KAYDON CORPORATION

Moderator: James O'Leary
April 28, 2008
10:00 a.m. CT

Operator: Welcome to the Kaydon Corporation first quarter 2008 earnings conference call.

Before the conference begins, the company would like to make the legal disclaimer that certain information on this formal discussion and may be included in the question and answer session is forward looking within the means of the Federal Securities laws.

These forward looking statements are only predictions based on the company's current expectations about future events.

While the company believes that any forward looking statement may be reasonable, actual results could differ materially since the statements are based on the company's current expectations and are subject to the risk of certainties beyond the company.

Listeners are cautioned to refer to the company's 2007 forum 10-K for a list of factors that could cause these results to differ from any anticipated and any former looking – forward looking statements.

The company does not undertake and expressly disclaims any obligation to update or alter its forward looking statement whether as a result of a new information, future events or otherwise except as a required by applicable law.

During the conference call, Kaydon spokespersons will reference certain non gap measurements to assist you in understanding such non gap measures as well as to comply with the SEC requirements. The company has included in their press release, reconciliations of the non-gap measures to their most directly compatible gap measures.

Today's conference is being recorded now.

I would like to turn the call over to Mr. James O'Leary, Chairman and Chief Executive Officer of Kaydon Corporation. Mr. O'Leary, please go ahead.

James O'Leary: Thanks William. Good morning and thanks for joining us today.

For those of you who are on the call promptly at 11:00, we apologize for starting a little bit late. We had a flood of people coming on, and wanted to give them a couple minutes to join us. But so, we apologize for the slightly later start, but welcome to our call today.

I'm joined this morning by Ken Crawford, Senior Vice President and Chief Financial Officer; and (Peter De'Chance), Senior Vice President responsible for corporate strategy and development.

I'm please to be reporting on our first quarter, which met our expectations, and was consistent with our overall plan for the year. More importantly, we're pleased to achieve all time Kaydon record for quarterly orders and quarter end back log. During the quarter we made considerable progress in our well defined initiatives to accelerate long term growth both internationally and insecurely strong markets, such as supplying the global alternative energy infrastructure build out.

Namely, wind energy. We'll discuss these liberally throughout today's calls, as both are integral to our long term profitable growth strategy.

As I've noted in prior calls, we want to provide as many of the building blocks needed to help set your expectations without departing from our policy of not providing explicit guidance. And our press release and our prepared remarks will address as many of these as practical.

And as the year goes on we'll continue to address these in sufficient detail so you can keep track of them relative to current expectations.

Now, let's review the current quarter.

During the quarter, we had record order entry of 204.3 million, up over 44 percent year over year. This leaves us with quarter end back log of almost 320 million, an increase of nearly 72 percent as compared to the first quarter of 2007 and 33.9 percent higher than the previous record, recently achieved in our fourth quarter of 2007. Total wind orders booked in the quarter exceeded 80 million due in large part to a significant single order of almost 64 million. Our book to bill ratio, excluding that order still taked above one, for the company as a whole, and for friction control products as a segment.

During the quarter, Kaydon had record first quarter sales of 123.3 million, up over 15 percent over the last year, driven by especially strong sales in our two larger segments, friction controls and velocity controls.

Gross profit for the quarter was 47.3 million, with 38.4 percent of sales, as compared to 44.8 million, or 41.9 percent of sales during last year's first quarter.

The temporary decline in gross margins was partially due to the wind energy expansion as we've discussed liberally in the past, and the inclusion of Avon whose profit contribution has minimized in the first few post closing quarters by acquisition accounting requirements. Ken will give you a lot more detail on that in a little while. We're also impacted by the absence of a major military order, which peaked at the end of 2006, and early 2007 and then dropped off.. It's not being replaced by another significant opportunity but one which doesn't fully ramp up until the end of the second quarter, and into the third quarter.

That's the end ramp up opportunity we discussed in prior calls.

Selling general administration expenses were 21.2 million, or 17.2 percent of sales during the first quarter of 2008, as compared to 18.5 million or 17.4 percent of sales in the first quarter of 2007. Operating income was 26.2 million as compared to 26.3, in the prior quarter. With an operating margin of 21.2 percent compared 24.6 percent last year. Again, with the decline due to the projects we're putting in and the military timing issue I discussed a second ago. First quarter 2008 interest income was 1.9 million. And it declined significantly from the 4.6 million earned in the first quarter earned in the first quarter of 2007.

This decline was due to lower interest rates achieved on investable balances, and the recognition of a $500,000 charge part of which had already been classified in other comprehensive income in the prior quarter.

Average interest rates decline from 5.1 percent to 3.4 percent due to lower rates and the impact of steps taken by us to preserve capital and liquidity, rather than pursue short term yields that are higher than what we're currently attaining. We look for safety and liquidity, rather than higher yield in the last two quarters.

The lower average investable balances resulted from the Avon acquisition. 2007 pension contributions to fully fund our pension plans and higher capital expenditures to support the capacity in our expansion projects and our stock repurchase activities. Net income equaled 16.6 million with 13.5 percent of sales, as compared to 18.2 million, or 17.1 percent of sales last year with (diludity PS) per share equaling .53 cents as compared to .57 cents in the prior quarter. With the biggest driver of the differential obviously being the interest we just discussed.

Now let's review our operating performance by major segment. Sales of friction control products increased 13.4 million to 74.1 million, 22 percent higher last compared to the last quarter of last year. This segment benefited from increased demand (for specially bearings) utilized in the wind energy, heavy equipment, machinery, and medical equipment markets partially offset by lower sales to the military, and (semi-conductor) markets.

We also benefited from strong sales as (foot roller bearings) notably to the Far East. Revenues and operating income from military sales in the first quarter were below the prior year's levels due in part to lower sales in the high volume legacy program that peaked in 2006, and early 2007. Operating income from friction control products increased to 17.1 million to 16.3 in the prior first quarter. Operating income and margins were affected by the ramp of our wind energy expansion project, and the inclusion of Avon, who's margin have negatively impacted in the short term, by acquisition accounting requirements.

Acquisition accounting adjustments totaled 800,000 during the fourth quarter of 2008. These factors will affect the segment's operating margin through the first half of 2008.

Which Ken will discuss momentarily. And rather than wait until the q-and-a, I'll tell you thus far, we're extremely happy with Avon, all on track, and we'd love to talk a little bit more about how it fits into our overall strategy for servicing the large turn table market during the q-and-a. Operating margin equaled 23.1 percent as compared to 26.9 percent, attained in the prior year.

After the initial impact of acquisition adjustments turned, Avon should generate gross and net contribution margins consistent with our existing wind energy business.

First quarter orders in this segment increased 59.5 million or 66.1 percent to a record 150 million during the quarter.

First quarter 2008 sales of velocity control products increased 3.1 million to 18.8 million, nearly 20 percent over the prior quarter, with strong sales from both our European and North American facilities.

Operating income increased to 5.6 million, with 36.3 higher than the first quarter of 2007 while operating margin rose to 29.7 percent. Both sales and operating income benefit from strong end market demand and the favorable impact of currency translation. Orders increased almost 20 percent over the prior first quarter, leaving backlog at all time record levels, with continued momentum in every end market we serve.

Sealing product sales were 11.5 million as compared to 12 million in the first quarter of 2007. Operating income of the selling product segment declined from 2.5 million, to 1.5 million, because of direct relocation expansion associated with our move from Baltimore to Knoxville.

And workers compensation claims which together totaled about 700,000, and the balance being the impact of lower sales. Orders during the first quarter of 2008 totaled 15.6 million, which was five percent higher than the prior year, as a commercial (aerospace) market in particular has been strong for our sealing products business.

Sales in our other businesses totaled 18.9 million during the first quarter of 2008. An increase from the first quarter of 2007, of about two percent. Principally due to higher demand for our

liquid filtration products. Operating income decreased about 22 percent to two million off a lower base, due to the lower profit contribution from certain of our noncore, non filtration businesses particularly those that are serving the residential plumbing market. In total, as well as by segment, order entry was extremely strong during the first quarter of 2008 as we achieved a quarterly record of 204.3 million, a 44.2 percent increase over last year's total. During the quarter we took a major wind energy order, which will utilize the capacity coming online later this year.

Non-wind orders were also strong, increasing both year over year and sequentially. The strong order activity resulted in record back log of almost 320 million, an increase of 71.7 percent as compared to the prior year first quarter, and 33.9 percent of our previous quarter-end record of 238.9 million, reported at the end of 2007. Remember, our back log consists of orders shippable over the next six quarters.

As we discussed in previous quarters, our large wind energy orders will ship a bit later than our non-wind orders largely due to wind capacity expansion projects come online and to the back half of this year. As a result, these large orders have continued to ship the timing of when our back log is expected to ship, and presently, we expect to ship approximately 35 percent of our back log during the next quarter, approximately 35 percent over the next two quarters, and the final 35 percent over the three subsequent quarters, stretching out over the 18 month period which we book back log.

Now, I'll turn it over to Ken to cover some key financial items.

Ken Crawford: Thanks Jim, and good morning everyone. I'm going to spend a fair amount of time on the cash investment contribution to earnings as it had a significant impact in the first quarter. And its impact respectively and the timing of the overall level of 2008 results will be significant.

During the first quarter of 2008, we earned 3.4 percent on average investable balances of $288.8 million.

In addition, we recorded a $500,000 charge to recognize the loss in value of an investment as a reduction in interest income. A portion of which was classified and accumulated other comprehensive income in the fourth quarter of 2007.

Interest income total $1.9 million in the fourth quarter, including the charge.

During the first quarter of 2007, we earned 5.1 percent and average investable balances of $366.3 million, which generated $4.6 million in interest income.

As Jim noted earlier, the lower average investable balances compared to the prior first quarter, resulted from the Avon acquisition. Our third quarter 2007 contribution to fund our pension plans, and the effects of capital expenditures to support our capacity expansion projects. The lower interest rates were caused by the recent general flight to safety in addition to proactive steps by the company to protect principle, and liquidity.

Sequentially, in the fourth quarter of 2007, we earned five percent interest on average investable balances of $307.2 million, which generated 3.9 million of interest income in the fourth quarter of last year. Together, the lower average interest rate, and the lower average investable balances, and the $500,000 charge on the loss of value investment, reduced first quarter 2008 interest income by $2.7 million, equivalent to five cents per share, on a diluted basis compared to the first quarter of 2007.

At the end of the first quarter this year, our investable balances totaled $290.8 million, which is $11.2 million lower than the beginning of 2008.

Of at least equal significance, looking forward into the balance of 2008, the feds recent interest rate reductions and the general spread compression caused by the current credit squeeze.

This will result in as much as a 260 basis point reduction in the second quarter interest rate earned, as we presently see it, relative to the same quarter in 2007, during which we earned 5.1 percent.

The lower interest rates and the expected reduction during the quarter in average investable balances, will reduce interest income by approximately $3 million compared to the second quarter of 2007.

That said, we believe our financial resources will provide us with the flexibility to take advantage of the potentially unique opportunities that may arise during a period where liquidity can be a competitive advantage.

Interest expense during both the first quarters of 2008 and 2007 was $2.4 million with our only long term debt outstanding being the $200 million convertible which will be addressable at the end of May. The effective tax rate during the first quarter of 2008 decreased to 35.4 percent compared with 36.1 percent in the prior first quarter. Primarily because of an increase in foreign sourced earnings. We expect the effective tax rate for 2008 to be approximately 35.4 percent. Net income for the first quarter was 16.6 million or 53 cents per share on a diluted basis, as compared to the first quarter '07 income of 18.2 million or 50 cents per share on a diluted basis.

Free cash flow during the first quarter of 2008 was a negative $2.1 million, compared to a positive 10.7 million in the prior year first quarter. This swing was due to the increased capital expenditures to generate long term profitable growth and working capital increase is supporting our sales growth. As significant year over year growth in sales cause higher cash usage to support higher working capital growth.

During the first quarter 2008, we invested $14.8 million in capital expenditures, doubled the 7.4 million invested in the first quarter last year. Capital expenditures will remain at high levels in 2008, as we take – as we expand to take advantage of the outstanding secular growth opportunities in wind energy.

We currently expect capital expenditures to be approximately 70 to $75 million in 2008.

Free cash flow for the last 12 months ended March 29th of 2008, totaled 7.4 million, as compared to free cash flow for the last 12 months ended March 31st 2007, of 63.4 million.

The comparative reduction was due to the 31.9 million increase in capital expenditures and lower cash from operating activities.

The lower cash from operating activities was due primarily to the increase in pension contributions and increased working capital, again to support our sales growth.

Free cash flow should be viewed as supplemental data, rather than as a substitute for alternative to the gap measure.

We've included in our earnings release a reconciliation of this metric to the most comparable gap measure for your reference. Cash and cash equivalents for short term investments totaled 276.2 million at the end of the first quarter this year, as compared to $287 million at the end of 2007. And long term debt remains unchanged at 200 million equal to 28.9 percent of total capitalization. During the first quarter we paid dividends of 4.2 million, or 15 cents per share. Repurchased $7.6 million worth of common shares, and invested 14.8 million in net capital expenditures. During the quarter we incurred approximately $800,000 of additional depreciation and (emerization) associated with acquisition accounting at Avon.

In addition, we incurred direct start up cost associated with our wind energy expansion, totaling approximately $500,000 and relocation and workers compensation costs at our ceiling products business, totaling approximately 700,000. We also encourage significant expenses associated with our efforts to grow our market share in international markets.

Now I'd like to turn the call back over to Jim.

James O'Leary: Thanks Ken. As I noted at the top of the call, we're pleased with the results achieved in the first quarter of 2008 which came in pretty much as expected, if you listened to our prior call. But more importantly, we made significant progress on our long term growth initiatives.

Our accelerated and increased expansion, and the large diameter bearing market, and our reprioritized efforts to grow our market share in high growth developing countries, such as – China, and India, should yield considerable benefits as we move into the second half of 2008, and into 2009. The record bookings achieved in the first quarter leave us with the highest back log in Kaydon history.

Our continued penetration in the fast growing wind energy market bolstered by last year's acquisition of Avon Bearings positions us well for the balance of 2008 and beyond. While margins in the first quarter were lower, due in part to the direct and indirect costs of this expansion, and the ceiling products relocation, we've positioned the company to take maximum advantage of the securely strong wind energy market, and the opportunities available to us to expand our international market share.

These will benefit us increasingly as the year progresses and we expect meaningful gains in the latter half of 2008, as the capacity comes online in our key growth markets. The company's recent an ongoing investment to expand capacity for large diameter wind energy bearings, and to

increase our international sales efforts should result in continued strong performance during 2008. However, as Ken noted, during the early part of the year, in particular the first quarter, direct and indirect costs associated with these initiatives, short term out sourcing costs, and lost overhead absorption make comparisons with the first two quarters of 2007 difficult and will affect the first half comparisons.

Really, exactly as how we discussed in the prior quarter, we've gone through today.

The costs associated with our initiatives, and the interests issue, impact comparability for the first two quarters of last year.

However, we expect to continue – we expect to begin realizing the benefits of these programs during the end of the second quarter, and for the full year of 2008. And the present we continue to expect our earnings per share growth for the full year to exceed our annual average target of 10 to 12 percent as the benefits of these initiatives contributes significantly to the last half of 2008 and into 2009.

In summary, we're pleased with our first quarter results. Our record quarter back end, back log positions as well as for the balances for 2008 and beyond as we expand our internal capabilities to serve segments and join strong secular growth. We expect meaningful gains during the latter half of 2008, as capacity comes online in our key growth markets, and more importantly, beyond 2008. We believe we're taking all the appropriate measure to maximize share holder value, well into the future. With a strong balance sheet and financial flexibility we'll continue to drive internal growth, while selectively evaluating external opportunities.

Finally, I'd like to thank each of our Kaydon employees for their efforts this quarter. They're our most valuable assets, and I'd like to thank them each for their contributions for this quarter. And with that William, we'll turn it over to you, to moderate q-and-a.

Operator: Sure. The question and answer session will be conducted electronically. If you'd like to ask a question, please do so by pressing the star key followed by the digit one on your touch-tone telephone. If you're suing a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. We'll proceed in the order that you signal us and we'll take as many questions as time permits. Once again, please press star one on your touch tone telephone to ask a question.

We'll move to our first question from Holden Lewis BB&T.

Holden Lewis: Thank you, good morning.

James O'Leary: Hey Holden, how are you?

Holden Lewis: I'm fine, thanks. I wanted to ask you about the margins I guess, in a broad sense I think. You go back to '06, and you were sort of running gross margins 41, 42 percent. Lately (obviously, it) has been depressed.

It just seems like there's a lot of moving pieced here – the Avon accounting, the, you know, the pressure from the construction, the (Mexicoober) bearing, the margin from wind, you know, as that comes on, I guess that's somewhat lower than ((inaudible)) corporate average. But you know, then of course the impact is (sealed).

When all of this smoke kind of clears from all of these things, you know, sort of at the end of 2008, I mean, where would you expect in general terms for the gross margin to settle in at once all those moving pieces are resolved, do you have anything – guidance for that?

James O'Leary: In total, in (average) I'd say, low 20s to mid 20s. And I'm glad you used the fourth quarter 2006, because that is probably the high water mark as we discussed, both on prior calls and in one and ones and in group presentations. That's the high watermark in the quarter that probably is not repeatable, certainly not on this cycle.

The mix of business was very orientated towards – as we talked about this military order, is very orientated towards legacy military programs, extremely high margin that ran through some of our, more profitable facilities. We had not yet begun any of the capacity expansion that we're talking about now. So if you looked at our capital standing over the preceding five, 10, 20 years, except for a few major projects, we're spending, you know, two to four percent of sales (was) barely maintenance.

The real expansion efforts now which we're saving in wind energy didn't start until the first quarter of '07. So you have the two things mixed that is heavily weighted towards legacy programs, particularly in military. It's before the explosion in growth that (Cooper) split (roller) bearings, which you know now in terms of operating margin are getting close to 20 percent. But that's still lower than the overall average of the company so, you've got extremely high margins, but lower than the highest margins in the industry.

I think that's still something we'd take all day long if it continues to grow with the rate it's been. And capacity utilization that if you're growing beyond the 400 million sales base that we've averaged over the preceding 10 years, it'll be pretty tough to repeat that type of performance. So when all this settles, you know, in a steady state with the capacity we got coming online and the existing mix, you know, particularly you mentioned (Cooper) but that's a good one to point to. It's probably in the low to mid 20s operating margin.

Holden Lewis: OK. And that compares to – I think in '06 your operating margin is about 24.4. So I mean you don't – it's not like you feel like your margins are going to step down much when everything clears out from where you've been in the past.

Ken Crawford: Are we talking 24 to 29 ...

James O'Leary: Yes. I think that the mid 20s is certainly attainable – that's our plan at this point.

And we also intend to have a gross margin that starts out – is in the 40s –the low 40s again by the time all this dust settles. So you're talking about a gross margin that may not get to 42, but it's certainly it'll be something that starts with a four, and operating margins in the 24, 25 percent range is certainly our plan.

Holden Lewis: OK and then the expenses for the wind expansion – obviously you continue to incur those. Have you accelerated those so maybe the cost we incur in '09 may be less than what we're doing in '08 or are you just (sort of) assuming given the gross there you can – that you're going to sort of see a steady state of expenses even going out into '09?

Ken Crawford: Steady state, because of the capacity constraints larger when you can order equipment and, you know, there's not a lot we can do to accelerate the things such as – hiring, training, and the like around them. So as long as we're adding capacity, you're going to have some of those issues, but as we have in the past, we'll be very explicit about when that capacity gets added, when it comes online, and the costs associated with it.

But nothing being front loaded for that from '09, because you really can't. You know, we're constrained by when the equipment arrives and when the infrastructure is ready.

Holden Lewis: OK. All right. Great thanks guys.

Ken Crawford: You're welcome, Holden, thank you.

Operator: We'll move to our next question from Peter Lisnic – Robert W. Baird.

Peter Lisnic: Good morning gentlemen.

Ken Crawford: Hey Pete.

Peter Lisnic: Do you mind giving out the exact wind order number, and then what the Avon impact was on orders as well?

James O'Leary: I thought we did give out the exact order – it was 80 million in total, and about 65 was the large single order.

Peter Lisnic: Yes. You said over 80, I didn't know if that was an exact, that's OK.

James O'Leary: That's close enough. Ken, do you got the Avon stuff?

Ken Crawford: Avon's wind orders were relatively minor in the first quarter, around $2 million.

Peter Lisnic: OK, thank you for that. And then just a follow up on Holden's question on the cost you incurred to ramp wind.

I thought in the fourth quarter we're looking at like $2 million number that you were talking about for this quarter, and then I thought I heard 500,000 as kind of the incremental expense in the first quarter here, so ...

James O'Leary: Yes. The $2 million was a combination of the wind ramp up, the Baltimore to Knoxville relocation, and also the costs associated with penetrating some of these distant markets that we talked about – China, India, and other.

And as we indicated I think, in both the press release and the prepared remarks, wind energy was half a million, the relocation expenses combined unfortunately were the fairly significant workers comp charge, were another 700,000.

And then we had significant costs associated with penetrating those distant markets that we didn't quantify.

So the two million we got close to in the quarter.

Peter Lisnic: OK. All right. Then Jim, longer term I guess, if you're looking at – you're basically firing out all cylinders – what – any changes in the long term strategy in terms of growth opportunities for wind in China, and India, acquisitions, any change in thinking along those fronts?

James O'Leary: No. I think at the top of the call I said, the quarter came in about where we expected – we're happy. I think more importantly, the quarter came in as we needed it to for the rest of this year and more importantly (to) '09 and beyond.

The growth opportunities we've identified and we added investment to almost quarterly during last year to (make) about two additional expansions, the last quarter, the acquisition of Avon.

You know, and other little expansions to improve through what we've gone along the way, you'll see in our Capex numbers – by the time the years out we're expanding to bolster what we're doing in the energy infrastructure market.

An incredibly hot market that continues to get stronger. The backup – I wouldn't say alternative use of equipment but where else this equipment would be used is heavy equipment. And if you go through the (Terrexes) the (Metatallex), the guide servicing heavy industrial usage globally, all those guys are deploying record back logs. That is the other use for this equipment, and for the capacity expansion.

So in terms of securely strong growth markets – you know, we're very comfortable we've made all the right steps over the last year. And we're continuing to focus on it and I think you'll see more capacity expansions over the next few quarters. Whether or not it comes in the form of large off shore manufacturing, or adding to what we've got already. It'll depend on the opportunity. And – you know, which customers in which markets were prioritizing at that point. And that's constantly in flux. I would say, we have several anchor clients – one in particular, and we're looking at where we can grow with the guys – going to be growing with the next five, 10 plus years.

In terms of internationally, you know, if you look at the velocity control segment in particular.

We had a great relative to the past couple years quarter North American business, but internationally continues to exceed our expectations from our facility in Germany, we're seeing great improvements all throughout the markets ((inaudible)) which would include Eastern Europe, they've taken over custody of growing our Indian operation, which we announced and are in the process of setting up over the next few quarters. Our filtration businesses, we've added an office in China, we're looking at an office in India. We've added international sales people throughout that division – (this is) our liquid filtration business.

So I think all the actions we're taking around two principle growth objectives, which will contribute meaningfully to a company of Kaydon's size which is large turn table business focused on energy infrastructure and the global heavy equipment market and international where – you know, we've talked a number of times about the fact that we're probably a bit under represented compared to

the (Pierre) group. We're seeing right now, considerable progress and we see huge opportunity going forward.

Peter Lisnic: OK. That's comprehensive. Thanks and well done.

James O'Leary: You're welcome, thank you.

Operator: We'll move to our next question from Walt Liptak – Barrington.

Walt Liptak: Hi, thanks, good morning, Walt with Barrington.

James O'Leary: Hey Walt.

Walt Liptak: Hey. Let me just – I just want to back up and just go over the order entry again and make sure I'm doing the math right. Your orders were up 86 million year over year – that's your incoming order growth right? The 204 last year you were at 109?

James O'Leary: No. Last year we were at 142.

Walt Liptak: OK. Last year, 142. OK. All right I have to go over ...

James O'Leary: The 109 was non-wind, Walt. We had 32 million in wind by last year.

Walt Liptak: OK. OK. Right. The 109's non-wind. OK. So if you back out the non-wind – you know, it looks like your non-wind orders are up 27 percent from last year, is that right? Or is that high?

James O'Leary: Our non-wind orders are up from 109 to 123. I don't think that's 27 percent.

Walt Liptak: OK. Still pretty decent growth.

James O'Leary: Right.

Walt Liptak: OK great. You know, you kind of addressed this with the first question – the margins in wind power on – the large wind power orders, you know, could you just quantify it or just talk a little bit more about how you feel about the pricing on that?

James O'Leary: We're extremely happy about the pricing on it; the margins will come in consistent with the low 20s mid 20-ish overall corporate average that we talked about. It'll be on the lower end because of the nature of the product, and the growth opportunity in it.

As far as the pricing, we're very happy with it.

I think as we talked about in previous quarters to start off this investment we focused on margins and return on capital and we executed some contracts that protect both over the nature of the investment – over the long term nature of the investment. Around that we've added some customers who were pricing more towards market. But we're not going (expecting) will be trying to grab the highest price for short orders we're trying to developed relationships with people who will go out for, you know, in some cases five plus years.

So we've balanced return on investment, margin protection with we think attractive pricing with everyone we do business with, without being perceived as gouging the short term opportunities so you know, without going into specific pricing, where it's sourced, where it's made, and who the customers are. All I can tell you is we're pretty happy with it.

Walt Liptak: OK. Can you tell us how many customers you have in wind now?

James O'Leary: We have over five.

Walt Liptak: OK and then if I could go back over to the costs, the marketing initiative. Can you quantify the incremental costs in this quarter and for next quarter?

James O'Leary: Yes. You know, Walt the reason we – you're talking about international?

Walt Liptak: Yes, for international.

James O'Leary: The reason we didn't do that, you know, I think the two million we left you guys with is probably about right. If you said – hey, I think it's 1.3 in total between the ceiling products which I think is easy to identify and the wind expansion which is relatively easy to identify.

You know, we're kind of at the point where a lot of the balance of the 700,000 is starting to blend in with ongoing operations. So I don't feel like we're doing you a service by saying those are non (recovery) going forwards, they're melding into existing operations, they're beginning to produce income so tell them yes, you know, for the next three quarters it'll be two million although it's starting to generate sales and profit and it doesn't feel like the right thing to do – the initial costs we handicapped at about 700, or, you know, the balance of that two million. But going forward, they're part of our ongoing operations.

Carving them out separately, not only is difficult, I don't think that's the right way to present it to you.

Walt Liptak: OK. Great.

James O'Leary: Does that make sense?

Walt Liptak: Yes.

Ken Crawford: Yes Walt, it's really more a first quarter '08 compared to first quarter '07 comparison on that differential because those costs as Jim said are built into our infrastructure currently.

Walt Liptak: OK, got it. All right thanks guys, have a great day.

James O'Leary: You're welcome, thank you Walt.

Operator: We'll move to our next question from Nigel Coe (with) Deutsche Bank.

Nigel Coe: Hi, good morning. I just want to pick up on a couple of points to discuss the ...

James O'Leary: You change the pronunciation of your name?

Nigel Coe: Yes. I am actually trying to keep a low profile here.

James O'Leary: How are you?

Nigel Coe: Good, thanks. So you made a point that you feel pretty good about the margin that you've got, which is pretty important given your back log structure ((inaudible)).

It sounds like you're pretty comfortable with the price ((inaudible)) you got there. But still prices I see are on a (tear), would it be fair to see that maybe there's some lag between, you know, seeing the inflation and actually passing that through?

James O'Leary: No. It wouldn't be fair, you would be explicitly correct. And we've talked before that a lot of the margin arrangements we have with – and customers who understand the need to help protect our return on investment for the long term.

That operates at a quarter lag, or a quarter to six months lag, we present them with invoices and loaded costs.

And you catch up, so in a constantly increasing environment, you're shooting about a quarter or two behind the curve. You catch up when it flattens out, and you pick up when it goes down.

But you're not happy when you're picking up because it's going down.

Nigel Coe: Right. OK and then secondly on the international costs, I mean you just talked a lot about that. But you know, are you prepared to share maybe a some of revenue contribution from – you know, these initiatives. I mean, what would you think would be a good number in your mind for 2009, as a payback?

James O'Leary: As a payback? And the payback for when we look individually – it's a good time to ask it since we just went through our some of our business plan reviews for the quarter. You know, we're typically looking at three to four year paybacks on adding some of the infrastructure. I think that's a bit misleading because you usually have a year or two where you're paying sales people (in the like) and not really getting meaningful pickups. I would say (Cooper) was well ahead of that, because they just hit the sweet spot of the curve with far east, particularly China and India. I think filtration will do better, in fact I have pretty high hopes that they're going to do better. But I'd say probably three years is not a wrong way to look at the payback.

The tough thing about looking at a payback on period costs is – you know, different than capital it's much hard to run a BCF on that type of thing but what we'd look at these as standalone

entities, we had nothing else around them, no other contribution, no other incremental benefit. I'd say probably about three to four years is when we're expecting to them to contribute. It's been better than that so far.

Nigel Coe: OK, great. And then finally, you talk about the ramp up on the wind towards the last (round) of this year. Would it be fair to (see that's) more a (four key) than the (three key) issue?

James O'Leary: When the contribution begins?

Nigel Coe: From when, Yes. When we ((inaudible)) that, you know, you're ramping up.

James O'Leary: It starts getting pretty meaningful in the third quarter, it's very meaningful in the forth. And then you're at a run rate in excess of a hundred million although the contribution for the year will be less than that so I'd say, you're – it should start in the third quarter, accelerate in the forth, and you will see a pretty big pick up in the second as well, but not as meaningful as the third and forth.

Nigel Coe: OK. And then just to run that out – so what key you think you'll be at the, you know, hundred million dollar plus run rates, ((inaudible)) for that?

James O'Leary: In excess of that by first quarter of 2009.

Nigel Coe: Great. Thanks Jim.

James O'Leary: You're welcome Nigel, thank you.

Operator: We'll take our next question for Ian Fleischer – FBR Capital Markets.

Ian Fleischer: Hi, good morning.

Ken Crawford: Hi Ian; how are you?

Ian Fleischer: Good. (Don) ((inaudible)), can you just touch on the client volume, is that – is any of that related to the movement of the facility or is it some other factors?

James O'Leary: I think it's largely timing. I think the hydrocarbon processing market slowed down a bit. The orders picked up considerably – and a lot of that had to do to the legacy aerospace program. So we're seeing a pretty big – we're seeing continued strength on commercial aerospace. But I'd space it's largely, a little bit of a slow down at hydrocarbon processing. And a little bit on time, and we didn't talk explicitly about it, but the nature of how people were placing orders in terms of bigger orders versus more even flow smaller batch continue to be the case, it just wasn't' significant enough to mention this time.

I'd say a little bit of softness, maybe people holding their fire, to see how the economy goes, and hydrocarbon processing off set, particularly in the order rate, because the orders were still pretty strong, and picked up in commercial aerospace.

Ian Fleischer: Right. And on velocity controls I guess, can you talk about maybe how the (weak) dollars is benefiting you with respect to exports – you know, into your distribution facility in Europe?

James O'Leary: Sure. I'm going to use that question to kind of go off on a modest tangent about dollar and our international sale. As we've talked about, our international sales are about 30 percent of the total company.

But I would say the benefit we're getting from robust international economies, global infrastructure build out, and currency, I make dollar denominated products more attractive. It's considerably

greater than the 30 percent – you know, a lot of our wind energy orders are shipping FOB to a domestic point, but we know they're going somewhere else, it's just harder to track because in some respects, our customers don't know. That same dynamic plays out in a lot of the things we make, and I'm going to come back to velocity controls. If you remember, our products are small pieces of big systems in a lot of cases, they're components of aerospace products, energy infrastructure products. Other things which are much bigger systems – many of which are ending up overseas so our FOB destination may not necessarily give you the whole story.

And in the case of velocity controls, we're helped by the strength internationally by a number of areas. A very easy one is we have a German facility, it services western Europe, eastern Europe, now India and a number of other markets, going great, record quarter after record quarter. We pick up considerably when you translate Euros to dollars, so you've got two very easily quantifiable benefits. The other benefit in our North American facility is one of their principle customers, you know, yes it does get eliminated in the company.

But one of the principle customers is through Germany and out through the rest of western Europe and eastern Europe.

And we also have a pretty reasonable and ((inaudible)) market, but in some cases because our product goes to capital equipment manufacturers who are shipping elsewhere, that's harder to quantify.

So I'd say, you know, we're getting a number of benefits from strengths overseas, weakness in dollar, and currency, and velocity controls two of very easily quantifiable one is not, and then if you extend that to other parts of our business, you know, particularly wind energy, we're absolutely benefiting from strength overseas. We're absolutely benefiting from global infrastructure build out. It's just harder for us to quantify in that 30 percent, because of who and how we ship to.

Ian Fleischer: Right. That's very helpful. Thanks very much.

James O'Leary: You're welcome.

Ken Crawford: Is that it, Ian?

Operator: We'll take our next question from Peter Thompson – Coho Partners.

Peter Thompson: Good morning Jim and Ken.

James O'Leary: Good morning.

Ken Crawford: Good morning.

Peter Thompson: Can I just ask you guys, if you disclosed it I didn't catch it. The wind number in the back log?

James O'Leary: We didn't disclose it. It's about $150 million, in our current $320 million back log.

Peter Thompson: Great and could you comment at all on your thoughts on the $200 million convert that's coming due next month?

James O'Leary: Yes. Well, we have a – for background we have a convertible that was issued about five years ago. Deeply in the money coming due and we will evaluate it; I can't tell you unequivocally what we'll do.

I will tell you the right thing is probably to step up repurchases both before and after as we've talked about on prior calls and as we've talked about in presentations. Whether or not it makes sense to take it out, it really depends on price of stock; there's a very healthy contribution of tax benefit from having this (instrument) outstanding alternative uses of cash. I mean, in the last year we put to work a hundred million then previously was hitting on the balance sheet earning five percent at 3.4, we're starting to see the acquisition market get a little bit better.

We will have, I would say significant Capex in the markets we've talked about going forward as well.

So, it's not obvious that we're ((inaudible)) is the right thing to do, it is obvious they're probably putting more to work in the form (Sherry purchases) is, and how we balance it to – we'll talk a little bit more about in our next quarter.

Peter Thompson: Can it be done – does it have to be an all or none type of deal?

James O'Leary: No. But the mechanics of how you do it, the signaling, given that you have to give note holders a – I think five days. They have a number of days, or perhaps a month to tender. They can be pretty significant run up in the price and a pretty big economic cost too, even our share holders. So again, if your alternative is stepped up repurchase, versus calling it, it's not obvious that calling it's the right thing to do.

Peter Thompson: Can I just ask one more last one, about just wind. Is it all in the friction area, or is some of it in velocity, and I'm just trying to ...

James O'Leary: It's pretty much all – what we've talked about is pretty much all in velocity – excuse me, all in friction. However, we just went through filtration products business review, and – you know,

some of the filtration of the oil separation products that we sell, are you know, going to turbines or people that we had previously thought of.

So there are some knock on benefits but I'd say grossly, predominantly the lion's share is friction control.

Peter Thompson: Perfect. Thanks so much and a great quarter you guys.

James O'Leary: You're welcome, thank you very much. William? We got time for one more if we got one.

Operator: Absolutely. We'll take our next question from Richard Marshall – Longbow Research.

Richard Marshall: Hi good morning.

James O'Leary: Hello Richard. How are you?

Richard Marshall: I'm OK. Just a quick one on the wind power. What impact has the uncertainty of the PTC credits had on wind orders to this point? Has it seen either any acceleration in orders or any cancellation possibly there?

James O'Leary: I would say that no impact whatsoever. Our customer's – our customer's a turbine manufacturer, his customer is the person who's simply utility putting up to own or operate the wind farm. And these guys have booked out through '09 and now some cases into '10.

I'm respective of PTC and I believe the contracts are written in a fashion that addresses the (cancelability) on those types of issues. So PTC has had no impact now going out for at least two to three years. We've seen no cancellations; we've seen an acceleration in demand. I would say

the current state of that issue – it's been passed through senate, has to get through congress, I think, you know, for a politician to say they think it's a bad idea is, you know, arguing for spousal abuse or kicking your dog, I just don't see that as being as a issue. You know, there are competing – there are competing issues as far as other uses of energy. Coal obviously is a big political issue. And you know, given the – it has an alternative to wind, we have to be recognizing that.

But today different than the last bust, is new portfolio standards and most of the states, over 50 percent of the states, a number of companies have, you know, imposed upon their suppliers carbon emissions audits, and carbon emissions expectations. Last week, you know, one of the body's ((inaudible)) said that carbon emissions in 2007 and the early part of 2008 was dramatically worst than they expected. So you know, there's nothing about the macro back drop that tells us that there are going to be issues with supporting wind energy, particularly off a ridiculously small base. (and) extremely large country like the United States. That would play out even more so, if you look at China and India. I think we'll see a lot of that at the Olympics this year.

Richard Marshall: OK. And looking at the big wind order that you had, the $64 million order, is that with the new customer or is that with your existing customer base?

James O'Leary: That would be within our existing customer base.

Richard Marshall: OK. And can you just quickly give us an update on the capacity expansion in Mexico and how that's going?

James O'Leary: Pretty much going exactly how we've talked about. By the end of the year we'll be at a run rate of 125. So that will be an excess of a hundred million, as we go into the first quarter of next year including Avon. I think our overall capacity will be closely to 150 million, it's going

exactly as we talked about and – you know, we're looking at additional opportunities to enhance and expand that. But it will be based on demand as we go, and demand continues to get stronger.

Richard Marshall: OK. So there's no change to the forecast for wind sales, 80 million this year, 130 million next year, is that correct?

James O'Leary: That's what we said before, that sounds right.

Richard Marshall: OK because I just heard you throw out 150 million.

James O'Leary: That's capacity.

Richard Marshall: OK. All right and just one quick thing on the velocity controls, how much – I mean you mentioned foreign currency, but you didn't really quantify it, can we get a quantifiable number on that one?

James O'Leary: Sure.

Ken Crawford: Yes. That segment itself on the top line it would have been about a million and on the operating margin, it would've been about half of that. And on a consolidated basis, you basically double those two numbers. Two million and a million.

Richard Marshall: OK. Great and just so we understand better, the velocity controls, can you tell us a little bit about the end markets that are driving that if they're specific the ones that are really (homing) especially overseas.

James O'Leary: Well it's – it is industrial capital spending, it's for presses, these are industrial shock absorbers, velocity control products including hydraulic dampeners, gas springs, and the end markets including (virtually) every aspect of capital spending continues to be strong.

And we're holding our breath waiting for it to slow down as well, but this was the best quarter our North American operations have had in a while. And we think it really is execution. You know, we think we're out performing a number of people in the market place.

Whether or not we're taking share – you know I can't give you an exact number on that, because there's a limited number of competitors. But I think we're out executing people in North American. Now in our European operations, you know, all the industrial numbers particularly those that are Capex driven still seem pretty strong. So all still good?

Richard Marshall: Great. All right, that's all I got. Thanks.

James O'Leary: You're welcome, thank you. Hey William if we have anybody else, hold and we'll take one more, otherwise I think it's maybe time to kill it. Do you have anybody else?

Operator: We'll move to our final question from Tim Curro – Value Holdings.

Tim Curro: It was pretty much answered, but regarding the share repurchases, you've averaged about 7 million a quarter for the last few quarters, should we expect that expenditure to increase given your earlier comments regarding the convert?

James O'Leary: Well I think we said, in the seven-ish – well, it's been seven, but we've talked about this as a predominant use of free cash flow, given the size of the cash on the balancing – I think seven is a minimum and you may see a bit heavier but that's a board decision, and we talk about it. At least quarterly.

Tim Curro: All right. Thank you very much.

James O'Leary: You're welcome. Thank you. William?

Operator: Yes sir?

James O'Leary: I think we're going to call it a day.

Operator: That concludes our conference for today, we thank you for your attendance, and have a nice day.

James O'Leary: Guys, that you very much. And thank you for attending.

END