore or any of its subsidiaries or affiliated companies, for services as directors, is $20,000 per annum, payable quarterly. Each member of the Audit Committee of the Board of Directors of Diamond Offshore receives a retainer of $2,500 per annum, payable quarterly, and each director of Diamond Offshore who is not an employee of Diamond Offshore or any of its subsidiaries or affiliated companies is paid a fee of $1,000 for attendance at each meeting of the Board of Directors and of the Audit Committee thereof in addition to the reasonable costs and expenses incurred by such directors in relation to their services as such.

BOARD OF DIRECTORS AND COMMITTEES. Diamond Offshore's Board of Directors has five members, and the Board has two standing committees. Further information concerning the Board's standing committees appears below.

EXECUTIVE COMMITTEE. The Executive Committee of the Board of Directors consists of three members, Mr. Tisch, Mr. Hofmann and Mr. Rose. The Executive Committee has all the powers and exercises all the duties of the Board of Directors in the management of the business of Diamond Offshore that may lawfully be delegated to it by the Board of Directors. These powers and duties include, among other things, declaring a dividend, authorizing the issuance of stock, recommending to stockholders mergers or a sale of substantially all of the assets of Diamond Offshore, providing advice and counsel to management of Diamond Offshore, reviewing management's recommendations for significant changes to the organizational structure of Diamond Offshore and recommending changes to the Board of Directors.

AUDIT COMMITTEE. The Audit Committee of the Board of Directors consists of two members, Mr. Ifshin and Mr. Troubh. The Audit Committee reviews and reports to the Board of Directors on the scope and results of audits by Diamond Offshore's independent auditors. See "-- Certain Relationships and Related Transactions -- Services Agreement." It recommends a firm of certified public accountants to serve as auditors for Diamond Offshore, subject to nomination by the Board of Directors and election by the stockholders, authorizes all audit and other professional services rendered by the auditor and periodically reviews the independence of the auditor. Membership on the Audit Committee is restricted to directors independent of management and free from any relationship that, in the opinion of the Board of Directors, would interfere with the exercise of independent judgment as a committee member. Directors who are affiliates of Diamond Offshore or officers or employees of Diamond Offshore or its subsidiaries or its affiliates are not qualified for Audit Committee membership.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION. During Diamond Offshore's fiscal year ended December 31, 1995, Diamond Offshore had no compensation committee or other committee of the Board of Directors performing similar functions. Decisions concerning compensation of executive officers were made during such fiscal year by persons who were members of Diamond Offshore's Board of Directors, including Robert E. Rose, an executive officer of Diamond Offshore.

NOMINATING COMMITTEE. During Diamond Offshore's fiscal year ended December 31, 1995, Diamond Offshore had no nominating committee or other committee of the Board of Directors performing similar functions.

EXECUTIVE OFFICER TENURE AND IDENTIFICATION

The executive officers of Diamond Offshore are elected annually by the Board of Directors to serve until the next annual meeting of the Board of Directors and until their successors are duly elected and qualified, or until their earlier death, resignation, disqualification or removal from office. Information with respect to the current executive officers of Diamond Offshore is set forth below.

NAME	AGE AS OF JANUARY 31, 1996	POSITION
Robert E. Rose..............	57	President, Chief Executive Officer and Director
Lawrence R. Dickerson.......	43	Senior Vice President and Chief Financial Officer
Thomas P. Richards..........	52	Senior Vice President -- Worldwide Operations
David W. Williams...........	38	Senior Vice President -- Contracts and Marketing
Richard L. Lionberger.......	45	Vice President, General Counsel and Secretary
Gary T. Krenek..............	37	Controller

Robert E. Rose has served as President and Chief Executive Officer of Diamond Offshore and as a director since June 1989.

Lawrence R. Dickerson has served as Senior Vice President of Diamond Offshore since April 1993 and has served as a Vice President and the Chief Financial Officer of Diamond Offshore since June 1989.

Thomas P. Richards has served as Senior Vice President of Diamond Offshore since September 1990. Since March 1996, Mr. Richards has been in charge of worldwide operations, and prior thereto, since March 1993, Mr. Richards was in charge of domestic operations. From 1990 to 1993 Mr. Richards was in charge of land operations.

David W. Williams has served as Senior Vice President of Diamond Offshore since December 1994 and was a Marketing Vice President between February 1992 and May 1994. Mr. Williams was employed by Noble Drilling Corporation, an offshore contract drilling company, from May 1994 through December 1994 as Vice President of Marketing. Mr. Williams worked in marketing positions at Odeco, an offshore contract drilling company, from 1990 to February 1992.

Richard L. Lionberger has served as Vice President, General Counsel and Secretary of Diamond Offshore since February 1992. Mr. Lionberger was engaged in the private practice of law from 1985 to 1992, principally as the owner of Lionberger & Associates, and was counsel for Diamond Offshore during that period.

Gary T. Krenek has served as Controller of Diamond Offshore since February 1992 and was Accounting Manager of Diamond Offshore since 1989.

EXECUTIVE COMPENSATION

The following table shows for the years ended December 31, 1995 and 1994 the cash compensation paid by Diamond Offshore, and a summary of certain other compensation paid or accrued for such year, to its Chief Executive Officer and each of Diamond Offshore's four other most highly compensated executive officers (the "Named Executive Officers") for service in all capacities with Diamond Offshore and its subsidiaries.

SUMMARY COMPENSATION TABLE

		ANNUAL COMPENSATION(1)(2)		
NAME AND PRINCIPAL POSITION	YEAR	SALARY	BONUS	ALL OTHER COMPENSATION(3)
Robert E. Rose	1995	$390,000	$230,000	$ 6,075
President and Chief Executive Officer	1994	363,315	--	6,075
Thomas P. Richards(4)	1995	210,128	60,000	5,913
Senior Vice President -- Domestic Operations	1994	199,615	--	5,913
Lawrence R. Dickerson	1995	190,000	107,000	5,727
Senior Vice President and Chief Financial Officer	1994	168,000	--	5,727
Ronald C. Johnson(5)	1995	178,928	--	5,913
Senior Vice President -- International Operations	1994	182,902	--	5,913
David W. Williams	1995	175,000	102,500	5,691
Senior Vice President -- Contracts and Marketing				
Richard L. Lionberger	1994	134,842	--	5,159
Vice President, General Counsel and Secretary				

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(1) Amounts exclude perquisites and other personal benefits because such compensation did not exceed the lesser or $50,000 and 10% of the total annual salary reported for each Named Executive Officer.

(2) Amounts include salary and bonus earned, as well as earned but deferred, by the Named Executive Officers.

(3) The amounts shown include (i) Diamond Offshore's contributions under the Retirement Plan referred to below for the years shown on behalf of the Named Executive Officers, as follows: Mr. Rose, 1994 and 1995 -- $5,625; Mr. Richards, 1994 and 1995 -- $5,625; Mr. Dickerson, 1994 and 1995 -- $5,625; Mr. Johnson, 1994 and 1995 -- $5,625; Mr. Williams, 1995 -- $5,625; and Mr. Lionberger, 1994 -- $5,057; and (ii) the term portion of the life insurance premiums paid by Diamond Offshore for the years shown on behalf of the Named Executive Officers, as follows: Mr. Rose, 1994 and 1995 -- $450; Mr. Richards, 1994 and 1995 -- $288; Mr. Dickerson, 1994 and 1995 -- $102; Mr. Johnson, 1994 and 1995 -- $288; Mr. Williams, 1995 -- $66; and Mr. Lionberger, 1994 -- $102.

(4) Mr. Richards became Senior Vice President -- Worldwide Operations in March 1996.

(5) Mr. Johnson ceased to be an executive officer of Diamond Offshore in March 1996.

Diamond Offshore maintains a defined contribution plan (the "Retirement Plan") designed to qualify under Section 401(k) of the Internal Revenue Code of 1986, as amended (the "Code"), pursuant to which Diamond Offshore contributes 3.75% of the participant's base and overtime salary subject to limitations of eligible salary. Employees are vested in all contributions as made.

In addition Diamond Offshore expects to adopt an Executive Deferred Compensation Plan pursuant to which Diamond Offshore will contribute any portion of the 3.75% of the base salary contribution to the Retirement Plan that cannot be contributed to the Retirement Plan because of the limitations of Sections 401(a)(17) and 415 of the Code. Additionally, the plan is expected to provide that participants may defer a percentage of their salary and bonuses pursuant to such plan. Participants in the plan will be highly compensated officers of Diamond Offshore and will be fully vested in all amounts paid into the plan. The plan is anticipated to be effective in 1996 and there is proposed to be a make-up Diamond Offshore contribution for any amounts that were not contributed to the Retirement Plan for 1994 and 1995 because of the Code limitations described above.

ANNUAL CASH BONUS INCENTIVES

Bonuses were awarded under the Diamond Offshore Management Bonus Program, which is intended to provide a means whereby certain selected officers and key employees of Diamond Offshore may develop a sense of proprietorship and personal involvement in the development and financial success of Diamond Offshore, and encourage the participants to remain with and devote their best efforts to the business of Diamond Offshore, thereby advancing the interests of Diamond Offshore and its stockholders. At the beginning of each year, the Executive Committee of the Diamond Offshore Board of Directors establishes a bonus pool (the "Annual Bonus Pool") equal to (i) a percentage (the "Applicable Percentage") ranging from 10% to 35% (as determined by the Executive Committee based on such committee's evaluation of Diamond Offshore during the prior year (the "performance year") relative to peer companies, and the performance of Diamond Offshore's share price and extraordinary events during the performance year) of the total salaries of all participants for the performance year, divided by (ii) the arithmetical average of (x) Diamond Offshore's cash flow plus capital expenses for the year prior to the performance year and (y) cash flow plus capital expenses as budgeted for the performance year, multiplied by (iii) actual cash flow plus capital expenses for such performance year. The Executive Committee establishes the bonus payout from the Annual Bonus Pool to each participant (not to exceed 30% of such participant's eligible salary) based upon corporate, group or individual performance, or a combination thereof, or such other subjective criteria as the Executive Committee may determine to be appropriate. The bonuses are payable in annual installments (50%, 25% and 25%) over the three calendar year period following the performance year and, with certain exceptions, are forfeited if not paid prior to termination of employment. In addition, certain executive officers, including Mr. Rose, received an additional bonus, to recognize the performance of certain executive officers of Diamond Offshore in consummating the Diamond Offshore Initial Public Offering. For performance year 1995, the Executive Committee elected to pay bonuses under the Diamond Offshore Management Bonus Program aggregating approximately $685,000 although the Annual Bonus Pool, if calculated based on the formula set forth in the Diamond Offshore Management Bonus Program and assuming the maximum permissible Applicable Percentage, would have been approximately $1.2 million. This deviation was based on the Executive Committee's subjective evaluation of the overall favorable performance of the eligible officers in 1995, particularly in connection with the successful completion of the Diamond Offshore Initial Public Offering.

EMPLOYMENT AGREEMENTS AND SEVERANCE AND CHANGE IN CONTROL ARRANGEMENTS

Diamond Offshore and Robert E. Rose entered into and subsequently extended an agreement, dated November 1, 1992 (the "Employment Agreement"), providing for, among other things, the employment of Mr. Rose as the President and Chief Executive Officer of Diamond Offshore until December 31, 1998. Mr. Rose currently receives a salary at an annual rate of $500,000, subject to such increases as the Board of Directors of Diamond Offshore may from time to time determine. Pursuant to the Employment Agreement, Mr. Rose and Diamond Offshore agree that during the term of Mr. Rose's employment under the Employment Agreement and for a period of one year immediately following termination of such employment by Diamond Offshore for cause, Mr. Rose will not engage in any other business which is in competition with Diamond Offshore without written consent from Diamond Offshore. The Employment Agreement provides that, for a 120-day period after consummation of a Change of Control (as defined in the Employment Agreement), Mr. Rose has the right to terminate his employment and Diamond Offshore would be obligated to continue to compensate him for a three-year period.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

CONTROLLING STOCKHOLDER. As of the date of this Prospectus, Loews beneficially owns approximately 51.6% of the outstanding shares of Diamond Offshore Common Stock. Diamond Offshore understands that Loews has no current intention of disposing of any of the shares of Diamond Offshore Common Stock owned by it. Loews entered into an agreement, dated October 10, 1995, with the underwriters of the Diamond Offshore Initial Public Offering providing that Loews will not, and will not permit its affiliates (other than Diamond Offshore) to offer, sell, contract to sell, pledge or otherwise dispose of, directly or indirectly, any shares of Diamond Offshore Common Stock or securities convertible into or exchangeable or exercisable for any shares of Diamond Offshore Common Stock for a period of one year after the date of such agreement, without the prior written consent of CS First Boston. After such date such shares may be sold (i) in accordance with Rule 144 promulgated under the Securities Act, (ii) in private offerings or (iii) upon registration under the Securities Act without regard to the volume limitations of Rule 144.

In general, under Rule 144 as currently in effect, Loews will be entitled to sell on the open market in broker's transactions within any three-month period a number of shares that does not exceed the greater of (i) 1% of the then outstanding shares of Diamond Offshore Common Stock (currently 678,933 shares) or (ii) the average weekly trading volume in Diamond Offshore Common Stock on the open market during the four calendar weeks preceding such sale.

Shares held by Loews may be freely sold if registered under the Securities Act. Diamond Offshore has agreed to use its best efforts, upon request by Loews, to register under the Securities Act any or all shares of Diamond Offshore Common Stock held by Loews and, under certain conditions, when shares of Diamond Offshore Common Stock are registered by Diamond Offshore. See "-- Transactions Between Diamond Offshore and Loews -- Registration Rights Agreement."

Loews incorporated Diamond Offshore as a wholly owned subsidiary in 1989 and owned all of the outstanding shares of Diamond Offshore Common Stock since that time until the consummation of the Diamond Offshore Initial Public Offering. Proceeds from the Diamond Offshore Initial Public Offering were used to repay all of Diamond Offshore's then outstanding indebtedness to Loews of $336.2 million and the remainder of such proceeds was used to pay Loews a special dividend of $2.1 million. By virtue of its ownership of a majority of the outstanding shares of Diamond Offshore Common Stock, Loews is in a position to control actions that require the consent of stockholders, including the election of directors, payment of dividends, amendment of Diamond Offshore's Restated Certificate of Incorporation and mergers or a sale of substantially all the assets of Diamond Offshore. In addition, certain officers, directors or employees of Loews serve on Diamond Offshore's Board of Directors. See "-- Directors." Loews and Diamond Offshore have entered into various agreements relating to the ongoing relationship between Loews and Diamond Offshore. See "-- Transactions Between Diamond Offshore and Loews."

Loews is a diversified holding company, incorporated under the laws of Delaware in 1969. Loews, through its subsidiaries, is engaged in a variety of distinct businesses, including the production and sale of cigarettes; the operation of hotels; through Diamond Offshore, the operation of oil and gas drilling rigs; through its approximately 84% ownership of CNA Financial Corporation, property, casualty and life insurance; and through its approximately 97% ownership of Bulova Corporation, the distribution and sale of watches and clocks. In 1995, the consolidated revenues of Loews were approximately $18.7 billion. The address of Loews is 667 Madison Avenue, New York, New York 10021-8087.

TRANSACTIONS BETWEEN DIAMOND OFFSHORE AND LOEWS. Diamond Offshore and Loews have entered into intercompany transactions and agreements incident to their respective businesses and may enter into material transactions and agreements from time to time. In connection with the Diamond Offshore Initial Public Offering, Diamond Offshore and Loews entered into agreements pursuant to which certain management, administrative and other services are provided by Loews to Diamond Offshore and certain other obligations were assumed by the parties. These agreements were not the result of arm's length negotiations between the parties.

The following description of certain terms of certain agreements, arrangements and transactions between Diamond Offshore and Loews accurately summarizes those terms thereof considered by Diamond Offshore to be material to a prospective investor in the Offered Shares and is qualified in its entirety by reference to the complete agreements filed as exhibits to the Registration Statement or, in the case of the Tax Sharing Agreement, the registration statement filed in connection with the Diamond Offshore Initial Public Offering.

Services Agreement. Diamond Offshore and Loews entered into a Services Agreement effective upon consummation of the Diamond Offshore Initial Public Offering (the "Services Agreement") pursuant to which Loews agreed to continue to perform certain administrative and technical services on behalf of Diamond Offshore. Such services include personnel, telecommunications, purchasing, internal auditing, accounting, data processing and cash management services, in addition to advice and assistance with respect to preparation of tax returns and obtaining insurance. Under the Services Agreement, Diamond Offshore is to reimburse Loews for (i) allocated personnel costs (such as wages, salaries, employee benefits and payroll taxes) of the Loews personnel actually providing such services and (ii) all out-of-pocket expenses related to the provision of such services. The Services Agreement may be terminated at Diamond Offshore's option upon 30 days' notice to Loews and at the option of Loews upon six months' notice to Diamond Offshore. In addition, Diamond Offshore has agreed to indemnify and hold harmless Loews for all claims and damages arising from the provision of services by Loews under the Services Agreement, unless due to the gross negligence or willful misconduct of Loews.

Tax Sharing Agreement. Diamond Offshore has been and will be included in the consolidated U.S. federal income tax returns filed by Loews with respect to all periods in which it was a wholly owned subsidiary of Loews. Prior to 1992, Diamond Offshore's profitable subsidiaries were allocated a share of the Loews consolidated federal income tax expense and no benefit was given to any of Diamond Offshore's subsidiaries generating taxable losses. Effective January 1, 1992, a Tax Sharing Agreement (the "Tax Sharing Agreement") with Loews was adopted to allow for the recognition of expenses and benefits related to taxable income or loss as if Diamond Offshore and its subsidiaries filed a separate consolidated return. Upon completion of the Diamond Offshore Initial Public Offering, Diamond Offshore was owned less than 80% by Loews and was therefore removed from the consolidated federal income tax return of Loews, which triggered the automatic termination of the Tax Sharing Agreement. Pursuant to a termination and settlement agreement entered into effective upon consummation of the Diamond Offshore Initial Public Offering, Diamond Offshore and Loews agreed to offset the net amount owed by Loews to Diamond Offshore as a result of the termination of the Tax Sharing Agreement against Diamond Offshore's notes payable to Loews. Such offset constituted a full settlement and satisfaction of Loews's payment obligations to Diamond Offshore arising upon termination of the Tax Sharing Agreement.

Registration Rights Agreement. Under a Registration Rights Agreement (the "Registration Rights Agreement") between Diamond Offshore and Loews, Diamond Offshore will file, upon the request of Loews, one or more registration statements under the Securities Act, subject to a maximum of three such requests, in order to permit Loews to offer and sell any Diamond Offshore Common Stock that Loews may hold. Subject to the restrictions described under "-- Controlling Stockholder" and "-- Registration Rights of Selling Stockholders," Loews may exercise these rights at any time, provided shares comprising at least 5% of the outstanding Diamond Offshore Common Stock are to be sold. Loews will bear the costs of any such registered offering, including any underwriting commissions relating to shares it sells in any such offering, any related transfer taxes and the costs of complying with non-U.S. securities laws, and any fees and expenses of separate counsel and accountants retained by Loews. The Registration Rights Agreement will terminate at such time as Loews's percentage of ownership of the outstanding Diamond Offshore Common Stock falls below 15%. Diamond Offshore has the right to require Loews to delay any exercise by Loews of its rights to require registration and other actions for a period of up to 90 days if, in the judgment of Diamond Offshore, any offering by Diamond Offshore then being conducted or about to be conducted would be adversely affected.

Subject to certain conditions, Diamond Offshore has also granted Loews the right to include its Diamond Offshore Common Stock in any registration statements covering offerings of Diamond Offshore Common Stock by Diamond Offshore, and Diamond Offshore will pay all costs of such offerings other than underwriting commissions and transfer taxes attributable to the shares sold on behalf of Loews. There is no limitation on the number of times that Loews may exercise this right with respect to registration statements relating to Diamond Offshore Common Stock. Diamond Offshore will indemnify Loews, and Loews will indemnify Diamond Offshore, against certain liabilities in respect of any registration statement or offering covered by the Registration Rights Agreement. The rights of Loews under the Registration Rights Agreement are transferable to affiliates of Loews.

TRANSACTIONS BETWEEN DIAMOND OFFSHORE AND THE SELLING STOCKHOLDERS. Pursuant to the Shareholders Agreement, each of Alphee and Ratos agreed to vote all shares of Arethusa Common Stock it owned in favor of the approval and adoption of the Amalgamation Agreement and in favor of the ratification of the Plan of Acquisition and the Fee Agreement, and against any change in a majority of the persons who constituted the Board of Directors of Arethusa. Under the Shareholders Agreement, each of Alphee and Ratos irrevocably appointed Acquisition Sub and its officers, agents and nominees, with full power of substitution, as proxy to so vote its shares of Arethusa Common Stock. Also pursuant to the Shareholders Agreement, each of Alphee and Ratos agreed to vote all shares of Arethusa Common Stock with respect to which it held a proxy for such purpose in favor of the ratification of the Fee Agreement and each of the actions that were to be taken by Arethusa pursuant thereto. In addition, Diamond Offshore granted the Selling Stockholders certain registration rights pursuant to the Shareholders Agreement. See "-- Registration Rights of Selling Stockholders."

REGISTRATION RIGHTS OF SELLING STOCKHOLDERS. Pursuant to the Plan of Acquisition and the Shareholders Agreement, Diamond Offshore agreed for the benefit of Alphee and Ratos to use its best efforts (i) to cause the Registration Statement to be filed and declared effective at the earliest practicable date and to remain effective until the Effective Time, to include this Prospectus intended to permit each of Alphee and Ratos to sell after the Effective Time without restriction, at its election, all or part of the shares of Diamond Offshore Common Stock received by such person in connection with the Acquisition and (ii) to maintain the continued effectiveness of the Registration Statement with respect to such shares, including this Prospectus for use by such persons, for a period of two years from the Effective Time, plus the aggregate number of days in all Suspension Periods (as such term is defined in the Shareholders Agreement) after the Effective Time (the "Required Period").

During the Required Period and assuming continued effectiveness of the registration statement covering their shares of Diamond Offshore Common Stock, Alphee and Ratos may sell such shares in or outside the United States through underwriters or dealers, through agents, or directly to one or more purchasers. The distribution of the shares of Diamond Offshore Common Stock offered by Alphee or Ratos may be effected from time to time in one or more transactions (which may involve crosses or block transactions) (i) on the NYSE (or on such other national stock exchanges on which the Diamond Offshore Common Stock may be listed from time to time) in transactions which may include special offerings, exchange distributions and/or secondary distributions pursuant to and in accordance with the rules of such exchanges, including sales to underwriters who will acquire the Offered Shares for their own account and resell them in one or more transactions or through brokers, acting as principal or agent, (ii) in the over-the-counter market, including sales through brokers, acting as principal or agent, (iii) in transactions other than on such exchanges or in the over-the-counter market, or a combination of such transactions, including sales through brokers, acting as principal or agent, (iv) through the issuance of securities by issuers other than Diamond Offshore convertible into, exchangeable for, or payable in such shares (whether such securities are listed on a national securities exchange or otherwise) or (v) through the writing of options on the shares (whether such options are listed on an options exchange or otherwise). Any such transactions may be effected at market prices prevailing at the time of sale, at prices related to such prevailing market prices, at negotiated prices or at fixed prices. Diamond Offshore has the right to require each of Alphee and Ratos to suspend use of any resale prospectus for any period (not to exceed 20 days in any one instance and, when combined with any other such periods, 60 days in any 12-month period) determined by Diamond Offshore if Diamond Offshore would, in the opinion of Diamond Offshore's counsel, be required to disclose in such prospectus information not otherwise then required by law to be publicly disclosed and, in the judgment of the Board of Directors of Diamond Offshore, such disclosure might adversely affect Diamond Offshore or any material business transaction or negotiation in which Diamond Offshore is then engaged.

Each of Alphee and Ratos will have the right to elect during the 180-day period beginning on the Effective Time (the "Initial Standstill Period") to proceed with one, and only one, and thereafter such shareholders shall have the right to proceed with one, and only one (for both such shareholders collectively) underwritten offering of their shares of Diamond Offshore Common Stock pursuant to the registration statement covering such shares, but if during the Initial Standstill Period, only one underwritten offering of Diamond Offshore Common Stock is effected pursuant to such registration statement, then each of Alphee and Ratos will have the right to proceed with one, and only one, underwritten offering thereafter until the end of the Required Period. During the Initial Standstill Period, and thereafter during the period commencing 14 days prior to the commencement of, and continuing through the completion of the public distribution of, shares of Diamond Offshore Common Stock in an underwritten public offering by Alphee or Ratos, Diamond Offshore and Loews have agreed not to effect any public sale or distribution of Diamond Offshore Common Stock, or any securities convertible into such stock, subject to certain exceptions. Diamond Offshore will pay the costs of all such underwritten offerings other than (i) underwriting commissions attributable to the shares of Diamond Offshore Common Stock sold on behalf of Alphee or Ratos, (ii) out-of-pocket costs incurred in connection with "road shows" and other marketing support involving members of Diamond Offshore's management, (iii) costs of any special audits, (iv) fees and expenses of underwriter's counsel and (v) any out-of-pocket expense (including fees and expenses of counsel) of Alphee or Ratos.

Subject to certain conditions, Diamond Offshore also granted each of Alphee and Ratos the right to include their shares of Diamond Offshore Common Stock in any registration statements covering offerings of Diamond Offshore Common Stock filed during the Required Period by Diamond Offshore for its own account or for holders of Diamond Offshore Common Stock other than Alphee or Ratos, and Diamond Offshore will pay all costs of such offerings other than underwriting commissions attributable to any shares sold on behalf of Alphee or Ratos. There is no limitation on the number of times that Alphee and Ratos may exercise this right during the Required Period with respect to registration statements relating to Diamond Offshore Common Stock.

Diamond Offshore will indemnify Alphee and Ratos, and each of Alphee and Ratos, severally, will indemnify Diamond Offshore, against certain liabilities in respect of any registration statement or resale prospectus covering offerings by Alphee or Ratos, as applicable, of shares of Diamond Offshore Common Stock. The rights of Alphee and Ratos under the Shareholders Agreement with respect to registration rights are transferable by each of Alphee and Ratos to their respective affiliates, but are not otherwise transferable without the prior written consent of Diamond Offshore.

STOCK OPTION PLANS

Pursuant to the Amalgamation Agreement, at the Effective Time, each Arethusa Option was assumed by Diamond Offshore and now constitutes a fully vested and currently exercisable option to acquire, on substantially the same terms and conditions (modified as described below) as were applicable under the Arethusa Stock Option Plans, the same number of shares of Diamond Offshore Common Stock as the holder thereof would have been entitled to receive pursuant to the Amalgamation had such holder exercised such Arethusa Option in full immediately prior to the Effective Time, at a price per share equal to the per share exercise price of the Arethusa Option being assumed divided by the Amalgamation Ratio. No fractional shares of Diamond Offshore Common Stock will be issued in connection with the exercise of any such Arethusa Option. Fractions of Diamond Offshore Common Stock resulting from any such exercise will be paid in cash based upon the market value of a share of Diamond Offshore Common Stock on the date of exercise. Except as otherwise described above, the Arethusa Stock Option Plans terminated as of the Effective Time. Diamond Offshore has filed with the Commission a registration statement on Form S-8 with respect to the shares of Diamond Offshore Common Stock subject to such Arethusa Options, as so amended by Diamond Offshore.

PRICE RANGE OF DIAMOND OFFSHORE COMMON STOCK

Diamond Offshore Common Stock is listed on the NYSE under the symbol "DO." The following table shows for the periods indicated the high and low closing prices of Diamond Offshore Common Stock as reported by the NYSE. No information is provided for Diamond Offshore Common Stock prior to the date of the Diamond Offshore Initial Public Offering.

	FISCAL YEAR ENDED DECEMBER 31,			
	1996		1995	
	HIGH	LOW	HIGH	LOW
Quarter Ended				
March 31	43 3/8	33 3/8	--	--
June 30(1)	50 1/2	43 1/2	--	--
December 31	--	--	34	24

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(1) As of April 11, 1996.

On April 11, 1996, the closing price of the Diamond Offshore Common Stock, as reported by the NYSE, was $50 1/2 per share. As of April 11, 1996, there were approximately 73 record holders, and approximately 1,400 beneficial holders, of Diamond Offshore Common Stock.

DESCRIPTION OF CAPITAL STOCK

The following description of certain terms of Diamond Offshore's capital stock accurately summarizes those terms considered by Diamond Offshore to be material to a prospective investor in the Offered Shares and is qualified in its entirety by reference to Diamond Offshore's Restated Certificate of Incorporation (the "Certificate"), a copy of which was included as an exhibit to the Registration Statement.

COMMON STOCK

The authorized capital stock of Diamond Offshore consists of 225,000,000 shares of capital stock, 200,000,000 of such shares being Diamond Offshore Common Stock, par value $0.01 per share. After giving effect to the issuance of shares of Diamond Offshore Common Stock in connection with the Acquisition (the exchange of each share of Arethusa Common Stock outstanding immediately prior to the Acquisition in consideration of 0.88 shares of Diamond Offshore Common Stock), there were 67,893,344 shares of Diamond Offshore Common Stock issued and outstanding, of which 8,375,455 shares were held by the Selling Stockholders. In addition, at the Effective Time, 1,000,000 shares of Diamond Offshore Common Stock were reserved for issuance upon the exercise of Arethusa Options assumed by Diamond Offshore.

Holders of Diamond Offshore Common Stock are entitled to one vote for each share held and are not entitled to cumulative voting for the purpose of electing directors and have no preemptive or similar right to subscribe for, or to purchase, any shares of Diamond Offshore Common Stock or other securities to be issued by Diamond Offshore in the future. Accordingly, the holders of more than 50% in voting power of the shares of Diamond Offshore Common Stock voting generally for the election of directors will be able to elect all of Diamond Offshore's directors. As described in "Management -- Certain Relationships and Related Transactions -- Controlling Stockholder," Loews beneficially owns approximately 51.6% of the outstanding shares of Diamond Offshore Common Stock and is in a position to control actions that require the consent of stockholders, including the election of directors, amendment of the Certificate and any mergers or any sale of substantially all of the assets of Diamond Offshore.

Holders of shares of Diamond Offshore Common Stock have no exchange, conversion or preemptive rights and such shares are not subject to redemption. All outstanding shares of Diamond Offshore Common Stock are duly authorized, validly issued, fully paid and non-assessable. Subject to the prior rights, if any, of holders of any outstanding class or series of capital stock having a preference in relation to Diamond Offshore Common Stock as to distributions upon the dissolution, liquidation and winding-up of Diamond Offshore and as to dividends, holders of Diamond Offshore Common Stock are entitled to share ratably in all assets of Diamond Offshore which remain after payment in full of all debts and liabilities of Diamond Offshore, and to receive ratably such dividends, if any, as may be declared by Diamond Offshore's Board of Directors from time to time out of funds and other property legally available therefor. See "Dividend Policy" and "Capitalization."

PREFERRED STOCK

The Board of Directors is authorized, without action by the holders of Diamond Offshore Common Stock, to issue up to 25,000,000 shares of preferred stock, $.01 par value (the "Preferred Stock"), in one or more series, to establish the number of shares to be included in each such series and to fix the designations, preferences, relative, participating, optional and other special rights of the shares of each such series and the qualifications, limitations and restrictions thereof. Such matters may include, among others, voting rights, conversion and exchange privileges, dividend rates, redemption rights, sinking fund provisions and liquidation rights that could be superior and prior to Diamond Offshore Common Stock.

The issuance of one or more series of the Preferred Stock could, under certain circumstances, adversely affect the voting power of the holders of Diamond Offshore Common Stock and could have the effect of discouraging or making more difficult any attempt by a person or group to effect a change in control of Diamond Offshore.

DELAWARE BUSINESS COMBINATION STATUTE

Diamond Offshore is a Delaware corporation and is subject to Section 203 ("Section 203") of the Delaware General Corporation Law (the "DGCL"). In general, Section 203 will prevent an "interested stockholder" (defined generally as a person owning 15% or more of a corporation's outstanding voting stock) of Diamond Offshore from engaging in a "business combination" (as therein defined) with Diamond Offshore for three years following the date such person became an interested stockholder, unless (i) before such person became an interested stockholder, the Board of Directors of Diamond Offshore approved the business combination in question, or the transaction which resulted in such person becoming an interested stockholder, (ii) upon consummation of the transaction that resulted in the interested stockholder becoming such, the interested stockholder owns at least 85% of the voting stock of Diamond Offshore outstanding at the time such transaction commenced (excluding stock held by directors who are also officers of Diamond Offshore and by employee stock plans that do not provide employees with rights to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer), or (iii) following the transaction in which such person became an interested stockholder, the business combination is approved by the Board of Directors of Diamond Offshore and authorized at a meeting of stockholders by the affirmative vote of the holders of not less than 66 2/3% of the outstanding voting stock of Diamond Offshore not owned by the interested stockholder. Under Section 203, the restrictions described above do not apply to certain business combinations proposed by an interested stockholder following the announcement (or notification) of one of certain extraordinary transactions involving Diamond Offshore and a person who had not been an interested stockholder during the preceding three years or who became an interested stockholder with the approval of Diamond Offshore's directors, and which transactions are approved or not opposed by a majority of the members of the Board of Directors then in office who were directors prior to any person becoming an interested stockholder during the previous three years or were recommended for election or elected to succeed such directors by a majority of such directors.

Section 203 does not apply to Loews because it has been more than three years since Loews became an interested stockholder.

POTENTIAL RESTRICTIONS ON SALES OF DIAMOND OFFSHORE COMMON STOCK TO NON-U.S. CITIZENS

Pursuant to recent amendments to United States maritime laws relating to sales of interests in and control of vessels owned by United States citizens to non-citizens, the Secretary of Transportation, acting through the United States Maritime Administration, has prior consent authority over certain transfers of Diamond Offshore's capital stock. See "Business -- Limitation on Ownership by Non-U.S. Citizens."

TRANSFER AGENT AND REGISTRAR

Chemical Mellon Shareholder Services, L.L.C., whose principal offices are located at 450 West 33rd Street, New York, New York 10001, acts as transfer agent and registrar for Diamond Offshore Common Stock.

PLAN OF DISTRIBUTION

Any distribution of the Offered Shares by the Selling Stockholders may be effected from time to time in one or more of the following transactions (which may involve crosses or block transactions): (i) on the NYSE (or on such other national stock exchanges on which the Diamond Offshore Common Stock may be listed from time to time) in transactions which may include special offerings, exchange distributions and/or secondary distributions pursuant to and in accordance with the rules of such exchanges, including sales to underwriters who will acquire the Offered Shares for their own account and resell them in one or more transactions or through brokers, acting as principal or agent, (ii) in the over-the-counter market, including sales through brokers, acting as principal or agent, (iii) in transactions other than on such exchanges or in the over-the-counter market, or a combination of such transactions, including sales through brokers, acting as principal or agent, (iv) through the issuance of securities by issuers other than Diamond Offshore convertible into, exchangeable for, or payable in such shares (whether such securities are listed on a national securities exchange or otherwise) or (v) through the writing of options on the shares (whether such options are listed on an options exchange or otherwise). Any such transactions may be effected at market prices prevailing at the time of sale, at prices related to such prevailing market prices, at negotiated prices or at fixed prices.

The Selling Stockholders and any such underwriters, brokers, dealers or agents, upon effecting the sale of the Offered Shares may be deemed "underwriters" as that term is defined by the Securities Act.

Underwriters participating in any offering made pursuant to this Prospectus (as amended or supplemented from time to time) may receive underwriting discounts and commissions, and discounts or concessions may be allowed or reallowed or paid to dealers, and brokers or agents participating in such transactions may receive brokerage or agent's commissions or fees.

In order to comply with the securities laws of certain states, if applicable, the Offered Shares will be sold in such jurisdictions only through registered or licensed brokers or dealers. In addition, in certain states the Offered Shares may not be sold unless the Offered Shares have been registered or qualified for sale in such state or any exemption from registration or qualification is available and complied with.

Pursuant to the Shareholders Agreement, Diamond Offshore agreed to cause the Registration Statement to include a resale prospectus that would permit the Selling Stockholders to sell the Offered Shares without restriction and to keep the Registration Statement continuously effective for the Required Period. Diamond Offshore has agreed to pay certain expenses in connection with such registration, including (1) all registration and filing fees, (2) fees and expenses of compliance with securities or blue sky laws (including reasonable fees and disbursements of counsel in connection with blue sky qualifications of the securities registered), (3) printing expenses, (4) internal expenses of Diamond Offshore (including, without limitation, all salaries and expenses of its officers and employees performing legal or accounting duties), (5) reasonable fees and disbursements of counsel for Diamond Offshore and customary fees and expenses for independent certified public accountants retained by Diamond Offshore (including the expenses of any comfort letters or costs associated with the delivery by independent certified public accountants of a comfort letter or comfort letters but excluding costs associated with special audits), (6) the reasonable fees and expenses of any special experts retained by Diamond Offshore in connection with such registration, (7) fees and expenses in connection with any review of underwriting arrangements by the National Association of Securities Dealers, Inc. including fees and expenses of any "qualified independent underwriter" in connection with an underwritten offering and (8) fees and disbursements of underwriters customarily paid by issuers or sellers of securities in connection with an underwritten offering. Diamond Offshore will not be responsible for any underwriting fees, discounts or commissions in connection with an underwritten offering or any out-of-pocket expenses (including counsel fees and expenses) of the Selling Stockholders or any fees and expenses of underwriters' counsel in connection with an underwritten offering. In addition, the Selling Stockholders have agreed to pay all costs of any special audits in connection with an underwritten offering and have agreed to pay, or in the case of an underwritten offering to cause the underwriters to pay, all out-of-pocket expenses of Diamond Offshore in connection with any domestic "road show" presentations. Diamond Offshore and the Selling Stockholders have agreed to indemnify each other and certain other persons against certain liabilities in connection with the offering of the Offered Shares including liabilities arising under the Securities Act. In connection with an underwritten offering, Diamond Offshore has agreed to indemnify any underwriter thereof and certain other persons to the same extent as provided with respect to the indemnification of the Selling Stockholder(s) if such underwriter agrees to indemnify Diamond Offshore to the same extent as provided with respect to the indemnification of Diamond Offshore by such Selling Stockholder(s). See "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders."

LEGAL MATTERS

The validity of the shares of Diamond Offshore Common Stock offered hereby will be passed on for Diamond Offshore by Weil, Gotshal & Manges LLP, Houston, Texas.

EXPERTS

The consolidated financial statements of Diamond Offshore as of December 31, 1995 and 1994, and for each of the three years in the period ended December 31, 1995 included herein have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report appearing herein and are included in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

The consolidated financial statements of Arethusa as of September 30, 1995 and 1994, and for each of the three years in the period ended September 30, 1995 included in this Prospectus, have been audited by Arthur Andersen & Co., independent public accountants, as indicated in their reports with respect thereto, and are included herein in reliance upon the authority of said firm as experts in accounting and auditing.

INDEX TO FINANCIAL STATEMENTS

INDEPENDENT AUDITORS' REPORT

Board of Directors and Stockholders
Diamond Offshore Drilling, Inc. and Subsidiaries
Houston, Texas

We have audited the accompanying consolidated balance sheets of Diamond Offshore Drilling, Inc. and subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Diamond Offshore Drilling, Inc. and subsidiaries as of December 31, 1995 and 1994, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles.

Deloitte & Touche LLP
Houston, Texas

January 29, 1996
(February 13, 1996 as to Note 12)

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	DECEMBER 31, 1995	DECEMBER 31, 1994
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 10,306	$ 17,770
Short-term investments	5,041	4,926
Accounts receivable	74,496	57,804
Rig inventory and supplies	15,330	15,024
Prepaid expenses and other	10,601	3,970
Total current assets	115,774	99,494
DRILLING AND OTHER PROPERTY AND EQUIPMENT, LESS ACCUMULATED DEPRECIATION	502,278	488,664
Total assets	$ 618,052	$ 588,158
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 18,322	$ 13,596
Accrued liabilities	33,929	28,377
Total current liabilities	52,251	41,973
NOTES PAYABLE TO LOEWS	--	394,777
DEFERRED TAX LIABILITY	72,907	27,342
Total liabilities	125,158	464,092
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Preferred stock (par value $.01, 25,000,000 shares authorized, none issued and outstanding at December 31, 1995)	--	--
Common stock (par value $.01, 200,000,000 shares authorized, 50,000,000 shares issued and outstanding and par value $1.00, 1,000 shares authorized, 100 shares issued and outstanding at December 31, 1995 and 1994, respectively)	500	1
Additional paid-in capital	665,107	289,685
Accumulated deficit	(171,444)	(164,418)
Cumulative translation adjustment	(1,269)	(1,202)
Total stockholders' equity	492,894	124,066
Total liabilities and stockholders' equity	$ 618,052	$ 588,158

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
REVENUES	$336,584	$307,918	$288,069
OPERATING EXPENSES:			
Contract drilling	259,560	256,919	228,211
General administrative	13,857	11,993	11,785
Depreciation	52,865	55,366	46,819
Gain on sale of assets	(1,349)	(1,736)	(3,201)
Total operating expenses	324,933	322,542	283,614
OPERATING INCOME (LOSS)	11,651	(14,624)	4,455
Other income (expense):			
Interest expense	(27,052)	(31,346)	(25,906)
Currency transaction losses	(191)	(1,316)	(1,474)
Other, net	1,789	861	1,255
LOSS BEFORE INCOME TAX BENEFIT	(13,803)	(46,425)	(21,670)
INCOME TAX BENEFIT	6,777	11,621	5,041
NET LOSS	$ (7,026)	$(34,804)	$(16,629)
PRO FORMA NET INCOME PER SHARE (NOTE 1)	$ 0.20		

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(IN THOUSANDS, EXCEPT NUMBER OF SHARES)

	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL PAID-IN CAPITAL	ACCUMULATED DEFICIT	CUMULATIVE TRANSLATION ADJUSTMENT	TOTAL STOCKHOLDERS' EQUITY
DECEMBER 31, 1992	100	$ 1	$ 389,685	$(112,985)	$(1,401)	$ 275,300
Net loss	--	--	--	(16,629)	--	(16,629)
Exchange rate changes, net	--	--	--	--	(310)	(310)
Dividend to Loews	--	--	(100,000)	--	--	(100,000)
DECEMBER 31, 1993	100	1	289,685	(129,614)	(1,711)	158,361
Net loss	--	--	--	(34,804)	--	(34,804)
Exchange rate changes, net	--	--	--	--	509	509
DECEMBER 31, 1994	100	1	289,685	(164,418)	(1,202)	124,066
Net loss	--	--	--	(7,026)	--	(7,026)
Exchange rate changes, net	--	--	--	--	(67)	(67)
Capital contribution	--	--	39,676	--	--	39,676
350,500-for-one stock split	35,049,900	350	(350)	--	--	--
Issuance of common stock from initial public offering	14,950,000	149	338,214	--	--	338,363
Dividend to Loews	--	--	(2,118)	--	--	(2,118)
DECEMBER 31, 1995	50,000,000	$500	$ 665,107	$(171,444)	$(1,269)	$ 492,894

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
OPERATING ACTIVITIES:			
Net loss	$ (7,026)	$(34,804)	$(16,629)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation	50,794	49,908	46,819
Write-down of asset	2,071	5,458	--
Gain on sale of assets and other	(1,349)	(1,736)	(3,201)
Accrued interest converted to notes payable to Loews	27,044	31,294	25,894
Deferred tax benefit	(7,472)	(13,534)	(8,053)
Changes in operating assets and liabilities:			
Accounts receivable	(16,692)	4,458	(16,376)
Rig inventory and supplies and other current assets	(4,896)	(698)	(1,393)
Accounts payable and accrued liabilities	10,278	1,455	6,184
Other, net	29	761	(341)
Net cash provided by operating activities	52,781	42,562	32,904
INVESTING ACTIVITIES:			
Purchase of St. Vincent Drilling Ltd	--	--	(10,600)
Acquisition of drilling rigs and related equipment	--	(25,000)	--
Capital expenditures	(66,646)	(21,146)	(14,345)
Proceeds from sale of assets	1,516	2,486	4,194
Change in short-term investments	(115)	95	20
Net cash used in investing activities	(65,245)	(43,565)	(20,731)
FINANCING ACTIVITIES:			
Net (repayments) borrowings (to) from Loews	(331,245)	10,000	(5,627)
Proceeds from issuance of common stock	338,363	--	--
Dividend to Loews	(2,118)	--	--
Net cash provided by (used in) financing activities	5,000	10,000	(5,627)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(7,464)	8,997	6,546
Cash and cash equivalents, beginning of year	17,770	8,773	2,227
Cash and cash equivalents, end of year	$ 10,306	$ 17,770	$ 8,773

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Business

Diamond Offshore Drilling, Inc. (the "Company") was incorporated in Delaware on April 13, 1989. Loews Corporation ("Loews"), a Delaware corporation of which the Company had been a wholly owned subsidiary prior to the initial public offering in October 1995 (the "Common Stock Offering"), owns 70.1% of the outstanding common stock of the Company (see Note 2).

The Company engages principally in the contract drilling of offshore oil and gas wells primarily for independent and major integrated oil companies and state-owned oil companies. The Company's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Southeast Asia and consists of 22 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 14 jack-up rigs and one drillship. The Company also operates 10 land rigs deployed in South Texas. All of the Company's offshore and land rigs are wholly owned.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company after elimination of significant intercompany transactions and balances.

Cash and Cash Equivalents

All short-term, highly liquid investments that have an original maturity of three months or less are considered cash equivalents.

Supplementary Cash Flow Information

Non-cash financing activities for the year ended December 31, 1995 included a capital contribution by Loews in September 1995 of $39.7 million which reduced the outstanding debt to Loews. In addition, $27.0 million of interest expense was accrued and included in "Notes payable to Loews" prior to such notes being repaid with a portion of the proceeds from the Common Stock Offering (see Note 2). In connection with the Common Stock Offering, the tax sharing agreement with Loews was terminated and all liabilities were settled by offsetting $50.9 million owed by Loews to the Company under the agreement against notes payable to Loews.

Non-cash financing activities for the years ended December 31, 1994 and 1993 included $31.3 million and $25.9 million, respectively, of interest expense accrued and included in "Notes payable to Loews." Non-cash financing activities for 1993 also included a $100.0 million dividend declared to Loews in the form of additional debt (see Note 7).

Rig Inventory and Supplies

Inventories primarily consist of replacement parts and supplies held for use in the operations of the Company. Inventories are stated at the lower of cost or estimated value.

Drilling and Other Property and Equipment

Drilling and other property and equipment is carried at cost. Maintenance and repairs are charged to income currently while replacements and betterments are capitalized. Costs incurred for major rig upgrades are accumulated in construction work in progress, with no depreciation recorded on the additions, until the month the upgrade is completed and the rig is placed into service. Upon retirement or other disposal of fixed assets, the cost and related accumulated depreciation are removed from the respective accounts and any gains or losses are included in the results of operations.

For financial reporting purposes, depreciation is provided on the straight-line method over the remaining estimated useful lives from the date the asset is placed into service. The estimated useful lives of the Company's offshore drilling rigs range from 10 to 25 years. Other property and equipment is estimated to have useful lives ranging from 3 to 10 years.

Impairment of Long-Lived Assets

The Company reviews its long-lived assets for impairment when changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

In 1995, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." SFAS No. 121 requires that long-lived assets and certain identifiable intangibles to be held and used be reported at the lower of carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to the Company are recorded at the lower of carrying amount or fair value less cost to sell. The adoption of SFAS No. 121 did not have a material effect on the Company's financial position or results of operations.

Income Taxes

Taxable income (loss) of the Company and its domestic subsidiaries was included in the consolidated U.S. federal income tax return of Loews and other members of the Loews affiliated group for all taxable periods ending prior to the Common Stock Offering. Thereafter, the taxable income (loss) of the Company and its domestic subsidiaries is included in the consolidated U.S. federal income tax return of the Company and its affiliated group.

Deferred income taxes are recognized for the effect of temporary differences between financial and tax reporting. Except for selective dividends, the Company intends to reinvest the unremitted earnings of its non-U.S. subsidiaries and postpone their remittance indefinitely. Thus, no additional U.S. taxes have been provided on earnings of these non-U.S. subsidiaries. The Company's non-U.S. income tax liabilities are based upon the results of operations of the various subsidiaries in those jurisdictions in which they are subject to taxation.

Revenue Recognition

Income from dayrate drilling contracts is recognized currently. In connection with such drilling contracts, the Company may receive lump-sum fees for the mobilization of equipment and personnel. The net of mobilization fees received and costs incurred to mobilize an offshore rig from one market to another is recognized over the term of the related drilling contract. Absent a contract, mobilization costs are recognized currently. Revenues received from customers for asset enhancements relating to specific contracts are deferred and amortized to income over the term of the drilling contract.

Income from offshore turnkey contracts is recognized on the completed contract method, with revenues accrued to the extent of costs until the specified turnkey depth and other contract requirements are met. Provisions for future losses on turnkey contracts are recognized when it becomes apparent that contract drilling expenses to be incurred on a specific contract will exceed the revenue from the contract.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Currency Translation

The Company's primary functional currency is the U.S. dollar. Certain of the Company's subsidiaries use the local currency in the country where they conduct operations as their functional currency. These subsidiaries translate assets and liabilities at year-end exchange rates while income and expense accounts are translated at average exchange rates. Translation adjustments are reflected in the stockholders' equity section titled "Cumulative translation adjustment." Currency transaction gains and losses are included in current operating results. Additionally, translation gains and losses of subsidiaries operating in hyperinflationary economies are included in operating results currently.

Research and Development Expenses

Research and development expenses are expensed when incurred and are reflected in the Consolidated Statements of Operations in "Contract drilling expenses." For the year ended December 31, 1995, research and development expenses of approximately $.6 million were incurred in connection with preliminary feasibility studies for the development of an ultra-large semisubmersible, the Ocean Legend. There were no research and development expenses for the years ended December 31, 1994 and 1993.

Pro Forma Net Income Per Share Data

As described in Note 2, after its initial public offering, the Company had 50,000,000 shares of common stock outstanding. Assuming the Common Stock Offering had occurred at the beginning of the period, the Company would have recognized net income of $10.0 million, or $0.20 per share, after adjusting for the after-tax effects of a reduction in interest expense.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimated.

Reclassifications

Certain amounts applicable to the prior periods have been reclassified to conform to the classifications currently followed. Such reclassifications do not affect earnings.

2. COMMON STOCK OFFERING

Pursuant to the Common Stock Offering, the Company sold 14,950,000 shares of common stock, including 1,950,000 shares from an over-allotment option. Subsequent to the Common Stock Offering, the exercise of the over-allotment option and a 350,500-for-one stock split, which was effective immediately prior to consummation of the Common Stock Offering, the Company had 50,000,000 shares of common stock outstanding.

Proceeds from the Common Stock Offering were used to repay all of the Company's then outstanding debt to Loews of $336.2 million and the remainder of such proceeds was used to pay Loews a special dividend of $2.1 million. In addition, pursuant to a termination and settlement agreement, all assets and liabilities under the tax sharing agreement with Loews were settled by offsetting amounts owed by Loews to the Company thereunder against notes payable to Loews (see Note 8).

3. SHORT-TERM INVESTMENTS

The Company has entered into a pledge agreement with a bank whereby the bank has or will extend various financial accommodations to or for the account of the Company, including issuing letters of credit, entering into foreign exchange contracts or permitting intra-day overdrafts. In consideration of and as a condition precedent to the making of such financial accommodations by the bank, the Company is required to maintain a pledged collateral account in which the bank has a continuing security interest. As of December 31, 1995 and 1994, the Company had $5.0 million and $4.9 million, respectively, in U.S. Treasury Bills deposited in such pledged collateral account.

4. DRILLING AND OTHER PROPERTY AND EQUIPMENT

Cost and accumulated depreciation of drilling and other property and equipment are summarized as follows:

	DECEMBER 31, 1995	DECEMBER 31, 1994
	(IN THOUSANDS)	
Drilling rigs and equipment	$ 689,438	$ 645,922
Construction work in progress	19,016	--
Land and buildings	3,655	3,599
Office equipment and other	6,300	5,391
	718,409	654,912
Less accumulated depreciation	(216,131)	(166,248)
Total	$ 502,278	$ 488,664

Construction Work in Progress

The Company entered into letters of intent with two major oil companies for three-year commitments on both the Ocean Quest and Ocean Star (formerly named Ocean Countess) pursuant to which the rigs are being upgraded to conduct drilling operations in the Gulf of Mexico deep water market. The upgrade projects include stability enhancements to provide additional hull buoyancy, the addition of a new mooring system, and drilling system upgrades. In connection with these upgrades, the Company mobilized the Ocean Star, which had been previously idle in the North Sea, to the Gulf of Mexico during the fourth quarter of 1995. Both rigs entered the shipyard to begin their upgrades in December 1995 and are scheduled to be placed into service in the fourth quarter of 1996. As of December 31, 1995, $6.6 million and $3.2 million of construction work in progress was related to the Ocean Quest and Ocean Star, respectively. The remaining $9.2 million of construction work in progress was related to upgrades to prepare the Ocean Baroness and Ocean Princess for contracts in Brazil and the North Sea, respectively.

Impairment of Assets

During 1995 and 1994, the Company recorded impairment losses of $2.1 million and $5.5 million, respectively, to decrease the carrying value of two semisubmersible drilling rigs (one located in the Gulf of Mexico and the other located in South America). The rig in the Gulf of Mexico was sold in the fourth quarter of 1995 and management plans to sell the rig in South America during 1996. The impairment losses represent the amount by which the carrying value of the rigs exceeded the fair value of such rigs, based on expected future cash flows to be generated by such rigs. The impairment losses, reflected in "Depreciation" in the Consolidated Statements of Operations, reduce the carrying value of both rigs to zero. Operating losses provided by the rig located in the Gulf of Mexico during the years ended December 31, 1995, 1994 and 1993 were approximately $2,000, $324,000 and $333,000, respectively. Operating income (loss) contributed by the rig located in South America during the years ended December 31, 1995, 1994 and 1993 was approximately $(.6) million, $(2.1) million and $2.4 million, respectively.

5. ACCRUED LIABILITIES

Accrued liabilities consist of the following:

	DECEMBER 31, 1995	DECEMBER 31, 1994
	(IN THOUSANDS)	
Compensation and benefits	$17,402	$15,480
Other	16,527	12,897
Total	$33,929	$28,377

6. FINANCIAL INSTRUMENTS

Concentrations of Credit Risk

Financial instruments which potentially subject the Company to significant concentrations of credit risk consist primarily of cash and trade accounts receivable. The Company maintains cash and cash equivalents and certain other financial instruments with various financial institutions. An accounting loss would occur if one or more of these institutions fails to perform according to the terms of its agreements. However, these financial institutions are located throughout the world, and the Company's strategy is designed to limit exposure to any one institution. The Company's periodic evaluations of the relative credit standing of these financial institutions are considered in the Company's investment strategy.

Concentrations of credit risk with respect to trade accounts receivable are limited due to the large number of entities comprising the Company's customer base. Since the market for the Company's services is the oil and gas industry, this customer base consists primarily of major oil companies and independent oil and gas producers. The Company provides allowances for potential credit losses when necessary. No such allowances were deemed necessary for the years presented. As of December 31, 1995 and 1994, the Company had no significant concentrations of credit risk.

Fair Values

SFAS No. 107 "Disclosure about Fair Value of Financial Instruments," requires the disclosure of the fair value of all financial instruments, both assets and liabilities, for which it is practicable to estimate fair value. The Company's financial instruments include short-term investments, accounts receivable and notes payable to Loews. The carrying amounts of the Company's financial instruments approximate fair value due to the nature of such instruments. The estimated fair value amounts have been determined by the Company using appropriate valuation methodologies and information available to management as of December 31, 1995 and 1994. Considerable judgment is required in developing these estimates, and accordingly, no assurance can be given that the estimated values are indicative of the amounts that would be realized in a free market exchange.

The carrying amount of the Company's investment in U.S. Treasury Bills is at fair value based upon the closing market prices obtained from public sources. The Company believes it has the ability to hold its fixed income investment until maturity. However, the Company may sell its securities and reinvest the proceeds to take advantage of opportunities generated by changing interest rates. Therefore, the Company considers its securities as available for sale.

7. NOTES PAYABLE TO AND TRANSACTIONS WITH LOEWS

As described in Note 2, a portion of the proceeds from the Common Stock Offering was used to repay all of the Company's then outstanding debt to Loews of $336.2 million. Prior to the Common Stock Offering, the Company received from Loews loans for acquisitions, capital expenditures and working capital depending on its cash requirements and cash position. These loans, net of amounts repaid, were $41.3 million and

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

$20.3 million, including interest at 10 percent per annum of $26.3 million and $24.7 million, during the years ended December 31, 1994 and 1993, respectively. Loews had represented to the Company that no repayment of the debt outstanding was required within twelve months and the debt was, therefore, classified as noncurrent at December 31, 1994.

On October 7, 1993, the Company declared a $100.0 million dividend to Loews in the form of additional debt, with interest accruing at 5 percent per annum. Interest accrued at December 31, 1994 and 1993 was $5.0 million and $1.2 million, respectively.

The Company and Loews have entered into a services agreement which was effective upon consummation of the Common Stock Offering (the "Services Agreement") pursuant to which Loews agreed to continue to perform certain administrative and technical services on behalf of the Company. Such services include personnel, telecommunications, purchasing, internal auditing, accounting, data processing and cash management services, in addition to advice and assistance with respect to preparation of tax returns and obtaining insurance. Under the Services Agreement, the Company is required to reimburse Loews for (i) allocated personnel costs (such as wages, salaries, employee benefits and payroll taxes) of the Loews personnel actually providing such services and (ii) all out-of-pocket expenses related to the provision of such services. The Services Agreement may be terminated at the Company's option upon 30 days' notice to Loews and at the option of Loews upon six months' notice to the Company. In addition, the Company has agreed to indemnify Loews for all claims and damages arising from the provision of services by Loews under the Services Agreement, unless due to the gross negligence or willful misconduct of Loews. Prior to the Common Stock Offering, Loews provided such services at an allocated rate. The Company has been charged $.7 million, $.9 million and $.6 million by Loews for these support functions during the years ended December 31, 1995, 1994 and 1993, respectively.

Subsequent to the Common Stock Offering, Loews provided the Company with a $150.0 million revolving line of credit available through October 31, 1996 or until alternative financing is arranged. Borrowings under the line of credit bear interest, at the Company's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. The line of credit is unsecured, has no financial or restrictive covenants, and the Company is not required to pay a commitment fee to Loews. As of December 31, 1995, there were no amounts outstanding under this line of credit.

8. INCOME TAXES

The Company and its subsidiaries were party to a tax sharing agreement with Loews and the Company has provided a tax provision calculated as if on a stand-alone basis for U.S. federal income tax purposes prior to the Common Stock Offering. In conjunction with the Common Stock Offering, the tax sharing agreement was terminated and all assets and liabilities were settled by offsetting amounts owed by Loews to the Company under the agreement against notes payable to Loews (see Note 2).

An analysis of the Company's income (taxes) benefits is as follows:

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
	(IN THOUSANDS)		
U.S. -- current	$ --	$ --	$ --
U.S. -- deferred	7,472	13,559	8,558
Non-U.S. -- current	(489)	(1,541)	(2,519)
Non-U.S. -- deferred	--	(25)	(505)
State and other	(206)	(372)	(493)
Total	$6,777	$11,621	$ 5,041

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Significant components of the Company's net deferred tax liability are as follows:

	DECEMBER 31, 1995	DECEMBER 31, 1994
	(IN THOUSANDS)	
DEFERRED TAX ASSETS:		
Net operating loss carryforwards	$ 15,641	$ 69,241
Investment tax credit carryforwards	7,638	8,838
U.S. taxes on foreign income	8,136	7,180
Workers compensation accruals(1)	2,971	930
Foreign tax credits	5,160	3,060
Other	432	1,432
Total deferred tax assets	$ 39,978	$ 90,681
DEFERRED TAX LIABILITIES:		
Drilling and other property and equipment	(98,401)	(106,288)
Non-U.S. deferred taxes	(10,146)	(10,060)
Other	(1,367)	(745)
Total deferred liabilities	(109,914)	(117,093)
Net deferred tax liability	$ (69,936)	$ (26,412)

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(1) Reflected in "Prepaid expenses and other" in the Company's Consolidated Balance Sheets.

In connection with the purchase of Odeco Drilling Inc. in 1992, the Company acquired net operating loss ("NOL") and investment tax credit ("ITC") carryforwards available to offset future taxable income. The amount of these acquired NOL and ITC carryforwards, which are expected to be utilized on future income tax returns, is $49.9 million and $8.8 million, respectively. At December 31, 1995, the Company has recorded a deferred tax asset for the NOL and ITC carryforwards available, including those generated subsequent to the Common Stock Offering, which expire as follows:

YEAR	TAX BENEFIT OF NET OPERATING LOSSES	INVESTMENT TAX CREDITS
	(IN THOUSANDS)	
2001	$ 8,134	$ --
2002	--	--
2003	2,627	7,638
2004	216	--
2005	66	--
2006	272	--
2008	2,321	--
2010	2,005	--
Total	$ 15,641	$7,638

No valuation allowance has been provided on the Company's deferred tax assets because management believes that future reversals of existing taxable temporary differences will generate taxable income sufficient to utilize these benefits. However, if the Company is unable to generate sufficient taxable income in the future through operating results, a valuation allowance will be required through a charge to expense.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

A reconciliation of the expected income tax benefit resulting from the use of statutory tax rates to the effective income tax benefit follows:

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
	(IN THOUSANDS)		
Income (loss) before income tax benefit:			
U.S.	$(19,591)	$(29,667)	$(26,290)
Non-U.S.	5,788	(16,758)	4,620
Worldwide	$(13,803)	$(46,425)	$(21,670)
Expected tax benefit at statutory rate	$ 4,831	$ 16,249	$ 7,585
Increase in U.S. statutory rate	--	--	(1,530)
Non-U.S. income (loss):			
Impact of taxation at different rates	1,270	1,716	198
Impact of non-U.S. losses for which a current tax benefit is not available	(1,004)	(6,094)	(2,490)
State taxes and other	1,680	(250)	1,278
Income tax benefit	$ 6,777	$ 11,621	$ 5,041

As a result of legislation enacted in August 1993, the federal tax rate for corporations was increased from 34 to 35 percent, effective January 1, 1993. An adjustment of $1.5 million to increase the net federal deferred tax liability was recorded in the third quarter of 1993 for the effect of such legislation.

Undistributed earnings of non-U.S. subsidiaries for which no deferred income tax provision has been made for possible future remittances totaled approximately $46.1 million at December 31, 1995. Substantially all of this amount represents earnings reinvested as part of the Company's ongoing business. It is not practicable to estimate the amount of taxes that might be payable on the eventual remittance of such earnings. On remittance, certain countries impose withholding taxes that, subject to certain limitations, are then available for use as tax credits against a U.S. tax liability, if any. The Company also has certain income tax loss carryforwards in non-U.S. tax jurisdictions to which it has assigned no value because of the uncertainty of utilization of these carryforwards.

9. EMPLOYEE BENEFIT PLANS

The Company maintains defined contribution retirement plans for its U.S. and U.K. employees. The plan for U.S. employees is designed to qualify under Section 401(k) of the Internal Revenue Code of 1986, as amended. Under the plan for U.S. employees, each participant may elect to defer taxation on a portion of his or her eligible earnings, as defined by the plan, by directing the Company to withhold a percentage of such earnings. A participating employee may also elect to make after-tax contributions to the plan. The Company contributes 3.75 percent of a participant's defined compensation. For the years ended December 31, 1995, 1994 and 1993, the Company's provision for contributions was $2.4 million, $2.3 million and $2.0 million, respectively.

The plan for U.K. employees provides that the Company contribute amounts equivalent to the employee's contributions generally up to a maximum of 3 percent of the employee's defined compensation per year. For the years ended December 31, 1995, 1994 and 1993, the Company's provision for contributions was $.2 million, $.2 million and $.3 million, respectively.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

10. COMMITMENTS AND CONTINGENCIES

The Company leases office facilities under operating leases which expire through the year 2000. Total rent expense amounted to $1.5 million, $1.5 million and $.9 million for the years ended December 31, 1995, 1994 and 1993, respectively. Minimum future rental payments under leases are approximately $327,000, $85,000, $15,000, $15,000 and $10,000 for the years 1996 to 2000, respectively (see Note 12).

Various claims have been filed against the Company in the ordinary course of business, particularly claims alleging personal injuries. Management believes that the Company has established adequate reserves on its books for any liabilities that may reasonably be expected to result from these claims. In the opinion of management, no pending or threatened claims, actions or proceedings against the Company are expected to have a material adverse effect on the Company's financial position or results of operations.

As security for certain bids and performance on certain contracts, the Company is contingently liable as of December 31, 1995 and 1994 in the amount of $.8 million and $1.1 million, respectively, under performance/bid bonds. On the Company's behalf, banks have issued letters of credit securing these bonds.

11. GEOGRAPHIC AREA ANALYSIS AND MAJOR CUSTOMERS

The following table summarizes, by geographic area, operating revenues and operating income (loss) for the years ended December 31, 1995, 1994 and 1993, and identifiable assets at the end of those periods.

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
	(IN THOUSANDS)		
OPERATING REVENUES:			
United States	$213,998	$203,198	$158,916
Europe/Africa	47,645	19,159	47,765
Australia/Southeast Asia	53,113	57,129	30,284
South America	21,828	26,133	32,489
Other areas	--	2,299	18,615
Total	$336,584	$307,918	$288,069
OPERATING INCOME (LOSS):			
United States	$ 19,002	$ 4,125	$ 12,255
Europe/Africa	5,753	(10,365)	(8,432)
Australia/Southeast Asia	(7,675)	2,783	(5,960)
South America	(5,429)	(11,546)	3,943
Other areas	--	379	2,649
Total	$ 11,651	$(14,624)	$ 4,455
IDENTIFIABLE ASSETS:			
United States	$386,282	$366,575	$327,370
Europe/Africa	165,277	125,773	153,619
Australia/Southeast Asia	36,705	48,059	47,386
South America	29,788	47,751	48,014
Other areas	--	--	15,773
Total	$618,052	$588,158	$592,162

A substantial portion of the Company's assets are mobile, therefore, asset locations at the end of the period are not necessarily indicative of the geographic distribution of the earnings generated by such assets during the periods.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

The assets located outside the U.S. include cash and cash equivalents of $1.3 million, $2.5 million and $3.3 million at December 31, 1995, 1994 and 1993, respectively.

The Company has performed drilling activities for certain major customers. For the year ended December 31, 1995, one customer contributed 16.5 percent of total revenues. For the year ended December 31, 1994, no single customer contributed 10.0 percent or more of total revenues. For the year ended December 31, 1993, one customer contributed 10.5 percent of total revenues.

12. SUBSEQUENT EVENTS

Arethusa (Off-Shore) Limited Acquisition

The Company and Arethusa (Off-Shore) Limited, a Bermuda company ("Arethusa"), have entered into an agreement to merge the two companies. The agreement provides that, upon consummation of the merger, holders of Arethusa stock will receive 17.9 million shares of common stock to be issued by the Company based on 20.3 million shares of Arethusa's common stock issued and outstanding and on a ratio of .88 shares for each share of issued and outstanding Arethusa common stock. The merger is subject to requisite shareholder approval. It is anticipated that the consummation of the merger will occur no later than July 31, 1996. The merger will be accounted for as a purchase for financial reporting purposes, and accordingly, the costs of the merger will be allocated to assets acquired and liabilities assumed based on their estimated fair market values.

Arethusa owns a fleet of 11 mobile offshore drilling rigs, operates two additional mobile offshore drilling rigs, and provides drilling services worldwide to domestic, international and state-owned oil and gas companies. For the year ended September 30, 1995, Arethusa reported revenues of $122.1 million, net income of $21.6 million, and net income per share of $1.06. The following pro forma information presents the consolidated results of operations, assuming consummation of the merger had occurred at the beginning of the period. The historical operating results for the Company included in the pro forma financial data have been adjusted to give effect to the Common Stock Offering and interest expense for working capital borrowings.

	PRO FORMA YEAR ENDED DECEMBER 31, 1995 (IN THOUSANDS, EXCEPT PER SHARE DATA)
Revenues	$456,750
Operating income	3,347
Net loss	(963)
Net loss per share	(0.01)

Building Purchase

In February 1996, the Company purchased for approximately $8.2 million the land and the eight-story building containing approximately 182,000 net rentable square feet on approximately 6.2 acres in which it had leased office space for its corporate headquarters. A portion of the building is currently occupied by other tenants under leases which expire through the year 2005. This purchase will reduce general and administrative expenses in the future by eliminating rent expense and will provide rental income from the leases, offset by depreciation and related interest expense. The Company, therefore, does not expect the result of this purchase to have a material effect on its results of operations.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Credit Facility

In February 1996, the Company executed a definitive credit agreement governing a $150.0 million credit facility with a group of banks (the "Diamond Offshore Bank Credit Facility"). This line of credit bears interest at the same per annum rate as the revolving line of credit with Loews. Borrowings are secured by security interests in certain of the Company's assets. The Diamond Offshore Bank Credit Facility also contains covenants that limit the amount of total consolidated debt, require the maintenance of certain consolidated financial ratios and limit dividends and similar payments. The Company is required to pay a commitment fee on the unused available portion of the maximum credit commitment. Upon execution of the definitive agreement for the Diamond Offshore Bank Credit Facility, the revolving line of credit with Loews was terminated.

13. UNAUDITED QUARTERLY FINANCIAL DATA

Unaudited summarized financial data by quarter for the years 1995 and 1994 is shown below. Per share information has not been provided for periods prior to the Common Stock Offering.

	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
1995:				
Revenues	$ 70,760	$ 76,106	$ 91,716	$ 98,002
Operating income (loss)	(8,730)	56	11,572	8,753
Income (loss) before income tax benefit	(16,861)	(8,299)	3,003	8,354
Net income (loss)	(11,572)	(2,770)	1,422	5,894
Pro forma net income per share(1)	--	--	--	0.13
1994:				
Revenues	$ 73,759	$ 75,074	$ 78,872	$ 80,213
Operating income (loss)	107	(3,248)	(4,535)	(6,948)
Loss before income tax benefit	(7,355)	(12,021)	(12,152)	(14,897)
Net loss	(8,555)	(8,505)	(7,929)	(9,815)

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(1) As described in Note 2, after its initial public offering, the Company had 50,000,000 shares of common stock outstanding. Assuming the Common Stock Offering had occurred at the beginning of the fourth quarter, the Company would have recognized net income of $6.4 million, or $0.13 per share, after adjusting for the after-tax effects of a reduction in interest expense.

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED CONDENSED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	DECEMBER 31, 1995	SEPTEMBER 30, 1995
ASSETS		
CURRENT ASSETS:		
Cash and cash investments	$ 27,215	$ 20,251
Restricted cash	2,345	2,469
Marketable equity securities	--	6,000
Accounts receivable	29,426	28,625
Supplies and spare parts, at cost	16,564	16,952
Prepayments and other current assets	1,305	1,206
Total current assets	76,855	75,503
MOBILE DRILLING RIGS AND EQUIPMENT, at cost	350,780	348,426
Accumulated depreciation	(119,244)	(111,102)
Net mobile drilling rigs and equipment	231,536	237,324
OTHER ASSETS	2,020	2,505
Total assets	$ 310,411	$ 315,332
LIABILITIES AND SHAREHOLDERS' INVESTMENT		
CURRENT LIABILITIES:		
Current maturities of long-term debt	$ 10,603	$ 10,603
Accounts payable	5,085	12,942
Accrued liabilities	3,625	4,050
Interest payable	641	662
Income taxes payable	328	302
Total current liabilities	20,282	28,559
LONG-TERM DEBT	58,587	62,175
DEFERRED CREDITS	700	1,000
OTHER LONG-TERM LIABILITIES	1,021	1,019
SHAREHOLDERS' INVESTMENT:		
Common stock, $.10 par value per share, 50,000 shares authorized, 20,333 shares issued and outstanding	2,033	2,033
Additional paid-in capital	218,800	218,800
Accumulated earnings	8,988	132
Unrealized gain on equity securities	--	1,614
Total shareholders' investment	229,821	222,579
Total liabilities and shareholders' investment	$ 310,411	$ 315,332

See accompanying notes.

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	THREE MONTHS ENDED DECEMBER 31,	
	1995	1994
CONTRACT DRILLING REVENUE	$40,364	$28,279
OPERATING EXPENSES:		
Direct costs	20,367	20,821
General and administrative	2,664	2,045
Depreciation	8,193	7,067
OPERATING INCOME (LOSS)	9,140	(1,654)
OPERATING INCOME (EXPENSE):		
Interest expense	(1,485)	(1,421)
Interest income	371	1,716
Gain on sales of equity securities	1,602	--
Loss on sales of assets	(17)	7
Other, net	(371)	(23)
INCOME (LOSS) BEFORE INCOME TAXES	9,240	(1,375)
TAX PROVISION	(384)	(315)
NET INCOME (LOSS)	$ 8,856	$(1,690)
EARNINGS (LOSS) PER COMMON SHARE	$ .44	$ (.08)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	20,333	20,333

See accompanying notes.

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	THREE MONTHS ENDED DECEMBER 31,	
	1995	1994
OPERATING ACTIVITIES:		
Net cash provided by operating activities	$12,324	$ 2,883
INVESTING ACTIVITIES:		
Capital expenditures for mobile drilling rigs and equipment	(7,936)	(2,051)
Proceeds from dispositions of equipment	12	18
Proceeds from sales-type lease of mobile drilling rig, net	--	1,414
Sales of marketable securities	5,988	--
Changes in other assets	164	105
Net cash used in investing activities	(1,772)	(514)
FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt	--	80,000
Principal payments on long-term debt	(3,588)	(71,809)
Payments for debt financing arrangements	--	(371)
Net cash provided by (used in) financing activities	(3,588)	7,820
NET INCREASE IN CASH AND CASH EQUIVALENTS	6,964	10,189
CASH AND CASH EQUIVALENTS, beginning of period	20,251	26,410
CASH AND CASH EQUIVALENTS, end of period	$27,215	$ 36,599

See accompanying notes.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

1. INTERIM FINANCIAL STATEMENTS

The condensed consolidated financial statements for the interim periods shown in this report have not been audited by independent public accountants but, in the opinion of management, all adjustments necessary for the fair presentation of these financial statements have been made. All such adjustments are of a normal recurring nature. Results of operations for interim periods are not necessarily indicative of results to be expected for the full fiscal year.

The condensed consolidated financial statements should be read in connection with the consolidated financial statements of Arethusa (Off-Shore) Limited ("Arethusa") as of September 30, 1995 and 1994, and for each of the three years in the period ended September 30, 1995 and the related notes thereto, included elsewhere herein.

2. PENDING MERGER OF ARETHUSA AND DIAMOND OFFSHORE DRILLING, INC.

On February 9, 1996, Arethusa and Diamond Offshore Drilling, Inc. ("Diamond Offshore") executed and delivered definitive agreements in connection with the previously announced proposed merger of the two companies. Merrill Lynch and CS First Boston, financial advisers to Arethusa and Diamond Offshore, respectively, have each rendered a fairness opinion in respect of the transaction and each company's Board of Directors has resolved to recommend the transaction to its shareholders.

Under the proposed merger each Arethusa share would be exchanged for .88 share of Diamond Offshore on a taxable basis to Arethusa's United States shareholders. The transaction is subject to approval by the shareholders of each company at meetings presently expected to be held in April. Commitments to vote in favor of the merger have been made by shareholders representing approximately 47% of Arethusa's shares and by Loews Corporation, representing approximately 70% of Diamond Offshore shares. If the Plan of Acquisition is terminated under certain circumstances, Arethusa must pay to Diamond Offshore a fee of up to $18 million.

Upon successful consummation of the merger, options awarded to officers, directors and employees of Arethusa will become fully vested and exercisable. Also, Arethusa Off-Shore Company ("AOC"), a wholly owned subsidiary of Arethusa, has entered into executive severance agreements with certain executive officers and has amended its severance policy for most shore based employees which will provide payment of certain additional benefits to the employees if they are terminated following the merger.

Additionally, on February 9, 1996 Arethusa declared a cash dividend of $.25 per common share payable on March 15 to shareholders of record as of March 1, 1996.

Additionally, subject to approval by Arethusa shareholders and to a successful merger, the exercise price of options granted under the 1993 Employee Stock Option Plan (approximately 462,000 shares granted) would be reduced by $3 per share. In the event the option exercise price is reduced to $7 per share, Arethusa would be required to record compensation expense in its financial statements for the difference between the revised exercise price of $7 per share and the market value on the date approval is received from shareholders. To the extent the market value of Arethusa shares continues to increase above the exercise price there will be an increased charge to compensation expense.

3. ACQUISITION OF THE ARETHUSA YATZY

In May 1995, Arethusa acquired the Arethusa Yatzy (see footnote 4 to Arethusa's September 30, 1995 Annual Report on Form 10-K). The following unaudited pro forma income statement data for the three months ended December 31, 1994 present the consolidated results of operations as if the acquisition had occurred on September 30, 1994. The unaudited pro forma income statement data also reflect two additional significant fiscal 1995 transactions, the sale of the Treasure Stawinner and the June 30, 1995 dividend and capital distribution (both discussed in footnote 5 to Arethusa's September 30, 1995 Annual Report on Form 10-K), as if each had occurred on September 30, 1994. Such unaudited pro forma financial data may not be indicative of the results of operations of Arethusa had the transactions been completed on such earlier date, nor is it necessarily indicative of future financial results.

PRO FORMA INCOME STATEMENT DATA
FOR THE THREE MONTHS ENDED DECEMBER 31, 1994
(IN THOUSANDS, EXCEPT PER SHARE DATA)

Contract Drilling Revenue	$28,393
Net Loss	$(2,095)
Net Loss Per Common Share	$ (.10)

The historical operating results for the Arethusa Yatzy included in the unaudited pro forma financial data have been adjusted for (i) duplicate administrative expenses, (ii) depreciation expense calculated based upon Arethusa's cost and estimated useful life, (iii) a reduction in insurance expense based upon Arethusa's lower insured value, and (iv) interest calculated based upon Arethusa's $30.0 million note.

4. COMMITMENTS AND CONTINGENCIES:

Operating Lease -- Arethusa is committed under a lease agreement for office space which continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1,023,000.

Litigation -- Arethusa is engaged in various claims and litigation arising from operations. In the opinion of management, uninsured losses, if any, resulting from these matters will not have a material adverse effect on Arethusa's results of operations or financial position.

Revenue Agent Reviews -- Revenue agent reviews are currently in progress with respect to certain of Arethusa's subsidiaries and operations in Indonesia and the United States. While Arethusa cannot predict with certainty the outcome of such reviews, management does not believe the ultimate outcome of these reviews will have a material adverse impact on Arethusa's consolidated financial position or results of operations.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors and Shareholders of
Arethusa (Off-Shore) Limited:

We have audited the accompanying consolidated balance sheets of Arethusa (Off-Shore) Limited (a Bermuda company) and subsidiaries as of September 30, 1995 and 1994, and the related consolidated statements of income, shareholders' investment and cash flows for each of the three years in the period ended September 30, 1995, which, as described in Note 1, have been prepared on the basis of accounting principles generally accepted in the United States. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Arethusa (Off-Shore) Limited and subsidiaries as of September 30, 1995 and 1994, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 1995, in conformity with accounting principles generally accepted in the United States.

ARTHUR ANDERSEN & CO.

Hamilton, Bermuda
November 14, 1995

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	SEPTEMBER 30, 1995	SEPTEMBER 30, 1994
ASSETS		
Current assets		
Cash and cash equivalents	$ 20,251	$ 26,410
Restricted cash	2,469	2,161
Equity securities	6,000	--
Accounts receivable	28,625	23,076
Lease receivable	--	57,321
Supplies and spare parts, at cost	16,952	12,591
Prepayments and other current assets	1,206	1,316
Total current assets	75,503	122,875
Mobile drilling rigs and equipment, at cost		
Drilling rigs --		
Semisubmersibles	267,417	227,768
Jack-ups	73,823	72,446
Drill pipe and other drilling equipment	5,767	5,450
Furniture, fixtures, automobiles and other	1,419	1,310
	348,426	306,974
Accumulated depreciation	(111,102)	(85,818)
Net mobile drilling rigs and equipment	237,324	221,156
Other assets	2,505	3,791
Total assets	$ 315,332	$ 347,822
LIABILITIES AND SHAREHOLDERS' INVESTMENT		
Current liabilities		
Current maturities of long-term debt	$ 10,603	$ 30,899
Accounts payable	12,942	8,317
Accrued liabilities	4,050	3,154
Interest payable	662	763
Income taxes payable	302	306
Total current liabilities	28,559	43,439
Long-term debt	62,175	40,910
Deferred credits	1,000	2,201
Other long-term liabilities	1,019	931
Commitments and contingencies (Note 10)		
Shareholders' Investment:		
Common stock, $.10 par value per share, 50,000 shares authorized, 20,333 shares issued and outstanding	2,033	2,033
Additional paid-in capital	218,800	274,386
Accumulated earnings	132	(16,078)
Unrealized gain on equity securities	1,614	--
Total shareholders' investment	222,579	260,341
Total liabilities and shareholders' investment	$ 315,332	$ 347,822

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

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	YEAR ENDED SEPTEMBER 30,		
	1995	1994	1993
Contract drilling revenue	$122,147	$120,212	$ 94,161
Operating expenses			
Direct costs	87,953	79,857	63,882
General and administrative	8,658	7,609	6,300
Depreciation	29,547	27,446	23,784
Total operating expenses	126,158	114,912	93,966
Operating income (loss)	(4,011)	5,300	195
Other income (expense)			
Interest expense	(6,311)	(6,090)	(10,194)
Interest income	5,692	5,842	6,196
Gains on sales of assets	27,820	330	1,015
Gain on sale of equity securities	67	--	--
Other, net	(193)	(253)	(154)
Total other income (expense)	27,075	(171)	(3,137)
Income (loss) before income taxes	23,064	5,129	(2,942)
Tax provision	(1,440)	(1,542)	(2,061)
Net income (loss)	$ 21,624	$ 3,587	$ (5,003)
Net income (loss) per common share	$ 1.06	$ .18	$ (.31)
Weighted average common shares outstanding	20,333	20,333	16,073

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

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' INVESTMENT
(IN THOUSANDS)

	COMMON STOCK				
	SHARES	PAR VALUE	ADDITIONAL PAID-IN CAPITAL	ACCUMULATED EARNINGS	UNREALIZED GAIN ON EQUITY SECURITIES
Balance at September 30, 1992	15,333	$1,533	$ 228,467	$ (14,662)	$ --
Net loss for fiscal year 1993	--	--	--	(5,003)	--
Issuance of Common Stock:					
-- Through Initial Public Offering	4,000	400	36,019	--	--
-- In connection with rig acquisitions	1,000	100	9,900	--	--
Balance at September 30, 1993	20,333	2,033	274,386	(19,665)	--
Net income for fiscal year 1994	--	--	--	3,587	--
Balance at September 30, 1994	20,333	2,033	274,386	(16,078)	--
Net income for fiscal year 1995	--	--	--	21,624	--
Dividend and capital distribution -- $3 per share	--	--	(55,586)	(5,414)	--
Unrealized gain on equity securities	--	--	--	--	1,614
Balance at September 30, 1995	20,333	$2,033	$ 218,800	$ 132	$1,614

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

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	YEAR ENDED SEPTEMBER 30,		
	1995	1994	1993
Operating activities			
Net income (loss)	$ 21,624	$ 3,587	$ (5,003)
Adjustments to reconcile net income (loss) to net cash provided by operating activities --			
Depreciation and amortization	29,547	27,187	23,794
Gains on sales of assets	(27,820)	(330)	(1,015)
Gain on sale of equity securities	(67)	--	--
Changes in operating assets and liabilities --			
(Increase) decrease in restricted cash	(308)	993	2,473
Increase in accounts receivable	(5,189)	(1,967)	(4,949)
Increase in supplies and spare parts	(554)	(931)	(729)
(Increase) decrease in prepayments and other current assets	110	(477)	193
Increase (decrease) in accounts payable	530	338	(695)
Increase in accrued liabilities	896	692	1,117
Decrease in interest payable	(101)	(710)	(439)
Increase (decrease) in income taxes payable	(4)	(137)	220
Total adjustments	(2,960)	24,658	19,970
Net cash provided by operating activities	18,664	28,245	14,967
Investing activities			
Acquisitions of mobile drilling rigs and equipment	(69,498)	(5,989)	(61,814)
Proceeds from dispositions of mobile drilling rigs and equipment, net	53,191	674	21,997
Proceeds from sales-type lease of mobile drilling rig, net	56,069	5,362	4,898
Changes in other assets, including deferral and reimbursement of mobilization expenditures	631	(3,027)	--
Investment in equity securities	(4,538)	--	--
Proceeds from sale of equity securities	218	--	--
Other	(66)	(8)	(56)
Net cash provided by (used in) investing activities	36,007	(2,988)	(34,975)
Financing activities			
Proceeds from issuance of long-term debt	110,000	--	25,000
Principal payments on long-term debt	(109,032)	(23,490)	(35,191)
Payments for debt financing arrangements	(798)	(84)	(589)
Dividend and capital distribution	(61,000)	--	--
Proceeds from issuance of common stock, net of issuance costs	--	--	36,419
Net cash provided by (used in) financing activities	(60,830)	(23,574)	25,639
Net increase (decrease) in cash and cash equivalents	(6,159)	1,683	5,631
Cash and cash equivalents, beginning of period	26,410	24,727	19,096
Cash and cash equivalents, end of period	$ 20,251	$ 26,410	$ 24,727

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

General Organization

Arethusa (Off-Shore) Limited (herein referred to as Arethusa or the Company) is a Bermuda corporation, incorporated on August 31, 1990. Arethusa was formed for the purpose of acquiring offshore drilling rigs and certain other property and equipment owned by Zapata Off-Shore Company and its subsidiaries (Zapata or ZOS), and on October 31, 1990, these assets were purchased for $298 million.

In June 1993, the Company effected a two-for-three reverse stock split and reduced the par value of its stock from $10 to $.10 per share. In connection with the reverse stock split, the shareholders authorized additional shares of common stock, resulting in a total of 50,000,000 shares authorized. In August 1993, Arethusa completed an Initial Public Offering (IPO) of 4,896,000 shares of common stock at an initial price to the public of $10 per share, of which 4,000,000 shares were sold by the Company and 896,000 shares were sold by a shareholder. These shares are publicly traded on the NASDAQ National Market System.

Consolidation

The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States, expressed in United States dollars and include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Equity Securities

As of September 30, 1995, the Company had investments in equity securities. In accordance with Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities", such equity securities are reflected in the accompanying balance sheet as available-for-sale securities at the quoted market value as of September 30, 1995. Unrealized gains on the investment are reported as a separate component of shareholders' investment, until realized. The quoted market value of the shares held by the Company may not be the value that would be realized should the Company dispose of all of the shares in a short period of time.

Supplies and Spare Parts

Supplies and spare parts are stated at average cost which does not exceed market value.

Mobile Drilling Rigs and Equipment

Mobile drilling rigs and equipment are recorded at cost. Depreciation is provided on the straight-line method without salvage value, using an estimated useful life, as follows:

	ESTIMATED USEFUL LIFE
Mobile drilling rigs	25 years
Drill pipe and other drilling equipment	4-6 years
Furniture, fixtures, automobiles and other	3-25 years

For mobile drilling rigs acquired, the estimated useful life is based upon when the asset was placed in service by its original owner but will not be less than five years.

Routine repairs and maintenance are charged to expense as incurred. Repair and maintenance expense totaled approximately $16,400,000, $14,500,000 and $10,100,000 for fiscal years 1995, 1994 and 1993, respectively. Major renewals and improvements are capitalized and are generally depreciated over five years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Upon disposal of assets subject to depreciation, the accounts are relieved of related costs and accumulated depreciation.

Mobilization Costs

When significant costs are incurred in connection with mobilizing a drilling rig for a new contract, such costs, net of any mobilization fees received, are deferred and amortized over the new contract term. When a rig is mobilized before obtaining a new contract, the market in the new locale is analyzed and the projected return on the mobilization investment is determined, and mobilization costs are deferred and amortized over a period not to exceed 24 months. Mobilization costs incurred in connection with rig purchases are capitalized as part of the purchase price and are depreciated over the life of the rig.

Interest Rate Swap Agreements

From time to time, the Company has entered into interest rate swap agreements whereby the Company has exchanged the floating interest rate under certain debt agreements for a fixed interest rate. The differential paid or received is accrued as interest rates change and recognized over the life of the agreements. No such financial instruments have been in effect since October 1993.

Revenue Recognition

Contract drilling revenues are recognized as earned, based on contractual drilling rates. Losses are recognized in the period in which the loss is identified.

Foreign Currency Translation

Arethusa accounts for foreign currency translation in accordance with SFAS No. 52, "Foreign Currency Translation." In connection therewith, the United States dollar was determined to be the functional currency as revenues are received and operating costs are paid primarily in United States dollars.

Earnings (Loss) per Share Data

Earnings (loss) per share data is based on the weighted average number of common shares and common equivalent shares outstanding during each year, if dilutive.

Fair Value of Financial Instruments

In December 1991, the Financial Accounting Standards Board issued SFAS No. 107, "Disclosures about Fair Value of Financial Instruments." The Company believes that the fair value of its financial instruments approximates their book value. This determination was made as follows:

Long-Term Debt. The fair value of the Company's long-term debt, all of which is floating rate, is estimated based on rates currently available to the Company for debt with similar maturities.

Currency Exchange Contracts. Currency exchange contracts in place on September 30, 1993, expired between October 1993 and December 1993. As market value gains and losses on currency exchange contracts are recognized as an offset to currency exchange losses in the statements of income (discussed in Note 8) in the period in which they occur, the carrying value is therefore equal to the fair value. At September 30, 1995 and 1994, no currency exchange contracts were outstanding.

Recent Accounting Pronouncement

In October 1995, the Financial Accounting Standards Board issued SFAS No. 123, "Accounting for Stock Based Compensation" which defines a fair value based method of accounting for an employee stock

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

option or similar equity instrument and is effective for fiscal years beginning after December 15, 1995. As allowed by SFAS No. 123, the Company plans to continue to measure compensation cost for their compensation plans using the intrinsic value based method of accounting prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" with pro forma disclosure in the future of the difference, if any, between compensation cost included in net income and the related cost measured under the fair value method.

2. RELATED-PARTY TRANSACTIONS:

Sale of 50-Percent Interest in Arethusa Heritage

On December 31, 1991, a subsidiary of Ymer Offshore AB (Ymer), a former shareholder of Arethusa, purchased a 50-percent interest in the Arethusa Heritage, for an aggregate purchase price of $10 million. The purchase price was paid $2 million in cash and the remaining $8 million in the form of a secured note.

As a part of this sale, Ymer and Arethusa also entered into option agreements in which Ymer had the right to sell back to Arethusa, and Arethusa had the right to repurchase, the Ymer interest in the rig at specified prices. Effective January 31, 1994, the Company repurchased this 50 percent interest in the Arethusa Heritage for $8.4 million. As payment for the repurchase, the Company paid $400,000 in cash and accepted cancellation of the $8.0 million promissory note which was due on January 31, 1994. The Company now owns 100% of the Arethusa Heritage.

As a result of these option agreements, Arethusa did not recognize this transaction as a sale. The Company recorded a deferred credit for the amount of the gain which was amortized based upon the approximate period of time the options were expected to be outstanding. For the years ended September 30, 1994 and 1993, respectively, Arethusa recognized $49,100 and $884,300 of gain, and $142,700 and $435,900 of interest income related to this transaction.

During fiscal years 1994 and 1993 Arethusa operated the Arethusa Heritage under a bareboat charter agreement. The charter fee totaled $357,300 and $1,076,100, respectively, during the years ended September 30, 1994 and 1993. This bareboat charter agreement terminated on January 31, 1994, in connection with Arethusa's repurchase of the 50-percent interest in the rig.

Yatzy Management and Operating Services Agreement

Prior to Arethusa's acquisition of the Yatzy in May 1995 (see Note 4), the rig was managed by Arethusa under a management and operating services agreement with Exmar, N.V. (a Belgium corporation which is related to Alphee S.A., a principal shareholder of the Company). Under the terms of the agreement, Arethusa was paid a management fee, and all operating expenses were paid by Exmar, N.V. This management fee totaled $374,500, $638,700 and $638,700 for fiscal 1995, 1994 and 1993 respectively, and the Company has recorded such fees as a reduction of Arethusa's administrative expenses.

Other Related-Party Transactions

The Company previously provided $710,000 in financing for the homes of the president and a vice president of Arethusa Off-Shore Company (AOC), a wholly owned subsidiary of Arethusa, who were recruited from outside the United States. These notes, which originally bore interest at 9 percent per annum, matured during fiscal 1994 and were renewed for additional three year terms. During fiscal year 1995, AOC agreed to take possession of the home of the vice president in full payment of his note. The remaining note receivable from the president is now payable in full in 1997, with interest due quarterly in arrears based upon the stated rate of 8.12 percent per annum. This note receivable is secured by a real estate lien note and the deed of trust for the home.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Ymer and International Maritime Investors S.A. (IMI), the majority shareholder of Alphee S.A., each guaranteed $4.5 million of the rig secured debt due August 20, 1996. The Company agreed to compensate Ymer and IMI at the rate of 1 1/2 percent per annum of the guaranteed amount. Such guarantees expired with the debt repayment in December 1994.

3. CASH FLOW INFORMATION:

For purposes of the statements of cash flows, all investments with an original maturity of three months or less are considered to be cash equivalents. Net cash used in operating activities reflects cash interest payments of approximately $7,109,000, $6,139,000 and $11,209,000; and income and withholding tax payments of approximately $1,389,000, $1,744,000 and $1,852,000 for fiscal years 1995, 1994 and 1993, respectively.

Restricted cash is comprised of balances maintained to guarantee the Company's performance under drilling contracts in Indonesia and India, and rig availability for certain drilling contract bids.

4. ASSET ACQUISITIONS:

Acquisition of the Arethusa Yatzy

On May 3, 1995, the Company acquired the Arethusa Yatzy (formerly the Yatzy), a dynamically-positioned semisubmersible drilling rig built in 1989. The rig has been managed by Arethusa since 1991 and in May 1995 began a drilling contract with Petroleos Brasileiros, S.A. (Petrobras), which is expected to keep the unit working offshore Brazil through November 1998. The purchase price was $50.2 million, $20.2 million of which was paid from existing cash balances and $30.0 million of which was funded through a new eight-year, rig-secured loan.

The following unaudited pro forma income statement data for the years ended September 30, 1995 and 1994, present the consolidated results of operations as if the acquisition had occurred at the beginning of the fiscal year 1994. The unaudited pro forma income statement data also reflect two additional significant fiscal 1995 transactions, the sale of the Treasure Stawinner discussed in Note 5 and the June 30, 1995, dividend and capital distribution of $61.0 million ($3.00 per share), as if each had occurred at the beginning of fiscal 1994. Since the gain on the sale of the Treasure Stawinner is a nonrecurring credit, this gain has not been included in this pro forma income statement data. If calculated as if the sale occured at the beginning of fiscal 1994, this gain amount would approximate $24.4 million. Such unaudited pro forma financial data may not be indicative of the results of operations of the Company had the transactions been completed on such earlier date, nor is it necessarily indicative of future financial results.

	1995	1994
	(IN THOUSANDS EXCEPT PER SHARE DATA)	
Contract Drilling Revenue	$120,166	$122,675
Net Income (Loss)	$ (8,496)	$ 883
Net Income (Loss) Per Common Share	$ (.42)	$ .04

The historical operating results for the Arethusa Yatzy included in the unaudited pro forma financial data, have been adjusted for (i) duplicate administrative expenses, (ii) depreciation expense calculated based upon Arethusa's cost and estimated useful life, (iii) a reduction in insurance expense based upon Arethusa's lower insured value, and (iv) interest expense calculated based upon Arethusa's $30.0 million note.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Acquisition of Arethusa Worker and Treasure Stawinner.

On August 20, 1993, Arethusa acquired two deepwater semisubmersible drilling rigs, the Arethusa Worker and the Treasure Stawinner, for $59.0 million in cash and 1,000,000 shares of common stock of the Company. Arethusa funded the cash portion of this acquisition with $34.0 million of cash proceeds from the IPO and $25.0 million of bank debt.

5. ASSET DISPOSITIONS:

Sale of the Treasure Stawinner

On June 30, 1995, Arethusa completed the Sale of the Treasure Stawinner for conversion to a floating production unit for Petrobras. Arethusa received $55.0 million in cash and has retained ownership of certain drilling equipment, which was removed from the rig and will be used by the Company for other purposes. Upon closing of the transaction, the Company recognized a gain of approximately $27.9 million, repaid $12.6 million of secured debt, and declared a $3 per share dividend and capital distribution to shareholders. The dividend/distribution totaled $61.0 million, and was paid on July 28, 1995 to shareholders of record as of July 14, 1995.

Sale of Miss Kitty

In July 1993, Arethusa sold the jackup Miss Kitty for $22.0 million in cash. Arethusa continues to operate the Miss Kitty pursuant to a bareboat charter agreement with the new owners which has recently been extended for an additional year through July 30, 1997. The Company realized a gain of $3.6 million which is being amortized ratably over the initial three-year charter term. The charter provides for a fixed charter fee of $9,765 per day for the first eighteen months, and thereafter a basic charter rate of $6,750 per day plus a revenue sharing component. The Company used $18.2 million of the proceeds to reduce outstanding debt.

Sale of Zapata Arctic

Effective March 30, 1992, Arethusa sold the Petrobras XXV (formerly the Zapata Arctic) to an affiliate of Petrobras, effected through a sales-type lease with a term of 10 years, for a gain of approximately $27.3 million. The lease stipulated a down payment of $2,642,500 and 40 quarterly installments, for total principal payments of $75,500,000 plus interest. The interest component of the installment was adjusted quarterly to the three-month London Interbank Market Rate plus 4 percent. At September 30, 1994 and 1993, this rate was 9.31 and 7.19 percent per annum, respectively.

The lessee had two options to purchase the rig for the then unpaid principal balance of the lease, in March 1995 or December 1997. On March 31, 1995 Petrobras exercised their purchase option under the lease of the Petrobras XXV. The Company transferred title of this rig to the Petrobras affiliate and received lease proceeds of $54.4 million in cash, which were used to pay $17.9 million of secured debt and $1.2 million in commissions.

Sale of Bonito II

Arethusa sold the Bonito II on December 31, 1991, for a gain of approximately $5.1 million. The buyer paid $25.3 million in cash for the rig and services provided by Arethusa in connection with the sale. Arethusa continues to operate the Bonito II pursuant to a bareboat charter agreement which currently extends to August 1996. The charter rate is currently $7,550 per day plus a revenue sharing component. The Company has the option to extend the charter for two additional one-year periods from August 1996.

During March 1994, the Bonito II ended its contract in India and was mobilized to the Gulf of Mexico where it commenced operations under a drilling contract in July 1994. In connection with this mobilization,

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

the Company and the owner agreed to share equally the mobilization costs. The net costs to be borne by the Company, which is approximately $1.7 million, is being deferred and amortized over a period of twenty-four months.

6. DEBT:

Long-term debt at September 30, 1995 and 1994, consists of the following (in thousands):

	1995	1994
Rig-secured debt due May 3, 2003	$ 30,000	$ --
Rig-secured debt due December 22, 1999	42,778	--
Rig-secured debt due October 30, 1996	--	52,809
Rig-secured debt due August 20, 1996	--	19,000
	72,778	71,809
Less -- Current maturities	(10,603)	(30,899)
	$ 62,175	$ 40,910

Rig-Secured Debt Due May 3, 2003

In connection with the acquisition of the Arethusa Yatzy on May 3, 1995, the Company entered into a credit agreement to borrow $30.0 million from its lending banks. Under the terms of the agreement, principal is payable in sixteen semi-annual installments of $1.9 million. Interest rates are based upon an average of the Reuters FRBD reference rates plus 1 1/2 percent per annum, and payable in arrears. The effective interest rate for fiscal year 1995 was 7.54 percent.

The loan is secured by a first mortgage on the Arethusa Yatzy. Loan covenants included, among other financial provisions, (a) maintenance of minimum collateral values, (b) restrictions on the sale of collateralized assets, (c) restrictions on declarations of dividends and (d) limitations on further indebtedness.

Rig-Secured Debt Due December 22, 1999

On December 20, 1994, the Company entered into a new credit agreement with its lending banks. Under this agreement, certain wholly-owned subsidiaries of the Company borrowed $80 million to refinance then existing rig-secured debt. During fiscal 1995 this loan was paid down by $37.2 million, which included three scheduled quarterly installments totalling $6.7 million, and two additional payments totalling $30.5 million made in connection with the monetization of the Petrobras XXV lease and the Sale of the Treasure Stawinner (see Note 5). Currently, quarterly payments on this loan total $1.7 million with a final payment of $15.4 million due in December 1999. Interest is payable quarterly in arrears and is based upon the London Interbank Market Rate plus 1 1/2 percent per annum. The effective interest rate for fiscal year 1995 was 7.97 percent.

The loan is secured by the first priority fleet mortgage on all rigs owned by the Company other than the Arethusa Yatzy. Other loan covenants are similar to those in the rig-secured debt due May 3, 2003.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Annual Maturities

The annual maturities of long-term debt (including the current portion), are as follows (in thousands):

Fiscal year ending September 30 --	
1996	$10,603
1997	10,603
1998	10,603
1999	10,603
2000	19,118
Thereafter	11,248
	$72,778

7. TAXES:

Arethusa's United States subsidiaries and Bermuda subsidiaries with operations in United States territorial waters provide taxes at the United States federal statutory rate. As of September 30, 1995, these subsidiaries collectively had United States net operating loss carryforwards of approximately $85.6 million for United States tax reporting purposes. These losses are available to benefit future United States tax expense and expire in fiscal years 2006 through 2010.

Arethusa's subsidiaries operating in the territorial waters of countries outside of the United States provide taxes at the rates applicable in those countries. The tax provision includes income and withholding taxes applicable to operations in India, Indonesia, Brazil and the Netherlands.

At the present time, no income, profit, capital or capital gain taxes are levied in Bermuda and, accordingly, no provision for such taxes has been recorded by the Company. In the event that such taxes are levied, the Company has received an undertaking from Bermuda Government exempting it from all such taxes until March 28, 2016.

Revenue agent reviews are currently in progress with respect to certain of the Company's subsidiaries and operations in Indonesia and the United States. While the Company cannot predict with certainty the outcome of such reviews, management does not believe the ultimate outcome of these reviews will have a material adverse impact on the Company's consolidated financial position or results of operations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

The Company's income (loss) before income taxes and income tax provision were (in thousands):

	INCOME (LOSS) BEFORE INCOME TAXES	TAX PROVISION
For the year Ended September 30, 1995:		
Bermuda	$ (179)	$ --
Non-Bermuda	23,245	(1,440)
	$23,064	$(1,440)
For the year Ended September 30, 1994:		
Bermuda	$ 247	$ --
Non-Bermuda	4,882	(1,542)
	$ 5,129	$(1,542)
For the year Ended September 30, 1993:		
Bermuda	$ (399)	$ --
Non-Bermuda	(2,543)	(2,061)
	$(2,942)	$(2,061)

Effective October 1, 1993, the Company adopted SFAS No. 109, "Accounting for Income Taxes," which requires recognition of deferred tax liabilities and assets for the expected future tax consequences of events that have not been recognized in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on differences between the financial statement carrying amounts and tax bases of assets and liabilities using enacted tax rates and laws in effect in the years in which the differences are expected to reverse. Prior-year financial statements were not restated for SFAS No. 109. The adoption of SFAS No. 109 had no material effect on the Company's consolidated financial position or results of operations.

No deferred taxes were required to be provided during fiscal 1995, 1994, or 1993.

The components of the net deferred tax asset (liability) as of September 30, 1995 and 1994, are as follows (in thousands):

	1995	1994
Deferred tax assets --		
Net U.S. operating loss carryforwards	$ 29,964	$ 24,481
Accruals and reserves	514	409
Valuation allowance	(23,543)	(19,761)
	6,935	5,129
Deferred tax liabilities --		
Excess of tax over book depreciation	(6,935)	(5,129)
Net deferred tax asset (liability)	$ --	$ --

8. CURRENCY EXCHANGE:

In an effort to minimize the effects of exchange rate fluctuations, the Company generally hedges its exposure through obtaining payment for drilling contracts in United States Dollars. During fiscal years 1994 and 1993, the Company also entered into currency exchange contracts to address specific risks. The Company does not engage in currency speculation. At September 30, 1993, the Company had contracts maturing between October and December 1993 requiring it to purchase $3.6 million in foreign currency (the equivalent

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

of 119.0 million Indian rupees). During fiscal year 1994, the Company committed to an additional $1.0 million of currency exchange contracts which matured between December 1993 and June 1994. There were no currency exchange contracts in place at September 30, 1995 or 1994. Market value gains and losses on the currency exchange contracts have been recognized as an offset to currency exchange losses in the statements of income. Total currency exchange losses recorded in the statements of income were approximately $1.2 million, $1.2 million and $1.8 million for fiscal years 1995, 1994 and 1993, respectively. These losses primarily resulted from operations in Brazil and India.

9. MAJOR CUSTOMERS AND CONCENTRATION OF CREDIT RISKS:

Arethusa's customer base includes major and independent oil and gas companies and government owned oil companies. During fiscal 1995, 1994 and 1993, the Company earned 52.1 percent, 54.3 percent, and 49.1 percent, respectively, of its revenues from major customers. A summary of the major customers for these years were as follows: year ended September 30, 1995 -- Petrobras and Shell Oil Company, 27.8 percent and 24.3 percent, respectively; year ended September 30, 1994 -- Petrobras, Marathon Oil Company, and Maxus Southeast Sumatra, Inc., 26.3 percent, 15.0 percent and 13.0 percent, respectively; year ended September 30, 1993 -- Indian Oil & Natural Gas Commission, Maxus Southeast Sumatra, Inc. and Petrobras, 17.4 percent, 15.8 percent and 15.9 percent, respectively.

10. COMMITMENTS AND CONTINGENCIES:

Operating Lease

Arethusa is committed under a lease agreement for office space which continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1,023,000. Under the terms of the lease, the Company only made cash payments to reimburse the landlord for operating expenses through December 31, 1993. The Company began making additional payments for base, rental installments on January 1, 1994. Rental charges are expensed on a straight-line basis over the term of the lease. The Company recognized rental expense of approximately $566,000, $552,000 and $524,000 of which approximately $203,000, $211,000 and $183,000 were paid as operating expenses in fiscal years 1995, 1994 and 1993, respectively. Estimated future minimum lease payments, excluding reimbursable operating expenses, under this operating lease are as follows (in thousands):

Fiscal year --	
1996	$ 373
1997	392
1998	463
1999	487
2000	509
Thereafter	989
	$3,213

Litigation

Arethusa is engaged in various claims and litigation arising from operations. In the opinion of management, uninsured losses, if any, resulting from these matters will not have a material adverse effect on Arethusa's results of operations or financial position.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

11. BENEFIT PLANS:

Pension Plan

AOC established a defined benefit pension plan effective October 1, 1992, which covers substantially all U. S. citizens and U. S. permanent residents who are employed by AOC. Employees are automatically enrolled in the plan following the completion of one year of service and are 100 percent vested after five years of service. Benefits are calculated and paid based on employees' years of credited service and average final compensation using an excess benefit formula integrated with social security covered compensation.

Pension costs are determined actuarially and funded to the extent allowable under the Internal Revenue Code. The plan's assets are invested in cash and cash equivalents, equity securities, government and corporate debt securities.

The significant actuarial assumptions as of the plan's year-end are set forth in the following table:

	SEPTEMBER 30,	
	1995	1994
Discount rate	7.5%	8.1%
Expected long-term rate	9.0%	9.0%
Compensation projection rate	5.0%	5.0%

The funded status as of September 30, 1995 and September 30, 1994, is set forth in the following table (in thousands):

	1995	1994
Benefit obligation -- Vested	$ (7,159)	$(5,394)
-- Non-vested	(663)	(254)
Accumulated benefit obligation	(7,822)	(5,648)
Effect of compensation projection	(3,061)	(2,916)
Projected benefit obligation	(10,883)	(8,564)
Plan assets at fair value	8,421	6,725
Projected benefit obligation in excess of plan assets	(2,462)	(1,839)
Unrecognized loss	2,329	1,339
Unrecognized prior service cost	(299)	--
Contributions	123	--
Accrued pension cost	$ (309)	$ (500)

Net periodic pension cost for the fiscal year ended September 30, 1995 and 1994 includes the following components (in thousands):

	1995	1994
Service cost of benefits earned	$ 566	$ 575
Interest cost on projected benefit obligations	692	619
Actual return on plan assets	(1,014)	227
Deferred gain (loss)	401	(855)
Amortization of loss	43	53
Amortization of prior service cost	(21)	--
Net period pension cost	$ 667	$ 619

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Profit-Sharing Plan

AOC established a defined contribution profit-sharing plan effective October 1, 1992 which covers substantially all U.S. citizens, U.S. permanent residents and third country national expatriates who are employed by AOC. The plan and trust agreement are intended to meet the requirements of Section 401(a) and all related sections of the Internal Revenue Code.

Employees may enroll in the plan following the completion of one year of service. Participants may elect to make contributions from 1 percent up to 16 percent of gross monthly salary to the plan: a maximum of 10 percent on a 401(k) basis; a maximum of 16 percent on a 401(m) basis. All amounts contributed to the plan are deposited in a trust with a national bank and administered by independent trustees.

At the end of the plan year on September 30, the Company will match a minimum of 10 percent up to a maximum of 100 percent of eligible basic contributions made by participants during the plan year. The basic rate of contribution used to determine the Company matching amount is 6 percent, on a 401(k) or 401(m) basis. The actual matching percentage is determined by the Company's Board of Directors at the end of the plan year. AOC made profit-sharing provisions of approximately $276,000, $134,000 and $120,000 for 1995, 1994 and 1993, respectively.

Employee Stock Option Plan

In August 1993, the Company adopted the Arethusa (Off-Shore) Limited 1993 Employee Stock Option Plan (the Employee Plan) pursuant to which a maximum aggregate of 666,667 shares of Common Stock are available for grant to eligible employees. Options granted pursuant to the Employee Plan vest in equal installments over three years and remain exercisable for a period of seven years, so long as the option holder remains an employee of the Company as of the date of exercise. The exercise price of options granted under the Employee Plan equal the market price of the Common Stock on the date of grant. The Employee Plan provides for the adjustment of the number of shares awarded thereunder, and the exercise price thereof, on any stock dividend, any subdivision or combination of the outstanding shares of Common Stock and any merger, consolidation, recapitalization of the Company or similar event which affects the issued and outstanding shares of Common Stock.

In August 1993, the Company granted 466,666 options at an option price of $10 per share, the market price in the IPO. Accordingly, no compensation expense has been recorded with respect to these options.

As of September 30, 1995 there were 308,000 exercisable options, and 4,667 options had been canceled and surrendered. No options have been exercised.

In September 1995 the board of directors approved a $3 per share reduction in the option price to $7 per share, subject to shareholder approval at the next annual general meeting. This action was proposed as a result of the $3 per share dividend and capital distribution paid by the Company in July 1995.

Non-employee Director Stock Option Plan

In February 1995, the Company's shareholders approved the Arethusa (Off-Shore) Limited 1994 Nonqualified Stock Option Plan for Non-Employee Directors ("Directors' Plan"), pursuant to which a maximum aggregate of 250,000 shares of common stock were authorized. Under the Directors' Plan eligible directors were granted an option to purchase 20,000 shares of the Company's common stock, at an exercise price equal to the fair market value of the common stock on the date of grant. Options granted under this plan vest in equal annual installments over a three-year period, and expire seven years from date of grant.

As of September 30, 1995, 160,000 options had been granted under the Directors' Plan; 100,000 of these options carry an option price of $11.25 based upon a May 1994 date of grant, and the remaining 60,000 options have an option price of $12.625 based on a February 1995 date of grant. In May 1995, approximately 33,000 options became exercisable. No options have been exercised or cancelled.

12. GEOGRAPHIC INFORMATION (UNAUDITED):

The nature of the Company's operations and assets requires movement among geographic areas in response to market conditions and contract requirements. Therefore, the operations and assets reported within a particular geographic area may not be indicative of a long-term operating commitment in that area. Assets are included in the geographic information shown below according to operating location (in thousands):

	UNITED STATES	NORTH SEA	SOUTHEAST ASIA	SOUTH AMERICA	INDIA	BERMUDA AND OTHER	ELIMINATIONS	TOTAL
Year Ended September 30, 1995 --								
Revenues	$ 72,008	$ 8,769	$ 6,902	$ 33,979	$ 7,289	$32,788	$(39,588)	$122,147
Operating income (loss)	(8,667)	(2,172)	(1,117)	7,022	1,488	(565)	--	(4,011)
Identifiable assets	170,159	29,736	16,937	82,331	2,797	13,372	--	315,332
Year Ended September 30, 1994 --								
Revenues	$ 64,273	$ 6,116	$15,593	$ 31,648	$10,255	$22,123	$(29,796)	$120,212
Operating income (loss)	(3,346)	(2,513)	3,910	7,662	281	(694)	--	5,300
Identifiable assets	163,610	31,501	33,165	116,982	2,408	156	--	347,822
Year Ended September 30, 1993 --								
Revenues	$ 40,994	$12,582	$14,887	$ 19,911	$16,307	$ --	$(10,520)	$ 94,161
Operating income (loss)	(9,383)	550	2,726	4,813	1,967	(478)	--	195
Identifiable assets	168,494	34,210	33,454	126,509	6,346	--	--	369,013

13. QUARTERLY FINANCIAL DATA (UNAUDITED):

Unaudited summarized data by quarter for fiscal 1995 and 1994 is as follows (in thousands, except per share amounts):

	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER	TOTAL
1995 --					
Contract drilling revenue	$28,279	$27,167	$32,232	$34,469	$122,147
Operating income (loss)	(1,654)	(3,246)	(525)	1,414	(4,011)
Income (loss) before income taxes	(1,375)	(2,957)	26,687	709	23,064
Net income (loss)	(1,690)	(3,232)	26,414	132	21,624
Net income (loss) per common share	$ (.08)	$ (.16)	$ 1.30	$ .01	$ 1.06
1994 --					
Contract drilling revenue	$30,147	$30,967	$29,219	$29,879	$120,212
Operating income	1,786	2,042	971	501	5,300
Income before income taxes	1,518	2,094	948	569	5,129
Net income	1,059	1,632	546	350	3,587
Net income per common share	$ .05	$ .08	$ .03	$ .02	$ .18

14. EVENT (UNAUDITED) SUBSEQUENT TO DATE OF REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS:

On December 7, 1995, Arethusa entered into a letter of intent with Diamond Offshore Drilling, Inc. ("Diamond Offshore") for the merger of the two companies. The terms of the proposed transaction provide that, upon satisfaction of certain conditions precedent, including execution of definitive agreements (which execution occurred February 9, 1996) and obtaining approval from Arethusa and Diamond Offshore shareholders and certain regulatory agencies, each of the issued and outstanding shares of Arethusa common stock would be converted into the right to receive .88 shares of Diamond Offshore common stock. On

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

February 9, 1996, Arethusa declared a cash dividend of $.25 per share to the holders of its common stock. Management anticipates the merger will be consummated no later than July 31, 1996.

Upon successful consummation of the merger, options awarded to certain officers, directors and employees of Arethusa will become fully vested and exercisable. Additionally, AOC has entered into executive severance agreements with certain executive officers and has amended its severance policy for most shore based employees which will provide payment of certain additional benefits to the employees if they are terminated following the merger.

Additionally, subject to approval by Arethusa shareholders and to a successful merger, the exercise price of options granted under the 1993 Employee Stock Option Plan (approximately 462,000 shares granted) would be reduced by $3 per share. In the event the option exercise price is reduced to $7 per share, Arethusa would be required to record compensation expense in its financial statements for the difference between the revised exercise price of $7 per share and the market value on the date approval is received from shareholders. To the extent the market value of Arethusa shares continues to increase above the exercise price there will be an increased charge to compensation expense.

NO DEALER, SALESMAN OR ANY OTHER PERSON HAS BEEN AUTHORIZED TO GIVE ANY INFORMATION OR TO MAKE ANY REPRESENTATION NOT CONTAINED IN THIS PROSPECTUS SUPPLEMENT OR THE PROSPECTUS AND, IF GIVEN OR MADE, SUCH INFORMATION OR REPRESENTATION MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY DIAMOND OFFSHORE OR ANY UNDERWRITER. THIS PROSPECTUS SUPPLEMENT AND THE PROSPECTUS DO NOT CONSTITUTE AN OFFER TO SELL OR A SOLICITATION OF AN OFFER TO BUY ANY OF THE SECURITIES OFFERED HEREBY IN ANY JURISDICTION TO ANY PERSON TO WHOM IT IS UNLAWFUL TO MAKE SUCH OFFER IN SUCH JURISDICTION. NEITHER THE DELIVERY OF THIS PROSPECTUS SUPPLEMENT OR THE PROSPECTUS NOR ANY SALE MADE HEREUNDER SHALL, UNDER ANY CIRCUMSTANCES, CREATE ANY IMPLICATION THAT THE INFORMATION HEREIN IS CORRECT AS OF ANY TIME SUBSEQUENT TO THE DATE HEREOF OR THAT THERE HAS BEEN NO CHANGE IN THE AFFAIRS OF DIAMOND OFFSHORE SINCE SUCH DATE.

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7,523,140 SHARES

[DIAMOND OFFSHORE LOGO]

COMMON STOCK

PROSPECTUS SUPPLEMENT

MERRILL LYNCH & CO.

CS FIRST BOSTON

SALOMON BROTHERS INC

May 20, 1996

Rule 424(b)(5)
Reg. No. 333-2680

PROSPECTUS SUPPLEMENT
(TO PROSPECTUS DATED APRIL 12, 1996)

7,523,140 SHARES
[DIAMOND OFFSHORE LOGO] DIAMOND OFFSHORE DRILLING, INC.
COMMON STOCK

All of the shares of common stock, par value $0.01 per share ("Diamond Offshore Common Stock"), of Diamond Offshore Drilling, Inc., a Delaware corporation ("Diamond Offshore"), offered hereby (the "Offered Shares") will be sold by Alphee S.A., a Luxembourg corporation ("Alphee"), and Forvaltnings AB Ratos, a Swedish corporation ("Ratos" and, together with Alphee, the "Selling Stockholders"). See "Selling Stockholders." Diamond Offshore will not receive any of the proceeds from the sale of the Offered Shares.

Of the 7,523,140 Offered Shares, 1,505,000 Offered Shares are being offered initially outside the United States and Canada (the "International Offering") by the International Managers (as defined herein) and 6,018,140 Offered Shares are being offered in the United States and Canada (the "U.S. Offering" and, together with the International Offering, the "Offerings") by the U.S. Underwriters (as defined herein). The public offering price and the aggregate underwriting discount per share will be identical for both Offerings. See "Underwriting."

Pursuant to the Plan of Acquisition dated as of February 9, 1996, as amended (as so amended, the "Plan of Acquisition"), among Diamond Offshore, Diamond Offshore (USA) Inc., a Delaware corporation ("Diamond Offshore (USA)"), AO Acquisition Limited, a Bermuda company ("Acquisition Sub"), and Arethusa (Off-Shore) Limited, a Bermuda company ("Arethusa"), and the Amalgamation Agreement dated as of February 9, 1996 (the "Amalgamation Agreement") between Arethusa and Acquisition Sub, Diamond Offshore acquired Arethusa (the "Acquisition") on the terms set forth in the Plan of Acquisition and Amalgamation Agreement. The Acquisition was consummated on April 29, 1996 (the "Effective Time"). Arethusa shareholders received 17,893,344 shares of Diamond Offshore Common Stock, representing approximately 26.4% of the total Diamond Offshore Common Stock currently outstanding, of which the Selling Stockholders received an aggregate of 8,375,455 shares.

Diamond Offshore Common Stock is listed on the New York Stock Exchange (the "NYSE") under the symbol "DO." On May 20, 1996, the closing price of the Diamond Offshore Common Stock on the NYSE was $49 3/8 per share.

FOR A DISCUSSION OF CERTAIN FACTORS THAT SHOULD BE CONSIDERED IN CONNECTION WITH AN INVESTMENT IN THE OFFERED SHARES, SEE "RISK FACTORS" BEGINNING ON PAGE 6 OF THE ACCOMPANYING PROSPECTUS.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS SUPPLEMENT OR THE ACCOMPANYING PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

	PRICE TO PUBLIC	UNDERWRITING DISCOUNT(1)	PROCEEDS TO SELLING STOCKHOLDERS(2)
Per Share	$49.25	$1.48	$47.77
Total(3)	$370,514,645	$11,134,247	$359,380,398

(1) Diamond Offshore and the Selling Stockholders have agreed to indemnify the several Underwriters (as defined herein) against certain liabilities, including certain liabilities under the Securities Act of 1933, as amended. See "Underwriting."

(2) Diamond Offshore has agreed to pay certain expenses of the Offerings estimated at $500,000. The Selling Stockholders have agreed to pay certain other expenses of the Offerings estimated at $167,500. The Underwriters have agreed to pay certain expenses of the Selling Stockholders estimated at $100,000.

(3) The Selling Stockholders have granted the U.S. Underwriters and the International Managers options, exercisable within 30 days after the date of this Prospectus Supplement, to purchase up to 601,814 and 150,501 additional shares of Diamond Offshore Common Stock, respectively, solely to cover over-allotments, if any. If such options are exercised in full, the total Price to Public, Underwriting Discount and Proceeds to Selling Stockholders will be $407,566,159, $12,247,674 and $395,318,485, respectively. See "Underwriting."

The Offered Shares are offered by the several Underwriters, subject to prior sale, when, as and if issued and accepted by them, subject to approval of certain legal matters by counsel for the Underwriters and certain other conditions. The Underwriters reserve the right to withdraw, cancel or modify such offer and to reject orders in whole or in part. It is expected that delivery of the Offered Shares will be made in New York, New York on or about May 24, 1996.

MERRILL LYNCH INTERNATIONAL

CS FIRST BOSTON

SALOMON BROTHERS INTERNATIONAL LIMITED

The date of this Prospectus Supplement is May 20, 1996.

IN CONNECTION WITH THESE OFFERINGS, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF DIAMOND OFFSHORE COMMON STOCK AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH TRANSACTIONS MAY BE EFFECTED ON THE NYSE OR OTHERWISE. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

DURING THESE OFFERINGS, CERTAIN PERSONS AFFILIATED WITH PERSONS PARTICIPATING IN THE DISTRIBUTION MAY ENGAGE IN TRANSACTIONS FOR THEIR OWN ACCOUNTS OR FOR THE ACCOUNTS OF OTHERS IN THE DIAMOND OFFSHORE COMMON STOCK PURSUANT TO EXEMPTIONS FROM RULES 10B-6, 10B-7, AND 10B-8 UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

DIAMOND OFFSHORE DRILLING, INC.

Diamond Offshore engages principally in the contract drilling of offshore oil and gas wells. Diamond Offshore's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Asia and, including those rigs acquired as a result of the Acquisition, consists of 30 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 19 jack-up rigs owned and/or operated by Diamond Offshore and one drillship. Diamond Offshore also operates 10 land rigs deployed in South Texas. Except for two jack-up rigs operated pursuant to bareboat charter contracts, all of Diamond Offshore's offshore and land rigs are wholly owned.

On April 29, 1996, Diamond Offshore consummated the Acquisition, thereby adding to its fleet Arethusa's 13 owned and/or operated mobile offshore drilling rigs. Arethusa provided drilling services worldwide to international and government-controlled oil and gas companies. Arethusa's eight semisubmersible rigs now owned by Diamond Offshore are located in the Gulf of Mexico and offshore Brazil and Arethusa's five jack-up rigs now owned by Diamond Offshore are located offshore India, Indonesia and Egypt, in the Gulf of Mexico and in the Dutch sector of the North Sea.

Diamond Offshore Common Stock is listed on the NYSE under the symbol "DO." For the period from April 12 through May 20, 1996, the high and low closing prices of Diamond Offshore Common Stock as reported by the NYSE were $52 5/8 and $44 1/4 per share, respectively. For the high and low closing prices for earlier periods, see "Management -- Price Range of Diamond Offshore Common Stock" in the accompanying Prospectus.

USE OF PROCEEDS

Diamond Offshore will not receive any of the proceeds from the sale of the Offered Shares by the Selling Stockholders.

SELLING STOCKHOLDERS

All of the Offered Shares being offered hereby are being offered by Alphee and Ratos. The following table sets forth information, as of the date of this Prospectus Supplement, relating to beneficial ownership (as defined in Rule 13d-3 of the Securities Exchange Act of 1934, as amended) of Diamond Offshore Common Stock by each Selling Stockholder.

NAME OF SELLING STOCKHOLDER	BENEFICIAL OWNERSHIP OF DIAMOND OFFSHORE COMMON STOCK PRIOR TO THE OFFERINGS		NUMBER OF SHARES OF DIAMOND OFFSHORE COMMON STOCK TO BE SOLD(1)	BENEFICIAL OWNERSHIP OF DIAMOND OFFSHORE COMMON STOCK AFTER THE OFFERINGS(1)	
	NUMBER	PERCENT	NUMBER	NUMBER	PERCENT
Alphee S.A. 11, Avenue de la Gare 1611 Luxembourg	4,708,248	6.9%	4,234,771	473,477	0.7%
Forvaltnings AB Ratos Drottninggatan 2 Stockholm, Sweden	3,667,207	5.4%	3,288,369	378,838	0.6%

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(1) In addition to the shares of Diamond Offshore Common Stock indicated, the Selling Stockholders have granted the U.S. Underwriters and the International Managers options, exercisable within 30 days after the date of this Prospectus Supplement, to purchase up to 601,814 and 150,501 additional shares of Diamond Offshore Common Stock, respectively, solely to cover over-allotments, if any. If such options are exercised in full, (a) the number of shares of Diamond Offshore Common Stock to be sold by Alphee and Ratos will be 4,658,248 and 3,617,207, respectively, and (b) beneficial ownership of Diamond Offshore Common Stock after the Offerings by Alphee and Ratos will be 50,000 (.07%) and 50,000 (.07%), respectively.

See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and the Selling Stockholders," "-- Registration Rights of Selling Stockholders" and "Plan of Distribution" in the accompanying Prospectus for additional information with respect to the Selling Stockholders.

CAPITALIZATION

The following table sets forth the capitalization of Diamond Offshore as of March 31, 1996 and as adjusted as of such date after giving effect to the Acquisition. This table should be read in conjunction with the Consolidated Financial Statements (including the Notes thereto) and the Unaudited Pro Forma Consolidated Condensed Financial Statements included elsewhere in this Prospectus Supplement.

	MARCH 31, 1996 (UNAUDITED)	
	HISTORICAL	AS ADJUSTED
	(IN THOUSANDS)	
Total debt	$ 15,000	$ 82,477
Stockholders' equity:		
Common stock, $.01 par value	500	679
Additional paid-in capital	665,107	1,215,605
Accumulated deficit	(152,712)	(152,712)
Cumulative translation adjustment	(1,263)	(1,263)
Total stockholders' equity	511,632	1,062,309
Total capitalization	$ 526,632	$ 1,144,786

SELECTED CONSOLIDATED FINANCIAL DATA

The following tables set forth selected consolidated historical and pro forma financial data for Diamond Offshore. The selected consolidated financial data were derived from the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore included in this Prospectus Supplement and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore included in this Prospectus Supplement. The results of operations for the three months ended March 31, 1996 are not necessarily indicative of results to be anticipated for the entire year.

	PRO FORMA THREE MONTHS ENDED MARCH 31, 1996	THREE MONTHS ENDED MARCH 31, 1996	1995
	(IN THOUSANDS, EXCEPT PER SHARE DATA)		
INCOME STATEMENT DATA:			
Total revenues	$147,662	$106,868	$ 70,760
Operating expenses:			
Contract drilling	86,454	66,157	61,751
General and administrative	5,552	3,103	3,140
Depreciation(1)	20,018	12,069	14,988
Gain on sale of assets	(157)	(157)	(389)
Operating income (loss)	35,795	25,696	(8,730)
Interest expense	(1,291)	--	(8,486)
Other income (expense), net	484	434	355
Income tax benefit (expense)	(7,861)	(7,398)	5,289
Net income (loss)	27,127	18,732	(11,572)
Net income per share	.40	0.37	--

	PRO FORMA MARCH 31, 1996	MARCH 31, 1996
	(IN THOUSANDS)	
BALANCE SHEET DATA:		
Working capital	$ 109,185	$ 70,480
Drilling and other property and equipment, net	1,083,485	533,645
Goodwill and other assets	28,956	3,984
Total assets	1,295,738	658,185
Long-term debt	71,874	15,000
Stockholders' equity	1,062,309	511,632

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(1) Effective January 1, 1996, Diamond Offshore revised the estimated useful lives for certain classes of its offshore drilling rigs. The estimated useful lives of Diamond Offshore's offshore drilling rigs, after the change in estimate, range from 10 to 25 years. The effect of such change reduced depreciation expense and increased net income for the three months ended March 31, 1996 by approximately $2.1 million and $1.5 million ($0.03 per share), respectively.

UNAUDITED PRO FORMA CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

The unaudited pro forma consolidated condensed financial statements as of and for the three months ended March 31, 1996 have been prepared based on the historical financial statements of Diamond Offshore and Arethusa as of and for the three months ended March 31, 1996. Such historical financial statements are unaudited but, in the opinion of management, include all adjustments necessary, consisting only of normal recurring accruals. The unaudited pro forma consolidated condensed income statement for the year ended December 31, 1995 has been prepared based on the historical financial statements of Diamond Offshore as of and for the year ended December 31, 1995 and based on pro forma income statement data for Arethusa that reflect adjustments to Arethusa's historical consolidated income statement for the year ended September 30, 1995 in connection with (i) the acquisition of the Arethusa Yatzy, (ii) the sale of the Treasure Stawinner and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of common stock, par value $0.10 per share, of Arethusa ("Arethusa Common Stock")) as if each had occurred at the beginning of fiscal year 1995. The pro forma income statement for the three months ended March 31, 1996 gives effect to the Acquisition. The pro forma income statement for the year ended December 31, 1995 gives effect to (i) the Acquisition, (ii) the initial public offering of Diamond Offshore Common Stock in October 1995 (the "Diamond Offshore Initial Public Offering") and, in connection therewith, the use of the proceeds to repay all of Diamond Offshore's then outstanding indebtedness to Loews Corporation, a Delaware corporation ("Loews"), and to fund the payment of a special dividend to Loews and (iii) interest expense for working capital borrowings, and commitment and other fees, under Diamond Offshore's $150.0 million credit facility with a group of banks (the "Diamond Offshore Bank Credit Facility"). The Acquisition was accounted for under the purchase method of accounting using a purchase price of $560.7 million, which was calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced. The pro forma consolidated condensed balance sheet was prepared assuming such transactions were consummated on March 31, 1996 and give effect to events directly attributable to the transactions, including those that are nonrecurring. The pro forma consolidated condensed income statement was prepared assuming the transactions were consummated as of the beginning of the period presented and give effect to events directly attributable to the transactions which are expected to have a continuing impact on the combined entity. These pro forma consolidated condensed financial statements should be read in conjunction with the other financial information of Diamond Offshore and Arethusa presented elsewhere in this Prospectus Supplement and the accompanying Prospectus. The pro forma consolidated condensed financial statements are presented for illustrative purposes only and are not necessarily indicative of actual results that would have been achieved had the transactions been consummated on such dates, and are not necessarily indicative of future results. The allocation of the purchase price is preliminary, as valuation and other studies have not been finalized. It is not expected that the final allocation of the purchase price will produce materially different results from those presented herein.

PRO FORMA CONSOLIDATED CONDENSED BALANCE SHEET
MARCH 31, 1996

	HISTORICAL(A)			
	DIAMOND OFFSHORE	ARETHUSA	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS)			
Cash and other current assets	$ 32,932	$ 49,722	$ (16,549)(b)	$ 66,105
Accounts receivable	87,624	29,568	--	117,192
Drilling and other property and equipment, net	533,645	230,853	318,987(c)	1,083,485
Goodwill and other assets	3,984	2,071	22,901(d)	28,956
Total assets	$ 658,185	$ 312,214	$ 325,339	$1,295,738
Current liabilities	$ 50,076	$ 20,536	$ 3,500(e)	$ 74,112
Long-term debt	15,000	56,874	--	71,874
Deferred credits and other liabilities	81,477	1,884	4,082(f)	87,443
Common stock	500	2,033	(1,854)(g)	679
Additional paid-in capital	665,107	218,800	331,698(g)	1,215,605
Accumulated earnings (deficit)	(152,712)	12,087	(12,087)	(152,712)
Cumulative translation adjustment	(1,263)	--	--	(1,263)
Total liabilities and stockholders' equity	$ 658,185	$ 312,214	$ 325,339	$1,295,738

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(a) There are no significant adjustments required to the historical financial statements of Diamond Offshore or Arethusa to conform accounting policies of the two companies.

(b) Adjustment for fair values of identifiable current assets acquired and for certain events directly attributable to the transaction. Such items include:

Severance, consulting, and salary continuation plans	$ (5,526)(1)
Financial advisory services	(7,500)(2)
Legal, accounting, and other	(2,500)(3)
Office lease cancellation	(1,023)(4)
	$(16,549)

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(1) Under the Plan of Acquisition, from and after the Effective Time, Diamond Offshore and Arethusa and their respective subsidiaries will honor in accordance with their terms certain Arethusa employment, severance, consulting and salary continuation plans.

(2) Arethusa has agreed to pay Merrill Lynch, Pierce, Fenner & Smith Incorporated a fee of $7.5 million for financial advisory services in connection with the Acquisition upon the closing of the Acquisition.

(3) Adjustment for legal, accounting, printing and other nonrecurring charges expected to be incurred in connection with the Acquisition.

(4) Arethusa is committed under a lease agreement for office space that continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1.0 million. Such payment has no future economic benefit to the combined company and is incremental to other costs incurred by either Arethusa or Diamond Offshore in the conduct of activities prior to the Effective Time.

(c) Adjustment for fair values, based on current appraisals, of the eight semisubmersible drilling rigs, three jack-up drilling rigs, and other property and equipment owned by Arethusa.

(d) Adjustment for fair values of identifiable assets and for the excess of the cost of Arethusa over the sum of the amounts assigned to identifiable assets acquired less liabilities assumed.

(e) Adjustment for the estimated unfunded termination liability related to the Arethusa defined benefit plan.

(f) Adjustment for fair values of liabilities assumed and for the deferred tax liability for estimated future tax effects of differences between the tax bases and the fair value amounts assigned to identifiable assets and liabilities of Arethusa, offset by net operating loss carryforwards of Arethusa of approximately $30.0 million. As a result of the Acquisition, Diamond Offshore will have available to it certain Arethusa net operating loss carryforwards to reduce future U.S. federal income taxes payable. Due to the change in ownership of Arethusa resulting from the Acquisition, there will be annual limitations on the amount of Arethusa tax carryforwards available to be utilized by Diamond Offshore.

(g) The pro forma financial statements reflect the purchase of 100% of the outstanding shares of Arethusa Common Stock for a total consideration of $560.7 million which is comprised of the following:

Diamond Offshore Common Stock to be issued	$539,296(1)
Options assumed	11,381(2)
Total equity consideration	550,677
Transaction costs	10,000(3)
Total consideration	$560,677

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(1) The value of the Diamond Offshore Common Stock to be issued in the Acquisition is calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995) of $30.14.

(2) Amount represents the fair value of the Arethusa Options assumed by Diamond Offshore pursuant to the Amalgamation Agreement. The fair value is based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995), the Amalgamation Ratio (as defined herein) and the option exercise price including the $3.00 reduction, which was approved by Arethusa shareholders at Arethusa's annual general meeting of shareholders on April 29, 1996.

(3) Amounts represent transaction costs directly associated with the Acquisition. See (b) above.

PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT
THREE MONTHS ENDED MARCH 31, 1996

	HISTORICAL			
	DIAMOND OFFSHORE	ARETHUSA	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)			
Revenues	$106,868	$ 40,794	$ --	$ 147,662
Operating expenses:				
Contract drilling	66,157	20,297	--	86,454
General and administrative	3,103	2,449	--	5,552
Depreciation and amortization	12,069	8,277	(328) (a)	20,018
Gain on sale of assets	(157)	--	--	(157)
Total operating expenses	81,172	31,023	(328)	111,867
Operating income (loss)	25,696	9,771	328	35,795
Other income (expense):				
Interest expense	--	(1,291)	--	(1,291)
Other, net	434	50	--	484
Income (loss) before income tax (expense) benefit	26,130	8,530	328	34,988
Income tax (expense) benefit	(7,398)	(348)	(115) (b)	(7,861)
Net income	$ 18,732	$ 8,182	$ 213	$ 27,127
Net income per common share	$ 0.37	$ 0.40		$ 0.40
Weighted average common shares outstanding	50,000	20,333		67,893(c)

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(a) To record the adjustment to depreciation expense and amortization of goodwill resulting from the allocation of the purchase price. The pro forma adjustment assumes an 18-year average estimated useful life for depreciation and a 20-year amortization period for goodwill.

(b) To record income tax expense on the effect of the pro forma adjustments to depreciation and amortization.

(c) Weighted average shares outstanding as if the issuance of 17.9 million shares to be issued by Diamond Offshore in consideration of the Arethusa Common Stock had taken place on January 1, 1996.

PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT
YEAR ENDED DECEMBER 31, 1995

	HISTORICAL DIAMOND OFFSHORE	PRO FORMA ARETHUSA(A)	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
Revenues	$336,584	$ 120,166	$ --	$ 456,750
Operating expenses:				
Contract drilling	259,560	86,532	--	346,092
General and administrative	13,857	9,033	--	22,890
Depreciation and amortization	52,865	29,008	3,897(b)	85,770
Gain on sale of assets	(1,349)	--	--	(1,349)
Total operating expenses	324,933	124,573	3,897	453,403
Operating income (loss)	11,651	(4,407)	(3,897)	3,347
Other income (expense):				
Interest expense	(27,052)	(6,697)	26,296(c)	(7,453)
Other, net	1,598	4,048	--	5,646
Income (loss) before income tax benefit (expense)	(13,803)	(7,056)	22,399	1,540
Income tax benefit (expense)	6,777	(1,440)	(7,840)(d)	(2,503)
Net income (loss)	$ (7,026)	$ (8,496)	$ 14,559	$ (963)
Net income per common share	$ 0.20(f)	$ (0.42)		$ (0.01)
Weighted average common shares outstanding	50,000(f)	20,333		67,893(e)

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(a) Pro forma income statement data for Arethusa reflect (i) the acquisition of the Arethusa Yatzy, which occurred on May 3, 1995, (ii) the sale of the Treasure Stawinner, which occurred June 30, 1995, and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of Arethusa Common Stock) as if each had occurred at the beginning of fiscal year 1995. Set forth below in this footnote (a) are the historical amounts, and the adjustments thereto, upon which the pro forma Arethusa amounts are based.

ARETHUSA PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT
YEAR ENDED SEPTEMBER 30, 1995

	HISTORICAL		ADJUSTMENTS			
	ARETHUSA	YATZY(1)	YATZY ACQUISITION	STAWINNER SALE	DIVIDEND/ CAPITAL DISTRIBUTION	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)					
Contract drilling revenue	$122,147	$12,315	$ --	$(14,296)(6)	$ --	$120,166
Operating expenses:						
Direct costs	87,953	8,060	(623)(5) (375)(2)	(8,483)(6)	--	86,532
General and administrative	8,658	--	375(2)	--	--	9,033
Depreciation	29,547	--	1,352(3)	(1,891)(6)	--	29,008
Total operating expenses	126,158	8,060	729	(10,374)	--	124,573
Operating income (loss)	(4,011)	4,255	(729)	(3,922)	--	(4,407)
Other income (expense):						
Interest expense	(6,311)	--	(1,168)(4)	782(6)	--	(6,697)
Interest income	5,692	--	--		(1,453)(7)	4,239
Gain (loss) on sale of assets	27,820	--	--	(27,885)(6)	--	(65)
Other, net	(126)	--	--	--	--	(126)
Income (loss) before income taxes	23,064	4,255	(1,897)	(31,025)	(1,453)	(7,056)
Tax provision	(1,440)	--	--	--	--	(1,440)
Net income (loss)	$ 21,624	$ 4,255	$(1,897)	$(31,025)	$(1,453)	$ (8,496)
Net income (loss) per common share	$ 1.06					$ (0.42)
Weighted average common shares outstanding	20,333					20,333

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(1) The historical financial information of the Yatzy operations for the period from October 1, 1994, through May 2, 1995 is based upon Arethusa records, as manager of the rig. The previous owner of the rig prepared financial information only on a semi-annual, calendar year basis; and was unable to provide the complete financial information for the twelve months ended September 30, 1995. Financial statement captions for which Yatzy historical information is not presented (historical depreciation and interest expense) would have been adjusted to reflect Arethusa's cost basis in the Arethusa Yatzy and Arethusa's financing of the rig. Pro forma Yatzy acquisition adjustments (3) and (4) discussed below provide fully for depreciation using Arethusa's cost basis in the Arethusa Yatzy and interest based on Arethusa's financing of the rig. Additionally, it is management's understanding that there are no other significant transactions or activities related to the historical operations of Yatzy which would have a material impact on the as-adjusted pro forma income statement. Therefore, management believes the resulting pro forma income statement is in compliance with Article 11 of Regulation S-X.

(2) To reclassify and eliminate the management fee paid to Arethusa from direct costs to general and administrative expenses.

(3) To reflect depreciation expense calculated based upon Arethusa's cost and estimated useful life of 25 years, which is consistent with Arethusa's previously established depreciation policy.

(4) To adjust for additional interest expense associated with Arethusa's $30.0 million note entered into in connection with the acquisition of the Arethusa Yatzy.

(5) To adjust for a reduction in insurance expense resulting from Arethusa's lower insured value for the Arethusa Yatzy.

(6) To reflect the elimination of historical operations, interest expense and gain on sale of assets for the Treasure Stawinner.

(7) To reflect the reduction in interest income resulting from the dividend and capital distribution made to shareholders in fiscal 1995.

(b) To record the additional depreciation expense and amortization of goodwill resulting from the allocation of the purchase price. The pro forma adjustment assumes an 18-year average estimated useful life for depreciation and a 20-year amortization period for goodwill.

(c) To adjust interest expense, assuming that the Diamond Offshore Initial Public Offering and repayment of indebtedness occurred on January 1, 1995.

(d) To record income tax expense on the effect of the pro forma adjustments to depreciation and amortization and interest expense.

(e) Weighted average shares outstanding as if both the October 1995 issuance of 15.0 million shares by Diamond Offshore through the Diamond Offshore Initial Public Offering and the 17.9 million shares to be issued by Diamond Offshore in consideration of the Arethusa Common Stock had taken place on January 1, 1995.

(f) After the Diamond Offshore Initial Public Offering, Diamond Offshore had 50.0 million shares of Diamond Offshore Common Stock outstanding. Assuming the Diamond Offshore Initial Public Offering had occurred at January 1, 1995, Diamond Offshore would have recognized net income of $10.0 million, or $0.20 per share of Diamond Offshore Common Stock, after adjusting for the after-tax effects of a reduction in interest expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with Diamond Offshore's Consolidated Financial Statements (including the Notes thereto) included elsewhere in this Prospectus Supplement.

RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 1996 AND 1995

Comparative data relating to Diamond Offshore's revenues and operating expenses by equipment type are listed below (eliminations offset dayrate revenues earned when Diamond Offshore's rigs are utilized in its turnkey operations). Diamond Offshore's drillship, Ocean Clipper I, is included in Other Semisubmersibles for discussion purposes.

	THREE MONTHS ENDED MARCH 31, 1996	THREE MONTHS ENDED MARCH 31, 1995	INCREASE/ (DECREASE)
	(IN THOUSANDS)		
REVENUES			
Fourth-Generation Semisubmersibles	$ 21,465	$ 11,703	$ 9,762
Other Semisubmersibles	52,995	35,511	17,484
Jack-ups	20,136	16,926	3,210
Turnkey	13,626	3,143	10,483
Land	5,102	5,475	(373)
Other	--	--	--
Eliminations	(6,456)	(1,998)	(4,458)
Total Revenues	$106,868	$ 70,760	$ 36,108
CONTRACT DRILLING EXPENSE			
Fourth-Generation Semisubmersibles	$ 7,898	$ 8,294	$ (396)
Other Semisubmersibles	31,490	30,774	716
Jack-ups	14,927	15,506	(579)
Turnkey	14,128	4,598	9,530
Land	4,772	4,709	63
Other	(602)	(132)	(470)
Eliminations	(6,456)	(1,998)	(4,458)
Total Contract Drilling Expense	$ 66,157	$ 61,751	$ 4,406
OPERATING INCOME (LOSS)			
Fourth-Generation Semisubmersibles	$ 13,567	$ 3,409	$ 10,158
Other Semisubmersibles	21,505	4,737	16,768
Jack-ups	5,209	1,420	3,789
Turnkey	(502)	(1,455)	953
Land	330	766	(436)
Other	602	132	470
General and Administrative Expense	(3,103)	(3,140)	37
Depreciation Expense	(12,069)	(14,988)	2,919
Gain on Sale of Assets	157	389	(232)
Total Operating Income (Loss)	$ 25,696	$ (8,730)	$ 34,426

REVENUES. The $9.8 million increase in revenues from fourth-generation semisubmersibles resulted from improvements in dayrates ($6.3 million) and increases in utilization ($3.5 million). The improvement in utilization for 1996 was partially attributable to the relocation between markets of two fourth-generation rigs during the comparable period of the prior year, reducing the days worked for these rigs during that period. The $17.5 million increase in revenues from other semisubmersibles was primarily attributable to increases in dayrates in both the North Sea and the Gulf of Mexico. These increases were partially offset by a reduction in revenues of approximately $4.8 million due to the Ocean Princess and the Ocean Baroness being out of service while modifications were being performed prior to these rigs beginning term contracts in the North Sea and South America, respectively. The $3.2 million increase in revenues from jack-ups resulted from increased utilization and dayrates in the Gulf of Mexico. The $10.5 million increase in turnkey revenues resulted from projects of greater magnitude completed during the first quarter of 1996 as compared to those completed during the same period of the prior year. In addition, Diamond Offshore performed overall project management services for two customers during the current year, generating approximately $2.7 million which is included in turnkey revenue for the first quarter of 1996.

CONTRACT DRILLING EXPENSE. Contract drilling expense for fourth-generation semisubmersibles, other semisubmersibles, and jack-ups was relatively unchanged from the first quarter of the prior year. The $9.5 million increase in turnkey expense resulted from more extensive turnkey wells drilled, project management services provided and cost overruns on one turnkey well during the current year.

GENERAL AND ADMINISTRATIVE EXPENSE. General and administrative expense of $3.1 million for the quarter ended March 31, 1996 was unchanged from the comparable period of the prior year.

DEPRECIATION EXPENSE. Depreciation expense of $12.1 million for the quarter ended March 31, 1996 included a change in accounting estimate to increase the estimated useful lives for certain classes of rigs which reduced depreciation expense by approximately $2.1 million, as compared to the quarter ended March 31, 1995. Partially offsetting this decrease were increases in depreciation for three rig upgrades performed in 1995 and capital expenditures associated with Diamond Offshore's continuing rig enhancement program. In addition, depreciation expense for the comparable period of the prior year included a $2.1 million write-down in the carrying value of a semisubmersible.

INTEREST EXPENSE. Diamond Offshore incurred $0.2 million of interest expense for the quarter ended March 31, 1996 as compared to $8.5 million for the same period of the prior year. This decrease was attributable to a reduction in the outstanding indebtedness resulting from the repayment of Diamond Offshore's loan from Loews in connection with the Diamond Offshore Initial Public Offering in October 1995. The $0.2 million of interest expense for 1996 has been capitalized to the cost of construction on the Ocean Quest and Ocean Star. See Notes 3 and 5 to Diamond Offshore's Consolidated Financial Statements included in this Prospectus Supplement.

INCOME TAX (EXPENSE) BENEFIT. The income tax (expense) benefit for the quarter ended March 31, 1996 was $(7.4) million as compared to $5.3 million for the comparable period of the prior year. This change resulted primarily from the increase of $43.0 million in Diamond Offshore's income before income tax (expense) benefit.

NET INCOME (LOSS). Net income for the quarter ended March 31, 1996 increased $30.3 million to $18.7 million, as compared to a net loss of $(11.6) million for the comparable period of the prior year. The increase resulted primarily from an increase in operating income of $34.4 million and a decrease in interest expense of $8.5 million, partially offset by an increase in income tax expense of $12.7 million.

OUTLOOK

The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances, including 3-D seismic, horizontal drilling, and subsea completion procedures. Both the Gulf of Mexico and the North Sea semisubmersible markets have experienced increased utilization and significantly higher dayrates through the first quarter of 1996. Customers are continuing to contract rigs serving those markets under term contracts (as opposed to contracts let on a single well or well-to-well basis). In the Gulf of Mexico, the Ocean Valiant's contract has been extended through 1996 at an increased dayrate. Contracts for Diamond Offshore's other semisubmersibles in the Gulf of Mexico continue to be primarily on a well-to-well or multi-well basis. However, term contract opportunities are becoming more prevalent. Diamond Offshore's drillship, the Ocean Clipper I, is scheduled to be upgraded during 1996 and 1997 to operate in the ultra-deep water market of the Gulf of Mexico with dynamic positioning capabilities, in connection with a four-year term contract with a major oil company that has been agreed to in principle. The oil company has an option to terminate the contract prior to its scheduled termination date upon payment to Diamond Offshore of a termination fee. See " -- Capital Resources" in this Prospectus Supplement.

In the North Sea, the Ocean Alliance is contracted for work through late 1996 and has received an increase in its dayrate. Diamond Offshore's three other marketed semisubmersibles in the North Sea are all committed under term contracts. The Ocean Nomad, which was relocated from South America, began its two-year contract in late November 1995. The Ocean Princess has completed the modifications necessary for its two-year contract which commenced in late March 1996. The Ocean Guardian is currently drilling pursuant to a one-year term contract expiring during the third quarter of 1996. Of the remaining semisubmersibles in Diamond Offshore's fleet, the Ocean Baroness completed modifications and began, in early April 1996, a three-year term contract for drilling offshore Brazil. In addition, the Ocean Zephyr, also operating offshore Brazil, is contracted to July 1997.

The market for jack-up rigs in the Gulf of Mexico appears to have stabilized and has shown some signs of strengthening in recent months. Dayrates have improved from those earned in early 1995; however, volatile natural gas prices and an oversupply of rigs prevented significant improvements through early 1996.

Historically, the offshore contract drilling market has been highly competitive and cyclical, and Diamond Offshore cannot predict the extent to which current conditions will continue.

LIQUIDITY

Net cash provided by operating activities for the three months ended March 31, 1996 increased by $13.0 million to $23.7 million, as compared to $10.7 million for the comparable period of the prior year. This increase was attributable to a $30.3 million increase in net income for the first quarter of 1996, partially offset by an increase of $13.1 million in accounts receivable, as compared to a decrease in accounts receivable of $4.6 million for the same period of the prior year. Cash used in investing activities increased $36.8 million primarily due to capital expenditures for major upgrades of $32.7 million and $8.2 million for the purchase during the first quarter of 1996 of the land and eight-story building in which Diamond Offshore has its corporate headquarters. Cash provided by financing activities for the three months ended March 31, 1996 increased $19.2 million primarily due to net borrowings of $15.0 million on the Diamond Offshore Bank Credit Facility as compared to $6.0 million net repayments on Diamond Offshore's indebtedness during the same period of the prior year.

Diamond Offshore uses funds available under the Diamond Offshore Bank Credit Facility, together with cash flow from operations, to fund its capital expenditure and working capital requirements. The Diamond Offshore Bank Credit Facility is a revolving line of credit for a five-year term providing a maximum credit commitment of $150.0 million until the second anniversary, at which time and at the end of each six-month period thereafter, the commitment will decrease by $12.5 million to a final maximum credit commitment of $75.0 million during the last six months. Borrowings under the Diamond Offshore Bank Credit Facility bear interest, at Diamond Offshore's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. Diamond Offshore is required to pay a commitment fee of .375% on the unused available portion of the maximum credit commitment. Borrowings are secured by security interests in certain of Diamond Offshore's assets. The Diamond Offshore Bank Credit Facility also contains covenants that limit the amount of total consolidated debt, require the maintenance of certain consolidated financial ratios and limit dividends and similar payments. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity" in the accompanying Prospectus. As of March 31, 1996, Diamond Offshore was in compliance with each of these covenants.

It is anticipated that the Diamond Offshore Bank Credit Facility will be used primarily to fund rig upgrades and similar capital expenditure requirements. In management's opinion, Diamond Offshore's cash generated from operations and borrowings available under the Diamond Offshore Bank Credit Facility are sufficient to meet its anticipated short- and long-term liquidity needs, including its capital expenditure requirements.

CAPITAL RESOURCES

Cash requirements for capital commitments result from rig upgrades to meet specific customer requirements and from Diamond Offshore's continuing rig enhancement program, including top-drive drilling system installations and water depth and drilling capability upgrades. Diamond Offshore expects to spend approximately $198.1 million, including interest expense to be capitalized, during 1996 for rig upgrades in connection with contract requirements. Included in this amount is approximately $55.8 million for 1996 expenditures in conjunction with the planned upgrade of the Ocean Clipper I to operate in deep water with dynamic positioning capabilities. In addition, approximately $124.7 million is included for the upgrades relating to a letter of intent and a contract for the Ocean Star and Ocean Quest, respectively. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Outlook" in the accompanying Prospectus. Because these projects are expected to be accompanied by term contracts at favorable dayrates, the expenditures are, in Diamond Offshore's opinion, financially justified. During the first quarter of 1996, $32.7 million was expended on these projects. Diamond Offshore expects to evaluate other projects as opportunities arise. In addition, Diamond Offshore has budgeted $40.4 million for 1996 capital expenditures associated with its continuing rig enhancement program. During the first quarter of 1996, $2.9 million was expended on this program. It is management's opinion that significant improvements in operating cash flow resulting from current conditions of improved dayrates and the increasing number of term contracts for rigs in certain markets, in conjunction with borrowings under the Diamond Offshore Bank Credit Facility, will be sufficient to meet these capital requirements.

Diamond Offshore is analyzing financing alternatives that may be available to it in the public or private capital markets. Proceeds of any such financing transactions may be used for repayment of higher cost debt, to fund rig upgrades, acquisitions or for other corporate purposes. Diamond Offshore's ability to effect any such financings will be dependent on its historical results of operations and its current financial condition and prospects at the time it seeks access to the capital markets, and to other factors beyond Diamond Offshore's control, including the prevailing interest rate environment and, with respect to offerings of common or preferred stock or debt obligations convertible into such common stock, other financial market conditions, and the investment community's perception of Diamond Offshore and the offshore contract drilling industry generally. Any such offering would be subject to the restrictions imposed by the Shareholders Agreement, dated as of February 9, 1996, as amended (as so amended, the "Shareholders Agreement"), among Diamond Offshore, Diamond Offshore (USA), Acquisition Sub, Alphee and Ratos, on public sales or distributions of Diamond Offshore Common Stock, or securities convertible into common stock, and until October 10, 1996, to obtaining the prior written consent of CS First Boston Corporation ("CS First Boston") as required by the underwriting agreement entered into in connection with the Diamond Offshore Initial Public Offering. See "Underwriting" in this Prospectus Supplement and "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity," "-- Capital Resources" and "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders" in the accompanying Prospectus.

Also, from time to time Diamond Offshore reviews acquisition opportunities, although Diamond Offshore has no current plans to purchase or otherwise acquire additional rigs, other than with respect to the Acquisition. See "-- Other" in this Prospectus Supplement.

OTHER

ACQUISITION OF ARETHUSA. Diamond Offshore consummated the Acquisition on April 29, 1996. Under the Plan of Acquisition and the Amalgamation Agreement, holders of Arethusa Common Stock will receive approximately 17.9 million shares of Diamond Offshore Common Stock to be issued by Diamond Offshore based on a ratio of .88 shares of Diamond Offshore Common Stock for each share of Arethusa common stock (the "Amalgamation Ratio").

SALE OF ASSET. Subsequent to March 31, 1996, Diamond Offshore entered into an agreement to sell its jack-up drilling rig, the Ocean Magallanes, to Cliffs Drilling Company for $4.5 million. The rig is currently stacked in Punta Arenas, Chile. The sale, expected to close during the second quarter of 1996, will generate an after-tax gain of approximately $2.0 million for Diamond Offshore.

CURRENCY RISK. Certain of Diamond Offshore's subsidiaries use the local currency in the country where they conduct operations as their functional currency. Currency environments in which Diamond Offshore has material business operations include the U.K., Australia and Brazil. Diamond Offshore generally attempts to minimize its currency exchange risk by seeking international contracts payable in local currency in amounts equal to Diamond Offshore's estimated operating costs payable in local currency and in U.S. dollars for the balance of the contract. Because of this strategy, Diamond Offshore has minimized its unhedged net asset or liability positions denominated in local currencies and has not experienced significant gains or losses associated with changes in currency exchange rates. However, contracts presently covering three of Diamond Offshore's four rigs operating in the U.K. sector of the North Sea are payable in U.S. dollars. Diamond Offshore has not hedged its exposure to changes in the exchange rate between U.S. dollars and pounds sterling for operating costs payable in pounds sterling, although it may seek to do so in the future.

Currency translation adjustments are accumulated in a separate section of stockholders' equity. However, when Diamond Offshore ceases its operations in a currency environment, the accumulated adjustments are recognized currently in results of operations. Translation gains and losses for Diamond Offshore's operations in Brazil have been recognized currently due to the hyperinflationary status of this environment. The effect on results of operations has not been material and is not expected to have a significant effect in the future due to the recent stabilization of currency rates in Brazil.

ACTIVE MOBILE OFFSHORE DRILLING RIGS

Information as of April 24, 1996 concerning the Diamond Offshore fleet of active mobile offshore drilling rigs is set forth in the table below.

TYPE AND NAME(A)	WATER DEPTH CAPABILITY (FT)	ATTRIBUTES(B)	YEAR BUILT/LATEST ENHANCEMENT(C)	CURRENT LOCATION	CUSTOMER(D)
FOURTH-GENERATION SEMISUBMERSIBLES(3):					
Ocean Alliance........	5,000	TDS; DP; 15K; 3M	1988/1995	North Sea	BP
Ocean America.........	5,000	TDS; SP; 15K; 3M	1988/1992	Gulf of Mexico	BP
Ocean Valiant.........	5,000	TDS; SP; 15K; 3M	1988/1995	Gulf of Mexico	Exxon
OTHER SEMISUBMERSIBLES(27):					
Arethusa Worker.......	3,300	TDS	1982/1992	Gulf of Mexico	Texaco
Ocean Voyager.........	3,200	TDS; VC	1973/1995	Gulf of Mexico	Enserch
Arethusa Yatzy(e).....	3,000	TDS; DP	1989	Brazil	Petrobras
Arethusa Lexington....	2,500	TDS; 3M	1976/1995	Gulf of Mexico	Marathon
Arethusa Neptune......	2,500	TDS; 3M	1977/1995	Gulf of Mexico	Kerr-McGee
Arethusa Concord......	2,200	TDS	1975/1995	Gulf of Mexico	Shell
Arethusa Saratoga.....	2,200	TDS; 3M	1976/1995	Gulf of Mexico	Shell
Arethusa Yorktown.....	2,200	TDS	1976/1989	Brazil	Petrobras
Ocean Endeavor........	2,000	TDS; VC	1975/1994	Gulf of Mexico	Oryx
Ocean Rover...........	2,000	TDS; VC; 15K	1973/1992	Gulf of Mexico	Amerada Hess
Ocean Prospector......	1,700	VC	1971/1981	Gulf of Mexico	Newfield(f)
Arethusa Whittington.........	1,500	TDS; 3M	1974/1995	Gulf of Mexico	Mobil
Ocean Bounty..........	1,500	TDS; VC; 3M	1977/1992	Australia/ Indonesia	BHPP
Ocean Guardian........	1,500	TDS; SP; 3M	1985	North Sea	BP
Ocean New Era.........	1,500	TDS	1974/1990	Gulf of Mexico	Hardy Oil & Gas(g)
Ocean Princess........	1,500	TDS; 15K	1977/1995	North Sea	Marathon
Ocean Epoch...........	1,200	TDS	1977/1990	Australia	BHPP
Ocean General.........	1,200	TDS	1976/1990	Vietnam	Pedco
Ocean Nomad...........	1,200	TDS	1975/1995	North Sea	Shell
Ocean Ambassador(h)...	1,100	TDS	1975/1995	Gulf of Mexico	Committed
Ocean Baroness........	1,100	TDS; VC	1973/1995	Brazil	Petrobras
Ocean Star(i)(j)......	850	VC	1974/1992	Gulf of Mexico	Committed
Ocean Century.........	800		1973	Gulf of Mexico	Stacked
Ocean Quest(k)........	800	VC	1973	Gulf of Mexico	Committed
Ocean Liberator.......	600		1974	Nigeria	Ashland
Ocean Victory.........	600	VC	1972	North Sea	Stacked
Ocean Zephyr..........	600		1972	Brazil	Petrobras
JACK-UPS(19):					
Ocean Titan...........	350	TDS; IS; 15K; 3M	1974/1989	Gulf of Mexico	LL&E
Ocean Tower...........	350	IS; 3M	1972	Gulf of Mexico	Sonat Exploration(l)
Bonito II(m)..........	300	TDS; IC	1983/1995	Gulf of Mexico	Unocal
Miss Kitty(n).........	300	IC	1982	Enroute	ONGC
Ocean King............	300	TDS; IC	1973/1989	Gulf of Mexico	Conoco
Ocean Nugget..........	300	TDS; IC	1976/1995	Gulf of Mexico	Amoco
Ocean Summit..........	300	SDS; IC	1972/1991	Gulf of Mexico	Forcenergy
Ocean Warwick.........	300	TDS; IS; SO	1971/1984	Gulf of Mexico	Stacked
Arethusa Heritage.....	250	TDS; IC	1981/1995	Egypt	EDC
Arethusa Sovereign....	250	TDS; IC	1981/1994	Indonesia	Maxus
Ocean Champion........	250	MS	1975/1985	Gulf of Mexico	Chevron
Ocean Columbia........	250	TDS; IC	1978/1990	Gulf of Mexico	Coastal Oil & Gas
Ocean Spartan.........	250	TDS; IC	1980/1994	Gulf of Mexico	Meridian
Ocean Spur............	250	TDS; IC	1981/1994	Gulf of Mexico	Houston Exploration(o)
Ocean Conquest........	200	MS	1978	Gulf of Mexico	Stacked
Ocean Crusader........	200	TDS; MC	1982/1992	Gulf of Mexico	Chevron
Ocean Drake...........	200	TDS; MC	1983/1986	Gulf of Mexico	Murphy
Arethusa Scotian......	180	TDS; IC; 15K	1981/1988	North Sea (Dutch sector)	Elf
Ocean Magallanes(p)...	150	IC	1980	Chile	Stacked
DRILLSHIP(1):					
Ocean Clipper I.......	1,200	SP	1976	Enroute	Committed(q)

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(a) Does not include one other semisubmersible rig held for disposition that is also not included in the discussion of Diamond Offshore's fleet.

(b) Attributes legend:

DP	--	Dynamically Positioned/Self-Propelled
MS	--	Mat-Supported Slot Rig
TDS	--	Top-Drive Drilling System
IC	--	Independent-Leg Cantilevered Rig
SDS	--	Side-Drive Drilling System
VC	--	Victory-Class
IS	--	Independent-Leg Slot Rig
SO	--	Skid-Off Capability
3M	--	Three Mud Pumps
MC	--	Mat-Supported Cantilevered Rig
SP	--	Self-Propelled
15K	--	15,000 psi Blowout Preventer

(c) Such enhancements include the installation of top-drive drilling systems, water depth upgrades, mud pump additions and increases in deck load capacity.

(d) For ease of presentation in this table, customer names have been shortened or abbreviated.

(e) Arethusa acquired the Arethusa Yatzy on May 3, 1995. Prior to this date the rig was operated by Arethusa under a management agreement.

(f) Turnkey operator is ADTI.

(g) Project manager is DOTS.

(h) Committed for two-well contract after completion of rig enhancements.

(i) Formerly named Ocean Countess.

(j) Committed under a letter of intent for a three-year term contract with Texaco in the Gulf of Mexico.

(k) Committed under a three-year term contract with Chevron in the Gulf of Mexico.

(l) Turnkey operator is Triton.

(m) Diamond Offshore charters the rig pursuant to a bareboat charter agreement which expires in August 1996. The rig is under contract for sale, upon closing of which such charter will terminate.

(n) Diamond Offshore operates the rig pursuant to a bareboat charter agreement which expires in July 1997. Diamond Offshore has the option to extend the charter agreement for one additional year. The rig is enroute to India following completion of leg repairs.

(o) Turnkey operator is Brown/R&B.

(p) Under contract for sale.

(q) Committed under an agreement in principle for a four-year term contract in the Gulf of Mexico following completion of rig enhancement.

UNDERWRITING

Subject to the terms and conditions set forth in the international purchase agreement (the "International Purchase Agreement") among Diamond Offshore, the Selling Stockholders and each of the underwriters named below (the "International Managers"), and concurrently with the sale of 6,018,140 shares of Diamond Offshore Common Stock to the U.S. Underwriters (as defined below), the Selling Stockholders have agreed to sell to the International Managers, and each of the International Managers severally has agreed to purchase from the Selling Stockholders, the number of shares of Diamond Offshore Common Stock set forth opposite its name below.

INTERNATIONAL MANAGER	NUMBER OF SHARES
Merrill Lynch International	505,000
CS First Boston Limited	500,000
Salomon Brothers International Limited	500,000
Total	1,505,000

Merrill Lynch International, CS First Boston Limited and Salomon Brothers International Limited are acting as representatives (the "International Representatives") of the International Managers.

Diamond Offshore and the Selling Stockholders have also entered into the U.S. purchase agreement (the "U.S. Purchase Agreement") with certain other underwriters in the United States and Canada (the "U.S. Underwriters" and, together with the International Managers, the "Underwriters") for whom Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch"), CS First Boston and Salomon Brothers Inc are acting as representatives (the "U.S. Representatives"). Subject to the terms and conditions set forth in the U.S. Purchase Agreement, and concurrently with the sale of 1,505,000 shares of Diamond Offshore Common Stock to the International Managers pursuant to the International Purchase Agreement, the Selling Stockholders have agreed to sell to the U.S. Underwriters, and the U.S. Underwriters severally have agreed to purchase from the Selling Stockholders, an aggregate of 6,018,140 shares of Diamond Offshore Common Stock. The public offering price per share of the Diamond Offshore Common Stock and the total underwriting discount per share are identical under the International Purchase Agreement and the U.S. Purchase Agreement.

In the International Purchase Agreement and the U.S. Purchase Agreement, the several International Managers and the several U.S. Underwriters, respectively, have agreed, subject to the terms and conditions set forth therein, to purchase all of the shares of Diamond Offshore Common Stock being sold pursuant to each such Purchase Agreement if any of such shares of Diamond Offshore Common Stock being sold pursuant to each such Purchase Agreement are purchased. Under certain circumstances, the commitments of non-defaulting International Managers or U.S. Underwriters (as the case may be) may be increased. The closings with respect to the sale of shares of Diamond Offshore Common Stock to be purchased by the International Managers and the U.S. Underwriters are conditioned upon one another.

The International Managers and the U.S. Underwriters have entered into an intersyndicate agreement (the "Intersyndicate Agreement") providing for the coordination of their activities. Under the terms of the Intersyndicate Agreement, the International Managers and the U.S. Underwriters are permitted to sell shares of Diamond Offshore Common Stock to each other for purposes of resale at the public offering price, less an amount not greater than the selling concession. Under the terms of the Intersyndicate Agreement, the International Managers and any dealer to whom they sell shares of Diamond Offshore Common Stock will not offer to sell or sell shares of Diamond Offshore Common Stock to persons who are United States and Canadian persons or to persons they believe intend to resell to persons who are United States and Canadian persons, and the U.S. Underwriters and any dealer to whom they sell shares of Diamond Offshore Common Stock will not offer to sell or sell shares of Diamond Offshore Common Stock to persons who are non-United States persons or non-Canadian persons or to persons they believe intend to resell to persons who are non-

The International Representatives have advised Diamond Offshore and the Selling Stockholders that the International Managers propose to offer the shares of Diamond Offshore Common Stock offered hereby to the public at the public offering price set forth on the cover page of this Prospectus Supplement, and to certain dealers at such price less a concession not in excess of $.90 per share of Diamond Offshore Common Stock. The International Managers may allow, and such dealers may reallow, a discount not in excess of $.10 per share of Diamond Offshore Common Stock on sales to certain other dealers. After the public offering, the public offering price, concession and discount may be changed.

The Selling Stockholders have granted an option to the International Managers, exercisable during the 30-day period after the date of this Prospectus Supplement, to purchase up to an aggregate of 150,501 additional shares of Diamond Offshore Common Stock at the public offering price, less the underwriting discount. The International Managers may exercise this option only to cover over-allotments, if any, made on the sale of Diamond Offshore Common Stock offered hereby. To the extent that the International Managers exercise this option, each International Manager shall be obligated, subject to certain conditions, to purchase the number of additional shares of Diamond Offshore Common Stock proportionate to such International Manager's initial amount reflected in the foregoing table. The Selling Stockholders also have granted an option to the U.S. Underwriters, exercisable during the 30-day period after the date of this Prospectus Supplement, to purchase up to an aggregate of 601,814 additional shares of Diamond Offshore Common Stock to cover over-allotments, if any, on terms similar to those granted to the International Managers.

The Selling Stockholders have agreed not to directly or indirectly sell, offer to sell, grant any option for sale of, contract or otherwise transfer any shares of Diamond Offshore Common Stock (except for the shares offered hereby) or any securities convertible into or exchangeable or exercisable for Diamond Offshore Common Stock for a period of 90 days after the date of this Prospectus Supplement (the "Underwriters' Restricted Period") without the prior written consent of Merrill Lynch. In addition, the Selling Stockholders have agreed that, during the Underwriters' Restricted Period, without the prior written consent of Merrill Lynch, the Selling Stockholders will not release Diamond Offshore from Diamond Offshore's obligation under the Shareholders Agreement not to effect, and to cause Loews to agree not to effect, any public sale or distribution of any securities the same as or similar to the Diamond Offshore Common Stock, or any securities convertible into or exchangeable into securities the same as or similar to the Diamond Offshore Common Stock (except pursuant to registrations on Form S-4 or any successor form, or Form S-8 or any successor form relating solely to securities offered pursuant to any benefit plan). See "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders" in the accompanying Prospectus.

Each International Manager represents and agrees that (a) it has not offered or sold and prior to the expiry of six months from the closing date of the Offerings, will not offer or sell any shares of Diamond Offshore Common Stock to persons in the United Kingdom, except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995, (b) it has complied and will comply with all applicable provisions of the Financial Services Act 1986 with respect to anything done by it in relation to the Diamond Offshore Common Stock in, from or otherwise involving the United Kingdom, and (c) it has only issued or passed on and will only issue or pass on to any person in the United Kingdom any document received by it in connection with the issue or sale of the Diamond Offshore Common Stock if that person is of a kind described in Article 11(3) of the Financial Services Act 1986 (Investment Advertisements) (Exemptions) Order 1995 or is a person to whom such document may otherwise lawfully be issued or passed on.

No action has been or will be taken in any jurisdiction (except in the United States) that would permit a public offering of the shares of Diamond Offshore Common Stock or the possession, circulation or distribution of this Prospectus Supplement or the accompanying Prospectus or any other material relating to Diamond Offshore, the Selling Stockholders or shares of Diamond Offshore Common Stock in any jurisdiction where action for that purpose is required. Accordingly, the shares of Diamond Offshore Common Stock may not be offered or sold, directly or indirectly, and neither this Prospectus Supplement or the accompanying Prospectus nor any other offering material or advertisements in connection with the shares of Diamond Offshore Common

Stock may be distributed or published, in or from any country or jurisdiction except in compliance with any applicable rules and regulations of such country or jurisdiction.

Purchasers of the shares of Diamond Offshore Common Stock offered hereby may be required to pay stamp taxes and other charges in accordance with the laws and practices of the country of purchase, in addition to the offering price set forth on the cover page of this Prospectus Supplement.

Pursuant to the terms of an engagement letter dated September 1, 1995 (as amended), Arethusa has agreed to pay Merrill Lynch $7.5 million for financial advisory services in connection with the Acquisition. Arethusa has also agreed to reimburse Merrill Lynch for its reasonable out-of-pocket expenses, including all reasonable fees and disbursements of counsel, and to indemnify Merrill Lynch and certain related persons against certain liabilities relating to or arising out of its engagement, including certain liabilities under the federal securities laws. In addition, during the past two years Merrill Lynch has performed investment banking services for Loews, an affiliate of Diamond Offshore, from time to time and has been compensated therefor. Such services have included, among other things, acting as manager of, or participating as a syndicate member in, various securities transactions of Loews and its subsidiaries and providing financial advisory services to Loews.

In consideration of financial advisory services rendered in connection with the Acquisition, Diamond Offshore has agreed to pay CS First Boston a $500,000 fee. In addition, Diamond Offshore has agreed to reimburse CS First Boston for all reasonable out-of-pocket expenses, including the fees and expenses of its legal counsel and any other advisor retained by CS First Boston resulting from or arising out of Diamond Offshore's engagement of CS First Boston with respect to the Acquisition, and has agreed to indemnify CS First Boston (and its directors, officers, employees, and persons controlling CS First Boston) against certain liabilities and expenses in connection with the Acquisition, including certain liabilities under federal securities laws.

The Underwriters do not intend to confirm sales of the shares of Diamond Offshore Common Stock offered hereby to any accounts over which they exercise discretionary authority.

Diamond Offshore, Loews and the Selling Stockholders have agreed to indemnify the Underwriters against certain liabilities, including certain liabilities under the Securities Act of 1933, as amended, or to contribute to payments the Underwriters may be required to make in respect thereof. The Underwriters have agreed to pay certain expenses of the Selling Stockholders incurred in connection with the sale of the Offered Shares estimated at $100,000.

LEGAL MATTERS

The validity of the shares of Diamond Offshore Common Stock offered hereby will be passed on for Diamond Offshore by Weil, Gotshal & Manges LLP, Houston, Texas. Certain legal matters will be passed on for the Underwriters by Skadden, Arps, Slate, Meagher & Flom, New York, New York.

INDEX TO PROSPECTUS SUPPLEMENT FINANCIAL STATEMENTS

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	MARCH 31, 1996	DECEMBER 31, 1995
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 3,867	$ 10,306
Short-term investments	5,110	5,041
Accounts receivable	87,624	74,496
Rig inventory and supplies	15,746	15,330
Prepaid expenses and other	8,209	10,601
Total current assets	120,556	115,774
DRILLING AND OTHER PROPERTY AND EQUIPMENT, LESS ACCUMULATED DEPRECIATION	533,645	502,278
OTHER ASSETS	3,984	--
Total assets	$ 658,185	$ 618,052
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 14,171	$ 18,322
Accrued liabilities	35,905	33,929
Total current liabilities	50,076	52,251
LONG-TERM DEBT	15,000	--
DEFERRED TAX LIABILITY	79,737	72,907
OTHER LIABILITIES	1,740	--
Total liabilities	146,553	125,158
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Preferred stock (par value $.01, 25,000,000 shares authorized, none issued and outstanding)	--	--
Common stock (par value $.01, 200,000,000 shares authorized, 50,000,000 shares issued and outstanding)	500	500
Additional paid-in capital	665,107	665,107
Accumulated deficit	(152,712)	(171,444)
Cumulative translation adjustment	(1,263)	(1,269)
Total stockholders' equity	511,632	492,894
Total liabilities and stockholders' equity	$ 658,185	$ 618,052

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	THREE MONTHS ENDED MARCH 31,	
	1996	1995
REVENUES	$106,868	$ 70,760
OPERATING EXPENSES:		
Contract drilling	66,157	61,751
General and administrative	3,103	3,140
Depreciation	12,069	14,988
Gain on sale of assets	(157)	(389)
Total operating expenses	81,172	79,490
OPERATING INCOME (LOSS)	25,696	(8,730)
OTHER INCOME (EXPENSE):		
Interest expense	--	(8,486)
Currency transaction gains (losses)	86	(34)
Other, net	348	389
INCOME (LOSS) BEFORE INCOME TAX (EXPENSE) BENEFIT	26,130	(16,861)
INCOME TAX (EXPENSE) BENEFIT	(7,398)	5,289
NET INCOME (LOSS)	$ 18,732	$(11,572)
NET INCOME PER SHARE	$ 0.37	
WEIGHTED AVERAGE SHARES OUTSTANDING	50,000	

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	THREE MONTHS ENDED MARCH 31, 1996	1995
OPERATING ACTIVITIES:		
Net income (loss)	$ 18,732	$(11,572)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	12,069	12,918
Gain on sale of assets	(157)	(389)
Write-down of asset	--	2,070
Accrued interest converted to notes payable to Loews	--	8,484
Deferred tax provision (benefit)	7,124	(5,489)
Changes in operating assets and liabilities:		
Accounts receivable	(13,128)	4,611
Rig inventory and supplies and other current assets	2,339	(9)
Other assets, non-current	(2,583)	--
Accounts payable and accrued liabilities	(2,175)	48
Other liabilities, non-current	1,740	--
Other, net	(288)	20
Net cash provided by operating activities	23,673	10,692
INVESTING ACTIVITIES:		
Capital expenditures	(43,757)	(6,981)
Proceeds from sales of assets	478	439
Change in short-term investments	(69)	--
Net cash used in investing activities	(43,348)	(6,542)
FINANCING ACTIVITIES:		
Borrowings on revolving line of credit	37,000	--
Repayments on revolving line of credit	(22,000)	--
Deferred financing costs	(1,764)	--
Net repayments to Loews	--	(6,000)
Net cash provided by (used in) financing activities	13,236	(6,000)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(6,439)	(1,850)
Cash and cash equivalents, beginning of period	10,306	17,770
Cash and cash equivalents, end of period	$ 3,867	$ 15,920

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL

The consolidated financial statements of Diamond Offshore Drilling, Inc. and subsidiaries (the "Company") should be read in conjunction with the Annual Report on Form 10-K for the year ended December 31, 1995 (File No. 1-13926).

Interim Financial Information

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all disclosures required by generally accepted accounting principles for complete financial statements. The consolidated financial information has not been audited but, in the opinion of management, includes all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation of the consolidated balance sheets, statements of operations, and statements of cash flows at the dates and for the periods indicated. Results of operations for interim periods are not necessarily indicative of results of operations for the respective full years.

Cash and Cash Equivalents

All short-term, highly liquid investments that have an original maturity of three months or less are considered cash equivalents.

Supplementary Cash Flow Information

Non-cash financing activities for the three months ended March 31, 1995 included $8.5 million of interest expense accrued and included in notes payable to Loews Corporation ("Loews"). There were no non-cash financing activities for the three months ended March 31, 1996. Cash payments made for interest on long-term debt for the three months ended March 31, 1996 totaled $37,000.

Drilling and Other Property and Equipment

For financial reporting purposes, depreciation is provided on the straight-line method over the remaining estimated useful lives from the date the asset is placed into service. The Company believes that certain offshore drilling rigs, due to their upgrade and design capabilities and maintenance history, have an operating life in excess of their depreciable life as originally assigned. For this reason, a change in accounting estimate, effective January 1, 1996, increased the estimated useful lives for certain classes of offshore drilling rigs. As compared to the original estimate of useful lives, the effect of such change reduced depreciation expense and increased net income for the three months ended March 31, 1996 by approximately $2.1 million and $1.5 million ($0.03 per share), respectively. The estimated useful lives of the Company's offshore drilling rigs, after the change in estimate, range from 10 to 25 years.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimated.

Reclassifications

Certain amounts applicable to the prior periods have been reclassified to conform to the classifications currently followed. Such reclassifications do not affect earnings.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

2. PENDING MERGER OF THE COMPANY AND ARETHUSA (OFF-SHORE) LIMITED

The Company and Arethusa (Off-Shore) Limited ("Arethusa"), a Bermuda corporation, have entered into an agreement to merge the two companies. The agreement provides that, upon consummation of the merger, holders of Arethusa stock will receive 17.9 million shares of common stock to be issued by the Company based on 20.3 million shares of Arethusa's common stock issued and outstanding and on a ratio of .88 shares for each share of issued and outstanding Arethusa common stock. The merger is subject to requisite shareholder approval at the April 29, 1996 annual meeting of both companies. The merger will be accounted for as a purchase for financial reporting purposes, and accordingly, the costs of the merger will be allocated to assets acquired and liabilities assumed based on their estimated fair market values.

Arethusa owns a fleet of 11 mobile offshore drilling rigs, operates two additional mobile offshore drilling rigs, and provides drilling services worldwide to international and government-controlled oil and gas companies. For the year ended September 30, 1995, Arethusa reported revenues of $122.1 million, net income of $21.6 million, and net income per share of $1.06.

3. DRILLING AND OTHER PROPERTY AND EQUIPMENT

Cost and accumulated depreciation of drilling and other property and equipment are summarized as follows:

	MARCH 31, 1996	DECEMBER 31, 1995
	(IN THOUSANDS)	
Drilling rigs and equipment	$ 705,957	$ 689,438
Construction work in progress	37,271	19,016
Land and buildings	11,845	3,655
Office equipment and other	6,761	6,300
	761,834	718,409
Less accumulated depreciation	(228,189)	(216,131)
Total	$ 533,645	$ 502,278

For the three months ended March 31, 1996, the Company capitalized total interest cost incurred of $.2 million in construction work in progress with respect to qualifying construction projects.

4. ACCRUED LIABILITIES

Accrued liabilities consist of the following:

	MARCH 31, 1996	DECEMBER 31, 1995
	(IN THOUSANDS)	
Compensation and benefits	$16,517	$ 17,402
Other	19,388	16,527
Total	$35,905	$ 33,929

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

5. LONG-TERM DEBT

In the first quarter of 1996, the Company executed a definitive credit agreement governing a $150.0 million credit facility with a group of banks (the "Credit Facility"). Borrowings under the Credit Facility bear interest, at the Company's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. The Company is required to pay a commitment fee of .375% on the unused available portion of the maximum credit commitment. Debt financing costs are deferred and amortized over the term of the debt. The weighted average interest rate on the Credit Facility, including commitment and arrangement fees, was 14.5% at March 31, 1996. Borrowings are secured by security interests in certain of the Company's assets. The Credit Facility also contains covenants that limit the amount of total consolidated debt, require the maintenance of certain consolidated financial ratios and limit dividends and similar payments.

[DIAMOND OFFSHORE LOGO]

8,375,455 SHARES

DIAMOND OFFSHORE DRILLING, INC.

COMMON STOCK

($.01 PAR VALUE)

PROSPECTUS

This Prospectus relates to 8,375,455 shares (the "Offered Shares") of common stock, par value $0.01 per share ("Diamond Offshore Common Stock"), of Diamond Offshore Drilling, Inc., a Delaware corporation ("Diamond Offshore"), which Offered Shares may be offered from time to time by and for the account of Alphee S.A., a Luxembourg corporation ("Alphee"), and/or Forvaltnings AB Ratos, a Swedish corporation ("Ratos" and, together with Alphee, the "Selling Stockholders"). Diamond Offshore will not receive any of the proceeds from the sale of the Offered Shares. Diamond Offshore will bear certain costs relating to the registration of the Offered Shares.

Pursuant to the Plan of Acquisition dated as of February 9, 1996, as amended (as so amended, the "Plan of Acquisition"), among Diamond Offshore, Diamond Offshore (USA) Inc., a Delaware corporation ("Diamond Offshore (USA)"), AO Acquisition Limited, a Bermuda company ("Acquisition Sub"), and Arethusa (Off-Shore) Limited, a Bermuda company ("Arethusa"), and the Amalgamation Agreement dated as of February 9, 1996 (the "Amalgamation Agreement") between Arethusa and Acquisition Sub, Diamond Offshore acquired Arethusa (the "Acquisition"), on the terms set forth in the Plan of Acquisition and Amalgamation Agreement. All of the information presented herein assumes consummation of the Acquisition on April 29, 1996. Arethusa shareholders received 17,893,344 shares of Diamond Offshore Common Stock, representing approximately 26.4% of the total Diamond Offshore Common Stock currently outstanding, of which the Selling Stockholders received an aggregate of 8,375,455 shares.

The Offered Shares may be offered for sale from time to time by the Selling Stockholders to or through underwriters or directly to other purchasers or through agents in one or more transactions on the New York Stock Exchange, Inc. (the "NYSE"), in the over-the-counter market, in one or more private transactions, or in a combination of such methods of sale, at prices and on terms then prevailing, at prices related to such prices, or at negotiated prices. The Selling Stockholders and any brokers and dealers through whom sales of the Offered Shares are made may be deemed to be "underwriters" within the meaning of the Securities Act of 1933, as amended, and the commissions or discounts and other compensation paid to such persons may be regarded as underwriters' compensation.

Diamond Offshore Common Stock is listed on the NYSE under the symbol "DO."

FOR A DISCUSSION OF CERTAIN FACTORS THAT SHOULD BE CONSIDERED IN CONNECTION WITH AN INVESTMENT IN THE OFFERED SHARES, SEE "RISK FACTORS" BEGINNING ON PAGE 6.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THIS PROSPECTUS MAY NOT BE USED PRIOR TO CONSUMMATION OF THE ACQUISITION.

The date of this Prospectus is April 12, 1996.

NO DEALER, SALESPERSON OR OTHER INDIVIDUAL HAS BEEN AUTHORIZED TO GIVE ANY INFORMATION OR MAKE ANY REPRESENTATION NOT CONTAINED IN THIS PROSPECTUS IN CONNECTION WITH THE OFFERING COVERED BY THIS PROSPECTUS. IF GIVEN OR MADE, SUCH INFORMATION OR REPRESENTATIONS MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY DIAMOND OFFSHORE, THE SELLING STOCKHOLDERS OR THE UNDERWRITERS. THIS PROSPECTUS DOES NOT CONSTITUTE AN OFFER TO SELL, OR A SOLICITATION OF AN OFFER TO BUY, THE OFFERED SHARES IN ANY JURISDICTION WHERE, OR TO ANY PERSON TO WHOM, IT IS UNLAWFUL TO MAKE SUCH OFFER OR SOLICITATION. NEITHER THE DELIVERY OF THIS PROSPECTUS NOR ANY SALE MADE HEREUNDER SHALL, UNDER ANY CIRCUMSTANCES, CREATE AN IMPLICATION THAT THERE HAS NOT BEEN ANY CHANGE IN THE FACTS SET FORTH IN THIS PROSPECTUS OR IN THE AFFAIRS OF DIAMOND OFFSHORE SINCE THE DATE HEREOF.

AVAILABLE INFORMATION

Diamond Offshore is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and, in accordance therewith, files reports and other information with the Securities and Exchange Commission (the "Commission"). Reports, proxy and information statements filed pursuant to Sections 14(a) and 14(c) of the Exchange Act and other information filed with the Commission can be inspected and copied at the public reference facilities maintained by the Commission at Room 1024, 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549, and at the following Regional Offices of the Commission: Chicago Regional Office, Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661 and New York Regional Office, 7 World Trade Center, Suite 1300, New York, New York 10048. Copies of such material can also be obtained at prescribed rates from the Public Reference Section of the Commission at its principal office at 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549. In addition, Diamond Offshore's reports, proxy and information statements filed pursuant to Sections 14(a) and 14(c) of the Exchange Act and other information concerning Diamond Offshore can be inspected at the offices of the NYSE, 20 Broad Street, New York, New York 10005, on which exchange Diamond Offshore securities are listed.

Diamond Offshore has filed with the Commission a Registration Statement (the "Registration Statement") under the Securities Act of 1933, as amended (the "Securities Act"), on Forms S-4/S-1 with respect to the securities offered hereby. This Prospectus also constitutes the prospectus of Diamond Offshore filed as part of the Registration Statement and does not contain all of the information set forth in the Registration Statement and the exhibits thereto, certain parts of which are omitted in accordance with the rules and regulations of the Commission. Statements made in this Prospectus as to the contents of any contract, agreement or other document referred to are not necessarily complete (but are accurate statements of those matters considered by Diamond Offshore to be material to a prospective investor in the Offered Shares); with respect to each such contract, agreement or other document filed as an exhibit to the Registration Statement, reference is made to the exhibit for a more complete description of the matter involved, and each such statement shall be deemed qualified in its entirety by such reference. The Registration Statement and any amendments thereto, including exhibits filed as a part thereof, are available for inspection and copying at the Commission's offices as described above.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF DIAMOND OFFSHORE COMMON STOCK AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH TRANSACTIONS MAY BE EFFECTED ON THE NYSE OR OTHERWISE. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

DURING THIS OFFERING, CERTAIN PERSONS AFFILIATED WITH PERSONS PARTICIPATING IN THE DISTRIBUTION MAY ENGAGE IN TRANSACTIONS FOR THEIR OWN ACCOUNTS OR FOR THE ACCOUNTS OF OTHERS IN THE DIAMOND OFFSHORE COMMON STOCK PURSUANT TO EXEMPTIONS FROM RULES 10B-6, 10B-7, AND 10B-8 UNDER THE EXCHANGE ACT.

PROSPECTUS SUMMARY

The following summary is qualified in its entirety by, and should be read in conjunction with, the more detailed information and the Consolidated Financial Statements (including the Notes thereto) included elsewhere in this Prospectus. Unless the context otherwise requires, references in this Prospectus to "Diamond Offshore" shall mean Diamond Offshore Drilling, Inc. and its consolidated subsidiaries including, from and after the consummation of the Acquisition on April 29, 1996 (the "Effective Time"), Arethusa and its consolidated subsidiaries. In this Prospectus, references to "dollars" and "$" are to United States dollars.

DIAMOND OFFSHORE

Diamond Offshore engages principally in the contract drilling of offshore oil and gas wells. Diamond Offshore's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Asia and consists of 30 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 19 jack-up rigs owned and/or operated by Diamond Offshore and one drillship. Diamond Offshore also operates 10 land rigs deployed in South Texas. Except for two jack-up rigs operated pursuant to bareboat charter contracts, all of Diamond Offshore's offshore and land rigs are wholly owned.

Market Overview. The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances (including 3-D seismic, horizontal drilling and subsea completion procedures) that have broadened opportunities for offshore exploration and development. Both the Gulf of Mexico and the North Sea semisubmersible markets have experienced increased utilization and significantly higher dayrates in 1995 and 1996, and customers increasingly are seeking to contract for rigs serving these markets under term contracts (as opposed to contracts let on a single well or well-to-well basis). As part of this trend, Diamond Offshore recently received a commitment from a major oil company for a four-year term contract for its drillship Ocean Clipper I, which will support an upgrade of the rig to operate in deep water with dynamic positioning capabilities. In addition, Diamond Offshore has entered into a contract and a letter of intent with two major oil companies for two Victory-class semisubmersibles to conduct deep water drilling operations in the Gulf of Mexico under three-year term contracts, in connection with which Diamond Offshore will significantly enhance these rigs. The market for jack-up rigs in the Gulf of Mexico, which weakened during 1994, appears to have stabilized during 1995 and has shown some signs of strengthening in recent months. Historically, however, the offshore contract drilling market has been highly competitive and cyclical, and Diamond Offshore cannot predict the extent to which current conditions will continue.

Business Strategy. Diamond Offshore seeks to maximize dayrates and rig utilization by continuously adapting to changes in its markets, improving the capabilities of its drilling rigs and increasing the quality of its service. The key elements of its strategy are to:

- Market worldwide its large, diverse fleet, which is capable of satisfying customer requirements in a variety of applications;

- Continue to enhance its fleet to meet customer demand for diverse drilling capabilities, including those required for deep water and harsh environment operations;

- Exploit the potential of Diamond Offshore's nine Victory-class semisubmersible rigs by pursuing projects that take advantage of this rig type's unique design to yield significantly enhanced rigs; and

- Maintain a program of continuous improvement of quality and safety through Diamond Offshore's Global Excellence Management System and further capitalize on customer recognition of Diamond Offshore's quality and safety achievements.

The Acquisition. On April 29, 1996 Diamond Offshore completed the Acquisition, thereby augmenting its fleet with Arethusa's 13 owned and/or operated mobile offshore drilling rigs. Arethusa provided drilling services worldwide to international and government-controlled oil and gas companies. The eight semisubmersible rigs owned by Arethusa are located in the Gulf of Mexico and offshore Brazil and the five jack-up rigs in its fleet are located offshore India, Indonesia and Egypt, in the Gulf of Mexico and in the Dutch sector of the North Sea.

Pursuant to the Acquisition, Diamond Offshore issued and sold to its wholly owned subsidiary Diamond Offshore (USA) 17,893,344 shares of Diamond Offshore Common Stock, representing approximately 26.4% of the total Diamond Offshore Common Stock currently outstanding, which were contributed by Diamond Offshore (USA) to the capital of Acquisition Sub and delivered by Acquisition Sub to Arethusa shareholders in consideration of all of the issued and outstanding shares of Arethusa common stock, par value $0.10 per share ("Arethusa Common Stock"). The Acquisition was accomplished pursuant to an amalgamation (the "Amalgamation") of Arethusa with Acquisition Sub, a wholly owned subsidiary of Diamond Offshore (USA). The surviving company in the Amalgamation, Diamond Offshore Exploration (Bermuda) Limited ("Diamond Offshore Exploration (Bermuda)"), succeeded to the assets and liabilities of Arethusa and Acquisition Sub and is continuing the business of Arethusa and Acquisition Sub as a wholly owned subsidiary of Diamond Offshore (USA). See "Business -- The Acquisition."

Fleet Size and Diversity. Diamond Offshore's large, diverse fleet, which includes some of the most technologically advanced rigs in the world, enables it to offer a broad range of services worldwide in various markets, including the deep water market, the harsh environment market (such as the North Sea), the conventional semisubmersible market and the jack-up market. Diamond Offshore believes that it is well positioned to compete in the most complex deep water and harsh environment markets with its three fourth-generation semisubmersibles, each of which is capable of drilling in water depths of up to 5,000 feet and operating in harsh environments. Diamond Offshore's 27 remaining semisubmersible rigs, including 16 that are capable of drilling in waters of 1,500 feet or more and three that are currently marketed for drilling in the North Sea, give Diamond Offshore a significant presence worldwide in the expanding semisubmersible market. In addition, Diamond Offshore owns and/or operates 19 jack-up rigs with diverse capabilities that operate in water depths of up to 350 feet, including 14 capable of drilling in water depths of 250 feet or more.

Diamond Offshore believes that its presence in multiple markets provides a competitive advantage. For example, Diamond Offshore believes that its experience with safety and other regulatory matters in the United Kingdom has been beneficial in Australia and in the Gulf of Mexico and that production experience gained through Brazilian and North Sea operations has application worldwide. Additionally, Diamond Offshore believes that its performance for a customer in one market segment or area enables Diamond Offshore to better understand that customer's needs and serve that customer in different market segments or other geographic locations.

Fleet Enhancements. Diamond Offshore has continued to enhance its fleet both to increase overall technical capabilities and to meet specific drilling requirements. Diamond Offshore plans to continue its program of selectively enhancing its rigs to meet customer demand for advanced features or capabilities, including those required for operation in the deep water or harsh environment markets. For example, Diamond Offshore upgraded the semisubmersible Ocean Voyager to operate in maximum water depths of 3,200 feet and has modified the semisubmersible Ocean Nomad to allow it to be certified for service in the U.K. sector of the North Sea, where it is operating under a two-year contract at improved dayrates. Diamond Offshore converted three of its 300-foot cantilever jack-up rigs from slot rigs, which Diamond Offshore believes has resulted in these rigs achieving higher dayrates and utilization. In addition, Diamond Offshore has added top-drive drilling systems to many rigs, so that 36 rigs in Diamond Offshore's fleet are now so equipped. From time to time Diamond Offshore is able to negotiate lump-sum payments or increased dayrates from a customer to offset a portion of the costs of specific upgrades undertaken to enhance a rig to meet such customer's requirements for a particular drilling project.

Victory-Class Enhancements. The design of the Victory-class semisubmersible rigs, including their cruciform hull configurations, long fatigue-life and advantageous stress characteristics, makes this class of rig particularly well-suited for significant upgrading projects. Currently, Diamond Offshore's Victory-class rigs are outfitted for service in maximum water depths of 600 to 3,200 feet. Five of Diamond Offshore's nine Victory-class rigs are equipped with top-drive drilling systems, two are modified for increased efficiency in the handling of subsea completion equipment and one has stability enhancements that allow increased variable deck load. In management's opinion, it is unlikely that new semisubmersibles will be built unless there is a substantial and sustained improvement in the market; therefore, Diamond Offshore believes that the relative ease and efficiency with which it can significantly enhance its Victory-class rigs is a competitive advantage in a market requiring increasing capability from offshore drilling rigs.

The Ocean Quest, one of Diamond Offshore's Victory-class rigs, is currently undergoing an upgrade pursuant to contract with a major oil company for a three-year commitment. The rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 3,500 feet. This project includes enhancements to provide additional hull buoyancy, which will allow a variable deck load exceeding 5,000 tons, the addition of a new self-contained chain/wire mooring system, and drilling system upgrades, including the installation of a top-drive drilling system, a 15,000 psi blowout prevention system, a third mud pump and 2,900 barrel liquid mud capacity. The Ocean Quest is scheduled to be placed in service in the fourth quarter of 1996. In addition, during the third quarter of 1995 Diamond Offshore entered into a letter of intent with another major oil company for a three-year commitment for a second Victory-class rig, the Ocean Star (formerly named Ocean Countess), pursuant to which the rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 4,500 feet. The upgrade project for the Ocean Star also includes stability enhancements, the installation of a new mooring system and drilling system upgrades similar to those planned for the Ocean Quest. The Ocean Star is scheduled to be placed in service late in the fourth quarter of 1996. Following the upgrades, Diamond Offshore believes that these rigs will be able to compete effectively in the fourth-generation deep water market. Diamond Offshore is currently pursuing other such upgrade opportunities for its seven remaining Victory-class rigs. However, there can be no assurance that the upgrades for the Ocean Quest and the Ocean Star will be completed as planned, or within Diamond Offshore's budget for these projects, or that the definitive drilling contract contemplated by the letter of intent relating to the Ocean Star will be executed. In addition, there can be no assurance as to if, when or to what extent upgrades will be made to other Victory-class rigs in Diamond Offshore's fleet.

Additional Victory-class upgrade potential exists, including conceptual plans Diamond Offshore is developing for the possible construction of an ultra-large semisubmersible, the Ocean Legend. The Ocean Legend is intended to take advantage of the cruciform design of the Victory-class semisubmersibles to "square off" the rig by adding large corner columns and other new equipment to yield a rig with capabilities beyond a traditional fourth-generation unit at a significantly reduced cost as compared to new construction. Diamond Offshore has completed its feasibility studies and has begun preliminary design engineering in connection with the upgrade. See Note 1 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein. Although Diamond Offshore is proposing the design to several major oil companies, there can be no assurance that the Ocean Legend can be built in a cost-effective manner, that if a Victory-class rig is so upgraded, there will be adequate demand for its services, or that competitors will not achieve capability beyond that of fourth-generation semisubmersibles through other means attractive to customers.

Quality. Diamond Offshore maintains a program to continuously improve quality and safety through its Global Excellence Management System ("GEMS"), which was instituted in 1993 to increase Diamond Offshore's commitment to quality of service, safety and the environment. Diamond Offshore also seeks to capitalize on customer recognition of Diamond Offshore's quality and safety achievements. Diamond Offshore is the only drilling contractor to have won more than once (in April 1994 and April 1995) the annually awarded U.S. Minerals Management Service National Safety Award for Excellence.

RISK FACTORS

In addition to the other information contained in this Prospectus and incorporated herein by reference, prospective investors should carefully consider the matters set forth below before purchasing any of the Offered Shares.

DEPENDENCE ON OIL AND NATURAL GAS INDUSTRY; INDUSTRY CONDITIONS

Diamond Offshore's business and operations depend principally upon the condition of the oil and gas industry and, specifically, the exploration and production expenditures of oil and gas companies. Historically, the offshore contract drilling industry has been highly competitive and cyclical, with periods of high demand, short rig supply and high dayrates followed by periods of low demand, excess rig supply and low dayrates. The offshore contract drilling business is influenced by a number of factors, including the current and anticipated prices of oil and natural gas, the expenditures by oil and gas companies for exploration and production and the availability of drilling rigs. For a number of years, depressed oil and natural gas prices and an oversupply of rigs have adversely affected the offshore drilling market, particularly in the Gulf of Mexico, where the prolonged weakness and uncertainty in the demand for and price of natural gas resulted in a significant decline in exploration and production activities. Demand for drilling services outside the United States, excluding the North Sea, has been less volatile in recent years, but remains dependent on a variety of political and economic factors beyond Diamond Offshore's control, including worldwide demand for oil and natural gas, the ability of the Organization of Petroleum Exporting Countries ("OPEC") to set and maintain production levels and pricing, the level of production of non-OPEC countries and the policies of the various governments regarding exploration and development of their oil and natural gas reserves.

COMPETITION

The contract drilling industry is highly competitive. Customers often award contracts on a competitive bid basis, and although a customer selecting a rig may consider, among other things, a contractor's safety record, crew quality and quality of service and equipment, the oversupply of rigs has created an intensely competitive market in which price is the primary factor in determining the selection of a drilling contractor. Diamond Offshore believes that competition for drilling contracts will continue to be intense for the foreseeable future because of the worldwide oversupply of drilling rigs and the ability of contractors to move rigs from areas of low utilization and dayrates to areas of greater activity and relatively higher dayrates. In addition, there are inactive non-marketed rigs or rigs being operated in non-drilling activities that could be reactivated to meet an increase in demand for drilling rigs in any given market. Such movement or reactivation or a decrease in drilling activity in any major market could depress dayrates and could adversely affect utilization of Diamond Offshore's rigs. See "Business -- Offshore Contract Drilling Services."

HISTORY OF OPERATING LOSSES

Diamond Offshore reported operating income of $11.7 million for the year ended December 31, 1995, operating loss of $14.6 million for the year ended December 31, 1994, operating income of $4.5 million for the year ended December 31, 1993, operating loss of $49.2 million for the year ended December 31, 1992 and operating loss of $15.4 million for the year ended December 31, 1991. Additionally, Diamond Offshore reported net loss of $7.0 million, $34.8 million, $16.6 million, $53.4 million and $26.6 million for the years ended December 31, 1995, 1994, 1993, 1992 and 1991, respectively. Diamond Offshore had total stockholders' equity of $492.9 million as of December 31, 1995, net of an accumulated deficit of $171.4 million. Diamond Offshore's financial results in the future will depend primarily on the utilization and dayrates of the rigs operated by Diamond Offshore and the cost of such operations. Although demand for drilling services has improved recently, an oversupply of rigs has existed since the early 1980's and has led to intense price competition among drilling contractors. There can be no assurance that Diamond Offshore's operating results will improve in future periods. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Results of Operations."

AVERAGE AGE OF FLEET

The average age of the Diamond Offshore fleet of offshore drilling rigs (calculated as of December 31, 1995 and measured from year built) is 17.7 years. Many of Diamond Offshore's rigs have been upgraded during the last five years with enhancements such as top-drive drilling systems, increases to water depth capability, mud pump additions or increases in deck load capacity, and Diamond Offshore believes that it will be feasible to continue to upgrade its fleet, particularly its Victory-class semisubmersible rigs, notwithstanding the average age of its fleet. However, there can be no assurance as to if, when or to what extent upgrades will be made to rigs in Diamond Offshore's fleet. In addition, to the extent Diamond Offshore is not able to enhance its fleet with upgrade projects, Diamond Offshore will have fewer rigs available to meet customer demand for harsh environment and deep water operations than if such projects had been successfully implemented.

CONTROL BY MAJOR STOCKHOLDER AND POTENTIAL CONFLICTS OF INTEREST

Loews Corporation, a Delaware corporation ("Loews"), beneficially owns approximately 51.6% of the outstanding shares of Diamond Offshore Common Stock and is in a position to control actions that require the consent of stockholders, including the election of directors, amendment of Diamond Offshore's Restated Certificate of Incorporation and any mergers or any sale of substantially all the assets of Diamond Offshore. In connection with the initial public offering, in 1995, of Diamond Offshore Common Stock (the "Diamond Offshore Initial Public Offering"), Loews and Diamond Offshore entered into certain agreements providing for certain rights and obligations of each of them. See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and Loews."

Diamond Offshore's Board of Directors includes, and is expected to continue to include, persons who are also directors or officers of, or otherwise represent, Loews. Diamond Offshore's Board of Directors presently consists of five directors, one of whom (James S. Tisch) is also a director and the President and Chief Operating Officer of Loews, and another of whom (Herbert C. Hofmann) is a Senior Vice President of Loews. See "Management -- Security Ownership of Management and Directors." Loews (other than through Diamond Offshore) and Diamond Offshore are generally engaged in businesses sufficiently different from each other as to make conflicts as to possible corporate opportunities unlikely. It is possible, however, that Loews may in some circumstances be in direct or indirect competition with Diamond Offshore, including competition with respect to certain business strategies and transactions that Diamond Offshore may propose to undertake. In addition, potential conflicts of interest exist or could arise in the future for such directors with respect to a number of areas relating to the past and ongoing relationships of Loews and Diamond Offshore, including tax and insurance matters, financial commitments, and sales of Diamond Offshore Common Stock pursuant to registration rights or otherwise. Although the affected directors may abstain from voting on matters in which the interests of Diamond Offshore and Loews are in conflict so as to avoid potential violations of their respective fiduciary duties to stockholders of the respective corporations, the presence of potential or actual conflicts could affect the process or outcome of Board deliberations, and no policies, procedures or practices have been adopted by Diamond Offshore to reduce or avoid such conflicts. There can be no assurance that such conflicts of interest will not materially adversely affect Diamond Offshore. See "Management -- Certain Relationships and Related Transactions."

ENVIRONMENTAL MATTERS

Diamond Offshore's operations are subject to numerous federal, state and local environmental laws and regulations that relate directly or indirectly to its operations, including certain regulations controlling the discharge of materials into the environment, requiring removal and clean-up under certain circumstances, or otherwise relating to the protection of the environment. For example, Diamond Offshore may be liable for damages and costs incurred in connection with oil spills for which it is held responsible. Laws and regulations protecting the environment have become increasingly stringent in recent years and may in certain circumstances impose "strict liability" and render a company liable for environmental damage without regard to negligence or fault on the part of such company. Such laws and regulations may expose Diamond Offshore to liability for the conduct of or conditions caused by others, or for acts of Diamond Offshore that were in compliance with all applicable laws at the time such acts were performed. The application of these requirements or the adoption of new requirements could have a material adverse effect on Diamond Offshore. See "Business -- Governmental Regulation."

The United States Oil Pollution Act of 1990 ("OPA '90") and similar legislation enacted in Texas, Louisiana and other coastal states address oil spill prevention and control and significantly expand liability exposure across all segments of the oil and gas industry. OPA '90, such similar legislation and related regulations impose a variety of obligations on Diamond Offshore related to the prevention of oil spills and liability for damages resulting from such spills. OPA '90 imposes strict and with limited exceptions joint and several liability upon each responsible party for oil removal costs and a variety of public and private damages. OPA '90 also imposes ongoing financial responsibility requirements on a responsible party. A failure to comply with ongoing requirements or inadequate cooperation in a spill may subject a responsible party, including in some cases Diamond Offshore, to civil or criminal enforcement action. Also, the U.S. Minerals Management Service is required to promulgate regulations to implement the financial responsibility requirements for offshore facilities. If implemented as written, the financial responsibility requirements of OPA '90 could have the effect of significantly increasing the amount of financial responsibility that oil and gas operators must demonstrate to comply with OPA '90. While industry groups and marine insurance carriers are seeking modification of these requirements, implementation of these requirements in their current form could adversely affect the ability of some of Diamond Offshore's customers to operate in U.S. waters, which could have a material adverse effect on Diamond Offshore. See "Business -- Governmental Regulation."

OPERATIONAL HAZARDS

Diamond Offshore's operations are subject to hazards inherent in the drilling of oil and gas wells such as blowouts, reservoir damage, loss of production, loss of well control, cratering or fires, the occurrence of which could result in the suspension of drilling operations, injury to or death of rig and other personnel and damage to or destruction of Diamond Offshore's, Diamond Offshore's customer's or a third party's property or equipment. Damage to the environment could also result from Diamond Offshore's operations, particularly through oil spillage or uncontrolled fires. In addition, offshore drilling operations are subject to perils peculiar to marine operations, including capsizing, grounding, collision and loss or damage from severe weather. Diamond Offshore has insurance coverage and contractual indemnification for certain risks but there can be no assurance that such coverage or indemnification will adequately cover Diamond Offshore's loss or liability in many circumstances or that Diamond Offshore will continue to carry such insurance or receive such indemnification. See "Business -- Indemnification and Insurance."

GOVERNMENTAL REGULATION AND TAX POLICY

Diamond Offshore's operations are subject to numerous governmental laws and regulations. In addition, demand for services in the drilling industry is dependent on the oil and gas exploration industry and accordingly is affected by changes in tax and other laws relating to the energy business generally.

Significant capital expenditures may be required to comply with governmental laws and regulations applicable to Diamond Offshore and such compliance could materially adversely affect the results of operations or competitive position of Diamond Offshore. It is possible that such regulations may in the future add significantly to the cost of operating offshore drilling equipment or may significantly limit drilling activity. See "Business -- Governmental Regulation."

OPERATIONS OUTSIDE THE UNITED STATES

Operations outside the United States accounted for approximately 36.4%, 34.0% and 44.8% of Diamond Offshore's total consolidated revenues for fiscal years 1995, 1994 and 1993, respectively. Operations outside the United States accounted for approximately 47.5%, 52.3% and 63.9% of Arethusa's total consolidated revenues for fiscal years 1995, 1994 and 1993, respectively. Diamond Offshore's non-U.S. operations are subject to certain political, economic and other uncertainties not encountered in U.S. operations, including risks of war and civil disturbances (or other risks that may limit or disrupt markets), expropriation and the general hazards associated with the assertion of national sovereignty over certain areas in which operations are conducted. Diamond Offshore's operations outside the United States may face the additional risk of fluctuating currency values, hard currency shortages, controls of currency exchange and repatriation of income or capital. No prediction can be made as to what governmental regulations may be enacted in the future that could adversely affect the international drilling industry.

TURNKEY CONTRACTS

Diamond Offshore, through Diamond Offshore Turnkey Services, Inc. ("DOTS"), a Delaware corporation and a direct, wholly owned subsidiary of Diamond Offshore, selectively engages in drilling services pursuant to turnkey drilling contracts under which DOTS agrees to drill a well to a specified depth for a fixed price. Generally, DOTS is not entitled to payment unless the well is drilled to the specified depth and profitability of the contract depends upon its ability to keep expenses within the estimates used by DOTS in determining the contract price. Drilling a well under a turnkey contract therefore typically requires a cash commitment by Diamond Offshore in excess of those drilled under conventional dayrate contracts and exposes DOTS to risks of potential financial losses that generally are substantially greater than those that would ordinarily exist when drilling under a conventional dayrate contract. The financial results of a turnkey contract depend upon the performance of the drilling unit, drilling conditions and other factors, some of which are beyond the control of DOTS. See "Business -- Offshore Contract Drilling Services."

SHARES AVAILABLE FOR FUTURE SALE

Subject to the restrictions described in "Management -- Certain Relationships and Related Transactions -- Controlling Stockholder" and "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders" and applicable law, Loews is free to sell any and all of the shares of Diamond Offshore Common Stock it owns. In addition, as described in "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders," each of Alphee and Ratos is free to sell, without restriction, at its election, all or part of the shares of Diamond Offshore Common Stock received by such person in connection with the Acquisition. No prediction can be made as to the effect, if any, that future sales of Diamond Offshore Common Stock, or the availability of Diamond Offshore Common Stock for future sale, may have on the market price of the Diamond Offshore Common Stock prevailing from time to time. Sales of substantial amounts of Diamond Offshore Common Stock or the perception that such sales might occur could adversely affect prevailing market prices for the Diamond Offshore Common Stock. In connection with the Diamond Offshore Initial Public Offering, Diamond Offshore agreed that it will not offer, sell, contract to sell, pledge or otherwise dispose of, directly or indirectly, or file with the Commission a registration statement under the Securities Act relating to any additional shares of Diamond Offshore Common Stock or securities convertible into or exchangeable or exercisable for any shares of Diamond Offshore Common Stock until October 10, 1996 without the prior written consent of CS First Boston Corporation ("CS First Boston"), except grants of employee stock options pursuant to any subsequently adopted plan or issuances upon any exercise thereof. Loews agreed to similar restrictions on behalf of itself and its affiliates (other than Diamond Offshore) with respect to shares of the Diamond Offshore Common Stock. Also in connection with the Diamond Offshore Initial Public Offering, Diamond Offshore and Loews entered into an agreement that provides Loews with certain rights to have the shares of Diamond Offshore Common Stock owned by Loews registered by Diamond Offshore under the Securities Act in order to permit the public sale of such shares. See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and Loews -- Registration Rights Agreement."

USE OF PROCEEDS

Diamond Offshore will not receive any proceeds from the sale of the Offered Shares by the Selling Stockholders.

SELLING STOCKHOLDERS

All the Offered Shares being offered hereby are being offered by Alphee and/or Ratos who hold 4,708,248 shares (or approximately 6.9%) and 3,667,207 shares (or approximately 5.4%) of the Diamond Offshore Common Stock, respectively, and who, in the aggregate, hold all 8,375,455 Offered Shares, representing approximately 12.3% of the outstanding shares of Diamond Offshore Common Stock. All of the Offered Shares are being offered hereby.

Diamond Offshore, Diamond Offshore (USA), Acquisition Sub, Alphee and Ratos entered into a Shareholders Agreement, dated as of February 9, 1996, as amended (as so amended, the "Shareholders Agreement"), and therein agreed to certain provisions concerning the Fee Agreement, dated as of February 9, 1996, as amended, between Diamond Offshore and Arethusa (as so amended, the "Fee Agreement"). See "Management -- Certain Relationships and Related Transactions -- Transactions Between Diamond Offshore and the Selling Stockholders" and "-- Registration Rights of Selling Stockholders."

DIVIDEND POLICY

There were no cash dividends declared by Diamond Offshore for 1995 or 1994, except for a $2.1 million special dividend paid to Loews in connection with the Diamond Offshore Initial Public Offering. See Note 2 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein. Diamond Offshore does not anticipate that it will declare or pay any dividends on the Diamond Offshore Common Stock in the foreseeable future. Diamond Offshore expects that it will retain all earnings for the development and growth of its business. Any future determination as to payment of dividends will be made at the discretion of the Board of Directors of Diamond Offshore and will depend upon Diamond Offshore's operating results, financial condition, capital requirements, general business conditions and such other factors that the Board of Directors deems relevant. In addition, the payment of cash dividends is limited by the terms of Diamond Offshore's $150.0 million credit facility with a group of banks (the "Diamond Offshore Bank Credit Facility"). Generally, the Diamond Offshore Bank Credit Facility limits cash dividends to the then "Available Amount," as therein defined, not to exceed in the aggregate $20.0 million plus at the date of determination an amount equal to (i) 25% of cumulative consolidated net income for fiscal quarters ending after January 1, 1996 and prior to such date minus (ii) 100% of cumulative consolidated net loss for fiscal quarters ending after January 1, 1996 and prior to such date. The "Available Amount," for any date of determination, means $70.0 million plus (i) a percentage of cumulative consolidated EBITDA (as defined in the Diamond Offshore Bank Credit Facility) for fiscal quarters ending after January 1, 1996 and prior to such date, less adjustments for interest expense, provisions for taxes and certain drilling contract revenues, plus (ii) amounts attributable to certain asset sales and issuances of equity, minus (iii) amounts attributable to certain capital expenditures and investments made prior to such date, and to cash dividends theretofore paid. At February 8, 1996 (the effective date of the Diamond Offshore Bank Credit Facility), the "Available Amount" equalled $70.0 million, and Diamond Offshore would have been permitted to pay cash dividends aggregating $20.0 million at such date within the limits imposed by the Diamond Offshore Bank Credit Facility. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity" and Note 12 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

CAPITALIZATION

The following table sets forth the capitalization of Diamond Offshore as of December 31, 1995 and as adjusted as of such date after giving effect to the Acquisition. This table should be read in conjunction with the Consolidated Financial Statements (including the Notes thereto) and the Unaudited Pro Forma Consolidated Condensed Financial Statements included elsewhere in this Prospectus.

	DECEMBER 31, 1995 (UNAUDITED)	
	HISTORICAL	AS ADJUSTED
	(IN THOUSANDS)	
Total debt	$ --	$ 72,778
Stockholders' equity:		
Common stock, $.01 par value	500	679
Additional paid-in capital	665,107	1,215,605
Accumulated deficit	(171,444)	(171,444)
Cumulative translation adjustment	(1,269)	(1,269)
Total stockholders' equity	492,894	1,043,571
Total capitalization	$ 492,894	$ 1,116,349

SELECTED CONSOLIDATED FINANCIAL DATA

The following tables set forth selected consolidated historical and pro forma financial data for Diamond Offshore. The selected consolidated financial data were derived from the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements (including the Notes thereto) of Diamond Offshore included elsewhere herein. The pro forma financial data reflect certain adjustments that give effect to the Acquisition, accounted for under the purchase method of accounting, and assuming that the Diamond Offshore Initial Public Offering had occurred at January 1, 1995. Such tables should be read in conjunction with the "Unaudited Pro Forma Consolidated Condensed Financial Statements" included elsewhere herein.

	YEAR ENDED DECEMBER 31,					
	1995 PRO FORMA	1995	1994	1993	1992(1)	1991
	(IN THOUSANDS, EXCEPT PER SHARE DATA)					
INCOME STATEMENT DATA:						
Total revenues....................	$ 456,750	$336,584	$307,918	$288,069	$214,885	$64,056
Operating expenses:						
Contract drilling..............	346,092	259,560	256,919	228,211	199,201	61,928
General and administrative......	22,890	13,857	11,993	11,785	15,401	3,416
Depreciation(2).................	85,770	52,865	55,366	46,819	49,667	14,545
Gain on sale of assets..........	(1,349)	(1,349)	(1,736)	(3,201)	(231)	(414)
Operating income (loss)...........	3,347	11,651	(14,624)	4,455	(49,153)	(15,419)
Interest expense..................	(7,453)	(27,052)	(31,346)	(25,906)	(28,591)	(7,296)
Other income (expense), net.......	5,646	1,598	(455)	(219)	(207)	106
Income tax benefit (expense)(3)...	(2,503)	6,777	11,621	5,041	24,575	(4,000)
Net loss..........................	(963)	(7,026)	(34,804)	(16,629)	(53,376)	(26,609)
Pro forma net income (loss) per share...........................	(0.01)	0.20(4)	--	--	--	--

	DECEMBER 31,					
	1995 PRO FORMA	1995	1994	1993	1992(1)	1991
	(IN THOUSANDS)					
BALANCE SHEET DATA:						
Working capital(5).................	$ 85,335	$ 63,523	$ 57,521	$ 52,904	$ 35,391	$ 8,960
Drilling and other property and equipment, net..................	1,052,118	502,278	488,664	498,740	478,454	94,574
Goodwill..........................	47,167	--	--	--	--	--
Total assets......................	1,268,930	618,052	588,158	592,162	582,418	117,414
Long-term debt(6).................	62,175	--	394,777	353,483	233,216	88,254
Stockholders' equity(7)...........	1,043,571	492,894	124,066	158,361	275,300	5,550

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(1) Diamond Offshore acquired all of the common stock of Odeco Drilling Inc., a Delaware corporation ("Odeco"), for approximately $376.6 million in cash effective January 1, 1992.

(2) Effective January 1, 1993, Diamond Offshore revised the estimated useful lives for certain classes of its offshore drilling rigs. The estimated useful lives of Diamond Offshore's offshore drilling rigs, after the change in estimate, range from 10 to 25 years. As compared to the original estimate of useful lives, this change resulted in a reduction of approximately $6.3 million in depreciation expense during 1993 and a corresponding increase in operating income.

(3) Prior to the Diamond Offshore Initial Public Offering, Diamond Offshore was included in the consolidated U.S. federal income tax return of Loews. Effective January 1, 1992, Diamond Offshore adopted Statement of Financial Accounting Standards ("SFAS") No. 109 "Accounting for Income Taxes" which utilizes the liability method of accounting for income taxes. For all preceding periods,

Accounting Principles Board Opinion No. 11, the deferral method, was utilized. The cumulative effect of adoption of SFAS No. 109 on Diamond Offshore's results of operations for the year ended December 31, 1992 was not material. Prior to 1992, Diamond Offshore's profitable subsidiaries were allocated a share of the Loews consolidated tax expense and no benefit was given to any of Diamond Offshore's subsidiaries generating taxable losses. Effective January 1, 1992, a tax sharing agreement with Loews was adopted to allow for the recognition of expenses and benefits related to taxable income and losses as if Diamond Offshore filed a separate consolidated return. In conjunction with the Diamond Offshore Initial Public Offering, the tax sharing agreement was terminated and all assets and liabilities were settled by offsetting these amounts against notes payable to Loews. For taxable periods subsequent to the Diamond Offshore Initial Public Offering, Diamond Offshore will file a consolidated U.S. federal income tax return on a stand-alone basis.

(4) Pro forma net income per share gives effect to the Diamond Offshore Initial Public Offering and the after-tax effects of a reduction in interest expense. Assuming the Diamond Offshore Initial Public Offering had occurred at January 1, 1995, Diamond Offshore would have recognized net income of $10.0 million, or $0.20 per share of Diamond Offshore Common Stock, after adjusting for the after-tax effects of a reduction in interest expense. See Note 1 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

(5) Pro forma working capital includes fair values of identifiable current assets acquired and liabilities assumed, including liabilities for certain costs directly associated with the Acquisition and current maturities of long-term debt of Arethusa assumed by Diamond Offshore.

(6) Long-term debt consisted solely of notes payable to Loews for the historical periods presented.

(7) In connection with the Diamond Offshore Initial Public Offering, Diamond Offshore paid a special dividend of $2.1 million to Loews with a portion of the proceeds. No other cash dividends were paid during the historical periods presented.

UNAUDITED PRO FORMA CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

The following unaudited pro forma consolidated balance sheet has been prepared based on the historical financial statements of Diamond Offshore as of and for the year ended December 31, 1995 and of Arethusa as of and for the year ended September 30, 1995. The following unaudited pro forma consolidated condensed income statement has been prepared based on the historical financial statements of Diamond Offshore as of and for the year ended December 31, 1995 and based on pro forma income statement data for Arethusa that reflect adjustments to Arethusa's historical consolidated income statement for the year ended September 30, 1995 in connection with (i) the acquisition of the Arethusa Yatzy, (iii) the sale of the Treasure Stawinner and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of Arethusa Common Stock) as if each had occurred at the beginning of fiscal year 1995. The pro forma financial statements give effect to (i) the Acquisition, (ii) the Diamond Offshore Initial Public Offering and, in connection therewith, the use of the proceeds to repay all of Diamond Offshore's then outstanding indebtedness to Loews and to fund the payment of a special dividend to Loews and (iii) interest expense for working capital borrowings, and commitment and other fees, under the Diamond Offshore Bank Credit Facility. The Acquisition was accounted for under the purchase method of accounting using a purchase price of $560.7 million, which was calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced. The pro forma consolidated condensed balance sheet was prepared assuming such transactions were consummated on December 31, 1995 and give effect to events directly attributable to the transactions, including those that are nonrecurring. The pro forma consolidated condensed income statement was prepared assuming the transactions were consummated as of the beginning of the period presented and give effect to events directly attributable to the transactions which are expected to have a continuing impact on the combined entity. These pro forma consolidated condensed financial statements should be read in conjunction with the other financial information of Diamond Offshore and Arethusa presented elsewhere in this Prospectus. The pro forma consolidated condensed financial statements are presented for illustrative purposes only and are not necessarily indicative of actual results that would have been achieved had the transactions been consummated on such dates, and are not necessarily indicative of future results. The allocation of the purchase price is preliminary, as valuation and other studies have not been finalized. It is not expected that the final allocation of the purchase price will produce materially different results from those presented herein.

PRO FORMA CONSOLIDATED CONDENSED BALANCE SHEET

	HISTORICAL(A)			
	DIAMOND OFFSHORE	ARETHUSA	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS)			
Cash and other current assets	$ 41,278	$ 46,878	$ (21,632)(b)	$ 66,524
Accounts receivable	74,496	28,625	--	103,121
Drilling and other property and equipment, net	502,278	237,324	312,516(c)	1,052,118
Goodwill and other assets	--	2,505	44,662(d)	47,167
Total assets	$ 618,052	$ 315,332	$ 335,546	$1,268,930
Current liabilities	$ 52,251	$ 28,559	$ 3,500(e)	$ 84,310
Long-term debt	--	62,175	--	62,175
Deferred credits and other liabilities	72,907	2,019	3,948(f)	78,874
Common stock	500	2,033	(1,854)(g)	679
Additional paid-in capital	665,107	218,800	331,698(g)	1,215,605
Accumulated earnings (deficit)	(171,444)	132	(132)	(171,444)
Unrealized gain on equity securities	--	1,614	(1,614)	--
Cumulative translation adjustment	(1,269)	--	--	(1,269)
Total liabilities and stockholders' equity	$ 618,052	$ 315,332	$ 335,546	$1,268,930

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(a) There are no significant adjustments required to the historical financial statements of Diamond Offshore or Arethusa to conform accounting policies of the two companies.

(b) Adjustment for fair values of identifiable current assets acquired and for certain events directly attributable to the transaction. Such items include:

Severance, consulting, and salary continuation plans	$ (5,526)(1)
Arethusa dividend	(5,083)(2)
Financial advisory services	(7,500)(3)
Legal, accounting, and other	(2,500)(4)
Office lease cancellation	(1,023)(5)
	$(21,632)

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(1) Under the Plan of Acquisition, from and after the Effective Time, Diamond Offshore and Arethusa and their respective subsidiaries will honor in accordance with their terms certain Arethusa employment, severance, consulting and salary continuation plans. See "Business -- The Acquisition -- Continuing Arethusa Severance, Consulting and Salary Continuation Plans."

(2) On March 15, 1996, in anticipation of the Acquisition, and as expressly permitted by the Plan of Acquisition, Arethusa paid a dividend of $0.25 per share of Arethusa Common Stock.

(3) Arethusa has agreed to pay Merrill Lynch a fee of $7.5 million for financial advisory services in connection with the Acquisition upon the closing of the Acquisition.

(4) Adjustment for legal, accounting, printing and other nonrecurring charges expected to be incurred in connection with the Acquisition.

(5) Arethusa is committed under a lease agreement for office space that continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1.0 million. Such payment has no future economic benefit to the combined company and is incremental to other costs incurred by either Arethusa or Diamond Offshore in the conduct of activities prior to the Effective Time.

(c) Adjustment for fair values, based on current appraisals, of the eight semisubmersible drilling rigs, three jack-up drilling rigs, and other property and equipment owned by Arethusa.

(d) Adjustment for fair values of identifiable assets and for the excess of the cost of Arethusa over the sum of the amounts assigned to identifiable assets acquired less liabilities assumed.

(e) Adjustment for the estimated unfunded termination liability related to the Arethusa defined benefit plan.

(f) Adjustment for fair values of liabilities assumed and for the deferred tax liability for estimated future tax effects of differences between the tax bases and the fair value amounts assigned to identifiable assets and liabilities of Arethusa, offset by net operating loss carryforwards of Arethusa of approximately $30.0 million. As a result of the Acquisition, Diamond Offshore will have available to it certain Arethusa net operating loss carryforwards to reduce future U.S. federal income taxes payable. Due to the change in ownership of Arethusa resulting from the Acquisition, there will be annual limitations on the amount of Arethusa tax carryforwards available to be utilized by Diamond Offshore.

(g) The pro forma financial statements reflect the purchase of 100% of the outstanding shares of Arethusa Common Stock for a total consideration of $560.7 million which is comprised of the following:

Diamond Offshore Common Stock to be issued	$539,296(1)
Options assumed	11,381(2)
Total equity consideration	550,677
Transaction costs	10,000(3)
Total consideration	$560,677

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(1) The value of the Diamond Offshore Common Stock to be issued in the Acquisition is calculated based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995) of $30.14.

(2) Amount represents the fair value of the Arethusa Options to be assumed by Diamond Offshore pursuant to the Amalgamation Agreement. The fair value is based on a seven-day average of the closing price of Diamond Offshore Common Stock at the time the Acquisition was announced (December 7, 1995), the Amalgamation Ratio and the option exercise price including the $3.00 reduction, which is subject to shareholder approval at the Arethusa Annual Meeting. See "Other Arethusa Annual Meeting Matters -- Decrease of Option Exercise Price."

(3) Amounts represent transaction costs directly associated with the Acquisition. See (b) above.

PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT

	HISTORICAL DIAMOND OFFSHORE	PRO FORMA ARETHUSA(A)	ADJUSTMENTS	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
Revenues	$336,584	$ 120,166	$ --	$ 456,750
Operating expenses:				
Contract drilling	259,560	86,532	--	346,092
General and administrative	13,857	9,033	--	22,890
Depreciation and amortization	52,865	29,008	3,897(b)	85,770
Gain on sale of assets	(1,349)	--	--	(1,349)
Total operating expenses	324,933	124,573	3,897	453,403
Operating income (loss)	11,651	(4,407)	(3,897)	3,347
Other income (expense):				
Interest expense	(27,052)	(6,697)	26,296(c)	(7,453)
Other, net	1,598	4,048	--	5,646
Income (loss) before income tax benefit (expense)	(13,803)	(7,056)	22,399	1,540
Income tax benefit (expense)	6,777	(1,440)	(7,840)(d)	(2,503)
Net income (loss)	$ (7,026)	$ (8,496)	$ 14,559	$ (963)
Net income per common share	$ 0.20(f)	$ (0.42)		$ (0.01)
Weighted average common shares outstanding	50,000(f)	20,333		67,893(e)

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(a) Pro forma income statement data for Arethusa reflect (i) the acquisition of the Arethusa Yatzy, which occurred on May 3, 1995, (ii) the sale of the Treasure Stawinner, which occurred June 30, 1995, and (iii) the dividend and capital distribution of $61.0 million ($3.00 per share of Arethusa Common Stock) as if each had occurred at the beginning of fiscal year 1995. Set forth below in this footnote (a) are the historical amounts, and the adjustments thereto, upon which the pro forma Arethusa amounts are based.

ARETHUSA PRO FORMA CONSOLIDATED CONDENSED INCOME STATEMENT

	HISTORICAL		ADJUSTMENTS			
	ARETHUSA	YATZY(1)	YATZY ACQUISITION	STAWINNER SALE	DIVIDEND/ CAPITAL DISTRIBUTION	PRO FORMA
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)					
Contract drilling revenue.........	$122,147	$12,315	$ --	$(14,296)(6)	$ --	$120,166
Operating expenses:						
Direct costs....................	87,953	8,060	(623)(5) (375)(2)	(8,483)(6)	--	86,532
General and administrative......	8,658	--	375(2)	--	--	9,033
Depreciation....................	29,547	--	1,352(3)	(1,891)(6)	--	29,008
Total operating expenses..............	126,158	8,060	729	(10,374)	--	124,573
Operating income (loss)...........	(4,011)	4,255	(729)	(3,922)	--	(4,407)
Other income (expense):						
Interest expense................	(6,311)	--	(1,168)(4)	782(6)	--	(6,697)
Interest income.................	5,692	--	--		(1,453)(7)	4,239
Gain (loss) on sale of assets...	27,820	--	--	(27,885)(6)	--	(65)
Other, net......................	(126)	--	--	--	--	(126)
Income (loss) before income taxes...........................	23,064	4,255	(1,897)	(31,025)	(1,453)	(7,056)
Tax provision.....................	(1,440)	--	--	--	--	(1,440)
Net income (loss).................	$ 21,624	$ 4,255	$(1,897)	$(31,025)	$(1,453)	$ (8,496)
Net income (loss) per common share...........................	$ 1.06					$ (0.42)
Weighted average common shares outstanding.....................	20,333					20,333

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(1) The historical financial information of the Yatzy operations for the period from October 1, 1994, through May 2, 1995 is based upon Arethusa records, as manager of the rig. The previous owner of the rig prepared financial information only on a semi-annual, calendar year basis; and was unable to provide the complete financial information for the twelve months ended September 30, 1995. Financial statement captions for which Yatzy historical information is not presented (historical depreciation and interest expense) would have been adjusted to reflect Arethusa's cost basis in the Arethusa Yatzy and Arethusa's financing of the rig. Pro forma Yatzy acquisition adjustments (3) and (4) discussed below provide fully for depreciation using Arethusa's cost basis in the Arethusa Yatzy and interest based on Arethusa's financing of the rig. Additionally, it is management's understanding that there are no other significant transactions or activities related to the historical operations of Yatzy which would have a material impact on the as-adjusted pro forma income statement. Therefore, management believes the resulting pro forma income statement is in compliance with Article 11 of Regulation S-X.

(2) To reclassify and eliminate the management fee paid to Arethusa from direct costs to general and administrative expenses.

(3) To reflect depreciation expense calculated based upon Arethusa's cost and estimated useful life of 25 years, which is consistent with Arethusa's previously established depreciation policy.

(4) To adjust for additional interest expense associated with Arethusa's $30.0 million note entered into in connection with the acquisition of the Arethusa Yatzy.

(5) To adjust for a reduction in insurance expense resulting from Arethusa's lower insured value for the Arethusa Yatzy.

(6) To reflect the elimination of historical operations, interest expense and gain on sale of assets for the Treasure Stawinner.

(7) To reflect the reduction in interest income resulting from the dividend and capital distribution made to shareholders in fiscal 1995.

(b) To record the additional depreciation expense and amortization of goodwill resulting from the allocation of the purchase price. The pro forma adjustment assumes an 18-year average estimated useful life for depreciation and a 20-year amortization period for goodwill.

(c) To adjust interest expense, assuming that the Diamond Offshore Initial Public Offering and repayment of indebtedness occurred on January 1, 1995.

(d) To record income tax expense on the effect of the pro forma adjustments to depreciation and amortization and interest expense.

(e) Weighted average shares outstanding as if both the October 1995 issuance of 15.0 million shares by Diamond Offshore through the Diamond Offshore Initial Public Offering and the 17.9 million shares to be issued by Diamond Offshore in consideration of the Arethusa Common Stock had taken place on January 1, 1995.

(f) After the Diamond Offshore Initial Public Offering, Diamond Offshore had 50.0 million shares of Diamond Offshore Common Stock outstanding. Assuming the Diamond Offshore Initial Public Offering had occurred at January 1, 1995, Diamond Offshore would have recognized net income of $10.0 million, or $0.20 per share of Diamond Offshore Common Stock, after adjusting for the after-tax effects of a reduction in interest expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with Diamond Offshore's Consolidated Financial Statements (including the notes thereto) included elsewhere herein.

RESULTS OF OPERATIONS

GENERAL

REVENUES. Diamond Offshore's revenues vary based upon demand, which affects the number of days the fleet is utilized and the dayrates received. Revenues can also increase or decrease as a result of the acquisition or disposal of rigs. In order to improve utilization or realize higher dayrates, Diamond Offshore may mobilize its rigs from one market to another. During periods of mobilization, however, revenues are generally adversely affected. As a response to changes in demand, Diamond Offshore may withdraw a rig from the market by stacking it or may reactivate a rig which was previously stacked, which may decrease or increase revenues, respectively.

Revenues from dayrate drilling contracts are recognized currently. When mobilization or enhancement is required for a contract, Diamond Offshore may receive a lump-sum payment to offset a portion of the cost of such requirements. Mobilization revenues less costs incurred to mobilize an offshore rig from one market to another are usually recognized over the term of the related drilling contract. In addition, payments received for rig enhancements are recognized as revenues over the term of the related drilling contract. Revenues from offshore turnkey contracts are recognized on the completed contract method, with revenues accrued to the extent of turnkey costs until the specified turnkey depth and other contract requirements are met.

OPERATING INCOME (LOSS). Operating income (loss) is primarily affected by revenue factors, but is also a function of varying levels of operating expenses. Operating expenses are not affected by changes in dayrates, nor are they necessarily significantly affected by fluctuations in utilization. For instance, if a rig is to be idle for a short period of time, Diamond Offshore realizes few decreases in operating expenses since the rig is typically maintained in a prepared state with a full crew. However, if the rig is to be idle for an extended period of time, Diamond Offshore may reduce the size of a rig's crew and take steps to "cold stack" the rig, which lowers expenses and partially offsets the impact on operating income associated with loss of revenues. Diamond Offshore recognizes as an operating expense maintenance activities such as painting, inspections and routine overhauls that maintain rather than upgrade its rigs. These expenses vary from period to period. Costs of rig enhancements are capitalized and depreciated over the expected useful lives of the enhancements. Depreciation expense decreases operating income in periods subsequent to capital upgrades. From time to time, Diamond Offshore sells assets in the ordinary course of its business and gains or losses associated with such sales are included in operating income (loss).

YEARS ENDED DECEMBER 31, 1995 AND 1994

Comparative data relating to Diamond Offshore's revenues and operating expenses by equipment type are listed below (eliminations offset dayrate revenues earned when Diamond Offshore's rigs are utilized in its turnkey operations). Diamond Offshore's drillship, Ocean Clipper I, is included in Other Semisubmersibles for discussion purposes.

	YEAR ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, 1994	INCREASE/ (DECREASE)
	(IN THOUSANDS)		
REVENUES			
Fourth-Generation Semisubmersibles	$ 67,393	$ 46,862	$ 20,531
Other Semisubmersibles	168,582	134,302	34,280
Jack-ups	68,829	89,883	(21,054)
Turnkey	27,121	25,296	1,825
Land	19,926	21,443	(1,517)
Other	4	11	(7)
Eliminations	(15,271)	(9,879)	(5,392)
Total Revenues	$336,584	$307,918	$ 28,666
CONTRACT DRILLING EXPENSE			
Fourth-Generation Semisubmersibles	$ 34,717	$ 30,207	$ 4,510
Other Semisubmersibles	129,795	124,090	5,705
Jack-ups	60,798	66,723	(5,925)
Turnkey	30,297	25,957	4,340
Land	17,899	18,240	(341)
Other	1,325	1,581	(256)
Eliminations	(15,271)	(9,879)	(5,392)
Total Contract Drilling Expense	$259,560	$256,919	$ 2,641
OPERATING INCOME (LOSS)			
Fourth-Generation Semisubmersibles	$ 32,676	$ 16,655	$ 16,021
Other Semisubmersibles	38,787	10,212	28,575
Jack-ups	8,031	23,160	(15,129)
Turnkey	(3,176)	(661)	(2,515)
Land	2,027	3,203	(1,176)
Other	(1,321)	(1,570)	249
General and Administrative Expense	(13,857)	(11,993)	(1,864)
Depreciation Expense	(52,865)	(55,366)	2,501
Gain on Sale of Assets	1,349	1,736	(387)
Total Operating Income (Loss)	$ 11,651	$(14,624)	$ 26,275

REVENUES. The $20.5 million increase in revenues from fourth-generation semisubmersibles resulted primarily from increases in dayrates in the North Sea and the Gulf of Mexico. In addition, $3.9 million in revenue for rig enhancements and mobilization fees in excess of mobilization costs was recognized during 1995. These increases were partially offset by a reduction of revenues resulting from the mobilization between markets of two fourth-generation rigs during the first quarter of 1995. The $34.3 million increase in revenues from other semisubmersibles is primarily attributable to increases in dayrates and utilization in both the North Sea and the Gulf of Mexico. In the North Sea, increases in utilization resulted in approximately $13.5 million of additional revenues and increases in dayrates resulted in approximately $4.2 million of additional revenues. In the Gulf of Mexico, increases in utilization resulted in approximately $12.6 million of additional revenues and increases in dayrates resulted in approximately $6.6 million of additional revenues. In addition, the operations of two of three rigs acquired during the second and third quarters of 1994 contributed a $6.0 million increase in other semisubmersible revenue. Also, revenues for rig enhancements of $2.5 million were recognized during 1995. These increases were partially offset by a reduction of revenues resulting from the mobilization between markets of three other semisubmersibles: the Ocean Nomad from South America to the North Sea, the Ocean Princess from Southeast Asia to the North Sea, and the Ocean Baroness from Trinidad to Brazil. The $21.1 million decrease in revenues from jack-ups resulted primarily from lower dayrates as compared to 1994 and a decline in utilization. The decline in utilization in the Gulf of Mexico caused a $5.8 million reduction in revenues, primarily from cold stacking two rigs located in the Gulf of Mexico in mid-1995, both of which were utilized during the prior year. Partially offsetting these decreases was an increase in utilization for two jack-ups which were moved from Venezuela to the Gulf of Mexico during the first half of 1994. Decreases in dayrates in the Gulf of Mexico caused a $14.0 million reduction in revenues for jack-ups. The $1.8 million increase in turnkey revenues resulted from an increase in the number of turnkey wells drilled. Eleven turnkey wells were drilled during the year ended December 31, 1995 as compared to nine wells drilled during the prior year. The $1.5 million decrease in land revenues resulted primarily from a decline in utilization as compared to 1994.

CONTRACT DRILLING EXPENSE. The $4.5 million increase in contract drilling expense for fourth-generation semisubmersibles resulted from improved utilization of the two rigs located in the Gulf of Mexico and increased expenses for the mobilization of two rigs during the first quarter of 1995 to relocate the rigs between the Gulf of Mexico and the North Sea. The $5.7 million increase in contract drilling expense for other semisubmersibles resulted primarily from additional operating costs of $9.4 million associated with the three rigs acquired in 1994, including mobilization costs of $4.0 million. In addition, improved utilization for a rig operating in the North Sea resulted in a $2.3 million increase in operating costs. These increases were partially offset by cost reductions of $5.7 million from the cold stacking of two rigs located in the Gulf of Mexico. One of these semisubmersibles, the Ocean Prospector, was cold stacked in the first quarter and reactivated during the fourth quarter of 1995. The other rig, the Ocean Quest, was cold stacked in the third quarter of 1994 and is currently undergoing significant rig enhancements in preparation for a three-year term contract anticipated to begin in the fourth quarter of 1996. The $5.9 million decrease in contract drilling expense for jack-ups resulted primarily from cost reductions associated with the cold stacking of two rigs in the Gulf of Mexico. The $4.3 million increase in turnkey expense resulted primarily from the increase in the number of turnkey wells drilled and cost overruns on one turnkey well in progress at December 31, 1995, for which an estimated loss of $3.6 million has been recorded.

GENERAL AND ADMINISTRATIVE EXPENSE. General and administrative expense increased $1.9 million in 1995 due to increases in staff and other administrative expenses and the commencement in 1995 of the Diamond Offshore Management Bonus Program, an incentive plan for cash bonuses to selected officers and key employees of Diamond Offshore.

DEPRECIATION EXPENSE. Depreciation expense of $52.9 million for 1995 included a $2.1 million write-down in the carrying value of a semisubmersible, as compared to a $5.5 million write-down on another semisubmersible included in depreciation expense for 1994. Partially offsetting this decrease was an additional $1.2 million of depreciation expense associated with the three rigs acquired during the second and third quarters of 1994.

GAIN ON SALE OF ASSETS. Gain on sale of assets for the year ended December 31, 1995 of $1.3 million resulted from the sale of a semisubmersible which was held for disposition and from sales of miscellaneous assets. Gain on sale of assets for the year ended December 31, 1994 of $1.7 million primarily resulted from the sale of eight land drilling rigs.

INTEREST EXPENSE. Interest expense for the year ended December 31, 1995 decreased $4.2 million to $27.1 million as compared to $31.3 million for the prior year. This decrease resulted from the payment of all of Diamond Offshore's outstanding indebtedness to Loews in connection with the Diamond Offshore Initial Public Offering.

FOREIGN CURRENCY TRANSACTION LOSSES. Foreign currency transaction losses of $.2 million for 1995 decreased $1.1 million from $1.3 million for 1994. This decrease is primarily due to a loss of $.7 million recognized in 1994 for the accumulated translation adjustment upon discontinuance of operations in Venezuela. See "-- Other."

OTHER INCOME (EXPENSE). Other income increased $.9 million to $1.8 million as compared to $.9 million for 1994. This increase is primarily attributable to additional interest income resulting from an increase in average cash balances during 1995.

INCOME TAX BENEFIT. The income tax benefit for the year ended December 31, 1995 decreased $4.8 million to $6.8 million, as compared to $11.6 million for 1994. This decrease resulted primarily from a decrease in Diamond Offshore's net loss before taxes of $32.6 million, as compared to 1994. See Note 8 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

NET LOSS. Net loss for 1995 decreased $27.8 million to $7.0 million, as compared to $34.8 million for 1994. The decrease resulted primarily from an increase in operating income of $26.3 million.

YEARS ENDED DECEMBER 31, 1994 AND 1993

Comparative data relating to Diamond Offshore's revenues and operating expenses by equipment type are listed below (eliminations offset dayrate revenues earned when Diamond Offshore's rigs are utilized in its turnkey operations). Diamond Offshore's drillship, Ocean Clipper I, is included in Other Semisubmersibles for discussion purposes.

	YEAR ENDED DECEMBER 31,		INCREASE/
	1994	1993	(DECREASE)
	(IN THOUSANDS)		
REVENUES			
Fourth-Generation Semisubmersibles	$ 46,862	$ 36,791	$ 10,071
Other Semisubmersibles	134,302	125,979	8,323
Jack-ups	89,883	94,137	(4,254)
Turnkey	25,296	18,038	7,258
Land	21,443	17,770	3,673
Other	11	934	(923)
Eliminations	(9,879)	(5,580)	(4,299)
Total Revenues	$307,918	$288,069	$ 19,849
CONTRACT DRILLING EXPENSE			
Fourth-Generation Semisubmersibles	$ 30,207	$ 25,090	$ 5,117
Other Semisubmersibles	124,090	114,434	9,656
Jack-ups	66,723	61,530	5,193
Turnkey	25,957	16,416	9,541
Land	18,240	15,503	2,737
Other	1,581	818	763
Eliminations	(9,879)	(5,580)	(4,299)
Total Contract Drilling Expense	$256,919	$228,211	$ 28,708
OPERATING INCOME (LOSS)			
Fourth-Generation Semisubmersibles	$ 16,655	$ 11,701	$ 4,954
Other Semisubmersibles	10,212	11,545	(1,333)
Jack-ups	23,160	32,607	(9,447)
Turnkey	(661)	1,622	(2,283)
Land	3,203	2,267	936
Other	(1,570)	116	(1,686)
General and Administrative Expense	(11,993)	(11,785)	(208)
Depreciation Expense	(55,366)	(46,819)	(8,547)
Gain on Sale of Assets	1,736	3,201	(1,465)
Total Operating Income (Loss)	$(14,624)	$ 4,455	$(19,079)

REVENUES. The $10.1 million increase in revenues from fourth-generation semisubmersibles resulted primarily from a $17.8 million increase in revenues from the two rigs located in the Gulf of Mexico during the year ended December 31, 1994, offset by a $7.7 million decrease in revenues from reduced utilization of the rig in the North Sea. The $8.3 million increase in revenues from other semisubmersibles resulted primarily from the operations of two of the three rigs acquired during the second and third quarters of 1994. The $4.3 million decrease in revenues from jack-ups resulted primarily from two rigs that were idle during the first half of 1994. During this period, the rigs were mobilized from Venezuela and refitted for operation in the Gulf of Mexico. The $7.3 million increase in turnkey revenues resulted from an increase in the number of turnkey wells drilled. Nine turnkey wells were drilled during the year ended December 31, 1994 as compared to four wells drilled during the prior year.

CONTRACT DRILLING EXPENSE. The $5.1 million increase in contract drilling expense for fourth-generation semisubmersibles resulted from improved utilization of the two rigs located in the Gulf of Mexico which was partially offset by reduced utilization for the rig located in the North Sea. The $9.7 million increase in contract drilling expense for other semisubmersibles resulted primarily from operating costs of $8.3 million associated with the three rigs acquired during the second and third quarters of 1994 and from an increase in mobilization costs of $2.2 million. These increases were partially offset by cost reductions of $3.7 million from the cold stacking, upon expiration of a term contract, of a rig in South America during the fourth quarter of 1994. The $5.2 million increase in contract drilling expense for jack-ups resulted primarily from increased costs incurred for the mobilization and shipyard maintenance of two rigs moved from Venezuela to the Gulf of Mexico during the first half of 1994. The $9.5 million increase in turnkey expense resulted from the additional number of wells drilled. In addition, cost overruns on one turnkey well resulted in additional expense, beyond that anticipated, of $2.3 million during the year ended December 31, 1994. The $2.7 million increase in contract drilling expense for land drilling operations resulted primarily from an increase in the number of land turnkey wells drilled during the year ended December 31, 1994 as compared to the prior year.

GENERAL AND ADMINISTRATIVE EXPENSE. General and administrative expense of $12.0 million for the year ended December 31, 1994 was relatively unchanged from the $11.8 million incurred during the prior year.

DEPRECIATION EXPENSE. Depreciation expense increased $8.5 million over the prior year, primarily as a result of Diamond Offshore's decision to decrease the carrying value of one of its other semisubmersible rigs by $5.5 million. In addition, depreciation expense increased $1.2 million associated with the acquisition of three rigs in the second and third quarters of 1994 and $1.1 million from the full year recognition of depreciation expense in 1994 associated with the acquisition of the remaining interest in a fourth-generation semisubmersible in March 1993.

GAIN ON SALE OF ASSETS. Gain on sale of assets for the year ended December 31, 1994 of $1.7 million primarily resulted from the sale of eight land drilling rigs. Gain on sale of assets for the year ended December 31, 1993 of $3.2 million primarily resulted from the sale of Diamond Offshore's three platform rigs.

INTEREST EXPENSE. Interest expense for the year ended December 31, 1994 increased $5.4 million to $31.3 million as compared to $25.9 million for the prior year. Interest expense consisted only of interest on notes payable to Loews. During 1994, notes payable to Loews increased $41.3 million due to $25.0 million of additional borrowings to finance the acquisition of three semisubmersibles purchased during the second and third quarters of 1994 and due to $31.3 million for interest accrued on notes payable to Loews.

FOREIGN CURRENCY TRANSACTION LOSSES. Foreign currency transaction losses of $1.3 million for the year ended December 31, 1994 were relatively unchanged from $1.5 million for the prior year.

OTHER INCOME (EXPENSE). Other income of $.9 million for the year ended December 31, 1994 was relatively unchanged from $1.3 million for the prior year.

INCOME TAX BENEFIT. The income tax benefit for the year ended December 31, 1994 increased $6.6 million to $11.6 million, as compared to $5.0 million for the prior year. This increase resulted primarily from the increase in Diamond Offshore's net loss before taxes from $21.7 million for the year ended December 31, 1993 to $46.4 million for the year ended December 31, 1994.

NET LOSS. Net loss for the year ended December 31, 1994 increased $18.2 million to $34.8 million, as compared to $16.6 million for the prior year. The increase resulted primarily from a decrease of $19.1 million in operating income and an increase of $5.4 million in interest expense. The increase in net loss was partially offset by an increase of $6.6 million in income tax benefit, as compared to the prior year.

OUTLOOK

The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances, including 3-D seismic, horizontal drilling, and subsea completion procedures. Both the Gulf of Mexico and the North Sea semisubmersible markets have experienced increased utilization and significantly higher dayrates in 1995 and 1996, and customers increasingly are seeking to contract rigs serving those markets under term contracts (as opposed to contracts let on a single well or well-to-well basis). In the Gulf of Mexico, the Ocean Valiant's contract has been extended through 1996 at an increased dayrate. Contracts for Diamond Offshore's other semisubmersibles in the Gulf of Mexico continue to be primarily on a well-to-well or multi-well basis. However, one rig has received a contract extension on a long-term basis through January 1998. Diamond Offshore's drillship, the Ocean Clipper I, is scheduled to be upgraded during 1996 and 1997 to operate in the ultra-deep water market of the Gulf of Mexico with dynamic positioning capabilities and other features, in connection with a four-year term contract with a major oil company that has been agreed to in principle. Also, as part of this trend, Diamond Offshore entered into a contract and a letter of intent with two major oil companies for the Ocean Quest and Ocean Star (formerly named Ocean Countess), respectively, to conduct deep water drilling operations in the Gulf of Mexico under three-year term contracts, in connection with which Diamond Offshore will significantly enhance these rigs. See "-- Capital Resources."

In the North Sea, the Ocean Alliance is contracted for work through late 1996 and has received an increase in its dayrate. Diamond Offshore's three other marketed semisubmersibles in the North Sea are all committed under long-term contracts. The Ocean Nomad, which was relocated from South America, began its two-year contract in late November 1995. The Ocean Princess has completed the modifications necessary for its two-year contract which commenced in late March 1996. The Ocean Guardian is currently drilling pursuant to a one-year term contract expiring during the third quarter of 1996. Of the remaining semisubmersibles in Diamond Offshore's fleet, the Ocean Baroness has a three-year term contract for drilling offshore Brazil through the first quarter of 1999. In addition, the Arethusa Yatzy and Ocean Zephyr, also operating offshore Brazil, are contracted to November 1998 and July 1997, respectively.

The market for jack-up rigs in the Gulf of Mexico, which weakened during 1994, appears to have stabilized and has shown some signs of strengthening in recent months. Dayrates have improved from those earned in early 1995; however, volatile natural gas prices and an oversupply of rigs prevented significant improvements through the end of 1995. Two of Diamond Offshore's jack-up rigs are committed through the first quarter of 1997, one drilling offshore Indonesia and the other in the Dutch sector of the North Sea.

Historically, the offshore contract drilling market has been highly competitive and cyclical, and Diamond Offshore cannot predict the extent to which current conditions will continue.

LIQUIDITY

Net cash provided by operating activities for the year ended December 31, 1995 increased by $10.2 million to $52.8 million, as compared to $42.6 million for the prior year. This increase was attributable to a $27.8 million decrease in net loss from 1994, partially offset by an increase of $16.7 million in accounts receivable in 1995, as compared to a decrease in accounts receivable of $4.5 million for the prior year. Cash used in investing activities increased $21.7 million primarily due to construction work in progress of $19.0 million for rig upgrades in 1995. Cash provided by financing activities for 1995 decreased due to repayment of Diamond Offshore's notes payable to Loews in conjunction with the Diamond Offshore Initial Public Offering.

Diamond Offshore's principal sources of funds have been cash flow from operations and borrowings on notes payable to Loews. Upon completion of the Diamond Offshore Initial Public Offering, Diamond Offshore used a portion of the net proceeds to repay such notes in full. The remainder of the proceeds was used to pay Loews a special dividend of $2.1 million. See Note 2 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

Diamond Offshore uses funds available under the Diamond Offshore Bank Credit Facility, together with cash flow from operations, to fund its capital expenditure and working capital requirements. The Diamond Offshore Bank Credit Facility is a revolving line of credit for a five-year term providing a maximum credit commitment of $150.0 million until the second anniversary, at which time and at the end of each six-month period thereafter, the commitment will decrease by $12.5 million to a final maximum credit commitment of $75.0 million during the last six months. Borrowings will bear interest, at Diamond Offshore's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. Diamond Offshore is required to pay a commitment fee of .375% on the unused available portion of the maximum credit commitment. Borrowings are secured by a first priority security interest in five semisubmersible drilling rigs, including Diamond Offshore's three fourth-generation rigs, a pledge of 65% of the capital stock of Diamond Offshore Limited, which owns the Ocean Alliance, and certain subsidiary guarantees. Under the Diamond Offshore Bank Credit Facility, Diamond Offshore is required to maintain a ratio of consolidated EBITDA (as defined) to consolidated interest expense of at least 2.50:1.00 and a ratio of consolidated indebtedness (including borrowings under such facility) to total capitalization (equal to the sum of such indebtedness plus consolidated net worth) of no more than 0.40:1.00. Diamond Offshore is also required to maintain a positive working capital balance. In addition, the agreement has covenants that limit aggregate capital expenditures, dividends and similar payments. See "Dividend Policy."

It is anticipated that the Diamond Offshore Bank Credit Facility will be used primarily to fund rig upgrades and similar capital expenditure requirements. In management's opinion, Diamond Offshore's cash generated from operations and borrowings available under the Diamond Offshore Bank Credit Facility are sufficient to meet its anticipated short and long-term liquidity needs, including its capital expenditure and debt service requirements.

CAPITAL RESOURCES

Cash requirements for capital commitments result from rig upgrades to meet specific customer requirements and from Diamond Offshore's continuing rig enhancement program, including top-drive drilling system installations and water depth and drilling capability upgrades. Diamond Offshore expects to spend approximately $208.1 million, including interest expense to be capitalized, during 1996 for significant rig upgrades in connection with contract requirements. Included in this amount is approximately $55.8 million for 1996 expenditures in conjunction with the scheduled upgrade of the Ocean Clipper I to operate in ultra-deep water with dynamic positioning capabilities and other features. In addition, approximately $124.7 million is included for the upgrades relating to the letter of intent and the contract for the Ocean Star (formerly named Ocean Countess) and Ocean Quest, respectively. Also included in this amount is approximately $10.0 million to upgrade the Arethusa Neptune to work in 3,000 feet of water. Because these projects are expected to be accompanied by term contracts at favorable dayrates, the expenditures are, in Diamond Offshore's opinion, financially justified. Diamond Offshore expects to evaluate other projects as opportunities arise. In addition, Diamond Offshore has budgeted $47.4 million for 1996 capital expenditures associated with its continuing rig enhancement program. It is management's opinion that significant improvements in operating cash flow resulting from current conditions of improved dayrates and the increasing number of term contracts for rigs in certain markets, in conjunction with borrowings under the Diamond Offshore Bank Credit Facility, will be sufficient to meet these capital requirements.

In connection with the Acquisition, Diamond Offshore assumed Arethusa's obligations with respect to approximately $69.2 million of secured indebtedness at December 31, 1995, which was outstanding under two separate facilities. In December 1994 Arethusa refinanced its then existing secured debt of $66.1 million with a new $80.0 million loan facility. See Note 6 to Arethusa's Consolidated Financial Statements included elsewhere herein. This loan facility was subsequently paid down by $38.9 million to $41.1 million at December 31, 1995. Currently, quarterly payments on this facility total $6.8 million per annum with a

December 1999 balloon payment of $15.4 million. Additionally, in connection with the acquisition of the Arethusa Yatzy (see Notes 4 and 6 to Arethusa's Consolidated Financial Statements included elsewhere herein), Arethusa drew upon a $30.0 million loan facility. Semi-annual payments totaling $3.8 million per annum are due under this facility, which brings total current maturities under these facilities to $10.6 million as of December 31, 1995. In management's view, cash generated from operations and borrowings available under the Diamond Offshore Bank Credit Facility will be sufficient to meet Diamond Offshore's debt service obligations under these facilities.

Diamond Offshore is analyzing financing alternatives that may be available to it in the public or private capital markets. Proceeds of any such financing transactions may be used for repayment of higher cost debt, to fund rig upgrades or acquisitions or for other corporate purposes. Diamond Offshore's ability to effect any such financings will be dependent on its historical results of operations and its current financial condition and prospects at the time it seeks access to the capital markets, and to other factors beyond Diamond Offshore's control, including the prevailing interest rate environment and, with respect to offerings of common or preferred stock or debt obligations convertible into such common stock, other financial market conditions, and the investment community's perception of Diamond Offshore and the offshore contract drilling industry generally. Any such offering would be subject to the restrictions imposed by the Shareholders Agreement on public sales or distributions of Diamond Offshore Common Stock, or securities convertible into common stock, and until October 10, 1996, to obtaining the prior written consent of CS First Boston as required by the underwriting agreement entered into in connection with the Diamond Offshore Initial Public Offering.

Also, from time to time Diamond Offshore reviews acquisition opportunities such as that presented by Arethusa, although Diamond Offshore has no current plans to purchase or otherwise acquire additional rigs.

OTHER

Certain of Diamond Offshore's subsidiaries use the local currency in the country where they conduct operations as their functional currency. Currency environments in which Diamond Offshore has material business operations include the United Kingdom, Australia and Brazil. Diamond Offshore generally attempts to minimize its currency exchange risk by seeking international contracts payable in local currency in amounts equal to Diamond Offshore's estimated operating costs payable in local currency and in U.S. dollars for the balance of the contract. Because of this strategy, Diamond Offshore in the past has minimized its unhedged net asset or liability positions denominated in local currencies and has not experienced significant gains or losses associated with changes in currency exchange rates. However, at present contracts covering three of Diamond Offshore's four rigs operating in the United Kingdom sector of the North Sea are payable in U.S. dollars. Diamond Offshore has not hedged its exposure to changes in the exchange rate between U.S. dollars and pounds sterling for operating costs payable in pounds sterling, although it may seek to do so in the future.

Currency translation adjustments are accumulated in a separate section of stockholders' equity. However, when Diamond Offshore ceases its operations in a currency environment, the accumulated adjustments are recognized currently in results of operations. During 1994, Diamond Offshore recognized a loss of $.7 million for the accumulated translation adjustment upon discontinuance of operations in Venezuela. Additionally, translation gains and losses for Diamond Offshore's operations in Brazil have been recognized currently due to the hyperinflationary status of this environment. The effect on results of operations has not been material and is not expected to have a significant effect in the future due to the recent stabilization of currency rates in Brazil.

In February 1996, Diamond Offshore purchased for approximately $8.2 million the eight-story building containing approximately 182,000 net rentable square feet on approximately 6.2 acres in which it had leased office space for its corporate headquarters. A portion of the building is currently occupied by other tenants under leases which expire through 2005. This purchase will reduce general and administrative expenses in the future by eliminating rent expense and will provide rental income from the leases, offset by depreciation and related interest expense. Diamond Offshore does not expect this purchase to have a material effect on its results of operations.

BUSINESS

GENERAL

Diamond Offshore engages principally in the contract drilling of offshore oil and gas wells. Diamond Offshore's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Asia and consists of 30 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 19 jack-up rigs and one drillship. Diamond Offshore also operates 10 land rigs deployed in South Texas. All of Diamond Offshore's offshore and land rigs are wholly owned except for two jack-up rigs operated pursuant to bareboat charters.

Diamond Offshore is a Delaware corporation with its principal executive offices located at 15415 Katy Freeway, Suite 400, Houston, Texas 77094, where its telephone number is (713) 492-5300.

BUSINESS STRATEGY

Diamond Offshore seeks to maximize dayrates and rig utilization by continuously adapting to changes in its markets, improving the capabilities of its drilling rigs and increasing the quality of its service. The key elements of its strategy are to:

- Market worldwide its large, diverse fleet, which is capable of satisfying customer requirements in a variety of applications;

- Continue to enhance its fleet to meet customer demand for diverse drilling capabilities, including those required for deep water and harsh environment operations;

- Exploit the potential of Diamond Offshore's nine Victory-class semisubmersible rigs by pursuing projects that take advantage of this rig type's unique design to yield significantly enhanced rigs; and

- Maintain a program of continuous improvement of quality and safety through Diamond Offshore's Global Excellence Management System and further capitalize on customer recognition of Diamond Offshore's quality and safety achievements.

INDUSTRY CONDITIONS

Diamond Offshore's business and operations depend principally upon the condition of the oil and gas industry and, specifically, the exploration and production expenditures of oil and gas companies. Historically, the offshore contract drilling industry has been highly competitive and cyclical, with periods of high demand, short rig supply and high dayrates followed by periods of low demand, excess rig supply and low dayrates. The offshore contract drilling business is influenced by a number of factors, including the current and anticipated prices of oil and natural gas, the expenditures by oil and gas companies for exploration and production and the availability of drilling rigs. For a number of years, depressed oil and natural gas prices and an oversupply of rigs have adversely affected the offshore drilling market, particularly in the Gulf of Mexico, where the prolonged weakness and uncertainty in the demand for and price of natural gas resulted in a significant decline in exploration and production activities. Demand for drilling services outside the United States, excluding the North Sea, has been less volatile in recent years, but remains dependent on a variety of political and economic factors beyond Diamond Offshore's control, including worldwide demand for oil and natural gas, the ability of OPEC to set and maintain production levels and pricing, the level of production of non-OPEC countries and the policies of the various governments regarding exploration and development of their oil and natural gas reserves.

The deep water and harsh environment markets for semisubmersible rigs have experienced improved demand and higher dayrates during the past year, due in part to the increasing impact of technological advances that have broadened opportunities for offshore exploration and development. Both the Gulf of Mexico and the North Sea semisubmersible markets experienced increased utilization and significantly higher dayrates in 1995 and 1996, and customers increasingly are seeking to contract for rigs serving these markets for a stated term (as opposed to contracts for the drilling of a single well or a group of wells). The market for jack-up rigs in the Gulf of Mexico, which weakened during 1994, appears to have stabilized during 1995 and has shown some signs of strengthening in recent months. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Outlook."

COMPETITION

The contract drilling industry is highly competitive. Customers often award contracts on a competitive bid basis, and although a customer selecting a rig may consider, among other things, a contractor's safety record, crew quality and quality of service and equipment, the oversupply of rigs has created an intensely competitive market in which price is the primary factor in determining the selection of a drilling contractor. Diamond Offshore believes that competition for drilling contracts will continue to be intense for the foreseeable future because of the worldwide oversupply of drilling rigs and the ability of contractors to move rigs from areas of low utilization and dayrates to areas of greater activity and relatively higher dayrates. In addition, there are inactive non-marketed rigs or rigs being operated in non-drilling activities that could be reactivated to meet an increase in demand for drilling rigs in any given market. Such movement or reactivation or a decrease in drilling activity in any major market could depress dayrates and could adversely affect utilization of Diamond Offshore's rigs. See "-- Offshore Contract Drilling Services."

THE ACQUISITION

BACKGROUND. In September 1995 Arethusa publicly announced that it was exploring strategic alternatives to maximize shareholder value, including a possible sale of Arethusa. Following completion of the Diamond Offshore Initial Public Offering, Diamond Offshore commenced an investigation of Arethusa and in November 1995 submitted a formal indication of interest in acquiring Arethusa, which was rejected. However, further discussions transpired that led to execution of a letter of intent on December 7, 1995 pursuant to which Diamond Offshore and Arethusa agreed to work together on an exclusive basis in an effort to agree on the terms of the definitive documentation for the Acquisition. Subsequent negotiations among representatives of Arethusa, Alphee, Ratos, Diamond Offshore and Loews took place in numerous meetings, telephone conversations and correspondence, following which the definitive documentation for the Acquisition was executed on February 9, 1996.

Diamond Offshore elected to proceed with the Acquisition principally because it viewed the Acquisition as a means of expanding its geographic areas of operation and the size of its semisubmersible fleet, including the addition of some units that may be suitable for upgrading. In addition, Diamond Offshore expects that the increase in the number of publicly traded shares of Diamond Offshore Common Stock resulting from the Acquisition, and the anticipated consequential increase in Diamond Offshore's market capitalization, will heighten trading volume and institutional interest in Diamond Offshore's securities, which should ultimately benefit all Diamond Offshore stockholders.

THE AMALGAMATION. Pursuant to the Plan of Acquisition and the Amalgamation Agreement, at the Effective Time, (1) Arethusa and Acquisition Sub have amalgamated and will continue their businesses as one amalgamated company under the name "Diamond Offshore Exploration (Bermuda) Limited," a wholly owned subsidiary of Diamond Offshore (USA), (2) each issued and outstanding share of Arethusa Common Stock (other than any such shares held by Diamond Offshore, Diamond Offshore (USA) or Acquisition Sub) was canceled and ceased to exist and each holder thereof became entitled to receive in consideration of each share so canceled 0.88 shares of Diamond Offshore Common Stock (the "Amalgamation Ratio") and (3) each share of Arethusa Common Stock held by Diamond Offshore, Diamond Offshore (USA) or Acquisition Sub (other than any such shares held in a fiduciary capacity or in satisfaction of a debt previously contracted) was canceled, retired and ceased to exist, and no payment of Diamond Offshore Common Stock was or will be made in respect thereof. Each certificate that immediately prior to the Effective Time represented a share or shares of Arethusa Common Stock now represents the right to receive, upon surrender of such certificate as provided in the Amalgamation Agreement and subject to the provisions set forth therein governing fractional shares, that number of shares of Diamond Offshore Common Stock determined by multiplying the number of shares of Arethusa Common Stock formerly represented by such certificate by the Amalgamation Ratio. From and after the Effective Time, the holders of certificates previously representing shares of Arethusa Common Stock ceased to have any other rights except as otherwise provided in the Amalgamation Agreement or by law.

MEMORANDUM OF ASSOCIATION; BYE-LAWS; DIRECTORS; OFFICERS. Under the Amalgamation Agreement, (1) at the Effective Time, the Memorandum of Association of Arethusa, as in effect immediately prior to the Effective Time, became the Memorandum of Association of Diamond Offshore Exploration (Bermuda), (2) the Bye-laws of Arethusa, as in effect immediately prior to the Effective Time, became the Bye-laws of Diamond Offshore Exploration (Bermuda), (3) the directors of Acquisition Sub immediately prior to the Effective Time became the directors of Diamond Offshore Exploration (Bermuda), each to hold office in accordance with the Memorandum of Association and Bye-laws of Diamond Offshore Exploration (Bermuda) until their respective successors are duly elected or appointed and qualified, and (4) the officers of Acquisition Sub immediately prior to the Effective Time became the officers of Diamond Offshore Exploration (Bermuda), each to hold office in accordance with the Bye-laws of Diamond Offshore Exploration (Bermuda) until their respective successors are duly elected or appointed and qualified.

CONTINUING ARETHUSA SEVERANCE, CONSULTING AND SALARY CONTINUATION PLANS. Under the Plan of Acquisition, from and after the Effective Time, Diamond Offshore will honor in accordance with their terms the following Arethusa employment, severance, consulting and salary continuation plans: (1) the Employment Agreement between Arethusa and Jan Rask, as amended (the "Rask Employment Agreement"), (2) the Severance Agreement between Arethusa Off-Shore Company, Arethusa's principal operating subsidiary ("AOC"), and O. Peter Blom, (3) the Severance Agreement between AOC and Vincent G. Bounds, (4) the Severance Agreement between AOC and Harris I. Knecht, (5) the Severance Agreement between AOC and Danny R. Richardson, (6) the Severance Agreement between AOC and James E. Traber, Jr., (7) the Severance Agreement between AOC and Charles R. Richter, (8) the AOC Severance Policy for all AOC shore-based employees, (9) the Arethusa 1993 Employee Stock Option Plan and (10) the Arethusa 1994 Nonqualified Stock Option Plan for Non-Employee Directors. To the extent permitted or required under applicable law, each employee of Arethusa or its subsidiaries will be given credit for all service with Arethusa or its subsidiaries (or service credited by Arethusa or its subsidiaries) under all employee benefit plans maintained by Arethusa, Diamond Offshore, Diamond Offshore (USA) or Acquisition Sub in which they participate or in which they become participants for purposes of eligibility and vesting.

In October 1994, Arethusa entered into the Rask Employment Agreement with Jan Rask. The Rask Employment Agreement provides for a current annual salary of $325,000. In addition, the Rask Employment Agreement provides that Arethusa will pay Mr. Rask bonus compensation as may from time to time be awarded by the Board of Directors of Arethusa and that Mr. Rask is entitled to participate in all employee benefit plans and other compensatory arrangements sponsored by Arethusa. The Rask Employment Agreement may be terminated by either party upon 180 days' prior written notice and by Arethusa at any time for "cause" (as therein defined). The Rask Employment Agreement provides that until December 31, 1996, Mr. Rask will agree to assist in the pursuit of certain types of business combinations and that Mr. Rask will receive a payment upon completion of any such transaction. As a result of the consummation of the Acquisition, Mr. Rask became entitled to a payment of $487,500 pursuant to the Rask Employment Agreement, $81,250 of which was previously paid.

In October 1995, AOC entered into Executive Severance Agreements (the "Arethusa Severance Agreements") with Messrs. Blom, Bounds, Knecht, Traber, Richardson and Richter. The Arethusa Severance Agreements provide that these executive officers will assist with activities arising in connection with proposed business combinations and provide for certain benefits if any of these executive officers are terminated or their employment is materially changed within 2.5 years following a merger, sale or change of control, where the change of control is to a competing drilling contractor, and the termination or change is either (a) by the ongoing company for reasons other than for cause or as a consequence of the executive's death, permanent disability or retirement, or (b) by the executive if the executive is not offered continued employment in an equivalent officer-level position in the Houston area, a compensation program at least equal to such executive's compensation (excluding bonus) immediately prior to such merger, sale or change of control and a comparable fringe benefit program. In such event, such executive officers will receive a lump sum cash payment equal to 30 times such executive's monthly base salary, outplacement consulting assistance and earned and accrued vacation. The consummation of the Acquisition results in such payments becoming due to each of such executive officers.

Under the Plan of Acquisition, following the Effective Time, except with respect to any collective bargaining agreements, Diamond Offshore or its subsidiaries will cause the employees of Arethusa and its subsidiaries to receive compensation, benefits, fringe benefits, plans, programs and arrangements that are no less favorable in the aggregate than the lesser of such compensation, benefits, fringe benefits, plans, programs and arrangements to which (1) such employees are entitled immediately prior the Effective Time or (2) similarly situated employees of Diamond Offshore are entitled. With respect to any welfare plan maintained by Arethusa or its subsidiaries or Diamond Offshore in which employees or former employees of Arethusa or its subsidiaries (or their dependents) participate after the Effective Time, Diamond Offshore will waive or cause to be waived any preexisting condition provision (except for preexisting conditions of any employee or former employee (or dependent) that are currently excluded under existing Arethusa welfare plans in which such employee or former employee (or dependent) currently participates) and each employee or former employee and his dependents will be given credit for any claims incurred prior to the Effective Time toward any applicable deductible under any such welfare plan.

All members of Arethusa's Board of Directors resigned at the Effective Time.

ARETHUSA STOCK OPTION PLANS. Pursuant to the Amalgamation Agreement, at the Effective Time, each outstanding option to purchase shares of Arethusa Common Stock under Arethusa's 1993 Employee Stock Option Plan (the "Arethusa Employee Plan") and Arethusa's 1994 Nonqualified Stock Option Plan for Non-Employee Directors (the "Arethusa Director Plan" and, together with the Arethusa Employee Plan, the "Arethusa Stock Option Plans"), whether or not then vested or exercisable (the "Arethusa Options") was assumed by Diamond Offshore. See "Management -- Stock Option Plans."

INDEMNIFICATION. Diamond Offshore, Diamond Offshore (USA) and Acquisition Sub agreed in the Plan of Acquisition that all rights to indemnification existing in favor of the present or former directors, officers and employees (as such) of Arethusa or any of its subsidiaries, as provided in Arethusa's Memorandum of Association or Bye-laws or similar documents of any of such subsidiaries, or any agreement to which Arethusa or any such subsidiary is a party as in effect at February 9, 1996 with respect to matters occurring prior to the Effective Time would survive the Amalgamation, and Diamond Offshore agreed to cause Diamond Offshore Exploration (Bermuda) to comply fully with Arethusa's obligations thereunder. In addition, from and after the Effective Time, in the Plan of Acquisition Diamond Offshore agreed to, and agreed to cause Diamond Offshore Exploration (Bermuda) to, indemnify, defend and hold harmless the present directors and officers of Arethusa against any costs and expenses (including reasonable attorneys' fees), judgments, fines, losses, claims, damages and liabilities, and amounts paid in settlement thereof with Diamond Offshore's consent, in connection with any claim, action, suit, proceeding or investigation relating to any of the transactions contemplated by the Plan of Acquisition, the Amalgamation Agreement or the Fee Agreement.

RIGHTS OF DISSENTING SHAREHOLDERS. After the Effective Time, shares of Arethusa Common Stock that were issued and outstanding immediately prior to the Effective Time held by Arethusa shareholders who did not vote in favor of the adoption and approval of the Amalgamation Agreement and who comply with Section 106(6), (6A), (6B) and (6C) of The Companies Act 1981 of Bermuda, as amended ("The Companies Act") will, at the election of Diamond Offshore (USA), either (1) be canceled and shares of Diamond Offshore Common Stock delivered in consideration thereof, subject to the rights of such shareholders under Section 106(6), (6A), (6B) and (6C) of The Companies Act, or (2) not be canceled and the holders thereof not be entitled to receive shares of Diamond Offshore Common Stock unless and until such holders have failed to perfect or have effectively withdrawn or lost their rights to appraisal under The Companies Act, whereupon such shares will be canceled and shares of Diamond Offshore Common Stock delivered in consideration thereof. Diamond Offshore has not elected whether to proceed with respect to any such shares under (1) or (2) as described in the preceding sentence above.

ACCOUNTING TREATMENT. The Acquisition will be accounted for using the purchase method of accounting pursuant to Opinion No. 16 of the Accounting Principles Board. The purchase method accounts for a business combination as the acquisition of one company by another. The acquiring corporation, Diamond Offshore, records assets less liabilities assumed. A difference between the cost of the acquired corporation, Arethusa, and the sum of the fair values of tangible and identifiable intangible assets less liabilities is recorded as goodwill. The reported income of Diamond Offshore after the Effective Time will include the operations of Arethusa after consummation of the Acquisition.

THE FLEET

Diamond Offshore's large, diverse fleet, which includes some of the most technologically advanced rigs in the world, enables it to offer a broad range of services worldwide in various markets, including the deep water market, the harsh environment market (such as the North Sea), the conventional semisubmersible market and the jack-up market.

SEMISUBMERSIBLES. Diamond Offshore owns and operates 30 semisubmersibles. Semisubmersible rigs consist of an upper working and living deck resting on vertical columns connected to lower hull members. Such rigs operate in a "semi-submerged" position, remaining afloat, off bottom, in a position in which the lower hull is from about 55 to 90 feet below the water line and the upper deck protrudes well above the surface. The rig is typically anchored in position and remains stable for drilling in the semi-submerged floating position due in part to its wave transparency characteristics at the water line.

Diamond Offshore owns and operates three of the world's 13 fourth-generation semisubmersibles. Fourth-generation semisubmersibles are larger than other semisubmersibles, are capable of working in harsh environments and have other advanced features. Diamond Offshore's existing fleet of three fourth-generation semisubmersibles are all capable of operating in water depths of up to 5,000 feet. Currently the Ocean Valiant and the Ocean America are located in deep water areas of the Gulf of Mexico and the Ocean Alliance is located in the harsh environment of the North Sea market west of the Shetland Islands. At present, nine of the world's fourth-generation semisubmersibles are contracted for service in the harsh environment North Sea market and four are operating in the deep water Gulf of Mexico market.

In addition to its fourth-generation semisubmersibles, Diamond Offshore owns and operates 27 other semisubmersibles (including nine Victory-class rigs), 18 of which operate in maximum water depths of between 1,000 to 2,500 feet, and three of which are capable of drilling in 3,000 feet or more of water. The diverse capabilities of most of these semisubmersibles enable them to work in both shallow and deep water environments in the United States and most markets outside the United States. Currently, 15 of these semisubmersibles are located in the Gulf of Mexico; four are located in the North Sea; four are located offshore Brazil; two are located offshore Australia; one is located offshore Nigeria; and one is located offshore Vietnam. In addition to these 27 semisubmersibles, Diamond Offshore owns one other semisubmersible held for disposition.

JACK-UPS. Diamond Offshore owns and/or operates a total of 19 jack-up rigs. Jack-up rigs are mobile, self-elevating drilling platforms equipped with legs that are lowered to the ocean floor until a foundation is established to support the drilling platform. The rig hull includes the drilling rig, jacking system, crew quarters, loading and unloading facilities, storage areas for bulk and liquid materials, heliport and other related equipment. Jack-ups are used extensively for drilling in water depths from 20 feet to 350 feet. The water depth limit of a particular rig is principally determined by the length of the rig's legs. A jack-up rig is towed by tugboats to the drillsite with its hull riding in the sea as a vessel with its legs retracted. Once over a drillsite, the legs are lowered until they rest on the seabed and jacking continues until the hull is elevated above the surface of the water. After completion of drilling operations, the hull is lowered until it rests in the water and then the legs are retracted for relocation to another drillsite.

The principal market for Diamond Offshore's jack-up rigs is currently the Gulf of Mexico, where 14 of Diamond Offshore's jack-up rigs are located. Of Diamond Offshore's jack-up rigs in the Gulf of Mexico, seven are independent-leg cantilevered rigs, two are mat-supported cantilevered rigs, two are independent-leg slot rigs, two are mat-supported slot rigs and one is an independent-leg slot rig that has been modified with skid-off capability. One of Diamond Offshore's jack-up rigs in the Gulf of Mexico is operated pursuant to a bareboat charter and the other 13 are wholly owned by Diamond Offshore. Diamond Offshore also owns and operates one jack-up rig offshore each of Indonesia, Egypt and The Netherlands, and Diamond Offshore operates one jack-up rig offshore India pursuant to a bareboat charter. One of Diamond Offshore's jack-ups is cold stacked in Chile. The jack-up located in the Gulf of Mexico that Diamond Offshore bareboat charters is also under contract for sale, upon closing of which such charter will terminate.

DRILLSHIP. Drillships, which are typically self-propelled, are positioned over a drillsite through the use of either an anchoring system or a computer controlled thruster (dynamic positioning) system similar to those used on certain semisubmersible rigs. Drillships normally require water depth of at least 200 feet in order to conduct operations. Diamond Offshore's drillship, the Ocean Clipper I, which uses a conventional anchoring system, is currently located offshore Africa. The Ocean Clipper I currently has water depth capability of 1,200 feet and variable deck load capacity in excess of 11,000 tons. However, the Ocean Clipper I is scheduled to be upgraded during the year 1996 through the first half of 1997 to operate in the ultra-deep water market of the Gulf of Mexico with dynamic positioning capabilities, 15,000 psi blowout preventers, three mud pumps and other refurbishments and upgrades. The drillship is anticipated to commence operation in the Gulf of Mexico following completion of the upgrade in the second quarter of 1997 pursuant to a four-year term contract with a major oil company that has been agreed to in principle. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Capital Resources."

FLEET ENHANCEMENTS. Diamond Offshore's strategy is to maximize dayrates and utilization by adapting to trends in its markets, including enhancing its fleet to meet customer demand for diverse drilling capabilities. Many of Diamond Offshore's rigs have been upgraded during the last five years with enhancements such as top-drive drilling systems, increases in water depth capability, mud pump additions or increases in deck load capacity. For example, Diamond Offshore upgraded the semisubmersible Ocean Voyager to operate in maximum water depths of 3,200 feet and has modified the semisubmersible Ocean Nomad to allow it to be certified for service in the United Kingdom sector of the North Sea, where it is operating under a two-year contract at improved dayrates. Diamond Offshore converted three of its 300-foot cantilever jack-up rigs from slot rigs, which Diamond Offshore believes has resulted in these rigs achieving higher dayrates and utilization. Also, Diamond Offshore has added top-drive drilling systems to many rigs, so that 36 rigs in Diamond Offshore's fleet are now so equipped.

Notwithstanding the average age of the Diamond Offshore fleet of 17.7 years (calculated as of December 31, 1995 and measured from year built), Diamond Offshore believes that it will be feasible to continue to upgrade its fleet, particularly its Victory-class semisubmersible rigs. The design of the Victory-class semisubmersible rigs, including their cruciform hull configurations, long fatigue-life and advantageous stress characteristics, makes this class of rig particularly well-suited for significant upgrading projects. Currently, Diamond Offshore's Victory-class rigs are outfitted for service in maximum water depths of 600 to 3,200 feet. Five of Diamond Offshore's nine Victory-class rigs are equipped with top-drive drilling systems, two are modified for increased efficiency in the handling of subsea completion equipment and one has stability enhancements that allow increased variable deck load. In management's opinion, it is unlikely that new semisubmersibles will be built unless there is a substantial and sustained improvement in the market; therefore, Diamond Offshore believes that the relative ease and efficiency with which it can significantly enhance its Victory-class rigs is a competitive advantage in a market requiring increasing capability from offshore drilling rigs.

The Ocean Quest, one of Diamond Offshore's Victory-class rigs, is currently undergoing an upgrade pursuant to a contract with a major oil company for a three-year commitment. The rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 3,500 feet. This project includes enhancements to provide additional hull buoyancy, which will allow a variable deck load exceeding 5,000 tons, the addition of a new self-contained chain/wire mooring system, and drilling system upgrades, including the installation of a top-drive drilling system, a 15,000 psi blowout prevention system, a third mud pump and 2,900 barrel liquid mud capacity. The Ocean Quest is scheduled to be placed in service in the fourth quarter of 1996. In addition, during the third quarter of 1995 Diamond Offshore entered into a letter of intent with another major oil company for a three-year commitment for a second Victory-class rig, the Ocean Star (formerly named Ocean Countess), pursuant to which the rig is being upgraded to conduct drilling operations in the Gulf of Mexico in water depths of up to 4,500 feet. The upgrade project for the Ocean Star also includes stability enhancements, the installation of a new mooring system and drilling system upgrades similar to those planned for the Ocean Quest. The Ocean Star is scheduled to be placed in service late in the fourth quarter of 1996. Following the upgrades, Diamond Offshore believes that these rigs will be able to compete effectively in the fourth-generation deep water market.

Additional Victory-class upgrade potential exists, including conceptual plans Diamond Offshore is developing for the possible construction of an ultra-large semisubmersible, the Ocean Legend. The Ocean Legend is intended to take advantage of the cruciform design of the Victory-class semisubmersibles to "square off" the rig by adding large corner columns and other new equipment to yield a rig with capabilities beyond a traditional fourth-generation unit at a significantly reduced cost as compared to new construction. Diamond Offshore has completed its feasibility studies and has begun preliminary design engineering in connection with the upgrade. See Note 1 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein. Although Diamond Offshore is proposing the design to several major oil companies, there can be no assurance that the Ocean Legend can be built in a cost-effective manner, that if a Victory-class rig is so upgraded, there will be adequate demand for its services, or that competitors will not achieve capability beyond that of fourth-generation semisubmersibles through other means attractive to customers.

For the year ended December 31, 1995, Diamond Offshore spent approximately $.6 million on conceptual design studies and related costs associated with the Ocean Legend project. Diamond Offshore expects to evaluate other projects as opportunities arise. Once a capital project is undertaken by Diamond Offshore, Diamond Offshore may later determine that completion of such project is infeasible based on its analysis of factors such as design criteria, anticipated costs of construction, market demand and availability of financing, and Diamond Offshore may be unable to recoup the expenditures made before such project is abandoned. In addition, to the extent Diamond Offshore determines that its fleet cannot be upgraded as it currently anticipates, Diamond Offshore will have fewer rigs available to compete in the harsh environment and deep water markets than if such upgrades had been successfully implemented.

More detailed information as of March 28, 1996 concerning the Diamond Offshore fleet of active mobile offshore drilling rigs is set forth in the table below.

TYPE AND NAME(A)	WATER DEPTH CAPABILITY (FT)	ATTRIBUTES(B)	YEAR BUILT/LATEST ENHANCEMENT(C)	CURRENT LOCATION	CUSTOMER(D)
FOURTH-GENERATION SEMISUBMERSIBLES(3):					
Ocean Alliance........	5,000	TDS; DP; 15K; 3M	1988/1995	North Sea	BP
Ocean America.........	5,000	TDS; SP; 15K; 3M	1988/1992	Gulf of Mexico	BP
Ocean Valiant.........	5,000	TDS; SP; 15K; 3M	1988/1995	Gulf of Mexico	Exxon
OTHER SEMISUBMERSIBLES(27):					
Arethusa Worker.......	3,300	TDS	1982/1992	Gulf of Mexico	Texaco
Ocean Voyager.........	3,200	TDS; VC	1973/1995	Gulf of Mexico	Enserch
Arethusa Yatzy(e).....	3,000	TDS; DP	1989	Brazil	Petrobras
Arethusa Lexington....	2,500	TDS; 3M	1976/1995	Gulf of Mexico	Marathon
Arethusa Neptune......	2,500	TDS; 3M	1977/1995	Gulf of Mexico	Kerr-McGee
Arethusa Concord......	2,200	TDS	1975/1995	Gulf of Mexico	Shell
Arethusa Saratoga.....	2,200	TDS; 3M	1976/1995	Gulf of Mexico	Shell
Arethusa Yorktown.....	2,200	TDS	1976/1989	Brazil	Petrobras
Ocean Endeavor........	2,000	TDS; VC	1975/1994	Gulf of Mexico	Oryx
Ocean Rover...........	2,000	TDS; VC; 15K	1973/1992	Gulf of Mexico	Amerada Hess
Ocean Prospector......	1,700	VC	1971/1981	Gulf of Mexico	Newfield(f)
Arethusa Whittington.........	1,500	TDS; 3M	1974/1995	Gulf of Mexico	Mobil
Ocean Bounty..........	1,500	TDS; VC; 3M	1977/1992	Australia/ Indonesia	Phillips
Ocean Guardian........	1,500	TDS; SP; 3M	1985	North Sea	BP
Ocean New Era.........	1,500	TDS	1974/1990	Gulf of Mexico	Hardy Oil & Gas(g)
Ocean Princess(h).....	1,500	TDS; 15K	1977/1995	North Sea	Committed
Ocean Epoch...........	1,200	TDS	1977/1990	Australia/ Indonesia	Enterprise
Ocean General.........	1,200	TDS	1976/1990	Vietnam	Fina
Ocean Nomad...........	1,200	TDS	1975/1995	North Sea	Shell
Ocean Ambassador......	1,100	TDS	1975/1995	Gulf of Mexico	LL&E
Ocean Baroness........	1,100	TDS; VC	1973/1995	Brazil	Committed
Ocean Star(i)(j)......	850	VC	1974/1992	Gulf of Mexico	Committed
Ocean Century.........	800		1973	Gulf of Mexico	Stacked
Ocean Quest(k)........	800	VC	1973	Gulf of Mexico	Committed
Ocean Liberator.......	600		1974	Nigeria	Ashland
Ocean Victory.........	600	VC	1972	North Sea	Stacked
Ocean Zephyr..........	600		1972	Brazil	Petrobras
JACK-UPS(19):					
Ocean Titan...........	350	TDS; IS; 15K; 3M	1974/1989	Gulf of Mexico	LL&E
Ocean Tower...........	350	IS; 3M	1972	Gulf of Mexico	Sonat Exploration(l)
Bonito II(m)..........	300	TDS; IC	1983/1995	Gulf of Mexico	Unocal
Miss Kitty(n).........	300	IC	1982	India	ONGC
Ocean King............	300	TDS; IC	1973/1989	Gulf of Mexico	Conoco
Ocean Nugget..........	300	TDS; IC	1976/1995	Gulf of Mexico	Amoco
Ocean Summit..........	300	SDS; IC	1972/1991	Gulf of Mexico	Forcenergy
Ocean Warwick.........	300	TDS; IS; SO	1971/1984	Gulf of Mexico	Stacked
Arethusa Heritage.....	250	TDS; IC	1981/1995	Egypt	EDC
Arethusa Sovereign....	250	TDS; IC	1981/1994	Indonesia	Maxus
Ocean Champion........	250	MS	1975/1985	Gulf of Mexico	Chevron
Ocean Columbia........	250	TDS; IC	1978/1990	Gulf of Mexico	Coastal Oil & Gas
Ocean Spartan.........	250	TDS; IC	1980/1994	Gulf of Mexico	Meridian
Ocean Spur............	250	TDS; IC	1981/1994	Gulf of Mexico	Houston Exploration(o)
Ocean Conquest........	200	MS	1978	Gulf of Mexico	Stacked
Ocean Crusader........	200	TDS; MC	1982/1992	Gulf of Mexico	Chevron
Ocean Drake...........	200	TDS; MC	1983/1986	Gulf of Mexico	Murphy
Arethusa Scotian......	180	TDS; IC; 15K	1981/1988	North Sea (Dutch sector)	Elf
Ocean Magallanes......	150	IC	1980	Chile	Stacked
DRILLSHIP(1):					
Ocean Clipper I.......	1,200	SP	1976	Africa	Committed(p)

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(a) Does not include one other semisubmersible rig held for disposition that is also not included in the discussion of Diamond Offshore's fleet.

(b) Attributes legend:

DP	--	Dynamically Positioned/Self-Propelled
MS	--	Mat-Supported Slot Rig
TDS	--	Top-Drive Drilling System
IC	--	Independent-Leg Cantilevered Rig
SDS	--	Side-Drive Drilling System
VC	--	Victory-Class
IS	--	Independent-Leg Slot Rig
SO	--	Skid-Off Capability
3M	--	Three Mud Pumps
MC	--	Mat-Supported Cantilevered Rig
SP	--	Self-Propelled
15K	--	15,000 psi Blowout Preventer

(c) Such enhancements include the installation of top-drive drilling systems, water depth upgrades, mud pump additions and increases in deck load capacity.

(d) For ease of presentation in this table, customer names have been shortened or abbreviated.

(e) Arethusa acquired the Arethusa Yatzy on May 3, 1995. Prior to this date the rig was operated by Arethusa under a management agreement.

(f) Turnkey operator is ADTI.

(g) Turnkey operator is DOTS.

(h) Preparing for a two-year term contract that commenced late March 1996.

(i) Formerly named Ocean Countess.

(j) Committed under a letter of intent for a three-year term contract with Texaco in the Gulf of Mexico.

(k) Committed under a three-year term contract with Chevron in the Gulf of Mexico.

(l) Turnkey operator is Triton.

(m) Diamond Offshore charters the rig pursuant to a bareboat charter agreement which expires in August 1996. The rig is under contract for sale, upon closing of which such charter will terminate.

(n) Diamond Offshore operates the rig pursuant to a bareboat charter agreement which expires in July 1997. Diamond Offshore has the option to extend the charter agreement for one additional year.

(o) Turnkey operator is Brown/R&B.

(p) Committed under an agreement in principle for a four-year term contract in the Gulf of Mexico following completion of rig enhancement.

OFFSHORE FLEET UTILIZATION

The following table sets forth certain information comparing the rig utilization of the respective fleets of Diamond Offshore and Arethusa relative to that of the offshore drilling industry as a whole during the year ended December 31, 1995 and during the three months ended March 31, 1996. Industry statistics and statistics for each of the companies were compiled by Offshore Data Services. Diamond Offshore's one drillship had an average utilization of 59.4% and 95.6% for the year ended December 31, 1995 and the three months ended March 31, 1996, respectively.

	AVERAGES FOR THREE MONTHS ENDED MARCH 31,			AVERAGES FOR THE YEAR ENDED DECEMBER 31,		
	1996			1995		
	DIAMOND OFFSHORE	ARETHUSA	INDUSTRY	DIAMOND OFFSHORE	ARETHUSA	INDUSTRY
FOURTH-GENERATION SEMISUBMERSIBLES:						
Total Rigs	3.0	--	13.0	3.0	--	13.0
Under Contract	3.0	--	13.0	3.0	--	13.0
Utilization Rate	100.0%	--	100.0%	100.0%	--	100.0%
OTHER SEMISUBMERSIBLES:						
Total Rigs	19.0	8.0	112.0	19.0	8.0	110.1
Under Contract	16.3	8.0	97.3	14.5	7.8	89.3
Utilization Rate	86.0%	100.0%	86.9%	76.3%	96.9%	81.2%
JACK-UPS:						
Total Rigs	14.0	5.0	302.3	14.0	5.0	306.8
Under Contract	11.0	5.0	254.3	10.6	4.8	249.1
Utilization Rate	78.6%	100.0%	84.1%	75.6%	95.0%	81.2%

MARKETS

Diamond Offshore's principal markets for its offshore contract drilling services are the Gulf of Mexico, Europe, including principally the United Kingdom sector of the North Sea, South America and Australia/Southeast Asia. Diamond Offshore actively markets its rigs worldwide. In the past, rigs in Diamond Offshore's fleet have also operated in the Mediterranean Sea, the Black Sea and other markets. See Note 11 to Diamond Offshore's Consolidated Financial Statements included elsewhere herein.

Diamond Offshore believes that its presence in multiple markets provides a competitive advantage. For example, Diamond Offshore believes that its experience with safety and other regulatory matters in the United Kingdom has been beneficial in Australia and in the Gulf of Mexico and that production experience gained through Brazilian and North Sea operations has potential application worldwide. Additionally, Diamond Offshore believes that its performance for a customer in one market segment or area enables Diamond Offshore to better understand that customer's needs and serve that customer in different market segments or other geographic locations.

OFFSHORE CONTRACT DRILLING SERVICES

Diamond Offshore's contracts to provide offshore drilling services vary in their terms and provisions. Diamond Offshore often obtains its contracts through competitive bidding, although it is not unusual for Diamond Offshore to be awarded drilling contracts without competitive bidding. Drilling contracts generally provide for a basic drilling rate on a fixed dayrate basis regardless of whether such drilling results in a successful well. Drilling contracts may also provide for lower rates during periods when the rig is being moved or when drilling operations are interrupted or restricted by equipment breakdowns, adverse weather or water conditions or other conditions beyond the control of Diamond Offshore. Under dayrate contracts, Diamond Offshore generally pays the operating expenses of the rig, including wages and the cost of incidental supplies. Revenues from dayrate contracts have historically accounted for a substantial portion of Diamond Offshore's revenues. In addition, Diamond Offshore has worked some of its rigs under dayrate contracts pursuant to which the customer also agrees to pay Diamond Offshore an incentive bonus based upon performance.

A dayrate drilling contract generally extends over a period of time covering either the drilling of a single well, a group of wells (a "well-to-well contract") or a stated term (a "term contract") and may be terminated by the customer in the event the drilling unit is destroyed or lost or if drilling operations are suspended for a specified period of time as a result of a breakdown of major equipment or in some cases due to other events beyond the control of either party. In addition, certain of Diamond Offshore's contracts permit the customer to terminate the contract early by giving notice and in some circumstances may require the payment of an early termination fee by the customer. The contract term in many instances may be extended by the customer exercising options for the drilling of additional wells at fixed or mutually agreed terms, including dayrates.

The duration of offshore drilling contracts is generally determined by market demand and the respective management strategy of the offshore drilling contractor and its customers. In periods of rising demand for offshore rigs, contractors typically prefer well-to-well contracts that give contractors the flexibility to profit from increasing dayrates. In contrast, during these periods customers with reasonably definite drilling programs typically prefer longer term contracts to maintain drilling prices at the lowest level possible. Conversely, in periods of decreasing demand for offshore rigs, contractors generally prefer longer term contracts to preserve dayrates at existing levels and ensure utilization, while the customers prefer well-to-well contracts that allow them to obtain the benefit of lower dayrates. In general, Diamond Offshore seeks to have a reasonable balance of single well, well-to-well and term contracts to minimize the downside impact of a decline in the market while still participating in the benefit of increasing dayrates in a rising market. Although many of Diamond Offshore's semisubmersible rigs are contracted on a term basis, Diamond Offshore's jack-up fleet is primarily committed for short-term single-well or well-to-well arrangements.

Diamond Offshore believes that more of its customers are seeking to establish continuing relationships with a small number of preferred drilling contractors rather than seeking bids for each drilling contract from a large number of contractors. Diamond Offshore also believes that those contractors who provide the highest quality and the greatest range of services will achieve preferred contractor status. In response to this change in customer attitude, in May 1993 DOTS began offering a portfolio of drilling and production services to complement Diamond Offshore's offshore contract drilling business. These services include overall project management and drilling and production operations on a turnkey or modified-turnkey basis. Under a turnkey contract, the drilling contractor agrees to perform a specified drilling service, such as drilling a well to a specified depth for a fixed price. The ability of the contractor to make a profit on this type of contract depends on the contractor's ability to complete the specified project while keeping expenses within the estimates used to determine the contract price. Under a turnkey contract, the drilling contractor bears the financial risk of delays in completion of the project. Since May 1993, DOTS has engaged in 22 turnkey drilling projects in the Gulf of Mexico and, in conjunction with a tanker owner, has completed an extended well test on a modified-turnkey basis for an operator in the North Sea. Diamond Offshore also intends to seek alternative uses for the rigs in its fleet that are no longer competitive in the drilling market and do not meet Diamond Offshore's criteria for modification. Such alternative uses may include employment of these rigs as mobile offshore production units or as a part of floating production systems. These operations have not been a significant part of Diamond Offshore's business. See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

BAREBOAT CHARTER CONTRACTS

Diamond Offshore operates two of its rigs pursuant to bareboat charter contracts. Under a bareboat charter, Diamond Offshore charters the use of a rig for a specified period and operates the rig as if it were owned.

BONITO II CONTRACT. Diamond Offshore operates the Bonito II under a bareboat charter agreement expiring in August 1996. Under the agreement, Diamond Offshore makes periodic payments to the rig owner consisting of (i) monthly basic charter hire payments and (ii) quarterly additional hire payments based on certain revenue/cost criteria. Diamond Offshore recognizes all revenues and costs, including the charter fee, in its financial statements. The rig is under contract for sale, upon closing of which such charter will terminate.

MISS KITTY CONTRACT. Diamond Offshore operates the Miss Kitty under a bareboat charter agreement initially expiring in July 1996, and recently extended to July 1997. Under the agreement, Diamond Offshore makes periodic payments to the rig owner consisting of (i) monthly basic charter hire payments and (ii) quarterly additional hire payments based on certain revenue/cost criteria. Diamond Offshore recognizes all revenues and costs, including the charter fee, in its financial statements.

LAND DRILLING OPERATIONS

In addition to its offshore drilling fleet, Diamond Offshore owns and operates 10 land rigs, all of which are currently located in South Texas, and a fleet of heavy-duty trucks designed to transport these rigs to drilling locations. Seven of Diamond Offshore's 10 land rigs are Cabot-design trailer-mounted rigs that are highly mobile and relatively sophisticated, making them more desirable to drilling contractors than non-trailer-mounted land rigs of similar capability. Diamond Offshore believes that these trailer-mounted rigs have achieved higher utilization rates than non-trailer-mounted rigs would have achieved. Diamond Offshore's land rigs typically operate under dayrate, footage or turnkey contracts (compensation under footage contracts is based on the number of feet drilled and involves more risk for a contractor than dayrate contracts and the potential for greater financial gains or losses), although most of its contracts are dayrate contracts.

More detailed information concerning Diamond Offshore's land drilling rigs, as of March 28, 1996, is set forth in the table below.

RIG NUMBER	TYPE OF RIG	DRILLING DEPTH CAPABILITY (FT)	CUSTOMER(1)
840...............	Oilwell 840-E	18,000	UPRC
851...............	National 80-B	15,000	Parker & Parsley
859...............	Brewster N-75	15,000	Quisto Exploration
865...............	Cabot 1200	14,000	Cox & Perkins
866...............	Cabot 1200	14,000	Enron Oil & Gas
863...............	Cabot 1000	13,000	Enron Oil & Gas
864...............	Cabot 1000	13,000	Coastal Oil & Gas
861...............	Cabot 900	11,000	Swift Energy
862...............	Cabot 900	11,000	Conoco
860...............	Cabot 750	9,500	Sanchez-O'Brien

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(1) For ease of presentation in this table, customer names have been shortened or abbreviated.

CUSTOMERS

Diamond Offshore provides offshore drilling services to a customer base that includes independent and major integrated oil companies and state-owned oil companies. Occasionally, several customers have accounted for 10.0% or more of Diamond Offshore's annual consolidated revenues, although the identity of such customers may vary from year to year. During 1995, Diamond Offshore performed services for approximately 90 different customers and British Petroleum Co., PLC ("BP"), accounted for 16.5% of Diamond Offshore's annual total consolidated revenues. During 1994, Diamond Offshore performed services for approximately 90 different customers and no single customer accounted for more than 8.2% of Diamond Offshore's annual total consolidated revenues. During 1993, Diamond Offshore performed services for approximately 85 different customers and BP accounted for 10.5% of Diamond Offshore's annual total consolidated revenues. Management believes that at current levels of activity Diamond Offshore has alternative customers for its services such that the loss of a single customer would not have a material adverse effect on Diamond Offshore on a long-term basis.

Diamond Offshore's services are marketed principally through its Houston office, with support from its regional offices in New Orleans, Louisiana; Aberdeen, Scotland; and Perth, Australia. Technical and administrative support for Diamond Offshore's operations is provided by its Houston office.

QUALITY

Diamond Offshore maintains a program to continuously improve quality and safety through GEMS, which was instituted in 1993 to increase Diamond Offshore's commitment to quality of service, safety and the environment. GEMS is a quality system that provides for formal procedures to assist in continuous improvement in Diamond Offshore's efforts to exceed customer expectations in safety, environmental concerns, equipment maintenance, rig enhancements, material handling and personnel training and performance. The key to GEMS is Diamond Offshore's end-of-well report, which is intended to ensure feedback for improvement and communication of Diamond Offshore's concern for customer satisfaction. Diamond Offshore also seeks to capitalize on customer recognition of Diamond Offshore's quality and safety achievements. Diamond Offshore is the only drilling contractor to have won more than once (in April 1994 and April 1995) the annually awarded U.S. Minerals Management Service National Safety Award for Excellence.

GOVERNMENTAL REGULATION

Diamond Offshore's operations are subject to numerous federal, state and local environmental laws and regulations that relate directly or indirectly to its operations, including certain regulations controlling the discharge of materials into the environment, requiring removal and clean-up under certain circumstances, or otherwise relating to the protection of the environment. For example, Diamond Offshore may be liable for damages and costs incurred in connection with oil spills for which it is held responsible. Laws and regulations protecting the environment have become increasingly stringent in recent years and may in certain circumstances impose "strict liability" and render a company liable for environmental damage without regard to negligence or fault on the part of such company. Such laws and regulations may expose Diamond Offshore to liability for the conduct of or conditions caused by others, or for acts of Diamond Offshore that were in compliance with all applicable laws at the time such acts were performed. The application of these requirements or the adoption of new requirements could have a material adverse effect on Diamond Offshore.

OPA '90 and similar legislation enacted in Texas, Louisiana and other coastal states address oil spill prevention and control and significantly expand liability exposure across all segments of the oil and gas industry. OPA '90, such similar legislation and related regulations impose a variety of obligations on Diamond Offshore related to the prevention of oil spills and liability for damages resulting from such spills. OPA '90 imposes strict and with limited exceptions joint and several liability upon each responsible party for oil removal costs and a variety of public and private damages. OPA '90 also imposes ongoing financial responsibility requirements on a responsible party. A failure to comply with such ongoing requirements or inadequate cooperation in a spill may subject a responsible party, including in some cases Diamond Offshore, to civil or criminal enforcement action. OPA '90 also requires the U.S. Minerals Management Service to promulgate regulations to implement the financial responsibility requirements for offshore facilities. If implemented as written, the financial responsibility requirements of OPA '90 could have the effect of significantly increasing the amount of financial responsibility that oil and gas operators must demonstrate to comply with OPA '90. While industry groups and marine insurance carriers are seeking modification of these requirements, implementation of these requirements in their current form could adversely affect the ability of some of Diamond Offshore's customers to operate in U.S. waters, which could have a material adverse effect on Diamond Offshore.

The Federal Water Pollution Control Act of 1972, commonly referred to as the Clean Water Act ("CWA"), prohibits the discharge of certain substances into the navigable waters of the U.S. without a permit. The regulations implementing the CWA require permits to be obtained by an operator before certain exploration or drilling activities occur. Violations of monitoring, reporting and permitting requirements can result in the imposition of civil and criminal penalties. The provisions of the CWA can also be enforced by citizens' groups. Many states have similar laws and regulations.

The Outer Continental Shelf Lands Act authorizes regulations relating to safety and environmental protection applicable to lessees and permittees operating on the Outer Continental Shelf. Specific design and operational standards may apply to Outer Continental Shelf vessels, rigs, platforms, vehicles and structures.

Violation of lease terms relating to environmental matters or regulations issued pursuant to the Outer Continental Shelf Lands Act can result in substantial civil and criminal penalties as well as potential court injunctions curtailing operations and the cancellation of leases. Such enforcement liabilities can result from either governmental or citizen prosecution.

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended ("CERCLA"), currently exempts crude oil, and the Resource Conservation and Recovery Act, as amended ("RCRA"), currently exempts certain drilling materials, such as drilling fluids and production waters, from the definitions of hazardous substances and hazardous wastes. However, Diamond Offshore's operations may involve the use or handling of other materials, such as fracturing fluids or acids, that may be classified as environmentally hazardous substances or wastes. There can be no assurance that such exemption will be preserved in future amendments of such acts, if any, or that more stringent laws and regulations protecting the environment will not be adopted. CERCLA assigns strict liability to each responsible party, as defined, for all response and remediation costs, as well as natural resource damages. Few defenses exist to the liability imposed by CERCLA.

Diamond Offshore's operations may involve the generation, use or handling of materials, such as unused fracturing fluids or acids, that may be classified as hazardous waste, and that are subject to RCRA and comparable state statutes. The Environmental Protection Agency ("EPA") and various state agencies have limited the disposal options for certain hazardous and nonhazardous wastes and are considering the adoption of stricter handling and disposal standards for nonhazardous wastes. RCRA currently exempts certain drilling materials, such as drilling fluids and production waters, from the definitions of hazardous wastes. There can be no assurance that such exemption will be preserved in future amendments of such acts, if any, or that more stringent laws and regulations protecting the environment will not be adopted.

The operations of Diamond Offshore are subject to the Clean Air Act, as amended, and comparable state statutes. Traditional air quality programs relating to the prevention of significant deterioration of air quality in areas with unacceptable pollution levels ("nonattainment areas") restrict drilling in affected areas. Amendments to the Clean Air Act were adopted in 1990 and contain provisions that may result in the imposition over the next decade of certain requirements with respect to air emissions, which requirements may require capital expenditures by Diamond Offshore. The EPA is currently developing regulations to implement these requirements. Pursuant to a mandate of the Clean Air Act, the EPA together with other agencies of the federal government is conducting a study of the effects of emissions from drilling activities in nonattainment areas on the Outer Continental Shelf. Upon completion of the study, these agencies will determine whether additional regulatory requirements are necessary for these nonattainment areas. Any greater degree of regulation in nonattainment areas would increase the cost associated with operation in those areas.

LIMITATION ON OWNERSHIP BY NON-U.S. CITIZENS

Diamond Offshore, as the owner of United States flag vessels, is subject to the Shipping Act, 1916, as amended ("Shipping Act"), which provides that a controlling interest in Diamond Offshore may not be acquired by a non-U.S. citizen without the consent of the U.S. Secretary of Transportation, acting through the United States Maritime Administration ("MARAD"). Current MARAD regulations authorize the transfer of a controlling interest in a company as long as the United States is not at war, the transferee is not a national of a country to which the transfer would be contrary to the foreign policy of the United States and the company's U.S. flag vessels remain documented under the U.S. flag after the transfer. In the absence of MARAD consent (either by the current regulations or otherwise) the transfer of a controlling interest in Diamond Offshore to non-U.S. citizens would enable MARAD to exercise various remedies under the Shipping Act including seizure of vessels, civil penalties and, in certain cases, criminal penalties.

INDEMNIFICATION AND INSURANCE

Diamond Offshore has generally been able to obtain contractual indemnification pursuant to which Diamond Offshore's customers agree to protect and indemnify Diamond Offshore to some degree from liability for reservoir, pollution and environmental damages, but there can be no assurance that Diamond

Offshore can obtain such indemnities in all of its contracts, that the level of indemnification that can be obtained will be meaningful, that such indemnification agreements will be enforceable or that the customer will be financially able to comply with its indemnity obligations. In addition, Diamond Offshore maintains insurance coverage against certain property damage, war risk (in the case of certain operations outside the U.S.), general liability and environmental liabilities, including pollution caused by sudden and accidental oil spills, but there can be no assurance that such insurance will continue to be available or carried by Diamond Offshore or if available and carried will be adequate to cover Diamond Offshore's loss or liability in many circumstances. Except with respect to its fourth-generation semisubmersibles, Diamond Offshore does not maintain business interruption insurance and may elect to discontinue this coverage for its fourth-generation semisubmersibles at any time.

EMPLOYEES

As of December 31, 1995, Diamond Offshore and Arethusa had approximately 2,500 and 1,101 employees, respectively (including international crews furnished through labor contractors), approximately 260 of which Diamond Offshore employees were union members. Diamond Offshore has experienced satisfactory labor relations and provides comprehensive benefit plans for its hourly paid employees. Diamond Offshore does not consider the possibility of a shortage of qualified personnel to be a material factor in its business. If demand for oil field services were to increase rapidly, retention of qualified people might become more difficult without significant increases in compensation.

PROPERTIES

Diamond Offshore owns an 18,000 square foot building and 20 acres of land in New Iberia, Louisiana used for its offshore drilling warehouse and storage facility, a 13,000 square foot building and five acres of land in Aberdeen, Scotland used in connection with its North Sea operations, a 15,000 square foot building and 10 acres of land in Alice, Texas for its land drilling office, warehouse and storage facility, six acres of land near Houston, Texas used as a warehouse facility and an eight-story office building located at 15415 Katy Freeway, Houston, Texas, where Diamond Offshore currently has its corporate headquarters in approximately 60,000 square feet of such building. Diamond Offshore leases approximately 29,000 square feet of office space in downtown Houston and various office, warehouse and storage facilities and lots in Louisiana, The Netherlands, the United Kingdom, Australia, India, Indonesia, Singapore and Brazil to support its offshore drilling operations.

In February 1996, Diamond Offshore purchased for approximately $8.2 million the eight-story building containing approximately 182,000 net rentable square feet on approximately 6.2 acres in which it had leased office space for its corporate headquarters. A portion of the building is currently occupied by other tenants under leases which expire through 2005. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Other."

LEGAL PROCEEDINGS

Various claims have been filed against Diamond Offshore in the ordinary course of business, particularly claims alleging personal injuries. Management believes that Diamond Offshore has established adequate reserves on its books for any liabilities that may reasonably be expected to result from these claims. In the opinion of management, no pending or threatened claims, actions or proceedings against Diamond Offshore are expected to have a material adverse effect on Diamond Offshore's financial position or results of operations.

MANAGEMENT

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

The table below sets forth certain information with respect to each person or entity known by Diamond Offshore to be the beneficial owner of more than 5% of Diamond Offshore Common Stock as of the Effective Time (based upon beneficial ownership of Diamond Offshore Common Stock, with respect to Loews, as of March 28, 1996 and Arethusa Common Stock, with respect to Alphee and Ratos, as of April 2, 1996).

TITLE OF CLASS	NAME AND ADDRESS OF BENEFICIAL OWNER	AMOUNT AND NATURE OF BENEFICIAL OWNERSHIP	PERCENT OF CLASS
Common Stock	Loews Corporation 667 Madison Avenue New York, N.Y. 10021-8087	35,050,000	51.6%
Common Stock	Alphee S.A. 11, Avenue de la Gare P.O. Box 2255 L-1022 Luxembourg	4,708,248	6.9%
Common Stock	Forvaltnings AB Ratos Drottninggatan 2 P.O. Box 1661, S-111 96 Stockholm, Sweden	3,667,207	5.4%

SECURITY OWNERSHIP OF MANAGEMENT AND DIRECTORS

The following table shows the amount and nature of beneficial ownership of Diamond Offshore Common Stock and Loews common stock beneficially owned by each director of Diamond Offshore, each Named Executive Officer of Diamond Offshore and all directors and officers of Diamond Offshore as a group, as of March 28, 1996. Directors and executive officers of Diamond Offshore individually and as a group own less than 1% of equity securities of Diamond Offshore, Loews or any subsidiary of Diamond Offshore. Except as otherwise noted, the named beneficial owner has sole voting power and sole investment power with respect to the number(s) of shares shown below.

NAME OF BENEFICIAL OWNER	DIAMOND OFFSHORE COMMON STOCK	LOEWS COMMON STOCK
James S. Tisch	0	80,000(1)
Herbert C. Hofmann	1,000(2)	400(2)
David M. Ifshin	0	0
Robert E. Rose	2,100(3)	0
Raymond S. Troubh	2,500	5,000
Lawrence R. Dickerson	500(3)	200
Ronald C. Johnson(4)	0	0
Thomas P. Richards	6,000(5)	0
David W. Williams	100	0
Richard L. Lionberger	0	0
All Directors and Executive Officers as a Group	12,300	85,950

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(1) In addition, 58,000 shares of Loews common stock are held by a charitable foundation as to which Mr. Tisch has shared voting and investment power.

(2) In addition, 350 shares of Loews common stock and 300 shares of Diamond Offshore Common Stock are owned by Mr. Hofmann's son, as to which shares Mr. Hofmann disclaims any beneficial ownership.

(3) Voting power and investment power with respect to shares listed with Mr. Rose and Mr. Dickerson are shared with each such individual's spouse.

(4) Mr. Johnson ceased to be an executive officer of Diamond Offshore in March 1996.

(5) The number of shares shown includes 4,000 shares owned by Richards Brothers Company, a Texas corporation, of which all non-voting common stock is owned by the children of Mr. Richards, and as to which Mr. Richards disclaims any beneficial ownership.

DIRECTORS

Diamond Offshore's Board of Directors presently consists of five directors. The directors are James S. Tisch, Herbert C. Hofmann, David M. Ifshin, Robert E. Rose and Raymond S. Troubh. Two of such directors, Mr. Troubh and Mr. Ifshin, are not directors, officers or employees of Loews or officers or employees of Diamond Offshore. All directors are elected annually to serve until the next annual meeting of stockholders and until their successors are duly elected and qualified. Each of the five directors is serving a term of one year to expire at the 1997 annual meeting of stockholders and until his successor is elected and qualifies or until his earlier death, resignation, disqualification or removal from office. Information with respect to the current directors of Diamond Offshore is set forth below.

NAME	POSITION	AGE AS OF JANUARY 31, 1996	DIRECTOR SINCE
James S. Tisch(1)........	Chairman of the Board	43	1989
Herbert C. Hofmann(1)....	Director	53	1992
David M. Ifshin(2).......	Director	47	1995
Robert E. Rose(1)........	Director, President and Chief Executive Officer	57	1989
Raymond S. Troubh(2).....	Director	69	1995

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(1) Member, Executive Committee of the Board of Directors.

(2) Member, Audit Committee of the Board of Directors.

James S. Tisch has served as the Chairman of the Board since 1995 and as a director of Diamond Offshore since June 1989. Mr. Tisch has served as President and Chief Operating Officer of Loews, a diversified holding company, since 1994 and prior thereto served as Executive Vice President of Loews for more than five years. Mr. Tisch, a director of Loews since 1986, also serves as a director of CNA Financial Corporation, an 84% owned subsidiary of Loews, and Gillett Holdings, Inc.

Herbert C. Hofmann has served as a director of Diamond Offshore since January 1992. Mr. Hofmann has served as Senior Vice President of Loews since January 1992, and prior thereto served as Vice President -- Operations Planning of Loews for more than five years. He has served as President and Chief Executive Officer of Bulova Corporation, a 97% owned subsidiary of Loews since August 1989, and as Chief Operating Officer of Bulova Corporation prior thereto. Bulova Corporation distributes and sells watches and clocks.

David M. Ifshin has served as a director of Diamond Offshore since November 1995. Mr. Ifshin currently holds several professional positions. Since 1993, he has served as a Senior Advisor of Galway Partners, Senior Vice President of Cassidy Associates, and as partner in the law firm Ifshin & Friedman. Between 1983 and 1993, Mr. Ifshin served as a Managing Director of Prudential Securities, Inc., Senior Vice President and Managing Director of Kemper Securities (Prescott, Ball & Turben), Director, Washington, Capital Markets Office of E.F. Hutton & Company, Inc. and a partner with the law firm of Manatt, Phelps, Rothenberg & Phillips.

Robert E. Rose has served as President and Chief Executive Officer of Diamond Offshore and as a director since June 1989.

Raymond S. Troubh has served as a director of Diamond Offshore since November 1995. Mr. Troubh is a financial consultant in New York City and a former Governor of the American Stock Exchange. For the past five years, Mr. Troubh has been the principal of Raymond Troubh & Company. Mr. Troubh also serves as a director of ADT Limited, America West Airlines, Inc., Applied Power Inc., ARIAD Pharmaceuticals, Inc., Becton, Dickinson and Company, Benson Eyecare Corporation, Foundation Health Corporation, General

American Investors Company, Manville Corporation, Olsten Corporation, Petrie Stores Corporation, Riverwood International Corporation, Time Warner Inc., Triarc Companies, Inc., and WHX Corporation.

DIRECTOR COMPENSATION. Directors who are employees of Diamond Offshore are not paid any fees or additional compensation for service as members of the Board of Directors or any committee thereof. The annual retainer payable to directors of Diamond Offshore who are not employees of Diamond Offshore or any of its subsidiaries or affiliated companies, for services as directors, is $20,000 per annum, payable quarterly. Each member of the Audit Committee of the Board of Directors of Diamond Offshore receives a retainer of $2,500 per annum, payable quarterly, and each director of Diamond Offshore who is not an employee of Diamond Offshore or any of its subsidiaries or affiliated companies is paid a fee of $1,000 for attendance at each meeting of the Board of Directors and of the Audit Committee thereof in addition to the reasonable costs and expenses incurred by such directors in relation to their services as such.

BOARD OF DIRECTORS AND COMMITTEES. Diamond Offshore's Board of Directors has five members, and the Board has two standing committees. Further information concerning the Board's standing committees appears below.

EXECUTIVE COMMITTEE. The Executive Committee of the Board of Directors consists of three members, Mr. Tisch, Mr. Hofmann and Mr. Rose. The Executive Committee has all the powers and exercises all the duties of the Board of Directors in the management of the business of Diamond Offshore that may lawfully be delegated to it by the Board of Directors. These powers and duties include, among other things, declaring a dividend, authorizing the issuance of stock, recommending to stockholders mergers or a sale of substantially all of the assets of Diamond Offshore, providing advice and counsel to management of Diamond Offshore, reviewing management's recommendations for significant changes to the organizational structure of Diamond Offshore and recommending changes to the Board of Directors.

AUDIT COMMITTEE. The Audit Committee of the Board of Directors consists of two members, Mr. Ifshin and Mr. Troubh. The Audit Committee reviews and reports to the Board of Directors on the scope and results of audits by Diamond Offshore's independent auditors. See "-- Certain Relationships and Related Transactions -- Services Agreement." It recommends a firm of certified public accountants to serve as auditors for Diamond Offshore, subject to nomination by the Board of Directors and election by the stockholders, authorizes all audit and other professional services rendered by the auditor and periodically reviews the independence of the auditor. Membership on the Audit Committee is restricted to directors independent of management and free from any relationship that, in the opinion of the Board of Directors, would interfere with the exercise of independent judgment as a committee member. Directors who are affiliates of Diamond Offshore or officers or employees of Diamond Offshore or its subsidiaries or its affiliates are not qualified for Audit Committee membership.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION. During Diamond Offshore's fiscal year ended December 31, 1995, Diamond Offshore had no compensation committee or other committee of the Board of Directors performing similar functions. Decisions concerning compensation of executive officers were made during such fiscal year by persons who were members of Diamond Offshore's Board of Directors, including Robert E. Rose, an executive officer of Diamond Offshore.

NOMINATING COMMITTEE. During Diamond Offshore's fiscal year ended December 31, 1995, Diamond Offshore had no nominating committee or other committee of the Board of Directors performing similar functions.

EXECUTIVE OFFICER TENURE AND IDENTIFICATION

The executive officers of Diamond Offshore are elected annually by the Board of Directors to serve until the next annual meeting of the Board of Directors and until their successors are duly elected and qualified, or until their earlier death, resignation, disqualification or removal from office. Information with respect to the current executive officers of Diamond Offshore is set forth below.

NAME	AGE AS OF JANUARY 31, 1996	POSITION
Robert E. Rose..............	57	President, Chief Executive Officer and Director
Lawrence R. Dickerson.......	43	Senior Vice President and Chief Financial Officer
Thomas P. Richards..........	52	Senior Vice President -- Worldwide Operations
David W. Williams...........	38	Senior Vice President -- Contracts and Marketing
Richard L. Lionberger.......	45	Vice President, General Counsel and Secretary
Gary T. Krenek..............	37	Controller

Robert E. Rose has served as President and Chief Executive Officer of Diamond Offshore and as a director since June 1989.

Lawrence R. Dickerson has served as Senior Vice President of Diamond Offshore since April 1993 and has served as a Vice President and the Chief Financial Officer of Diamond Offshore since June 1989.

Thomas P. Richards has served as Senior Vice President of Diamond Offshore since September 1990. Since March 1996, Mr. Richards has been in charge of worldwide operations, and prior thereto, since March 1993, Mr. Richards was in charge of domestic operations. From 1990 to 1993 Mr. Richards was in charge of land operations.

David W. Williams has served as Senior Vice President of Diamond Offshore since December 1994 and was a Marketing Vice President between February 1992 and May 1994. Mr. Williams was employed by Noble Drilling Corporation, an offshore contract drilling company, from May 1994 through December 1994 as Vice President of Marketing. Mr. Williams worked in marketing positions at Odeco, an offshore contract drilling company, from 1990 to February 1992.

Richard L. Lionberger has served as Vice President, General Counsel and Secretary of Diamond Offshore since February 1992. Mr. Lionberger was engaged in the private practice of law from 1985 to 1992, principally as the owner of Lionberger & Associates, and was counsel for Diamond Offshore during that period.

Gary T. Krenek has served as Controller of Diamond Offshore since February 1992 and was Accounting Manager of Diamond Offshore since 1989.

EXECUTIVE COMPENSATION

The following table shows for the years ended December 31, 1995 and 1994 the cash compensation paid by Diamond Offshore, and a summary of certain other compensation paid or accrued for such year, to its Chief Executive Officer and each of Diamond Offshore's four other most highly compensated executive officers (the "Named Executive Officers") for service in all capacities with Diamond Offshore and its subsidiaries.

SUMMARY COMPENSATION TABLE

NAME AND PRINCIPAL POSITION	YEAR	ANNUAL COMPENSATION(1)(2) SALARY	BONUS	ALL OTHER COMPENSATION(3)
Robert E. Rose	1995	$390,000	$230,000	$ 6,075
President and Chief Executive Officer	1994	363,315	--	6,075
Thomas P. Richards(4)	1995	210,128	60,000	5,913
Senior Vice President -- Domestic Operations	1994	199,615	--	5,913
Lawrence R. Dickerson	1995	190,000	107,000	5,727
Senior Vice President and Chief Financial Officer	1994	168,000	--	5,727
Ronald C. Johnson(5)	1995	178,928	--	5,913
Senior Vice President -- International Operations	1994	182,902	--	5,913
David W. Williams	1995	175,000	102,500	5,691
Senior Vice President -- Contracts and Marketing				
Richard L. Lionberger	1994	134,842	--	5,159
Vice President, General Counsel and Secretary				

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(1) Amounts exclude perquisites and other personal benefits because such compensation did not exceed the lesser or $50,000 and 10% of the total annual salary reported for each Named Executive Officer.

(2) Amounts include salary and bonus earned, as well as earned but deferred, by the Named Executive Officers.

(3) The amounts shown include (i) Diamond Offshore's contributions under the Retirement Plan referred to below for the years shown on behalf of the Named Executive Officers, as follows: Mr. Rose, 1994 and 1995 -- $5,625; Mr. Richards, 1994 and 1995 -- $5,625; Mr. Dickerson, 1994 and 1995 -- $5,625; Mr. Johnson, 1994 and 1995 -- $5,625; Mr. Williams, 1995 -- $5,625; and Mr. Lionberger, 1994 -- $5,057; and (ii) the term portion of the life insurance premiums paid by Diamond Offshore for the years shown on behalf of the Named Executive Officers, as follows: Mr. Rose, 1994 and 1995 -- $450; Mr. Richards, 1994 and 1995 -- $288; Mr. Dickerson, 1994 and 1995 -- $102; Mr. Johnson, 1994 and 1995 -- $288; Mr. Williams, 1995 -- $66; and Mr. Lionberger, 1994 -- $102.

(4) Mr. Richards became Senior Vice President -- Worldwide Operations in March 1996.

(5) Mr. Johnson ceased to be an executive officer of Diamond Offshore in March 1996.

Diamond Offshore maintains a defined contribution plan (the "Retirement Plan") designed to qualify under Section 401(k) of the Internal Revenue Code of 1986, as amended (the "Code"), pursuant to which Diamond Offshore contributes 3.75% of the participant's base and overtime salary subject to limitations of eligible salary. Employees are vested in all contributions as made.

In addition Diamond Offshore expects to adopt an Executive Deferred Compensation Plan pursuant to which Diamond Offshore will contribute any portion of the 3.75% of the base salary contribution to the Retirement Plan that cannot be contributed to the Retirement Plan because of the limitations of Sections 401(a)(17) and 415 of the Code. Additionally, the plan is expected to provide that participants may defer a percentage of their salary and bonuses pursuant to such plan. Participants in the plan will be highly compensated officers of Diamond Offshore and will be fully vested in all amounts paid into the plan. The plan is anticipated to be effective in 1996 and there is proposed to be a make-up Diamond Offshore contribution for any amounts that were not contributed to the Retirement Plan for 1994 and 1995 because of the Code limitations described above.

ANNUAL CASH BONUS INCENTIVES

Bonuses were awarded under the Diamond Offshore Management Bonus Program, which is intended to provide a means whereby certain selected officers and key employees of Diamond Offshore may develop a sense of proprietorship and personal involvement in the development and financial success of Diamond Offshore, and encourage the participants to remain with and devote their best efforts to the business of Diamond Offshore, thereby advancing the interests of Diamond Offshore and its stockholders. At the beginning of each year, the Executive Committee of the Diamond Offshore Board of Directors establishes a bonus pool (the "Annual Bonus Pool") equal to (i) a percentage (the "Applicable Percentage") ranging from 10% to 35% (as determined by the Executive Committee based on such committee's evaluation of Diamond Offshore during the prior year (the "performance year") relative to peer companies, and the performance of Diamond Offshore's share price and extraordinary events during the performance year) of the total salaries of all participants for the performance year, divided by (ii) the arithmetical average of (x) Diamond Offshore's cash flow plus capital expenses for the year prior to the performance year and (y) cash flow plus capital expenses as budgeted for the performance year, multiplied by (iii) actual cash flow plus capital expenses for such performance year. The Executive Committee establishes the bonus payout from the Annual Bonus Pool to each participant (not to exceed 30% of such participant's eligible salary) based upon corporate, group or individual performance, or a combination thereof, or such other subjective criteria as the Executive Committee may determine to be appropriate. The bonuses are payable in annual installments (50%, 25% and 25%) over the three calendar year period following the performance year and, with certain exceptions, are forfeited if not paid prior to termination of employment. In addition, certain executive officers, including Mr. Rose, received an additional bonus, to recognize the performance of certain executive officers of Diamond Offshore in consummating the Diamond Offshore Initial Public Offering. For performance year 1995, the Executive Committee elected to pay bonuses under the Diamond Offshore Management Bonus Program aggregating approximately $685,000 although the Annual Bonus Pool, if calculated based on the formula set forth in the Diamond Offshore Management Bonus Program and assuming the maximum permissible Applicable Percentage, would have been approximately $1.2 million. This deviation was based on the Executive Committee's subjective evaluation of the overall favorable performance of the eligible officers in 1995, particularly in connection with the successful completion of the Diamond Offshore Initial Public Offering.

EMPLOYMENT AGREEMENTS AND SEVERANCE AND CHANGE IN CONTROL ARRANGEMENTS

Diamond Offshore and Robert E. Rose entered into and subsequently extended an agreement, dated November 1, 1992 (the "Employment Agreement"), providing for, among other things, the employment of Mr. Rose as the President and Chief Executive Officer of Diamond Offshore until December 31, 1998. Mr. Rose currently receives a salary at an annual rate of $500,000, subject to such increases as the Board of Directors of Diamond Offshore may from time to time determine. Pursuant to the Employment Agreement, Mr. Rose and Diamond Offshore agree that during the term of Mr. Rose's employment under the Employment Agreement and for a period of one year immediately following termination of such employment by Diamond Offshore for cause, Mr. Rose will not engage in any other business which is in competition with Diamond Offshore without written consent from Diamond Offshore. The Employment Agreement provides that, for a 120-day period after consummation of a Change of Control (as defined in the Employment Agreement), Mr. Rose has the right to terminate his employment and Diamond Offshore would be obligated to continue to compensate him for a three-year period.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

CONTROLLING STOCKHOLDER. As of the date of this Prospectus, Loews beneficially owns approximately 51.6% of the outstanding shares of Diamond Offshore Common Stock. Diamond Offshore understands that Loews has no current intention of disposing of any of the shares of Diamond Offshore Common Stock owned by it. Loews entered into an agreement, dated October 10, 1995, with the underwriters of the Diamond Offshore Initial Public Offering providing that Loews will not, and will not permit its affiliates (other than Diamond Offshore) to offer, sell, contract to sell, pledge or otherwise dispose of, directly or indirectly, any shares of Diamond Offshore Common Stock or securities convertible into or exchangeable or exercisable for any shares of Diamond Offshore Common Stock for a period of one year after the date of such agreement, without the prior written consent of CS First Boston. After such date such shares may be sold (i) in accordance with Rule 144 promulgated under the Securities Act, (ii) in private offerings or (iii) upon registration under the Securities Act without regard to the volume limitations of Rule 144.

In general, under Rule 144 as currently in effect, Loews will be entitled to sell on the open market in broker's transactions within any three-month period a number of shares that does not exceed the greater of (i) 1% of the then outstanding shares of Diamond Offshore Common Stock (currently 678,933 shares) or (ii) the average weekly trading volume in Diamond Offshore Common Stock on the open market during the four calendar weeks preceding such sale.

Shares held by Loews may be freely sold if registered under the Securities Act. Diamond Offshore has agreed to use its best efforts, upon request by Loews, to register under the Securities Act any or all shares of Diamond Offshore Common Stock held by Loews and, under certain conditions, when shares of Diamond Offshore Common Stock are registered by Diamond Offshore. See "-- Transactions Between Diamond Offshore and Loews -- Registration Rights Agreement."

Loews incorporated Diamond Offshore as a wholly owned subsidiary in 1989 and owned all of the outstanding shares of Diamond Offshore Common Stock since that time until the consummation of the Diamond Offshore Initial Public Offering. Proceeds from the Diamond Offshore Initial Public Offering were used to repay all of Diamond Offshore's then outstanding indebtedness to Loews of $336.2 million and the remainder of such proceeds was used to pay Loews a special dividend of $2.1 million. By virtue of its ownership of a majority of the outstanding shares of Diamond Offshore Common Stock, Loews is in a position to control actions that require the consent of stockholders, including the election of directors, payment of dividends, amendment of Diamond Offshore's Restated Certificate of Incorporation and mergers or a sale of substantially all the assets of Diamond Offshore. In addition, certain officers, directors or employees of Loews serve on Diamond Offshore's Board of Directors. See "-- Directors." Loews and Diamond Offshore have entered into various agreements relating to the ongoing relationship between Loews and Diamond Offshore. See "-- Transactions Between Diamond Offshore and Loews."

Loews is a diversified holding company, incorporated under the laws of Delaware in 1969. Loews, through its subsidiaries, is engaged in a variety of distinct businesses, including the production and sale of cigarettes; the operation of hotels; through Diamond Offshore, the operation of oil and gas drilling rigs; through its approximately 84% ownership of CNA Financial Corporation, property, casualty and life insurance; and through its approximately 97% ownership of Bulova Corporation, the distribution and sale of watches and clocks. In 1995, the consolidated revenues of Loews were approximately $18.7 billion. The address of Loews is 667 Madison Avenue, New York, New York 10021-8087.

TRANSACTIONS BETWEEN DIAMOND OFFSHORE AND LOEWS. Diamond Offshore and Loews have entered into intercompany transactions and agreements incident to their respective businesses and may enter into material transactions and agreements from time to time. In connection with the Diamond Offshore Initial Public Offering, Diamond Offshore and Loews entered into agreements pursuant to which certain management, administrative and other services are provided by Loews to Diamond Offshore and certain other obligations were assumed by the parties. These agreements were not the result of arm's length negotiations between the parties.

The following description of certain terms of certain agreements, arrangements and transactions between Diamond Offshore and Loews accurately summarizes those terms thereof considered by Diamond Offshore to be material to a prospective investor in the Offered Shares and is qualified in its entirety by reference to the complete agreements filed as exhibits to the Registration Statement or, in the case of the Tax Sharing Agreement, the registration statement filed in connection with the Diamond Offshore Initial Public Offering.

Services Agreement. Diamond Offshore and Loews entered into a Services Agreement effective upon consummation of the Diamond Offshore Initial Public Offering (the "Services Agreement") pursuant to which Loews agreed to continue to perform certain administrative and technical services on behalf of Diamond Offshore. Such services include personnel, telecommunications, purchasing, internal auditing, accounting, data processing and cash management services, in addition to advice and assistance with respect to preparation of tax returns and obtaining insurance. Under the Services Agreement, Diamond Offshore is to reimburse Loews for (i) allocated personnel costs (such as wages, salaries, employee benefits and payroll taxes) of the Loews personnel actually providing such services and (ii) all out-of-pocket expenses related to the provision of such services. The Services Agreement may be terminated at Diamond Offshore's option upon 30 days' notice to Loews and at the option of Loews upon six months' notice to Diamond Offshore. In addition, Diamond Offshore has agreed to indemnify and hold harmless Loews for all claims and damages arising from the provision of services by Loews under the Services Agreement, unless due to the gross negligence or willful misconduct of Loews.

Tax Sharing Agreement. Diamond Offshore has been and will be included in the consolidated U.S. federal income tax returns filed by Loews with respect to all periods in which it was a wholly owned subsidiary of Loews. Prior to 1992, Diamond Offshore's profitable subsidiaries were allocated a share of the Loews consolidated federal income tax expense and no benefit was given to any of Diamond Offshore's subsidiaries generating taxable losses. Effective January 1, 1992, a Tax Sharing Agreement (the "Tax Sharing Agreement") with Loews was adopted to allow for the recognition of expenses and benefits related to taxable income or loss as if Diamond Offshore and its subsidiaries filed a separate consolidated return. Upon completion of the Diamond Offshore Initial Public Offering, Diamond Offshore was owned less than 80% by Loews and was therefore removed from the consolidated federal income tax return of Loews, which triggered the automatic termination of the Tax Sharing Agreement. Pursuant to a termination and settlement agreement entered into effective upon consummation of the Diamond Offshore Initial Public Offering, Diamond Offshore and Loews agreed to offset the net amount owed by Loews to Diamond Offshore as a result of the termination of the Tax Sharing Agreement against Diamond Offshore's notes payable to Loews. Such offset constituted a full settlement and satisfaction of Loews's payment obligations to Diamond Offshore arising upon termination of the Tax Sharing Agreement.

Registration Rights Agreement. Under a Registration Rights Agreement (the "Registration Rights Agreement") between Diamond Offshore and Loews, Diamond Offshore will file, upon the request of Loews, one or more registration statements under the Securities Act, subject to a maximum of three such requests, in order to permit Loews to offer and sell any Diamond Offshore Common Stock that Loews may hold. Subject to the restrictions described under "-- Controlling Stockholder" and "-- Registration Rights of Selling Stockholders," Loews may exercise these rights at any time, provided shares comprising at least 5% of the outstanding Diamond Offshore Common Stock are to be sold. Loews will bear the costs of any such registered offering, including any underwriting commissions relating to shares it sells in any such offering, any related transfer taxes and the costs of complying with non-U.S. securities laws, and any fees and expenses of separate counsel and accountants retained by Loews. The Registration Rights Agreement will terminate at such time as Loews's percentage of ownership of the outstanding Diamond Offshore Common Stock falls below 15%. Diamond Offshore has the right to require Loews to delay any exercise by Loews of its rights to require registration and other actions for a period of up to 90 days if, in the judgment of Diamond Offshore, any offering by Diamond Offshore then being conducted or about to be conducted would be adversely affected.

Subject to certain conditions, Diamond Offshore has also granted Loews the right to include its Diamond Offshore Common Stock in any registration statements covering offerings of Diamond Offshore Common Stock by Diamond Offshore, and Diamond Offshore will pay all costs of such offerings other than underwriting commissions and transfer taxes attributable to the shares sold on behalf of Loews. There is no limitation on the number of times that Loews may exercise this right with respect to registration statements relating to Diamond Offshore Common Stock. Diamond Offshore will indemnify Loews, and Loews will indemnify Diamond Offshore, against certain liabilities in respect of any registration statement or offering covered by the Registration Rights Agreement. The rights of Loews under the Registration Rights Agreement are transferable to affiliates of Loews.

TRANSACTIONS BETWEEN DIAMOND OFFSHORE AND THE SELLING STOCKHOLDERS. Pursuant to the Shareholders Agreement, each of Alphee and Ratos agreed to vote all shares of Arethusa Common Stock it owned in favor of the approval and adoption of the Amalgamation Agreement and in favor of the ratification of the Plan of Acquisition and the Fee Agreement, and against any change in a majority of the persons who constituted the Board of Directors of Arethusa. Under the Shareholders Agreement, each of Alphee and Ratos irrevocably appointed Acquisition Sub and its officers, agents and nominees, with full power of substitution, as proxy to so vote its shares of Arethusa Common Stock. Also pursuant to the Shareholders Agreement, each of Alphee and Ratos agreed to vote all shares of Arethusa Common Stock with respect to which it held a proxy for such purpose in favor of the ratification of the Fee Agreement and each of the actions that were to be taken by Arethusa pursuant thereto. In addition, Diamond Offshore granted the Selling Stockholders certain registration rights pursuant to the Shareholders Agreement. See "-- Registration Rights of Selling Stockholders."

REGISTRATION RIGHTS OF SELLING STOCKHOLDERS. Pursuant to the Plan of Acquisition and the Shareholders Agreement, Diamond Offshore agreed for the benefit of Alphee and Ratos to use its best efforts (i) to cause the Registration Statement to be filed and declared effective at the earliest practicable date and to remain effective until the Effective Time, to include this Prospectus intended to permit each of Alphee and Ratos to sell after the Effective Time without restriction, at its election, all or part of the shares of Diamond Offshore Common Stock received by such person in connection with the Acquisition and (ii) to maintain the continued effectiveness of the Registration Statement with respect to such shares, including this Prospectus for use by such persons, for a period of two years from the Effective Time, plus the aggregate number of days in all Suspension Periods (as such term is defined in the Shareholders Agreement) after the Effective Time (the "Required Period").

During the Required Period and assuming continued effectiveness of the registration statement covering their shares of Diamond Offshore Common Stock, Alphee and Ratos may sell such shares in or outside the United States through underwriters or dealers, through agents, or directly to one or more purchasers. The distribution of the shares of Diamond Offshore Common Stock offered by Alphee or Ratos may be effected from time to time in one or more transactions (which may involve crosses or block transactions) (i) on the NYSE (or on such other national stock exchanges on which the Diamond Offshore Common Stock may be listed from time to time) in transactions which may include special offerings, exchange distributions and/or secondary distributions pursuant to and in accordance with the rules of such exchanges, including sales to underwriters who will acquire the Offered Shares for their own account and resell them in one or more transactions or through brokers, acting as principal or agent, (ii) in the over-the-counter market, including sales through brokers, acting as principal or agent, (iii) in transactions other than on such exchanges or in the over-the-counter market, or a combination of such transactions, including sales through brokers, acting as principal or agent, (iv) through the issuance of securities by issuers other than Diamond Offshore convertible into, exchangeable for, or payable in such shares (whether such securities are listed on a national securities exchange or otherwise) or (v) through the writing of options on the shares (whether such options are listed on an options exchange or otherwise). Any such transactions may be effected at market prices prevailing at the time of sale, at prices related to such prevailing market prices, at negotiated prices or at fixed prices. Diamond Offshore has the right to require each of Alphee and Ratos to suspend use of any resale prospectus for any period (not to exceed 20 days in any one instance and, when combined with any other such periods, 60 days in any 12-month period) determined by Diamond Offshore if Diamond Offshore would, in the opinion of Diamond Offshore's counsel, be required to disclose in such prospectus information not otherwise then required by law to be publicly disclosed and, in the judgment of the Board of Directors of Diamond Offshore, such disclosure might adversely affect Diamond Offshore or any material business transaction or negotiation in which Diamond Offshore is then engaged.

Each of Alphee and Ratos will have the right to elect during the 180-day period beginning on the Effective Time (the "Initial Standstill Period") to proceed with one, and only one, and thereafter such shareholders shall have the right to proceed with one, and only one (for both such shareholders collectively) underwritten offering of their shares of Diamond Offshore Common Stock pursuant to the registration statement covering such shares, but if during the Initial Standstill Period, only one underwritten offering of Diamond Offshore Common Stock is effected pursuant to such registration statement, then each of Alphee and Ratos will have the right to proceed with one, and only one, underwritten offering thereafter until the end of the Required Period. During the Initial Standstill Period, and thereafter during the period commencing 14 days prior to the commencement of, and continuing through the completion of the public distribution of, shares of Diamond Offshore Common Stock in an underwritten public offering by Alphee or Ratos, Diamond Offshore and Loews have agreed not to effect any public sale or distribution of Diamond Offshore Common Stock, or any securities convertible into such stock, subject to certain exceptions. Diamond Offshore will pay the costs of all such underwritten offerings other than (i) underwriting commissions attributable to the shares of Diamond Offshore Common Stock sold on behalf of Alphee or Ratos, (ii) out-of-pocket costs incurred in connection with "road shows" and other marketing support involving members of Diamond Offshore's management, (iii) costs of any special audits, (iv) fees and expenses of underwriter's counsel and (v) any out-of-pocket expense (including fees and expenses of counsel) of Alphee or Ratos.

Subject to certain conditions, Diamond Offshore also granted each of Alphee and Ratos the right to include their shares of Diamond Offshore Common Stock in any registration statements covering offerings of Diamond Offshore Common Stock filed during the Required Period by Diamond Offshore for its own account or for holders of Diamond Offshore Common Stock other than Alphee or Ratos, and Diamond Offshore will pay all costs of such offerings other than underwriting commissions attributable to any shares sold on behalf of Alphee or Ratos. There is no limitation on the number of times that Alphee and Ratos may exercise this right during the Required Period with respect to registration statements relating to Diamond Offshore Common Stock.

Diamond Offshore will indemnify Alphee and Ratos, and each of Alphee and Ratos, severally, will indemnify Diamond Offshore, against certain liabilities in respect of any registration statement or resale prospectus covering offerings by Alphee or Ratos, as applicable, of shares of Diamond Offshore Common Stock. The rights of Alphee and Ratos under the Shareholders Agreement with respect to registration rights are transferable by each of Alphee and Ratos to their respective affiliates, but are not otherwise transferable without the prior written consent of Diamond Offshore.

STOCK OPTION PLANS

Pursuant to the Amalgamation Agreement, at the Effective Time, each Arethusa Option was assumed by Diamond Offshore and now constitutes a fully vested and currently exercisable option to acquire, on substantially the same terms and conditions (modified as described below) as were applicable under the Arethusa Stock Option Plans, the same number of shares of Diamond Offshore Common Stock as the holder thereof would have been entitled to receive pursuant to the Amalgamation had such holder exercised such Arethusa Option in full immediately prior to the Effective Time, at a price per share equal to the per share exercise price of the Arethusa Option being assumed divided by the Amalgamation Ratio. No fractional shares of Diamond Offshore Common Stock will be issued in connection with the exercise of any such Arethusa Option. Fractions of Diamond Offshore Common Stock resulting from any such exercise will be paid in cash based upon the market value of a share of Diamond Offshore Common Stock on the date of exercise. Except as otherwise described above, the Arethusa Stock Option Plans terminated as of the Effective Time. Diamond Offshore has filed with the Commission a registration statement on Form S-8 with respect to the shares of Diamond Offshore Common Stock subject to such Arethusa Options, as so amended by Diamond Offshore.

PRICE RANGE OF DIAMOND OFFSHORE COMMON STOCK

Diamond Offshore Common Stock is listed on the NYSE under the symbol "DO." The following table shows for the periods indicated the high and low closing prices of Diamond Offshore Common Stock as reported by the NYSE. No information is provided for Diamond Offshore Common Stock prior to the date of the Diamond Offshore Initial Public Offering.

	FISCAL YEAR ENDED DECEMBER 31,			
	1996		1995	
	HIGH	LOW	HIGH	LOW
Quarter Ended				
March 31	43 3/8	33 3/8	--	--
June 30(1)	50 1/2	43 1/2	--	--
December 31	--	--	34	24

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(1) As of April 11, 1996.

On April 11, 1996, the closing price of the Diamond Offshore Common Stock, as reported by the NYSE, was $50 1/2 per share. As of April 11, 1996, there were approximately 73 record holders, and approximately 1,400 beneficial holders, of Diamond Offshore Common Stock.

DESCRIPTION OF CAPITAL STOCK

The following description of certain terms of Diamond Offshore's capital stock accurately summarizes those terms considered by Diamond Offshore to be material to a prospective investor in the Offered Shares and is qualified in its entirety by reference to Diamond Offshore's Restated Certificate of Incorporation (the "Certificate"), a copy of which was included as an exhibit to the Registration Statement.

COMMON STOCK

The authorized capital stock of Diamond Offshore consists of 225,000,000 shares of capital stock, 200,000,000 of such shares being Diamond Offshore Common Stock, par value $0.01 per share. After giving effect to the issuance of shares of Diamond Offshore Common Stock in connection with the Acquisition (the exchange of each share of Arethusa Common Stock outstanding immediately prior to the Acquisition in consideration of 0.88 shares of Diamond Offshore Common Stock), there were 67,893,344 shares of Diamond Offshore Common Stock issued and outstanding, of which 8,375,455 shares were held by the Selling Stockholders. In addition, at the Effective Time, 1,000,000 shares of Diamond Offshore Common Stock were reserved for issuance upon the exercise of Arethusa Options assumed by Diamond Offshore.

Holders of Diamond Offshore Common Stock are entitled to one vote for each share held and are not entitled to cumulative voting for the purpose of electing directors and have no preemptive or similar right to subscribe for, or to purchase, any shares of Diamond Offshore Common Stock or other securities to be issued by Diamond Offshore in the future. Accordingly, the holders of more than 50% in voting power of the shares of Diamond Offshore Common Stock voting generally for the election of directors will be able to elect all of Diamond Offshore's directors. As described in "Management -- Certain Relationships and Related Transactions -- Controlling Stockholder," Loews beneficially owns approximately 51.6% of the outstanding shares of Diamond Offshore Common Stock and is in a position to control actions that require the consent of stockholders, including the election of directors, amendment of the Certificate and any mergers or any sale of substantially all of the assets of Diamond Offshore.

Holders of shares of Diamond Offshore Common Stock have no exchange, conversion or preemptive rights and such shares are not subject to redemption. All outstanding shares of Diamond Offshore Common Stock are duly authorized, validly issued, fully paid and non-assessable. Subject to the prior rights, if any, of holders of any outstanding class or series of capital stock having a preference in relation to Diamond Offshore Common Stock as to distributions upon the dissolution, liquidation and winding-up of Diamond Offshore and as to dividends, holders of Diamond Offshore Common Stock are entitled to share ratably in all assets of Diamond Offshore which remain after payment in full of all debts and liabilities of Diamond Offshore, and to receive ratably such dividends, if any, as may be declared by Diamond Offshore's Board of Directors from time to time out of funds and other property legally available therefor. See "Dividend Policy" and "Capitalization."

PREFERRED STOCK

The Board of Directors is authorized, without action by the holders of Diamond Offshore Common Stock, to issue up to 25,000,000 shares of preferred stock, $.01 par value (the "Preferred Stock"), in one or more series, to establish the number of shares to be included in each such series and to fix the designations, preferences, relative, participating, optional and other special rights of the shares of each such series and the qualifications, limitations and restrictions thereof. Such matters may include, among others, voting rights, conversion and exchange privileges, dividend rates, redemption rights, sinking fund provisions and liquidation rights that could be superior and prior to Diamond Offshore Common Stock.

The issuance of one or more series of the Preferred Stock could, under certain circumstances, adversely affect the voting power of the holders of Diamond Offshore Common Stock and could have the effect of discouraging or making more difficult any attempt by a person or group to effect a change in control of Diamond Offshore.

DELAWARE BUSINESS COMBINATION STATUTE

Diamond Offshore is a Delaware corporation and is subject to Section 203 ("Section 203") of the Delaware General Corporation Law (the "DGCL"). In general, Section 203 will prevent an "interested stockholder" (defined generally as a person owning 15% or more of a corporation's outstanding voting stock) of Diamond Offshore from engaging in a "business combination" (as therein defined) with Diamond Offshore for three years following the date such person became an interested stockholder, unless (i) before such person became an interested stockholder, the Board of Directors of Diamond Offshore approved the business combination in question, or the transaction which resulted in such person becoming an interested stockholder, (ii) upon consummation of the transaction that resulted in the interested stockholder becoming such, the interested stockholder owns at least 85% of the voting stock of Diamond Offshore outstanding at the time such transaction commenced (excluding stock held by directors who are also officers of Diamond Offshore and by employee stock plans that do not provide employees with rights to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer), or (iii) following the transaction in which such person became an interested stockholder, the business combination is approved by the Board of Directors of Diamond Offshore and authorized at a meeting of stockholders by the affirmative vote of the holders of not less than 66 2/3% of the outstanding voting stock of Diamond Offshore not owned by the interested stockholder. Under Section 203, the restrictions described above do not apply to certain business combinations proposed by an interested stockholder following the announcement (or notification) of one of certain extraordinary transactions involving Diamond Offshore and a person who had not been an interested stockholder during the preceding three years or who became an interested stockholder with the approval of Diamond Offshore's directors, and which transactions are approved or not opposed by a majority of the members of the Board of Directors then in office who were directors prior to any person becoming an interested stockholder during the previous three years or were recommended for election or elected to succeed such directors by a majority of such directors.

Section 203 does not apply to Loews because it has been more than three years since Loews became an interested stockholder.

POTENTIAL RESTRICTIONS ON SALES OF DIAMOND OFFSHORE COMMON STOCK TO NON-U.S. CITIZENS

Pursuant to recent amendments to United States maritime laws relating to sales of interests in and control of vessels owned by United States citizens to non-citizens, the Secretary of Transportation, acting through the United States Maritime Administration, has prior consent authority over certain transfers of Diamond Offshore's capital stock. See "Business -- Limitation on Ownership by Non-U.S. Citizens."

TRANSFER AGENT AND REGISTRAR

Chemical Mellon Shareholder Services, L.L.C., whose principal offices are located at 450 West 33rd Street, New York, New York 10001, acts as transfer agent and registrar for Diamond Offshore Common Stock.

PLAN OF DISTRIBUTION

Any distribution of the Offered Shares by the Selling Stockholders may be effected from time to time in one or more of the following transactions (which may involve crosses or block transactions): (i) on the NYSE (or on such other national stock exchanges on which the Diamond Offshore Common Stock may be listed from time to time) in transactions which may include special offerings, exchange distributions and/or secondary distributions pursuant to and in accordance with the rules of such exchanges, including sales to underwriters who will acquire the Offered Shares for their own account and resell them in one or more transactions or through brokers, acting as principal or agent, (ii) in the over-the-counter market, including sales through brokers, acting as principal or agent, (iii) in transactions other than on such exchanges or in the over-the-counter market, or a combination of such transactions, including sales through brokers, acting as principal or agent, (iv) through the issuance of securities by issuers other than Diamond Offshore convertible into, exchangeable for, or payable in such shares (whether such securities are listed on a national securities exchange or otherwise) or (v) through the writing of options on the shares (whether such options are listed on an options exchange or otherwise). Any such transactions may be effected at market prices prevailing at the time of sale, at prices related to such prevailing market prices, at negotiated prices or at fixed prices.

The Selling Stockholders and any such underwriters, brokers, dealers or agents, upon effecting the sale of the Offered Shares may be deemed "underwriters" as that term is defined by the Securities Act.

Underwriters participating in any offering made pursuant to this Prospectus (as amended or supplemented from time to time) may receive underwriting discounts and commissions, and discounts or concessions may be allowed or reallowed or paid to dealers, and brokers or agents participating in such transactions may receive brokerage or agent's commissions or fees.

In order to comply with the securities laws of certain states, if applicable, the Offered Shares will be sold in such jurisdictions only through registered or licensed brokers or dealers. In addition, in certain states the Offered Shares may not be sold unless the Offered Shares have been registered or qualified for sale in such state or any exemption from registration or qualification is available and complied with.

Pursuant to the Shareholders Agreement, Diamond Offshore agreed to cause the Registration Statement to include a resale prospectus that would permit the Selling Stockholders to sell the Offered Shares without restriction and to keep the Registration Statement continuously effective for the Required Period. Diamond Offshore has agreed to pay certain expenses in connection with such registration, including (1) all registration and filing fees, (2) fees and expenses of compliance with securities or blue sky laws (including reasonable fees and disbursements of counsel in connection with blue sky qualifications of the securities registered), (3) printing expenses, (4) internal expenses of Diamond Offshore (including, without limitation, all salaries and expenses of its officers and employees performing legal or accounting duties), (5) reasonable fees and disbursements of counsel for Diamond Offshore and customary fees and expenses for independent certified public accountants retained by Diamond Offshore (including the expenses of any comfort letters or costs associated with the delivery by independent certified public accountants of a comfort letter or comfort letters but excluding costs associated with special audits), (6) the reasonable fees and expenses of any special experts retained by Diamond Offshore in connection with such registration, (7) fees and expenses in connection with any review of underwriting arrangements by the National Association of Securities Dealers, Inc. including fees and expenses of any "qualified independent underwriter" in connection with an underwritten offering and (8) fees and disbursements of underwriters customarily paid by issuers or sellers of securities in connection with an underwritten offering. Diamond Offshore will not be responsible for any underwriting fees, discounts or commissions in connection with an underwritten offering or any out-of-pocket expenses (including counsel fees and expenses) of the Selling Stockholders or any fees and expenses of underwriters' counsel in connection with an underwritten offering. In addition, the Selling Stockholders have agreed to pay all costs of any special audits in connection with an underwritten offering and have agreed to pay, or in the case of an underwritten offering to cause the underwriters to pay, all out-of-pocket expenses of Diamond Offshore in connection with any domestic "road show" presentations. Diamond Offshore and the Selling Stockholders have agreed to indemnify each other and certain other persons against certain liabilities in connection with the offering of the Offered Shares including liabilities arising under the Securities Act. In connection with an underwritten offering, Diamond Offshore has agreed to indemnify any underwriter thereof and certain other persons to the same extent as provided with respect to the indemnification of the Selling Stockholder(s) if such underwriter agrees to indemnify Diamond Offshore to the same extent as provided with respect to the indemnification of Diamond Offshore by such Selling Stockholder(s). See "Management -- Certain Relationships and Related Transactions -- Registration Rights of Selling Stockholders."

LEGAL MATTERS

The validity of the shares of Diamond Offshore Common Stock offered hereby will be passed on for Diamond Offshore by Weil, Gotshal & Manges LLP, Houston, Texas.

EXPERTS

The consolidated financial statements of Diamond Offshore as of December 31, 1995 and 1994, and for each of the three years in the period ended December 31, 1995 included herein have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report appearing herein and are included in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

The consolidated financial statements of Arethusa as of September 30, 1995 and 1994, and for each of the three years in the period ended September 30, 1995 included in this Prospectus, have been audited by Arthur Andersen & Co., independent public accountants, as indicated in their reports with respect thereto, and are included herein in reliance upon the authority of said firm as experts in accounting and auditing.

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INDEPENDENT AUDITORS' REPORT

Board of Directors and Stockholders
Diamond Offshore Drilling, Inc. and Subsidiaries
Houston, Texas

We have audited the accompanying consolidated balance sheets of Diamond Offshore Drilling, Inc. and subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Diamond Offshore Drilling, Inc. and subsidiaries as of December 31, 1995 and 1994, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles.

Deloitte & Touche LLP
Houston, Texas

January 29, 1996
(February 13, 1996 as to Note 12)

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	DECEMBER 31, 1995	DECEMBER 31, 1994
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 10,306	$ 17,770
Short-term investments	5,041	4,926
Accounts receivable	74,496	57,804
Rig inventory and supplies	15,330	15,024
Prepaid expenses and other	10,601	3,970
Total current assets	115,774	99,494
DRILLING AND OTHER PROPERTY AND EQUIPMENT, LESS ACCUMULATED DEPRECIATION	502,278	488,664
Total assets	$ 618,052	$ 588,158
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 18,322	$ 13,596
Accrued liabilities	33,929	28,377
Total current liabilities	52,251	41,973
NOTES PAYABLE TO LOEWS	--	394,777
DEFERRED TAX LIABILITY	72,907	27,342
Total liabilities	125,158	464,092
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Preferred stock (par value $.01, 25,000,000 shares authorized, none issued and outstanding at December 31, 1995)	--	--
Common stock (par value $.01, 200,000,000 shares authorized, 50,000,000 shares issued and outstanding and par value $1.00, 1,000 shares authorized, 100 shares issued and outstanding at December 31, 1995 and 1994, respectively)	500	1
Additional paid-in capital	665,107	289,685
Accumulated deficit	(171,444)	(164,418)
Cumulative translation adjustment	(1,269)	(1,202)
Total stockholders' equity	492,894	124,066
Total liabilities and stockholders' equity	$ 618,052	$ 588,158

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
REVENUES	$336,584	$307,918	$288,069
OPERATING EXPENSES:			
Contract drilling	259,560	256,919	228,211
General administrative	13,857	11,993	11,785
Depreciation	52,865	55,366	46,819
Gain on sale of assets	(1,349)	(1,736)	(3,201)
Total operating expenses	324,933	322,542	283,614
OPERATING INCOME (LOSS)	11,651	(14,624)	4,455
Other income (expense):			
Interest expense	(27,052)	(31,346)	(25,906)
Currency transaction losses	(191)	(1,316)	(1,474)
Other, net	1,789	861	1,255
LOSS BEFORE INCOME TAX BENEFIT	(13,803)	(46,425)	(21,670)
INCOME TAX BENEFIT	6,777	11,621	5,041
NET LOSS	$ (7,026)	$(34,804)	$(16,629)
PRO FORMA NET INCOME PER SHARE (NOTE 1)	$ 0.20		

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(IN THOUSANDS, EXCEPT NUMBER OF SHARES)

	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL PAID-IN CAPITAL	ACCUMULATED DEFICIT	CUMULATIVE TRANSLATION ADJUSTMENT	TOTAL STOCKHOLDERS' EQUITY
DECEMBER 31, 1992	100	$ 1	$ 389,685	$(112,985)	$(1,401)	$ 275,300
Net loss	--	--	--	(16,629)	--	(16,629)
Exchange rate changes, net	--	--	--	--	(310)	(310)
Dividend to Loews	--	--	(100,000)	--	--	(100,000)
DECEMBER 31, 1993	100	1	289,685	(129,614)	(1,711)	158,361
Net loss	--	--	--	(34,804)	--	(34,804)
Exchange rate changes, net	--	--	--	--	509	509
DECEMBER 31, 1994	100	1	289,685	(164,418)	(1,202)	124,066
Net loss	--	--	--	(7,026)	--	(7,026)
Exchange rate changes, net	--	--	--	--	(67)	(67)
Capital contribution	--	--	39,676	--	--	39,676
350,500-for-one stock split	35,049,900	350	(350)	--	--	--
Issuance of common stock from initial public offering	14,950,000	149	338,214	--	--	338,363
Dividend to Loews	--	--	(2,118)	--	--	(2,118)
DECEMBER 31, 1995	50,000,000	$500	$ 665,107	$(171,444)	$(1,269)	$ 492,894

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
OPERATING ACTIVITIES:			
Net loss	$ (7,026)	$(34,804)	$(16,629)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation	50,794	49,908	46,819
Write-down of asset	2,071	5,458	--
Gain on sale of assets and other	(1,349)	(1,736)	(3,201)
Accrued interest converted to notes payable to Loews	27,044	31,294	25,894
Deferred tax benefit	(7,472)	(13,534)	(8,053)
Changes in operating assets and liabilities:			
Accounts receivable	(16,692)	4,458	(16,376)
Rig inventory and supplies and other current assets	(4,896)	(698)	(1,393)
Accounts payable and accrued liabilities	10,278	1,455	6,184
Other, net	29	761	(341)
Net cash provided by operating activities	52,781	42,562	32,904
INVESTING ACTIVITIES:			
Purchase of St. Vincent Drilling Ltd	--	--	(10,600)
Acquisition of drilling rigs and related equipment	--	(25,000)	--
Capital expenditures	(66,646)	(21,146)	(14,345)
Proceeds from sale of assets	1,516	2,486	4,194
Change in short-term investments	(115)	95	20
Net cash used in investing activities	(65,245)	(43,565)	(20,731)
FINANCING ACTIVITIES:			
Net (repayments) borrowings (to) from Loews	(331,245)	10,000	(5,627)
Proceeds from issuance of common stock	338,363	--	--
Dividend to Loews	(2,118)	--	--
Net cash provided by (used in) financing activities	5,000	10,000	(5,627)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(7,464)	8,997	6,546
Cash and cash equivalents, beginning of year	17,770	8,773	2,227
Cash and cash equivalents, end of year	$ 10,306	$ 17,770	$ 8,773

The accompanying notes are an integral part of the consolidated financial statements.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Business

Diamond Offshore Drilling, Inc. (the "Company") was incorporated in Delaware on April 13, 1989. Loews Corporation ("Loews"), a Delaware corporation of which the Company had been a wholly owned subsidiary prior to the initial public offering in October 1995 (the "Common Stock Offering"), owns 70.1% of the outstanding common stock of the Company (see Note 2).

The Company engages principally in the contract drilling of offshore oil and gas wells primarily for independent and major integrated oil companies and state-owned oil companies. The Company's fleet of mobile offshore drilling rigs is one of the largest in the world and includes the largest fleet of semisubmersible rigs. The fleet is deployed in the Gulf of Mexico, the North Sea, Africa, South America, Australia and Southeast Asia and consists of 22 semisubmersible rigs (including three of the world's 13 fourth-generation semisubmersibles), 14 jack-up rigs and one drillship. The Company also operates 10 land rigs deployed in South Texas. All of the Company's offshore and land rigs are wholly owned.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company after elimination of significant intercompany transactions and balances.

Cash and Cash Equivalents

All short-term, highly liquid investments that have an original maturity of three months or less are considered cash equivalents.

Supplementary Cash Flow Information

Non-cash financing activities for the year ended December 31, 1995 included a capital contribution by Loews in September 1995 of $39.7 million which reduced the outstanding debt to Loews. In addition, $27.0 million of interest expense was accrued and included in "Notes payable to Loews" prior to such notes being repaid with a portion of the proceeds from the Common Stock Offering (see Note 2). In connection with the Common Stock Offering, the tax sharing agreement with Loews was terminated and all liabilities were settled by offsetting $50.9 million owed by Loews to the Company under the agreement against notes payable to Loews.

Non-cash financing activities for the years ended December 31, 1994 and 1993 included $31.3 million and $25.9 million, respectively, of interest expense accrued and included in "Notes payable to Loews." Non-cash financing activities for 1993 also included a $100.0 million dividend declared to Loews in the form of additional debt (see Note 7).

Rig Inventory and Supplies

Inventories primarily consist of replacement parts and supplies held for use in the operations of the Company. Inventories are stated at the lower of cost or estimated value.

Drilling and Other Property and Equipment

Drilling and other property and equipment is carried at cost. Maintenance and repairs are charged to income currently while replacements and betterments are capitalized. Costs incurred for major rig upgrades are accumulated in construction work in progress, with no depreciation recorded on the additions, until the month the upgrade is completed and the rig is placed into service. Upon retirement or other disposal of fixed assets, the cost and related accumulated depreciation are removed from the respective accounts and any gains or losses are included in the results of operations.

For financial reporting purposes, depreciation is provided on the straight-line method over the remaining estimated useful lives from the date the asset is placed into service. The estimated useful lives of the Company's offshore drilling rigs range from 10 to 25 years. Other property and equipment is estimated to have useful lives ranging from 3 to 10 years.

Impairment of Long-Lived Assets

The Company reviews its long-lived assets for impairment when changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

In 1995, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." SFAS No. 121 requires that long-lived assets and certain identifiable intangibles to be held and used be reported at the lower of carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to the Company are recorded at the lower of carrying amount or fair value less cost to sell. The adoption of SFAS No. 121 did not have a material effect on the Company's financial position or results of operations.

Income Taxes

Taxable income (loss) of the Company and its domestic subsidiaries was included in the consolidated U.S. federal income tax return of Loews and other members of the Loews affiliated group for all taxable periods ending prior to the Common Stock Offering. Thereafter, the taxable income (loss) of the Company and its domestic subsidiaries is included in the consolidated U.S. federal income tax return of the Company and its affiliated group.

Deferred income taxes are recognized for the effect of temporary differences between financial and tax reporting. Except for selective dividends, the Company intends to reinvest the unremitted earnings of its non-U.S. subsidiaries and postpone their remittance indefinitely. Thus, no additional U.S. taxes have been provided on earnings of these non-U.S. subsidiaries. The Company's non-U.S. income tax liabilities are based upon the results of operations of the various subsidiaries in those jurisdictions in which they are subject to taxation.

Revenue Recognition

Income from dayrate drilling contracts is recognized currently. In connection with such drilling contracts, the Company may receive lump-sum fees for the mobilization of equipment and personnel. The net of mobilization fees received and costs incurred to mobilize an offshore rig from one market to another is recognized over the term of the related drilling contract. Absent a contract, mobilization costs are recognized currently. Revenues received from customers for asset enhancements relating to specific contracts are deferred and amortized to income over the term of the drilling contract.

Income from offshore turnkey contracts is recognized on the completed contract method, with revenues accrued to the extent of costs until the specified turnkey depth and other contract requirements are met. Provisions for future losses on turnkey contracts are recognized when it becomes apparent that contract drilling expenses to be incurred on a specific contract will exceed the revenue from the contract.

Currency Translation

The Company's primary functional currency is the U.S. dollar. Certain of the Company's subsidiaries use the local currency in the country where they conduct operations as their functional currency. These subsidiaries translate assets and liabilities at year-end exchange rates while income and expense accounts are translated at average exchange rates. Translation adjustments are reflected in the stockholders' equity section titled "Cumulative translation adjustment." Currency transaction gains and losses are included in current operating results. Additionally, translation gains and losses of subsidiaries operating in hyperinflationary economies are included in operating results currently.

Research and Development Expenses

Research and development expenses are expensed when incurred and are reflected in the Consolidated Statements of Operations in "Contract drilling expenses." For the year ended December 31, 1995, research and development expenses of approximately $.6 million were incurred in connection with preliminary feasibility studies for the development of an ultra-large semisubmersible, the Ocean Legend. There were no research and development expenses for the years ended December 31, 1994 and 1993.

Pro Forma Net Income Per Share Data

As described in Note 2, after its initial public offering, the Company had 50,000,000 shares of common stock outstanding. Assuming the Common Stock Offering had occurred at the beginning of the period, the Company would have recognized net income of $10.0 million, or $0.20 per share, after adjusting for the after-tax effects of a reduction in interest expense.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimated.

Reclassifications

Certain amounts applicable to the prior periods have been reclassified to conform to the classifications currently followed. Such reclassifications do not affect earnings.

2. COMMON STOCK OFFERING

Pursuant to the Common Stock Offering, the Company sold 14,950,000 shares of common stock, including 1,950,000 shares from an over-allotment option. Subsequent to the Common Stock Offering, the exercise of the over-allotment option and a 350,500-for-one stock split, which was effective immediately prior to consummation of the Common Stock Offering, the Company had 50,000,000 shares of common stock outstanding.

Proceeds from the Common Stock Offering were used to repay all of the Company's then outstanding debt to Loews of $336.2 million and the remainder of such proceeds was used to pay Loews a special dividend of $2.1 million. In addition, pursuant to a termination and settlement agreement, all assets and liabilities under the tax sharing agreement with Loews were settled by offsetting amounts owed by Loews to the Company thereunder against notes payable to Loews (see Note 8).

3. SHORT-TERM INVESTMENTS

The Company has entered into a pledge agreement with a bank whereby the bank has or will extend various financial accommodations to or for the account of the Company, including issuing letters of credit, entering into foreign exchange contracts or permitting intra-day overdrafts. In consideration of and as a condition precedent to the making of such financial accommodations by the bank, the Company is required to maintain a pledged collateral account in which the bank has a continuing security interest. As of December 31, 1995 and 1994, the Company had $5.0 million and $4.9 million, respectively, in U.S. Treasury Bills deposited in such pledged collateral account.

4. DRILLING AND OTHER PROPERTY AND EQUIPMENT

Cost and accumulated depreciation of drilling and other property and equipment are summarized as follows:

	DECEMBER 31,	
	1995	1994
	(IN THOUSANDS)	
Drilling rigs and equipment	$ 689,438	$ 645,922
Construction work in progress	19,016	--
Land and buildings	3,655	3,599
Office equipment and other	6,300	5,391
	718,409	654,912
Less accumulated depreciation	(216,131)	(166,248)
Total	$ 502,278	$ 488,664

Construction Work in Progress

The Company entered into letters of intent with two major oil companies for three-year commitments on both the Ocean Quest and Ocean Star (formerly named Ocean Countess) pursuant to which the rigs are being upgraded to conduct drilling operations in the Gulf of Mexico deep water market. The upgrade projects include stability enhancements to provide additional hull buoyancy, the addition of a new mooring system, and drilling system upgrades. In connection with these upgrades, the Company mobilized the Ocean Star, which had been previously idle in the North Sea, to the Gulf of Mexico during the fourth quarter of 1995. Both rigs entered the shipyard to begin their upgrades in December 1995 and are scheduled to be placed into service in the fourth quarter of 1996. As of December 31, 1995, $6.6 million and $3.2 million of construction work in progress was related to the Ocean Quest and Ocean Star, respectively. The remaining $9.2 million of construction work in progress was related to upgrades to prepare the Ocean Baroness and Ocean Princess for contracts in Brazil and the North Sea, respectively.

Impairment of Assets

During 1995 and 1994, the Company recorded impairment losses of $2.1 million and $5.5 million, respectively, to decrease the carrying value of two semisubmersible drilling rigs (one located in the Gulf of Mexico and the other located in South America). The rig in the Gulf of Mexico was sold in the fourth quarter of 1995 and management plans to sell the rig in South America during 1996. The impairment losses represent the amount by which the carrying value of the rigs exceeded the fair value of such rigs, based on expected future cash flows to be generated by such rigs. The impairment losses, reflected in "Depreciation" in the Consolidated Statements of Operations, reduce the carrying value of both rigs to zero. Operating losses provided by the rig located in the Gulf of Mexico during the years ended December 31, 1995, 1994 and 1993 were approximately $2,000, $324,000 and $333,000, respectively. Operating income (loss) contributed by the rig located in South America during the years ended December 31, 1995, 1994 and 1993 was approximately $(.6) million, $(2.1) million and $2.4 million, respectively.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

5. ACCRUED LIABILITIES

Accrued liabilities consist of the following:

	DECEMBER 31, 1995	DECEMBER 31, 1994
	(IN THOUSANDS)	
Compensation and benefits	$17,402	$15,480
Other	16,527	12,897
Total	$33,929	$28,377

6. FINANCIAL INSTRUMENTS

Concentrations of Credit Risk

Financial instruments which potentially subject the Company to significant concentrations of credit risk consist primarily of cash and trade accounts receivable. The Company maintains cash and cash equivalents and certain other financial instruments with various financial institutions. An accounting loss would occur if one or more of these institutions fails to perform according to the terms of its agreements. However, these financial institutions are located throughout the world, and the Company's strategy is designed to limit exposure to any one institution. The Company's periodic evaluations of the relative credit standing of these financial institutions are considered in the Company's investment strategy.

Concentrations of credit risk with respect to trade accounts receivable are limited due to the large number of entities comprising the Company's customer base. Since the market for the Company's services is the oil and gas industry, this customer base consists primarily of major oil companies and independent oil and gas producers. The Company provides allowances for potential credit losses when necessary. No such allowances were deemed necessary for the years presented. As of December 31, 1995 and 1994, the Company had no significant concentrations of credit risk.

Fair Values

SFAS No. 107 "Disclosure about Fair Value of Financial Instruments," requires the disclosure of the fair value of all financial instruments, both assets and liabilities, for which it is practicable to estimate fair value. The Company's financial instruments include short-term investments, accounts receivable and notes payable to Loews. The carrying amounts of the Company's financial instruments approximate fair value due to the nature of such instruments. The estimated fair value amounts have been determined by the Company using appropriate valuation methodologies and information available to management as of December 31, 1995 and 1994. Considerable judgment is required in developing these estimates, and accordingly, no assurance can be given that the estimated values are indicative of the amounts that would be realized in a free market exchange.

The carrying amount of the Company's investment in U.S. Treasury Bills is at fair value based upon the closing market prices obtained from public sources. The Company believes it has the ability to hold its fixed income investment until maturity. However, the Company may sell its securities and reinvest the proceeds to take advantage of opportunities generated by changing interest rates. Therefore, the Company considers its securities as available for sale.

7. NOTES PAYABLE TO AND TRANSACTIONS WITH LOEWS

As described in Note 2, a portion of the proceeds from the Common Stock Offering was used to repay all of the Company's then outstanding debt to Loews of $336.2 million. Prior to the Common Stock Offering, the Company received from Loews loans for acquisitions, capital expenditures and working capital depending on its cash requirements and cash position. These loans, net of amounts repaid, were $41.3 million and

$20.3 million, including interest at 10 percent per annum of $26.3 million and $24.7 million, during the years ended December 31, 1994 and 1993, respectively. Loews had represented to the Company that no repayment of the debt outstanding was required within twelve months and the debt was, therefore, classified as noncurrent at December 31, 1994.

On October 7, 1993, the Company declared a $100.0 million dividend to Loews in the form of additional debt, with interest accruing at 5 percent per annum. Interest accrued at December 31, 1994 and 1993 was $5.0 million and $1.2 million, respectively.

The Company and Loews have entered into a services agreement which was effective upon consummation of the Common Stock Offering (the "Services Agreement") pursuant to which Loews agreed to continue to perform certain administrative and technical services on behalf of the Company. Such services include personnel, telecommunications, purchasing, internal auditing, accounting, data processing and cash management services, in addition to advice and assistance with respect to preparation of tax returns and obtaining insurance. Under the Services Agreement, the Company is required to reimburse Loews for (i) allocated personnel costs (such as wages, salaries, employee benefits and payroll taxes) of the Loews personnel actually providing such services and (ii) all out-of-pocket expenses related to the provision of such services. The Services Agreement may be terminated at the Company's option upon 30 days' notice to Loews and at the option of Loews upon six months' notice to the Company. In addition, the Company has agreed to indemnify Loews for all claims and damages arising from the provision of services by Loews under the Services Agreement, unless due to the gross negligence or willful misconduct of Loews. Prior to the Common Stock Offering, Loews provided such services at an allocated rate. The Company has been charged $.7 million, $.9 million and $.6 million by Loews for these support functions during the years ended December 31, 1995, 1994 and 1993, respectively.

Subsequent to the Common Stock Offering, Loews provided the Company with a $150.0 million revolving line of credit available through October 31, 1996 or until alternative financing is arranged. Borrowings under the line of credit bear interest, at the Company's option, at a per annum rate equal to a base rate (equal to the greater of (i) the prime rate announced by Bankers Trust Company or (ii) the Federal Funds rate plus .50%) plus .25% or the Eurodollar rate plus 1.25%. The line of credit is unsecured, has no financial or restrictive covenants, and the Company is not required to pay a commitment fee to Loews. As of December 31, 1995, there were no amounts outstanding under this line of credit.

8. INCOME TAXES

The Company and its subsidiaries were party to a tax sharing agreement with Loews and the Company has provided a tax provision calculated as if on a stand-alone basis for U.S. federal income tax purposes prior to the Common Stock Offering. In conjunction with the Common Stock Offering, the tax sharing agreement was terminated and all assets and liabilities were settled by offsetting amounts owed by Loews to the Company under the agreement against notes payable to Loews (see Note 2).

An analysis of the Company's income (taxes) benefits is as follows:

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
	(IN THOUSANDS)		
U.S. -- current	$ --	$ --	$ --
U.S. -- deferred	7,472	13,559	8,558
Non-U.S. -- current	(489)	(1,541)	(2,519)
Non-U.S. -- deferred	--	(25)	(505)
State and other	(206)	(372)	(493)
Total	$6,777	$11,621	$ 5,041

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Significant components of the Company's net deferred tax liability are as follows:

	DECEMBER 31, 1995	DECEMBER 31, 1994
	(IN THOUSANDS)	
DEFERRED TAX ASSETS:		
Net operating loss carryforwards	$ 15,641	$ 69,241
Investment tax credit carryforwards	7,638	8,838
U.S. taxes on foreign income	8,136	7,180
Workers compensation accruals(1)	2,971	930
Foreign tax credits	5,160	3,060
Other	432	1,432
Total deferred tax assets	$ 39,978	$ 90,681
DEFERRED TAX LIABILITIES:		
Drilling and other property and equipment	(98,401)	(106,288)
Non-U.S. deferred taxes	(10,146)	(10,060)
Other	(1,367)	(745)
Total deferred liabilities	(109,914)	(117,093)
Net deferred tax liability	$ (69,936)	$ (26,412)

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(1) Reflected in "Prepaid expenses and other" in the Company's Consolidated Balance Sheets.

In connection with the purchase of Odeco Drilling Inc. in 1992, the Company acquired net operating loss ("NOL") and investment tax credit ("ITC") carryforwards available to offset future taxable income. The amount of these acquired NOL and ITC carryforwards, which are expected to be utilized on future income tax returns, is $49.9 million and $8.8 million, respectively. At December 31, 1995, the Company has recorded a deferred tax asset for the NOL and ITC carryforwards available, including those generated subsequent to the Common Stock Offering, which expire as follows:

YEAR	TAX BENEFIT OF NET OPERATING LOSSES	INVESTMENT TAX CREDITS
	(IN THOUSANDS)	
2001	$ 8,134	$ --
2002	--	--
2003	2,627	7,638
2004	216	--
2005	66	--
2006	272	--
2008	2,321	--
2010	2,005	--
Total	$ 15,641	$7,638

No valuation allowance has been provided on the Company's deferred tax assets because management believes that future reversals of existing taxable temporary differences will generate taxable income sufficient to utilize these benefits. However, if the Company is unable to generate sufficient taxable income in the future through operating results, a valuation allowance will be required through a charge to expense.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

A reconciliation of the expected income tax benefit resulting from the use of statutory tax rates to the effective income tax benefit follows:

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
	(IN THOUSANDS)		
Income (loss) before income tax benefit:			
U.S.	$(19,591)	$(29,667)	$(26,290)
Non-U.S.	5,788	(16,758)	4,620
Worldwide	$(13,803)	$(46,425)	$(21,670)
Expected tax benefit at statutory rate	$ 4,831	$ 16,249	$ 7,585
Increase in U.S. statutory rate	--	--	(1,530)
Non-U.S. income (loss):			
Impact of taxation at different rates	1,270	1,716	198
Impact of non-U.S. losses for which a current tax benefit is not available	(1,004)	(6,094)	(2,490)
State taxes and other	1,680	(250)	1,278
Income tax benefit	$ 6,777	$ 11,621	$ 5,041

As a result of legislation enacted in August 1993, the federal tax rate for corporations was increased from 34 to 35 percent, effective January 1, 1993. An adjustment of $1.5 million to increase the net federal deferred tax liability was recorded in the third quarter of 1993 for the effect of such legislation.

Undistributed earnings of non-U.S. subsidiaries for which no deferred income tax provision has been made for possible future remittances totaled approximately $46.1 million at December 31, 1995. Substantially all of this amount represents earnings reinvested as part of the Company's ongoing business. It is not practicable to estimate the amount of taxes that might be payable on the eventual remittance of such earnings. On remittance, certain countries impose withholding taxes that, subject to certain limitations, are then available for use as tax credits against a U.S. tax liability, if any. The Company also has certain income tax loss carryforwards in non-U.S. tax jurisdictions to which it has assigned no value because of the uncertainty of utilization of these carryforwards.

9. EMPLOYEE BENEFIT PLANS

The Company maintains defined contribution retirement plans for its U.S. and U.K. employees. The plan for U.S. employees is designed to qualify under Section 401(k) of the Internal Revenue Code of 1986, as amended. Under the plan for U.S. employees, each participant may elect to defer taxation on a portion of his or her eligible earnings, as defined by the plan, by directing the Company to withhold a percentage of such earnings. A participating employee may also elect to make after-tax contributions to the plan. The Company contributes 3.75 percent of a participant's defined compensation. For the years ended December 31, 1995, 1994 and 1993, the Company's provision for contributions was $2.4 million, $2.3 million and $2.0 million, respectively.

The plan for U.K. employees provides that the Company contribute amounts equivalent to the employee's contributions generally up to a maximum of 3 percent of the employee's defined compensation per year. For the years ended December 31, 1995, 1994 and 1993, the Company's provision for contributions was $.2 million, $.2 million and $.3 million, respectively.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

10. COMMITMENTS AND CONTINGENCIES

The Company leases office facilities under operating leases which expire through the year 2000. Total rent expense amounted to $1.5 million, $1.5 million and $.9 million for the years ended December 31, 1995, 1994 and 1993, respectively. Minimum future rental payments under leases are approximately $327,000, $85,000, $15,000, $15,000 and $10,000 for the years 1996 to 2000, respectively (see Note 12).

Various claims have been filed against the Company in the ordinary course of business, particularly claims alleging personal injuries. Management believes that the Company has established adequate reserves on its books for any liabilities that may reasonably be expected to result from these claims. In the opinion of management, no pending or threatened claims, actions or proceedings against the Company are expected to have a material adverse effect on the Company's financial position or results of operations.

As security for certain bids and performance on certain contracts, the Company is contingently liable as of December 31, 1995 and 1994 in the amount of $.8 million and $1.1 million, respectively, under performance/bid bonds. On the Company's behalf, banks have issued letters of credit securing these bonds.

11. GEOGRAPHIC AREA ANALYSIS AND MAJOR CUSTOMERS

The following table summarizes, by geographic area, operating revenues and operating income (loss) for the years ended December 31, 1995, 1994 and 1993, and identifiable assets at the end of those periods.

	YEAR ENDED DECEMBER 31,		
	1995	1994	1993
	(IN THOUSANDS)		
OPERATING REVENUES:			
United States	$213,998	$203,198	$158,916
Europe/Africa	47,645	19,159	47,765
Australia/Southeast Asia	53,113	57,129	30,284
South America	21,828	26,133	32,489
Other areas	--	2,299	18,615
Total	$336,584	$307,918	$288,069
OPERATING INCOME (LOSS):			
United States	$ 19,002	$ 4,125	$ 12,255
Europe/Africa	5,753	(10,365)	(8,432)
Australia/Southeast Asia	(7,675)	2,783	(5,960)
South America	(5,429)	(11,546)	3,943
Other areas	--	379	2,649
Total	$ 11,651	$(14,624)	$ 4,455
IDENTIFIABLE ASSETS:			
United States	$386,282	$366,575	$327,370
Europe/Africa	165,277	125,773	153,619
Australia/Southeast Asia	36,705	48,059	47,386
South America	29,788	47,751	48,014
Other areas	--	--	15,773
Total	$618,052	$588,158	$592,162

A substantial portion of the Company's assets are mobile, therefore, asset locations at the end of the period are not necessarily indicative of the geographic distribution of the earnings generated by such assets during the periods.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

The assets located outside the U.S. include cash and cash equivalents of $1.3 million, $2.5 million and $3.3 million at December 31, 1995, 1994 and 1993, respectively.

The Company has performed drilling activities for certain major customers. For the year ended December 31, 1995, one customer contributed 16.5 percent of total revenues. For the year ended December 31, 1994, no single customer contributed 10.0 percent or more of total revenues. For the year ended December 31, 1993, one customer contributed 10.5 percent of total revenues.

12. SUBSEQUENT EVENTS

Arethusa (Off-Shore) Limited Acquisition

The Company and Arethusa (Off-Shore) Limited, a Bermuda company ("Arethusa"), have entered into an agreement to merge the two companies. The agreement provides that, upon consummation of the merger, holders of Arethusa stock will receive 17.9 million shares of common stock to be issued by the Company based on 20.3 million shares of Arethusa's common stock issued and outstanding and on a ratio of .88 shares for each share of issued and outstanding Arethusa common stock. The merger is subject to requisite shareholder approval. It is anticipated that the consummation of the merger will occur no later than July 31, 1996. The merger will be accounted for as a purchase for financial reporting purposes, and accordingly, the costs of the merger will be allocated to assets acquired and liabilities assumed based on their estimated fair market values.

Arethusa owns a fleet of 11 mobile offshore drilling rigs, operates two additional mobile offshore drilling rigs, and provides drilling services worldwide to domestic, international and state-owned oil and gas companies. For the year ended September 30, 1995, Arethusa reported revenues of $122.1 million, net income of $21.6 million, and net income per share of $1.06. The following pro forma information presents the consolidated results of operations, assuming consummation of the merger had occurred at the beginning of the period. The historical operating results for the Company included in the pro forma financial data have been adjusted to give effect to the Common Stock Offering and interest expense for working capital borrowings.

	PRO FORMA YEAR ENDED DECEMBER 31, 1995 (IN THOUSANDS, EXCEPT PER SHARE DATA)
Revenues	$456,750
Operating income	3,347
Net loss	(963)
Net loss per share	(0.01)

Building Purchase

In February 1996, the Company purchased for approximately $8.2 million the land and the eight-story building containing approximately 182,000 net rentable square feet on approximately 6.2 acres in which it had leased office space for its corporate headquarters. A portion of the building is currently occupied by other tenants under leases which expire through the year 2005. This purchase will reduce general and administrative expenses in the future by eliminating rent expense and will provide rental income from the leases, offset by depreciation and related interest expense. The Company, therefore, does not expect the result of this purchase to have a material effect on its results of operations.

DIAMOND OFFSHORE DRILLING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Credit Facility

In February 1996, the Company executed a definitive credit agreement governing a $150.0 million credit facility with a group of banks (the "Diamond Offshore Bank Credit Facility"). This line of credit bears interest at the same per annum rate as the revolving line of credit with Loews. Borrowings are secured by security interests in certain of the Company's assets. The Diamond Offshore Bank Credit Facility also contains covenants that limit the amount of total consolidated debt, require the maintenance of certain consolidated financial ratios and limit dividends and similar payments. The Company is required to pay a commitment fee on the unused available portion of the maximum credit commitment. Upon execution of the definitive agreement for the Diamond Offshore Bank Credit Facility, the revolving line of credit with Loews was terminated.

13. UNAUDITED QUARTERLY FINANCIAL DATA

Unaudited summarized financial data by quarter for the years 1995 and 1994 is shown below. Per share information has not been provided for periods prior to the Common Stock Offering.

	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER
	(IN THOUSANDS, EXCEPT PER SHARE DATA)			
1995:				
Revenues	$ 70,760	$ 76,106	$ 91,716	$ 98,002
Operating income (loss)	(8,730)	56	11,572	8,753
Income (loss) before income tax benefit	(16,861)	(8,299)	3,003	8,354
Net income (loss)	(11,572)	(2,770)	1,422	5,894
Pro forma net income per share(1)	--	--	--	0.13
1994:				
Revenues	$ 73,759	$ 75,074	$ 78,872	$ 80,213
Operating income (loss)	107	(3,248)	(4,535)	(6,948)
Loss before income tax benefit	(7,355)	(12,021)	(12,152)	(14,897)
Net loss	(8,555)	(8,505)	(7,929)	(9,815)

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(1) As described in Note 2, after its initial public offering, the Company had 50,000,000 shares of common stock outstanding. Assuming the Common Stock Offering had occurred at the beginning of the fourth quarter, the Company would have recognized net income of $6.4 million, or $0.13 per share, after adjusting for the after-tax effects of a reduction in interest expense.

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED CONDENSED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	DECEMBER 31, 1995	SEPTEMBER 30, 1995
ASSETS		
CURRENT ASSETS:		
Cash and cash investments	$ 27,215	$ 20,251
Restricted cash	2,345	2,469
Marketable equity securities	--	6,000
Accounts receivable	29,426	28,625
Supplies and spare parts, at cost	16,564	16,952
Prepayments and other current assets	1,305	1,206
Total current assets	76,855	75,503
MOBILE DRILLING RIGS AND EQUIPMENT, at cost	350,780	348,426
Accumulated depreciation	(119,244)	(111,102)
Net mobile drilling rigs and equipment	231,536	237,324
OTHER ASSETS	2,020	2,505
Total assets	$ 310,411	$ 315,332
LIABILITIES AND SHAREHOLDERS' INVESTMENT		
CURRENT LIABILITIES:		
Current maturities of long-term debt	$ 10,603	$ 10,603
Accounts payable	5,085	12,942
Accrued liabilities	3,625	4,050
Interest payable	641	662
Income taxes payable	328	302
Total current liabilities	20,282	28,559
LONG-TERM DEBT	58,587	62,175
DEFERRED CREDITS	700	1,000
OTHER LONG-TERM LIABILITIES	1,021	1,019
SHAREHOLDERS' INVESTMENT:		
Common stock, $.10 par value per share, 50,000 shares authorized, 20,333 shares issued and outstanding	2,033	2,033
Additional paid-in capital	218,800	218,800
Accumulated earnings	8,988	132
Unrealized gain on equity securities	--	1,614
Total shareholders' investment	229,821	222,579
Total liabilities and shareholders' investment	$ 310,411	$ 315,332

See accompanying notes.

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	THREE MONTHS ENDED DECEMBER 31,	
	1995	1994
CONTRACT DRILLING REVENUE	$40,364	$28,279
OPERATING EXPENSES:		
Direct costs	20,367	20,821
General and administrative	2,664	2,045
Depreciation	8,193	7,067
OPERATING INCOME (LOSS)	9,140	(1,654)
OPERATING INCOME (EXPENSE):		
Interest expense	(1,485)	(1,421)
Interest income	371	1,716
Gain on sales of equity securities	1,602	--
Loss on sales of assets	(17)	7
Other, net	(371)	(23)
INCOME (LOSS) BEFORE INCOME TAXES	9,240	(1,375)
TAX PROVISION	(384)	(315)
NET INCOME (LOSS)	$ 8,856	$(1,690)
EARNINGS (LOSS) PER COMMON SHARE	$ .44	$ (.08)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	20,333	20,333

See accompanying notes.

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	THREE MONTHS ENDED DECEMBER 31,	
	1995	1994
OPERATING ACTIVITIES:		
Net cash provided by operating activities	$12,324	$ 2,883
INVESTING ACTIVITIES:		
Capital expenditures for mobile drilling rigs and equipment	(7,936)	(2,051)
Proceeds from dispositions of equipment	12	18
Proceeds from sales-type lease of mobile drilling rig, net	--	1,414
Sales of marketable securities	5,988	--
Changes in other assets	164	105
Net cash used in investing activities	(1,772)	(514)
FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt	--	80,000
Principal payments on long-term debt	(3,588)	(71,809)
Payments for debt financing arrangements	--	(371)
Net cash provided by (used in) financing activities	(3,588)	7,820
NET INCREASE IN CASH AND CASH EQUIVALENTS	6,964	10,189
CASH AND CASH EQUIVALENTS, beginning of period	20,251	26,410
CASH AND CASH EQUIVALENTS, end of period	$27,215	$ 36,599

See accompanying notes.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

1. INTERIM FINANCIAL STATEMENTS

The condensed consolidated financial statements for the interim periods shown in this report have not been audited by independent public accountants but, in the opinion of management, all adjustments necessary for the fair presentation of these financial statements have been made. All such adjustments are of a normal recurring nature. Results of operations for interim periods are not necessarily indicative of results to be expected for the full fiscal year.

The condensed consolidated financial statements should be read in connection with the consolidated financial statements of Arethusa (Off-Shore) Limited ("Arethusa") as of September 30, 1995 and 1994, and for each of the three years in the period ended September 30, 1995 and the related notes thereto, included elsewhere herein.

2. PENDING MERGER OF ARETHUSA AND DIAMOND OFFSHORE DRILLING, INC.

On February 9, 1996, Arethusa and Diamond Offshore Drilling, Inc. ("Diamond Offshore") executed and delivered definitive agreements in connection with the previously announced proposed merger of the two companies. Merrill Lynch and CS First Boston, financial advisers to Arethusa and Diamond Offshore, respectively, have each rendered a fairness opinion in respect of the transaction and each company's Board of Directors has resolved to recommend the transaction to its shareholders.

Under the proposed merger each Arethusa share would be exchanged for .88 share of Diamond Offshore on a taxable basis to Arethusa's United States shareholders. The transaction is subject to approval by the shareholders of each company at meetings presently expected to be held in April. Commitments to vote in favor of the merger have been made by shareholders representing approximately 47% of Arethusa's shares and by Loews Corporation, representing approximately 70% of Diamond Offshore shares. If the Plan of Acquisition is terminated under certain circumstances, Arethusa must pay to Diamond Offshore a fee of up to $18 million.

Upon successful consummation of the merger, options awarded to officers, directors and employees of Arethusa will become fully vested and exercisable. Also, Arethusa Off-Shore Company ("AOC"), a wholly owned subsidiary of Arethusa, has entered into executive severance agreements with certain executive officers and has amended its severance policy for most shore based employees which will provide payment of certain additional benefits to the employees if they are terminated following the merger.

Additionally, on February 9, 1996 Arethusa declared a cash dividend of $.25 per common share payable on March 15 to shareholders of record as of March 1, 1996.

Additionally, subject to approval by Arethusa shareholders and to a successful merger, the exercise price of options granted under the 1993 Employee Stock Option Plan (approximately 462,000 shares granted) would be reduced by $3 per share. In the event the option exercise price is reduced to $7 per share, Arethusa would be required to record compensation expense in its financial statements for the difference between the revised exercise price of $7 per share and the market value on the date approval is received from shareholders. To the extent the market value of Arethusa shares continues to increase above the exercise price there will be an increased charge to compensation expense.

3. ACQUISITION OF THE ARETHUSA YATZY

In May 1995, Arethusa acquired the Arethusa Yatzy (see footnote 4 to Arethusa's September 30, 1995 Annual Report on Form 10-K). The following unaudited pro forma income statement data for the three months ended December 31, 1994 present the consolidated results of operations as if the acquisition had occurred on September 30, 1994. The unaudited pro forma income statement data also reflect two additional significant fiscal 1995 transactions, the sale of the Treasure Stawinner and the June 30, 1995 dividend and capital distribution (both discussed in footnote 5 to Arethusa's September 30, 1995 Annual Report on Form 10-K), as if each had occurred on September 30, 1994. Such unaudited pro forma financial data may not be indicative of the results of operations of Arethusa had the transactions been completed on such earlier date, nor is it necessarily indicative of future financial results.

PRO FORMA INCOME STATEMENT DATA
FOR THE THREE MONTHS ENDED DECEMBER 31, 1994
(IN THOUSANDS, EXCEPT PER SHARE DATA)

Contract Drilling Revenue	$28,393
Net Loss	$(2,095)
Net Loss Per Common Share	$ (.10)

The historical operating results for the Arethusa Yatzy included in the unaudited pro forma financial data have been adjusted for (i) duplicate administrative expenses, (ii) depreciation expense calculated based upon Arethusa's cost and estimated useful life, (iii) a reduction in insurance expense based upon Arethusa's lower insured value, and (iv) interest calculated based upon Arethusa's $30.0 million note.

4. COMMITMENTS AND CONTINGENCIES:

Operating Lease -- Arethusa is committed under a lease agreement for office space which continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1,023,000.

Litigation -- Arethusa is engaged in various claims and litigation arising from operations. In the opinion of management, uninsured losses, if any, resulting from these matters will not have a material adverse effect on Arethusa's results of operations or financial position.

Revenue Agent Reviews -- Revenue agent reviews are currently in progress with respect to certain of Arethusa's subsidiaries and operations in Indonesia and the United States. While Arethusa cannot predict with certainty the outcome of such reviews, management does not believe the ultimate outcome of these reviews will have a material adverse impact on Arethusa's consolidated financial position or results of operations.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors and Shareholders of
Arethusa (Off-Shore) Limited:

We have audited the accompanying consolidated balance sheets of Arethusa (Off-Shore) Limited (a Bermuda company) and subsidiaries as of September 30, 1995 and 1994, and the related consolidated statements of income, shareholders' investment and cash flows for each of the three years in the period ended September 30, 1995, which, as described in Note 1, have been prepared on the basis of accounting principles generally accepted in the United States. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Arethusa (Off-Shore) Limited and subsidiaries as of September 30, 1995 and 1994, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 1995, in conformity with accounting principles generally accepted in the United States.

ARTHUR ANDERSEN & CO.

Hamilton, Bermuda
November 14, 1995

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	SEPTEMBER 30, 1995	SEPTEMBER 30, 1994
ASSETS		
Current assets		
Cash and cash equivalents	$ 20,251	$ 26,410
Restricted cash	2,469	2,161
Equity securities	6,000	--
Accounts receivable	28,625	23,076
Lease receivable	--	57,321
Supplies and spare parts, at cost	16,952	12,591
Prepayments and other current assets	1,206	1,316
Total current assets	75,503	122,875
Mobile drilling rigs and equipment, at cost		
Drilling rigs --		
Semisubmersibles	267,417	227,768
Jack-ups	73,823	72,446
Drill pipe and other drilling equipment	5,767	5,450
Furniture, fixtures, automobiles and other	1,419	1,310
	348,426	306,974
Accumulated depreciation	(111,102)	(85,818)
Net mobile drilling rigs and equipment	237,324	221,156
Other assets	2,505	3,791
Total assets	$ 315,332	$ 347,822
LIABILITIES AND SHAREHOLDERS' INVESTMENT		
Current liabilities		
Current maturities of long-term debt	$ 10,603	$ 30,899
Accounts payable	12,942	8,317
Accrued liabilities	4,050	3,154
Interest payable	662	763
Income taxes payable	302	306
Total current liabilities	28,559	43,439
Long-term debt	62,175	40,910
Deferred credits	1,000	2,201
Other long-term liabilities	1,019	931
Commitments and contingencies (Note 10)		
Shareholders' Investment:		
Common stock, $.10 par value per share, 50,000 shares authorized, 20,333 shares issued and outstanding	2,033	2,033
Additional paid-in capital	218,800	274,386
Accumulated earnings	132	(16,078)
Unrealized gain on equity securities	1,614	--
Total shareholders' investment	222,579	260,341
Total liabilities and shareholders' investment	$ 315,332	$ 347,822

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

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	YEAR ENDED SEPTEMBER 30,		
	1995	1994	1993
Contract drilling revenue	$122,147	$120,212	$ 94,161
Operating expenses			
Direct costs	87,953	79,857	63,882
General and administrative	8,658	7,609	6,300
Depreciation	29,547	27,446	23,784
Total operating expenses	126,158	114,912	93,966
Operating income (loss)	(4,011)	5,300	195
Other income (expense)			
Interest expense	(6,311)	(6,090)	(10,194)
Interest income	5,692	5,842	6,196
Gains on sales of assets	27,820	330	1,015
Gain on sale of equity securities	67	--	--
Other, net	(193)	(253)	(154)
Total other income (expense)	27,075	(171)	(3,137)
Income (loss) before income taxes	23,064	5,129	(2,942)
Tax provision	(1,440)	(1,542)	(2,061)
Net income (loss)	$ 21,624	$ 3,587	$ (5,003)
Net income (loss) per common share	$ 1.06	$ .18	$ (.31)
Weighted average common shares outstanding	20,333	20,333	16,073

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

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' INVESTMENT
(IN THOUSANDS)

	COMMON STOCK SHARES	COMMON STOCK PAR VALUE	ADDITIONAL PAID-IN CAPITAL	ACCUMULATED EARNINGS	UNREALIZED GAIN ON EQUITY SECURITIES
Balance at September 30, 1992	15,333	$1,533	$ 228,467	$ (14,662)	$ --
Net loss for fiscal year 1993	--	--	--	(5,003)	--
Issuance of Common Stock:					
-- Through Initial Public Offering	4,000	400	36,019	--	--
-- In connection with rig acquisitions	1,000	100	9,900	--	--
Balance at September 30, 1993	20,333	2,033	274,386	(19,665)	--
Net income for fiscal year 1994	--	--	--	3,587	--
Balance at September 30, 1994	20,333	2,033	274,386	(16,078)	--
Net income for fiscal year 1995	--	--	--	21,624	--
Dividend and capital distribution -- $3 per share	--	--	(55,586)	(5,414)	--
Unrealized gain on equity securities	--	--	--	--	1,614
Balance at September 30, 1995	20,333	$2,033	$ 218,800	$ 132	$1,614

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

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	YEAR ENDED SEPTEMBER 30,		
	1995	1994	1993
Operating activities			
Net income (loss)	$ 21,624	$ 3,587	$ (5,003)
Adjustments to reconcile net income (loss) to net cash provided by operating activities --			
Depreciation and amortization	29,547	27,187	23,794
Gains on sales of assets	(27,820)	(330)	(1,015)
Gain on sale of equity securities	(67)	--	--
Changes in operating assets and liabilities --			
(Increase) decrease in restricted cash	(308)	993	2,473
Increase in accounts receivable	(5,189)	(1,967)	(4,949)
Increase in supplies and spare parts	(554)	(931)	(729)
(Increase) decrease in prepayments and other current assets	110	(477)	193
Increase (decrease) in accounts payable	530	338	(695)
Increase in accrued liabilities	896	692	1,117
Decrease in interest payable	(101)	(710)	(439)
Increase (decrease) in income taxes payable	(4)	(137)	220
Total adjustments	(2,960)	24,658	19,970
Net cash provided by operating activities	18,664	28,245	14,967
Investing activities			
Acquisitions of mobile drilling rigs and equipment	(69,498)	(5,989)	(61,814)
Proceeds from dispositions of mobile drilling rigs and equipment, net	53,191	674	21,997
Proceeds from sales-type lease of mobile drilling rig, net	56,069	5,362	4,898
Changes in other assets, including deferral and reimbursement of mobilization expenditures	631	(3,027)	--
Investment in equity securities	(4,538)	--	--
Proceeds from sale of equity securities	218	--	--
Other	(66)	(8)	(56)
Net cash provided by (used in) investing activities	36,007	(2,988)	(34,975)
Financing activities			
Proceeds from issuance of long-term debt	110,000	--	25,000
Principal payments on long-term debt	(109,032)	(23,490)	(35,191)
Payments for debt financing arrangements	(798)	(84)	(589)
Dividend and capital distribution	(61,000)	--	--
Proceeds from issuance of common stock, net of issuance costs	--	--	36,419
Net cash provided by (used in) financing activities	(60,830)	(23,574)	25,639
Net increase (decrease) in cash and cash equivalents	(6,159)	1,683	5,631
Cash and cash equivalents, beginning of period	26,410	24,727	19,096
Cash and cash equivalents, end of period	$ 20,251	$ 26,410	$ 24,727

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

General Organization

Arethusa (Off-Shore) Limited (herein referred to as Arethusa or the Company) is a Bermuda corporation, incorporated on August 31, 1990. Arethusa was formed for the purpose of acquiring offshore drilling rigs and certain other property and equipment owned by Zapata Off-Shore Company and its subsidiaries (Zapata or ZOS), and on October 31, 1990, these assets were purchased for $298 million.

In June 1993, the Company effected a two-for-three reverse stock split and reduced the par value of its stock from $10 to $.10 per share. In connection with the reverse stock split, the shareholders authorized additional shares of common stock, resulting in a total of 50,000,000 shares authorized. In August 1993, Arethusa completed an Initial Public Offering (IPO) of 4,896,000 shares of common stock at an initial price to the public of $10 per share, of which 4,000,000 shares were sold by the Company and 896,000 shares were sold by a shareholder. These shares are publicly traded on the NASDAQ National Market System.

Consolidation

The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States, expressed in United States dollars and include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Equity Securities

As of September 30, 1995, the Company had investments in equity securities. In accordance with Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities", such equity securities are reflected in the accompanying balance sheet as available-for-sale securities at the quoted market value as of September 30, 1995. Unrealized gains on the investment are reported as a separate component of shareholders' investment, until realized. The quoted market value of the shares held by the Company may not be the value that would be realized should the Company dispose of all of the shares in a short period of time.

Supplies and Spare Parts

Supplies and spare parts are stated at average cost which does not exceed market value.

Mobile Drilling Rigs and Equipment

Mobile drilling rigs and equipment are recorded at cost. Depreciation is provided on the straight-line method without salvage value, using an estimated useful life, as follows:

	ESTIMATED USEFUL LIFE
Mobile drilling rigs	25 years
Drill pipe and other drilling equipment	4-6 years
Furniture, fixtures, automobiles and other	3-25 years

For mobile drilling rigs acquired, the estimated useful life is based upon when the asset was placed in service by its original owner but will not be less than five years.

Routine repairs and maintenance are charged to expense as incurred. Repair and maintenance expense totaled approximately $16,400,000, $14,500,000 and $10,100,000 for fiscal years 1995, 1994 and 1993, respectively. Major renewals and improvements are capitalized and are generally depreciated over five years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Upon disposal of assets subject to depreciation, the accounts are relieved of related costs and accumulated depreciation.

Mobilization Costs

When significant costs are incurred in connection with mobilizing a drilling rig for a new contract, such costs, net of any mobilization fees received, are deferred and amortized over the new contract term. When a rig is mobilized before obtaining a new contract, the market in the new locale is analyzed and the projected return on the mobilization investment is determined, and mobilization costs are deferred and amortized over a period not to exceed 24 months. Mobilization costs incurred in connection with rig purchases are capitalized as part of the purchase price and are depreciated over the life of the rig.

Interest Rate Swap Agreements

From time to time, the Company has entered into interest rate swap agreements whereby the Company has exchanged the floating interest rate under certain debt agreements for a fixed interest rate. The differential paid or received is accrued as interest rates change and recognized over the life of the agreements. No such financial instruments have been in effect since October 1993.

Revenue Recognition

Contract drilling revenues are recognized as earned, based on contractual drilling rates. Losses are recognized in the period in which the loss is identified.

Foreign Currency Translation

Arethusa accounts for foreign currency translation in accordance with SFAS No. 52, "Foreign Currency Translation." In connection therewith, the United States dollar was determined to be the functional currency as revenues are received and operating costs are paid primarily in United States dollars.

Earnings (Loss) per Share Data

Earnings (loss) per share data is based on the weighted average number of common shares and common equivalent shares outstanding during each year, if dilutive.

Fair Value of Financial Instruments

In December 1991, the Financial Accounting Standards Board issued SFAS No. 107, "Disclosures about Fair Value of Financial Instruments." The Company believes that the fair value of its financial instruments approximates their book value. This determination was made as follows:

Long-Term Debt. The fair value of the Company's long-term debt, all of which is floating rate, is estimated based on rates currently available to the Company for debt with similar maturities.

Currency Exchange Contracts. Currency exchange contracts in place on September 30, 1993, expired between October 1993 and December 1993. As market value gains and losses on currency exchange contracts are recognized as an offset to currency exchange losses in the statements of income (discussed in Note 8) in the period in which they occur, the carrying value is therefore equal to the fair value. At September 30, 1995 and 1994, no currency exchange contracts were outstanding.

Recent Accounting Pronouncement

In October 1995, the Financial Accounting Standards Board issued SFAS No. 123, "Accounting for Stock Based Compensation" which defines a fair value based method of accounting for an employee stock

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

option or similar equity instrument and is effective for fiscal years beginning after December 15, 1995. As allowed by SFAS No. 123, the Company plans to continue to measure compensation cost for their compensation plans using the intrinsic value based method of accounting prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" with pro forma disclosure in the future of the difference, if any, between compensation cost included in net income and the related cost measured under the fair value method.

2. RELATED-PARTY TRANSACTIONS:

Sale of 50-Percent Interest in Arethusa Heritage

On December 31, 1991, a subsidiary of Ymer Offshore AB (Ymer), a former shareholder of Arethusa, purchased a 50-percent interest in the Arethusa Heritage, for an aggregate purchase price of $10 million. The purchase price was paid $2 million in cash and the remaining $8 million in the form of a secured note.

As a part of this sale, Ymer and Arethusa also entered into option agreements in which Ymer had the right to sell back to Arethusa, and Arethusa had the right to repurchase, the Ymer interest in the rig at specified prices. Effective January 31, 1994, the Company repurchased this 50 percent interest in the Arethusa Heritage for $8.4 million. As payment for the repurchase, the Company paid $400,000 in cash and accepted cancellation of the $8.0 million promissory note which was due on January 31, 1994. The Company now owns 100% of the Arethusa Heritage.

As a result of these option agreements, Arethusa did not recognize this transaction as a sale. The Company recorded a deferred credit for the amount of the gain which was amortized based upon the approximate period of time the options were expected to be outstanding. For the years ended September 30, 1994 and 1993, respectively, Arethusa recognized $49,100 and $884,300 of gain, and $142,700 and $435,900 of interest income related to this transaction.

During fiscal years 1994 and 1993 Arethusa operated the Arethusa Heritage under a bareboat charter agreement. The charter fee totaled $357,300 and $1,076,100, respectively, during the years ended September 30, 1994 and 1993. This bareboat charter agreement terminated on January 31, 1994, in connection with Arethusa's repurchase of the 50-percent interest in the rig.

Yatzy Management and Operating Services Agreement

Prior to Arethusa's acquisition of the Yatzy in May 1995 (see Note 4), the rig was managed by Arethusa under a management and operating services agreement with Exmar, N.V. (a Belgium corporation which is related to Alphee S.A., a principal shareholder of the Company). Under the terms of the agreement, Arethusa was paid a management fee, and all operating expenses were paid by Exmar, N.V. This management fee totaled $374,500, $638,700 and $638,700 for fiscal 1995, 1994 and 1993 respectively, and the Company has recorded such fees as a reduction of Arethusa's administrative expenses.

Other Related-Party Transactions

The Company previously provided $710,000 in financing for the homes of the president and a vice president of Arethusa Off-Shore Company (AOC), a wholly owned subsidiary of Arethusa, who were recruited from outside the United States. These notes, which originally bore interest at 9 percent per annum, matured during fiscal 1994 and were renewed for additional three year terms. During fiscal year 1995, AOC agreed to take possession of the home of the vice president in full payment of his note. The remaining note receivable from the president is now payable in full in 1997, with interest due quarterly in arrears based upon the stated rate of 8.12 percent per annum. This note receivable is secured by a real estate lien note and the deed of trust for the home.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Ymer and International Maritime Investors S.A. (IMI), the majority shareholder of Alphee S.A., each guaranteed $4.5 million of the rig secured debt due August 20, 1996. The Company agreed to compensate Ymer and IMI at the rate of 1 1/2 percent per annum of the guaranteed amount. Such guarantees expired with the debt repayment in December 1994.

3. CASH FLOW INFORMATION:

For purposes of the statements of cash flows, all investments with an original maturity of three months or less are considered to be cash equivalents. Net cash used in operating activities reflects cash interest payments of approximately $7,109,000, $6,139,000 and $11,209,000; and income and withholding tax payments of approximately $1,389,000, $1,744,000 and $1,852,000 for fiscal years 1995, 1994 and 1993, respectively.

Restricted cash is comprised of balances maintained to guarantee the Company's performance under drilling contracts in Indonesia and India, and rig availability for certain drilling contract bids.

4. ASSET ACQUISITIONS:

Acquisition of the Arethusa Yatzy

On May 3, 1995, the Company acquired the Arethusa Yatzy (formerly the Yatzy), a dynamically-positioned semisubmersible drilling rig built in 1989. The rig has been managed by Arethusa since 1991 and in May 1995 began a drilling contract with Petroleos Brasileiros, S.A. (Petrobras), which is expected to keep the unit working offshore Brazil through November 1998. The purchase price was $50.2 million, $20.2 million of which was paid from existing cash balances and $30.0 million of which was funded through a new eight-year, rig-secured loan.

The following unaudited pro forma income statement data for the years ended September 30, 1995 and 1994, present the consolidated results of operations as if the acquisition had occurred at the beginning of the fiscal year 1994. The unaudited pro forma income statement data also reflect two additional significant fiscal 1995 transactions, the sale of the Treasure Stawinner discussed in Note 5 and the June 30, 1995, dividend and capital distribution of $61.0 million ($3.00 per share), as if each had occurred at the beginning of fiscal 1994. Since the gain on the sale of the Treasure Stawinner is a nonrecurring credit, this gain has not been included in this pro forma income statement data. If calculated as if the sale occured at the beginning of fiscal 1994, this gain amount would approximate $24.4 million. Such unaudited pro forma financial data may not be indicative of the results of operations of the Company had the transactions been completed on such earlier date, nor is it necessarily indicative of future financial results.

	1995	1994
	(IN THOUSANDS EXCEPT PER SHARE DATA)	
Contract Drilling Revenue	$120,166	$122,675
Net Income (Loss)	$ (8,496)	$ 883
Net Income (Loss) Per Common Share	$ (.42)	$ .04

The historical operating results for the Arethusa Yatzy included in the unaudited pro forma financial data, have been adjusted for (i) duplicate administrative expenses, (ii) depreciation expense calculated based upon Arethusa's cost and estimated useful life, (iii) a reduction in insurance expense based upon Arethusa's lower insured value, and (iv) interest expense calculated based upon Arethusa's $30.0 million note.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Acquisition of Arethusa Worker and Treasure Stawinner.

On August 20, 1993, Arethusa acquired two deepwater semisubmersible drilling rigs, the Arethusa Worker and the Treasure Stawinner, for $59.0 million in cash and 1,000,000 shares of common stock of the Company. Arethusa funded the cash portion of this acquisition with $34.0 million of cash proceeds from the IPO and $25.0 million of bank debt.

5. ASSET DISPOSITIONS:

Sale of the Treasure Stawinner

On June 30, 1995, Arethusa completed the Sale of the Treasure Stawinner for conversion to a floating production unit for Petrobras. Arethusa received $55.0 million in cash and has retained ownership of certain drilling equipment, which was removed from the rig and will be used by the Company for other purposes. Upon closing of the transaction, the Company recognized a gain of approximately $27.9 million, repaid $12.6 million of secured debt, and declared a $3 per share dividend and capital distribution to shareholders. The dividend/distribution totaled $61.0 million, and was paid on July 28, 1995 to shareholders of record as of July 14, 1995.

Sale of Miss Kitty

In July 1993, Arethusa sold the jackup Miss Kitty for $22.0 million in cash. Arethusa continues to operate the Miss Kitty pursuant to a bareboat charter agreement with the new owners which has recently been extended for an additional year through July 30, 1997. The Company realized a gain of $3.6 million which is being amortized ratably over the initial three-year charter term. The charter provides for a fixed charter fee of $9,765 per day for the first eighteen months, and thereafter a basic charter rate of $6,750 per day plus a revenue sharing component. The Company used $18.2 million of the proceeds to reduce outstanding debt.

Sale of Zapata Arctic

Effective March 30, 1992, Arethusa sold the Petrobras XXV (formerly the Zapata Arctic) to an affiliate of Petrobras, effected through a sales-type lease with a term of 10 years, for a gain of approximately $27.3 million. The lease stipulated a down payment of $2,642,500 and 40 quarterly installments, for total principal payments of $75,500,000 plus interest. The interest component of the installment was adjusted quarterly to the three-month London Interbank Market Rate plus 4 percent. At September 30, 1994 and 1993, this rate was 9.31 and 7.19 percent per annum, respectively.

The lessee had two options to purchase the rig for the then unpaid principal balance of the lease, in March 1995 or December 1997. On March 31, 1995 Petrobras exercised their purchase option under the lease of the Petrobras XXV. The Company transferred title of this rig to the Petrobras affiliate and received lease proceeds of $54.4 million in cash, which were used to pay $17.9 million of secured debt and $1.2 million in commissions.

Sale of Bonito II

Arethusa sold the Bonito II on December 31, 1991, for a gain of approximately $5.1 million. The buyer paid $25.3 million in cash for the rig and services provided by Arethusa in connection with the sale. Arethusa continues to operate the Bonito II pursuant to a bareboat charter agreement which currently extends to August 1996. The charter rate is currently $7,550 per day plus a revenue sharing component. The Company has the option to extend the charter for two additional one-year periods from August 1996.

During March 1994, the Bonito II ended its contract in India and was mobilized to the Gulf of Mexico where it commenced operations under a drilling contract in July 1994. In connection with this mobilization,

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

the Company and the owner agreed to share equally the mobilization costs. The net costs to be borne by the Company, which is approximately $1.7 million, is being deferred and amortized over a period of twenty-four months.

6. DEBT:

Long-term debt at September 30, 1995 and 1994, consists of the following (in thousands):

	1995	1994
Rig-secured debt due May 3, 2003	$ 30,000	$ --
Rig-secured debt due December 22, 1999	42,778	--
Rig-secured debt due October 30, 1996	--	52,809
Rig-secured debt due August 20, 1996	--	19,000
	72,778	71,809
Less -- Current maturities	(10,603)	(30,899)
	$ 62,175	$ 40,910

Rig-Secured Debt Due May 3, 2003

In connection with the acquisition of the Arethusa Yatzy on May 3, 1995, the Company entered into a credit agreement to borrow $30.0 million from its lending banks. Under the terms of the agreement, principal is payable in sixteen semi-annual installments of $1.9 million. Interest rates are based upon an average of the Reuters FRBD reference rates plus 1 1/2 percent per annum, and payable in arrears. The effective interest rate for fiscal year 1995 was 7.54 percent.

The loan is secured by a first mortgage on the Arethusa Yatzy. Loan covenants included, among other financial provisions, (a) maintenance of minimum collateral values, (b) restrictions on the sale of collateralized assets, (c) restrictions on declarations of dividends and (d) limitations on further indebtedness.

Rig-Secured Debt Due December 22, 1999

On December 20, 1994, the Company entered into a new credit agreement with its lending banks. Under this agreement, certain wholly-owned subsidiaries of the Company borrowed $80 million to refinance then existing rig-secured debt. During fiscal 1995 this loan was paid down by $37.2 million, which included three scheduled quarterly installments totalling $6.7 million, and two additional payments totalling $30.5 million made in connection with the monetization of the Petrobras XXV lease and the Sale of the Treasure Stawinner (see Note 5). Currently, quarterly payments on this loan total $1.7 million with a final payment of $15.4 million due in December 1999. Interest is payable quarterly in arrears and is based upon the London Interbank Market Rate plus 1 1/2 percent per annum. The effective interest rate for fiscal year 1995 was 7.97 percent.

The loan is secured by the first priority fleet mortgage on all rigs owned by the Company other than the Arethusa Yatzy. Other loan covenants are similar to those in the rig-secured debt due May 3, 2003.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Annual Maturities

The annual maturities of long-term debt (including the current portion), are as follows (in thousands):

Fiscal year ending September 30 --	
1996	$10,603
1997	10,603
1998	10,603
1999	10,603
2000	19,118
Thereafter	11,248
	$72,778

7. TAXES:

Arethusa's United States subsidiaries and Bermuda subsidiaries with operations in United States territorial waters provide taxes at the United States federal statutory rate. As of September 30, 1995, these subsidiaries collectively had United States net operating loss carryforwards of approximately $85.6 million for United States tax reporting purposes. These losses are available to benefit future United States tax expense and expire in fiscal years 2006 through 2010.

Arethusa's subsidiaries operating in the territorial waters of countries outside of the United States provide taxes at the rates applicable in those countries. The tax provision includes income and withholding taxes applicable to operations in India, Indonesia, Brazil and the Netherlands.

At the present time, no income, profit, capital or capital gain taxes are levied in Bermuda and, accordingly, no provision for such taxes has been recorded by the Company. In the event that such taxes are levied, the Company has received an undertaking from Bermuda Government exempting it from all such taxes until March 28, 2016.

Revenue agent reviews are currently in progress with respect to certain of the Company's subsidiaries and operations in Indonesia and the United States. While the Company cannot predict with certainty the outcome of such reviews, management does not believe the ultimate outcome of these reviews will have a material adverse impact on the Company's consolidated financial position or results of operations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

The Company's income (loss) before income taxes and income tax provision were (in thousands):

	INCOME (LOSS) BEFORE INCOME TAXES	TAX PROVISION
For the year Ended September 30, 1995:		
Bermuda	$ (179)	$ --
Non-Bermuda	23,245	(1,440)
	$23,064	$(1,440)
For the year Ended September 30, 1994:		
Bermuda	$ 247	$ --
Non-Bermuda	4,882	(1,542)
	$ 5,129	$(1,542)
For the year Ended September 30, 1993:		
Bermuda	$ (399)	$ --
Non-Bermuda	(2,543)	(2,061)
	$(2,942)	$(2,061)

Effective October 1, 1993, the Company adopted SFAS No. 109, "Accounting for Income Taxes," which requires recognition of deferred tax liabilities and assets for the expected future tax consequences of events that have not been recognized in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on differences between the financial statement carrying amounts and tax bases of assets and liabilities using enacted tax rates and laws in effect in the years in which the differences are expected to reverse. Prior-year financial statements were not restated for SFAS No. 109. The adoption of SFAS No. 109 had no material effect on the Company's consolidated financial position or results of operations.

No deferred taxes were required to be provided during fiscal 1995, 1994, or 1993.

The components of the net deferred tax asset (liability) as of September 30, 1995 and 1994, are as follows (in thousands):

	1995	1994
Deferred tax assets --		
Net U.S. operating loss carryforwards	$ 29,964	$ 24,481
Accruals and reserves	514	409
Valuation allowance	(23,543)	(19,761)
	6,935	5,129
Deferred tax liabilities --		
Excess of tax over book depreciation	(6,935)	(5,129)
Net deferred tax asset (liability)	$ --	$ --

8. CURRENCY EXCHANGE:

In an effort to minimize the effects of exchange rate fluctuations, the Company generally hedges its exposure through obtaining payment for drilling contracts in United States Dollars. During fiscal years 1994 and 1993, the Company also entered into currency exchange contracts to address specific risks. The Company does not engage in currency speculation. At September 30, 1993, the Company had contracts maturing between October and December 1993 requiring it to purchase $3.6 million in foreign currency (the equivalent

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

of 119.0 million Indian rupees). During fiscal year 1994, the Company committed to an additional $1.0 million of currency exchange contracts which matured between December 1993 and June 1994. There were no currency exchange contracts in place at September 30, 1995 or 1994. Market value gains and losses on the currency exchange contracts have been recognized as an offset to currency exchange losses in the statements of income. Total currency exchange losses recorded in the statements of income were approximately $1.2 million, $1.2 million and $1.8 million for fiscal years 1995, 1994 and 1993, respectively. These losses primarily resulted from operations in Brazil and India.

9. MAJOR CUSTOMERS AND CONCENTRATION OF CREDIT RISKS:

Arethusa's customer base includes major and independent oil and gas companies and government owned oil companies. During fiscal 1995, 1994 and 1993, the Company earned 52.1 percent, 54.3 percent, and 49.1 percent, respectively, of its revenues from major customers. A summary of the major customers for these years were as follows: year ended September 30, 1995 -- Petrobras and Shell Oil Company, 27.8 percent and 24.3 percent, respectively; year ended September 30, 1994 -- Petrobras, Marathon Oil Company, and Maxus Southeast Sumatra, Inc., 26.3 percent, 15.0 percent and 13.0 percent, respectively; year ended September 30, 1993 -- Indian Oil & Natural Gas Commission, Maxus Southeast Sumatra, Inc. and Petrobras, 17.4 percent, 15.8 percent and 15.9 percent, respectively.

10. COMMITMENTS AND CONTINGENCIES:

Operating Lease

Arethusa is committed under a lease agreement for office space which continues until August 30, 2002. The lease may be canceled in December 1996 for a lump-sum payment of approximately $1,023,000. Under the terms of the lease, the Company only made cash payments to reimburse the landlord for operating expenses through December 31, 1993. The Company began making additional payments for base, rental installments on January 1, 1994. Rental charges are expensed on a straight-line basis over the term of the lease. The Company recognized rental expense of approximately $566,000, $552,000 and $524,000 of which approximately $203,000, $211,000 and $183,000 were paid as operating expenses in fiscal years 1995, 1994 and 1993, respectively. Estimated future minimum lease payments, excluding reimbursable operating expenses, under this operating lease are as follows (in thousands):

Fiscal year --	
1996	$ 373
1997	392
1998	463
1999	487
2000	509
Thereafter	989
	$3,213

Litigation

Arethusa is engaged in various claims and litigation arising from operations. In the opinion of management, uninsured losses, if any, resulting from these matters will not have a material adverse effect on Arethusa's results of operations or financial position.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

11. BENEFIT PLANS:

Pension Plan

AOC established a defined benefit pension plan effective October 1, 1992, which covers substantially all U. S. citizens and U. S. permanent residents who are employed by AOC. Employees are automatically enrolled in the plan following the completion of one year of service and are 100 percent vested after five years of service. Benefits are calculated and paid based on employees' years of credited service and average final compensation using an excess benefit formula integrated with social security covered compensation.

Pension costs are determined actuarially and funded to the extent allowable under the Internal Revenue Code. The plan's assets are invested in cash and cash equivalents, equity securities, government and corporate debt securities.

The significant actuarial assumptions as of the plan's year-end are set forth in the following table:

	SEPTEMBER 30,	
	1995	1994
Discount rate	7.5%	8.1%
Expected long-term rate	9.0%	9.0%
Compensation projection rate	5.0%	5.0%

The funded status as of September 30, 1995 and September 30, 1994, is set forth in the following table (in thousands):

	1995	1994
Benefit obligation -- Vested	$ (7,159)	$(5,394)
-- Non-vested	(663)	(254)
Accumulated benefit obligation	(7,822)	(5,648)
Effect of compensation projection	(3,061)	(2,916)
Projected benefit obligation	(10,883)	(8,564)
Plan assets at fair value	8,421	6,725
Projected benefit obligation in excess of plan assets	(2,462)	(1,839)
Unrecognized loss	2,329	1,339
Unrecognized prior service cost	(299)	--
Contributions	123	--
Accrued pension cost	$ (309)	$ (500)

Net periodic pension cost for the fiscal year ended September 30, 1995 and 1994 includes the following components (in thousands):

	1995	1994
Service cost of benefits earned	$ 566	$ 575
Interest cost on projected benefit obligations	692	619
Actual return on plan assets	(1,014)	227
Deferred gain (loss)	401	(855)
Amortization of loss	43	53
Amortization of prior service cost	(21)	--
Net period pension cost	$ 667	$ 619

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

Profit-Sharing Plan

AOC established a defined contribution profit-sharing plan effective October 1, 1992 which covers substantially all U.S. citizens, U.S. permanent residents and third country national expatriates who are employed by AOC. The plan and trust agreement are intended to meet the requirements of Section 401(a) and all related sections of the Internal Revenue Code.

Employees may enroll in the plan following the completion of one year of service. Participants may elect to make contributions from 1 percent up to 16 percent of gross monthly salary to the plan: a maximum of 10 percent on a 401(k) basis; a maximum of 16 percent on a 401(m) basis. All amounts contributed to the plan are deposited in a trust with a national bank and administered by independent trustees.

At the end of the plan year on September 30, the Company will match a minimum of 10 percent up to a maximum of 100 percent of eligible basic contributions made by participants during the plan year. The basic rate of contribution used to determine the Company matching amount is 6 percent, on a 401(k) or 401(m) basis. The actual matching percentage is determined by the Company's Board of Directors at the end of the plan year. AOC made profit-sharing provisions of approximately $276,000, $134,000 and $120,000 for 1995, 1994 and 1993, respectively.

Employee Stock Option Plan

In August 1993, the Company adopted the Arethusa (Off-Shore) Limited 1993 Employee Stock Option Plan (the Employee Plan) pursuant to which a maximum aggregate of 666,667 shares of Common Stock are available for grant to eligible employees. Options granted pursuant to the Employee Plan vest in equal installments over three years and remain exercisable for a period of seven years, so long as the option holder remains an employee of the Company as of the date of exercise. The exercise price of options granted under the Employee Plan equal the market price of the Common Stock on the date of grant. The Employee Plan provides for the adjustment of the number of shares awarded thereunder, and the exercise price thereof, on any stock dividend, any subdivision or combination of the outstanding shares of Common Stock and any merger, consolidation, recapitalization of the Company or similar event which affects the issued and outstanding shares of Common Stock.

In August 1993, the Company granted 466,666 options at an option price of $10 per share, the market price in the IPO. Accordingly, no compensation expense has been recorded with respect to these options.

As of September 30, 1995 there were 308,000 exercisable options, and 4,667 options had been canceled and surrendered. No options have been exercised.

In September 1995 the board of directors approved a $3 per share reduction in the option price to $7 per share, subject to shareholder approval at the next annual general meeting. This action was proposed as a result of the $3 per share dividend and capital distribution paid by the Company in July 1995.

Non-employee Director Stock Option Plan

In February 1995, the Company's shareholders approved the Arethusa (Off-Shore) Limited 1994 Nonqualified Stock Option Plan for Non-Employee Directors ("Directors' Plan"), pursuant to which a maximum aggregate of 250,000 shares of common stock were authorized. Under the Directors' Plan eligible directors were granted an option to purchase 20,000 shares of the Company's common stock, at an exercise price equal to the fair market value of the common stock on the date of grant. Options granted under this plan vest in equal annual installments over a three-year period, and expire seven years from date of grant.

As of September 30, 1995, 160,000 options had been granted under the Directors' Plan; 100,000 of these options carry an option price of $11.25 based upon a May 1994 date of grant, and the remaining 60,000 options

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

have an option price of $12.625 based on a February 1995 date of grant. In May 1995, approximately 33,000 options became exercisable. No options have been exercised or cancelled.

12. GEOGRAPHIC INFORMATION (UNAUDITED):

The nature of the Company's operations and assets requires movement among geographic areas in response to market conditions and contract requirements. Therefore, the operations and assets reported within a particular geographic area may not be indicative of a long-term operating commitment in that area. Assets are included in the geographic information shown below according to operating location (in thousands):

	UNITED STATES	NORTH SEA	SOUTHEAST ASIA	SOUTH AMERICA	INDIA	BERMUDA AND OTHER	ELIMINATIONS	TOTAL
Year Ended September 30, 1995 --								
Revenues	$ 72,008	$ 8,769	$ 6,902	$ 33,979	$ 7,289	$32,788	$(39,588)	$122,147
Operating income (loss)	(8,667)	(2,172)	(1,117)	7,022	1,488	(565)	--	(4,011)
Identifiable assets	170,159	29,736	16,937	82,331	2,797	13,372	--	315,332
Year Ended September 30, 1994 --								
Revenues	$ 64,273	$ 6,116	$15,593	$ 31,648	$10,255	$22,123	$(29,796)	$120,212
Operating income (loss)	(3,346)	(2,513)	3,910	7,662	281	(694)	--	5,300
Identifiable assets	163,610	31,501	33,165	116,982	2,408	156	--	347,822
Year Ended September 30, 1993 --								
Revenues	$ 40,994	$12,582	$14,887	$ 19,911	$16,307	$ --	$(10,520)	$ 94,161
Operating income (loss)	(9,383)	550	2,726	4,813	1,967	(478)	--	195
Identifiable assets	168,494	34,210	33,454	126,509	6,346	--	--	369,013

13. QUARTERLY FINANCIAL DATA (UNAUDITED):

Unaudited summarized data by quarter for fiscal 1995 and 1994 is as follows (in thousands, except per share amounts):

	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER	TOTAL
1995 --					
Contract drilling revenue	$28,279	$27,167	$32,232	$34,469	$122,147
Operating income (loss)	(1,654)	(3,246)	(525)	1,414	(4,011)
Income (loss) before income taxes	(1,375)	(2,957)	26,687	709	23,064
Net income (loss)	(1,690)	(3,232)	26,414	132	21,624
Net income (loss) per common share	$ (.08)	$ (.16)	$ 1.30	$ .01	$ 1.06
1994 --					
Contract drilling revenue	$30,147	$30,967	$29,219	$29,879	$120,212
Operating income	1,786	2,042	971	501	5,300
Income before income taxes	1,518	2,094	948	569	5,129
Net income	1,059	1,632	546	350	3,587
Net income per common share	$ .05	$ .08	$ .03	$ .02	$ .18

14. EVENT (UNAUDITED) SUBSEQUENT TO DATE OF REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS:

On December 7, 1995, Arethusa entered into a letter of intent with Diamond Offshore Drilling, Inc. ("Diamond Offshore") for the merger of the two companies. The terms of the proposed transaction provide that, upon satisfaction of certain conditions precedent, including execution of definitive agreements (which execution occurred February 9, 1996) and obtaining approval from Arethusa and Diamond Offshore shareholders and certain regulatory agencies, each of the issued and outstanding shares of Arethusa common stock would be converted into the right to receive .88 shares of Diamond Offshore common stock. On

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ARETHUSA (OFF-SHORE) LIMITED AND SUBSIDIARIES -- (CONTINUED)

February 9, 1996, Arethusa declared a cash dividend of $.25 per share to the holders of its common stock. Management anticipates the merger will be consummated no later than July 31, 1996.

Upon successful consummation of the merger, options awarded to certain officers, directors and employees of Arethusa will become fully vested and exercisable. Additionally, AOC has entered into executive severance agreements with certain executive officers and has amended its severance policy for most shore based employees which will provide payment of certain additional benefits to the employees if they are terminated following the merger.

Additionally, subject to approval by Arethusa shareholders and to a successful merger, the exercise price of options granted under the 1993 Employee Stock Option Plan (approximately 462,000 shares granted) would be reduced by $3 per share. In the event the option exercise price is reduced to $7 per share, Arethusa would be required to record compensation expense in its financial statements for the difference between the revised exercise price of $7 per share and the market value on the date approval is received from shareholders. To the extent the market value of Arethusa shares continues to increase above the exercise price there will be an increased charge to compensation expense.

NO DEALER, SALESMAN OR ANY OTHER PERSON HAS BEEN AUTHORIZED TO GIVE ANY INFORMATION OR TO MAKE ANY REPRESENTATION NOT CONTAINED IN THIS PROSPECTUS SUPPLEMENT OR THE PROSPECTUS AND, IF GIVEN OR MADE, SUCH INFORMATION OR REPRESENTATION MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY DIAMOND OFFSHORE OR ANY UNDERWRITER. THIS PROSPECTUS SUPPLEMENT AND THE PROSPECTUS DO NOT CONSTITUTE AN OFFER TO SELL OR A SOLICITATION OF AN OFFER TO BUY ANY OF THE SECURITIES OFFERED HEREBY IN ANY JURISDICTION TO ANY PERSON TO WHOM IT IS UNLAWFUL TO MAKE SUCH OFFER IN SUCH JURISDICTION. NEITHER THE DELIVERY OF THIS PROSPECTUS SUPPLEMENT OR THE PROSPECTUS NOR ANY SALE MADE HEREUNDER SHALL, UNDER ANY CIRCUMSTANCES, CREATE ANY IMPLICATION THAT THE INFORMATION HEREIN IS CORRECT AS OF ANY TIME SUBSEQUENT TO THE DATE HEREOF OR THAT THERE HAS BEEN NO CHANGE IN THE AFFAIRS OF DIAMOND OFFSHORE SINCE SUCH DATE.

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7,523,140 SHARES

[DIAMOND OFFSHORE LOGO]

COMMON STOCK

PROSPECTUS SUPPLEMENT

MERRILL LYNCH INTERNATIONAL

CS FIRST BOSTON

SALOMON BROTHERS
INTERNATIONAL LIMITED

May 20, 1996