

Graham Corporation
First Quarter Fiscal 2010 Quarterly Results Teleconference & Webcast
July 31, 2009

Operator: Greetings, and welcome to the Graham Corporation First Quarter Fiscal 2010 Quarterly Results Conference Call. It is now my pleasure to introduce your host, Mrs. Deborah Pawlowski, Investor Relations, for Graham Corporation. Thank you, Mrs. Pawlowski, you may now begin.

Deborah Pawlowski: Thank you, and good morning, everyone. We appreciate your joining us today on Graham's fiscal 2010 first quarter financial results call. On the call, I have with me today Jim Lines, President and CEO of Graham, and Jeff Glajch, Chief Financial Officer. Jim and Jeff will be reviewing the results of the quarter and also provide a review of the Company's strategy and outlook during this contraction in the business cycle. 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 and 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 at the Company's website or also at www.sec.gov.

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

Jim Lines: Thank you, Debbie, and welcome, everyone, to our first quarter conference call. First quarter financial results were excellent, all things considered. Sales were off 27% when compared with the first quarter last year, but they were in line with our expectation for the quarter. Gross margin in the quarter was unusually high for the level of revenue. We had significant margin lift due to lower costs for materials. Savings in materials look to have been short term, as we have already started to see material costs rise from their lows. Our procurement personnel did quite well, having been opportunistic while both costs were declining and suppliers were hungry to win new business.

The order environment declined sequentially with new orders at \$8.8 million. Quarterly order level has remained erratic during the past year, and we expect it will continue to be unpredictable and erratic for several quarters going forward. We continue to be aggressive to win new business. However, customers are just not making purchase commitments at the moment.

On a positive note, new orders through the start of this week were over \$5 million for July. Quotation activity is high, and we are encouraged about the outlook once the markets do recover. We believe recovery in our markets will be led by the Middle East and Asia, followed later by South America. Recovery in North America is hard to predict, but is not currently in sight for the refining of petrochemical markets. In our Middle East market, there are two projects in Saudi Arabia that have been reactivated. Each is a 400,000 barrel-per-day refinery requiring substantial amounts of specialized equipment like those Graham designs and manufactures. There are also signs of activity elsewhere in our Middle East markets. China continues to invest in new refining and petrochemical production capacity supported by its economic stimulus efforts.

I've been very pleased with our progress to grow our market share in the Chinese refining market. We have won seven orders for large ejector systems required by refineries in China during the past three years, bringing our market share in that period, we believe, to over 50%. Also in Asia is activity for fertilizer and petrochemical-producing facilities. Some is revamping work, and others are for new plants. Regarding South America, in the coming couple of years, we expect to see significant refining and petrochemical projects in Brazil, Venezuela, Columbia, and elsewhere on the continent. As I noted, we're not expecting much activity in the next one or two years for the U.S. refining or Canadian Oil Sands projects.

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In summary, activity in the international markets is picking up somewhat and, as a result, our sales mix will be more international in the coming years. It is clear the global economic downturn is having a measurable effect on the energy markets. Economists, energy producers, and market specialists are revising downward long-term demand forecasts. An example is OPEC's annual World Oil Outlook, which has lowered its projection for crude oil demand in 2030 by 8 million barrels-per-day when comparing their 2008 to 2009 forecast. That reduction is appreciable, and investment decisions are being evaluated currently due to changes in demand profile, crude oil pricing, and differentials between cost of high and lower quality crudes, utilization rates, project capital investment requirements, and the impact of proposed energy policies. This is a period of transition in our markets. However, our commitment to the energy markets has not changed, and our belief is that there is a demand for energy in all forms, be it fossil, alternate, nuclear, or renewable. We continue to expand and create growth opportunities, both organically and via acquisitions.

While in this transition, or down period, our strategy is to remain profitable. We are affirming our prior guidance for fiscal year 2010 to generate positive cash flow. Cash usage in our first quarter was related to timing and not to structural changes in the business. We continue to strengthen Graham, as it currently is, through becoming a faster company, internal development, investments in IT and production equipment to improve quality, reduce lead time and/or expand capacity, continuing to support our customers while they aren't spending, building stronger relationships, staying close to upcoming projects, and using our strong and flexible balance sheet to enable the Company to achieve higher levels of sustained earnings through acquisitions. Ultimately, we believe this downturn is an opportunity. Our plan is to emerge into the next up-cycle with greater market share, able to grow more rapidly than during the past up-cycle, have improved operating performance, enjoy greater product and market diversity, and being the supplier our customers want for their engineered-to-order equipment requirements.

The energy markets are inherently cyclical. As we execute our strategy for process improvement and growth, the effects of the cyclical markets will be dampened and earnings, we believe, more consistent. Predicting the timing for when our markets will recover is difficult. While we see excellent quotation activity across diverse end-use and geographic markets, when customers will step up to the table and place purchase order commitments is not clear to us.

As I mentioned, we are holding our prior guidance for revenue, gross margin, and SG&A in fiscal 2010. It is too early to begin to frame 2011 and in analyzing 2011 scenarios, there is both upside and downside risk from 2010. It is all dependent upon when customers begin making purchase commitments. We will continue to update you each quarter on our market fundamentals and our perspective on how they relate to our business.

Let me turn it over to Jeff now for a more detailed discussion on the first quarter.

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

Net sales in the first quarter of fiscal 2010 were \$20.1 million, a \$7.5 million decline compared with \$27.6 million in the first quarter of fiscal 2009. This level of sales was consistent with our expectations incorporated in our full-year guidance that we provided in May, projecting a 30% to 40% sales decline in fiscal 2010. Condenser sales were strong in the first quarter at \$5.2 million, 12% above the first quarter of fiscal 2009. These sales were driven by orders that Graham won early last fiscal year. However, sales across all other product categories, ejectors, aftermarket, heat exchangers, and pumps, were off a collective 35% in the first quarter of fiscal 2010, compared with last year's first quarter. By industry, as expected, we saw a shift away from refining, especially in the United States. Sales to refiners were down to 46% of total sales in the first quarter of fiscal 2010, compared with 52% in the same period last year; 24% of sales were to the chemical and petrochemical industries, up from 19%, and 30% were to the power industry and other industrial applications, up slightly from 29% last year.

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Graham's sales to the U.S. market in the first quarter of fiscal 2010 declined \$8.3 million, or 45%, to \$10.2 million, compared with last year's first quarter, and represented 51% of total sales. Somewhat offsetting this decrease was a \$900,000 increase in international sales to \$9.9 million, or 49% of total sales. In the quarter, we saw an increase in sales to Asia, but weakness in all other international markets. As we have mentioned in the past, we can have significant fluctuations quarter-to-quarter, and it is better to view the trends in our business by looking at the trailing 12 months. As Jim mentioned, looking forward, we do expect to see sales mix shifting toward Asia and the Middle East and away from the United States. For the trailing 12 months ending June 30, 2009, sales to Asia were almost 20% of total sales, up from 13% at the end of fiscal 2009.

We had unusually strong gross margins in the first quarter relative to the level of sales. Gross profit was \$8.3 million, or 41.1% of sales, compared with \$12.2 million, or 44.2% of sales, in last year's first quarter. The quarter's relatively high gross margin percentage was related to the rapid decline in specialty and other material costs used in manufacturing our products and, as Jim had indicated, opportunistic negotiations by our purchasing department. In addition, many of the orders that were shipped in this past quarter were placed before the industry dynamics changed. As we look forward over the next several quarters, we do not expect to see gross margin levels as sustainable and expect margins for fiscal 2010 will likely be at the upper end of the 28% to 31% range we have previously given as guidance.

For the first quarter of 2010, SG&A expenses were \$3.2 million, or 16.1% of sales, compared with \$3.8 million, or 13.8% of sales, in the first quarter last year. The restructuring that we undertook at the end of fiscal 2009, as well as lower commission costs related to the decline in sales, resulted in \$600,000 lower SG&A costs compared with last year's first quarter. For our previous guidance, we continue to expect that SG&A for fiscal 2010 will be in the \$13 to \$14 million range.

Interest income in the first quarter of fiscal 2010 declined to \$18,000 compared with \$131,000 in the same period last year, primarily as a result of the significant decline in U.S. Treasury yields. Our investments are in U.S. Treasury certificates with maturities of 91 to 180 days. Our effective tax rate for the quarter was just over 30%, down from 33% in last year's first quarter. We estimate our effective tax rate for fiscal 2010 to be between 30% and 31%. We are able to maintain our allowable level of tax deductions on lower than expected pre-tax income, which reduces the overall tax rate appreciably from the 35% we realized in fiscal 2009.

Given the advantages we gained in material costs in the first quarter, we had a strong bottom line despite the condition of our customers' markets. Our net income was \$3.5 million, with earnings per diluted share of \$0.35. This compares with last year's net income of \$5.7 million and EPS of \$0.56. We have repurchased 303,000 shares since our share buyback program was initiated early this calendar year, and that reduced our weighted average outstanding share level used in the EPS calculations.

Orders and backlog are continuing to show the impact of our customers' reductions in capital investment. Orders received in the first quarter of fiscal 2010 were \$8.8 million, down from \$27.8 million in the same period last year. As we have mentioned in the past, we expect quarterly orders during this disruptive period in the cycle to be quite erratic, and we suggest using trailing 12-month information to understand our order trends. Geographically, first quarter orders decreased across all regions, led by the United States and Asia. As noted in both releases this morning, we did receive a \$3.4 million Chinese refinery order very early in the second quarter. At the end of June 2009, backlog was \$37 million, 23% below the \$43.8 million backlog at the end of March 2009. We expect 85% of this existing backlog to ship within the next 12 months.

The quarter-end backlog number included \$4.2 million in orders on hold related to suspended projects. This number is slightly lower than the \$4.4 million level at the fiscal year-end in March, as one order for \$235,000 was moved back to active status. We did not have any cancellations or additional orders put on hold in the quarter.

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Graham's balance sheet remains strong, with cash, cash equivalents and investments totaling \$45.3 million on June 30, 2009, down slightly from \$46.2 million at the end of fiscal 2009. We used \$500,000 in cash for operations in the first quarter, whereas last year we generated \$6.9 million. This change was primarily due to the timing of receivables combined with lower net income. Our accounts receivable balance was up \$16.1 million from \$7 million at the end of March, but again, this is simply timing. We have seen no appreciable change in uncollectible receivable positions. In addition, in the first month of the second quarter, we have collected well over one-half of the outstanding receivables from June 30th and have significantly added to our overall cash position. Our cash conversion cycle at the end of the quarter also reflected the timing issue. It was up to 41 days, which compares with 17 days at the end of fiscal 2009. We expect cash conversion to reduce to a more normalized level in the second quarter and to continue to generate cash throughout the rest of fiscal 2010. We have no borrowings on our \$30 million bank line and are utilizing it solely for outstanding letters of credit, which totaled \$9.7 million at the end of the quarter.

Capital expenditures were \$80,000 in the first quarter of fiscal 2010 compared with \$219,000 in the first quarter last year. We still expect to pursue our capital plan, which is an important part of our internal development activities and, as Jim discussed, this will allow us to be able to capture an even greater market share in the next up-cycle. Capital expenditures for fiscal 2010 will be approximately \$1 million, and half that investment is for productivity improvements.

That concludes my remarks. Jim, I'll turn this back to you.

Jim Lines: Thank you, Jeff. Operator, please open the call for questions.

Operator: Thank you. Our first question comes from James Bank from Sidoti & Company.

James Bank: Hi, good morning. Jim, the backlog that we have in U.S. or domestic projects, how much is represented in the \$37 million of backlog you reported this morning?

Jim Lines: I don't have that statistic at my fingertips.

James Bank: Well, I guess what I'm trying to get at is that the high-priced inflationary work clearly worked in your favor with the gross margin in the first quarter. Is that, more or less, worked through, or is there still some of that still in that \$37 million?

Jim Lines: We still have in the \$37 million sales that will be for the U.S. market. The margin improvement that we enjoyed in our first quarter wasn't so much tied to geographic sales mix but more tied to the fact that the raw materials market had a rapid decline, and our procurement team was able to take advantage of that and come in well below our costs that we had estimated for those projects. We saw materials hit the floor and remain there for a few months, December through March, and our procurement team, as they were buying the materials for the projects where revenue was being recognized in the first quarter, did a great job to take advantage and be opportunistic at that time. So, it wasn't geographic-related, in my opinion, it was more the timing of where materials were.

James Bank: I guess, then, that would imply that it's probably not repeatable given your guidance?

Jim Lines: We don't believe so. Now, having said that, we're going to be aggressive in the market with our suppliers. There are times when there's capacity available at a given supplier where we're seeing them come off market pricing, and our procurement team, I'm expecting them to be as disciplined as they were in the first quarter and to take advantage of those opportunities. But we're not projecting and we would not recommend in your modeling to look at our first quarter margin as being sustainable.

James Bank: Because that leads me to this question. In regard to the guidance, to even go toward the high end of your guidance, if I want to assume \$70 million in sales, maybe it's \$13 million in SG&A, and go to the higher range of your gross margin guidance, I'm still hitting a single-digit earnings per share in September, December, and March quarters of this year. It's

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somewhat draconian and, obviously, grossly different from what you guys did in the first quarter, am I reading this correctly?

Jeffrey Glajch: Yes, you are.

James Bank: Jeff, this is one for you, please. The tax rate for the full year, I thought we were looking for 34%, but maybe with the first quarter at 30%, should I take it down a little bit?

Jeffrey Glajch: Yes, I think the tax rate for the year, we're looking to be in the 30% to 31% range.

James Bank: Is that something I should probably use in out-years as well?

Jeffrey Glajch: Depending on how you're viewing the out-years. I think if you're viewing the out-years with a similar level of profitability as this year, then yes. If you're viewing them with lower profitability, you could probably take it down a point or two. If you're viewing them with higher profitability, you could probably take it up a point or two.

James Bank: Then, looking at fiscal 2011, the SG&A, what you are guiding toward this year, is this, more or less, fixed? Could we assume \$13 to \$14 million in spend for fiscal 2011?

Jeffrey Glajch: I think that's going to be, to some extent, a function of the top line. Clearly, if it's similar to where we're at, I think that's a fair assessment. Again, similar to my comments on taxes, if you go up a little or down a little bit, there could be a little bit of a swing there. But I think that's a fair assessment as a first pass.

James Bank: Okay. And then, last question, when you guys use the word "measurably," and I'm not trying to put you on the spot here, but, "a measurable volatility" that you expect in orders, is it something that would look like what happened throughout fiscal 2009? I think we had \$27 million in June and \$17, then down to \$8 and then back up to \$20, now we're kind of back down to \$8, is that kind of volatility we should expect?

Jim Lines: Regrettably, yes.

James Bank: Okay. That's all I have. Thank you very much for your time.

Operator: Thank you. Our next question is coming from Dick Ryan from Dougherty & Company.

Dick Ryan: Good morning. Just a couple of questions on the backlog, 85% ships over the next 12 months, can you give out a little perspective as to how much might ship in the remainder of FY 2010?

Jim Lines: The majority of it will. There's a little carryover into FY 2011. The majority ships in FY 2010. With the exception of the \$4.2 million that is on suspension. The timing of that, when they are released to proceed is not clear, but we would expect conversion of the majority of the \$37, less the \$4 million on suspension, in fiscal 2010.

Dick Ryan: Okay. That was going to be my next question; if you could give a status or an update of the \$4.2 million and what could get that either moving to the left or to the right?

Jim Lines: In a follow-up with our customers that we do routinely to assess the quality of the backlog, they've only been able to indicate that they are still on suspension. We're projecting they would be released and revenue realized in 2011, but it's hard for them to predict, and they're not able to give us reliable indications of when the projects will reactivate, unfortunately. But they're not cancelled.

Dick Ryan: And nothing else is cancelled in Q1, anything else put on suspension? Obviously not, if this \$4.2 million is the same from the fourth quarter, correct?

Jeffrey Glajch: It was actually slightly different, it was \$4.4 million at the end of the fourth quarter. We did have one project that was just under \$250,000 dollars that had been on hold and has been released back into active status.

Dick Ryan: On the share buy-back, what's left under the program?

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Jeffrey Glajch: The program, actually, had expired in the last day or two, but has been extended by our Board for another 12 months. So, there was one million total shares less the 303,000 that have already been bought back, leaving just under 700,000 shares available to be repurchased.

Dick Ryan: As you look over the next one or two years, Jeff, you talked about the tax rate going forward, if that shifts more internationally, what could that do to margin expectations, if anything?

Jim Lines: Well, we've indicated that the 40-ish% gross margin that we had most of last year and in our first quarter, regardless of geographic sales mix, wasn't going to be sustainable. We would project that, in an up-cycle, mid- to upper-30s for gross margin, and near the bottom of the cycle, mid- to low-20s for gross margin.

Dick Ryan: Okay. Any significant price pressure going on on the competitive side, Jim?

Jim Lines: Yes. We're all very hungry. There aren't many projects where the buyers are stepping to the table, and we're seeing very aggressive pricing by everyone. We're seeing the buyers even add to their advantage, so there is price pressure.

Dick Ryan: Okay, that's great. Thank you.

Jeffrey Glajch: Dick, this is Jeff Glajch. I just want to clarify one thing on the backlog, I want to make sure that as you're thinking through this, you're thinking through it correctly and that we've stated it correctly. When we said that the backlog was \$37 million at the end of the quarter and that 85% of that is expected to ship in the next 12 months, that's 85% of the \$37 million, not of the \$37 million minus what's on hold. Inherent in the \$37 million is that \$4.2 million that's on hold, but our 85% number's off the \$37 million, not the \$37 million less the \$4.2 million.

Operator: Thank you. Our next question is coming from Greg Garner from Singular Research.

Greg Garner: Good morning. Just a quick clarification as a follow-up on that last question regarding the backlog. The \$37 million, 85% of which can be shipped in the next year, that \$4.2 million, you mentioned that may be shipped and most likely would return to an order in fiscal year 2010 to ship in fiscal year 2011, is that correct?

Jim Lines: There are orders currently in our backlog. We would project that as the customers release the projects, and revenue would be recognized in 2011. 15% of the backlog that we indicated would not ship in the next 12 months is the \$4.2 million.

Greg Garner: Okay, I understand that. I just wanted to get the timing for when you believe it would turn into revenue, but it looks like it's probably going to be a fiscal year 2011 event. You mentioned the excellent quotation activity. Is there any way to quantify that relative to the level of quotation activity in the last couple of quarters? I just want to get a sense for whether this activity is a result of projects that come back to you for a better price or are there a lot of new projects out there that they're just several years in advance to get pricing on? Can you give us a little color on that?

Jim Lines: A metric that we monitor continually is the level or the value of outstanding firm quotations. We classify a firm quotation as a project that we feel will move to equipment purchase. The aggregate value of the firm quotations, and we've mentioned this on prior conference calls, really hasn't changed appreciably over the last 12 to 18 months. It's been running at around \$250 million consistently. It may be down 10% but back up to \$250 million on average, so we haven't really noticed a discernible difference throughout the cycle and the value of our aggregate firm quotations. And I've mentioned this before, we're not clear. It's hard to predict when the buyers step to the table to make purchase commitments. But we are very busy in our sales management and quotation areas, keeping up with all the activity.

Greg Garner: And is there quite a bit more activity in the areas that you believe are going to recover more quickly?

Jim Lines: Yes, the Middle East, South America, and Asia.

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Greg Garner: Before, you've mentioned that margins in China were not the best, but it certainly seems like that's a good revenue growth area. How should I look at gross margins on this international versus domestic? Should I perceive international margins on the gross margin side to be a couple of percentage points lower?

Jim Lines: That's a fair model to use, yes.

Greg Garner: Thanks, and congratulations to the procurement team, they obviously did a good job.

Operator: Thank you. Our next question is coming from Michael Heaberg from Axiom Asset Management.

Michael Heaberg: Hi, Jim. Two quick questions for you. First of all, can you give us some sense of, of the seven orders you've gotten out of China, what kind of a close ratio you have. In other words, essentially how many quotes does that represent?

Jim Lines: For the seven that we won, and these are large ejector systems for a particular service in a refinery vacuum distillation application, we've made quotations on 12 projects that have proceeded in that timeframe, and we won seven counting the order that was announced yesterday. So, it's slightly over 60%.

Michael Heaberg: Second question, a couple of times you briefly referenced acquisitions as a strategy for growth. Can you give us any further color on what you might be looking for there?

Jeffrey Glajch: Sure, this is Jeff. We have laid out our acquisition thought process, and we're looking for one of two avenues, either a geographic expansion or product line expansion. Right now, all of our manufacturing is here in western New York, and we believe there's an advantage to our potentially having local manufacturing in other parts of the world, specifically Asia or the Middle East, and maybe China or India.

The other leg is more of a product line expansion to be able to offer our customers a broader array of products into a similar customer set as we have now. Those are the two avenues we're looking down. We are very active there, but we still think we're early in the process, and we're very patient.

Operator: Thank you. Our next question is coming from Rick Hoss from Roth Capital Partners.

Rick Hoss: Good morning, gentlemen. A question on the geographic distribution. We obviously saw a significant shift away from the United States, which I think you've been fairly vocal about with the expectation that Asia and international will eventually shift to become the majority of your revenue, at least, in the next several years. There has been quite a bit of industry news out lately, just two days ago, of China National Offshore announcing plans to expand a refinery with Shell. I was hoping you could just give us a little bit more appreciation for the opportunity in China, not only from a size perspective, but also from how quickly something like this could ramp up. Obviously, we'd see it in bookings and backlog, but as far as your expectations for how something could start to contribute in the fiscal timeframe, if you could?

Jim Lines: We're excited about the opportunities in China and the magnitude of those opportunities over an extended period of time. We believe China will continue to invest in its refining capacity along with its petrochemical-producing capacity. We've seen that in a given year, not more than three or four projects move together. There's just a supply chain constraint there, whether it's the EPC, the technical process licensors in China. We've not seen much more than that. So, that gives us a frame of the amount of business that would be available in a given year to win. If history repeats itself going forward, and I don't see supply chain dynamics changing where that three or four becomes 10 in a given year for refining.

Outside of refining and the petrochemicals, we are seeing the Chinese customers evaluate and go ahead with integrative refineries which would couple the refinery with a petrochemical-producing plant, increasing the scope for Graham, ethylene plants, other petrochemical-

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producing plants, that adds greater opportunity for those three or four projects that are moving together.

Also, China is involved in new fertilizer plant construction and other petrochemical-producing plants, such as coal-to-liquids. So, China represents a very large opportunity for us. Speaking specifically about refining, we don't see it as much more than three or four projects in a given year.

Rick Hoss: Along with Jeff's commentary a couple of minutes ago regarding acquisitive targets, would you consider something in power generation, and if so, would it be limited to the U.S. or would it also be a potential for a Chinese firm or a new product that was targeted in China?

Jim Lines: We absolutely would consider something in the power generation area and, geographically, we would not be limited to the U.S. It could certainly be outside of the U.S.

Rick Hoss: Could you say that if you were looking at expanding your product offering through a product targeted at power gen, would it be more likely to occur in the U.S.?

Jim Lines: It could go either way.

Rick Hoss: I think you've been fairly clear about indicating a desire to expand your capacity in China for more of your refining products. But, looking at power gen, I was just curious to see if it would be focused in China as well, or if it's just regionally agnostic?

Jim Lines: We are regionally agnostic. Obviously, if we look at a U.S. example, we would certainly want a situation where we could export also, but we are agnostic on where that actually occurs.

Operator: Thank you. Our next question is coming from George Walsh from Gilford Securities.

George Walsh: Jim, I wondered if you could speak a bit to the motivations in the macro decision-making for the purchase commitments of customers in relation to what you're seeing it now with what's impacting them as raw material costs, and perhaps the cracks spread between sweet and sour crudes, and on any other macro factors in the current status and maybe things that may change in the future to motivate them?

Jim Lines: George, what we see, in the U.S. market in particular, for the refining sector is that a number of things are affecting investment decisions, one being a reduction in demand, another being, consistent with reduction in demand, utilization levels for U.S. refiners has dropped from the low 90s to low 80s and are projected to go further into the upper 70's over the next 12 to 18 months. Also, the spreads. Many of the refiners had made significant investments to have feedstock diversity, be able to process for quality, lower-cost sour crudes. The spread, or the differential between sweet and sour, has narrowed. In some cases there is no difference, and that's affecting their profitability. And lastly, and very largely, is the energy policy that's being contemplated, which may be punitive to refiners, refiners that process sour crudes, refiners that have large emissions of carbons. So, there are several variables that are affecting investment decisions in the U.S.

If we move outside the U.S. and look at the Middle East or Asia, that's more triggered, we felt, by the costs of the projects coming down. We've seen in Saudi Arabia that a couple project announcements have come up where they're proceeding now with two or three refineries in Saudi Arabia linked to a reduction in the cost to build the plant. One was noted to be about a 20% reduction, from \$12 billion to under \$10 billion. We have mentioned in prior conference calls, our customers were moving to put projects on hold six to nine, 12 months ago while they expected costs to come down. They've seen some costs come down, we think they've hit the inflection point and are starting to come up, and hopefully that's the catalyst to get back into investing.

George Walsh: Now, Jim, is that mostly raw materials, or are they actually getting them re-bid a bit, because there is competition for work, there's lower margins on the part of engineers and others involved in the project?

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Jim Lines: There are two factors. One, of course, is, as you said, raw materials. Secondly, to their advantage, there's a scarcity of major project work available right now, maybe one or two at a given point in time, compared with 12 to 18 months ago when there were many, many available at a given time. So, they're being opportunistic in negotiating with the EPCs and negotiating with the equipment suppliers to get very good pricing. Not only have raw material costs come down, they're also being more aggressive with their procurement strategies to lower their costs further.

George Walsh: Do you think if something like the energy policy, like cap and trade, I don't want say dies or something, but if it really does not go through, that would have a major impact with the refineries? That they would have a better idea what they're facing in the future?

Jim Lines: Yes, that would help.

George Walsh: Okay, because even Valero, on their call, were quite adamant that they felt this was not a good policy and was very punitive for them.

Jim Lines: That's correct.

George Walsh: Okay, also, with M&A, I was just curious, one of the outlines you gave for parameters was a revenue stream of about \$60 million. How do you look at that? Is that something where you're looking at other cyclical companies and businesses? Is that something where that's peak revenue or that would be the current run rate, or just how do you view that?

Jeffrey Glajch: This is Jeff. We're looking at a range up to \$60 million, not that we wouldn't go above that or go below the bottom part of our range, which we suggested in the past to be maybe \$20 million. But we're looking kind of at a steady state, not that that wouldn't be a peak number or that would be a lower number, more an average-type number.

George Walsh: All right, thanks. Once again, congratulations on managing well in a in a tough quarter.

Jim Lines: Thank you, George.

Operator: Thank you. At this time, we have no further questions. I'd like to turn the call back over to Mr. Lines for any closing comments.

Jim Lines: Well, thank you, everyone, for your interest and your questions, and we look forward to updating you on this after the second quarter. Thank you.