

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(MARK ONE)

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1998
OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NO. 1-7615

KIRBY CORPORATION

(Exact name of registrant as specified in its charter)

NEVADA

(State or other jurisdiction of
incorporation or organization)

74-1884980

(I.R.S. Employer
Identification No.)

1775 ST. JAMES PLACE, SUITE 200
HOUSTON, TEXAS

77056-3453
(Zip Code)

(Address of principal executive offices)

Registrant's telephone number, including area code: (713) 435-1000

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

| TITLE OF EACH CLASS | NAME OF EACH EXCHANGE ON WHICH REGISTERED |
|---------------------|---|
|---------------------|---|

| | |
|--|----------------------------|
| COMMON STOCK -- \$.10 PAR VALUE PER SHARE | NEW YORK STOCK EXCHANGE |
|--|----------------------------|

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: NONE

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

As of February 25, 1999, 20,295,894 shares of common stock were outstanding. The aggregate market value of common stock held by nonaffiliates of the registrant, based on the closing sales price of such stock on the New York Stock Exchange on February 24, 1999 was \$286,761,742. For purposes of this computation, all executive officers, directors and 10% beneficial owners of the registrant are deemed to be affiliates. Such determination should not be deemed an admission that such executive officers, directors and 10% beneficial owners are affiliates.

DOCUMENTS INCORPORATED BY REFERENCE

The Company's definitive proxy statement in connection with the Annual Meeting of the Stockholders to be held April 20, 1999, to be filed with the Commission pursuant to Regulation 14A, is incorporated by reference into Part III of this report.

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PART I

ITEM 1. BUSINESS

THE COMPANY

Kirby Corporation (the "Company") was incorporated in Nevada on January 31, 1969 as a subsidiary of Kirby Industries, Inc. ("Industries"). The Company became publicly owned on September 30, 1976 when its common stock was distributed pro rata to the stockholders of Industries in connection with the liquidation of Industries. At that time, the Company was engaged in oil and gas exploration and production, marine transportation and property and casualty insurance. Since then, through a series of acquisitions and divestitures, the Company has become primarily a marine transportation company and is no longer engaged in the oil and gas or the property and casualty insurance businesses. In 1990, the name of the Company was changed from "Kirby Exploration Company, Inc." to "Kirby Corporation" because of the changing emphasis of its business.

Unless the context otherwise requires, all references herein to the Company include the Company and its subsidiaries.

The Company's principal executive office is located at 1775 St. James Place, Suite 200, Houston, Texas 77056, and its telephone number is (713) 435-1000. The Company's mailing address is P.O. Box 1745, Houston, Texas 77251-1745.

BUSINESS AND PROPERTY

The Company, through its subsidiaries, conducts operations in two business segments: marine transportation and diesel repair.

The Company's marine transportation segment is engaged in the inland transportation of industrial chemicals, petrochemical feedstocks, agricultural chemicals and refined petroleum products by tank barges, and the offshore transportation of dry-bulk, container and palletized cargoes by barge. The Company's marine transportation segment is strictly a provider of transportation services and does not assume ownership of any of the products that it transports. All of the Company's vessels operate under the U.S. flag and are qualified for domestic trade under the Jones Act.

The Company's diesel repair segment is engaged in the overhaul and repair of diesel engines and related parts sales in three distinct markets: the marine market, providing aftermarket service for vessels powered by large, medium-speed diesel engines utilized in the various inland and offshore marine industries; the locomotive market, providing aftermarket service for the shortline and the industrial railroad markets; and the stationary market, providing aftermarket service for small power generation applications and stand-by generation components of the nuclear industry.

The Company was engaged through subsidiaries in the offshore transportation of refined petroleum products by tankers and harbor service operations. On March 16, 1998, all of the tankers and harbor service operations were sold and the tanker and harbor service operations for the 1997 year were reflected as discontinued operations and previously reported financial statements were restated. See "Discontinued Operations" on page 16 of Item 1 and Note 2 to the notes to financial statements included under Item 8 elsewhere herein for further disclosures on the sale of the tanker and harbor service operations.

Effective September 30, 1998, the Company sold its remaining 45% voting common stock interest in a property and casualty insurance company operating exclusively in the Commonwealth of Puerto Rico. See "Insurance" on page 15 of Item 1 and Note 3 to the notes to financial statements included under Item 8 elsewhere herein for further disclosure.

The Company and its transportation and diesel repair subsidiaries have approximately 1,570 employees, all of which are in the United States.

The following table sets forth by segment the revenues, operating profits and identifiable assets attributable to the continuing principal activities of the Company for the periods indicated (in thousands):

| | YEARS ENDED DECEMBER 31, | | |
|---|--------------------------|-----------|-----------|
| | 1996 | 1997 | 1998 |
| Revenues from unaffiliated customers: | | | |
| Marine transportation..... | \$249,594 | \$256,108 | \$244,839 |
| Diesel repair..... | 70,422 | 79,136 | 82,241 |
| Other..... | 3,568 | 1,290 | 5,175 |
| Consolidated revenues..... | \$323,584 | \$336,534 | \$332,255 |
| Operating profits: | | | |
| Marine transportation..... | \$ 38,172 | \$ 39,542 | \$ 37,661 |
| Diesel repair..... | 5,376 | 6,189 | 8,050 |
| Impairment of long-lived assets..... | -- | -- | (8,333) |
| Equity in earnings of insurance affiliate..... | 43,548 | 45,731 | 37,378 |
| Loss on sale of insurance affiliate..... | 2,171 | 4,609 | 1,325 |
| Equity in earnings of marine affiliates..... | -- | -- | (10,536) |
| Other income..... | 3,912 | 3,084 | 946 |
| General corporate expenses..... | 3,568 | 1,290 | 5,175 |
| Interest expense..... | (5,786) | (4,864) | (5,375) |
| Earnings from continuing operations before taxes on income..... | (13,349) | (13,378) | (11,898) |
| Earnings from continuing operations before taxes on income..... | \$ 34,064 | \$ 36,472 | \$ 17,015 |
| Identifiable assets: | | | |
| Marine transportation..... | \$320,816 | \$321,158 | \$301,020 |
| Diesel repair..... | 48,012 | 47,290 | 38,588 |
| Investment in insurance affiliate..... | 368,828 | 368,448 | 339,608 |
| Investments in marine affiliates..... | 44,554 | 45,320 | -- |
| Discontinued operations..... | 12,697 | 16,256 | 12,795 |
| General corporate assets..... | 59,365 | 49,036 | -- |
| Consolidated assets..... | 39,086 | 38,899 | 37,896 |
| Consolidated assets..... | \$524,530 | \$517,959 | \$390,299 |

MARINE TRANSPORTATION

The Company is engaged in marine transportation as a provider of services by barge for both the inland and offshore markets. As of February 25, 1999, the equipment owned or operated by the Company's marine transportation segment was comprised of 523 inland tank barges, 128 inland towboats, three inland bowboats, six offshore dry-cargo barges and seven offshore tugboats with the following specifications and capacities:

| CLASS OF EQUIPMENT | NUMBER IN CLASS | AVERAGE AGE (IN YEARS) | BARREL CAPACITIES |
|-------------------------------|--------------------|---------------------------|----------------------|
| Inland tank barges: | | | |
| Regular double skin: | | | |
| 20,000 barrels and under..... | 236 | 23.7 | 2,772,000 |
| Over 20,000 barrels..... | 163 | 18.4 | 4,392,000 |
| Specialty double skin..... | 38 | 28.3 | 599,000 |

| | | | |
|-----------------------------------|-----|------|-----------------------|
| Single skin: | | | |
| 20,000 barrels and under..... | 32 | 31.3 | 539,000 |
| Over 20,000 barrels..... | 54 | 30.5 | 1,378,000 |
| | --- | --- | ----- |
| Total inland tank barges..... | 523 | 23.6 | 9,680,000 |
| | === | === | ===== |
| Inland towing vessels: | | | |
| Inland towboats: | | | |
| 2,000 horsepower and under..... | 100 | 24.0 | |
| Over 2,000 horsepower..... | 28 | 25.3 | |
| | --- | --- | ----- |
| Total inland towboats..... | 128 | 24.3 | |
| | === | === | ===== |
| Inland bowboats..... | 3 | 24.8 | |
| | === | === | ===== |
| | | | DEADWEIGHT TONNAGE |
| | | | ----- |
| Offshore dry-cargo barges(*)..... | 6 | 22.3 | 106,000 |
| | === | === | ===== |
| Offshore tugboats(*)..... | 7 | 22.4 | |
| | === | === | ===== |

(*) Includes four barges and five tugboats owned by Dixie Fuels Limited and one barge and tugboat owned by Dixie Fuels II, Limited, partnerships in which a subsidiary of the Company owns a 35% and 50% interest, respectively.

The following table sets forth the marine transportation revenues and percentage of such revenues for the marine transportation segment for the periods indicated (dollars in thousands):

| REVENUES BY PRODUCT OR OPERATION | YEARS ENDED DECEMBER 31, | | | | | |
|------------------------------------|--------------------------|------|-----------|------|-----------|------|
| | 1996 | | 1997 | | 1998 | |
| | AMOUNTS | % | AMOUNTS | % | AMOUNTS | % |
| Marine transportation -- Inland: | | | | | | |
| Liquid petroleum products..... | \$231,747 | 93% | \$237,828 | 93% | \$238,170 | 97% |
| Marine transportation -- Offshore: | | | | | | |
| Liquid petroleum products..... | 5,285 | 2 | 7,952 | 3 | 4,509 | 2 |
| Dry-bulk..... | 3,059 | 1 | 2,807 | 1 | 2,160 | 1 |
| Break-bulk..... | 9,661 | 4 | 7,529 | 3 | -- | -- |
| | 18,005 | 7 | 18,288 | 7 | 6,669 | 3 |
| Intercompany transactions..... | (158) | -- | (8) | -- | -- | -- |
| | \$249,594 | 100% | \$256,108 | 100% | \$244,839 | 100% |
| | ===== | === | ===== | === | ===== | === |

MARINE TRANSPORTATION INDUSTRY FUNDAMENTALS

The United States possesses a long coastline providing numerous ports and harbors, complemented by a network of interconnected rivers and canals that serve the nation as water highways. Recognizing the advantages to commerce, over the past decades the United States expanded and improved on its inherent natural waterways for commerce and growth. The waterway system extends into numerous states, with over 90% of the United States population served by domestic shipping.

Today, the nation's waterways serve as the backbone of the United States distribution system with over 1.1 billion short tons of cargo moved annually by domestic shipping. The inland waterway system extends approximately 26,000 miles, 11,000 miles of which are generally considered significant for domestic commerce. The navigable waterways link the United States heartland to the world.

Marine transportation is an efficient means of transportation of bulk products. A standard 10,000 barrel inland tank barge carries the equivalent cargo of 15 rail cars or 60 tractor-trailer trucks. A typical lower Mississippi River tow of 30 barges carries as much cargo as 450 rail cars or 1,800 trucks.

Based on cost, marine transportation is the most efficient means of transportation of bulk products compared with rail and trucks. Inland water transportation carries approximately 15% of domestic intercity freight at less than 2% of domestic intercity freight costs. Inland barge transportation is also the safest mode of transportation per ton mile in the United States. The United States inland tank barge industry is diverse and independent with a mixture of integrated transportation companies, small operators and captive fleets owned by United States refining and petrochemical companies.

INLAND TANK BARGE INDUSTRY

The Company operates within the United States inland tank barge industry, which provides marine transportation of bulk liquid cargoes for customers along the United States inland waterway system. Among the most significant segments of this industry are the transporters of industrial chemicals, petrochemical feedstocks, agricultural chemicals and refined petroleum products. The Company operates in each of these segments. The use of marine transportation by the petroleum and petrochemical industry is a major reason for the location of domestic refineries and petrochemical facilities on navigable inland waterways and along the Gulf Coast. Much of the United States farm belt is likewise situated within access to the inland waterway system, relying on marine transportation of farm products, including agricultural chemicals. The Company's principal distribution system encompasses the Gulf Intracoastal Waterway from Brownsville, Texas to St. Marks, Florida, the Mississippi River System and the Houston Ship Channel. The Mississippi River System includes the Arkansas, Illinois, Missouri, Ohio and Tennessee Rivers and the Tombigbee Waterway.

The Company believes that the total number of tank barges that operate in the inland waters of the United States has declined from approximately 4,200 in 1981 to approximately 2,800 in 1998. The Company believes this decrease primarily resulted from: increasing age of the domestic tank barge fleet resulting in scrapping; rates inadequate to justify new construction; reduction in financial and tax incentives which previously encouraged speculative construction of new equipment; stringent operating standards to adequately cope with safety and environmental risk; and an increase in environmental regulations that mandate expensive equipment modification which some owners are unwilling or unable to undertake given current rate levels and the age of their fleets.

Although well maintained tank barges can be efficiently operated for more than 30 years, the cost of hull work for required annual Coast Guard certifications, as well as general safety and environmental concerns, force operators to periodically reassess their ability to recover maintenance costs. Previously, tax and financing incentives to operators and investors to construct tank barges, including short-life tax depreciation, investment tax credits and government guaranteed financing, led to growth in the supply of domestic tank barges to a peak of approximately 4,200 in 1981. These tax incentives have since been eliminated, although the government guaranteed financing programs, dormant since the mid-eighties, have been more active since 1993. The supply of tank barges resulting from the earlier programs has slowly aligned with demand for tank barge services, primarily through attrition, as discussed above.

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While the United States tank barge fleet has decreased in size, domestic production of petrochemicals, a major component of the industry's revenues, has continued to increase annually. Growth in the economy, continued growth of the United States population and the continued substitution of plastics and synthetics in a wide variety of products have been major factors behind the increase of capacity in the petrochemical industry. Texas and Louisiana, which are within the Company's area of operations, currently account for approximately 80% of the total United States production of petrochemicals.

A well maintained tank barge will be serviceable for more than 30 years. The average age of the nation's tank barge fleet is over 22 years old, with only 16% of the fleet built in the last 10 years. Single skin barges comprise approximately 18% of the nation's tank barge fleet, with an average age of 29 years. These single skin barges are being driven from the nation's tank barge fleet by market forces, environmental concerns and rising maintenance costs to

keep such fleets afloat and in service.

The Company also believes that the current consolidating industry will be less prone to overbuilding of the nation's tank barge fleet. Of the approximate 450 tank barges built since 1989, 74, or 16%, were built by the Company. The balance was primarily special purpose barges or barges constructed for specific contracts. Currently, the only significant building is by an oil company to replace its aging captive fleet.

The Company is also engaged in dry-cargo barge operations, providing transportation of dry-bulk cargoes, and containerized and palletized cargoes, including United States Government preference agricultural commodities. Such products and cargoes are transported primarily between domestic ports along the Gulf of Mexico and along the Atlantic Seaboard, with occasional trips to Caribbean and South American ports.

COMPETITION IN THE INLAND TANK BARGE INDUSTRY

The Company operates in the highly competitive marine transportation market for commodities transported on the Mississippi River System, the Gulf Intracoastal Waterway and the Houston Ship Channel. The industry has become increasingly concentrated in recent years as smaller and/or economically weaker companies have gone out of business or have been acquired by larger or stronger companies. The Company's competition has historically been based primarily on price; however, shipping customers, through increased emphasis on safety, the environment, quality and a greater reliance on a "single source" supply of services, are more frequently requiring that their supplier of inland tank barge services have the capability to handle a variety of tank barge requirements, offer distribution capability throughout the inland waterway system, and offer flexibility, safety, environmental responsibility, financial responsibility, adequate insurance and quality of service consistent with the customer's own operations.

The Company's direct competitors are primarily noncaptive marine transportation companies. "Captive" companies are those companies that are owned by major oil and/or petrochemical companies which, although competing in the inland barge market to varying extents, primarily transport cargoes for their own account. The Company is the largest inland tank barge carrier, based on its 523 barges and 9,680,000 barrels of available capacity. It has approximately 25% of the independent tank barge capacity and 19% of the total domestic tank barge capacity.

While the Company competes primarily with other barge companies, it also competes with companies owning refined product and chemical pipelines, and, to a much lesser extent, rail tank cars and tank trucks in some areas and markets. The Company believes that inland marine transportation of bulk liquid products enjoys a substantial cost advantage over rail and truck transportation. The Company also believes that refined products and chemical pipelines, although often a less expensive form of transportation than tank barges, are not as adaptable to diverse products and are generally limited to fixed point-to-point distribution of commodities in high volumes over extended periods of time.

MARINE TRANSPORTATION OPERATIONS

The Company provides marine transportation services for the following markets: industrial chemicals, agricultural chemicals, refined petroleum products and barge fleetings services. The Company's marine transportation segment operates a fleet of 523 inland tank barges, 128 inland towboats and three inland

bowboats, one offshore dry-cargo barge and one offshore tugboat. Through partnerships, the marine transportation segment operates five offshore dry-cargo barges and six offshore tugboats.

Inland Operations. The Company's inland marine transportation operations are conducted through a wholly-owned subsidiary, Kirby Inland Marine, Inc. ("Kirby Inland Marine"), and its subsidiaries. Inland operations consist of the Canal, Linehaul and River fleets, as well as barge fleetings services performed by Western Towing Company ("Western").

The Canal fleet transports petrochemical feedstocks, processed chemicals

and refined petroleum products along the Gulf Intracoastal Waterway, the Mississippi River below Baton Rouge and in the Houston Ship Channel. Petrochemical feedstocks are transported from one refinery to another refinery for further processing. Processed chemicals are moved to waterfront terminals and chemical plants, while refined products are transported to waterfront terminals in Florida for distribution.

The Linehaul fleet transports petrochemical feedstocks, processed chemicals, agricultural chemicals and lube oils along the Gulf Intracoastal Waterway, Mississippi River and the Illinois and Ohio Rivers. Loaded barges are collected at Baton Rouge from Gulf Coast refineries and chemical plants, and are transported from Baton Rouge upriver to waterfront terminals and plants on the Mississippi, Illinois and Ohio Rivers on regularly scheduled Linehaul tows. Barges are dropped off and picked up going up and down river.

The River fleet transports petrochemical feedstocks, processed chemicals, agricultural chemicals and refined petroleum products along the Mississippi, Illinois, Ohio and Arkansas Rivers. Petrochemical feedstocks and processed chemicals are transported to waterfront petrochemical and chemical plants, while agricultural chemicals and refined petroleum products are transported to waterfront terminals. The River fleet operates unit tows, where a towboat and generally a static group of barges operate on consecutive voyages between a loading point and a discharge point.

The transportation of petrochemical feedstocks and processed chemicals is generally consistent throughout the year. Transportation of refined petroleum products and agricultural chemicals are generally more seasonal. Movements of refined petroleum products generally increase during the summer driving season, and movements of agricultural chemicals generally increase during the spring and fall planting seasons.

Marine transportation services are conducted under long-term contracts with customers with whom the Company has long-standing relationships, as well as under short-term and spot contracts. Currently, approximately 80% of the revenues are derived from term contracts and 20% are derived from spot market movements.

For increased environmental protection, all of the inland tank barges used in the transportation of industrial chemicals are of double skin construction and, where applicable, are capable of controlling vapor emissions to meet occupational health and safety regulations and air quality concerns.

The Company, over the last several years, through consolidation within the inland tank barge market, has become one of the most capable inland tank barge operators, and one with the ability to offer to its customers distribution capabilities throughout the Mississippi River System and the Gulf Intracoastal Waterway. Such consolidation offers economies of scale to better match barges, towboats, products and destinations.

Through the Company's proprietary vessel management computer system, the Company's fleet of 523 barges and 128 towboats is dispatched from centralized dispatch at the Company's corporate office. Electronic orders are communicated to the vessel personnel, with reports of towing activities communicated electronically back to the corporate office. The electronic interface between the corporate office and the vessel personnel enables the Company to more effectively match customer needs to barge capabilities, thereby maximizing utilization of the Company's barge and towboat fleet.

Western operates what the Company believes is the largest commercial barge fleet service (temporary barge storage facilities) in the ports of Houston, Galveston and Freeport, Texas, and on the Mississippi River at Baton Rouge, Louisiana. Western provides service for Kirby Inland Marine's barges, as well as outside customers, transferring barges within the areas noted, as well as fleeting barges.

Kirby Logistics Management, a division of Kirby Inland Marine, offers barge tankerman services and related distribution services to the Company and to third parties.

Offshore Operations. The Company's offshore fleet is comprised of one offshore dry-cargo barge and tugboat unit, and equipment owned through two

limited partnerships, Dixie Fuels Limited ("Dixie Fuels") and Dixie Fuels II, Limited ("Dixie Fuels II") in which a subsidiary of the Company owns a 35% and 50% interest, respectively.

The ocean-going dry-bulk barge and tugboat unit is engaged in the transportation of dry-bulk commodities including sugar, limestone rock, grain and scrap steel, primarily between domestic ports along the Gulf of Mexico and along the Atlantic Seaboard, with occasional trips to Caribbean and South American ports.

Dixie Bulk Transport, Inc. ("Dixie Bulk"), a subsidiary of the Company, as general partner, manages the operations of Dixie Fuels, which operates a fleet of four ocean-going dry-bulk barges, four ocean-going tugboats and one shifting tugboat. The remaining 65% interest in Dixie Fuels is owned by Electric Fuels Corporation ("EFC"), an affiliate of Florida Power Corporation ("Florida Power"). Dixie Fuels operates primarily under term contracts of affreightment, including a contract that expires in the year 2002 with EFC to transport coal across the Gulf of Mexico to Florida Power's facility at Crystal River, Florida.

Dixie Fuels also has a 12-year contract, which commenced in 1989, with Holnam, Inc. ("Holnam") to transport Holnam's limestone requirements from a facility adjacent to the Florida Power facility at Crystal River to Holnam's plant in Theodore, Alabama. The Holnam contract provides cargo for a portion of the return voyage for the vessels that carry coal to Florida Power's Crystal River facility. Dixie Fuels is also engaged in the transportation of coal, fertilizer and other bulk cargoes on a short-term basis between domestic ports and transportation of grain from domestic ports to ports primarily in the Caribbean Basin.

Dixie Bulk, as general partner, also manages the operations of Dixie Fuels II, which operates an ocean-going dry-bulk and container barge and tugboat unit. The remaining 50% interest in Dixie Fuels II is owned by EFC. Dixie Fuels II is engaged in the transportation of dry-bulk cargo and containers between domestic ports, ports in the Caribbean Basin and international ports as cargo offers.

During 1998, the Company sold its two offshore tank barge and tug units. The two units, one of which was a 157,000 barrel single skin barge and one a 165,000 barrel double skin barge, provided service in the transportation of refined petroleum products and chemicals primarily in domestic coastwise service.

The Company, through its subsidiary AFRAM Carriers, Inc. ("AFRAM"), was engaged in the worldwide transportation by freighters of dry-bulk, container and palletized cargoes, primarily for departments and agencies of the United States Government. In 1996, the Company scrapped one freighter, and in 1997, the Company scrapped the remaining two freighters, concluding the Company's exit from the transportation of such cargoes by freighters; however, the Company may occasionally transport such cargoes by ocean-going dry-bulk barges.

CONTRACTS AND CUSTOMERS

The majority of the marine transportation contracts are for terms of one to ten years. Currently, the Company operates under longer term contracts with The Dow Chemical Company ("Dow"), Chevron Chemical Company, EFC, Holnam, and Baytank (Houston) Inc., among others. While these companies have generally been customers of the Company's marine transportation segment for several years and management anticipates a continuing relationship, there is no assurance that any individual contract will be renewed. Dow, with which the Company has a contract through 2004, accounted for 13% of the Company's revenues in 1998 and 1997 and 12% in 1996.

EMPLOYEES

The Company's marine transportation operations have approximately 1,250 employees, of which approximately 1,000 are vessel crew members. Of the 1,000 vessel crew members only a small bargaining unit

of approximately 40 employees in the Company's offshore operation are subject to a collective bargaining agreement with a labor organization.

During 1997 and 1998, a maritime union representing primarily deepsea

officers sought to organize inland towing industry employees. In April 1998, that organization called for an inland towing industry wide work stoppage in an attempt to gain voluntary recognition from inland towing industry employers. The work stoppage was generally ineffective industry wide and had minimal impact on the Company. The union continues to seek recognition throughout the inland towing industry through petitioning for certification elections. The Company has not been presented with any petitions.

PROPERTIES

The principal office of Kirby Inland Marine is located in Houston, Texas, in facilities under a lease that expires in August 2003. Kirby Inland Marine's operating locations are on the Mississippi River at Baton Rouge, Louisiana, and Greenville, Mississippi, and in Houston, Texas near the Houston Ship Channel. The Baton Rouge and Houston facilities are owned and the Greenville facility is leased. Western's facilities are located on a 10.24 acre tract of land owned by Kirby Inland Marine lying between the San Jacinto River and Old River Lake near Houston, Texas. The principal office of the Company's offshore operations is in Belle Chasse, Louisiana in owned facilities.

GOVERNMENTAL REGULATIONS

General. The Company's marine transportation operations are subject to regulation by the United States Coast Guard, federal laws, state laws and certain international conventions.

The majority of the Company's inland tank barges are inspected by the United States Coast Guard and carry certificates of inspection. The Company's inland and offshore towing vessels and offshore dry-bulk barges are not subject to United States Coast Guard inspection requirements. The Company's offshore towing vessels and offshore dry-bulk barges are built to American Bureau of Shipping ("ABS") classification standards and are inspected periodically by ABS to maintain the vessels in class. The crew employed by the Company aboard vessels, including captains, pilots, engineers, tankermen and ordinary seamen, is licensed by the United States Coast Guard.

The Company is required by various governmental agencies to obtain licenses, certificates and permits for its vessels depending upon such factors as the cargo transported, the waters in which the vessels operate and other factors. The Company is of the opinion that the Company's vessels have obtained and can maintain all required licenses, certificates and permits required by such governmental agencies for the foreseeable future.

The Company believes that additional safety and environmental related regulations may be imposed on the marine industry in the form of personnel licensing, navigation equipment and contingency planning requirements. Generally, the Company endorses the anticipated additional regulations and believes it is currently operating to standards at least the equal of such anticipated additional regulations.

Jones Act. The Jones Act is a federal cabotage law that restricts domestic marine transportation in the United States to vessels built and registered in the United States, manned by United States citizens and owned and operated by United States citizens. For corporations to qualify as United States citizens for the purpose of domestic trade, 75% of the corporations' beneficial stockholders must be United States citizens. The Company presently meets all of the requirements of the Jones Act for its owned vessels.

Compliance with United States ownership requirements of the Jones Act is very important to the operations of the Company and the loss of Jones Act status could have a significant negative effect for the Company. The Company monitors the citizenship requirements under the Jones Act of its employees and beneficial stockholders and will take action as necessary to ensure compliance with the Jones Act requirements.

The requirements that the Company's vessels be United States built and manned by United States citizens, the crewing requirements and material requirements of the Coast Guard, and the application of

United States labor and tax laws, significantly increases the cost of U.S. flag vessels when compared with comparable foreign flag vessels. The Company's

business would be adversely affected if the Jones Act were to be modified so as to permit foreign competition that is not subject to the same United States Government imposed burdens.

During the past several years, the Jones Act cabotage and cargo preference laws, see "Preference Cargo" below, have come under attack by interests seeking to facilitate foreign flag competition for trades and cargoes reserved for U.S. flag vessels under the Jones Act and cargo preference laws. These efforts have been consistently defeated by large margins in the United States Congress. The Company believes that continued efforts will be made to modify or eliminate the cabotage provisions of the Jones Act and the cargo preference laws. If such efforts are successful, it could have an adverse effect on the Company.

Preference Cargo. Federal law requires that preference be given to U.S. flag vessels in the transportation of certain United States Government impelled cargoes (cargoes shipped either by the United States Government or by a foreign nation with the aid or guarantee of the United States Government). Markets subject to cargo preference in which the Company participates include foreign food aid and Eximbank cargoes. Currently, 75% of the United States Government's directed foreign aid and agricultural assistance programs, which include grains and other food concessions, are required to be transported in U.S. flag vessels. Such programs benefited the Company's offshore break-bulk ships prior to their scrapping and currently benefit dry-bulk barge and tug units, some of which occasionally work in this trade. The transportation of such cargo accounted for approximately 6% of the Company's revenue in 1997 and in 1996, but produced minimal revenue in 1998.

The preference cargo law is often opposed by interests which perceive they would benefit from the ability to transport preference cargoes aboard foreign flag vessels. Like the cabotage provision of the Jones Act, the Company is of the opinion that continued efforts will be made to significantly reduce, or remove completely, the requirement that 75% of such cargoes be transported in U.S. flag vessels. Further, the agricultural aid cargoes represent a material United States Government budget line item. The amount of United States Government spending in this area has declined since 1993, resulting in increased competition for the reduced number of shipments at lower transportation rates. Given current operations of the Company, any further reduction in Government spending on preference cargoes would not have a significant adverse effect on the Company's operations.

User Fees. Federal legislation requires that inland marine transportation companies pay a user fee in the form of a tax based on propulsion fuel used by vessels engaged in trade along the inland waterways that are maintained by the United States Army Corps of Engineers. Such user fees are designed to help defray the costs associated with replacing major components of the inland waterway system such as locks and dams, and to build new waterway projects. A significant portion of the inland waterways on which the Company's vessels operate is maintained by the Corps of Engineers.

The Company presently pays a federal fuel tax of 24.3 cents per gallon, reflecting a 4.3 cents per gallon transportation fuel tax imposed in October 1993 and a 20 cents per gallon waterway use tax. There can be no assurance that additional user fees, either for inland waterways infrastructure, or such things as aids to navigation infrastructure, may not be imposed in the future.

ENVIRONMENTAL REGULATIONS

The Company's operations are affected by various regulations and legislation enacted for protection of the environment by the United States Government, as well as many coastal and inland waterway states.

Water Pollution Regulations. The Federal Water Pollution Control Act of 1972, as amended by the Clean Water Act of 1977, the Comprehensive Environmental Response, Compensation and Liability Act of 1981 and the Oil Pollution Act of 1990 ("OPA"), impose strict prohibitions against the discharge of oil and its derivatives or hazardous substances into the navigable waters of the United States. These acts impose civil and criminal penalties for any prohibited discharges and impose substantial strict liability for cleanup of these discharges and any associated damages. Certain states also have water pollution laws that prohibit discharges

into waters that traverse the state or adjoin the state and impose civil and criminal penalties and liabilities similar in nature to those imposed under federal laws.

The OPA and various state laws of similar intent substantially increased over historic levels statutory liability of owners and operators of vessels for oil spills, both in terms of limit of liability and scope of damages. The Company considers its most significant pollution liability exposure to be the carriage of persistent oils, such as lube oils. The Company restricts the carriage of persistent oils in inland tank barges to double hull barges only.

One of the most important requirements under the OPA is that all newly constructed tank barges engaged in the transportation of oil and petroleum in the United States must be double hulled and all existing single hull tank barges be retrofitted with double hulls or phased out of domestic service between January 1, 1995 and 2015.

The Company manages its exposure to losses from potential discharges of pollutants through the use of well maintained and equipped vessels, the safety, training and environmental programs of the Company and the Company's insurance program. In addition, the Company uses double skin barges in the transportation of more hazardous substances. There can be no assurance, however, that any new regulations or requirements or any discharge of pollutants by the Company will not have an adverse effect on the Company.

Financial Responsibility Requirement. Commencing with the Federal Water Pollution Control Act of 1972, as amended, vessels over three hundred gross tons operating in the Exclusive Economic Zone of the United States have been required to maintain evidence of financial ability to satisfy statutory liabilities for oil and hazardous substance water pollution. This evidence is in the form of a Certificate of Financial Responsibility ("COFR") issued by the United States Coast Guard. The majority of the Company's tank barges are subject to this COFR requirement and the Company has fully complied with this requirement since its inception.

The OPA amended the COFR requirements principally by significantly increasing the financial ability requirements. The new rules severely limited the ability of marine transportation companies to utilize insurance as a means of satisfying the financial ability requirement under OPA. The principal alternative to the use of insurance under the new rule requires marine transportation companies to demonstrate net worth and working capital equal to the maximum statutory limit of liability under the OPA and the Comprehensive Environmental Response, Compensation and Liability Act of 1981.

Each of the marine transportation subsidiaries of the Company has obtained COFRs pursuant to the OPA amendments for all vessels requiring COFRs. The Company does not foresee any current or future difficulty in maintaining the COFR certificates under current rules.

Clean Air Regulations. The Federal Clean Air Act of 1979 ("Clean Air Act") requires states to draft State Implementation Plans ("SIPs") designed to reduce atmospheric pollution to levels mandated by this act. Several SIPs provide for the regulation of barge loading and degassing emissions. The implementation of these regulations requires a reduction of hydrocarbon emissions released into the atmosphere during the loading of most petroleum products and the degassing and cleaning of barges for maintenance or change of cargo. These new regulations will require operators who operate in these states to install vapor control equipment on their barges. The Company expects that future toxic emission regulations will be developed and will apply this same technology to many chemicals that are handled by barge. Most of the Company's barges engaged in the transportation of petrochemicals, chemicals and refined products are already equipped with vapor control systems. Although a risk exists that new regulations could require significant capital expenditures by the Company and otherwise increase the Company's costs, the Company believes that, based upon the regulations that have been proposed thus far, no material capital expenditures beyond those currently contemplated by the Company and no increase in costs are likely to be required.

Contingency Plan Requirement. The OPA and several state statutes of similar intent require the majority of the vessels operated by the Company to maintain approved oil spill contingency plans as a condition of operation. The Company has approved plans that comply with these requirements. The OPA also requires development of regulations for hazardous substance spill contingency plans. The United States Coast

Guard has not yet promulgated these regulations; however, the Company anticipates that they will not be significantly more difficult than the oil spill plans.

Occupational Health Regulations. The Company's vessel operations are primarily regulated by the United States Coast Guard for occupational health standards. The Company's shore personnel are subject to the United States Occupational Safety and Health Administration regulations. The Coast Guard has promulgated regulations that address the exposure to benzene vapors, which require the Company, as well as other operators, to perform extensive monitoring, medical testing and record keeping of seamen engaged in the handling of benzene and benzene containing cargo transported aboard vessels. It is expected that these regulations may serve as a prototype for similar health regulations relating to the carriage of other hazardous liquid cargoes. The Company believes that it is in compliance with the provisions of the regulations that have been adopted and does not believe that the adoption of any further regulations will impose additional material requirements on the Company. There can be no assurance, however, that claims will not be made against the Company for work related illness or injury, or that the further adoption of health regulations will not adversely affect the Company.

Insurance. The Company's marine transportation operations are subject to the hazards associated with operating vessels carrying large volumes of bulk cargo in a marine environment. These hazards include the risk of loss of or damage to the Company's vessels, damage to third parties from impact, fire or explosion as a result of collision, loss or contamination of cargo, personal injury of employees and third parties, pollution and other environmental damages. The Company maintains insurance coverage against these hazards. Risk of loss of, or damage to the Company's vessels is insured through hull insurance policies currently insuring approximately \$480 million in hull values. Vessel operating liabilities such as collision, cargo, environmental and personal injury, are insured primarily through the Company's participation in mutual insurance associations and other reinsurance arrangements under which protection against such hazards is in excess of \$2 billion for each incident except in the case of oil pollution, which, in conjunction with the other excess liability coverage maintained by the Company, is limited to \$700 million for each incident. However, because it is mutual insurance, the Company is exposed to funding requirements and coverage shortfalls in the event claims by the Company or other members exceed available funds and reinsurance.

Environmental Protection. The Company has a number of programs that were implemented to further its commitment to environmental responsibility in its operations. One such program is environmental audits of barge cleaning vendors principally directed at management of cargo residues and barge cleaning wastes. Another program is the participation by the Company in the American Waterways Operators Responsible Carrier program, the Chemical Manufacturer's Association Responsible Care program and the American Petroleum Institute STEP program, all of which are oriented to continuously reducing the barge industry's and chemical and petroleum industries' impact on the environment, including the distribution services area.

Safety. The Company manages its exposure to the hazards associated with its business through safety, training and preventive maintenance efforts. The Company places considerable emphasis on safety through a program oriented toward extensive monitoring of safety performance for the purpose of identifying trends and initiating corrective action, and for the purpose of rewarding personnel achieving superior safety performance. The Company believes that its safety performance consistently places it among the industry leaders as evidenced by what it believes are lower injury frequency and pollution incident levels than many of its competitors.

The Company was honored by the Department of Transportation and the United States Coast Guard in September 1995 as the recipient of the William M. Benkert Award, the premier national award which recognizes excellence in all aspects of marine safety and environmental protection. The Company was the first recipient of this award for the large vessel operator category. Given the national concern over the transportation of hazardous material and oil products, this award is independent affirmation of the Company's policies and achievements in the area of marine safety and environmental protection.

Training. The Company believes that among the major elements of a successful and productive work force are effective training programs. The Company also believes that training in the proper performance of a job enhances

both the safety and quality of the service provided. New technology, regulatory compliance,

personnel safety, quality and environmental concerns create additional demands for training. The Company fully endorses the development and institution of effective training programs.

Centralized training is provided through the training department which is charged with developing, conducting and maintaining training programs for the benefit of all of the Company's operating entities. It is also responsible for ensuring that training programs are both consistent and effective. The Company's training facility includes state of the art equipment and instruction aids, including a working towboat, tank barge and shore tank facilities. During 1998, approximately 1,100 students completed courses at the training facility.

Quality. In 1996, the Company's commitment to quality performance was implemented through a major business process redesign project, and the continued maintenance and improvement of our Quality Assurance Systems.

The business process redesign project focused on three functional areas, customer billing, purchasing and maintenance, and resulted in significant changes in processes and structures. Projected outcomes include faster billing preparation and collection cycles, reduced costs for purchased products and services as a result of leveraged buying and more efficient maintenance of our vessels and associated equipment.

Throughout the 1990s, the Company made a substantial commitment to the implementation, maintenance and improvement of Quality Assurance Systems in compliance with the International Quality Standard, ISO 9002. Currently, all of the Company's marine transportation units serving the liquid and dry-cargo markets have been certified, many of them earning "firsts" among their peers. These Quality Assurance Systems have enabled both shore and vessel personnel to effectively manage the changes which occur in the working environment. In addition, such Quality Assurance Systems have enhanced the Company's already excellent safety and environmental performance.

DIESEL REPAIR

The Company is presently engaged in the overhaul and repair of large medium-speed diesel engines and related parts sales through three operating subsidiaries, Marine Systems, Inc. ("Marine Systems"), Engine Systems, Inc. ("Engine Systems") and Rail Systems, Inc. ("Rail Systems"). Through each of its three operating subsidiaries, the Company sells genuine replacement parts, provides service mechanics to overhaul and repair engines and maintains facilities to rebuild component parts or entire engines. The Company serves the marine market and stand-by power generation market, the shortline and industrial railroad markets, and components of the nuclear industry. No single customer of the diesel repair segment accounted for more than 10% of the Company's revenues in 1998, 1997 or 1996. The diesel repair segment also provides services to the Company's marine transportation segment, which accounted for approximately 4% of the diesel repair segment's total 1998 revenues and approximately 2% of its revenues for 1997 and 1996. Such revenues are eliminated in consolidation and not included in the table below.

The following table sets forth the revenues for the diesel repair division for the periods indicated (dollars in thousands):

| | YEARS ENDED DECEMBER 31, | | | | | |
|---------------------------|--------------------------|------|----------|------|----------|------|
| | 1996 | | 1997 | | 1998 | |
| | AMOUNTS | % | AMOUNTS | % | AMOUNTS | % |
| Overhaul and repairs..... | \$41,642 | 59% | \$46,911 | 59% | \$43,107 | 52% |
| Direct parts sales..... | 28,780 | 41 | 32,225 | 41 | 39,134 | 48 |
| | \$70,422 | 100% | \$79,136 | 100% | \$82,241 | 100% |

MARINE SYSTEMS OPERATIONS

Through Marine Systems, the Company is engaged in the overhaul and repair of marine diesel engines, reduction gear repair, line boring, block welding services and related parts sales for customers in the marine industry. The marine diesel repair industry services tugboats and towboats powered by large diesel engines

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utilized in the inland and offshore barge industries. It also services marine equipment and offshore drilling equipment used in the offshore petroleum exploration and oil service industry, marine equipment used in the offshore commercial fishing industry and vessels owned by the United States Government.

Marine Systems operates through three divisions providing in-house and in-field repair capabilities. These three divisions are: Gulf Coast (based in Houma, Louisiana); Midwest (based in Paducah, Kentucky); and West Coast (based in Seattle, Washington). All three of Marine Systems' divisions are nonexclusive authorized service centers for the Electro-Motive Division of General Motors Corporation ("EMD") selling parts and service. Marine Systems' Gulf Coast and Midwest divisions concentrate on larger medium-speed diesel engines, primarily those manufactured by EMD, that are more commonly used in the inland and offshore barge and oil service industries. The West Coast division concentrates on the large EMD engines used by the offshore commercial fishing industry, the military and commercial businesses on the West Coast, and customers in Alaska. Marine Systems' emphasis is on service to its customers and can send its crews from any of its divisions to service customers' equipment anywhere in the world.

MARINE SYSTEMS CUSTOMERS

Major customers of Marine Systems include inland and offshore dry-bulk and tank barge operators, oil service companies, petrochemical companies, offshore fishing companies, other marine transportation entities and the United States Coast Guard, Navy and Army.

Since Marine Systems' business can be cyclical and is linked to the relative health of the diesel power tugboat and towboat industry, the offshore supply boat industry, the oil and gas drilling industry, the military and the offshore commercial fishing industry, there is no assurance that its present gross revenues can be maintained in the future. The results of the diesel repair service industry are largely tied to the industries it serves, and, therefore, have been somewhat influenced by the cycles of such industries.

MARINE SYSTEMS COMPETITIVE CONDITIONS

Marine Systems' primary competitors are approximately 10 independent diesel repair companies and authorized EMD distributors in each of its three divisions. Certain operators of diesel powered marine equipment elect to maintain in-house service capabilities. While price is a major determinant in the competitive process, reputation, consistent quality, expeditious service, experienced personnel, access to parts inventories and market presence are significant factors. A substantial portion of Marine Systems' business is obtained by competitive bids. Marine Systems has entered into preferential service agreements with certain large operators of diesel powered marine equipment, providing such operations with one source of support and service for all of their requirements at pre-negotiated prices.

Many of the parts sold by Marine Systems are generally available from other distributors; however, Marine Systems is one of a limited number of authorized resellers of EMD parts. Although the Company believes it is unlikely, termination of Marine Systems' relationship with its suppliers could adversely affect its business.

ENGINE SYSTEMS OPERATIONS

Through Engine Systems, the Company is engaged in the overhaul and repair of diesel engines for power generation, marine and nuclear applications. In July 1996, a subsidiary of the Company purchased the operating assets of MKW Power Systems, Inc., a subsidiary of Wartsila Diesel, N.A. ("MKW"). The acquisition expanded the diesel repair segment's relationship with EMD to an authorized distributorship for 17 eastern states and the Caribbean, and as the exclusive

worldwide distributor of EMD products to the nuclear industry. As the exclusive East Coast distributor, the Company gains a better pricing structure for parts purchased.

Effective July 1997, Engine Systems entered into an agreement with Stewart & Stevenson Services, Inc., allowing Stewart & Stevenson to sell EMD engines within Engine Systems' distributorship territory. Engine Systems will receive an annual fee based on sales within the distributorship territory. Engine Systems, as well

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as Marine Systems, also serves as United States marine parts distributors for Falk Corporation, a marine reduction gear manufacturer.

ENGINE SYSTEMS CUSTOMERS

The major customers of Engine Systems are East Coast inland and offshore dry-bulk, tank barge and harbor docking operators, the United States Coast Guard and aircraft carriers of the United States Navy. In addition, Engine Systems provides service to the power generation industry (Disney World, Dade County, Florida and Bahamas Electricity Corporation), and the worldwide nuclear power industry, through parts for standby generators.

ENGINE SYSTEMS COMPETITIVE CONDITIONS

Engine Systems is currently the major source of genuine EMD parts and authorized service for customers in power generation, marine and industrial applications in 17 eastern states and the Caribbean, its distributorship territory. Generic parts, remanufactured parts and non-authorized services supporting existing applications of EMD engines are available to existing applications in Engine Systems' distributorship territory; however, many customers will give preference to Engine Systems due to its access to preferred genuine EMD replacement parts.

Engine Systems is also the exclusive distributor of EMD parts for the nuclear industry worldwide. Specific regulations relating to equipment used in nuclear power generation require extensive testing and certification of replacement parts. Non-genuine parts and parts not properly tested and certified cannot be used in the nuclear applications.

RAIL SYSTEMS OPERATIONS

Through Rail Systems, the Company is engaged in the overhaul and repair of locomotive diesel engines and sale of replacement parts for locomotives serving the shortline and the industrial railroads within the continental United States. Rail Systems serves as an exclusive distributor for EMD providing replacement parts, service and support to these markets. EMD is the world's largest manufacturer of diesel-electric locomotives, a position it has held for over 70 years.

RAIL SYSTEMS CUSTOMERS

Shortline railroads have been a growing component of the United States railroad industry since deregulation of the railroads in the 1970s. Generally, shortline railroads have been created through the divestiture of branch routes from the major railroad systems. These short routes provide switching and short haul of freight, with an emphasis on responsive and reliable service. Currently, about 500 shortline railroads in the United States operate approximately 2,400 EMD engines. Approximately 280 United States industrial users operate approximately 1,300 EMD engines. Generally, the EMD engines operated by the shortline and industrial users are older and, therefore, may require more maintenance.

RAIL SYSTEMS COMPETITIVE CONDITIONS

As an exclusive United States distributor for EMD parts, Rail Systems provides all EMD parts sales to these markets, as well as providing rebuild and service work. Currently, other than Rail Systems, there are several primary companies providing service for the shortline and industrial locomotives. In addition, the industrial companies, in some cases, provide their own service.

EMPLOYEES

Marine Systems, Engine Systems and Rail Systems together have approximately 230 employees.

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PROPERTIES

The principal offices of Marine Systems and Rail Systems are located in Houma, Louisiana. Rail Systems relocated to Houma from Nashville, Tennessee in late 1998. Parts and service facilities are located in Houma, Louisiana; in Paducah, Kentucky and in Seattle, Washington. The Paducah, Kentucky and Seattle, Washington locations are on leased property and the Houma location is situated on approximately seven acres of Company owned land. The principal office of Engine Systems is located in Rocky Mount, North Carolina with service facilities in Chesapeake, Virginia and Medley, Florida. Each of Engine Systems' locations is on leased property.

INSURANCE

Effective September 30, 1998, the Company sold its remaining 45% voting common stock interest and its non-voting preferred stock interest in Universal Insurance Company ("Universal") for \$36,000,000 in cash. Universal, a property and casualty insurance company in the Commonwealth of Puerto Rico, was formed by the Company in 1972. In September 1992, the Company merged Universal with Eastern America Insurance Company ("Eastern America"), a subsidiary of Eastern America Insurance Group, Inc. ("Eastern America Group"). In accordance with a shareholders agreement among the Company, Universal and Eastern America Group, through redemption rights, Universal had the obligation to purchase the Company's entire interest in Universal gradually, over a 15 year period. The Company closed the sale on October 7, 1998 and the cash proceeds were used to reduce the Company's revolving line of credit.

Under an anticipated redemption schedule, the Company would have received a stream of cash payments between now and the year 2008 totaling \$62,000,000. The \$36,000,000 received represented the present value of the payment stream. Including prior redemptions and the final sale, the Company received total payments of \$58,000,000 for its interest in Universal.

REINSURANCE OPERATION

Prior to 1991, the Company participated in the international reinsurance market through Mariner Reinsurance Company Limited ("Mariner"), a wholly-owned subsidiary of the Company domiciled in Bermuda. From 1991 to present, Mariner has been in run-off, paying claims on business written prior to 1991 and not underwriting any new business.

Effective May 31, 1995, Mariner entered into Commutation Agreements with parties representing the majority of its outstanding underwriting liabilities ("Commuting Parties") and simultaneously executed documents granting the Commuting Parties absolute interest in any assets of Mariner which remain upon liquidation of Mariner. Since May 31, 1995, Mariner has continued in run-off, as a solvent insurance company under Bermuda law and regulation, paying claims of parties other than the Commuting Parties, while seeking to consummate further commutations as well. The effect of the May 31, 1995 transaction between Mariner and the Commuting Parties was to transfer to the Commuting Parties all of Mariner's interest in the equity and surplus assets of Mariner, if any, remaining at the time of the ultimate liquidation of Mariner. Loss of the Company's equity in Mariner was fully reserved in 1994 and the transaction was charged against that reserve in 1995.

CAPTIVE INSURANCE OPERATION

The Company utilizes a Bermuda domiciled wholly-owned insurance subsidiary, Oceanic Insurance Limited ("Oceanic"), to insure risks of the Company and its marine transportation and diesel repair subsidiaries and affiliated entities. Oceanic procures reinsurance in international markets to limit its exposure to losses.

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DISCONTINUED OPERATIONS

On March 16, 1998, the Company announced the completion of the sale of its U.S. flag product tanker and harbor service operations for \$38,600,000 in cash. Under the terms of a purchase agreement dated January 28, 1998, Kirby sold two offshore tankers and its harbor service operations to Hvide Marine Incorporated and five offshore tankers were sold to August Trading Company, Inc.

The offshore tanker and harbor service operations' financial results were accounted for as discontinued operations as of December 31, 1997, and previously reported financial statements were restated to reflect the discontinuation of the operations. See "Note 2" to the financial statements included under Item 8 elsewhere herein for further disclosures on the sale of the tanker and harbor service operations.

ITEM 2. PROPERTIES

The information appearing in Item 1 is incorporated herein by reference. The Company and Kirby Inland Marine currently occupy leased office space at 1775 St. James Place, Suite 200, Houston, Texas under a lease that expires in August 2003. The Company believes that its facilities are adequate for its needs and additional facilities would be readily available.

ITEM 3. LEGAL PROCEEDINGS

See "Note 13" to the financial statements included under Item 8 elsewhere herein for a discussion of legal proceedings.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

During the fourth quarter of the fiscal year ended December 31, 1998, no matter was submitted to a vote of security holders through solicitation of proxies or otherwise.

EXECUTIVE OFFICERS OF THE REGISTRANT

The executive officers of the Company are as follows:

| NAME - - - - - | AGE --- | POSITIONS AND OFFICES ----- |
|-----------------------------|------------|---|
| George A. Peterkin, Jr..... | 71 | Chairman of the Board of Directors |
| J.H. Pyne..... | 51 | President, Director and Chief Executive Officer |
| Norman W. Nolen..... | 56 | Senior Vice President, Treasurer, Assistant Secretary and Chief Financial Officer |
| G. Stephen Holcomb..... | 53 | Vice President, Controller and Assistant Secretary |
| Ronald C. Dansby..... | 59 | President -- Inland Division, Kirby Inland Marine |
| Dorman L. Strahan..... | 42 | President -- Marine Systems |
| Mark R. Buese..... | 42 | Vice President -- Administration |
| Jack M. Sims..... | 56 | Vice President -- Human Resources |

No family relationship exists among the executive officers or among the executive officers and the directors. Officers are elected to hold office until the annual meeting of directors, which immediately follows the annual meeting of stockholders, or until their respective successors are elected and have qualified.

George A. Peterkin, Jr. holds a degree in business administration from the University of Texas and has served the Company as Chairman of the Board since April 1995. He has served as a Director of the Company since 1973 and served as President of the Company from 1976 to April 1995. He had served as a Director of Industries from 1969 to 1976 and as President of Industries from 1973 to 1976. Prior to that, he was President of Kirby Inland Marine from 1953 through 1972.

J.H. Pyne holds a degree in liberal arts from the University of North Carolina and has served as President and Chief Executive Officer of the Company since April 1995. He has served as a Director of the Company since 1988 and President of Kirby Inland Marine since 1984. He had served as Executive Vice President of the Company from 1992 to April 1995. He also served in various operating and administrative capacities with Kirby Inland Marine from 1978 to 1984, including Executive Vice President from January to June 1984. Prior to joining Kirby Inland Marine, he was employed by Northrop Services, Inc. and served as an officer in the United States Navy.

Norman W. Nolen is a Certified Public Accountant and holds an M.B.A. degree from the University of Texas and a degree in electrical engineering from the University of Houston. He has served as Senior Vice President, Treasurer and Chief Financial Officer of the Company since February 15, 1999. Prior to joining the Company, he served as Senior Vice President, Treasurer and Chief Financial Officer for Weatherford International, Inc. from 1991 to 1998. He served as Corporate Treasurer of Cameron Iron Works from 1980 to 1990 and as a corporate banker with Texas Commerce Bank from 1968 to 1980.

G. Stephen Holcomb holds a degree in business administration from Stephen F. Austin State University and has served the Company as Vice President, Controller and Assistant Secretary since January 1989. He also served as Controller from 1987 through 1988 and as Assistant Controller and Assistant Secretary from 1976 through 1986. Prior to that, he was Assistant Controller of Industries from 1973 to 1976. Prior to joining the Company, he was employed by Cooper Industries, Inc.

Ronald C. Dansby holds a degree in business administration from the University of Houston and has served the Company as President -- Inland Division of Kirby Inland Marine since 1994. He also serves as President of Kirby Inland Marine, Inc. of Texas, having joined the Company in connection with the acquisition of Alamo Inland Marine Co. ("Alamo") in 1989. He had served as President of Alamo since 1974. Prior to that, he was employed by Alamo Barge Lines and Monsanto Chemical from 1962 to 1973.

Dorman L. Strahan attended Nicholls State University and has served the Company as President of Marine Systems since 1986, President of Rail Systems since 1993 and President of Engine Systems since July 1996. After joining the Company in 1982 in connection with the acquisition of Marine Systems, he served as Vice President of Marine Systems until 1985.

Mark R. Buese holds a degree in business administration from Loyola University and has served the Company, or one of its subsidiaries, as Vice President -- Administration since 1993. He has also served as Vice President of Kirby Inland Marine since 1985 and served in various sales, operating and administrative capacities with Kirby Inland Marine from 1978 through 1985.

Jack M. Sims holds a degree in business administration for the University of Miami and has served the Company, or one of its subsidiaries, as Vice President -- Human Resources since 1993. Prior to joining the Company in March 1993, he served as Vice President -- Human Resources for Virginia Indonesia Company from 1982 through 1992, Manager Employee Relations for Houston Oil and Minerals Corporation from 1977 through 1981 and in various professional and managerial positions with Shell Oil Company from 1967 through 1977.

PART II

ITEM 5.MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's common stock is traded on the NYSE under the symbol KEX. The following table sets forth the high and low sales prices per share for the common stock for the periods indicated as reported by The Wall Street Journal.

| SALES PRICES | |
|--------------|-------|
| HIGH | LOW |
| ----- | ----- |

| | | |
|--|----------|---------|
| 1997 | | |
| First Quarter..... | \$19 3/4 | \$17 |
| Second Quarter..... | 19 7/8 | 16 3/8 |
| Third Quarter..... | 20 5/8 | 18 1/4 |
| Fourth Quarter..... | 21 1/8 | 17 7/8 |
| 1998 | | |
| First Quarter..... | 24 11/16 | 19 1/16 |
| Second Quarter..... | 25 11/16 | 21 1/2 |
| Third Quarter..... | 25 11/16 | 20 |
| Fourth Quarter..... | 21 9/16 | 17 1/4 |
| 1999 | | |
| First Quarter (through February 24, 1999)..... | 20 | 16 3/4 |

As of February 25, 1999, the Company had 20,295,894 outstanding shares held by approximately 1,350 stockholders of record.

The Company does not have an established dividend policy. Decisions regarding the payment of future dividends will be made by the Board of Directors based on the facts and circumstances that exist at that time. Since 1989, the Company has not paid any dividends on its common stock.

ITEM 6. SELECTED FINANCIAL DATA

The comparative selected financial data of the Company and consolidated subsidiaries is presented for the five years ended December 31, 1998. The tanker and harbor service operations' financial results for 1997 have been accounted for as discontinued operations and previously issued financial statements have been restated. The information should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations of the Company and the Financial Statements and Schedules included under Item 8 elsewhere herein (in thousands, except per share amounts):

| | FOR THE YEARS ENDED DECEMBER 31, | | | | |
|--|----------------------------------|------------------|------------------|------------------|------------------|
| | 1994(1) | 1995(1) | 1996(1) | 1997 | 1998 |
| Revenues: | | | | | |
| Marine transportation..... | \$255,462 | \$267,687 | \$249,594 | \$256,108 | \$244,839 |
| Diesel repair..... | 45,269 | 50,538 | 70,422 | 79,136 | 82,241 |
| Insurance(2)..... | 65,812 | 45,239 | -- | -- | -- |
| Investment income and other..... | 9,554 | 7,800 | 817 | 883 | 1,658 |
| Gain on disposition of assets..... | 415 | 10 | 2,751 | 407 | 3,517 |
| Realized gain on investments..... | 1,222 | 868 | -- | -- | -- |
| | <u>\$377,734</u> | <u>\$372,142</u> | <u>\$323,584</u> | <u>\$336,534</u> | <u>\$332,255</u> |
| Net earnings from continuing operations..... | | | | | |
| | \$ 16,969 | \$ 6,958 | \$ 21,208 | \$ 22,705 | \$ 10,109 |
| Discontinued operations: | | | | | |
| Earnings (loss) from discontinued operations, net of income taxes.... | (316) | 2,425 | 6,021 | 2,943 | -- |
| Estimated loss on sale of discontinued operations, net of income taxes.... | -- | -- | -- | (3,966) | -- |
| | <u>(316)</u> | <u>2,425</u> | <u>6,021</u> | <u>(1,023)</u> | <u>--</u> |
| Net earnings..... | <u>\$ 16,653</u> | <u>\$ 9,383</u> | <u>\$ 27,229</u> | <u>\$ 21,682</u> | <u>\$ 10,109</u> |
| Earnings (loss) per share of common stock: | | | | | |
| Basic: | | | | | |
| Continuing operations..... | \$.60 | \$.25 | \$.83 | \$.93 | \$.46 |
| Discontinued operations..... | (.01) | .09 | .24 | (.04) | -- |
| | <u>\$.59</u> | <u>\$.34</u> | <u>\$ 1.07</u> | <u>\$.89</u> | <u>\$.46</u> |
| Diluted: | | | | | |
| Continuing operations..... | \$.59 | \$.25 | \$.82 | \$.92 | \$.46 |

| | | | | | |
|--------------------------------------|--------|--------|---------|--------|--------|
| Discontinued operations..... | (.01) | .09 | .24 | (.04) | -- |
| | ----- | ----- | ----- | ----- | ----- |
| | \$.58 | \$.34 | \$ 1.06 | \$.88 | \$.46 |
| | ===== | ===== | ===== | ===== | ===== |
| Weighted average shares outstanding: | | | | | |
| Basic..... | 28,290 | 27,561 | 25,555 | 24,381 | 21,847 |
| Diluted..... | 28,790 | 27,772 | 25,781 | 24,594 | 22,113 |

DECEMBER 31,

| | ----- | ----- | ----- | ----- | ----- |
|----------------------------------|-----------|-----------|-----------|-----------|-----------|
| | 1994 (1) | 1995 (1) | 1996 (1) | 1997 | 1998 |
| | ----- | ----- | ----- | ----- | ----- |
| Property and equipment, net..... | \$284,444 | \$275,184 | \$277,622 | \$272,384 | \$256,899 |
| Total assets..... | \$667,472 | \$498,084 | \$524,530 | \$517,959 | \$390,299 |
| Long-term debt..... | \$159,497 | \$179,226 | \$181,950 | \$154,818 | \$142,885 |
| Stockholders' equity..... | \$222,976 | \$205,333 | \$205,754 | \$218,269 | \$141,040 |

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- (1) Comparability with prior periods is affected by the following: the Company's ownership of the voting stock of Universal declining to 47% on July 18, 1995, and the recording of the Company's investment in Universal on the equity method of accounting effective July 1, 1995; and the purchase of the assets of MKW in July 1996.
- (2) The Company changed its method of reporting its investment in Universal from a consolidated basis to the equity method of accounting effective July 1, 1995.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Statements contained in this Form 10-K that are not historical facts, including, but not limited to, any projections contained herein, are forward-looking statements and involve a number of risks and uncertainties. Such statements can be identified by the use of forward-looking terminology such as "may," "will," "expect," "anticipate," "estimate" or "continue" or the negative thereof or other variations thereon or comparable terminology. The actual results of the future events described in such forward-looking statements in this Form 10-K could differ materially from those stated in such forward-looking statements. Among the factors that could cause actual results to differ materially are: adverse economic conditions, industry competition and other competitive factors, adverse weather conditions such as high water, low water, fog and ice, marine accidents, construction of new equipment by competitors, including construction with government assisted financing, government and environmental laws and regulations, and the timing, magnitude and number of acquisitions made by the Company.

In March 1998, the Company completed the sale of its offshore tanker and harbor service operations. In accordance with a definitive purchase agreement dated January 28, 1998, the Company sold two tankers and its harbor service operations to Hvide Marine Incorporated and five tankers to August Trading Company, Inc. for a combined purchase price of \$38,600,000 in cash. The offshore tanker and harbor service operations' financial results have been accounted for as discontinued operations as of December 31, 1997, and previously reported financial statements have been restated to reflect the discontinuation of the operations. Such financial results as of December 31, 1997 included a provision for operations during the phase-out period, January 1, 1998 through the date of sale.

RESULTS OF OPERATIONS

The Company reported net earnings of \$10,109,000, or \$.46 per share, on revenues of \$332,255,000 for the 1998 year, compared with net earnings from continuing operations of \$22,705,000, or \$.92 per share, on revenues of \$336,534,000 for the 1997 year, and net earnings from continuing operations of \$21,208,000, or \$.82 per share, on revenues of \$323,584,000 for the 1996 year.

Marine transportation revenues totaled \$244,839,000, or 74% of total revenues for 1998, compared with \$256,108,000, or 76% of total revenues from 1997, and \$249,594,000, or 77% of total revenues for 1996. Diesel repair revenues for 1998 totaled \$82,241,000, or 25% of total revenues for 1998, compared with \$79,136,000, or 24% of total revenues for 1997, and \$70,422,000, or 22% of total revenues for 1996. Investment income and other income, earned primarily through the Company's captive insurance company, totaled \$1,658,000 for 1998, \$883,000 for 1997 and \$817,000 for 1996.

The Company reported net gains from the disposition of assets in each year, predominately from the sale of marine equipment. For the 1998 year, the Company reported a net gain of \$3,517,000, which includes a \$3,900,000 net gain from the sale of an offshore liquid tank barge and tug unit in October. During the 1998 year, the Company also recorded a loss on the scrapping of two ammonia barges and other equipment totaling a net loss of approximately \$400,000. For the 1997 year, the Company reported a net gain of \$407,000, primarily from the sale of two offshore freighters. For the 1996 year, a net gain of \$2,751,000 resulted primarily from the sale of two inland towboats and six inland asphalt barges.

The 1998 results included a third quarter financial loss totaling \$10,536,000, \$6,849,000 after taxes, or \$.31 per share, from the sale of the Company's remaining 45% voting common stock interest and its non-voting preferred stock interest in Universal for \$36,000,000 in cash. The Company's investment in Universal was accounted for under the equity method of accounting. The sale is more fully described below.

The 1998 results also included a third quarter reduction in the carrying value of an offshore tank barge and tug unit totaling \$8,333,000, \$5,416,000 after taxes, or \$.24 per share. Such reduction was in accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." The reduction is more fully described below.

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MARINE TRANSPORTATION

The Company, through its subsidiaries, is a provider of marine transportation services, operating a fleet of 523 inland tank barges and 128 inland towing vessels, transporting industrial chemicals and petrochemicals, refined petroleum products and agricultural chemicals along the United States inland waterways. The Company's marine transportation operation also includes one offshore dry-bulk barge and tug unit. The Company also serves as managing partner of a 35% owned offshore marine partnership, consisting of four dry-bulk barge and tug units, and as managing partner of a 50% owned offshore marine partnership, consisting of one dry-bulk barge and tug unit. The partnerships are accounted for under the equity method of accounting.

The Company's marine transportation segment reported 1998 transportation revenues of \$244,839,000, a decrease of 4% compared with \$256,108,000 reported for the 1997 year, and a decrease of 2% compared with \$249,594,000 reported for the 1996 year.

1998 Marine Transportation Revenues

Marine transportation revenues for the 1998 year reflected a continued upward trend in spot market rates and contract renewals were generally at higher rates. The marine transportation segment operates under long-term contracts, short-term contracts and spot movements of products. During 1998, approximately 80% of movements were under term contracts and 20% were spot market movements. Chemical and petrochemical volumes increased gradually from 1997 levels, while refined product movements and liquid fertilizer movements declined slightly. Both refined product and liquid fertilizer movements were negatively impacted by increased volumes produced in Midwest facilities, reducing ton miles moved during 1998 versus 1997. The decline in the price of diesel fuel during 1998 also negatively impacted 1998 marine transportation revenues compared with the 1997 year. In certain contracts, diesel fuel consumed is passed through to the customer, and with lower diesel fuel prices during 1998, revenues were lower.

During the 1998 year, the Company experienced numerous navigational delays, primarily weather related. During September 1998, the Company was negatively impacted by two hurricanes and one tropical storm along the Gulf of Mexico, significantly reducing fleet efficiency. Loss of revenues due to the storm

events was estimated at \$600,000 and additional operating expenses incurred were estimated at \$400,000. The effects of the three storm events reduced the Company's net earnings by an estimated \$.02 to \$.03 per share. During the 1998 fourth quarter, navigational delays also negatively impacted revenues and increased operating expenses. Delays were experienced in numerous areas of operations at various times during the quarter, the result of heavy rains in Southeast and Central Texas, flooding on the Arkansas River, and low water on the Ohio River. The delays increased transit time, thereby reducing operating efficiencies.

In October 1998, the Company sold its two offshore tank barge and tug units, exiting the market for the coastwise transportation of liquid petroleum products. One of the units was fully employed through September 1998 and the other unit was employed only through July 1998. In 1997, the Company also scrapped two remaining U.S. flag offshore break-bulk freighters. The 1997 year reflected revenues of \$15,481,000 from the tank barge and tug units sold in 1998 and the freighters scrapped in 1997. The 1998 year reflected revenues of \$4,509,000 from the tank barge and tug units before their sale.

1997 Marine Transportation Revenues

Marine transportation revenues for the 1997 year totaled \$256,108,000, an increase of 3% compared with \$249,594,000 for the 1996 year. The 1997 revenues reflected a modest increase in utilization and spot market rates, and the renewal of contracts generally at higher rates. During the second half of 1996 and during 1997, the segment decreased its active inland tank barge fleet capacity by a net 3%, removing from service older single skin barges when it was not prudent to continue to maintain or overhaul the barges. Chemical and petrochemical volumes held at 1996 levels, while refined product volumes improved during 1997 over 1996. The 1997 year was negatively impacted by the flooding on the Mississippi River System during the months of February through April. During the majority of the 1997 first quarter, the upper Mississippi River and Ohio River experienced high water and flooding conditions, with river closures in selected areas and mandated regulatory operating restrictions. During the month of March and extending into April, the lower Mississippi

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River, the Company's principal area of operations, experienced high water not seen in such severity since 1983. The effects of the flooding throughout the Mississippi River System reduced the Company's revenues and increased its expenses, resulting in a reduction in net earnings by an estimated \$.11 per share for the 1997 year.

During 1997, the Company scrapped its last two of three U.S. flag offshore break-bulk freighters, which were engaged in the transportation of food-aid commodities and related products under the United States Government's preference food-aid programs. Excess equipment capacity and lack of available cargo, which resulted in low rates, led to the decision to scrap the Company's remaining two freighters. One freighter was scrapped in September 1997, after a food-aid voyage to North Korea. The last freighter was scrapped in October 1997 following a food-aid trip to East Africa. In September 1996, after a food-aid trip to North Korea, the Company scrapped its first freighter. The freighters were scrapped overseas, taking advantage of higher foreign scrap metal prices.

1996 Marine Transportation Revenues

Marine transportation revenues for the 1996 year totaled \$249,594,000, a decrease of 7% compared with \$267,687,000 for the 1995 year. Contract volumes for the movement of chemicals were stable and rates flat during 1996; however, spot market volumes remained soft, with week-to-week variations in demand, and certain spot market pricing pressure. The contract and spot market movements of refined products in the Mississippi River declined to some degree. Such reduction in volumes resulted in lower rates for spot market river movements. The Gulf Intracoastal Waterway movements of refined products remained weak for the entire 1996 year, resulting in lower rates for such movements. Additional Midwest refinery capacity and some improved pipeline efficiencies through debottlenecking were the primary reasons for the decline in refined products volumes and rates.

The principal reason for the 7% decline in marine transportation revenues for 1996 compared with 1995 was the significant weakness in the movement of United States Government preference food-aid cargo and military household goods. Revenues derived from that market for 1996 fell 64% to \$9,661,000 compared with

\$26,658,000 in 1995. Excess equipment capacity and a reduction in available movements resulted in inadequate rates. During 1996, the Company averaged only one of its freighters being employed. As noted above, the Company scrapped one freighter in September 1996 and scrapped the remaining two freighters in 1997.

Marine Transportation Costs and Expenses

Costs and expenses, excluding interest expense and the impairment of a long-lived asset discussed below, for the marine transportation segment for the 1998 year totaled \$207,178,000, down 4% compared with 1997 costs and expenses of \$216,566,000, and down 2% compared with 1996 costs and expenses of \$211,422,000. Each year reflected higher equipment costs, health and welfare costs, and inflationary increases in costs and expenses. Specific events which affected the costs and expenses for each of the last three years are more fully described below.

1998 Marine Transportation Costs and Expenses

As stated above, the 1998 year included an impairment of a long-lived asset of \$8,333,000. The carrying value of an offshore tank and barge tug was written down in the 1998 third quarter in accordance with SFAS No. 121. The unit was sold on October 30, 1998, for a price approximating the revised carrying value of the unit.

The 1998 year also included approximately \$4,500,000 of higher vessel labor costs when compared with the 1997 year. During the 1998 year, the Company increased afloat labor compensation by approximately 20%. Due to a tight afloat labor market, the 20% increase was necessary not only to retain current employees, but also to increase compensation to levels which were competitive with other industries so as to attract new personnel into the Company for the future. The 20% compensation increase reflected a 6% increase effective March 1, an 11% increase effective August 1, as well as increased longevity pay, trip pay, travel pay and

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mileage reimbursement. In addition, during 1998, due to afloat labor shortages, the Company incurred approximately \$900,000 of additional costs associated with hiring outside labor, principally tankermen.

During 1998, marine transportation costs and expenses reflected higher maintenance costs as compared with the 1997 year. The higher maintenance costs were due to the Company competing for shipyard space with companies participating in the oil and gas drilling activities in the Gulf of Mexico and a fleet which is continuing to age. During the 1998 second half, such competition diminished due to the decline in drilling activities.

1997 Marine Transportation Costs and Expenses

As discussed under 1997 Marine Transportation Revenues, the segment incurred additional expenses associated with the 1997 February through April flooding in the Mississippi River, reflecting the higher costs and equipment utilization associated with the flooding. During 1997, the marine transportation segment achieved a sustainable reduction in costs and expenses of approximately \$3,400,000 (\$2,200,000 after taxes, or \$.09 per share) from its cost reduction efforts implemented in 1996, as more fully discussed under the 1996 Marine Transportation Costs and Expenses. Savings obtained from cost reductions during 1997 were partially offset by continued higher vessel labor and vessel maintenance costs. The Company competed with the same labor pool and for the same shipyard space as companies which participated in the oil and gas drilling activities in the Gulf of Mexico, which were lucrative at that time. For comparative purposes, the 1997 year included \$7,261,000 of costs and expenses associated with revenues generated by the Company's two remaining U.S. flag offshore break-bulk freighters which were scrapped in September and October 1997.

1996 Marine Transportation Costs and Expenses

Effective January 1, 1996, the transportation segment changed the estimated depreciable lives of its inland tank barges and towboats. Vessel upgrades and enhanced maintenance standards resulted in useful lives beyond the original estimated lives. The change in the estimated lives provided a more consistent matching of revenues and depreciation expense over the economic useful lives of the inland barges and towboats. The depreciable lives of inland double skin

barges were changed from an average of 22 years to 30 years and inland towboats were changed from an average of 22 years to 35 years. Changes were made on single skin barges on a barge-by-barge basis, with shorter lives recorded in anticipation of early retirements when appropriate. Salvage values were also assigned to certain inland vessels where it was reasonable to expect that the vessel would have a residual value at the end of its depreciable life. The result of the change in depreciable lives was to reduce 1996 depreciation expense by approximately \$2,500,000 (\$1,625,000 after taxes, or \$.06 per share).

During 1996, the Company focused its efforts on decreasing costs and expenses and improving operating efficiencies. Reorganizational changes were made during 1996, resulting in office closures and the consolidation of the majority of sales, traffic, maintenance and accounting functions in Houston, Texas. The Company incurred reorganization expense in 1996 of approximately \$2,700,000 (\$1,755,000 after taxes, or \$.07 per share).

The Company's freighters, reduced from three to two in 1996, experienced significant idle time as demand was very sporadic. In addition, the write-down of the freighters in 1995, in accordance with SFAS No. 121, substantially reduced depreciation and amortization expenses applicable to the freighters.

Marine Transportation Operating Income

Operating income for the marine transportation segment for the 1998 year totaled \$37,661,000, a decrease of 5% compared with \$39,542,000 for the 1997 year, and 1% lower than the \$38,172,000 of operating income for the 1996 year. Operating margins for 1998 were 15.4% compared with 15.4% for 1997 and 15.3% for 1996.

The Company's investment in two offshore marine partnerships, accounted for under the equity method of accounting, reported earnings for the 1998 year of \$946,000, down 69% from earnings of \$3,084,000 for 1997 and down 76% compared with earnings from the partnerships of \$3,912,000 for 1996. During the 1998 fourth quarter, the carrying value of the offshore dry-cargo barge and tug unit owned through the Dixie

Fuels II partnership was reduced by \$5,900,000, \$2,950,000 to the Company. The impairment, in accordance with SFAS No. 121, was recorded as a reduction in equity in earnings of marine affiliates. The 1998 year benefited from lower scheduled maintenance on the partnership's vessels and higher coal volume requirements. The 1997 year reflected higher maintenance and lower coal requirements. The 1996 year reflected enhanced coal and limestone rock contract volume movements.

DIESEL REPAIR

The Company is engaged through its diesel repair segment in the overhaul and servicing of large medium-speed diesel engines employed in marine, power generation and rail applications. The diesel repair segment is divided into three subsidiaries organized around the markets they serve. Marine Systems operates on the Gulf Coast and West Coast and in the Midwest through three facilities that repair and overhaul marine diesel engines and reduction gears, and sells parts and accessories. Rail Systems is the exclusive distributor of aftermarket parts to shortline and industrial railroads for EMD and provides replacement parts, service and support nationwide to shortline railroads and industrial companies that operate locomotives. Engine Systems, organized in July 1996 with the purchase of the assets of MKW, expanded the Company's relationship with EMD to an authorized distributorship for 17 eastern states and the Caribbean. In addition, Engine Systems serves as the exclusive worldwide distributor of EMD products to the nuclear industry.

The Company's diesel repair segment reported 1998 diesel repair revenues of \$82,241,000, an increase of 4% compared with \$79,136,000 reported for the 1997 year, and an increase of 17% compared with \$70,422,000 reported for the 1996 year.

1998 Diesel Repair Revenues

The 4% increase in diesel repair revenues for 1998 over 1997 was primarily due to a strong demand nationwide for direct parts sales. For the 1998 first half, the Gulf Coast market remained strong due to the oil and gas drilling

activities and related oil services activities in the Gulf of Mexico. During the 1998 second half, the Gulf Coast market did experience a modest decline in activities, as the Gulf of Mexico drilling market subsided. The East Coast, Midwest and West Coast markets remained positive, supported by the continued strong overall economy. During the 1998 year, the Company exited the power control business line acquired from MKW in 1996. The diesel repair segment reported revenues from that business line of \$5,100,000 during 1998 compared with \$6,600,000 for the 1997 year.

1997 Diesel Repair Revenues

Diesel repair revenues for the 1997 year totaled \$79,136,000, a 12% increase compared with \$70,422,000 for the 1996 year, reflecting the inclusion of MKW for the entire year, as the assets were acquired in July 1996. During 1997, the segment eliminated certain MKW unprofitable business lines. Diesel repair revenues for the 1997 year were negatively impacted by deferred overhauls from Midwest inland towing customers due to spring flooding and by Midwest dry-cargo customers due to slow grain exports. The Gulf Coast market remained strong due to the continued enhanced drilling activities and related oil services activities in the Gulf of Mexico. The East Coast market was supported by a strong overall economy, while the West Coast market remained depressed due to a continued weak North Pacific fishing market.

1996 Diesel Repair Revenues

Diesel repair revenues for the 1996 year totaled \$70,422,000, an increase of 39% compared with \$50,538,000 for the 1995 year. The 1996 year included approximately \$12,600,000 of revenues generated from the acquisition of MKW in July 1996. In addition, the 1996 year benefited from enhanced drilling activities and related oil services activities in the Gulf of Mexico, and continued health of the inland tank barge and dry-cargo industry in its Gulf Coast and Midwest markets. The West Coast market was hampered by a depressed offshore fishing market and as a result, during 1996 the diesel repair segment shifted its focus from the South Pacific fishing fleet to the North Pacific fishing fleet.

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Diesel Repair Costs and Expenses

Costs and expenses, excluding interest expense, for the diesel repair segment for 1998 totaled \$74,191,000 compared with \$72,947,000 for 1997 and \$65,046,000 for 1996. The 2% increase for 1998 over 1997 and the 14% increase for 1998 over 1996 reflected the overall continued growth of the diesel repair segment. The increases were net of cost reduction efforts from the consolidation of operations and savings in general and administrative expenses.

Diesel Repair Operating Income

The diesel repair segment's operating income for 1998 was \$8,050,000, an increase of 30% compared with \$6,189,000 for 1997, and 50% over 1996 operating income of \$5,376,000. Operating margins for 1998 were 9.8% compared with 7.8% for 1997 and 7.6% for 1996.

PROPERTY AND CASUALTY INSURANCE

Effective September 30, 1998, the Company sold its remaining 45% voting common stock interest and its non-voting preferred stock interest in Universal for \$36,000,000 in cash. Universal, a property and casualty insurance company in the Commonwealth of Puerto Rico, was formed by Kirby in 1972. In September 1992, the Company merged Universal with Eastern America, a subsidiary of Eastern America Group. In accordance with a shareholders agreement among the Company, Universal and Eastern America Group, through redemption rights, Universal had the obligation to purchase the Company's entire interest in Universal gradually, over a 15 year period. The Company closed the sale on October 7, 1998 and the cash proceeds were used to reduce the Company's revolving line of credit.

Under an anticipated redemption schedule, the Company would have received a stream of cash payments between now and the year 2008 totaling \$62,000,000. The \$36,000,000 received represented the present value of the payment stream. Including prior redemptions and the final sale, the Company received total payments of \$58,000,000 for its interest in Universal.

The Company recognized, during the 1998 third quarter, a pre-tax loss for financial purposes of \$10,536,000 on the Universal transaction. The Company's investment in Universal, accounted for under the equity method of accounting, was based on the estimated receipt of \$62,000,000 of redemption payments to the Company over the next eleven years, and the recording of the remaining built-in gain on the sale.

The amount recorded by the Company as equity in earnings for the Company's investment in Universal was influenced by anticipated future redemptions by Universal of its common stock. The Company also had a 100% ownership in Universal's non-voting preferred stock. Because the preferred stock was collateralized by a separate portfolio of U.S. Treasury Securities, the Company accounted for this preferred stock under SFAS No. 115. Therefore, the interest earned, as well as the realized gains from the sale of U.S. Treasury Securities collateralizing the preferred stock, were included as part of equity in earnings of the insurance affiliate. During 1998, 1997 and 1996, the Company recorded \$790,000, \$1,044,000 and \$980,000, respectively, of interest earned from its investment in U.S. Treasury Securities. In 1997 and 1996, the Company recognized \$465,000 and \$592,000, respectively, of realized gains from the sale of such U.S. Treasury Securities. In addition, during the 1997 year, the Company recognized as equity in earnings of insurance affiliate, \$2,500,000 of cash received from Universal as the result of a resolution of a previously reserved Universal contingency for outstanding litigation. The litigation was fully reserved on Universal's records and was set aside as part of the merger in 1992 of Universal with Eastern America Group.

For the 1998 year, in addition to the loss on the sale of the Company's remaining interest in Universal as noted above, the Company recorded equity in earnings from Universal of \$1,325,000 for the first nine months of 1998, compared with \$4,609,000 for the 1997 year and \$2,171,000 for the 1996 year.

DISCONTINUED OPERATIONS

The Company's offshore tanker and harbor service operations were accounted for as discontinued operations as of December 31, 1997, and previously reported financial statements were restated. In accordance

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with the purchase agreement noted above, the Company's offshore tanker and harbor service operations were sold in March 1998.

The Company reported a 1997 net loss from discontinued operations of \$1,023,000, or \$.04 per share, compared with net earnings from discontinued operations of \$6,021,000, or \$.24 per share, for the 1996 year. The 1997 year included an estimated \$3,966,000 net loss, or \$.16 per share, from the sale of the operations. The estimated net loss included a provision for an operating loss of \$700,000 during the phase-out period, January 1, 1998 through the date of sale.

The Company's discontinued marine transportation operations reported 1997 marine transportation revenues of \$66,434,000, relatively flat compared with revenues of \$66,773,000 reported for 1996. Costs and expenses for the discontinued operations totaled \$62,002,000 for 1997, reflecting a 7% increase over \$57,700,00 for 1996. Operating income for the discontinued operations totaled \$4,598,000 for 1997, 51% lower than operating income of \$9,354,000 reported for 1996.

The offshore discontinued tanker market was very volatile during the years 1995 through 1997. Reduced demand for movements of products during certain seasons, as well as unanticipated and unneeded increases in capacity, lead to a very volatile offshore tanker market, and a market where periodic lay-ups of tankers occurred with increased regularity. Such volatility contributed to the Company's decision to exit the tanker and harbor service operations, and concentrate on the core inland tank barge and diesel repair businesses.

FINANCIAL CONDITION, CAPITAL RESOURCES AND LIQUIDITY

Balance Sheet

Total assets as of December 31, 1998 were \$390,299,000, a decrease of 25% compared with \$517,959,000 as of December 31, 1997 and 26% lower than the December 31, 1996 total assets of \$524,530,000. The December 31, 1997 and 1996 total assets included \$49,036,000 and \$59,365,000, respectively, of assets

attributable to the discontinued tanker and harbor service operations and \$45,320,000 and \$44,554,000, respectively, of assets attributable to the Company's investment in Universal, which were sold in October 1998. The December 31, 1997 and 1996 total assets also reflected the carrying value of the two offshore tank barge and tug units sold in October 1998.

The available-for-sale securities of \$20,795,000 as of December 31, 1998 and \$21,773,000 as of December 31, 1997 were investments of Oceanic, the Company's wholly-owned captive insurance subsidiary.

Total liabilities as of December 31, 1998 totaled \$249,259,000, a decrease of 17% compared with \$299,690,000 as of December 31, 1997, and 22% lower than the December 31, 1996 total liabilities of \$318,776,000. The 52% decrease in accounts payable and 66% decrease in other accrued liabilities from December 31, 1997 to 1998 primarily reflected the sale of the offshore tanker and harbor service operations and the two offshore tank barge and tug units. The 8% reduction in long-term debt from \$149,485,000 in 1997 to \$137,552,000 in 1998 reflected net payments on debt more fully described below. The 17% decrease in deferred income taxes from \$48,409,000 in 1997 to \$40,045,000 in 1998 primarily reflected the sale of Universal.

Stockholders' equity as of December 31, 1998 totaled \$141,040,000 compared with \$218,269,000 as of December 31, 1997 and \$205,754,000 as of December 31, 1996. The 1998 stockholders' equity balance reflected the Company's purchase of its common stock under the Dutch Auction self-tender offer and open market repurchases. The 1997 and 1996 stockholders' equity year-end balances also reflect the Company's repurchase programs as more fully described in Treasury Stock Purchases below.

Long-Term Financing

The Company has a \$100,000,000 revolving credit agreement (the "Credit Agreement") with Chase Bank of Texas, N.A., as agent bank. On September 19, 1997, the Company agreed to new terms with Chase regarding the Credit Agreement, superseding the previous Credit Agreement dated March 18, 1996. Under the new terms, the maturity date was extended to September 19, 2002 from December 31, 1998. The new

Credit Agreement reduced the margin of interest paid on its borrowings, provided adjusted interest rates based on the Company's senior credit rating and eliminated certain financial covenants. The new Credit Agreement also contains usual and customary events of default. The Credit Agreement was amended effective January 30, 1998 to provide a one-time allowance for the disposition of assets at the subsidiary level. The amendment also modified the minimum net worth covenant and fixed charge calculation. The Credit Agreement was also amended effective November 30, 1998 to modify the minimum net worth covenant to allow for anticipated activity under the Company's stock repurchase program. The Company was in compliance with all covenants as of December 31, 1998. Proceeds under the Credit Agreement may be used for general corporate purposes, the purchase of existing or new equipment, the purchase of the Company's common stock, or for possible business acquisitions. As of December 31, 1998, \$26,000,000 was outstanding under the Credit Agreement.

In December 1994, the Company established a \$250,000,000 medium term note program providing for the issuance of fixed rate or floating rate notes with the maturities of nine months or longer. The shelf registration program, registered with the Securities and Exchange Commission, was activated in March 1995 with the issuance of \$34,000,000 of the authorized notes. The issued medium term notes bore interest at an average fixed rate of 7.77% and matured on March 10, 1997. Proceeds from sale of the notes were used to retire the Company's outstanding bank term loan in the amount of \$10,286,000, due June 1, 1997, and to reduce the Company's outstanding revolving credit loans by \$23,714,000. The Company's outstanding bank term loan in the amount of \$10,666,000, due March 6, 1997, was retired on March 20, 1995 with proceeds borrowed under the Company's revolving credit agreements. In June 1995, the Company issued \$45,000,000 of authorized notes, bearing a fixed interest rate of 7.25%, with a maturity of June 1, 2000. Proceeds from the sale of the notes were used to reduce the Company's outstanding revolving credit loans. In January 1997, the Company issued \$50,000,000 of the authorized medium term notes at a fixed interest rate of 7.05%, due January 29, 2002. Proceeds from the sale of notes were used to retire \$34,000,000 of medium term notes due March 10, 1997, with the balance

used to reduce the Company's revolving Credit Agreement noted above. The \$34,000,000 notes were classified as long-term at December 31, 1996, as the Company had the ability and intent to refinance the notes either by selling new medium term notes, or through the Company's revolving Credit Agreement. As of December 31, 1998 and 1997, \$121,000,000 was available under the medium term note program to provide financing for future business and equipment acquisitions and fund working capital requirements.

Business Acquisitions and Developments

On July 31, 1996, a subsidiary of the Company purchased the operating assets of MKW for approximately \$5,700,000 in cash plus approximately \$8,500,000 for MKW's working capital. The acquisition expanded the diesel repair segment's relationship with EMD to an authorized distributorship for 17 eastern states and the Caribbean.

Capital Expenditures

In May 1994, the Company entered into a contract for the construction of 12 double skin 29,000 barrel capacity inland tank barges for use in the movement of industrial chemicals and refined products. In February 1995, the Company exercised the option under the contract to construct 12 additional barges. During 1995, nine of the tank barges were placed in service, 13 were placed in service during 1996, one was placed in service in January 1997 and the last barge was placed in service in February 1997. A third option for the construction of 12 additional barges was not exercised. In addition, in April 1995, the Company entered into a contract for the construction of two double skin 17,000 barrel capacity inland tank barges for use in the industrial chemical market. One barge was placed in service in October 1995 and the second barge in January 1996. The construction project cost approximately \$1,500,000 per barge. Funds for the construction project were available through the Company's Credit Agreement and cash provided by operating activities.

In 1998, the Company purchased 17 existing inland tank barges for use in the linehaul fleet and four existing inland towboats were purchased for use in the fleet and shifting operation. During 1996, one existing inland towboat was purchased for use in the fleet and shifting operation. In 1995, one existing

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double skin inland tank barge and four existing inland towboats were purchased for use in the industrial chemical market, and four existing double skin inland tank barges and three existing inland towboats were purchased for use in the refined products market. In addition, during 1995, two existing inland towboats were purchased for use in the fleet and shifting operation and two existing double skin inland tank barges were purchased for use in the agricultural chemical market. As of December 31, 1998, the Company had no material commitments for capital expenditures.

Treasury Stock Purchases

On March 23, 1998, the Company purchased 3,066,922 shares of its common stock under a Dutch Auction self-tender offer at a price of \$24.50 per share. The Company announced the self-tender offer on February 17, 1998, expressing its intentions to purchase up to 3,000,000 shares of its common stock at a purchase price ranging from \$21.00 to \$24.50 per share. The tender offer expired on March 16, 1998. The Company elected to increase the size of the 3,000,000 share tender offer and to accept all shares tendered at a price of \$24.50 per share. The 3,066,922 shares purchased represented approximately 12.6% of the Company's common stock outstanding immediately prior to the offer. Funding of the tender offer was from the Company's Credit Agreement.

During 1998, the Company purchased in the open market 739,000 shares of its common stock at a total price of \$15,541,000, for an average price of \$21.04 per share. During 1997, the Company purchased 626,000 shares of its common stock at a total price of \$11,699,000, for an average price of \$18.70 per share. During 1996, the Company purchased 1,587,000 shares of its common stock at a total price of \$26,331,000, for an average price of \$16.60 per share. Since January 1, 1999, the Company has purchased 479,000 shares of its common stock at a total purchase price of \$8,309,000, for an average price of \$17.35 per share. The Company as of February 25, 1999, had 596,000 shares remaining under its Board of Directors' 6,250,000 total open market purchase authorization. The treasury stock purchases were financed by borrowing under the Company's Credit Agreement.

The Company is authorized to purchase its common stock on the New York Stock Exchange and in privately negotiated transactions. When purchasing its common stock, the Company is subject to price, trading volume and other market considerations. Shares purchased may be used for reissuance upon the exercise of stock options, in future acquisitions for stock or for other appropriate corporate purposes.

Liquidity

The Company generated net cash provided by operating activities of continuing operations of \$37,029,000, \$48,024,000 and \$44,778,000 for the years ended December 31, 1998, 1997 and 1996, respectively. Universal, prior to the completion of the sale of the Company's remaining interest in October 1998, did not contribute cash flow for 1998 and 1996, as the Company recognized cash flow from Universal only upon receipt of actual distributions. In 1997, the Company received a \$2,000,000 cash distribution from Universal.

The Company also accounts for its ownership in 35% and 50% owned marine partnerships under the equity method of accounting, recognizing cash flow only upon the receipt or disbursements of cash from the partnerships. For the 1998 year, the Company received \$4,407,000 of cash from the marine partnerships, disbursed cash to the marine partnerships of \$475,000 in 1997 and received \$3,200,000 of cash from the marine partnerships in 1996.

Funds generated are available for capital construction projects, treasury stock repurchases, asset acquisitions, repayment of borrowings associated with treasury stock acquisitions or asset acquisitions and for other operating requirements. In addition to its net cash flow provided by operating activities, the Company also has available as of February 25, 1999, \$86,000,000 under its revolving credit agreement and \$121,000,000 available under its medium term note program. The Company's fixed principal payments during the next 12 months are \$5,333,000.

During the last three years, inflation has had a relatively minor effect on the financial results of the Company. The marine transportation segment has long-term contracts which generally contain cost escalation

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clauses whereby certain costs, including fuel, can be passed through to its customers. The repair portion of the diesel repair segment is based on prevailing current market rates.

Year 2000

Certain computer systems, software programs, and semiconductors are not capable of recognizing certain dates in 1999 and after December 31, 1999, and will read dates in the year 2000 and thereafter as if those dates represent the year 1900 or thereafter, or will fail to process those dates. This "Year 2000 Issue" could result in the failure of certain systems or other errors that could disrupt normal business activities.

The Company has designed and implemented an action plan to determine the likely exposures of the Company and its subsidiaries to the Year 2000 Issue and to take the necessary action to minimize the impact of those exposures. The Company's Year 2000 action plan addresses both internal and external exposures to the Year 2000 Issue.

With respect to the Company's internal Year 2000 exposures, the action plan addresses both land-based and vessel-based systems. The land-based systems include all of the Company's network components, core corporate software applications, personal computers, telephone systems, building management control systems and critical office equipment. The vessel-based systems include electronic navigation equipment, diesel engine controlling systems, and fire and other emergency monitors and alarms.

The Company's external exposures to the Year 2000 Issue include vendors and suppliers of critical services including communications, fuel and supplies, barge cleaning and repair, and government waterways maintenance and management. The Company's external exposures also include general business support services such as electric power, telephone, and banking services, as well as customers' accounts payable systems. The Company may experience Year 2000 problems as a result of these external exposures. The Company is attempting to address all Year 2000 exposures in advance; however, the Company could potentially

experience temporary disruptions to certain aspects of activities or operations as a result of the external exposures noted above. It is not possible to determine whether or to what extent any or all of these exposures are likely to occur or the costs involved in any of the exposures. However, the costs to the Company could be material.

The Company's Year 2000 action plan divides the Company's actions with respect to its internal and external exposures to the Year 2000 Issue into three sequential stages:

- Investigation. This stage includes the physical inventorying of all computer systems, software applications, and equipment relying on computer software or embedded semiconductors, communicating with the manufacturers and distributors regarding, and establishing procedures to evaluate and test, Year 2000 compliance, and the completion of that evaluation and testing. This stage has been substantially completed with respect to the Company's network components, core corporate software applications, personal computers, and telephone systems. The Company is in the process of communicating with manufacturers and distributors of other critical equipment, systems, and services. Those efforts are expected to be completed by the end of the first quarter of 1999.
- Remediation. This stage involves the repair or replacement of the Company's equipment and systems which have been identified as not being Year 2000 compliant in the investigation stage and the validation of the compliance of the equipment and systems which have been repaired or replaced. This stage has been substantially completed with respect to the Company's network components, core corporate software applications, personal computers, and telephone systems. The remainder of the Company's efforts in this stage are expected to be completed by mid-1999.
- Contingency Planning. Dependent on the findings of the investigation stage, the Company's actions in this stage may include the development of business scenarios likely to result from Year 2000 compliance failures by external suppliers or their equipment, systems or services, and the development of remedies to minimize the consequences of such failures on the Company's business. Those remedies may include preventative measures and "work around" solutions. This stage is expected to be complete by the end of the third quarter of 1999.

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While the Company expects that the stages of its Year 2000 action plan will be completed as indicated above, the Company must rely on third parties, including government agencies, manufacturers, distributors, vendors and suppliers, to provide information and to take actions which are beyond the Company's control. In addition, it is not possible for the Company to predict either the timeliness or the substance of the information and actions provided by third parties. Accordingly, the Company can also not predict whether or to what extent the information provided by third parties will affect the timely completion of each stage of the Year 2000 action plan, as the information provided by third parties may require additional investigation, remediation, and/or contingency planning. Further, the Company's ability to timely complete its Year 2000 action plan is dependent upon the ability of third party manufacturers and distributors to provide necessary replacement equipment during the remediation stage.

The total amount expended on the Year 2000 action plan through December 31, 1998 is less than \$100,000. Remaining costs related to the Year 2000 action plan are not expected to be material. The Company will continue to utilize internal resources to assist in the implementation of the Year 2000 action plan. The costs expended in 1998 and the costs anticipated to be expended in 1999 do not include the Company's internal costs, as the Company does not track such costs separately. The costs also do not include software upgrades that, while Year 2000 compliant, were not specifically upgraded for the Year 2000 issue. The completion of the Year 2000 action plan is expected to significantly reduce both the level of uncertainty related to the Company's reliance on third parties for Year 2000 compliance and the possibility of significant interruptions of normal business operations. The forward-looking statements contained in this discussion should be read in conjunction with the Company's disclosure in the opening paragraph of this Management's Discussion and Analysis.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk from changes in the interest rates on certain of its outstanding debt and changes in fuel prices. The outstanding loan balance under the Company's revolving credit agreement bears interest at a variable rate based on prevailing short-term interest rates in the United States and Europe. Notes issued under the Company's medium term note program may bear fixed or variable interest rates, although the notes issued to date have all been fixed rate notes. The potential impact on the Company of fuel price increases is limited because most of its term contracts contain escalation clauses under which increases in fuel costs, among others, can be passed on to the customers, while its spot contract rates are set based on prevailing fuel prices. The Company does not presently use financial or commodity derivative instruments to manage its interest or fuel costs. The Company has no foreign exchange risks.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The response to this item is submitted as a separate section of this report (see Item 14, page 59).

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

The Company has had no disagreements with its independent accountants as contemplated in Item 304 of Regulation S-K.

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PART III

ITEMS 10 THROUGH 13.

The information for these items is incorporated by reference to the definitive proxy statement to be filed by the Company with the Commission pursuant to the Regulation 14A within 120 days of the close of the fiscal year ended December 31, 1998, except for the information regarding executive officers which is provided in a separate item caption, "Executive Officers of the Registrant," and is included as an unnumbered item following Item 4 in Part I of this Form 10-K.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Kirby Corporation:

We have audited the accompanying consolidated balance sheets of Kirby Corporation and consolidated subsidiaries as of December 31, 1998 and 1997 and the related consolidated statements of earnings, stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 1998. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion of these consolidated financial statements based on our audits. We did not audit the consolidated financial statements of Universal Insurance Company and its subsidiaries, an equity-owned unconsolidated subsidiary sold effective September 30, 1998 (Note 3). The Company's investment in this company at December 31, 1997 was \$45,320,290, and its equity in earnings for the years ended December 31, 1997 and 1996 was \$4,609,000 and \$2,171,000, respectively. Those financial statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Universal Insurance Company and its subsidiaries, is based solely on the report of the other auditors.

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 and the reports of the other auditors provide a

reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kirby Corporation and consolidated subsidiaries as of December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1998 in conformity with generally accepted accounting principles.

KPMG LLP

Houston, Texas
February 4, 1999

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

BALANCE SHEETS
DECEMBER 31, 1997 AND 1998

ASSETS

| | 1997 | 1998 |
|---|-------------------|-----------|
| | ----- | ----- |
| | (\$ IN THOUSANDS) | |
| Current assets: | | |
| Cash and cash equivalents..... | \$ 2,043 | \$ 861 |
| Available-for-sale securities..... | 21,773 | 20,795 |
| Accounts receivable: | | |
| Trade -- less allowance for doubtful accounts..... | 70,137 | 53,586 |
| Insurance claims and other..... | 14,458 | 16,919 |
| Inventory -- finished goods, at lower of average cost or market..... | 14,875 | 14,181 |
| Prepaid expenses and other..... | 7,359 | 4,829 |
| Deferred income taxes..... | 1,468 | 1,187 |
| Current assets of discontinued operations..... | 3,684 | -- |
| | ----- | ----- |
| Total current assets..... | 135,797 | 112,358 |
| | ----- | ----- |
| Property and equipment, at cost: | | |
| Marine transportation equipment..... | 433,383 | 428,676 |
| Land, buildings and equipment..... | 37,636 | 37,767 |
| | ----- | ----- |
| | 471,019 | 466,443 |
| Accumulated depreciation..... | 198,635 | 209,544 |
| | ----- | ----- |
| | 272,384 | 256,899 |
| | ----- | ----- |
| Investments in affiliates: | | |
| Insurance affiliate..... | 45,320 | -- |
| Marine affiliates..... | 16,256 | 12,795 |
| | ----- | ----- |
| | 61,576 | 12,795 |
| | ----- | ----- |
| Goodwill -- less accumulated amortization of \$2,128,000 (\$2,164,000 in 1997)..... | 6,652 | 5,368 |
| Sundry..... | 4,562 | 2,879 |
| Long-term assets of discontinued operations..... | 36,988 | -- |
| | ----- | ----- |
| | \$517,959 | \$390,299 |
| | ===== | ===== |

LIABILITIES AND STOCKHOLDERS' EQUITY

| | | |
|--|----------|----------|
| Current liabilities: | | |
| Current portion of long-term debt..... | \$ 5,333 | \$ 5,333 |
| Income taxes payable..... | 4,319 | 504 |
| Accounts payable..... | 26,712 | 12,918 |

| | | |
|---|-----------|-----------|
| Accrued liabilities: | | |
| Interest..... | 1,515 | 1,414 |
| Insurance premiums and claims..... | 27,287 | 25,664 |
| Bonus, pension and profit-sharing plans..... | 9,979 | 8,981 |
| Taxes -- other than on income..... | 2,797 | 2,920 |
| Other..... | 12,615 | 4,326 |
| Deferred revenues..... | 5,046 | 3,880 |
| | ----- | ----- |
| Total current liabilities..... | 95,603 | 65,940 |
| | ----- | ----- |
| Long-term debt -- less current portion..... | 149,485 | 137,552 |
| Deferred income taxes..... | 48,409 | 40,045 |
| Other long-term liabilities..... | 6,193 | 5,722 |
| | ----- | ----- |
| | 204,087 | 183,319 |
| | ----- | ----- |
| Contingencies and commitments..... | -- | -- |
| Stockholders' equity: | | |
| Preferred stock, \$1.00 par value per share. Authorized 20,000,000 shares..... | -- | -- |
| Common stock, \$.10 par value per share. Authorized 60,000,000 shares, issued 30,907,000 shares..... | 3,091 | 3,091 |
| Additional paid-in capital..... | 159,016 | 159,122 |
| Accumulated other comprehensive income..... | 572 | 338 |
| Retained earnings..... | 136,945 | 147,054 |
| | ----- | ----- |
| | 299,624 | 309,605 |
| Less cost of 10,137,000 shares in treasury (6,619,000 in 1997)..... | 81,355 | 168,565 |
| | ----- | ----- |
| | 218,269 | 141,040 |
| | ----- | ----- |
| | \$517,959 | \$390,299 |
| | ===== | ===== |

See accompanying notes to financial statements.

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

STATEMENTS OF EARNINGS
FOR THE YEARS ENDED DECEMBER 31, 1996, 1997 AND 1998

| | 1996 | 1997 | 1998 |
|--|--|-----------|-----------|
| | ----- | ----- | ----- |
| | (\$ IN THOUSANDS, EXCEPT PER SHARE AMOUNTS) | | |
| Revenues: | | | |
| Marine transportation..... | \$249,594 | \$256,108 | \$244,839 |
| Diesel repair..... | 70,422 | 79,136 | 82,241 |
| Investment income and other..... | 817 | 883 | 1,658 |
| Gain on disposition of assets..... | 2,751 | 407 | 3,517 |
| | ----- | ----- | ----- |
| | 323,584 | 336,534 | 332,255 |
| | ----- | ----- | ----- |
| Costs and expenses: | | | |
| Costs of sales and operating expenses..... | 206,465 | 218,123 | 212,242 |
| Selling, general and administrative..... | 40,411 | 40,345 | 39,473 |
| Taxes, other than on income..... | 6,992 | 7,796 | 7,646 |
| Depreciation and amortization..... | 28,386 | 28,113 | 27,383 |
| Impairment of long-lived assets..... | -- | -- | 8,333 |
| | ----- | ----- | ----- |
| | 282,254 | 294,377 | 295,077 |
| | ----- | ----- | ----- |
| Operating income..... | 41,330 | 42,157 | 37,178 |
| Equity in earnings of insurance affiliate..... | 2,171 | 4,609 | 1,325 |
| Loss on sale of insurance affiliate..... | -- | -- | (10,536) |
| Equity in earnings of marine affiliates..... | 3,912 | 3,084 | 946 |
| Interest expense..... | (13,349) | (13,378) | (11,898) |
| | ----- | ----- | ----- |

| | | | |
|--|-----------|-----------|-----------|
| Earnings from continuing operations before taxes on income..... | 34,064 | 36,472 | 17,015 |
| Provision for taxes on income: | | | |
| United States..... | 12,856 | 12,842 | 6,906 |
| Puerto Rico..... | -- | 925 | -- |
| | 12,856 | 13,767 | 6,906 |
| Net earnings from continuing operations..... | 21,208 | 22,705 | 10,109 |
| Discontinued operations: | | | |
| Earnings from discontinued operations, net of taxes on income..... | 6,021 | 2,943 | -- |
| Estimated loss on sale of discontinued operations, including provision of \$700,000 for operating losses during the phase-out period, net of taxes on income.... | -- | (3,966) | -- |
| Net earnings (loss) from discontinued operations..... | 6,021 | (1,023) | -- |
| Net earnings..... | \$ 27,229 | \$ 21,682 | \$ 10,109 |
| Net earnings (loss) per share of common stock: | | | |
| Basic: | | | |
| Continuing operations..... | \$.83 | \$.93 | \$.46 |
| Discontinued operations..... | .24 | (.04) | -- |
| Net earnings..... | \$ 1.07 | \$.89 | \$.46 |
| Diluted: | | | |
| Continuing operations..... | \$.82 | \$.92 | \$.46 |
| Discontinued operations..... | .24 | (.04) | -- |
| Net earnings..... | \$ 1.06 | \$.88 | \$.46 |

See accompanying notes to financial statements.

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

STATEMENTS OF STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 1996, 1997 AND 1998

| | 1996 | 1997 | 1998 |
|--|-------------------|-----------|------------|
| | (\$ IN THOUSANDS) | | |
| Common stock: | | | |
| Balance at beginning and end of year..... | \$ 3,091 | \$ 3,091 | \$ 3,091 |
| Additional paid-in capital: | | | |
| Balance at beginning of year..... | \$158,383 | \$158,712 | \$ 159,016 |
| Excess (deficit) of cost of treasury stock sold over proceeds received upon exercise of stock options..... | 148 | (135) | (982) |
| Tax benefit realized from stock option plans..... | 181 | 439 | 1,088 |
| Balance at end of year..... | \$158,712 | \$159,016 | \$ 159,122 |
| Accumulated other comprehensive income: | | | |
| Balance at beginning of year..... | \$ 1,978 | \$ (32) | \$ 572 |
| Unrealized net gain (loss) in value of available-for-sale securities, net of tax..... | (2,010) | 604 | (234) |
| Balance at end of year..... | \$ (32) | \$ 572 | \$ 338 |
| Retained earnings: | | | |
| Balance at beginning of year..... | \$ 88,034 | \$115,263 | \$ 136,945 |
| Net earnings for the year..... | 27,229 | 21,682 | 10,109 |
| Balance at end of year..... | \$115,263 | \$136,945 | \$ 147,054 |
| Treasury stock: | | | |

| | | | |
|--|-------------|-------------|--------------|
| Balance at beginning of year..... | \$ (46,153) | \$ (71,280) | \$ (81,355) |
| Purchase of treasury stock..... | (26,331) | (11,699) | (91,247) |
| Cost of treasury stock sold upon exercise of stock options..... | 1,204 | 1,624 | 4,037 |
| | ----- | ----- | ----- |
| Balance at end of year..... | \$ (71,280) | \$ (81,355) | \$ (168,565) |
| | ===== | ===== | ===== |
| Comprehensive income: | | | |
| Net earnings for year..... | \$ 27,229 | \$ 21,682 | \$ 10,109 |
| Other comprehensive income (loss), net of tax..... | (2,010) | 604 | (234) |
| | ----- | ----- | ----- |
| Total comprehensive income..... | \$ 25,219 | \$ 22,286 | \$ 9,875 |
| | ===== | ===== | ===== |

See accompanying notes to financial statements.

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 1996, 1997 AND 1998

| | 1996 | 1997 | 1998 |
|--|-------------------|-----------|-----------|
| | ----- | ----- | ----- |
| | (\$ IN THOUSANDS) | | |
| Cash flows from operating activities: | | | |
| Net earnings..... | \$ 27,229 | \$ 21,682 | \$ 10,109 |
| Adjustments to reconcile net earnings to net cash provided by continuing operations: | | | |
| Income from discontinued operations..... | (6,021) | (2,943) | -- |
| Estimated loss on sale of discontinued operations..... | -- | 3,966 | -- |
| Depreciation and amortization..... | 28,386 | 28,113 | 27,383 |
| Provision for doubtful accounts..... | 282 | 394 | 133 |
| Provision (credit) for deferred income taxes..... | 795 | 2,790 | (4,967) |
| Gain on disposition of assets..... | (2,751) | (407) | (3,517) |
| Deferred scheduled maintenance costs..... | (446) | 328 | 923 |
| Loss on sale of insurance affiliate..... | -- | -- | 10,536 |
| Equity in earnings of insurance affiliate, net of redemptions..... | (2,171) | (109) | (1,325) |
| Equity in earnings of marine affiliates, net of distributions and contributions..... | (712) | (3,559) | 3,461 |
| Impairment of long-lived assets..... | -- | -- | 8,333 |
| Other..... | 4 | -- | -- |
| Increase (decrease) in cash flows resulting from changes in: | | | |
| Accounts receivable..... | (8,079) | (5,171) | 13,821 |
| Inventory..... | (2,176) | 1,486 | 32 |
| Other assets..... | (7,101) | (2,534) | 3,729 |
| Income taxes payable..... | 3,264 | 731 | (3,815) |
| Accounts payable..... | 6,472 | (3,806) | (13,994) |
| Accrued and other liabilities..... | 7,803 | 7,063 | (13,813) |
| | ----- | ----- | ----- |
| Net cash provided by operating activities of continuing operations..... | 44,778 | 48,024 | 37,029 |
| Net cash provided by (used in) operating activities of discontinued operations..... | 19,290 | 15,476 | (1,583) |
| | ----- | ----- | ----- |
| Net cash provided by operating activities..... | 64,068 | 63,500 | 35,446 |
| | ----- | ----- | ----- |
| Cash flows from investing activities: | | | |
| Proceeds from sale and maturities of investments..... | 6,861 | 1,935 | 1,950 |
| Purchase of investments..... | (9,583) | (5,237) | (789) |
| Capital expenditures..... | (36,413) | (24,506) | (27,445) |
| Purchase of assets of diesel repair company, net of assumed liabilities..... | (14,211) | -- | -- |
| Proceeds from disposition of assets..... | 11,975 | 4,044 | 14,066 |
| Proceeds from disposition of businesses..... | -- | -- | 39,989 |
| Proceeds from sale of insurance affiliate..... | -- | -- | 36,000 |
| Investing activities of discontinued operations..... | (355) | (1,893) | (275) |
| | ----- | ----- | ----- |
| Net cash provided by (used in) investing | | | |

| | | | |
|---|-----------|-----------|-----------|
| activities..... | (41,726) | (25,657) | 63,496 |
| Cash flows from financing activities: | | | |
| Borrowings (payments) on bank revolving credit agreements, net..... | 8,400 | (37,800) | (6,600) |
| Increase in long-term debt..... | -- | 50,000 | -- |
| Payments on long-term debt..... | (5,676) | (39,333) | (5,333) |
| Purchase of treasury stock..... | (26,331) | (11,700) | (91,247) |
| Proceeds from exercise of stock options..... | 1,352 | 1,489 | 3,056 |
| Net cash used in financing activities..... | (22,255) | (37,344) | (100,124) |
| Increase (decrease) in cash and invested cash..... | 87 | 499 | (1,182) |
| Cash and invested cash, beginning of year..... | 1,457 | 1,544 | 2,043 |
| Cash and invested cash, end of year..... | \$ 1,544 | \$ 2,043 | \$ 861 |
| Supplemental disclosures of cash flow information: | | | |
| Cash paid during the year: | | | |
| Interest..... | \$ 12,915 | \$ 12,640 | \$ 11,635 |
| Income taxes..... | \$ 9,569 | \$ 9,762 | \$ 18,998 |
| Noncash investing and financing activity: | | | |
| Assumption of liabilities in connection with purchase of assets of diesel repair company..... | \$ 2,623 | \$ -- | \$ -- |

See accompanying notes to financial statements.

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1996, 1997 AND 1998

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND OPERATIONS

Principles of Consolidation. The consolidated financial statements include the accounts of Kirby Corporation and its subsidiaries ("the Company"). All material intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to reflect current presentation of financial information.

Operations. The Company is currently engaged in two segments as follows:

Marine Transportation -- Marine transportation by U.S. flag vessels on the United States inland waterway system and in United States coastwise trade. The principal products transported include petrochemical feedstocks, processed chemicals, agricultural chemicals, refined petroleum products, coal, limestone, grain and sugar.

Diesel Repair -- Overhaul and repair of large, medium-speed diesel engines, reduction gear repair and sale of related parts and accessories for customers in the marine industry, power generation industry, and the shortline and industrial railroad industry.

Accounting Policies:

Cash Equivalents. Cash equivalents consist of short-term, highly liquid investments with maturities of three months or less at date of purchase.

Available-for-Sale Securities. The Company's wholly-owned captive insurance subsidiary has available-for-sale investments reported at fair value with the net unrealized gain or loss on such investments recorded as a separate component of shareholders' equity, net of deferred tax. Investments are recorded on a trade date basis with balances pending settlement accrued in the balance sheet. Realized gains and losses on sales of investments are determined on the basis of average cost. Investment income is recognized when earned and includes the amortization of premiums or discount on investments.

Accounts Receivable. In the normal course of business, the Company extends credit to its customers. The Company regularly reviews the accounts and makes adequate provisions for potentially uncollectable balances. It is the Company's opinion that the accounts have no impairment, other than that for which provisions have been made. Included in accounts receivable as of December 31,

1997 and 1998 are \$11,440,000 and \$6,129,000, respectively, of accruals for diesel repair work in process which have not been invoiced as of the end of each year.

The Company's marine transportation and diesel repair operations are subject to hazards associated with such businesses. The Company maintains insurance coverage against these hazards with mutual insurance and reinsurance companies. As of December 31, 1997 and 1998, the Company had receivables of \$13,040,000 and \$12,478,000, respectively, from the mutual insurance and reinsurance companies to cover anticipated claims over the Company's deductible.

Depreciation. Property and equipment is depreciated on the straight-line method over the estimated useful lives of the assets as follows: marine transportation equipment, 6-35 years; buildings, 10-25 years; other equipment, 2-10 years; leasehold improvements, term of lease.

Concentrations of Credit Risk. Financial instruments which potentially subject the Company to concentrations of credit risk are primarily trade accounts receivables. The Company's marine transportation customers include the major oil refiners and petrochemical companies. The diesel repair customers are offshore well service companies, inland and offshore marine transportation companies, commercial fishing companies, electric utilities and the United States Government. Credit risk with respect to these trade

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND OPERATIONS -- (CONTINUED)
receivables is generally considered minimal because of the credit history of such companies as well as the Company having procedures in effect to monitor the credit worthiness of customers.

Fair Value of Financial Instruments. Cash, accounts receivable, accounts payable and accrued liabilities approximate fair value due to the short-term maturity of these financial instruments. The fair value of the Company's investments are more fully described in Note 5, Investments, and the fair value of the Company's debt instruments are more fully described in Note 6, Long-Term Debt. The Company does not hold or issue derivative financial instruments.

Property, Maintenance and Repairs. Property is recorded at cost. Improvements and betterments are capitalized as incurred. When property items are retired, sold, or otherwise disposed of, the related cost and accumulated depreciation are removed from the accounts with any gain or loss on the disposition included in income. Routine maintenance and repairs are charged to operating expense as incurred on an annual basis. Scheduled major maintenance on ocean-going vessels is recognized as prepaid maintenance costs when incurred and charged to operating expense over the period between such scheduled maintenance, generally ranging from 23 to 34 months.

Environmental Liabilities. The Company expenses costs related to environmental events as they incur or when a loss is considered probable.

Goodwill. The excess of the purchase price over the fair value of identifiable net assets acquired in transactions accounted for as a purchase are included in goodwill. The goodwill is amortized over the period of the lives of the underlying marine transportation or diesel repair assets acquired in the transaction, which generally approximates 15 years. Management monitors the recoverability of the goodwill on an ongoing basis based on projections of the future cash flows, excluding interest expense, of acquired assets.

Taxes on Income. The Company follows the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The Company files a consolidated federal income tax return with its domestic subsidiaries and its Bermudian subsidiary, Oceanic Insurance Limited ("Oceanic").

Treasury Stock. The Company follows the average cost method of accounting for treasury stock transactions.

Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of. The Company reviews long-lived assets and certain identifiable intangibles for impairment by vessel class. For purposes of determining fair value, the Company estimates future cash flows expected to be generated, assuming the above asset groups, less the future cash outflows expected to be necessary to obtain the inflows.

In September 1998, the Company reduced the carrying value of an offshore liquid tank barge and tug unit by taking an \$8,333,000 pre-tax impairment charge. The after-tax effect of the charge was \$5,416,000 or \$.24 per share. The unit was sold in October 1998 for a price approximating the revised carrying value of the unit. No gain or loss was recognized from the sale of the unit.

In December 1998, a marine partnership in which the Company owns a 50% interest, reduced the carrying value of an offshore dry-cargo barge and tug unit by taking a \$5,900,000 pre-tax impairment charge in

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND OPERATIONS -- (CONTINUED) accordance with SFAS No. 121. The Company's portion of the charge was \$2,950,000 and the after-tax effect of the charge to the Company was \$1,918,000 or \$.09 per share. The Company's portion of the charge is reflected in equity in earnings of marine affiliates on the statement of earnings.

Adoption of New Accounting Standards. As more fully described in Note 9, Stock Option Plans, the Company has five employee stock option plans for selected officers and other key employees, two Director stock option plans for nonemployee Directors of the Company, and a 25,000 share nonqualified stock option granted to Robert G. Stone, Jr., former Chairman of the Board and current Director of the Company. SFAS "Accounting for Stock-Based Compensation" ("SFAS No. 123") provides for a company to either apply a fair value based method of accounting for its stock-based compensation plans, or to continue to follow the intrinsic value method of accounting prescribed by Accounting Principles Board ("APB") Opinion No. 25 "Accounting for Stock Issued to Employees."

The Company follows APB Opinion No. 25; however, under the fair value based method of SFAS No. 123, the Company's net earnings and earnings per share for the years ended December 31, 1996, 1997 and 1998 would have been reduced as follows (in thousands, except per share amounts):

| | 1996 | | 1997 | | 1998 | |
|---|----------------|-----------|----------------|-----------|----------------|-----------|
| | AS REPORTED | PRO FORMA | AS REPORTED | PRO FORMA | AS REPORTED | PRO FORMA |
| Net earnings from continuing operations..... | \$21,208 | \$20,251 | \$22,705 | \$20,527 | \$10,109 | \$7,598 |
| Net earnings per share from continuing operations: | | | | | | |
| Basic..... | \$.83 | \$.79 | \$.93 | \$.84 | \$.46 | \$.35 |
| Diluted..... | \$.82 | \$.79 | \$.92 | \$.83 | \$.46 | \$.34 |
| Net earnings (loss) from discontinued operations..... | \$ 6,021 | \$ 6,021 | \$(1,023) | \$(1,023) | \$ -- | \$ -- |
| Net earnings (loss) per share from discontinued operations: | | | | | | |
| Basic..... | \$.24 | \$.24 | \$ (.04) | \$ (.04) | \$ -- | \$ -- |
| Diluted..... | \$.24 | \$.23 | \$ (.04) | \$ (.04) | \$ -- | \$ -- |
| Net earnings..... | \$27,229 | \$26,272 | \$21,682 | \$19,504 | \$10,109 | \$7,598 |
| Net earnings per share: | | | | | | |
| Basic..... | \$ 1.07 | \$ 1.03 | \$.89 | \$.80 | \$.46 | \$.35 |

Diluted..... \$ 1.06 \$ 1.02 \$.88 \$.79 \$.46 \$.34

The weighted average fair value of options granted during 1996, 1997 and 1998 was \$12.12, \$11.44 and \$15.71, respectively. The fair value of each option was determined using the Black-Scholes option valuation model. The key input variables used in valuing the options were as follows: average risk-free interest rate based on 10-year Treasury bonds -- 6.2% for 1996, 6.6% for 1997 and 5.6% for 1998; stock price volatility -- 48% for 1996, 51% for 1997 and 59% for 1998; and estimated option term -- 9 years. Under the provisions of SFAS No. 123, the pro forma disclosures above include only the effects of stock options granted by the Company subsequent to December 31, 1994. During this initial phase-in period, the pro forma disclosures as required by SFAS No. 123 are not representative of the effects on reported net income for future years as options vest over several years and additional awards are generally made each year.

The FASB issued SFAS No. 130, "Reporting Comprehensive Income" ("SFAS No. 130") in June 1997, which establishes standards for reporting and display of comprehensive income and its components

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND OPERATIONS -- (CONTINUED) in a full set of financial statements. Comprehensive income includes all changes in a company's equity, except those resulting from investments by owners and distributions to owners, including among other things, foreign currency transaction adjustments and unrealized gains and losses on available-for-sale securities. Effective January 1, 1998, the Company adopted SFAS No. 130.

The FASB issued SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information" ("SFAS No. 131"), in June 1997 which establishes standards for reporting information about operating segments in annual financial statements and requires that enterprises report selected information about operating segments in interim reports issued to shareholders. Effective December 31, 1998, the Company adopted SFAS No. 131.

The Company's reportable segments are strategic business units that offer different services. Each segment has a separate management team, as the segments require different technology and marketing strategies. The Company's reportable segments are marine transportation and diesel repair, as set forth under Operations above, and described in Note 14, Segment Data.

The FASB issued SFAS No. 132, "Employees' Disclosures about Pension and Other Postretirement Benefits" ("SFAS No. 132") in February 1998, which revised employer's disclosures about pension and other postretirement benefit plans. SFAS No. 132 did not change the measurement of recognition of those plans. The statement standardized the disclosure requirements for pension and other postretirement benefits to the extent practicable, requiring additional information on changes in the benefit obligations and fair value of plan assets that will facilitate financial analysis and eliminate certain disclosures. Effective December 31, 1998, the Company adopted SFAS No. 132, restating all previously reported benefit plan disclosures to conform with the new disclosure requirements, the effects of which are more fully described in Note 10, Retirement Plans.

(2) DISCONTINUED OPERATIONS

During the 1997 fourth quarter, the Company announced its intention to review alternative strategies concerning certain offshore assets. In this regard, the Company entered into a definitive purchase agreement, dated January 28, 1998, to sell its U.S. flag offshore product tanker operation and its harbor service operation. In accordance with the purchase agreement, on March 16, 1998, Hvide Marine Incorporated acquired the Company's harbor service operation and two tankers, and August Trading, Inc. acquired five tankers, for a combined purchase price of \$38,600,000 in cash, subject to certain adjustments. The U.S. flag offshore product tankers transported refined products from the U.S. Gulf Coast to Florida and the East Coast, with occasional voyages to the U.S. West Coast. The Company's harbor service operation primarily provided towing, docking and shifting services for vessels calling at the ports of Beaumont, Port Arthur and Orange, Texas and the port of Lake Charles, Louisiana.

The offshore tanker and harbor service operations' financial results were accounted for as discontinued operations as of December 31, 1997, and previously reported financial statements were restated to reflect the discontinuation of the operations. The Company recorded a financial net loss of \$3,966,000 as of December 31, 1997 for the sale of the tanker and harbor service operations.

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(2) DISCONTINUED OPERATIONS -- (CONTINUED)

A summary of the financial position of the discontinued operations as of December 31, 1997 included in the accompanying balance sheets follows (in thousands):

| | 1997 |
|----------------------------------|----------|
| | ----- |
| ASSETS | |
| Current assets..... | \$11,742 |
| Property and equipment, net..... | 36,481 |
| Sundry..... | 813 |
| | ----- |
| | \$49,036 |
| | ===== |
| LIABILITIES | |
| Current liabilities..... | \$ 8,449 |
| Deferred taxes..... | 1,299 |
| Other long-term liabilities..... | 1,379 |
| | ----- |
| | \$11,127 |
| | ===== |

A summary of the results of the discontinued operations included in the accompanying statements of earnings for the years ended December 31, 1996 and 1997 follows (in thousands):

| | 1996 | 1997 |
|--|----------|----------|
| | ----- | ----- |
| Revenues: | | |
| Marine transportation..... | \$66,773 | \$66,434 |
| Loss on disposition of assets..... | (81) | -- |
| Other..... | 362 | 166 |
| | ----- | ----- |
| | 67,054 | 66,600 |
| | ----- | ----- |
| Costs and expenses: | | |
| Costs of sales and operating expenses..... | 46,023 | 49,819 |
| Selling, general and administrative..... | 5,008 | 5,236 |
| Taxes, other than income..... | 250 | 322 |
| Depreciation and amortization..... | 6,419 | 6,625 |
| | ----- | ----- |
| | 57,700 | 62,002 |
| | ----- | ----- |
| Operating income..... | 9,354 | 4,598 |
| Interest expense..... | -- | -- |
| | ----- | ----- |
| Earnings before taxes on income..... | 9,354 | 4,598 |
| Provision for taxes on income..... | (3,333) | (1,655) |
| | ----- | ----- |
| Net earnings..... | \$ 6,021 | \$ 2,943 |
| | ===== | ===== |

Estimated loss on sale of discontinued operations, including provision for net operating losses of \$700,000 during the

| | | | |
|--|-------|----|-----------|
| phase-out period (less applicable income tax benefit of \$2,135,000)..... | \$ | -- | \$(3,966) |
| | ===== | | ===== |

(3) SALE OF REMAINING INTEREST IN UNIVERSAL INSURANCE COMPANY

Effective September 30, 1998, the Company sold its remaining 45% voting common stock interest and its non-voting preferred stock interest in Universal Insurance Company ("Universal") for \$36,000,000 in cash. Universal, a property and casualty insurance company in the Commonwealth of Puerto Rico, was formed by the Company in 1972. In September 1992, the Company merged Universal with Eastern America Insurance

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(3) SALE OF REMAINING INTEREST IN UNIVERSAL INSURANCE COMPANY -- (CONTINUED)

Company ("Eastern America"), a subsidiary of Eastern America Insurance Group, Inc. ("Eastern America Group"). In accordance with a shareholders agreement among the Company, Universal and Eastern America Group, through redemption rights, Universal had the obligation to purchase the Company's entire interest in Universal gradually, over a 15 year period. The Company closed the sale on October 7, 1998 and the cash proceeds were used to reduce the Company's revolving line of credit.

Under an anticipated redemption schedule, the Company would have received a stream of cash payments between now and the year 2008 totaling \$62,000,000. The \$36,000,000 received represented the present value of the payment stream. Including prior redemptions and the final sale, the Company received total payments of \$58,000,000 for its interest in Universal.

The Company recognized, during the 1998 third quarter, a pre-tax loss for financial purposes of \$10,536,000 on the Universal transaction. The Company's investment in Universal, accounted for under the equity method of accounting, was based on the estimated receipt of \$62,000,000 of redemption payments to the Company over the next eleven years, and the recording of the remaining built-in gain on the sale.

(4) ACQUISITION

On July 31, 1996, a subsidiary of the Company purchased the operating assets of MKW Power Systems, Inc., a subsidiary of Wartsila Diesel, N.A. ("MKW"), for approximately \$5,700,000 in cash plus approximately \$8,500,000 for MKW's working capital. The acquisition expanded the diesel repair segment's relationship with the Electro-Motive Division of General Motors ("EMD") to an authorized distributorship for 17 eastern states and the Caribbean. Funding for the transaction was provided through the Company's bank revolving credit agreement. Operations of the assets acquired from MKW were included as part of the Company's operations effective July 31, 1996, in accordance with the purchase method of accounting.

(5) INVESTMENTS

The Company's wholly-owned captive insurance subsidiary accounts for investments in debt and equity securities in accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities" ("SFAS No. 115"), which establishes certain criteria for the accounting and reporting of investments in debt and equity securities that have readily determinable fair values. Investments in debt and equity securities as of December 31, 1997 and 1998 qualify as available-for-sale securities in accordance with SFAS No. 115. Realized gains and losses on the sale of the securities in the statements of earnings are computed by using the specific cost of the security when originally purchased and include net unrealized holding gains and losses as a separate component of accumulated other comprehensive income and in the reconciliation of comprehensive income included in the statement of stockholders' equity, net of tax liability (benefit) of \$(17,000), \$308,000 and \$182,000 at December 31, 1996, 1997 and 1998, respectively.

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(5) INVESTMENTS -- (CONTINUED)

A summary of the investments as of December 31, 1997 and 1998 is as follows (in thousands):

| TYPE OF INVESTMENT | AMORTIZED COST | GROSS UNREALIZED LOSSES | GROSS UNREALIZED GAINS | FAIR VALUE AS SHOWN IN THE BALANCE SHEET |
|--|----------------|-------------------------|------------------------|--|
| December 31, 1997: | | | | |
| Short-term investments..... | \$ 367 | \$ -- | \$ -- | \$ 367 |
| Bonds and notes: | | | | |
| United States corporate bonds..... | 5,439 | (40) | 60 | 5,459 |
| United States Government bonds and issues..... | 6,078 | -- | 173 | 6,251 |
| Mortgage backed securities..... | 5,978 | -- | 59 | 6,037 |
| Foreign corporate securities..... | 3,489 | -- | 170 | 3,659 |
| | ----- | ----- | ----- | ----- |
| | \$21,351 | \$ (40) | \$462 | \$21,773 |
| | ===== | ===== | ===== | ===== |
| December 31, 1998: | | | | |
| Short-term investments..... | \$ 347 | \$ -- | \$ -- | \$ 347 |
| Bonds and notes: | | | | |
| United States corporate bonds..... | 4,652 | (110) | 263 | 4,805 |
| United States Government bonds and issues..... | 5,191 | (2) | 227 | 5,416 |
| Foreign government bonds..... | 1,382 | -- | 24 | 1,406 |
| Mortgage backed securities..... | 7,652 | (3) | 96 | 7,745 |
| Foreign corporate securities..... | 1,057 | (7) | 26 | 1,076 |
| | ----- | ----- | ----- | ----- |
| | \$20,281 | \$ (122) | \$636 | \$20,795 |
| | ===== | ===== | ===== | ===== |

A summary of the available-for-sale securities by maturities as of December 31, 1997 and 1998 is as follows (in thousands):

| | 1997 | | 1998 | |
|-----------------------------|----------------|--------------|----------------|--------------|
| | AMORTIZED COST | MARKET VALUE | AMORTIZED COST | MARKET VALUE |
| Investment maturing within: | | | | |
| One to five years..... | \$ 5,464 | \$ 5,485 | \$ 2,994 | \$ 3,035 |
| Five to ten years..... | 5,079 | 5,292 | 8,451 | 8,839 |
| Greater than ten years..... | 10,808 | 10,996 | 8,836 | 8,921 |
| | ----- | ----- | ----- | ----- |
| | \$21,351 | \$21,773 | \$20,281 | \$20,795 |
| | ===== | ===== | ===== | ===== |

(6) LONG-TERM DEBT

Long-term debt at December 31, 1997 and 1998 consisted of the following (in thousands):

| | 1997 | 1998 |
|---|-----------|-----------|
| Long-term debt, including current portion: | | |
| Revolving credit loans due September 19, 2002..... | \$ 32,600 | \$ 26,000 |
| Medium term notes due June 1, 2000..... | 45,000 | 45,000 |
| Medium term notes due January 29, 2002..... | 50,000 | 50,000 |
| 8.22% senior notes, \$5,000,000 due annually through June 30, 2002..... | 25,000 | 20,000 |
| Other long-term debt..... | 2,218 | 1,885 |
| | ----- | ----- |
| | \$154,818 | \$142,885 |

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(6) LONG-TERM DEBT -- (CONTINUED)

The aggregate payments due on the long-term debt in each of the next five years are as follows (in thousands):

| | |
|-----------------|-----------|
| 1999..... | \$ 5,333 |
| 2000..... | 50,333 |
| 2001..... | 5,333 |
| 2002..... | 81,333 |
| 2003..... | 333 |
| Thereafter..... | 220 |
| | ----- |
| | \$142,885 |
| | ===== |

The Company has a \$100,000,000 revolving credit agreement (the "Credit Agreement") with Chase Bank of Texas, N.A. ("Chase") as agent bank. On September 19, 1997 the Company agreed to new terms with Chase regarding the Credit Agreement, superseding the previous Credit Agreement dated March 18, 1996. Under the new term, the maturity date was extended to September 19, 2002 from December 31, 1998. The new Credit Agreement reduced the margin of interest paid on its borrowings, provided adjusted interest rates based on the Company's senior credit rating and eliminated certain financial covenants. The new Credit Agreement also contains usual and customary events of default. The Credit Agreement was amended effective January 30, 1998, to provide a one-time allowance for the disposition of assets at the subsidiary level. The amendment also modified the minimum net worth covenant and fixed charge calculation. The Credit Agreement was also amended effective November 30, 1998 to modify the minimum net worth covenant to allow for anticipated activity under the Company's stock repurchase program. The Company was in compliance with all covenants as of December 31, 1998. Proceeds under the Credit Agreement may be used for general corporate purposes, the purchase of existing or new equipment, the purchase of the Company's common stock, or for possible business acquisitions. At December 31, 1998, the amount outstanding under the Credit Agreement totaled \$26,000,000 and the average interest rate was 6.14%. The average borrowing under the Credit Agreement during 1998 was \$46,570,000, computed by using the daily balance, and the weighted average interest rate was 6.18% computed by dividing the interest expense under the Credit Agreement by the average Credit Agreement borrowings. The maximum Credit Agreement borrowings outstanding at any month end during 1998 totaled \$62,800,000. At December 31, 1998, the Company had \$74,000,000 available for takedown under the Credit Agreement.

The Company has on file a shelf registration on Form S-3 with the Securities and Exchange Commission providing for the issue of up to \$250,000,000 of medium term notes ("Medium Term Notes") at fixed or floating interest rates with maturities of nine months or longer. Activities under the Medium Term Notes program have been as follows (in thousands):

| | OUTSTANDING BALANCE | INTEREST RATE | AVAILABLE BALANCE |
|--|------------------------|------------------|----------------------|
| | ----- | ----- | ----- |
| Medium Term Notes program..... | \$ -- | | \$250,000 |
| Issuance March 1995 (Maturity March 10, 1997)..... | 34,000 | 7.77% | 216,000 |
| Issuance June 1995 (Maturity June 1, 2000)..... | 45,000 | 7.25% | 171,000 |
| | ----- | | |
| Outstanding December 31, 1995 and 1996..... | 79,000 | | 171,000 |
| Issuance January 1997 (Maturity January 29, 2002)..... | 50,000 | 7.05% | 121,000 |
| Payment March 1997..... | (34,000) | | 121,000 |
| | ----- | | |
| Outstanding December 31, 1997 and 1998..... | \$ 95,000 | | \$121,000 |

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(6) LONG-TERM DEBT -- (CONTINUED)

Proceeds from the issuance of Medium Term Notes have been used to retire certain bank credit agreements, reduce the Company's Credit Agreement and retire the \$34,000,000 of Medium Term Notes due March 10, 1997. The \$121,000,000 available balance as of December 31, 1998 may be used for future business and equipment acquisitions, working capital requirements and reductions of the Company's Credit Agreement.

In August 1992, the Company's principal marine transportation subsidiary entered into a \$50,000,000 private placement of 8.22% senior notes due June 30, 2002. Principal payments of \$5,000,000, plus interest, are due annually through June 30, 2002. At December 31, 1998, \$20,000,000 was outstanding under the senior notes.

The Company is of the opinion that the amounts included in the consolidated financial statements for outstanding debt materially represent the fair value of such debt at December 31, 1997 and 1998.

(7) TAXES ON INCOME

Earnings from continuing operations before taxes on income and details of the provision for taxes on income from continuing operations for United States and Puerto Rico operations for the years ended December 31, 1996, 1997 and 1998 are as follows (in thousands):

| | 1996 | 1997 | 1998 |
|---|----------|----------|----------|
| | ----- | ----- | ----- |
| Earnings before taxes on income: | | | |
| United States..... | \$31,893 | \$31,863 | \$15,690 |
| Puerto Rico..... | 2,171 | 4,609 | 1,325 |
| | ----- | ----- | ----- |
| | \$34,064 | \$36,472 | \$17,015 |
| | ===== | ===== | ===== |
| Provision (credit) for taxes on income: | | | |
| United States: | | | |
| Current..... | \$11,586 | \$ 9,265 | \$11,016 |
| Deferred..... | 385 | 2,741 | (5,017) |
| State and local..... | 885 | 836 | 907 |
| | ----- | ----- | ----- |
| | 12,856 | 12,842 | 6,906 |
| Puerto Rico..... | -- | 925 | -- |
| | ----- | ----- | ----- |
| | \$12,856 | \$13,767 | \$ 6,906 |
| | ===== | ===== | ===== |

Earnings from discontinued operations before taxes on income and details of the provision for taxes on income from United States discontinued operations for the years ended December 31, 1996 and 1997 are as follows (in thousands):

| | 1996 | 1997 |
|--------------------------------------|---------|---------|
| | ----- | ----- |
| Earnings before taxes on income..... | \$9,354 | \$4,598 |
| | ===== | ===== |
| Provision for taxes on income: | | |
| Current..... | \$ 710 | \$ 977 |
| Deferred..... | 2,586 | 661 |
| State and local..... | 37 | 17 |
| | ----- | ----- |

\$3,333 \$1,655
 ===== =====

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(7) TAXES ON INCOME -- (CONTINUED)

During the three years ended December 31, 1996, 1997 and 1998, tax benefits related to the exercise of stock options that were allocated directly to additional paid-in capital totaled \$181,000, \$439,000 and \$1,088,000, respectively.

The Company's provision for taxes on income varied from the statutory federal income tax rate for the years ended December 31, 1996, 1997 and 1998 due to the following:

| | 1996 | 1997 | 1998 |
|--|-------|-------|-------|
| | ---- | ---- | ---- |
| United States income tax statutory rate..... | 35.0% | 35.0% | 35.0% |
| Puerto Rico taxes..... | -- | 2.3 | -- |
| State and local taxes..... | 2.1 | 2.1 | 5.3 |
| Foreign tax credit..... | -- | (2.5) | -- |
| Other..... | .2 | .7 | .3 |
| | ---- | ---- | ---- |
| | 37.3% | 37.6% | 40.6% |
| | ===== | ===== | ===== |

The tax effects of temporary differences that give rise to significant portions of the current deferred tax assets and non-current deferred tax assets and liabilities at December 31, 1996, 1997 and 1998 are as follows (in thousands):

| | 1996 | 1997 | 1998 |
|---|-------------|-------------|-------------|
| | ----- | ----- | ----- |
| Current deferred tax assets: | | | |
| Compensated absences..... | \$ 772 | \$ 814 | \$ 659 |
| Allowance for doubtful accounts..... | 258 | 290 | 356 |
| Other..... | (430) | 364 | 172 |
| | ----- | ----- | ----- |
| | \$ 600 | \$ 1,468 | \$ 1,187 |
| | ===== | ===== | ===== |
| Non-current deferred tax assets and liabilities: | | | |
| Deferred tax assets: | | | |
| Alternative minimum tax credit carryforwards..... | \$ 11,383 | \$ 12,561 | \$ -- |
| Postretirement health care benefits..... | 2,054 | 2,252 | 1,962 |
| Marine insurance claims reserves..... | 628 | 839 | 764 |
| Other..... | 965 | 2,816 | 1,723 |
| | ----- | ----- | ----- |
| | 15,030 | 18,468 | 4,449 |
| | ----- | ----- | ----- |
| Deferred tax liabilities: | | | |
| Property..... | (40,632) | (46,643) | (43,703) |
| Undistributed earnings from foreign subsidiaries..... | (15,896) | (16,145) | -- |
| Deferred state taxes..... | (657) | (707) | (757) |
| Scheduled vessel maintenance costs..... | (3,746) | (3,382) | (34) |
| | ----- | ----- | ----- |
| | (60,931) | (66,877) | (44,494) |
| | ----- | ----- | ----- |
| | \$ (45,901) | \$ (48,409) | \$ (40,045) |
| | ===== | ===== | ===== |

The Company has determined that it is more likely than not that the deferred tax assets will be realized and a valuation allowance for such assets

is not required.

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(8) LEASES

The Company and its subsidiaries currently lease various facilities and equipment under a number of cancelable and noncancelable operating leases. Total rental expense for the years ended December 31, 1996, 1997 and 1998 follows (in thousands):

| | 1996 | 1997 | 1998 |
|------------------------------------|---------|---------|---------|
| | ----- | ----- | ----- |
| Rental expense: | | | |
| Marine equipment..... | \$1,803 | \$1,803 | \$1,803 |
| Other buildings and equipment..... | 1,050 | 1,398 | 1,423 |
| Sublease rental..... | (10) | (10) | (10) |
| | ----- | ----- | ----- |
| Net rental expense..... | \$2,843 | \$3,191 | \$3,216 |
| | ===== | ===== | ===== |

Rental commitments under noncancelable leases are as follows (in thousands):

| | LAND, BUILDINGS AND EQUIPMENT |
|-----------------|-------------------------------------|
| | ----- |
| 1999..... | \$3,088 |
| 2000..... | 1,200 |
| 2001..... | 741 |
| 2002..... | 571 |
| 2003..... | 420 |
| Thereafter..... | 484 |
| | ----- |
| | \$6,504 |
| | ===== |

(9) STOCK OPTION PLANS

The Company has five employee stock option plans which were adopted in 1976, 1982, 1989, 1994 and 1996 for selected officers and other key employees. The 1976 Employee Plan, as amended, provided for the issuance until 1986 of incentive and non-qualified stock options to purchase up to 1,000,000 shares of common stock. The 1982 Employee Plan provided for the issuance until 1992 of incentive and non-qualified stock options to purchase up to 600,000 shares of common stock. The 1989 Employee Plan provides for the issuance of incentive and nonincentive stock options to purchase up to 600,000 shares of common stock. The 1994 Employee Plan provides for the issuance of incentive and non-qualified stock options to purchase up to 1,000,000 shares of common stock. The 1996 Employee Plan provides for the issuance of incentive and non-qualified stock options to purchase up to 900,000 shares of common stock. The 1976, 1982 and 1989 stock option plans authorize the granting of limited stock appreciation rights.

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(9) STOCK OPTION PLANS -- (CONTINUED)

Changes in options outstanding under the employee plans described above for the years ended December 31, 1996, 1997 and 1998 are summarized as follows:

| | NON-QUALIFIED OR NONINCENTIVE STOCK OPTIONS | | OPTION PRICE RANGE PER SHARE |
|------------------------------------|---|-------------|---------------------------------|
| | OUTSTANDING | EXERCISABLE | |
| Outstanding December 31, 1995..... | 1,211,400 | 643,500 | \$ 3.69-\$21.38 |
| Granted..... | 961,000 | -- | \$16.44-\$19.50 |
| Became exercisable..... | -- | 247,162 | \$12.94-\$21.38 |
| Exercised..... | (90,500) | (90,500) | \$ 6.56-\$18.31 |
| Canceled or expired..... | (58,500) | (30,000) | \$12.94-\$18.31 |
| Outstanding December 31, 1996..... | 2,023,400 | 770,162 | \$ 3.69-\$21.38 |
| Granted..... | 42,500 | -- | \$18.56 |
| Became exercisable..... | -- | 161,163 | \$12.94-\$21.38 |
| Exercised..... | (133,550) | (133,550) | \$ 3.69-\$18.31 |
| Canceled or expired..... | (15,000) | (3,000) | \$16.31-\$18.56 |
| Outstanding December 31, 1997..... | 1,917,350 | 794,775 | \$ 3.69-\$21.38 |
| Granted..... | 18,000 | -- | \$19.88 |
| Became exercisable..... | -- | 108,537 | \$16.31-\$21.38 |
| Exercised..... | (288,300) | (288,300) | \$ 3.69-\$21.38 |
| Canceled or expired..... | (96,100) | (1,050) | \$16.31-\$19.50 |
| Outstanding December 31, 1998..... | 1,550,950 | 613,962 | \$ 6.56-\$21.38 |

At December 31, 1998, 778,914 shares were available for future grants under the employee plans and 125,500 shares of the outstanding stock options under the employee plans were issued with limited stock appreciation rights.

The Company has two Director stock option plans, which were adopted in 1989 and 1994 for nonemployee Directors of the Company. The 1989 Director Plan provides for the issuance of nonincentive options to Directors of the Company to purchase up to 150,000 shares of common stock. The 1994 Director Plan provides for the issuance on non-qualified options to Directors of the Company, including Advisory Directors, to purchase up to 100,000 shares of common stock. The Director plans are intended as an incentive to attract and retain qualified, independent directors.

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(9) STOCK OPTION PLANS -- (CONTINUED)

Changes in options outstanding under the Director plans described above for the years ended December 31, 1996, 1997 and 1998 are summarized as follows:

| | NON-QUALIFIED OR NONINCENTIVE STOCK OPTIONS | | OPTION PRICE RANGE PER SHARE |
|------------------------------------|---|-------------|---------------------------------|
| | OUTSTANDING | EXERCISABLE | |
| Outstanding December 31, 1995..... | 91,500 | 91,500 | \$ 7.56-\$21.38 |
| Granted..... | 20,500 | -- | \$16.63-\$17.94 |
| Became exercisable..... | -- | 20,500 | \$16.63-\$17.94 |
| Exercised..... | (20,000) | (20,000) | \$7.56 |
| Outstanding December 31, 1996..... | 92,000 | 92,000 | \$ 7.56-\$21.38 |
| Granted..... | 10,500 | -- | \$17.06 |
| Became exercisable..... | -- | 10,500 | \$17.06 |
| Exercised..... | (1,500) | (1,500) | \$16.69 |

| | | | |
|------------------------------------|---------|---------|-----------------|
| Canceled or expired..... | (7,500) | (7,500) | \$16.69-\$21.38 |
| ----- | ----- | ----- | ----- |
| Outstanding December 31, 1997..... | 93,500 | 93,500 | \$ 7.56-\$21.38 |
| Granted..... | 17,000 | -- | \$19.88-\$25.50 |
| Became exercisable..... | -- | 17,000 | \$19.88-\$25.50 |
| ----- | ----- | ----- | ----- |
| Outstanding December 31, 1998..... | 110,500 | 110,500 | \$ 7.56-\$25.50 |
| ===== | ===== | ===== | ===== |

The Company has a 1993 nonqualified stock option for 25,000 shares granted to Robert G. Stone, Jr. at an exercise price of \$18.625, all of which are currently exercisable. The grant serves as an incentive to retain the optionee as a member of the Board of Directors of the Company.

(10) RETIREMENT PLANS

The marine transportation subsidiaries sponsor defined benefit plans for certain ocean-going personnel. The plan benefits are based on an employee's years of service. The plans' assets primarily consist of fixed income securities and corporate stocks. Funding of the plans is based on actuarial computations that are designed to satisfy minimum funding requirements of applicable regulations and to achieve adequate funding of projected benefit obligations.

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(10) RETIREMENT PLANS -- (CONTINUED)

The following table presents the funded status and amounts recognized in the Company's consolidated balance sheet for the Company's defined benefit plans (in thousands):

| | 1997 | 1998 |
|---|----------|------------|
| | ----- | ----- |
| CHANGE IN BENEFIT OBLIGATION | | |
| Benefit obligation at beginning of year..... | \$15,941 | \$17,609 |
| Service cost..... | 1,257 | 1,143 |
| Interest cost..... | 1,205 | 1,402 |
| Amendments..... | -- | 735 |
| Actuarial (gain) loss..... | (289) | 1,581 |
| Curtailement loss..... | -- | 178 |
| Benefits paid..... | (505) | (720) |
| ----- | ----- | ----- |
| Benefit obligation at end of year..... | 17,609 | 21,928 |
| ----- | ----- | ----- |
| CHANGE IN PLAN ASSETS | | |
| Fair value of plan assets at beginning of year..... | 15,243 | 18,551 |
| Actual return on plan assets..... | 3,240 | 2,671 |
| Employer contribution..... | 573 | 382 |
| Benefits paid..... | (505) | (720) |
| ----- | ----- | ----- |
| Fair value of plan assets at end of year..... | 18,551 | 20,884 |
| ----- | ----- | ----- |
| Funded status..... | 942 | (1,044) |
| Unrecognized net actuarial gain..... | (2,526) | (1,699) |
| Unrecognized prior service cost..... | 992 | 1,446 |
| Unrecognized net transition obligation..... | 74 | 57 |
| ----- | ----- | ----- |
| Accrued pension liability..... | \$ (518) | \$ (1,240) |
| ===== | ===== | ===== |

The components of pension expense are as follows (in thousands):

| 1996 | 1997 | 1998 |
|-------|-------|-------|
| ----- | ----- | ----- |

| | | | |
|--|----------|----------|----------|
| Service cost..... | \$ 1,357 | \$ 1,257 | \$ 1,143 |
| Interest cost..... | 1,090 | 1,205 | 1,402 |
| Expected return on assets..... | (1,150) | (1,406) | (1,691) |
| Amortization of transition obligation..... | 17 | 17 | 17 |
| Amortization of prior service cost..... | 192 | 192 | 258 |
| Amortization of actuarial gain..... | -- | (12) | (47) |
| Less partnerships' allocation..... | (32) | (22) | (85) |
| Curtailement charge..... | -- | -- | 22 |
| | ----- | ----- | ----- |
| Net pension expense..... | \$ 1,474 | \$ 1,231 | \$ 1,019 |
| | ===== | ===== | ===== |

The Company sponsors defined contribution plans for all shore-based employees and certain ocean-going personnel. Maximum contributions to these plans equal the lesser of 15% of the aggregate compensation paid to all participating employees, or up to 20% of each subsidiary's earnings before federal income tax after certain adjustments for each fiscal year. The aggregate contributions to the plans were approximately \$3,871,000, \$3,929,000 and \$3,836,000 in 1996, 1997 and 1998, respectively.

In addition to the Company's defined benefit pension plans, the Company sponsors an unfunded defined benefit health care plan that provides limited postretirement medical benefits to employees, who meet

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(10) RETIREMENT PLANS -- (CONTINUED)

minimum age and service requirements, and eligible dependents. The plan is contributory, with retiree contributions adjusted annually.

In connection with the Company's sale of its discontinued operations, the Company recognized the reversal of previously accrued health care plan benefits for non-vested active employees. The effect of the reversal was used to reduce an insignificant unrecognized prior service cost obligation, with the remaining amount of approximately \$1,100,000 included as a reduction of the estimated loss from the sale of the discontinued operations.

The following table presents the unfunded defined benefit health care plan's funded status and amounts recognized in the Company's consolidated balance sheet (in thousands):

| | 1997 | 1998 |
|---|----------|----------|
| | ----- | ----- |
| CHANGE IN BENEFIT OBLIGATION | | |
| Benefit obligation at beginning of year..... | \$ 6,181 | \$ 5,609 |
| Service cost..... | 364 | 317 |
| Interest cost..... | 478 | 415 |
| Actuarial loss (gain)..... | 50 | (81) |
| Curtailement (gain) loss..... | (1,110) | 233 |
| Benefits paid..... | (330) | (619) |
| Less partnerships' allocation..... | (24) | (19) |
| | ----- | ----- |
| Benefit obligation at end of year..... | 5,609 | 5,855 |
| | ----- | ----- |
| CHANGE IN PLAN ASSETS | | |
| Fair value of plan assets at beginning of year..... | -- | -- |
| Employer contribution..... | 330 | 619 |
| Benefits paid..... | (330) | (619) |
| | ----- | ----- |
| Fair value of plan assets at end of year..... | -- | -- |
| | ----- | ----- |
| Funded status..... | (5,609) | (5,855) |
| Unrecognized net actuarial loss..... | 277 | 196 |
| Unrecognized prior service cost..... | 85 | 72 |
| | ----- | ----- |

| | | |
|--|----------|----------|
| Accrued postretirement benefit cost..... | \$ 5,247 | \$ 5,587 |
| | ===== | ===== |

The components of postretirement benefit expense are as follows (in thousands):

| | 1996 | 1997 | 1998 |
|---|-------|-------|-------|
| | ---- | ---- | ---- |
| Service cost..... | \$381 | \$364 | \$317 |
| Interest cost..... | 434 | 478 | 415 |
| Amortization of prior service cost..... | 8 | 8 | 5 |
| Less partnerships' allocation..... | (21) | (22) | (20) |
| | ---- | ---- | ---- |
| Postretirement benefit expense..... | \$802 | \$828 | \$717 |
| | ===== | ===== | ===== |

The Company's unfunded defined benefit health care plan, which provides limited postretirement medical benefits, limits cost increases in the Company's contribution to 4% per year. For measurement purposes, a 4% annual rate of increase in the per capita cost of covered benefits (i.e., health care cost trend rate) was assumed for future periods. Accordingly, a 1% increase in the health care cost trend rate assumption would have no effect on the amounts reported.

The discount rate used in determining the accumulated postretirement benefit obligation was 6.75% at December 31, 1998 and 7.25% at December 31, 1997 and 1996.

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(11) EARNINGS PER SHARE OF COMMON STOCK

The following table presents basic and diluted earnings (loss) per share calculations for the years ended December 31, 1996, 1997 and 1998 (in thousands, except earnings per share):

| | INCOME (LOSS) (NUMERATOR) | SHARES (DENOMINATOR) | EARNINGS (LOSS) PER SHARE |
|--|------------------------------|-------------------------|------------------------------|
| | ----- | ----- | ----- |
| For the year ended December 31, 1996: | | | |
| Basic earnings per share: | | | |
| Continuing operations..... | \$21,208 | 25,555 | \$.83 |
| Discontinued operations..... | 6,021 | 25,555 | .24 |
| | ----- | ----- | ----- |
| | \$27,229 | 25,555 | \$1.07 |
| | ===== | ===== | ===== |
| Effect of dilutive securities: | | | |
| Employee and director common stock options.... | | 226 | |
| Diluted earnings per share: | | | |
| Continuing operations..... | \$21,208 | 25,781 | \$.82 |
| Discontinued operations..... | 6,021 | 25,781 | .24 |
| | ----- | ----- | ----- |
| | \$27,229 | 25,781 | \$1.06 |
| | ===== | ===== | ===== |
| For the year ended December 31, 1997: | | | |
| Basic earnings (loss) per share: | | | |
| Continuing operations..... | \$22,705 | 24,381 | \$.93 |
| Discontinued operations..... | (1,023) | 24,381 | (.04) |
| | ----- | ----- | ----- |
| | \$21,682 | 24,381 | \$.89 |
| | ===== | ===== | ===== |
| Effect of dilutive securities: | | | |
| Employee and director common stock options.... | | 213 | |

| | | | |
|--|----------|--------|--------|
| Diluted earnings (loss) per share: | | | |
| Continuing operations..... | \$22,705 | 24,594 | \$.92 |
| Discontinued operations..... | (1,023) | 24,594 | (.04) |
| | ----- | ----- | ----- |
| | \$21,682 | 24,594 | \$.88 |
| | ===== | ===== | ===== |
| For the year ended December 31, 1998: | | | |
| Basic earnings per share: | | | |
| Net earnings..... | \$10,109 | 21,847 | \$.46 |
| | ===== | ===== | ===== |
| Effect of dilutive securities: | | | |
| Employee and director common stock options.... | | 266 | |
| Diluted earnings per share: | | | |
| Net earnings..... | \$10,109 | 22,113 | \$.46 |
| | ===== | ===== | ===== |

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(12) QUARTERLY RESULTS (UNAUDITED)

The unaudited quarterly results for the year ended December 31, 1997 are as follows (in thousands, except per share amounts):

| | THREE MONTHS ENDED | | | |
|---|--------------------|------------------|-----------------------|----------------------|
| | MARCH 31, 1997 | JUNE 30, 1997 | SEPTEMBER 30, 1997 | DECEMBER 31, 1997 |
| | ----- | ----- | ----- | ----- |
| Revenues..... | \$80,264 | \$88,968 | \$84,219 | \$83,083 |
| Costs and expenses..... | 73,752 | 76,743 | 72,783 | 71,099 |
| | ----- | ----- | ----- | ----- |
| Operating income..... | 6,512 | 12,225 | 11,436 | 11,984 |
| Equity in earnings of insurance affiliate..... | 401 | 2,911 | 422 | 875 |
| Equity in earnings of marine affiliates..... | 863 | 531 | 778 | 912 |
| Interest expense..... | (3,374) | (3,450) | (3,293) | (3,261) |
| | ----- | ----- | ----- | ----- |
| Earnings from continuing operations before taxes on income..... | 4,402 | 12,217 | 9,343 | 10,510 |
| Provision for taxes on income..... | (1,780) | (4,526) | (3,470) | (3,991) |
| | ----- | ----- | ----- | ----- |
| Earnings from continuing operations..... | 2,622 | 7,691 | 5,873 | 6,519 |
| Earnings (loss) for discontinued operations, net of taxes on income..... | 2,117 | 414 | 76 | (3,630) |
| | ----- | ----- | ----- | ----- |
| Net earnings..... | \$ 4,739 | \$ 8,105 | \$ 5,949 | \$ 2,889 |
| | ===== | ===== | ===== | ===== |
| Net earnings (loss) per share of common stock: | | | | |
| Basic earnings (loss) per share: | | | | |
| Continuing operations..... | \$.11 | \$.31 | \$.24 | \$.27 |
| Discontinued operations..... | .08 | .02 | -- | (.15) |
| | ----- | ----- | ----- | ----- |
| Net earnings..... | \$.19 | \$.33 | \$.24 | \$.12 |
| | ===== | ===== | ===== | ===== |
| Diluted earnings (loss) per share: | | | | |
| Continuing operations..... | \$.11 | \$.31 | \$.24 | \$.27 |
| Discontinued operations..... | .08 | .02 | -- | (.15) |
| | ----- | ----- | ----- | ----- |
| Net earnings..... | \$.19 | \$.33 | \$.24 | \$.12 |
| | ===== | ===== | ===== | ===== |

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(12) QUARTERLY RESULTS (UNAUDITED) -- (CONTINUED)

The unaudited quarterly results for the year ended December 31, 1998 are as follows (in thousands, except per share amounts):

| | THREE MONTHS ENDED | | | |
|---|--------------------|------------------|-----------------------|----------------------|
| | MARCH 31, 1998 | JUNE 30, 1998 | SEPTEMBER 30, 1998 | DECEMBER 31, 1998 |
| Revenues..... | \$82,748 | \$84,884 | \$82,753 | \$81,870 |
| Costs and expenses..... | 73,099 | 72,500 | 71,832 | 69,313 |
| Impairment of long-lived assets..... | -- | -- | 8,333 | -- |
| Operating income..... | 9,649 | 12,384 | 2,588 | 12,557 |
| Equity in earnings of insurance affiliate..... | 494 | 413 | 418 | -- |
| Loss on sale of insurance affiliate..... | -- | -- | (10,536) | -- |
| Equity in earnings (loss) of marine affiliates..... | 716 | 1,149 | 1,034 | (1,953) |
| Interest expense..... | (2,767) | (3,232) | (3,236) | (2,663) |
| Earnings (loss) before taxes on income..... | 8,092 | 10,714 | (9,732) | 7,941 |
| (Provision) benefit for taxes on income..... | (3,052) | (4,039) | 3,161 | (2,976) |
| Net earnings (loss)..... | \$ 5,040 | \$ 6,675 | \$ (6,571) | \$ 4,965 |
| Net earnings (loss) per share of common stock: | | | | |
| Basic..... | \$.21 | \$.31 | \$ (.31) | \$.24 |
| Diluted..... | \$.21 | \$.31 | \$ (.31) | \$.24 |

Quarterly basic and diluted earnings (loss) per share of common stock may not total to the full year per share amounts, as the weighted average number of shares outstanding for each quarter fluctuates as a result of the assumed exercise of stock options.

(13) CONTINGENCIES AND COMMITMENTS

There are various suits and claims against the Company, none of which in the opinion of management will have a material effect on the Company's financial condition, results of operations or cash flows.

Management has recorded necessary reserves and believes that it has adequate insurance coverage or has meritorious defenses for the foregoing claims and contingencies.

Certain Significant Risks and Uncertainties. The Company's marine transportation segment is engaged in the inland marine transportation of industrial chemicals, petrochemical feedstocks, agricultural chemicals and refined petroleum products by tank barge along the Mississippi River System, Gulf Intracoastal Waterway and Houston Ship Channel. In addition, the segment is engaged in the offshore marine transportation of dry-bulk cargo, containers and palletized cargo by barge. Such products are transported between United States ports, with emphasis on the Gulf of Mexico and along the Northeast Seaboard and Caribbean Basin ports, with occasional voyages to South American, West African and European ports.

The Company's diesel repair segment is engaged in the overhaul and repair of large diesel engines and related parts sales in the marine, locomotive and power generator markets. The marine market serves vessels powered by large diesel engines utilized in the various inland and offshore marine industries. The locomotive market serves the shortline and industrial railroad markets, and the power generator market serves the stationary industries.

(13) CONTINGENCIES AND COMMITMENTS -- (CONTINUED)

During 1998, the Company's marine transportation segment accounted for 77%

of the Company's assets and the diesel repair segment accounted for 10%. Of total consolidated revenues, the marine transportation segment generated 74% during 1998, and the diesel repair segment generated 25%. Operating profits, excluding equity in earnings of affiliates and general corporate expenses, included an 82% contribution from the marine transportation segment and 18% contribution from the diesel repair segment.

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 amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. However, in the opinion of management, the amounts would be immaterial.

The customer base includes the major industrial chemical and petrochemical manufacturers, agricultural chemical manufacturers and refining companies in the United States. Approximately 80% of the movements of such products are under long-term contracts, ranging from one year to 10 years. While the manufacturing and refining companies have generally been customers of the Company for numerous years (some as long as 30 years) and management anticipates a continuing relationship, there is no assurance that any individual contract will be renewed. The Dow Chemical Company accounted for 13% of the Company's revenues in 1998 and 1997 and 12% in 1996.

Major customers of the diesel repair segment include the inland and offshore dry-bulk and tank barge operators, oil service companies, petrochemical companies, offshore fishing companies, other marine transportation entities, the United States Coast Guard, Navy and Army, shortline railroads, industrial owners of locomotives, and stationary applications. The marine segment operates as non-exclusive authorized service centers for EMD and the locomotive segment serves as the exclusive distributorship of EMD aftermarket parts sales and services to the shortline and industrial railroad market. The acquisition of MKW in July 1996, more fully described in Note 4, Acquisition, expanded the diesel repair segment's relationship with EMD to an authorized distributorship for 17 eastern states and the Caribbean. The results of the diesel repair segment are largely tied to the industries it serves and, therefore, can be influenced by the cycles of such industries. The diesel repair segment's relationship with EMD has been maintained for 30 years. No single customer of the diesel repair segment accounted for more than 10% of the Company's revenues in 1996, 1997 and 1998.

Weather can be a major factor in the day-to-day operations of the marine transportation segment. Adverse weather conditions, such as fog in the winter and spring months, can impair the operating efficiencies of the fleet. Shipments of products can be significantly delayed or postponed by weather conditions, which are totally beyond the control of management. River conditions are also factors which impair the efficiency of the fleet and can result in delays, diversions and limitations on night passages, horsepower requirements and size of tows. Additionally, much of the inland waterway system is controlled by a series of locks and dams designed to provide flood control, maintain pool levels of water in certain areas of the country and facilitate navigation on the inland river system. Maintenance and operations of the navigable inland waterway infrastructure is a government function handled by the Corps of Engineers with costs shared by industry. Significant changes in governmental policies or appropriations with respect to maintenance and operations of the infrastructure could adversely affect the Company.

The Company's marine transportation segment is subject to regulations by the United States Coast Guard, federal laws, state laws and certain international conventions. The Company believes that additional safety, environmental and occupational health regulations may be imposed on the marine industry. The Company believes that it is currently operating to standards at least the equal of such anticipated additional regulations. However, there can be no assurance that any such new regulations or requirements, or any discharge of pollutants by the Company, will not have an adverse effect on the Company.

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(13) CONTINGENCIES AND COMMITMENTS -- (CONTINUED)

The Company's marine transportation segment competes principally in markets

subject to the Jones Act, a federal cabotage law that restricts domestic marine transportation in the United States to vessels built and registered in the United States, and manned and owned by United States citizens. During the past several years, the Jones Act cabotage provisions have come under attack by interests seeking to facilitate foreign flag competition in trades reserved for domestic companies and vessels under the Jones Act. The efforts have been consistently defeated by large margins in the United States Congress. The Company believes that continued efforts will be made to modify or eliminate the cabotage provisions of the Jones Act. If such efforts are successful, certain elements could have an adverse effect on the Company.

(14) SEGMENT DATA

The Company adopted SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information," in 1998. The segment information for 1996 and 1997 has been restated from prior years' presentations in order to conform to the 1998 presentation.

The Company evaluates the performance of its segments based on operating income before income taxes, interest income and expense, gains or losses on sale of assets, accounting changes, and nonrecurring items. Intersegment sales are not significant.

KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(14) SEGMENT DATA -- (CONTINUED)

The following table sets forth by reportable segment the revenues, profit or loss, identifiable assets, depreciation and amortization and capital expenditures attributable to the continuing principal activities of the Company for the years ended December 31, 1996, 1997 and 1998 (in thousands):

| | 1996 | 1997 | 1998 |
|---|-----------|-----------|-----------|
| | ----- | ----- | ----- |
| Revenues: | | | |
| Marine transportation..... | \$249,594 | \$256,108 | \$244,839 |
| Diesel repair..... | 70,422 | 79,136 | 82,241 |
| Other..... | 3,568 | 1,290 | 5,175 |
| | ----- | ----- | ----- |
| | \$323,584 | \$336,534 | \$332,255 |
| | ===== | ===== | ===== |
| Segment profit (loss): | | | |
| Marine transportation..... | \$ 38,172 | \$ 39,542 | \$ 37,661 |
| Diesel repair..... | 5,376 | 6,189 | 8,050 |
| Other..... | (9,484) | (9,259) | (28,696) |
| | ----- | ----- | ----- |
| | \$ 34,064 | \$ 36,472 | \$ 17,015 |
| | ===== | ===== | ===== |
| Total assets: | | | |
| Marine transportation..... | \$320,816 | \$321,158 | \$301,020 |
| Diesel repair..... | 48,012 | 47,290 | 38,588 |
| Other..... | 155,702 | 149,511 | 50,691 |
| | ----- | ----- | ----- |
| | \$524,530 | \$517,959 | \$390,299 |
| | ===== | ===== | ===== |
| Depreciation and amortization: | | | |
| Marine transportation..... | \$ 25,818 | \$ 24,921 | \$ 23,977 |
| Diesel repair..... | 883 | 980 | 917 |
| Other..... | 1,685 | 2,212 | 2,489 |
| | ----- | ----- | ----- |
| | \$ 28,386 | \$ 28,113 | \$ 27,383 |
| | ===== | ===== | ===== |
| Capital expenditures and business acquisitions: | | | |
| Marine transportation..... | \$ 33,123 | \$ 20,161 | \$ 24,521 |
| Diesel repair..... | 14,785 | 521 | 1,103 |
| Other..... | 2,716 | 3,824 | 1,821 |
| | ----- | ----- | ----- |
| | \$ 50,624 | \$ 24,506 | \$ 27,445 |
| | ===== | ===== | ===== |

The following table presents the details of "Other" segment profit (loss) for the years ended December 31, 1996, 1997 and 1998 (in thousands):

| | 1996 | 1997 | 1998 |
|--|------------|------------|-------------|
| | ----- | ----- | ----- |
| General corporate expenses..... | \$ (5,786) | \$ (4,864) | \$ (5,375) |
| Interest expense..... | (13,349) | (13,378) | (11,898) |
| Equity in earnings of affiliates..... | 6,083 | 7,693 | 2,271 |
| Gain on sale of assets..... | 2,751 | 407 | 3,517 |
| Impairment of long-lived assets..... | -- | -- | (8,333) |
| Loss on sale of equity investment..... | -- | -- | (10,536) |
| Other..... | 817 | 883 | 1,658 |
| | ----- | ----- | ----- |
| | \$ (9,484) | \$ (9,259) | \$ (28,696) |
| | ===== | ===== | ===== |

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KIRBY CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

(14) SEGMENT DATA -- (CONTINUED)

The following table presents the details of "Other" total assets as of December 31, 1996, 1997 and 1998 (in thousands):

| | 1996 | 1997 | 1998 |
|--------------------------------|-----------|-----------|----------|
| | ----- | ----- | ----- |
| General corporate assets..... | \$ 39,086 | \$ 38,899 | \$37,896 |
| Investments in affiliates..... | 57,251 | 61,576 | 12,795 |
| Discontinued operations..... | 59,365 | 49,036 | -- |
| | ----- | ----- | ----- |
| | \$155,702 | \$149,511 | \$50,691 |
| | ===== | ===== | ===== |

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PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

1. Financial Statements:

Included in Part III of this report:

Report of KPMG LLP, Independent Public Accountants, on the financial statements of Kirby Corporation and Consolidated Subsidiaries for the years ended December 31, 1996, 1997 and 1998.

Balance Sheets, December 31, 1997 and 1998.

Statements of Earnings, for the years ended December 31, 1996, 1997 and 1998.

Statements of Stockholders' Equity, for the years ended December 31, 1996, 1997 and 1998.

Statements of Cash Flows, for the years ended December 31, 1996, 1997 and 1998.

Notes to Financial Statements, for the years ended December 31, 1996, 1997 and 1998.

2. Financial Statement Schedules

All schedules are omitted as the required information is inapplicable or the information is presented in the consolidated financial statements or related notes.

3. Reports on Form 8-K

There were no reports on Form 8-K filed for the three months ended December 31, 1998.

4. Exhibits

| EXHIBIT NO. ----- | DESCRIPTION OF EXHIBIT ----- |
|-------------------------|---|
| 3.1 | -- Restated Articles of Incorporation of Kirby Exploration Company, Inc. (the "Company"), as amended (incorporated by reference to Exhibit 3.1 of the Registrant's 1989 Registration Statement on Form S-3 (Reg. No. 33-30832)). |
| 3.2 | -- Certificate of Amendment of Restated Articles of Incorporation of the Company filed with the Secretary of State of Nevada April 30, 1990 (incorporated by reference to Exhibit 3.2 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1990). |
| 3.3 | -- Bylaws of the Company, as amended (incorporated by reference to Exhibit 3.2 of the Registrant's 1989 Registration Statement on Form S-3 (Reg. No. 33-30832)). |
| 3.4 | -- Amendment to Bylaws of the Company effective April 24, 1990 (incorporated by reference to Exhibit 3.4 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1990). |
| 4.1 | -- Indenture, dated as of December 2, 1994, between the Company and Texas Commerce Bank National Association, Trustee, (incorporated by reference to Exhibit 4.3 of the Registrant's 1994 Registration Statement on Form S-3 (Reg. No. 33-56195)). |
| 10.1+ | -- 1976 Stock Option Plan of Kirby Exploration Company, as amended, and forms of option agreements provided for thereunder and related documents (incorporated by reference to Exhibit 10.1 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1981). |

| EXHIBIT NO. ----- | DESCRIPTION OF EXHIBIT ----- |
|-------------------------|--|
| 10.2+ | -- 1982 Stock Option Plan for Kirby Exploration Company, and forms of option agreements provided for thereunder and related documents (incorporated by reference to Exhibit 10.5 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1982). |
| 10.3+ | -- Amendment to 1982 Stock Option Plan for Kirby Exploration Company (incorporated by reference to Exhibit 10.5 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1986). |
| 10.4 | -- Indemnification Agreement, dated April 29, 1986, between the Company and each of its Directors and certain key employees (incorporated by reference to Exhibit 10.11 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1986). |
| 10.5+ | -- 1989 Employee Stock Option Plan for the Company, as amended (incorporated by reference to Exhibit 10.11 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1989). |
| 10.6+ | -- 1989 Director Stock Option Plan for the Company, as amended (incorporated by reference to Exhibit 10.12 of the Registrant's Annual Report on Form 10-K for the year |

- 10.7 -- ended December 31, 1989).
- 10.7 -- Loan Agreement between Dixie Fuels Limited and NCNB Leasing Corporation, dated as of February 4, 1992 (incorporated by reference to Exhibit 10.10 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1991).
- 10.8 -- Note Purchase Agreement, dated as of August 12, 1992, among Dixie Carriers, Inc., The Variable Annuity Life Insurance Company, Provident Mutual Life and Annuity Company of America, among others (incorporated by reference to Exhibit 10.1 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1992).
- 10.9+ -- Deferred Compensation Agreement dated August 12, 1985 between Dixie Carriers, Inc., and J. H. Pyne (incorporated by reference to Exhibit 10.19 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1992).
- 10.10 -- Agreement and Plan of Merger, dated April 1, 1993, among Kirby Corporation, AFRAM Carriers, Inc. and AFRAM Lines (USA) Co., Ltd. and the shareholders of AFRAM Lines (USA) Co., Ltd. (incorporated by reference to Exhibit 2.1 of the Registrant's Current Report on Form 8-K dated May 3, 1993).
- 10.11+ -- 1994 Employee Stock Option Plan for Kirby Corporation (incorporated by reference to Exhibit 10.21 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1993).
- 10.12+ -- 1994 Nonemployee Director Stock Option Plan for Kirby Corporation (incorporated by reference to Exhibit 10.22 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1993).
- 10.13+ -- 1993 Stock Option Plan of Kirby Corporation for Robert G. Stone, Jr. (incorporated by reference to Exhibit 10.23 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1993).
- 10.14+ -- Amendment to 1989 Director Stock Option Plan for Kirby Exploration Company, Inc. (incorporated by reference to Exhibit 10.24 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1993).

| EXHIBIT NO. ----- | DESCRIPTION OF EXHIBIT ----- |
|-------------------------|--|
| 10.15 | -- Purchase Agreement, dated November 16, 1994, by and between The Dow Chemical Company and Dow Hydrocarbons and Resources, Inc., and Dixie Marine, Inc. (incorporated by reference to Exhibit 10.25 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1994). |
| 10.16 | -- Distribution Agreement, dated December 2, 1994, by and among Kirby Corporation and Merrill Lynch, Pierce, Fenner & Smith Incorporated, Salomon Brothers Inc, and Wertheim Schroder & Co. Incorporated (incorporated by reference to Exhibit 1.1 of the Registrant's Current Report on Form 8-K dated December 9, 1994). |
| 10.17+ | -- 1996 Employee Stock Option Plan for Kirby Corporation (incorporated by reference to Exhibit 10.24 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1996). |
| 10.18+ | -- Amendment No. 1 to the 1994 Employee Stock Option Plan for Kirby Corporation (incorporated by reference to Exhibit 10.25 of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1996). |
| 10.19 | -- Credit Agreement, dated September 19, 1997, among Kirby Corporation, the Banks named therein, and Texas Commerce Bank National Association as Agent and Funds Administrator (incorporated by reference to Exhibit 10.0 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1997). |
| 10.20 | -- First Amendment to Credit Agreement, dated January 30, |

- 1998, among Kirby Corporation, the Banks named therein, and Chase Bank of Texas, N.A. as Agent and Funds Administrator (incorporated by reference to Exhibit B2 of the Registrant's Tender Offer Statement on Schedule 13E-4 filed with the Securities and Exchange Commission on February 17, 1998).
- 10.21 -- Asset Purchase Agreement, dated January 28, 1998, by and between Hvide Marine Incorporated, Sabine Transportation Company (an Iowa corporation), Kirby Corporation, Sabine Transportation Company (a Delaware corporation) and Kirby Tankships, Inc. (incorporated by reference to Exhibit 2.1 of the Registrant's Current Report on Form 8-K dated March 25, 1998).
 - 10.22* -- Second Amendment to Credit Agreement, dated November 30, 1998, among Kirby Corporation, the Banks named therein, and Chase Bank of Texas, N.A. as Agent and Funds Administrator.
 - 21.1* -- Principal Subsidiaries of the Registrant.
 - 23.1* -- Consent of KPMG LLP.
 - 27.1* -- Financial Data Schedule.
 - 28.1* -- Independent Auditors' Report of Deloitte & Touche LLP.

- - - - -

* Filed herewith

+ Management contract, compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

KIRBY CORPORATION
(Registrant)

By: /s/ NORMAN W. NOLEN

Norman W. Nolen
Senior Vice President

Dated: February 25, 1999

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| SIGNATURE ----- | CAPACITY ----- | DATE ---- |
|---|--|-------------------|
| /s/ GEORGE A. PETERKIN, JR. ----- George A. Peterkin, Jr. | Chairman of the Board and Director of the Company | February 25, 1999 |
| /s/ J. H. PYNE ----- J. H. Pyne | President, Director of the Company and Principal Executive Officer | February 25, 1999 |
| /s/ NORMAN W. NOLEN ----- Norman W. Nolen | Senior Vice President, Treasurer, Assistant Secretary of the Company and Principal Financial Officer | February 25, 1999 |
| /s/ G. STEPHEN HOLCOMB ----- G. Stephen Holcomb | Vice President, Contoller, Assistant Secretary of the Company and Principal Accounting Officer | February 25, 1999 |

| | | |
|-----------------------------|-------------------------|-------------------|
| /s/ GEORGE F. CLEMENTS, JR. | Director of the Company | February 25, 1999 |
| George F. Clements, Jr. | | |
| /s/ C. SEAN DAY | Director of the Company | February 25, 1999 |
| C. Sean Day | | |
| /s/ BOB G. GOWER | Director of the Company | February 25, 1999 |
| Bob G. Gower | | |
| /s/ WILLIAM M. LAMONT, JR. | Director of the Company | February 25, 1999 |
| William M. Lamont, Jr. | | |
| /s/ ROBERT G. STONE, JR. | Director of the Company | February 25, 1999 |
| Robert G. Stone, Jr. | | |
| /s/ THOMAS M. TAYLOR | Director of the Company | February 25, 1999 |
| Thomas M. Taylor | | |
| /s/ J. VIRGIL WAGGONER | Director of the Company | February 25, 1999 |
| J. Virgil Waggoner | | |

INDEX TO EXHIBITS

| EXHIBIT NO. ----- | DESCRIPTION OF EXHIBIT ----- |
|-------------------------|---|
| 10.22 | -- Second Amendment to Credit Agreement, dated November 30, 1998, among Kirby Corporation, the Banks named therein, and Chase Bank of Texas, N.A. as Agent and Funds Administrator. |
| 21.1 | -- Principal Subsidiaries of the Registrant. |
| 23.1 | -- Consent of KPMG LLP. |
| 27.1 | -- Financial Data Schedule. |
| 28.1 | -- Independent Auditors' Report of Deloitte & Touche LLP. |

SECOND AMENDMENT
TO
CREDIT AGREEMENT

THIS SECOND AMENDMENT TO CREDIT AGREEMENT dated as of November 30, 1998 (this "Amendment") is among KIRBY CORPORATION, a Nevada corporation (the "Borrower"), the banks named on the signature pages hereto, and CHASE BANK OF TEXAS, N.A. (formerly known as Texas Commerce Bank National Association), as Funds Administrator and Agent (the "Agent").

PRELIMINARY STATEMENT

(1) Pursuant to that certain Credit Agreement dated as of September 19, 1997, among the Borrower, the banks named therein (the "Banks"), the Agent as the fund administrator and the Agent, the Banks have made a revolving credit facility available to the Borrower upon the terms and conditions set forth therein. Said Credit Agreement was amended by that certain First Amendment to Credit Agreement dated as of January 30, 1998, among the Borrower, the Banks, the Agent and the funds administrator. Said Credit Agreement as amended by the First Amendment to Credit Agreement is herein referred to as the "Existing Credit Agreement".

(2) The Borrower has requested that certain provisions of the Existing Credit Agreement be further amended, and the Banks and the Agent have agreed to amend such provisions to the extent and in the manner set forth herein.

Accordingly, in consideration of the foregoing and the mutual covenants set forth herein, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

SECTION 1.01. DEFINED TERMS. All capitalized terms defined in the Existing Credit Agreement, and not otherwise defined herein shall have the same meanings herein as in the Existing Credit Agreement. Upon the effectiveness of this Amendment, each reference (a) in the Existing Credit Agreement to "this Agreement," "hereunder," "herein" or words of like import shall mean and be a reference to the Existing Credit Agreement, as amended hereby, (b) in the Notes and the other Loan Documents to the Existing Credit Agreement shall mean and be a reference to the Existing Credit Agreement, as amended hereby, and (c) in the Loan Documents to any term defined by reference to the Existing Credit Agreement shall mean and be a reference to such term as defined in the Existing Credit Agreement, as amended hereby.

SECTION 1.02. REFERENCES, ETC. The words "hereof," "herein" and "hereunder" and words of similar import when used in this Amendment shall refer to this Amendment as a whole and not to any particular provision of this Amendment. In this Amendment, unless a clear contrary intention appears the word "including" (and with correlative meaning "include") means including, without limiting the generality of any description preceding such term. No provision of this Amendment shall be interpreted or constructed against any Person solely because that Person or its legal representative drafted such provision.

ARTICLE II

AMENDMENTS TO EXISTING CREDIT AGREEMENT

SECTION 2.01. AMENDMENT TO SECTION 6.01(C). Section 6.01(c) of the Existing Credit Agreement is amended and restated to read as follows:

"(c) Minimum Net Worth. Permit Net Worth, measured as of the last day of any calendar quarter, to be less than the sum of (i) the Base Equity Amount (as defined below), plus (ii) the lesser of (A) a cumulative

amount equal to fifty percent (50%), if positive, zero percent (0%), if negative, of Net Income for each fiscal year ending after September 19, 1997 and

(B) \$75,000,000. As used herein, the term "Base Equity Amount" means the sum of (1) \$136,000,000 minus (2) an amount equal to the lesser of (x) \$50,000,000 and (y) the net reduction in Net Worth after December 31, 1997 attributable to Borrower's sale, issuance or repurchase of its capital stock."

SECTION 2.02. AMENDMENT TO SECTION 6.11. Section 6.11 of the Existing Credit Agreement is deleted in its entirety.

ARTICLE III

CONDITIONS TO EFFECTIVENESS

SECTION 3.01. CONDITIONS TO EFFECTIVENESS. This Amendment shall become effective upon receipt by the Agent of the following, each in form and substance reasonably satisfactory to the Agent and in such number of counterparts as may be reasonably requested by the Agent:

(a) This Amendment duly executed by the Borrower and the Majority Banks.

(b) A certificate of the secretary or an assistant secretary of the Borrower certifying (i) true and correct copies of resolutions adopted by the Board of Directors of the Borrower (A) authorizing the execution, delivery and performance by the Borrower of this Amendment, and (B) authorizing officers of the Borrower to execute and deliver this Amendment, and (ii) the incumbency and specimen signatures of the officers of the Borrower executing this Amendment or any other document on behalf of the Borrower.

(c) A certificate of a Responsible Officer of the Borrower certifying that, after giving effect to this Amendment, (i) the representations and warranties contained in Article IV are true and correct on and as of such date, as though made on and as of such date, and (ii) no Default has occurred and is continuing, or would result from the execution, delivery or performance of this Amendment.

(d) Certificates of appropriate public officials as to the existence and good standing of the Borrower in the States of Nevada and Texas.

ARTICLE IV

REPRESENTATIONS AND WARRANTIES

In order to induce the Bank Group to enter into this Amendment, the Borrower hereby represents and warrants to the Bank Group as follows:

SECTION 4.01. EXISTING CREDIT AGREEMENT. After giving effect to the execution and delivery of this Amendment and the consummation of the transactions contemplated hereby, and with this Amendment constituting one of the Loan Documents, the representations and warranties set forth in Article IV of the Existing Credit Agreement are true and correct on the date hereof as though made on and as of such date.

SECTION 4.02. NO DEFAULT. After giving effect to the execution and delivery of this Amendment and the consummation of the transactions contemplated hereby, no Default or Event of Default has occurred and is continuing as of the date hereof.

ARTICLE V

MISCELLANEOUS

SECTION 5.01. AFFIRMATION OF LOAN DOCUMENTS. The Borrower hereby acknowledges and agrees that all of its obligations under the Existing Credit Agreement, as amended hereby, and the other Loan Documents shall remain in full force and effect following the execution and delivery of this Amendment, and such obligations are hereby affirmed, ratified and confirmed by the Borrower.

SECTION 5.02. COSTS AND EXPENSES. The Borrower agrees to pay on demand all reasonable costs and expenses incurred by the Agent and the Funds Administrator in connection with the preparation, execution, delivery, filing, administration and recording of this Amendment and any other agreements delivered in connection with or pursuant to this Amendment, including, without limitation, the reasonable fees and out-of-pocket expenses of Andrews & Kurth L.L.P., special

counsel to the Agent.

SECTION 5.03. SUCCESSORS AND ASSIGNS. This Amendment shall be binding upon and inure to the benefit of the Borrower and the Bank Group and their respective successors and assigns.

SECTION 5.04. CAPTIONS. The captions in this Amendment have been inserted for convenience only and shall be given no substantive meaning or significance whatsoever in construing the terms and provisions of this Amendment.

SECTION 5.05. COUNTERPARTS. This Amendment may be executed in any number of counterparts and by different parties hereto in separate counterparts, each of which when so executed and delivered shall be deemed to be an original and all of which taken together shall constitute but one and the same instrument.

SECTION 5.06. GOVERNING LAW. This Amendment shall be governed by, and construed in accordance with, the laws of the State of Texas.

SECTION 5.07. FINAL AGREEMENT OF THE PARTIES. THE EXISTING CREDIT AGREEMENT (INCLUDING THE EXHIBITS THERETO), AS AMENDED BY THIS AMENDMENT, THE NOTES AND THE OTHER LOAN DOCUMENTS REPRESENT THE FINAL AGREEMENT BETWEEN THE PARTIES AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES. THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN THE PARTIES.

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4

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be executed by their respective officers thereunto duly authorized as of the date first above written.

KIRBY CORPORATION

By: /s/ G. STEPHEN HOLCOMB

Name: G. Stephen Holcomb
Title: Vice President

CHASE BANK OF TEXAS, N.A. (formerly known as Texas Commerce Bank National Association), as Funds Administrator, as Agent, and individually as one of the Banks

By: /s/ MICHAEL ONDRUCH

Name: Michael Ondruch
Title: Vice President

ABN AMRO BANK N.V.

By: /s/ DIEGO PUIGGARI

Name: Diego Puiggari
Title: Group Vice President

By: /s/ GLENN SROKA

Name: Glenn Sroka
Title: Credit Officer

CITIBANK, N.A.

By: /s/ JOHN F. HEUSS

Name: John F. Heuss
Title: Vice President

FIRST UNION NATIONAL BANK, as
successor to CoreStates Bank, N.A.

By: /s/ MICHAEL J. LABRUM

Name: Michael J. Labrum
Title: Vice President

DEPOSIT GUARANTY NATIONAL BANK

By: /s/ E. ANTHONY THOMAS

Name: E. Anthony Thomas
Title: Senior Vice President

WELLS FARGO BANK (TEXAS), N.A.

By: /s/ NIPUL V. PATEL

Name: Nipul V. Patel
Title: Assistant Vice President

KIRBY CORPORATION

PRINCIPAL SUBSIDIARIES OF THE REGISTRANT

| | PLACE OF INCORPORATION ----- |
|--|------------------------------------|
| KIRBY CORPORATION -- PARENT AND REGISTRANT..... | Nevada |
| SUBSIDIARIES OF THE PARENT AND REGISTRANT | |
| Kirby Inland Marine, Inc.(1)..... | Delaware |
| General Energy Corporation(1)..... | Delaware |
| Kirby Exploration Company of Texas(1)..... | Delaware |
| Kirby Terminals, Inc.(1)..... | Texas |
| Sabine Transportation Company(1)..... | Delaware |
| Kirby Pioneer, Inc.(1)..... | Delaware |
| AFRAM Carriers, Inc.(1)..... | Delaware |
| Marine Systems, Inc.(1)..... | Louisiana |
| Rail Systems, Inc.(1)..... | Delaware |
| Engine Systems, Inc.(1)..... | Delaware |
| Americas Marine Express, Inc.(1)..... | Delaware |
| Kirby Tankships, Inc.(1)..... | Delaware |
| Kirby Marine Transportation Corporation(1)..... | Texas |
| Sabine Marine Transportation Company(1)..... | Delaware |
| Dixie Offshore Transportation Company(1)..... | Delaware |
| Mariner Reinsurance Company Limited(1)..... | Bermuda |
| Oceanic Insurance Limited(1)..... | Bermuda |
| CONTROLLED CORPORATIONS | |
| Dixie Bulk Transport, Inc. (subsidiary of Kirby Inland Marine, Inc.) (1)..... | Delaware |
| Western Towing Company (subsidiary of Kirby Inland Marine, Inc.) (1)..... | Texas |
| Kirby Inland Marine, Inc. of Louisiana (subsidiary of Kirby Inland Marine, Inc.) (1)..... | Delaware |
| Kirby Inland Marine, Inc. of Texas (subsidiary of Kirby Inland Marine, Inc.) (1)..... | Delaware |
| Kirby Inland Marine, Inc. of Mississippi (subsidiary of Kirby Inland Marine, Inc.) (1)..... | Delaware |
| Dixie Carriers, Inc. (subsidiary of Kirby Inland Marine, Inc.) (1)..... | Texas |
| East Cross Sea Transport, Inc. (subsidiary of AFRAM Carriers, Inc.)..... | Panama |
| Four Fletcher Commerce, Inc. (subsidiary of AFRAM Carriers, Inc.)..... | Florida |

(1) Included in the consolidated financial statements.

INDEPENDENT AUDITORS' CONSENT

We consent to the incorporation by reference in the Registration Statements (No. 33-62116), (No. 33-56195) on Form S-3 and (No. 33-681400), (No. 2-67954), (No. 2-84789), (No. 33-57621), (No. 33-57625) on Form S-8 of Kirby Corporation and consolidated subsidiaries of our report dated February 4, 1999, relating to the consolidated balance sheets of Kirby Corporation and consolidated subsidiaries as of December 31, 1998 and 1997 and the related consolidated statements of earnings, stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 1998, which report appears in the December 31, 1998 Annual Report on Form 10-K of Kirby Corporation.

KPMG LLP

Houston, Texas
February 25, 1999

<ARTICLE> 5

<LEGEND>

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM CONSOLIDATED BALANCE SHEETS AND STATEMENTS OF EARNINGS AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of
Universal Insurance Company
San Juan, Puerto Rico

We have audited the consolidated balance sheet of Universal Insurance Company and its subsidiaries as of December 31, 1997, and the related consolidated statements of earnings, stockholders' equity and cash flows for the years ended December 31, 1996 and 1997 (not presented separately herein). 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 Universal Insurance Company and its subsidiaries at December 31, 1997, and the results of their operations and their cash flows for the years ended December 31, 1996 and 1997 in conformity with generally accepted accounting principles.

Deloitte & Touche LLP

San Juan, Puerto Rico
February 18, 1998