

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended July 2, 2005
or
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission file number 1-11406

KADANT INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware 52-1762325
(State or Other Jurisdiction (I.R.S. Employer Identification No.)
of Incorporation or Organization)

One Acton Place, Suite 202 01720
Acton, Massachusetts (Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: (978) 776-2000

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether or not the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 4, 2005
Common Stock, \$.01 par value	13,894,703

PART I - FINANCIAL INFORMATION

Item 1 - Financial Statements

KADANT INC.

Condensed Consolidated Balance Sheet
(Unaudited)

Assets

(In thousands)	July 2, 2005	January 1, 2005
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Current Assets:		
Cash and cash equivalents	\$ 46,221	\$ 82,089
Accounts receivable, less allowances of \$2,479 and \$1,678	41,879	30,022
Unbilled contract costs and fees	18,111	10,258
Inventories (Note 5)	38,295	27,316
Deferred tax asset	9,013	6,691
Other current assets	7,639	6,703
Assets of discontinued operation (Note 14)	14,919	15,650
Total Current Assets	176,077	178,729
Property, Plant, and Equipment, at Cost	85,239	68,224
Less: Accumulated depreciation and amortization	51,402	51,160
	33,837	17,064
Other Assets	19,447	11,342
Intangible Assets	37,574	3,694
Goodwill	121,732	74,408

Total Assets

\$388,667
=====

\$285,237
=====

The accompanying notes are an integral part of these condensed consolidated financial statements.

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KADANT INC.

Condensed Consolidated Balance Sheet (continued)
(Unaudited)

Liabilities and Shareholders' Investment

(In thousands, except share amounts)	July 2, 2005	January 1, 2005
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Current Liabilities:		
Current maturities of long-term obligations (Note 6)	\$ 9,037	\$ -
Accounts payable	24,724	21,327
Accrued payroll and employee benefits	13,478	11,261
Accrued warranty costs (Note 8)	3,766	3,582
Accrued restructuring costs (Note 9)	9,289	10,026
Accrued income taxes	5,345	886
Other current liabilities	17,036	10,419
Liabilities of discontinued operation (Note 14)	6,572	7,578
	-----	-----
Total Current Liabilities	89,247	65,079
	-----	-----
Deferred Income Taxes	21,295	4,370
	-----	-----
Long-Term Obligations (Note 6)	51,980	-
	-----	-----
Other Long-Term Liabilities	11,407	3,327
	-----	-----
Minority Interest	1,174	-
	-----	-----
Shareholders' Investment:		
Preferred stock, \$.01 par value, 5,000,000 shares authorized; none issued	-	-
Common stock, \$.01 par value, 150,000,000 shares authorized; 14,604,520 shares issued	146	146
Capital in excess of par value	97,525	98,450
Retained earnings	135,251	129,173
Treasury stock at cost, 709,817 and 689,407 shares	(17,930)	(18,158)
Deferred compensation	(299)	(50)
Accumulated other comprehensive items (Note 2)	(1,129)	2,900
	-----	-----
Total Liabilities and Shareholders' Investment	\$388,667	\$285,237
	=====	=====

The accompanying notes are an integral part of these condensed consolidated financial statements.

KADANT INC.

Condensed Consolidated Statement of Income
(Unaudited)

	Three Months Ended	
(In thousands, except per share amounts)	July 2, 2005	July 3, 2004
Revenues	\$ 65,086	\$ 52,652
Costs and Operating Expenses:		
Cost of revenues	40,385	32,255
Selling, general, and administrative expenses	18,497	14,575
Research and development expenses	1,247	581
	60,129	47,411
Operating Income	4,957	5,241
Interest Income	379	318
Interest Expense	(473)	(4)
Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense	4,863	5,555
Provision for Income Taxes	1,654	1,558
Minority Interest Expense	62	14
Income from Continuing Operations	3,147	3,983
Income (Loss) from Discontinued Operation (net of income tax expense of \$111 in 2005 and income tax benefit of \$130 in 2004) (Note 14)	207	(240)
Net Income	\$ 3,354	\$ 3,743
Basic Earnings per Share (Note 3):		
Continuing Operations	\$.23	\$.28
Discontinued Operation	.01	(.02)
Net Income	\$.24	\$.26
Diluted Earnings per Share (Note 3):		
Continuing Operations	\$.22	\$.27
Discontinued Operation	.02	(.01)
Net Income	\$.24	\$.26
Weighted Average Shares (Note 3):		
Basic	13,891	14,218
Diluted	14,181	14,555

The accompanying notes are an integral part of these condensed consolidated financial statements.

KADANT INC.

Condensed Consolidated Statement of Income
(Unaudited)

(In thousands, except per share amounts)	Six Months Ended	
	July 2, 2005	July 3, 2004
Revenues	\$115,830	\$100,152
Costs and Operating Expenses:		
Cost of revenues	72,367	60,288
Selling, general, and administrative expenses	33,391	28,346
Research and development expenses	2,295	1,469
	108,053	90,103
Operating Income	7,777	10,049
Interest Income	851	647
Interest Expense	(475)	(12)
Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense	8,153	10,684
Provision for Income Taxes	1,857	3,353
Minority Interest Expense	62	14
Income from Continuing Operations	6,234	7,317
Loss from Discontinued Operation (net of income tax benefit of \$84 and \$456) (Note 14)	(156)	(846)
Net Income	\$ 6,078	\$ 6,471
Basic Earnings per Share (Note 3):		
Continuing Operations	\$.45	\$.51
Discontinued Operation	(.01)	(.05)
Net Income	\$.44	\$.46
Diluted Earnings per Share (Note 3):		
Continuing Operations	\$.44	\$.50
Discontinued Operation	(.01)	(.06)
Net Income	\$.43	\$.44
Weighted Average Shares (Note 3):		
Basic	13,909	14,220
Diluted	14,196	14,579

The accompanying notes are an integral part of these condensed consolidated financial statements.

KADANT INC.

Condensed Consolidated Statement of Cash Flows
(Unaudited)

(In thousands)	Six Months Ended	
	July 2, 2005	July 3, 2004
Operating Activities:		
Net income	\$ 6,078	\$ 6,471
Loss from discontinued operation (Note 14)	156	846
Income from continuing operations	6,234	7,317
Adjustments to reconcile income from continuing operations to net cash provided by operating activities:		
Depreciation and amortization	2,719	1,833
Provision for losses on accounts receivable	44	218
Loss (gain) on sale of property, plant, and equipment	30	(140)
Minority interest expense	62	14
Other non-cash items	34	312
Changes in current accounts, net of effects of acquisition:		
Accounts receivable	2,402	(232)
Unbilled contract costs and fees	(6,125)	(878)
Inventories	3,066	(416)
Other current assets	902	(83)
Accounts payable	(1,619)	1,297
Other current liabilities	(2,866)	(980)
Net cash provided by operating activities	4,883	8,262
Investing Activities:		
Acquisition, net of cash acquired (Note 4)	(101,365)	-
Capitalized acquisition costs (Note 4)	3,073	-
Acquisition of minority interest in subsidiary	-	(318)
Purchases of property, plant, and equipment	(875)	(919)
Proceeds from sale of property, plant, and equipment	9	1,279
Other, net	(1,041)	(93)
Net cash used in investing activities	(100,199)	(51)
Financing Activities:		
Proceeds from issuance of short- and long-term obligations (Note 6)	60,000	-
Increase in short- and long-term obligations (Note 4)	4,000	-
Net proceeds from issuance of Company common stock	639	4,598
Purchases of Company common stock	(2,085)	(6,159)
Repayments of long-term obligations	-	(598)
Net cash provided by (used in) financing activities	62,554	(2,159)
Exchange Rate Effect on Cash	(2,675)	698
Net Cash (Used in) Provided by Discontinued Operation	(431)	240
(Decrease) Increase in Cash and Cash Equivalents	(35,868)	6,990
Cash and Cash Equivalents at Beginning of Period	82,089	74,412
Cash and Cash Equivalents at End of Period	\$ 46,221	\$ 81,402
Non-cash Investing Activities:		
Fair value of assets acquired	\$156,667	\$ -
Cash paid for acquired business	(104,531)	-
Obligation to be paid for acquired business	(4,000)	-
Liabilities assumed of acquired business	\$ 48,136	\$ -

The accompanying notes are an integral part of these condensed consolidated financial statements.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. General

The interim condensed consolidated financial statements and related notes presented have been prepared by Kadant Inc. (also referred to in this document as "we," "Kadant," "the Company," or "the Registrant") without audit and, in the opinion of management, reflect all adjustments of a normal recurring nature necessary for a fair statement of the Company's financial position at July 2, 2005, its results of operations for the three- and six-month periods ended July 2, 2005, and July 3, 2004, and cash flows for the six-month periods ended July 2, 2005, and July 3, 2004. Interim results are not necessarily indicative of results for a full year.

The condensed consolidated balance sheet presented as of January 1, 2005, has been derived from the consolidated financial statements that have been audited by the Company's independent auditors. The condensed consolidated financial statements and related notes are presented as permitted by Form 10-Q and do not contain certain information included in the annual consolidated financial statements and related notes of the Company. The condensed consolidated financial statements and notes included herein should be read in conjunction with the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended January 1, 2005, filed with the Securities and Exchange Commission.

Results for the six-month period ended July 3, 2004 have been reclassified to reflect the Company's composite building products business as a discontinued operation (Note 14).

2. Comprehensive Income

Comprehensive income combines net income and "other comprehensive items," which represents certain amounts that are reported as components of shareholders' investment in the accompanying condensed consolidated balance sheet, including foreign currency translation adjustments and deferred gains and losses on foreign currency contracts. The components of comprehensive income are as follows:

(In thousands)	Three Months Ended		Six Months Ended	
	July 2, 2005	July 3, 2004	July 2, 2005	July 3, 2004
Net Income	\$ 3,354	\$ 3,743	\$ 6,078	\$ 6,471
Other Comprehensive Items:				
Foreign Currency Translation Adjustments	(2,997)	(949)	(3,663)	1,087
Deferred Loss on Foreign Currency Contracts	(266)	(14)	(366)	(36)
	(3,263)	(963)	(4,029)	1,051
Comprehensive Income	\$ 91	\$ 2,780	\$ 2,049	\$ 7,522

Notes to Condensed Consolidated Financial Statements
(Unaudited)

3. Earnings per Share

Basic and diluted earnings per share are calculated as follows:

(In thousands, except per share amounts)	Three Months Ended		Six Months Ended	
	July 2, 2005	July 3, 2004	July 2, 2005	July 3, 2004
Income from Continuing Operations	\$ 3,147	\$ 3,983	\$ 6,234	\$ 7,317
Income (Loss) from Discontinued Operation	207	(240)	(156)	(846)
Net Income	\$ 3,354	\$ 3,743	\$ 6,078	\$ 6,471
Basic Weighted Average Shares	13,891	14,218	13,909	14,220
Effect of Stock Options	290	337	287	359
Diluted Weighted Average Shares	14,181	14,555	14,196	14,579
Basic Earnings per Share:				
Continuing Operations	\$.23	\$.28	\$.45	\$.51
Discontinued Operation	.01	(.02)	(.01)	(.05)
Net Income	\$.24	\$.26	\$.44	\$.46
Diluted Earnings per Share:				
Continuing Operations	\$.22	\$.27	\$.44	\$.50
Discontinued Operation	.02	(.01)	(.01)	(.06)
Net Income	\$.24	\$.26	\$.43	\$.44

Options to purchase approximately 218,000 and 222,400 shares of common stock for the second quarters of 2005 and 2004, respectively, and 222,700 and 234,700 shares of common stock for the first six months of 2005 and 2004, respectively, were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price for the common stock and the effect of their inclusion would have been anti-dilutive.

4. Acquisition

On May 11, 2005, the Company acquired all the outstanding stock of The Johnson Corporation (Kadant Johnson), a leading supplier of steam and condensate systems, components, and controls used primarily in the dryer section of the papermaking process and during the production of corrugated boards, metals, plastics, rubber, and textiles. Kadant Johnson was a privately held company based in Three Rivers, Michigan with approximately 575 employees and 2004 annual revenues of \$76,092,000. The purchase price for the acquisition was \$101,458,000 in cash, subject to a further post-closing adjustment, and \$3,073,000 of acquisition-related costs. In addition to the consideration paid at closing, the Company issued a letter of credit to the sellers for \$4,000,000 related to certain tax assets of Kadant Johnson, the value of which the Company expects to realize. This amount is subject to adjustment based on The Johnson Corporation's final tax returns for 2004 and 2005. This additional consideration, of which \$600,000 is included in other current liabilities and \$3,400,000 is included other long-term liabilities in the accompanying condensed consolidated balance sheet, is due over the next five years as follows: 15% in May of 2006, 2007, 2008 and 2009, and 40% in May 2010.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

4. Acquisition (continued)

The parties also agreed in the purchase agreement to an earn-out provision, based on the achievement of certain revenue targets between the closing date (May 11, 2005) and July 1, 2006, which could increase the purchase price by up to \$8,000,000. This contingent consideration will be accounted for as an increase in goodwill, if and when the revenue targets are achieved.

To fund a portion of the purchase price, the Company entered into a term loan and revolving credit facility (see Note 6 for further discussion).

Pursuant to the purchase agreement, at the closing of the acquisition \$12,750,000 of the purchase price was deposited into an escrow fund, primarily to secure certain indemnification obligations of the sellers. On the 18th-month anniversary of the closing, the balance of the escrow fund in excess of \$2,000,000 and amounts held for unresolved claims will be distributed to the sellers. The remainder of the escrow fund will be held until the fifth anniversary of the closing to satisfy certain tax, environmental, and other indemnity claims.

The following table summarizes the purchase method of accounting for the acquisition and the estimated fair values of the assets acquired and the liabilities assumed (in thousands):

Allocation of Purchase Price	
Cash and Cash Equivalents	\$ 4,071
Accounts Receivable, net	17,733
Notes Receivable	5,577
Inventory	13,280
Other Current Assets	5,258
Property, Plant, and Equipment	18,551
Long-Term Deferred Tax Assets	8,689
Other Assets	657
Intangible Assets	34,480
Goodwill	48,371

Total Assets Acquired	\$156,667

Accounts Payable	\$ 6,578
Other Current Liabilities	15,242
Short- and Long-Term Debt	3,286
Long-Term Deferred Tax Liabilities	17,148
Other Liabilities	4,727
Minority Interest	1,155

Total Liabilities Assumed	48,136

Net Assets Acquired	\$108,531
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Consideration Paid:	
Cash	\$ 41,458
Debt	60,000
Short- and Long-Term Obligations	4,000
Acquisition Costs	3,073

Total Consideration Paid	\$108,531
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Notes to Condensed Consolidated Financial Statements
(Unaudited)

4. Acquisition (continued)

The estimated values of current assets, excluding inventory, and current liabilities were based upon their historical costs in the hands of the seller on the date of acquisition due to their short-term nature. Inventory and property, plant, and equipment were recorded at estimated fair value based primarily on cost and market approaches.

The following are the identifiable intangible assets acquired and the respective periods over which the assets will be amortized on a straight-line basis:

(In thousands)	Amount	Life
Existing technology	\$ 7,840	11 years *
Customer relationships	15,700	17 years *
Distribution network	2,400	17 years
Trade name	8,100	Indefinite
Licensing agreement	400	20 years
Non-compete agreements	40	3 years

	\$ 34,480	
	=====	

* approximate weighted-average lives

The amount assigned to identifiable intangible assets acquired was based on their respective fair values determined as of the acquisition date by an outside valuation consultant, using income and cost approaches. The excess of the purchase price over the tangible and identifiable intangible assets was recorded as goodwill and amounted to approximately \$48,371,000. In accordance with current accounting standards, the goodwill will not be amortized and will be tested for impairment annually in the fourth quarter of the Company's fiscal year, as required by Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets."

The amortization expense associated with these acquired intangibles was \$268,000 in the second quarter of 2005. The estimated future amortization expense associated with these acquired intangible assets is \$983,000 in the second half of 2005; \$1,967,000 in 2006; \$1,967,000 in 2007; \$1,952,000 in 2008; \$1,943,000 in 2009; \$1,943,000 in 2010; and the remaining \$15,357,000 thereafter.

The acquisition was recorded under the purchase method of accounting as of May 11, 2005 and the operating results of Kadant Johnson were included in Kadant's condensed consolidated statement of income from the acquisition date of May 11, 2005 to July 2, 2005.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

4. Acquisition (continued)

The following condensed consolidated statement of income is presented as if the acquisition of Kadant Johnson had been made at the beginning of the periods presented. This information is not necessarily indicative of what the actual condensed combined statement of income of Kadant and Johnson would have been for the periods presented, nor does it purport to represent the future combined results of operations of Kadant and Johnson.

(In thousands)	Six Months Ended	
	July 2, 2005	July 3, 2004
Revenues	\$ 145,031	\$ 138,142
Operating (Loss) Income *	(2,553)	13,824
(Loss) Income from Continuing Operations	(2,676)	7,843
Loss from Discontinued Operation	(156)	(846)
Net (Loss) Income	\$ (2,832)	\$ 6,997
Basic (Loss) Earnings per Share:		
(Loss) Income from Continuing Operations	\$ (.19)	\$.55
Net (Loss) Income	\$ (.20)	\$.49
Diluted (Loss) Earnings per Share:		
(Loss) Income from Continuing Operations	\$ (.19)	\$.54
Net (Loss) Income	\$ (.20)	\$.48

* Included in operating loss for the first six months of 2005 was \$11.0 million in one-time bonuses and \$3.1 million in acquisition-related costs incurred by The Johnson Corporation prior to the acquisition.

5. Inventories

The components of inventories are as follows:

(In thousands)	July 2, 2005	January 1, 2005
Raw Materials and Supplies	\$ 18,060	\$ 12,849
Work in Process	7,538	6,047
Finished Goods (includes \$635 and \$611 at customer locations)	12,697	8,420
	\$ 38,295	\$ 27,316

6. Short- and Long-Term Obligations

The components of short- and long-term obligations are as follows:

(In thousands)	July 2, 2005	January 1, 2005
Current Portion of Term Loan	\$ 9,000	\$ -
Other Short-Term Obligations	37	-
Current Maturities of Long-Term Obligations	\$ 9,037	\$ -
Long-Term Portion of Term Loan	\$ 51,000	\$ -
Other Long-Term Obligations	980	-
Long-Term Obligations	\$ 51,980	\$ -

Notes to Condensed Consolidated Financial Statements
(Unaudited)

6. Short- and Long-Term Obligations (continued)

To fund a portion of the purchase price for the acquisition of Kadant Johnson, the Company entered into a term loan and revolving credit facility (the "Credit Agreement") effective May 9, 2005 in the aggregate principal amount of up to \$85,000,000, including a \$25,000,000 revolver. The Credit Agreement is among Kadant, as Borrower, the Foreign Subsidiary Borrowers from time to time parties thereto, the several banks and other financial institutions or entities from time to time parties thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent. On May 11, 2005, the Company borrowed \$60,000,000 under the term loan facility, which is repayable in equal quarterly installments over a five-year period. The aggregate principal to be repaid each year is as follows: \$4,500,000, \$9,000,000, \$10,500,000, \$13,500,000, \$15,000,000, and \$7,500,000 in 2005, 2006, 2007, 2008, 2009, and 2010, respectively. Interest on the revolving loan and the term loan accrues and is payable quarterly in arrears at one of the following rates selected by Kadant: (a) the prime rate plus an applicable margin initially set at 0% for 2005, and up to 0.25% thereafter or, (b) a Eurocurrency rate plus an applicable margin initially set at 1% for 2005, and between 0.625% and 1.25% thereafter. The applicable margin is determined based upon Kadant's total debt to earnings before interest, taxes, depreciation and amortization (EBITDA) ratio.

In connection with the Credit Agreement, Kadant agreed to pay a commitment fee, payable quarterly, at an initial rate of 0.25% per annum of the unused amount of revolving credit commitments, subject to adjustment based upon Kadant's total debt to EBITDA ratio (resulting in a per annum rate of between 0.175% and 0.275%).

Debt issuance costs were approximately \$646,000 and are included in other assets in the accompanying condensed consolidated balance sheet. These costs are being amortized to interest expense over five years based on the effective-interest method. As of July 2, 2005, the unamortized debt issuance costs were approximately \$616,000.

The obligations of Kadant under the Credit Agreement may be accelerated upon the occurrence of an event of default under the Credit Agreement, which include customary events of default including, without limitation, payment defaults, defaults in the performance of affirmative and negative covenants, the inaccuracy of representations or warranties, bankruptcy- and insolvency-related defaults, defaults relating to such matters as ERISA, uninsured judgments and the failure to pay certain indebtedness, and a change of control default.

In addition, the Credit Agreement contains negative covenants applicable to Kadant and its subsidiaries, including financial covenants requiring Kadant to comply with a maximum consolidated leverage ratio of either 2.5 or 3.0 and a minimum consolidated fixed charge coverage ratio of 1.5, and restrictions on liens, indebtedness, fundamental changes, dispositions of property, making certain restricted payments (including dividends and stock repurchases), investments, transactions with affiliates, sale and leaseback transactions, swap agreements, changing Kadant's fiscal year, negative pledges, arrangements affecting subsidiary distributions, and entering into new lines of business. As of July 2, 2005, Kadant was in compliance with these covenants.

The loans under the Credit Agreement are guaranteed by certain domestic subsidiaries of Kadant and secured by a pledge of 65% of the stock of the Company's first-tier foreign subsidiaries and the Company's subsidiary guarantors pursuant to a guarantee and pledge agreement effective May 9, 2005 in favor of JPMorgan Chase Bank, N.A., as agent on behalf of the lenders.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

7. Swap Agreement

Kadant entered into a swap agreement (the "Swap Agreement"), which was effective May 17, 2005, to convert \$36,000,000 of the principal balance of the \$60,000,000 term loan from a floating rate to a fixed rate of interest. The Swap Agreement has a five-year term, the same quarterly payment dates as the hedged portion of the term loan and reduces proportionately in line with the amortization of the term loan. Under the Swap Agreement, Kadant will receive a 3-month LIBOR rate and pay a fixed rate of interest of 4.125%. The net effect on interest expense for the hedged portion of the term loan (\$36,000,000) is that Kadant will pay a fixed interest rate of up to 5.375% (the sum of the 4.125% fixed rate under the Swap Agreement and the applicable margin of up to 1.25% on the term loan). The guarantee provisions and the default and financial covenants, as well as certain restrictions on the payment of dividends, included in the Credit Agreement, which are outlined in Note 6, also apply to the Swap Agreement.

The Swap Agreement has been designated as a cash flow hedge and is carried at fair value. As of July 2, 2005, the unrealized loss associated with the Swap Agreement was \$127,000, which is included in other long-term liabilities in the accompanying condensed consolidated balance sheet. Management believes that any credit risk associated with the swap is remote based on the creditworthiness of the financial institution issuing the Swap Agreement.

8. Warranty Obligations

The Company provides for the estimated cost of product warranties at the time of sale based on our actual historical return rates and repair costs. In the Pulp and Papermaking Systems (Papermaking Systems) segment, the Company typically negotiates the terms regarding warranty coverage and length of warranty depending on the products and applications. While the Company engages in extensive product quality programs and processes, the Company's warranty obligation is affected by product failure rates, repair costs, service delivery costs incurred in correcting a product failure, and supplier warranties on parts delivered to the Company. Should actual product failure rates, repair costs, service delivery costs, or supplier warranties on parts differ from the Company's estimates, revisions to the estimated warranty liability would be required.

The changes in the carrying amount of the Company's product warranties for the three- and six-month periods ended July 2, 2005 and July 3, 2004 are as follows:

(In thousands)	Three Months Ended		Six Months Ended	
	July 2, 2005	July 3, 2004	July 2, 2005	July 3, 2004
Balance at Beginning of Period	\$ 3,755	\$ 3,921	\$ 3,582	\$ 3,661
Provision charged to income	117	574	970	1,373
Usage	(238)	(1,011)	(912)	(1,593)
Acquired warranty obligation	232	-	232	-
Other, net (a)	(100)	(24)	(106)	19
Balance at End of Period	\$ 3,766	\$ 3,460	\$ 3,766	\$ 3,460

(a) Represents the effects of currency translation.

See Note 14 for warranty information related to the discontinued operation.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

9. Restructuring Costs

In an effort to improve operating performance at the Papermaking Systems segment's Kadant Lamort subsidiary in France, the Company approved a proposed restructuring of that subsidiary on November 18, 2004. This restructuring was initiated to strengthen Kadant Lamort's competitive position in the European paper industry. Under French law, the proposed restructuring required consultation with Kadant Lamort's workers' council, which consists of elected employees supported by trade union representatives, before implementation. The restructuring originally proposed the reduction of up to 136 full-time positions across all functions in France, and is expected to be implemented in 2005. The Company accrued a restructuring charge of \$9,235,000 in the fourth quarter of 2004, in accordance with Statement of Financial Accounting Standards (SFAS) No. 112, "Employers' Accounting for Postemployment Benefits - An Amendment of Financial Accounting Standards Board (FASB) Statements No. 5 and 43," for severance and other termination costs in connection with the workforce reduction. As a result of the restructuring, the Company expects to realize a curtailment resulting in a reduction in the accrued liability associated with Kadant Lamort's pension plan of approximately \$800,000, which will be recognized in 2005 when the restructuring plan has been implemented. In addition, during the fourth quarter of 2004, the Company recorded restructuring costs of \$280,000, which were accounted for in accordance with SFAS No. 112, related to severance costs of 11 employees at one of the Papermaking Systems segment's U.S. subsidiaries.

A summary of the changes in accrued restructuring costs is as follows:

(In thousands)	Severance
Balance at January 1, 2005	\$10,026
Usage	(150)
Currency translation	(587)

Balance at July 2, 2005	\$ 9,289
	=====

The specific restructuring measures and associated estimated costs are based on the Company's best judgments under prevailing circumstances. The Company believes that the restructuring reserve balance is adequate to carry out the restructuring activities formally identified and committed to during the fourth quarter of 2004, and anticipates that all actions related to these liabilities will be completed in 2005.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

10. Business Segment Information

The Company has combined its operating entities into one reportable operating segment, Papermaking Systems. In addition, the Company has two separate product lines; Fiber-based Products and Casting Products, which are included in the "Other" category below. In classifying operational entities into a particular segment, the Company considered how management assesses performance and makes operating decisions and aggregated businesses with similar economic characteristics, products and services, production processes, customers, and methods of distribution.

(In thousands)	Three Months Ended		Six Months Ended	
	July 2, 2005	July 3, 2004	July 2, 2005	July 3, 2004
Revenues (a):				
Pulp and Papermaking Systems	\$ 62,528	\$ 50,933	\$110,099	\$ 96,497
Other (c)	2,558	1,719	5,731	3,655
	-----	-----	-----	-----
	\$ 65,086	\$ 52,652	\$115,830	\$100,152
	=====	=====	=====	=====
Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense (a):				
Pulp and Papermaking Systems (b)	\$ 5,934	\$ 6,152	\$ 9,310	\$ 12,495
Corporate and Other (c,d)	(977)	(911)	(1,533)	(2,446)
	-----	-----	-----	-----
Total Operating Income	4,957	5,241	7,777	10,049
Interest (Expense) Income, Net	(94)	314	376	635
	-----	-----	-----	-----
	\$ 4,863	\$ 5,555	\$ 8,153	\$ 10,684
	=====	=====	=====	=====
Capital Expenditures (a):				
Pulp and Papermaking Systems	\$ 612	\$ 505	\$ 752	\$ 835
Corporate and Other (c,d)	97	50	123	84
	-----	-----	-----	-----
	\$ 709	\$ 555	\$ 875	\$ 919
	=====	=====	=====	=====
			July 2, 2005	January 1, 2005
Total Assets:				
Pulp and Papermaking Systems			\$341,147	\$196,248
Corporate and Other (c,d)			32,601	73,339
			-----	-----
Total Assets from Continuing Operations			373,748	269,587
Total Assets from Discontinued Operations			14,919	15,650
			-----	-----
			\$388,667	\$285,237
			=====	=====

(a) The results for Kadant Johnson are included from the acquisition date of May 11, 2005 to July 2, 2005.

(b) Includes a pre-tax gain of \$970 in the six-month period ending July 3, 2004, which resulted from renegotiating a series of agreements with one of the Company's licensees.

(c) Other includes the results from the Fiber-based Products business and Casting Products business.

(d) Corporate primarily includes general and administrative expenses.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

11. Stock-Based Compensation Plans and Pro Forma Stock-Based Compensation Expense

As permitted by SFAS No. 148, "Accounting for Stock-based Compensation - Transition and Disclosure," and SFAS No. 123, "Accounting for Stock-based Compensation" (SFAS No. 123), the Company has elected to continue to apply Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB Opinion No. 25), and related interpretations to account for its stock-based compensation plans. No stock-based employee compensation cost related to stock option awards is reflected in net income, as all options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of grant. Had compensation cost for awards granted after 1994 under the Company's stock-based compensation plans been determined based on the fair values at the grant dates consistent with the method set forth under SFAS No. 123, the effect on certain of the Company's financial results would have been as follows:

(In thousands, except per share amounts)	Three Months Ended		Six Months Ended	
	July 2, 2005	July 3, 2004	July 2, 2005	July 3, 2004
Income from Continuing Operations	\$ 3,147	\$ 3,983	\$ 6,234	\$ 7,317
Income (Loss) from Discontinued Operation	207	(240)	(156)	(846)
Net Income As Reported	3,354	3,743	6,078	6,471
Deduct: Total stock-based employee compensation expense determined under the fair-value-based method for all awards, net of tax	(147)	(623)	(349)	(1,129)
Pro forma net income	\$ 3,207	\$ 3,120	\$ 5,729	\$ 5,342
Basic Earnings per Share:				
As reported:				
Income from continuing operations	\$ 0.23	\$ 0.28	\$ 0.45	\$ 0.51
Net income	\$ 0.24	\$ 0.26	\$ 0.44	\$ 0.46
Pro forma:				
Income from continuing operations	\$ 0.22	\$ 0.24	\$ 0.42	\$ 0.44
Net income	\$ 0.23	\$ 0.22	\$ 0.41	\$ 0.38
Diluted Earnings per Share:				
As reported:				
Income from continuing operations	\$ 0.22	\$ 0.27	\$ 0.44	\$ 0.50
Net income	\$ 0.24	\$ 0.26	\$ 0.43	\$ 0.44
Pro forma:				
Income from continuing operations	\$ 0.21	\$ 0.23	\$ 0.41	\$ 0.42
Net income	\$ 0.23	\$ 0.21	\$ 0.40	\$ 0.37

12. Employee Benefit Plans

One of the Company's U.S. subsidiaries has a noncontributory defined benefit retirement plan. Benefits under the plan are based on years of service and employee compensation. Funds are contributed to a trustee as necessary to provide for actuarially determined costs, generally equal to the minimum amounts required by the Employee Retirement Income Security Act (ERISA). The same subsidiary has a post-retirement welfare benefits plan (reflected in the table below in "Other Benefits"). No future retirees are eligible for the post-retirement welfare benefits plan, and the plan includes a limit on the subsidiary's contributions.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

12. Employee Benefit Plans (continued)

No cash contributions are expected for the U.S. subsidiary's noncontributory defined benefit retirement plan and no cash contributions, other than funding current benefit payments, are expected for the other pension and post-retirement welfare benefits plans in 2005.

On December 8, 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Act) was enacted that provides for a Medicare prescription drug benefit beginning in 2006 and federal subsidies to employers who provide drug coverage to retirees. The Company's accumulated postretirement benefit obligation or net periodic postretirement benefit cost do not reflect any amount associated with the subsidy as the Company has not yet determined whether the benefits provided by the plan are actuarially equivalent to or better than Medicare Part D under the Act.

13. Recent Accounting Pronouncements

Share-Based Payment

On December 16, 2004, the FASB issued SFAS No. 123 (revised 2004) "Share-Based Payment" (SFAS No. 123R). SFAS No. 123R replaces SFAS No. 123, supersedes APB Opinion No. 25, and amends SFAS No. 95 "Statement of Cash Flows." SFAS No. 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. SFAS No. 123R is effective for the Company on January 1, 2006. The pro forma disclosures previously permitted under SFAS No. 123 will no longer be an alternative to financial statement recognition. As permitted by SFAS No. 123, the Company currently accounts for share-based payments to employees using APB Opinion No. 25's intrinsic value method and, as such, generally recognizes no compensation cost for employee stock options. Under SFAS 123R, companies must determine the appropriate fair value model to be used at the date of adoption. The transition methods include prospective and retrospective adoption options. Management is evaluating the requirements of SFAS No. 123R. The impact of the adoption of SFAS No. 123R cannot be predicted at this time because it will vary based on the levels of share-based payments granted in the future and the options then outstanding.

Inventory Costs

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4," which requires that abnormal amounts of idle facility expense, freight, handling costs and wasted material be recognized as current-period charges. This Statement also introduces the concept of "normal capacity" and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. Unallocated overheads must be recognized as an expense in the period in which they are incurred. SFAS No. 151 will be effective for the Company on January 1, 2006. Management is currently evaluating the requirements of SFAS No. 151 and the impact this standard will have on its financial statements.

14. Discontinued Operation

On October 27, 2004, the Company's board of directors approved a plan and management committed to sell the Company's composite building products business (composites business) after making a determination that the business no longer aligned with the Company's long-term strategy. The Company intends to sell the composites business as a going concern and has engaged an investment banking firm for that purpose. The Company plans to sell this business in 2005 at a price that is reasonable compared to its carrying value. As a result of this decision, the Company evaluated whether the composites business should be classified as a discontinued operation under SFAS No. 144. The Company has presented the composites business in the accompanying condensed consolidated financial statements as a discontinued operation, as all the criteria under SFAS No. 144 have been met. All prior periods have been restated to reflect the composites business as a discontinued operation.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

14. Discontinued Operation (continued)

Operating results for the composites business are as follows:

(In thousands)	Three Months Ended		Six Months Ended	
	July 2, 2005	July 3, 2004	July 2, 2005	July 3, 2004
Revenues	\$ 5,548	\$ 5,130	\$ 10,784	\$ 9,357
Income (Loss) Before Provision for Income Taxes	318	(370)	(240)	(1,302)
Income Tax (Provision) Benefit	(111)	130	84	456
Income (Loss) From Discontinued Operation	\$ 207	\$ (240)	\$ (156)	\$ (846)

The major classes of assets and liabilities of the discontinued operation included in the accompanying condensed consolidated balance sheet are as follows:

(In thousands)	July 2, 2005	January 1, 2005
Cash and cash equivalents	\$ -	\$ 39
Accounts receivable, less allowances	1,705	2,252
Inventories	3,861	4,035
Other current assets	1,966	1,981
Property, plant, and equipment, at cost, net	6,803	6,760
Other assets	584	583
Total Assets	14,919	15,650
Accounts payable	1,262	1,446
Accrued warranty costs	3,486	4,327
Other current liabilities	924	905
Other liabilities	900	900
Total Liabilities	6,572	7,578
Net Assets	\$ 8,347	\$ 8,072

The composites business offers a standard limited warranty to the original owner of its decking and roofing products, limited to repair or replacement of the defective product or a refund of the original purchase price. The composites business records an estimate for warranty-related costs at the time of sale based on actual historical return rates and repair costs, as well as other analytical tools for estimating future warranty claims. These estimates are revised for variances between actual and expected claims rates. The analysis of expected warranty claims rates includes detailed assumptions associated with potential product returns, including the type of product sold, temperatures at the location of installation, density of boards, and other factors. Certain assumptions, such as the effect of weather conditions and high temperatures on the product installed, include inherent uncertainties that are subject to fluctuation, which could impact future warranty provisions. Due to the highly subjective nature of these assumptions, the Company has recorded its best estimate of the cost of expected warranty claims. It is reasonably possible that the ultimate settlement of such claims may exceed the amount recorded.

Notes to Condensed Consolidated Financial Statements
(Unaudited)

14. Discontinued Operation (continued)

The composites business experienced warranty issues that affected its profitability in 2003 and 2004. There was a substantial increase in warranty claims in 2004, with the most significant increase occurring in the three-month period ended October 2, 2004. During the first six months of 2004, the majority of the claims were associated with contraction of certain decking products. In the three-month period ended October 2, 2004, the increased claims were associated with a new issue concerning excessive oxidation that affected the integrity of the plastic used in some of the decking products manufactured prior to October 2003. As a result of the increase in claims received and the estimate for future potential claims, the Company increased its warranty expense in 2004 compared to prior periods. Included in this increased warranty expense was the cost of exchanging material held by the composites business' distributors with new material and its best estimate of costs related to future potential valid claims arising from installed products.

A summary of the changes in accrued warranty costs in the six-month periods ended July 2, 2005 and July 3, 2004 is as follows:

(In thousands)	Six Months Ended	
	July 2, 2005	July 3, 2004
Balance at Beginning of Period	\$ 4,327	\$ 869
Provision	633	1,330
Usage	(1,474)	(728)
Balance at End of Period	\$ 3,486 =====	\$ 1,471 =====

The Company likely will not be able to transfer all the liabilities of the composites business in a sale. Any changes associated with the carrying value of liabilities that are not assumed by a buyer would continue to impact the Company's consolidated results after the sale is completed.

Item 2 - Management's Discussion and Analysis of Financial Condition and Results

of Operations

This Quarterly Report on Form 10-Q includes forward-looking statements that are not statements of historical fact, and may include statements regarding possible or assumed future results of operations. Forward-looking statements are subject to risks and uncertainties and are based on the beliefs and assumptions of our management, using information currently available to our management. When we use words such as "believes," "expects," "anticipates," "intends," "plans," "estimates," "should," "likely," "will," "would," or similar expressions, we are making forward-looking statements.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties, and assumptions. Our future results of operations may differ materially from those expressed in the forward-looking statements. Many of the important factors that will determine these results and values are beyond our ability to control or predict. You should not put undue reliance on any forward-looking statements. We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future events, or otherwise. For a discussion of important factors that may cause our actual results to differ materially from those suggested by the forward-looking statements, you should read carefully the section captioned "Risk Factors" in this Report.

Overview

Company Background

We are a leading supplier of equipment used in the global papermaking and paper recycling industry and are also a manufacturer of granules made from papermaking byproducts. Our continuing operations consist of one reportable operating segment, Pulp and Papermaking Systems (Papermaking Systems), and two separate product lines; Fiber-based Products and Casting Products. In classifying operational entities into a particular segment, we considered how our management assesses performance and makes operating decisions, and aggregated businesses with similar economic characteristics, products and services, production processes, customers, and methods of distribution. We also manage a composite building products business (composites business), which is presented as a discontinued operation in the accompanying condensed consolidated financial statements as a result of our decision to sell that business.

We were incorporated in Delaware in November 1991 to be the successor-in-interest to several papermaking equipment businesses of Thermo Electron Corporation (Thermo Electron). In November 1992, we completed an initial public offering of a portion of our outstanding common stock. On July 12, 2001, we changed our name to Kadant Inc. from Thermo Fibertek Inc. In August 2001, Thermo Electron disposed of its remaining equity interest in us by means of a stock dividend to its shareholders. In May 2003, we moved the listing of our common stock to the New York Stock Exchange, where it continues to trade under the symbol "KAI."

Pulp and Papermaking Systems Segment

Our Papermaking Systems segment designs and manufactures stock-preparation systems and equipment, paper machine accessory equipment, and water-management systems for the paper and paper recycling industries. With the acquisition of The Johnson Corporation (Kadant Johnson) in May 2005, we added fluid handling systems, which improve dryer performance during the papermaking process. Our principal products include:

- Stock-preparation systems and equipment: custom-engineered systems and equipment, as well as standard individual components, for pulping, de-inking, screening, cleaning, and refining recycled and virgin fibers for preparation for entry into the paper machine during the production of recycled paper;

Overview (continued)

- Paper machine accessory equipment: doctoring systems and related consumables that continuously clean papermaking rolls to keep paper machines running efficiently; doctor blades made of a variety of materials to perform functions including cleaning, creping, web removal, and application of coatings; and profiling systems that control moisture, web curl, and gloss during paper production;
- Water-management systems: systems and equipment used to continuously clean paper machine fabrics and to drain, purify, and recycle process water during paper sheet formation; and
- Fluid handling: rotary joints, precision unions, steam and condensate systems, components, and controls used primarily in the dryer section of the papermaking process and during the production of corrugated boxboard, metals, plastics, rubber, and textiles.

Other

Our other business lines include the Fiber-based Products business and Casting Products business.

Our Fiber-based Products business produces biodegradable, absorbent granules from papermaking byproducts for use primarily as carriers for agricultural, home lawn and garden, and professional lawn, turf and ornamental applications, as well as for oil and grease absorption.

Our Casting Products business manufactures grey and ductile iron castings.

Discontinued Operation

We produce composite building products, including decking and railing systems and roof tiles, made from recycled fiber, plastic, and other material, which are marketed through distributors primarily to the building industry.

On October 27, 2004, our board of directors approved a plan and management committed to sell our composites business after making a determination that the business no longer aligned with our long-term strategy. We intend to sell the composites business as a going concern and are working with an investment banking firm for that purpose. We plan to sell the composites business by the end of 2005 at a price that is reasonable compared to its carrying value. The composites business had total assets and liabilities of \$14.9 million and \$6.6 million, respectively, as of July 2, 2005, including accrued warranty costs of \$3.5 million, which we may retain in the sale of the business. In addition, revenues and net income for the second quarter of 2005 were \$5.5 million and \$0.2 million, respectively, and the revenues and net loss for the first six months of 2005 were \$10.8 million and \$0.2 million, respectively. The composites business has been presented as a discontinued operation in the accompanying condensed consolidated financial statements for all periods presented.

International Sales

During the first six months of 2005 and 2004, approximately 62% and 61%, respectively, of our sales were to customers outside the United States, principally in Europe and Asia. We generally seek to charge our customers in the same currency in which our operating costs are incurred. However, our financial performance and competitive position can be affected by currency exchange rate fluctuations affecting the relationship between the U.S. dollar and foreign currencies. We seek to reduce our exposure to currency fluctuations through the use of forward currency exchange contracts. We may enter into forward contracts to hedge certain firm purchase and sale commitments denominated in currencies other than our subsidiaries' functional currencies. These contracts hedge transactions principally denominated in U.S. dollars.

Overview (continued)

Application of Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of our condensed consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that reflect significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that our most critical accounting policies, upon which our financial condition depends and which involve the most complex or subjective decisions or assessments, are those described in "Management's Discussion and Analysis of Financial Condition and Results of Operations" under the section captioned "Application of Critical Accounting Policies and Estimates" in Item 7 of our Annual Report on Form 10-K for the fiscal year ended January 1, 2005, filed with the Securities and Exchange Commission. There have been no material changes to these critical accounting policies since fiscal year-end 2004 that warrant further disclosure.

Industry and Business Outlook

Our products are primarily sold to the pulp and paper industry. The paper industry had been in a prolonged downcycle for the past several years. While the performance of paper producers, especially in North America, has been gradually improving over the past year, the industry is continuing to experience sluggish demand. The profitability of paper producers is still being negatively affected by higher operating costs, especially higher energy and chemical costs. We believe paper companies are still cautious about increasing their capital and operating spending in the current market environment. We expect, however, if the market recovers, paper companies will increase their capital and operating spending, which would have a positive effect on paper company suppliers, such as Kadant, although the timing of such effect is difficult to predict. We continue to concentrate our efforts on several initiatives intended to improve our operating results, including: (i) integrating the Kadant Johnson acquisition, (ii) penetrating new markets outside the paper industry, (iii) opening a stock-preparation production plant in China, (iv) increasing aftermarket sales, (v) completing the Kadant Lamort restructuring, and (vi) selling the composites business. In addition, we continue to focus our efforts on managing our operating costs, capital expenditures, and working capital.

In an effort to improve operating performance at our Kadant Lamort subsidiary in France, we approved a proposed restructuring of that subsidiary on November 18, 2004. This restructuring is intended to strengthen Kadant Lamort's competitive position in the European paper industry. Under French law, the proposed restructuring required consultation with Kadant Lamort's workers' council, which represents the employees, before implementation. The restructuring originally proposed the reduction of up to 136 full-time positions in France. We accrued a restructuring charge of \$9.2 million in the fourth quarter of 2004 for severance and other termination costs in connection with the workforce reduction. Kadant Lamort experienced intermittent work stoppages by employees protesting the proposed restructuring while the consultations with the workers' council were in process. We recently completed the necessary consultations with the workers' council and expect the restructuring to be fully implemented by the fourth quarter of 2005. We expect that Kadant Lamort will continue to experience significant operating losses until these restructuring actions are completed.

We continue to pursue market opportunities outside North America. In the last several years, China has become a significant market for our stock-preparation equipment. To capitalize on this growing market, we plan to build a manufacturing and assembly facility in China for our stock-preparation equipment and related aftermarket products.

Overview (continued)

Revenues from China are primarily derived from large capital orders, the timing of which is often difficult to predict. For the past several quarters, our customers in China have experienced delays in obtaining financing for their capital addition and expansion projects, which we believe is due to efforts by the Chinese government to control economic growth, which are reflected in a slowdown in financing approvals in China's banking system. This has caused delays in receiving orders and, as a result, will delay our recognizing revenue on these projects to periods later than originally expected. We plan to use our new facility in China as a base for increasing our aftermarket business, which we believe will be more predictable.

On May 11, 2005, we acquired all the outstanding stock of Kadant Johnson, a leading supplier of steam and condensate systems, components, and controls used primarily in the dryer section of the papermaking process and during the production of steel, plastics, rubber, and textiles. Kadant Johnson was a privately held company based in Michigan with approximately 575 employees at operations in North and South America, Europe and Asia. Kadant Johnson's primary products include rotary joints, syphons, and related steam and condensate systems. The purchase price was \$101.5 million in cash, subject to a further post-closing adjustment as outlined in the purchase agreement for Kadant Johnson, and \$3.1 million in acquisition related costs. In addition to the cash consideration, we issued a letter of credit to the sellers for \$4 million, subject to adjustment, related to certain tax assets of Kadant Johnson, the value of which we expect to realize. The parties also agreed in the purchase agreement to an earn-out provision, based on the achievement of certain revenue targets between the closing date and July 1, 2006, which could increase the purchase price by up to \$8 million. The majority of the results for Kadant Johnson will be reported in the Pulp and Papermaking Systems segment within the fluid handling product line. Results associated with the Casting Products business will be reported in "Other."

Our 2005 guidance reflects expected revenues and earnings per share from continuing operations, which excludes the results from our composite building products business (accounted for as a discontinued operation). For the third quarter of 2005, we expect to earn between \$.19 to \$.21 per diluted share, on revenues of \$65 to \$67 million. For the full year, we expect to earn between \$.92 to \$1.00 per diluted share, on revenues of \$250 to \$260 million.

Results of Operations

Second Quarter 2005 Compared With Second Quarter 2004

The following table sets forth our unaudited condensed consolidated statement of income expressed as a percentage of total revenues for the second fiscal quarters of 2005 and 2004. The results of operations for the fiscal quarter ended July 2, 2005 are not necessarily indicative of the results to be expected for the full fiscal year.

	Three Months Ended	
	July 2, 2005	July 3, 2004
Revenues	100%	100%
Costs and Operating Expenses:		
Cost of revenues	62	61
Selling, general, and administrative expenses	28	28
Research and development expenses	2	1
	92	90
Operating Income	8	10
Interest Income (Expense), net	-	1
Income from Continuing Operations Before Provision for Income Taxes and Minority Interest Expense	8	11
Provision for Income Taxes	3	3
Minority Interest Expense	-	-
Income from Continuing Operations	5	8
Income (Loss) from Discontinued Operation	-	(1)
Net Income	5%	7%

Revenues

Revenues increased \$12.4 million, or 24%, to \$65.1 million in the second quarter of 2005 from \$52.7 million in the second quarter of 2004. Revenues in the second quarter of 2005 include an \$11.1 million, or 21%, increase from recently acquired Kadant Johnson, and the favorable effect of currency translation of \$1.2 million, or 2%, due to a weaker U.S. dollar relative to most of the functional currencies in countries in which we operate.

Revenues for the second quarters of 2005 and 2004 from our Papermaking Systems segment and other businesses are as follows:

(In thousands)	Three Months Ended	
	July 2, 2005	July 3, 2004
Revenues:		
Pulp and Papermaking Systems	\$ 62,528	\$ 50,933
Other	2,558	1,719
	\$ 65,086	\$ 52,652

Results of Operations (continued)

Pulp and Papermaking Systems Segment. Revenues at the Papermaking Systems segment increased \$11.6 million, or 23%, to \$62.5 million in the second quarter of 2005 from \$50.9 million in the second quarter of 2004. Revenues in the second quarter of 2005 include a \$10.6 million, or 21%, increase from recently acquired Kadant Johnson, and the favorable effect of currency translation described above, all of which related to this segment.

Revenues at the Papermaking Systems segment by product line are as follows:

(In millions)	Three Months Ended		Increase (Decrease)	Increase (Decrease) Excluding Effect of Currency Translation
	July 2, 2005	July 3, 2004		
Product Line:				
Stock-Preparation Equipment	\$ 29.2	\$ 26.9	\$ 2.3	\$ 1.7
Accessories	15.3	15.9	(0.6)	(1.1)
Water-Management	7.0	7.8	(0.8)	(0.9)
Fluid Handling	10.6	-	10.6	10.6
Other	0.4	0.3	0.1	0.1
	-----	-----	-----	-----
	\$ 62.5	\$ 50.9	\$ 11.6	\$ 10.4
	=====	=====	=====	=====

Revenues from the segment's stock-preparation equipment product line increased \$2.3 million, or 9%, in the second quarter of 2005 compared to the second quarter of 2004, including a \$0.6 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues from the stock-preparation equipment product line increased \$1.7 million, or 6%, due to a \$7.7 million increase in sales in our North American-based business due to strong sales in our Chemi-Washer(TM) product line. This increase was offset in part by a \$3.9 million, or 37%, decrease in sales in China in the second quarter of 2005 related to the timing of several large orders and to continued delays by customers in securing their financing approvals from the Chinese government. In addition, sales in Europe decreased \$2.1 million, or 20%, in the second quarter of 2005 due to continuing weakness in the European market for stock-preparation capital equipment.

Revenues from the segment's accessories product line decreased \$0.6 million, or 4%, in the second quarter of 2005 compared to the second quarter of 2004, including a \$0.5 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues from the segment's accessories product line decreased \$1.1 million, or 7%, due to a decrease in sales in North America and Europe due to weaker demand for our capital equipment.

Revenues from the segment's water-management product line decreased \$0.8 million, or 10%, in the second quarter of 2005 compared to the second quarter of 2004, including a \$0.1 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues from the segment's water-management product line decreased \$0.9 million, or 12%, due primarily to weak demand for our capital equipment in North America.

Revenues from the fluid handling product line were \$10.6 million in the second quarter of 2005, which reflects the results for Kadant Johnson from the acquisition date of May 11, 2005 to July 2, 2005.

Results of Operations (continued)

Other. Revenues from the Fiber-based Products business increased \$0.4 million, or 19%, to \$2.1 million in the second quarter of 2005 from \$1.7 million in the second quarter of 2004, primarily as a result of an increase in sales to an existing customer of Biodac(TM), our product family of biodegradable granules that we produce from papermaking byproducts. Revenues from the Casting Products business were \$0.5 million in the second quarter of 2005.

Gross Profit Margin

Gross profit margin was 38% in the second quarter of 2005 compared to 39% in the second quarter of 2004.

Gross profit margins for the second quarters of 2005 and 2004 for our Papermaking Systems segment and our other businesses are as follows:

	Three Months Ended	
	July 2, 2005	July 3, 2004
Gross Profit Margin:		
Pulp and Papermaking Systems	38%	38%
Other	37	45
	38%	39%

The gross profit margin at the Papermaking Systems segment was 38% in the second quarter of 2005 and 2004. The fluid handling product line contributed a 3% increase in gross profit margins in the second quarter of 2005, which was offset by lower margins in our stock-preparation product line. The gross profit margin at our other businesses decreased to 37% in the second quarter of 2005 from 45% in the second quarter of 2004 due to the inclusion of lower margins at the Casting Products business.

Operating Expenses

Selling, general, and administrative expenses as a percentage of revenues remained constant at 28% in the second quarters of 2005 and 2004. Selling, general, and administrative expenses increased to \$18.5 million in the second quarter of 2005 from \$14.6 million in the second quarter of 2004, an increase of \$3.9 million, or 27%, due primarily to the inclusion of \$4.1 million in selling, general, and administrative expenses from Kadant Johnson. In addition, an increase of \$0.4 million in the second quarter of 2005 was due to the unfavorable impact of foreign currency translation in the Papermaking Systems segment compared to the second quarter of 2004.

Research and development expenses were \$1.2 million and \$0.6 million in the second quarters of 2005 and 2004, respectively, and represented 2% and 1% of revenues in the 2005 and 2004 periods, respectively.

Interest Income

Interest income increased to \$0.4 million in the second quarter of 2005 from \$0.3 million in the second quarter of 2004 primarily due to higher prevailing interest rates, offset in part by a decrease in the average cash balances resulting from the May 2005 acquisition of Kadant Johnson.

Interest Expense

Interest expense increased to \$0.5 million in the second quarter of 2005 from \$4 thousand in the second quarter of 2004 due to interest expense associated with the \$60.0 million in borrowings entered into in May 2005 to fund the Kadant Johnson acquisition.

Results of Operations (continued)

Income Taxes

Our effective tax rate was 34% and 28% in the second quarters of 2005 and 2004, respectively. The 28% effective tax rate in the second quarter of 2004 consisted of our 35% recurring tax rate offset by a 7% non-recurring tax benefit resulting from a reduction of \$0.4 million in tax reserves primarily associated with our foreign operations, as the reserves were no longer required.

Income from Continuing Operations

Income from continuing operations decreased to \$3.1 million in the second quarter of 2005 from \$4.0 million in the second quarter of 2004, a decrease of \$0.9 million, or 21%. The largest components of this decrease can be attributed to a decrease in gross profit margins and an increase in interest expense (see Gross Profit Margin and Interest Expense above for further discussion).

Income (Loss) from Discontinued Operation

The discontinued operation had net income of \$0.2 million in the second quarter of 2005 compared to a net loss of \$0.2 million in the second quarter of 2004, due primarily to a \$0.4 million increase in revenues, and a \$0.3 million decrease in operating expenses, which was offset by a \$0.2 million increase in income taxes.

First Six Months 2005 Compared With First Six Months 2004

The following table sets forth our unaudited condensed consolidated statement of income expressed as a percentage of total revenues for the first six months of 2005 and 2004. The results of operations for the first six months of 2005 are not necessarily indicative of the results to be expected for the full fiscal year.

	Six Months Ended	
	July 2, 2005	July 3, 2004
Revenues	100%	100%
Costs and Operating Expenses:		
Cost of revenues	62	60
Selling, general, and administrative expenses	29	28
Research and development expenses	2	2
	93	90
Operating Income	7	10
Interest Income, net	-	1
Income from Continuing Operations Before Provision for		
Income Taxes and Minority Interest Expense	7	11
Provision for Income Taxes	2	4
Minority Interest Expense	-	-
Income from Continuing Operations	5	7
Loss from Discontinued Operation	-	(1)
Net Income	5%	6%

Results of Operations (continued)

Revenues

Revenues increased \$15.6 million, or 16%, to \$115.8 million in the first six months of 2005 from \$100.2 million in the first six months of 2004. Revenues in the 2005 period include a \$10.6 million, or 11%, increase from recently acquired Kadant Johnson, and the favorable effect of currency translation of \$2.3 million due to a weaker U.S. dollar relative to most of the functional currencies in countries in which we operate.

Revenues by segment for the first six months of 2005 and 2004 were as follows:

(In thousands)	Six Months Ended	
	July 2, 2005	July 3, 2004
Revenues:		
Pulp and Papermaking Systems	\$ 110,099	\$ 96,497
Other	5,731	3,655
	<u>\$ 115,830</u>	<u>\$ 100,152</u>

Pulp and Papermaking Systems Segment. Revenues at the Papermaking Systems segment increased \$13.6 million, or 14%, to \$110.1 million in the first six months of 2005 from \$96.5 million in the first six months of 2004. Revenues in the first six months of 2005 include the favorable effect of currency translation described above, all of which related to this segment.

Revenues at the Papermaking Systems segment by product line are as follows:

(In millions)	Three Months Ended		Increase (Decrease)	Increase (Decrease) Excluding Effect of Currency Translation
	July 2, 2005	July 3, 2004		
Product Line:				
Stock-Preparation Equipment	\$ 53.8	\$ 48.6	\$ 5.2	\$ 4.0
Accessories	30.6	31.9	(1.3)	(2.2)
Water-Management	14.3	15.3	(1.0)	(1.2)
Fluid Handling	10.6	-	10.6	10.6
Other	0.8	0.7	0.1	0.1
	<u>\$ 110.1</u>	<u>\$ 96.5</u>	<u>\$ 13.6</u>	<u>\$ 11.3</u>

Revenues from the segment's stock-preparation equipment product line increased \$5.2 million, or 11%, in the first six months of 2005 compared to the first six months of 2004, including a \$1.2 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues from the stock-preparation equipment product line increased \$4.0 million, or 8%, due to a \$9.9 million, or 76%, increase in sales in our North American-based business. These increases were offset in part by a \$4.9 million, or 28%, decrease in sales in China in the first six months of 2005 due to continued delays by customers in securing their financing approvals from the Chinese government. In addition, sales in Europe decreased \$1.0 million, or 5%, in the first six months of 2005 due to continued weakness in the European market for stock-preparation capital equipment.

Results of Operations (continued)

Revenues from the segment's accessories product line decreased \$1.3 million, or 4%, in the first six months of 2005 compared to the first six months of 2004, including a \$0.9 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues from the segment's accessories product line decreased \$2.2 million, or 7%, due to a decrease in sales in North America and Europe.

Revenues from the segment's water-management product line decreased \$1.0 million, or 6%, in the first six months of 2005 compared to the first six months of 2004, including a \$0.2 million increase from the favorable effect of currency translation. Excluding the effect of currency translation, revenues from the segment's water-management product line decreased \$1.2 million, or 8%, due primarily to a decrease in capital sales in North America.

Revenues from the fluid handling product line were \$10.6 million in the first six months of 2005, which reflects the results for Kadant Johnson from the acquisition date of May 11, 2005 to July 2, 2005.

Other. Revenues from the Fiber-based Products business increased \$1.5 million, or 43%, to \$5.2 million in the first six months of 2005 from \$3.7 million in the first six months of 2004, primarily as a result of an increase in sales to an existing customer of Biodac(TM), our product family of biodegradable granules that we produce from papermaking byproducts. Revenues from the Casting Products business were \$0.5 million in the first six months of 2005.

Gross Profit Margin

Gross profit margin was 38% in the first six months of 2005 compared to 40% in the first six months of 2004.

Gross profit margins for the first six months of 2005 and 2004 for our Papermaking Systems segment and our other businesses are as follows:

	Six Months Ended	
	July 2, 2005	July 3, 2004

Gross Profit Margin:		
Pulp and Papermaking Systems	37%	40%
Other	40	39
	-----	-----
	38%	40%

The gross profit margin at the Papermaking Systems segment decreased to 37% in the first six months of 2005 from 40% in the first six months of 2004. The fluid handling product line contributed a 1% increase in gross profit margins in the first six months of 2005, which was offset by lower margins in our stock-preparation product line. The gross profit margin at our other businesses was 40% and 39% in the first six months of 2005 and 2004, respectively.

Operating Expenses

Selling, general, and administrative expenses as a percentage of revenues were 29% and 28% in the first six months of 2005 and 2004, respectively. Selling, general, and administrative expenses increased to \$33.4 million in the first six months of 2005 from \$28.3 million in the first six months of 2004, an increase of \$5.1 million, or 18%. The \$5.1 million increase was primarily due to \$4.1 million of selling, general, and administrative expenses in the 2005 period associated with Kadant Johnson and a gain of approximately \$1.0 million in the first quarter of 2004. The gain in the first quarter of 2004 resulted from the renegotiation of a series of agreements with one of our licensees, which lowered selling, general, and administrative expenses in that period.

Results of Operations (continued)

Research and development expenses were \$2.3 million and \$1.5 million and represented 2% of revenues in the first six months of 2005 and 2004. Included in the \$0.8 million increase in research and development expenses were \$0.2 million of research and development expenses associated with Kadant Johnson.

Interest Income

Interest income increased to \$0.9 million in the first six months of 2005 from \$0.6 million in the first six months of 2004 primarily due to higher prevailing interest rates.

Interest Expense

Interest expense increased to \$0.5 million in the first six months of 2005 from \$12 thousand in the first six months of 2004 due to interest expense associated with the \$60.0 million in borrowings entered into in May 2005 to fund the Kadant Johnson acquisition.

Income Taxes

Our effective tax rate was 23% and 31% in the first six months of 2005 and 2004, respectively. The 23% effective tax rate in the first six months of 2005 consisted of our 34% recurring tax rate, offset by an 11% non-recurring tax benefit associated with a reimbursement of \$0.9 million received from our former parent company, Thermo Electron, pursuant to our tax matters agreement for tax years in which we were included in Thermo Electron's consolidated tax return. The 31% effective tax rate in the first six months of 2004 consisted of a 35% recurring tax rate, offset by a 4% non-recurring tax benefit resulting from a reduction of \$0.4 million in tax reserves primarily associated with our foreign operations, as the reserves were no longer required.

Income from Continuing Operations

Income from continuing operations decreased to \$6.2 million in the first six months of 2005 from \$7.3 million in the first six months of 2004, a decrease of \$1.1 million, or 15%. The largest component of this decrease can be attributed to a decrease in gross profit margins (see Gross Profit Margin above for further discussion).

Loss from Discontinued Operation

The loss from our discontinued operation decreased to \$0.2 million in the first six months of 2005 from \$0.8 million in the first six months of 2004, due primarily to a \$1.4 million increase in revenues.

Liquidity and Capital Resources

Consolidated working capital, including the discontinued operation, was \$86.8 million at July 2, 2005, compared with \$113.7 million at January 1, 2005. Included in working capital are cash and cash equivalents of \$46.2 million at July 2, 2005, compared with \$82.1 million at January 1, 2005. At July 2, 2005, \$23.9 million of cash and cash equivalents were held by our foreign subsidiaries.

Our operating activities provided \$4.9 million and \$8.3 million of cash during the first six months of 2005 and 2004, respectively. The most significant components of the cash provided in the first six months of 2005 were the cash provided by income from continuing operations of \$6.2 million and a non-cash charge for depreciation and amortization expense of \$2.7 million. The remaining portion of the cash provided in the first six months of 2005 is comprised of the following offsetting components. An increase in unbilled contract costs and fees used cash of \$6.1

Liquidity and Capital Resources (continued)

million in the first six months of 2005. A decrease in inventories in the first six months of 2005 provided cash of \$3.1 million. A decrease in other current liabilities used cash of \$2.9 million in the first six months of 2005. A decrease in accounts receivable in the first six months of 2005 provided an increase in cash of \$2.4 million primarily at the Papermaking Systems segment, due to the timing of payments.

Our investing activities used cash of \$100.2 million and \$51 thousand in the first six months of 2005 and 2004, respectively. During the first six months of 2005, we used cash of \$101.4 million to acquire the stock of The Johnson Corporation. In addition, during the first six months of 2005, \$3.1 million of deferred acquisition costs associated with the Kadant Johnson acquisition were capitalized to goodwill.

Our financing activities provided cash of \$62.6 million in the first six months of 2005 and used cash of \$2.2 million in the first six months of 2004. During the first six months of 2005, we received proceeds of \$60 million from a term loan we entered into to fund a portion of the purchase price for Kadant Johnson. We also increased our short- and long-term obligations by \$4 million, which represents additional consideration for Kadant Johnson to be paid over the next five years. In addition, we used cash of \$2.1 million to purchase our common stock on the open market. In the first six months of 2004, we used cash of \$6.2 million to purchase our common stock on the open market and received \$4.6 million from the issuance of common stock in connection with the exercise of employee stock options.

Our discontinued operation used cash of \$0.4 million in the first six months of 2005 and provided cash of \$0.2 million in the first six months of 2004. The use of cash of \$0.4 million in the first six months of 2005 was primarily due to a decrease in accrued warranty costs of \$0.8 million, and the loss from discontinued operation of \$0.2 million, offset by a decrease in accounts receivable of \$0.5 million.

On October 22, 2004, the American Jobs Creation Act of 2004 (the Act) was signed into law. The Act creates a temporary incentive for U.S. multinationals to repatriate accumulated income earned outside the U.S. at an effective tax rate of 5.25%. On December 21, 2004, the Financial Accounting Standards Board (FASB) issued FASB Staff Position, "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004" (FAS No. 109-2). FAS No. 109-2 allows companies additional time to evaluate the effect of the law on unrepatriated foreign earnings, and whether they continue to qualify for the exception in SFAS No. 109, "Accounting for Income Taxes," to recognizing deferred tax liabilities, and would require explanatory disclosures from those who need the additional time. Through July 2, 2005, we have not provided U.S. income taxes on approximately \$52.3 million of unremitted foreign earnings because such earnings were intended to be indefinitely reinvested outside the U.S. Whether we will ultimately utilize and benefit from the provisions of the Act depends on a number of factors, including the results of reviewing future Congressional guidance before a decision can be made. Until that time, we will make no change in our current intention to indefinitely reinvest accumulated earnings of our foreign subsidiaries, except in instances in which we can remit such earnings without a significant associated tax cost. We do not expect that this will have a material adverse effect on our current liquidity. Absent the repatriation incentive of the Act, we believe that any U.S. tax liability due upon remittance of such earnings would be immaterial due to the availability of U.S. foreign tax credits generated from such remittance. The related foreign tax withholding, which would be required if we remitted the foreign earnings to the U.S., would be approximately \$1.9 million.

In May 2004, our board of directors authorized the repurchase of up to \$30 million of our equity securities in the open market or in negotiated transactions through May 18, 2005. Prior to January 1, 2005, we had repurchased 460,400 shares of our common stock under this authorization for \$9.3 million. For the period from January 2, 2005 through May 18, 2005, we repurchased an additional 109,700 shares of our common stock under this authorization for \$2.1 million. On May 6, 2005, our board of directors authorized the repurchase of up to \$15 million of our equity securities in the open market or in negotiated transactions for the period from May 18, 2005 through May 18, 2006. As of July 2, 2005, we had repurchased 1,200 shares of our common stock under this new authorization for \$25 thousand.

Liquidity and Capital Resources (continued)

We completed our acquisition of Kadant Johnson on May 11, 2005 for \$101.5 million in cash, subject to a further post-closing adjustment as outlined in the purchase agreement for Kadant Johnson, and \$3.1 million in acquisition related costs. In addition to the cash consideration, we issued a letter of credit to the sellers for \$4 million, subject to adjustment, related to certain tax assets of Kadant Johnson, the value of which we expect to realize. We also agreed in the purchase agreement to an earn-out provision, based on the achievement of certain revenue targets between the closing date and July 1, 2006, which could increase the purchase price by up to \$8 million. To fund \$60 million of the purchase price, we entered into a term loan and revolving credit facility (the Credit Agreement) effective as of May 9, 2005 in the aggregate principal amount of up to \$85 million, including a \$25 million revolver. The Credit Agreement includes a \$60 million five-year term loan, which is repayable in equal quarterly installments over a five-year period. The aggregate principal to be repaid each year is as follows: \$4.5 million, \$9 million, \$10.5 million, \$13.5 million, \$15 million, and \$7.5 million in 2005, 2006, 2007, 2008, 2009, and 2010, respectively. Interest on the revolving loan and the term loan accrues and is payable quarterly in arrears at one of the following rates selected by us: (a) the prime rate plus an applicable margin initially set at 0% for 2005, and up to 0.25% thereafter or, (b) a eurocurrency rate plus an applicable margin initially set at 1% for 2005, and between 0.625% and 1.25% thereafter. The applicable margin is determined based upon our total debt to earnings before interest, taxes, depreciation and amortization (EBITDA) ratio.

The obligations for us under the Credit Agreement may be accelerated upon the occurrence of an event of default under the Credit Agreement, which include customary events of default including, without limitation, payment defaults, defaults in the performance of affirmative and negative covenants, the inaccuracy of representations or warranties, bankruptcy- and insolvency-related defaults, defaults relating to such matters as ERISA, uninsured judgments and the failure to pay certain indebtedness, and a change of control default.

In addition, the Credit Agreement contains negative covenants applicable to us and our subsidiaries, including financial covenants requiring us to comply with a maximum consolidated leverage ratio of either 2.5 or 3.0 and a minimum consolidated fixed charge coverage ratio of 1.5, and restrictions on liens, indebtedness, fundamental changes, dispositions of property, making certain restricted payments (including dividends and stock repurchases), investments, transactions with affiliates, sale and leaseback transactions, swap agreements, changing our fiscal year, negative pledges, arrangements affecting subsidiary distributions, and entering into new lines of business. As of July 2, 2005, we are in compliance with all the covenants in the Credit Agreement.

The loans under the Credit Agreement are guaranteed by certain of our domestic subsidiaries and secured by a pledge of 65% of the stock of our first-tier foreign subsidiaries and our subsidiary guarantors pursuant to a guarantee and pledge agreement effective as of May 9, 2005 in favor of JPMorgan Chase Bank, N.A., as agent on behalf of the lenders.

Although we currently have no material commitments for capital expenditures, we plan to make expenditures during the remainder of 2005 for property, plant, and equipment of approximately \$3.9 million, including \$1.2 million for our manufacturing and assembly facility in China to support our stock-preparation equipment business. This estimate excludes the capital expenditure requirement for Kadant Johnson, which will not have a significant effect on our liquidity in the second half of 2005.

Our future liquidity position will be primarily affected by the level of cash flows from operations and the amount of cash expended on debt repayments, capital projects, stock repurchases, or additional acquisitions, if any. We believe that our existing resources, together with the cash available from our credit facility and the cash we expect to generate from continuing operations, will be sufficient to meet the capital requirements of our operations for the foreseeable future.

Risk Factors

In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, we wish to caution readers that the following important factors, among others, in some cases have affected, and in the future could affect, our actual results and could cause our actual results in 2005 and beyond to differ materially from those expressed in any forward-looking statements made by us, or on our behalf.

Our business is dependent on the condition of the pulp and paper industry.

We sell products primarily to the pulp and paper industry, which is a cyclical industry. Generally, the financial condition of the global pulp and paper industry corresponds to the condition of the general economy, as well as to a number of other factors, including pulp and paper production capacity relative to demand. In recent years, the industry in certain geographic regions, notably North America, has been in a prolonged downcycle, resulting in depressed pulp and paper prices, decreased spending, mill closures, consolidations, and bankruptcies, all of which have adversely affected our business. As paper companies consolidate in response to market weakness, they frequently reduce capacity and postpone or even cancel capacity addition or expansion projects. These cyclical downturns can cause our sales to decline and adversely affect our profitability.

Our business is subject to economic, currency, political, and other risks associated with international sales and operations.

During the first six months of 2005 and 2004, approximately 62% and 61%, respectively, of our sales were to customers outside the United States, principally in Europe and Asia. International revenues are subject to a number of risks, including the following:

- agreements may be difficult to enforce and receivables difficult to collect through a foreign country's legal system;
- foreign customers may have longer payment cycles;
- foreign countries may impose additional withholding taxes or otherwise tax our foreign income, impose tariffs, or adopt other restrictions on foreign trade; and
- the protection of intellectual property in foreign countries may be more difficult to enforce.

Although we seek to charge our customers in the same currency in which our operating costs are incurred, fluctuations in currency exchange rates may affect product demand and adversely affect the profitability in U.S. dollars of products we provide in international markets where payment for our products and services is made in their local currencies. Any of these factors could have a material adverse impact on our business and results of operations.

A significant portion of our international sales has, and may in the future, come from China. An increase in revenues, as well as our planned operation of a manufacturing and assembly facility in China, will expose us to increased risk in the event of changes in the policies of the Chinese government, political unrest, unstable economic conditions, or other developments in China or in U.S.-China relations that are adverse to trade, including enactment of protectionist legislation or trade restrictions. Orders from customers in China, particularly for large systems that have been tailored to a customer's specific requirements, involve increased credit risk due to payment terms that are applicable to doing business in China. In addition, the timing of these orders is often difficult to predict.

Risk Factors (continued)

We are subject to intense competition in all our markets.

We believe that the principal competitive factors affecting the markets for our products include quality, price, service, technical expertise, and product innovation. Our competitors include a number of large multinational corporations that may have substantially greater financial, marketing, and other resources than we do. As a result, they may be able to adapt more quickly to new or emerging technologies and changes in customer requirements, or to devote greater resources to the promotion and sale of their services and products. Competitors' technologies may prove to be superior to ours. Our current products, those under development, and our ability to develop new technologies may not be sufficient to enable us to compete effectively. Competition, especially in China, could increase if new companies enter the market or if existing competitors expand their product lines or intensify efforts within existing product lines.

Our debt may adversely affect our cash flow and may restrict our investment opportunities.

On May 9, 2005, we entered into a Credit Agreement, consisting of a \$60 million five-year term loan and a \$25 million revolver. On May 11, 2005, we borrowed \$60 million to fund the acquisition of Kadant Johnson under the term loan. We may also obtain additional long-term debt and working capital lines of credit to meet future financing needs, which would have the effect of increasing our total leverage.

Our leverage could have negative consequences, including:

- increasing our vulnerability to adverse economic and industry conditions,
- limiting our ability to obtain additional financing,
- limiting our ability to pay dividends on or repurchase our capital stock,
- limiting our ability to acquire new products and technologies through acquisitions or licensing, and
- limiting our flexibility in planning for, or reacting to, changes in our business and the industries in which we compete.

Our indebtedness bears interest at floating rates pursuant to the terms of the Credit Agreement. As a result, our interest payment obligations on this indebtedness will increase if interest rates increase. To reduce the exposure to floating rates, we have converted \$36 million, or 60%, of our indebtedness to a fixed rate of interest through an interest rate swap.

Our ability to satisfy our obligations and to reduce our total debt depends on our future operating performance and on economic, financial, competitive, and other factors beyond our control. Our business may not generate sufficient cash flows to meet these obligations or to successfully execute our business strategy. If we are unable to service our debt and fund our business, we may be forced to reduce or delay capital expenditures or research and development expenditures, seek additional financing or equity capital, restructure or refinance our debt or sell assets. We may not be able to obtain additional financing or refinance existing debt or sell assets on terms acceptable to us or at all.

Risk Factors (continued)

Restrictions in our Credit Agreement may limit our activities.

Our Credit Agreement contains, and future debt instruments to which we may become subject may contain, restrictive covenants that limit our ability to engage in activities that could otherwise benefit us, including restrictions on our ability and the ability of our subsidiaries to:

- incur additional indebtedness,
- pay dividends on, redeem or repurchase our capital stock,
- make investments,
- create liens,
- sell assets,
- enter into transactions with affiliates, and
- consolidate, merge or transfer all or substantially all of our assets and the assets of our subsidiaries.

We are also required to meet specified financial ratios under the terms of our Credit Agreement. Our ability to comply with these financial restrictions and covenants is dependent on our future performance, which is subject to prevailing economic conditions and other factors, including factors that are beyond our control such as foreign exchange rates, interest rates, changes in technology, and changes in the level of competition.

Our failure to comply with any of these restrictions or covenants may result in an event of default under our Credit Agreement, which could permit acceleration of the debt under that instrument and require us to repay that debt before its scheduled due date.

If an event of default occurs, we may not have sufficient funds available to make the required payments under our indebtedness. If we are unable to repay amounts owed under our Credit Agreement, those lenders may be entitled to foreclose on and sell the collateral that secures our borrowings under that agreement.

Our inability to successfully integrate Kadant Johnson into our business could have a material adverse effect on our business.

On May 11, 2005, we acquired Kadant Johnson. Over the coming months, we will be working to integrate Kadant Johnson into our business. This integration will involve the merger of employees, products and services over multiple U.S. and international locations. We may not be successful in integrating this business into our current structure, or in obtaining the anticipated cost savings or synergies from the acquisition. To meet our quarterly certification requirements and in anticipation of incorporating Kadant Johnson into our 2006 Sarbanes-Oxley compliance process, we will also be performing a detailed review of Kadant Johnson's internal control structure to ensure that its controls over financial reporting are consistent with our policies and procedures. Given the multi-location structure of the Kadant Johnson business, this review will take significant time and effort, similar to our Sarbanes-Oxley compliance efforts in 2004, and will involve significant cost. We may identify control deficiencies during this process. Our ability to realize the value of the goodwill and other intangibles recorded for this acquisition will depend on the future cash flows of the Kadant Johnson business. If these future cash flows are below what we anticipated, we may incur future impairment losses associated with goodwill and intangibles, which could have a material adverse effect on our results of operations.

Risk Factors (continued)

Our inability to successfully identify and complete acquisitions or successfully integrate any new or previous acquisitions could have a material adverse effect on our business.

Our strategy includes the acquisition of technologies and businesses that complement or augment our existing products and services. Promising acquisitions are difficult to identify and complete for a number of reasons, including competition among prospective buyers and the need for regulatory, including antitrust, approvals. We do incur costs from time to time associated with potential acquisitions, which are deferred during the due diligence phase. Future operating results could be negatively impacted in any quarter in which we determine that a potential acquisition will not close and these associated costs are expensed. Any acquisition we may complete may be made at a substantial premium over the fair value of the net assets of the acquired company. We may not be able to complete future acquisitions, integrate any acquired businesses successfully into our existing businesses, make such businesses profitable, or realize anticipated cost savings or synergies, if any, from these acquisitions. In addition, we have previously acquired several companies and businesses. As a result of these acquisitions, we have recorded significant goodwill on our condensed consolidated balance sheet, and in conjunction with the adoption of SFAS No. 142, "Goodwill and Other Intangible Assets," in 2002, we recorded a transitional impairment charge upon the adoption of this standard. Any future impairment losses identified will be recorded as reductions to operating income, which could have a material adverse effect on our results of operations. Our ability to realize the value of the goodwill that we have recorded will depend on the future cash flows of these businesses. These cash flows depend, in part, on how well we have integrated these businesses.

Our inability to successfully complete the proposed restructuring of our Kadant Lamort subsidiary would have a negative effect on our future operating results.

In an effort to improve operating performance at our Kadant Lamort subsidiary in France, we approved a proposed restructuring of that subsidiary on November 18, 2004. This restructuring is intended to strengthen Kadant Lamort's competitive position in the European paper industry. Under French law, the proposed restructuring required consultation with Kadant Lamort's workers' council, which represents the employees, before implementation. The restructuring originally proposed the reduction of up to 136 full-time positions in France. Kadant Lamort experienced intermittent work stoppages by employees protesting the proposed restructuring while the consultations with the workers' council were in process. We recently completed the necessary consultations with the workers' council and expect the restructuring to be fully implemented by the fourth quarter of 2005. We expect that this subsidiary will continue to experience operating losses until these restructuring actions are completed. If we were unable to complete this restructuring, our future operating results would be negatively impacted.

We may not be successful in selling our composite building products business.

On October 27, 2004, our board of directors approved a plan to sell our composite building products business (the "composites business"). We cannot predict on what terms we may sell the business or if we will be successful in selling this business at all. There are certain liabilities associated with our composites business, such as warranty obligations, which we will likely not be able to transfer to a future buyer. If we are not able to transfer these liabilities with the sale, it could have a material adverse effect on our future results of operations. Under applicable accounting rules, the results of the composites business will be reported as a discontinued operation; however, we will continue to report these results in our consolidated financial statements. For as long as we continue to own the composite building products business, our consolidated performance will continue to be subject to the risks and uncertainties related to that business, including the risks identified in the following Risk Factors.

Risk Factors (continued)

Our performance in the market for composite building products will depend on our ability to manufacture and distribute our composite building products.

Development, formulation, manufacturing, and commercialization of our composite building products require significant testing and technical expertise and our efforts may not be successful. Growth of our composites business requires ongoing market acceptance. Our composites business is subject to intense competition, particularly in the decking market, from traditional wood products and other composite lumber manufacturers, many of whom have greater financial, technical, and marketing resources than we do. As a result, we may be unable to compete successfully in this market. We have limited experience manufacturing these products at volume, cost, and quality levels sufficient to satisfy expected demand, and we have in the past and may continue to encounter difficulties in connection with any large-scale manufacturing or commercialization of these products. Our capacity may not be sufficient to meet demand without significant additional investment. In addition, the majority of our production is dependent upon a single piece of equipment. If that equipment were to fail for an extended period of time, it would have a material adverse effect on our revenues from this business in that period. We rely on distributors in the building products industry to market, distribute, and sell our products. We may be unable to produce our products in sufficient quantity to interest or retain these distributors or to add new distributors. In addition, the announcement of our proposed sale of the composites business and warranty issues may impact our relationships with our existing and proposed new distributors and may cause them to reduce or curtail their purchases of our products. If we are unable to distribute our products effectively, our revenues will decline and we will have to incur additional expenses to market these products directly.

The failure of our composite building products to perform over long periods of time could result in potential liabilities.

Our composite building products are relatively new, have not been on the market for long periods of time, and may be used in applications about which we may have little knowledge or limited experience. Because we have limited historical experience, we may be unable to predict the potential liabilities related to product warranty or product liability issues. If our products fail to perform over their warranty periods, we may not have the ability to protect ourselves adequately against this potential liability, which could adversely affect our operating results. In 2003 and 2004, we experienced a significant increase in warranty claims and warranty expense related to our composite decking products including, but not limited to, contraction of certain deck boards and excessive oxidation that affects the integrity of the plastic used in some of our decking products. Included in the increased warranty expense was the cost of exchanging material held by our distributors with new material that, we believe, is not susceptible to this oxidation issue, and our best estimate of costs related to future potential valid claims arising from installed product. Although we increased the warranty provisions accordingly, we cannot guarantee that the reserves established will be sufficient if we incur warranty claims higher than anticipated. In addition, there can be no assurance that other problems will not develop. A continued high level of warranty claims or expenses and/or failure of our products to perform or to be accepted in the marketplace would have an adverse impact on the profitability of our business and our ability to sell the composites business on favorable terms.

Risk Factors (continued)

Economic conditions could adversely affect demand for our composite building products.

Demand for our composite building products is affected by several factors beyond our control, including economic conditions. Recent demand for our products has been driven, in part, by the availability of low-interest mortgage and home equity loans. A further increase in interest rates or tightened credit could adversely affect demand for home remodeling projects, including demand for our products.

Seasonality and weather conditions could adversely affect our business.

In general, the building products industry experiences seasonal fluctuations in sales, particularly in the fourth and first quarters, when holidays and adverse weather conditions in some regions usually reduce the level of home improvement and new construction activity. In addition, our composite building products are used or installed in outdoor construction applications, and our sales volume, bookings, gross margins, and operating income can be negatively affected by adverse weather. Operating results will tend to be lower in quarters with lower sales, which are not entirely offset by a corresponding reduction in operating costs. In addition, we may also experience lower gross profit margins in the fourth and first quarters due to seasonal incentive discounts offered to our distributors. As a result of these factors, we believe sequential period-to-period comparisons of our operating results are not reliable indicators of future performance, and the operating results for any one quarterly period may not be indicative of operating results to be expected for a full year.

We are dependent on a single mill for the raw material used in our fiber-based granules, and we may not be able to obtain raw material on commercially reasonable terms. In addition, the manufacture of our composite building products and fiber-based granules is subject to commodity price risks.

We are dependent on a single paper mill for the fiber used in the manufacture of our fiber-based granules and composite building products. This mill has the exclusive right to supply the papermaking byproducts used in the manufacturing process. Although we believe our relationship with the mill is good, the mill could decide not to renew its contract with us at the end of 2005, or may not agree to renew on commercially reasonable terms. If this were to occur, we would be forced to find an alternative supply for this raw material. We may be unable to find an alternative supply on commercially reasonable terms or could incur excessive transportation costs if an alternative supplier were found, which would increase our manufacturing costs and might prevent prices for our products from being competitive.

In addition, we use natural gas in the production of our fiber-based granular products. We seek to manage our exposure to natural gas price fluctuations by entering into short-term forward contracts to purchase specified quantities of natural gas from a supplier. We may not be able to effectively manage our exposure to natural gas price fluctuations.

Our composite building products also contain plastics, which are subject to wide fluctuations in pricing and availability. Higher energy costs can increase the price of plastic significantly and rapidly. We may be unable to obtain sufficient quantities at reasonable prices, which would adversely affect our profitability and ability to produce a sufficient quantity of our products or to produce our products at competitive prices.

Our inability to protect our intellectual property could have a material adverse effect on our business. In addition, third parties may claim that we infringe their intellectual property, and we could suffer significant litigation or licensing expense as a result.

We place considerable emphasis on obtaining patent and trade secret protection for significant new technologies, products, and processes because of the length of time and expense associated with bringing new products through the development process and into the marketplace. Our success depends in part on our ability to develop patentable products and obtain and enforce patent protection for our products both in the United States and in other countries. We

Risk Factors (continued)

own numerous U.S. and foreign patents, and we intend to file additional applications, as appropriate, for patents covering our products. Patents may not be issued for any pending or future patent applications owned by or licensed to us, and the claims allowed under any issued patents may not be sufficiently broad to protect our technology. Any issued patents owned by or licensed to us may be challenged, invalidated, or circumvented, and the rights under these patents may not provide us with competitive advantages. A patent relating to our fiber-based granular products expired in the second quarter of 2004. As a result, we could be subject to increased competition in this market, which could have an adverse effect on this business. In addition, competitors may design around our technology or develop competing technologies. Intellectual property rights may also be unavailable or limited in some foreign countries, which could make it easier for competitors to capture increased market position. We could incur substantial costs to defend ourselves in suits brought against us or in suits in which we may assert our patent rights against others. An unfavorable outcome of any such litigation could have a material adverse effect on our business and results of operations. In addition, as our patents expire, we rely on trade secrets and proprietary know-how to protect our products. We cannot be sure the steps we have taken or will take in the future will be adequate to deter misappropriation of our proprietary information and intellectual property.

We seek to protect trade secrets and proprietary know-how, in part, through confidentiality agreements with our collaborators, employees, and consultants. These agreements may be breached, we may not have adequate remedies for any breach, and our trade secrets may otherwise become known or be independently developed by our competitors.

Third parties may assert claims against us to the effect that we are infringing on their intellectual property rights. We could incur substantial costs and diversion of management resources in defending these claims, which could have a material adverse effect on our business, financial condition, and results of operations. In addition, parties making these claims could secure a judgment awarding substantial damages, as well as injunctive or other equitable relief, which could effectively block our ability to make, use, sell, distribute, or market our products and services in the United States or abroad. In the event that a claim relating to intellectual property is asserted against us, or third parties not affiliated with us hold pending or issued patents that relate to our products or technology, we may seek licenses to such intellectual property or challenge those patents. However, we may be unable to obtain these licenses on commercially reasonable terms, if at all, and our challenge of the patents may be unsuccessful. Our failure to obtain the necessary licenses or other rights could prohibit the sale, manufacture, or distribution of our products and, therefore, could have a material adverse effect on our business, financial condition, and results of operations.

Fluctuations in our quarterly operating results may cause our stock price to decline.

Given the nature of the markets in which we participate and the effect of Staff Accounting Bulletin (SAB) No. 104, "Revenue Recognition," we may not be able to reliably predict future revenues and profitability, and unexpected changes may cause us to adjust our operations. A large proportion of our costs are fixed, due in part to our significant selling, research and development, and manufacturing costs. Thus, small declines in revenues could disproportionately affect our operating results. Other factors that could affect our quarterly operating results include:

- failure of our products to pass contractually agreed upon acceptance tests, which would delay or prohibit recognition of revenues under SAB No. 104;
- adverse changes in demand for and market acceptance of our products;
- competitive pressures resulting in lower sales prices of our products;
- adverse changes in the pulp and paper industry;
- delays or problems in our introduction of new products;
- our competitors' announcements of new products, services, or technological innovations;
- contractual liabilities incurred by us related to guarantees of our product performance;
- increased costs of raw materials or supplies, including the cost of energy; and
- changes in the timing of product orders.

Risk Factors (continued)

Anti-takeover provisions in our charter documents, under Delaware law, and in our shareholder rights plan could prevent or delay transactions that our shareholders may favor.

Provisions of our charter and bylaws may discourage, delay, or prevent a merger or acquisition that our shareholders may consider favorable, including transactions in which shareholders might otherwise receive a premium for their shares. For example, these provisions:

- authorize the issuance of "blank check" preferred stock without any need for action by shareholders;
- provide for a classified board of directors with staggered three-year terms;
- require supermajority shareholder voting to effect various amendments to our charter and bylaws;
- eliminate the ability of our shareholders to call special meetings of shareholders;
- prohibit shareholder action by written consent; and
- establish advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted on by shareholders at shareholder meetings.

In addition, our board of directors has adopted a shareholder rights plan intended to protect shareholders in the event of an unfair or coercive offer to acquire our company and to provide our board of directors with adequate time to evaluate unsolicited offers. Preferred stock purchase rights have been distributed to our common shareholders pursuant to the rights plan. This rights plan may have anti-takeover effects. The rights plan will cause substantial dilution to a person or group that attempts to acquire us on terms that our board of directors does not believe are in our best interests and those of our shareholders and may discourage, delay, or prevent a merger or acquisition that shareholders may consider favorable, including transactions in which shareholders might otherwise receive a premium for their shares.

Item 3 - Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk from changes in interest rates and foreign currency exchange rates, which could affect our results of operations and financial condition.

We borrowed \$60 million in May 2005 to fund a portion of the Kadant Johnson acquisition. Through an interest rate swap \$36 million, or 60%, of the borrowing has been converted to a fixed rate of interest. The remaining portion of the borrowing bears a variable rate of interest based on LIBOR. A 100-basis-point increase in LIBOR rates at July 2, 2005, would increase our annual pre-tax interest expense by \$0.2 million.

Except as described above, our exposure to market risk from interest rates and foreign currency exchange rates has not changed materially from our exposure at year-end 2004.

Item 4 - Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

In May 2005 we acquired Kadant Johnson, a private company with internal control procedures that had not been designed for public company reporting. Prior to our acquisition, Kadant Johnson's independent certified public accountants identified material weaknesses in Kadant Johnson's controls over the inventory reserve calculation and financial close procedures. Kadant Johnson adjusted their inventory obsolescence reserve before the acquisition date by restating prior periods to increase their reserve in compliance with our policy and generally accepted accounting principles. In addition, we added internal control procedures to ensure that Kadant Johnson's disclosure controls, as they relate to Kadant's consolidated financial reporting, were adequate and in compliance with our policies and procedures. As a result, we made a number of changes to internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) during the second quarter of 2005 including:

- reviewing and strengthening Kadant Johnson's tax accounting process,
- reviewing and strengthening Kadant Johnson's intercompany reconciliation process,
- enhancing the documentation relating to Kadant Johnson's reserve calculations for accounts receivable and warranty to comply with its policies, and
- accelerating and improving Kadant Johnson's financial close procedures.

We are continuing the process of evaluating Kadant Johnson's internal controls and, as of the date of this quarterly report, have not yet completed our evaluation. We do not anticipate that our evaluation of the internal controls of Kadant Johnson will be complete by December 31, 2005 and, as permitted, we will be excluding this acquisition from our reporting under Section 404 of the Sarbanes-Oxley Act of 2002 at December 31, 2005.

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of July 2, 2005. The term "disclosure controls and procedures," as defined in Securities Exchange Act Rules 13a-15(e) and 15d-15(e), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports that it files or submits under the Securities Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives, and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based upon the evaluation of our disclosure controls and procedures as of July 2, 2005, our Chief Executive Officer and Chief Financial Officer concluded that as of July 2, 2005, our disclosure controls and procedures were effective at the reasonable assurance level.

(b) Changes in Internal Control Over Financial Reporting

Other than the changes resulting from our acquisition of Kadant Johnson outlined above, there have not been any changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) during the fiscal quarter ended July 2, 2005 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides information about purchases by us of our common stock during the three months ended July 2, 2005:

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans
4/3/05 - 4/30/05	-	-	-	\$ 20,650,526
5/1/05 - 5/31/05	110,900	\$18.80	110,900	\$ 14,975,285
6/1/05 - 7/2/05	-	-	-	\$ 14,975,285
Total:	-	-	-	-

(1) On May 6, 2005, our board of directors authorized the repurchase of up to \$15 million of our equity securities in the open market or in negotiated transactions for the period from May 18, 2005 through May 18, 2006. As of July 2, 2005, we had repurchased 1,200 shares of our common stock for \$25 thousand under this authorization. In addition, in May 2005 we repurchased 109,700 shares of common stock for \$2.1 million under a previous authorization, which expired on May 18, 2005.

Item 4 - Submission of Matters to a Vote of Security Holders

On June 7, 2005, at the annual meeting of shareholders, the shareholders elected two directors, John M. Albertine and Thomas C. Leonard, to the class of directors whose three-year term expires at Kadant's annual meeting of shareholders in 2008. Mr. Albertine received 11,193,179 shares voted in favor of his election and 211,878 shares voted against. Mr. Leonard received 11,299,774 shares voted in favor of his election and 105,283 shares voted against.

Item 6 - Exhibits

See Exhibit Index on the page immediately preceding exhibits.

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KADANT INC.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized as of the 11th day of August, 2005.

KADANT INC.

/s/ Thomas M. O'Brien

Thomas M. O'Brien
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

KADANT INC.
EXHIBIT INDEX

Exhibit Number	Description of Exhibit

10.1	International Swap Dealers Association, Inc. Master Agreement dated May 25, 2005 between Kadant Inc. and Citizens Bank of Massachusetts and Swap Confirmation dated May 18, 2005.
31.1	Certification of the Principal Executive Officer of the Registrant Pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of the Principal Financial Officer of the Registrant Pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended.
32	Certification of the Chief Executive Officer and the Chief Financial Officer of the Registrant Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

ISDA(R)

International Swap Dealers Association, Inc.

MASTER AGREEMENT

dated as of

.....and.....

have entered and/or anticipate entering into one or more transactions (each a "Transaction") that are or will be governed by this Master Agreement, which includes the schedule (the "Schedule"), and the documents and other confirming evidence (each a "Confirmation") exchanged between the parties confirming those Transactions.

Accordingly, the parties agree as follows: -

1. Interpretation

(a) Definitions. The terms defined in Section 14 and in the Schedule will have the meanings therein specified for the purpose of this Master Agreement.

(b) Inconsistency. In the event of any inconsistency between the provisions of the Schedule and the other provisions of this Master Agreement, the Schedule will prevail. In the event of any inconsistency between the provisions of any Confirmation and this Master Agreement (including the Schedule), such Confirmation will prevail for the purpose of the relevant Transaction.

(c) Single Agreement. All Transactions are entered into in reliance on the fact that this Master Agreement and all Confirmations form a single agreement between the parties (collectively referred to as this "Agreement"), and the parties would not otherwise enter into any Transactions.

2. Obligations

(a) General Conditions.

(i) Each party will make each payment or delivery specified in each Confirmation to be made by it, subject to the other provisions of this Agreement.

(ii) Payments under this Agreement will be made on the due date for value on that date in the place of the account specified in the relevant Confirmation or otherwise pursuant to this Agreement, in freely transferable funds and in the manner customary for payments in the required currency. Where settlement is by delivery (that is, other than by payment), such delivery will be made for receipt on the due date in the manner customary for the relevant obligation unless otherwise specified in the relevant Confirmation or elsewhere in this Agreement.

(iii) Each obligation of each party under Section 2(a)(i) is subject to (1) the condition precedent that no Event of Default or Potential Event of Default with respect to the other party has occurred and is continuing, (2) the condition precedent that no Early Termination Date in respect of the relevant Transaction has occurred or been effectively designated and (3) each other applicable condition precedent specified in this Agreement.

(b) Change of Account. Either party may change its account for receiving a payment or delivery by giving notice to the other party at least five Local Business Days prior to the scheduled date for the payment or delivery to which such change applies unless such other party gives timely notice of a reasonable objection to such change.

(c) Netting. If on any date amounts would otherwise be payable:-

(i) in the same currency; and

(ii) in respect of the same Transaction,

by each party to the other, then, on such date, each party's obligation to make payment of any such amount will be automatically satisfied and discharged and, if the aggregate amount that would otherwise have been payable by one party exceeds the aggregate amount that would otherwise have been payable by the other party, replaced by an obligation upon the party by whom the larger aggregate amount would have been payable to pay to the other party the excess of the larger aggregate amount over the smaller aggregate amount.

The parties may elect in respect of two or more Transactions that a net amount will be determined in respect of all amounts payable on the same date in the same currency in respect of such Transactions, regardless of whether such amounts are payable in respect of the same Transaction. The election may be made in the Schedule or a Confirmation by specifying that subparagraph (ii) above will not apply to the Transactions identified as being subject to the election, together with the starting date (in which case subparagraph (ii) above will not, or will cease to, apply to such Transactions from such date). This election may

be made separately for different groups of Transactions and will apply separately to each pairing of Offices through which the parties make and receive payments or deliveries.

(d) Deduction or Withholding for Tax.

(i) Gross-Up. All payments under this Agreement will be made without any deduction or withholding for or on account of any Tax unless such deduction or withholding is required by any applicable law, as modified by the practice of any relevant governmental revenue authority, then in effect. If a party is so required to deduct or withhold, then that party ("X") will:-

(1) promptly notify the other party ("Y") of such requirement;

(2) pay to the relevant authorities the full amount required to be deducted or withheld (including the full amount required to be deducted or withheld from any additional amount paid by X to Y under this Section 2(d)) promptly upon the earlier of determining that such deduction or withholding is required or receiving notice that such amount has been assessed against Y;

(3) promptly forward to Y an official receipt (or a certified copy), or other documentation reasonably acceptable to Y, evidencing such payment to such authorities; and

(4) if such Tax is an Indemnifiable Tax, pay to Y, in addition to the payment to which Y is otherwise entitled under this Agreement, such additional amount as is necessary to ensure that the net amount actually received by Y (free and clear of Indemnifiable Taxes, whether assessed against X or Y) will equal the full amount Y would have received had no such deduction or withholding been required. However, X will not be required to pay any additional amount to Y to the extent that it would not be required to be paid but for:-

(A) the failure by Y to comply with or perform any agreement contained in Section 4(a)(i), 4(a)(iii) or 4(d); or

(B) the failure of a representation made by Y pursuant to Section 3(f) to be accurate and true unless such failure would not have occurred but for (I) any action taken by a

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taxing authority, or brought in a court of competent jurisdiction, on or after the date on which a Transaction is entered into (regardless of whether such action is taken or brought with respect to a party to this Agreement) or (II) a Change in Tax Law.

(ii) Liability. If:-

(1) X is required by any applicable law, as modified by the practice of any relevant governmental revenue authority, to make any deduction or withholding in respect of which X would not be required to pay an additional amount to Y under Section 2(d)(i)(4);

(2) X does not so deduct or withhold; and

(3) a liability resulting from such Tax is assessed directly against X,

then, except to the extent Y has satisfied or then satisfies the liability resulting from such Tax, Y will promptly pay to X the amount of such liability (including any related liability for interest, but including any related liability for penalties only if Y has failed to comply with or perform any agreement contained in Section 4(a)(i), 4(a)(iii) or 4(d)).

(e) Default Interest; Other Amounts. Prior to the occurrence or effective designation of an Early Termination Date in respect of the relevant Transaction, a party that defaults in the performance of any payment obligation will, to the extent permitted by law and subject to Section 6(c), be required to pay interest (before as well as after judgment) on the overdue amount to the other party on demand in the same currency as such overdue amount, for the period from (and including) the original due date for payment to (but excluding) the date of actual payment, at the Default Rate. Such interest will be calculated on the basis of daily compounding and the actual number of days elapsed. If, prior to the occurrence or effective designation of an Early Termination Date in respect of the relevant Transaction, a party defaults in the performance of any obligation required to be settled by delivery, it will compensate the other party on demand if and to the extent provided for in the relevant Confirmation or elsewhere in this Agreement.

3. Representations

Each party represents to the other party (which representations will be deemed to be repeated by each party on each date on which a Transaction is entered into and, in the case of the representations in Section 3(f), at all times until the termination of this Agreement) that:-

(a) Basic Representations.

(i) Status. It is duly organised and validly existing under the laws of the jurisdiction of its organisation or incorporation and, if relevant under such laws, in good standing;

(ii) Powers. It has the power to execute this Agreement and any other documentation relating to this Agreement to which it is a party, to deliver this Agreement and any other documentation relating to this Agreement that it is required by this Agreement to deliver and to perform its obligations under this Agreement and any obligations it has under any Credit Support Document to which it is a party and has taken all necessary action to authorise such execution, delivery and performance;

(iii) No Violation or Conflict. Such execution, delivery and performance do not violate or conflict with any law applicable to it, any provision of its constitutional documents, any order or judgment of any court or other agency of government applicable to it or any of its assets or any contractual restriction binding on or affecting it or any of its assets;

(iv) Consents. All governmental and other consents that are required to have been obtained by it with respect to this Agreement or any Credit Support Document to which it is a party have been obtained and are in full force and effect and all conditions of any such consents have been complied with; and

(v) Obligations Binding. Its obligations under this Agreement and any Credit Support

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Document to which it is a party constitute its legal, valid and binding obligations, enforceable in accordance with their respective terms (subject to applicable bankruptcy, reorganisation, insolvency, moratorium or similar laws affecting creditors' rights generally and subject, as to enforceability, to equitable principles of general application (regardless of whether enforcement is sought in a proceeding in equity or at law)).

(b) Absence of Certain Events. No Event of Default or Potential Event of Default or, to its knowledge, Termination Event with respect to it has occurred and is continuing and no such event or circumstance would occur as a result of its entering into or performing its obligations under this Agreement or any Credit Support Document to which it is a party.

(c) Absence of Litigation. There is not pending or, to its knowledge, threatened against it or any of its Affiliates any action, suit or proceeding at law or in equity or before any court, tribunal, governmental body, agency or official or any arbitrator that is likely to affect the legality, validity or enforceability against it of this Agreement or any Credit Support Document to which it is a party or its ability to perform its obligations under this Agreement or such Credit Support Document.

(d) Accuracy of Specified Information. All applicable information that is furnished in writing by or on behalf of it to the other party and is identified for the purpose of this Section 3(d) in the Schedule is, as of the date of the information, true, accurate and complete in every material respect.

(e) Payer Tax Representation. Each representation specified in the Schedule as being made by it for the purpose of this Section 3(e) is accurate and true.

(f) Payee Tax Representations. Each representation specified in the Schedule as being made by it for the purpose of this Section 3(f) is accurate and true.

4. Agreements

Each party agrees with the other that, so long as either party has or may have any obligation under this Agreement or under any Credit Support Document to which it is a party:-

(a) Furnish Specified Information. It will deliver to the other party or, in certain cases under subparagraph (iii) below, to such government or taxing authority as the other party reasonably directs:-

(i) any forms, documents or certificates relating to taxation specified in the Schedule or any Confirmation;

(ii) any other documents specified in the Schedule or any confirmation; and

(iii) upon reasonable demand by such other party, any form or document that may be required or reasonably requested in writing in order to allow such other party or its Credit Support Provider to make a payment under this Agreement or any applicable Credit Support Document without any deduction or withholding for or on account of any Tax or with such deduction or withholding at a reduced rate (so long as the completion, execution or submission of such form or document would not materially prejudice the legal or commercial position of the party in receipt of such demand), with any such form or document to be accurate and completed in a manner reasonably satisfactory to such other party and to be executed and to be delivered with any reasonably required certification,

in each case by the date specified in the Schedule or such Confirmation or, if none is specified, as soon as reasonably practicable.

(b) Maintain Authorisations. It will use all reasonable efforts to maintain in full force and effect all consents of any governmental or other authority that are required to be obtained by it with respect to this Agreement or any Credit Support Document to which it is a party and will use all reasonable efforts to obtain any that may become necessary in the future.

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(c) Comply with Laws. It will comply in all material respects with all applicable laws and orders to which it may be subject if failure so to comply would materially impair its ability to perform its obligations under this Agreement or any Credit Support Document to which it is a party.

(d) Tax Agreement. It will give notice of any failure of a representation made by it under Section 3(f) to be accurate and true promptly upon learning of such failure.

(e) Payment of Stamp Tax. Subject to Section 11, it will pay any Stamp Tax levied or imposed upon it or in respect of its execution or performance of this Agreement by a jurisdiction in which it is incorporated, organised, managed and controlled, or considered to have its seat, or in which a branch or office through which it is acting for the purpose of this Agreement is located ("Stamp Tax Jurisdiction") and will indemnify the other party against any Stamp Tax levied or imposed upon the other party or in respect of the other party's execution or performance of this Agreement by any such Stamp Tax Jurisdiction which is not also a Stamp Tax Jurisdiction with respect to the other party.

5. Events of Default and Termination Events

(a) Events of Default. The occurrence at any time with respect to a party or, if applicable, any Credit Support Provider of such party or any Specified Entity of such party of any of the following events constitutes an event of default (an "Event of Default") with respect to such party:-

(i) Failure to Pay or Deliver. Failure by the party to make, when due, any payment under this Agreement or delivery under Section 2(a)(i) or 2(e) required to be made by it if such failure is not remedied on or before the third Local Business Day after notice of such failure is given to the party;

(ii) Breach of Agreement. Failure by the party to comply with or perform any agreement or obligation (other than an obligation to make any payment under this Agreement or delivery under Section 2(a)(i) or 2(e) or to give notice of a Termination Event or any agreement or obligation under Section 4(a)(i), 4(a)(iii) or 4(d)) to be complied with or performed by the party in accordance with this Agreement if such failure is not remedied on or before the thirtieth day after notice of such failure is given to the party;

(iii) Credit Support Default.

(1) Failure by the party or any Credit Support Provider of such party to comply with or perform any agreement or obligation to be complied with or performed by it in accordance with any Credit Support Document if such failure is continuing after any applicable grace period has elapsed;

(2) the expiration or termination of such Credit Support Document or the failing or ceasing of such Credit Support Document to be in full force and effect for the purpose of this Agreement (in either case other than in accordance with its terms) prior to the satisfaction of all obligations of such party under each Transaction to which such Credit Support Document relates without the written consent of the other party; or

(3) the party or such Credit Support Provider disaffirms, disclaims, repudiates or rejects, in whole or in part, or challenges the validity of, such Credit Support Document;

(iv) Misrepresentation. A representation (other than a representation under Section 3(e) or (f)) made or repeated or deemed to have been made or repeated by the party or any Credit Support Provider of such party in this Agreement or any Credit Support Document proves to have been incorrect or misleading in any material respect when made or repeated or deemed to have been made or repeated;

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(v) Default under Specified Transaction. The party, any Credit Support Provider of such party or any applicable Specified Entity of such party (1) defaults under a Specified Transaction and, after giving effect to any applicable notice requirement or grace period, there occurs a liquidation of, an acceleration of obligations under, or an early termination of, that Specified Transaction, (2) defaults, after giving effect to any applicable notice requirement or grace period, in making any payment or delivery due on the last payment, delivery or exchange date of, or any payment on early termination of, a Specified Transaction (or such default continues for at least three Local Business Days if there is no applicable notice requirement or grace period) or (3) disaffirms, disclaims, repudiates or rejects, in whole or in part, a Specified Transaction (or such action is taken by any person or entity appointed or empowered to operate it or act on its behalf);

(vi) Cross Default. If "Cross Default" is specified in the Schedule as applying to the party, the occurrence or existence of (1) a default, event of default or other similar condition or event (however described) in respect of such party, any Credit Support Provider of such party or any applicable Specified Entity of such party under one or more agreements or instruments relating to Specified Indebtedness of any of them (individually or collectively) in an aggregate amount of not less than the applicable Threshold Amount (as specified in the Schedule) which has resulted in such Specified Indebtedness becoming, or becoming capable at such time of being declared, due and payable under such agreements or instruments, before it would otherwise have been due and payable or (2) a default by such party, such Credit Support Provider or such Specified Entity (individually or collectively) in making one or more payments on the due date thereof in an aggregate amount of not less than the applicable Threshold Amount under such agreements or instruments (after giving effect to any applicable notice requirement or grace period);

(vii) Bankruptcy. The party, any Credit Support Provider of such party or any applicable Specified Entity of such party:-

(1) is dissolved (other than pursuant to a consolidation, amalgamation or merger); (2) becomes insolvent or is unable to pay its debts or fails or admits in writing its inability generally to pay its debts as they become due; (3) makes a general assignment, arrangement or composition with or for the benefit of its creditors; (4) institutes or has instituted against it a proceeding seeking a judgment of insolvency or bankruptcy or any other relief under any bankruptcy or insolvency law or other similar law affecting creditors' rights, or a petition is presented for its winding-up or liquidation, and, in the case of any such proceeding or petition instituted or presented against it, such proceeding or petition (A) results in a judgment of insolvency or bankruptcy or the entry of an order for relief or the making of an order for its winding-up or liquidation or (B) is not dismissed, discharged, stayed or restrained in each case within 30 days of the institution or presentation thereof; (5) has a resolution passed for its winding-up, official management or liquidation (other than pursuant to a consolidation, amalgamation or merger); (6) seeks or becomes subject to the appointment of an administrator, provisional liquidator, conservator, receiver, trustee, custodian or other similar official for it or for all or substantially all its assets; (7) has a secured party take possession of all or substantially all its assets or has a distress, execution, attachment, sequestration or other legal process levied, enforced or sued on or against all or substantially all its assets and such secured party maintains possession, or any such process is not dismissed, discharged, stayed or restrained, in each case within 30 days thereafter; (8) causes or is subject to any event with respect to it which, under the applicable laws of any jurisdiction, has an analogous effect to any of the events specified in clauses (1) to (7) (inclusive); or (9) takes any action in furtherance of, or indicating its consent to, approval of, or acquiescence in, any of the foregoing acts; or

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(viii) Merger Without Assumption. The party or any Credit Support Provider of such party consolidates or amalgamates with, or merges with or into, or transfers all or substantially all its assets to, another entity and, at the time of such consolidation, amalgamation, merger or transfer:

(1) the resulting, surviving or transferee entity fails to assume all the obligations of such party or such Credit Support Provider under this Agreement or any Credit Support Document to which it or its predecessor was a party by operation of law or pursuant to an agreement reasonably satisfactory to the other party to this Agreement; or

(2) the benefits of any Credit Support Document fail to extend (without the consent of the other party) to the performance by such resulting, surviving or transferee entity of its obligations under this Agreement.

(b) Termination Events. The occurrence at any time with respect to a party or, if applicable, any Credit Support Provider of such party or any Specified Entity of such party of any event specified below constitutes an Illegality if the event is specified in (i) below, a Tax Event if the event is specified in (ii) below or a Tax Event Upon Merger if the event is specified in (iii) below, and, if specified to be applicable, a Credit Event Upon Merger if the event is specified pursuant to (iv) below or an Additional Termination Event if the event is specified pursuant to (v) below:-

(i) Illegality. Due to the adoption of, or any change in, any applicable law after the date on which a Transaction is entered into, or due to the promulgation of, or any change in, the interpretation by any court, tribunal or regulatory authority with competent jurisdiction of any applicable law after such date, it becomes unlawful (other than as a result of a breach by the party of Section 4(b)) for such party (which will be the Affected Party):-

(1) to perform any absolute or contingent obligation to make a payment or delivery or to receive a payment or delivery in respect of such Transaction or to comply with any other material provision of this Agreement relating to such Transaction; or

(2) to perform, or for any Credit Support Provider of such party to perform, any contingent or other obligation which the party (or such Credit Support Provider) has under any Credit Support Document relating to such Transaction;

(ii) Tax Event. Due to (x) any action taken by a taxing authority, or brought in a court of competent jurisdiction, on or after the date on which a Transaction is entered into (regardless of whether such action is taken or brought with respect to a party to this Agreement) or (y) a Change in Tax Law, the party (which will be the Affected Party) will, or there is a substantial likelihood that it will, on the next succeeding Scheduled Payment Date (1) be required to pay to the other party an additional amount in respect of an Indemnifiable Tax under Section 2(d)(i)(4) (except in respect of interest under Section 2(e), 6(d)(ii) or 6(e)) or (2) receive a payment from which an amount is required to be deducted or withheld for or on account of a Tax (except in respect of interest under Section 2(e), 6(d)(ii) or 6(e)) and no additional amount is required to be paid in respect of such Tax under Section 2(d)(i)(4) (other than by reason of Section 2(d)(i)(4)(A) or (B));

(iii) Tax Event Upon Merger. The party (the "Burdened Party") on the next succeeding Scheduled Payment Date will either (1) be required to pay an additional amount in respect of an Indemnifiable Tax under Section 2(d)(i)(4) (except in respect of interest under Section 2(e), 6(d)(ii) or 6(e)) or (2) receive a payment from which an amount has been deducted or withheld for or on account of any Indemnifiable Tax in respect of which the other party is not required to pay an additional amount (other than by reason of Section 2(d)(i)(4)(A) or (B)), in either case as a result of a party consolidating or amalgamating with, or merging with or into, or transferring all or substantially all its assets to, another entity (which will be the Affected Party) where such action does not constitute an event described in Section 5(a)(viii);

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(iv) Credit Event Upon Merger. If "Credit Event Upon Merger" is specified in the Schedule as applying to the party, such party ("X"), any Credit Support Provider of X or any applicable Specified Entity of X consolidates or amalgamates with, or merges with or into, or transfers all or substantially all its assets to, another entity and such action does not constitute an event described in Section 5(a)(viii) but the creditworthiness of the resulting, surviving or transferee entity is materially weaker than that of X, such Credit Support Provider or such Specified Entity, as the case may be, immediately prior to such action (and, in such event, X or its successor or transferee, as appropriate, will be the Affected Party); or

(v) Additional Termination Event. If any "Additional Termination Event" is specified in the Schedule or any Confirmation as applying, the occurrence of such event (and, in such event, the Affected Party or Affected Parties shall be as specified for such Additional Termination Event in the Schedule or such Confirmation).

(c) Event of Default and Illegality. If an event or circumstance which would otherwise constitute or give rise to an Event of Default also constitutes an Illegality, it will be treated as an Illegality and will not constitute an Event of Default.

6. Early Termination

(a) Right to Terminate Following Event of Default. If at any time an Event of Default with respect to a party (the "Defaulting Party") has occurred and is then continuing, the other party (the "Non-defaulting Party") may, by not more than 20 days notice to the Defaulting Party specifying the relevant Event of Default, designate a day not earlier than the day such notice is effective as an Early Termination Date in respect of all outstanding Transactions. If, however, "Automatic Early Termination" is specified in the Schedule as applying to a party, then an Early Termination Date in respect of all outstanding Transactions will occur immediately upon the occurrence with respect to such party of an Event of Default specified in Section 5(a)(vii)(1), (3), (5), (6) or, to the extent analogous thereto, (8), and as of the time immediately preceding the institution of the relevant proceeding or the presentation of the relevant petition upon the occurrence with respect to such party of an Event of Default specified in Section 5(a)(vii)(4) or, to the extent analogous thereto, (8).

(b) Right to Terminate Following Termination Event.

(i) Notice. If a Termination Event occurs, an Affected Party will, promptly upon becoming aware of it, notify the other party, specifying the nature of that Termination Event and each Affected Transaction and will also give such other information about that Termination Event as the other party may reasonably require.

(ii) Transfer to Avoid Termination Event. If either an Illegality under Section 5(b)(i)(1) or a Tax Event occurs and there is only one Affected Party, or if a Tax Event Upon Merger occurs and the Burdened Party is the Affected Party, the Affected Party will, as a condition to its right to designate an Early Termination Date under Section 6(b)(iv), use all reasonable efforts (which will not require such party to incur a loss, excluding immaterial, incidental expenses) to transfer within 20 days after it gives notice under Section 6(b)(i) all its rights and obligations under this Agreement in respect of the Affected Transactions to another of its Offices or Affiliates so that such Termination Event ceases to exist.

If the Affected Party is not able to make such a transfer it will give notice to the other party to that effect within such 20 day period, whereupon the other party may effect such a transfer within 30 days after the notice is given under Section 6(b)(i).

Any such transfer by a party under this Section 6(b)(ii) will be subject to and conditional upon the prior written consent of the other party, which consent will not be withheld if such other party's policies in effect at such time would permit it to enter into transactions with the transferee on the terms proposed.

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(iii) Two Affected Parties. If an Illegality under Section 5(b)(i)(1) or a Tax Event occurs and there are two Affected Parties, each party will use all reasonable efforts to reach agreement within 30 days after notice thereof is given under Section 6(b)(i) on action to avoid that Termination Event.

(iv) Right to Terminate. If:-

(1) a transfer under Section 6(b)(ii) or an agreement under Section 6(b)(iii), as the case may be, has not been effected with respect to all Affected Transactions within 30 days after an Affected Party gives notice under Section 6(b)(i); or

(2) an Illegality under Section 5(b)(i)(2), a Credit Event Upon Merger or an Additional Termination Event occurs, or a Tax Event Upon Merger occurs and the Burdened Party is not the Affected Party,

either party in the case of an Illegality, the Burdened Party in the case of a Tax Event Upon Merger, any Affected Party in the case of a Tax Event or an Additional Termination Event if there is more than one Affected Party, or the party which is not the Affected Party in the case of a Credit Event Upon Merger or an Additional Termination Event if there is only one Affected Party may, by not more than 20 days notice to the other party and provided that the relevant Termination Event is then continuing, designate a day not earlier than the day such notice is effective as an Early Termination Date in respect of all Affected Transactions.

(c) Effect of Designation.

(i) If notice designating an Early Termination Date is given under Section 6(a) or (b), the Early Termination Date will occur on the date so designated, whether or not the relevant Event of Default or Termination Event is then continuing.

(ii) Upon the occurrence or effective designation of an Early Termination Date, no further payments or deliveries under Section 2(a)(i) or 2(e) in respect of the Terminated Transactions will be required to be made, but without prejudice to the other provisions of this Agreement. The amount, if any, payable in respect of an Early Termination Date shall be determined pursuant to Section 6(e).

(d) Calculations.

(i) Statement. On or as soon as reasonably practicable following the occurrence of an Early Termination Date, each party will make the calculations on its part, if any, contemplated by Section 6(e) and will provide to the other party a statement (1) showing, in reasonable detail, such calculations (including all relevant quotations and specifying any amount payable under Section 6(e)) and (2) giving details of the relevant account to which any amount payable to it is to be paid. In the absence of written confirmation from the source of a quotation obtained in determining a Market Quotation, the records of the party obtaining such quotation will be conclusive evidence of the existence and accuracy of such quotation.

(ii) Payment Date. An amount calculated as being due in respect of any Early Termination Date under Section 6(e) will be payable on the day that notice of the amount payable is effective (in the case of an Early Termination Date which is designated or occurs as a result of an Event of Default) and on the day which is two Local Business Days after the day on which notice of the amount payable is effective (in the case of an Early Termination Date which is designated as a result of a Termination Event). Such amount will be paid together with (to the extent permitted under applicable law) interest thereon (before as well as after judgment) in the Termination Currency, from (and including) the relevant Early Termination Date to (but excluding) the date such amount is paid, at the Applicable Rate. Such interest will be calculated on the basis of daily compounding and the actual number of days elapsed.

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(e) Payments on Early Termination. If an Early Termination Date occurs, the following provisions shall apply based on the parties' election in the Schedule of a payment measure, either "Market Quotation" or "Loss", and a payment method, either the "First Method" or the "Second Method". If the parties fail to designate a payment measure or payment method in the Schedule, it will be deemed that "Market Quotation" or the "Second Method", as the case may be, shall apply. The amount, if any, payable in respect of an Early Termination Date and determined pursuant to this Section will be subject to any Set-off.

(i) Events of Default. If the Early Termination Date results from an Event of Default:-

(1) First Method and Market Quotation. If the First Method and Market Quotation apply, the Defaulting Party will pay to the Non-defaulting Party the excess, if a positive number, of (A) the sum of the Settlement Amount (determined by the Non-defaulting Party) in respect of the Terminated Transactions and the Termination Currency Equivalent of the Unpaid Amounts owing to the Non-defaulting Party over (B) the Termination Currency Equivalent of the Unpaid Amounts owing to the Defaulting Party.

(2) First Method and Loss. If the First Method and Loss apply, the Defaulting Party will pay to the Non-defaulting Party, if a positive number, the Non-defaulting Party's Loss in respect of this Agreement.

(3) Second Method and Market Quotation. If the Second Method and Market Quotation apply, an amount will be payable equal to (A) the sum of the Settlement Amount (determined by the Non-defaulting Party) in respect of the Terminated Transactions and the Termination Currency Equivalent of the Unpaid Amounts owing to the Non-defaulting Party less (B) the Termination Currency Equivalent of the Unpaid Amounts owing to the Defaulting Party. If that amount is a positive number, the Defaulting Party will pay it to the Non-defaulting Party; if it is a negative number, the Non-defaulting Party will pay the absolute value of that amount to the Defaulting Party.

(4) Second Method and Loss. If the Second Method and Loss apply, an amount will be payable equal to the Non-defaulting Party's Loss in respect of this Agreement. If that amount is a positive number, the Defaulting Party will pay it to the Non-defaulting Party; if it is a negative number, the Non-defaulting Party will pay the absolute value of that amount to the Defaulting Party.

(ii) Termination Events. If the Early Termination Date results from a Termination Event:-

(1) One Affected Party. If there is one Affected Party, the amount payable will be determined in accordance with Section 6(e)(i)(3), if Market Quotation applies, or Section 6(e)(i)(4), if Loss applies, except that, in either case, references to the Defaulting Party and to the Non-defaulting Party will be deemed to be references to the Affected Party and the party which is not the Affected Party, respectively, and, if Loss applies and fewer than all the Transactions are being terminated, Loss shall be calculated in respect of all Terminated Transactions.

(2) Two Affected Parties. If there are two Affected Parties:-

(A) if Market Quotation applies, each party will determine a Settlement Amount in respect of the Terminated Transactions, and an amount will be payable equal to (I) the sum of (a) one-half of the difference between the Settlement Amount of the party with the higher Settlement Amount ("X") and the Settlement Amount of the party with the lower Settlement Amount ("Y") and (b) the Termination Currency Equivalent of the Unpaid Amounts owing to X less (II) the Termination Currency Equivalent of the Unpaid Amounts owing to Y; and

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(B) if Loss applies, each party will determine its Loss in respect of this Agreement (or, if fewer than all the Transactions are being terminated, in respect of all Terminated Transactions) and an amount will be payable equal to one-half of the difference between the Loss of the party with the higher Loss ("X") and the Loss of the party with the lower Loss ("Y").

If the amount payable is a positive number, Y will pay it to X; if it is a negative number, X will pay the absolute value of that amount to Y.

(iii) Adjustment for Bankruptcy. In circumstances where an Early Termination Date occurs because "Automatic Early Termination" applies in respect of a party, the amount determined under this Section 6(e) will be subject to such adjustments as are appropriate and permitted by law to reflect any payments or deliveries made by one party to the other under this Agreement (and retained by such other party) during the period from the relevant Early Termination Date to the date for payment determined under Section 6(d)(ii).

(iv) Pre-Estimate. The parties agree that if Market Quotation applies an amount recoverable under this Section 6(e) is a reasonable pre-estimate of loss and not a penalty. Such amount is payable for the loss of bargain and the loss of protection against future risks and except as otherwise provided in this Agreement neither party will be entitled to recover any additional damages as a consequence of such losses.

7. Transfer

Subject to Section 6(b)(ii), neither this Agreement nor any interest or obligation in or under this Agreement may be transferred (whether by way of security or otherwise) by either party without the prior written consent of the other party, except that:-

(a) a party may make such a transfer of this agreement pursuant to a consolidation or amalgamation with, or merger with or into, or transfer of all or substantially all its assets to, another entity (but without prejudice to any other right or remedy under this Agreement); and

(b) a party may make such a transfer of all or any part of its interest in any amount payable to it from a Defaulting Party under Section 6(e).

Any purported transfer that is not in compliance with this Section will be void.

8. Contractual Currency

(a) Payment in the Contractual Currency. Each payment under this Agreement will be made in the relevant currency specified in this Agreement for that payment (the "Contractual Currency"). To the extent permitted by applicable law, any obligation to make payments under this Agreement in the Contractual Currency will not be discharged or satisfied by any tender in any currency other than the Contractual Currency, except to the extent such tender results in the actual receipt by the party to which payment is owed, acting in a reasonable manner and in good faith in converting the currency so tendered into the Contractual Currency, of the full amount in the Contractual Currency of all amounts payable in respect of this Agreement. If for any reason the amount in the Contractual Currency so received falls short of the amount in the Contractual Currency payable in respect of this Agreement, the party required to make the payment will, to the extent permitted by applicable law, immediately pay such additional amount in the Contractual Currency as may be necessary to compensate for the shortfall. If for any reason the amount in the Contractual Currency so received exceeds the amount in the Contractual Currency payable in respect of this Agreement, the party receiving the payment will refund promptly the amount of such excess.

(b) Judgments. To the extent permitted by applicable law, if any judgment or order expressed in a currency other than the Contractual Currency is rendered (i) for the payment of any amount owing in

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respect of this Agreement, (ii) for the payment of any amount relating to any early termination in respect of this Agreement or (iii) in respect of a judgment or order of another court for the payment of any amount described in (i) or (ii) above, the party seeking recovery, after recovery in full of the aggregate amount to which such party is entitled pursuant to the judgment or order, will be entitled to receive immediately from the other party the amount of any shortfall of the Contractual Currency received by such party as a consequence of sums paid in such other currency and will refund promptly to the other party any excess of the Contractual Currency received by such party as a consequence of sums paid in such other currency if such shortfall or such excess arises or results from any variation between the rate of exchange at which the Contractual Currency is converted into the currency of the judgment or order for the purposes of such judgment or order and the rate of exchange at which such party is able, acting in a reasonable manner and in good faith in converting the currency received into the Contractual Currency, to purchase the Contractual Currency with the amount of the currency of the judgment or order actually received by such party. The term "rate of exchange" includes, without limitation, any premiums and costs of exchange payable in connection with the purchase of or conversion into the Contractual Currency.

(c) Separate Indemnities. To the extent permitted by applicable law, these indemnities constitute separate and independent obligations from the other obligations in this Agreement, will be enforceable as separate and independent causes of action, will apply notwithstanding any indulgence granted by the party to which any payment is owed and will not be affected by judgment being obtained or claim or proof being made for any other sums payable in respect of this Agreement.

(d) Evidence of Loss. For the purpose of this Section 8, it will be sufficient for a party to demonstrate that it would have suffered a loss had an actual exchange or purchase been made.

9. Miscellaneous

(a) Entire Agreement. This Agreement constitutes the entire agreement and understanding of the parties with respect to its subject matter and supersedes all oral communication and prior writings with respect thereto.

(b) Amendments. No amendment, modification or waiver in respect of this Agreement will be effective unless in writing (including a writing evidenced by a facsimile transmission) and executed by each of the parties or confirmed by an exchange of telexes or electronic messages on an electronic messaging system.

(c) Survival of Obligations. Without prejudice to Sections 2(a)(iii) and 6(c)(ii), the obligations of the parties under this Agreement will survive the termination of any Transaction.

(d) Remedies Cumulative. Except as provided in this Agreement, the rights, powers, remedies and privileges provided in this Agreement are cumulative and not exclusive of any rights, powers, remedies and privileges provided by law.

(e) Counterparts and Confirmations.

(i) This Agreement (and each amendment, modification and waiver in respect of it) may be executed and delivered in counterparts (including by facsimile transmission), each of which will be deemed an original.

(ii) The parties intend that they are legally bound by the terms of each Transaction from the moment they agree to those terms (whether orally or otherwise). A Confirmation shall be entered into as soon as practicable and may be executed and delivered in counterparts (including by facsimile transmission) or be created by an exchange of telexes or by an exchange of electronic messages on an electronic messaging system, which in each case will be sufficient for all purposes to evidence a binding supplement to this Agreement. The parties will specify therein or through another effective means that any such counterpart, telex or electronic message constitutes a Confirmation.

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(f) No Waiver of Rights. A failure or delay in exercising any right, power or privilege in respect of this Agreement will not be presumed to operate as a waiver, and a single or partial exercise of any right, power or privilege will not be presumed to preclude any subsequent or further exercise, of that right, power or privilege or the exercise of any other right, power or privilege.

(g) Headings. The headings used in this Agreement are for convenience of reference only and are not to affect the construction of or to be taken into consideration in interpreting this Agreement.

10. Offices; Multibranch Parties

(a) If Section 10(a) is specified in the Schedule as applying, each party that enters into a Transaction through an Office other than its head or home office represents to the other party that, notwithstanding the place of booking office or jurisdiction of incorporation or organisation of such party, the obligations of such party are the same as if it had entered into the Transaction through its head or home office. This representation will be deemed to be repeated by such party on each date on which a Transaction is entered into.

(b) Neither party may change the Office through which it makes and receives payments or deliveries for the purpose of a Transaction without the prior written consent of the other party.

(c) If a party is specified as a Multibranch Party in the Schedule, such Multibranch Party may make and receive payments or deliveries under any Transaction through any Office listed in the Schedule, and the Office through which it makes and receives payments or deliveries with respect to a Transaction will be specified in the relevant Confirmation.

11. Expenses

A Defaulting Party will, on demand, indemnify and hold harmless the other party for and against all reasonable out-of-pocket expenses, including legal fees and Stamp Tax, incurred by such other party by reason of the enforcement and protection of its rights under this Agreement or any Credit Support Document to which the Defaulting Party is a party or by reason of the early termination of any Transaction, including, but not limited to, costs of collection.

12. Notices

(a) Effectiveness. Any notice or other communication in respect of this Agreement may be given in any manner set forth below (except that a notice or other communication under Section 5 or 6 may not be given by facsimile transmission or electronic messaging system) to the address or number or in accordance with the electronic messaging system details provided (see the Schedule) and will be deemed effective as indicated:-

(i) if in writing and delivered in person or by courier, on the date it is delivered;

(ii) if sent by telex, on the date the recipient's answerback is received;

(iii) if sent by facsimile transmission, on the date that transmission is received by a responsible employee of the recipient in legible form (it being agreed that the burden of proving receipt will be on the sender and will not be met by a transmission report generated by the sender's facsimile machine);

(iv) if sent by certified or registered mail (airmail, if overseas) or the equivalent (return receipt requested), on the date that mail is delivered or its delivery is attempted; or

(v) if sent by electronic messaging system, on the date that electronic message is received,

unless the date of that delivery (or attempted delivery) or that receipt, as applicable, is not a Local Business Day or that communication is delivered (or attempted) or received, as applicable, after the close of business on a Local Business Day, in which case that communication shall be deemed given and effective on the first following day that is a Local Business Day.

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(b) Change of Addresses. Either party may by notice to the other change the address, telex or facsimile number or electronic messaging system details at which notices or other communications are to be given to it.

13. Governing Law and Jurisdiction

(a) Governing Law. This Agreement will be governed by and construed in accordance with the law specified in the Schedule.

(b) Jurisdiction. With respect to any suit, action or proceedings relating to this Agreement ("Proceedings"), each party irrevocably:-

(i) submits to the jurisdiction of the English courts, if this Agreement is expressed to be governed by English law, or to the non-exclusive jurisdiction of the courts of the State of New York and the United States District Court located in the Borough of Manhattan in New York City, if this Agreement is expressed to be governed by the laws of the State of New York; and

(ii) waives any objection which it may have at any time to the laying of venue of any Proceedings brought in any such court, waives any claim that such Proceedings have been brought in an inconvenient forum and further waives the right to object, with respect to such Proceedings, that such court does not have any jurisdiction over such party.

Nothing in this Agreement precludes either party from bringing Proceedings in any other jurisdiction (outside, if this Agreement is expressed to be governed by English law, the Contracting States, as defined in Section 1(3) of the Civil Jurisdiction and Judgments Act 1982 or any modification, extension or re-enactment thereof for the time being in force) nor will the bringing of Proceedings in any one or more jurisdictions preclude the bringing of Proceedings in any other jurisdiction.

(c) Service of Process. Each party irrevocably appoints the Process Agent (if any) specified opposite its name in the Schedule to receive, for it and on its behalf, service of process in any Proceedings. If for any reason any party's Process Agent is unable to act as such, such party will promptly notify the other party and within 30 days appoint a substitute process agent acceptable to the other party. The parties irrevocably consent to service of process given in the manner provided for notices in Section 12. Nothing in this Agreement will affect the right of either party to serve process in any other manner permitted by law.

(d) Waiver of Immunities. Each party irrevocably waives, to the fullest extent permitted by applicable law, with respect to itself and its revenues and assets (irrespective of their use or intended use), all immunity on the grounds of sovereignty or other similar grounds from (i) suit, (ii) jurisdiction of any court, (iii) relief by way of injunction, order for specific performance or for recovery of property, (iv) attachment of its assets (whether before or after judgment) and (v) execution or enforcement of any judgment to which it or its revenues or assets might otherwise be entitled in any Proceedings in the courts of any jurisdiction and irrevocably agrees, to the extent permitted by applicable law, that it will not claim any such immunity in any Proceedings.

14. Definitions

As used in this Agreement:-

"Additional Termination Event" has the meaning specified in Section 5(b).

"Affected Party" has the meaning specified in Section 5(b).

"Affected Transactions" means (a) with respect to any Termination Event consisting of an Illegality, Tax Event or Tax Event Upon Merger, all Transactions affected by the occurrence of such Termination Event and (b) with respect to any other Termination Event, all Transactions.

"Affiliate" means, subject to the Schedule, in relation to any person, any entity controlled, directly or indirectly, by the person, any entity that

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controls, directly or indirectly, the person or any entity directly or indirectly under common control with the person. For this purpose, "control" of any entity or person means ownership of a majority of the voting power of the entity or person.

"Applicable Rate" means:-

- (a) in respect of obligations payable or deliverable (or which would have been but for Section 2(a)(iii)) by a Defaulting Party, the Default Rate;
- (b) in respect of an obligation to pay an amount under Section 6(e) of either party from and after the date (determined in accordance with Section 6(d)(ii)) on which that amount is payable, the Default Rate;
- (c) in respect of all other obligations payable or deliverable (or which would have been but for Section 2(a)(iii)) by a Non-defaulting Party, the Non-default Rate; and
- (d) in all other cases, the Termination Rate.

"Burdened Party" has the meaning specified in Section 5(b).

"Change in Tax Law" means the enactment, promulgation, execution or ratification of, or any change in or amendment to, any law (or in the application or official interpretation of any law) that occurs on or after the date on which the relevant Transaction is entered into.

"consent" includes a consent, approval, action, authorisation, exemption, notice, filing, registration or exchange control consent. "Credit Event Upon Merger" has the meaning specified in Section 5(b).

"Credit Support Document" means any agreement or instrument that is specified as such in this Agreement. "Credit Support Provider" has the meaning specified in the Schedule.

"Default Rate" means a rate per annum equal to the cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount plus 1% per annum.

"Defaulting Party" has the meaning specified in Section 6(a).

"Early Termination Date" means the date determined in accordance with Section 6(a) or 6(b)(iv).

"Event of Default" has the meaning specified in Section 5(a) and, if applicable, in the Schedule.

"Illegality" has the meaning specified in Section 5(b).

"Indemnifiable Tax" means any Tax other than a Tax that would not be imposed in respect of a payment under this Agreement but for a present or former connection between the jurisdiction of the government or taxation authority imposing such Tax and the recipient of such payment or a person related to such recipient (including, without limitation, a connection arising from such recipient or related person being or having been a citizen or resident of such jurisdiction, or being or having been organised, present or engaged in a trade or business in such jurisdiction, or having or having had a permanent establishment or fixed place of business in such jurisdiction, but excluding a connection arising solely from such recipient or related person having executed, delivered, performed its obligations or received a payment under, or enforced, this Agreement or a Credit Support Document).

"law" includes any treaty, law, rule or regulation (as modified, in the case of tax matters, by the practice of any relevant governmental revenue authority) and "lawful" and "unlawful" will be construed accordingly.

"Local Business Day" means, subject to the Schedule, a day on which commercial banks are open for business (including dealings in foreign exchange and foreign currency deposits) (a) in relation to any obligation under Section 2(a)(i), in the place(s) specified in the relevant Confirmation or, if not so

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specified, as otherwise agreed by the parties in writing or determined pursuant to provisions contained, or incorporated by reference, in this Agreement, (b) in relation to any other payment, in the place where the relevant account is located and, if different, in the principal financial centre, if any, of the currency of such payment, (c) in relation to any notice or other communication, including notice contemplated under Section 5(a)(i), in the city specified in the address for notice provided by the recipient and, in the case of a notice contemplated by Section 2(b), in the place where the relevant new account is to be located and (d) in relation to Section 5(a)(v)(2), in the relevant locations for performance with respect to such Specified Transaction.

"Loss" means, with respect to this Agreement or one or more Terminated Transactions, as the case may be, and a party, the Termination Currency Equivalent of an amount that party reasonably determines in good faith to be its total losses and costs (or gain, in which case expressed as a negative number) in connection with this Agreement or that Terminated Transaction or group of Terminated Transactions, as the case may be, including any loss of bargain, cost of funding or, at the election of such party but without duplication, loss or cost incurred as a result of its terminating, liquidating, obtaining or reestablishing any hedge or related trading position (or any gain resulting from any of them). Loss includes losses and costs (or gains) in respect of any payment or delivery required to have been made (assuming satisfaction of each applicable condition precedent) on or before the relevant Early Termination Date and not made, except, so as to avoid duplication, if Section 6(e)(i)(1) or (3) or 6(e)(ii)(2)(A) applies. Loss does not include a party's legal fees and out-of-pocket expenses referred to under Section 11. A party will determine its Loss as of the relevant Early Termination Date, or, if that is not reasonably practicable, as of the earliest date thereafter as is reasonably practicable. A party may (but need not) determine its Loss by reference to quotations of relevant rates or prices from one or more leading dealers in the relevant markets.

"Market Quotation" means, with respect to one or more Terminated Transactions and a party making the determination, an amount determined on the basis of quotations from Reference Market-makers. Each quotation will be for an amount, if any, that would be paid to such party (expressed as a negative number) or by such party (expressed as a positive number) in consideration of an agreement between such party (taking into account any existing Credit Support Document with respect to the obligations of such party) and the quoting Reference Market-maker to enter into a transaction (the "Replacement Transaction") that would have the effect of preserving for such party the economic equivalent of any payment or delivery (whether the underlying obligation was absolute or contingent and assuming the satisfaction of each applicable condition precedent) by the parties under Section 2(a)(i) in respect of such Terminated Transaction or group of Terminated Transactions that would, but for the occurrence of the relevant Early Termination Date, have been required after that date. For this purpose, Unpaid Amounts in respect of the Terminated Transaction or group of Terminated Transactions are to be excluded but, without limitation, any payment or delivery that would, but for the relevant Early Termination Date, have been required (assuming satisfaction of each applicable condition precedent) after that Early Termination Date is to be included. The Replacement Transaction would be subject to such documentation as such party and the Reference Market-maker may, in good faith, agree. The party making the determination (or its agent) will request each Reference Market-maker to provide its quotation to the extent reasonably practicable as of the same day and time (without regard to different time zones) on or as soon as reasonably practicable after the relevant Early Termination Date. The day and time as of which those quotations are to be obtained will be selected in good faith by the party obliged to make a determination under Section 6(e), and, if each party is so obliged, after consultation with the other. If more than three quotations are provided, the Market Quotation will be the arithmetic mean of the quotations, without regard to the quotations having the highest and lowest values. If exactly three such quotations are provided, the Market Quotation will be the quotation remaining after disregarding the highest and lowest quotations. For this purpose, if more than one quotation has the same highest value or lowest value, then one of such quotations shall be disregarded. If fewer than three quotations are provided, it will be deemed that the Market Quotation in respect of such Terminated Transaction or group of Terminated Transactions cannot be determined.

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"Non-default Rate" means a rate per annum equal to the cost (without proof or evidence of any actual cost) to the Non-defaulting Party (as certified by it) if it were to fund the relevant amount.

"Non-defaulting Party" has the meaning specified in Section 6(a).

"Office" means a branch or office of a party, which may be such party's head or home office.

"Potential Event of Default" means any event which, with the giving of notice or the lapse of time or both, would constitute an Event of Default.

"Reference Market-makers" means four leading dealers in the relevant market selected by the party determining a Market Quotation in good faith (a) from among dealers of the highest credit standing which satisfy all the criteria that such party applies generally at the time in deciding whether to offer or to make an extension of credit and (b) to the extent practicable, from among such dealers having an office in the same city.

"Relevant Jurisdiction" means, with respect to a party, the jurisdictions (a) in which the party is incorporated, organised, managed and controlled or considered to have its seat, (b) where an Office through which the party is acting for purposes of this Agreement is located, (c) in which the party executes this Agreement and (d) in relation to any payment, from or through which such payment is made.

"Scheduled Payment Date" means a date on which a payment or delivery is to be made under Section 2(a)(i) with respect to a Transaction.

"Set-off" means set-off, offset, combination of accounts, right of retention or withholding or similar right or requirement to which the payer of an amount under Section 6 is entitled or subject (whether arising under this Agreement, another contract, applicable law or otherwise) that is exercised by, or imposed on, such payer.

"Settlement Amount" means, with respect to a party and any Early Termination Date, the sum of:-

(a) the Termination Currency Equivalent of the Market Quotations (whether positive or negative) for each Terminated Transaction or group of Terminated Transactions for which a Market Quotation is determined; and

(b) such party's Loss (whether positive or negative and without reference to any Unpaid Amounts) for each Terminated Transaction or group of Terminated Transactions for which a Market Quotation cannot be determined or would not (in the reasonable belief of the party making the determination) produce a commercially reasonable result.

"Specified Entity" has the meanings specified in the Schedule.

"Specified Indebtedness" means, subject to the Schedule, any obligation (whether present or future, contingent or otherwise, as principal or surety or otherwise) in respect of borrowed money.

"Specified Transaction" means, subject to the Schedule, (a) any transaction (including an agreement with respect thereto) now existing or hereafter entered into between one party to this Agreement (or any Credit Support Provider of such party or any applicable Specified Entity of such party) and the other party to this Agreement (or any Credit Support Provider of such other party or any applicable Specified Entity of such other party) which is a rate swap transaction, basis swap, forward rate transaction, commodity swap, commodity option, equity or equity index swap, equity or equity index option, bond option, interest rate option, foreign exchange transaction, cap transaction, floor transaction, collar transaction, currency swap transaction, cross-currency rate swap transaction, currency option or any other similar transaction (including any option with respect to any of these transactions), (b) any combination of these transactions and (c) any other transaction identified as a Specified Transaction in this Agreement or the relevant confirmation.

"Stamp Tax" means any stamp, registration, documentation or similar tax.

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"Tax" means any present or future tax, levy, impost, duty, charge, assessment or fee of any nature (including interest, penalties and additions thereto) that is imposed by any government or other taxing authority in respect of any payment under this Agreement other than a stamp, registration, documentation or similar tax.

"Tax Event" has the meaning specified in Section 5(b).

"Tax Event Upon Merger" has the meaning specified in Section 5(b).

"Terminated Transactions" means with respect to any Early Termination Date (a) if resulting from a Termination Event, all Affected Transactions and (b) if resulting from an Event of Default, all Transactions (in either case) in effect immediately before the effectiveness of the notice designating that Early Termination Date (or, if "Automatic Early Termination" applies, immediately before that Early Termination Date).

"Termination Currency" has the meaning specified in the Schedule.

"Termination Currency Equivalent" means, in respect of any amount denominated in the Termination Currency, such Termination Currency amount and, in respect of any amount denominated in a currency other than the Termination Currency (the "Other Currency"), the amount in the Termination Currency determined by the party making the relevant determination as being required to purchase such amount of such Other Currency as at the relevant Early Termination Date, or, if the relevant Market Quotation or Loss (as the case may be), is determined as of a later date, that later date, with the Termination Currency at the rate equal to the spot exchange rate of the foreign exchange agent (selected as provided below) for the purchase of such Other Currency with the Termination Currency at or about 11:00 a.m. (in the city in which such foreign exchange agent is located) on such date as would be customary for the determination of such a rate for the purchase of such Other Currency for value on the relevant Early Termination Date or that later date. The foreign exchange agent will, if only one party is obliged to make a determination under Section 6(e), be selected in good faith by that party and otherwise will be agreed by the parties.

"Termination Event" means an Illegality, a Tax Event or a Tax Event Upon Merger or, if specified to be applicable, a Credit Event Upon Merger or an Additional Termination Event.

"Termination Rate" means a rate per annum equal to the arithmetic mean of the cost (without proof or evidence of any actual cost) to each party (as certified by such party) if it were to fund or of funding such amounts.

"Unpaid Amounts" owing to any party means, with respect to an Early Termination Date, the aggregate of (a) in respect of all Terminated Transactions, the amounts that became payable (or that would have become payable but for Section 2(a)(iii)) to such party under Section 2(a)(i) on or prior to such Early Termination Date and which remain unpaid as at such Early Termination Date and (b) in respect of each Terminated Transaction, for each obligation under Section 2(a)(i) which was (or would have been but for Section 2(a)(iii)) required to be settled by delivery to such party on or prior to such Early Termination Date and which has not been so settled as at such Early Termination Date, an amount equal to the fair market value of that which was (or would have been) required to be delivered as of the originally scheduled date for delivery, in each case together with (to the extent permitted under applicable law) interest, in the currency of such amounts, from (and including) the date such amounts or obligations were or would have been required to have been paid or performed to (but excluding) such Early Termination Date, at the Applicable Rate. Such amounts of interest will be calculated on the basis of daily compounding and the actual number of days elapsed. The fair market value of any obligation referred to in clause (b) above shall be reasonably determined by the party obliged to make the determination under Section 6(e) or, if each party is so obliged, it shall be the average of the Termination Currency Equivalents of the fair market values reasonably determined by both parties.

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IN WITNESS WHEREOF the parties have executed this document on the respective dates specified below with effect from the date specified on the first page of this document.

Citizens Bank of Massachusetts

Kadant Inc.

By: s/s Michael Smith
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Name: Michael Smith
Title: Vice President
Date: 6/30/2005

By: s/s Daniel J. Walsh
.....
Name: Daniel J. Walsh
Title: Treasurer
Date: 5/25/2005

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SCHEDULE
to the Master Agreement
dated as of May 13, 2005

between

CITIZENS BANK OF MASSACHUSETTS,
a bank organized under the laws
of Massachusetts ("Party A")

and

KADANT INC., a corporation
organized under the laws of
Massachusetts ("Party B")

Part 1
Termination Provisions

In this Agreement:

(a) "Specified Entity" means in relation to Party A for the purpose of:

Section 5(a)(v), NONE

Section 5(a)(vi), NONE

Section 5(a)(vii), NONE

Section 5(b)(iv), NONE

and in relation to Party B for the purpose of:

Section 5(a)(v), NONE

Section 5(a)(vi), NONE

Section 5(a)(vii), NONE

Section 5(b)(iv), NONE

(b) The definition of "Specified Transaction" in Section 14 is hereby amended by adding the text "repurchase transaction, reverse repurchase transaction," after the text "foreign exchange transaction" and before the text "cap transaction".

(c) "Cross Default". For the purpose of this Agreement:

(i) with respect to Party A, the Cross Default provisions of Section 5 (a)(vi) will apply and the "Threshold Amount" means 2% of "Total Capital and Reserves" of Citizens Financial Group, Inc. as shown on the most recent annual audited financial statements of Citizens Financial Group, Inc.; and

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(ii) with respect to Party B, the Cross Default provisions are not applicable, however the "Additional Event of Default" provision relating to cross default in Part 5(c) herein shall be applicable.

(d) The "Credit Event Upon Merger" provisions of Section 5(b)(iv) will not apply to Party A or Party B.

(e) The "Automatic Early Termination" provision of Section 6(a) will not apply to Party A or Party B.

(f) "Payments on Early Termination". For the purpose of Section 6(e) of this Agreement:

- (i) Market Quotation will apply.
- (ii) The Second Method will apply.

(g) "Termination Currency" means United States Dollars.

(h) "Additional Termination Event" will not apply.

Part 2
Tax Representations

(a) Payer Tax Representation. For the purpose of Section 3(e), Party A and Party B hereby make the following representation:

It is not required by any applicable law, as modified by the practice of any relevant governmental revenue authority, of any Relevant Jurisdiction to make any deduction or withholding for or on account of any Tax from any payment (other than interest under Section 2(e), 6(d)(ii) or 6(e)) to be made by it to the other party under this Agreement. In making this representation, it may rely on:

- (i) the accuracy of any representation made by the other party pursuant to Section 3(f);
- (ii) the satisfaction of the agreement of the other party contained in Section 4(a)(i) or 4(a)(iii) and the accuracy and effectiveness of any document provided by the other party pursuant to Section 4(a)(i) or 4(a)(iii); and
- (iii) the satisfaction of the agreement of the other party contained in Section 4(d);

provided that it shall not be a breach of this representation where reliance is placed on clause (ii) and the other party does not deliver a form or document under Section 4(a)(iii) by reason of material prejudice to its legal or commercial position.

(b) Payee Tax Representations. For the purpose of Section 3(f), Party A and Party B make the representation(s) specified below:

- (i) The following representation applies to Party A:
Party A is a bank organized under the laws of Massachusetts.

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> (ii) The following representation applies to Party B:

Party B is a corporation organized under the laws of Massachusetts.

Part 3
Agreement to Deliver Documents

For the purpose of Sections 4(a) (i) and (ii) of this Agreement, each party agrees to deliver the following documents, as applicable:

(a) Tax forms, documents or certificates to be delivered are:

Party required to deliver document	Form/Document/Certificate	Date by which to be delivered
Party A and Party B	Department of the Treasury Internal Revenue Service Form W-9	On or before execution of this Agreement

(b) Other documents to be delivered are:

Party required to deliver document	Form/Document/Certificate	Date by which to be delivered	Covered by Section 3(d) Representation
Party A and Party B	Signature authentication satisfactory to the other party hereto substantially in the form attached hereto as Exhibit A	On or before execution of this Agreement	YES
Party B	Copy (certified by an officer) of the board resolution (or equivalent authorizing documentation) permitting the entering into of this Agreement and Transactions hereunder substantially in the form attached hereto as Exhibit B	On or before execution of this Agreement	YES

Part 4
Miscellaneous

(a) Addresses for Notices. For the purposes of Section 12(a) of this Agreement:

(i) All notices or communications to Party A shall, with respect to a particular Transaction, be sent to the address, telex number, or facsimile number reflected in the Confirmation of that Transaction, and any notice for purposes of Sections 5 or 6 shall be sent to:

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Address: Citizens Bank of Massachusetts
One Citizens Plaza
Providence, RI 02903

Attention: Mr. Michael Smith
Treasury Operations

Telephone: (401) 282-7250
Facsimile: (401) 282-5219
E-Mail: michael.smith@citizensbank.com

with a mandatory copy to:

Address: Citizens Bank of Massachusetts
One Citizens Plaza
Providence, RI 02903

Attention: William Lingard
Telephone: (617) 994-7114
Facsimile: (617) 723-9371

- (ii) All notices or communications to Party B shall be sent to the address, telex number, or facsimile number reflected below:

Address: Kadant Inc.
1 Acton Place, Suite 202
Acton, MA 01720

Attention: Daniel J. Walsh
Telephone: (978) 776-2020
Facsimile: (978) 635-1593

- (b) Process Agent. For the purpose of Section 13 (c) of this Agreement:
Party A appoints as its Process Agent: Not applicable.
Party B appoints as its Process Agent: Not applicable.
- (c) Offices. Section 10(c) will apply to this Agreement.
- (d) Multibranch Party. For the purpose of Section 10(c) of this Agreement:
(i) Party A is not a Multibranch Party.
(ii) Party B is not a Multibranch Party.
- (e) Calculation Agent. The Calculation Agent is Party A.
- (f) Credit Support Document. NOT APPLICABLE
- (g) Credit Support Provider. Credit Support Provider means: NOT APPLICABLE
- (h) Governing Law. This Agreement will be governed by and construed in accordance with the laws of the State of New York (without reference to choice of law doctrine).
- (i) Netting of Payments. Subparagraph (ii) of Section 2 (c) of this Agreement will apply.

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(j) "Affiliate" will have the meaning specified in Section 14 of this Agreement.

Part 5
Other Provisions

(a) Definitions. The definitions and provisions contained in the 2000 ISDA -----

Definitions (the "2000 ISDA Definitions") as published by the International Swaps and Derivatives Association, Inc. are hereby incorporated into this Agreement by reference. For these purposes, all references in the 2000 ISDA Definitions to a "Swap Transaction" shall be deemed to apply to each Transaction entered into hereunder.

(b) Set-off. Without affecting the provisions of the Agreement requiring -----

the calculation of certain net payment amounts, all payments under this Agreement will be made without set-off or counterclaim; provided, however, that upon the designation of any Early Termination Date, in addition to and not in limitation of any other right or remedy (including any right to set off, counterclaim, or otherwise withhold payment or any recourse to any Credit Support Document) under applicable law the Non-defaulting Party or Non-affected Party (in either case, "X") may without prior notice to any person set off any sum or obligation (whether or not arising under this Agreement and whether matured or unmatured, whether or not contingent and irrespective of the currency, place of payment or booking office of the sum or obligation) owed by the Defaulting Party or Affected Party (in either case, "Y") to X against any sum or obligation (whether or not arising under this Agreement, whether matured or unmatured, whether or not contingent and irrespective of the currency, place of payment or booking office of the sum or obligation) owed by X to Y and, for this purpose, may convert one currency into another at a market rate determined by X. If any sum or obligation is unascertained, X may in good faith estimate that sum or obligation and set-off in respect of that estimate, subject to X or Y, as the case may be, accounting to the other party when such sum or obligation is ascertained.

(c) Additional Event of Default. It shall constitute an Event of Default -----

under this Agreement if there should occur and be continuing, unwaived and uncured, an Event of Default under the Credit Agreement. As used herein, "Credit Agreement" shall mean the Credit Agreement, dated as of May 9, 2005, by and among Party B as Borrower, JPMorgan Chase Bank, N.A., as Administrative Agent, and the several lenders from time to time party thereto, as such agreement may be amended, restated, modified, or extended from time to time hereafter (the "JPM Credit Agreement") and any credit agreement that in whole or substantial part replaces the JPM Credit Agreement, as such replacement agreement shall be amended, restated, modified or replaced from time to time, provided, however, that if there is no Credit Agreement in effect or if Party A shall cease to be a party to any Credit Agreement, "Credit Agreement" shall mean the Credit Agreement as it existed immediately prior to such event.

(d) Representations and Warranties. Section 3(a) is amended by adding the -----

following paragraphs (vi) and (vii):

- (vi) No Agency. It is entering into this Agreement and each Transaction as principal (and not as agent or in any other capacity, fiduciary or otherwise).
- (vii) Eligible Contract Participant. It is an "eligible contract participant" as defined in the U.S. Commodity Exchange Act.

(e) Relationship Between Parties. Each party will be deemed to represent to -----

the other party on the date on which it enters into a Transaction that (absent a written agreement between the parties that expressly imposes affirmative obligations to the contrary for that Transaction):

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- (i) Non-Reliance. It is acting for its own account, and it has made its own independent decisions to enter into that Transaction and as to whether that Transaction is appropriate or proper for it based upon its own judgment and upon advice from such advisers as it has deemed necessary. It is not relying on any communication (written or oral) of the other party as investment advice or as a recommendation to enter into that Transaction; it being understood that information and explanations related to the terms and conditions of a Transaction shall not be considered investment advice or a recommendation to enter into that Transaction. No communication (written or oral) received from the other party shall be deemed to be an assurance or guarantee as to the expected results of that Transaction.
 - (ii) Assessment and Understanding. It is capable of assessing the merits of and understanding (on its own behalf or through independent professional advice), and understands and accepts the terms, conditions and risks of that Transaction. It is also capable of assuming, and assumes, the risks of that Transaction.
 - (iii) Status of Parties. The other party is not acting as a fiduciary for or an adviser to it in respect of that Transaction.
- (f) Waiver of Jury Trial. Each party hereby irrevocably waives any and all -----
right to trial by jury in any suit, action or proceeding arising out of or relating to this Agreement or any Transaction and acknowledges that this waiver is a material inducement to the other party's entering into this Agreement.
- (g) Consent to Recording. The parties agree that each may electronically -----
record all telephonic conversations between them and that any such recordings may be submitted in evidence to any court or in any Proceedings for the purpose of establishing any matters pertinent to any Transaction.
- (h) Outstanding Specified Transactions. Upon the effectiveness of this -----
Agreement, unless otherwise agreed to in writing by the parties to this Agreement with respect to specific Specified Transactions, all Specified Transactions then outstanding between Offices of the parties listed in Section 4(d) shall be subject to the terms hereof.
- (i) Severance. In the event any one or more of the provisions contained in -----
this Agreement should be held invalid, illegal or unenforceable in any respect, such provisions shall be severed from this Agreement to the extent of such invalidity, illegality or unenforceability, unless such severance shall substantially impair the benefits of the remaining portions of this Agreement. The Agreement after such severance shall remain the valid, binding and enforceable obligation of the parties hereto.
- (j) Payment Instructions. All payments to be made hereunder in respect of -----
Transactions shall be made in accordance with standing payment instructions provided by the parties (or as otherwise specified in a Confirmation).

CITIZENS BANK

Date: 18 May 2005

Kadant, Inc.
1 Acton Place, Suite 202
Acton, Massachusetts 01720

Dear Sirs:

Our Reference: CBD12594
Re: USD Amortizing Interest Rate Swap

The purpose of this document is to set forth the terms and conditions of the transaction entered into between Citizens Bank of Massachusetts ("CBMA") and yourselves ("Counterparty") on the trade date specified below (the "Transaction"). This document will constitute a "Confirmation" as referred to in the ISDA Master Agreement specified below.

The definitions and provisions contained in the 2000 ISDA Definitions, (the "Definitions"), as published by the International Swaps and Derivatives Association, Inc. ("ISDA") are incorporated into this Confirmation. In the event of any inconsistency between the Definitions and provisions and this Confirmation, this Confirmation will govern.

This Confirmation evidences a complete and binding agreement between Counterparty and CBMA as to the terms of the Transaction to which this Confirmation relates. In addition, Counterparty and CBMA agree to use all reasonable efforts promptly to negotiate, execute and deliver an agreement in the form of the ISDA Master Agreement (Multicurrency-Cross Border) (the "ISDA Form") published by the ISDA, with such modifications as Counterparty and CBMA shall in good faith agree (the "Agreement"). Upon the execution by Counterparty and CBMA of such Agreement, this Confirmation will supplement, form part of, and be subject to the Agreement. Until we execute and deliver that Agreement, this Confirmation, together with all other documents referring to the ISDA Form (each a "Confirmation") confirming transactions (each a "Transaction") entered into between us (notwithstanding anything to the contrary in a Confirmation), shall supplement, form part of, and be subject to an agreement in the form of the ISDA Form as if we had executed an agreement in such form (but without any Schedule) on the Trade Date of the first such Transaction between us. For purposes thereof, the Second Method and market quotation shall apply. All provisions contained in the Agreement shall govern this Confirmation except as expressly modified below. In the event of any inconsistency between this Confirmation and either the ISDA Form or the Agreement, this Confirmation will govern for the purpose of this transaction.

The terms of the particular transaction to which this confirmation relates are as follows:

Notional Amount	See Schedule A
Trade Date	13 May 2005

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CITIZENS BANK

Effective Date 17 May 2005
Termination Date 11 May 2010, subject to adjustment in accordance with the Modified Following Business Day Convention.

Fixed Amounts

Fixed Rate Payer Kadant, Inc.
Fixed Rate Payer Payment Dates The last of each March, June, September and December from and including 30 June 2005 to and including the Termination Date subject to adjustment in accordance with the Modified Following Business Day Convention.

Fixed Rate 4.125 pct
Fixed Rate Day Count Fraction Actual/360

Floating Amounts

Floating Rate Payer CBMA
Floating Rate Payer Payments Dates The last day of each March, June, September and December from and including 30 June 2005 to and including the Termination Date subject to adjustment in accordance with the Modified Following Business Date Convention.

Floating Rate for initial Calculation Period 3.131940 (exclusive of Spread where applicable)

Floating Rate Option USD-LIBOR-BBA
Designated Maturity 3 Months

Spread None
Floating Rate Day Count Fraction Actual/360

Reset Dates The first day of each Calculation Period.

Business Days New York and London
Calculation Agent CBMA

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CITIZENS BANK

Payments to Counterparty:

Account Number:	To be advised
Account Name:	To be advised
Bank:	To be advised

So long as no Event of Default or Termination Event shall have occurred and then be continuing with respect to Counterparty, the parties hereto agree that Counterparty may terminate this Transaction by at least [5] Business days prior notice to CBMA of its intention to do so, whereupon (a) the obligations of the parties to make any further payments under Section 2(a)(i) of the Agreement in respect of such Transaction shall terminate, (b) the Calculation Agent shall determine a Settlement Amount in accordance with the provisions of the ISDA Master Agreement and provide a statement with respect thereto and (c) a termination payment shall be made on the Early Termination Date as if such Transaction were a Terminated Transaction and Counterparty was the Affected Party.

Counterparty and CBMA represent that each party is acting for its own account and, that each party has made its own independent decisions to enter into this Transaction and as to whether this transaction is appropriate or proper for it based on its own judgment and upon advice from such advisors as it has deemed necessary. Neither party is relying upon any communication (written or oral) from the other party as investment advice or as a recommendation to enter into this Transaction. Information and explanations related to the terms and conditions of this Transaction shall not be considered investment advice or a recommendation to enter into this Transaction. No assurances or guarantees (written or oral) as to the expected results of this Transaction have been received by either party. Each party is capable of evaluating and understanding the terms, risks and conditions of this Transaction. Each party is capable of assuming, and assumes, the financial and other risks of this Transaction.

Counterparty understands that the Transaction entered into under this agreement does not constitute a deposit and is not insured by the Federal Deposit Insurance Corporation, Federal Reserve Board, Office of the Comptroller of the Currency or any state or federal banking agency.

All inquiries regarding payments and/or rate re-settings should be sent to:

CBMA:
Citizens Bank of Massachusetts
One Citizens Plaza
Providence, RI 02903
Attn: Treasury
Michael Liberatore Phone 401-282-1126
 Fax 401-282-7718

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CITIZENS BANK

Counterparty:
Kadant, Inc.
1 Acton Place, Suite 202
Acton, Massachusetts 01720

Please confirm that the foregoing correctly sets forth the terms of our agreement by executing a copy of this Confirmation enclosed for that purpose and returning it to us via mail at the address listed above.

For and on behalf of Citizens Bank of Massachusetts

By: /s/ Kristen Silva

Name: Kristen Silva
Title: Authorized Signatory

Kadant, Inc.

By: /s/ Daniel J. Walsh

Name: Daniel J. Walsh
Title: Treasurer

Calculation Period		Notional Amount (USD)	
17 May 2005	to	30 June 2005	36,000,000.00
30 June 2005	to	30 September 2005	36,000,000.00
30 September 2005	to	30 December 2005	34,650,000.00
30 December 2005	to	31 March 2006	33,300,000.00
31 March 2006	to	30 June 2006	31,950,000.00
30 June 2006	to	29 September 2006	30,600,000.00
29 September 2006	to	29 December 2006	29,250,000.00
29 December 2006	to	30 March 2007	27,900,000.00
30 March 2007	to	29 June 2007	26,550,000.00
29 June 2007	to	28 September 2007	25,200,000.00
28 September 2007	to	31 December 2007	23,400,000.00
31 December 2007	to	31 March 2008	21,600,000.00
31 March 2008	to	30 June 2008	19,800,000.00
30 June 2008	to	30 September 2008	18,000,000.00
30 September 2008	to	31 December 2008	15,750,000.00
31 December 2008	to	31 March 2009	13,500,000.00
31 March 2009	to	30 June 2009	11,250,000.00
30 June 2009	to	30 September 2009	9,000,000.00
30 September 2009	to	31 December 2009	6,750,000.00
31 December 2009	to	31 March 2010	4,500,000.00
31 March 2010	to	11 May 2010	2,250,000.00

Please be advised all dates are subject to adjustment in accordance with the Modified Following Business Day Convention.

CERTIFICATION

I, William A. Rainville, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the fiscal quarter ended July 2, 2005 of Kadant Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 11, 2005

/s/ William A. Rainville

 William A. Rainville
 Chief Executive Officer

CERTIFICATION

I, Thomas M. O'Brien, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the fiscal quarter ended July 2, 2005 of Kadant Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles ;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 11, 2005

/s/ Thomas M. O'Brien

 Thomas M. O'Brien
 Chief Financial Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. Section 1350, the undersigned, William A. Rainville, Chief Executive Officer, and Thomas M. O'Brien, Chief Financial Officer, of Kadant Inc., a Delaware corporation (the "Company"), do hereby certify, to our best knowledge and belief, that:

The Quarterly Report on Form 10-Q for the fiscal quarter ended July 2, 2005 of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in this Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 11, 2005

/s/ William A. Rainville

William A. Rainville
Chief Executive Officer

/s/ Thomas M. O'Brien

Thomas M. O'Brien
Chief Financial Officer