

**KAYDON CORP**

**Moderator: Rick Mosteller**  
**February 23, 2009**  
**10:00 am CT**

Operator: Good day everyone and welcome to today's Kaydon Corporation conference call.

At this time, I'd like to turn the call over to Mr. Mosteller. Please go ahead.

Rick Mosteller: Welcome to the Kaydon Corporation Fourth Quarter and Full Year 2008 earnings conference call.

Before the conference begins, the company would like to make the legal disclaimer that certain information in this formal discussion and that may be included in the question and answer session is forward-looking within the meaning 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 statements made are reasonable, actual results could differ materially since the statements are based on the company's current expectation and are subject to risk and uncertainties beyond the control of the company. Listeners are cautioned to refer to the company's 2007 Form 10K for a list of factors that could cause its results to differ from those anticipated in any forward-looking statements.

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

During this conference call, Kaydon spokespersons will refer to certain non-GAAP measures. To assist you in understanding these non-GAAP measures as well as to comply with SEC requirements, the company has included in its press release a reconciliation of these non-GAAP measures to the most directly comparable GAAP measures.

Today's conference is being recorded. Now, I would like to turn the call over to Mr. Jim O'Leary, Chairman and Chief Executive Officer of Kaydon Corporation.

James O'Leary: Thanks Rick, and thank you all for joining Rick, myself and Ken Crawford, our Chief Accounting Officer this morning to review our fourth quarter and full year results.

First, I'm going to commit to you that our comments - our prepared comments will be considerably shorter than usual. I wish I could commit to you that they would be sweeter but, unfortunately that's not the business environment that we're operating in.

They will be shorter for two reasons, number one we released our results on a preliminary basis in order to accommodate some presentations we had last week so really there's nothing in here that's new - a little bit expanded, a little bit more segment data. And we will be putting our 10K out shortly so obviously be on the lookout for that. I'd also encourage you to take a look at our Website or we filed our 8K last week, the presentation that we gave that way you'll have kind of the complete compendium of data.

Our remarks will be a bit shorter because there's nothing new relative to a week ago, a little bit more expansive.

The other reason our commentary will be a bit shorter is not only is there nothing new from a couple of weeks ago we've been talking about a slowdown probably from as early as June and I promise you I take no satisfaction on maybe having been early in talking about this but when you look at when people were discussing when a recession may have begun, I think the pundits now say it could be as far as two or three quarters ago, which is about when we saw things slowdown.

In fact, we probably saw that as early as June, our book and ship business stand a bit softer and the last two quarters we've been talking about really two things which is direction and magnitude and we'll talk a little bit about a third today which is direction, magnitude and duration. But, the things we're seeing today are directionally consistent with what we've talked about on the last few calls and released earlier last week.

The magnitude depending on the business segment and your perspective arguably a little bit worse or a little bit better. Again, I think that depends on business unit, business end market and in totality I'd probably say a little bit worse in terms of magnitude.

Duration, we can talk about some of the assumptions we're planning our business for, for the upcoming year but duration is obviously the wildcard I think everybody in business and in the investment business is wrestling with today.

We'll give you our thoughts but we won't be changing our policy on guidance, particularly when it seems like more companies are pulling it rather than giving more. We will be expansive in our perspective on what we are doing to prepare ourselves for any eventualities which I think is the more critical thing at a time like this. Now, in to the prepared remarks.

While fiscal 2008 was a record year in terms of both sales and EBITDA and I again, can promise you it sure didn't feel like a record year, we did see business conditions weaken as the year

progressed affecting each of our businesses. In general recessionary conditions we saw as early as June spread and grew in intensity as 2008 went on.

This was exacerbated by a number of things including dollar strengthening particularly against the British pound which negatively impacted both export volume and ((inaudible)) related foreign results. Also, interest income declined to negligible levels due to the global flight to safety consistently impacting EPS comparisons. Remember, we carry well over \$200 million of cash and when you compare year-over-year the decline in interest rates had a significant impact on interest income and therefore reported EPS.

Sales increased 7% to a fourth quarter record of \$132.4 million. Operating income was \$22.4 as compared to \$32.2 million in the prior year's fourth quarter which if you recall included a \$5 million gain on the sale of a component of our reporting segments. Fiscal 2008's fourth quarter operating results included about \$1.3 million of due diligence costs which were written off on unconsummated transactions and an asset impairment.

So, as to not repeat these items I'll just state that operating income, EBITDA and EPS comparisons for the fourth quarter and the full year are all impacted by these discrete results and we'll take you threw them one last time before the call is over. But, fourth quarter and full year both '07 and '08 are impacted by the \$5 million last year gain and the \$1.3 million of write offs and impairments this year.

EBITDA, a non-GAAP measure was \$29.6 million in the fourth quarter of 2008 as compared to \$37.9 million last year's fourth quarter. EBITDA for the full year 2008 was a record \$132.9 million as compared to \$132.5 last year. Gross operating and EBITDA margins were all negatively affected by changes in product mix largely due to declines in higher margin industrial business and offsetting increases in lower margin businesses.

Also, with the large drops in volume, the fourth quarter was particularly impacted by loss absorption and inefficiencies in certain of our plants particularly those are book and ship which were below optimal capacity levels.

Selling, general and administrative expenses were \$23.7 million or 17.9% of sales in the fourth quarter of 2008 compared to \$16 million or 13% of sales in the fourth quarter of 2007 almost entirely due to the absence of the \$5 million gain on sale recorded last year at this time and the previously mentioned costs incurred this quarter of \$1.3 million.

Excluding these items SG&A on a non-GAAP basis would have been \$22.4 million or 16.9% of sales as compared to \$21.1 million or 17.0% of sales last year. Contribution from interest and investments was \$4.3 million lower than the prior year's fourth quarter or 8 cents per share which included a \$1 million pre-tax loss of 2 cents per share on restricted investment we've talked about before and which Ken will describe in more detail in a few minutes.

The effective tax rate during the fourth quarter was 37.5% compared to a 32.6% rate in last year's fourth quarter which again Ken will discuss in more detail in a little while. Net income for the fourth quarter was \$13.8 million or 41 cents per share on a fully diluted basis as compared to \$22.7 million or 70 cents per share on a diluted basis last year. Again, all of the items affecting comparability previously mentioned occurred in the fourth quarters and full fiscal years respectively of the last two years.

Now, let's review segment operating performance starting with friction controls, our largest segment. Friction controls sales increased to \$85.8 million or 12.9% when compared to the fourth quarter of 2007 as we saw higher demand for specialty bearings utilized principally in the wind energy, military and heavy equipment markets. This year also includes a full year sales of Avon as compared to just two year sales last year - excuse me, two month sales included in the fourth quarter of last year.

Sales of the specialty machinery business and the semiconductor markets did decline significantly as did most sales to North American distribution and for exports. Also, while sales for spilt roller bearings were higher in local currencies, namely the British Pound, they declined when turned in to US dollars due to the steep drop in that cross rate in the fourth quarter.

Fourth quarter of 2008 operating income was \$17.7 million which decreased from the \$25.3 million recorded last year largely due to the absence of the \$5 million gain. Also, operating margins declined due to product mix shift, loss absorptions and the absence of gain.

While wind energy and military remain strong relative to last year, their contribution did not offset softness in our higher margin end markets. In particular the industrial machinery and export businesses in which orders are often booked and shipped in the same quarter slowed from June on in 2008.

Also, as we have discussed before, within the military business we've seen a continued shift from higher margin aerospace business to lower but still high margin but lower relative margin on vehicle business. Wind energy sales totaled \$24 million in the fourth quarter 78.8% higher than in the prior year's fourth quarter.

Full year 2008 wind energy sales totaled \$80.5 million compared to 2007 sales of \$32.9. The growth in this business reflects the investments we've made over the past few years and the business we believe will be strong for the long term.

Moving to velocity controls, fourth quarter 2008 sales of velocity control products totaled \$13.8 million as compared to \$15.6 in the prior year's fourth quarter. North American industrial ships were lower than the prior year's fourth quarter due to the severe industrial slowdown that grew as the fourth quarter progressed.

Operating income declined to \$1.8 million due to lower sales, cost to exit a smaller facility after our expansion to a larger German facility and increased selling, general and administrative costs associated with our expanding in to Asian markets. Those two items costs in Germany and the expansion in to some Asian markets were about \$1/2 million between the two.

Fourth quarter operating margin was 13.4% compared to 21.9% in the prior year's fourth quarter mainly due to the items just noted and due to loss absorption accompanying the drop in volume we saw in the fourth quarter.

Now, moving to sealing products, sales of sealing products were \$11 million compared to \$11.2 million in the fourth quarter 2007. Sales of sealing products declined as lower volume which was only partially offset by higher pricing.

Operating income declined to \$900,000 due to lower volume and an \$800,000 impairment on property and equipment. The asset impairment was associated with the initial stages of our new leadership team's effort there to adjust the overall capacity of the business to the current environment and reviewing where we should and how much we should have for the longer term.

In our other business segments sales of the company's remaining businesses equal \$21.8 million during the fourth quarter of 2008, an increase of \$800,000 in the fourth quarter of the prior year resulting from higher demand for liquid and air filtration products. These increases were partially offset by reduced volume and lower prices principally from metal alloy products. Operating income was \$3.1 million in the fourth quarter of 2008 as compared to \$2.9 million in the prior year's fourth quarter.

Talking a little bit about order entry and backlog and where we stand as of today. Order entries during the fourth quarter of 2008 totaled \$90.5 million compared to \$118 million in the prior year's

fourth quarter. Order entry declined in the fourth quarter as customers reacted to adverse macroeconomic conditions. December in particular was slow as customers pushed out both new orders and receipts of inventory during the last half of that month.

We've also responded to a request from our customers to adjust shipping schedules as their end users are reacting to the global financial crisis as well. As I noted last quarter, much of our near term planned wind expansion was booked at the end of the third quarter. We expected and did see a drop in new orders as we discussed then. Wind backlog today stands at about \$150 million.

The global macro economic weakness and conditions in the credit markets exacerbated this, causing customers across all of our markets to proceed with extreme caution in this environment. Global actions taken recently in the United States and internationally to ease the credit markets and stimulate economic activity may take some time before the benefits of those actions will be felt by the company and its customers.

We completed 2008 with backlog totaling \$312.6 million as compared to \$238.9 million at the end of 2007. Backlog again includes orders expected to be shipped over the next six quarters. As we note in our press release we expect shipments and as a results revenues and earnings to be more weighted towards the latter half of 2009 than in past years as the beginning of the year is expected to be the most challenging quarter.

As fiscal stimulus takes effect and business conditions and credit markets improve, we expect to see some stabilization towards the latter half of the first half of this year, so the latter half of the second quarter and some improvement thereafter.

Ken, I'll turn it over to him to discuss some financial items and then I'll wrap up and then turn it back to you for questions.

Kenneth Crawford: Thanks Jim and good morning everyone. During the fourth quarter of 2008 we incurred a net loss of \$300,000 on our investments. This included realized losses of \$200,000 on the sale of a portion of a restricted investment and recognized losses of \$800,000 to reflect the lower net asset value of the remaining investment as credit market conditions have caused the value of this investment to continue to decline.

These losses were only partially offset by the \$700,000 earned on our average investable balances of \$249.3 million. Overall, during the quarter excluding the investment losses we earned about 1% on our investments.

During the fourth quarter of 2007, we earned approximately 5% on average investible balances of \$307.2 million which generated \$3.9 million of interest income. The lower average investable balances resulted from our capital expenditure program; increased working capitals to support sales growth; our stock repurchase actions; the enhanced dividend and the purchase of Avon.

The lower interest rates were caused by lower rates available on the market and by proactive steps taken by the company to protect principal and liquidity. Interest income is also down sequentially as during the third quarter of 2008, we earned 2.2% on average investable balances of \$269.2 million. These items resulted in a reduction of \$4.3 million in fourth quarter interest income compared to the prior fourth quarter and that was equivalent to 8 cents per share on a diluted basis compared with last year's fourth quarter.

At the end of 2008, our investible balances totaled \$237.9 million which is \$63.8 million lower than at this time in 2007. While our investable balances continue to provide us with significant liquidity when liquidity is at a premium, we are currently earning very little interest on these balances due to the global market conditions. We expect that interest income in the first quarter 2009 will be negligible compared to \$1.9 million of interest income earned during the first quarter of 2008.

At December 31, 2008, our net position held in the restricted investment totaled \$4.9 million. This enhanced cash investment is being liquidated by the fund issuer. In January of 2009, we received an additional distribution of \$800,000 at approximately book value and now the remaining book value of this investment is \$4.1 million.

Our current cash and cash equivalent investments today are principally in money market funds that invest solely in short term treasury securities. This provides the highest level of safety available, although the returns are currently negligible.

Interest expense during the fourth quarter 2008 totaled less than \$100,000 representing the amortization of fees on our line of credit as we completed the conversion of our debt in to equity during the third quarter of 2008. Interest expense in the fourth quarter of 2007 was \$2.4 million. The conversion of the debt and the related reduction in interest expense has no impact on diluted earnings per share due to the accounting treatment of the underlying convertible debt instrument.

The effective tax rate during the fourth quarter of 2008 increased to 37.5% compared to 32.6% in the prior fourth quarter. The fourth quarter tax rate was unfavorably impacted by the reduction in the federal tax benefit of the domestic production activities deduction due to lower taxable income caused in part by a \$11.9 million contribution to our qualified pension plans made late in 2008.

The fourth quarter 2007 effective tax rate was favorably impacted by the tax benefit associated with the company's disposition of an idle facility and by adjustments to the company's deferred tax accounts.

Net income for the fourth quarter was \$13.8 million or 41 cents per share on a diluted basis compared to fourth quarter 2007 net income of \$22.7 million or 70 cents per share on a diluted basis and again, each period includes the items that Jim has mentioned previously.

EBITDA is a non-GAAP liquidity measure we consider an important indicator of financial health. During the quarter EBITDA was \$29.6 million compared to fourth quarter 2007 EBITDA of \$37.9 million which included the aforementioned gain on sale. EBITDA for the full year 2008 totaled a record \$132.9 million compared to 2007 EBITDA of \$132.5 million which included the gain.

Free cash flow is another non-GAAP liquidity measure we consider to be an important indicator of the company's health as it reflects our ability to generate cash and access to both growth and maintenance capital investments.

During the fourth quarter, the company's free cash flow was a net outflow of \$5.5 million. This is due to \$13.7 million of capital expenditures and the \$11.9 million contribution to partially fund our qualified pension plans.

Capital expenditures in the last two years have totaled \$59.5 million and \$54.1 million respectfully due principally to our wind energy expansion. We expect capital expenditures to drop to approximately half that level in 2009 as most of the wind energy investment is now behind us.

Again, EBITDA and free cash flow should be viewed as supplemental data rather than as substitutes or alternatives to the comparable GAAP measure. We've included in our earnings release a reconciliation of these metrics to the most comparable GAAP measure for your reference. Cash and cash equivalents plus short term investments totaled \$233 million at the end of the fourth quarter 2008 compared to \$287 million at the end of 2007.

The company now has no outstanding debt due to the third quarter 2008 completion of our debt conversion. Outstanding debt at the end of '07 was \$200 million. During the fourth quarter we paid dividends of \$5.7 million or 17 cents per share. We repurchased 483,700 shares of common stock for \$14.1 million and we invested \$13.7 million in net capital expenditures.

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

James O'Leary: Thank you Ken. While the current economic environment remains challenging, we've taken several steps to improve our results and position us for the longer term. These actions will allow us to take maximum benefit of the eventual improvement in business conditions.

Notably, we've frozen executive salaries; eliminated across the board salary increases; closed or eliminated a number of benefit and profit sharing programs; and significantly curtailed both temporary labor and overtime.

We've also implemented targeted staff cuts at most locations. Finally, we've developed additional profit protection programs should conditions weaken further.

So, to sum it up, everywhere there's a variable cost or a proactive step we could take to protect profitability in the current environment, we've done so. And, we're looking at additional measures should this take another leg down so that we're ready with the Plan B should it be necessary.

These measures together with our strong balance sheet and ample liquidity should allow us to successfully navigate these challenging times. With no outstanding debt and \$233 million at year end of unrestricted cash, we are exceptionally well positioned for the longer term.

I'd like to thank each of our Kaydon employees for their efforts in 2008 and respectively for their efforts in what's likely to be a very challenging 2009.

Operator, that concludes our formal presentation and we would be glad to take questions.

Operator: Thank you so much. At this time if you would like to ask a question, you may do so now by pressing the star key followed by the digit 1 on your touch tone telephone. If you are using a speakerphone, please pick up your handset or depress your mute function to allow your signal to reach our equipment. Once again, that was star 1 to ask a question.

And we'll take our first question from Peter Lisnic with Robert Baird.

(John): Good morning, it's actually (John) ((inaudible)) for Pete.

James O'Leary: Hey John.

(John): When you guys kind of talk about that Plan B or the things that you have still to pull in terms of the levers. What relative to the environment today has to happen for you guys to feel the need I guess to kind of go forward with those? I mean is it something where you're reassigning every month or do you need to see another step down on industrial demand to kind of make you pull the trigger there?

James O'Leary: We're assessing it every month. If you look at our backlog relative to pretty much any recession Kaydon has gone through before and really relative to the great many industrial companies out there, the backlog looks pretty good. As we mentioned in our remarks and in our press release we are working with customers on push outs and the likes. We're working with them to restructure around their needs.

Every month we're going over that, every month we're going over headcount relative to shipments expected over the next quarter and if we find out that push outs and retiming of shipments are really effectively cancellations, we would take down headcount in a number of locations where we have not done it yet because we need to meet the demand over the next two quarters. That's really an every single month action, (John).

If you saw a big, big step down meaning the credit markets not only don't get better, they worsen, customers just out right cancel and you find out we haven't taken a gradual weakening, it's a big step down we would be probably a lot quicker on across the board cuts. But right now our backlog and our expected shipments over the next two quarters probably mean we should stay our hand because we don't want to disappoint customers who may have business.

(John): Okay, that's helpful. And then kind of switching to the wind outlook here, I assume that would be one of the businesses you're talking about where the year has become kind of significantly more back half weighted. Could you just talk maybe as you look a little beyond kind of the near term financing pressures there what the outlook would be for 2010? And kind of with the production tax credit have been extended are your customers maybe a little bit more bullish about the long term outlook?

James O'Leary: We're not going to talk about 2010 because I think we're on quarter-to-quarter and as you just asked us before a month-to-month assessment. So, 2010 other than we expect the business to be there and our capacity is depending on where the prices are between \$180 and \$200 million.

We're not moving forward with additional capacity right now as we talked about two quarters ago but, if 2010 is anywhere close to where it was to have been even a few months ago we would be hopeful that we could come close to selling that out than I think we could have said a month ago.

I'm kind of picking those dates because I think they're important. A month ago I think the sentiment was terrible. There was real concern over what would go through in the stimulus plan. Customers were appropriately nervous and we were working with them on the action steps they have to take in order to protect their business but not accept large amounts of inventory until they know their customers are going forward.

A couple of days ago the administration signed in to legislation a stimulus plan which was extremely beneficial to our customers and therefore to us. A three year PTC which can be turned in to an investment tax credit a year ago I would have said that's close to the holy grail, the holy grail being the national renewable portfolio standard. That is an extremely powerful important thing.

A couple of customers we have talked to have said that's pretty close to everything they would have liked to have seen in the stimulus package. The challenge still and there are some grants and I would be out of my element now because I'm still waiting to see how the actual granting mechanism will work to get financing going in the short term.

But I think the big challenge is saying business will be back to where we at one point expected it to be over at least the next quarter and a half probably as much as the first two quarters of this year, is the need for the credit markets to really return to normal.

So, the PTC extended for three years, able to be used as an investment tax credit which is a powerful mechanism for spurring investment. I think an administration that is continuing to be supportive of what had been previously been pointed out to be one of the things that I think in four or eight years they'd like to point to as the center piece of their administration, I think all those things are good but it will be nice to have a credit market and some healthier, better functioning capital markets.

I don't want to go too long on this but T. Boone Pickens was on TV again this morning strongly advocating wind energy, talking up the Pickens Plan with a number of other business leaders and it feels not as good as it did two quarters ago but, it feels a lot better than it did two months ago and we're watching it month-by-month.

(John): Okay, thank you for that. I'll get back in queue.

James O'Leary: Okay, you're welcome.

Operator: And we'll go next to Edward Marshall with Sidoti & Company.

Edward Marshall: Good morning guys.

James O'Leary: Hey, how are you?

Edward Marshall: Good. I know you said orders were down for the wind in the fourth quarter, did you actually have a number? Did I miss it?

James O'Leary: No but, it was negligible.

Edward Marshall: The percent of the business that's tied to the book and ship business on a yearly basis, do you know what that is? Have you broken it out before?

Kenneth Crawford: We estimate that our book and ship business is about \$25 to \$30 million a quarter if that's what you're asking.

Edward Marshall: Right, that's exactly what I'm asking. Per quarter?

Kenneth Crawford: Per quarter until it comes out of backlog and currently it's coming out of backlog at about 30% to 35% of our beginning backlog so the rest is \$25 to \$30 million which would be book and ship business.

James O'Leary: And Ed, obviously that is an estimate because some of our business and I think the one I'd point to which is illustrative particularly if you're new to the company as I know you are, if you look at our velocity controls business, it's not all book and ship but they operate off a much smaller backlog of a much longer lead time backlog than some of our other businesses and most if it goes to industrial distribution.

If you look at how quickly that business dropped off that many not definitionally be book and ship as we refer to the stuff in friction controls but its awful close and it's probably the most economic activity sensitive business we have and I think the fourth quarter demonstrated that.

Edward Marshall: I see. Have you been seeing the benefits of lower material costs flowing through the system yet for the model you have?

James O'Leary: We're starting to see it but I think it will probably be at least a quarter or so until it starts to hit the P&L in a meaningful way. You have to remember the one thing which we've talked about in the past two is we're starting to see it but in a major part of our business and the most raw material intensified part of our business which is the wind energy and the heavy equipment businesses.

We do have pass-throughs where we got benefit on the way up or price relief on the way up of cost increases, we have to give a good deal of that back on the way down so it will not move in lock step. We are getting relief, we're getting it on parts of the business but our most raw material intensive business is the one where we have pass throughs and it operates both ways.

Edward Marshall: I see. So you are feeling the impact of the price squeeze now push back from the customers?

James O'Leary: No, we're seeing the benefit of cost decreases in certain parts of our businesses. And it's not a push back, these are contractual obligations where they gave us relief on the way up and we passed on the relief on the way back.

Edward Marshall: I see. And then because the opportunity of holding cash is so high or apparently so high on a year-over-year basis, uses of cash outside of the obvious share repurchase and dividend?

James O'Leary: Well the cost of holding it are high but the cost of losing it if you spend it on the wrong things is pretty high too.

I don't feel as terrible with 1% as I would if I didn't have any cash and I was trying to put together a bank syndicate in this environment. The uses, we expect to see our capital expenditures to go down by at least 50% so if we were at \$60ish last year we'll be in the \$30ish ballpark. That is also subject to scrutiny also, if business conditions soften you'll see more free cash flow come out vis-à-vis reductions in CapEx. But, we'll still spend on maintenance and new products.

We've got a project as we mentioned in our prepared remarks that we're deploying in Asia, both China and India which the next couple of quarters is going to dictate where we're going to be in the next couple of years so we're continuing on things like that.

You saw a stepped up repurchase program in the fourth quarter, probably our most in terms of shares and dollars, probably our most aggressive share repurchase activity in a while. I think you'll continue to see that. We're not going to go out and spend everything on shares.

I can remember two years ago people advocating taking out our convert which then would have been in the 50s or 60s, other people saying we should buy every share back at 40s, other people saying we should buy back every 30s. In an environment like this I think there is a high value to

strong steady, be in the market, be very price sensitive and leave yourself the optionality for when business comes back.

We are very aggressively looking at acquisitions but again, the same way I'm price sensitive on our shares, I'm price sensitive on acquisitions particularly in this environment. The \$800 or \$900 of the \$1.3 we've talked about was for due diligence costs where I'd say we got closer than we have in a while on some deals that I thought would have added considerably to our long term value but in this environment and without a financing market unfortunately it wasn't meant to be so we'll continue to look at share repurchases.

We have a dividend that is higher than it's been in 10 years, I cannot commit to you what we'll do at the next meeting, that's the board's decision but obviously we have a dividend that's a use of cash as well. I think all those things together mean we're going to continue to do everything to satisfy as many of our constituencies as possible.

We're not going to do any one single thing that takes away the optionality of satisfying most of those constituencies but, we're free cash flow positive at a time like this and we've got plenty of places to use it. I would expect we could build some cash if the acquisitions or if our prices trade at a range where we'd rather hold on to some dry powder.

Edward Marshall: Excellent. Thanks guys, thanks for your comments.

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

Operator: And we will go to our next question from Eli Lustgarten with Longbow Securities.

Eli Lustgarten: Good morning.

James O'Leary: Hi Eli.

Kenneth Crawford: Morning.

Eli Lustgarten: Having cash is nice in this environment, I guess.

James O'Leary: It's good in every environment but especially good in this environment.

Eli Lustgarten: A couple of technical questions, you put \$11.9 million in to the pension fund driving the tax rate up. The tax rate for '09 and what about the pension, where does the pension stand at this point for the year? You did a contribution in '09.

James O'Leary: I'm glad you asked about the pension. In fact there are two - we'll answer your question directly, but two things you guys should think about in modeling and as I pointed out. We're not going to change our policy on guidance but your assumptions on depreciation remember we specifically talked about depreciation in the press release for a reason.

EBITDA and EBITDA margins will probably be more important as you guys look at how quarters roll out at least the next four because the depreciation is considerably higher now that all the equipment is back in service. That's a fixed cost so you'll probably see a smaller profit contribution on comparable shipments in the first and second quarter than you had historically.

On pension, we put \$11.9 million in. We're looking at putting possibly a few more dollars in to fully fund and to stay compliant on a regulatory basis. But, the pension expense next year will go from flat to a contribution in '08 to probably about a \$6 million P&L hit going forward. That's not unusual for companies that have defined benefit plans but it's bigger than it's been in probably three or four years.

We were fully funded last year which basically took away the full contribution but the combination of market losses and we were about even the benchmarks - with all our benchmarks, a little better than a few but I'd say even across the board. That coupled with one of the biggest things as well, in a low interest rate environment you're accumulated benefit obligations go up considerably so those things together mean that we'll have a pension drag for a good part of the next year absent a miraculous recovery of the stock market.

We may put a little bit more in but one of the things we did recently was we closed our defined benefit plan to new entrants. We've put in a defined contribution plan or expanded a defined contribution plan with no match which I think is responsive to what a lot of other companies we do where we compete with them for labor. We're looking at ways to neutralize that going forward but you will see a little bit more of a pension drag beginning next year than you have at least the last three years.

Eli Lustgarten: The tax rates, do you have any guidance on the tax rate for '09 at this point?

Kenneth Crawford: 35% to 35 1/2%.

Eli Lustgarten: 35, 35 1/2 - now, as far as wind shipments to, you did \$80.5 million. Based on the stretch outs and where you sit today are we sort of looking at a flattish shipment year in wind? Is that probably the best guess we can hold at this point or is there still some growth?

James O'Leary: We'd expect there to be growth but I'll give you but I'll give you a better guess probably next quarter when I'd have a better educated guess. Flat would be disappointing, it's not going to be as good as we thought three months ago but we still hope to do a bit better than this year.

Eli Lustgarten: Okay, can you talk about the conditions you're seeing in the first couple of months of this year? I just got off another conference call and they were down 30% in the first two months. Are

we seeing the typical 20% to 25% declines in volumes the first two months of the year that we've seen across the board?

James O'Leary: It's a big higher than that and a lot of it has to do with we started off weaker in January because nobody was ordering anything. We started it off hatefully bad in the early part of the year. It's starting to get better but we're no better than that comment you just mentioned.

I don't want to give you much more color than that because I'm not too sure that we've got enough data for it to be representative particularly we do have a few segments which we talked about with the stimulus plan that are starting to feel a little bit better. But I don't think there's enough data to say we're any better than the statistic you just threw out.

Eli Lustgarten: Is there anything going on in pricing other than pass through and the pass give backs of the indexes at this point? Is the rest of pricing relatively stable or is there any instances of a change going on?

James O'Leary: There's a couple of instances which are anecdotal where we've had people come back to us on price. Remember, we don't really have an across the board price increase other than one or two lines of business where we're going out to distribution for regular price increases. Most of our stuff is either customized or sufficiently different where the concept of price increase relative to negotiated value added is clearly distinguishable.

So, I wouldn't say we're not getting price but we are anecdotally particularly in heavy equipment and a few markets. You guys read the same headlines as us, we've had people come back to us but nothing I'd say is across the board and nothing that is meaningful at this point but, that's mid February.

Eli Lustgarten: All right, thank you.

James O'Leary: You're welcome, Eli. Thank you.

Operator: And we'll take our next question comes from Walter Liptak with Barrington Research.

Walter Liptak: Hi, thanks, good morning.

James O'Leary: Hi Walt.

Kenneth Crawford: Morning.

Walter Liptak: So you're not giving guidance but you are talking about the backlog and when that ships. I apologize, I got on the call late but you're saying 25% to 30% of the backlog should ship in the first quarter, is that right?

Kenneth Crawford: No, 30% to 35% of the backlog we find currently is shipping in the next subsequent quarter. I said that book and ship business typically runs in range of \$25 to \$30 million.

Walter Liptak: So, you add the two together to get to a revenue guidance.

James O'Leary: We are not giving revenue guidance and we're not changing our policy. In fact, I think most people are pulling guidance. We'll continue to the same with what we've historically said, the 30% to 35% of backlog shippable, some of that would include things that may be book and ship. You can't take to two add it up and come up with the revenue guidance. If you do, it's your number.

Walter Liptak: Okay, I hear you. I understand. The swing - the (delta) in pension of \$6 million would that flow through each quarter or is that front end loaded?

James O'Leary: Over the year.

Walter Liptak: Over the year it will flow through each quarter? Okay, in the backlog, have you given any composition of what the backlog looks like? Of the \$312 million how much is wind related, defense, aerospace, etc.?

James O'Leary: We told you that \$160 is wind and consistent with prior year we don't break it down beyond that.

Walter Liptak: Okay, okay. Thanks very much.

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

Operator: And we'll go next to Peter Thompson with Coho Partners.

Peter Thompson: All of them have been answered, thanks a lot.

James O'Leary: Thank you Peter. I like that; we told you we were going to be short and sweet. Peter was short and sweet.

Operator: Once again, everyone, that is star 1 if you have a question. If your question has been answered, you may press the pound key to remove yourself from the queue.

We'll take our next question comes from Richard Marshall with Longbow Research.

Richard Marshall: Good morning. Can you give us an update on your capacity additions in the wind business? Is that pretty much where you thought it would be at this point? Just kind of update us on that.

James O'Leary: Pretty much where we thought we'd be. I'd say done for all intents and purposes, done. Richard, if you took a look at the presentation we gave a week or so ago and compare that to prior presentations you'd see about \$8 million of CapEx fall from 2008 in to 2009, that's just timing as to when you cut the checks. The capacity is pretty much online, pretty much consistent with the spending, maybe a little better than what we expected.

This may be what you are referring to, more significant capacity expansions that we talked about as approved and we were working with customers on potentially going forward with in July or August on our conference call for the second quarter, all that's on hold until the business environment gets better, until our customers are back booking capacity expansions.

The next wave of capacity is absolutely on hold. The original capacity expansion is on track, pretty much up and running fully in the first, second quarter this year and we're standing fast until the business conditions improve.

Richard Marshall: So with respect to the original plan I guess would that be phase two or three? Can you kind of break that down? I don't remember exactly where - it seems like that plan may have shifted a little bit from the original. I think it was - it looks like from your chart like it was \$150 million in capacity roughly right now?

James O'Leary: That is exactly where the price past twos are. We'd ((inaudible)) at the \$140 or \$150 in the original guidance would have been \$180 to \$200 by the end of this year and whether it's phase one, two or three I think is irrelevant now because some of it has spilled in to another. The original capacity expansion is pretty much done beginning of this year.

Richard Marshall: Okay, great. Are you running at full capacity in those facilities?

James O'Leary: We are not full capacity until in to this quarter, beginning of next. But, based on the willingness of customers to accept deliveries, we are much further along than we were this time last year.

Richard Marshall: Looking at your wind orders, are you seeing any cancellations or postponements in your wind backlog?

James O'Leary: Yes, we have seen postponements. Whether they're cancellations; we've had changes in mix; we've worked with people on push outs and there's a couple of people that would have been new customers that we're keeping an eye on because they were new customers and new entrants to this market. But, we're working with everybody on what their response has to be to utilities and credit issues.

Richard Marshall: Is there any change in the geographic mix of that business? Is it still primary what was it half North America, a little more than half North America there?

James O'Leary: We've never said that because I don't know if we're smart enough to know that. Most of our shipments, most of our FOB points are domestic but the product has been ending up all over the world; 50/50 is not a bad guess. (SEC) transplants and a number of multinational players coming through the United States I think that would continue to be the case.

People making or continuing to make commitments to the North American market but whether or not they're turbines or ending up elsewhere or not I'm not sure they know until they're prepared to ship and we don't necessarily get that information on a real time basis.

Richard Marshall: Okay, great. Just the last thing, you've mentioned the stimulus package, do you have any estimate of what your exposure might be there?

Kenneth Crawford: Our exposure might be there?

Richard Marshall: What's the sales opportunity might be from the stimulus package?

James O'Leary: If the stimulus package gets things back to where it was three or four months ago, we'd be shipping all the capacity that we can which would be probably \$140 to \$160. And in a perfect year ago scenario would have been around \$180 with prices being the same.

But, I think that Eli asked the question, \$80 something is what we did this year, we probably expect to do better but unless business comes back to where it was three months ago, which is possible, but I don't think it's possible until back half of this year at the earliest because of credit conditions. Full capacity would be that slide where it shows us peaking out at \$180.

Richard Marshall: Okay, great. Thanks very much.

James O'Leary: You're welcome.

Operator: And we'll take our next question from Steve Barger with Keybank Capital Markets.

Steve Barger: Hey, good morning.

James O'Leary: Hey Steve.

Steve Barger: I know it's month-to-month on the outlook for the wind stuff but is it your sense that any competitors who may have had machine orders in queue to enter this business have been putting

capacity in place recently? And any idea of where we are in terms of capacity relative to megawatts that the industry can produce right now in North America?

James O'Leary: I'd refer you to the EER stuff which I think is being updated currently for the second question. On new capacity, nothing we haven't talked about before and nothing that one or two of our very good peers have also talked about recently.

Steve Barger: Okay, next question. Are any - the transactions that weren't consummated, are they off the table for good? Or, is there a potential for you to come back to them once the financing markets or the credit markets would loosen up a bit?

James O'Leary: I think they're all potentially things that could be resuscitated. You know, what happened at the end of last year and a lot of you guys know how these processes work. If you were out in the market, bankers took you out in June or July.

You were compared to a couple of notable small mid large cap companies like Kaydon that typically traded a very high EBITDA multiples. And by the time you got to where you had to make a decision are you going to proceed with selling your business, those multiples are down anywhere between, you know, 40% to 50%.

So, if you thought you were going to get sold at 10 times and you find out that the peer group that you went out to market on is based at five times, it's a big psychological impediment to go over. Coupled with the fact that without a financing marketing unless a business had no working capital needs, it would be kind of reckless of me to spend all our money and not have dry powder liquidity in case it does take another step down.

So, the absence of a credit market and the fact that I think sellers' shock over how big prices changed had a lot to do with it. I think two things have to happen now. You know, things have to

season a bit whether or not this is a new valuation paradigm for companies across the board or not, it takes a little while for that to settle in and for the M&A market to get going again.

I think absolutely critical to that happening whether prices are five times or ten times is there needs to be a credit market. We left everything on good terms. I think we handled everything with both the advisors and the sellers as gracefully as possible given that when you go in to a deal that you wanted to happen both buyer and seller but, it just wasn't meant to be. But, all those things are on good terms.

I do think it's going to take a little while Steve, for that to come back because a lot of people who did go to the market last year also thought they had to get something done even if at a lower price because they were concerned about capital gains. I don't think there's a real fear in this environment that there's going to be a capital gains increase of any significance any time soon.

Steve Barger: Right. Okay, that's great. Thanks.

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

Operator: And taking a follow-up question comes from Peter Lisnic with Robert Baird.

(John): Good morning again. Could you guys just talk a little bit about inventory, kind of in the system for you guys and how much you actually have to run your plants in the first quarter? It seems like kind of the back half of the year inventory crept up a bit and just kind of what are your thoughts there or do you have a working capital target for 2009?

James O'Leary: Well, they did creep up largely because of timing and deferred shipments at year end as we talked about the last two weeks people pretty much shut down. We have an internal target, we

don't provide that on these calls but a big focus is working that down and as we noted in our press release and in our comments, we're a bit under capacitized right now.

Some of our higher margins facilities which are typically book and ship are operating at less than optimal capacization. It shouldn't be a surprise to anybody. I expect that to persist at least through the first quarter or two until we see whether or not business resumes at reasonable levels.

(John): Okay, but based on what you're saying it sounds like your target is that inventory will be down year-over-year by year end?

James O'Leary: Absolutely.

(John): That's it; thank you.

James O'Leary: Less inventory is always our target.

Operator: And we'll take our next question which is a follow-up question from Walter Liptak with Barrington Research.

Walter Liptak: Hi thanks. Okay, I'd like to see I can get a little more clarity on the push outs that you talked about. You said that you're seeing some push outs with the wind customers. I wonder if there are other sectors or any other color you'd like to give on what other customers might be pushing things out.

James O'Leary: Wind and heavy equipment, those would be the two where we operate off of longer backlogs. More significant is the cessation of book and ship business. And on some of the other

stuff that is shorter backlog, the push outs are less significant or less magnitude in dollar terms than wind and heavy equipment.

But, that's where you have very long lead time, Walt. I think the more significant issue is just you have book and ship business that has slowed down, it slowed down in June and didn't pick up and got worse as the year progressed.

Walter Liptak: Okay, that's it for me, thanks.

James O'Leary: Operator, we're getting a little close. We'll probably take one more question if there are any and then call it a day.

Operator: And we'll take our last follow-up question comes from Eli Lustgarten with Longbow Securities.

Eli Lustgarten: Good morning again. Just two very quick questions.

James O'Leary: Longbow was all over this call today, Eli.

Eli Lustgarten: I'm sorry.

James O'Leary: Longbow is all over this call between you and Richard.

Eli Lustgarten: Hey, good companies deserve good attention.

James O'Leary: There you go; I like that.

Eli Lustgarten: The military business the shift towards vehicles has that business pretty well stabilized through the whole year or is there some shipment timing on that business also?

James O'Leary: There may be some shipment timing but the program that we're on which is MRAP and the programs which are being discussed which is MRAP Light, I can't point to what the new commitment on the part of the government is because I don't think they've articulated it.

But the reason I feel like it should be reasonably good and it could be some timing issues while the administration sorts through other priorities but with what sounds like a real commitment to Afghanistan and what's going to be a slow withdrawal, if there is a withdrawal from Iraq, with more Afghanistan commitment I think that argues that you're going to have a need for either MRAP, MRAP light is the one that's being discussed as kind of following up on that both of which have the same content for our products.

So, the vehicle business sounds like it is pretty good. It still feels like it is pretty good. I wish I could - well, I don't know if I wish because it would be an argument for a less safe world. The helicopter in the aerospace business which really carried us in '06, beginning of '07 is still at lower levels but it has been replaced with the vehicle business largely.

It is a very good program for us we expect it to continue and while there might be some timing issues everything the administration has said so far argues that you'll probably see that plateau at a reasonably high level.

Eli Lustgarten: One final question, you suggested the year is back end loaded. Should we be thinking whatever estimates we want to come up with that about a third of it is earned in the first half and two thirds in the second half? Is that the standard back end loading we're talking about?

James O'Leary: I think that would be pretty accurate. If I were giving you that estimate and I said, "Oh boy, you're going to have that much business in the back half of the year. And do you have a capacization problem?" meaning you couldn't ship it even if the business is there?

If you look at two thirds of any reasonable (estimate), if you look at two thirds of this year being in the back half we've already had a couple of quarters operating at that very high level so, you know, as long as demand is there and business comes back we should be able to do that.

But, I do think probably about one third, two thirds is not unreasonable and the reason I gave you some color on pension and depreciation before is because those shipping patterns probably argue for a little bit lighter profitability, only because you've got the fixed costs being earned evenly over the four quarters whether there was quarter, quarter, quarter, quarter shipments or one third, two thirds.

Eli Lustgarten: All right, thank you very, very much.

James O'Leary: You're welcome.

Operator: And with that, there are no further questions. I'd like to turn the call back over to you for any closing remarks.

James O'Leary: Operator, thank you very much. Thank you for all joining us on this call. We recognize these are challenging times and I just want to leave you assured that we're taking all steps necessary so that we're not only doing well during them or relatively well but we're positioning ourselves to do extremely well on the other side and we're hoping the other side is soon but my prognostication skills are no better than yours. But we're doing all the things we need on the variable costs and the long term fixed costs to position ourselves for then.

So operator, thank you and again, thank you for taking the time today.

Operator: Once again, this does conclude today's call. We thank you for your participation and ask that you have a wonderful day.

END