Jeff Glajch: Good morning. I'm Jeff Glajch, CFO of Graham Corporation.

Slide 2: Before we begin, let me point out our safe harbor statement. At your leisure, please take a look at that.

Slide 4: Graham Corporation, based in Western New York, is an 80-year old manufacturer of engineered-to-order equipment for the energy sector. We provide key equipment into the refining, petrochemical, power and U.S. Navy markets. We have a market cap of about $260 million and institutional ownership of approximately 80%.

You can see that in the first quarter about two-thirds of our sales were to the refining market. That is an abnormally high number for us, normally the number is 25% to perhaps 35%. Chemical/petrochemical is also normally at that same level, the power market and Navy typically are each in the 15% to 20% range.

Slide 5: What does Graham do? We make process critical equipment for the energy markets. Our equipment is engineered-to-order. It's unique. We do not make model numbers. If you call and ask for model number 37, model number 37 doesn't exist. Everything that we make is engineered-to-order, and has a very high cost of failure to our customers. What does that mean? It means that if our equipment doesn't work, their facility is not going to operate at the optimal level that it needs to, and it will cost them a lot of money.

There are very tight tolerances for the equipment that we make. If it's not engineered correctly and if it's not manufactured correctly, it will not operate in the most efficient manner and it will cause our customers a great deal of difficulty. It's equipment that is required for our customers to operate, whether it's refinery, petrochemical or other plants. It is required. It is difficult, but not impossible to replace. Finally, it has a low relative cost. If you think about a new refinery that might cost $3 billion, $4 billion, $5 billion, our equipment might be one-tenth to two-tenths of 1% of that total cost. So it has a high cost of failure, it's critical equipment, yet on a relative basis, it's a small cost of the capital put into a new facility.

Slide 6: What differentiates us from others in our key markets? First thing is our consultative selling process. Our process around selling to our customers is not simply replying to an RFQ. Rather, when our customers are building a facility, from the point when they decide to build the facility until the facility is actually operational is typically about a five-year process. Our equipment goes out for RFQ perhaps 18 months to 24 months into that five-year process, but we don't start our work with them at that time. We actually start in month zero, or month one, in the concept phase, in the front-end engineering and design phase, in the EPC selection phase. Throughout that entire process we're working with our end users to help them understand how our equipment will work with their equipment, to understand the tradeoffs between capital costs and operating costs, and to make sure that our equipment can be designed to work specifically in their situation. So, all of that's important and all that is part of the value we bring to our customers. Our competitors do not do that. They look at that as a cost. We look at that as a part of the selling process.

Additionally, you should understand our complex project management. We have the ability to stop and start a project very efficiently throughout the process. For example, I'll use a typical refining order, from order to shipment might be a 12-month time period. During that 12 months, we're doing engineering work for the first six months. We're not recognizing any revenue. I'll speak to how we recognize revenue in a second, but rather we are incurring costs. We are doing the engineering work. We're working with the end users. We're going back and forth. As they're making a change, we might need to make a change.

Ultimately, about six months into that 12-month process, the engineering is approved, the designs are approved, and we start manufacturing. One of the things that can occur, once we start manufacturing, is we have to go back to make an adjustment. We're making that adjustment because our customers are making adjustments to how they're going to build their facility. So, we sometimes have to make an adjustment to what we're doing.

For revenue recognition, we do not start recognizing revenue until we put direct labor into a job. So, in a 12-month process, that first six months of engineering work, we're not recognizing any revenue. We're recognizing revenue once we start production in line with the direct labor hours that we put in, ultimately to completion of the project.

Finally, we have very tight tolerances. To our customers, good is not good enough. They need precise tolerances of what we manufacture, often to the thousandths of an inch. We have the ability to not only engineer that but ultimately to fabricate that.

Slide 7: We have a wide range of projects. We look at them in two buckets; large orders and short cycle orders. Our large orders are approximately two-thirds of our revenue. There may be only 50 to 75 orders per year, but it's about two-thirds of our revenue. Our short cycle orders, which might be 2,500 of 3,000 orders per year, make up the other one-third of revenue. A large order, in an industrial situation or commercial situation, typically runs from $250 thousand to perhaps $5 million to $6 million. On occasion, we'll have a commercial order larger than that. Then, our orders with the U.S. Navy will be much, much larger than that, they can be up to $20 million or $30 million. The Navy orders are not completed in 12 months, but rather can take two, three, four, five, sometimes six years.

Short cycle orders are typically small orders. They can be in and out within anywhere from a couple weeks to a couple of months. They can be replacement components. They can be small pieces of equipment. While they do require some engineering, the amount of engineering relative to a large order is typically very nominal.

Slide 8: We talked about four key markets. You can see them listed here. We actually have a fifth called other, which incorporates some other end markets. The largest markets for us are the refining and the petrochemical market. In the refining market, we provide equipment into refineries for a number of reasons. One is for new capacity. One is for revamps, retrofits. Then there are significant spares or replacement orders. That would be short cycle orders, as I just mentioned. As we look at the refining market over the past couple of quarters, we're seeing a revitalization of the North American refining market, primarily driven by that middle column, the revamps and retrofits.

It's our belief that going forward the North American market is where the majority of the capital will be spent as refineries are trying to identify how to get incrementally more volume out of an existing refinery. In the international market, which is starting to pick up now in the refining side, we believe more of that investment will be on the new capacity side. Certainly, there will be some revamps and retrofits, and we have seen those, but we expect the international market to be more driven by new capacity.

While the chemical and petrochemical market had lagged a little bit, as the refining market has started to recover, over the past quarter or two, we've seen some significant activity. We have significant activity in our pipeline today. New capacity there is important for us and that is driven initially by the North American market, but there are also opportunities in the Middle East and in Asia. It has been about four years or so since we saw the last wave of petrochemical work in the North American market.

The U.S. Navy is an interesting business for us. It's a business that we had been intermittently for the first 70 years of our company. The company was founded and primarily served the U.S. Navy in the 1930s and during World War II. But the U.S. Navy, for a long time was, I'll call it, a convenience. So what I mean by convenience, and shame on us, historically, it was a convenience such that when our commercial markets were weak, we enjoyed working with the U.S. Navy, but when our commercial markets were strong, we didn't have the capacity. We've changed that. We have a completely different approach with the Navy and they have seen this over the past 10 years or so. We've invested a significant amount of capital to support the U.S. Navy. We are dedicated to providing equipment to the U.S. Navy, whether the commercial markets are weak or strong. We have dedicated capacity for them.

We have provided equipment into nuclear carriers since 2009. A nuclear carrier that was built with our equipment was delivered in 2015. The next order came over the past year or so and we will be delivering that equipment over the next couple of years. Our performance and our execution on the nuclear carrier work has led to us providing equipment to the nuclear submarine market. That's a much bigger market for us because a nuclear carrier is built every five years to seven years. The overall content that's available to us on a carrier might be $35 million to $40 million. So if you do the math, you'll find the nuclear carrier on average can provide us with $5 million to $7 million worth of revenue per year. Nuclear submarines on the other hand, there are two to three built per year and they have $15 million to $25 million worth of content available to us. So, if you do the math there, a nuclear submarine on average can provide $40 million to $50 million a year.

We've been successful in breaking into the Virginia Class submarine, a program that has been going on for a couple of decades and we've taken some market share there. On the Colombia Class submarine, which is the new submarine coming out, we have taken our first couple of submarine orders and have been working with the prime contractor for the Navy on the Columbia Class.

Our market share in the Navy has grown from a $5 million to $7 million business, this fiscal year we're looking for that to be somewhere in the mid-teens, and as we look into our next fiscal year, which will be fiscal year 2020 we expect our revenue with the Navy to be north of $20 million. So that's been a really nice growth platform for us. We've been talking for a couple of years about how we might get to that $20 million to $25 million range. As we're approaching that now, based on what's in our backlog already, we're working to grow that beyond $20 million to $25 million, and take it to $30 million, $35 million, $40 million, or perhaps $50 million going forward.

In the power market, we're primarily in alternate energy. The largest portion for us is the nuclear power market, which has been soft for a little while. We're starting to see some improved activity though over the past few quarters. We also provide equipment into the alternate energy markets to smaller facilities.

Then, other is a handful of other end markets such as cryogenics or edible oils. Those tend to be orders that are not particularly consistent and when they come in we execute on them and we move forward.

The key to note though, is we're seeing a recovery. We've gone through about a three year down cycle in the refining and petrochem markets. We started to see a recovery as orders started to pick up about three quarters ago. We had very strong order levels in the quarters that ended in December and March. The order levels in the June quarter were not quite as strong. Typically, in the early part of a recovery, which is where we believe we are right now, you'll see a little bit of volatility in orders. Even at the order level that we had this last quarter, there are some good projects out there as our pipeline has gotten quite a bit stronger over the past nine months or so.

Slide 9: Fiscal year 2018, which ended about four months ago, was a very rough one. We believe that the last three quarters of that fiscal year represented the market bottom. We announced our earnings for the first quarter last week and saw significant step up in revenue and a significant step up in profitability. As you'll see, towards the end of the presentation, the guidance that we provided earlier in the year, we updated and increased last week.

As we look at our business, we believe there's a strong opportunity for a recovery and significant revenue growth off of where we've been. To be fair, where we've been has been a market bottom, but we believe there's significant upside, not just off that bottom, but with multiple years worth of growth beyond that. We target an average EBITDA margin of greater than 17%. If you went back to the last cycle as it started to recover, you'll see that's exactly where we were, between 17% and 19%. Right now, we are in the low double-digit range. As we look forward over the next couple of years, we believe we can get above that 17% range. We also target 12% return on invested capital over the cycle.

Slide 10: Our backlog is strong. Our backlog at the end of March was a record at almost $118 million. It slid very slightly in the quarter that ended in June, but still at $115 million, is one of the strongest backlogs we've ever had. You'll notice on the chart on the left that a little over half of our backlog is with the U.S. Navy. Very happy to have that, it's a great business to be in, but that backlog is elongated. I mentioned earlier that a typical refining project might be 9 to 15 months. U.S. Navy projects can be anywhere from a couple of years to five or six years. So, that backlog is going to be there for a long time. From an operational standpoint, it's excellent backlog to have, because it gives us the ability to plan our manufacturing over a multi-year period.

If you look at the rest of the backlog, you can see refining is about 21% and petrochem is about 11%. Both of those have been growing over the past few quarters. If I went back nine months ago, our total backlog as you can see here, was about $73 million. Of that $73 million, a little over $50 million was U.S. Navy and only $22 million was commercial, non-Navy backlog. Again, we love having the Navy backlog, but it's very elongated and it's going to take a number of years to convert that. When we were down to $22 million worth of commercial backlog that was a pretty rough place to be.

Let's look at the business today. We have $115 million of backlog and over $50 million is commercial. In the last three quarters, we've more than doubled the commercial backlog. For the rest of this fiscal year, we believe our backlog will continue to grow and we'll see an even stronger backlog at the end of fiscal 2019. Where we see that growth occurring is on the commercial side. We don't expect the Navy backlog to significantly increase. In fact, I would expect it'll probably decrease during this fiscal year, just because there are not large opportunities with the Navy that will come to order this year. However, we do see some large opportunities beyond the Navy. Importantly, our commercial backlog went from $22 million to $50 million, we believe that will be significantly larger as we exit fiscal 2019.

So again, we're very pleased to start to see a recovery in the refining and petrochemical markets and we believe we'll start seeing that more so in our orders and ultimately in our revenue going forward.

Slide 11: We also have a very good balance sheet. You'll see in a couple of slides that we have approximately $75 million in cash. We have no bank debt. So we're looking to grow inorganically, along with growing organically. We're excited about the organic opportunities, but we can't sit and wait to just take advantage of those. We have a balance sheet that's an asset. As a physical asset, we need to convert it into an operating business.

What are we looking for? We're looking for an engineered-to-order products company in the energy industry. We're looking for a strong management team with a customer and quality focus. From a size standpoint, we're looking at $20 million to $60 million in revenue. The way I think about pricing, we're looking for a business that has a strong management team that has a good profitability level with EBITDA margins somewhere in the low double-digits to low-teens.

Our fourth criteria is that our cash return must exceed our cost of capital. The only way to get a return that's an equity type return on an IRR basis is by paying a reasonable price, not overpaying at 10 or 12 times EBITDA, but rather paying 6 to 8 times EBITDA. If you pay 6 or 8 times EBITDA and you've got a low to mid-teen EBITDA level business, you're paying roughly one-time sales. It's amazing, how the math works.

We stick to this strong pricing discipline. We're not going to overpay. We're not willing to buy something simply to improve our topline and not get a return on that investment for our shareholders. We're very disciplined. We've walked away from a number of opportunities where we just couldn't get comfortable with the pricing. So we're going to keep that discipline. I would rather sit on the cash than make a bad acquisition. That being said, we're going to continue looking very hard.

Slide 13: Quick financial overview. As you can see, our fiscal 2015 represented the top of the last cycle. Last cycle was a tepid recovery for a couple of years. Going into fiscal 2015, it looked like this was a multi-year recovery and then the bottom fell out of the oil markets in late calendar 2014 and, as we all know we had a lot of volatility in the oil and the energy markets over the past few years.

The last three years have been very rough for us. We saw a drop of one-third from fiscal 2015 to fiscal 2016, yet we continued to be profitable. We stayed at that lower level in fiscal 2017 and saw another drop of nearly 20% in fiscal 2018. Yet we remained profitable. So even in a very rough environment, probably the roughest environment that we've seen in 30 or 40 years, we continued to remain profitable.

That being said, for fiscal 2019, our guidance is $95 million to $105 million, which is up somewhere in the 20% to 30% range. This will actually take us to a level that, from a revenue standpoint, will be one of our strongest years. But this, we believe, is the beginning of an up cycle and we believe that there's multiple years of revenue expansion ahead. The core markets are very strong and we supplemented that with what is now a much stronger Navy market. If you went back to fiscal 2015 and that was our peak Navy market, it was barely $10 million for us, so we will obviously move that pretty far forward.

Slide 14: I talked about our balance sheet a little bit ago. We have $75 million of cash. Our operating cash flow is strong. The first quarter was low, but that's just timing on working capital. We continued to generate cash in the down cycle. When we get into an up cycle, we generate a lot of cash. So our balance sheet will continue to grow if we don't use that cash for an acquisition. That's why it's important for us to use that cash. Capital expenditures happen to be very small for us, on average it tends to be about $2 million to $2.5 million a year, which is in line with our D&A. So there's a net wash there.

We don't see significant capital needs going forward unless there's a specific need to support our Navy work and that would only be if we knew more Navy work was coming.

Finally, working capital utilization, we're typically between zero and 10% of sales from a working capital standpoint. So what's important there is, as we grow from our bottom $77 million to $95 million to $105 million and then beyond that, we don't need an enormous amount of working capital. Many businesses have working capital needs of 20% of sales, so as they grow they don't see a lot of cash flow because they're using it for working capital. We don't expect to see that. The jump from 2% to 4% was a big jump for us. So we expect to keep that number at a very low level. So we don't need much of our cash for working capital.

Slide 15: Talking about cash generation, we went back and looked over the past dozen years, so you can see we've generated almost $110 million in net income over that time period. If you look at the four bars in the far right side of the chart you can see that we've taken that $110 million and turned it into about $125 million worth of cash. When I think about earnings and I think about cash flow, I think about them as being relatively equivalent. In fact, this will show our cash flows are above our net income. There will be timing differences but over time we're going to generate a lot of cash and we're going to continue to add to our balance sheet. The proof is what we've done in the past. We believe we've got that same path going forward.

Slide 16: Quickly, on working capital allocation. On the left side is our cash from operations. The first thing we look to do is to reinvest in organic growth. But again, our capital needs tend to be fairly small. We do pay a dividend, which we have significantly increased over the past number of years. It's now at about $4 million a year or $0.40 a share with a yield of about 1.5%. For a company of our size, we think it's important to have a steady, consistent dividend and we think it differentiates us from others in our space.

Regarding the cash on the balance sheet, I've already talked about our focus on acquisitions. Our second focus is acquisitions and our third focus is acquisitions. We have a stock repurchase program shown here. We have done two stock repurchases over the past 10 years. We're not a company that likes to buy shares back just because we have cash. The two times we've done stock repurchases have been very selective when we felt the market overreacted on the downside to something that was going on across the market. We did purchase some shares but it's a very small amount of our total cash and it's not our intent to repurchase significant shares going forward.

Slide 17: I talked about our dividend. It has grown from about $0.08 per share, which was, quite frankly, a nominal dividend, up to $0.40 per share. We had a program in place for about four years of increasing it on an annual basis and a couple of them were step changes to really get us close to where we are. We did not increase it for the last couple of years because we were in a rough market space. However, we did just increase it last week from $0.36 to $0.40 a share. Our expectation going forward is to see those types of increases on an annual basis.

I mentioned our institutional share ownership has grown, from about one-third to about 75% to 80% over the past number of years.

Slide 18: Our guidance. We increased our revenue guidance on the earnings call last Friday. It had been $90 million to $95 million, we moved it to $95 million to $105 million, again representing approximately 20% to 30% growth over last year. Gross margins are starting to move up, but they are not to the level that we would like them to be. We look at our business in mid-cycle as being a low 30% gross margin business. This is typical in the early stage of a recovery where pricing is intermittent. As we move forward, we would expect that gross margin to step up.

SG&A. We have been investing. We are investing with the expectation of being able to support additional growth over the next couple of years. Our SG&A has stepped up a little bit.

Our tax rate dropped into the low 20s. We're a patriotic tax payer. If you were to look back over the last number of years, we were in the 30% to 32% range most years, with the tax cut that occurred last December, we'll be down in the 20% to 22% range.

Slide 19: So there's a whole bunch of investment highlights listed here. I think the important thing is that we're in markets that are good markets but have gone through a rough period. We're now seeing a recovery. We've seen our backlog grow. We're starting to see that convert into revenue and ultimately into profitability. We've got a very strong business model that can make money in a downturn, but can make a lot of money in an up cycle. We believe we have entered the beginning of that up cycle.

With that I only have a few minutes. But if I can answer any questions I would welcome them. Yes, sir.

Q&A

Q: [Question Inaudible]

Jeff Glajch: Great question. The question was, what percentage of the business is maintenance and spares, and what is the margin structure of that? Early on, I showed a chart that shows that two-thirds of our business is large projects and one-third is smaller projects. The vast majority of that one-third, probably 80% of it, so about a quarter of our total business would fall into maintenance and spares.

From a profitability standpoint, it is a higher margin business, it's our highest margin business. So one of the things that we have been focused on, is growing that aftermarket business. We don't sell service contracts per se, but we sell replacement equipment with our service team supporting our customers. We've done a couple of things: we have located a couple of service people in the company down to the Gulf Coast, and we have a third one that's going to be spending a good amount of time down there also to try to get closer to the customers on the existing operating plants.

As I mentioned earlier, we expect the North American market to be driven by retrofits and upgrades. We want to be in the plants before those decisions are made. So, by having the service team in there, we're seeing an increase in our aftermarket business. We believe, ultimately, that helps us not only in aftermarket, but also on those upgrades and retrofits.

Yes sir.

Q: [Question Inaudible]

Jeff Glajch: Sure. Good question. What are some of the drivers for the cycle that we see coming? First, we see some pent-up demand. Following a significant down cycle, particularly a lengthy one, and this was both very deep and lasted about three years or so, there's pent-up demand.

This happens for a couple of reasons. One is, global capacity for energy needs continues to increase in North America and in Europe. You don't see that increase in developing economies in the Middle East and in Asia. You see a significant increase requirement for energy. So that's part of the driver on the international side. Then on the domestic side, our customers are looking to upgrade their existing facilities to get more efficiency and to get more output from a barrel of crude oil. So, we believe, both of those are key drivers at the beginning of the current cycle for the refining side.

On the petrochem side, some of it is supply driven. In North America, low cost and plentiful natural gas is helping to drive investment in North American petrochemical. If you went back to the 1970's, 1980's and 1990's, you would have seen that the North American petrochemical market was a healthy place to be. If you look at the decade of the 2000's, it was a very unhealthy place to be because natural gas was so expensive and there were alternatives outside North America.

As natural gas has become cheaper, you can produce at a very low cost. In North America there's a significant focus on investing in petrochemical plants. As I mentioned, about four or five years ago, we went through the first wave. We believe we're at the beginning of the second wave. We don't believe the second wave will be as big as the first wave, but it is going to represent some meaningful opportunities for us in North America. Then, we're continuing to see investment in petrochemicals outside of North America, again Middle East in Asia particularly.

Jeff Glajch: Okay. Well, thank you very much. If anybody has any questions, I'll be around after the presentation. Have a nice day.