

Transcript of ShawCor's Second Quarter 2006 Results Conference Call

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OPERATOR: Good morning, ladies and gentlemen. Thank you for standing by. Welcome to the ShawCor second quarter financial results conference call. At this time, all participants are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. Instructions will be provided at that time for you to queue up for questions. If anyone has any difficulties hearing the conference, please press * 0 for operator assistance at any time.

I will now turn the conference call over to Bill Buckley, President and Chief Executive Officer; Gary Love, Vice-President, Finance and Chief Financial Officer; and Jim McTurnan, Vice-President, Legal.

Please go ahead, Mr. McTurnan.

JIM McTURNAN (Vice-President, Legal, ShawCor Ltd.): Thank you, Melissa.

Today's conference call includes forward-looking statements that involve estimates, judgements, risks and uncertainties that may cause actual results to differ materially from those projected. The uncertainties include, among others, economic conditions, levels of drilling and pipeline activity, environmental and regulatory risks, liability claims, exchange rate fluctuations, political risk and raw material prices.

Further information on risks that could affect the company can be found in ShawCor's 2005 annual report and annual information form, as well as the quarterly reports for the first and second quarters of 2006.

Copies of these are available on SEDAR at www.sedar.com and may also be found on the ShawCor website at www.shawcor.com.

I'll now hand the meeting over to Bill Buckley.

WILLIAM BUCKLEY (President and Chief Executive Officer, ShawCor Ltd.): Thank you, Jim, and good morning, everyone. Thank you for joining us this morning.

I can say that we are quite pleased with our second quarter results and our earnings of \$0.34 per share. These results represent a significant improvement over the prior year. The improvement is due to a combination of factors. First, we had strong levels of activity in almost all of our business units and we're also seeing the effects of our operational improvement programs. This has been reflected both in the strong earnings and the strong margins.

I'd like to take some time this morning to discuss the major projects that we've recently secured and their impact on our outlook. But before doing so, I'll ask our new CFO, Gary Love, to provide you with some background on the second quarter results.

By way of introduction, Gary has been onboard with ShawCor in the position of Vice-President and Senior Controller, overseeing our divisional controllers since the beginning of this year. Gary joined ShawCor as part of Alan Thomas's planned retirement and I would like to say that Alan and Gary achieved a very smooth transition.

Gary?

GARY LOVE (Vice-President, Finance, Chief Financial Officer, ShawCor Ltd.): Well, thank you very much, Bill.

First, let me say how pleased I am to be speaking with you this morning. The seven months that I have spent at ShawCor and my travels to our many global operations have confirmed my belief that ShawCor has a tremendous future and we have a great team working to realize that potential.

Now, before commenting on the quarterly report, I'd like to remind you that our second quarter press release, if you don't already have it, is available on our website at www.shawcor.com.

Now Bill briefly noted our strong results in the quarter and I'd like to take a few minutes to elaborate on the underlying factors that resulted in the reported performance.

Revenues for the second quarter of 263 million were up 14 per cent over the second quarter of 2005. This growth was evident in our pipeline and pipe service segment with revenue of 227 million, up 14 per cent year over year, and also in our petrochemical and industrial segment, where sales of 36 million increased about 13 per cent.

Now if we look first at the pipeline segment, the most significant development in the second quarter was the continuation of very strong pipe coating demand in North America with sales increasing by about

70 per cent over the prior year. This was driven by strong, small diameter demand, both in Western Canada and in Mexico.

The other key factor in the second quarter was our project activity in the Far East. Our new Indonesian facility in Kabil operated at very high utilization rates throughout the quarter, as did our Malaysia facility. Work completed on major pipe coating projects, such as Ca Mau and South Sumatra to West Java, saw our Far East region revenues more than double compared with the prior year.

Now detracting somewhat from the otherwise strong sale performance in pipe coating was our Europe/Africa region where the completion of coating in the first quarter of 2006 on the Ormen Lange project in Norway and the Balgzand to Bacton project in the U.K. caused a 56-per-cent decline in year-over-year sales. And along similar lines, we were also impacted by project delays in Nigeria. On a year-over-year comparative basis, our other pipeline segment businesses reported about a 3-per-cent increase in revenue.

Now if we look at the second quarter of 06 and compare it to the first quarter of this year, sales in the pipeline and pipe service segment were up about 2 per cent. Now this exceeded our expectations and, in a large part, was due to the continuation of the strong pipe coating activity in Western Canada and those large projects that I mentioned a moment ago in Malaysia and Indonesia.

Now if we turn to our petrochemical and industrial segment, sales increased by 13 per cent year over year and also increased by 3 per cent over the first quarter of this year.

As mentioned on previous conference calls, the ShawFlex custom wire and cable business is booming with significant activity throughout the Canadian resource sector and in particular, work that we're doing in connection with oil sands developments.

DSG's revenues were broadly unchanged from the prior year but did improve modestly from the first quarter of this year on a slight pickup in the European automotive market.

As a final note on revenues in the quarter, I'd like to highlight the impact the strengthening of the Canadian dollar has had on the translation of our foreign currency entities. I mentioned earlier that our consolidated sales increased by 14 per cent over the second quarter of 2005. Now when we factor out the impact of the higher Canadian dollar, our underlying business growth in revenues on a year-over-year basis was closer to 25 per cent.

Now turning to operating income from continuing operations, we again reported strong results at 35.8 million, an improvement of 188 per cent over the second quarter of 2005. While both of our segments showed year-over-year improvement, the dramatic change was in our pipeline and

pipe service segment where operating income grew from 12.9 million in the second quarter of 2005 to 36.3 million in the second quarter of 2006.

This improvement was driven by the strong revenue growth and improved operating margins in the North American and Far Eastern regions of Bredero Shaw.

Compared to the first quarter of 2006, operating income in the pipeline and pipe service segment fell by about \$1 million with operating margins declining from 16.6 per cent to 16 per cent.

Despite the weak performance from the North Sea and Nigeria, operating margins overall continued to improve at Bredero Shaw. So this slight reduction in pipeline segment margins from the first quarter was, in fact, attributable to lower margins at Canusa-CPS and the seasonal decrease in Guardian pipe inspection activity during spring break-up in Western Canada.

On a final note, on our pipeline segment results from the second quarter, you will notice that our share of earnings in an associated company reached 1.7 million in the quarter versus 1.3 million in the first quarter of 06 and breakeven a year ago. This result is indicative of the operational performance of our Saudi Arabia joint venture which is currently experiencing very strong market conditions.

Turning to the petrochemical and industrial segment, operating earnings, at 3.9 million, were improved by 11 per cent from the prior year

but down from the 4.6 million reported in the first quarter. Operating margins in this segment, at 10.8 per cent, were greatly affected by the impact of higher material prices, including copper at ShawFlex and polyethylene at DSG.

The sharp escalation in copper in April and May was particularly difficult to manage as the increases occurred so rapidly that full pass-through to customers was not achieved. We do expect though that with commodity situation somewhat more stable now, we will see margin improvement at ShawFlex in succeeding quarters.

In addition, the capacity expansions that we are currently undertaking at ShawFlex will allow us to reduce our sales order lead time and better match the purchase cost of copper with the commodity cost that's embedded in our selling prices.

Now, with respect to currency translation, the impact of the stronger Canadian dollar on the translation of foreign entities reduced reported Canadian dollar operating income by \$2.4 million.

If we look at depreciation in the second quarter that came in at 9.5 million, which was down about \$2 million from the prior year and \$600,000 lower than the first quarter. In both cases, the reductions are attributable mainly to the lower amortization in Norway following the completion of the Ormen Lange project. This reduction was mitigated somewhat by the commencement of our new facility in Indonesia. In the

second half of 2006, we will see increases in depreciation as our new plants in Brazil and Portland start up operations.

So with operating income down slightly from the first quarter and depreciation down 600,000, EBITDA came in at 45.3 million or \$0.60 per share; the EBITDA margin of 17.2 per cent in the second quarter compared with 18.4 per cent in the first quarter. But of course, this was vastly improved from the 10.4 per cent EBITDA margin in the second quarter of 2005.

The income tax expense of 10.4 million in the second quarter represents an effective tax rate of just under 29 per cent. This is considerably below our expected tax rate of 34 per cent.

Three factors are affecting our tax rate. One, we continue to utilize tax losses in the U.S., the benefit of which has not been previously recognized. Therefore, as we generate income in the U.S., we realize a reduction in our overall tax rate.

In the second quarter, the benefit from the U.S. losses was partially offset by losses from operations, principally Nigeria, where we are not booking any tax benefit.

Finally, we did see – and this is the third factor – the benefit of lower corporate tax rates in Canada, both at the federal and Alberta provincial, level which had the affect of reducing our tax rate by about 3 percentage points.

So in summary, net income from continuing operations at 24.9 million, or \$0.34 per share, is greatly improved from the 7.6 million, or \$0.10 per share a year ago and was even slightly ahead of our first quarter result of 24.7 million, or \$0.33 per share. Subtracting the tax benefit from the second quarter result would have reduced the earnings per share to approximately \$0.32 per share.

With respect to cash flows, cash provided by continuing operations for the second quarter before working capital changes was 31.4 million, or \$0.42 per share. This improved 188 per cent from the year ago and that improvement, of course, was consistent with the growth in operating income. Net working capital increased by 2 million in the second quarter, but that was basically in line with the sales increase.

A note that in the first quarter of this year, we recorded a large reduction in working capital mainly as a result of the wind down of the Ormen Lange project which released receivables and inventory investments. Year to date, the change in working capital provides a source of cash flow of \$14 million.

Capital spending in the quarter totalled 12.6 million with the major projects being the purchase of an inactive coating line in the Far East that we will redeploy in that region, the purchase of land in Alberta to support several new booked large-diameter pipe coating contracts, the

commencement of spending on our new facility in Portland, Oregon, and new capacity to relieve bottlenecks and both Canusa-CPS and ShawFlex.

The final item of note in our quarterly cash flow is the dividend which is now being paid quarterly versus semi-annually in prior years. This provides for an effective doubling of the yield. In addition to the dividend payments, we also purchased during the second quarter approximately 236,000 class "A" shares under our normal course issuer bid. We did those purchases at an average price of \$17.80 per share for a total cost of \$4.2 million.

Year to date, our balance sheet has continued to strengthen. Our cash resources year to date have increased by 45 million. At the end of the second quarter, we had total cash resources of 246 million. We have no net debt and if we look at our gross-debt-to-capital-ratio, it currently stands at I think a very conservative 0.13 to 1.

On that note, I'll turn it back to you, Bill.

WILLIAM BUCKLEY: Thank you, Gary.

Now I'd like to provide you with some of our operational highlights from the second quarter, as well as offering you some background on the new contracts which we've recently been awarded.

During the quarter, at Bredero Shaw, business activity was very strong in our mid and Far East regions. This offset the significant reduction in activity at our North Sea facilities as a result of the completion

of the Langeled project. In our Americas region, activity was only slight reduced in the quarter when more significant declines are normally experienced due to seasonality.

One of the important operational highlights in the quarter was the strong performance of our new Indonesian facility in Kabil. After a very fast ramp-up in the first quarter, Kabil operated at near capacity levels during the second quarter. This facility is world class and provides us with a strategic advantage in this important region.

Other key operational developments in the second quarter included the completion of our new (thermo-tight facility in Brazil, the preparation of our Ras al Kaimah facility in the Emirates to commence the KOC project which involves corrosion and concrete weight coating on 56-inch diameter pipe.

In the quarter, we also began the installation of equipment at our new coating facility in Portland, Oregon. Operations at Bredero Shaw were also focused on the necessary measures to contain our cost structure in Europe and Africa.

With the completion of coating on the Langeled and Balgzand to Bacton projects, we undertook actions in the second quarter to substantially reduce costs in Scotland and Norway and to demobilize facilities that will be inactive for the next 12 months.

Although we incurred approximately 1.8 million in onetime cost, these measures will generate benefits for the balance of 2006 and 2007. Beyond 2007, we expect the North Sea region to provide growth as significant new projects come on stream in this region.

Our other divisions also accomplished notable operational objectives that will benefit future results. At both Canusa-CPS and ShawFlex, we are adding capacity to meet growing demand. At Guardian, we achieved significant progress in the second quarter in preparing a new facility that is collocated with a major customer to offer integrated pipe inspection and refurbishment.

We have suggested in previous conference calls that our second half 2006 will weaken significantly from the pace set in the first half strictly due to project timing. This is still our expectation. We have indicated that we expect large diameter project activity to begin to increase in 2007 and provide significant growth in 2008. Recent contract awards confirm our expectations.

During the second quarter, we announced two major new contract awards, the Corridor and TMX projects in Western Canada and the Rockies Express project in the U.S.A. With the Rockies Express project, we have been awarded the pipe coating contract for the first phase of the construction and will commence coating in the fall. The award of further phases of Rockies Express could see the project extend into 2008.

More recently, we've been awarded contracts for the Wapasu and southern access phase one projects in Western Canada with a combined value of approximately \$30 million. The Wapasu project will be coated with our proprietary high-performance composite coating, or HPCC.

In the Far East, our project backlog would indicate some softening in the second half but as in North America, we see a return to current levels in 2007 with further growth potential depending on our success in securing some of the major large-diameter orders that we're currently bidding. The largest of these is the Papua New Guinea project. That alone could absorb much of the industry's capacity in the Far East. We are confident that our new Kabil, Indonesia facility and our large facility in Kuantan, Malaysia will play an important role in this project.

With the recently announced Rockies Express project, our order backlog stands at 308 million. The Wapasu and southern access phase one projects noted earlier will add another 30 million. Based on our current bid activity, we expect our backlog to increase as we move through the second half.

Now on one final note, with respect to our proposed acquisition of Garneau Inc., the plan of arrangement was approved by the Garneau shareholders back on May 30th and was subsequently ratified by the Alberta court. As we press released yesterday, the Competition Bureau is continuing its comprehensive review of this transaction. We cannot close

this transaction until we receive the necessary clearance and we cannot confirm to you, at this time, that the deal will proceed but we are continuing to work with the Bureau.

In summary, the two strong quarters reported year to date are solid evidence that our improvement initiatives are being realized. The next step in margin improvement will occur as we generate better utilization of our large-diameter pipe coating facilities and we expect this to occur in 2008 and begin in early 2007.

In the interim, we have a very strong balance sheet that provides us with an advantage versus our competitors and will enable us to take advantage of the opportunities presented by the growth in the large-diameter project activity.

And with that, we'll turn the call back to the operator for questions.
Operator?

OPERATOR: Thank you. Ladies and gentlemen, we will now conduct the question-and-answer session. If you have a question, please press the * followed by the 1 on your touchtone phone. You will hear a tone acknowledging your request. Your questions will be polled in the order they are received. Please ensure you lift the handset if you're using a speakerphone before pressing any keys.

The first question comes from Dana Benner, from Westwind Partners. Please go ahead.

DANA BENNER: Thanks and good morning, gentlemen.

WILLIAM BUCKLEY: Good morning, Dana.

DANA BENNER: I just wonder if you could provide us a little bit of guidance on the back half of the year here. You know, obviously you've put up some very good numbers for the first half and, you know, reasonably consistent margins; but I would imagine you're looking at these margins quite favourably, certainly in relation to where you've been the last few years and you probably have a target of moving them even higher.

So I just wonder if perhaps you could give us a bit of colour on the back half of this year and then whether you think you may have even another point or two to go on margins, principally on the pipeline and pipe services side next year?

WILLIAM BUCKLEY: Yes. Dana, in the second half, our revenues are going to be down substantially and that's related to the project timing. And with that, our profits will be down but our margins will also go down due to the utilization factor. We can bring down our variable costs but we can't affect our fixed costs to a great extent in our fixed plants.

So generally, we are seeing improved margins due to better execution. That improvement will continue but you will notice in our numbers in the second half some deterioration in margins that's related to plant utilization.

DANA BENNER: And then I guess as you look out to next year, acknowledging the product mix or I guess the job mix that you currently have in backlog, large diameter, small, mid, etcetera, you know, and of course, I'm sure you'll be pursuing optimal execution, what's reasonable to target? Can you guys do 17 to 18-per-cent margins in that segment or is that a little aggressive?

WILLIAM BUCKLEY: Well, Dana, as we go into next year, we expect that through 2007, we'll see activity increase in the Far East region and Mideast regions. And they should get quite active as we get towards the end of 2007. Then we see the North Sea coming back in 2008 with the NEG project and the Troll project hitting in the 2008 timeframe.

Through that whole period though, we expect the Americas region to be quite strong. And with that, you should see margins that reflect the execution improvement that we've commented on before. You should see margins that are improved because of the utilization in our facilities and you should see some further margin improvement that I don't think is reflected yet but will be in the future, that's going to be a result of just the increased levels of activity and us beginning to have some pricing power in large diameter.

DANA BENNER: So that sounds to me like you think you can move your margins at least a couple of points higher next year with good execution.

WILLIAM BUCKLEY: As we move towards the end of next year, I think you'll see the margins improving and then I think 2008 is when you see those three factors coming together.

DANA BENNER: Great. And, sorry, I missed your tax rate guidance. Is it 34 through the balance of this year and through next year?

GARY LOVE: Thirty-four has really been our historical expected rate, or at least over the last few years. It's going to come down and for the balance of this year, I think it's going to be closer to 31, 32.

The reduction in rates that we saw in the second quarter were, in a sense, one-time factors. It's because we did get a recovery of what had been provided in the first quarter. So the second quarter was certainly benefited by that. On a go-forward basis, it's going to be closer to 31, 32 rather than the sort of historical 34 per cent level.

DANA BENNER: Great. That's all I've got, guys. Thank you.

WILLIAM BUCKLEY: Thank you.

OPERATOR: Your next question comes from John Rogers, from D.A. Davidson. Please go ahead.

JOHN ROGERS: Hi, good morning.

WILLIAM BUCKLEY: Good morning.

JOHN ROGERS: You mentioned the impact of higher copper prices but I was curious about energy prices and oil prices and how they were

affecting your costs and what your expectations were going forward now and whether you can pass all those through, especially in the coatings?

WILLIAM BUCKLEY: Yes, good question. Energy costs impact our plants, our coating plants. We do a lot of seating of the pipe and heating of our materials as we process them. To date, we've had those increases. We've also had perhaps more significant cost increases in our coating plants that have been related to what's been happening with polyethylene and iron ore. And you know, with some lag, we have been able to pass those through to our clients.

In some of our other businesses – you mention energy costs in particular – in some of our other businesses, particularly our Guardian business, a lot of that business is done with trucks that go to drill rig locations to effect the work. And there, rising fuel costs have been a challenge and I would say that they have been successful in passing through the majority of those cost increases to date.

JOHN ROGERS: Okay. And then, secondly, I was just curious on the second portion of the Rockies Express coating, when do you expect that contract to be let?

WILLIAM BUCKLEY: We don't expect that to be let until early 2007.

JOHN ROGERS: Okay. Okay, great. Thank you.

OPERATOR: Your next question comes from Neil Jacobs, from Beaudry Capital. Please go ahead.

NEIL JACOBS: Hi. Good morning. Congratulations on the quarter and thanks for the very thorough review. I just have one minor question which is, you mentioned I guess, the NOLs in the U.S.

WILLIAM BUCKLEY: Um-hmm.

NEIL JACOBS: How big is that NOL and how long do you foresee it lasting?

GARY LOVE: Approximately 30 million U.S. and it will certainly be available for use as we go forward. We would expect to utilize it between now and either end of 07 or at some point in 08.

NEIL JACOBS: And how do you, just out of curiosity for the Rocky Mountain Express, will that all be U.S. based?

WILLIAM BUCKLEY: Yes.

NEIL JACOBS: Okay.

WILLIAM BUCKLEY: Sorry, the coating for the Rockies Express order will actually be done in two of our facilities. It'll be done in our Portland, Oregon, facility and also in our Camrose, Alberta, facility. And the split is about equal.

NEIL JACOBS: Right. But for tax treatment, is it all treated as U.S. income or not?

WILLIAM BUCKLEY: No. No, the income will be dependent on where the coating's done. But certainly the new facility in Portland, Oregon, it's our expectation that that will help us in utilizing the NOLs.

NEIL JACOBS: Gotcha. Thanks a lot.

WILLIAM BUCKLEY: Thank you.

OPERATOR: Your next question comes from David Sachs, from Lucchi(phon) Capital. Please go ahead.

DAVID SACHS: Good morning, gentlemen.

WILLIAM BUCKLEY: Good morning.

DAVID SACHS: A couple of quick questions. One, if you could address the Garneau timeline as to what happens next, when do we expect to hear from the competition committee? How close to finish on the review are they?

And then if you could amplify a little bit on your comments on pricing power for large-diameter pipe in the upcoming cycle? Maybe you can give us some hint as to what it looked like in the last large-diameter pipe cycle in terms of our ability to up-charge and what the value per tonne is for large-diameter pipe versus maybe standard drill pipe? Thanks.

WILLIAM BUCKLEY: David, with respect to your first question, the Competition Bureau is going through a process. At the moment, they're conducting field interviews. They've also circulated a rather extensive information request to several industry participants and they're waiting to get these back and then they'll complete their analysis of that information when they get it back.

The timing on that could be three to four weeks before they get all the information that they've requested back and then, as I say, they need time for analysis. We've met with the Bureau and we're continuing to provide them with information to help them with their determination and we expect that we will be meeting with them again within that two- or three-week period.

With respect to your second question on pricing power, the last time we saw large-diameter pricing power in our business was in 1998 and you can go back and kind of look at those numbers to get a feel for what margins looked like in that type of an environment. We expect that, as I mentioned, we'll begin to see the impacts of increased margins due to pricing later in 2007. Some of those jobs we're beginning to bid now and we'll see the full effect in 2008.

DAVID SACHS: You also mentioned you'd be starting to coat the Rocky Mountain project in the fall. Is that earlier than you had initially thought?

WILLIAM BUCKLEY: No. That's about the timing that we expected. We expect we'll be coating in Portland right now in October-November. Timing depends a little bit on mobilization of our facility and our client's facility.

But that's about the timing we expected and I guess we had been working on this order for a long time and felt that we were going to receive it but the actual purchase order we actually got rather recently.

DAVID SACHS: On these long-term contracts, what type of pricing protection do you have based on raw material issues or work to the extent that your pipe supplier is either delinquent in terms of getting you the pipe? What kind of protections to you have?

WILLIAM BUCKLEY: We have some protections. In terms of pipe delivery, we have some protections built into our contract that speaks specifically to that. On the raw material side, we have two methods of addressing raw material escalation during a project. One is the use of escalation clauses. The other is to work with our suppliers and to actually obtain fixed prices for a given contract. And generally, we move to fixing prices with our raw material suppliers as we get closer to a firm contract date.

DAVID SACHS: Okay, and just one last question on the large-diameter pipe cycle. You're saying the last significant pricing power timeframe was in 1998. I don't believe the shape or the size of the cycle in 1998 was nearly as large as what we're looking at. At least, presently. In North America, there's 5.9 million tonnes of quotations out for bid, excluding Alaska today, which could give us over 9 million tonnes in North America, all scheduled between end of this year and 2010 or 2011.

Based on what your understanding is industry capacity is, how would the industry deal with such a large quantity or demand bubble coming for large-diameter pipe?

WILLIAM BUCKLEY: Yes. David, I think your observation is accurate. We anticipate that the revenue bubble in this cycle compared to 1998 will be much higher. But in response to your specific question, what we are seeing is we're seeing pipe coming into North America or proposed to come in to North America for these projects from overseas.

And back in 1998, the major project at that time in North America was the Alliance pipeline and that, of course, was built with all domestic Canadian or U.S. pipe.

So how the bubble's going to get served this time is by maxing out all the capacity in the mills in North America. Additional capacity is being added and there's been announcement on that by the steel companies, including a recent announcement in the last couple of weeks on some new capacity coming on. So the domestic suppliers are expanding their capacity to meet the need and some of the capacity is going to get filled definitely from pipe from offshore.

DAVID SACHS: And if it's delivered from offshore, you'd be coating it domestically. So it comes uncoated?

WILLIAM BUCKLEY: To date, on the projects that we're working on, that's how it is going to come in on the projects that we have bid that is

using offshore pipe. The reason for that, generally, David, is that there can be coating damage if the pipe is coated offshore and then put on vessels and then unloaded and then put on rail cars and then taken to the right of way. So the preferred method is to coat it as close to the right of way as possible. So that argues in favour of the coating being done in North America for these North American projects.

DAVID SACHS: And one last follow up on this. In the types of coating that you're looking at deploying today, it seems like you're using more proprietary coatings than there might have been in existence seven or eight years ago in the last cycle. So does that suggest, on top of the pricing leverage that we might get, given the proprietary coatings, perhaps the margins are dramatically different as well?

WILLIAM BUCKLEY: Without speaking specifically to the margins, I can tell you that we have a very strong R&D and product development program running in the company right now with the objective of providing more proprietary products to the marketplace.

And we want to do those and provide those products to our customers to save them money on their projects. So our high performance composite coating in all of its variations, with side extrusion and with rock jacket covers put on it, allow our customers in some of these remote pipelines to put the pipeline in the trench, use as found backfill, not be

required to bring in sand padding machines or bring in select backfill and this can have significant savings for our clients.

So we have a number of development programs underway. That's just one of them. We work closely with our clients to find ways in which we can bring coatings to their projects that are going to save them money on their total project cost. And we'll continue to do that. That is a major thrust in our Bredero-Shaw business today and it's been a thrust in all of our other businesses for many years.

DAVID SACHS: And is there adequate coating capacity in the market today to serve this demand increase that you're foreseeing in (inaudible) besides ShawCor is in a position to serve the North American market. And then maybe you could talk geographically about the other major regions as well. Thanks.

WILLIAM BUCKLEY: Yes. Generally, there's other coaters throughout North America but in terms of the capacity requirements, as we project them going forward, we're putting plans in place to make sure that we have all of the capacity that our clients need for their projects.

And I'd just point to the 130-acre site that we acquired, we announced in this last month that we acquired. That's for double jointing of pipe. But it also gives us expansion space in Camrose and we're expanding our capacity in our Regina facility. We've put our HPCC coating

in there earlier this year. That capability is there and it's quite likely that we'll continue to expand in the Camrose area to meet our clients' needs.

So there's not a problem of there not being sufficient coating capacity in Canada to meet this bubble. We're fortunate that we have the strong balance sheet that we have and we're definitely committed to investing that money to put the capacity in place to meet our clients' needs so there is no shortfall.

DAVID SACHS: Okay. I'll get back in queue. Thank you.

WILLIAM BUCKLEY: Thank you.

OPERATOR: Your next question comes from Neil Jacobs, from Beaudry Capital. Please go ahead.

NEIL JACOBS: I guess just as a follow up to that question, I was quite intrigued by your comments on the PNG pipeline. Where in your opinion does that stand? Is it a foregone conclusion that it's going to happen? That capacity for the region, can they go ahead and build that without involving you in some way?

WILLIAM BUCKLEY: I guess it's possible but not very likely because we have the majority of the pipe-coating capacity in that region.

In terms of likelihood of the project going ahead, we've had preliminary bids in for several months now. We're currently being asked to put in firm bids and those are actually going in over the next 60-day period.

We expect, from the client that letters of intent, at least the plan now, the schedule now indicates that letters of intent will be issued by the clients and there's two involved in this project, two consortia, but the letters of intent will be issued in the first quarter of next year.

There has been a little slippage in the project. If you look back over the last 12 months, it's about three months behind their original schedule from a year ago.

The gas that will come into Australia will go down south and be connected into the grid that goes down all the way in to New South Wales. And then there is also a lateral that's quite important that will go across the Bay of Carpentaria and that's to bring gas to a major aluminium refinery there.

So I understand the contracts are in place for the gas purchases but you're never sure that these projects are going ahead until you have the purchase order.

NEIL JACOBS: Gotcha. And your capacity in the region, how do you measure it? How big is it?

WILLIAM BUCKLEY: Well, we don't give out specific numbers on that, but we have the Kabil plant, the new Kabil facility that we put in place and that replaced an older, outdated facility that we had in Indonesia. It's now located on a deepwater port. It's got our latest technology in a very modern-type setting and it's a first-class facility with good capacity.

By way of comparison, the second facility that will likely be involved in this project in our Kuantan, Malaysia, facility and on that one site in Kuantan, we have five coating plants, if you like. So it's our largest facility. As a matter of fact, it's the largest coating facility in the world.

The third plant that will come into play on this is our smaller but effective plant that we have in Australia and it's located just south of Sydney.

NEIL JACOBS: Great. Thanks a lot and good luck.

WILLIAM BUCKLEY: Thank you.

OPERATOR: Your next question comes from David Sachs, from Lucchi Capital. Please go ahead.

DAVID SACHS: Yes, just a quick follow up on the balance sheet. Any thoughts in terms of whether it be dividend increase, share repurchase or what the environment looks like for growth of the acquisition as you look at your balance sheet today? It's been a really long time.

WILLIAM BUCKLEY: Yes, David, our balance sheet is quite strong right now. When we look at the ramp-up in business that's coming through 2007 and 2008, there's going to be some pretty significant capex costs and working capital costs. But beyond that, we think there's going to be some significant opportunities for new mobilizations and we want to have basically our powder dry to be able to take advantage of those and convert

those into global share gain. We think there will also be opportunities for some new geographical expansions. We want to be ready for those.

In addition, between now and then, you know, we're always looking for acquisition and joint venture opportunities and the good news is we have a balance sheet that can support any of those good initiatives that we can identify. So that's where our focus is right now in terms of utilizing the balance sheet.

We were though, able, on May 9th to announce that we're going to double our dividend and make it quarterly instead of semi-annually and we continue to look at bringing those kinds of values to our shareholders as well.

DAVID SACHS: Okay. Last question for me. Since I'm closer to the North American market and have a better understanding of the demand circumstances around large-diameter pipe in this country, could you perhaps walk around the globe and talk about North Sea and the Far East and South America in terms of whether they're common on similar demand opportunities that you see over the next even beyond 2007 and 2008, but where do you think there will be significant production or demand requirements?

WILLIAM BUCKLEY: Yes, okay. Between now and sort of like 2008 period, you're seeing North America's strong and it's going to get stronger. In the Far East, you're seeing major projects like Papua New Guinea

perhaps hitting and being executed in the 2007-2008 timeframe. Middle East is going to be quite strong with gas and LNG plants. And then, as I said, towards later in 07 and in 08, that's when the North Sea comes back with a couple of major projects. The North European Gas project, which is the Gazprom project, to bring Russian gas down into Germany and to do that completely offshore. And the other project, which is the Troll project, and that's for the Troll development which is in Norwegian waters.

Beyond that, where we think development is going to go is Russia obviously is going to be a very, very important provider of pipeline activity for the industry. They have arguably 30-32 per cent of the world's gas. They will want to bring that to market. It will probably go to markets in Europe and perhaps China as well.

There will be activity, more significant development activity, we believe, in China and that market will become increasingly important beyond the 2008 timeframe. And then finally India and bringing more energy to the Indian subcontinent will become increasingly important.

So those are the markets that we see as being increasingly important beyond that 2008 horizon.

DAVID SACHS: Okay, great. Thank you very much.

OPERATOR: Ladies and gentlemen, if there are any additional questions at this time, please press the * followed by the 1. As a reminder,

if you are using a speakerphone, please lift the handset before pressing the keys.

Gentlemen, there are no further questions at this time. Please continue.

WILLIAM BUCKLEY: Okay. Thank you, Operator, and thanks to everyone who called in today and thank you for your questions.

OPERATOR: Ladies and gentlemen, this concludes the conference call for today. Thanks for participating. You may now disconnect your lines.
