Operator: Greetings and welcome to the Graham Corporation fourth quarter 2010 quarterly financial results conference call. It is now my pleasure to introduce your host, Mrs. Deborah Pawlowski, IR for Graham Corporation. Thank you, Mrs. Pawlowski. You may begin.

Deborah Pawlowski: Thank you, and good morning, everyone. We appreciate your joining us today on Graham's fiscal 2010 fourth quarter financial results call. On the call with me today are Jim Lines, President and CEO of Graham, and Jeff Glajch, Chief Financial Officer. Jim will briefly review the fourth quarter's performance and will discuss the Company's strategy and outlook, as well as his perspective on the state of the industries we serve, while Jeff will be reviewing the Company's performance in the recent quarter and the full fiscal year.

You should have a copy of the earnings release that was put out this morning, and if not, you can access it at the Company's website which is www.graham-mfg.com. In addition, we have posted supplemental slides on the website to provide a visual overview of our results. As you are aware, we may make some forward-looking statements during the formal discussion, as well as during the Q&A. These statements apply to future events that are subject to risks and uncertainties, as well as other factors that could cause actual results to differ from what was stated here today. These risks and uncertainties and other factors are provided in the earnings release, as well as other documents filed by the Company with the Securities and Exchange Commission. These documents can be found both at the Company's website and at www.sec.gov.

With that, let me turn it over to Jim to begin the discussion.

Jim Lines Thank you, Debbie, and good morning everyone.

The fourth quarter closed a challenging and remarkable year. Challenging given the effect of the global financial crisis that led to a rapid collapse in our markets that we saw in our order book in fiscal 2009, that played itself out through our revenue decline in fiscal 2010. On the other hand, the year was remarkable in many positive ways. We've demonstrated that the Company not only could out-perform during periods of strong demand, but also deliver solid financial results in a steep downturn.

The attention we provide to our customers is a critical component of our success, as we set a new record for orders in the year. Our company-wide commitment to improving Graham each day drove tangible gains in operational excellence, safety and error reduction that ultimately were reflected in our ability to protect margin, despite significantly lower revenue. This market downtown has been particularly sharp, and I am pleased with how our managers and employees have navigated the Company through this period. We aren't completely through the downturn and still have a couple of quarters to contend with. We believe the concluded fourth quarter and the next two quarters should represent the bottom of this cycle for us.

During the fourth quarter, we had a good level of bookings, considering market conditions. Bookings were $18.3 million. Notable orders in the quarter were a large order for a South American crude oil refining project, two orders for geothermal power generation, one is for Africa and the other for a U.S. installation and a $5 million order for an ethylene-producing facility in Asia.

While market conditions appear to be improving, we expect quarterly order levels to remain erratic and unpredictable. Although as you can see from these orders, the drivers of demand for our products as we move forward, as we've discussed before, will be in the oil refining and petrochemical applications emerging economies in Asia, the Middle East and South America. We expect the North American market will not pick up any time soon, specifically from U.S. oil refining and Canadian oil sands markets. However, we are noticing a pick-up in bidding activity for U.S. alternative energy projects such as biomass energy, municipal waste energy and geothermal power generation. The margin potential can be quite a bit lower for these projects, and we are facing different competitors from those in the traditional refining and petrochemical markets. Our near-term view remains positive, based on the activity in the pipeline. Our sales engineering team is busy developing proposals for early-stage project work that could materialize into orders several quarters out. Our order levels will vary greatly by quarter. We are expecting backlog to expand by year-end, based on planned 5% to 15% year-over-year sales growth.

Sales in the quarter were $13.8 million and were in line with our expectation. Gross and operating margin were 31% and 8.6%, respectively. With the level of factory utilization and the amount of sub-contracting in the quarter, I am quite pleased with our profitability.

There was exceptionally strong cash flow from operations in the fourth quarter, and consequently, for the full year. $17.5 million in cash from operations was generated in the fourth quarter and $30.3 million in the full year. Both were driven principally by unusually strong customer deposits that will translate into purchases of materials in fiscal 2011. Jeff will elaborate in greater detail on this.

We structured the Company to remain profitable at this level of utilization, while permitting ongoing investment in internal development and continuous improvement.

As we mentioned in the last quarter, we expect similar sales and profit levels in the first and second quarters of fiscal 2011. The latter half of fiscal 2011 sales are planned to expand, as should profitability. We plan to continue to invest in internal development and process improvement in order to strengthen the Company and be in a solid position to capitalize to a greater degree than last cycle on a market recovery.

We expect this market recovery will be different from prior recoveries. It will be led by developing and emerging economies, rather than by developed economies. This will present new challenges and exciting opportunities. Our prior and ongoing investments in people, processes, IT and production equipment ready the Company for the upcoming recovery.

Moreover, our acquisition program is advancing well. Our focus is clear. We are looking at companies that provide engineered-to-order, long-sale cycle products, serve the energy markets, have a strong customer- and quality-minded culture, current revenue in the $20 to $60 million range, provide opportunities for geographic operations on market expansion and will yield a return in excess of our cost of capital. We've had a number of conversations with various companies, and I am encouraged by the strategic fit several targets see in becoming part of Graham. We will continue to remain disciplined in our identification, analysis, consummation and ultimately integration of acquisitions.

Let me turn it over to Jeff for a detailed review of the quarter and highlights on the year.

Jeff Glajch: Thank you, Jim, and good morning, everyone. I will start with a review of sales and operations activity, before moving on to orders, backlog and our outlook for fiscal 2011.

As you saw in our press release, net sales in the fourth quarter of fiscal 2010 were $13.8 million, an $11 million decline compared with last year's fourth quarter, but a $1.6 million increase from the trailing third quarter of this fiscal year. As expected, Graham's sales have continued to shift toward international and away from the U.S. market. Fourth quarter fiscal 2010 sales were 67% international and 33% domestic, practically the inverse of the 36% international and 64% domestic in last year's fourth quarter, and expanding this year's year-to-date trend of 52% international and 48% domestic in the first three quarters of fiscal 2010. Compared with last year's fourth quarter, international sales increased to $9.3 million, up $300,000, while U.S. sales declined to $4.5 million, down $11.3 million.

For fiscal 2010, net sales were $62.2 million, down 38.5% from fiscal 2009. International sales made up 55% of the total, while U.S. sales made up the remaining 45%.

International sales, in fiscal 2010, decreased by 8% to $34.3 million. Within the international markets, Asia sales were $20.3 million, up 53% from $13.3 million last year, while sales to all other international markets were $14 million, down 42% from $24.1 million last year. We have made great strides, continuing to penetrate the Asian market, especially since we opened an office in China in 2006. We believe our brand in Asia is strong and there remains significant growth potential for Graham in this important growing market.

U.S. sales declined to $27.9 million, off 56% from last year's total of $63.7 million, more reflecting the shift where less capital is being invested in the refining and petrochemical markets.

By industry, sales dollars declined across all segments in the fourth quarter. The most pronounced decrease in dollars was in refining, especially in the U.S. Sales to refiners were down to 34% of total sales in the fourth quarter of this fiscal year, compared with 37% in the same period last year. 45% of sales were to the petrochemical industry, up from 35%, and 21% of sales were to the power industry and other industrial applications, down from 28% last year.

For fiscal 2010, refining industry sales accounted for 41% of total sales, down from 46% last year. Petrochemical sales for this period increased to 35%, up from 27% last year, while sales for power and other industrial applications decreased to 24% from 27% last year.

Before I discuss orders, I want to reiterate what we have mentioned in the past, that we expect quarterly orders during this and most periods, to be erratic, and we suggest using trailing 12-month information to best understand our order trends. Orders in the fourth quarter of fiscal 2010 were $18.3 million, down 11% from the fourth quarter of fiscal 2009. Full-year orders were a record $108.3 million, up 47% from $73.9 million in fiscal 2009.

Backlog on March 31, 2010, of $94.3 million was also a record, up from $89.8 million on December 31, 2009, and nearly double the March 31, 2009, level of $48.3 million. Backlog has increased from its low point in fiscal 2010 of $37 million on June 30, 2009, as we have seen three consecutive quarters of book-to-bill ratios above 1.0.

Orders in the fourth quarter were 61% international and 39% domestic. For the full year, orders were split evenly between international and domestic. International orders grew in fiscal 2010 to $54 million, up $11.6 million or 27% from fiscal 2009. Domestic orders were $54.3 million, up $22.9 million or 73% from last fiscal year. The domestic increase was primarily due to a large order in excess of $25 million from Northrop Grumman to support the U.S. Navy. Excluding this project, international orders would have been in excess of 65% of total orders.

Looking forward to the next few quarters, we continue to see our sales and order mix shifting toward Asia, the Middle East and South America and away from the United States.

It is important to note that we expect only 50% to 60% of our current $94.3 million backlog to ship over the next 12 months. Historically, our 12-month conversion of backlog is usually 85% to 90%. However, the U.S. Navy project and a couple of large Middle East refinery projects have a longer conversion period than normal. The U.S. Navy project alone, which makes up approximately 30% of our backlog, is not expected to begin to convert to sales until the beginning of fiscal 2012. Our backlog is split as follows: 37% in refining, 15% in chemical and petrochemical and 48% for power and other projects. Included in the latter category, is the aforementioned Navy project.

At the end of fiscal 2010, we still had $7 million worth of orders in our backlog for projects currently on hold. While this number had not changed in the fourth quarter of fiscal 2010, we did receive a notice of cancellation of one project within the past couple of weeks, which will reduce our backlog by $1.5 million.

Our gross margin continues to be relatively strong in the fourth quarter, given our level of sales. Gross profit was $4.3 million, or 31.1% of sales, compared with $9.6 million, or 38.8% of sales in last year's fourth quarter.

For fiscal 2010, our gross profit was $22.2 million, or 35.7% of sales, compared with $41.7 million, or 41.3% of sales in fiscal 2009. Clearly, for the year, the impact of lower sales volumes adversely impacted the gross profit dollar level, as well as the under-loading of our production facility, which negatively impacted our gross margin percentage.

For the fourth quarter of fiscal 2010, SG&A expenses were $3.1 million, or 22.5% of sales, compared with $3.5 million, or 14.1% of sales in the fourth quarter last year. In last year's fourth quarter, fiscal 2009 that is, we also incurred $600,000 of non-recurring costs related to restructuring expenses.

For fiscal 2010, SG&A and other expenses were $12.2 million, or 19.6% of sales, compared with $15.4 million, or 15.2% of sales in fiscal 2009. The restructuring initiatives we undertook, both at the end of fiscal 2009 and in the second quarter of fiscal 2010, combined with lower costs related to the decline in sales, accounted for the reduction in SG&A dollars in the current fiscal year.

Interest income in the fourth quarter of fiscal 2010, declined to $11,000, compared with $30,000 in the same period last year, as a result of the continuing decline in U.S. Treasury yields. Our investments are in U.S. Treasury securities with maturities up to 180 days.

For fiscal 2010, interest income was $55,000, compared with $416,000 in fiscal 2009, despite a significantly higher cash and investments balance.

Our effective tax rate in the fourth quarter was almost 49%, however, this included a $311,000 charge to reduce a historical deferred tax benefit for New York State tax credits, which we do not believe we will be able to utilize. Excluding this charge, the effective tax rate was below 23%. For fiscal 2010, our year-to-date tax rate is 36.8%, though excluding the tax adjustments in the second and fourth quarter, the current year effective rate is just above 29%.

Net income in the fourth quarter of fiscal 2010, was $600,000, down 83% from last year's fourth quarter. On a per-diluted-share basis, earnings were $0.06 compared with $0.35 last year. Adjusting out the one-time state tax charge mentioned previously, net income was $900,000, or $0.09 per diluted share. For fiscal 2010, net income was $6.4 million, compared with $17.5 million in fiscal 2009. We believe we had good financial results, given the significant effect deleveraging has on our business with lower volume. We have structured the business to work through the trough in our markets, and we will be quite happy to get through the next couple of quarters and begin to see growth in the second half of fiscal 2011.

Graham's balance sheet remains strong with cash, cash equivalents, and investments totaling $74.6 million at the end of March, up from $57.7 million at the end of December and $46.2 million at the end of fiscal 2009. While we are very pleased with this increase, it is important to note that the vast majority of our cash and investments improvement in the fourth quarter came from a large increase in customer advances, which grew to $22 million, up from $6 million at the end of December. This increase came from a handful of customers who provided higher up-front and near-term progress payments, to lock in raw material costs. The $6 million level from December is in line with a normal cash advance balance from our customers. We expect the customer deposit level to remain higher than normal throughout fiscal 2011, though we do expect it to generally reduce over that period, hence using, rather than generating, cash in this category.

For fiscal 2010, we generated $30.3 million from operating activities, approximately one-half of which came from the customer deposit increase just discussed. Excluding the customer deposit increase, we still generated $14.1 million, which given our weakened markets, is a significant accomplishment. The cash generation in fiscal 2010 resulted from a combination of strong operating income, despite the market downturn, and continued improvements in working capital. We have no borrowings on our $30 million bank line and are utilizing it solely for outstanding letters of credit, which totaled $9.6 million on March 31, 2010.

Capital expenditures were $0.5 million in the fourth quarter of fiscal 2010, and $1 million for the full year. In fiscal 2009, our capital expenditures were just below $300,000 in the fourth quarter and $1.5 million for the full year.

As we look ahead to fiscal 2011, we see it as a tale of two halves. The first half of fiscal 2011 will look a lot like the last two quarters, namely with sales levels of $12 to $14 million per quarter and gross margin in the mid- to upper-20%. In the second half of fiscal 2011, we expect to see significant improvement in sales, and growth in margin, versus the first half of the year.

For the full year of fiscal 2011, we expect to see sales 5% to 15% above fiscal 2010 or $65 to $72 million, with gross profit margin of 27% to 31%. Despite higher revenue and the improved utilization which comes with it, the margin is expected to be below fiscal 2010, due to the competitiveness in the market for orders over the past few quarters and the shift of our business toward emerging markets in the power-generation arena, as Jim mentioned earlier. We also do not expect to repeat the raw material savings that we achieved in the first half of fiscal 2010. SG&A for fiscal 2011 should be in the range of $12.5 million to $13 million, and we expect an effective tax rate of 30% to 33%.

From a cash standpoint, we expect our operating cash flow may be negative in some periods, primarily due to the unwinding of a significant portion of the $16 million increase in customer deposits that I mentioned earlier. Beyond that, our operating cash flow will continue to be strong, as it has in the depth of this downturn.

We expect our capital spending in fiscal 2011 to be between $2.8 million and $3.3 million. We need to make a major investment in specific manufacturing equipment for the Navy project. That investment, alone, will be approximately $1.5 million, around one-half of the total capital for fiscal 2011.

We expect order levels over the upcoming quarters to continue to be erratic, and while we generally expect the book-to-bill ratio to exceed 1.0 and our backlog to grow, we are likely to see some quarters where the book-to-bill is below 1.0.

In closing, we believe the fourth quarter was successful, despite the depressed level of sales, as we continue to remain profitable, generate cash, increase our record backlog, stay close to our customers, focus on internal improvements, and position ourselves well for the beginning of the improvements in our markets, particularly in the international arena. We do not believe we are completely out of the woods yet, but we have seen strong orders over the past few quarters. We expect to remain profitable in the first half of 2011, as we did in the latter half of 2010, despite the low sales level, and expect to see a noticeable sequential improvement in sales and earnings in the second half of fiscal 2011.

That concludes my remarks. Jim, back to you.

Jim Lines: Thank you, Jeff. Operator, please open the line for questions at this time.

Operator: Thank you. Our first question is from the line of George Walsh of Gilford Securities.

George Walsh: Jim, could you give a little more detail about the deposits you're getting from customers? It seems a little different from what I've seen over the years. Is there something special going on that you're getting more of this money up front? Is it a matter of your negotiating, or conditions in the commodities markets or any other factor that you may see there?

Jim Lines: In general, George, we don't see a change going forward in how we historically had been able to negotiate progress payments. What we did have was a handful of contracts, wherein we were able to negotiate more forward progress payments, as we negotiated with our customers to try to lock in our material costs. They helped participate in that locking-in of our costs by advancing us money through negotiations. They were supportive of that. They understood the situation, and we negotiated that with a handful of customers. However, I don't see a pattern change going forward, in general.

George Walsh: It was mostly the international customers you got that from?

Jim Lines: Some were international and one, in particular, was U.S.-based.

George Walsh: Would there be anything in the accident with BP in the Gulf that you see has any potential impact on you, in terms of refining business?

Jim Lines: That's a pretty significant event that's happening right now, I'll reply in a broad sense. I think it will support, perhaps, further investment in the oil sands, which is beneficial to us, as there could be fear in deep-water drilling in the Gulf of Mexico. I don't think, in general, it's going to change the long-term demand pattern that we project for oil-based products and then demand for our equipment. However, I do think there'll be a short-term reaction to what has occurred, and hopefully foster investment in the oil sands.

George Walsh: Any new trends in the oil sands, that you're seeing, in terms of momentum of investment in projects?

Jim Lines: One of the things we like about the oil sands activity is that we're seeing investment occur now in the extraction side, developing the sites for the production of oil sands that ultimately then must be upgraded. Where Graham's equipment is required is in the upgrading sections. That's been going on in the production side and has to translate, at some point, to investment being made in upgrading capacity, which is where our large ejector systems and steam surface condensers are required.

We're encouraged by what's happening now.

George Walsh: On a quantitative basis, between getting these deposits up front, you've got a record backlog, the cash position is strong, so that seems very good. But you do say qualitatively, you feel that the recovery is somewhat tentative. Is that just a standard caution or are there other elements that you might want to expand on, versus some of the quantitative elements that are setting up pretty well for fiscal year 2011.

Jim Lines: It's a good question. We're somewhat hesitant, in that we don't believe our markets are in full recovery, and clearly, we would expect some fragility in the recovery, based on what's happening with currency changes, like the European situation. They all could have a short-term effect. Looking beyond 2011, which is what we're doing, we are very positive in the outlook and the requirements for capital investment and new petrochemical facilities, new refining facilities, new power-generating facilities. We have to get through this period of time which is unpredictable and a time to be cautious.

While we had a very strong level of bookings last year, even removing the Navy project, I was very pleased with our level of bookings for fiscal 2010, but our sales team was focused on where the opportunities were. I have to admit, there were small pockets of opportunity and our team did a great job capitalizing on those small pockets. In general, there are a limited number of projects. That makes the competitive environment hypersensitive to pricing and protracted negotiations, all of which don't favor, necessarily, the early part of 2011. Looking beyond these tough couple of quarters and looking beyond 2011 itself, I'm very encouraged by what we see in the pipeline and the opportunities for Graham.

George Walsh: Well, you've done a good job, Jim, and the whole team, in navigating the downcycle, and you stayed profitable. It's a cyclical business. It's the nature of it, but you kept the balance sheet very strong and you stayed profitable during a difficult time, so I just want to congratulate you and the whole team on that.

Operator: Our next question comes from the line of Chris McCampbell of Stifel Nicolaus.

Chris McCampbell: Where would you say we are in the cycle of building the backlog? Do we still have some quarters where we may be able to continue to grow that, or are we going to be quickly reaching a point where we start shipping and so the backlog will roll over a little bit?

Jim Lines: Well, as we've mentioned, the first two quarters of fiscal 2011 will be comparable to the last two quarters of fiscal 2010. We have a nice backlog, a high-quality backlog. It gives us visibility out beyond 2011. I do feel, with what our view is into the pipeline, that we'll have backlog expand by the end of the year, but within the year, quarter-by-quarter, there could be quarters where the backlog drops somewhat and there could be quarters where the backlog has an appreciable gain. Nothing that's different from the past.

Chris McCampbell: In terms of the candidates you're looking at with acquisition possibilities, would they share the same cycle or are you looking at companies that may be able to benefit from later cycle or even early cycle, where you're diversifying the cycle?

Jeffrey Glajch: I think the candidates that we've been looking at fall into both categories. There are some that would be in a similar cycle to us, but there are others that would be somewhat off-cycle and could potentially improve our cyclicality a little bit.

Chris McCampbell: Are you looking strictly at situations where you would just use cash and not stock?

Jeffrey Glajch: Most likely, but certainly there are scenarios where a seller might be interested in some stock, but we'd be very conservative there. We don't want to dilute our existing shareholders by any meaningful amount.

Operator: Our next question comes from the line of Dick Ryan of Dougherty & Company.

Dick Ryan: Jim, when you look at the pipeline of opportunities, can you give us a feel, quantitatively, for the size of opportunities that you're considering?

Jim Lines: I'll first speak to it geographically. We see much of the pipeline for activity that's emanating from Asia, the Middle East and South America, as we've said in the past. On the U.S. market side, we are seeing our pipeline increase for opportunities in power-generation applications. So going to the size of the projects, for power-generation applications in the U.S. market, these tend to be good sized orders, but smaller in size compared with a refining project.

As I mentioned earlier in the call, the margin potential can be dramatically different for those opportunities due to the buying criteria of the customer, as well as the competitive landscape that we face in that market place. When we move to our more traditional markets of refining and petrochemical, into the Middle East, South America and Asia, the size there for the projects can vary between $1 million to $5 million to $7 million. We have a good population of those opportunities in the pipeline over the next 12 to 18 months.

Dick Ryan: I think you've got a pretty good batting average of oil refining jobs in China and the ethylene award in the most recent quarter. Does that give a little bit of a forward feel for what could be developing in the chemical processing environment? I mean, is that a precursor of other jobs in the pipeline?

Jim Lines: We have won, during the last two quarters, two nice ethylene projects for Asia. One was for India; one was for northern Asia. We are bidding on a number of ethylene projects. My belief is those won't materialize for 6 to 18 months in new orders, remembering our sales cycle is such that we wish to be involved very early. So that gives us good visibility into the pipeline, and I would say petrochem lags a little bit behind what we're seeing for investment by the refining market.

Operator: There are no further questions in the queue at this time. I would now like to turn the floor back over to management for closing comments.

Jim Lines: Thank you, everyone for your time this morning. As we communicated on the call, we're very pleased with our performance in fiscal 2010. We're very encouraged by how the Company is positioned to get through 2011, and we're very excited about looking beyond 2011, based on what we see in the pipeline and the improvements we put into the business, and our acquisition program, to move Graham to a higher level of performance. We look forward to updating you during the July call. Thank you.