

2004 To Do:

- ACHIEVE FULL YEAR PROFITABILITY
- STRENGTHEN LIQUIDITY + CASH POSITION
- COMPLETE + DELIVER LEGACY PROJECTS (UNDER FORECAST)
- CONCLUDE CAPITAL RESTRUCTURING PROGRAM
- RESOLVE R+W SITUATION
- GROW J. RAY BACKLOG

Positioning for the Future



2004 Annual Report

Fellow Shareholders

Marine Construction Services

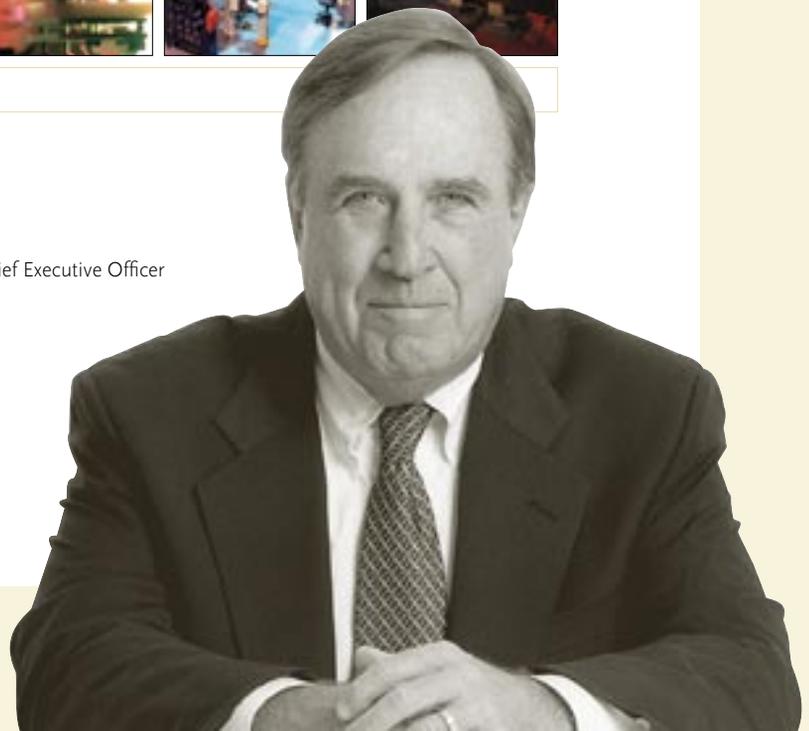


Since becoming your CEO and Chairman in 2000, my goals have remained consistent. We expect to build sustainable profitability around our three “franchise name” businesses, improve liquidity, strengthen the balance sheet and simplify our corporate structure. During 2004, McDermott International, Inc. (“McDermott”) achieved substantial progress in these areas and as a result, McDermott is better positioned for the future.



Government Operations

Bruce W. Wilkinson, Chairman of the Board and Chief Executive Officer



McDermott is the parent company of three distinct operating subsidiaries. BWX Technologies, Inc. ("BWXT") provides nuclear material and equipment, primarily for the U.S. Navy, and it manages and operates ("M&O") various sites for the U.S. Department of Energy. BWXT is a specialized company in our nation's defense industry and is reflected in our "government operations" segment. J. Ray McDermott ("J. Ray") is a leading marine construction company, serving the growing worldwide offshore oil and gas industry. Its operations are reflected in our "marine construction services" segment. J. Ray and BWXT are the primary operations represented in McDermott's consolidated financial statements in the enclosed Form 10-K.

Our third subsidiary, The Babcock & Wilcox Company ("B&W"), is not consolidated with McDermott's financial statements and it hasn't been since B&W's Chapter 11 bankruptcy filing in early 2000. B&W's insolvency did not result from its normal business operations, but rather was due to an overwhelming number of personal injury claims filed against it related to asbestos. A summary of B&W's 2004 financial results, however, is included for your review in Note 20 in the enclosed Form 10-K.

Major highlights from 2004

2004 was a busy and productive year at McDermott. Much was accomplished and the results we generated reflect a tremendous amount of effort by our entire team. The achievements we attained will position McDermott for a brighter future. Some of the major highlights include:

- BWXT achieved operating income of \$109.9 million, a new record for this business unit. It also maintained a \$1.7 billion backlog of work and won a major M&O contract;
- J. Ray contributed \$83.8 million in operating income through a combination of improved operating results, completion of the four remaining legacy projects below the revised estimate, and by selling certain non-strategic assets;
- The capital structure refinancing, which began in 2003, was completed. J. Ray culminated this effort with a new letter of credit facility, and it strengthened its liquidity and cash flow during the year;
- As a result of a stronger J. Ray, the "going-concern" uncertainty that was previously expressed about this business has now been removed;
- A multi-year effort to retrieve \$38 million from a terminated U.K. pension plan was completed, representing our share of the surplus plan assets which was received in early 2005; and
- Together, these solid segment results led McDermott to achieve 2004 net income of \$0.90 per diluted share.

Positioning for the future: 2004 Year in Review

McDermott entered 2004 with momentum but there was still much to accomplish. Issues we faced included to: complete J. Ray's legacy loss projects within the revised estimate or ideally, under it; better match the capacity of J. Ray's assets and resources with its backlog by winning new awards; sell underutilized or non-strategic assets and lower the cost structure; improve J. Ray's financial strength and liquidity to eliminate doubts about its business model; continue to book new work at BWXT, win M&O contracts and lower its costs; and resolve the B&W bankruptcy. These weren't easy issues to resolve, but our approach was to take them head on.

First and foremost, the operations needed to perform. BWXT was a shining star. While this unit's results will vary quarter-to-quarter like our other businesses, it has remained consistently profitable, driving its costs lower and adding new work. As a result, BWXT produced record income, secured \$389 million in new manufacturing awards and was awarded a major M&O contract. J. Ray was also up to the task. As the new leadership team's processes and procedures continued to gain traction, the improvements were reflected in J. Ray's financial results. During 2004, J. Ray completed its four remaining legacy loss projects with results better than estimated at the beginning of the year. This performance generated \$47 million of improvements on these projects which was reflected as



Strengthen Liquidity & Cash Position

How We Did It

Cash and liquidity are vital ingredients for engineering and construction companies like McDermott. In early 2004, we focused on improving this metric through our liquidity improvement plan. Key activities included performing better on projects than earlier estimates, resolving a multi-year pension issue, completing a new letter-of-credit facility, selling non-core assets and focusing on our cash expenditures.

What It Means

McDermott is stronger financially today than in recent years. At December 31, 2004, our company had more liquidity than debt, and we are better positioned with improved flexibility to operate in the industry.

Our focus on cash will continue as we move forward in 2005.

2004 operating income. It also meant that the associated cash expected to be spent remained in our accounts. J. Ray performed well on its other projects and also signed \$1.1 billion of new work and change orders, which demonstrates our customers' ongoing confidence in the business. Together, the improved operations enabled substantial progress to be made in addressing the other issues as well.

Liquidity concerns had been an issue at J. Ray, primarily as a result of the legacy loss projects and questions regarding its ability to obtain financing. As the performance on the loss projects continually improved in 2004, so did J. Ray's cash forecast. To further enhance cash, we implemented the liquidity improvement plan. Assets were evaluated and those that were non-strategic or didn't earn an acceptable return were slated for divestiture. In 2004, J. Ray sold three vessels and one idle fabrication facility generating over \$80 million in sales proceeds. The asset sales also enabled J. Ray to recognize \$30 million in gains. While most of the cash obtained from the sales is currently restricted by J. Ray's bond indenture, these proceeds are expected to fund J. Ray's capital expenditure program for 2005. Another part of our plan was to complete our capital restructuring program with a new letter-of-credit facility. This \$25 million facility was signed in August 2004. As a result of the liquidity improvement plan, better operating performance and its \$156 million of unrestricted cash at year end, the going concern language associated with J. Ray has been removed from its audited financial statements.

Managing our cost structure is an ongoing effort at McDermott. BWXT's customers expect it. J. Ray is a cyclical business, and managing costs is the only way to address that reality. Both businesses were successful in this regard during 2004. It was the key driver to BWXT's record financial performance. And, with J. Ray reducing costs in certain areas that were slowing, it helped minimize the impact on its financial results.

All in all, the plans we executed in 2004 were successful and the price of McDermott shares began to reflect our achievements. McDermott shares ended the year trading at \$18.36, a 2004 appreciation of over 53 percent and a new five-year high.



Complete & Deliver J. Ray Legacy Projects

How We Did It

In 2001, J. Ray was awarded several large projects from our customers. In hindsight, some of the jobs were risky and the contracting strategy was flawed. However, the new J. Ray team still needed to deliver the finished product.

In 2004, this mission was accomplished, and with better results than previous estimates.

What It Means

Credibility. J. Ray proved that despite financial hardships, it delivers what it promises. Our customers received the quality projects they wanted and are now producing hydrocarbons. In the future, when customers have a challenging project, they'll know J. Ray will get it done. It's what we do.

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The future: 2005 and beyond

While McDermott is better positioned for the future, some challenges and issues remain.

The largest remaining item from our 2004 “to do” list is resolving the B&W Chapter 11 bankruptcy, which continues to require substantial effort. B&W's bankruptcy related to its use of asbestos in products prior to McDermott's acquisition of it in 1979 and the hundreds of thousands of claims that have followed.

Similar to my discussion in last year's letter, I foresee two paths to resolve B&W's bankruptcy. The first alternative is through our negotiated settlement currently in the court system. The current settlement involves providing to a plaintiff's trust 100 percent of B&W's stock, issuing a \$92 million note, delivering 4.75 million shares of McDermott stock with price guarantees and assigning over \$1 billion of insurance coverage. In December 2003, our shareholders voted to give our board of directors the authority to approve this settlement. In October 2004, the bankruptcy court issued its recommendation. The final steps include obtaining a confirmation order from the federal district court, resolving any appeals that may be filed and board approval. It is difficult to predict when this settlement may become effective, but it could be resolved as early as this summer, or if appeals are filed, it could continue through 2006.

The preferred alternative for resolving B&W's bankruptcy continues to be national legislation that would create a trust fund for victims of asbestos exposure. This trust would be funded by companies such as B&W and their insurers, not taxpayers or the government. Asbestos-related claimants who are ill would be timely compensated while those with no signs of illness would receive medical monitoring only, unless they later become impaired. Under such a plan, American companies could be comfortable hiring in the U.S manufacturing sector again. An untold number of cases would leave our courts. American businesses would know their obligations with certainty and would no longer be subject to a “lottery” system of jury trials. Most importantly, the truly ill would be

paid quickly and in many cases, in amounts greater than obtained through the court system. In B&W's case, for instance, no claims have been paid, even to the truly ill, since filing bankruptcy in February 2000.

In 2004, legislation was proposed in the U.S. Senate creating such a national trust, however it was blocked by the minority party and never reached the floor for a vote. In early 2005, Senator Arlen Specter, chairman of the Judiciary Committee, revived, modified and plans to propose legislation. You can assist in the prospect of its passage by contacting your Senators to convey your support for asbestos resolution legislation. I urge you to do so. It is my sincere hope that ownership of B&W can be maintained as a result of this legislation currently under study. The outcome, however, remains speculative as of this writing.

There are other issues, of course, that we face entering 2005 and beyond. J. Ray ended 2004 with \$1.25 billion in backlog, and it needs to grow this amount in 2005. To build its backlog, J. Ray must continually bid work effectively and profitably, and win a sufficient number of bids. At the same time, however, J. Ray must manage costs to reflect its workload and achieve consistent profitability regardless of the cycle. While J. Ray provided substantial income in 2004, some of the sources of that income will not repeat. Examples include the gains on sales of assets and the income generated from improvements in the legacy projects. J. Ray's business is lumpy, cyclical and competitive; these facts will not change, so we must manage this reality. BWXT needs to continue to win awards both in its manufacturing and M&O operations, maintain its customers' confidence, control its costs and drive its profits. At the corporate level, McDermott must continue to manage the cost of the pension plans it sponsors as well as the increased accounting and regulatory costs due to Sarbanes-Oxley. These are just a few.

I am pleased however that, with the exception of the B&W bankruptcy resolution, most of the issues we face now relate to normal operations in our day-to-day business. We have progressed beyond a crisis, or fire-fighting, mode. The concerns of the last few years regarding liquidity, volatile loss projects and financing capability are now largely behind McDermott. This is not to say it will all be easy in the future, but it should certainly be more in our control.

As always, I've tried to be frank and open in this letter, discussing the big picture items affecting your company. The attached 10-K provides much more detail and information particularly on our financials, and I encourage you to review it fully.

I am honored to be the Chairman and Chief Executive Officer of McDermott International, Inc. Not a day goes by where I'm not thankful for the privilege to serve our shareholders in this role. Again in 2004, I was fortunate enough to meet personally with the majority of our shareholder base in meetings and conferences. I value the input, opinions and inquiries about our company.

I also want to thank the employees of the McDermott family for all their hard work and efforts throughout 2004. I am gratified to be a colleague of these dedicated men and women working for a common set of goals. Through our efforts, McDermott is positioned for the future, and the future is now.

Best regards,



Bruce W. Wilkinson, Chairman of the Board and Chief Executive Officer

March 2005

J Ray McDermott



OVERVIEW

J. Ray McDermott provides offshore solutions to the oil and gas industry with engineering, fabrication and marine operations in the Americas, Middle East, Caspian and Asia Pacific. An industry leader since 1947, the company has the technical expertise and resources to provide a broad range of services, including design, project management, fabrication, transportation and installation.

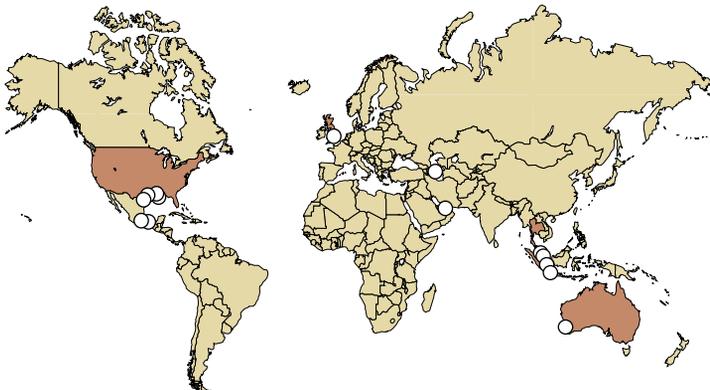
J. Ray achieved a financial turnaround in 2004 with operating income of \$83.8 million. The company improved its underlying business, completed all projects that generated losses in prior years, sold non-strategic assets and reduced costs. Entering 2005 in much improved financial condition, J. Ray maintains a profitable backlog and is actively bidding on new projects.

2004 HIGHLIGHTS

- Spar projects completed: Devils Tower and Front Runner. With Medusa, delivered in 2003, all the Spars are now producing for their customers.
- Other notable projects completed: Belanak FPSO – Batam; three of four BP topside projects (Holstein, Mad Dog and Thunder Horse) – Morgan City; Carina & Aires – Argentina; and Central Azeri deck – Caspian
- Gulf of Mexico Marine installations: Shell Llano; Cameron Highway Oil Pipeline Systems; Taylor Energy Simba
- Total Recordable Incident Rate reduced to 0.78 in 2004, from 1.14 in 2003. J. Ray is an industry leader in safety performance.
- Noteworthy project awards/expansions in 2004: Dolphin, Saudi Aramco and RasGas – Middle East; John Brookes and Sakhalin Island – Asia Pacific; and Azeri, Chirag and Gunashli – Caspian



J. RAY McDERMOTT BACKLOG
Dollars in Billions



J. RAY McDERMOTT

WORLDWIDE OPERATIONS

- Houston, Texas
- New Orleans, Louisiana
- Morgan City, Louisiana
- Harbor Island, Texas
- Mexico City, Mexico
- Veracruz, Mexico
- Wembley, England
- Baku, Azerbaijan
- Dubai, United Arab Emirates
- Batam, Indonesia
- Jakarta, Indonesia
- Kuala Lumpur, Malaysia
- Singapore
- Perth, Australia

BWXT



OVERVIEW

Fifty years ago BWX Technologies, Inc. (BWXT) supplied nuclear components for the world's first atomic-powered submarine, the USS NAUTILUS, setting a marker from which numerous milestones would spawn.

Today, BWXT and its joint ventures continue to lead change as it conducts the government operations business for McDermott.

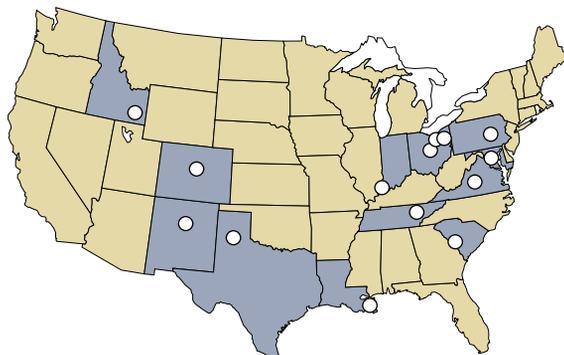
BWXT delivers nuclear innovations and manufacturing capabilities to government and commercial clients. The company supports the U.S. in safely converting and disposing of Cold War nuclear materials. It also provides environmental remediation, waste management and analytical services and manages and operates facilities and sites for the Department of Energy.

2004 HIGHLIGHTS

- BWXT's backlog of \$1.7 billion is strengthened with 2004 manufacturing awards in excess of \$389 million.
- Battelle Energy Alliance and team member BWXT win \$4.8 billion Idaho National Laboratory M&O contract.
- Significant upgrades continue at the Y-12 National Security Complex with approval for the Highly Enriched Uranium Materials Facility, the largest design effort at Y-12 in more than a decade.
- 10,000th plutonium pit was repackaged at BWXT Pantex, a milestone that also incorporates improvements in production time and reduces radiation exposure.
- BWXT facilities improve safety performance by 48 percent.
- BWXT safely cleans up Parks Township site; Nuclear Regulatory Commission releases site for unrestricted use.
- BWXT launches initiative in support of continuous security improvement efforts of U.S. Government customers.



BWXT BACKLOG
Dollars in Billions



BWXT OPERATIONS

- New Orleans, Louisiana
- Amarillo, Texas
- Los Alamos, New Mexico
- Golden, Colorado
- Idaho Falls, Idaho
- Aiken, South Carolina
- Oak Ridge, Tennessee
- Lynchburg, Virginia
- Mt. Vernon, Indiana
- Miamisburg, Ohio
- Alliance, Ohio
- Barberton, Ohio
- Pittsburgh, Pennsylvania
- Washington, DC

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Chairman of the Board and
Chief Executive Officer of
McDermott International, Inc.

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President,
Smith Technologies

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Former Chairman of the Board and
Chief Executive Officer,
Newmont Mining Corporation

BRUCE DeMARS^{1 3 4}

Partner, RSD, LLC; Admiral,
United States Navy (Retired)

JOE B. FOSTER^{1 3}

Former Chairman of the Board
and Chief Executive Officer,
Newfield Exploration Company;
Former Interim Chairman of the Board,
President and Chief Executive Officer,
Baker Hughes Incorporated

ROBERT L. HOWARD^{2 3}

Former Vice President,
Shell Oil Company

OLIVER D. KINGSLEY, JR.^{2 3}

Former President and
Chief Operating Officer,
Exelon Corporation

D. BRADLEY McWILLIAMS^{1 2}

Former Senior Vice President and
Chief Financial Officer,
Cooper Industries Ltd.

THOMAS C. SCHIEVELBEIN^{1 2}

Former President,
Northrop Grumman Newport News

RICHARD E. WOOLBERT^{2 3}

Former Executive Vice President and
Chief Administrative Officer,
McDermott International, Inc.

¹ Audit Committee

² Compensation Committee

³ Governance Committee

⁴ Lead Director

Officers of McDermott International, Inc. and Subsidiaries

Corporate Staff

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Chairman of the Board and
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FRANCIS S. KALMAN

Executive Vice President and
Chief Financial Officer

JOHN T. NESSER, III

Executive Vice President,
General Counsel and Corporate Secretary

LOUIS J. SANNINO

Executive Vice President,
Human Resources,
Health, Safety and Environmental

JAMES R. EASTER

Vice President, Finance and Treasurer

THOMAS A. HENZLER

Vice President and
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Babcock & Wilcox

DAVID L. KELLER

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BRANDON C. BETHARDS

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Fossil Power Division

EILEEN M. COMPETTI

President,
Diamond Power International, Inc.

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Vice President and General Manager,
B&W Service Company

MICHAEL G. MORASH

Vice President and General Manager,
B&W Construction Company

RICHARD E. REIMELS

President,
Babcock & Wilcox Canada

MARVIN D. SEHN

Controller

J. Ray McDermott

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President and Chief Operating Officer

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Vice President and General Manager,
Middle East and Caspian Operations

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Vice President, Controller/IT

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Vice President, Project Services

F. RICKEY OEHRLEIN

Vice President,
Caspian Operations

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Vice President and General Manager,
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BWX Technologies

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Nuclear Equipment Division

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