TWIN DISC, INC.
2011 FOURTH QUARTER FINANCIAL RESULTS
August 2, 2011, 14:00 ET

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Twin Disc Incorporated Fiscal 2011 Fourth Quarter Financial Results Conference Call. During today's presentation, all parties will be in a listen-only mode. Following the presentation, the conference will be opened for questions. If you have a question at that time, please press the star, followed by the one, on your touch-tone phone, and if you need operator assistance at any time during the call, you may press star, zero; and for participants using the speaker equipment, it will be necessary to pick up your handset before making your selection. This conference is being recorded today, Tuesday, August 2nd, 2011.

I would now like to turn the conference over to Mr. Stan Berger. Go ahead, sir.

Stan Berger: Thank you, Jo [ph]. On behalf of the management of Twin Disc, we are extremely pleased that you have taken the time to participate in our call and thank you for joining us to discuss the company’s fiscal 2011 fourth quarter and full-year financial results and business outlook.

Before I introduce management, I would like to remind everyone that certain statements made during the course of this conference call, especially those that state management’s intentions, hopes, beliefs, expectations or predictions for the future, are forward-looking statements. It is important to remember that the company’s actual results could differ materially from those projected in such forward-looking statements. Additional information concerning factors that could cause actual results to differ materially from those in the forward-looking statement is contained in the company’s annual report on Form 10-K, copies of which may be obtained by contacting either the company or the SEC.

By now you should have received a copy of the news release, which was issued this morning before the market opened. If you have not received a copy, please call Annette Mianecki at 262-638-4000 and she will send a copy to you.

Hosting the call today are Michael Batten, Twin Disc’s Chairman and Chief Executive Officer; John Batten, President and Chief Operating Officer; and Chris Eperjesy, the company’s Vice President of Finance, Chief Financial Officer and Treasurer.

At this time I will turn the call over to Mike Batten. Mike?

Mike Batten: Thank you, Stan and good day everyone. Welcome to our fourth quarter and fiscal 2011 year-end conference call. I will begin with a brief summary statement and then John, Chris and I will be ready to take your questions. We assume that you have already seen our press release, so I will be brief.

As you all know, Twin Disc has been benefitting from a strong surge in demand from the oil and gas industry. This has resulted from three factors: first, the improving macro-outlook for unconventional drilling around the world; second, the increasing service intensity of the fracturing process; and third, the acceptance of our transmission as the new high horsepower standard of reliability and durability in the industry. Demand for our 8500 Series transmission has been very strong, and our new 7500 Series transmission entered production at the end of the fourth quarter. We are very encouraged about the prospects for these innovative products going forward.

As you have seen from our press release, net earnings rose exponentially on a 36% increase in sales for fiscal year 2011, as a result of the operating leverage gained by the volume increase, improved manufacturing efficiencies and absorption, as well as the favorable mix of business. Gross margins improved year-over-year to 34.7% from 26.6% the year before. Net earnings attributable to Twin Disc for the fiscal year 2011 were $18.8 million or $64 per diluted share compared to $597,000 or $0.05 per diluted share for fiscal 2010.

Net sales rose to $97.4 million for the fourth quarter, compared to $64.3 million for the same period a year ago. Gross margins rose to 37.1% in the three-month period, up from 30.2% recorded in the same period a year ago. Net earnings for the current fourth quarter reached $7.6 million or $0.66 per diluted share, compared to $2 million or $0.18 per diluted share last year. EBITDA for the fiscal ear 2011 was a strong $43.5 million or $0.14 per sale—14% of sales, compared to $13.7 million for fiscal 2010 or 6% of sales. During the fourth quarter, EBITDA was $16.3 million or 17% of sales, compared to $7.4 million or 12% of sales for the same three months of the previous year.

As indicated above, our strong year and fourth quarter were in large measure driven by the strength of the oil and gas industry. However, we have seen some more modest improvements in our other selected market areas, namely industrial, marine and military sectors. Our six-month backlog has risen to another record level of $147 million, compared to $140 million in March and $84 million last year. Our product market and geographic diversity continues to help us weather the softer demand of the many—of many of the world economies, and we remain confident in our design differentiation and new product innovation to continue our growth outlook.

That concludes my prepared remarks for today and now John, Chris and I will happy to take your questions. Jo, will you please open the lines for questions?

Operator: Thank you, sir. Ladies and gentlemen, as a reminder, if you have a question, it is star, one on your touch-tone phone at this time. If you would like to withdraw your question, please press the star, followed by the two, and remember, if you're using speaker equipment, you will need to lift the handset before making your selection. One moment for our first question.

And our first question comes from the line of Peter Lisnic with Robert W. Baird. Go ahead please.

Peter Lisnic: Good afternoon everyone.

Speaker: Make it easier to hear.

Speaker: Hi, Peter.

Peter Lisnic: **I guess the first question on backlog, the number up sequentially and at a record level, can you just help us understand what the components of that increase were? I know you mentioned oil and gas, but I'm particularly interested in what sort of impact the 7500, now that you're producing it and shipping it, what that may have had impactwise on the backlog.**

John Batten: Well, Pete, the first part, all of our products were up in the fourth quarter in the backlog. We had a nice increase in industrial and marine particularly. The 7500, we shipped a handful of units in the fourth quarter. Those actually got in and out of the backlog, so the units we have on order now are not reflected in that backlog; those will be in the first part of this fiscal year.

Peter Lisnic: **So—okay, so those are not in the current disclosed backlog?**

Mike Batten: Correct.

Peter Lisnic: **Okay, can you give us an anecdotal feel for what the, you know, product reception for the 7500 has been, what we might look for in terms of demand for that product?**

John Batten: I would say that the testing in the field has gone well. The customers are anxious to get their hands on it, so I would anticipate, you know, as far as any one product, it will have, I would say, the most impact as one product because it right now, or as we last reported, it was zero in the fourth quarter, so it will have a nice impact going forward.

Peter Lisnic: Okay, perfect, and then, I guess maybe this one's for Chris. **Chris, you're sort of running in what I'd call unchartered gross margin territories. We kind of look forward to continued sales growth, which I think you point out in the press release. How should we think about two things: one would be the gross margin leverage in the next fiscal year; and then the leverage on the ME&A line, which I know is impacted by,**

you know, variable comp costs this year, kind of what should those two things sort of look like as we grow forward and the top-line continues to grow?

Mike Batten: Pete, this is Mike, I'll take that one if you don't mind. Basically, we were very encouraged by the factors that brought together the gross margin of the fourth quarter. It was very reassuring to be able to see that number, but as we look forward to the balance of the year—or the new year, I should say—we are—there'd be a little bit more process in responding to your question in that we do anticipate a recovery of our more traditional products and markets, which don't share the same gross margin that some of the products that are presently shipping. So we have responded in the past that gross margins in the middle 30's are where we target ourselves and if we're able to, from quarter to quarter, exceed that, we'll be very happy. But in looking out, say through the balance of this year, with recovery coming from a number of different sectors, I think something in the middle 30's is probably better to plan on and then if we're able to do better, we'll report that.

And Pete, on your ME&A question, you know, 2011 was a year where we restored the incentive compensation plan; in 2010, there wasn't one. We came close to the full payout on those awards, so I wouldn't expect a big increase year-over-year there. The stock did comp within the ME&A, you know, there were a number of things that happened there: one, the awards were in the money, so to speak, but more importantly, there was a significant increase in the share price from—I think it started out the fiscal year just over 11 and finished right around 40. So I wouldn't anticipate that the number would be as great. It will probably be a little bit lower in 2011. But I guess to answer your question, there should be on increased sales some opportunity for leverage on that ME&A line.

Peter Lisnic: Okay, that is perfect. I will jump back in queue, and nice quarter.

Mike Batten: Thank you.

Speaker: Thank you.

Operator: Our next question comes from the line of Neal Miller with Fidelity. Go ahead, sir.

Neal Miller: Hi, Michael, live long-distance here. **Three energy related questions, if I could. The first is the reference you made to reliability and durability and yet, what I was thinking about is you're part of an overall truck component structure and what I'm wondering about is, I had heard that the uptime or the repair cycle used to be seven years and now it's maybe one year, and what that leads me to is a question about whether the—you know, what full utilization is. In other words, if you're part of something else that's down and then people want the same level of horsepower, then they have to have more redundancy or more gadgets, so any kind of comment there?**

Mike Batten: Hi, Neal, it's good to talk to you again. The uptime obviously on frac rigs is a big concern for all the users and it is—we have to be concerned about our part in the—in that activity. I mean, obviously, we're only one component of many—several components that are utilized on the rig, so we're focused on maintaining the highest reliability and durability that we can and uptime that we can in the transmission side of the equation. We have been—anecdotally and from market experience seen that our transmissions are lasting longer than others in the field and so we're encouraged by that kind of a reputation that we get in the marketplace. So that's good news for Twin Disc.

I can't speak to other components in the system, but we're looking at what we can do, as I said, on the transmission. The higher intensity of the service required for unconventional drilling, which is where the market is going rapidly, really brings to bear, as you point out in your question, the issue of how quickly these units are used up, so to speak, because of the kind of usage that they're getting, far greater than ever before. So the market is looking for reliability and durability and that's one of the factors that we see that we can bring to the market, both with the 8500 and the 7500, as it makes its way into the market this year. So I hope that answers your question, Neal.

Neal Miller: Yes, that's really helpful. **A second question, kind of getting at the same area in a different way, is the backlog for pressure pumping equipment in the sense that the bocken [ph]—every picture you see of Minot, North Dakota is below water, etc. and I think the severity of the winter, the snow pack, plus the runoff, have delayed an awful lot going on in that area, which is kind of a hotbed for unconventional drilling, and is there any sense here as to the—in essence, the backlog, was created on a seasonal basis, that overall is there much more equipment that the world needs than is being met?**

Mike Batten: Well, I think clearly, the market itself, the macro outlook for unconventional drilling around the world is growing significantly, so it's just not in one place, it is around North American and it is going to Europe to a lesser extent, but—and also, we see developments in China and elsewhere in the Asian theater. So a lot of the rigs that are being built are (a) being built to replace equipment that is worn out; they're being built to add to the existing stock of equipment that is out there because the demand—some of the figures we've seen is looking at increasing the capability from 6 million horsepower to 9 million horsepower during this period of time so—in fracing rigs, so it's a—there are multiple demand structures. So to the extent that the bocken may be somewhat of a soft area and a drag on demand, yet we're not seeing it impacting our backlog at this point in time, because there are many other applications that will take these transmissions.

Neal Miller: Sure appreciate that. **The last question would be on capacity utilization and the [inaudible] your operation, how long does it—you know, can**

you just discuss how long it takes or what sort of time cycle there is that's in your backlog?

Mike Batten: Well, typically, our backlogs have run out as far as nine months, but we've been adding capacity selectively to accommodate the demand in this area. The fact that we've been able to run up our shipments over the past year and will continue to grow those shipments, both the 8500 and now the 7500, we have adequate physical capacity to accomplish the task ahead. Now, having said that, John and I both would be—that's to say that, you know, the supply chain could always be an issue. We don't see that at the moment, but we have an extensive supply chain and one never knows. So that would be the caveat on the other side. But we're feeling pretty comfortable about our ability to ramp-up to the demand that we are seeing and we project in the marketplace.

Neal Miller: Great quarter. Thanks so much.

Mike Batten: Thanks Neal.

Operator: And our next question comes from the line of Greg Garner with Singular Research. Go ahead, sir.

Greg Garner: Thank you for taking my question. First of all, congratulations on a nice quarter.

Speakers: Thank you.

Greg Garner: **One item, I remember last quarter, it was mentioned that there was about a 5 or 7 million pushout due to some supply constraints, as I recall. I just want to research were these recorded in the fourth quarter and was there any pushout for the fourth quarter?**

John Batten: Most of those 7 million made it into the fourth quarter and they're really—the magnitude of a pushout from the fourth quarter to the first quarter was a lot smaller. As you can get from the sales revenue line, the factories pushed out everything they could.

Greg Garner: **Okay, in the capacity expansion plans for next year, can you characterize the product that you are focusing on? Is it safe to assume it's for the 7500?**

John Batten: That would be a safe assumption, but the capacity expansion also would affect the commercial marine units here in Racine and other land-based transmission products.

Greg Garner: **Okay, and the fact that there is not any 7500's in the backlog, is that because you haven't been actively marketing it until you could deliver it? Is that how that works?**

John Batten: No, it's—we have—what we did was we went through the field test process and then those applications that were approved, we took orders for some of those and we actually shipped, so the order and the shipment happened in the same quarter, so it didn't register in the backlog. But we now have orders that were placed this fiscal year that will show up in the Q1 backlog.

Greg Garner: **Okay, and any sense on the demand for this relative to the 8500? Because in the last—there's been a movement for a higher demand for the 8500 than anticipated, say a year ago, and now if the 7500's there, what's your read on the 7500 versus the 8500 market size or demand?**

John Batten: I think—I think that overall the market potential for the 7500 is still larger than the 8500, given its size and weight and being able to get on frac rigs that don't need special permits to move, and smaller frac rigs for Asia and Eastern Europe. So I'm still confident the 7500 has a bigger market potential than the 8500. Customers are anxious to get it. It's still going to be—when we get into production as we are now, the lead times on this unit are going to be a lot shorter than any other frac transmission because we have availability of inventory and capacity to produce.

Greg Garner: **And dealing with size, that does that make it more—also more applicable to European and Asian choices?**

John Batten: Absolutely, it can fit on a body load frac rig, which is, you know, a non-tractor trailer arrangement, and it can sit on smaller horsepower frac rigs that, you know, that don't need permits to move around the U.S. or Canada.

Greg Garner: Mm-hmm. **To the joystick, can you characterize where that is? As I remember, there was initial orders to boatyards and I just want to get a sense for the marine market.**

John Batten: Sure, it is in production and has been for just about six months now, and it is doing very well at some of our targeted customer areas. We have a lot of projects going on in Australia, Asia, some of the builders in Taiwan, in Europe, in the U.S., so there's a lengthy application review and process to get all of the components and decide what the system is, but you'll see that ramp-up during this fiscal year, with a number of applications, orders and then shipment.

Greg Garner: Okay. **In just back going to question about the capacity utilization increasing with this huge increase in expenditure planned for this next fiscal year, is there any way to quantify the total capacity increase or the increase for oil and gas or anything along those lines you could share?**

John Batten: No, we typically don't give out, you know, those types of numbers, but it is—I mean, it has a significant impact in the amount that we can ship specifically in oil and gas.

Greg Garner: Okay, particularly if you could turn it—have a quick turnaround on orders.

John Batten: Exactly.

Greg Garner: Yes, okay, well thank you very much.

John Batten: Thank you.

Operator: And our next question comes from the line of Jon Braatz with Kansas City Capital. Go ahead, sir.

Jon Braatz: Good afternoon, gentlemen.

Mike Batten: Hi, Jon.

Jon Braatz: **There is a well-defined—as you evaluate your business, the first quarter is always the softest, but with business being so good, the 7500 coming onstream, will we have the seasonality—would you expect the seasonality to be similar in 2012 that you—that you've seen in prior years?**

Mike Batten: Jon, this Mike, and I guess that we could anticipate that seasonality in general will continue to exist, but that the variation between the quarters probably will be narrower, because I think we're going to see a better first quarter.

Jon Braatz: Mm-hmm, okay. **What is the lead time on the 8500? If I order one today, when do I get it? And because the lead time, I assume, is going to be longer for the 8500, have you seen any cancellations of 8500's and replacements with 7500 orders?**

John Batten: No, to answer the first part, it'd be about nine months.

Jon Braatz: Okay.

John Batten: And as we increase capacity, we're hoping to always to bring that down, and we have not seen any 8500 cancellations for the 7500. That's not to say that it won't happen going forward in this quarter, but a lot of the attitude is if it's, you know, don't fix what isn't broken.

Jon Braatz: Okay.

John Batten: So we've converted new customers in this latest run-up to 8500.

Jon Braatz: Mm-hmm.

John Batten: Specifically, people that we had targeted for the 7500. So, you know, they'd never used that model before, and now they're using the 8500 and they're looking to add capacity with the addition of the 7500.

Jon Braatz: Okay.

John Batten: And yes, the 7500, the lead time starting out will be shorter than the nine months for the 8500.

Jon Braatz: Okay. **The—going back to the joystick, I believe it's more of an OEM product. Is there any retrofit applications for the joystick or is it principally OEM?**

John Batten: It's principally OEM. There's a very—if you have—certainly it's possible to retrofit any vessel, but that is very cost prohibitive.

Jon Braatz: Okay.

John Batten: If you have our control system and our Quickshift transmissions already in the boat, that is a much easier proposition than if you have somebody else's control system and/or somebody else's transmission. You're pulling all of that stuff out and replacing it new, and there's a lot of—the labor involved in that is very expensive.

Jon Braatz: **Is it a big enough market and a big enough opportunity for, you know—and it's going to be tough with the explosion of sales in the oil and gas area—but is it enough for us to—to move the needle, so to speak, and for us to see it?**

John Batten: I think if you look at the overall marine market going forward and the possibilities for the EJS in our marine sales—

Jon Braatz: Mm-hmm.

John Batten: I think you'll see it move the needle in a very stagnant down market.

Jon Braatz: Okay, one last question. **You did reference in your—in your press release, new product development, you know, during the last three or four years, you didn't back off that and we're seeing the fruits of your work. What can you tell us maybe what your currently looking at and doing in terms of new products? Are there other applications, particularly in the oil and gas area, that you're working on?**

Mike Batten: Well, I'll take than one, Jon. The issue is this. We are working on incremental developments to EJS controls and the like, and so we're not ready to come public with it, but there will be enhancements that will happen there and we'll be working in other market areas other than just pleasure craft at the moment to apply those EJS controls. So that will be more or less an incremental kind of development. We are working on some other longer-range activities that we're not going to talk about. It's a little bit premature to be talking about the activities that we're working on, either in terms of organic development or external acquisitive development.

Jon Braatz: Okay, all right, thank you very much.

Speaker: [Unintelligible]

Operator: And we have a follow-up question from the line of Peter Lisnic with Robert W. Baird. Go ahead, sir.

Peter Lisnic: All right, I'll try to be quick. **Can you give us a sense with all the activity in oil and gas, just what the aftermarket business there is looking like, you know, demand trends and do you see the aftermarket being a bigger part of the business than, you know, maybe previous historical metrics would suggest?**

John Batten: Pete, it's John. I think, you know, specifically back to three or four years ago, the aftermarket is a much bigger piece this time around because there was a lot of maintenance on those rigs that were built just a few years ago and I think, if you talk to anybody in the industry, I think this time around, there's a lot more preventative maintenance on the rigs, and so—and to an earlier question, 7,000 hours down to 1,000 hours, so it's more or less in line with what we're hearing. It's just in unconventional drilling, the utilization rates and the number of hours per day are way up, and so that brings the time down, so rather than wait until something breaks, they're going in and doing a lot of maintenance and scheduling it in advance. So we see the aftermarket part being a much bigger part this time than it was last time and it will be forward. It's a growing part of the business.

Peter Lisnic: **And is there a way of maybe estimating or sizing that opportunity for you or giving us some context relative to what it used to be, or is it just a little bit too vague at this point?**

John Batten: I would say, Pete, it's probably a little bit too vague at this point. I mean, it was—the last run-up it was a pretty small part, because the run-up was so quick and so short, we almost never got around to it, so I don't want to—I know a lot of the stuff that's been ordered now was really to go after the existing fleet, but certainly there's a lot more attention to the aftermarket component of it now.

Peter Lisnic: **Okay, and then the marine, I think the comments have been, you know, better, getting better, and the backlog, I guess, was up in the quarter. Can you give us a little bit of color on the—on sort of the individual pieces of marine patrol work and pleasure and kind of give us a sense as to what's happening demandwise in each of those?**

John Batten: Sure, the demand—you know, pleasure craft continues its limited improvement. We're seeing orders that are directly attributable to EJS. In the work boat areas, I think for us commercial, all has been improving very nicely. I would say one of the caveats is, is that the activity in the Gulf Coast with respect to offshore oil and gas is still pretty slow. I mean, the number of rigs out there and the new permits are way down, but orders in Asia are growing. We're seeing some activity in Europe and certainly the brown water, the river traffic here in the U.S., is doing very nicely. You know, very good to see the year-over-year improvement, and particularly in the fourth quarter in the backlog.

Peter Lisnic: Okay, all right, that is good for me. Thanks again for your time.

Speakers: Thanks, Pete.

Operator: And our next question comes from the line of Adriano Almeida with Cramer Rosenthal. Go ahead please.

Adriano Almeida: Hey, gentlemen, how are you?

Speakers: Hey, how are you doing?

Adriano Almeida: Pretty good. A lot of people have asked questions already, so I kind of don't have too many incremental ones and I did miss the frontend of the call, maybe you mentioned this. **Have you guys been able to exercise pricing power on the oil and gas side beyond what your cost inflation is?**

Mike Batten: Adriano, it's Mike. We've been able to pass along inflationary increases each year as we move forward, but we're mindful of our position in the market and don't want to get too far out ahead in a demand opportunity. Our mission here is to provide solid products to our customers for the long term and we're going to keep our pricing with respect to inflation intact, but not to go beyond that.

Adriano Almeida: **Okay, but there has been inflation, right, on the input cost? So it's fair to assume that the price you're quoting today is higher than what you were quoting, say six months ago, for the equipment?**

John Batten: Six months ago?

Adriano Almeida: Yes.

John Batten: No, six months ago—six months ago, the pricing would be the same.

Adriano Almeida: Okay.

John Batten: But you might not have the same answer three months from now.

Adriano Almeida: Okay, so there's—

Mike Batten: Adriano, we don't want to be [inaudible] The issue is that we basically set annual pricing unless there's going to be a huge inflationary requirement, so what John is saying is that our prices were effective October 1—

John Batten: Adriano, that's correct. The prices are higher now than they were six months ago.

Adriano Almeida: Okay.

Mike Batten: Yes, we just tripped over the line.

Adriano Almeida: **All right, another thing I was wondering about is, in terms of anecdotal evidence—I know it's very murky for especially folks on the outside of the industry—to really understand market share shifts, but I think it's reasonable to assume you guys have gain share in this upturn. Do you see evidence, say in the aftermarket for instance, where your guys are going out and delivering or selling a transmission that was previously an Allison or a Cat transmission that's being replaced by a Twin? Is there evidence of that?**

John Batten: I would say more of the evidence has been just the shift in the new construction to the higher horsepower.

Adriano Almeida: Okay.

John Batten: And I think we have benefitted significantly from that and I think Cat has benefitted to some extent, because they have the other 3000 horsepower transmission.

Adriano Almeida: Okay.

John Batten: It's just a huge shift to that horsepower level.

Adriano Almeida: Okay.

John Batten: For—in replacing one with the other.

Adriano Almeida: Yes, because that plays to your strength.

John Batten: Yes.

Adriano Almeida: **Okay, I have one more here. Now just putting my kind of trying to think about potential problems hat on, I assume the two CMC machines you've installed are up and running and already producing product, is that correct?**

John Batten: That is correct.

Adriano Almeida: **Now, when you—as you ramp-up the 7500, there's a piece of the manufacturing that actually is more labor intensive and requires some skill, are you going to have to hire new people? Is there like a kind of a training model next year in terms of, you know, getting guys? Because there have been other people in the space that have kind of stumbled in terms of responding to the big ramp-up in demand that you're all seeing?**

John Batten: To answer that question, we do need more people, and we've actually—we've hired most of them. We're up, just in the workforce in Racine, out in the shop, about 10%, and significant other temps in, which is allowing us to free up the skilled labor for just this activity. So we've been working on that over the course of the year.

Adriano Almeida: Okay, so—and in terms of the capacity ramp-up—the 7500's that you delivered in the quarter, they went through that kind of—the whole manufacturing footprint that's going to deliver the rest or is there some more buildup?

John Batten: Well, again, I don't completely understand (inaudible), but we did use the fourth quarter—the small shipments of the 7500 were basically used as, you know, the final prove-out of our manufacturing process for it, so just everything from the machining through assembly.

Adriano Almeida: **Now, but you've delivered those in the fourth quarter, right?**

John Batten: Right, yes.

Adriano Almeida: **They're a part of revenue, although they're not in backlog.**

John Batten: Yes.

Adriano Almeida: And are those—I'm just wondering to what extent those were actually—because my understanding is that the certification happened like right in the final days of the quarter.

John Batten: Correct.

Adriano Almeida: **And so, what, did you come around and make, you know, 10 transmissions in a couple of days? Or I just want to understand how that happened, how could deliver in June.**

John Batten: There is an engineering release and manufacturing release, so we had, you know, the design and the prototype design and we had engineering sign off, and so we were able to ship—because there weren't any major changes, we were able to ship units that we had the inventory for.

Adriano Almeida: **Okay, and the ones that were out in the field as part of the field tests, the proofing—**

John Batten: Yes.

Adriano Almeida: **Are those—what happens to those? Do they get sold to the customer?**

John Batten: No, we end up—those are still—I mean, we're continuing to test, even though we're in production, so we're finishing all those field tests and we'll bring these units back for inspection.

Adriano Almeida: Okay.

John Batten: And then there's different arrangements that we have with the customers for those units, but assuming there's nothing wrong with those units, those—it will probably be around the oil patch that's winging it.

Adriano Almeida: Okay, great. Well, thank you very much guys. Good job now.

Speaker: All right, thank you Adriano.

Operator: And our next question is a follow-up question from the line of Neal Miller with Fidelity. Go ahead please.

Neal Miller: **Yes, picking up on the last questioner's comment on the competitive environment, I'm wondering about your advantages. As I recall, your transmissions are somewhat dedicated, whereas Caterpillar can use the transmission that they produce in multiple ways, but I guess the question I have is, you know, with all the makeup going on with standby power around the world and that sort of thing, is Caterpillar and those sorts—the competitors more focused on their base markets, as opposed to the energy market? I'm just kind of wondering about the competitive environment from that angle.**

Mike Batten: I guess, Neal, we wouldn't comment on our good competitors in what their plans are or what they're trying to do. I think what we can talk about is what we're trying to accomplish in our markets and how we see our advantages. And you're right, I think that our design approach here and being in the market with the 8500 at a very propitious time when the market wanted to go to 3000 horsepower, found a transmission that could handle it and was suited to the ratio selections that were necessary, and hitting sort of the big wave of unconventional gas demand where the market wants a paradigm shift, going from 1500 to 2250 to 3000 horsepower, we got very fortunate in being there with the right product and establishing a nice share position with a good product. So, yes, other people are in the market with differing approaches to their transmissions and I think we've been fortunate to have good timing, good products and an exceptional quality to be where we are at the present time.

Neal Miller: Great, thanks.

Mike Batten: Okay.

Operator: And our next questions is also a follow-up question from the line of Jon Braatz with Kansas City Capital. Go ahead, sir.

Jon Braatz: **Sort of a follow-up to the last question, it sounds like one of your competitors, Allison, really has been sort of left out of the high horsepower market, and I don't want you to comment on whether you think they're going to enter it or not, but if they made a decision to build a higher horsepower transmission, from that decision to a product, how long—how long does it take do you think to have something commercially available?**

Mike Batten: Well, that’s a good question, Jon, and a lot depends upon how much they’re willing to devote to the design phase, how much resource they would put in from a design point of view. If you’re starting with a clean sheet of paper, it could be as many as four years to get a product into the marketplace. If you’re looking at some other approach, it might be less. But it takes a while to take one of these transmissions from a clean sheet of paper and bring it through the design phase, the test phase and then finally get it into production. So as many as four years and—then they might be able to do it in fewer years, I wouldn’t want to comment.

Jon Braatz: Okay. **Did it take you four years with the 7500?**

Mike Batten: It took us a better part of it. When you consider the design work that was done, alternative design. You know, we took—we ran tests for the better part of a year.

Jon Braatz: Okay.

Mike Batten: We’ve been talking about the 7500 publicly for over a year, probably five quarters anyway, and we’re now—just now in production. But we’re a conservative bunch, so someone might not take it the same way.

Jon Braatz: Okay, Chris, I have sort of a cash flow question. **What type of investment in working capital—what level of investment in working capital would you anticipate as the volumes strengthen, if you want to say that? It looks like it’s going to be a good year next year, but what kind of—type of investment would you anticipate in the working capital, especially inventory?**

Chris Eperjesy: Right, that’s a tough question to answer because a lot of the—to build in invest—sorry, in working capital you saw this year was in the anticipation of the 7500 release now in 2012, so there’s some big level of increase that was anticipated for that buildup that potentially could be relieved.

Jon Braatz: Okay.

Chris Eperjesy: But clearly, if there’s a significant increase in sales, there’ll be an increase in working capital, but I think that it will be a positive in terms of marketing cash flow.

Jon Braatz: Okay, great. Thank you.

Operator: And our next question comes from the line of Shawn Boyd with Westcliff Capital Management. Go ahead, sir.

Shawn Boyd: Good afternoon and congrats on the quarter.

Speakers: Thank you, Shawn.

Shawn Boyd: Just a couple, if I may. **On the non-oil and gas for a second, great to hear that we're hearing these additional improving, can you maybe walk us through the markets for a second and talk about where we are in terms of sort of current revenues versus previous peak back in 2008?**

Mike Batten: Shawn, we don't normally comment on the size of the markets that we're talking about that we participate in, but John can give you an update on sort of the directional move of what these spaces are doing. John?

John Batten: Yes, Shawn, just starting with marine, I mean, the two obviously going into the recession, transmission with oil and gas a big component, marine and industrial all took a big hit and transmissions driven by oil and gas rebounded very quickly. On the other components of that business, the military and the ARF business stayed very steady through the whole downturn. So that part of the business for us as a whole fared much better, rebounded very quickly.

Marine and industrial, depending upon the market, you know, with pleasure craft and marine saw a 50% decline in the markets, so that has been a longer recover period and that recovery is being driven by commercial activity in Southeast Asia, India, China and in the Gulf Coast, when you look at the river traffic. And I would say we're not back to where we were, but we've got a nice recovery going.

Industrial took a similar hit, and our industrial business is driven by activity in Europe and North America. That didn't take quite the punishment that the marine markets did, but that has shown some pretty good recovery and I'd say we're better off on the comparison you're looking at there than we on in marine, but marine is starting to come back a little bit stronger now. So all in all, if you go back to peak at $332 million, obviously we're not back to that peak as a whole company yet but what's really driving us in the last 12 months has been transmissions in oil and gas.

Shawn Boyd: Okay.

John Batten: But the other businesses are starting to pick up now too.

Shawn Boyd: Right, and that's the reason for the question. I understand you guys don't break it out in terms of revenues, but understanding where we are versus peak is helpful, so those comments are great. **And on the industrial side, and perhaps on commercial marine, in terms of the weakness that we're seeing in Europe, and then also a little of the macro slowdown we're starting to see here in the U.S., any of that filtering through and slowing this recovery at all?**

John Batten: I'd say right now, certainly the situation in Europe has just been a much longer situation that we're dealing with and the growth rates are not as strong as they are in other parts of the world. Too early too tell on the macro situation right here in the U.S., but a lot of our business, more and more of the percentage, is being driven by Asia, you know, specifically India, China, Indonesia, Malaysia, so all in all, we're still doing pretty well there. So I think it's too early to tell on the macro-economic situation in the U.S. We obviously would like for the situation there to be better.

Shawn Boyd: Sure, okay. **In terms of the growth rates, if we think about—you know what, let's hold off on that. If we think about the growth rate over on oil and gas, and what you had in this past year—and again, I understand you want to keep breakouts away from the conversation—but, is the growth or the rent in the 7500 that is now starting to really take hold and will in the coming quarters, is that enough to allow you to keep your current growth rate in the oil and gas segment in fiscal 2012?**

John Batten: That—that's one I don't know I can answer right now. It certainly will allow us to continue to grow, whether or not at the same rate, I would say no. Just because the 8500, the entire supply chain was proven out, you know, four and five years ago.

Shawn Boyd: Mm-hmm.

John Batten: And a lot of the 7500 suppliers who have a similar—who share some with the 8500, some are new, and so there's going to be a learning curve here on the 7500 that was not here for the last year on the 8500 as we were expanding production. So—and we continue to grow, but it's in this slower pace.

Shawn Boyd: Got it. Okay, that's helpful. **And in terms of the overall capex build, well, two questions on that. If the—in business now, we're looking very closely at making sure that we can handle both the 8500 and the 7500 on the oil and gas, is that—what chunk of that budget—is that budget spread evenly throughout the entire company or is it heavily weighted to the oil and gas segment?**

John Batten: It's John again. It's spread pretty evenly. A lot of the capex is going to be in, you know, domestic operations and some of the European operations, and they're doing manufacturing for the oil and gas products, but other products as well, industrial and marine.

Shawn Boyd: **Okay, and thinking about revenue capacity, that increase again being pretty substantial, is that sufficient to handle another, you know, very high growth year—another 35-36% kind of revenue growth sort of year?**

John Batten: Yes.

Shawn Boyd: Okay. **The last question for me is on the ME&A, if I look at that kind of two ways, saying let's just back-out the incentive comp and the product's expense for a second and say what are the core operating**

expenses of this company, we hit about $18 million for the fourth quarter and about $62 million on the year, again, just keeping stock base comp and bonus expense out of the way for a minute, is that $18 million a quarter a sufficient level for you guys as you go into 2012? I mean, that's kind of a step up from where we've been in the previous couple of quarters, but I'm looking at that capex coming up and the growth of the company and, you know, trying to use some sort of the mark here. Can you help me on that?

Chris Eperjesy: That's not a bad analysis to do. The clearly the growth that may occur in the sales will not be similar in ME&A. I mean, it will be a much smaller percentage. There is, you know, from quarter to quarter, there may be particular projects we're working on that may either create a spike or a downturn in ME&A, but I think that's a pretty reasonable number to use.

Shawn Boyd: Got it. Okay, hey, that's it for me. Thanks and congratulations on the quarter, guys.

Speaker: Thank you.

John Batten: Thanks, Shawn.

Operator: And our next question comes from the line of George Gaspar, private investor. Go ahead sir.

George Gaspar: Good afternoon. **A follow-on question on the marketing horizon on the 8500 unit and 7500 unit. If you look across and review the deliveries that you've made recently in the last, say six months, and your backlog that you have currently, can you—in terms of your marketing, can you track the geographical areas in the United States where a the majority of this equipment is going or does it just go to central sites and then feed-out from there or do you spend the time trying to track where the equipment is actually being deployed at any specific point? And then, secondly, is there—in terms of the 7500, is there geographically a better horizon for that in a certain area of the United States versus in others? Can you talk at all about this?**

John Batten: Sure. We do track where the transmissions are going. We don't release that information, but we do know obviously where the initial shipment goes for the rig manufacturer and then each rig manufacturer tends to have an operating hub in each one of the sale [inaudible] and so we know where the fleet is and then pretty much know where—you know, which fields they're going to be operating at. Certainly, our distributors, the guys—the service techs, know exactly what field in they're in.

On the second part, the 7500 is going to do much better in places like the Marcellus Shale in the eastern U.S. and Pennsylvania—smaller, tighter roads. And then if we just play that out on a global level, Eastern Europe, Northern India, China, where the infrastructure isn't as good and the roads aren't as wide, that is where the 7500 is going to have more of an impact on us than say the 8500.

George Gaspar: Okay, interesting. All right, thank you. An additional question: **There was some indication on employment discussion here. My question regarding manufacturing employment, can you give us a number as to what you had in manufacturing employment say six months ago—where you were at the end of the fiscal year here and where you might see yourselves out at calendar year end 2011?**

John Batten: It's not going to change—it won't have changed much in that time horizon. We don't give out the significant numbers in manufacturing, but a lot of the adds that I was talking about happened in the first part of this fiscal year, anticipating—well, not anticipating—reacting to the huge surge at that point of just the 8500, but now with the 7500 coming on and just the increase in volume in our marine transmission products, we had to add people at the beginning of the year, but those adds have become stable over the last six months and we don't anticipate a big increase going forward in the next six months.

George Gaspar: **So would you say that—with that comment, you're making improvements in your manufacturing processes to effectively be able to produce more with—product with similar employment?**

John Batten: Correct, an increase in capex, and a lot of the extra volume that comes in is going to be at our supply date.

George Gaspar: I see. Okay, thank you.

Operator: And we have another follow-up question from Jon Braatz with Kansas City Capital. Go ahead, sir.

Jon Braatz: **If I've done the arithmetic correctly, your cash balances could rise quite sharply here over the next 12 months. What are your thoughts—I know you're a cyclical business, or can be a cyclical business. What are your thoughts about returning that cash maybe to shareholders either in a form of—I suppose not share repurchases, but maybe dividends at this time?**

Mike Batten: Jon, yes, we are seeing a buildup in cash. Part of that will be used, of course, with capex and typically, the discussion of dividends is considered by the board at our January meeting, so I wouldn't want to comment on that subject any more than to give you that information at this time. Also, we are involved in an active acquisition program and, of course, the use of cash would be helpful in that activity were we to come to agreement on an acquisition. We typically are following a number of different opportunities, and as you know, you never can predict what is going to come when. So—but, we'll talk more about your dividend question later on in the year.

Jon Braatz: Okay, no problem. Thank you very much.

Speakers: Okay, thanks Jon.

Operator: And there are no further questions at this time. I will turn it back to management for any closing remarks.

Mike Batten: Thank you Jo. Again, we thank you all for joining the conference call today and we appreciate your continuing interest in Twin Disc. We hope that we've answered all of your questions. It's been a lively engagement and I'm pleased that you've had that many questions. If you have any follow-on questions, please feel free to call Chris or John or myself here at the office, we'll be around, and we look forward to speaking with you again in October following the close of our first quarter.

Jo, we'll turn it back to you now.

Operator: Thank you, sir. Ladies and gentlemen, that does conclude the Twin Disc Incorporated Fiscal 2011 Fourth Quarter Financial Results Call. Thank you for your participation. You may now disconnect.

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