Graham Corporation
Annual Meeting of Shareholders Webcast
July 30, 2009

James Lines: Thank you, Carol. Thank you, Jerry. And good morning, everyone, welcome to the 2009 Annual Meeting for Graham Corporation. The agenda today will be a review of 2009 highlights. Jeff will review our financial performance. I'll touch on the markets and give an overview of the outlook.

2009 was a year of stark contrasts. The first half of the year was a continuation of strong demand and excellent financial performance. In the second half, we saw demand change abruptly downward while the Company still maintained a solid operating performance. I would like to acknowledge and thank our employees and the management team for the dedication and effort to continually make Graham a better company each day.

Our employees responded quickly when the markets changed abruptly and were disciplined and focused on delivering for the second half of the year a fine performance. While the top line and bottom lines were excellent, we also continued our cash management discipline. The Board of Directors in January initiated a stock repurchase program and also enacted a two-for-one stock split in October. We added Jeff Glajch to the leadership team. Jeff is a fine addition to the team. He is our Vice President and Chief Financial Officer.

Let me go into more detail on the highlights for last year. Revenue was over $100 million. We had record margins. Gross margin was approximately 41%, operating margin was above 26%, and we recorded record net income of $17.5 million. We also improved our cash management with our cash conversion cycle, one of our key business metrics, being lowered from 31 days at the end of 2008 to 17 days at the end of fiscal 2009. We accomplished these records through focusing on continuous improvement, having that become the Graham Way, striving for excellence, recognizing no matter how good we are, we can still become better.

Our capital plan. We've invested in a targeted way to expand capacity either through automation or through investments in our plants to create capacity to reduce lead time or improve the quality of our products and services. Importantly, to support our revenue and profit objectives, we had a disciplined sales management process and order selection criteria. To further expand the business, we effectively outsourced production last year. We effectively outsourced about 10% of our production. Also, we outsourced about 12% to 15% of our noncritical engineering, not our critical IP. We also enacted and implemented effectively supply chain initiatives to help control costs, and we focused on internal development within the organization to make Graham a stronger company and to prepare for its future.

We had a number of areas that we focused on strategically. One, it's very important that we recognize that Graham's markets are inherently cyclical. The energy markets are cyclical. They've had periods of ups and downs in the past, and we expect that to be the case going forward. So, managing growth from 2005 through 2009 was key; keeping our eye on how the Company wanted to be positioned going into a downturn. We did not see this downturn, but we recognized there would be a downturn at some point in our future, and we wanted to be prepared for it. We managed our growth thinking about variable costs rather than fixed costs, outsourcing, targeted use of overtime, the use of contract employees, and striving diligently to increase capacity, leverage the business, again, through our capital plan, through our process improvement initiatives, and through the employee development programs that we've enacted. All have delivered very beneficial results in 2009 and we will enjoy those results in 2010, 2011, 2012 and each year going forward. Again, a strong commitment within our Company to continually improve, strive for excellence, and recognize, as I said earlier, no matter how good we are, we can still become better.

Also, on the sales side, on the marketing side, focusing on where we believe the business will be in the future, Asia, in particular China, the Middle East, and South America. Our sales teams have spent a lot of time in those areas doing the important work of building relationships, understanding what's coming up in the pipeline, and positioning our Company to take advantage of those opportunities. And we did, in 2008 and 2009, enjoy benefits from that.

Also, as the markets changed at the midpoint of the last fiscal year, our management team responded very quickly to the change. We right-sized the Company to what we thought the demand would be in 2010 and have the right cost structure to remain profitable through the downturn, but keep a balanced approach, not just managing the business for 2010, but making sure we're keeping our eye on where we want to be in the future, five and ten years out.

Graham is and has been a global company. Although here in Batavia, where we've been for over 70 years, our brand is global. We're recognized around the world. Our brand stands for quality, reliability, and strong engineering excellence. As you can see from the geographic and industry mix of sales in the refining sector, it was largely international. Large orders were won throughout Asia and the Middle East, and there was some work won in the U.S.A. In the petrochemical markets, most of that work is outside of the U.S.A. Again, we're positioned to win in those markets, the international markets. We've won in China and North Africa, the Caribbean, and Mexico.

In power generation, we had a nice order for Turkey. The combined cycle power plant in Turkey is going through backlog now, and we supply a host of other end-use markets: edible oils, heating, ventilating and air conditioning, industrial gases. Those are mostly U.S. markets, but also they are international as well.

I'll turn it over to Jeff for a detailed discussion on our financial performance in 2009.

Jeffrey Glajch: Thank you, Jim. I do want to point out to everyone that this presentation is available on our website, *www.graham-mfg.com,* now as well as to look at in the future.

I'm going to just briefly go through a review of our financial performance over the past year and give you some indication of the trends we have seen. As you can see, Graham has grown over the past four years at an annual growth rate of 25%, growing from just over $40 million to our record level of $100 million in 2009. This growth was accomplished in many ways, but one of the things that we continue to focus on is how to continue to improve the productivity of the organization. As you can see, our productivity, as measured by sales per employee, has more than doubled during that time period from $172,000 per employee to more than $374,000. At the same time, as Jim mentioned, we focused significantly on our cash management. One area of our cash management is inventory turnover. Our inventory turns have doubled over the past four-year period also, from just under 6 to over 12 times per year, or more than one per month.

Throughout this process, as we've grown the revenue, we've also looked at our gross margin. As you can see, from 2005 to 2009, we've grown our margins from the high teens to the 40% range in both 2008 and 2009. Obviously, these are very high-level margins, and we were able to take advantage of some of the opportunities and the tightness in the supply chain in the markets over the past couple of years. We are very, very happy to achieve these levels of margins and enhance our bottom line.

What has that done from an earnings standpoint? We achieved record earnings in 2009 of $1.71 per share, or over $17.4 million. You can see the progression from 2005 to just about break-even and, particularly, the step up in 2008 and 2009 as we took advantage of the strength of the cycle.

From a balance sheet perspective, as we're focusing on earnings, we're also looking at our balance sheet and trying to continue to strengthen it. If you look at our cash investments, cash equivalents and investments, you see, again, back in 2005 where the number was below $3 million. We've grown that dramatically, particularly over the last couple of years, and we now have $46 million of cash on our balance sheet with no debt. We believe, as Jim mentioned, that as we go forward in 2010, we'll continue to be profitable and we'll continue to generate cash in fiscal year 2010.

If you look at the balance sheet again, you see no debt. The long-term liabilities are simply things such as deferred taxes, but we have no bank debt. Our current ratio has improved also significantly from 2005 where it was at approximately 2 to 1, to 2009 where it's 3.5 to 1.

Finally, cash management. As Jim mentioned, our cash cycle has improved from 31 days down to 17 days, in fiscal year 2009, which is a dramatic increase, as you can see, from fiscal year 2005. We continue to want to keep our cash cycle at a very low level. It will be challenging in fiscal year 2010 to keep it down to 17 days, but we do believe we're going to keep it in a range of 15 to 30 or 35 days across the entire fiscal year.

With that, I'd like to give it, back to Jim. Thank you.

James Lines: Now, I'd like to give a brief overview of what's happening in our markets. Clearly, they changed abruptly about nine months ago. In the energy market, the global recession has slowed demand growth appreciably. Actually, there's been demand deterioration in the U.S. market. Consumption has declined and is expected to continue to decline in 2009 and 2010. Energy policies by the government may have a negative effect on our markets. Also, due to the recession, there's overcapacity in our markets. Utilization rates are down from 90% to around 80% and are projected to go lower as 2009 moves on. On the positive side, though, we are seeing opportunities in the expanding economies, the emerging and developing markets of China, the Middle East, and South America. Graham's brand is stronger, and we expect to be able to capitalize on those opportunities.

This slide is an interesting comparison of how the market was viewed in 2008. This is the refining market. It was projected in 2008 that between 2008 and 2030, there would be a 50% increase in oil demand. In the most recent report, which came out in July, it has now been downgraded from a 50% increase through 2030 to roughly 25%, that is still very healthy. That still will create a lot of demand for our products. But we have to recognize that the demand profile has changed. Consumption is dropping, energy policies are having an effect, crude oil pricing is lower than it was a year ago, and capacity utilization has to be used up before new investment is being made.

This slide gives an indication of where the business will come from, again, from the refining sector. This is from an OPEC report released in mid-July. Markets that will be active are international markets, primarily in Asia, more importantly in China. About one-half of the incremental distillation capacity to come onstream between now and 2015 is projected to be in Asia. The Middle East will have significant growth as well, and the U.S. also will have growth in distillation capacity. Distillation capacity is a measure of refining investment, and we view that as one of the metrics that we monitor for looking outward for growth opportunities.

The petrochemical markets actually began to slow before the refining market because they followed their normal supply and demand pattern. We do expect to see limited investment by the U.S. markets both in refining and petrochemical over the next couple of years. We just don't see it in the short term. However, the Middle East and Asia, we expect, will make investments in new petrochemical capacity. We are evaluating integrated refineries and petrochemical facilities that require very large amounts our equipment in both processes and also the fertilizer market and other petrochemical applications are active in Asia.

With regard to the power market, we've participated in the power generation market in a smaller end of the market, typically cogeneration plants, geothermal power plants, and waste-to-energy facilities, not central power stations. We have seen activity pick up for that work now, and also we're projecting, from what we're reading, that the nuclear market will be active in the years to come. Globally, there are very large power projects that we currently aren't participating in, but there is opportunity for us to evaluate there, as that shows growth potential.

In a more long-term look, our vision is to be a leader in the design and manufacture of engineered-to-order products to the energy markets. There are two key distinctions. One is engineered-to-order. We believe the energy markets value quality, specialized engineering know-how, and the ability to understand how the equipment integrates into these very sophisticated processes. They will make decisions based on experience and value, as opposed to simply based on price. We also believe in the energy markets. They are cyclical, as we mentioned earlier, but long-term, the demand profile for energy is up, and we think energy is the right place for Graham.

This slide gives an indication of the dramatic shift that we've experienced in our sales and backlog. We've peaked with bookings in 2008 for $107 million; in 2009 the bookings had dropped appreciably to just under $74 million. Consequently, our backlog lowered from year-end 2008 of $75 million to just over $48 million entering fiscal 2010.

Our near-term strategy is to continue with our commitment to improve Graham. That involves developing our people, improving our processes, and continuing on with our capital plan. For our customers, even though they may not be buying right now, we will stay close to them. We will strengthen our sales organization. We will gain market advantage and watch carefully the pipeline for opportunities and capitalize on those opportunities.

As to performance in this downturn, we expect to remain profitable and to generate positive cash flow. We will evaluate our position during this disruptive time in our markets and strive to capture greater market share. What's important is, we want to manage the business over the long term. We'll manage this down cycle, but our eye is on the upturn. And during the upturn, we want to be ready to ascend the growth curve more rapidly than we did last cycle. We want to take market share, and we'll continue to invest in and expand our business.

The steps we took during the growth period of 2005 through 2009, I feel, have prepared Graham well for this downturn. No one likes a downturn; they are very tough times. But our Company was positioned well for a downturn with the way we managed the growth. We managed it with variable costs, our strive to improve our processes, reduce lead time, and change our cost basis.

This slide is a comparison of the last peak, which was fiscal year 1998, and the downturn, which actually took two years to materialize in 2000. There was a 35% drop in the top line. At that point, we saw our Company pretty much reach a break-even point, with 1% operating margin. This year, we're seeing the top line erode in one year, from $100 million to our guidances between a 30% to 40% reduction for fiscal 2010. Our expectation is that our gross margin will be between 28% and 31%, and our operating margin will be around 9%. So, we have a different operating performance than we had in the past, based on the steps we took during the last four years. We're prepared for this downturn. We're not happy that we're in a downturn, but we feel we will perform differently in this downturn than our Company has performed in the past.

As always, we want to make sure we're focused on all of our markets, not just refining and petrochem. Power generation is important, and other markets such as edible oils, industrial gases, biofuels, and cryogenic applications, that cover the broad spectrum under the energy umbrella. The pipeline of activity is pretty robust right now. Our sales and application personnel are very busy, almost as active as we were 12 to 18 months ago. So, we really haven't seen a discernible drop-off in our pipeline activity. When will customers step up to the table to place purchase orders? Well, that's been difficult to predict. But we like the way the pipeline looks, we like the way the projects are progressing, and we're aware of those projects. Our sales model keeps us aware very early, and we expect and hope to capitalize on those opportunities when the customers do step to the table. Refining is active, petrochem is active, and power gen is active from a quotation perspective.

We've worked hard to build our balance sheet to be in a position to capitalize on opportunities that will occur during a downturn. We've enacted an acquisition program. The key facet of that was bringing Jeff onboard, with his background and capabilities in that area. There are two legs to our acquisition strategy. One is geographic expansion, the other is product diversity. We're focused on engineered-to-order products and looking for companies that have a strong management team and a commitment to the customer and to quality. Our targets must have a return that will exceed our cost of capital, and we've set a revenue range of up to $60 million. As we continue to improve our balance sheet, that does not preclude that we will not look at acquisitions that are above $60 million in revenue.

When I stood here last year, I didn't envision the way the markets would unfold over the last 12 months. This slide is a comparison of how Graham's stock price compared from July last year to now as well as the Dow Jones or the Russell Index. It's been very dramatic, there's been a very steep change, and I recognize that those shareholders that invested in Graham last year have had to bear some losses. But if we look at how Graham is over the long term, comparing where Graham was at the start of the growth cycle in 2004, $100 invested in Graham on January 2, 2004, would be worth $600 today. $100 invested in the Dow Jones average, S&P 500, or the Russell 2000 would be worth about $100 today. So, Graham has done well, great value for our shareholders through this period of growth, and I believe that it will be a solid investment going forward.

With that, we'll gladly take whatever questions you might have.

Male Speaker: How has Graham prepared itself to take advantage of opportunities in alternate energy? Ethanol might not materialize as what was initially envisioned, so how is Graham prepared to take advantage of those opportunities?

James Lines: I think we're prepared very well. If we look at alternate energy, and under that umbrella there are a lot of processes: gas-to-liquids, coal-to-liquids, solar, geothermal, those are all areas where Graham has been for quite some time. The same process licensors or contracting specialist companies that were working on, refining projects or petrochemical projects, are also participating in those projects. So, our sales channel is effectively being managed, and our Company is positioned, we believe appropriately, to take advantage of those opportunities. We're not quite sure in the U.S. which way the energy policy will go, but I feel our Company is prepared to participate. We're agnostic to energy; we'll participate in any of the energy processes, because they require heat transfer and they require vacuum products, for the most part. That's what we do, that's what we do very well, and there'll be opportunities for us.

We appreciate your time and your interest in Graham. And thank you very much. We'll be around for socializing for a little bit, to answer questions one-on-one, if you wish.